

Summary of Recommendation

<u>Capital Structure</u>	<u>Ratio</u> %	<u>Cost Rate</u> %	<u>Weighted Cost</u> %
Long-Term Debt	46.53	7.97	3.71
Preferred Stock	7.59	7.31	.55
Common Equity	<u>45.88</u>	<u>10.90</u>	<u>5.00</u>
	<u>100.00</u>		<u>9.26</u>

(R.D. at 179).

In its Exceptions, PP&L argued that as a threshold matter, the ALJ's proposed 10.9% equity allowance cannot be reconciled with recent Commission cost of capital findings. For example, within the past month the Commission determined that the cost of equity for a water utility was 11.25%. Pa. P.U.C. v. Pennsylvania-American Water Co., Docket No. R-00943231 (July 24, 1995), ("PAWC"); see also Pa. P.U.C. v. Roaring Creek Water Co., Docket No. R-00943177 (May 31, 1995), ("Roaring Creek") (11.0%). And, last December, the Commission awarded West Penn Power Company -- a utility with an A+ bond rating and no nuclear investment exposure -- an equity return rate of 11.5%. (PP&L Exceptions at 26).

PP&L continued that the ALJ's recommendation is far too low is also confirmed by recent regulatory decisions from other jurisdictions. See, e.g., Re Portland General Electric Co., 160 PUR4th 201, 271 (1995) (11.6%); Re Hawaii Electric Light Co., 159 PUR4th 290, 325 (1995) (11.5% prior to upward adjustment for company-specific risk factors); Re Sierra Pacific Power Co., 158 PUR4th 217, 241-242 (1995) (setting authorized equity returns for California's electric utilities ranging from 11.3% to 12.1%); Re Commonwealth Edison Co., 158 PUR4th 458, 521 (1994) (12.28%); Re Madison Gas & Electric Co., 158 PUR4th 168, 178 (1994) (11.7%); Re Wisconsin Power & Light Co., 158 PUR4th 80, 93 (1994) (11.5%). (PP&L Exceptions at 26-27).

According to PP&L, the principal flaw in the ALJ's analysis rests in his averaging of results. PP&L cites Pa. P.U.C. v. Columbia Gas of Pa., Docket No.. R-891468 (September 20, 1990) (Order, pp. 118-119) ("Columbia 1990") for the proposition that the Commission has properly held in the past, this technique [averaging] only invites abuse. Specifically, PP&L cites Columbia 1990 as follows:

"[c]ost of equity recommendations should be based upon specific market based costs, rather than by a method which averages the recommendations of the various parties."

(Columbia 1990 at 118-119).

Even in the most extreme situation, argues PP&L, the averaging of results is a poor substitute for informed judgment and thoughtful analysis. In this proceeding, asserts PP&L, the use of such an approach is especially egregious. As noted earlier by PP&L, the ALJ chose to average the findings of the OTS, OCA and PPLICA witnesses and, in so doing, gave no weight whatsoever to the evidence submitted by the Company. Consequently, it is the position of PP&L that the Recommended Decision does not act to "decrease expert witness bias", as suggested (R.D., p. 171), but instead tilted the scales decisively toward those who, from the outset, have aggressively opposed PP&L's requested rate increase. (PP&L Exceptions at 30-31).

Moreover, and wholly apart from the issue of witness bias, PP&L argues that the ALJ's averaging of results is at odds with his stated purpose. PP&L notes that at page 163 of the Recommended Decision, the ALJ indicates that he believes barometer group data should be given "slightly less weight" than data for PP&L itself. However, PP&L posits that his use of the midpoint of the average dividend yields proposed by the opposing

party witnesses has exactly the opposite effect. This according to PP&L is because the OCA and PPLICA produced dividend yields for two different barometer groups. Accordingly, PP&L maintains that an average of their respective dividend yield findings accords two-thirds weight to barometer group data and only one-third weight to PP&L data. (PP&L Exceptions at 30).

Compounding this problem, according to PP&L, is the fact that the 7.5% OCA dividend yield set forth on page 164 of the Recommended Decision appears to be the rounded average of the OCA's two barometer group findings and, as such, completely disregards his recommended DCF yield for PP&L. PP&L argues that if only equal weight had been given to the OCA's 8.46% yield for PP&L, the midpoint of the ALJ's dividend yield range would have approximated 7.96%, or 33 basis points higher than his 7.63% recommendation. PP&L contends that if "slightly less weight" were accorded the barometer group data, as the ALJ implies would be appropriate, the figure obviously would be even higher.

PP&L argues further that the final flaw in the ALJ's averaging of results is attributable to the fact that all three opposing party witnesses developed proposed yields for PP&L and PP&L's barometer group. PP&L argues that rather than inputting multiple (i.e. initial and updated) dividend yield values for PP&L and the same group of utilities, the ALJ should have considered only the most current yield data presented by the close of the record as follows:

Baudino Barometer Group (PPLICA St. 8, p. 32)	7.35%
Kahal Barometer Group (OCA St. 1A, Sch. MIK-6, p. 1 Update)	7.41%
Moul Barometer Group (OCA St. 1A, Sch. MIK-4, p. 1 Update)	7.52%

PP&L
(OCA St. 1A, Sch, MIK-7, p. 1 Update) 8.46%

(PP&L Exceptions at 31).

PP&L counters that utilizing the midpoint of the range of values, which also has the effect of giving equal weight to PP&L and barometer group data, produces an unadjusted dividend yield of 7.91%.

PP&L next argues that the ALJ's recommended 3.15% growth rate, which similarly is based on an averaging or midpoint approach, is deficient for many of the same reasons that undermine his dividend yield finding. More importantly, says PP&L, his proposed 10.9% equity allowance, even if achieved, would not generate anything near the level of growth which he concluded investors could reasonably expect.

This is confirmed by the following table, which is comparable in format to that developed by Mr. Moul in his rebuttal testimony (PP&L St. 12-R, p. 6) and reproduced in the PP&L's Initial Brief (p. 229):

Recommended ROE	PP&L Book Value	Earnings Per Share	Amount Retained Per Share	Calculated Growth Rate
10.9%	\$15.79	\$1.72	\$1.67	0.32%

(PP&L Exceptions at 32).

In its Reply Exceptions, the OCA responds to PP&L's Exception wherein PP&L criticizes the ALJ's return on equity recommendation as being "woefully inadequate" and compares it to recent return on equity determinations made by this Commission and Commission's in other jurisdictions. Specifically, the OCA cites the testimony of its witness as follows:

I would note that a recent Edison Electric Institute (EEI) survey finds that electric utility ROE awards for 1994 averaged about 11.5 percent. (See Electric Utility Week, page 11, March 20, 1995.) While this is slightly higher than my present recommendation, capital costs have declined considerably from 1994, particularly compared to late 1994 levels.

OCA St. 1A at 9.

The OCA submits that any comparison to other Commission decisions, including those in other jurisdictions, must also consider the changes in the capital market. (OCA Reply Exceptions at 9).

The OCA addresses the PP&L Exception that the ALJ's recommendation is flawed because his analysis utilized the averaging of results. The OCA notes that PP&L contends that the ALJ's exclusion of the dividend yield data and growth rate supplied by PP&L witness Moul was in error. However, argues the OCA, the exclusion of the particular data because of "quarterly compounding and the ex-dividend adjustment" was appropriate. In addition, the OCA maintains that the ALJ's finding that PP&L's 4.0% growth rate was overstated "by at least 50 basis points" is also supported by the evidence. (OCA Reply Exceptions at 10).

Next the OCA addresses the PP&L Exception wherein PP&L asserts that the data relied upon by the ALJ was biased because it utilized both barometer group and PP&L specific data. PP&L Exc. at 30-31. The OCA submits, however, that PP&L stock is not the only source of data for a DCF analysis. The OCA cites the testimony of its witness as follows:

In conducting a single company DCF analysis, there is always the risk that the historical and market data for that firm may be atypical of what investors could reasonably expect in

the future. Employing a group of firms has the advantage of averaging out the unusually high and low observations.

OCA St. 1 at 24.

The OCA again cites the testimony of its witness as follows:

I believe that proxy groups--if correctly selected--should produce more reliable, stable estimates than single company DCF studies. In addition, it should be noted that PP&L is in the process of reorganizing in order to facilitate investments in non-utility ventures. While this activity is nominal at present, it could become significant in the future.

OCA St. 1 at 35.

Accordingly, the OCA maintains that the ALJ's reliance on the DCF analyses of the proxy groups, as well as for PP&L, produced a reliable DCF result. (OCA Reply Exceptions at 11).

In its Exceptions, the OTS notes that PP&L relied on cost of capital findings in recent Commission decisions. The OTS continues that, aside from the fact that the Commission, on numerous occasions, has chastised parties for comparing the Commission's cost of capital findings in other proceedings, the following is additional evidence as to why the Commission's cost of capital finding in other proceedings is not applicable to the circumstances surrounding PP&L:

The information provided in OTS Surrebuttal Exhibit No. 1, indicates that the 30-year Treasury Bond Yield peaked during the week ending November 11, 1994 at about 8.16[%]. The 30-year Treasury bond when PP&L filed its rebuttal testimony was 7.02%. Therefore, the 30-year Treasury bond yield has declined by 114 basis points.

(OTS Reply Exceptions at 13).

Therefore, the OTS points out that the above passage indicates that the 30-year Treasury bond yield has significantly declined since the Commission made cost of capital findings in the cases cited by PP&L in its Reply Exceptions.

The OTS continues that the Commission is reluctant to compare cost of capital findings in its own cases, and is even more reluctant to compare such findings with those of other jurisdictions. The OTS continued that notably absent from PP&L's comparison list of cost of capital findings from other jurisdictions was Potomac Edison Company, docketed at NO. 94-0027-E-42T, issued March 17, 1995. In that proceeding, the West Virginia Public Service Commission allowed a cost of capital of 10.85% for the Monongahela Power Company. (Id.)

The OTS then addressed PP&L's criticism of the averaging of results. The OTS opined that the ALJ acted reasonably by only considering reasonable numbers.

In its Reply Exceptions, PPLICA argues that the cases cited by PP&L for the proposition that the equity return recommendation in the case is too low, actually confirm the reasonableness of the recommended equity allowance. PPLICA notes that in PAWC, supra, the Commission made a common equity allowance of 11.25%, 35 basis points above the recommended allowance herein. PPLICA notes further that in PAWC, the Commission rejected both the risk premium and CAPM methodologies and relied exclusively on DCF. (PPLICA Reply Exceptions at 2-3). PPLICA notes that in Roaring Creek, supra, the Commission allowed an equity return of 11.0%. (PPLICA Reply Exceptions at 2-3).

PPLICA notes that in West Penn, supra, the Commission approved an equity return allowance of 11.5%. However, PPLICA points out that the 11.5% equity return included an adjustment

for good performance. PPLICA argues that without the performance adjustment, the return in West Penn is comparable to the recommended equity return herein. (PPLICA Exceptions at 3).

Upon our review of the positions of the parties, we agree with the ALJ's decision not to consider PP&L's proposals in his averaging of the parties positions for several reasons. First, we find that the use of "ex-dividend" prices in its computation of the dividend yield serves to unrealistically inflate the dividend yield data. We note that this approach to the dividend yield computation is not regularly used in rate of return proceedings before us.

Second, we believe that the ALJ was correct in rejecting PP&L's proposal to increase the growth rate recommendation by an additional 50 basis points for what PP&L terms "market-wide factors." We find that the evidence of record in the instant proceeding does not support the adjustment proposed by PP&L.

We observe that the dividend yield analysis submitted by the four parties who actively participated in the litigation of the issue of equity return, demonstrates that the dividend yield for the PP&L-specific calculation exceeds the average yield for each of the barometer groups employed by the parties. Further, we note, that the most recent six-month and spot dividends for PP&L exceed 8%. For the different barometer groups, the highest dividend yield is approximately 7.86% unadjusted for growth. We find the PP&L stand-alone position can be used as a check, on the reasonableness of our final recommendation but should not be used as the final determinant of our final allowance. Without endorsing a particular method, we will adopt an unadjusted dividend yield of 7.86%

For the growth rate percentage, we observe that the range of recommendations from the particular parties is from 2.8% to 3.5%. We agree with the ALJ that none of the parties growth rate recommendations are particularly persuasive. We do find that for purposes of a growth rate determination in this proceeding, PP&L's argument cited previously herein, that forecasts suggest that PP&L's growth will lag behind the barometer due to the extended length of time since the Company's last rate case, is supportive of a growth rate determination of 3.5%.

Thus, for purposes of this proceeding we will adopt a dividend yield of 7.66% adjusted for the next period growth of 8.0%. We will adopt a growth rate of 3.5%. The combination of the dividend yield and growth rate result in a DCF-based equity return allowance of 11.5%.

The following table summarizes our equity return conclusions:

<u>Capital Structure</u>	<u>Summary of Recommendation</u>		
	<u>Ratio</u> %	<u>Cost Rate</u> %	<u>Weighted Cost</u> %
Long-Term Debt	46.53	7.97	3.71
Preferred Stock	7.59	7.31	.55
Common Equity	<u>45.88</u>	<u>11.50</u>	<u>5.28</u>
	<u>100.00</u>		<u>9.54</u>

5. RP and CAPM Methods

PP&L was the only party in the matter before us to file an equity return recommendation based upon the RP and CAPM methods. The ALJ did not consider these methods and based his equity return recommendation on his DCF calculation and judgement. (R.D. at 163).

In its Exceptions, PP&L notes that the Commission has in recent years based its rate of return allowances on the DCF method. PP&L urges the Commission to "keep an open mind" on the various methods of calculating an equity return allowance. (PP&L Exceptions at 29). In Reply Exceptions, the OCA and support the ALJ's determination to rely exclusively on the DCF method.

On the basis of the record before us herein, we conclude that there is no reason for us to divert from our practice of considering the DCF method exclusively for equity rate of return determinations. Accordingly, PP&L's Exceptions regarding this issue are denied.

Finally, in its Exceptions, PP&L criticizes the ALJ's determination that managerial performance, and particularly its unparalleled efforts to maintain rate stability over the past ten years, may be ignored because the Company did not include "a quantified request for an equity bonus" in its initial filing (R.D., p. 176). PP&L counters that it has not sought a specific "equity bonus." According to PP&L, it has merely asked that the Commission consider its accomplishments and grant it an equity allowance at the upper end of the zone of reasonableness. PP&L continues that Section 523 of the Public Utility Code does not obligate a utility to quantify a potential "reward". Instead, says PP&L, it directs the Commission to consider evidence regarding "the efficiency, effectiveness and adequacy of service" and to make appropriate rate adjustments in response thereto. PP&L argues that such evidence was presented by PP&L. (PP&L Exceptions at 32).

In its Reply Exceptions, the OCA notes that although PP&L does not ask for a specific "equity bonus," the Company does seek a higher return on equity in recognition of efficient management. The OCA submits that the ALJ's recommendation to reject an "equity bonus" is well supported by the evidence of

record and case law. See generally, Pa. P.U.C. v. Metropolitan Edison Company, 141 PUR 4th 336, 406 (1993) (Performance adjustment denied, no evidence that Company's performance had been exemplary); Pa. P.U.C. v. National Fuel Gas Distribution Corp., 73 Pa. PUC 552, 611-612, 121 PUR4th 434 (1990) (Performance award unwarranted, NFGD is obligated to provide adequate, efficient and reasonable service).

The OCA continued that the ALJ recognized that PP&L had not, prior to its Main Brief, asked for an adjustment related to management performance. The OCA submits that for the reasons discussed above, PP&L is not entitled to receive a "reward" of a 13.00% return on equity for quality of service. (OCA Reply Exceptions at 10).

Upon our consideration of the position of the parties, we find that this discussion deals with what is essentially a non-issue. In our view, the position of PP&L presented in their Exceptions is essentially evidence that PP&L should be given an equity return at or near the top of a reasonable range because of what it perceives to be its excellent management practices. We find this discussion to be moot in this matter because the rate of return allowance does come from the high end of the reasonable range for DCF calculations. Moreover, are of the opinion that we should not consider the RP or CAPM methods to produce a higher rate of return for "good management." Accordingly, PP&L's Exceptions are denied.

