BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of West Penn Power Company d/b/a Allegheny Power for Approval of its Energy Efficiency and Conservation Plan Approval of Recovery of Plan Costs through a Reconcilable Adjustment Clause and Approval of Matters Relating to the Energy Efficiency and Conservation Plan	: : : : : : : :	Docket No. M-2009-2093218

DIRECT TESTIMONY OF

RAYMOND E. VALDES

ON BEHALF OF

WEST PENN POWER COMPANY d/b/a ALLEGHENY POWER

STATEMENT NO. 3

Dated: June 29, 2009

Q. Please state your name and business address.

A. My name is Raymond E. Valdes, and my business address is 800 Cabin Hill Drive, Greensburg, Pennsylvania 15601.

Q. By whom are you employed and in what capacity?

A. I am employed as General Manager, Retail Pricing Services for Allegheny Energy Service Corporation. My time is devoted to tasks performed for the regulated utility companies of Allegheny Energy, Inc. The regulated utility companies include West Penn Power Company, serving customers in Pennsylvania; The Potomac Edison Company, serving customers in Virginia, Maryland, and West Virginia; and Monongahela Power Company, serving customers in West Virginia.

Q. Have you testified or submitted testimony in other proceedings?

A. Yes, I have testified in proceedings before the Public Service Commission of Maryland, the Public Utilities Commission of Ohio, the Public Service Commission of West Virginia, the Virginia State Corporation Commission, the Pennsylvania Public Utility Commission, and the Pennsylvania Senate Consumer Protection and Professional Licensure Committee.

Q. What are your duties, responsibilities, and educational and professional qualifications?

A. I am a graduate of the University of Pittsburgh where I earned a Bachelor of Science in Electrical Engineering. I have been employed by Allegheny Energy Service Corporation for over 18 years, and have held positions of Engineer, Power Services; Engineer, Rates; Regulatory Specialist; Senior Consultant; and my current position of General Manager, Retail Pricing Services. My current duties include managing activities relative to revenue forecasting, retail rate design, and the development and maintenance of retail tariffs.

Q. Mr. Valdes, what does your testimony address?

A. My testimony will address what the Commission described in its January 16, 2009 Implementation Order for Act 129 as the three main issues related to cost recovery for Energy Efficiency and Conservation Plans ("EE&C Plan"). Those issues are: 1) determination of costs; 2) allocation of costs to customer classes; and 3) the cost recovery tariff mechanism.

Q. What standards did you employ for dealing with these issues?

A. On the issue of costs, the first standard was to limit the costs for the EE&C Plan to an amount not exceeding an annual average of two percent of West Penn Power Company's d/b/a Allegheny Power ("Allegheny Power" or "Company") total annual revenue as of December 31, 2006, for each year of the EE&C Plan from 2009 through 2013. The second standard relevant to costs is the requirement that costs requested for recovery be related to the EE&C programs and measures, including capital and expense items, as well as administrative costs; and that such costs be reasonable and prudent.

On the issue of allocation of costs to customer classes, Allegheny Power has used reasonable and generally accepted cost of service principles to allocate EE&C Plan costs and administrative costs based on the benefits a specific tariff and tariff rate schedule will obtain from programs and measures. This standard requires an analysis of what costs relate to a specific group of customers, what costs relate to multiple groups of customers, and what costs relate to system-wide plan benefits. This cost allocation standard arises from Act 129's legal mandate that the electric distribution company ("EDC") "ensure that measures approved are financed by the same customer class that will receive the direct energy and conservation benefits."[1]

The primary standard for design of the cost recovery tariff mechanism proposed for recovery of EE&C Plan costs was that it be a Section 1307[2] type cost recovery mechanism that ensures full and current recovery of prudent and reasonable costs, including administrative costs incurred in the provision or management of the plan, that have been approved by the Commission. An additional standard the Commission has made applicable to the cost recovery mechanism is that where EE&C Plan programs benefit both shopping and non-shopping customers, the charge be non-bypassable by shopping customers and structured in a way that it does not affect the EDC's price to compare.

Determination of Costs

[1] 66 Pa. C.S. §2806.1 (a)(11)
[2] 66 Pa. C.S. §1307

Q. What are the total costs for Allegheny Power's EE&C Plan?

A. The proposed EE&C Plan expenditures in total are $94,249,873, as seen in Table 6C of the EE&C Plan template ("Template"). In addition, Table 6C of the Template sets forth a breakout of costs by the customer classes designated by the Commission (Residential – including low income, Commercial/Industrial – Small, Commercial/Industrial – Large, and Governmental/Non-Profit). This table shows specific EE&C Plan costs and the allocation of common costs to each customer group.

