COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
COMMONWEALTH KEYSTONE BUILDING
400 NORTH STREET, HARRISBURG, PA 17120

BUREAU OF
INVESTIGATION
&
ENFORCEMENT

March 15, 2021

Via Electronic Filing
Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

Re: Pennsylvania Public Utility Commission v.
PECO Energy Company – Gas Division
Docket No.: R-2020-3018929
I&E Reply Brief

Dear Secretary Chiavetta:

Enclosed for electronic filing please find the **Reply Brief of the Bureau of Investigation and Enforcement** for the above-captioned proceeding.

Copies are being served on parties of record per the attached Certificate of Service. *Due to the temporary closing of the PUC's offices, I&E is only providing electronic service.* Should you have any questions, please do not hesitate to contact me.

Sincerely,

Scott B. Granger
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SBG/ac
Enclosures

cc: Honorable Christopher P. Pell – Office of Administrative Law Judge (*via email*)
Pamela McNeal, Legal Assistant – Office of Administrative Law Judge (*via email)*
Per Certificate of Service

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:		
	:		
v.	:	Docket Nos.	R-2020-3018929
	:		C-2020-3022400
PECO Energy Company – Gas Division	:		C-2020-3022414
Base Rates	:		C-2020-3022745

REPLY BRIEF
OF
THE BUREAU OF INVESTIGATION & ENFORCEMENT

Scott B. Granger
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Bureau of Investigation & Enforcement
Pennsylvania Public Utility Commission
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Dated: March 15, 2021

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I. INTRODUCTION

A. Description of Company

See main briefs of the parties.

B. Procedural History

The history of this proceeding was addressed in I&E's Main Brief ("I&E MB") and in the main briefs submitted by PECO Energy Company – Gas Division ("PECO" or "Company" or "PECO MB"); the Office of Consumer Advocate ("OCA MB"); the Office of Small Business Advocate ("OSBA MB"); the Coalition for Affordable Utility Services and Energy Efficiency in Pennsylvania ("CAUSE-PA MB"); and, the Philadelphia Area Industrial Energy Users Group ("PAIEUG MB") and does not need to be restated here.

I&E now submits this Reply Brief ("I&E RB") in response to the main briefs of PECO, OCA, OSBA, CAUSE-PA, and PAIEUG and in support of the arguments and recommendations made by the I&E witnesses, the record evidence presented, and I&E's Main Brief. Overall, the arguments made in the parties' main briefs have been raised consistently throughout the litigation process and have already been addressed in I&E's direct and surrebuttal testimony, as well as in I&E's Main Brief. This reply brief will enhance its previously set forth arguments in this reply brief as necessary.

C. Overview of PECO Gas Filing

See main briefs of parties.

D. Burden of Proof

I&E fully addressed the applicable burden of proof in its Main Brief.[1]

I&E reiterates that PECO Gas has failed to meet its burden and therefore I&E respectfully requests that Deputy Chief Administrative Law Judge Christopher P. Pell ("ALJ Pell") and the Commission adopt the adjustments and the overall revenue requirement set forth in the record evidence presented by I&E and in I&E's I&E Main Brief.

II. SUMMARY OF ARGUMENT

Reiterating the arguments from I&E's Main Brief, I&E continues to assert that PECO has failed to meet its burden of proof. Further, I&E asserts that the record evidence supports a finding that only a revenue increase of $26.3 million is warranted. This recommendation is based upon I&E's direct and surrebuttal testimony and supporting exhibits, as well as the arguments set forth in I&E's Main and Reply Briefs.

RATE BASE - In summary, I&E's total rate base recommendation, not including the adjustments accepted by the Company, is to reduce the Company's revised rate base by $46,821,000 from $2,463,555,000 to $2,416,734,000. I&E recommends the accumulated depreciation claim be reduced by approximately $804,000 from $892,383,000 to $891,579,000 which is contingent upon I&E's adjustments to the plant in service.

[1] *See* I&E MB, p. 4.

I&E asserts the Natural Gas Reliability project is 28% completed with $33,888,385 spent to date. As the Company is unlikely to spend 94.6% of the remaining total project costs in the FPFTY, I&E recommends an allowance of $34,856,625. Therefore, I&E recommends that the Company's claim for plant additions in the FPFTY be reduced by $47,624,803 from $82,481,428 to $34,856,625.

I&E recommends the disallowance of the Company's $35,059,000 pension asset claim and a reduction of $35,059,000 to the Company's rate base claim.

I&E recommends the Company's materials and supplies, gas in storage, customer deposits, and customer advances for construction claims in the FPFTY be determined using an updated thirteen-month average ended September 2020 as shown on I&E Exhibit No. 3, Schedule 1, and that the Company provide periodic updates to the Commission's Bureaus of Technical Utility Services and Investigation and Enforcement regarding actual capital expenditures, plant additions, and retirements by month.

REVENUES - I&E recommends that the Company include revenue under proposed rates from forfeited discounts equal to 0.195% of Gas Service Revenues upon determination of the total revenue granted by the Commission. Resulting in I&E recommending that the revenue from forfeited discounts be increased by approximately $358,000 from $926,000 to $1,284,000 under proposed rates for the FPFTY ending June 30, 2022.

EXPENSES - I&E recommends an allowance of $41,350,285 based on a reduction of $858,715 to PECO's claim of $42,209,000 payroll expense. Additionally, I&E recommends an allowance of $5,797,603 for employee benefits based on a reduction of

$120,397 to PECO's claim of $5,918,000. Further, I&E recommends an allowance of $32,940,000 based on a reduction of $10,015,000 to PECO's claim of $42,955,000 for contracting/materials cost.

I&E recommends a walk-up adjustment for inflation to the HTY actual outside services based on the Consumer Price Index (CPI) factors of 2.75% and 2.03% to determine the FTY and FPFTY allowances. I&E recommends an allowance of $13,437,856 or a reduction of $3,134,144 to the Company's $16,572,000 claim for outside services net of the "cost to achieve" adjustment of $370,000.

I&E recommends an allowance of $270,000 based on a reduction of $780,000 to PECO's claim of $1,050,000 for OPEB expense. Further, I&E recommends a disallowance of the $370,000 amortized ($1,111,000 ÷ 3) costs to achieve expense claim in its entirety. I&E recommends an allowance of $58,469 based on a reduction of $80,933 to PECO's claim of $139,402 for employee activity costs. Additionally, I&E recommends an allowance of $862,153 based on a reduction of $169,847 to PECO's claim of $1,032,000 for travel, meals and entertainment. Further, I&E recommends an allowance of $588,135 based on a reduction of $67,762 to PECO's industry organization membership expense claim of $655,897.

I&E recommends an allowance of $2,727,500 based on a reduction of $1,772,500 to PECO's claim of $4,500,000 for energy efficiency and conservation. Further, I&E recommends a 60-month normalization period for rate case expense resulting in a reduction of $208,200 to PECO's claim of $520,000. I&E recommends an updated allowance of $28,200 ($141,000 ÷ 5-year amortization) based on a reduction of $18,800 to PECO's revised claim of $47,000 for regulatory initiative costs.

Finally, I&E recommends an allowance of $3,135,234 for CWC based on a reduction of $301,766 to the Company's updated claim of $3,437,000. I&E's updated CWC recommendation is not a final recommendation, as all adjustments to the Company's claims must be continually brought together through the ratemaking process known as "iteration."

TAXES - I&E recommends an allowance of $3,699,145 for payroll tax expense based on a reduction of $76,855 to PECO's claim of $3,776,000.

RATE OF RETURN - I&E recommends the following rate of returns for PECO Gas:

Type of Capital	Ratio	Cost Rate	Weighted Cost
Long-Term Debt	46.62%	3.84%	1.79%
Common Equity	53.38%	10.24%	5.47%
Total	100.00%		7.26%

Further, I&E recommends using the Company's claimed capital structure and the Company's updated claimed long-term debt cost rate of 3.84% for the FPFTY.

