

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket Nos. R-2009-2139884
	:	
Philadelphia Gas Works	:	
	:	
Philadelphia Gas Works' Revised Petition	:	
For Approval of Energy Conservation and	:	P-2009-2097639
Demand Side Management	:	

STATEMENT OF THE
OFFICE OF CONSUMER ADVOCATE
IN SUPPORT OF THE JOINT PETITION
FOR SETTLEMENT OF ALL ISSUES

The Office of Consumer Advocate (OCA), a signatory party to the foregoing Joint Petition for Settlement of Rate Investigation (Settlement) in the above-captioned proceeding, respectfully requests that the terms and conditions of the Settlement be approved by the Administrative Law Judge (ALJ) and the Pennsylvania Public Utility Commission (Commission). The Settlement resolves all issues regarding the request for an increase in distribution revenues by Philadelphia Gas Works (PGW or Company) and also resolves all issues as to the Company's pending Demand Side Management (DSM) Petition. The OCA submits that the proposed Settlement is in the public interest.

I. INTRODUCTION

PGW is a municipal public utility company, owned by the City of Philadelphia and managed and operated by the Philadelphia Facilities Management Corporation, a non-profit

Pennsylvania corporation. The natural gas service being furnished or rendered by PGW became subject to the regulation and control of the Pennsylvania Public Utility Commission on July 1, 2000, pursuant to the Natural Gas Choice and Competition Act, 66 Pa. C.S. Section 2212. PGW furnishes natural gas service to approximately 494,500 residential, commercial and industrial customers in the City of Philadelphia, Pennsylvania.

On December 18, 2009, Philadelphia Gas Works (PGW) filed Supplement No. 36 to its Tariff Gas- Pa. P.U.C. No. 2 at Docket No. R-2009-2139884. In its filing, the Company requested that the Commission maintain its \$60 million distribution rate increase from the December 2008 Extraordinary Rate Order. The Company further proposed to increase current distribution rates to produce additional annual operating revenues of \$42.5 million. According to the Company's filed materials, this additional \$42.5 million in new revenues was needed to fund PGW's post-employment benefits other than pensions (OPEBs) pursuant to Government Accounting Standards Board Statement No. 45. The Company's request would have increased overall distribution rates by 4.8%. According to the Company's filing, a typical residential heating customer with an annual usage of 92 Mcfs, would have seen an increase of \$8.54 per month, or a 6.5% increase (Exh. A-III.E.20).

PGW also proposed to implement a suite of Demand Side Management programs (DSM) in docket number P-2009-2097639. PGW included a revised DSM program with its distribution base rate filing. On December 18, 2009, PGW filed a Motion to Consolidate the DSM proceeding (at docket number P-2009-2097639) with this base rate proceeding. On February 11, 2010, the motion was granted by the Commission and the two cases were consolidated. The proposed DSM plan is composed of seven separate programs. PGW proposed to spend approximately \$54 million on these programs over five years.

Complaints in opposition to the proposed revenue increase were filed by the OCA, the Office of Small Business Advocate (OSBA), Tenant Union Representative Network (TURN), Philadelphia Housing Authority (PHA), Philadelphia Industrial and Commercial Gas Users Group (PICGUG), the Clean Air Council (CAC), and several individual customers. The Commission's Office of Trial Staff (OTS) filed a Notice of Appearance and a Petition to Intervene was filed by the Retail Energy Supply Association (RESA) and granted on March 2, 2010.

On February 11, 2010, the Commission entered an Order initiating an investigation of PGW's proposed rate increase and assigning the case to the Office of Administrative Law Judge. ALJ Charles E. Rainey was assigned to preside over the case. As part of its Order, the Commission suspended the effective date of PGW's proposed tariff by operation of law until September 16, 2010, unless permitted by Commission Order to become effective at an earlier date.

