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November 17, 2015

Via Electronic Filing

Rosemary Chiavetta, Secretary
PA Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: Petition of Philadelphia Gas Works for Waiver of Provisions of Act 11 to Increase the Distribution System Improvement Charge Cap and to Permit Levelization of DSIC Charges, Docket No. P-2015-2501500

Dear Secretary Chiavetta:

Oh behalf of Philadelphia Gas Works ("PGW") enclosed for filing please find its Reply Brief with regard to the above-referenced matter. Copies of the above filing have been served in accordance with the attached Certificate of Service.

Sincerely,



Daniel Clearfield

DC/lww
Enclosure

cc: Hon. Christopher P. Pell w/enc.
Hon. Marta Guhl, w/enc.
Cert. of Service w/enc.

CERTIFICATE OF SERVICE

I hereby certify that this day I served a copy of PGW's Reply Brief upon the persons listed below in the manner indicated in accordance with the requirements of 52 Pa. Code Section 1.54.

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

PETITION OF PHILADELPHIA GAS :
WORKS FOR WAIVER OF PROVISIONS : Docket No. P-2015-2501500
OF ACT 11 TO INCREASE THE :
DISTRIBUTION SYSTEM :
IMPROVEMENT CHARGE CAP AND TO :
PERMIT LEVELIZATION OF DSIC :
CHARGES :

**PHILADELPHIA GAS WORKS'
REPLY BRIEF**

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Docket No. D-2015-24681411

I. INTRODUCTION AND STATEMENT OF THE CASE¹

Philadelphia Gas Works (“PGW” or “Company”) hereby submits this Reply Brief in response to the Briefs of the Office of Consumer (“OCA”), the Office of Small Business Advocate (“OSBA”) and a group of six commercial customers (Philadelphia Industrial and Commercial Gas Users Group, known as “PICGUG”).

While claiming to agree that PGW’s antiquated cast iron distribution mains need to be replaced more quickly, all of the above parties oppose increasing PGW’s Distribution System Improvement Charge (“DSIC”) by just \$11 million a year or about 1.6% of PGW’s intrastate revenues.² They have raised these protests despite the fact that, due to lower natural gas costs, even after this modest increase, DSIC customer rates will actually be several hundred dollars less than in 2013, when PGW initiated its DSIC.

The obvious conclusion is that this is the ideal time to effectuate a modest increase in PGW’s DSIC charge. The proposed increase will cut PGW’s projected cast iron main replacement time by almost one-half, a significant improvement in the timeline for reducing PGW’s cast iron main inventory, one of the largest of any natural gas distribution company, reduce repair costs and cut leaks. However, if PGW is denied the right to increase its DSIC to 7.5% (not including reconciliation) it simply will not be able to further accelerate its main replacement program at this time and would have to revisit the issue in PGW’s next base rate case (scheduled to be filed for rates to be effective in 2017). Then, PGW would only be able to

¹ For ease of reference, PGW’s Reply Brief uses numbering that tracks the Main Brief outline, and certain numbered items may not be addressed in this Reply Brief. Any terms with initial capitalization that are not defined in this Reply Brief are defined in PGW’s Main Brief. The term “MB” is used to cite to Main Briefs.

² PGW Petition at 14. PGW’s total revenues, in Fiscal Year 2014, was \$759,136. See PGW’s Final Stratified Management and Operations Report, Docket No. D-2015-2468141 (dated August 2015) at Exh. V-3.

advance its program – after already losing at least two years of acceleration – if its rate levels permit such additional expenditures without threatening the overall financial health of the Company. Further, if PGW is not able to begin to bill customers at the new, higher rate in January, after the Commission rules on PGW’s Petition, the Company will only be able to collect less than ½ of the incremental \$11 million in 2016, thereby slowing its planned 2016 main replacement.

Recognizing the benefits of further accelerating PGW’s main replacement program without delay, the PUC’s Bureau of Investigation and Enforcement (“I&E”) has endorsed PGW’s Petition, as modified by additional procedures and commitments as set forth in a Stipulation entered into between PGW and I&E and has recommended that PGW be permitted to start billing at the 7.5% level on or after January, 2016. This agreement with I&E is significant because it represents an endorsement by: 1) the PUC division with the primary responsibility in the Commonwealth to advance and maintain natural gas safety (the Gas Safety Division); and 2) the entity within the PUC charged with representing the public interest in ratemaking and service matters.³ Accordingly, I&E’s endorsement in this type of proceeding should provide the Commission with sufficient assurances that PGW has shown that waiving the 5% DSIC in favor of a 7.5% cap is appropriate to “ensure and maintain adequate, efficient, safe reliable and reasonable service” and is in the public interest.⁴

While the Parties opposing PGW’s Petition raise a variety of arguments most of them are a variation on “we want the benefits but don’t want to pay (even a modest amount) to receive them.” But the reality is that:

³ See, I&E MB at 2-3.

⁴ I&E MB at 8-11.

– none of these parties has any experience with natural gas distribution system safety issues, in contrast to the Commission’s Gas Safety Division; and

– these parties apparently do not have a clear understanding of PGW’s financial status or its unique ratemaking methodology, which limits PGW to only one source to finance capital improvements – its ratepayers (either through direct pay or via bonds). Forcing PGW to use existing funds in lieu of a DSIC increase is either contrary to that ratemaking methodology and law (*i.e.*, appropriating the City Fee) or would create a cash hole for the Company and additional financial risk that would threaten the relative financial health that PGW has been able to attain – with the PUC’s help – over the last several years.⁵ Accordingly, PGW respectfully requests that the Commission reject these arguments and grant PGW’s Petition, as modified by the PGW/I&E Stipulation.

IV. WAIVER OF 5% LIMITATION AND AUTHORIZATION FOR HIGHER MAXIMUM ALLOWABLE DSIC

B. Standard For Granting The Waiver Of 5% Cap

All of the parties except two agree that the standard for determining whether the Commission should waive the statutory cap in Act 11 is whether such waiver will “ensure and maintain adequate, efficient, safe, reliable and reasonable service.”⁶ The OCA notes that if a utility presents evidence that satisfies the “ensure and maintain adequate, efficient, safe, reliable and reasonable service” standard then “the Commission has discretion whether or not to grant a waiver.” While PGW does not disagree (the Commission always has discretion), such discretion

⁵ With regard to the City Fee, and as explained below, if requested by the Commission, PGW would be willing to formally ask its owner, the City of Philadelphia, to grant back the City Fee in order to use it for additional main replacement, over and above that made possible by increasing PGW’s DSIC to 7.5%.

⁶ 66 Pa. C.S. § 1358(a)(1).

obviously must be exercised in a manner that is not arbitrary and capricious and advances the public interest.⁷

The only parties that appear to disagree that the appropriate standard is as stated above are OSBA and PICGUG. OSBA maintains that “in order to meet its burden on [the issue of increasing the CAP] PGW must demonstrate that there are no reasonable alternatives for providing efficient, safe, reliable and reasonable service beyond the requested waiver.”⁸

Similarly, PICGUG claims that the cap may not be raised unless PGW proves that raising the cap is “necessary” to ensure a safe system, which allegedly means exhausting all other funding alternatives.⁹ Neither party cites any legal authority for these contentions, because there is none in Act 11.¹⁰ If the General Assembly intended that a utility seeking to waive the statutory 5% cap had to show that there were “no other alternatives” to adequately fund its accelerated infrastructure program it would have said so. It did not.¹¹ OSBA further asserts that “if the General Assembly had intended that utilities could evade the legislated cap by simply making vague claims that they would possibly be negatively impacted by the cap there would have been

⁷ *Accord*, I&E MB at 6. (“I&E avers that increasing PGW’s DSIC to 7.5%, independent of reconciliation, is in the public interest because it will facilitate PGW’s replacement of dangerous cast iron mains in a more timely manner ultimately promoting safe and effective service to PGW’s customers.”).