I&E continues to recommend using the Discounted Cash Flow ("DCF") method as the primary method to determine the cost of common equity, and using the results of the Capital Asset Pricing Model ("CAPM") as a comparison to the DCF results. I&E recommends a cost of common equity of 10.24%. I&E urges that PECO Energy should not be awarded additional basis points for management performance for providing adequate, efficient, safe, and reasonable service.

Finally, I&E recommends that the Company should be afforded the opportunity to earn an overall rate of return of 7.26% based on the calculated weighted averages.

CUSTOMERS PROGRAMS AND MISCELLANEOUS ISSUES - The Company states that it has not created a regulatory asset for COVID related costs and is not making a claim in this case to recover its expenses and lost revenues.

I&E recommends allowing up to 40 feet of main line per contracted residential customer at no cost with certain limitations for PECO's Neighborhood Gas program. Further, I&E also recommends an annual amortized allowance of $5,000,000 ($25,000,000 ÷ 5 years) for the capital costs associated with the proposed change to the Neighborhood Gas program, or a reduction of $2,500,000 ($7,500,000 - $5,000,000).

I&E made recommendations regarding PECO's Distribution Integrity Management Program ("DIMP") and PECO's methods of monitoring and reducing risk and damages to PECO's distribution system.

RATE STRUCTURE – PECO provided an updated cost-of-service study ("COSS") and I&E based its customer cost analysis on the updated COSS. I&E believes the Company's revised COSS is reasonable except for the calculation of the relative rate of return as discussed in revenue allocation.

I&E identified several issues regarding the Company's proposed rate allocation methodology and concluded that the Company's proposed revenue allocation is not reasonable and should be rejected. Based on I&E's proposed revenue allocation schedule and taking into consideration the issues brought forth by the OCA and OSBA, I&E developed its recommended revised revenue allocation. Further, I&E recommends that only the rates of those rate classes that receive an increase be scaled back proportionately based on the COSS ultimately approved by the Commission; and, I&E continues to recommend that the customer charges be included in the scale back of rates. Finally, I&E identified the concept of gradualism as one of the tools of discretion in the Commission's tool box.

I&E notes that even though the Company's proposed $16.00 customer charge may be supported by the customer cost analysis; the $4.25 increase from $11.75 to $16.00, or 36%, is a significant increase that should not be granted. I&E recommends that any increase to the residential customer charge be included in the scale back of rates if the Commission grants less than the full requested increase. Finally, I&E recommends the Commission apply the relevant sections of the Public Utility Code to any proposed Distribution System Improvement Charge ("DSIC") cost allocation.

I&E recommends the Company provide an update to the competitive alternative analysis for any negotiated gas service customer that has not had their alternative fuel source verified for a period of 5 years or more at the point at which PECO files a base rate case.

CONCLUSION – PECO Gas has not met its burden of proof as the record evidence presented by PECO Gas does not substantiate a revenue increase of $68.7 million. Instead, based on the weight of the record evidence, the Commission should grant PECO Gas only the I&E recommended revenue increase of $26.3 million.

III. OVERALL POSITION ON RATE INCREASE REQUEST

As presented in I&E's Main Brief, I&E's total recommended revenue requirement for the Company is $616,358,000.[2] This recommended revenue requirement represents an increase of $26,344,000 to the claimed present rate revenues of $590,014,000.[3] I&E's recommended revenue increase of $26.3 million represents a $42.4 million reduction to PECO's initial request of a $68.7 million increase and a 4.46% overall increase in revenue.[4]

IV. RATE BASE

I&E's total rate base recommendation, not including the adjustments accepted by the Company, is to reduce the Company's revised rate base by $46,821,000 from $2,463,555,000 to $2,416,734,000.[5]

A. Fair Value

PECO reiterated its total revised rate base claim for the FPFTY ending June 30, 2022, is $2,463,555,000 in its main brief.[6] And, as stated in I&E's Main Brief, I&E does not accept the Company's revised claim as it only accepted some of I&E's recommendations.[7] I&E continues to assert support for I&E's remaining recommendations regarding the Company's plant additions and accrued depreciation claims.[8]

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[2] *See* I&E MB, p. 12.
[3] *Id.*
[4] *Id.*
[5] *Id.*, p. 21.
[6] PECO MB, p. 14.
[7] I&E MB, p. 14.
[8] *Id.*, pp. 13-21.

B. Utility Plant in Service

PECO made its arguments regarding the projected plant additions related to the Natural Gas Reliability project in this section of its main brief,[9] while I&E made its arguments in Section IV. RATE BASE, D. Additions to Rate Base 1. Projected Plant Additions below.[10] I&E will again address PECO's arguments on projected plant additions below.

C. Depreciation Reserve – Annual/Accumulated

I&E recommended that the overall accumulated depreciation should be decreased by approximately $804,000[11] corresponding with the I&E recommendation to remove a portion of the Natural Gas Reliability project plant addition *infra*.[12]

PECO argued that I&E's adjustment to reduce accumulated depreciation by $804,000 is concomitant to the adjustment I&E proposed to the Company's claimed level of plant additions for the Natural Gas Reliability Project.[13] The Company then argued, if I&E's proposed adjustment to reduce PECO's FPFTY plant in service balances for the Natural Gas Reliability project is not adopted, then no concomitant rate base adjustment would be necessary.[14]

I&E disagrees and is continuing to recommend the adjustment to plant additions discussed above; and therefore, I&E is continuing to recommend the Company's overall accumulated depreciation claim be decreased by approximately $804,000.[15]

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9 PECO MB, pp. 14-20.
10 I&E MB, pp. 15-17.
11 I&E MB, p. 14.
12 *Id.*, p. 14.
13 PECO MB, p. 21.
14 *Id.*
15 I&E MB, p. 15.

D. Additions to Rate Base

1. Projected Plant Additions

I&E recommended the disallowance of $47,624,803 of the projected $82,481,428 in claimed plant additions for the "Natural Gas Reliability - Install 11.5 miles of OHP gas main, upgrade LNG plant and construct a new gate station" project[16] which results in the claimed $82,481,428 being reduced to $34,856,625.[17]

PECO argued that I&E witness Cline mistakenly treated the three components of the Natural Gas Reliability project as a single, linear project,[18] when, in fact, the three components will be constructed, placed into service, and will be able to provide service to customers independently.[19] PECO's explanation included a long discussion of PECO's laddered budgeting process and how they eventually arrived at their projections.[20] But, PECO's explanation doesn't cure the questions I&E had from the start as I&E explained in its main brief.[21] I&E sought clarity on this issue from the start and PECO's responses changed throughout the litigation process.

On one hand, PECO claimed that approximately 50% of the aggregate costs will be spent in 2021; that the new reliability station and 11.5-mile gas main are scheduled to be in service by the end of the FPFTY; and, that the entirety of the Natural Gas Reliability project is scheduled to be in service by the end of 2022.[22] PECO, however,

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16 I&E MB, pp. 16-17.
17 *Id.*, p. 17.
18 PECO MB, p. 20.
19 PECO MB, p. 20.
20 *Id.*, pp. 16-19 (responding to OCA witness Morgan).
21 I&E MB, pp. 15-17.
22 *Id.*, pp. 15-16.

has not been consistent with other responses it provided to I&E. PECO's statement that the entirety of the project is scheduled to be in service by the end of 2022 is not consistent with the in-service date of June 2023 provided in the Company's response to I&E-RB-4-D.[23] The Company provided no evidence or support for its updated claim of the end of 2022 for its in-service date for the Natural Gas Reliability project other than simply "stating" that it was updating.[24] Additionally, as the FPFTY ends June 30, 2022, the Company's newest projection of end of 2022 for the in-service date necessarily means that the project will not be fully in-service within the FPFTY.[25] Finally, the Company's attempt to "correct" its testimony through oral rejoinder suffers from the same inconsistencies.[26]

