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March 1, 2010

VIA ELECTRONIC FILING AND UNITED STATES MAIL

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building, 2nd Floor
400 North Street
Harrisburg, PA 17120

**Re: Petition of Duquesne Light Company for Approval of its
Smart Meter Procurement and Installation Plan
Docket No: M-2009-2123948**

Dear Secretary McNulty:

Enclosed for filing please find Duquesne Light's Reply Exceptions, with respect to the Exceptions filed by various parties to the Initial Decision of Administrative Law Judge Robert P. Meehan, in the above-referenced proceeding.

If you have any questions, please feel free to contact me.

Sincerely yours,

A handwritten signature in black ink, appearing to be "G. Jack", written over a faint rectangular box.

Gary A. Jack
Assistant General Counsel

Enclosure

cc: Administrative Law Judge Meehan (via E-Mail and United States Mail)
Cheryl Walker Davis, Director, Office of Special Assistants (via E-Mail and United States Mail)
See Service List (via E-Mail and U.S. First Class Mail)

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

DUQUESNE LIGHT COMPANY :
Smart Meter Procurement and : Docket No. M-2009-2123948
Installation Program :

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the Reply Exceptions of Duquesne Light Company in the above-referenced proceeding has been served upon the following persons, in the manner indicated, in accordance with the requirements of § 1.54 (relating to service by a participant):

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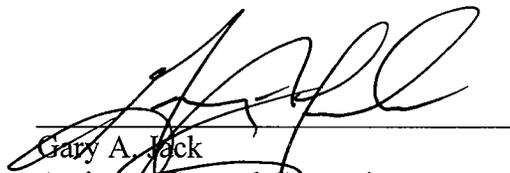
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Dated March 1, 2010

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

DUQUESNE LIGHT COMPANY	:	
Petition for Approval of Smart Meter	:	Docket No. M-2009-2123948
Procurement and Installation Plan	:	
	:	

**REPLY EXCEPTIONS OF
DUQUESNE LIGHT COMPANY**

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Dated: March 1, 2010

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I. Introduction

On January 28, 2010, the Office of Administrative Law Judge issued the Initial Decision (I.D.) of Administrative Law Judge Robert P. Meehan in this matter. In the I.D., ALJ Meehan ruled on Duquesne Light's Petition for Approval of its Smart Meter Technology Procurement and Installation Plan ("SMPI Plan"), Docket No. M-2009-2123948, and associated issues raised by various parties throughout such proceeding. Duquesne Light did not raise Exceptions in response to the I.D., as it is Duquesne Light's position that Judge Meehan did an excellent job balancing the interests of the various parties raised throughout the proceeding. Judge Meehan weighed the positions of all parties, and issued a fair and balanced initial decision. Thus, Judge Meehan's I.D. should be largely upheld by the Commission.

However, several parties disagreed with various aspects of Judge Meehan's I.D., and therefore filed Exceptions. More specifically, Exceptions were filed by the Office of Consumer Advocate ("OCA"), the Office of Small Business Advocate ("OSBA"), the Office of Trial Staff ("OTS"), Duquesne Industrial Intervenors ("DII"), the Department of Environmental Protection ("DEP"), and Citizen Power ("CP"). Duquesne Light will take this opportunity to respond to the Exceptions raised by each of these parties, and to reaffirm the fact that Judge Meehan's I.D. should stand as issued, and the Exceptions filed by all parties should be rejected, with the caveat that Duquesne Light does see merit in OSBA Exception No. 2.

II. Reply Exceptions

A. RETURN ON EQUITY

The ALJ rejected the positions set forth by the parties on this issue, and devised the following process to determine return on equity:

First, the primary consideration should be the return found reasonable in its most recent fully-litigated base rate proceeding,

provided such proceeding was concluded within three years of the effective date of the time Duquesne seeks to update its SMC. Second, this return on equity should be compared to the equity returns for electric utilities in the Quarterly Earnings Report. If the equity returns in the Quarterly Earnings Report deviate more than 0.50% above or below the equity return from the most recent fully-litigated case, the lesser of the determined or published equity return shall be used for the rate of return calculation for the SMC for the next quarter. In the event Duquesne has not had a fully-litigated rate case within three years of the effective date of a change in its SMC, then the equity returns for electric utilities in the Quarterly Earnings Report shall be used as a proxy for the equity return in the rate of return calculation of the SMC, and continue to serve as a proxy for that calculation until such time as the Commission determines a reasonable return on equity for Duquesne in a fully-litigated rate case.

I.D., p. 28.

Duquesne Light supports the ALJ's recommendation with respect to determining Return on Equity, as while it is not what was originally proposed by Duquesne Light, the multi-step process devised by the ALJ could result in a fair method of determining Return on Equity. As a result, as demonstrated below, the Exceptions filed by OCA and OTS (OCA No. 2 and OTS No. 3) should be rejected, and the ALJ's recommendations should be adopted. While this process leaves a lot of discretion and authority to FUS' determination of an appropriate standard return on equity, it has worked with water company distribution system improvement charges (DSIC), and there is no reason that it cannot work for an electric smart meter surcharge. Duquesne Light's interpretation of the ALJ's I.D. is that FUS would calculate a smart meter return based on a representative proxy group for Duquesne Light. To the extent that there is ambiguity on this issue, as other parties have suggested, Duquesne Light would ask that the Commission to clarify the FUS responsibility.

