COMMONWEALTH OF PENNSYLVANIA

July 27, 2023

E-FILED

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

Re: Pennsylvania Public Utility Commission v. Philadelphia Gas Works / Docket No. (R-2023-3037933)

Dear Secretary Chiavetta:

Enclosed please find the Main Brief, on behalf of the Office of Small Business Advocate ("OSBA"), in the above-captioned proceeding.

Copies will be served on all known parties in this proceeding, as indicated on the attached Certificate of Service.

If you have any questions, please do not hesitate to contact me.

Sincerely,

/s/ Sharon E. Webb

Sharon E. Webb
Assistant Small Business Advocate
Attorney ID No. 73995

Enclosures
cc: Robert D. Knecht
Parties of Record

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	**R-2023-3037933**
Office of Consumer Advocate	:	**C-2023-3038846**
Office of Small Business Advocate	:	**C-2023-3038885**
Philadelphia Industrial And Commercial Gas User Group	:	**C-2023-3039059**
Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.	:	**C-2023-3038727**
James M. Williford	:	**C-2023-3039130**
	:	
v.	:	
	:	
Philadelphia Gas Works	:	
Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.	:	
	:	
v.	:	**C-2021-3029259**
	:	
Philadelphia Gas Works	:	

MAIN BRIEF
ON BEHALF OF THE
OFFICE OF SMALL BUSINESS ADVOCATE

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Assistant Small Business Advocate
Attorney ID No. 73995

For: NazAarah Sabree
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Dated: July 27, 2023

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I. INTRODUCTION AND PROCEDURAL HISTORY

A. Introduction

The Office of Small Business Advocate ("OSBA") is an agency of the Commonwealth of Pennsylvania authorized by the Small Business Advocate Act (Act 181 of 1988, 73 P.S. §§ 399.41 – 399.50) to represent the interests of small business consumers as a party in proceedings before the Pennsylvania Public Utility Commission ("Commission"). On February 27, 2023, Philadelphia Gas Works ("PGW" or "Company") filed Supplement No. 159 to Philadelphia Gas Work's Gas Service Tariff –Pa. P.U.C. No. 2, and proposed Supplement No. 105 to Philadelphia Gas Works Supplier Tariff-Pa. P.U.C. No 1 ("Supplement No. 105"). The proposed Tariffs, if approved by the Commission, would increase the retail distribution rates of Philadelphia Gas Works ("PGW" or "Company") by $85.5 million per year before the effects on universal service charges and distribution system improvement charges are recognized. In addition to the rate filing, PGW filed a Petition for Waiver seeking a waiver of the application of the statutory definition of the fully projected future test year ("FPFTY") to permit PGW to use a FPFTY beginning September 1, 2023 in this proceeding.

On March 9, 2023, the OSBA filed a Complaint, alleging that the materials filed by PGW may be insufficient to justify the rate increase requested and that the Company's present and proposed rates, rules, and conditions of service may be unjust, unreasonable, unduly discriminatory, and otherwise contrary to law, particularly as they pertain to small business customers.

In accordance with 52 Pa. Code § 5.502 and the procedural schedule established in this matter by Orders entered on May 10, 2023, the OSBA submits this Main Brief opposing the relief requested by PGW in its tariff filings.

B. Procedural History

On February 27, 2023, PGW filed Supplement No. 159 to Philadelphia Gas Work's Gas Service Tariff –Pa. P.U.C. No. 2, and proposed Supplement No. 105 to Philadelphia Gas Works Supplier Tariff-Pa. P.U.C. No 1 ("Supplement No. 105"). The proposed Tariffs, if approved by the Commission, would increase the retail distribution rates of Philadelphia Gas Works ("PGW" or "Company") by $85.5 million per year (before the effects on universal service charges and distribution system improvement charges are recognized). In addition to the rate filing, PGW also filed a Petition for Waiver seeking a waiver of the application of the statutory definition of the fully projected future test year ("FPFTY") to permit PGW to use a FPFTY beginning September 1, 2023.

On February 28. 2023, the Bureau of Investigation and Enforcement ("I&E) filed a Notice of Appearance. Gray's Ferry Cogeneration Partnership ("GFCP") and Vicinity Energy Philadelphia, Inc. ("VEPI") (collectively "Vicinity") filed a Complaint (docketed at C-2023-3038727). On March 7, 2023, the Office of Consumer Advocate filed a Complaint and Notice of Appearance (docketed at C-2023-3038846). On March 9, 2023, the OSBA filed its Notices of Appearance and Formal Complaint (docketed at C-2023-3038885) in response to PGW's tariff filings. On March 17, 2023, the Philadelphia Industrial and Commercial Gas Users Group ("PICGUG") filed a Formal Complaint (docketed at R-2023-3039059). The Coalition for Affordable Utility Services and Energy Efficiency in Pennsylvania ("CAUSE-PA") filed a Petition to Intervene on April 12, 2023. The Tenant Union Representative Network ("TURN") and POWER Interfaith both filed Petitions to Intervene on April 25, 2023.

By Order entered April 20, 2023, pursuant to 66 Pa. §1308(d), PGW's Supplement No. 159 to Philadelphia Gas Work's Gas Service Tariff –Pa. P.U.C. No. 2, and proposed Supplement

No. 105 to Philadelphia Gas Works Supplier Tariff-Pa. P.U.C. No. 1 were suspended by operation of law until November 28, 2023. The Commission ordered an The Commission ordered an investigation into the lawfulness, justness, and reasonableness of the rates, rules, and regulations contained in the proposed Supplement No. 159 and 105.

A Pre-Hearing Conference Order and Notice were issued on April 20, 2023, scheduling a telephonic prehearing conference in this matter for April 28, 2023, before Administrative Law Judges ("ALJ") Eranda Vero and Arlene Ashton. A litigation schedule was established at the Pre-Hearing Conference and memorialized in the ALJs' Pre-Hearing Order issued on May 10, 2023.

On May 5, 2023, pursuant to a Commission order at Docket No. C-2021-3029259, the Company submitted supplemental direct testimony and exhibits regarding the proposed rates, rules and regulations to govern gas service provided to Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc. ("GFCP/VEPI"). These materials included a tariff page for a proposed Rate GS-XLT under which service would be provided to GFCP/VEPI..

Four public input hearings were held May 23, 2023 and May 24, 2023.

On May 31, 2023, the OSBA submitted the direct testimony of Robert D. Knecht.

On June 26, 2023, the OSBA submitted the rebuttal testimony of Robert. D. Knecht. On July 7, 2023, the OSBA submitted the surrebuttal testimony of Mr. Knecht.

Evidentiary hearings were held before ALJs Vero and Ashton on July 11 and 12, 2023. At the July 11, 2023 hearing, the OSBA moved the testimony of its witness, Robert D. Knecht, into the record.

II. LEGAL STANDARDS

A. Burden of Proof

Section 332(a) of the Public Utility Code, 66 Pa. C.S. § 332(a), provides that the party seeking a rule or order from the Commission has the burden of proof in that proceeding. It is axiomatic that "[a] litigant's burden of proof before administrative tribunals as well as before most civil proceedings is satisfied by establishing a preponderance of evidence which is substantial and legally credible." *Samuel J. Lansberry, Inc. v. Pennsylvania Public Utility Commission*, 578 A.2d 600, 602 (Pa. Cmwlth. 1990).

Although the burden of proof remains with the public utility throughout the rate proceeding, when a party proposes an adjustment to a ratemaking claim of a utility, the proposing party bears the burden of presenting some evidence or analysis tending to demonstrate the reasonableness of the adjustment. *Pa. PUC v. Aqua Pennsylvania, Inc.*, Docket No. R-00072711 (Order entered July 17, 2008). "Section 315(a) of the Code, 66 Pa. C.S. § 315(a), applies since this is a proceeding on Commission Motion. However, after the utility establishes a prima facie case, the burden of going forward or the burden of persuasion shifts to the other parties to rebut the prima facie case." *Pa. PUC v. Philadelphia Gas Works*, Docket No. R-00061931 (Order entered September 28, 2007), at 12.

The burden of proof to establish the justness and reasonableness of every element of the utility's rate increase rests solely upon the public utility. 66 Pa. C.S. § 315(a). "It is well-established that the evidence adduced by a utility to meet this burden must be substantial." *Lower Frederick Township. v. Pa. PUC*, 409 A.2d 505, 507 (Pa. Cmwlth. 1980).