Therefore, I&E recommends the Commission accept I&E's calculation that the Natural Gas Reliability project is 28% completed with $33,888,385 spent to date.[27] Further, I&E recommends the Commission accept I&E's allowance for the determined remaining cost share through the end of the FPFTY, or $34,856,625.[28] Therefore, I&E recommends that the Company's claim for plant additions in the FPFTY be reduced by $47,624,803 from $82,481,428 to $34,856,625.[29]

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23 *Id.*, p. 16.
24 *Id.*
25 *Id.*
26 PECO MB, p. 20.
27 I&E MB, p. 16.
28 *Id.*, p. 17.
29 *Id.*

2. Pension Asset

I&E recommended disallowance of the Company's $35,059,000 claim or a reduction of $35,059,000 to the Company's rate base claim.[30]

PECO continues to argue the claimed pension asset consists of $35.1 million of investor-supplied capital that was actually contributed to PECO's pension fund and assumed for ratemaking purposes to be included in PECO's plant accounts, but was not recorded in PECO's plant accounts because GAAP rules will not allow it.[31] PECO states it has included the pension asset in rate base in this case because, unless it is given rate base recognition, PECO will never recover the carrying costs it incurs on those investor-supplied funds.[32] PECO's arguments have been addressed in I&E's Main Brief and are incorporated here.[33]

I&E reiterates, the pension asset represents a mismatch from a GAAP accounting perspective (use of an accrual method for plant accounts) and a cash contribution method for the expense account in ratemaking, and these differences between GAAP expense and cash contributions in any given year should not be viewed as a valid reason to inflate the plant amounts in rate base.[34] The pension asset of $35.1 million should not be included in PECO's plant accounts to recover the previously unrecovered associated carrying cost.[35] Rather, the pension asset arises from the mismatch in GAAP accounting and

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[30] I&E MB, p. 20.
[31] PECO MB, pp. 22-23.
[32] *Id.*, p. 23.
[33] I&E MB, pp. 17-20.
[34] *Id.*, pp. 17-18.
[35] *Id.*, p 18.

ratemaking treatment of pension costs (an accounting journal entry), and there is no real infusion of capital or funds by the investors/stockholders that is eligible for return on investment.[36] Additionally, the accumulated balance of the pension asset should not be categorized or described as a utility asset that is used and useful in providing utility services to ratepayers, and therefore, should not be included as an eligible asset in the rate base claim to recover the associated carrying cost (i.e., earning a return on it).[37]

Further, "Black box" settlements allow the parties to reach an amicable agreement which is by definition a negotiated compromise on the part of all parties and does not necessarily represent the positions the parties would have adopted during litigation.[38] The purpose is to avoid the expense of litigation and at the same time preserve all arguments raised during the litigation for future litigation if the parties ever deem it necessary to litigate a contested issue. PECO is correct, settlements do not set precedent, and to use settlements in that manner here would have a chilling effect on settlement negotiations in the future.

Finally, I&E asserts that it is I&E's understanding that over time, differential amounts (positive/negative) between the sum amount recorded for accrual accounting purposes per GAAP and the sum amount of annual cash contributions shall match or change to a liability account.[39] These differences between GAAP expense and cash contributions in any given year should not be viewed as a valid reason to inflate the plant

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36 I&E MB, pp. 18-19.
37 *Id.*, p. 19.
38 *Id.*, pp. 19-20.
39 *Id.*, p. 20.

amounts in rate base. Therefore, I&E continues to recommend the disallowance of the Company's $35,059,000 pension asset claim and a reduction of $35,059,000 to the Company's rate base claim.

3. Uncontested Items

The Company included its cash working capital methodology as an uncontested item.[40] But, as the Company points out, I&E made an expense adjustment to cash working capital that I&E addressed in Section VI. R. of its main brief[41] and which PECO disputes.[42]

In its main brief, I&E discussed materials and supplies, gas in storage, customer deposits, and customer advances for construction claims in the FPFTY be determined using an updated thirteen-month average ended September 2020 as shown on I&E Exhibit No. 3, Schedule 1.[43] The Company appears to be in agreement.[44]

Further, I&E continues to assert that the Company provide the Commission's Bureaus of Technical Utility Services and Investigation and Enforcement with an update to PECO Exhibits MJT-1 and MJT-2, Schedule C-2, no later than October 31, 2021, which should include actual capital expenditures, plant additions, and retirements by month from July 1, 2020 through June 30, 2021.[45] I&E also continues to assert an additional update be provided comparing projected additions and retirements with actual additions and retirements through June 30, 2022, no later than October 1, 2022.[46]

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40 PECO MB, pp. 24-25.
41 I&E MB, p. 50.
42 PECO MB., p. 25.
43 I&E MB, p. 21.
44 PECO MB, p. 25.
45 I&E MB, p. 21.
46 *Id.*

E. Conclusion

I&E's continuing total rate base recommendation, not including the adjustments accepted by the Company, is to reduce the Company's revised rate base by $46,821,000 from $2,463,555,000 to $2,416,734,000.[47]

V. REVENUES

A. Forfeited Discounts

I&E recommended that the revenue from forfeited discounts be increased by approximately $358,000 from $926,000 to $1,284,000 under proposed rates for the FPFTY ending June 30, 2022.[48]

The Company argues, PECO's pro forma revenues reflected this relationship by including a forfeited discount rate in the gross revenue conversion factor that is used to determine the amount of revenue increase required.[49] PECO states its approach is reasonable and appropriately reflects the payment characteristics of the Company's current customer base because forfeited discounts are imposed based on past due balances of accounts receivables.[50]

I&E continues to argue that the Company's explanation of how it calculates its projected forfeited discount revenue illustrated why that projection is understated.[51] Specifically, the time period shown on PECO Exhibit RJS-1-R does not include a year in

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47 *Id.*
48 I&E MB, p. 23.
49 PECO MB, p. 27.
50 *Id.*
51 I&E MB, p. 23.

which the Company increased its rates.[52] Furthermore, PECO's explanation of its methodology does not indicate that the increase in rates from the present base rate proceeding was factored into the analysis.[53] Therefore, a three-year average of the historic relationship of forfeited discounts and total revenue applied to the projected revenue at proposed rates remains the most reasonable method of projecting forfeited discounts.[54]

I&E continues to recommend that the Company include revenue under proposed rates from forfeited discounts equal to 0.195% of Gas Service Revenues upon determination of the total revenue granted by the Commission.[55] Therefore, I&E recommends that the revenue from forfeited discounts be increased by approximately $358,000 from $926,000 to $1,284,000 under proposed rates for the FPFTY ending June 30, 2022.

VI. EXPENSES

The public utility requesting a rate increase and seeking to recover expenses has the burden of showing that the rate requested, including all claimed expenses, is just and reasonable.[56]

A. Payroll and Payroll Related Expense

I&E continues to recommend an allowance of $41,350,285 for payroll expense, or a reduction of $858,715 ($42,209,000 - $41,350,285) to the Company's claim.[57]

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[52] *Id.*
[53] *Id.*
[54] *Id.*
[55] *Id.*
[56] I&E MB, p. 28 (citations omitted).
[57] I&E MB, p. 26.