1. **Duquesne Light Reply to OCA Exception No. 2: The ALJ Properly Rejected OCA's Return On Equity Proposal, And Devised A Fair Method Of Determining Return On Equity.**

OCA's Exception No. 2 states that "The ALJ Erred In Not Accepting the OCA's Recommendation That A 10.1% Return on Equity Be Used For Computing the SMC Until Such Time as the Commission Conducts a Generic Proceeding to Establish the Procedure for Determining the Return on Equity to be Used When There Has Been No Recently Litigated Base Rate Case." OCA Exceptions, p. 6. It is Duquesne Light's position that the ALJ decided appropriately, and OCA's position was properly rejected.

With respect to OCA's arguments that the ALJ should have ordered a generic proceeding to determine a procedure for determining a proxy equity return, Duquesne Light agrees that could result in a workable solution. OCA Exceptions, p. 10. However, in the interests of time and with the knowledge of what has occurred with the water company DSIC, it would not result in a superior determination to the ALJ's recommendation. It was not in error for the ALJ to forgo initiating a proceeding ---- for which he likely does not have authority to grant ---- and establish a procedure based on an existing process such as the FUS quarterly earnings reports.

Regarding OCA's argument to utilize the 10.1% ROE from the Met-Ed and Penelec cases, Duquesne Light disagrees. The ROE for Met-Ed and Penelec is not reflective of the credit rating, the cost of equity, nor the risk profile of Duquesne Light. Duquesne Light Main Brief ("MB"), p. 28. An ROE for one utility cannot simply be applied to another utility, as many issues are involved in a public utility commission determining an ROE for a company, including customer service, operational performance, and management. Duquesne Light MB, p. 28; Duquesne Light Reply Brief ("RB"), p. 17. See also Pa. PUC v. Philadelphia Suburban Water Co., 71 Pa. PUC 593, 92-93 (Dec. 29, 1989) ("informed judgment" must be used in determining the rate of return, examining the actual circumstances of the utility). Furthermore, the Met-Ed case was decided in 2006, and the Penelec case was decided in 2007; thus, both cases are outside

of the three year period deemed reasonable by the ALJ in this matter. I.D., p. 28; Met-Ed Base Rate proceeding, Docket No. R-00061366; Penelec Base Rate proceeding, Docket No. R-00061367.

For the reasons set forth above, it is Duquesne Light's position that the I.D. with respect to determining ROE should stand, and OCA's Exception should be rejected.¹

2. Duquesne Light Reply to OTS Exception No. 3: Duquesne Light Believes That The ALJ Correctly Determined The ROE Issue, And That OTS' Objections Are Without Merit.

OTS Exception No. 3 states that "The ALJ Erroneously Modified the OTS Recommendation for Determining Duquesne's Cost of Common Equity." OTS Exceptions, p. 11. Essentially the ALJ adopted the OTS approach, but with certain modifications. OTS claims that the ALJ's approach relies on data that does not reflect current economic conditions, because it found that the most reflective return on common equity would be that from a fully-litigated base rate case concluded up to three years before an SMC update. OTS Exceptions, p. 12-13. According to OTS, three years is too long of a period in such a turbulent financial world. *Id.* at 13. Thus, OTS has requested that the Commission reject all portions of the ALJ's proposal relying on returns on common equity from fully-litigated base rate cases dating up to three years from the SMC update. *Id.* at 14. However, to the extent that the ALJ's proposal coincides with OTS' recommendation, OTS requests that it be sustained. *Id.*

Duquesne Light supports the ALJ's determination to use three years as one aspect in the determination of appropriate ROE. Duquesne Light posits that the best return on equity for a

¹ To the extent that the Commission decides to substantively examine or overturn the ALJ's recommendation on ROE, Duquesne Light has indicated that it would consider it appropriate to utilize a barometer group to determine ROE, provided that the group is made up of companies that have attributes similar to Duquesne Light, and that such process appropriately incentivizes utilities, recognizing that the smart meter plan is for the public benefit; although, the results of a fully litigated or settled case should supersede. Duquesne Light MB, p. 28; Bordo, DLC Ex. E, pps. 2-3; Duquesne Light RB, p. 17. However, given the ALJ's finding on this issue, the Commission should uphold the ALJ's recommendation.

given utility is to use a determined return on equity using company characteristics. However, in conjunction with this position, the ALJ had to pick some period of time after which the results from the base rate case proceeding would be considered stale. Three years is a reasonable period of time, and was supported by several parties in this matter in the Main Briefs. See OCA MB, p. 24; Duquesne Light MB, p. 27. See also OTS MB and RB (OTS made no specific objection to the three year period in briefs).

B. CAPITAL STRUCTURE

The ALJ rejected the proposals of OCA and OTS with respect to capital structure, and accepted Duquesne Light's proposed use of a utility's actual equity ratio, with a level of 59%, for future smart meter cost recovery proceedings. I.D., pps. 30-31. Duquesne Light supports the ALJ's finding with respect to Capital Structure, as while the 59% equity ratio does not match Duquesne Light's actual equity ratio of 67%, it is within a zone of reasonableness and supported as an upper limit. Thus, as demonstrated below the Exceptions filed by OCA and OTS (OCA No. 3 and OTS No. 4) in this regard should be rejected.

1. Duquesne Light Reply to OCA Exception No. 3: The ALJ Properly Rejected OCA's Proposal To Utilize The 51% Equity Ratio From Met-Ed And Penelec.

OCA Exception No. 3 states that "The ALJ Erred In Adopting Duquesne's Claimed Equity Ratio of 59% For Purposes of Setting the SMC." OCA Exceptions, p. 11. OCA believes that the Commission should adopt the OCA's proposal for a proxy equity ratio of 51% from the Met-Ed and Penelec base rate cases. Id. at 14.