A prehearing conference was held before ALJ Rainey on March 2, 2010. At the prehearing conference ALJ Rainey set a procedural schedule for litigation. In addition, the ALJ ordered the scheduling of five public input hearings in PGW's service territory. The Prehearing Order entered by ALJ Rainey confirmed the procedural schedule and adopted certain modified rules for discovery. Pursuant to ALJ Rainey's directive, afternoon and evening public input hearings were held on April 6, 2010 and April 7, 2010 in Philadelphia and an evening session was held on April 8, 2010.¹

Throughout the course of the proceeding, the OCA engaged in formal and informal discovery designed to thoroughly investigate all aspects of the Company's proposed rate increase and

¹ Public Input Hearings were held on April 6, 2010 at the Community College of Philadelphia at 1:00PM and 6:00PM, on April 7, 2010 at 1:00PM at the Community Academy of Philadelphia and at 7:00PM at the George Washington High School, and on April 8, 2010 at 6:00PM at the Dorothy Emanuel Recreation Center.

DSM programs. The OCA submitted the Direct Testimony of Thomas S. Catlin, Michael A. Bleiweis, Richard W. LeLash, Glenn A. Watkins, Dr. David Nichols and Roger D. Colton on March 26, 2010. The OCA submitted the Rebuttal Testimony of Richard W. LeLash, Glenn A. Watkins and Roger D. Colton on April 23, 2010 and the Surrebuttal Testimony of Thomas S. Catlin, Michael A. Bleiweis, Richard W. LeLash, Glenn A. Watkins, Dr. David Nichols and Roger D. Colton on May 4, 2010.

In advance of the scheduled dates for hearings, the parties reached a Settlement agreement in principle. Hearings were held on May 10, 2010 and May 12, 2010 to address procedural issues. ALJ Rainey granted the request to suspend the remainder of the procedural schedule. The parties have agreed to the stipulation of the admission of all parties' testimonies into the record without the need for cross examination. The parties moved that those testimonies be entered into the record in a separate Motion filed on May 17, 2010.

As noted above, and discussed further below, the OCA submits that the proposed Settlement is in the public interest and should be approved. The OCA will discuss below several of the key provisions of the Settlement that are of particular importance to the OCA. The OCA expects that the other parties will address those provisions of the Settlement that were the direct focus of their efforts in this matter.

II. REVENUE REQUIREMENT (Joint Settlement ¶¶ 16, 18)

The proposed Settlement will allow PGW to file new tariff rates designed to provide an overall rate increase of \$16 million in annual revenues for service rendered on or after the Commission enters an Order approving the Settlement, instead of its requested \$42.5 million increase. Settlement, ¶ 16. This represents a 1.81% overall increase as compared to the 4.8% increase originally requested by PGW. As is discussed in more detail below, for residential

customers, rates will increase by 2.91%, as compared to the 6.5% increase that PGW originally requested. Under the Company's initial filing, a typical residential heating customer with an annual usage of 92 Mcfs, would have seen an increase of \$8.54 per month, but under the Settlement, the total bill increase will be approximately \$3.58 per month.

Additionally, the Settlement provides that PGW will not file for another general base rate increase for at least 24 months from the date that the Commission approves the Settlement. Settlement, ¶ 18. Thus, for at least two years from the date of entry of the Commission's Order, PGW's ratepayers will be assured of some level of distribution rate stability.

Based on OCA's analysis of the Company's filing and discovery responses received, the rate increase under the proposed Settlement represents a result that would be within the range of likely outcomes in the event of full litigation of the case. The increase is appropriate and, when accompanied by other important provisions contained in the Settlement, yields a result that is just and reasonable.

III. OPEB FUNDING (Joint Settlement ¶¶ 16, 19, 20)

In its filing, PGW sought the recovery of the accrual basis costs of providing post-employment benefits other than pensions (OPEBs) pursuant to Government Accounting Standards Board Statement No. 45 (GASB 45). The costs for which PGW was seeking recovery through this base rate filing had two components: (1) the annual accrual basis costs for benefits earned in Fiscal Year (FY) 2011 plus the amortization of the Unfunded Accrued Actuarial Liability (UAAL) over 30 years, and (2) the Net OPEB Obligation that it had been required to accrue over the period from FY 2007 when GASB 45 became effective through FY 2010. The combined effect of these costs as proposed by PGW was a \$66.88 million claim, an increase of \$42.5 million over the pay-as-you-go

costs of \$24.346 million reflected in current rates. PGW proposed to amortize the Net OPEB obligation accrued from FY 2007 to FY 2010 over a five year period.