B. Just and Reasonable Rates

Section 1301 of the Public Utility Code, 66 Pa. C.S. § 1301, provides that "every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the commission."

Furthermore, Section 523 of the Public Utility Code, 66 Pa. C.S. § 523, requires the Commission to "consider . . . the efficiency, effectiveness and adequacy of service of each utility when determining just and reasonable rates." In exchange for customers paying rates for service, which include the cost of utility plant in service and a rate of return, a public utility is obligated to provide safe, adequate, and reasonable service. "[I]n exchange for the utility's provision of safe, adequate and reasonable service, the ratepayers are obligated to pay rates which cover the cost of service which includes reasonable operation and maintenance expenses, depreciation, taxes and a fair rate of return for the utility's investors . . . In return for providing safe and adequate service, the utility is entitled to recover, through rates, these enumerated costs." *Pa. PUC v. Pennsylvania Gas & Water Co.*, 61 Pa. PUC 409 (1986), at 415-16. *See also* 66 Pa. C.S. § 1501. As a result, the legislature has given the Commission discretionary authority to deny a proposed rate increase, in whole or in part, if the Commission finds "that the service rendered by the public utility is inadequate." 66 Pa. C.S. § 526(a).

III. SUMMARY OF ARGUMENT

The ALJs and the Commission should be aware that, when measuring PGW's rate increase, the Company did not reset its Distribution System Improvement Charge ("DSIC") to zero, the base rate increase will also result in a DSIC increase.

Additionally, the increases in residential tariff rates will translate into an increase in costs for PGW's Customer Responsibility Program ("CRP") and therefore in the Universal Service and Efficiency Charge ("USEC").

Rather than the claimed $85.2 million, the Company's proposals in this proceeding will result in an increase of $101.3 million.[1] The OSBA analysis calculates, measured as a percent of YE 2023 city equity, PGW's current rates will produce a return on equity (inclusive of the city fee) of 12.9 percent, with a zero increase. With the proposed increase, the return on equity will be at least 23.1 percent.[2]

While the lion's share of utilities that the Commission regulates are rate base/rate-of-return regulated utilities, PGW is a cash flow regulated utility. For rate of return utilities, the Commission can exclude costs that it deems not reasonably allowed in utility rates. However, as a cash flow utility, PGW only has one source of revenue to cover its costs and its debt service requirements -- its ratepayers. The Commission should focus on ensuring that contributions by ratepayers benefit ratepayers and not other parties. The power of PGW's stakeholders to extract additional rents from PGW can be minimized by keeping rates to the bare minimum necessary to avoid a financial crisis. By keeping rates as low as possible, the Commission keeps PGW in a heightened state of alert with respect to controlling costs.

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[1] OSBA Statement No. 1, Table RDK-1.

[2] OSBA Statement No. 1 at 2.

The OSBA does not offer a specific revenue requirement proposal in this proceeding. However, the OSBA makes two observations regarding the Company's requested rate increase. First, the Company's financial forecasts in its last base rates proceeding included costs that proved to be far in excess of the costs it actually occurred. Specifically, PGW's actual to budget cost variances in FY 2021 and FY 2022 were favorable $98.7 million and $85.5 million respectively.[3] As a result, while PGW's ratepayers were struggling to cope with the pandemic, PGW was amassing some $416 million in year-end ratepayer funded equity between HTY 2019 in the last base rate case to HTY 2022 in the current case.[4] The OSBA respectfully submits that PGW's financial forecasts are not a reliable basis upon which to set rates in this proceeding.

Second, under Commission regulation, PGW has been permitted to set rates sufficiently high to allow it to increase its ratepayer-financed book equity by over $1 billion from 2007 to 2023.[5] In this proceeding, PGW incredibly claims that Commission regulation of PGW is perceived to be a negative risk factor, and therefore PGW should be awarded even larger rate increases.[6] The OSBA submits that PGW will simply never be satisfied with the rate increases awarded by the Commission, and that it is high time for the Commission to re-think its policy of allowing PGW to continue to amass vast amounts of book equity on the backs of its ratepayers.

On the subject of cost allocation, PGW proposes to use the 50/50 A&E method for mains costs allocation in this proceeding, consistent with Commission precedent. However, the Commission has recently made it clear that, for matters of cost allocation, Commission precedent even for a specific utility is not binding, and that cost allocation will be evaluated in each

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[3] OSBA Statement No. 1 at 14, Table RDK-3.

[4] OSBA Statement No. 1 at 13, Table RDK-2.

[5] OSBA Statement No. 1 at 12-13.

[6] OSBA Statement No. 1 at 10-11.

proceeding based on the evidence. The OSBA notes that three of the four experts offering cost allocation testimony in this proceeding opine that PGW's approach is not consistent with cost causation. However, acknowledging the Commission precedent and PGW's practice since 2007, OSBA's expert developed two different class cost of service studies, one using PGW's A&E method, and one using a customer-demand ("CD") method. The OSBA respectfully submits that these two methods provide a reasonable range of cost allocation results for rate-setting in this proceeding.

The second contentious cost allocation issue in this proceeding involves the assignment of mains costs to the Rate IT interruptible service class. PGW proposes to treat these customers as firm for cost allocation purposes, for the very credible reason that there have been no interruptions for nearly 20 years. Consistent with its past practice, PGW has again made no effort to undertake an evaluation of any actual benefit provided by the interruptibility of Rate IT customers. Given this history, OSBA respectfully submits that PGW's proposal to treat Rate IT customers as firm for cost allocation purposes is reasonable for this proceeding. However, OSBA respectfully recommends that the Commission direct PGW to undertake a detailed evaluation of any avoided costs associated with the interruptibility of Rate IT customers for the next base rates case.

PGW currently recovers costs associated with its universal service and energy conservation ("USEC") programs through a volumetric charge that applies to residential, government, and small to medium non-residential customers. Rate IT and Rate GTS customers are currently exempt from the charge. Three expert witnesses in this proceeding opine that non-residential customers do not benefit from the USEC programs and therefore should not bear the costs for the programs. This view, however, conflicts with long-standing PGW practice that pre-

dates Commission regulation of PGW. In this proceeding, however, PGW proposes to require Rate GS-XLT (formerly GTS) customers to contribute to the recovery of USEC costs. However, as originally proposed by the Company, the current volumetric nature of the USEC charge would produce an absurd charge for that class. This fact highlights a fundamental unfairness associated with the volumetric USEC charge, namely that the implicit tax rate for these social programs is, inequitably, much higher for non-residential customers than for residential customers. It is also inequitable for Rate IT customers to be exempted from this responsibility, as the social benefits of the USEC programs presumably inure to all Pennsylvanians. The OSBA recommends that universal service costs be allocated and recovered on a percentage of base rates charges basis, similar to the DSIC mechanism.

For assigning the rate increase among the various classes, the OSBA agrees with the Commonwealth Court that revenue allocation should reflect the principle of moving rates more into line with allocated cost, subject to rate gradualism considerations. Because the OSBA proposes a change in how USEC costs are recovered from each rate class, the rate gradualism principle must be applied to the total rate change, and not simply the base rate impacts. Thus, for example, the reduction in USEC charges to the GS-Commercial class resulting from the change in method allows for a larger base rate increase for that class. OSBA respectfully submits that the overall revenue allocation proposal posited by Mr. Knecht in his direct testimony reasonably reflects the implications of the change in USEC costing, the differences in class revenue-cost ratios, and the principle of rate gradualism.

Regarding service to GFCP/VEPI, PGW proposes that service be provided under a new rate class, Rate GS-XLT, with base rates set at the cost of service derived in the supplemental

filing, the application of USEC, OPEB, ECR and DSIC surcharges, and a market-based charge for alternative receipt service ("ARS"). The OSBA's positions are as follows:

a. The OSBA agrees with PGW that a separate rate class for GFCP/VEPI is appropriate, given the size of the customer and the nature of distribution service (i.e., through dedicated facilities paid-for by GFCP/VEPI).

b. Base rates tariff charges should reasonably reflect the cost of providing service to GFCP/VEPI, excluding any mains plant costs, but including metering, appropriate system regulation, O&M costs associated with the dedicated facilities, and A&G costs.