Duquesne Light strongly disagrees with OCA that the 51% equity ratio should be applied from the Met-Ed and Penelec base rate cases. Duquesne Light MB, p. 30. It is Duquesne Light's belief that actual numbers should be used (or if not actual, as close to actual numbers as

is permissible), and that the Commission should align recovery with actual costs to the extent possible. The equity ratio from Met-Ed and Penelec is not representative of Duquesne Light's actual capital structure nor the costs that it incurs for financing. Duquesne Light MB, p. 30; Duquesne Light RB, p. 18; Bordo Rebuttal DLC Ex. E, pp. 5-6; Sears Rebuttal, OTS St. 1-R, p. 6-7; Transcript, p. 124 (OCA Witness Catlin acknowledges that applying the Med-Ed capital structure is not a perfect solution). See also Emporium Water Co. v. Pa PUC, 955 A.2d 456, 462 (Cmmw. Ct. 2008) (cost of capital should give consideration to a utility's financial structure, credit standings, interest, risks, and any other peculiar factors of the utility involved); Pa PUC v. Pennsylvania Gas and Water Co., 1993 Pa PUC LEXIS 135, 107-108 (Pa. PUC 1993) (PG&W's capital structure was deemed reasonable, as it was representative of the capital structure that PG&W would experience during the life of the requested rate relief).

OCA asserts that the 59% equity ratio is inappropriate because it is based on a settled proceeding; however, OCA fails to recognize that Duquesne Light's actual capital structure is 67%. Duquesne Light MB, p. 29. Duquesne lowered its request to a 59% equity ratio because it was reflective of an agreed capital structure and fell below a 60% equity ratio which is a level that Duquesne Light believes is reasonable. Duquesne Light RB, p. 19. Furthermore, while OCA points to Exhibits TSC-1 and TSC-2 to attempt to demonstrate that 59% equity ratio is too high, it continues to ignore the fact that equity ratios should be based on the actual numbers of the company (or close to actual)- one cannot haphazardly apply an equity ratio from one utility to another.² See Emporium Water Co., 955 A.2d at 462; Duquesne Light RB, p. 19 ("actual capital structure should be utilized for companies, as it is today with water companies with respect to the distribution system improvement charge, so long as it falls within a reasonable range. Duquesne

² TSC-1 and TSC-2 were exhibits to OCA Witness Thomas Catlin's Direct Testimony. TSC-1 addresses "Common Equity Ratios of Electric Utility Distribution Companies," and TSC-2 addresses "Common Equity Ratios of Bureau of Fixed Utility Service Electric Utility Barometer Group."

MB, p. 30; Sears Rebuttal, OTS Statement No. 1-R, p. 9”). Further, Alliant Energy, which is listed on TSC-2 representing common equity ratios of the FUS barometer group, has an equity ratio of 58.6%, which is very similar to the equity ratio approved by the ALJ for Duquesne Light. Duquesne Light MB, p. 30.

With respect to OCA’s arguments that the 59% equity ratio does not satisfy an earlier settlement, Duquesne Light agrees with the ALJ that such settlement agreement is inapplicable here as this is not a base rate proceeding. I.D., p. 31. Moreover, Duquesne Light believes that even if it were applicable, a 59% equity ratio in this context is a reasonable proxy for the actual Duquesne Light capital structure.

For the reasons set forth above, OCA’s Exception No. 3 should be denied.

2. Duquesne Light Reply to OTS Exception No. 4: The ALJ Properly Rejected OTS’ Recommendation To Use A Barometer Group To Determine The Appropriate Capital Structure.

OTS Exception No. 4 states that “The ALJ Has Erroneously Rejected the OTS Recommendation that the Commission use a Representative Capital Structure for Duquesne (And All Other EDCs) in the Recovery of Smart Meter Costs that is Based upon a Commission Established Barometer Group Used for the Quarterly Earnings Report.” OTS Exceptions, p. 15. More specifically, OTS excepts to the ALJ’s determination to utilize Duquesne Light’s 59% equity ratio for use in future smart meter cost recovery proceedings as long as its actual equity ratio exceeds that level. OTS Exceptions, p. 16.

Duquesne Light supports the ALJ’s adoption of using actual capital structure within a zone of reasonableness, as in Duquesne Light’s circumstances. Duquesne Light MB, p. 29; Pennsylvania Gas & Water Co., 1993 Pa. PUC LEXIS at 107-108. As indicated in response to OCA Exception No. 3, the actual capital structure (or as close to it as possible) of the utility

should be used, and recovery should be aligned with actual costs to the extent possible. Duquesne Light MB, p. 30; Bordo Rebuttal, DLC Ex. E, p. 3-4. Actual capital structure of Pennsylvania water companies is used by the water industry to calculate the return for additional water plant in service pursuant to the distribution service improvement charge (“DSIC”), utilizing actual capital structure. Duquesne Light MB, p. 30; OTS St. No. 1-R, pps. 6-7. A barometer group is not the appropriate way to determine capital structure, because, at least for the barometer electric companies currently relied upon by FUS, as demonstrated in DLC Cross Exam Ex. 1, the companies are not representative of Duquesne Light; the companies used are much larger, none operates in Pennsylvania; only one operates in PJM; several are in the gas distribution business; and many of the companies own electric generation. Duquesne Light MB, p. 31; Emporium Water Co., 955 A.2d at 462. Thus, OTS Exception No. 4 should be rejected, and the ALJ’s finding that “OTS made no showing that the use of a representative capital structure would result in each EDC recovering its reasonable and prudent smart meter costs, a result permitted by Section 2807(f)” should stand. OTS Exceptions, p. 15; I.D., p. 30.