⁸ OSBA MB at 7.

⁹ PICGUG MB at 4-5.

¹⁰ PICGUG claims that the PUC’s Implementation Order added the requirement that a party must show that the waiver was “necessary” but PICGUG has concocted a meaning for “necessary” that is illogical and contrary to its common meaning, and, in any event, the Commission may not add a requirement that doesn’t exist in the law.

¹¹ 66 Pa. C.S. § 1358(a)(1) (“The commission may upon petition grant a waiver of the 5% limit under this paragraph for a utility in order to ensure and maintain adequate, efficient, safe, reliable and reasonable service.”).

little reason to establish the consumer protection in the first place.”¹² First, granting a waiver from the cap, in accordance with the standard set forth in the law is not an “evasion;” if the General Assembly had intended that the 5% cap be inviolate it would not have put in the waiver process in the Statute. Second, PGW agrees that a waiver of the cap would not be appropriate if it was merely based on vague claims about possible negative impact of the cap. But, contrary to OSBA’s implication, PGW’s request is supported by persuasive evidence of the need to further expedite its at risk main replacement program in order to maintain the safety and reasonableness of its service, and that a 7.5% DSIC expenditure level is reasonable.¹³ PGW showed that the 7.5% cap level (exclusive of reconciliation) was reasonable because:

- it reduced the projected time it would replace all cast iron main by almost ½;¹⁴
- the expedited main replacement would, over time, reduce leaks, breaks, unaccounted for gas and pipe repair and maintenance costs;¹⁵ and
- in light of these benefits, the effect on customers was extremely modest.¹⁶

OSBA’s unsupported assertions should be rejected.

C. Has PGW Met the Standard for Waiver of 5% Cap?

1. The Parties’ Arguments in Support of Their Claim That PGW Should Be Required to Fund the DSIC From Alternative Sources Are Baseless and Should Be Rejected

¹² OSBA MB at 7.

¹³ See, PGW MB at 8-33.

¹⁴ PGW St. 1 at 10.

¹⁵ PGW St. 1 at 12.

¹⁶ Appendix A to PGW Petition at A-20.

Despite their professed claim that they support PGW's position that an accelerated main replacement program would be prudent to ensure the safety and reasonableness of its natural gas distribution system,¹⁷ OCA and OSBA (PICGUG does not bother to comment either way) insist that PGW's Petition should nonetheless be rejected particularly in light of the "total bill impact" on customers. Accordingly, the parties claim that PGW should be forced to first pursue other funding sources such as internal generation.¹⁸ These claims are outside the scope of this proceeding and not supported by the record.

First, as indicated in PGW's Main Brief, there is simply no basis for suggesting that PGW must search out other sources of funding rather than utilizing the mechanism approved by the General Assembly to fund accelerated main replacement. There is nothing in Act 11 which suggests such an inquiry and PGW submits that such contentions are not appropriate for a DSIC proceeding.¹⁹ There is absolutely no support for the notion that PGW must prove that it does not have other sources of revenue – essentially that its existing rates are not excessive – before it may modestly increase its DSIC in order to undertake accelerated main replacement found to be appropriate to ensure safe and reliable service. To the extent that OCA (or the other parties

¹⁷ See Tr. 102-103; OSBA St. 1 at 3.

¹⁸ OCA MB at 9-14; see also PICGUG MB at 5-6.

¹⁹ See, *Implementation of Act 11 of 2012*, Docket No. M-2012-2293611, Final Implementation Order entered Aug. 2, 2012 ("Implementation Order") at p. 6 fn 18. While OCA cites the provisions in Act 11 which require the Commission to reset a utility's DSIC to zero if the utility is earning an excess of an authorized rate of return (OCA MB at 9), OCA has misunderstood this section. First, this resetting provision does not apply to the level of the DSIC cap but creates a separate process by which the Commission can zero out the DSIC at any point if an investor-owned utility is found to be earning excessively. This separate process does not authorize the arguments about "alternative funding" that OCA (as well as OSBA and PICGUG) have made here. Moreover, even though it acknowledged that, for PGW, any such independent analysis would have to be pursued pursuant to the PGW ratemaking standard set forth at 52 Pa. Code § 69.2703, OCA presented no evidence whatsoever that would indicate that the Company's rates, overall, are excessive with or without increased DSIC funding levels. In any event, this clearly is a separate process that can be pursued by the Commission or OCA after the Commission rules on PGW's Petition to waive the DSIC cap.

making this claim) believes PGW's rates are excessive it can file a complaint with the PUC to that effect or raise them in PGW's next base rate case. While any and all of these claims of "alternative" revenues could be addressed in those forums (and result in a denial of a rate increase or even a base rate decrease), they are completely inappropriate here.

Importantly, the PUC has made clear that the DSIC "is intended to be a straightforward mechanism which is easy to calculate, easy to audit and which does not require a full rate case analysis," and [the DSIC] "is not intended to revisit matters decided [in past rate cases]."²⁰

The PUC was certainly correct in its decision to block considering such issues in a DSIC proceeding; permitting these "alternative funding" analyses would result in the unfair "cherry picking" arguments in which the OCA, OSBA and PICGUG have engaged. That the issues raised by these parties are actually for PGW's next rate case can be seen by reviewing the PUC's policy statement setting forth the variety of factors that must be examined in establishing just and reasonable rate levels for PGW. That statement indicates that, in setting just and reasonable rate levels for PGW the Commission will examine a number of factors, including PGW's level of year end cash, its debt to equity ratios and the "the level of financial performance needed to maintain or improve PGW's bond rating..." None of the opposing parties has presented any evidence analyzing all of these various factors, and plucking one item from that list without considering the effect on the Company and ratepayers of all the other items is not only outside the scope of this proceeding but would be wrong and grossly unfair.

But perhaps just as important, there is absolutely no basis for suggesting that PGW has "other funding sources" that could be safely utilized to fund accelerated main replacement. Initially, it is important to recall that, as a municipally-owned natural gas distribution company,

²⁰ Implementation Order at 29.

PGW is owned by the citizens of Philadelphia – it has no shareholders. Moreover, as a “cash flow regulated” Company, PGW does not earn a return on its \$1.2 billion distribution system; its sole source of funding for operations is from ratepayers or by issuing bonds (the costs of which are also paid by ratepayers). Moreover, PGW does not make a dime on its DSIC; 100% of the dollars billed are used to fund accelerated main replacement authorized by its LTIP.²¹ Thus, when parties demand that PGW should not be permitted to increase its DSIC surcharge but should instead fund accelerated main replacement from non-ratepayer sources of funding such as “cost savings” or by reducing its end of year cash balances, the parties fail to grasp that all of these “sources of funds” ultimately are from ratepayers. Utilizing these sources rather than the DSIC merely means that PGW’s existing base rates would be commandeered, and the deficiencies created would have to be filled in PGW’s next rate case. In the meantime however, such an approach would threaten PGW’s financial health, risk downgrading PGW’s bonds, and could put the Company on the downward spiral that resulted in its requiring extraordinary rate relief just a few years ago.