The OCA had two significant concerns with regard to PGW's request for the recovery of OPEB costs. OCA witness Catlin first recommended that a 20-year amortization period be utilized for the net OPEB obligation to mitigate the effect of the adoption of GASB 45 on ratepayers and stabilize revenue requirements over the next several years. OCA St. 3 at 8. Mr. Catlin noted that this recommendation was consistent with the 20-year time period established in the Commission's policy statement regarding recovery of the OPEB costs that investor owned utilities deferred after the adoption of Statement of Financial Account Standards (SFAS) No. 106. Id.; 52 Pa. Code § 69.351.

The second concern identified by the OCA was the lack of an established irrevocable trust in which the amounts collected from ratepayers to fund accrual basis OPEB costs would be deposited. OCA St. 3 at 9-11. Mr. Catlin testified that such a trust fund is necessary to ensure the availability of the funds to pay future OPEB costs and to minimize the amounts that must be collected as a result of the return earned on the invested trust funds. Id. The Settlement reached in this docket addresses both of the OCA's concerns.

First, the Settlement calls for an increase in rates of \$16 million to assist in funding the incremental OPEB costs. Settlement, ¶ 19. The Settlement provides that PGW will amortize the Net OPEB Obligation over 30 years instead of the five years originally requested by the Company. Id. Additionally, in order to mitigate the impact of changing from recovery of OPEB costs on a pay-as-you-go basis to recovery on an accrual basis under GASB 45, the Settlement provides for \$15 million annually for an initial five year period for funding of the Unfunded Actuarial Accrued

Liability (UAAL). Settlement, ¶ 19. This funding mechanism will continue until PGW's next distribution rate case or until the end of a 5-year period, whichever comes first. Settlement, ¶ 20.

Second, the Settlement requires that PGW establish an irrevocable trust fund for OPEB collections prior to any effective date for the rate increase. Settlement, ¶ 19. PGW has agreed to establish this trust and to make monthly deposits to this trust so that \$18.503 million annually is deposited in trust to fund the UAAL and the net OPEB obligation. PGW has agreed to use existing revenues to fund the difference between the \$16 million collected through the Rider and the \$18.503 million necessary to fund its OPEB obligations. Settlement, ¶¶ 19, 20.

The OCA would also note that \$16 million of the \$18.503 million to be deposited in the trust will be collected through a Rider that reconciles for over- and under-collections. The Rider will be collected on a volumetric basis for all customer classes. The Rider will assist PGW in the collection of this OPEB amount.

Based on the OCA's analysis of the Company's filing and discovery responses received, the treatment of OPEBs under the proposed Settlement is appropriate and, when accompanied by other important provisions contained in the Settlement, yields a result that is just and reasonable.

IV. DEBT REPAYMENT (Joint Settlement ¶ 17)

In the Settlement, the Company has committed to make principal debt repayments on a monthly basis and agrees that it will not sell new money bonds (after the issuance currently scheduled for July 2010) for at least three years. Settlement, ¶ 17. As of the end of the test year, FY2010, PGW projects to have over \$1.2 billion of outstanding long-term debt, including a new issue of approximately \$150 million presently scheduled to be issued in July. *See* Exh. JRB-2a, page 4. Additionally, during the Stay Out period, PGW will provide quarterly reports to the Commission

and the active parties listing its monthly debt repayments with the amounts of principal and interest for each clearly set out.

The OCA submits that these provisions assure that PGW will continue to pay down the portions of long-term debt that become due over the period ending with FY2015 and that no incremental long-term debt is to be issued over the next three years.

V. SWAP ARRANGEMENT (Joint Settlement ¶ 21)

In PGW's recent emergency rate proceeding, the details and possible termination fees for an interest rate swap agreement (Swap Arrangement) were a key issue. PGW had originally entered into the Swap Agreement as a means to smooth out the projected interest payments on its variable rate bonds. PGW had provided testimony during the emergency rate proceeding as to its intentions to terminate the Swap Arrangement, which as of 12/31/2008 would have required a one-time termination payment of approximately \$64 million. OCA St. 1 at 14. Subsequent to the emergency rate proceeding, PGW continued to investigate its options as to the Swap Arrangement.