C. COST ALLOCATION

Duquesne Light proposed to allocate the common costs of smart meter deployment to the customer groups based upon the number of meters in each group. Pfrommer Direct, DLC Ex. D, p. 9. This allocation was supported by OSBA and DII, and was contested by OCA and Citizen Power. OCA proposed to allocate common costs on the basis of energy and demand; an allocator for assigning the common costs should be based on the arithmetic average of the percentage shares of each group’s energy use at the meter and each group’s contribution to Duquesne’s annual single coincident peak. OCA MB, pps. 30, 36 OCA’s approach was supported by Citizen Power. Citizen Power MB, p. 8. While OSBA supported Duquesne

Light's cost allocation proposal, it offered a secondary alternative if Duquesne's allocation was not adopted: allocate the common costs in proportion to the allocation of the meter costs. OSBA MB, p. 14. The ALJ ultimately rejected the positions of Duquesne Light and OCA, and adopted the alternative position of OSBA. I.D., pps. 19-20. As detailed below, while the ALJ did not adopt Duquesne Light's original proposal, his determination was reasonable, and thus Duquesne Light would support the Commission's rejection of the exceptions of OCA, OSBA, DII and Citizen Power (OCA Exceptions Nos. 4 and 5, OSBA Exception No. 1, DII Exception No. 1 and Citizen Power Exception No. 1). However, if the Commission determines to reject the OSBA's alternative cost allocation methodology, the common cost allocation methodology proposed by Duquesne Light based upon the number of meters in each class should be adopted, and is preferable.

1. **Duquesne Light Reply to OCA Exception No. 4 and Citizen Power Exception No. 1: The ALJ Correctly Rejected OCA's Proposal With Respect To Common Cost Allocation.**

The OCA and Citizen Power except to the ALJ's rejection of OCA's proposed approach to cost allocation. OCA's Exception No. 4 states that "The ALJ Erred In Rejecting the OCA's Approach to the Allocation of Common Smart Meter Costs. OCA Exceptions, p. 14.³ The ALJ rejected OCA's cost allocation approach, based upon energy and demand, as opposed to Duquesne Light's recommendation to allocate common costs based upon the number of meters, as it is "both theoretical and speculative as to which and how customers in the various classes will "benefit" from the [Smart Meter Program] and, in [the Judge's] opinion, is not based on

³ Citizen Power filed a short document excepting to the ALJ's rejection of OCA's common cost allocation recommendation. Citizen Power Exceptions, p. 5. Citizen Power Exception No. 1 states that "The ALJ erred in rejecting [] The Office of Consumer Advocate's ("OCA") recommendation that the common costs of the SMPI Plan be allocated between the single-phase meter group and the multi-phase meter group based upon the arithmetic average of the percentage shares of each group's energy at meter and each group's contribution to Duquesne's annual single coincident peak." Citizen Power Exceptions, p. 5. Given that Citizen Power is simply supporting OCA's position, Duquesne Light will combine the responses, but will refer to OCA.

reasonable cost of service practices.” I.D. at 19. As discussed in more detail below, Duquesne Light supports the ALJ’s decision on this point, and strongly disagrees with OCA’s proposed cost allocation method. Duquesne Light MB, p. 22; Duquesne Light RB, p. 11; Pfrommer Rebuttal, DLC Ex. D-R, pps. 6-7.

OCA excepts to the ALJ’s assertion that OCA’s cost allocation methodology is not based on reasonable cost of service practices; OCA asserts that its proposal is fully consistent with cost of service principles. OCA Exceptions, p. 17. Common costs should be allocated based upon cost causation, using reasonable cost of services practices. Duquesne Light MB, p. 22; Pfrommer Rebuttal, DLC Ex. D-R, p. 6. This is appropriate because all of the functions of the common infrastructure (collect, back haul, store and maintain data) are required equally for each meter, regardless of the benefits realized or the size of the customer or meter. Id. This is further provided for by the Commission’s Implementation Order: “[t]hose costs that provide benefit across multiple classes should be allocated among the appropriate classes using reasonable cost of service practices.” Implementation Order (“I.O.”), p. 32. However, OCA’s proposal to allocate costs based upon unknown and un-quantified benefits cannot be deemed to be based upon reasonable cost of service practices.⁴ As stated by OSBA in its Main Brief, the “customer benefit” standard, as stated by OCA, can lead to a morass of conflicting interpretations regarding what the benefits of smart meter implementation are, and what benefits the customers receive. OSBA MB, p. 13. Reasonable cost of service practices would allocate these costs based upon the costs incurred due to the particular customers; not based upon benefits.⁵ This is exactly what

⁴ Citizen Power recognizes in its Exceptions that OCA’s proposal is not consistent with typical mechanical cost of service practices. Citizen Power Exceptions, p. 6.

⁵ In an attempt to demonstrate that its cost allocation theory based upon benefits is proper and is in line with cost of service principles, OCA cites to the Lloyd case, previously cited by DII and Duquesne to demonstrate that the polestar/cost of providing service principle trumps all other ratemaking principles. OCA Exceptions, p. 18; Lloyd v. Pa. PUC, 904 A.2d 1010 (Pa. Cmmw. Ct. 2006). OCA points to the Lloyd case’s discussion of the Sustainable Energy Fund (SEF) in an attempt to demonstrate that allocation based upon benefits is appropriate. OCA

Duquesne Light proposed: the costs would be recovered based upon the number of meters, because each meter, regardless of the type, relies equally on the common infrastructure to transmit data. OCA's proposal, on the other hand, is purely speculative and subjective ---- how does one measure a benefit to a customer of a smart meter with ample certainty to charge costs on that basis? It is impossible and intangible. As a result, OCA's exception on this matter must be denied.