Just as important, PGW is already utilizing any cost savings or additional IGF it has managed to produce since its last rate case to fund increases in expenses and in its capital budget since its last rate case. As PGW’s acting Chief Financial Officer Joseph Golden explained,

PGW is utilizing all funds received since the last rate case in 2010 to fund the net increases and decreases of operating expenses and also in our capital budget. In 2010 we had a capital budget of approximately \$58 million. In 2015 that budget – we didn’t close our year end books yet but that is anticipated to be about \$90 million including the DSIC component; and if you take that out it still a

²¹ The OCA references a statement by OSBA claiming that DSIC changes will add to City equity implying that PGW is somehow trying to improve its financial position through the DSIC. OCA MB at 11, ft. 3. This is nonsense. OSBA and OCA have misread the financial analysis provided by PGW. The improvement in City equity comes from an assumption in PGW’s financial analysis of two base rate increases – one in 2017 for \$40 million and one in 2021 for \$20 million. PGW St. 3-R at 4. PGW does not make a dime as a result of its DSIC; every dollar billed is used to finance main replacement. Any dollars not so used are returned to ratepayers, with interest.

great increase from our 2010 level. In 2016 we're forecasting approximately a \$110 million spend which would include only a portion of the increase in DSIC proposed here today.²²

Importantly, it should be noted that PGW's "non-DSIC" construction budget which must be funded by the Company's internally generated funds ("IGF"), produced from current rates. IGF is referenced as an "alternative source of revenue" by OCA and OSBA.²³ But PGW's IGF is already funding PGW's legacy, 18 mile per year main replacement program as well as the cost of construction for a variety of items necessary to maintain adequate service including maintaining PGW's gas processing plants, field services and replacement of customer service lines.²⁴ So to the extent PGW has additional IGF it is already spoken for.

Nonetheless, both OCA and OSBA continued to insist that PGW could utilize its existing internally generated funds to fund increased main replacement without any adverse financial effects on the Company. Both appear to have completely ignored additional testimony of Mr. Golden who explained that any such attempt to fund an additional \$11 million a year for accelerated main replacement from the IGF produced by PGW's base rates would create serious financial risks for the Company.

Even if it were appropriate to consider base rates as a funding source for this program, it would not be feasible to fund the proposed main replacement program through existing base rates without having a negative effect on the Company's financial health. Mr. Knecht's chart on page 5 of his testimony (Table IEC-1) shows PGW's current budget projections assuming that its

²² Tr. 68; Exh. JFG-2.

²³ OSBA St. 1 at 4; OCA St. 1 at 10-11.

²⁴ Tr. 70. In a pre "Act 11" the Commission considered and rejected similar arguments from the OCA and OSBA demanding that a water distribution utility utilize other sources of funding rather than increase its DSIC cap. See, *PA PUC v. Aqua Pennsylvania, Inc.* R-2008-2079310 (July 23, 2009). After reviewing the claims by OCA and OSBA and Aqua's response that any additional funds were being used to fund its non-DSIC construction the Commission stated that "we recognize that there are other sources of capital that may delay or offset increases in the DSIC surcharge. However, these funding sources do not eliminate need to increase the cap." *Id.* at 14.

accelerated main replacement is funded via DSIC and it receives a \$40 million base rate increase in September 2017 and a \$20 million base rate increase in fiscal year 2021. Understandably, those financial indicators are not seriously eroded during the period reviewed. However, Mr. Knecht fails to recognize that using some \$11 million from PGW's existing base rates to fund these additional capital improvements would erode its financial indicators to unacceptable levels. . . . Attached hereto is a report from an investment rating service. The report has made clear that, to maintain its current, mid-level bond rating (which has improved from the "one step above junk bond" level in 2008), PGW needs to have at least 60-90 days of cash on hand at fiscal year-end. PGW's currently projected level of cash . . . equates to approximately 65 days of cash on hand at fiscal year-end. Funding \$11 million of accelerated main replacement from base rates would reduce PGW's cash levels to 59 days of cash on hand, below the level at least one investment service characterizes as the minimum for a public power company of "mid-range" financial strength.²⁵

Mr. Golden also explained that funding the DSIC increase from current base rates would also reduce PGW's coverages to 1.59x and have a negative effect on its debt-to-total capitalization ratio. Mr. Golden summarized the concerns as follows:

The Commission is well aware that PGW has only recently emerged from over a decade of extreme financial distress in which it had to ask for and receive at least three emergency or extraordinary rate increases, regularly hit up against its maximum short-term borrowing ability, and, due to the complete lack of internally generated funds, had to issue long-term debt such that its debt to total capitalization ratio reached approximately 85%. PGW had to fully utilize its short-term debt (commercial paper) program merely to have sufficient cash on hand throughout the year to pay its obligations, leaving it with no "cushion" or fallback for contingencies. Due to the Commission's willingness to permit PGW to receive necessary rate increases, as well as PGW's work to improve efficiencies, increase collections and manage expenses, PGW's financial position has improved in the last few years. . . . The Company certainly would not risk this recent improvement in its financial position by incurring the significant obligation represented by the main acceleration program PGW has proposed here without the assurance that the additional expenditures will be funded from the DSIC – or some other new source of revenues. To do otherwise would risk the

²⁵ PGW St. 3-R at 4-5. PICGUG criticized Mr. Golden's use of the Fitch Report claiming that, since it was written for the "public power" industry and was not specific to PGW it was "misleading." PICGUG unfairly ignored Mr. Golden's testimony in which he explained that the report was indicative of what rating agencies are looking for from PGW, since the Company is similar to the types of companies considered in the Fitch Report. Tr. 83-84.

financial health of the Company that has been so long in developing and redound to the detriment of its customers.²⁶

Similarly, OSBA's argument that PGW could simply use short or long-term borrowing to finance its accelerated main replacement program until its next base rate case without any negative financial effects is also inconsistent with the evidence and should be rejected.²⁷ With respect to OSBA's assertion that PGW could use its short-term borrowing capacity to finance the \$11 million per year Mr. Golden responded as follows:

Short-term borrowing in the amount of even \$11 million would put a strain on our available commercial paper program. At the end of fiscal 2015, PGW had already utilized \$30 million of that \$120 million program. We anticipate in our fiscal '16 which just started September 1st to utilize approximately another \$50 million from that program.

So we would already have utilized \$80 million of the \$120 million program, and that would only leave us about \$40 million for short-term either capital or operating needs. For operating needs that was the original intention of the commercial paper program for working capital through the winter and the operating period. It's now been expanded to include short-term capital.²⁸

OSBA's contention that PGW could issue long-term bonds is similarly unwarranted. First, the process of issuing bonds is complicated, requiring not only PGW approval but City Council approval and is "a much more laborious process."²⁹

²⁶ PGW St. 3-R at 5-7.

²⁷ OSBA MB at 8-11.

²⁸ Tr. 72-73. Additionally the OSBA contention that the relevant period to examine is only the next two years until PGW files its next base rate case is misplaced. Since PGW finances its accelerated main replacement on a "pay as you go basis" all of the dollars it expends in a particular year are either recovered in that year from the DSIC or recovered in the reconciliation factor. Thus, if PGW were to reset its DSIC to roll unrecovered costs into base rates there would be no dollars in the DSIC to roll in. As Mr. Golden stated "I don't anticipate that [the DSIC] will be rolled in to base rates at our next request. I think it would stay as a surcharge." Tr. 71.