Prior to filing the instant rate case, PGW did terminate a small portion of the Swap Arrangement, at a cost of approximately \$3.7 million. The bulk of the Swap Arrangement remains in place. As outlined in the direct testimony of OCA witness Richard LeLash, the OCA had serious reservations about any future payments that might be required in order to terminate this last vestige of the original Swap Arrangement. OCA St. 1 at 14. As Mr. LeLash explained:

To put the swap agreement into perspective, it is useful to understand the magnitude of its potential cost to PGW. According to Mr. Bogdonavage's response to discovery request OCA Set I-34, toward the end of 2008 its associated mark to market value was a loss of between \$54 and \$64 million. Even as recently as November 2009, it still had a mark to market loss of \$35 million. Indeed, in the last extraordinary rate proceeding, it appears that the inherent cost risk of the swap agreement was a critical factor in the level of rates that were ultimately authorized for the Company.

OCA St. 1 at 14. The Settlement provisions herein address and adequately resolve the OCA's concerns on this issue.

First, PGW has agreed that it will not seek rate recovery for any future, one-time termination payments associated with the Swap Arrangement. Settlement ¶ 21(a). Second, PGW has agreed that if the need to terminate the Swap Arrangement arises in the future, it will engage in a cost/benefit analysis to determine the most prudent time to do so in order to provide the best outcome for ratepayers. Settlement ¶ 21(b), (c). Finally, PGW has agreed to not enter into any new interest rate swaps for a period of three years without first giving the Commission and the parties 60 days notice. Settlement ¶ 21(d). This notice would enable the parties to analyze any possible course of action on this issue before a new interest rate swap was consummated.

Based on the OCA's analysis of the Company's filing and discovery responses received, the resolution of the Swap Arrangement is appropriate and in the public interest.

VI. REVENUE ALLOCATION (Joint Settlement ¶22, Settlement Exhibit 1)

The allocation of any proposed rate increase among the customer classes was a major issue in this proceeding. In its filing, the Company proposed to increase residential rates by \$45.010 million of the originally requested \$42.5 million. PGW St. 8, Exh. HSG-7C (Updated 3/14/10); Settlement Exh. 1. OCA witness Watkins disagreed with the Company's cost of service study and resulting allocation of the requested increase. OCA St. 4 at 24. Given the size of the Residential class (relative to the total system), the Residential class' lower rate of return, and all other firm classes higher rates of return, Mr. Watkins recommended that the Residential class absorb 100% of the authorized increase in revenues in this case. Id. He based his recommendation on making progress towards the system average return as well as on the principles of gradualism and the avoidance of rate shock. As Mr. Watkins explained:

I view this case as one in which rate stability and gradualism are especially important. In terms of rate stability, I do not believe it is in the public interest for base rates to bounce up and down. In terms of gradualism, my proposal for the Residential class to absorb the entire rate increase makes significant strides in moving to cost of service, yet tempers an abrupt move toward cost of service.

OCA St. 4 at 23-24. Mr. Watkins also recommended that if PGW was allowed to maintain the \$60 million revenue increase from the emergency proceeding, but was awarded no additional increase, and if the Commission wanted to take this opportunity to move all rate classes closer to cost of service unity, then rate reductions could be made to the Commercial, Municipal, Industrial and Public Housing Authority classes. OCA St. 4 at 26. Mr. Watkins based his recommendation on his cost of service study that utilized the Peak and Average methodology and found that the revenue reductions should total no more than four percent of base rate (non gas, non USEC, and no REC) revenues. Id. In addition to the Company and the OCA, OSBA witness Knecht, OTS witness Kubas and PHA witness Pender made revenue allocation proposals. All of these witnesses proposed assigning a higher revenue increase to the Residential class than the Company or the OCA. OSBA St. 1 at 14-24; OTS St. 4 at 7-12; PHA St. 2 at 3-9.