The OCA also excepts to the ALJ's characterization of OCA's cost allocation method as "theoretical and speculative," and submits that it has provided ample evidence for its theory, and points to Duquesne Light's Department of Energy Stimulus Funding Application and data contained therein, potential customer participation in dynamic pricing programs as support for its theory, as well as calculations provided by Dr. Swan regarding the expected benefits. OCA Exceptions, p. 22-25. As alluded to above, the ALJ was quite accurate in characterizing OCA's cost allocation method as "theoretical and speculative." First, OCA's reliance on Duquesne Light's stimulus application is incorrect. The criteria utilized and examined in the federal stimulus application were different than that utilized in the SMPI plan. Duquesne Light MB, p. 24. Notably, OCA failed to take into account that the stimulus "benefits" only looked at the first year of smart meter installation, which was only 8,000 meters. *Id.* at 23. Further, OCA incorrectly presumed that the stimulus filing, and associated exhibits, would have the same implementation plan as the SMPI Plan. *Id.* at 24. However, the stimulus filing relied upon different criteria, roll-out, and a control group of meters, etc., and cannot be utilized to predict benefits (even if that were the appropriate way to allocate costs). Duquesne Light RB, p. 11.

Exceptions, pp. 18-19. However, OCA has misapplied this case. With respect to SEF, all classes were charged a flat kWh surcharge; there was no cost causation argument, nor were there customer or rate class benefits decided. The benefits discussion was limited to a determination of whether or not to continue to fund the SEF. Lloyd, 904 A.2d at 1024-1027.

Thus, the data that OCA relies on from Duquesne Light's stimulus application is inappropriate. Id. Second, OCA's reliance on customer participation in dynamic pricing programs is unfounded. Pfrommer Rebuttal, DLC Ex. D-R, pps. 6-7; Duquesne Light MB, p. 23. Duquesne's experience proves that assumptions cannot be made regarding customer behavior. Duquesne Light, MB, p. 23; Pfrommer Rebuttal, DLC Ex. D-R, ps. 6-7. Further, despite OCA's argument to the contrary, Duquesne Light believes that the benefits of smart meters have already been largely realized for Large C&I customers, and the smart meter implementation will benefit the other customer classes to a greater extent (again, however, Duquesne Light does not believe that costs should be allocated based upon benefits). OCA Exceptions, p. 25. OCA's argument that Large C&I customers will benefit more because options will be expanded to them is similarly without merit – any programs that are offered as a result of smart meters will be offered to all classes. See Duquesne Light MB, p. 23; Pfrommer Rebuttal, DLC Ex. D-R, pps. 6-7.⁶

Finally, OCA excepts to the ALJ's characterization of OCA's allocation method as resulting in "an unreasonable allocation of the common costs to the multi-phase meter group," consisting of primarily commercial and industrial customers. OCA Exceptions, p. 25; I.D. at 19. OCA states that it has demonstrated that commercial and industrial customers account for the majority of usage and demand on the Duquesne system and therefore will receive the majority of benefits. OCA Exceptions, p. 26. It is not appropriate to allocate costs based upon benefits that OCA perceives are gained by one group or another. The fair and correct way to allocate these costs is based upon the number of meters as originally proposed by Duquesne Light, and this would disperse the costs equally and fairly among both groups (single-phase or poly-phase).

⁶ Even if the appropriate method to allocate costs were based upon benefits, which it is not, there is no record evidence presented by OCA or any other party of the correct and definitive method in which benefits could be allocated among the classes. There is no information in the record that would enable Duquesne Light to allocate costs based upon benefits.

For the reasons set forth above, the ALJ was correct in rejecting OCA's proposed cost allocation methodology.

2. Duquesne Light Reply to OCA Exception No. 5, OSBA Exception No. 1 and DII Exception No. 1: Duquesne Light Has No Objection To The ALJ's Acceptance Of OSBA's Alternative Cost Allocation Methodology. However, If Rejected, The Common Cost Allocation Methodology Proposed By Duquesne Light Based Upon The Number Of Meters In Each Class Should Be Adopted.

OCA, OSBA and DII claim that the ALJ erred in accepting OSBA's alternative cost allocation proposal. OCA Exceptions, p. 26; OSBA Exceptions, p. 4; DII Exceptions, p. 5. OCA's Exception No. 5 states that "The ALJ Erred In Adopting the OSBA's Proposal for Allocating Common Smart Meter Costs." OCA Exceptions, p. 26. OSBA's Exception No. 1 states that "The ALJ erred in rejecting Duquesne's recommendation to allocate the common costs based on the number of meters in each rate class group." OSBA Exceptions, p. 3. DII's Exception No. 1 states that "The I.D. Erred in Concluding That the Company's Smart Meter Plan Common Costs Should be Allocated Among Customer Classes In the Same Proportion as the Direct Costs Allocated To Each Customer Class." DII Exceptions, p. 5.

OCA has asked the Commission to adopt its proposed cost allocation method. OCA Exceptions, pps. 27-28. Conversely, OSBA has indicated that while it is the party that proposed the alternative, its preferred method of cost allocation is Duquesne Light's initial proposal to allocate common costs based upon the number of meters, because: (1) Duquesne Light's approach was consistent with the Commission's Implementation Order, and with cost allocation practices; and (2) ALJs in two other smart meter proceedings, PECO and First Energy, have adopted the common cost allocation methodology as proposed by Duquesne Light. OSBA Exceptions, pps. 4-6. Similarly, DII has asked that the Commission adopt Duquesne Light's originally proposed method, as it fits within the Commission's long-standing precedent for

establishing rates based on a utility's cost of providing the service, as required by the Implementation Order. DII Exceptions, p. 5-6.