²⁹ Tr. 73.

But even if PGW were able to issue bonds before the next rate case, focusing only on the next two years and only on debt service has skewed the adverse effects that additional bond financing would have both on the Company and customers. As Mr. Golden explained “Mr. Knecht completely ignored the fact that customers must pay not only the debt service but the debt service coverage at an additional 50% for any bonds issued.”³⁰ An additional 50% “upcharge” would exist not only for the next two years until PGW’s next rate case but for the entire length of the bonds, usually 20 years, adding millions and millions of dollars that could be used for capital improvements. The OSBA analysis purporting to show that this long-term borrowing would be cheaper also appeared to actually borrow the money to pay the debt service in order to artificially keep cash balances at reasonable levels,³¹ and fails to account for PGW’s 4% uncollectible rate which would also affect the Company’s cash flow.³² Thus, even if PGW were able to issue a bond for just \$22 million before its next rate case, it would nonetheless have to find several million dollars a year to pay the cost of issuance, the debt service, the debt service coverage and the increased uncollectible amounts – all without any new source of funds to cover these additional costs. Mr. Golden’s original conclusion that the “pay as you go” approach is for ratepayers than bond financing.³³

But even if the long-term effects on customers were ignored, the OSBA approach would be bad for PGW’s financial health. Financing with bonds would add almost \$200 million of debt that would carry with it approximately \$12 - \$14 million debt service component and increase

³⁰ Tr. 73; PGW St. 3-R at 9.

³¹ Tr. 74.

³² *Id.*

³³ PGW St. 3-R at 9-10.

PGW's debt to total capitalization ratio, something that Mr. Golden indicated "I don't think . . . would be viewed very favorably [by bond rating analysts]... when there is another option available."³⁴

PGW has and will continue to use long-term debt to finance portions of its capital budget. In fact, it continues to contemplate issuing about \$250 million of debt in 2016 and another \$100 million in 2020.³⁵ Part of that debt will be used to continue to finance its existing legacy 18 mile program that is financed through base rates. It simply does not make any sense for PGW to incur still more debt – increasing its debt to total capitalization ratio and imposing additional unnecessary charges on customers when a much more reasonable and appropriate funding mechanisms – the DSIC – exists.

2. PICGUG's Claims that Reduced Cash On Hand are not a Valid Basis for Denying PGW's Petition

PICGUG contends that the 5% cap should not be waived until PGW reduces its cash on hand by \$25 million.³⁶ PICGUG's contention should be rejected because it was raised for the first time in its Brief. Even considered on its merits, the possibility of using a one-time reduction in cash on hand to fund accelerated main replacement is not viable, and would actually harm PGW's financial strength.

PICGUG never presented this contention on the record and this unfair sandbagging should not be permitted. However, if the Commission is going to consider this argument it can look to the testimony of PGW witness Golden to show that it is completely without merit. PGW

³⁴ Tr. 76.

³⁵ *Id.*

³⁶ PICGUG MB at 9-11.

witness Golden explained that, based on this experience and understanding, the level of cash on hand is a key determinant of the financial strength of a cash flow regulated utility and an indication of the adequacy of rates for a cash flow company.³⁷ Mr. Golden further testified that the bond rating agencies are looking for PGW to increase its days of cash on hand to provide continued financial flexibility and maintain or increase its current bond ratings.³⁸ In comparison, funding PGW's accelerated main replacement program from cash on hand (i.e., from current base rates) would reduce PGW's available levels of year-end cash.³⁹

The record shows that PGW's cash on hand cannot be reduced without the risk of impacting PGW's bond ratings. Reducing the level of year-end cash could risk a downgrade by rating agencies.⁴⁰ Currently, PGW is projected to have 65 days of cash on hand at fiscal year-end.⁴¹ Reducing cash on hand by \$11 million (just ½ of the amount suggested by PICGUG) would reduce PGW's cash levels to 59 days of cash on hand, well below the level at least one investment service characterizes as the minimum for a public power company of "mid-range" financial strength.⁴² PICGUG offered no testimony to show that PGW could reduce cash on hand without jeopardizing its current bond ratings. Having only recently improved its bond

³⁷ Tr. 82, 87, 90-91; PGW St. 3-R at 5-7. See 52 Pa. Code § 69.2703(a)(1).

³⁸ Tr. 82, 87, 90-91; PGW St. 3-R at 5-7.

³⁹ PGW St. 3-R at 5-7.

⁴⁰ *Id.*

⁴¹ PGW St. 3-R at 5.

⁴² PGW St. 3-R at 5-7; Exhibit JFG-1, FitchRatings, U.S. Public Power Rating Criteria at 9. As noted, Mr. Golden testified that Exhibit JFG-1 was indicative of his discussions with rating agencies indicating what they expected from PGW. Tr. 87. Consequently, contrary to PICGUG's claims, Exhibit JFG-1, together with Mr. Golden's testimony, fully supports his contentions. See PICGUG MB at 10.

ratings, PGW is not in a strong financial position so as to permit it to place its improved cash levels and its bond ratings in jeopardy.

Also PICGUG's logic is fundamentally flawed. The level of non-borrowed year-end cash is a relevant factor in PGW's existing and established rates.⁴³ Here, PICGUG's is seeking to change a key component of established rates, without a base rate case and without any examination of the other rate components. Under PICGUG's logic, it could simply request that in order to "fund" infrastructure improvements, a return on equity for an investor-owned utility could be reduced from 12% to 10% and the resulting "excess rates" could be similarly appropriated. That cannot be done (legally), and the Commission should not, in this proceeding, direct PGW to reduce its cash on hand to fund the accelerated replacement of "at risk" mains in the context of a DSIC proceeding.

That being said, nothing in the records support the reduction of cash on hand as a viable under the circumstances. PICGUG's contention appears to be based entirely on a recommendation in the PUC Staff Report.⁴⁴ The PUC Staff Report explained that the option of reducing cash on hand should be used if, *inter alia*, PGW had the ability to fund seasonal fluctuations with its commercial paper program.⁴⁵ PICGUG offered no testimony on how PGW could fund its seasonal fluctuations. The use of commercial paper is not viable for the reasons discussed by Mr. Golden in response to OSBA's contention that PGW use short-term borrowing

⁴³ 52 Pa. Code § 69.2703(a)(1) (" In determining just and reasonable rate levels for PGW, the Commission will consider, among other relevant factors: ... (1) PGW's test year-end and (as a check) projected future levels of non-borrowed year-end cash.").

⁴⁴ Staff Report: Inquiry into Philadelphia Gas Works' Pipeline Replacement Program, dated April 21, 2015 at 6, 51-52 ("PUC Staff Report").

⁴⁵ PUC Staff Report at 52.

to finance main replacements.⁴⁶ And, even if financing was viable, PICGUG did nothing to (a) compare the costs of funding seasonal fluctuations with commercial paper as opposed to keeping cash on hand or (b) show that PGW's increased reliance on debt funding would be viewed by the rating agencies. PICGUG's last minute, unsupported allegations should be rejected.

3. OCA and PICGUG Claims That PGW Should Be Forced to Make a Formal Request That the City Grant Back its City Fee In Lieu of a DSIC Increase Should Be Rejected

Finally, the Parties have once again demanded that PGW appropriate the \$18 million City Fee in lieu of increasing PGW's DSIC to fund accelerated main replacement.⁴⁷ Seemingly recognizing that, by law, the PUC does not have the authority to forcibly appropriate the only compensation the City receives for owning the Gas Works,⁴⁸ during the hearing the witnesses testified that PGW should "ask" the Administration to forgo its compensation – akin to "asking" the equity owners of a public utility to give up their dividends in order to make a contribution to finance main replacement.