The Company addressed I&E's recommended allowance arguing the fundamental error in I&E's calculation is that the figure of 602 represents the actual filled positions for the HTY and does not include any budgeted "vacant" positions.[58] Therefore, there is no basis for adjusting that figure by a "vacancy" rate.[59] The Company mistakenly argued further, I&E's recommended employee vacancy rate should be applied only to the proposed 37 additional/new positions to be filled by end of the FPFTY, payroll expense will merely be reduced by $46,200 instead of $858,715.[60]

Reiterating the arguments made in I&E's Main Brief, I&E noted that PECO did experience normal employee vacancies when the monthly actual filled positions are compared to the budgeted monthly positions during the last three fiscal years,[61] which I&E summarized.[62] Secondly, PECO's assertion that the FPFTY 639 budgeted positions do not include vacant positions is not reliable nor acceptable because PECO's FPFTY payroll expense claim is calculated based on the total budgeted 639 positions to be maintained/filled throughout the FPFTY.[63] Adjusting payroll expense by applying PECO's average annual normal vacancy rate of 2.10% to the 639 budgeted positions to determine the FPFTY payroll expense allowance represents a fair and reasonable adjustment to PECO's payroll expense claim.[64] I&E's method of applying the vacancy rate of 2.10% to the total 639 budgeted positions because normal vacancies will occur

[58] PECO MB, p. 31.
[59] *Id.*
[60] *Id.*
[61] I&E MB, p. 25.
[62] *Id.*
[63] I&E MB, pp. 25-26.
[64] *Id.*, p. 26.

across the board in the total budgeted positions and not merely with respect to the proposed new positions is correct and should be adopted by the Commission.[65] I&E continues to recommend an allowance of $41,350,285, and accordingly, a reduction of $858,715 to PECO's claim of $42,209,000 payroll expense. As a result, I&E continues to also recommend an allowance of $5,797,603 for employee benefits expense, or a reduction of $120,397 ($5,918,000 - $5,797,603) to the Company's claim.[66]

B. Contracting and Materials Expense

I&E continues to recommend an allowance of $32,940,000, or a reduction of $10,015,000 ($42,955,000 - $32,940,000) for contracting/materials cost.[67] I&E's recommendation is based on an average of the last three years' expense because PECO's peculiar and significant increase in the FTY and FPFTY claims are unsupported and speculative; and, the Company has experienced budgeted underspent expense levels in the prior three fiscal years.[68]

The Company argues the actual amount incurred by the Company during the HTY was significantly lower than expected due to temporary impacts from the COVID-19 pandemic.[69] For example, the Company asserts construction work stoppages in March through June 2020 reduced the need to locate Company facilities, and COVID-related restrictions reduced work levels in the Company's mapping plan and slowed the

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65 *Id.*
66 *Id.*
67 I&E MB, p. 29.
68 *Id.*, p. 27.
69 PECO MB, p. 32.

Company's efforts to repair non-emergent leaks.[70] The Company estimates that these COVID-related impacts reduced its HTY contracting and materials expense by approximately $6 million.[71] Concluding, this result was an anomaly and not indicative of future levels of the Company's contracting and materials expense.[72]

I&E reiterates the arguments made in its main brief.[73] The Company's claims are unsupported, as the Company states, they are "estimates." In the absence of a detailed explanation and support for the significant increase of 51.09% from the HTY to the FTY expense claim, neither the FTY nor the FPFTY expense claims are reasonable, prudent or reliable because the FTY increase is reflected in the FPFTY claim.[74] The Company has provided no substantial evidence to support the claim that all the projected expense increases in the FTY for new planned activities will continue to be incurred in the FPFTY.[75]

Finally, the Company's actual contracting and materials expenses were underspent by 11.42% in 2017-18, 2.76% in 2018-19, and 24.46% in 2019-20 as compared to the budgeted expense in the respective fiscal years.[76] I&E asserts that its recommendation based on an average of the last three years' expense is reasonable and an appropriate basis for determining the FPFTY allowance for the contracting and materials expense, and therefore I&E continues to recommend an allowance of $32,940,000, or a reduction

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70 *Id.*
71 *Id.*
72 *Id.*
73 I&E MB, pp. 27-29.
74 *Id.*, p. 28.
75 *Id.*
76 I&E MB, pp. 28-29.

of $10,015,000 ($42,955,000 - $32,940,000) for contracting/materials cost.[77]

C. Outside Services (including Exelon Business Service Company Charges)

I&E continues to recommend a walk-up adjustment for inflation from the HTY to the FTY and then to the FPFTY resulting in an allowance of $13,437,856 or a reduction of $3,134,144 ($16,572,000 - $13,437,856) to the Company's claim for outside services net of the "cost to achieve" adjustment of $370,000.[78] I&E's recommendation for outside services is based on forecasted CPI inflation factors for the FTY and FPFTY in contrast to the Company's speculative and unsupported significant increase of 26.55% from the HTY to the FTY, and then an additional 4.57% increase from the FTY to the FPFTY claim.[79]

The Company continues to argue that the FPFTY claim for total Exelon Business Services Co. (EBSC) charges is $22,000,000 and the FTY claim of $21,000,000 is lower than the historic three-year average; therefore, the FPFTY claim for EBSC is consistent with the historic three-year average.[80] Then, PECO attempts to clarify that the FPFTY outside services expense claim of $16.5 million represents a combination of: (a) EBSC contracting charges; and (b) PECO contracting charges, allocated to FERC Account 923.[81]

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[77] *Id.*, p. 29.
[78] I&E MB, p. 29.
[79] *Id.*, pp. 29-30, *citing* I&E St. No. 1, pp. 20-22.
[80] PECO MB, p. 34.
[81] *Id.*

I&E disagrees and continues to assert that the Company is attempting to justify the unsupported significant increase of 26.55% in the FTY over the HTY actual expense, and an additional 4.57% increase up to the FPFTY claim for outsides services expense, by comparing the FPFTY total EBSC cost with the historic three-year average of EBSC costs.[82] Summarizing I&E's Main Brief, PECO had been experiencing a declining trend in both the EBSC costs and the contracting service costs for the three years prior to the FTY.[83] The FPFTY EBSC claim of $15,290,000 is higher by 15.53% over the historic three-year average of $13,234,000.[84] Similarly, the FPFTY contracting service claim of $726,000 is higher by 15.79% over the historic three-year average of $627,000.[85] The percentage of the jump to the FPFTY is not supported and the Company's assertion of reasonableness is not convincing.

I&E continues to recommend a walk-up adjustment for inflation from the HTY to the FTY and then to the FPFTY that adjusts the HTY actual outside services for inflation based on the Consumer Price Index (CPI) factors of 2.75% and 2.03% to determine the FTY and FPFTY allowances is fair and reasonable.

D. Other Post-Employment Benefits Expense

I&E continues to recommend an allowance of $270,000, or a reduction of $780,000 ($1,050,000 - $270,000) for OPEB expense.[86] I&E's recommendation is based on continuing the FTY claim as the FPFTY allowance because the Company's projected

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82 I&E MB, p. 30.
83 *Id.*
84 *Id.*, pp. 30-31.
85 *Id.*, p. 31.
86 I&E MB, p. 33.

increases in the FTY and FPFTY claims are based on assumptions, which are not supported.[87] Therefore, the significant increase of 74.28% in the FPFTY expense claim over the FTY expense claim is not supported, nor reasonable, or reliable.[88]

The Company continues to argue that the OPEB plan design change resulted in a re-measurement of the Company's OPEB obligation, which resulted in a prior service credit recorded to other comprehensive income.[89] Further, the Company conveniently states that its claim was supported in testimony.[90]

I&E reiterates the arguments made in its main brief that the Company's arguments are not supported by the information provided by the Company.[91] Further, in the absence of detailed information about the service credit adjustments reflected in the OPEB costs of the last three fiscal years and the adjustments made in the FTY and FPFTY OPEB claims, I&E's recommendation based on the FTY claim amount is appropriate and reasonable.[92] I&E continues to recommend an allowance of $270,000 and accordingly, a reduction of $780,000 to PECO's claim of $1,050,000 for OPEB expense.[93]

E. Costs to Achieve Exelon/PHI Merger

I&E continues to recommend a disallowance of the $370,000 cost to achieve expense adjustment in its entirety, which was included in the FPFTY outside services expense claim.[94] I&E makes this recommendation because the Company's claim for

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87 *Id.*, p. 32.
88 *Id.*
89 PECO MB, p. 36.
90 *Id.*, p. 37.
91 I&E MB, pp. 32-33.
92 *Id.*, p. 33.
93 *Id.*
94 I&E MB, p. 35.

recovery of historic merger cost results in a retroactive recovery in rates in the absence of the Commission's prior permission to defer the merger related costs for ratemaking purposes.[95] Additionally, the merger costs were incurred during 2016 through 2018, prior to the HTY, and the offsetting merger related savings were also realized in prior years.[96] Furthermore, the Company has not proposed retroactive sharing of those savings with ratepayers.[97]

PECO asserted the Commission should reject I&E's proposed disallowance arguing the Commission may permit recovery of prior period unanticipated, extraordinary, and non-recurring expenses without violating the prohibition against retroactive ratemaking.[98] PECO also argues the proposed three-year amortization period is reasonable.[99]

I&E disagrees and reiterates that the Company did not request or receive permission to defer the prior period merger related costs for ratemaking purposes and all those costs were incurred during 2016 through 2018 prior to the HTY.[100] Further, PECO's claim in this instance does not fall within any exception to the general rule against retroactive ratemaking as the accrual of the merger costs was not unanticipated or extraordinary.[101]

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[95] *Id.*, p. 34.
[96] *Id.*
[97] *Id.*
[98] PECO MB, p. 38.
[99] *Id.*
[100] I&E MB, pp. 34-35, (citation omitted).
[101] *Id.*, p. 35.