Duquesne Light did not file Exceptions to ALJ Meehan's I.D., and as specifically stated in its Reply Brief, Duquesne has no objection to OSBA's alternative cost allocation proposal, as it is a reasonable approach. Duquesne RB, p. 12. However, as with OSBA, Duquesne Light prefers the original cost allocation proposal made by Duquesne Light in its filing because "the number of meters drives these costs which are incurred to support the smart meter infrastructure" and because the costs per meter are consistent to make the smart meter fully functional regardless of the meter type, and this approach, as pointed out by DII, fits squarely within the Commission's precedent for establishing rates based upon a utility's cost of providing the service and meets the requirements of the Implementation Order. Duquesne Ex. D-R, Pfrommer Rebuttal, pp. 5-8; DII Exceptions, p. 6; Implementation Order, p. 32 ("[t]hose costs that provide benefit across multiple classes should be allocated among the appropriate classes using reasonable cost of service practices.")

D. INTEREST

OTS's Exceptions Nos. 1 and 2 raised with respect to the ALJ's determination on interest should be denied.

1. Duquesne Light Reply to OTS Exception No. 1: The ALJ Properly Decided Not To Adopt The OTS Recommendation For One Directional Interest Recovery On Over-Collections.

OTS Exception No. 1 states that "The ALJ Erroneously Failed to Adopt or Address the OTS Recommendation for One Directional Interest Recovery on Over-Collections." OTS Exceptions, p. 6. The ALJ found in the I.D. that "[a]ll over- and under-recovery calculations will include interest at 6%." I.D. at 21. OTS is uncertain whether its proposal was adopted, and

states that it may be presumed that the ALJ accepted OTS' proposal, given that the ALJ adopted OTS' uniform annual reconciliation schedule; however, clarification is necessary. Id. at 7.

As an initial matter, Duquesne Light believes that the I.D. speaks for itself. The I.D. specifically states that “[a]ll over- and under-recovery calculations will include interest at 6%” (emphasis added). I.D. at 21. Thus, this would appear to reject OTS' proposed one-directional treatment of interest, by recognizing that both over and under-recovery will include interest. The ALJ's acceptance of OTS' recommendation regarding the uniform annual reconciliation schedule is a different issue than interest, and was agreed to by the parties. Duquesne Light MB, p. 32. The interest issue, on the other hand, was disputed, and in Duquesne Light's opinion, was addressed by the I.D.

Further, Duquesne Light disagrees with OTS' recommended one-directional interest. Duquesne Light MB, p. 26; Pfrommer Rebuttal, DLC Ex. D-R, p. 8. Duquesne Light must raise new capital for the financing of smart meters. To the extent that Duquesne Light under-collects, it will also need to finance the shortfall in collection. If a utility has to pay interest on any over-collection, then it too should be able to collect interest on any under-collection. Interest should be symmetrical in order to be fair to both the customer and the utility.

2. **Duquesne Light Reply to OTS Exception No. 2: While Duquesne Light Does Not Object To Calculate Interest At The Residential Mortgage Rate, Duquesne Light Accepts The ALJ's Recommendation Of 6% Interest.**

OTS Exception No. 2 states that “The ALJ Erroneously Failed to Adopt or Address the OTS Recommendation to Calculate Interest at the Residential Mortgage Rate.” OTS Exceptions, p. 10.

Duquesne Light originally proposed to calculate interest at the legal rate of interest (6%). However, in its Main Brief, Duquesne Light stated in its “Issues Raised and Accepted By Duquesne” section that it would accept the OTS position by stating:

4. OTS believes that the appropriate interest rate to use for reconciliation is the monthly residential mortgage lending rate published in the PA bulletin. Sears Direct, OTS St. 1, pp. 19-20; Transcript, pps. 169-170. Duquesne does not object to this. Pfrommer Rebuttal, DLC Ex. D-R, p. 8.

Duquesne Light MB, p. 32. However, the ALJ determined that interest would be set at 6%. I.D., p. 21 (“[a]ll over- and under- recovery calculations will include interest at 6%.”). Duquesne Light does not take exception to this finding by the ALJ, and agrees that 6% is a reasonable and preferred level of interest.

E. RATE ISSUES

1. Duquesne Light Reply to OCA Exception No. 1: Duquesne Light Maintains That The Projected End-Of-Quarter Plant in Service Value Should Be Utilized.

OCA Exception No. 1 states that “For purposes of clarification, the OCA excepts to the ALJ’s determination regarding rate base valuation for quarterly SMC updates.” OCA Exceptions, p. 4.

The parties agree to quarterly updates of smart meter plant in service balances. OCA disagrees with Duquesne’s proposal to utilize the projected end-of-quarter plant in service value, as OCA maintains that this will invariably lead to over-recovery, as the end-of-quarter plant will exceed the actual plant balance over the course of the quarter and over the year. OCA Exceptions, p. 5. Thus, OCA would rather use the projected average plant balance for the quarter when setting the SMC prospectively. Id. OCA notes that the ALJ did not address this issue, and asks for clarification. Id.

Duquesne Light submits that the projected end-of quarter is appropriate. Duquesne Light is committing significant resources to complete the installation of the smart meter network, and projected end-of quarter will assist with timely recovery. Duquesne proposed quarterly updates to more closely align revenue with capital outlay and to mitigate over- or under-recovery. Duquesne disagrees with OCA's contention that end of quarter projections will lead to over-recovery. Under-recovery situations could also occur, and OCA's average method will certainly lead to under-recovery. Calculating a projected average plant in service value for a 90 day period adds an additional level of complexity and uncertainty because it will require monthly projections which are not part of the overall plan. Thus, for the reasons listed above, in the event that the Commission decides to rule on this issue, it should find that the projected plant in service should be valued at the projected end-of-quarter level.