So, PGW asked the Deputy City Finance Director, who rejected the request.⁴⁹

Not content with PGW's voluntary efforts, both OCA and PICGUG now assert that the PUC should (seemingly) order PGW to "formally" ask the City to grant back the City Fee.⁵⁰ PICGUG goes farther and suggests that the "formal request" should be made to City Council (which, as a legislative body, does not, on its own, have the authority to grant back the City Fee).

⁴⁶ See, Section IV(C)(2) of this Reply Brief, *supra*.

⁴⁷ OCA MB at 11-12, PICGUG MB at 11-13.

⁴⁸ See PGW MB at 11.

⁴⁹ PGW MB at 30.

⁵⁰ OCA MB at 12; PICGUG MB at 12-13.

There are many reasons why the City could rightly conclude that using the City Fee for accelerated main replacement is unfair and inappropriate, but the more important point is that trying to avoid a DSIC increase in favor of this alternative will obviously delay the acceleration, perhaps for years, while the issue is debated and vetted. Accordingly, if the PUC requests that it do so, PGW would be willing to make a formal request (in the form of a letter) to the City appropriate representatives asking them to consider contributing the City Fee to finance additional cast iron main replacement (after granting PGW's portion to increase its DSIC to 7.5%), and report back to the PUC on the response. PGW submits that this compromise fairly resolves and legitimate interest the PUC might have in assuring that all potential avenues to achieve accelerated main replacement are considered while avoiding any delay in accelerating the replacement of its at risk facilities.

4. OCA's Claims About the Effect of the DSIC Cap Increase on Ratepayers Are Not a Valid Basis for Denying PGW's Petition and Should Be Rejected

The OCA continues to argue that, whether or not PGW meets its burden of showing that its DSIC cap should be increased to 7.5% the Commission should nonetheless refuse to grant the request because of the alleged effect on PGW's ratepayers, many of whom PGW points out are low income.⁵¹ However, as noted, PGW showed that the increase in DSIC to 7.5% would have a relatively small effect on customers. The increase in charges resulting from a hike in the cap from 5% to 7.5% is as follows:

⁵¹ OCA MB at 12-14.

Incremental Impact – Average Residential Heating Customer Bill	
DSIC	7.50%
Customer Impact (\$) - Year	\$19.80
Customer Impact (\$) - Month	\$1.65
Customer Impact (%)	1.7%

Based on 83 MCF per year and June 2015 rates.

Incremental Impact – Average Commercial Heating Customer Bill	
DSIC	7.50%
Customer Impact (\$) - Year	\$63.63
Customer Impact (\$) - Month	\$5.30
Customer Impact (%)	1.5%

Based on 363 MCF per year and June 2015 rates.

Incremental Impact – Average Industrial Heating Customer Bill	
DSIC	7.50%
Customer Impact (\$) - Year	\$163.99
Customer Impact (\$) - Month	\$13.67
Customer Impact (%)	1.5%

Based on 943 MCF per year and June 2015 rates.⁵²

The OCA nonetheless insists that the effect on customers will be greater because PGW had not actually achieved a 5% DSIC rate in the last few quarters and that the Commission should look at the actual impact on customers.⁵³ But the actual total bill impact of the increase in the DSIC from 5% to 7.5% is actually negative. As Mr. Dybalski testified:

⁵² PGW St. 2 at 6.

⁵³ OCA MB at 12-13.

Actual customer impacts in fact will not reflect a DSIC percentage change from 5% to 7.5% – the customers will actually see a net decrease in their rates. In 2016, bills are actually projected to be lower than in July, 2013. At the inception of the DSIC billing in July, 2013 the average residential heating customer using 83 Mcf would have been billed in total \$1,427.70 per year at the 5% DSIC cap. . . [T]he average residential heating customer using 83 Mcf would be billed in total \$1,217.16 per year at a 7.5% DSIC cap, or \$210.54 less per year.⁵⁴

The OCA dismisses the DSIC’s actual effect on the ground that the net decrease that the customers will actually experience will be caused by lower gas rates; but that is precisely the point. Increasing PGW’s DSIC at this time is especially appropriate because lower natural gas rates have reduced customer bills significantly over the last several years. Thus, this is actually the best time in which to increase funding to replace antiquated distribution facilities that will rebound to the benefit of all customers.

OCA also argued that the extremely small increases required to fund higher DSIC levels would be particularly difficult for customers in “deep poverty” (which OCA defined as household with incomes of 50% or less of the Federal Poverty Level.⁵⁵ But, as the OCA frankly admitted in its Brief, PGW customers that are in “deep poverty” will actually not see any increase from the DSIC because such customers likely will be enrolled in the Company’s Customer Responsibility Program (“CRP”) in which customers pay a fixed rate based on their income rather than on the actual level of the bill. While OCA speculated that some of these customers might not be enrolled in the CRP program, it provided absolutely no evidence to that effect other than the contention of its witness, Ms. Everette, who initially did not appear to even

⁵⁴ PGW St. 2-R at 10.

⁵⁵ OCA MB at 14.

understand that low-income customers enrolled in PGW's CRP program would not be affected by the DSIC increase.⁵⁶

PGW acknowledges that its service territory has a large proportion of its residential customers who are low income. The Company is concerned about those customers and has a number of programs and initiatives designed to help them deal with their natural gas bills. Those programs include its CRP program, its low income weatherization program – CRP Home Comfort (“LIURP”) and several other efforts.⁵⁷ It would be neither legal nor fair however, to deny PGW's Petition for a modest increase in its DSIC because of the unproven assertions about the “ability to pay” of some PGW's customers.⁵⁸

D. 7.5% Cap For DSIC Expenditures

1. OCA's Claim that the Commission May Not Increase PGW's DSIC Cap Until a Revised LTIP is Submitted and Approved is Baseless and Should Be Rejected

PGW, I&E and EDF agree that PGW's proposal to waive the 5% limitation and approve a 2½ percentage point increase in the maximum allowed DSIC from 5% to 7.5% (not including reconciliation) for construction purposes should be approved and placed into effect on or after January 1, 2016.⁵⁹ OCA, on the other hand, claims that the Commission cannot grant PGW's

⁵⁶ See, Tr. 116-117.

⁵⁷ These additional programs include Customer Assistance and Referral Evaluation Services (which provides referral services for low-income, special needs customers), the Hardship Fund (which provides grants to customers who have had their utility service terminated or are in danger of termination) and LIHEAP enrollment assistance. PGW uses targeted outreach activities to ensure that customers are aware of the various programs it offers. Outreach activities include outbound calls, direct mail, community presentations in low-income communities, referrals from customer service representatives, social media and advertising campaigns. *Philadelphia Gas Works Universal Service and Energy Conservation Plan for 2014-2016 Submitted in Compliance with 52 Pa. Code § 62.4*, Docket No. M-2013-2366301, Final Order at 10-11, 58-61 (Order entered August 22, 2014) (“USECP Final Order”).

⁵⁸ PGW St. 2-R at 8-9.

⁵⁹ PGW MB at 17-31; I&E MB at 16-24; EDF MB at 7-8.