   Rate GS-XLT should contribute to USEC costs, based on the percentage of base rates charges proposed by OSBA.

   Rate GS-XLT should not be subject to the OPEB rider, as the OPEB costs are reflected in the cost basis for Rate GS-XLT base rates charges.

   Rate GS-XLT should not be subject to the ECR rider, unless and until PGW incurs EE&C costs associated with Rate GS-XLT customers.

   Re the DSIC, the OSBA concludes that it would be preferable for Rate GS-XLT to retain responsibility for any costs associated with major capital projects on the dedicated mains serving that facility.

   ARS is a gas supply arrangement ("swap"), in which GFCP/VEPI is effectively granted access to valuable upstream gas transmission capacity on Tetco's "Philadelphia Lateral," thereby using capacity that is paid for by GCR customers. The OSBA generally agrees with PGW that the charge for ARS should reflect the market value of the upstream capacity. The OSBA respectfully submits that the value for that capacity should be determined by putting that capacity out for competitive bid under an asset management arrangement. Moreover, because this transaction involves upstream gas supply capacity, the revenues associated with this service should be credited to the GCR and not base rates. The OSBA does not object to including this capacity release revenue in the GCR "sharing" mechanism,

such that 75 percent of the revenues are credited to the GCR and 25 percent are credited to base rates.

c. Except in extraordinary circumstances, GFCP/VEPI does not rely on PGW's low-pressure distribution system, and should not be allocated costs associated with that system. For those extraordinary circumstances, GFCP/VEPI should take service under regular tariff rates.

d. PGW's position in previous base rates cases, namely that GFCP/VEPI does not rely on PGW's distribution system, except for the dedicated lines for which GFCP/VEPI contributed the capital, was correct. PGW's assertions in the GFCP/VEPI complaint proceeding, the GCR, and the initial filing in this proceeding that GFCP/VEPI relied on the distribution system to deliver ARS volumes was nonsense and should be ignored.

Regarding GS-Commercial rate design, PGW proposes to increase the customer charge from $25.35 per month to $34.00, an increase of 34 percent. This increase would result in a customer charge that is reasonably consistent with allocated customer costs for small customers within the GS-Commercial class, but would be at the very high end of customer charges for commercial customers amongst Pennsylvania NGDCs. The OSBA respectfully submits that the Company's proposed charge should be accepted, but scaled back to reflect any reduction in the overall approved revenue requirement.

IV. ARGUMENT

A. Revenue Requirement

The OSBA did not provide a specific recommendation with regard to PGW's proposed revenue requirement.

B. Expenses

The OSBA is not addressing this issue in this Main Brief.

C. Rate Structure

1. Cost of Service

A utility class cost of service study ("CCOSS") is an analytical tool which assigns a utility's test year revenue requirement among the utility's rate classes.[7] PGW's CCOSS models provided in this proceeding are "embedded" cost of service studies, meaning that the allocated costs are the average book revenue requirements, rather than marginal costs.

This proceeding involves three cost allocation issues subject to debate: classification and allocation of mains costs, assignment of mains costs to Rate IT customers, and the assignment of cost responsibility for universal service and energy conservation ("USEC") program costs.

Cost allocation for a gas distribution utility often hinges on the methodologies chosen for the classification and allocation of mains costs. As noted in Mr. Knecht's direct testimony, PGW's mains costs allocation was last litigated in 2007 at Docket No. R-00061931 (Order entered September 28, 2007, p.80). In that proceeding, the Commission rejected PGW's proposal to include a customer component for mains costs, and it adopted the use of a 50/50 weighted average-and-excess allocator for all mains costs. This A&E method was applied to the Company's compliance filing in that proceeding, and was also used in the Company's 2010 base rate case.[8] For this proceeding, PGW proposes to continue using the 50/50 A&E method. Mr. Knecht however, finds this approach to be inconsistent with cost causation, and that there are economies of scale associated with serving larger customers. For purposes of analysis, and in acknowledgment of past Commission practice, Mr. Knecht developed two COSS simulations,

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[7] Mr. Knecht discusses the purpose and principles of an CCOSS in his Direct Testimony. *See* OSBA Statement No. 1 at 15-16

[8] OSBA Statement No 1 at 22.

one using the Company's A&E method, and the other using a customer-demand ("CD") method.[9]

Mr. Knecht presented the follow overview of PGW's CCOSS in this proceeding:

> The costs being allocated represent the Company's revenue requirement for the fully projected future test year ("FPFTY"), namely the twelve-months ending August 31, 2024. The Company's CCOSS was originally filed in pdf format (i.e., without an electronic version) in PGW Exhibit CEH-1 ("Filed CCOSS"). An electronic version was subsequently provided in response to OSBA-I-2. With the Company's update to its filing on May 5, 2023, a "supplemental" pdf version of the CCOSS was filed as Exhibit CEH-1S ("May 5 CCOSS"), and an electronic version of that model was provided on May 9, 2023 in response to PICGUG-III-4.
>
> Although PGW is a "cash-flow" regulated utility, it has a return component in its revenue requirement, inclusive of both interest on debt and net income. In addition, while it is not subject to income taxes, PGW incurs an annual $18 million fee to the City of Philadelphia (its shareholder). Both these revenue requirement items must be allocated.
>
> Also, the various components of a utility's rates, and the associated costs, are regulated separately, or may be subject to customer bypass through competition. In addition, revenues associated with specific cost items in the utility's revenue requirement, such as an energy efficiency program, may be recognized as class revenues or an offset to costs. Thus, it is not always clear whether and how various revenues and costs should be included in a utility's base rates CCOSS. PGW is particularly complicated in that regard, having more than its share of separate tariff charges.[10]

Given the difficulties and controversy surrounding the classification and allocation of mains costs, the Company approached the issue as explained by Mr. Knecht as follows:

> Assigning mains costs among the various rate classes is often one of the most contentious aspects of an NGDC's cost allocation study, for three primary reasons. First, mains represent a substantial portion of the Company's rate base. Since expenses are typically allocated in the same manner as plant, mains cost allocation represents the primary basis upon which other costs are allocated (O&M, and indirectly, A&G). Second, mains are "joint use" assets, meaning that many of the

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[9] OSBA Statement No. 1 at 26.

[10] *See* OSBA Statement No. 1at 15. For a detailed review of Mr. Knecht's understanding of PGW's proposed CCOSS treatment of the costs and revenues associated with its various tariff components. *See* OSBA Statement No. 1at 16-18.

system mains are used by more than one customer class at a time. As such, economic theory provides only limited guidance as to how such costs should be allocated. Moreover, it is difficult to identify the specific factors which cause the costs to be incurred. Finally, the different theories used by cost allocation analysts produce substantially different cost allocation results, and thus the choice of a specific methodology will have a significant impact on the rates paid by each rate class.

With respect to the theory of how mains costs should be allocated, there are some areas of general agreement. First, there is agreement that the cost allocation should, to the extent practicable, reflect "cost causation," such that costs are assigned to the rate classes that cause the costs to be incurred. There is also general agreement that NGDC mains must be installed in order to interconnect all the utility's customers, and they must have sufficient capacity to reliably meet the peak demands of the customers served under design conditions.[11] Finally, there is general agreement that mains costs exhibit significant economies of scope and scale. That is, it is more cost effective for one utility to serve a particular geographic area than to allow for competition. In addition, as the carrying capacity of a main increases, its cost increases at a much lower rate. Thus, all other factors being equal, the cost per unit of maximum carrying capacity for any particular main declines as mains diameter increases.

After that, agreement ends. Some (but far from all) analysts believe that, because the system must interconnect many customers, some portion of mains costs are causally related to customer count (i.e., that some mains costs should be *classified* as customer-related). The supporting argument for this position is that it requires more footage of mains to connect many smaller customers than one larger customer, even if total demand is the same. In addition, a NGDC is more likely to be able to use larger, less costly pipe to serve larger customers than to serve smaller customers. There is some statistical evidence in support of this relationship, but it is far from universally accepted.[12] To that end, there are methodologies that have been developed for estimating such a "customer component" of mains costs, but they are theoretically and conceptually weak.[13]

In this proceeding, parties take various positions regarding the classification and allocation of mains costs. As noted above, PGW proposes to apply the 50/50 A&E approach, for reasons of Commission precedent. However, PGW Witness Heppenstall concludes that, on

[11] PGW confirms that its distribution system is sized to meet customers' design day demands. PICGUG-I-3.