IX. RATE STRUCTURE

A. Cost of Service

In this proceeding, PP&L proposed to utilize the 12 coincident peak (12 CP) cost methodology to allocate generating and transmission plant costs. This is, essentially, the same cost allocation proposed in the Company's immediately preceding base rate case. (PP&L Stmt. No. 7, p. 5). This approach assigns production and transmission demand costs on the basis of the average of the twelve monthly coincident class demands occurring at the system average peak. The Company pointed out that the 12 CP method recognizes not only that generating costs are incurred to meet peak demand requirements but also that these demand requirements continue throughout the year.

The Company's cost of service study also accounts for the existence of interruptible load by first allocating costs to the classes having an interruptible option (ISA, LP-4 and LP-5) according to their coincident peak demands, and then providing credit equal to the value of interruptible load on PP&L system. The Company proposed that this value be based on the cost of a peaking unit, a natural gas fired combustion turbine, at \$300/kwh (PP&L St. 9, pp. 13-14; PP&L St. 9-R, pp. 24-25). The Company also proposed that the resulting credit in the amount of \$86 million be subtracted from the cost of generating facilities assigned proportionally to the classes with the interruptible option. (PP&L St. 7, pp. 9-10).

The Company explained that, for a variety of reasons, primarily for economic development reasons and gradualism, it proposed an interruptible credit above the level reflected in the cost of service study. While conceding that its applied value of \$300/kw may overstate the value of the interruptible capacity, the Company emphasized that interruptible load is not as reliable a resource as generating capacity controlled by the Company. The Company added that because it has had adequate generating

capacity, interruptible customers have in fact received service that is essentially firm service. (R.D., pp. 192-193).

With respect to its distribution plant cost allocations, the Company classified its distribution plant investment and operating expenses by means of a minimum size system method calculation. See Ex. JMK-3. Under the Company's proposal, a "minimum size" system capable of providing reliable electrical service to customers is used to identify the applicable customer and demand-related cost components. (PP&L Stmt. 7, p. 11). The Company proposed that this data be used, along with other non-cost factors, to determine an appropriate customer charge. The Company maintained that its approach is supported by the minimum system guidelines of the National Association of Regulatory Utility Commissioners ("NARUC") manual and devised to determine the current cost of its minimum system (PP&L St. 7-R., p. 20).

Several parties objected to the Company's cost of service study and offered alternative methodologies or revisions to the Company's proposal. At page 265 of its Main Brief, the OCA outlined its position with respect to the Company's cost of study as follows:

The OCA recommends three modifications to the Company's class cost of service study. First, the OCA proposes that production and transmission related costs be allocated using the Peak and Average methodology. Second, the OCA proposes that the distribution demand allocators be adjusted to account for the load-carrying capability of the minimum distribution system. Third, the OCA proposes that the value of interruptible credits to other ratepayers in the cost study be the current value of peaking capacity to the system. OCA St. 3 at 4.

In addition, the OCA recommends that the Company's proposed customer charge increase

for Rates RS and RTS be rejected. The Company has not established that an increase in the customer charge is justified. Dr. Johnson has also recommended that the Commission reject PP&L's proposal to increase the number of energy blocks for the residential classes from two to three. The Company has presented no valid reason for this increase in energy blocks.

Lastly, the OCA has recommended that the RTS rate schedule be closed prospectively with current customer locations being grandfathered under the existing rate schedule. Additionally, the OCA recommends that the RTS class be given no greater a percentage increase than the RS class, or in the alternative, the 2.3¢/kwh rate differential that currently exists between the two rate schedules be maintained.

In its cost of service study, the OCA utilized the peak and average methodology. The OCA argued that peak and average methodology properly accounts for the both the energy and demand components of power production investment. (OCA M.B., p. 267). The OCA further asserted that classification of the production and transmission investment should be based upon an understanding of the generation planning process in order to understand the reasons for the incurrence of the capacity costs. The OCA explained that the generation planning process must be reflected to the fullest extent possible in the cost of service study in order to make a determination of the reasonable relationship between cost incurrence and cost responsibility. (OCA M.B., p. 268). In the OCA's view, the peak and average methodology provides a solid balance of both the amount of capacity required to meet system coincident peak requirements and the energy requirements of the classes. (OCA M. B., p. 269).

The OCA also argued that the Company's minimum distribution system study is flawed. The OCA maintained that the Company's method overstates the amount of costs that are

considered to be customer related. The OCA offered an adjustment which, in its view, would reduce the overstatement. The OCA proposed the adoption of its witness Johnson's alternative distribution demand allocator, as reflected in the OCA's cost of service study.

The OCA also challenged the Company's interruptible rate component of its cost of service study. The OCA expressed concern that the value of peaking capacity is relatively low. The OCA proposed that interruptible customers be assigned a portion of the production investment. The OCA attempted to discredit the proposals of PPLICA and Beth Steel regarding the treatment of production investment for interruptible customers, arguing that the arguments are flawed and should be rejected. (R.D., p. 197).

The OCA concluded that its cost of service study which incorporates the peak and average methodology should be utilized as a guide for allocating any revenue increase, or revenue decrease. Additionally, the OCA proposed that the D10 allocator taken from the OCA's cost of service study should be used to allocate the capacity related costs which are demand allocated in the Company's ECR. (OCA M.B., pp. 288-289; See Exh. CEJ-1, Sch. 4).

The PPLICA proposed that the Company's 12 CP coincident peak allocation methodology be utilized, as modified by PPLICA's suggested adjustments, for the purpose of revenue increase allocation. While the PPLICA is of the opinion that a single coincident winter peak is the ideal cost of service study, it would accept the Company's methodology, with certain proposed modifications. The PPLICA offered three specific adjustments to the Company's cost of service study. First, the PPLICA disagreed with the Company's treatment of its interruptible load in its cost of service study. The PPLICA argued that the value of interruptible load as a capacity credit is undervalued in the

Company's cost of service study analysis. The PPLICA argued that the Company's study should include a revenue credit relating to interruptible load which is equal to the revenue credits actually being proposed, as embodied in the rate proposals. The PPLICA also proposed that the cost of paying these revenues credits be allocated to all customers classes, on the basis of the 12 CP production demand allocation factor. This measure, in the PPLICA's view, would remedy the mismatch contained in the Company's analysis.

In addition, the PPLICA proposed to adjust the demand/energy basis for allocation of the NUG output payments in the roll-in of the ECR. The PPLICA pointed out that the Company has included and allocated on a 100% energy basis approximately \$220 million of NUG purchased power expenses in its retail cost of service analysis. The PPLICA argued that in recovering NUG expenses within the ECR on an assigned demand and energy basis, the Company failed to provide a consistent allocation of these expenses relative to the treatment of the revenues associated with the recovery of these costs from customers within the ECR. (PPLICA M.B., p. 50).

The PPLICA proffered that the above cited mismatch could be corrected by adopting the following the adjustment:

An appropriate cost of service study analysis must classify the same portion of NUG expenses as demand related as are classified as demand related by the Company in its ECR revenue analysis contained in Schedule D-3 of this proceeding. PP&L Exhibit Future 1. To correct the Company's cost of service study, the retail portion of NUG purchased power expenses of approximately \$200 million should be classified as 16.38% demand-related and 83.62% energy related. With this adjustment, the allocation of NUG expenses in the cost-of-service study consistent with PP&L's treatment of NUG expenses within its ECR.

PPLICA Statement No, 7, p. 31. Otherwise, in ignoring the demand/energy classification of NUG payments in the cost of service analysis and allocating 100% of the retail NUG payment cost in the rate classes on an energy basis, a greater than proportionate share of NUG expenses are allocated to high load factor customer classes such as Rate Schedule LP-5. Thus, the cost of service assigns revenues associated with NUG payments on a less than proportionate basis, and it results in a lower rate of return on rate base being identified for rate schedule LP-5. In order to produce a reasonable estimate of each class' cost of service, this mismatch must be corrected. Id. at 32. PP&L is in agreement with the need to incorporate this correction. See PP&L Statement No. 7-R, p. 19.

(PPLICA M.B., p. 51).

The PPLICA also proposed an adjustment of the Company's treatment and allocation of Economic Development Initiative ("EDI") and Industrial Development Initiatives ("IDI") revenue credits in the cost of service study. The PPLICA proffered that because the intent of EDI/IDI programs was to benefit to all PP&L customers, a reasonable cost of service treatment of the EDI/IDI credits would assign the cost for those credits to all rate classes, rather than assign the cost of the credits only to the rate classes of the customers receiving the credits. The PPLICA added that the flaw in the Company's allocation of these costs is evidenced by the fact that Rate ISA contains only one customer who is receiving approximately \$872,000.00 in EDI/IDI credits. (PPLICA M.B., p. 53). The PPLICA concluded that its proposal is consistent with the Company's allocation of costs associated with customer assistance programs designed primarily for residential load. (PPLICA M.B. at 54).

Other parties generally supporting the use of the 12 CP method were Beth Steel and the OSBA. The UCC supported the 1 CP

method stating the view that this method was more cost based.
(R.D., pp. 200-203).

In the R.D., ALJ Christianson recommended the adoption of the Company's 12 CP method as the acceptable cost of service study. The ALJ concluded that the 12 CP method is reasonable and represents, as argued by the Company, a middle of the road approach. (R.D., p. 204-205).

On the issue of interruptible service, the ALJ reasoned as follows:

I agree with PP&L that interruptible service does not act like additional generation plant and that we are dealing with a peaking situation when we deal with interruptible load. Moreover, PP&L does not fully control interruptible customers for purposes of load reduction and these customers do enjoy rather good service, especially considering the rather adequate capacity enjoyed by PP&L currently.... For allocation purposes, PP&L appears to do a proper "peak" analysis. PP&L uses a combustion turbine as a measure of cost saved. I agree with that approach. I also tend to agree with OCA criticism and note that OCA seems to fundamentally agree with the PP&L approach. However, I reject the calculation variance offered by OCA.

The PP&L analysis seems to be fundamentally realistic and based on the PP&L system. I also agree with PP&L about its choices, for ratemaking purposes. I view the interruptible customers as members of their normal classes, members who have been, for a few years, given a particular break, based on both the theoretical interruptible considerations and the more practical considerations of meeting competition and industrial development.

I do have one more comment concerning interruptible industrial customers. This relates to the cost of paying the revenue credits associated with interruptible service. PPLICA would allocate these costs

(or, more correctly, revenue shortfalls) to all customer classes, on the basis of the 12 CP production demand allocation factor. It views this adjustment as a correction of the mismatch contained in the Company analysis. PPLICA appears to have additional disagreements with the PP&L analysis but, on this one point, I find myself in agreement with PPLICA. Various programs benefit one class of customers directly, and only the participating customers within that class. However, the theory seems to be that all customers in the system benefit because of sales which would otherwise be lost, or for other similar reasons.

I am talking about such programs as residential conservation programs, commercial and industrial development programs and these interruptible rates. Unless we are dealing with an overtly eleemosynary situation, the theory must be that the program somehow benefits the utility's customers generally. Unless there is some particular reason why benefits are limited only to the particular class in question, normally benefits would be spread over the entire customer base because revenue realized benefits all customers. There is no proper way of distinguishing only those customers who happen to be in the particular class, along with the customer enjoying the direct benefits of the program.

Based on these considerations, I agree with PPLICA. This agreement will be touched on later, in the discussion of rate design. Whatever the cost of service merits of the various parties' arguments, I repeat my view that, for me, interruptible service rate considerations are more a matter of ratemaking than cost of service theory.

(R.D, pp. 206-207)

With respect to the minimum system proposed by the Company, the ALJ accepted the PP&L method as well as the Company approach relating to the CEPFOD argument concerning certain operating and operating and maintenance costs.

In considering the PPLICA's proposed adjustment to the Company's NUG capacity allocation, the ALJ explained:

As PPLICA argues at pages 50-51 of its main brief, PP&L has recognized a demand component for NUG payments, for purposes of the ECR calculation. PPLICA asserts that PP&L is being consistent when it allocates NUG capacity, on a strictly energy basis, for base rate purposes. The PPLICA argument appears to be logical, even though PP&L has stated that its NUG payments are on an energy basis. Clearly, there is some capacity value involved here, for both native load and PJM purposes. I agree with the PPLICA argument and recommend that its energy/demand allocation method be utilized.

(R.D., p. 208)

In addition, the ALJ recommended that we reject the proposal offered by the PPLICA that a new rate category for interruptible industrial customers be created.

The ALJ also recommended that we accept the PPLICA's proposal that EDI/IDI revenue credits be assigned to all customer classes and not just to those rate classes in which customers receiving credits reside. Specifically, the ALJ stated:

On one more issue, I agree with PPLICA. This concerns the EDI/IDI credits, as discussed commencing at page 52 of the PPLICA main brief. Once again, I agree in theory and practice that the program benefits all PP&L customers. I see no good reason to view secondary benefits as limited only to industrial or commercial customers. In fact, no matter what the theory, I agree with the argument that cost of this activity be spread over all customers.

Either they all benefit from the situation or they should all share in the tax to raise revenue for the EDI/IDI program. I also agree with the argument that the broader

spreading of this cost (revenue lack) helps avoid the spreading of the cost on the customer given the cost benefit, or cost break. As PPLICA points out, this situation becomes especially acute with respect to Schedule ISA, which now contains only one customer, Beth Steel.

(R.D., p. 209)

Exceptions to the ALJ's Recommended Decision were filed by the OCA, Bethlehem, the PPLICA, and UCC.

The OCA objects to the ALJ's recommendation arguing that its peak and average method is the proper method to be utilized in this proceeding. The OCA contends that the peak and average methodology is the only methodology proposed in this proceeding that properly recognizes both the amount of capacity required to meet the system peak demands and the energy demands of the class. (OCA Exc., p. 45). The OCA also avers that the importance of these energy demands in classifying and allocating production investment has been recognized by us in previous Commission decisions. The OCA further asserts that its proposed peak and average method was adopted by us in Pennsylvania Public Utility Commission v. West Penn Power, 73 Pa. P.U.C. 454 (1990). The OCA submits that the peak and average method should be adopted as a reasonable and appropriate guide in determining revenue allocation in this proceeding because it reflects the cost responsibility of the classes for the PP&L system. (OCA Exc., p. 46).

The OCA also challenges the ALJ's recommendation that the Company's minimum system study be adopted. The OCA is of the opinion that the Company's method overstates the amount of costs that are considered to be customer related. The OCA submits that its proposed adjustment to the Company's minimum system study as reflected in Dr. Johnson's cost of service study reduces the

Company's overstatement. The OCA summates that its proposal to adjust the demand allocator to account for the load carrying capability of the system so that the customer related component could be more accurately identified is reasonable and should be adopted. (OCA Exc., p. 48).

The UCC urges us to reject the ALJ's recommendation to adopt the Company's 12 CP method arguing that the 1 CP method, advanced by its witness, accurately reflects the cost of service responsibility (UCC Exc., p. 5). The UCC further asserts that the ALJ's reliance on PP&L's argument regarding the impact of off-peak scheduled maintenance on its available capacity is unsupported in the record. The UCC also argues that maximum capacity requirement occurs more in the winter peak period than it does during spring or fall months. (UCC Exc., p. 9-10).

Beth Steel excepted to the ALJ's recommendation to accept the Company's allocation of generation costs to interruptible customers and the Company's adjustment to rate base to reflect the value of interruptible load. (Beth Steel Exc., p. 3). Beth Steel reiterates the position as stated in its Main Brief that because the Company does not plan generation facilities to serve its interruptible load and that load does not cause the Company to incur any generation-related capital costs, it is inappropriate to assign capacity costs to the interruptible load customers. (Beth Steel Exc., p. 3).

In its Exceptions, the PPLICA questions the ALJ's recommendation to accept the Company's \$3.00/kw per month "value" for interruptible load for cost of service study. The PPLICA points out that while it opposed the Company's "resource value approach" for rate design purposes, it maintained that if the approach was deemed appropriate for cost of service study purposes, the \$3.00/kw per month credit utilized by the Company was an understatement which should be adjusted. The PPLICA adds

that it proposed that the \$6.00 and \$8.00/kW credits proposed by PP&L in its rate design for interruptible customers should be reflected in the Company's cost of service study. The PPLICA submits that the Company's cost of service study should be further adjusted to reflect an interruptible credit of \$6.00/kW (two hour notice interruptible load) and \$8.00/kW (30 minute notice interruptible load). The PPLICA concludes that the ALJ erred in approving the Company's cost of service study without recommending the implementation of the aforementioned adjustment which reflects the true value of interruptible load as proposed by the Company in its rate design. (PPLICA Exc., p. 22).