Additionally, I&E reiterates that the merger related savings of approximately $4.30 million were already realized in prior years and the Company has not proposed retroactive sharing of those savings with the ratepayers.[102] Most importantly, the Company has already saved, at a minimum, $0.5 million in 2016, $0.9 million in 2017, $0.9 million in 2018, $1.00 million in 2019, and $1.00 million in 2020, aggregating $4.30 million in the last five years.[103] The Company is seeking recovery of prior period total merger cost of $1,111,000 over a three-year amortization period, which is unsupported, inappropriate and unreasonable; and, I&E continues to recommend a disallowance of the $370,000 ($1,111,000 ÷ 3) costs to achieve expense claim in its entirety.[104]

F. General Assessments

I&E took no position regarding the Company's claim for general assessments.

G. Research and Development Expenses

I&E took no position regarding the Company's claim for research and development expenses.

H. Employee Activity Costs

I&E continues to recommend an allowance of $58,469, or a reduction of $80,933 ($139,402 - $58,469) to the Company's claim for employee activity costs.[105]

The Company argued that I&E's position is contrary to the Commission's prior decision rejecting similar adjustments.[106] The Company asserted the costs challenged by

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[102] *Id.*
[103] *Id.*
[104] *Id.*
[105] I&E MB, p. 38.
[106] PECO MB., p. 41.

I&E relate to employee recognition events, which the Commission has found may properly be included in a utility's operating expenses for ratemaking purpose.[107]

I&E disagrees and incorporates the arguments made in its main brief.[108] The ratepayers should not be required to fund the Company's decisions to offer special events to its employees and their families that are arguably not employee recognition events, as it is not a reasonable or prudent expense.[109] I&E continues to recommend an allowance of $58,469, and accordingly, a reduction of $80,933 to PECO's claim of $139,402.[110]

I. Travel, Meals and Entertainment

I&E continues to recommend an allowance of $862,153, or a reduction of $169,847 ($1,032,000 - $862,153) for travel, meals, and entertainment expense.[111] I&E's recommendation is based on applying the CPI inflation factor of 2.03% to the FTY claim to determine a FPFTY allowance, and the rejection of PECO's significant increase of 22.13% in the FPFTY claim as unsupported, speculative, and inconsistent with the Company's assertion for an increased claim due to general inflation.[112]

The Company continued its argument, that PECO's budgeted data for the FTY and FPFTY are more representative of the current and future conditions than the HTY data.[113]

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107 *Id.*
108 I&E MB, pp. 37-38.
109 *Id.*, p. 38.
110 *Id.*
111 I&E MB, p. 40.
112 *Id.*, pp. 38-39.
113 PECO MB, p. 42.

I&E rejects the Company's argument as unsupported and unreasonable, and reiterates the arguments made in its main brief. I&E recommends an allowance of $862,153 based on a reduction of $169,847 to PECO's claim of $1,032,000.

J. Membership Dues

I&E continues to recommend an allowance of $588,135 based on a reduction of $67,762 ($655,897 - $588,135) to PECO's industry organization membership expense claim of $655,897.[114]

The Company argued that its budgeted amounts for membership dues in the FTY and FPFTY are reasonable.[115] Asserting the Company's actual membership dues expense has fluctuated in the prior three years.[116]

I&E rejects the Company's arguments and incorporates the arguments from its main brief asserting that these increases are speculative and unreliable because they are not consistent with acceptable inflation rates.[117] I&E continues to recommend an allowance of $588,135 based on a reduction of $67,762 ($655,897 - $588,135) to PECO's industry organization membership expense claim of $655,897.

K. Injuries and Damages

I&E took no position regarding the Company's claim for injuries and damages.

L. Property Taxes

I&E took no position regarding the Company's claim for property taxes.

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114 I&E MB, pp. 41-42.
115 PECO MB, p. 43.
116 *Id.*
117 I&E MB, pp. 40-41.

M. Energy Efficiency and Conservation Program Costs

I&E continues to recommend an allowance of $2,727,500, or a reduction of $1,772,500 ($4,500,000 - $2,727,500) to the expanded EE&C program cost.[118] I&E's recommendation was primarily based on the limited historic participation rate of PECO's current rebate programs and the reasons set forth in I&E's main brief.[119]

The Company acknowledged that past customer participation levels have not met projections and argued a more targeted marketing efforts and trade ally engagement were planned to increase customer participation and justified the full program funding proposed by PECO.[120]

I&E reiterates, the Company's speculation that a 16% increase in Energy Star™ rebates in the fourth quarter of 2020, as compared with the fourth quarter of 2019, supports PECO's inflated customer participation forecasts and the Company's request for a significantly increased FPFTY claim of $4,500,000 (a 65% increase) for the expanded EE&C programs in contrast to the current program cost of $2,727,500, is not reasonable, prudent, nor supported.[121] I&E continues to recommend an allowance of $2,727,500 based on a reduction of $1,772,500 to PECO's claim of $4,500,000.

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118 I&E MB p. 46.
119 *Id.*, p. 43.
120 PECO MB, pp. 45-46.
121 I&E MB, pp. 43-46.

N. Rate Case Expense Normalization

I&E continues to recommend an allowance of $311,800 ($1,559,000 ÷ 5 years), or a reduction of $208,200 ($520,000 - $311,800) to the Company's FPFTY claim.[122] The I&E recommendation to normalize rate case expense over a period of 60 months (five years) was based on PECO's historic rate case filing frequency in contrast to PECO's request for a 36-month amortization period.[123]

The Company continued to argue its proposed three-year normalization of rate case expense is reasonable and should be adopted because PECO's projected need for rate relief in three years will be driven by the capital requirements of the Company's planned infrastructure improvement programs.[124] Additionally, the Company again references the 2012 PPL Electric Utilities Corporation and the 2017 UGI Utilities, Inc. - Electric Division rate cases.[125]

I&E disagrees and incorporates the arguments made in I&E's main brief reiterating that the Commission has continually found in favor of I&E's recommendation for a normalization period based on the actual historic filing frequency.[126] I&E continues to recommend a 60-month normalization period for rate case expense, and accordingly, a reduction of $208,200 to PECO's claim of $520,000.

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[122] I&E MB, p. 47.
[123] *Id.*, p. 46.
[124] PECO MB, p. 47.
[125] *Id.*, p. 48.
[126] I&E MB, p. 47, (citations omitted).

O. Regulatory Initiatives

I&E continues to recommend an updated allowance of $28,200 ($141,000 ÷ 5-year amortization), or a reduction of $18,800 ($47,000 - $28,200) to PECO's revised claim of $47,000.[127] The I&E recommendation is based on a five-year amortization period in contrast to the Company's claimed three-year amortization for regulatory initiative costs.[128]

The Company continues to argue that a five-year amortization of this expense is unreasonable and should be rejected because the Company's proposed three-year amortization is consistent with three-year normalization period claimed for rate case expense, which is reasonable and should be adopted.[129]

I&E rejects the three-year amortization and continues to recommend an allowance of $28,200 ($141,000 ÷ 5-year amortization), or a reduction of $18,800 ($47,000 - $28,200) to PECO's revised claim of $47,000.