Petition to increase its DSIC to 7.5% until PGW has filed and the PUC has approved a modification to its LTIIIP. OCA claims that the Commission cannot determine whether the additional funds will “ensure and maintain adequate, efficient, safe and reliable reasonable service” until the specific amendments to the LTIIIP are filed. It also suggests that both Act 11 and the Commission’s regulations require this. Neither of these arguments is supported by the law or the record and they should be rejected.

First, Section 1352 states that “in order to be eligible to recover costs under Section 1353 (relating to distribution system improvement charge) a utility must submit a long-term infrastructure improvement plan. There is no similar requirements indicated in order to increase the 5% cap as permitted in Section 1358. Similarly, the PUC’s LTIIIP regulation specifically contemplates that a utility may file a “modification” to its LTIIIP. Again, the regulations only require that if a utility’s LTIIIP “expires” the utility must file and have approved a new LTIIIP in order to have a DSIC.⁶⁰ PGW has an LTIIIP in place that expires in 2017.⁶¹ Accordingly, there is nothing in the Act or the PUC rules that prohibit the Commission from taking the independent act of permitting an increase in PGW’s DSIC, with the proviso that PGW will not utilize the additional funds until a modification in PGW’s LTIIIP is approved.

Moreover, the OCA is similarly wrong in its claim that only by reviewing PGW’s revised LTIIIP may the Commission determine whether PGW has satisfied the standard for waiving the 5% cap. As explained extensively in PGW’s Main Brief, PGW already has an LTIIIP that has been approved by the Commission.⁶² That LTIIIP provides a comprehensive review and analysis

⁶⁰ 52 Pa. Code § 121.5.

⁶¹ PGW Exh. DPM-1 at 12.

⁶² PGW Exh. DPM-1.

of the at risk facilities and provides a detailed prioritization of those facilities based on benchmarking studies and the Companies' existing distribution integrity management plan.⁶³ The existing, approved Plan also: 1) identifies the types and ages of eligible property for which PGW is seeking recovery, together with the identification tools and considerations used; 2) the age range for the mains to be replaced in Phase one of PGW's Plan; 3) an initial schedule for the planned replacement of all of PGW's cast iron main, including main to be replaced in subsequent periods; 4) how the acceleration will ensure and maintain adequate, efficient, safe reliable and reasonable service, including a discussion of the benchmarking and risk analysis studies utilized⁶⁴; 5) how PGW ensured that the Plan was cost effective; and 6) a workforce management and training plan designed to ensure that the utility will have access to a qualified workforce.⁶⁵ The revised LTIIP will simply update these extensive analyses as well as incorporate any changes in PGW's DIMP as a result of discussions with the PUC's Gas Safety Division. PGW elected to hold off filing a revised LTIIP so that it could incorporate the results of the Commission's Order here as well as the updated findings of two independent studies: a benchmarking study and a prioritization study (the preliminary results of which have been provided to PGW).⁶⁶ PGW witness Murray, the Company's Senior Vice President of Customer Affairs and Operations testified that while, to incorporate the additional DSIC spending, "PGW is currently updating some of the studies [on] which the LTIIP was based "[PGW doesn't] expect it to be updated dramatically from what we have currently. It would just be update[d] with more

⁶³ PGW Exh. DPM-1 at 2-20.

⁶⁴ PGW described the results of independent studies by Advantica and GL Noble Denton as well as its own filed observations and the effects of its "prudent main replacement program." PGW Exh. DPM-1 at 15-20.

⁶⁵ PGW Exh. DPM-1 at 20-26.

⁶⁶ Tr. 40-41; PGW St- 1-R at 5-7.

recent information regarding the prioritization and benchmarking studies that we have going on currently.”⁶⁷ He went on to characterize the results of the updated LTIP as follows:

Q. So, based on the preliminary results of those [benchmarking] studies and your own investigation, do you expect the priorities for PGW’s main replacement are going to change materially in the amended LTIP?

A. Not materially, no.

Significantly, I&E agrees with PGW that it may begin to charge at the higher 7.5% level while its revised LTIP is considered by the Commission. In its Brief, I&E stated as follows:

PGW has agreed to implement its 7.5% DSIC and to begin to bill customers at this increased level on or after January 1, 2016. PGW has further agreed that prior to the DSIC implementation, it will submit a Petition to the Commission to amend its LTIP. Among other things, its LTIP will address non-compliance issues that were previously identified by I&E’s Gas Safety Division. Taking into account PGW’s aforementioned plan, as well as other safeguards that are addressed below, I&E supports PGW’s plan to implement its 7.5% cap for DSIC expenditures as modified by and in accordance with the Stipulation.

I&E makes its recommendation for several reasons. First, adequate safeguards already exist under Act 11 and through existing federal requirement to ensure that if PGW is permitted to bill customers at the increased level and in the timeframe proposed, ratepayer money will not be misspent. Furthermore, via the Stipulation, PGW has added additional guarantees of compliance with federal regulations and it has also articulated a plan to provide reports that will allow I&E’s Gas Safety Division to monitor its compliance. Finally, additional opportunities for oversight and comment by interested parties are already included in the LTIP process that PGW must undertake, and PGW has agreed not to undertake any main replacement made possible by any incremental increase in DSIC funding unless and until the Commission approves its revised LTIP. Quite simply, time is of the essence in this matter, and now that appropriate avenues of oversight exist, PGW’s request should be approved. Accordingly, I&E recommends approval of the 7.5% DSIC cap in accordance with the process outlined in the Stipulation because it will facilitate PGW safe, and expedited replacement of at-risk pipeline, which is in the public interest.⁶⁸

⁶⁷ Tr. 41.

⁶⁸ I&E MB at 16-17 (footnotes omitted).

This substantial endorsement by I&E, representing the Commission's Bureau of Gas Safety should provide the Commission with adequate assurance that PGW's suggested approach to filing a revised LTIP is both reasonable and prudent and should be approved.

Importantly, the I&E endorsement recognizes that delaying the increase in the DSIC until mid-2016 simply will delay PGW's main replacement efforts with no justification. Since PGW has agreed to refund with interest any amounts collected from ratepayers at the higher DSIC level if the PUC delays or fails to approve PGW's modified LTIP, OCA never articulated any harm to customers that PGW's proposal would create. OCA's demand that the Commission should not grant PGW's Petition until it files a modified LTIP to reflect the additional incremental funding for accelerated main replacement is unsupported, unreasonable and should be rejected.

E. 10% Cap For Reconciliation – The Arguments of OCA and PICGUG in Opposition to the 10% Cap For Reconciliation Should Be Rejected

PGW, I&E and EDF agree that PGW's proposal to waive the 5% limitation and approve a total, 10% cap including any reconciliation recovery should be approved and granted.⁶⁹

OCA and PICGUG argue that PGW has not established a need to have an additional percentage for under-collections (the 7.5% to 10% cap).⁷⁰ They are wrong. The circumstances justifying an additional percentage are established by the record and are clearly explained in PGW's Main Brief.⁷¹ PGW's cash-flow methodology and its (proposed) use of a levelized and annualized DSIC make PGW different from investor-owned utilities using rate base

⁶⁹ PGW MB at 31-33; I&E MB at 24-27; EDF MB at 8.

⁷⁰ OCA MB at 24-27; PICGUG MB at 13-14.