[12] http://publicsde.regie-energie.qc.ca/projets/235/DocPrj/R-3867-2013-B-0005-Demande-Piece-2013_11_15.pdf

[13] OSBA Statement No. 1 at 20. *Citing* http://publicsde.regie-energie.qc.ca/projets/235/DocPrj/R-3867-2013-C-ACIG-0028-Preuve-RappExp-2015_02_26.pdf at Exhibit IEc-3 in that document.

a cost causation basis, mains costs should include a customer component.[14] Witness LaConte also advocates for using a customer component of 20 percent, based on analysis presented in the last base rate proceeding.[15] Witness LaConte also rejects the 50/50 weighting in the A&E demand allocator, in favor of a load factor weighting. Mr. Knecht demonstrates that a traditional minimum system analysis based on data provided in this proceeding would result in a customer component of 65 percent, and he recommends relying on the historical zero-intercept method value of 25 percent, combined with a design day demand allocation factor.[16] Mr. Knecht also includes a simulation of the CCOSS with the 50/50 A&E approach. Witness Watkins, however, rejects both the use of a customer component for costs and the 50/50 A&E method in favor of a 50/50 peak-and-average costing method.

As Mr. Knecht explained, the Commission has approved, or at least implicitly approved, all of these methods in recent decisions involving Pennsylvania NGDCs.[17] As such, precedent provides little value for evaluating this debate.

In his direct testimony, Mr. Knecht provides a detailed explanation for why a customer component is needed to reflect the economies of scale of extending the distribution to serve larger customers relative to smaller customers, why mains costs are never sized to meet average demand, and why the zero-intercept method is a more reasonable and moderate approach to deriving a customer component for mains demand than the minimum system method.[18] These arguments will not be repeated here. The OSBA observes, however, that Mr. Knecht's CD

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[14] PGW Statement No. 5-R at 5.

[15] PICGUG Statement No. 1 at 20.

[16] OSBA Statement No. 1 at 28.

[17] OSBA Statement No. 1 at 22-24.

[18] OSBA Statement No. 1 at 25-29; OSBA Statement No. 1-R at 8, 12; OSBA Statement No. 1-SR at 6-7.

method is a moderate approach among various extremes, and it reasonably reflects the obvious that it costs less per unit of peak demand to extend the gas distribution system to serve larger customers than to serve smaller customers. The OSBA recommends that the Commission adopt Mr. Knecht's CD method for classifying and allocating mains costs in this proceeding.

The second major issue for cost allocation in this proceeding is the treatment of Rate IT "interruptible" transportation service. For allocation of base rates costs, PGW generally proposes to treat Rate IT customers as firm.[19] Under PGW's CCOSS method, current rate revenues from Rate IT fall far short of allocated costs, with a class rate of return at current rates of *negative* 3.4 percent (compared to system average of 7.7 percent).[20]

The OSBA readily acknowledges that interruptible service as provided in Rate IT imposes costs on customers in that class that are not faced by firm service customers, and that interruptible service can theoretically provide benefits to firm service ratepayers by deferring the need to expand the distribution system to meet peak loads.[21] In this proceeding, as in the past, PGW has again failed to produce any credible cost analysis demonstrating whether or not Rate IT customers provide any actual benefit to firm service customers associated with avoided costs. The only credible fact is that Rate IT customers have not been interrupted for more than 20 years.

Mr. Knecht summarized this situation in surrebuttal testimony as follows:

> Unfortunately, the Company retains its internally inconsistent positions. First, it treats Rate IT as entirely firm for cost allocation purposes, an makes no attempt to determine a dollar value associated with customer interruptibility. Second, it proposes to require the Rate IT customers to comply with the existing tariff

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[19] As a technical matter, PGW does not allocate any universal service costs to Rate IT, nor does it credit Rate IT with universal service revenues in its CCOSS. See, for example, Exhibit CEH-1 at Schedule E page 3 account 921 and Schedule E page 4 CRP Forgiveness.

[20] OSBA Statement No. 1 at 39, Table RDK-5.

[21] OSBA Statement No. 1 at 29 (footnote 32), OSBA Statement No. 1-SR at 7-8.

language regarding alternative fuel or demonstrated interruptibility requirements, despite indicating that the Company has no expectation of ever interrupting these customers.

In proposing to retain the tariff requirements for Rate IT, Witness Teme cites to the Company's review of the potential for a firm transportation service rate class provided in Exhibit FT-3. In that review, it appears that the Company's primary concern about relaxing the tariff requirements for Rate IT would be the potential migration of some larger Rate GS Industrial customers to Rate IT, and the concomitant loss of revenues. This problem arises primarily due to pricing Rate IT far below costs, and exempting it from the various riders that apply to GS-Industrial customers, most obviously the USEC surcharge. The obvious solution to this problem would be to close Rate IT to new entrants, grandfather the current customers for eligibility in the class, and gradually transition the Rate IT tariff charges to a firm service rate category.

However, for this proceeding, we are (once again) left with the problem that there is no reasonable way to determine either the value (if any) of the interruptibility of Rate IT customers or some reasonable compensation to those customers for the cost they incur in meeting the tariff requirements.

I can therefore only offer the numbers. In my updated CCOSS analysis in RDK WPSR1, the base rate cost of providing firm service to Rate IT is lies between $23.1 and $34.0 million, before any assignment of USEC costs that apply to other firm service customers. At my proposed rates, total revenues from Rate IT would be $16.5 million, implying a revenue shortfall of $6.6 to $17.5 million per year (depending on the CCOSS used). The Commission will need to apply its judgment as to whether rate discounts of this magnitude are sufficient to compensate the Rate IT customers for their interruptibility. For the purposes of this testimony, I simply deem the discounts to be sufficient, recognizing that the Company continues to fail to provide the necessary evidence and that there have been no interruptions for nearly 20 years.[22]
OSBA Statement No. 1-SR at 7-9.

The OSBA respectfully recommends that Mr. Knecht's approach be adopted in this proceeding. The OSBA further recommends that the Commission require PGW to undertake a serious evaluation as to the specific magnitude of avoided cost benefits associated with Rate IT customers. If no such benefits are identified, PGW should begin transitioning these customers to firm service.

[22] OSBA Statement No. 1-SR at 7-9.

The last major issue of contention regarding cost allocation is the assignment of universal service costs to the various rate classes. The OSBA has an economic interest in PGW's universal service programs because most non-residential customers are required (at this time) to pay the Universal Service and Energy Conservation Surcharge ("USEC").[23] As Mr. Knecht testified, from a cost causation standpoint, universal service costs should only be assigned to the classes who are eligible for the benefits, namely residential customers.[24] This conclusion was echoed by PICGUG witness LaConte and GFCP/VEPI Witness Crist.[25] The assignment of universal service costs to some non-residential classes predates PGW coming under the Commission's jurisdiction in 2000.

It is not reasonable to recover the costs of these programs from non-residential customers because non-residential customers are ineligible to participate in the universal service programs.[26]

As set forth more fully in the testimony of Mr. Knecht, PGW is the only natural gas distribution company ("NGDC") for which non-residential customers are required to pay universal service costs.[27] Furthermore, the Commission has specifically declined to allocate universal service costs to non-residential customers in numerous proceedings and has adopted a policy that the cost of universal service programs should be borne entirely by the residential

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[23] OSBA Statement No. 1 at 33.

[24] OSBA Statement No. 1 at 32

[25] PICGUG Statement No. 1R at 10, Vicinity Statement No. 1 at 25-26.

[26] OSBA Statement No. 1 at 32.