P. Manufactured Gas Plant Remediation Expense

I&E took no position regarding the Company's claim for its manufactured gas plant remediation expense.

Q. Depreciation Expense – Annual / Accumulated

See Section IV. RATE BASE, C. Depreciation Reserve, *supra*.

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127 I&E MB, p. 49.
128 *Id.*, p. 48.
129 PECO MB, pp. 48-49.

R. Cash Working Capital – Iteration

I&E continues to recommend an allowance of $2,902,236 or reduction of $320,764 ($3,223,000 22 - $2,902,236) to the Company's cash working capital claim.[130] I&E's recommendation includes modification of the Company's claim based on all recommended adjustments to O&M expenses.[131]

Finally, I&E's updated CWC recommendation is not a final recommendation, as all adjustments to the Company's claims must be continually brought together in the Administrative Law Judge's Recommended Decision and again in the Commission's Final Order. This process, known as "iteration," effectively prevents the determination of a precise calculation until all adjustments have been made to the Company's claims.[132]

VII. TAXES

I&E continues to recommend an allowance of $3,699,145 for payroll tax expense, or a reduction of $76,855 ($3,776,000 - $3,699,145) to the Company's claim.[133] I&E's recommendation for a reduction of payroll tax expense was based on I&E's recommended reduction to payroll expense.[134]

PECO disagreed with the I&E payroll tax expense adjustment based on PECO's denial of I&E's payroll expense adjustment.[135]

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130 I&E MB, p. 50.
131 *Id.*
132 *Id.*
133 I&E MB, p. 51.
134 *Id.*, pp. 24-27, 51.
135 PECO MB, p. 31.

Additionally, I&E took no position on the OCA's testimony regarding PECO's Federal and State income taxes.[136]

VIII. RATE OF RETURN

A. Introduction - Rate of Return Standards

I&E incorporates its discussion and arguments regarding its rate of return calculations in its main brief;[137] and, I&E continues to recommend the following rate of return[138] for PECO Gas:

Type of Capital	Ratio	Cost Rate	Weighted Cost
Long-Term Debt	46.62%	3.84%	1.79%
Common Equity	53.38%	10.24%	5.47%
Total	100.00%		7.26%

Rate of return is the revenue an investment generates in the form of net income; and is generally expressed as a percentage of the amount of capital invested over a given period of time.[139] A fair and reasonable overall rate of return is one that will allow the utility an opportunity to recover those costs prudently incurred by all classes of capital used to finance the rate base during the prospective period in which its rates will be in effect.[140]

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136 *Id.*, pp. 51-52.
137 I&E MB, pp. 51-53.
138 *Id.*, p. 51.
139 *Id.*, p. 52.
140 *Id.*

B. Capital Structure.

I&E continues to recommend using the Company's claimed capital structure as it falls within the range of the I&E proxy group's 2019 capital structures, which is the most recent information available at the time of I&E's analysis.[141]

C. Cost of Long-Term Debt

I&E continues to recommend using the Company's updated claimed long-term debt cost rate of 3.84% for the FPFTY, which results in a weighted cost of debt of 1.79%.[142] The Company's claimed cost rate of long-term debt is reasonable, as it is representative of the industry.[143]

D. Cost of Common Equity

I&E incorporates the arguments made in its main brief, and I&E continues to recommend using the Discounted Cash Flow method as the primary method to determine the cost of common equity[144] while also using the results of the Capital Asset Pricing Model as a comparison to the DCF results.[145] As a result of I&E's DCF analysis I&E recommended a cost of common equity of 10.24%.[146]

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141 I&E MB, p. 54; PECO MB, p. 56.
142 I&E MB, p. 54.
143 *Id.*; PECO MB, p. 58.
144 I&E MB, pp. 54-56.
145 *Id.*, pp. 54-55.
146 *Id.*, p. 55.

PECO continues to propose a cost of equity of 10.95%[147] which I&E rejects.[148] PECO also raised an issue regarding the development of the barometer (proxy) group.[149] But, as I&E noted, the Commission has stated its support for I&E's methodology for determining proxy groups in the recent *Columbia Gas* base rate proceeding.[150]

PECO also raised issues regarding dividend yield, growth rate, and a leverage adjustment.[151] But, through the Commission's acceptance of the Recommended Decision's acceptance of I&E's Discounted Cash Flow methodology in *Columbia Gas*, I&E's methodology regarding the dividend yield and growth rate were accepted, while the company's proposed leverage adjustment was rejected.[152] Therefore, I&E continues to recommend a cost of common equity of 10.24%.

E. Management Performance Points Request

I&E continues to assert that true management effectiveness is earning a higher return through its efficient use of resources and cost cutting measures.[153] The greater net income resulting from cost savings and true efficiency in management and operations is then available to be passed on to shareholders.[154] PECO Energy, or any utility, should not be awarded additional basis points for doing what they are required to do in order to provide adequate, efficient, safe, and reasonable service under 66 Pa. C.S.A. §1501.[155]

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147 PECO MB, p. 60.
148 I&E MB, p. 56.
149 PECO MB, p. 60-61.
150 I&E MB, pp. 58-59. See *Pa. P.U.C. v. Columbia Gas of Pennsylvania Inc. ("Columbia Gas")*, pp. 121-131, Docket No. R-2020-3018835 (Order entered February 19, 2021).
151 PECO MB, pp. 61-64.
152 I&E MB, pp. 54-56. *See also*, *Columbia Gas*, pp. 123-124, 130-131.
153 I&E MB, p. 56.
154 *Id.*
155 *Id.*

The Company continues to argue that an additional 25 basis points should be added for strong management performance.[156] PECO made the same arguments in its main brief that it has consistently made in written testimony.[157]

I&E rejects the Company's arguments and incorporates the arguments made in I&E's main brief.[158] Further, I&E reiterates that even a modest increase in the cost of equity by an additional 25 basis points translates to an additional $3,285,458 that would flow through to the ratepayers.[159] Additionally, the Commission recently affirmed the Administrative Law Judge's denial of management performance points in *Columbia Gas*.[160] I&E asserts that PECO Energy should not be awarded additional basis points.

F. Other Parties' Equity Cost Rate Recommendations

PECO continues to raise the same issues regarding I&E's cost of common equity calculations and recommendation that have been addressed and rejected in I&E's Main Brief;[161] by I&E witness Keller;[162] and most recently by the Commission in its *Columbia Gas* decision.[163]

As I&E noted *supra*, the Commission, in *Columbia Gas*, just stated its support for I&E's methodology of determining proxy groups for rate of return analysis.[164] Further, in *Columbia Gas*, the Commission adopted the Recommended Decision which adopted

156 PECO MB, p. 69.
157 *Id.*, pp. 69-71.
158 I&E MB, pp. 56-58.
159 *Id.*, p. 57.
160 *Id.*, p. 57-58.
161 I&E MB, pp. 54-59.
162 I&E St. No. 2, pp. 6-48; I&E St. No. 2-SR, pp. 3-37.
163 *See Columbia Gas*, pp. 103-141, Docket No. R-2020-3018835, Order entered February 19, 2021.
164 I&E MB, p. 58. *See also Columbia Gas*, pp. 110-112.

I&E's position for determining the appropriate cost of equity.[165] And by adopting the Recommended Decision agreeing with I&E, the Commission approved I&E's methodology regarding the dividend yield and growth rate while[166] rejecting Columbia's proposed size and leverage adjustments as flawed.[167] Finally, the proposed management performance points were discussed and rejected *supra* in Section VIII. E.

G. Conclusion as to Overall Rate of Return

I&E continues to recommend that the Company should be afforded the opportunity to earn an overall rate of return of 7.26%.[168] This recommended overall rate of return is comprised of a 46.62% long-term debt/53.38% equity capital structure at a cost rate of 3.84% and 10.24%, respectively.[169]

IX. CUSTOMERS PROGRAMS AND MISCELLANEOUS ISSUES

A. Recommendations Related to the COVID-19 Emergency

I&E took no position regarding this issue.