On consideration of the positions of the parties, we shall adopt the ALJ recommendation to use the Company's 12 CP method as the basic cost of service model herein. This method has served to accurately reflect the allocation of generation and transmission costs for PP&L. However, we find the modifications to PP&L's cost of service study as advocated by PPLICA to be persuasive for purposes of the revenue increase allocation. We shall adopt the PPLICA recommendations to the extent delineated, below, in the body of this Opinion and Order.

The ALJ's recommendation concerning issues relating to the Company's NUG capacity allocation³⁰ and the Company's minimum system study are adopted and PP&L is so directed to implement these revisions. We do not, however, adopt the ALJ's recommendation to accept PPLICA's EDI/IDI credit proposal.³¹

³⁰ We note that the Company recommended an adjustment in its final accounting exhibits to exclude from the ECR revenue adjustment credit on line 4 of pages 83-84 of Ex. JMK-2 the effect of the NUG output payment demand/energy allocation. (PP&L M.B., p 247; PP&L St. 7-R, p. 19).

³¹ See discussion on Economic Development Credits, Section IX, H, infra.

Accordingly, the respective Exceptions of the OCA, the UCC, PPLICA and Beth Steel are granted and denied consistent with our following determinations.

Finally, we observe that PPLICA proposed a rate design which would treat the LP-5 and LP-6 interruptible customers as a separate class. (See PPLICA Exc., p. 7 citing PPLICA Stmt. No. 7, pp. 59-64). Its arguments supportive of this position are that: (a) such customers receive a service that is decidedly inferior in quality as a result of the prospect of interruptibility; and (b) as a result of a customers' selection of interruptible service, explicit demand/energy charges are imposed which differ from the LP-5 firm demand and energy charge; therefore, the Company's existing rate design implicitly recognizes that interruptible customers are a separate class. (PPLICA Exc., p. 8).

Again, we find the PPLICA position that the interruptible customers be treated as a separate class to be persuasive.

B. Revenue Distribution

The Commission here faces the task of deciding, based on the major customer classes, how to distribute the revenue increase we approve today. One approach is to impose an across-the-board similar to that in the PP&L case involving the Susquehanna 1 plant. Another approach would be to utilize the cost-of-service study. The standard approach is a mix of these two with a view to avoiding major impacts on customer classes via the practice of gradualism. (R.D., p. 210).

There is considerable interest given to the distribution problem in this proceeding. The parties addressed

the matter in differing degrees although only the OTS opted to not specifically address this problem by submitting a recommendation on off-peak treatment for rate schedule SE, street lighting. (R.D., p. 211).

The question of distributing a reduced increase (below the increase requested by the company) is always a difficult question. The usual practice is to allow the different classes different rates of return under existing rates with the basic goal of moving all classes toward the same overall rate of return. Few parties differ over this basic goal but many recommendations are provided concerning limitations on movement toward system rate of return, often based on concerns about gradualism, and avoiding too great an increase, or even decrease, to a particular class of customers. (R.D., pp. 211-212).

Beth Steel provides a detailed and strenuous defense of its ISA contract and rate. Beth Steel claims that it is responding to results produced by the PPLICA development. Before reaching the difference of opinion with PPLICA, Beth Steel refers to the PPLICA main brief, at pages 2-3 of the Beth Steel reply brief. Beth Steel endorses the views set forth in the preamble to the main brief of PPLICA. In particular, Beth Steel concurs with the PPLICA sentiment regarding the competitive arena in which all companies operate today. (R.D., p. 213).

PPLICA's main focus is on the competitive problems of business customers and related considerations. PPLICA's members are PP&L's larger customers whose competitive vitality is critical to the health of the local and state economies. PPLICA is of the view that PP&L is attempting to gain what revenues they can under the existing "monopoly" regulatory model before competition makes such revenue difficult or impossible to secure. PPLICA references the overall increase sought by PP&L and

indicates its opposition, for various reasons, to these elements of the overall increase. (R.D., p. 213).

PPLICA also takes considerable exception to some of PP&L's revenue elements. One of these is interruptible power. After noting that the interruptible service rate would even increase 22 percent if there is no overall increase, PPLICA views any other proposed results to be extreme and argues against them. (R.D., p. 214). Another variable to PPLICA is real world considerations, as opposed to theoretical concerns, as reflected in the cost-of-service studies. PPLICA raises what it views as broad philosophical concerns, as opposed to detailed ratemaking choices, in the proceeding. (R.D., pp. 214-215).

PPLICA rate increase allocation by proposing a 50 percent reduction in existing subsidies for each rate class provided that no rate schedule receives an increase in excess of 1.5 times the average increase. PPLICA proposes this approach as a systematic movement toward cost of service-based rates consistent with the gradualism principle. PPLICA also notes that their proposal for rate schedule increases capped at 1.5 times the average increase is consistent with PP&L's proposal. (R.D., pp. 217-218).

However, PPLICA also opposes PP&L's rate increase -- in particular that of the interruptible customers of rate schedules LP-4 and LP-5. PPLICA claims that such an increase i.e., nearly three times the system average, would result in a 22% rate increase for those large customers even if there is no overall increase in this proceeding. (R.D., pp. 218-219).

PPLICA next discusses competitive trends and gradualism, with a particular emphasis on jobs, and rejects any comparison with PP&L's rates prior to 1992. PPLICA claims that PP&L's proposal fails to move toward an average rate of return

for all classes and claims that every party has sought to minimize their own rates at the expense of other types of customers. (R.D., pp. 218-219).

PP&L also claims that the parties have provided sharply contrasting proposals for allocation of the increase among the various rate classes. PP&L then invokes gradualism and the basic principles of moving all classes closer to system average return, limiting increases to one and a half times the system average increase, and allocating some rate increase to all classes to correct what PP&L views as the overstated discount in rate design for interruptible customers. (R.D., p. 215).

PP&L opposes the positions of other parties on the ground that their positions will shift substantial costs to one class or another. PP&L gives various examples of the impact of the parties' positions although those results would vary depending on the cost of service study. PP&L alternatively seeks a proportional setback or scaleback in the event the proposed increases are reduced by the Commission. (R.D., pp. 215-216).

The OTS does not devote particular sections of its briefs to this topic although OTS does discuss various rate design issues. The OCA provides a table comparing rates of return of major classes and generally agrees with PP&L's attempt to move each class closer to the system average. The OCA notes, however, that it uses a different cost of service study which starts with different rates of return at present rates. The OCA would restrict the increase to any one class to 1.33 times the overall increase. (R.D., pp. 216-217).

After this, there follows a discussion of the RTS problem. The OCA would resolve the problem with a proposed revenue allocation for RTS and RS equal to the system average increase. The OCA supports a 16 percent increase for the ISA

class and notes PPLICA's support for that approach. (R.D., p. 216).

In the alternative, the OCA proposes a lesser overall increase spread in proportion to the increase in total revenues consistent with the OCA's general recommendation. The OCA would give first priority to a reduced revenue from the classes with the highest current rates of return. The OCA views the ISA class situation as one not approved by the Commission as just and reasonable given the 1989 Commission Order and a recent 1990 Roaring Creek decision. The OCA then criticizes the allocations of other parties. The OCA claims that OSBA's proposal for the ISA class is not reasonable nor is PP&L's proposal to hold down their rates supported by the record. (R.D., pp. 216-217).

The OSBA views small business rates as historically high, very much above their cost of service. The OSBA views PP&L's proposals as resulting in improved relative rates of return for the GS-1 and GS-3 classes. The OSBA firmly believes that their cost of service would support substantial decreases for GS-1 customers and minimal increases for GS-3 customers consistent with the gradualism principle. The OSBA fails to present an alternative distribution proposal but notes that GS-1 rates are far out of line and suggests an automatic adjustment mechanism for reducing rates each year. (R.D., pp. 219-220).

The OSBA resumes with a critical review of the OCA and PPLICA proposals with details on the resulting rate shifts and increases. The OSBA's focus on GS customers results in considerable disagreement with OCA but less disagreement with PPLICA. (R.D., pp. 219-220).

The OSBA next discusses the problem of allocating a reduced revenue deficiency. The OSBA, after noting that a proportional scaleback is the traditional method of managing

reduced revenue increases, opts for a weighted method as a means of moving the rate classes closer to cost-base rates. The OSBA has an interesting automatic rate reduction proposal although that departs from traditional ratemaking. (R.D., pp. 221).

The DOD then discusses cost of service and revenue allocation. The DOD, after considering the potential for discrimination, argues for a separate industrial interruptible rate class. The DOD supports PP&L's proposal in that regard but takes no position relating to CEPFOD's arguments on RS and RTS rates. However, the DOD supports moving toward an overall rate of return using the gradualism principle. (R.D., p. 221).

The U/CC discusses this topic under the heading of interclass subsidies and concludes that subsidies for residential are already too high and that PP&L's proposed revenue distribution only aggravates the problem. The USS proposes a reduction in interclass subsidies by limiting the range to three times the relationship between any class increase and the overall increase. (R.D., pp. 222-223).

Beth Steel addresses the revenue allocation for LP-4 and LP-5 interruptible customers and the increase for rate schedule ISA. Beth Steel views the interruptible increase as inconsistent with cost of service studies and competitive conditions. Beth Steel claims that the LP-4 and LP-5 classes are showing above average rate of return and suggest that this should result in a lesser increase in the interruptible rates or, in the alternative, rates that are not competitive. (R.D., pp. 222-234).

Beth Steel then addresses the interruptible service problem given PP&L's proposal for interruptible service. Beth Steel urges the Commission to reject PP&L's proposal or, in the alternative, to develop an interruptible tariff to avoid the

problem of creating an inferior interruptible service within the LP-5 and LP-6 categories. (R.D., pp. 222-234).

CEPFOD provides some contributions to allocation discussion although its main focus is on rate schedule RTS. It also provides some input relating to schedule RS although consideration of their issues are deferred until rate design is discussed below. (R.D., pp. 224-225).

The ALJ, after a considerable commentary on the problems of utility regulation in light of the OSBA's innovative proposal, opted for PP&L's general proposal with some modifications based on the cost of service study consistent with the principle of gradualism. In the alternative, the ALJ recommended that the Commission consider the OSBA's proposal to proportionally allocate any less-than-requested increase approved by the Commission. (R.D., pp. 225-227).

PP&L supports the ALJ's adoption, with some minor changes, of their cost of service study and rate design proposals. PP&L claims that the opposing parties take issue with many of those findings in order to secure beneficial results for their rate class by imposing substantial costs on other parties. PP&L alleges that the ALJ properly recognized that PP&L's proposals steer a reasonable, middle course among the competing rate classes. PP&L urges the Commission to adopt the ALJ's findings in that regard and endorse the reasoned and well-balanced resolution. (PP&L R. Exc., pp. 32-33).

The OCA excepts to the ALJ's recommendations. (Exc., pp. 48-49; OCA R. Exc., pp. 26-27). The OCA claims that the ALJ failed to provide a specific revenue distribution but, instead, apparently opted for PP&L's proposal with some modifications. The OCA also claims that the ALJ's acceptance of the OCA's proposal for their RTS class will change PP&L's proposal for that class. The OCA particularly notes that the increase for the RTS rate class under PP&L's proposal will be substantially the same as increase for the RS rate class. The OCA believes their proposal is more reasonable. That is because there would only be an increase of between 5.93% and 15.56%, with most increases around 11% to 11.7%, or near the system average even if the entire rate increase were adopted. (OCA Exc., pp. 48-49 citing OCA M.B., p. 291).

The OCA also comments on the OSBA's proposal to reduce GS rates. The OCA opposes that idea and urges the Commission to adopt proportional scaleback.³² The OCA is concerned that the OSBA's proposal, which appears to utilize the subtraction methodology of a "constant differential," will result in decreases for some classes i.e., the GS classes, while other classes i.e., the residential classes, will experience above-average increases. The OCA claims that this subtraction methodology, as opposed to the traditional multiplication methodology of proportional scaleback, distorts the relationship to the system average increase, violates the principle of gradualism, and results in disproportionate increases for some classes -- particularly the residential class.

The OCA's Reply Exceptions expand on that claim. The OCA claims that their review of Appendix A to the OSBA's

³² Under a proportional scaleback, if the Company received one-half of its request, then each class' increase would be cut in half.

Exceptions, which presents an example of the scaleback methods, demonstrates that the proposal distorts relationships to the system average with disproportionate increases.³³ In particular, the OCA claims that the preference for a relatively uniform system average rate of increase for some classes i.e., the GS classes, is being accomplished, at the cost of other rate design principles such as rate continuity and gradualism for other classes i.e., the residential classes. (OCA R. Exc., pp. 26-27).

The OCA concludes that it is simply unfair to displace the principles of rate continuity and gradualism with system average rate increases given the disproportionate results. The OCA urges the Commission to utilize a proportional scaleback. (OCA Exc., pp. 48-49; OCA R. Exc., pp. 26-27).

The OSBA supports PP&L's conceptual approach for several reasons. First, the OSBA claims that the Company's approach attempts to address the fact that the Company's business customers, in particular those paying GS-1 and GS-3 rates, are paying substantially higher electric rates than warranted by their cost of service. The OSBA cites the GS-1 rate class return, which is nearly twice the system average, as proof of that fact. The OSBA also cites the GS-3 rate class return, which is roughly 1.36 times the system average and the second highest return of the major classes, as further proof of that fact. (OSBA R. Exc., pp. 5-8 citing OSBA M.B., pp. 13-14). The OSBA further cites the Company's November 1994 report of PP&L's Social

³³ For example, the Company had proposed that the RS class be capped to effect the principle of gradualism. As shown on OSBA Appendix A, the RS class would have received an increase 1.3 times the system average under the Company's original proposal. Looking at Appendix A, however, one can see that under the constant differential method, the RS class receives an increase that is 2.34 times the system average increase, while under the weighted method, the increase is 1.57 times. On the other hand, under both of the OSBA's methods, the GS-1 class receives a rate reduction while the residential classes receive significant rate increases.

Initiatives Task Force to support that fact. The report concludes as follows:

The small business customer (e.g., mom-and-pop stores) is the forgotten customer at PP&L. There are nearly 120,000 small general service customers, and as a group, they pay the highest electric rates. In addition, they receive the least amount of customer service and support from the company. These customers often play a role in maintaining the viability of the neighborhoods where they are located.

(OSBA R. Exc., p. 6 citing OTS Cross Examination Exhibit No. 16, Attachment 1, page 10).

The OSBA concludes that the Company's conceptual approach is warranted because it begins to address the historic problem of rate disparity vis a vis the business customer in utility rate policy. (OSBA R. Exc., p. 6).

However, the OSBA excepts to the ALJ's use of the "traditional scaleback approach" if the overall increase is below the one sought. (OSBA Exc., p. 3 citing R.D., p. 226). The OSBA claims that the ALJ's recommended adoption of the weighted scaleback approach for small increases and calls for improved scalebacks with any level of increase should be extended to use of a weighted scaleback for higher revenue awards. (OSBA Exc., pp. 3-4 citing R.D., p. 226).

The OSBA believes the ALJ's concern with any disproportionate rate impacts, resulting from the OSBA's weighted scaleback approach, is ameliorated by their witness' testimony that use of the OSBA's methodology at varying levels of rate relief can mitigate that result. (OSBA Exc., p. 4 citing Robert D. Knecht and OSBA Exhibit 4). The OSBA's proposal evaluates the rate increase using the proportional scaleback and the constant

differential scaleback³⁴ which are then combined to produce a weighted average of the two methods. (OSBA Exc., pp. 4-5 citing OSBA Main Brief, pp. 23-28). Of course, the relative impact of the two different methods depends largely upon the final increase. (OSBA Exc., p. 4-5 citing OSBA Stmt. No. 1 at 11; OSBA Stmt. No. R1, pp. 30-32).³⁵ The OSBA claims that this weighted scaleback approach provides greater progress toward cost-based rates than PP&L's proportional scaleback method.³⁶ (OSBA Exc., p. 5 citing OSBA Stmt. No. 1, p. 9).