2. Duquesne Light Reply to OSBA Exception No. 2: OSBA's Exception Has Merit And Should Be Granted, Thereby Reinstating Duquesne Light's Original Cost Recovery Methodology.

OSBA Exception No. 2 states that "The ALJ erred in applying a blanket approval to Duquesne's acceptance of proposed SMIP modifications, as such blanket approval applies to the issue of the OCA's proposal for single-phase customer rate design." OSBA Exceptions, p. 8. More specifically, OSBA is concerned with a proposed rate design change to recover some costs via a kWh charge. OCA proposed during the proceeding that common costs assigned or allocated to residential customers be recovered within the Residential rate class group via a surcharge-per-kWh charge. OCA Statement No. 2, pps. 11-13. In rebuttal testimony, while this was different than Duquesne Light's original proposal to recover SMPI costs through a reconcilable surcharge mechanism via a customer charge (all customers in each group would pay the same regardless of meter type or consumption), Duquesne Light agreed to adopt this, in a yet to be determined form,

for Residential customers. Pfrommer Rebuttal, DLC Ex. D-R, pps. 4-5. OSBA maintains that this is problematic and presents an open issue, because no party has presented evidence as to how the costs would be allocated to separate rate classes within the rate class groups (i.e. Residential and Small C&I are both contained in the single-phase meter group, yet for recovery purposes, they are treated differently). *Id.* at 10.

Upon review of OSBA's exception, Duquesne Light believes that OSBA makes a good point in this regard. While the matter could perhaps be addressed in the upcoming compliance filing, OSBA is correct that there is an open issue regarding how to separate rate classes within the rate class groups. Since the particulars of the kWh rate design were not addressed in testimony and at hearing, Duquesne Light maintains, upon further reflection, that it would be inappropriate at this point for it to be adopted. Thus, Duquesne Light believes that the most prudent course of action at this point and time is for the Commission to adopt Duquesne Light's original proposal to recover both meter and common costs via a fixed charge per meter per month, i.e. a fixed charge for each customer based on their meter type(s) (single-phase or poly-phase). Pfrommer Direct, DLC Ex. D, p. 9. Should the rate design be desired to be modified in the future, that can be proposed and reviewed by all parties and the Commission.

F. METER CAPABILITIES AND PLAN DEADLINES

The exceptions raised by DEP with respect to meter capabilities and plan deadlines (DEP Exceptions Nos. 1 and 2) should be rejected.

1. Duquesne Light Reply to DEP Exception No. 1: The ALJ Correctly Decided Not To Require Duquesne Light To Deploy Smart Meters That Include HAN At This Time.

DEP Exception No. 1 states "The ALJ Erred in Not Explicitly Requiring That Duquesne's Smart Meters Meet the Definition of "Smart Meter Technology" in Act 129 and the

Commission's Implementation Order." DEP Exceptions, p. 4. More specifically, DEP excepts to the ALJ's rejection of DEP's position that Duquesne Light should be required to deploy smart meters that enable Home Area Network ("HAN") devices or similarly capable method with open protocols. DEP Exceptions, p. 5-6. DEP asserts that this is not one of the capabilities that can be evaluated during the Grace Period for cost-effectiveness, and that this capability is necessary under the terms of Section 2807(g) of Act 129. DEP Exceptions, p. 5.

Duquesne Light believes that the ALJ's I.D. on this point should stand. DEP is attempting to interpret the plain language of Section 2807(g) to include a requirement for HAN or a similarly capable method with open protocols. However, DEP does not point to the language in Section 2807(g) that purportedly includes this requirement, nor does it provide a rationale regarding why it believes that Section 2807(g) includes this requirement; rather DEP simply states that the requirements for HAN or a similarly capable method of open protocols is a mandatory requirement of Section 2807(g), rather than the Commission's Implementation Order on smart meters.

A review of Section 2807(g) and the Implementation Order proves otherwise. Section 2807(g) makes no mention of HAN or a similarly capable method of open protocols. However, the Implementation Order specifically references this requirement. I.O., p. 23 ("the Commission will require EDC smart meters to have a capability to provide raw near real time consumption data through a HAN or similarly capable method with open protocols"). See also I.O., p. 16, 21, 22. The Implementation Order also states that "[t]he Commission recognizes that some of the requirements for smart meters outlined in Section C of this Order go beyond the minimum requirements set forth in Act 129," and thus the Commission directed EDCs to perform a cost-benefit analysis on all of the additional capabilities during the Grace Period. I.O., p. 29. The

Implementation Order further states that “[t]o the extent that an EDC or another party demonstrates that a particular Commission imposed requirement is not cost effective, the Commission will have the option of waiving a particular requirement for that EDC or all EDCs. This waiver authority does not extend to the minimum requirements delineated in 66 Pa.C.S. § 2807(g).” Id. at 31. Review of the Implementation order clearly shows that the requirement for HAN or a similarly capable method with open protocols is one of the issues discussed in Section C of the Implementation Order (i.e. the section that includes the items to be reviewed in a cost-benefit analysis and potentially waived if not cost effective), and is not specifically delineated in Section 2807(g). I.O., pps. 15-23; Section 2807(g). Thus, this issue is specifically to be examined during the Grace Period, and may be waived after the cost-benefit analysis, as correctly determined by the ALJ.