Under the Settlement, PGW's total distribution rate increase will be \$16 million. The rate increase will be allocated such that residential customers will see a distribution rate increase of \$20 million while most other rate classes will see a reduction in their rates. Settlement, ¶ 22. Under the lower revenue requirement (\$16 million versus \$42.5 million) agreed to in the Settlement, this allocation allows for all customer classes to make significant progress toward the system average return without undue rate shock being experienced by any one class. As was mentioned above, for residential customers, rates will increase by 2.91%, as compared to the 6.5% increase that PGW originally requested. Under the Company's initial filing, a typical residential heating customer with

an annual usage of 92 Mcfs, would have seen an increase of \$8.54 per month, but under the Settlement, the total bill increase will be approximately \$3.58 per month.

Indeed, in this proceeding, the Company submitted a cost of service study that showed wide ranging disparities in the returns being provided by the various customer classes. The Company's study showed several of the classes with indexed rates of return above the system average and other classes providing revenues below the system average. The Company's cost of service at current rates for the Residential Class showed an indexed Rate of Return of 0.77. Settlement Exh.1.² Under the Settlement, the Residential Class' indexed Rate of Return moves to 0.89, which represents a significant step towards the system average return. Settlement Exh. 1.

The OCA would also note that in the 2008 Emergency Rate Proceeding filed by PGW, the \$60 million revenue increase approved by the Commission was applied using the Company's then current Cost of Service allocations. P.U.C. v. PGW, Docket No. R-2008-2073938 at 32 (Order Entered December 19, 2008). In other words, the \$60 million revenue increase was allocated in such a way as to preserve the different rate classes' existing rate of returns, and the issue of allocation of those funds was specifically reserved for resolution in this proceeding. Id. at 47. Accordingly, the allocation agreed to by the parties in this Settlement effectuates not only a reallocation of the \$60 million of emergency rate relief but also a collection of the \$16 million increase agreed to in this Settlement.

² Under the OCA's Cost of Service Study, the indexed Rate of Return was 0.64 at current rates. OCA St. 4 at 25. The OCA would note, however, that its Cost of Service Study does not reflect the changes to OPEB expense resulting from the Settlement. The OCA is unable to modify its Cost of Service Study to reflect this change and, therefore, cannot produce an updated Cost of Service at current rates calculation. The 0.77 in the Company's Settlement Exhibit does capture this change in OPEB expense.

Based on the OCA's review of the cost of service studies presented in this proceeding and the varying revenue allocation proposals presented by the other parties and the OCA, the OCA views the Settlement to be within the range of reasonable outcomes from full litigation of this case. The revenue allocation under the Settlement represents a compromise and falls within the litigation positions of the Joint Petitioners. The OCA would note that the Settlement does not resolve the differences of the parties as to methodology or specific cost allocation issues on a going forward basis, but the allocation agreed to here is intended to move all rate classes toward the system average Rate of Return while at the same time respecting the principles of gradualism and avoidance of rate shock. The OCA submits that the revenue allocation agreed to in the Settlement is appropriate at this time, and, when accompanied by other important provisions contained in the Settlement, yields a result that is just and reasonable.

VII. DSM PROGRAMS (Joint Settlement ¶¶ 24, 25)

A. Introduction

PGW proposed to implement seven individual Demand Side Management (DSM) programs including: (1) Enhanced Low-Income Retrofit, a program designed to improve the efficiency of existing houses' building shells, space and water heating equipment, and lighting, and an expansion of the Company's existing Low Income Usage Reduction Program (LIURP), the Conservation Works Program (CWP); (2) Comprehensive Residential Heating Retrofit, similar to the Enhanced Low-Income Retrofit program, except for non-low-income residential customers; (3) Premium Appliances and Heating Equipment, which will promote high efficiency appliances and systems to residential and non-residential customers; (4) Commercial and Industrial Equipment Efficiency Upgrades, which will promote additional high-energy equipment and systems to non-residential customers; (5) Commercial and Industrial Retrofit, which will offer supplemental

measures to the Commercial and Industrial Equipment Efficiency Upgrades program; (6) Municipal Facilities Comprehensive Efficiency Retrofit, a program which will offer technical advice on improvement of City of Philadelphia buildings and facilities; and (7) High-Efficiency Construction, promoting efficient buildings and systems in residential and non-residential new construction. PGW St. 10 at Exh. JJP-6, 31-46; OCA St. 6 at 5. The Company proposed a total five year budget of approximately \$54 million. PGW St. 10 at Exh. JJP-6, 2-3; OCA St. 6 at 6.