The OSBA's Appendix A in its Exceptions provide us with more detail on their weighted scaleback approach. The OSBA claims that their comparison table shows the actual dollar and percentage increases that result from use of the proportional scaleback, constant differential scaleback and weighted scaleback approaches with a revenue deficiency of \$61.744 million. (OSBA Exc., pp. 6-8).

The OSBA used the method and formulae thoroughly described in Mr. Knecht's direct and rebuttal testimony. (OSBA Exc., p. 5 citing OSBA Stmt. No. 1, pp. 11-12; OSBA Exhibit 4; OSBA Stmt. No. R1, pp. 30-32). In particular, the OSBA notes

³⁴ The constant differential method is described in the OSBA's Main Brief at 22-23, with reference to OSBA Stmt. No. 1 at 9. Under that approach, the difference between the class increase and the system increase in the approved revenue allocation is maintained at whatever increase is ultimately adopted.

³⁵ In the case of an increase on the order of the ALJ's recommendation, substantially more weight (75%) is afforded the results of a proportional scaleback, with less weight (25%) being given to the results of the constant differential scaleback. (OSBA Exc., p. 8).

³⁶ As explained by the OSBA's witness, "the constant differential method produces progress toward cost-based rates that is more similar to the original proposal than the proportional scaleback approach." (OSBA Exc., pp. 4-5 citing OSBA Stmt. No. 1, p. 9).

that Exhibit 4 of their witness' testimony furnishes the same information for hypothetical revenue deficiencies of \$64.5 million, \$129 million and \$193.5 million. (OSBA Exc., p. 5 citing OSBA Stmt. No. 1).³⁷

The OSBA notes that there would be a minimal reduction of .7% in the GS-1 revenues using the weighted scaleback approach. The OSBA claims that PP&L's cost of service study, which shows that the GS-1 class is contributing twice the system average at present rates, and the ALJ's rejection of the OSBA's proposal, which calls for an annual automatic adjustment mechanism for the GS-1 class, support such a modest decrease in GS-1 rates. (OSBA Exc., p. 6 citing PP&L Exhibit ODK-3 and R.D., p. 261).³⁸ The OSBA claims that the weighted scaleback approach is better than the proportional scaleback because it makes greater progress toward cost-based rates by decreasing the contribution of those classes whose rate of return contribution is greater than those classes whose rate of return contribution is lesser. (OSBA Exc., p. 7).

³⁷ For example, Appendix A shows a \$61.744 million revenue deficiency. This would result in an increase of 3.4% to the Residential class using proportional scaleback, an increase of 6.1% if the constant differential scaleback is employed. Using weighted scaleback, however, the Residential class is 4.1%. For a GS-3 customer, the proportional scaleback increase is 1.5%, a negative 2.4% using the constant differential scaleback, and a .5% increase using weighted scaleback. (OSBA Exc., p. 8 citing Appendix A).

³⁸ For example, if the Commission were to award PP&L one-half of its requested revenue increase, the Residential increase would be 7.6% using a proportional scaleback, but would be 8.5% if a weighted scaleback were employed. By contrast, the GS-3 class would experience a 3.4% increase using proportional scaleback and a 2.1% increase using weighted scaleback. At a rate level granting PP&L one-half of their requested rate relief, the GS-1 rates would increase by 1.9% under proportional scaleback and would remain unchanged using a weighted scaleback approach. (OSBA Exc., p. 8 citing OSBA Exhibit 4).

Finally, the OSBA claims that the OCA's proposed revenue distribution would result in a significant shifting of revenue responsibility from the residential class to the Company's small business classes. In view of the facts that PP&L's small businesses are already providing substantial subsidies to the residential customers and have been recently identified by the Company's internal task force as the "forgotten customer at PP&L," the OSBA claims that such a shift is unreasonably and unfairly perpetuating the existing imbalances in PP&L's rate structure. (OSBA R. Exc., pp. 6-7 citing OSBA M.B., pp. 17-19).

The OSBA concludes that the hypothetical examples using weighted scaleback, which vary depending upon the revenue deficiency ultimately determined by the Commission, establish that their approach imposes no unusual increases on any customer class. The OSBA urges the Commission to direct PP&L to implement their weighted scaleback approach depending on the level of rate relief ultimately determined in this proceeding. (OSBA R. Exc., pp. 8-9).

PPLICA claims that the ALJ erred in failing to adjust the recommended increase in operating revenues to reflect any actual increase in annual operating revenues requested by PP&L. (PPLICA Ex., pp. 24-26; PP&L R. Exc., pp. 25-26). PPLICA points out that PP&L agreed to offset their proposed \$261 million rate increase to reflect a credit of \$21 million in revenues for off-system sales provided PP&L were permitted to recover the costs for these off-system sales. (PPLICA Ex., p. 24). However, PPLICA points out that the off-system sales revenue should be reflected in the ALJ's calculations for PP&L's overall rate increase even though the ALJ has recommended against recovery of the costs for those sales. (PPLICA Ex., pp. 24-25).

PPLICA urges the Commission amend the ALJ's Recommended Decision concerning "pro forma present rates" to reflect the ALJ's approval of PP&L's alternative proposal at page 275 of the R.D. (PPLICA Exc., p. 26).

PPLICA also urges the Commission to allocate their ultimate revenue deficiency determination consistent with PPLICA's proposals to limit increases to the interruptible class to 1.5 times the system and limit interclass subsidies to 50%. (PPLICA R. Exc., p. 25). Finally, PPLICA argues against the OSBA's proposal for weighted scaleback in favor of traditional scaleback because it, unlike the OSBA's proposal, better achieves removal of interclass subsidy consistent with the principle of gradualism. (PPLICA R. Exc., p. 26).

U/CC excepts to the ALJ's attempts to reduce interclass subsidization. (U/CC Exc., pp. 11-15). U/CC excepts to current business class subsidies which U/CC claims amount to \$227.5 million per year from the GS-1, GS-3, LP-4 and LP-5 classes and which U/CC claims constitute almost 88.2% of PP&L's jurisdictional increase or about 18.2 cents per dollar paid by these classes. U/CC claims that PP&L's proposed revenue allocation based on rates of return has the perverse effect of moving rates further away from costs and exacerbating interclass subsidies. (U/CC Exc., pp. 12-14).

U/CC urges the Commission to reduce subsidies by 50% although limit the resulting increases to no more than 300% of PP&L's overall jurisdictional increase of 11.7%. U/CC also urges the Commission to reduce subsidies by a uniform percentage and to keep the Rate ISA as it exists because of the special nature of the underlying contract. (U/CC Exc., pp. 13-14).

On consideration of this issue, we shall affirm the ALJ's recommendation with the proviso that the position of

PPLICA, (and Beth Steel to the extent consistent) that the increase to the interruptible class be limited to 1.5 times the system average and limit interclass subsidies to 50% is granted. (See R.D., pp. 225-228). In particular, we agree with the ALJ that the complexity of the issue and avoidance of unintended results from novel innovations support use of a safe, as opposed to innovative, approach. We conclude that the ALJ's use of the straight scaleback as capped by the PPLICA proposal is in the public interest because it does move the rate classes closer toward the established overall rate of return than would otherwise be the case with novel innovations. While we recognize the possibility that movement of all classes toward a uniform rate of return contribution could have adverse consequence as proposed by U/CC, our review of the record in light of the impending changes in the electric industry caution for a more traditional approach at this time.

C. Rate Schedule RS

PP&L proposes an RS customer charge of \$7.20, a 50 percent increase over the present charge. It states that its cost study shows the relevant cost as \$17.51 per customer per month. It also refers to billing and metering costs per customer as \$10.18 per month. It considers this charge it proposes to be a reasonable balance. It mentions that the increase is only \$2.40 which, in the PP&L view, would not impose undue hardships on rate RS customers, particularly since costs shifted from the customer charge should be recovered in the first billing block of usage charges. (R.D., pp. 227-228). PP&L points out that the customer charge was set at \$4.80 over 10 years ago and argues that it is now outdated. It refers to other proposals concerning this charge. It notes that OTS proposed an increase of \$1.10 and that CEPFOD proposed a similar increase. PP&L notes the OCA's opposition. (R.D., pp. 227-231).

PP&L defends its third billing block for rate schedule RS. It states that it has sought to ensure a more equitable recovery of both unrecovered customer-related costs and demand-related costs in the early blocks of the rate, rather than the trailing block. PP&L notes CEPFOD's and OCA's opposition.

The OTS addresses the residential customer charge. It reviews the background and provides its recommendation of an increase of \$1.10, to \$5.90 per month, at the overall requested increase. The OTS views their approach as consistent with Pennsylvania practice and reviews the support for their claim before concluding that a much lower increase is warranted. The OTS continues by addressing various other PP&L positions in support. OTS suggests that even a \$2.40 per month increase could be a hardship. (R.D., pp. 227-229).

The OCA discusses both the RS charge and the RTS customer charge of \$15 per month. The OCA claims that PP&L has failed to justify these substantial increases. The OCA associates these charges with metering and billing costs. The OCA suggests that PP&L is seeking to recover more than this amount. It suggests that PP&L cost figures include too much and should be reduced. It finds a basic cost of \$4.73 monthly. It also finds an RTS cost below the current charge. (R.D., pp. 227-229).

The Sierra Club next addresses the residential customer charge. Sierra Club discusses the charge in connection with monopolistic services and apparently supports a charge based on one's level of consumption. (R.D., pp. 227-229).

PP&L responds to the parties' positions. PP&L cursorily discussed the Sierra Club position in a footnote at page 109. PP&L views the OCA's position as one pertaining largely to basic customer costs.

The ALJ viewed the proposed customer charges as supported by cost studies and as reasonable -- at least in theory. The ALJ recommended limiting the increase to 35 percent and PP&L's third block proposal. The ALJ did so because the increase is based on the inflation rate over the past 10 years which, if accepted as recommended, would be approximately three times PP&L's proposed overall increase. The ALJ did not recommend such a limitation on the RTS customer charge which, as indicated below, is much more modest. (R.D., pp. 230-231).

PP&L supports the ALJ's recommendation for a 35% increase but further opposes the ALJ's recommendation that the change be scaled back to reflect any lesser increase. (PP&L Exc., pp. 57-58; PP&L R. Exc., pp. 35-36). The OCA opposes the recommendation on the ground that the current customer charge should remain at the current levels and that the third block declining rate should be rejected. (OCA Exc., pp. 50-53; OCA R. Exc., p. 24). Sierra Club vigorously objects to the recommendation on the ground that increasing the customer charge while decreasing the third block charge will send customers the wrong message on energy conservation. (Sierra Club Exc., pp. 30-33). CEPFOD argues that the ALJ's recommendation on a third block is unjustified and the OTS recommends denial of Respondent's exceptions. (CEPFOD Exc., pp. 3-7; OTS R. Exc., p. 39).

After careful deliberation on the issue, we believe that a 35% increase in the customer charge is appropriate. We also believe that a declining rate third block charge is appropriate as recommended by the ALJ. We do so because the customer charge is approximately that of the inflation rate over the past ten years and, as such, represents an attempt to move class charges closer together consistent with the principles of gradualism and rate continuity. Furthermore, we also conclude that the third block rate is appropriate because imposition of

charges for such a block makes customers aware of their increased consumption even if that consumption rate may be priced at a lesser rate.

D. Rate Schedule RTS

PP&L's position is that this rate schedule is only available to customers who install certain electric thermal storage systems equipped with timing devices that permit PP&L to pre-set the time during which electric heat and/or hot water heating occurs. This rate, in comparison to rate schedule RS, has a lower per kwh charge in a single billing block, a higher monthly demand rate and additional demand charges for usage over 2 kw during peak periods. PP&L makes the following claim in that regard:

Rate Schedule RTS was developed as a load management tool during the early 1980s, when the Company sought to reduce peak load growth. The thermal storage technology offered the opportunity to shift heating load from the peak period of the day through the use of timing devices. Thermal storage provided significant advantages over other load management tools (PP&L St. 8-R, pp. 13-15). In particular, the Company's peak load growth in the mid- to late-1970s and early 1980s displayed a growing morning peak problem. Thermal storage would allow the Company to shift heating load to the evening, alleviating the morning peak

(R.D., pp. 231 to 241 citing PP&L St. 6-R, pp. 10-11; Exh. JJS-10 and JJS-11; Tr. 2123).

PP&L notes that Rate Schedule RTS was introduced in 1984 and attracted approximately 14,000 customers by early 1995. By the late 1980s, the Company became aware that a general shift in peak usage towards the evening by non-RTS customers would, over the long term (after 1995), create an evening peak on PP&L's system, which would reduce the benefits of the RTS rate. (R.D., pp. 231-241 citing PP&L St. 6-R, pp. 3-7). Consequently, the

Company began phasing out advertising promotions and grants for thermal storage customers in 1991 and by 1995 it had entirely discontinued them. As a result, fewer and fewer customers have subscribed to the RTS service in recent years: 806 in 1993, 549 in 1994, and only 145 in the first quarter of 1995. (R.D., pp. 231-241 citing PP&L St. 6-R, p. 8; Ex. JJS-9). PP&L also commenced a pilot program to study the effect and feasibility of installing direct dispatch controls on RTS units, permitting the Company to use real-time pricing and improve the relative revenue contribution from RTS units. (R.D., pp. 231-241 citing Tr. 723-27; PP&L St. 8-R, pp. 17-18).

PP&L proposes to modify the rate schedule by accepting new customers only until December 31, 1995, (2) thereafter allowing eligible persons to use the new rate schedule to incorporate newer technology and appropriate terms, conditions and rates, (3) providing service to existing RTS locations through the life of the existing thermal storage units, and (4) proposing no reduction in the existing 2.3¢ per kilowatt hour differential between RTS and RS customers before December 31, 1999. (R.D., p. 232).

PP&L claims that this proposal is broadly similar to the OCA's and was favorably received by the OCA's witness. PP&L claims the proposal is based on changing load patterns and changes in technology. PP&L views the proposal as a good balance of all customer interests, despite the RTS low rate of return, and concludes that no investigation is warranted. PP&L notes that the RTS rate does contribute to fixed cost and does improve the Company peak load profile even though the negative return of the RTS class on a fully-allocated basis is a matter of concern for PP&L. (R.D., pp. 232-234).

PP&L's dismisses most of CEPFOD's claims as irrelevant to the issue. PP&L claims that RTS was a load management tool,

that it did have some success, and that RTS helps achieve important load management objectives. PP&L further claims that the program's failure was not discerned until 1987 and denies that it ignored the problem until today. (R.D., pp. 239-240).

The OTS' position, described through their witness, is that any increase must first be recovered from the RTS rate class. The OTS also proposes an investigation of the RTS rate schedule -- partly from the concern that some customers were induced to go to this service with overly optimistic promises. (R.D., p. 234).

The OCA has significant concerns about this RTS rate schedule. The OCA is concerned that the cost study shows a negative rate of return for this class and that PP&L has proposed a 17.39 percent increase for these customers. The OCA is concerned that this is higher than the increase proposed for RS customers. The OCA further points out that some RTS customers may experience an improper increase under the circumstances. (R.D., pp. 234-236).

The OCA further points out that this rate did not produce the results intended by PP&L. OCA would not unduly emphasize the cost of service results, considering the nature of this service. It proposes modifications, providing details. The OCA comments favorably on the fact that PP&L has since adopted many of the OCA's recommendations. (R.D., p. 235).

The OCA discusses two further points of disagreement. First, the OCA declines to endorse a date certain for terminating entry i.e., December 31, 1999. Second, the OCA disagrees with a closing date. The OCA prefers to have the rate close with the issuance of the Commission Order. PP&L seeks some time for customer response. It states that, in the alternative, PP&L be directed to fully inform applicants of the conditions relating to

this rate, prior to their signing up for service. The OCA disagrees with the CEPFOD proposals and views them as unduly burdensome. (R.D., pp. 234-236).

CEPFOD also has a position with regard to residential rate design. CEPFOD's primary recommendation is to abolish the RTS rate and to require credits by PP&L to RTS ratepayers. CEPFOD views the matter as blatantly market expansive by providing these high user customers with relatively cheap electric service. (R.D., pp. 236-239).

CEPFOD further claims that PP&L is seeking to maximize sales. CEPFOD details alleged promotional efforts and massive subsidies before suggesting that PP&L be prohibited from harming current ratepayers to compensate for their policy miscalculations. CEPFOD claims that it has been unfairly hurt by subsidization and that PP&L has long been aware of the peaking problem. (R.D., pp. 237-239).