Duquesne Light intends to analyze this capability and will submit information on HAN in future filings. Duquesne Light MB, p. 6. In fact, at this point, Duquesne Light plans to purchase meters that will enable communications with HAN devices. Id. at 7. However, because HANs are located inside the home on the customer side of the meter, the device is one for customers to purchase directly or through a third party. Id. Nonetheless, given the analysis to be undertaken by Duquesne Light, this issue should not be decided at this point. The ALJ was correct in interpreting the plain language of the Commission requirements, and not requiring Duquesne Light to include this HAN capability in the smart meter deployment at this time, but rather providing Duquesne Light with the Grace Period to analyze this issue. I.D., p. 33-34. (The I.D. recognized that Duquesne Light can analyze this issue during the Grace Period cost/benefit analysis, and thus “the Commission does not need to decide this issue at this time.”).

2. Duquesne Light Reply to DEP Exception No. 2: Duquesne Light’s Proposed Dates As Set Forth In Its Plan And Briefs Should Stand.

DEP Exception No. 2 states that “The ALJ Erred in Declining to Order Duquesne to Meet the Deadlines Established in the Company’s Smart Meter Implementation Plan, Act 129 and the Implementation Order.” DEP Exceptions, p. 6. DEP further asserts that the ALJ’s conclusion of law that “[a]djustments, modifications, revisions to the proposed SMP made for the first time in briefs should be rejected”, I.D. at 36” is overly broad and not legally supported. DEP Exceptions, p. 9.

Duquesne Light disagrees that the Commission should adopt this Exception. First, the ALJ rejected DEP’s position outright because DEP failed to present any witness. See I.D., p. 35. Thus, the ALJ was not required to make a substantive decision on this matter, as DEP suggests the ALJ did, because DEP did not meet its requirements to set forth its facts and positions through witnesses.⁷ Philadelphia Suburban Water Co., 71 Pa. PUC at 129-132.⁸ This decision on behalf of the ALJ was correct and perfectly within the bounds of the law. Id.; I.D., 35. Thus, as a procedural matter, the Commission should uphold the ALJ’s ruling on this issue.

However, Duquesne Light will provide a brief response, in the event that the Commission chooses to substantively examine this Exception. Duquesne Light has every intention to meet the deadlines set forth in its plan. There is no statement or supposition in any Duquesne Light documentation ---- or in any other party’s evidence ---- that indicates that Duquesne Light will need to exceed the Grace Period, or that it will not have the infrastructure or meters installed in a

⁷ DEP claims that “the ALJ agreed with Duquesne’s argument [] in [that] “there are many matters that need analysis, evaluation and decision-making”, and that “like any large scale project with numerous interdependent components, the proposed schedule will not be exact.” Initial Decision at 34.” DEP Exceptions, p. 7. However, the DEP is simply citing the portion of the I.D. where the ALJ recited Duquesne Light’s position; the ALJ never made a finding on these issues, as DEP’s procedural deficiencies preempted such a determination.

⁸ While DEP asserts that case law on this issue is not applicable to it and distinguishable from DEP’s circumstances, DEP has pointed to no law in support of its position that it can raise issue for the first time in briefs.

timely fashion.⁹ Duquesne Light has proposed dates, which could change based upon a variety of factors, including Commission approvals, unforeseen circumstances, and other matters perhaps out of Duquesne Light's control. Duquesne Light has every intention to meet the proposed deadlines; however, if something in the process causes unforeseen delays, Duquesne Light may need to adjust its schedule.¹⁰ Duquesne Light could have proposed a particular quarter for a filing, but chose to try to be more specific by proposing exact dates as approximations of future filings. With respect to any material moving of dates for future filings, Duquesne Light would submit such issues to the parties and the Commission for review.

G. UNIFORMITY AMONG EDCS

OTS has asserted a general exception, urging the Commission "to recognize the value of ruling uniformly on each EDC's submitted SMT plan." OTS Exceptions, p. 6. OTS has urged the Commission to review all EDC smart meter plans with a goal of uniformity, so that ultimate determinations on issues are mirrored across EDCs. OTS Exceptions, pps. 4-6. While Duquesne Light understands that there can be a benefit with uniformity on some issues, it does not mean that every issue needs to be decided or treated the same for each Pennsylvania EDC. A one-size-fits all approach is not appropriate because each utility has submitted a different plan, and each utility has different circumstances that the Commission must evaluate when making decisions. Further, it is sometimes good for the Commission to try different approaches – so there can be benefits to treating EDCs differently to explore the results. Thus, Duquesne Light disagrees with

⁹ All of the milestone and filing deadlines are set forth in Duquesne Light's Main Brief, on pages 8-9 and 11-12. However, notably, Duquesne Light intends to have its smart meter network installed by October 1, 2012, which is the end of the Grace Period. Petition, p. 12. Further, Duquesne Light intends to have all smart meters installed by the end of 2018, in advance of the deadline requested by DEP. Plan, p. 13.

¹⁰ For example, the Grace Period begins upon Plan approval. If the Commission needs additional time to review the plans, and thus the Order is issued later than expected (April 1), the dates in Duquesne Light's plan will likely shift to some degree.

the OTS' exception in this regard to the extent it is asking for uniformity on all matters, but agrees that the Commission should review uniformity.

III. Conclusion

For the reasons set forth in Duquesne Light's Main and Reply Briefs and the foregoing Reply Exceptions, Duquesne Light respectfully requests that the Commission deny the Exceptions of all parties, with the exception of OSBA Exception No. 2, and adopt the Recommended Decision in this proceeding without modification.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'GAC', written over a horizontal line.

Gary A. Jack
Assistant General Counsel
Erin Higgins Creahan
Senior Attorney

March 1, 2010