As discussed in the Direct Testimony of OCA witness David Nichols, the OCA had several concerns regarding specific program design and implementation elements and the proposed costs and cost recovery mechanism, including PGW's proposal for recovery of net lost revenues. OCA St. 6 at 3-4. Specifically, the OCA recommended that the Commission review the Company's DSM Plan on a year-by-year basis, including proposed spending levels; that the total spending budget be set at no more than 1% of PGW's projected gross intrastate operating revenues; that the cost recovery mechanism not include net lost revenues; that various program design changes be implemented specifically as to the Premium Appliances Heating Equipment program, the Commercial and Industrial Retrofit Program, and the Comprehensive Residential Heating Retrofit Program (CRHRP); and that the Company take explicit steps to coordinate the delivery of the DSM programs with those of PECO Energy Company, including the CFL replacement program. OCA St. 6 at 3-4. The Settlement addresses each of these issues.

B. Overall Program

The Settlement provides that PGW shall be permitted to file a proposed five year DSM program with the Commission in accordance with the provisions of the Settlement that will allow all customers the opportunity to participate in measures specifically designed to lower natural gas usage and thereby reduce total gas costs for all ratepayers. Settlement, ¶ 24(a). The Settlement

provides support for Commission approval of the DSM Programs for an initial two year period (FY 2011 and FY 2012). Thereafter, PGW will make annual filings with the Commission and the parties four months prior to the end of the initial implementation period and four months prior to the end of each subsequent program year. Settlement, ¶ 24(a). The annual filing will include information on the program activities to date; future operational plans for the next program year; and the budget for the next year. Prior to the end of Fiscal Year 2012, the annual filing will also contain a budget proposal for the following program year. All parties have specifically reserved the right to comment on these future plans and the proposed budget in the annual review proceedings. Settlement, ¶ 24(a). All parties also have the right in their comments to the annual filing to propose modifications to the program, or to propose the termination, in whole or in part, of any part of the implementation plan, or a specific program within the DSM program. Further, any party may also request that the Commission resolve any issue raised by the annual filing that is not resolved through the comment process. Settlement, ¶ 24(a).

PGW's Plan for a comprehensive suite of DSM programs for all customer classes should provide benefits to all PGW customers. OCA St. 6 at 5-6, 13-14. The DSM Plan, serving all customer classes, will maximize the efficiencies available in PGW's service territory and will have the maximum impact on the reduction of total gas costs for all ratepayers. The Settlement allows for a comprehensive program so that all customer classes can participate.

The annual review of these programs also provides an important protection for customers. PGW has proposed a significant expansion to the scope and scale of its DSM programs, well beyond the current PGW Low Income Usage Reduction Program (LIURP). Such an annual review process is necessary in order to allow the Company to make "mid-course" corrections and to evaluate whether its measures are effectively accomplishing the goals set forth in the Plan.

Importantly, the Settlement provides all parties the opportunity to comment on each of the Company's annual filings and to attempt to resolve any issues with the Company or other parties. However, if these issues cannot be resolved, the parties still retain the right to bring the matter to the Commission for resolution.

C. Cost and Cost Recovery

Costs for PGW's DSM program will be recovered through a 1307-type automatic adjustment clause, the Efficiency Cost Recovery Mechanism (ECRM). The Settlement establishes specific limits as to the spending levels that may be recovered through the ECRM. For the first two years of the program (FY 2011 and FY 2012), the annual spending budget will not exceed 1% of PGW's total projected gross intrastate operating revenues. Settlement, ¶ 24(b). During this two year period, PGW will fully fund the Enhanced Low Income Retrofit Program at the budget levels included in the Company's filing: \$6,783,440 for FY 2011 and \$6,708,440 for FY 2012. Thereafter, the annual budgets for FY 2013 through FY 2015 will be determined in the annual reporting process, but the annual spending budgets will not exceed the levels set forth in the Company's original filing. Settlement, ¶ 24(b). PGW also had requested the recovery of net lost revenues in the ECRM. In this Settlement, PGW agrees to not make a claim for lost revenues during the Stay Out period. Settlement, ¶ 24(g).