[27] OSBA Statement No. 1 at 35.

customers of NGDCs and of electric distribution companies ("EDCs").[28] Furthermore, the Commission's policy of not allocating universal service costs to non-residential customers was appealed to the Commonwealth Court and affirmed.[29]

The OSBA has participated in each of PGW's last two base rate proceedings, the emergency rate relief proceeding in 2007 (Docket Nos. R-00061931), and the follow-up base rates proceeding in 2009 (R-2009-2139884). The OSBA, through the testimony on Mr. Knecht, advanced a similar proposal in both of those proceedings. In the 2007 base rates case, the Administrative Law Judges concluded:

> The arguments and authorities cited by OSBA and PICGUG are reasonable. However, PGW, OCA and Action Alliance also have valid arguments. It is clear that the Commission is moving to have the costs of universal service programs assigned to the residential customers. In the previous proceedings, a cost of service study was not available. Therefore, the issue can be addressed in this proceeding. Nevertheless, based on the amount of the increase and the revenue allocation that we are proposing, OSBA's proposal would be overwhelming to the residential customers. Although that the entire cost would not be reassigned at one time, when we look at the final year, the increase of 3.8% in addition to the current base rate increase and any increases in the GCR result in rate shock. This is not gradualism. It should be noted that we are

[28] The Commission has specifically declined to allocate universal service costs to non-residential customers in numerous gas proceedings, including the following: (a) Valley Energy, Inc. at Docket No. R-00049345; (b) Equitable Gas Company at Docket No. P-00052192; and (c) PPL Gas Utilities Corporation at Docket No. R-00061398. The Commission has also declined to allocate universal service costs to non-residential customers in numerous electric proceedings, including the following: (a) PPL Electric Utilities Corporation at Docket No. R-00049255, and (b) Metropolitan Edison Company and Pennsylvania Electric Company at Docket Nos. R-00061366 and R-00061367. The OCA appealed the Commission's decision in the Metropolitan Edison Company and Pennsylvania Electric Company case to the Commonwealth Court. The Commonwealth Court affirmed the Commission's decision with regard to allocating universal service costs solely to the residential class. *Popowsky v. Pennsylvania Public Utility Commission*, 960 A. 2d 189 (Pa. Cmwlth. 2008). Furthermore, in the *Customer Assistance Programs: Funding Levels and Cost Recovery Mechanisms Final Investigatory Order*, Docket No. M-00051923 (Order entered December 18, 2006), the Commission decided it will continue its current policy of allocating CAP costs only to residential customers, in that only residential customers are eligible for universal service programs. Specifically, the Commission stated: "*After careful consideration of the comments and the arguments presented, the Commission will continue its current policy of allocating CAP costs to the only customer class whose members are eligible for the program – residential customers.* ***The Commission believes that we should not initiate a policy change that could have a detrimental impact on economic development and the climate for business and jobs within the Commonwealth.***" (emphasis added).

[29] *Popowsky v. Pennsylvania Public Utility Commission*, 960 A. 2d 189 (Pa. Cmwlth. 2008).

> recommending First Dollar Relief which means that the residential customers will be assigned the majority of the rate increase. We cannot burden these customers with an increase in the universal service costs also. Consequently, we are recommending that PGW's current allocation of universal service costs be retained and OSBA's proposal be rejected.[30]

In its Order approving the 2007 base rates case, the Commission approved both the ALJs' recommendation and the ALJs' accompanying rationale:

> We will adopt the ALJs' recommendation regarding allocation of the USEC program. We agree with the ALJs' reasoning that a realignment of the costs in this proceeding would simply overburden the residential classes given that we are adopting the ALJs' recommendation regarding allocation of the $25 million increase. Because that substantial realignment goes far to bring all rate classes closer to a cost of service basis, we find that our decision on this one issue is consistent with the principles enunciated in Lloyd. As we have noted, Lloyd has not eliminated the principles of rate shock and gradualism, but it has required that we be guided primarily by cost of service. In the over-all context of this proceeding, one can hardly argue that application of the principles of gradualism and rate shock concerns to this one issue depart from Lloyd given the revenue allocation approach adopted for the primary $25 million increase.

In ruling on the USEC issue in the 2007 base rates case, the Commission agreed that cost causation is an appropriate measure for universal service, but rejected the OSBA's proposal on the basis of rate shock. The 2010 base rates case was resolved by settlement. As part of the settlement in the 2010 case, the OSBA agreed not to pursue the argument any further in that proceeding.[31] However, the Settlement provides that the withdrawal of any argument by a party to the Settlement (*e.g.*, the OSBA's argument against non-residential customers paying for

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[30] Recommended Decision, Docket No. R-00061931, July 24, 2007, pages 80-81.

[31] *See* Settlement at Paragraph 38, R-2009-2139884.

universal service) is without prejudice and allows the OSBA to raise its argument about the allocation of universal service costs in a future proceeding.[32]

The OSBA is not proposing to modify the Commission's long-standing policy of allocating universal service costs to non-residential customers in this proceeding but reserves the right to raise the issue in a future case.

Mr. Knecht analysis, presented in Table RDK-4 reflects the inequity of the policy. As noted by Mr. Knecht, this issue is further complicated by the transition of Vicinity from contractually bound to some form of regular rate.

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[32] *Id.*

Table RDK-4 PGW Universal Service Implied Tax Rates: Current Rates		
	Cost $000	**Percent of Non-GCR Revenues**
Residential	$61,938	15.7%
Commercial	$18,351	25.6%
Industrial	$1,503	26.3%
Municipal	$1,703	29.8%
PHA-GS	$330	17.7%
PHA-Rate 8	$745	24.6%
NGV	$36	91.4%
Interruptible	$0	0.0%
GTS/GFCP	$0	0.0%
Total	**$84,606**	**17.0%**
Source: RDK WP2.		

OSBA Statement No. 1 at 33.

While PGW's filed CCOSS and its May 5 CCOSS don't assign any universal service costs to Vicinity, PGW Statement No. 6-SD (May 5th filing) indicates that Rate GS-XLT will be subject to all current surcharges-including USEC.[33] While Mr. Knecht noted the Company proposed to include the proposed Rate GS-XLT in the volumetric assignment of universal service costs, the Company's proposal would result in a $19.2 million dollar USEC charge for Rate GS-XLT. Given the magnitude of the charge, and while that may not therefore be a serious proposal, as Mr. Knecht further testified, there is no reason that GS-XLT should be entirely exempt from some reasonable responsibility for universal service costs.[34]

[33] OSBA Statement No. 1 at 33

[34] OSBA Statement No 1 at 34.

To that end, as set forth in Mr. Knecht's direct testimony the OSBA proposes that universal service costs be allocated and recovered on a percentage of base rates basis, similar to the DSIC mechanism.[35]

At the end of the day, the results of Mr. Knecht's approach to cost allocation are presented in Table RDK-5 which provides the following comparison of class rates of return at current rates.

Table RDK-5 Comparison of CCOSS Results Class Rate of Return at Current Rates			
	PGW Filed CCOSS	**RDK CCOSS A&E**	**RDK CCOSS CD**
Residential	9.5%	9.4%	8.3%
Commercial	8.2%	6.3%	7.9%
Industrial	8.7%	8.1%	10.8%
Municipal	4.6%	2.3%	3.3%
PHA-GS	7.3%	8.5%	7.8%
PHA-Rate 8	8.8%	8.5%	10.4%
NGV	-1.5%	-1.1%	3.4%
IT	-3.4%	-3.4%	-0.5%
GS-XLT	-16.6	-14.0%	-14.0%
Total	**7.7%**	**7.7%**	**7.7%**
Sources: RDK WP2, RDK WP4, RDK WP5			

OSBA Statement No. 1 at 39

As Mr. Knecht testified:

> The results of these simulations reflect a reasonably similar pattern. The Residential, Industrial, and Rate 8 classes produce rates of return above system average in all three CCOSSs. Further, The Commercial and PHA classes exhibit rates of return modestly above and below system average. The Municipal, NGV, IT and GS-XLT class returns are all consistently well below system average.

Note also that the differences between the RDK A&E and RDK CD methods are relatively modest, and that incorporating a moderate customer component to mains

[35] OSBA Statement No, 1 at 34

> cost allocation does not result in an unduly large shift in costs for the Rate IT or other non-residential rate classes.

OSBA Statement No. 1 at 40.

The OSBA respectfully submits that Mr. Knecht's cost allocation analysis provides reasonable guidance for revenue allocation and rate design in this proceeding.