CEPFOD reviews the positions taken by the parties, including its own positions. It suggests that PP&L should not be rewarded for its imprudence, by allowing it to shift the RTS subsidy to other customers. It characterizes its position as being based on several undisputed facts. It first states that PP&L knew that the RTS rate was a load management failure during 1987. It further asserts that rate RTS is a subsidized service. It states that rate RTS increases the evening peak for PP&L. (R.D., pp. 238-239).

CEPFOD goes on to discuss the competition aspect with oil and gas suppliers. It refers especially to price competition. It refers to the negative rate of return and characterizes this as not a recent development. It also refers to incremental cost. It suggests that rate RTS does not contribute to fixed cost recovery. It also suggests that the

rate does not recover fuel costs. It goes on to refer to timers and various developments. It regards PP&L modifications as too late. It also characterizes its own recommendations as fair to all customers. (R.D., pp. 238-239).

CEPFOD then refers to the third RS block and to the RS customer charge increase. It indicates that demand charges should be paid by heating customers. It provides additional numbers relating to blocking and the customer charge. It takes the position that they are not cost-supported. (R.D., pp. 239-240).

The ALJ recommended adoption of the PP&L/OCA proposal with some modification. The ALJ modifications are to accept the PP&L delay time but recommend that the customer notice be required as outlined by OCA. The ALJ noted CEPFOD concerns, particularly with regard to policy failure and competitive impact, but concluded that CEPFOD's position was overstated notwithstanding the record evidence of negative rates of return and pricing differentials. (R.D., pp. 240-241).

PP&L and the OCA support the ALJ's recommendation by claiming that the ALJ properly rejected CEPFOD's misplaced arguments and properly refused to endorse OTS' proposals for rate investigations. (PP&L R. Exc., pp. 34-35; OCA R. Exc., p. 25). Both OTS and CEPFOD except to the recommendation by decrying the ALJ's refusal to recommend an investigation or a determination that PP&L was refusing to eliminate a subsidy with anti-competitive impacts. (OTS Exc., pp. 20-22; CEPFOD Exc., pp. 7-10).

After consideration of the positions of the parties, we shall affirm the ALJ. We agree with the ALJ that the facts in this case do not warrant the investigation requested by the OTS. In addition, we do not believe the facts warrant the conclusion

drawn by CEPFOD that PP&L's approach to rates constitutes anti-competitive behavior. We draw this conclusion, in part, because PP&L has presented sufficient credible testimony explaining their approach and, in addition, has presented several reasonable proposals for managing any shortcomings with this rate that underscore, in our opinion, the absence of any deliberately anti-competitive behavior.

E. Interruptible Service

In this proceeding, PP&L proposed to significantly alter the interruptible rate option under schedules, LP-4 and L-5³⁹. (See PP&L discussion under this topic heading, rate schedules LP-4 and LP-5 and LP-6, interruptible option, at page 270 of PP&L's main brief).

Under the current rate structure, customers whose loads are interruptible pay reduced demand and energy charges as compared to firm customers. The exact level of savings, or discount, from the firm rate, is dependent upon the customer's classification, size, relative firm and interruptible load, on-peak load factor, and total hours use of demand. (PP&L Stmt. 8, pp. 12-13).

In addition to the benefit to be received by the utility of load retention (a response of the utility to economic concerns of customers, some of whom were at risk of closure, and contraction or relocation of operations), interruptible load enabled the utility to avoid the need for generation capacity

³⁹ Rate Schedule IS-1 in the interruptible option for greenhouse lighting. Interruptible Service by Agreement ("ISA") provides for interruptible rates and service by individual contract to large customers who take service at 66,000 volts or higher. LP-6 -- Large Power Service at Transmission Voltage (High Load Factor) Rate, is a new rate representing the Company's response to prevent load loss from energy intensive industrial users with multi-plant locations. (PP&L Stmt. 8, pp. 8-9).

designed to meet short duration peak. The avoided generation capacity designed to meet such peaks was argued by PP&L to be comparable to a combustion turbine unit. Id.; 10.

The interruptible rate options at issue in this proceeding would replace the reduced demand and energy charges with an interruptible load credit. The interruptible load credit would be deducted from the billing amount the customer would pay on the appropriate firm service rate. It is available for customers with at least 1,000 KW of interruptible load on firm rate schedules LP-4, LP-5, and the new LP-6⁴⁰. The credit is derived as follows:

$$\begin{aligned} & (\text{Billing KW} - \text{Firm KW}) \times (\text{On-peak Load factor}) \times \\ & (\$/\text{KW}) \end{aligned}$$

As noted above, PP&L's approach to valuation of interruptible load is to view such as a capacity equivalent resource. That is to say, PP&L would equate the value of interruptible load to the annual carrying cost of a combustion turbine peaking unit. Under this theory, the load which can be interrupted avoids the necessity for the utility to make a comparable investment in such a peaking unit generating addition. (See PP&L Stmt. No. 9). Consequently, the former interruptible service option rates have been replaced with an interruptible credit which is applied to firm rates. This credit is based on the cost of a new combustion turbine peaking unit. The proposed credit is \$6 per kilowatt per month and \$8 per kilowatt per month, depending on notice requirements.

⁴⁰ PP&L also proposed for customers on LP-6 with at least 10,000 KW of interruptible load and who can reach firm power levels within 1.2 hour, will receive an additional monthly credit of \$2 per KW.

A recent analysis prepared by the Company indicated that combustion turbines can be installed at a cost of approximately \$300 per kilowatt, with a resulting carrying charge of \$45/KW per year. Id.

PPLICA and Beth Steel, primarily, oppose the PP&L revision to the interruptible rate.⁴¹

PP&L argues in support of its interruptible rate that such rates are not out of line. Also, PP&L argues that the rate levels it proposes are just and reasonable. Here, it refers to the rate decreases for interruptible customers in 1992. PP&L states that, relative to 1984, the interruptible customers will receive a 5 percent rate decrease in the instant case. Therefore, PP&L characterizes the rates for interruptible service option customers as still far lower than rates available to firm large power customers.

By way of historical development, PP&L states that the interruptible credit was set at a higher level than was justified by cost, in the hope of encouraging economic development and preventing load loss. It states that it filed to close the rate during 1994. (See Commission Order at Docket No. R-00943081, et al.). It emphasizes that the current proposal represents a return to the status quo and further argues against the allegation that this filing would impose a rate shock on these interruptible customers. According to the Company, PPLICA and the industrial customers opposing the revisions would prefer, in PP&L's view, to freeze in place a mistaken interruptible credit, as a permanent rate benefit.

⁴¹ These, and other parties, in certain overlapping discussion also oppose PP&L's treatment of interruptible capacity for rate design purposes as well. (See discussion at Section A;B, supra.).

PPLICA vigorously opposed the PP&L revisions. We shall focus on the points raised in its contentions, finding overlap in PPLICA's position and those of the other parties who disagreed with the Company's proposals.

PPLICA explained that the proposed design is essentially a flat kilowatt rate with an adjustment for load factor. Under the current tariff, a demand charge is applicable to the billing kilowatts and then two energy blocks (plus the ECR) apply. PPLICA then proceeded to compare the two rate designs. It stated that PP&L had also proposed a 500 megawatt cap on interruptible load. PPLICA argued that, given that the effective amount of interruptible load for the cap has been identified as 460 megawatts, only 40 megawatts of interruptible load are available. By means of a footnote, it requests that the matter of adding incremental load beyond the cap should be clarified. It references transcript pages 810-811, which provided some clarification.

PPLICA observed that the overall LP-5 revenue increase is shown as 15.45 percent, as compared to the overall system average increase of 11.7 percent. It further observed that this includes a 27 percent increase for interruptible customers.

PPLICA stated that it is adamantly opposed to PP&L's interruptible rate design changes. It states that PP&L has effectively transformed the interruptible service into a firm service rate with a load insensitive credit. It views this as a dramatic change in rate design philosophy, causing an unprecedented increase in rates without any meaningful justification. It views the change as going against current competitive trends, the principle of gradualism and the recognized sensitivity of this state's economy.

PPLICA, therefore, recommended three schedules, LP-5 firm, LP-6 firm and LP-5/L-6 interruptible. It states that the basic PP&L design for the two proposed firm rate schedules is reasonable but that the PPLICA recommended revenue increase should be used. PPLICA also proposes to apply the 1.5 times system average increase for the interruptible rate. This would be an overall increase to the interruptible customers of 17.55 percent, based on the entire revenue requirement being met. It characterizes this as a substantial increase. It provides a schedule detailing information. It states that the overall LP-5 revenue class (including LP-5 and LP-6 plus the proposed LP-5/LP-6 interruptible) would receive a 10.9 percent increase. PPLICA also indicates that it recommends, for rate design, an interruptible credit that is approximately the same as that proposed by PP&L.

PPLICA also addressed the PP&L "resource value approach" to interruptible rates. This assumes that interruptible service is a substitute for peaking capacity. The rates are based on value while other customers have their rates, presumably, based on embedded cost, in accordance with standard cost of service studies. PPLICA would view this as making interruptible load a resource to be purchased by PP&L rather than a low reliability service offered by PP&L. PPLICA opposes this treatment of interruptible service. It would prefer rates based on cost of service. Presumably, this would be cost of service without the capacity element included.

PPLICA continues with the view that interruptible service is lower quality service. It also characterizes the situation proposed by PP&L as the selling back of interruptible service capacity by the customers to PP&L. PPLICA views this approach as faulty. It discusses active load management, the value of capacity and other related matters. It again refers to

its proposal that the increase be limited to 1.5 times system average. It further argues for cost of service ratemaking.

In addition to responding to PP&L proposals, PPLICA refers to the OCA resource value approach. Its criticisms of the OCA alternative are similar to the criticisms of PP&L's approach. It is also opposed to the market-based valuation method.

The main PPLICA response concerning interruptible rates begins at page 3 of its reply brief. It indicates disagreement with PP&L's view of its leadership relating to economic development initiatives. It focuses attention on the proposed rate increases for interruptible customers. It would not look back 10 years to the last case where there was no interruptible service, as is presently structured. It views the PP&L initiative as an inappropriate manner in which to meet competition.

PPLICA views its own proposal as one which reduces cross-subsidization and which moves all rates toward the system average. It also discusses the possibility of self-generation of electricity by customers. Additionally, PPLICA discusses the valuation method of ratemaking for interruptible service. (See PPLICA Reply Brief, p. 6). It does not agree with PP&L that the PP&L proposal is a reasonable, middle-of-the-road position. It draws a distinction between cost allocation and valuation ratemaking. It views PP&L as confused concerning these matters. It further discusses its 1.5 times cap proposal. It indicates its view that the PP&L proposal is out of balance, unjust and unreasonable. It discusses competition and competitive threats. It views the PP&L position as not striking the proper balance. It discusses the PP&L theory and impacts on PPLICA members.

PPLICA further discusses the PP&L EDI/IDI credits and alternatives to the existing interruptible rates. PPLICA would

prefer the interruptible rate option to various possibilities of alternatives. It also states that PP&L has mischaracterized the PPLICA proposal. It states that it is not recommending lower rates but only rates lower than those proposed by PP&L. It further discusses the Commission action to close the interruptible offering. It distinguishes this from the current proposal to increase rates. It would further distinguish rates for 1984 or even 1992. It views the interruptible program as a good program still and disagrees with the PP&L argument that the interruptible proposal was flawed even in 1992.

PPLICA states that the interruptible program has worked. It closes with a reference to its 1.5 times increase cap proposal and movement toward a system average rate of return. It also refers to the principle of gradualism.

Beth Steel, in discussions under the headings of cost of service study and revenue allocation, also disagreed with the proposed change in the interruptible service option.

ALJ Christianson, as a general matter accepted the PP&L proposals. He accurately noted that PP&L appeared to be phasing out this interruptible service under the favorable, existing terms, indicating a preference for more carefully structured and limited rate reductions. The PP&L proposal which indicated a preference for "value of service" ratemaking rather than "cost of service" ratemaking was viewed as entirely appropriate, given the context.

ALJ Christianson reasoned as follows:

I would rather overtly go to the value of service theory rather than pretend that we are really dealing with cost of service when we are dealing with attempts to meet competition or keep customers. There are

many principles involved in ratemaking and cost of service is only one of them.

Especially as a utility enters the competitive arena, value of service (what the market will bear) must become relatively more important, in comparison to cost of service analysis. Of course, steps should be taken to protect "core" or monopolistic customers and the overall revenue requirement should still be met. However, selective rate reductions rather than cost-based programs, appear to be the wave of the future.

To some degree this is occurring in other utility industries, such as the gas industry. The reductions are tailored to maximize revenue realized while keeping the customer. There must, of course, be an irreducible minimum beyond which money is lost, rather than gained, for the system. However, above that minimum, there is considerable latitude. The consequences of this decision by PP&L might be painful for various customers but I agree with PP&L that the broader picture should be taken into account. These customers are asking what PP&L has done for the customer lately. PP&L is looking to 10 years or more of experience in the past and the immediate future.

I have made some adjustments in the cost of service and allocation category but recommend that no additional adjustments be made here under the heading of rate design. I view the interruptible customers as simply customers within the general class and not as a separate class. They take service like other industrial customers and, to some degree, allow interruption. I also point out that PP&L does have a considerable amount of available capacity, so that interruption might often be more a theoretical possibility than a real problem. In any case, I am recommending no further adjustments to this PP&L proposal.

(R.D., pp. 250-251).

The PPLICA filed extensive Exceptions to the ALJ recommendation to adopt PP&L's proposal regarding revisions to interruptible rates. (PPLICA Exc., pp. 3-23).

First, the PPLICA argues that the recommendation violates principles of gradualism. It would emphasize that the increase to the interruptible rates constitute, on average, a 22% increase (assuming no revenue increase for the Company) and a 28% increase (assuming the full rate increase request is granted). (PPLICA Exc., p. 4; 5-6.). This is objectionable according to the PPLICA argument, especially in light of the fact that the ALJ recommendations result in an average increase, systemwide, of 2.7%.

Supportive of its reliance on the view that the R.D. impermissibly violates principles of gradualism as a consideration in ratemaking, PPLICA cites Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 74 Pa. P.U.C. 1, 211-212 (1990); Pennsylvania Public Utility Commission v. National Fuel Gas Distribution Corporation, 73 Pa. P.U.C. 552, 621 (1990); Pennsylvania Public Utility Commission v. Western Pennsylvania Water Company, 95 PUR4th 470, 515-516 (1988); and Pennsylvania Public Utility Commission v. Pennsylvania-American Water Company, 97 PUR4th 469, 507-508 (1988).

PPLICA also presses its view that interruptible service constitutes a separate class.⁴²

Bethlehem Steel also filed Exceptions to the R.D. repeating many of the concerns articulated by PPLICA.

⁴² As noted above, under PPLICA's proposal, its rate design would treat the LP-5 and LP-6 interruptible customers as a separate class. See PPLICA Exc., p. 7, n. 1.

On consideration of the positions of the parties, we find merit in the Exceptions of PPLICA and Beth Steel. Therefore, we shall grant the PP&L proposed revisions to the interruptible rate option with the following modifications principally articulated by PPLICA.

We conclude that the interruptible rate option customers should be treated as a separate class, and we shall so direct PP&L to develop tariffs accomplishing this revision. Further, arguments which are grounded in principles of gradualism, when viewed in the proper context, are persuasive that the rate increase for the interruptible rate option class be limited to 1.5 times the system average as developed in the presentation of PPLICA.

The approach used by PP&L, in valuing interruptible load as related to a combustion peaking unit is a dramatic departure from the design of the interruptible rate option currently in use on its system. Interruptible customers do, in fact, receive an inferior quality of service than firm customers. Further, we accept PPLICA's criticisms of the flaws in the determination of the credit resulting from subjective assessments of value to interruptible option customers. (PPLICA Exc., pp. 25-26). Therefore, the approach taken by the Company which is grounded on value of service considerations may be acceptable as a matter of theory. Yet, it overlooks the economic realities faced by this class of customer and violates principles of gradualism in rates.

Based on the foregoing, we shall grant the Exceptions of PPLICA and Beth Steel, to the extent consistent with PPLICA. We, hereby, reject PP&L's proposed rate design which would eliminate the separate interruptible tariff and replace this with an interruptible credit. We direct the Company to retain the rate design consistent with the recommendations contained herein.