The OCA submits that the proposed annual spending budgets for FY 2011 and 2012 are reasonable. OCA witness Nichols recommended that PGW's annual budget not exceed 1% of corresponding annual revenues until the Company's programs show demonstrated results. OCA St. 6 at 19-21. Re-evaluating the budget level after FY 2012 will allow for the Company to gain experience with a comprehensive DSM program and to adjust the program budgets on a going forward basis in a reasonable manner. The Settlement allows the Company and the parties to re-

evaluate the budget as the program develops and progresses and ensures annual reviews of the level and types of expenditures. The Settlement also provides that “in no event shall [the annual budget for FY 2013-2015] exceed the original level for that year proposed by the Company in this proceeding.” Settlement, ¶ 24(b). This provides an important cap on the maximum level of expenditures permitted in the Company’s subsequent year budgets over the course of the five year plan.

Finally, the Settlement calls for the elimination of the lost revenues from the calculation of the ECRM for the duration of the Stay Out period. The OCA had opposed this claim on both legal and policy grounds. Removal of this claim eliminates a contentious issue that could have impeded the development of a robust DSM program.

D. Program Roll-out and Design Changes

The Settlement provides for several timing changes to the proposed program roll-out and a change to the coordination initiatives included in the program design. The Premium Appliances and Heating Equipment rebate program and the Commercial Retrofit Program will be rolled out at least three months earlier than the dates proposed in the Company’s filing. Settlement, ¶ 24(c). OCA witness Nichols recommended that these programs be rolled out earlier because the Premium Appliances and Heating Equipment rebate program is the single most cost-effective program in PGW’s Plan and would allow both residential *and* non-residential customers the early opportunity to participate in the DSM programs. OCA St. 6 at 22. The Commercial Retrofit Program would provide additional efficiency services to non-residential customers. *Id.* at 23.

The Comprehensive Residential Heating Retrofit Program (CRHRP) -- a program for non-low-income residential customers -- will roll-out at least six months later than the Company’s original proposed roll-out. Settlement, ¶ 24 (c). OCA witness Nichols recommended delay on this

program because these programs are more difficult to market and deliver than are the other programs within this Plan. This program will require an adequate infrastructure of delivery vendors in an environment where new electric utility energy efficiency programs, expanded federal weatherization dollars and the Company's proposed low-income house retrofit program will all be competing for delivery vendors. Additionally, the OCA submits that it will be important to first see how the Conservation Works Program (CWP) for low-income customers is expanded into the Enhanced Low-Income Retrofit before launching the CRHRP. OCA St. 6 at 21-22.

When PGW does roll-out the CRHRP, PGW has agreed to the use of a modest fee for the initial energy audit. Settlement, ¶ 24(f). The OCA submits that this proposal is reasonable. PECO, who will be providing a similar program in the same general area, has also proposed that a fee be charged for its energy audit in its Act 129 Energy Efficiency and Conservation Plan (EE&C Plan).

In accord with the recommendations of OCA witness Nichols, the Company will coordinate its DSM programs with other programs in its service territory, including the Act 129 programs deployed by PECO. OCA St. 6 at 23-24. PGW will report on these efforts and provide a matrix of linkages to other programs with its compliance filing and in each annual program filing. Settlement, ¶ 24(e). To the extent possible, the OCA submits that it would be most cost-effective to attempt to leverage other available resources and to coordinate resources and visits with other existing programs, such as PECO's Act 129 EE&C program.

In the Settlement, PGW has also agreed that it will only include the delivery of Compact Fluorescent Lamps (CFLs) in its program in instances in which PECO will agree to provide the devices or pay for them. Settlement, ¶ 24(d). CFLs are electricity saving devices. While the house retrofit programs may provide a useful delivery vehicle for CFL installation, the cost of the

CFLs should not be recovered from PGW ratepayers. In addition, a CFL replacement program is a part of PECO's Act 129 EE&C program and costs for this program are being recovered through PECO's program. OCA St. 6 at 24. PGW's DSM Plan should work cooperatively, rather than competitively, with PECO's CFL replacement program.

E. Conclusion

Based on the OCA's analysis, PGW's DSM Plan as modified by the Settlement is reasonable and in the public interest, and therefore, should be approved.