B. Universal Service Programs

I&E took no position regarding this issue other than the adjustments I&E made to the energy efficiency program costs in Section VI. EXPENSES, M. Energy Efficiency and Conservation Program Costs in its main brief[170] and in this reply brief *supra*.

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165 I&E MB, p. 59. *See also Columbia Gas*, pp. 137-141.
166 I&E MB, pp. 54-59. *See also*, *Columbia Gas*, pp. 123-124, 130-131.
167 *Id.*, p. 141.
168 I&E MB, p. 59.
169 *Id.*
170 I&E MB, pp. 43-46.

C. Neighborhood Gas Pilot Rider ("NGPR")

I&E continues to recommend allowing up to 40 feet of main line per contracted residential customer at no cost with certain limitations such as abnormal underground conditions or unusual permit requirements as stated by the Company.[171] I&E also continues to recommend an annual allowance of $5,000,000 ($25,000,000 ÷ 5 years) for the capital costs associated with the proposed change to the NGPR or a reduction of $2,500,000 ($7,500,000 - $5,000,000) to the Company's claim.[172]

PECO argues the Company has seen rapid uptake of natural gas service by potential customers.[173] Claiming that its assumption that 66% of customers will take service over 20 years should be updated to better align with NGPR data.[174] Second, the Company claims it continues to see strong interest in the NGPR in 2020 despite the impacts of the COVID-19 pandemic.[175] Based on the Company's claimed customer interest in the NGPR, the Company expects installed projects to increase by 25 neighborhoods per year under the revised program.[176] But these are simply baseless assumptions.

The I&E reiterates from its main brief that I&E's recommendation is based on the fact that the Company has only spent $15,500,000 since the beginning of the NGPR despite having a spending limit of $25,000,000[177] demonstrating the Company has not

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[171] I&E MB, p. 62.
[172] *Id.*
[173] PECO MB, p. 87.
[174] *Id.*
[175] *Id.*
[176] *Id.*
[177] I&E MB, p. 61.

spent the amount currently allocated to the NGPR.[178] I&E's recommendation was also based on the Company's current CIAC calculation which assumes 66% of customers would take service over a 20-year period; however, only 44% of eligible customers have taken service since the inception of the NGPR.[179] Further, I&E continues to assert the Company may be able expand its program sufficiently to achieve its originally projected targets, but there is no data to support increasing the funding for this program at this time based on historic performance where there was a decrease in inquiries regarding the NGPR, the number of main extension projects, and number of residential customers having gas available from the NGPR from 2019 to 2020.[180]

I&E continues to recommend allowing up to 40 feet of main line per contracted residential customer at no cost with certain limitations such as abnormal underground conditions or unusual permit requirements as stated by the Company. Further, I&E also continues to recommend an annual allowance of $5,000,000 ($25,000,000 ÷ 5 years) for the capital costs associated with the proposed change to the NGPR or a reduction of $2,500,000 ($7,500,000 - $5,000,000) to the Company's claim.

D. Energy Efficiency and Conservation Programs

I&E's stated positions regarding PECO's energy efficiency and conservation programs and the associated costs is set forth in Section VI. EXPENSES, M. Energy Efficiency and Conservation Program Costs of its main brief[181] and this reply brief *supra*.

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178 *Id.*
179 *Id.*
180 *Id.*, p. 62.
181 I&E MB, p. 43-46.

Further, promising to return unspent monies to customers regarding a program in which past customer participation levels have not met projections and program expenditures have been less than the budgeted amounts, is not substantial credible evidence supporting a claimed need for increased funding to the underperforming program.

E. Quality of Service

1. Distribution Integrity Management Program

I&E made recommendations regarding PECO's Distribution Integrity Management Program in I&E witness Elena Bozhko's PROPRIETARY direct and surrebuttal testimony.[182] The focus of I&E's recommendations is to improve PECO's methodology for both monitoring and reducing risk and damage to the PECO distribution system. I&E is not intending to be hypercritical of PECO's existing methodology, but rather to recommend improvements. Finally, for purposes of brevity and to avoid including large amounts of proprietary information in this Main Brief, I&E refers the reader to Ms. Bozhko's PROPRIETARY direct and surrebuttal testimonies where the confidential discussions and recommendations can be found.

PECO correctly identifies the controlling federal and state statutes and regulations in its main brief.[183] And, PECO correctly states that the federally-mandated Distribution Integrity Management Program provides utilities with a methodology to use to identify and resolve risks to the distribution system which includes a rigorous framework for

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[182] I&E MB, pp. 63-64, *citing* I&E St. No. 4 PROPRIETARY, pp. 6-24; I&E St. No. 4-SR PROPRIETARY, pp. 7-9.
[183] PECO MB, p. 90.

analyzing, ranking, and mitigating threats, and evaluating the effectiveness of those risk mitigation actions.[184]

With I&E's experience regarding working with the various natural gas distribution companies in the real-world application of the controlling federal and state statutes and regulations in mind, I&E's recommendations are suggested methods to improve both the monitoring and reduction of risk and damages to the PECO distribution system.[185]

2. Leaks and Excavation Damage

See I&E's reply in Section IX. E. 1. Distribution Integrity Management Program above. Two of the main causes of reportable incidents are pipeline leaks caused by corrosion and damage to pipelines caused by third parties.[186] And, as stated above, I&E continues to recommend the suggested methods to both monitor and reduce risk and damages to the PECO distribution system as discussed in I&E witness Bozhko's PROPRIETARY direct and surrebuttal testimonies.[187]

X. RATE STRUCTURE

To summarize, a utility's rate structure implements the Commission's approved revenue increase to determine how the overall increase will be allocated among the utility's various rate classes.[188] Once a class revenue allocation is determined, development of a rate design will address how the tariffed rates and rate elements will

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184 *Id.*
185 I&E MB, pp. 63-64, *citing* I&E St. No. 4 PROPRIETARY, pp. 6-24; I&E St. No. 4-SR PROPRIETARY, pp. 7-9.
186 I&E MB, p. 64.
187 *See* I&E St. No. 4 PROPRIETARY, pp. 6-24; I&E St. No. 4-SR PROPRIETARY, pp. 2-9.
188 I&E MB, p. 64-65.

generate the allocated revenues.[189] Public utility rates should enable the utility to recover its cost of providing service and should allocate this cost among the utility's customers in a just, reasonable and nondiscriminatory manner.[190]

A. Cost of Service

1. PECO Revised Gas Cost of Service Study ("COSS")

PECO ultimately provided an updated cost-of-service study in response to discovery requests from OSBA.[191] I&E based its customer cost analysis on the updated COSS.[192] The customer cost analysis is a part of the analysis of a COSS that is used to determine the appropriate fixed customer charges for the various classes and meter sizes; and it includes customer costs only.[193]

2. Opposing Party Recommendations

I&E agrees with using the Average and Excess methodology, as presented by the Company, as a reasonable method to allocate costs and revenues in this proceeding.[194] I&E has also supported the Peak and Average methodology in previous cases.[195] I&E believes that both COSS methodologies are reasonable solutions when performing a COSS for natural gas utilities.[196] In this case, I&E determined that the Company's proposed allocation methodology is reasonable.[197]

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189 *Id.*, p. 64.
190 *Id.*, p. 65, (citation omitted).
191 *Id.*, p. 65.
192 *Id.*
193 *Id.*
194 I&E MB, p. 65.
195 *Id.*, p. 66.
196 *Id.*
197 *Id.* *See also* PECO MB, pp. 99-103.

I&E continues to believe the Company's revised COSS is reasonable except for the calculation of the relative rate of return as discussed in B. Revenue Allocation *infra*.