⁷¹ PGW MB at 11-12, 31-33.

methodologies.⁷² If PGW's DSIC is levelized and annualized, an additional percentage needs to be available for PGW to recover any amount for under-collections.⁷³ If not, main replacements in future years may suffer in order to assure collection of any under-collection.⁷⁴

OCA contends that PGW's past experience with under-collections shows that there is no support for allowing an additional percentage for under-collection.⁷⁵ OCA has missed the point. Regardless of size, OCA has acknowledged that under-collections have existed in the past.⁷⁶ That being acknowledged, the OCA appears to be taking the position that – if PGW plans to replace “at risk” mains using the full 7.5% level it should not be given the ability to collect monies from under collections. This means that PGW would either have to reduce its replacements, to account for any under-collection, or forego recovering the under-collections. Reducing PGW's annual main replacement is simply not consistent with the clear objective of utilizing the 7.5% DSIC fully each year for main replacement. Having PGW keep its replacement activity at the \$33 million level and not recover for under-collections from the prior year is inconsistent with Act 11 and the nature of automatic adjustment clauses.⁷⁷

OCA further contends that there is a harm in setting the additional percentage at 2.5%.⁷⁸ OCA is misreading PGW's proposal. The 2.5% is a maximum percentage for under-

⁷² PGW MB at 11-33, 35-39.

⁷³ PGW MB at 31-33.

⁷⁴ *Id.*

⁷⁵ OCA MB at 24-25.

⁷⁶ *Id.*

⁷⁷ See 66 Pa. C.S. § 1358(e)(3) (“The difference between revenue and costs shall be recouped or refunded, as appropriate, in accordance with section 1307(e) over a one-year period...”).

⁷⁸ OCA MB at 26.

collections.⁷⁹ As explained in the record and in PGW's Main Brief, the 2.5% is not automatic.⁸⁰ The actual percentage above 7.5% will be determined based on actual under-collections. So, by itself, the maximum percentage (which is dedicated to the collection of under-collection amounts) does not harm any customer. Currently PGW's under-collection is just .3%, which produces a total proposed DSIC percentage of 7.64%.⁸¹

V. WAIVERS TO PERMIT LEVELIZATION AND ANNUALIZATION OF DSIC-ELIGIBLE COSTS⁸²

B. PGW Has Correctly Set Forth the Standard For Granting The Waivers For Levelization And Annualization

PGW, I&E, OCA and EDF agree that the standard for the requested waivers to levelize and annualize PGW's DSIC is set forth in Section 2212.⁸³

OCA contends that it is also appropriate to consider the standard under Section 1358(a) for waiving the DSIC cap.⁸⁴ The OCA states that Act 11 does not contemplate the waiver of this consumer protection, and implies that waivers of Act 11 (other than of the 5% cap) should not be permitted. That interpretation of Act 11 is not supported by the clear language in Section 2212 or the Commission's prior interpretation and application of Section 2212.⁸⁵

⁷⁹ PGW MB at 31-33.

⁸⁰ *Id.*

⁸¹ Corrected Attachment A to PGW's Petition, Gas Service Tariff – Pa P.U.C. No. 2 at 2 (filed September 9, 2015).

⁸² PICGUG did not take a position on levelization and annualization. PICGUG MB at 14.

⁸³ PGW MB at 34; I&E MB at 29; OCA MB at 27; EDF MB at 6.

⁸⁴ OCA MB at 27-28.

⁸⁵ *See, e.g., PUC v. PGW*, PUC Docket No. R-2008-2073938, Reconsideration Opinion and Order (entered March 26, 2009) (relating to the grant of several waivers, including waiver of portions of 66 Pa. C.S. § 1308(e), to the extent necessary to give full effect to the rate relief, conditions and directives set forth in the Commission's prior order).

That being said, OCA's interpretation does not appear to be relevant because, as noted below, OCA appears willing to concede that the applicable statutory standard for the subject waivers has been satisfied.⁸⁶

C. Has PGW Satisfied The Standard For Granting Waivers Permitting Levelization And Annualization ?

PGW has satisfied the standard, under Section 2212, for granting waivers permitting levelization and annualization.⁸⁷ I&E and EDF agrees with that conclusion.⁸⁸

OCA acknowledges that PGW's circumstances are different from the other investor-owned utilities using a DSIC.⁸⁹ But, the OCA does not take an explicit position on whether (or not) the applicable statutory standard for waiver has been satisfied.⁹⁰ Rather, OCA submits that if the Commission determines that the waiver should be granted and approved, then that waiver should be subject to certain conditions.⁹¹ PGW has effectively agreed to OCA's key "conditions" as set forth in Section V.D of this Reply Brief and Section V of PGW's Main Brief.

1. OSBA's Arguments Against the Granting of a Waiver Permitting Levelization And Annualization Should Be Rejected

OSBA contends that the statutory standard has not been satisfied.⁹² To support this argument, OSBA notes that the Commission did not approve the use of a levelized and

⁸⁶ See OCA MB at 28.

⁸⁷ PGW MB at 35-44.

⁸⁸ I&E MB at 29-32; EDF MB at 9-10.

⁸⁹ OCA MB at 28.

⁹⁰ OCA MB at 28-32.

⁹¹ *Id.*

⁹² OSBA MB at 11-12

annualized DSIC when PGW first sought approval to implement a DSIC In 2013.⁹³ That Order stated:

While PGW, as a [City Natural Gas Distribution Operation] CNGDO, may seek a waiver or suspension of provisions of Act 11 pursuant to Section 2212(c) of the Public Utility Code, we find that PGW has not provided legal or factual basis for a waiver or suspension of the applicable statutory provisions to allow PGW to recover annualized costs through the DSIC. Accordingly, we shall reject PGW's request for a waiver that would allow use of annualized construction costs."⁹⁴

However, that order did not foreclose this issue for all time. Rather, the Commission left the door open for PGW to file a renewed waiver request to allow PGW to recover annualized costs through the DSIC.⁹⁵ If this issue were permanently foreclosed, I&E would not have supported the request for levelization and annualization and the PUC Staff Report would not have suggested that PGW should seek to levelize and annualize its billings for DSIC-eligible costs.⁹⁶

In fact, the Staff Report explains:

While the Commission agreed that PGW had not presented legal or factual basis to recover annualized costs through the DSIC, it noted that PGW has the opportunity to seek a waiver or suspension of Act 11, pursuant to Section 2212(c) of the Public Utility Code. Based on actual experience with PGW's unique DSIC mechanism and circumstances over the past two years, Staff recognized that it may be beneficial to reconsider this option if re-proposed by PGW. Staff analysis indicates that this change in mechanism would facilitate the recovery of additional DSIC revenue that could be used to further expedite main replacement, but may not match on a quarterly basis what PGW has actually completed.⁹⁷

⁹³ OSBA MB at 12.

⁹⁴ *Petition of Philadelphia Gas Works for Approval of a Distribution System Improvement Charge*, PUC Docket No. P-2012-2337737, Opinion and Order entered on May 9, 2013 ("Final DSIC Order") at 6 (emphasis added).

⁹⁵ PGW MB at 38. Of course, the Commission may, at any time, after notice and after opportunity to be heard, rescind or amend any order made by it. 66 Pa. C.S. §§ 501, 703(g). The decision in 2013 was made before PGW's actual experience with its DSIC mechanism.

⁹⁶ PUC Staff Report at 5-6, 42-44.

⁹⁷ PUC Staff Report at 44.