VIII. BAD DEBT OFFSET (Settlement, ¶ 26)

A. Overview

PGW collects its universal service costs, or Customer Responsibility Program (CRP) costs, through a reconcilable Universal Service and Energy Conservation (USEC) Rider. PGW projects these universal service costs based on historic participation in the various programs. On a monthly basis, PGW determines its actual universal service costs. OCA St. 5 at 4. For the CRP, those actual universal service costs include the CRP credits and the arrearage forgiveness credits granted. The actual CRP costs incurred are reconciled to past collections, and the surcharge is adjusted up or down for under- and over-collections at the time of PGW's Section 1307(f) proceedings.

The natural gas bill for a CRP participant is comprised of two parts: (1) the portion of the bill that is at or below an affordable percentage of income and (2) the portion of the bill that is above an affordable percentage of income. *Id.* at 6. The amount above the affordable percentage is referred to as the CRP credit (or CRP shortfall) and is recovered from all other customers. Before a low-income customer becomes a CRP participant, the portion of the bill the customer cannot afford to pay, becomes uncollectible and is recovered in the uncollectible expense in base rates. A problem

arises between base rate cases when a reconcilable rider is used such as PGW's USEC. When a low-income customer enrolls in CRP between base rate cases, the portion of the bill that the customer could not pay and that was included as an uncollectible expense in base rates now becomes the CRP credit and is recovered again on a dollar-for-dollar basis through the USEC. OCA St. 5 at 7. A Bad Debt Expense Offset (Offset) is necessary to address this double recovery. A similar adjustment is needed for arrearage forgiveness as the same form of double recovery results between base rates and the USEC Rider.

B. Settlement

The Settlement provides that PGW will implement an Offset to its CRP credit amounts and pre-program arrearages of 7.1% on a monthly basis in the calculation of its USEC Rider for incremental participants in the CRP. Settlement, ¶ 26. The Offset will be applied to the CRP credit that is associated with incremental CRP participants over 84,000 participants. This level will be re-set in each distribution base rate proceeding. *Id.* As OCA witness Roger Colton discussed in his Direct Testimony and calculated in his Appendix A, Step-by-Step Determination of Bad Debt Double Recovery, the Offset is necessary in order to prevent the double recovery of bad debt expense through the USEC.³

As explained in Appendix A of his Direct Testimony, OCA witness Colton found that there is a double recovery of bad debt expense when more customers move into the CRP program than projected during the base rate case. OCA St. 5 at Appendix A. As Mr. Colton explained, the USEC should only recover the incremental costs of CRP participation that are not reflected in base rates. OCA St. 5 at 12-13. Mr. Colton found that to the extent that CRP

³ For a thorough discussion on this issue, see the Direct Testimony of OCA witness Roger Colton at OCA St. 5, Appendix A.

participation exceeds the base number of customers included in the Company's filing, the costs used to establish the USEC rates will result in an overstatement of the USEC and a double recovery of costs. Id.

The Settlement resolves this Offset issue identified by OCA witness Colton. The OCA submits that the Settlement represents a reasonable resolution of this issue. The Settlement provides a 7.1% adjustment to CRP credits and arrearage forgiveness amounts included in the USEC for incremental CRP participants over 84,000 participants. This will provide the necessary off-set to avoid double recovery of bad debt and pre-program arrearages through the USEC.

IX. CONCLUSION

The terms and conditions of the Settlement provide for an overall distribution rate increase of \$16 million. The Settlement provides what the OCA submits is a reasonable allocation of the requested increase to residential customers given the results of the Company's and the OCA's cost of service studies. The OCA submits that, taken as a whole, the reduction in the proposed revenue increase, the rate case stay-out, the OPEB funding obligations, the DSM Program, and the bad debt arrearage forgiveness offset, along with all of the other terms and conditions of the Settlement described above, represent a fair and reasonable Settlement of all outstanding issues raised by the parties in this proceeding.

WHEREFORE, for the foregoing reasons, the Office of Consumer Advocate submits that the proposed Settlement is in the public interest and respectfully requests the ALJ and the Commission to approve it.

Respectfully Submitted,



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