2. Revenue Allocation

"Revenue allocation is the assignment of the dollar net increase or decrease to each of the Company's rate classes in a base rates proceeding. From a cost recovery standpoint, revenue allocation addresses *inter-class* cross-subsidization issues while rate design addresses *intra-class* cross-subsidization issues."[36] The seminal case on revenue allocation is the *Lloyd* decision, where the Commonwealth Court held that the cost of service was the "polestar" criterion for revenue allocation in a rate proceeding.[37]

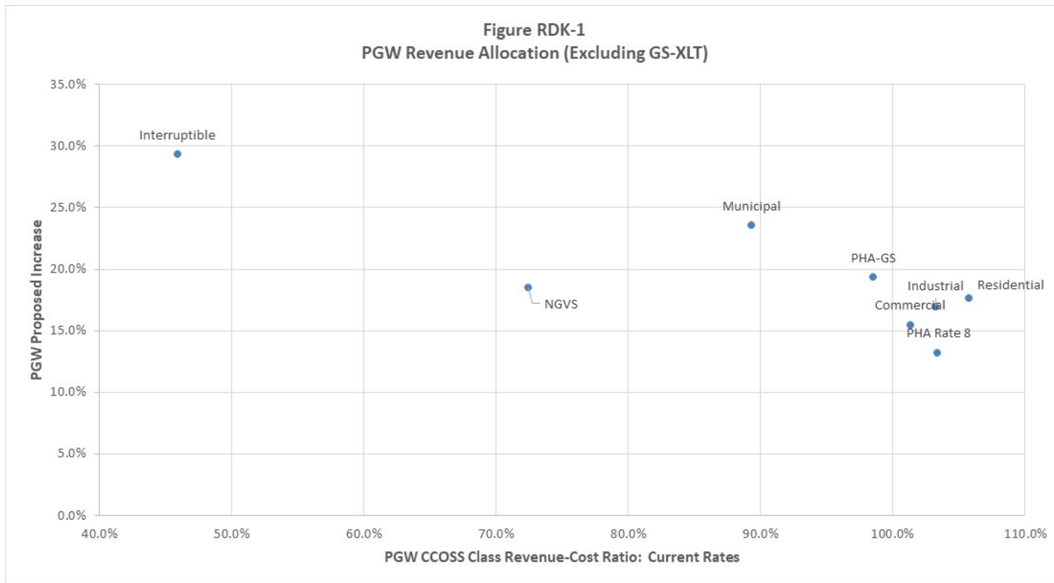
Mr. Knecht discusses the details of revenue allocation in his Direct Testimony. *See* OSBA Statement No. 1 at 40-41. Ultimately, Mr. Knecht summarized PGW's revenue allocation as follows:

> The Company's revenue allocation appears to be at least loosely based on the results of its CCOSS simulation. It assigns the largest percentage increase, nearly 30 percent, to the Rate IT class, reflecting that class' low revenue-cost ratio. This represents about 1.5 times the system average base rate increase, which may be PGW's upper bound for revenue allocation.
>
> Figure RDK-1 below shows the Company's proposed percentage rate increases plotted against the class revenue-cost ratio at present rates. In general, a cost-based revenue allocation should show a declining pattern, with classes that have higher revenue-cost ratios see smaller rate increases. In preparing this graph, I used the total class increases inclusive of USEC and DSIC impacts, rather than the Company's narrower definition of the rate increase. This also makes this

[36] OSBA Statement No. 1, at 40

[37] *Lloyd v. Pa. PUC*, 904 A.2d 1010 (Pa. Cmwlth. 2006).

comparison comparable to my own revenue allocation proposals that reflect changes to the USEC cost recovery.



After reviewing PGW's proposed revenue allocation, Mr. Knecht concluded as follows:

> As shown, the Company's proposal is directionally consistent with its CCOSS results, but the relative increases for the regular rate classes are bunched together with little differentiation reflecting cost of service.

OSBA Statement No. 1, at 42.

To address the issues of uncertainty regarding a cost allocation methodology and the shortcomings in PGW's CCOSS results, Mr. Knecht developed revenue allocation proposals based on his two CCOSS simulations. He applied the following methodology to both:

- Base rates for the proposed GS-XLT class were set equal to allocated cost, resulting in an increase of about $950,000 for both scenarios. I did not apply a rate gradualism constraint to this class because the per-mcf costs are minimal (base rates increase from about 9 cents per mcf to 13 cents per mcf).

- Rate increases for the rate classes with low revenue-cost ratios were assigned a rate increase at 1.5 times the system average, which I use as an upper bound for the rate gradualism constraint. In both CCOSS simulations, these classes include Municipal and IT, and for the CD COSS, the NGV class.

- Rate increases for classes with revenue-cost ratios near unity are assigned increases of 1.0 times the system average. For the A&E CCOSS, this includes the Industrial, PHA and Rate 8 classes. For the CD CCOSS, this includes Commercial and PHA classes.

- Rate increases for classes moderately below unity were assigned increases at 1.25 times system average. This applied to the Commercial class in the A&E CCOSS, and the NGV class in the CD CCOSS.

- Rate increases for classes moderately above unity were assigned increases at 0.75 times system average. This applied to the Industrial and Rate 8 classes in the CD CCOSS.

- Residential class increases were derived by difference and checked for realism. This approach resulted in rate increases for the Residential class at 16.2 percent and 17.1 percent for the A&E and CD CCOSSs respectively, both a little below the Company's proposed increase for that class and below the system average increase.

- Using an iterative algorithm, USEC charges are derived for each class based on 17.9 percent of base rate revenues (inclusive of OPEB surcharge revenues). For the GS-XLT class, the USEC charge is added to the cost-based base rate charges to produce the overall rate increase. For the other rate classes, the base rate and DSIC charges were derived from the total rate increase (from the multiples listed above) less the rate changes associated with the modified USEC charges.[38]

Mr. Knecht summarized the Company's and his revenue allocation proposals in the following table:

Table RDK-6
Comparison Revenue Allocation Proposals

	PGW Proposal		RDK A&E		RDK CD	
	$000	%	$000	%	$000	%
Residential	80,515	17.6%	73,830	16.2%	78,264	17.1%
Commercial	13,910	15.4%	19,752	21.9%	15,802	17.5%
Industrial	1,217	16.9%	1,265	17.5%	949	13.2%
Municipal	1,743	23.5%	1,951	26.3%	1,951	26.3%
PHA-GS	424	19.3%	385	17.5%	385	17.5%
PHA-Rate 8	497	13.2%	662	17.5%	496	13.2%
NGV	14	18.4%	20	26.3%	16	21.9%

[38] The calculations supporting this algorithm are provided in the RDK WP4 and RDK WP5 workpapers.

Interruptible	3,743	29.3%	3,362	26.3%	3,362	26.3%
GS-XLT	0	0.0%	950	84.1%	950	84.1%
Total	102,064	17.5%	102,177	17.6%	102,175	17.6%
Sources: RDK WP2, RDK WP4, RDK WP5						

OSBA Statement No. 1 at 44.

It is important to recognize that Mr. Knecht's proposal reflects the results both of the re-assignment of USEC costs and the allocation of the base rate increase. As Mr. Knecht explained, this is a "package deal," which balances the impacts of both types of changes with consideration of the principle of rate gradualism.[39] The specific impacts on the USEC, DSIC and base rates charges are all detailed in Mr. Knecht's workpapers, labeled RDK WP4 and RDK WP5.

In that context, however, Mr. Knecht's analysis indicates that the differences across the various rate classes are relatively modest and that these alternatives provide a reasonable range for revenue allocation in this proceeding.[40]

As a final note, the OSBA observes that Mr. Knecht's allocation of rate increase to Rate GS-XLT is relatively modest compared to PGW's various proposals. This results because it is OSBA's position that the Alternative Receipt Service to GFCP/VEPI is a GCR issue, and that revenues associated with that service should be credited to the customers who pay for the capacity used to provide the service, namely the GCR customers. That issue is more fully addressed in Section D, however it should be noted here that the ARS revenues will provide considerable value to smaller customer ratepayers, but it they are not reflected in base rates.

[39] OSBA Statement No. 1-SR at 15.

[40] OSBA Statement No. 1 at 44.