B. Revenue Allocation

1. PECO Revised Revenue Allocation

The Company revised its proposed revenue allocation in order to conform to its revised COSS and also to eliminate the differences between the system average rates of return for the GC and L rate classes as required under the terms of the 2008 base rate case settlement at Docket No. R-2008-2028934.[198] I&E identified several issues regarding the Company's proposed rate allocation methodology.[199]

The Company is proposing a 389% increase for the L rate class and approximately 27% increases for the GR and TS-F classes while proposing rate decreases for the remaining classes.[200] First, the 389% rate increase for the L rate class is excessive and violates the concept of gradualism and could result in rate shock for those customers.[201] Second, I&E agrees with the rebuttal testimony of OCA witness Watkins regarding the unfairness of certain rate classes receiving rate increases while other rate classes are receiving rate decreases.[202] For these two reasons, the Company's proposed revenue allocation is not reasonable and should be rejected.[203] Ultimately, I&E continues to recommend a revised revenue allocation as discussed below.

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198 PECO MB, p. 112.
199 I&E MB, pp. 67-69.
200 PECO MB, p. 112.
201 I&E MB, p. 67.
202 *Id.*
203 *Id.*

2. Opposing Party (I&E) Alternative Revenue Allocations

To summarize, I&E's final proposed revenue allocation was arrived at using the data provided by the Company in PECO Exhibits JD-1R through JD-6R by first creating a schedule that shows the calculation of relative rates of return based on proposed revenue, expenses, taxes, net income and rate base by class.[204]

Then, based on I&E's proposed revenue allocation schedule and taking into consideration the issues brought forth by the OCA and OSBA, I&E developed its recommended revenue allocation.[205] Additionally, the revenue increases shown in I&E Exh. No. 3-SR, Sch. 4 include adjustments for the GPC and MFC reductions.[206]

3. Scale Back of Rates / Gradualism

PECO noted that the parties are in general agreement regarding the scale back that should occur, subject to certain specific differences, if the Commission grants less than PECO's requested revenue increase.[207]

I&E originally recommended that the only rate classes that should receive a scale back, should the Commission grant less than the Company's full requested increase, were the residential, TS-I, and TS-F classes.[208] I&E revised its proposed scale-back as a result of its revised revenue allocation.[209] Therefore, I&E recommends that only the rates of those rate classes that receive an increase be scaled back proportionately based on the

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204 I&E MB, p. 68, *citing* I&E St. No. 3-SR, p. 21.
205 *Id.*, p. 68, *citing* I&E Exh. No. 3-SR, Sch. 4.
206 *Id.*
207 PECO MB, p. 114.
208 I&E MB, p. 69.
209 *Id.*

COSS ultimately approved by the Commission.[210] Further, I&E continues to recommend that the customer charges be included in the scale back of rates.[211]

Finally, I&E noted that gradualism is a well-established ratemaking concept that seeks to limit the immediate increases customers receive when rates are increased and instead seeks to implement significant rate changes on a more gradual basis over time.[212] If the Commission should approve a rate increase, then the Commission has the discretion to apply the concept of gradualism if the Commission determines the rate increase would result in a sudden and excessive increase that would violate the concept of gradualism.[213]

C. Allocation of Universal Service Program Costs

I&E took no position with regard to the OCA's and CAUSE-PA's recommendation that the Company allocate universal service costs to all customer classes.[214] I&E notes that the Company, OSBA, and PAIEUG oppose the recommendation.[215]

D. Tariff Structure / Rate Design

1. Residential Customer Charge

I&E noted that even though the Company's proposed $16.00 customer charge is supported by the customer cost analysis, the $4.25 increase from $11.75 to $16.00, or

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210 *Id.*
211 *Id.*
212 I&E MB, p. 69.
213 *Id.*, (citation omitted).
214 *See* PECO MB, p. 115.
215 *Id.*

36%, is a significant increase that should not be granted.[216] I&E disagrees with the Company that the customer charges of other natural gas distribution companies should be the determining factor for the rates of PECO customers.[217] I&E continues to recommend that any increase in the customer charge be included in the scale back of rates if the Commission grants less than the full requested increase.[218]

2. Non-Residential Customer Rate Design

I&E reiterates that any analysis regarding the setting of non-residential customer charges and rate design should include a review of the COSS; the customer cost analysis; and, the relative rate of return regarding rate allocation.[219]

3. DSIC Cost Allocation

I&E reiterates that application of the Distribution System Improvement Charge and related cost allocation is governed by the Public Utility Code.[220] I&E recommends the Commission apply the relevant sections of the Public Utility Code to any proposed DSIC cost allocation methodology.

4. Negotiated Gas Service

I&E continues to recommend that the Company provide an update to the competitive alternative analysis for any customer that has not had their alternative fuel source verified for a period of 5 years or more at the point at which PECO files a base

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216 I&E MB, p. 70.
217 *Id.*
218 *Id.*
219 I&E MB, p. 71.
220 I&E MB, p. 71, (citation omitted).

rate case.[221] I&E also continues to recommend that the Company cease NGS service to any customer that does not have a verified alternative supply and switch those customers to the appropriate tariffed rate.[222] Further, I&E continues to recommend that, in future base rate cases, PECO separate the costs and revenues of customers discounted or reduced rates in their own class in the cost of service study.[223]

The Company agreed with an OCA recommendation but rejected I&E's and OSBA's recommendations.[224] The Company repeated its arguments that the Company's Commission-approved tariff for Rate NGS does not require the Company to re-evaluate customer eligibility for Rate NGS at any specified time, except when a customer initially applies for service.[225] Arguing further, requiring the Company to review the eligibility of its Rate NGS customers every five years would potentially create instability for the Company's Rate NGS customers and make it less likely that customers would enter into competitive agreements with the Company.[226] Concluding, such customers might be more likely to pursue alternatives to PECO service, ultimately resulting in a risk of lost revenues that would negatively impact all PECO gas customers.[227]

I&E rejects PECO's arguments and reiterates, it is important to periodically analyze competitive alternatives to ensure that the rates of flex rate customers are not discounted lower than is necessary to avoid the customer choosing the alternative supply.

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[221] I&E MB, p. 73.
[222] *Id.*
[223] *Id.*
[224] PECO MB, p. 126.
[225] *Id.*, p. 127.
[226] *Id.*
[227] *Id.*

Providing excessive discounts to customers would be harmful to both the Company and its customers since the other customers make up the revenue shortfall that results when flex-rate customers pay less than tariff rates.[228] The rates of non-negotiated customers will always be higher than if the negotiated customers were paying non-discounted rates whether the Company is providing service to those customers or not.[229] The only safeguard that customers have to protect them from absorbing the costs from excessively discounted rates is the verification of competitive alternatives for the negotiated rate customers.[230]

5. Theft/Fraud Investigation Charge

I&E took no position regarding this issue.

E. Summary and Alternatives

I&E's overall rate structure analysis included the noted reviews of the COSS; the customer cost analysis; and the relative rate of return regarding rate allocation.[231] Further, I&E's proposed monthly customer charge; as well as its gradualism and scale back recommendations, are all based on sound Commission ratemaking policies and precedent, and, should be implemented in this proceeding.[232]

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[228] I&E MB, p. 73.
[229] *Id.*
[230] *Id.*
[231] I&E MB, pp. 65-74.
[232] *Id.*, pp. 70-74.

XI. CONCLUSION

I&E respectfully submits that for all the reasons presented in I&E's Main Brief and this I&E Reply Brief, PECO Gas has not met its burden of proof as the record evidence presented by PECO Gas does not substantiate a revenue increase of $68.7 million. Instead, based on the weight of the record evidence, Your Honor and the Commission should only grant PECO Gas the I&E recommended revenue increase of $26.3 million.

Respectfully submitted,

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Prosecutor
PA Attorney ID No. 63641

Dated: March 15, 2021

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No.: R-2020-3018929
	:	
PECO Energy Company – Gas Division	:	

<u>CERTIFICATE OF SERVICE</u>

I hereby certify that I am serving the foregoing **Reply Brief** dated March 15, 2021, in the manner and upon the persons listed below.

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