Additionally, PGW notes that factual and legal support for the levelization and annualization of PGW's DSIC is set forth in the Main Briefs of PGW and I&E.⁹⁸

D. Implementation Of The Waivers For Levelization And Annualization⁹⁹

Each of the three conditions, proposed by the OCA, should be either rejected or adopted as modified and agreed to by PGW.

1. OCA's Proposed Accounting Controls Have Been Satisfied

OCA's proposed accounting controls have been satisfied.¹⁰⁰ The record shows that there is no need for additional accounting controls.¹⁰¹ The existing proposal by PGW does not permit any diversion of DSIC revenues for any other purpose.¹⁰² This point was acknowledged in the cross-examination of OCA witness Everette.¹⁰³ She acknowledged that PGW's proposal would satisfy OCA's suggestion on this point.¹⁰⁴

2. OCA's Proposed Quarterly Update Demands Are Satisfied by PGW's Triggers for Quarterly Adjustments

⁹⁸ See PGW MB at 35-44; I&E MB at 29-32.

⁹⁹ PGW notes that (1) the OSBA did not make any explicit arguments against the grant and approval of a total 10% cap including any reconciliation recovery. See OSBA MB at 11-12; and (2) PICGUG did not take a position on levelization and annualization. PICGUG MB at 14. PICGUG noted that its silence on this issue should not be taken as support for levelization and annualization. *Id.*

¹⁰⁰ The OCA is concerned that dollars collected by the DSIC are actually used DSIC projects. OCA MB at 29.

¹⁰¹ As explained in PGW's Main Brief, there is no need to further segregate DSIC revenues from other revenues. PGW MB at 43. Simply put, the existing audit and reconciliation process, which is not impacted by PGW's request for levelization and annualization, does not permit any diversion of DSIC revenues for any other purpose. See PGW St. 2 at 11-13; PGW St. 2-R at 7-8.

¹⁰² *Id.*

¹⁰³ Tr. 114-115, 117-118.

¹⁰⁴ Tr. 117-118.

To the extent they call for something more than PGW has agreed to do, OCA's proposed quarterly update demands are satisfied by PGW's triggers for quarterly adjustments.¹⁰⁵ The record does not show that there is a need to change PGW's DSIC percentage on a quarterly basis. As explained in its Main Brief, PGW proposed to make quarterly changes when certain triggers are satisfied.¹⁰⁶ In PGW's Main Brief, PGW stated that it was willing to revise the DSIC percentage if its projected total billings and expenditures for the remainder of the year indicate that a material over or under-collection is likely to develop. The reasonable standard for materiality would be plus or minus 2% (approximately \$660,000).¹⁰⁷ In its Main Brief, PGW indicated that it is most likely to be able to make that projection in the last quarter (October 1), but, for clarity, PGW would make that adjustment whenever its total over/under collection projected to year end exceeded 2% of the DSIC (\$660,000).

The OCA apparently objects to the fact that PGW would not make an adjustment if there is any difference between projected collections and projected expenditures in any given quarter.¹⁰⁸ OCA's position is unreasonable. This would require revisions in the percentage be made in each and every quarter regardless of materiality.¹⁰⁹ That approach is inconsistent with both (a) the way the 2% trigger works in the GCR¹¹⁰ and (b) the view of PUC Staff, which noted that, ideally, the DSIC should remain relatively level throughout the year in order to pass costs

¹⁰⁵ PGW notes that it has agreed to submit quarterly reports showing DSIC expenditures and billings for the quarter. PGW MB at 2, 40.

¹⁰⁶ PGW MB at 41-43.

¹⁰⁷ *Id.*

¹⁰⁸ See OCA MB at 30.

¹⁰⁹ OCA MB at 30-31.

¹¹⁰ 52 Pa. Code § 53.64(b).

equally to all customers.¹¹¹ Moreover, mandatory quarterly changes are simply not reasonable for the reasons set forth in Section V.D.3 of PGW's Main Brief.

3. OCA's Proposed Change To PGW's Budget Billing Program Should Be Rejected

The OCA's proposed change to PGW's budget billing program should be rejected. The record does not show that there is a need to increase awareness of PGW's Budget Billing program. As explained in Section V.D.5 of PGW's Main Brief, nothing in the record suggests that PGW's residential customers are not aware of PGW's budget billing program and/or a need to modify the budget billing program itself.

First, it appears that OCA witness Everette may have misunderstood PGW's budget billing program. PGW offers a budget-billing plan to residential customers that averages the cost of gas service over a 12-month period. In accordance with its tariff, PGW reviews customer accounts at least three times during the 12-month period and makes adjustments, if necessary, to keep monthly payments in line with projected and actual charges.¹¹² PGW also reviews accounts at least once yearly to bill for actual usage, pursuant to a true up bill.¹¹³ Accordingly, budget billing does not levelize a customer's charge for 12 months. In fact, budget billing charges are adjusted each quarter.

Second, there is no reason why PGW should do more to ensure that additional customers enroll in its budget billing program. As of October 2015, PGW had over 42,000 customers in its

¹¹¹ PUC Staff Report at 5-6, 42-44.

¹¹² PGW Gas Service Tariff – Pa P.U.C. No. 2, Second Revised Page No. 26.

¹¹³ *Id.*

(non-payment agreement) budget billing program.¹¹⁴ In addition, PGW offers payment agreements to many of its customers.¹¹⁵ PGW witness Dybalski's testimony states that "residential customers were provided with 77,936 (non-CAP, PGW and PUC provided) payment agreements in 2014; of this number 53,491 agreements were for confirmed low-income customers."¹¹⁶ Most customers on payment arrangements are also on budget billing.¹¹⁷ Furthermore, and as noted PGW already offers numerous programs to help low income customers maintain utility service.¹¹⁸

Consequently, the Commission should not require PGW to modify its budget billing program at this time or further encourage customers to participate in the program.

VI. CONCLUSION

For the reasons set forth above and in its Main Brief, PGW respectfully requests that the Commission grant waivers of portions of 66 Pa. C.S. §§ 1358 and 2212(c) and issue an order consistent with PGW's Petition, as modified in its Main Brief and by the PGW/I&E Stipulation to:

- (i) waive the current DSIC cap of 5% of distribution revenues, a) approve a 2½ percentage point increase in the maximum allowed DSIC from 5% to 7.5% (not including reconciliation) for construction purposes, and b) approve a total, 10% cap including any reconciliation recovery, both for service rendered on or after January 1, 2016;

¹¹⁴ PGW St. No. 2-R, at 8.

¹¹⁵ PGW St. No. 2-R, at 8-9.

¹¹⁶ PGW St. No. 2-R, at 9.

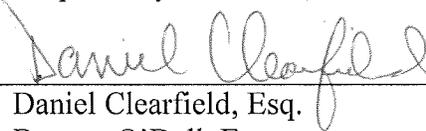
¹¹⁷ *Id.*

¹¹⁸ USECP Final Order at 10.

- (ii) waive or suspend the requirements of Act 11 so as to permit PGW to use an annual, levelized charge as the basis for establishing a DSIC, subject to subsequent true-up for PGW's actual experience;
- (iii) authorize the filing, on one day's notice, of a PGW tariff supplement attached as Attachment A to PGW's Petition, codifying these changes after the submission of a compliance tariff; and
- (iv) take any other action in the public interest.

PGW is proposing that the Commission approve the above-described changes to PGW's DSIC in an expedited manner so that the charge becomes effective as soon as possible after the Commission's approves PGW's Petition and as close to January 1, 2016 as possible.

Respectfully submitted,



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