3. Rate Design for GS-Commercial Class

Mr. Knecht, in his Direct Testimony, provided a more detailed summary of PGW's proposed rate design for the GS-Commercial class.[41] As noted in his testimony, the only items that PGW proposes to change are the customer charge and the delivery charge, as well as an adjustment to the merchant function charge ("MFC") to reflect the updated historical average uncollectible rates.[42]

PGW's approach will result in relatively larger rate increases for small commercial customers compared to the larger commercial customers that the OSBA represents. As Mr. Knecht noted in his testimony, determining the correct cost to use for Commercial customers is not simple due, in part, to the wide range of sizes in the customer class. In sum, using an average customer-related cost is not reasonable as it forces the small customers to pay for the more expensive meters and services required for the larger customers.[43]

> In order to overcome the inadequacies of PGW's approach, Mr. Knecht suggests establishing different customer charges within the class, differentiated by size, in order to mitigate the intra-class cross subsidization.[44] As PGW did not propose such an approach, Mr. Knecht explained why it was appropriate to set the customer charge for the class based on the customer-related costs for serving small customers within the class. To do so, Mr. Knecht observed that customer costs for the small Commercial customers are similar in to those for residential customers. Mr. Knecht therefore relied on the customer costs for the residential class for evaluating the Company's customer charge proposal, making an adjustment for uncollectibles. The results of Mr. Knecht's analysis, reflect those costs at the full revenue requirement of approximately $31 to $35 per month.[45]

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[41] OSBA Statement No. 1 at 47.

[42] OSBA Statement No. 1 at 48.

[43] OSBA Statement No. 1 at 48

[44] OSBA Statement No. 1 at 48

[45] OSBA Statement No. 1 at 49. *See also*, RDK WP4 for a detailed comparison.

a. Customer Charge

Mr. Knecht presented a comparison of the customer charges for other Pennsylvania natural gas distribution companies for commercial service in his direct testimony. Table RDK-8 (See page 49 of OSBA Statement No. 1) reflect that PGW's customer charge, although currently at the low end of the range, would move it to the other end of the range. In light of the customer cost information in RDK WP4, and recognizing PGW's status as one of the highest cost NGDCs in the Commonwealth, Mr, Knecht concluded that the Company's proposed increase for GS is at the upper edge of what would be reasonable, if the entire rate increase were to be granted.

The OSBA therefore recommends that, if the overall requirement is scaled back, so too should the proposed increase to the GS Commercial customer charge.

b. Other Tariff Changes

The OSBA did not address these issues its Main Brief.

D. GFCP/VEPI – Class GS-XLT

The Briefing Order for this proceeding requires that parties address the following issues related to service to GFCP/VEPI:

> a) the proper rate class for Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc., including, if necessary, whether a special rate class is appropriate,
>
> b) the appropriate methodology to determine Philadelphia Gas Works' actual cost of service for Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.
>
> c) whether and, if so, to what extent Philadelphia Gas Works' transportation service to Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc., utilizes PGW's low pressure distribution system, and if so, what impact does such use have upon the

> Philadelphia Gas Work's actual cost of service and the resulting "just and reasonable" rate for Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.
>
> d) whether Philadelphia Gas Works should be held to its prior position in base rate proceedings that Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc., do not utilize Philadelphia Gas Works' distribution system.

As Mr. Knecht testified, the general issues of allocating costs to GFCP/VEPI have been extensively reviewed at Docket Nos. C-2021-3029259 and R-2023-3038069. The Commission has deferred that problem to this proceeding, without providing any guidance regarding a general approach for developing rates for this service.

The OSBA was an active party in the GFCP/VEPI dockets referenced above. Mr. Knecht's detailed testimony from Docket Nos. C-2021-3029259 and R-2023-3038069 is attached to his Direct Testimony in these proceedings as Exhibit RDK-4.[46]

Mr. Knecht summarized his views on developing rates for GFCP/VEPI as follows:

> - I disagree with the Company's proposed costing treatment of ARS as if it involved delivering gas from its receipt from the Tetco Skippack Lateral to the cogeneration plant. Except in rare circumstances, gas is delivered to GFCP/VEPI via dedicated mains from the Philadelphia Lateral. PGW does not size its distribution system to provide gas flows to GFCP/VEPI across its system. The ARS is a gas supply arrangement, and it should be priced as such. The price for the ARS service should reflect the relative value of GFCP/VEPI obtaining service through the Philadelphia Lateral compared to its cost of delivering to the Skippack Lateral. The revenues earned by PGW for ARS should be credited to GCR customers, who pay for the capacity on the Philadelphia Lateral and who could benefit from release of that capacity if it were not serving GFCP/VEPI.[47]

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[46] OSBA Statement No. 1 at 37.

[47] It could be reasonably argued that 25 percent of the revenues associated with the ARS swap arrangement should be credited to base rates, pursuant to the 75/25 GCR sharing mechanism for capacity release/off-system sales margins. I have not attempted to reflect this consideration in my cost allocation analysis, although the Commission should determine whether it should reduce the Company's revenue requirement in this proceeding for that credit. Based on the $6.1 million offered by GFCP/VEPI in the GCR proceeding, a 25 percent credit would imply a reduction in the base rate revenue requirement of at least $1.5 million.

- The value of the Philadelphia Lateral capacity that PGW has implicitly been providing to GFCP/VEPI substantially exceeds the amounts paid by the customer, to the detriment of PGW's GCR ratepayers.

- PGW has not demonstrated a need for the capacity on the Philadelphia Lateral that is used to serve GFCP/VEPI, as it has not exercised its rights to constrain the ARS service over the 25-year life of the contract between the parties.

- In general, many Pennsylvania NGDCs use either direct assignment of costs or negotiated rates to price delivery service to large industrial customers.

- PGW's poor record-keeping makes it impossible to identify the specific costs associated with the facilities used to provide service to GFCP/VEPI, or to determine how much of those costs has already been contributed by GFCP/VEPI.[48] PGW reports a net book value for the dedicated facilities of $1.209 million.[49]

- Service to GFCP/VEPI facilities other than service to the Grays Ferry cogen plant through the dedicated mains should be provided under regular PGW tariffs.

In his proposal to address the incorporation of GFCP/VEPI as a non-contract customer, Mr. Knecht provided the following approach for both cost allocation and revenue allocation in his CCOSS in RDK WP4 and WP5:

- Proposed base rate revenues are set to class allocated base rates costs.
- Design day demand for the Rate GS-XLT class is set at the 56,000 Dth/day requirement specified by GFCP/VEPI in the complaint proceeding.
- No mains plant or meters plant costs are assigned to the class, reflecting the likelihood that GFCP/VEPI's predecessors paid for the facilities serving the plant.
- System metering/regulating plant is allocated to GS-XLT using the peak demand allocator consistent with the Company's approach for other class. However, if it is demonstrated that GFCP/VEPI do not rely on any such Company equipment (or if it paid for it), this allocation should be modified.
- The allocator for mains O&M costs is modified to include a provision for the $1.21 million net book value of the mains assets serving GFCP/VEPI, to reflect PGW's obligation to maintain that plant;
- ECR costs and revenues are set to zero;

[48] VIC-I-1, VIC-I-5.

[49] VIC-I-7.

- OPEB surcharge revenues are set to zero;
- Within the CCOSS, universal service costs and revenues cancel out. The USEC charge for Rate GS-XLT is derived in the revenue allocation section below, following the percent of base rates method discussed above.

OSBA Statement No, 1 at 38-39.

For those reasons, the OSBA respectfully responds to the Briefing Order regarding GFCP/VEPI as follows:

a. The OSBA agrees with PGW that a separate rate class for GFCP/VEPI is appropriate, given the size of the customer and the nature of distribution service (i.e., through dedicated facilities paid-for by GFCP/VEPI).

b. Base rates tariff charges should reasonably reflect the cost of providing service to GFCP/VEPI, excluding any mains plant costs, but including metering, appropriate system regulator costs, O&M costs associated with the dedicated facilities, and A&G costs.

Rate GS-XLT should contribute to USEC costs, based on the percentage of base rates charges proposed by OSBA. Rate GS-XLT should not be subject to the OPEB rider, as the OPEB costs are reflected in the cost basis for Rate GS-XLT base rates charges. Rate GS-XLT should not be subject to the ECR rider, unless and until PGW incurs EE&C costs associated with Rate GS-XLT customers. Re the DSIC, the OSBA concludes that it would be preferable for Rate GS-XLT to retain responsibility for any costs associated with major capital projects on the dedicated mains serving that facility.