Exceptions and replies to the contrary are, hereby, denied.

F. Rate Schedule SE, Street Lighting

The OTS, through its witness Mr. Yarolin has recommended that Rate Schedule SE be considered an off-peak service. The service, used by 58 customers, is not used during peak hours for seven of the twelve months of the year. The OTS reasoned was that the charge can place a financial strain on a given community and that street lighting is a community service from which all customers benefit. There was a further suggestion of higher on-peak rates for winter months and lower off-peak rates for summer months.

PP&L responded that Rate Schedule SE has consistently contributed to monthly system peaks since the rate was established in 1982. It found no change of circumstances sufficient to support the OTS revision. It refers to three generalized statements at public hearings. It also indicates that the proposal would redistribute but not necessarily reduce cost to the communities. PP&L further indicates that off-peak rates are generally used for customers who can shift load. That is not the case in this situation.

ALJ Christianson recommended against adoption of the OTS proposal, stating that:

On this topic, I agree with PP&L. I sympathize with the municipalities and the problems they have with price increases. However, I find no good basis in theory for the OTS proposal. This is not strictly an off-peak service and I agree with PP&L that off-peak rates are normally used to move customers away from peaks. Street lighting demand does not move like industrial demand can move.

There might be some argument on ability-to-pay but this is not normally accepted as a basic theory of ratemaking. OTS also argues about the general service provided by street lighting, indicating that some of the cost should be spread on the customer base generally. This theory has some support and there are other proposals to spread cost over all customers. However, application of this theory approaches the "tax" theory of utility ratemaking, which has been approached reluctantly up until now. I do not recommend application of that theory here. In any case, the public must pay for this service one way or another, either through utility rates or through taxes.

ALJ Christianson observed that some work could be done about providing added notice to municipal customers, considering their budget problems. However, that idea was not before him in this proceeding and went beyond the scope of an individual rate proceeding. Therefore, he recommended the rejection of this OTS initiative.

The OTS pressed its proposal in its Exceptions. It would emphasize that the ability to shift load is not the sole criterion for whether a service is off-peak. Additionally, the OTS stresses the financial impact on affected municipalities of its proposal.

On consideration of the Exceptions of the OTS, we are not persuaded that the contribution of the rate to PP&L's system necessitates a change in the rate's classification. We will, therefore, deny the OTS Exceptions.

G. Rate Schedule ISA

The topic of Rate Schedule ISA has also been discussed under the context of cost of service and allocation. Beth Steel

addressed this subject in depth in its reply brief. PP&L indicates that OCA has stated that a contract should not block application of a portion of the rate increase to this class. PP&L responds briefly to this allegation but also states that the rate class was designed as a competitive response. It indicates that arbitrary withdrawal of this contract would likely risk loss of load. PP&L refers briefly, in closing, to the testimony provided by OCA.

The presiding ALJ accepted the PP&L theory of meeting competition and retaining load. He would not, therefore, disturb the contract. He concluded that the Roaring Creek precedent does not really apply here.

On consideration of this issue, we shall adopt the reasoning and recommendation of the ALJ.

H. Economic Development Credits (EDI/IDI)

Since 1987, the Company has offered to its industrial customers a series of economic development initiatives ("EDI") and industrial Development initiatives ("IDI"). EDI was made available in 1987 and IDI was implemented in 1992. To receive EDI credits, customers must have signed contracts agreeing to expand production or expand physical facilities. The program provides credits of 1 cent per kWh and \$2 per kWh to encourage the expansion of use of existing commercial. Under the program, credits were only provided to customers who were able to submit data demonstrating an intent to expand physical plant and add production capacity. Absent such a showing, EDI/IDI credits were not made available to the customers.

The Company maintained that the program has provided substantial benefits to the participants and helped to retain 20 plants in the Company's service territory. (PP&L St. 8-R, p. 39). The Company also asserted that the program has deterred a number of industrial customers from constructing substantial on-site cogeneration capacity over the past ten years which would have resulted in major losses of the incremental sales produced by the EDI/IDI participants. (PP&L St. 8-R).

In this proceeding, the Company proposed to allocate the cost of these programs to the beneficiary rate classes. The Company also indicated that its shareholders have funded these programs for several years. The Company further advocated that if the program, as modified and proposed in this proceeding, is not approved by the Commission, the program should be terminated and the shareholders should not be required to fund the program.

The Company opposed the OCA's proposal that the cost of the programs be shared with the shareholders and that the Company be required to continue the programs. The Company further

refuted the OCA's assertion that it is seeking economic development costs to captive residential or commercial customers.

The Company also stated that it would have no objection to the Sierra Club's proposal to require companies to perform or present DSM audits, as part of the program requirements.

The PPLICA argued that because the initiatives benefit all customers classes, the costs should be allocated among all customer classes. The PPLICA further maintained that the Company's program places a disproportionate burden on industrial customers. The PPLICA also asserted that a more reasonable approach would be to allow the credits on a system wide basis.

The ALJ recommended the adoption of the PPLICA's proposal to spread the cost of the EDI/IDI credits among all rate classes. The ALJ further stated:

I conclude that these programs are fundamentally sound and should be allowed to continue, subject to ongoing review by the Company and the Commission. I find record support for the PP&L positions. These sorts of initiatives are not unique to the electric utility industry and, while they should be carefully monitored, they are a part of contemporary life with respect to utility ratemaking.

As PP&L capacity becomes more in line with demand, these programs should be re-examined. However, I recommend that the Commission allow them to continue, for now. I would not impose the 50/50 sharing proposed by OCA, largely because I find these programs to be cost-justified. As indicated above, I would spread the cost over all ratepayers, and not simply the classes containing the customers directly involved with the programs. This burdens so-called captive customers but I accept this burden, for now. As the electric utility industry enters the competitive mode, this program, as I have indicated above,

should clearly be re-examined and subject to ongoing re-examination. However, for now, I accept the PP&L positions, except for the spreading of cost.

(R.D., p. 260).

The OCA excepted to the ALJ's recommendation arguing that its proposal represents an appropriate sharing of costs of the EDI/IDI program which benefits the ratepayers as well as the shareholders. (OCA Exc., p. 55). The OCA disputes the Company's contention that all of the load would have been lost without the full rate discounts. The OCA further avers that the Company failed to present real evidence to support this assumption. The OCA summates that its revenue adjustment of \$12,665,535 reflecting a 50/50 sharing of revenue shortfalls from the provision of discounted rates under the program should adopted.

In its Exceptions, the Company urges us to reject the ALJ's recommendation. Specifically, the Company states that:

The proposed adjustment should be rejected. While all customers, both participants and non-participants, may benefit from these programs. those benefits are not shared equally. Participants receive much greater benefits, and the cost of these programs should be allocated accordingly. Cost should be allocated on those factors which cause a cost to be incurred. The "cause" of the cost here is the rate discount to industrial customers receiving the EDI/IDI discounts. The "cost" of these discounts therefore should be allocated to the industrial customer classes which receive those discounts.

Finally, the recommended adjustment is inconsistent with the Commission's treatment of similar costs and lost revenues produced by Demand-Side Management (DSM) programs (PP&L St. 8-R, p. 38). The Commission's current DSM Order (Docket No. I-900005) requires recovery of cost and lost revenues

from the classes receiving direct benefits from the programs (Id.). The ALJ's recommendation, therefore, is inappropriate and should be rejected.

(PP&L Exc., pp. 56-57) (Footnote deleted).

Upon careful review of the record and the arguments of the Parties, we conclude that it is reasonable and appropriate to allocate the costs of the EDI/IDI programs among the industrial customer classes, as proposed by the Company. Accordingly, we will grant the Company's Exceptions.

I. GS-1 Rate Adjustments

We find no indication of exceptions filed with respect to the ALJ recommendation to reject the OSBA proposal for a gradual reduction in allocated class revenues over a number of years. We, hereby accept the resolution of this issue consistent therewith.

J. Demand Side Management⁴³

We note that ALJ Christianson considered the various alternatives to the current PP&L demand-side management ("DSM") program. He opined that many of the ideas "might be good," but he concluded that "much of the development [was] beyond the scope

⁴³ On December 13, 1993, we entered a Corrected Opinion and Order ("1993 Order") in Investigation into Demand Side Management by Electric Utilities UNIFORM COST RECOVERY MECHANISM at Docket No. I-00900005 ("DSM Investigation"). The 1993 Order authorized jurisdictional electric utilities to implement a Demand Side Cost Rate ("DSCR") surcharge to recover direct and collateral DSM program costs, subject to annual review for four years. Further, the Office of Administrative Law Judge was directed to address demand-side management and integrated resource planning as issues in future utility rate cases.

On April 8, 1994, we entered another Opinion and Order ("1994 Order") in DSM Investigation. The 1994 Order clarified our 1993 Order and denied a Petition for Stay or Supersedeas Pending Appeal. We stated at page 26 of the 1994 Order that "[w]e are convinced that it is in the public interest to aggressively and without delay implement the DSM programs as set forth in our" 1993 Order.

An appeal of our 1993 and 1994 Orders was taken to the Commonwealth Court. On January 9, 1995, the Commonwealth Court affirmed our 1993 Order in all respects except to that part allowing the recovery of incentives and costs of physical facilities through the surcharge mechanism and adopting the calculation for incentives. That part was reversed, and the case was remanded to us on the lost revenue issue. Our 1994 Order was vacated. (Pa. Industrial Energy Coalition v. Pa. P.U.C., 653 A.2d 1336 (Commonwealth Court, 1995). ("PIEC"))

The Pennsylvania Supreme Court has accepted our appeal of the Commonwealth Court decision in PIEC. The appeal is docketed at No. 75 M.D. Appeal Docket 1995. The issues are whether the Commonwealth Court properly determined that Section 523 incentives cannot be used in a Section 1307 cost recovery mechanism and whether the Commonwealth Court properly remanded to us the issue of our legal authority to award recovery of lost revenues. Oral arguments are anticipated in Spring 1996.

of this ratemaking proceeding." He recommended no modifications. (R.D., p. 265.)

In taking exception to the Recommended Decision on the DSM issue, the Sierra Club raises two Exceptions concerning DSM:

Sierra Club Exception 1: The ALJ should not have excluded the proffered Sierra Club direct testimony as to its proposal regarding DSM, incentives, and lost revenues in setting PP&L's rates.

(Sierra Club Exceptions, pp. 14-18.)

Sierra Club Exception 7: The ALJ should have adopted the Sierra Club proposal to require maximum cost-effective DSM, verified by third-party audits, as a prerequisite to DSM certification and economic discount rates.

(Sierra Club Exceptions, pp. 33-39.)

In support of its first Exception, the Sierra Club characterizes its proposal as "the appropriate method for addressing these matters while the DSM Order of the Commonwealth Court" is before the Supreme Court. (Sierra Club Exc., p.17.) The Sierra Club argues that if we do not address DSM cost recovery in this case, the opportunity to address PP&L incentives and lost revenue issues may not come again until PP&L's next general base rate case, which PP&L predicts will not be until the next century. (Sierra Exc., pp. 16-17.)

In support of its seventh Exception, the Sierra Club characterizes its proposal as "flexible," "affordable," "less of a burden," and "simple to administer." (Sierra Exc., pp. 35-36.) The Sierra Club further asserts that our failure to adopt its proposal will place us in a reactive, negative mode of responding to changes in the electric utility industry. The Sierra Club argues that under its proposal other customers would benefit from

increased local economic activity as industrial customers invest in DSM measures and increase production. (Sierra Exc., pp. 37 & 39.)

The Sierra Club also dealt with DSM matters in its Main Brief, asking the ALJ to reconsider his decision to exclude consideration of incentives and lost revenues relating to DSM from this proceeding. (Sierra M.B., pp. 13-14.) The Sierra Club further recommended cost-effective DSM programs relating to all customers and having shareholders absorb some lost revenues. The Sierra Club sought creation of a system benefits charge based on electric sales by the utility; referred to stranded benefits and other emerging matters such as peak reduction measures and performance-based incentives; recommended a non-bypassable system benefits charge for recovering DSM costs; and advocated future public input hearings for PP&L customers. The Sierra Club referred to the experience in New York and other states, as well as to the Federal Energy Regulatory Commission and the "freedom" allowed to the states concerning this matter. (Sierra M.B., pp. 18-25.)

In its Reply Exceptions, PPLICA asserts that the Sierra Club's DSM Exceptions should be summarily denied as an untimely resurrection of an issue which should have been the subject of a petition for interlocutory review. (PPLICA's R.E., pp. 17-20.) Substantively, PPLICA challenges the Sierra Club for failing to provide a rationale for energy audits of industrial customers but not for other customers. Further, PPLICA asserts that the Sierra Club's witness was uninformed as to important facts and that, as a result, the Sierra Club proposal is "poorly developed" and without foundation. (PPLICA R.E., pp. 21-22.)

PP&L discussed DSM issues starting at page 288 of its Main Brief, arguing that it had justified the scope and focus of its DSM programs. PP&L maintained that it has adequate capacity

for the immediate future and that accelerated investment in DSM would not reduce its capital costs. It also stated that it spends more than other major jurisdictional utilities, despite the continued uncertainty over recovery mechanisms. PP&L further discussed these matters starting at page 128 of its Reply Brief, stating that it did not object to a non-binding audit but did not favor the broad recommendations made by the Sierra Club. PP&L described the Sierra Club proposal as poorly defined and premature. PP&L suggested that the DSM issues were a matter best addressed in DSM Investigation at Docket No. I-00900005.

Initially, we must determine whether the Sierra Club is properly raising the DSM issue via its Exceptions, after having raised the issue at the Hearing and in its Briefs. We note that the threshold for interlocutory review is a high one. The standards for interlocutory review are found in Section 331(e) of the Public Utility Code, 66 Pa. C.S. §331(e), and in Sections 5.302 and 5.303 of our Regulations, 52 Pa. Code §§5.302 & 5.303. We interpreted these standards in Application of Knights Limousine Service, Inc., 59 PaPUC 538 (1985) (Knights). As we said in Knights, we do not routinely grant interlocutory review except upon a showing by a petitioner of extraordinary circumstances or compelling reasons. Such showing may be accomplished, for example, by a petitioner proving that without interlocutory review some harm would result that would not be reparable through normal avenues, that the relief sought should be granted now rather than later, or that granting interlocutory review would prevent substantial prejudice or expedite the proceeding.

Additionally, Section 5.404 of our Regulations, 52 Pa. Code §5.404, provides that:

At any stage of the hearing or thereafter the Commission or the presiding officer may call for

further admissible evidence upon an issue and require that the evidence be presented by the participants concerned, either at the hearing or at the adjournment thereof.

In light of the threshold for interlocutory review and our ability to call for evidence, we cannot conclude that a party's sole recourse to challenge a ruling of an ALJ relative to the exclusion of evidence should be predicated upon a petition for interlocutory review. Having reviewed the record as developed in this proceeding, we conclude that the Sierra Club has properly requested that we reconsider herein ALJ Christianson's prior decision to exclude evidence relating to DSM issues.

Turning now to whether the evidence should have been excluded, we recognize that the proposal offered by the Sierra Club is arguably neither novel nor extreme. For example, New York requires DSM audits as a condition for receiving a flexible rate. The New Jersey Senate is considering enacting legislation to impose a similar requirement. We cannot ignore, however, the fact that certain DSM issues are presently pending before the Pennsylvania Supreme Court with oral arguments anticipated in Spring 1996.

In our opinion, whether Pennsylvania should adopt the Sierra Club's proposal is not a question for a specific rate case involving only one utility. Additionally, to attempt to fashion DSM proposals in anticipation of the decision of the Pennsylvania Supreme Court would be tantamount to trying to hit an invisible, moving target. In our opinion, the issues raised by the Sierra Club should be raised in DSM Investigation, Docket No. I-00900005, after the Pennsylvania Supreme Court renders its opinion.

We further note in passing that PPLICA's challenge to the Sierra Club's proposal and assertion that it should be rejected for a failure to require energy audits for all customers is without merit. In our opinion and without addressing the merits of the Sierra Club's proposal, we believe that the proposal is clear that any customer, regardless of customer class, for whom a utility seeks a DSM rate would be subject to an audit under the proposal.

Accordingly, the Sierra Club's first and seventh Exceptions are denied.