ARS service is a gas supply arrangement ("swap"), in which GFCP/VEPI is granted access to valuable upstream capacity on Tetco's "Philadelphia Lateral" that is paid for by GCR customers. The OSBA generally agrees with PGW that the charge for ARS should reflect the market value of the upstream capacity, and the OSBA respectfully submits that the value for that capacity should be determined by putting that capacity out for competitive bid under an asset

management arrangement. Moreover, because this transaction involves upstream gas supply capacity, the revenues associated with this service should be credited to the GCR and not base rates. The OSBA would not object to including this capacity in the GCR "sharing" mechanism, such that 75 percent of the revenues are credited to the GCR and 25 percent are credited to base rates.

c. Except in extraordinary circumstances, GFCP/VEPI does not rely on PGW's low-pressure distribution system, and should not be allocated costs associated with that system. For those extraordinary circumstances, GFCP/VEPI should take service under regular tariff rates.

d. PGW's position in previous base rates cases, namely that GFCP/VEPI (mostly) does not rely on PGW's distribution system, except for the dedicated lines for which GFCP/VEPI contributed the capital, was correct. PGW's assertions in the GFCP/VEPI complaint proceeding, the GCR, and the initial filing in this proceeding that GFCP/VEPI relied on the distribution system to deliver ARS volumes was nonsense and should be ignored.

E. Customer Service Issues

The OSBA will not address these issues its Main Brief.

F. Low-Income Customer Service Issues

Other than addressing the recovery of USEC costs from all rate classes, the OSBA will not address these issues in its Main Brief.

G. Pipeline Replacement/Alternatives

The OSBA will not address these issues its Main Brief.

H. Miscellaneous Issues

The OSBA will not address any miscellaneous issues its Main Brief.

V. **CONCLUSION**

Wherefore, the OSBA respectfully requests that the ALJs and the Commission adopt the OSBA's customer-demand ("CD") method for classifying and allocating mains costs in adopted his proceeding.

Rate IT should be treated as firm service customers for cost allocation purposes in this proceeding. However, PGW is directed to undertake a detailed evaluation of any avoided costs associated with the interruptibility of Rate IT customers for the next base rates case.

Furthermore, if the overall revenue requirement is scaled back, so too should the proposed increase to the GS Commercial customer charge.

Respectfully Submitted,

/s/ Sharon E. Webb

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Dated: July 27, 2023

Appendix A

Findings of Fact

1) On February 27, 2023, Philadelphia Gas Works ("PGW" or "Company") filed Supplement No. 159 to Philadelphia Gas Work's Gas Service Tariff –Pa. P.U.C. No. 2, and proposed Supplement No. 105 to Philadelphia Gas Works Supplier Tariff-Pa. P.U.C. No 1 ("Supplement No. 105") with the Pennsylvania Public Utility Commission ("Commission"). The proposed Tariffs, if approved by the Commission, would increase the retail distribution rates of Philadelphia Gas Works ("PGW" or "Company") by $85.5 million per year before the effects on universal service charges and distribution system improvement charges are recognized. In addition to the rate filing, PGW filed a Petition for Waiver seeking a waiver of the application of the statutory definition of the fully projected future test year ("FPFTY") to permit PGW to use a FPFTY beginning September 1, 2023 in this proceeding.

2) Rather than the claimed $85.2 million, the Company's proposals in this proceeding, including the effects of universal service and distribution system improvement charges, will result in an increase of $101.3 million.[1]

3) On March 9, 2023, the Office of Small Business Advocate ("OSBA") filed a formal Complaint in opposition to Supplement Nos. 159 and 105.

4) On May 5, 2023, pursuant to a Commission order at Docket No. C-2021-3029259, the Company submitted supplemental direct testimony and exhibits regarding the proposed rates, rules and regulations to govern gas service provided to Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc. ("GFCP/VEPI"). These materials included a tariff page for a proposed Rate GS-XLT under which service would be provided to GFCP/VEPI.

5.) Base rates tariff charges should reasonably reflect the cost of providing service to GFCP/VEPI, excluding any mains plant costs, but including metering, appropriate system regulation, O&M costs associated with the dedicated facilities, and A&G costs.

6.) Rate GS-XLT should contribute to USEC costs, based on the percentage of base rates charges proposed by the OSBA.

7.) PGW proposes to use the 50/50 A&E method for mains costs allocation in this proceeding, consistent with Commission precedent.

5) Three of the four cost allocation experts in this proceeding opine that PGW's approach is not consistent with cost causation.

[1] OSBA Statement No. 1, Table RDK-1.

6) In acknowledging the Commission precedent and PGW’s practice since 2007, OSBA’s expert developed two different cost of service studies, one using PGW’s A&E method, and one using a customer-demand (“CD”) method.

7) The assignment of mains costs to the Rate IT interruptible service class is a contentious cost allocation issue in this proceeding.

8) PGW proposes to treat these customers as firm, for the very credible reason that there have been no interruptions for nearly 20 years.

9) Consistent with its past practice, PGW has again made no effort to undertake an evaluation of any actual benefit provided by the interruptibility of Rate IT customers.

Appendix B

Conclusions of Law

1) Section 1301 of the Public Utility Code, 66 Pa. C.S. § 1301, provides that "every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the commission."

2) The burden of proof to establish the justness and reasonableness of every element of the utility's rate increase rests solely upon the public utility. 66 Pa. C.S. § 315(a). "It is well-established that the evidence adduced by a utility to meet this burden must be substantial." *Lower Frederick Township. v. Pa. PUC*, 409 A.2d 505, 507 (Pa. Cmwlth. 1980).

3) Although the burden of proof remains with the public utility throughout the rate proceeding, when a party proposes an adjustment to a ratemaking claim of a utility, the proposing party bears the burden of presenting some evidence or analysis tending to demonstrate the reasonableness of the adjustment. *Pa. PUC v. Aqua Pennsylvania, Inc.*, Docket No. R-00072711 (Order entered July 17, 2008). "Section 315(a) of the Code, 66 Pa. C.S. § 315(a), applies since this is a proceeding on Commission Motion. However, after the utility establishes a prima facie case, the burden of going forward or the burden of persuasion shifts to the other parties to rebut the prima facie case." *Pa. PUC v. Philadelphia Gas Works*, Docket No. R-00061931 (Order entered September 28, 2007), at 12.

4) Furthermore, Section 523 of the Public Utility Code, 66 Pa. C.S. § 523, requires the Commission to "consider . . . the efficiency, effectiveness and adequacy of service of each utility when determining just and reasonable rates." In exchange for customers paying rates for service, which include the cost of utility plant in service and a rate of return, a public utility is obligated to provide safe, adequate, and reasonable service. "[I]n exchange for the utility's provision of safe, adequate and reasonable service, the ratepayers are obligated to pay rates which cover the cost of service which includes reasonable operation and maintenance expenses, depreciation, taxes and a fair rate of return for the utility's investors . . . In return for providing safe and adequate service, the utility is entitled to recover, through rates, these enumerated costs." *Pa. PUC v. Pennsylvania Gas & Water Co.*, 61 Pa. PUC 409 (1986), at 415-16. *See also* 66 Pa. C.S. § 1501. As a result, the legislature has given the Commission discretionary authority to deny a proposed rate increase, in whole or in part, if the Commission finds "that the service rendered by the public utility is inadequate." 66 Pa. C.S. § 526(a).

5) PGW's mains cost allocation was last litigated in 2007 at Docket No. R-00061931. (Order entered September 8, 2007, at 80).

Appendix C

Proposed Ordering Paragraphs

1) The Office of Small Business's CD method for classifying and allocating mains costs in this proceeding.

2) The Office of Small Business's proposed customer class revenue allocation is adopted for purposes of this proceeding.

3) A proportional scale back of the Office of Small Business's revenue allocation is adopted for the allocation of customer class revenue increases at the reduced overall revenue increase.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	**R-2023-3037933**
Office of Consumer Advocate	:	**C-2023-3038846**
Office of Small Business Advocate	:	**C-2023-3038885**
Philadelphia Industrial And Commercial Gas User Group	:	**C-2023-3039059**
Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.	:	**C-2023-3038727**
James M. Williford	:	**C-2023-3039130**
	:	
v.	:	
	:	
Philadelphia Gas Works	:	
Grays Ferry Cogeneration Partnership and Vicinity Energy Philadelphia, Inc.	:	
	:	
v.	:	**C-2021-3029259**
	:	
Philadelphia Gas Works	:	

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been served via email (*unless other noted below*) upon the following persons, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

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