X. ADDITIONAL ISSUES

There remain various other matters which do not fall easily under the various topic headings which have been used so far. The main topic remaining is the ECR or energy cost rate, a mechanism whereby a utility is reimbursed for what it spends on energy.

A. The Energy Cost Rate Itself

PP&L addresses this matter in its Main Brief, commencing at page 290. It responds to a DOD development at hearing. This PP&L discussion relates somewhat to a claim by Sierra Club at page 16 of its Main Brief. There the Sierra Club suggests that the ECR be eliminated unless the Company can show that it is maximizing benefits of wholesale market purchases for customers.

PP&L argues that the ECR is used by each Pennsylvania electric utility and is a Commission-approved mechanism allowed pursuant to Section 1307 of the Public Utility Code, 66 Pa. C.S. §1307. It traces the ECR back to 1978 and refers to substantial benefits and levelization of costs. Premised on our review of the record, we accept the position espoused by PP&L and we make no change to the ECR mechanism, within the context of this proceeding.

B. The ECR and Off-System Sales

The PP&L's discussion of this topic commences at page 291 of its Main Brief. It begins this discussion with a useful background statement, at pages 291-293, which we deem it instructive to recite hereinbelow:

In this proceeding, the Company has proposed an innovative modification of the ECR to reflect the expected return of capacity costs and revenues attributable to off-system capacity sales that will terminate in the near future. The Company's proposal specifically addresses the return of a 945 MW slice of system capacity and energy sold to Jersey Central Power & Light Co. ("JCP&L").

In PP&L's 1982 base rate case the Commission determined that PP&L had excess generating capacity and, as a remedy, disallowed recovery of all return on a 945 MW slice of the Company's system. After that case, PP&L sold that capacity to JCP&L. In the Company's 1984 base rate case, all of the costs and revenues associated with that 945 MW were allocated out of PUC jurisdictional rates. The same approach was followed in this filing.

On January 1, 1996, this sale to JCP&L begins to wind down over a five-year period. One-fifth of the 945 MW, or 189 MW will return to PP&L each year. Absent an innovative solution, PP&L will have to choose among three alternatives for addressing this returning capacity: (1) find another buyer in the bulk power market, (2) file periodic retail base rate cases, or (3) absorb the associated costs.

After analysis, PP&L concluded that none of these three options was satisfactory or in the public interest. The bulk power market is becoming increasingly competitive and prices are being driven inexorably toward marginal costs. Periodic base rate filings require the commitment of significant resources by all participants, most particularly the Commission and its staff. And, finally, the Company is not in a financial position to begin absorbing additional costs. Accordingly, PP&L developed an innovative alternative which it presented in this case.

Under its proposal in this case, the Company would reflect the full costs of each "slice" of returning capacity in the ECR, as well as credit all revenues from off-system

sales. The capacity could serve a range of uses that would ultimately benefit customers, e.g., serving native load, or making off-system capacity-related PJM installed credit, output reservation and transmission entitlement sales.

At the end of the second paragraph, PP&L drops the following footnote:

PP&L also has sold capacity and energy to Atlantic City Electric (125 MW slice of all coal-fired plants) and Baltimore Gas & Electric (125 MW slice of the Susquehanna Plant). The Company has followed the same ratemaking practices with these sales as it has with the JCP&L sale and would intend to follow the same ECR treatment.

PP&L points out that this returning capacity can provide a valuable resource for meeting customer demand or to provide other valuable functions, such as making additional off-system sales. This could produce considerable revenue which would be credited to customers, under the PP&L plan.

PP&L notes opposition, by three witnesses. PPLICA, the OCA, DOD and the Sierra Club address this matter.

PP&L provides as the fundamental basis for opposition the idea that the costs are not subject to ongoing review. The Company recognizes that its proposal is innovative and novel but expresses disappointment with the responses of the other parties. PP&L points out that the costs of the returning facilities are known, that customers would immediately see the benefits from off-system capacity sales, that the proposal will tend to avoid base rate proceedings, and that monitoring can deal with overearnings. PP&L urges the Commission to examine the proposal carefully and to reject the positions of the opposition.

Starting at page 294 of its Main Brief, PP&L proposes the taking of two steps if its main proposal is not accepted. PP&L, at pages 294-295, provides a brief and coherent statement concerning these two steps, which follows:

Should the Commission not accept the Company's proposal, then fairness and sound ratemaking principals require that two steps be taken as to the ECR.

First, if the Commission decides to exclude from the ECR any capacity costs associated with expiring contracts, then all revenues from off-system capacity-related sales also should be excluded from the ECR and treated as an element of base rates only (PP&L St. 7-R, pp. 34-35). This is the traditional ratemaking practice and would permit the Company to retain revenues from incremental off-system capacity-related sales to at least partially offset the cost of capacity returning under expiring agreements. Significantly, even Mr. Baron notes the propriety of this approach (PPLICA St. 7, p. 76).

Second, the Company should be entitled to retain all energy-related savings made possible by the return of this capacity to PP&L. For example, when the first increment of JCP&L capacity returns on January 1, 1996, the Company's capacity costs will increase by about \$35 million and its energy costs will decrease by about \$15 million. Under current regulatory practice in Pennsylvania, the Company's shareholders would absorb a \$35 million cost increase and ratepayers would automatically receive a \$15 million cost decrease through the ECR. Under the Company's preferred proposal, both the capacity costs and the energy savings would be reflected in the ECR, along with all of the revenues received from other off-system capacity-related sales. If the Company's preferred proposal is rejected, however, at a minimum, the Company should be permitted to retain the energy savings to offset a portion of the capacity costs that produced those

savings. Although this would not be a complete solution to the problem, it would at least avoid the fundamental mismatch of costs and savings described above and could help the Company avoid the need for an immediate rate filing to reflect the returning JCP&L capacity and energy (PP&L St. 7-R, p. 35).

The ALJ characterized the foregoing as fair steps which should be taken, and he recommended that we adopt them in the event that the basic proposal was not approved. In the ALJ's view, these two steps would essentially keep the capacity off the books until there is a base rate case.

The OCA discusses this matter, commencing at page 313 of its Main Brief and at page 133 of its Reply Brief. The OCA states that the main proposal has the effect of raising the total rate increase request in this case to approximately \$440 million, rather than the \$261 million identified by PP&L. The OCA would reject the proposal, pointing out that these capacity costs have not been in jurisdictional rates for nearly 10 years. It suggests a danger of overearnings by PP&L. It suggests that PP&L can always bring a base rate case.

The OCA suggests that the PP&L proposal would essentially circumvent the review of issues critical to the determination of rates. It gives the example of the excess capacity issue. It also discusses the possibility of what it terms "perverse incentives". It states that, if PP&L fails in its marketing efforts, then it would automatically receive full recovery of costs from ratepayers. It addresses various PP&L arguments and refers to the testimony of its own witness. It also refers to incentives for cost control. It views the PP&L proposal as one-sided.

The OCA would also reject the PP&L argument that it be permitted to retain the energy savings from this capacity, if its

proposal is denied. The OCA views this argument as not reasonable, in the context of this proceeding. It states that this alternative proposal would continue to allow PP&L to selectively pick the ratemaking treatment that is most advantageous to it, at a particular point in time. It suggests that the alternative proposal could result in ratepayers paying energy rates through the ECR which are higher than PP&L's actual cost of energy supply.

The OCA, in its Reply Brief, submits that PP&L has overlooked serious flaws in its proposal. It states that, if the PP&L load is not growing, it will be necessary to determine whether the returning capacity is excess capacity. The OCA again touches on the overearnings problem. It also again discusses what it terms perverse incentives. These relate to the possible failure of marketing efforts and the automatic recovery from ratepayers of cost, through the ECR. The OCA again suggests rejection of the primary PP&L proposal. The OCA also states that the alternative PP&L proposal, to retain the energy savings associated with this capacity, is premature and should not be adopted in this case. PP&L should retain the right to make such a proposal in an appropriate proceeding.

DOD discusses this topic in its Main Brief, commencing at page 16. It suggests a shifting of business risks to the ratepayers. It notes that the OTS witness appears to support PP&L. DOD then refers to testimony of its own witness suggesting a modification of the ECR, by returning to methods used before 1994. DOD also suggests that base rate treatment of capacity is the appropriate regulatory treatment, not use of the ECR. DOD further refers to a recent PP&L contract for sale of capacity to JCP&L. It suggests that this sale could be relevant. It further suggests some PP&L agreement with the DOD position.

The Sierra Club addresses this matter very briefly at page 16 of its Main Brief. It would deny the PP&L proposal until and unless the Commission can find that PP&L has complied with new competitive bidding regulations, in dedicating the capacity and energy for its customers.

PPLICA addresses this matter, starting at page 32 of its Main Brief and at page 43 of its Reply Brief. It states that PP&L wants automatic increases to its retail customers, to offset reduced future revenues associated with this JCP&L transaction. It refers to \$35.5 million in revenue requirement for January 1, 1996 and corresponding increases over five years. It further states that the credit associated would be approximately \$20.8 million for the test year. PPLICA argues that the proposal would amount to requiring the Commission to approve, prospectively, single issue rate increases, without consideration of other matters.

PPLICA continues with reference to the approximately \$21 million offsetting ECR credit, which it discusses elsewhere in its Brief. It further states that, should the PP&L proposal relating to JCP&L be rejected, PP&L will withdraw its proposal to credit the ECR for off-system capacity revenues but credit base rates, again resulting in the net increase to base rates of \$240 million. PPLICA refers to risks being transferred. PPLICA would retain this matter in base rates. In its Reply Brief, PPLICA refers to PP&L Statement No. 7-R, pages 34-35, and to PP&L's alternative proposal. While PPLICA indicates opposition to the fundamental PP&L proposal, it indicates agreement with the proposal that, if the Commission decides to exclude from the ECR any capacity costs associated with expiring wholesale contracts, then all revenues from off-system capacity-related sales should be excluded from the ECR and treated as an element of base rates only. It refers to PPLICA Statement No. 7, page 77. PPLICA

further indicates its opposition to the approach of crediting revenues to the ECR.

PP&L addresses this matter in its Reply Brief, commencing at page 134. It refers to the OCA blanket opposition to the fundamental PP&L proposal, arguing that the OCA narrowly focuses on hypothetical and ignores the very real benefits of the PP&L proposal, particularly immediate benefits of revenue credits through the ECR. PP&L disagrees with the OCA position that the PP&L alternative is not reasonable. PP&L refers to fundamental unfairness of placing the full cost of the returning facilities on PP&L, but giving the full net benefit of energy savings to ratepayers. It views the OCA rationale as lacking merit.

PP&L further views the OCA proposal that PP&L address this matter in an ECR case as inappropriate. It states that the Commission has before it all facts necessary to decide this issue now and argues that the Commission should make the requested modification. It argues that the first slice will return very shortly after the new rates go into effect and that an overearnings situation is not likely at that point.

The ALJ notes, at page 274-275 of his R.D., that the primary PP&L proposal might be a good idea but that he regards it as overly innovative and too automatic. PP&L argues that it would serve, probably, to avoid base rate proceedings. However, as expensive as they are, asserts the ALJ, base rate proceedings are a proper tool for managing utilities and setting appropriate rates. The ECR mechanism serves to avoid more frequent rate proceedings, as energy costs fluctuate. However, there is a rationale for the ECR and appropriate checks involved in the ECR mechanism.

The ALJ further notes that he does not see the necessary checks and balances in the primary PP&L proposal, and

that it appears to depart too far from traditional ratemaking. PP&L points out that complaints can be brought against its ongoing rates. However, asserts the ALJ, this can be a cumbersome and slow process.

The ALJ concludes, at page 275 of his R.D. that although the PP&L primary proposal is tempting, he recommends that it be rejected. On the other hand, he finds the PP&L alternative proposal to be acceptable. Moreover, he agrees with the fundamental unfairness argument of PP&L. He concludes by recommending that the Commission accept this alternative proposal which is provided at pages 294-295 of the PP&L Main Brief and at pages 34-35 of PP&L Statement No. 7-R, of Mr. Kleha.

PP&L, the OCA, and the Sierra Club filed Exceptions to the recommendation of the ALJ on this issue. PP&L, the OCA, and PPLICA filed Reply Exceptions.

In its Exceptions, PP&L argues that the ALJ's rejection of its request to include in its ECR the cost of capacity that will become available to the Company over the next five years, is without merit. Furthermore, PP&L asserts that the ALJ's reasons for rejecting the inclusion of the costs of off-system sales in the ECR are clearly outweighed by the substantial benefits that would accrue from acceptance of this proposal. PP&L contends that the ALJ's concern that this proposal is too "innovative" and too "automatic" is without foundation, and that the benefits to be afforded by the Company's proposal clearly outweigh any drawbacks.

PP&L further asserts that it has advanced an innovative proposal to reflect the cost of each "slice" of capacity returning from JCP&L in its ECR and, at the same time, to credit all revenues from off-system capacity-related sales. PP&L states that its proposal has several substantial benefits. The ALJ's

concern that the Company's proposal lacks sufficient checks and balances is unfounded and is perhaps a result of the proposal's novel approach. PP&L concludes that the Company's proposal will produce significant benefits for customers and is in the public interest. (PP&L Exc., pp. 52-53)

In response to PP&L Exceptions on this issue, the OCA submits that the ALJ properly recognized that PP&L's proposal lacks sufficient checks and balances to assure that ratepayers are paying rates that are just and reasonable. The OCA rejoins that although the Company identifies one of the primary benefits of its proposal as being the avoidance of base rate filings, the ALJ properly found that base rate proceedings are a proper tool for managing utilities and setting appropriate rates (R.D. pp. 274-275). The OCA argues that, by including these costs in rates automatically, PP&L effectively seeks authority to increase its rates an additional \$177 million by 1999. Additionally, these costs have not been included in Pennsylvania jurisdictional rates for over ten years. Therefore the OCA concludes that the Company's proposal creates perverse incentives for the Company in marketing this capacity off-system. For these reasons, argues the OCA, the ALJ correctly rejects the Company's proposal. (OCA R. Exc., pp. 28-29)

PPLICA also filed Reply Exceptions to the Exceptions of PP&L on this issue. PPLICA argues that, contrary to the assertions of PP&L, the PP&L proposal lacked the necessary checks and balances necessary to ensure a reasonable cost recovery. PPLICA observes that the PP&L proposal departs too far from traditional ratemaking and that the complaint process outlined by PP&L, as a check or balance, is too cumbersome and slow to be deemed a reasonable check on this proposal.

Additionally, PPLICA submits that this proposal is unreasonable in any event. This proposal would amount to

requiring that the Commission approve, prospectively, single issue rate increases without consideration given to any offsetting expenses, revenues, or other factors which may negate the necessity for the increases proposed by PP&L in the future. PPLICA concludes that the revenue requirement associated with the generating capacity being sold should not be an issue in this base rate proceeding as those revenue requirements are allocated to PP&L's wholesale jurisdiction. (PPLICA R. Exc., pp. 12-14)

The OCA also filed Exceptions to the ALJ's recommendation on this issue. It is the position of the OCA that, while the ALJ properly rejects the Company's initial proposal to recover the capacity costs associated with expiring off-system sales, the ALJ improperly recommends acceptance of the Company's alternative proposal. Under the Company's alternative proposal, PP&L recommended that, if ECR recovery of the capacity related costs was denied, then all revenues from off-system capacity-related sales should also be excluded from the ECR and treated as an element of base rates in this case. In addition, the Company asked that it be granted authority, in this case, to retain the energy savings related to this returning capacity, if its proposal is denied.

The OCA continues that, while it does not object to the ALJ's approval of the Company's proposal to exclude off-system sales from the ECR and treat them as an element of base rates, the ALJ did not reflect the approximately \$20.8 million of revenues from these sales in base rates in determining the Company's pro forma revenues. The OCA further excepts to the ALJ's approval, in this proceeding, of the Company's proposal to retain the energy savings associated with this capacity in any future ECR cases. The OCA is not arguing at this time that the Company be prohibited from retaining these energy savings, but is arguing that it is premature to rule on this request at this time

when the full circumstances surrounding the appropriateness of such request cannot be known.

(OCA Exc., pp. 58-59)

PP&L responds to the OCA's Exception by noting that the OCA and PPLICIA have asserted that, if the Company's primary ECR proposal is rejected, the amount of the rate increase should be recalculated to reflect approximately \$20 million of off-system capacity-related sales revenues included in the ECR. PP&L states that, if its primary proposal is rejected, the Company is not opposed to the transfer of these revenues into base rates.

Next, PP&L responds to the OCA's Exception discussed supra, i.e., that the ALJ erred in adopting the Company's alternative proposal to exclude from the ECR both the capacity costs and energy savings associated with the returning capacity. PP&L argues that its approach on this issue is fair, reasonable and appropriate and provides for consistent treatment of capacity costs and energy savings. The OCA has argued that the Company's proposal is premature and inappropriately seeks "blanket" approval. In fact, the Company does not seek any "blanket" approval, it simply seeks establishment of consistent ratemaking treatment of the capacity costs and energy cost savings associated with the returning capacity. PP&L also asserts that approval now will not provide the Company with any additional discretion or opportunity to increase its profits. (PP&L R. Exc., p. 38)

The Sierra Club also excepts to the recommendation of the ALJ, arguing that the ALJ should have recommended terminating the Company's ECR in order to foster the most economically efficient purchases of energy resources. (Sierra Exc., pp. 20-22)

In response to the Exception of the Sierra Club, the Company notes that the Club presented no evidence to support its proposal. In contrast, asserts the Company, the many benefits of the ECR are addressed in PP&L's Initial Brief, pp. 290-291, and fully support its continuation. (PP&L R. Exc., p. 38)

On review of this issue, we concur with the ALJ's recommendation, that the Company's primary proposal be rejected but that the Company's alternative proposal be accepted.

Although this issue is presented in the context of ECR, it is really a second "excess capacity" matter. In 1983, the Commission found 945 MW of excess capacity equivalent to the PP&L ownership of the new Susquehanna 1 plant and excluded a return on PP&L's investment in a 12.6% slice of its system. All return of investment through depreciation, as well as operation and maintenance expenses, was included in rates. In 1985, the Commission disallowed all common equity return on the 945 MW of Susquehanna 2, and PP&L sold the capacity by contract to JCP&L. As noted in our discussion supra, these contracts are now expiring, and PP&L's primary proposal on this issue was to include all costs and sales of such capacity in the ECR. As discussed supra, we reject this primary proposal.

Alternatively, the Company proposes, and the ALJ recommends, keeping all expenses and revenues derived from this capacity off-system until such time as they are included in base rates. We approve this recommendation as part of the normal ratemaking process. The capacity associated with the JCP&L contract should remain non-jurisdictional, and the Company is free to market an eventual total of 945 MW of capacity, thereby retaining revenues from the incremental off-system capacity related sales.

Therefore, the Exceptions of the Company, the OCA, and the Sierra Club are all denied, to the extent they are inconsistent with our resolution of this issue, outlined supra.

C. Exclusion of Sierra Club Testimony

The Sierra Club, starting at page 13 of its Main Brief, requests that the ALJ's exclusion of certain testimony by its witness be reversed. It provides a plan, for use if the ALJ's ruling is reversed. PPLICA responds to this request, commencing at page 45 of its Reply Brief. In addition, PP&L touches on this matter, commencing at page 128 of its Reply Brief. PP&L opposes a reversal of the ALJ's ruling.

PPLICA responded in greater detail, starting at page 45 of its Reply Brief. It observes that the original Motion to Strike was made by PPLICA. It outlined the substantial argument which was presented at that time. PPLICA referred to a one month delay before the Sierra Club asked that the ALJ certify the matter up to the Commission, which request was rejected by the ALJ. PPLICA referred to the argument at the briefing stage of this matter as well as Commission regulations. It stresses the need for timeliness of requests. It even addressed some of the merits of the Sierra Club positions.

The ALJ states that he is in fundamental agreement with the positions taken by PPLICA, concerning this matter, and that he would adhere to his original ruling and to his ruling denying certification. The ALJ notes that the Sierra Club did not bring the matter before the Commission itself, prior to the close of the record, or at any time before briefs were filed.

On review, we agree with the ALJ's disposition of this matter.

D. OCA Financial Impact

The OCA addressed this topic, commencing at page 321 of its Main Brief. It referred to testimony in the rebuttal phase, by PP&L's witness Berish. This witness responded to the OCA rate reduction recommendation. The OCA submitted that the Berish argument, that the OCA recommendations would unreasonably impair PP&L's financial condition, is based on incorrect assumptions and must be dismissed.

The OCA provides further arguments. Among other things, the OCA referred to rate of return. The ALJ stated that he discerned no reason to address this matter, directly, and that he brought up this matter only to point out the OCA argument and for the sake of completeness. The ALJ then observed that the OCA would reduce PP&L test year rates by \$66,464,000.

We also note the OCA argument on this issue for the sake completeness. The ALJ is correct that this argument by the OCA does not require further comment.

E. PP&L Public Input Issues

PP&L, commencing at page 296 of its Main Brief, provided several pages of discussion relating to Public Input hearings. The ALJ stated that he referred to this section largely for the sake of completeness, and to point out the arguments presented by the party.

PP&L reviewed, and characterized, testimony. It grouped comments into four major categories. It provided some of its own responses. It touched on such matters as its proposal to modify its rate schedule RTS position. It also touched on impact for individual businesses and economic development in the region. It addressed the contributions of Mr. Epstein in some detail. It

viewed certain issues raised by Mr. Epstein as totally refuted by PP&L and not relevant and suggested that they be disregarded.

The ALJ states that he sees no reason to specifically rule on what PP&L presented here and that he deals with some of these matters elsewhere in his Recommended Decision.

As with the immediately preceding heading, we are noting the public input issues here for the sake of completeness. As noted by the ALJ, this topic does not require a specific ruling.

IX. CONCLUSION

Based on the foregoing, we conclude that the Company has demonstrated entitlement to file tariffs or tariff supplements affording it an opportunity to achieve additional annual revenues of \$2,507,896,000 or an increase of \$85,125,000 over existing rates;

THEREFORE, IT IS ORDERED:

1. That Pennsylvania Power & Light Company shall not place into effect the rates contained in Supplement No. 50 to Tariff Electric-Pa. P.U.C. No. 200, the same having been found to be unjust, unreasonable and, therefore, unlawful.

2. That Pennsylvania Power & Light Company may file tariffs or tariff supplements containing rates, provisions, rules and regulations which are consistent with this Opinion and Order and are designed to produce annual operating revenues not in excess of \$2,507,896,000 on a Pennsylvania jurisdictional basis.

3. That the tariffs or tariff supplements mentioned in paragraph two, above, may be filed to become effective on one day's notice.

4. That Pennsylvania Power & Light Company shall file detailed calculations, with its tariff filing, which shall demonstrate, to the Commission's satisfaction, that the filed rates comply with the Commission's order concerning this proceeding.

5. That Pennsylvania Power & Light Company shall comply with all directives, conclusions and recommendations contained in the body of the Recommended Decision, which are not the subject of an individual directive in these ordering

paragraphs, as fully as if they were the subject of a specific ordering paragraph.

6. That the complaints filed by other parties to this base rate proceeding, docketed at R-00943271, that is, docket numbers R-00943271C0001 through R-00943271C0145, are granted or denied to the extent consistent with the Recommended Decision.

7. That, upon Commission approval of the tariffs filed in compliance with the Commission's order, these proceedings at R-00943271 shall be closed.

BY THE COMMISSION

John G. Alford
Secretary

ORDER ADOPTED: September 27, 1995

ORDER ENTERED:

TABLE I
PENNSYLVANIA POWER & LIGHT COMPANY
INCOME SUMMARY
(Thousands of Dollars)

	Pennsylvania Public Utility Commission Jurisdictional Basis						
	Pro Forma Present Rates (1)	Company Adjustments	Pro Forma Present Rates (Revised) (2)	Commission Adjustments	Commission Pro Forma Present Rates	Commission Revenue Increase	Total Allowable Revenues
	\$	\$	\$	\$	\$	\$	\$
Operating Revenue	2,402,255	(368)	2,401,887	0	2,401,887	106,971	2,508,858
Expenses:							
& M Expense	1,372,927	2,481	1,375,408	(66,162)	1,309,246		1,309,246
Depreciation	320,797	0	320,797	(15,274)	305,523	0	305,523
Regulatory Debits/Credits	(29,208)	0	(29,208)	0	(29,208)	0	(29,208)
Taxes, Other	186,553	(17)	186,536	0	186,536	5,456	191,992
Income Taxes:							
State	54,478	(387)	54,091	6,200	60,291	11,156	71,447
Federal	154,601	(1,099)	153,502	15,210	168,712	31,626	200,338
Deferred Income Taxes	(15,424)	0	(15,424)	5,348	(10,078)	0	(10,078)
Investment Tax Credit	(8,625)	0	(8,625)	0	(8,625)	0	(8,625)
Emission Allowances	(466)	0	(466)	0	(466)	0	(466)
Total Expenses	2,035,633	978	2,036,611	(54,680)	1,981,931	48,238	2,030,169
Net Inc. Available for Return	366,622	(1,346)	365,276	54,680	419,956	58,733	478,689
Rate Base	5,017,178	530	5,017,708	0	5,017,708		5,017,708
Rate of Return	7.31%		7.28%				9.54%

(1) PP&L Exhibit Future 1, Schedule D-1

(2) PP&L Exhibit Future 1 (Revised), Schedule D-1

TABLE II
PENNSYLVANIA POWER & LIGHT COMPANY
SUMMARY OF ADJUSTMENTS
(Thousands of Dollars)

PENNSYLVANIA PUBLIC UTILITY COMMISSION JURISDICTIONAL BASIS

Adjustments	Rate Base	Revenues	Expenses	Depreciation	Taxes-Other	State Income Tax	Federal Income Tax	Deferred Income Taxes
	\$	\$	\$	\$	\$	\$	\$	\$
RATE BASE:								
Excess Capacity								
REVENUES:								
EXPENSES:								
Benefit Savings/Employee Red.			(171)			19	53	
Susq. Unit I "Early Window" Deferral			(2,035)			224	634	
Environmental Remediation Costs			(326)			38	102	
Uncollectible Accounts:								
Regular Uncollectible Accounts			(1,234)			136	384	
On-Track Program			(130)			14	41	
Rate Case Expense			(373)			41	116	
Nuclear Decommissioning:								
Contingency Factor			(2,516)			277	784	
Post-Shutdown Earnings			(2,436)			268	759	
Trust Fund Rate			(9,157)			1,006	2,853	
Fossil Fuel Plant Decommissioning			(45,284)			4,977	14,107	
Social Programs			(2,500)			275	779	
			0			0	0	
			0			0	0	
DEPRECIATION EXPENSE:								
Fossil Fuel Plant Depreciation				(15,274)				5,346
TAXES:								
Consolidated Tax Savings						0	(2,161)	
Adjustments to Taxable Income						(851)	(2,413)	
Tax Deficiency Accruals						(213)	(804)	
Interest Synchronization (Table III)						(9)	(24)	
TOTALS	<u>0</u>	<u>0</u>	<u>(66,162)</u>	<u>(15,274)</u>	<u>0</u>	<u>6,200</u>	<u>15,210</u>	<u>5,346</u>

TABLE Ia
PENNSYLVANIA POWER & LIGHT COMPANY
INCOME SUMMARY
(Thousands of Dollars)

	Pennsylvania Public Utility Commission Jurisdictional Basis				
	Total Allowable Revenues	Alternative ECR Adjustment	Adjusted Allowable Revenues	Required Revenue Decrease	Net Allowable Revenues
	\$	\$	\$	\$	\$
Operating Revenue	2,508,858	20,884	2,529,742	(21,846)	2,507,896
Expenses:					
O & M Expense	1,309,246		1,309,246	0	1,309,246
Depreciation	305,523	0	305,523	0	305,523
Regulatory Debits/Credits	(29,208)	0	(29,208)	0	(29,208)
Taxes, Other	191,992		191,992	(1,114)	190,878
Income Taxes:					
State	71,447	2,295	73,742	(2,278)	71,464
Federal	200,338	6,506	206,844	(6,459)	200,385
Deferred Income Taxes	(10,078)	0	(10,078)	0	(10,078)
Investment Tax Credit	(8,625)	0	(8,625)	0	(8,625)
Emission Allowances	(466)	0	(466)	0	(466)
Total Expenses	2,030,169	8,801	2,038,970	(9,851)	2,029,119
Net Inc. Available for Return	478,689	12,083	490,772	(12,083)	478,689
Rate Base	5,017,708		5,017,708		5,017,708
Rate of Return	9.54%		9.78%		9.54%

(1) PP&L Exhibit Future 1, Schedule D-1

(2) PP&L Exhibit Future 1 (Revised), Schedule D-1

PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania

PENNSYLVANIA P.U.C.
ET AL.

v.

PENNSYLVANIA POWER
& LIGHT COMPANY

PUBLIC MEETING-
SEPTEMBER 27, 1995
SEP-95-OSA-219*
DOCKET NO. R-943271

STATEMENT OF COMMISSIONER JOHN HANGER

Today's majority decision provides an overall rate increase of approximately \$ 107 million, averaging 4.8%. This is considerably below the \$261 million requested by PP&L which would have increased base rates for the first time since 1985 by an average of 11.7%. While I support the majority position on most issues, as indicated in the polling of the issues on August 31, I would reach a different result on several issues. I am especially delighted to see that the final result concerning industrial customers who receive interruptible service is dramatically different than as polled originally.

Not all customers receive the same percentage increase, depending primarily on their class of service and levels of usage. As originally polled, industrial customers on interruptible rates would have received a whopping increase of 22%, even if no general rate increase were granted. This is because the company proposed to eliminate interruptible service as a distinct class of service and to switch interruptible pricing entirely to a "value of service" approach. All other customer classes have their rates determined based primarily on "cost of service".

The final result today revises the result on this issue as originally polled to recognize that interruptible service is a distinct class of service that is inferior to firm service. As a result, the entire rate increase for interruptible customers will be reduced to about 5-7%, as opposed to an increase of more than 25% based on the August 31 polling.

Interruptibility remains a fact of life. It is not just a theoretical possibility. As recently as the heat wave this summer, with record-shattering usage, PP&L's interruptible customers had service curtailed from July 31 through August 4, 1995 so that other customers could continue to receive service reliably. Interruptible service remains a valuable tool for utilities to manage peak load. It also remains a desirable option for customers who can take advantage of lower prices by agreeing to be interrupted in the event that it is necessary.

Since PP&L does not take into account the need to provide service to interruptible customers in its generation planning, it is appropriate to exclude generation from cost of service allocations for interruptible customers. Thus, interruptible service is a distinct class of service that has a much lower cost

of service, and interruptible customers should receive recognition of these facts in ratemaking. The final decision today does just that.

The value of service principles proposed by the company are appropriate considerations in ratemaking as well, but should not be adopted in this case. To do so would yield exorbitant rate increases which contradict cost of service principles as well as the important principle of gradualism. The rate increase for all other classes of services has been limited to 1.5 times the system average increase, and there is no reason to impose an increase that is as much as ten times the average increase on this one class of customers. Imposing rate shock on the largest employers in Pennsylvania would be an insane result. It can only result in stifled economic development and the loss of existing jobs.

Moreover, it would be especially counterproductive since the affected customers are precisely those most able and willing to seek alternative electric service in an increasingly competitive electric industry. Forcing the largest customers off the system or giving them more and more competitive discounts only serves to impose the existing fixed costs of operating PP&L on the smaller and smaller class of core customers who do not have competitive alternatives. Permitting competition to benefit only a small group of customers leaves everyone else worse off. Consequently, it is imperative that a fair and orderly transition that gives all customers choice be started as soon as possible. Only when all customers have the power of choice can competition benefit all ratepayers.

Finally, this case and the proposed merger of PP&L and Peco Energy indicate the urgency of moving forward to address the increasing role of competition in the electric industry. In particular, the issues of excess capacity, rate of return, interruptible service, and economic development/competitive rates clearly indicate the pervasiveness of impending competition. If Pennsylvania does not address these issues now, they will not disappear. To the contrary, it is far more likely that competitive pressures will expand even further, making a reasonable transition to customer choice more difficult. We must take the reins to guide these developments. The sooner that we do so the better it will be for Pennsylvania's consumers, and the utilities and their shareholders and employees.

September 26, 1995
Dated

John Hanger
JOHN HANGER, COMMISSIONER