Q. In your view, are these proposed expenditures reasonable and prudent?

A. The proposed expenditures are reasonable and prudent for several reasons. The Total Resource Cost ("TRC") test applied to the EE&C Plan, as well as the net present value and cost-benefit analysis conducted by Allegheny Power, validates that the costs are reasonable from a ratemaking perspective. In addition, to the extent these costs are incurred via agreements based on a competitively bid request-for-proposal process, that process assures the services being obtained are competitively priced. I note that these "tests" of reasonableness are applicable to the costs, including administrative costs, that were incurred prior to the EE&C Plan being filed and the effective date of the surcharge that will collect EE&C Plan costs, which is on or before November 1, 2009.

Allocation of Costs to Customer Classes

Q. How were the specific EE&C Plan costs and common costs allocated to the various EE&C programs?

A. Costs specific to a particular program were directly assigned to that specific program. Common costs were calculated separately for the residential customer class and the non-residential customer class. These common costs, separated by customer class, were then allocated to specific programs or equally shared by each program that would have applicability to the common costs. For example, if a particular program did not have an applicability for the common cost, then it was not included in the per program allocation.

Q. What tariffs are relevant to the allocation of costs to customers?

A. I began by examining Allegheny Power's two retail tariffs; Tariff No. 37 which governs the service connection to Pennsylvania State University's ("PSU") University Park main campus in State College, and Tariff No. 39 which governs other service connections provided by Allegheny Power in Pennsylvania.

Q. Please describe how EE&C Plan program costs will be allocated to customers.

A. The Commission has directed that EE&C Plan programs and measures be grouped according to general customer classifications such as residential, small commercial/industrial, large commercial/industrial and governmental/school/non-profit. However, the tariffs and tariff rate schedules applicable to our customers are not perfectly aligned with these customer classifications. Also, Act 129 requires that measures be financed by the same customer class, i.e. tariff and tariff rate schedule, that will receive the direct energy and conservation benefits. Therefore, it was necessary to examine each

EE&C Plan program and analyze its relationship to the customers in each tariff and tariff rate schedule.

One of Allegheny Power's rate schedules, Schedule 30, which covers mid-size commercial and industrial customers with billing demands from 100 to 2,000 kilowatts, is so broad that customers must be segregated so as to identify and match customers to the portfolio groupings set by the Commission. For Schedule 30, a convenient delineation point is the 500 kilowatt threshold established in the Retail Electric Default Service Program and Competitive Procurement Plan at Docket No. P-00072342. This delineation point separates Schedule 30 customers into those with a billed demand less than 500 kilowatts and those with a billed demand of 500 kilowatts or greater. As such, Schedule 30 customers with a billed demand less than 500 kilowatts are included in "Schedule 30 (small)" and are classified as small commercial/industrial, and Schedule 30 customers with a billed demand of 500 kilowatts or greater are included in "Schedule 30 (large)" and are classified as large commercial/industrial.

Tariffs and tariff rate schedules were grouped as follows:

1. Residential: Tariff No. 39, Schedule 10
2. Small Commercial & Industrial: Tariff No. 39, Schedules 20, 22 and 30 (small)
3. Large Commercial & Industrial: Tariff No. 39, Schedules 30 (large), 40, 41, 44, 46 and Tariff No. 37

4. Governmental/School/Non-Profit: All applicable non-residential tariffs and tariff rate schedules.

These are reasonable classifications of tariffs and tariff rate schedules to portfolio groups and allows a reasonable matching of EE&C Plan programs with the customer groups generally intended to benefit from the programs.

Q. Are there modifications to the general approach to cost allocation you employed that you wish to highlight?

A. Yes. In general, it was fairly straightforward to align residential program costs with the residential Schedule 10. However more analysis was needed with respect to the non-residential programs as follows:

1. The Commercial Lighting Efficiency Program would typically be allocated only to Schedules 20, 22 and 30 (small) of the small commercial/industrial customer grouping. However, we recognized that Schedule 30 (large) and Tariff No. 37 include customers that have the potential to utilize these programs. Therefore, a rate was designed so that these customers would pay, on average, an amount proportional on a demand basis to the same monthly amount as Schedule 30 (small) customers. Demand was selected as the basis since capacity is better than energy as an indicator of customer size. For example, if an average Schedule 30 (large) customer has a demand that is four times greater than the demand for an average Schedule 30 (small) customer,

then the surcharge impact for an average Schedule 30 (large) customer is designed to be four times that of an average Schedule 30 (small) customer. This modification helps limit the magnitude of the surcharge rate for Schedule 30 (large) and Tariff No. 37 customers to reflect that their larger electrical load requirements are not solely attributable to an increased lighting requirement.

2. Schedule 20 is the only grouping where LED Traffic Signals were applicable, so all LED Traffic Signal Program costs were allocated to Schedule 20.
3. The 500 kilowatt delineation point for Schedule 30 does not always align with customers expected to participate in certain EE&C Plan programs. Therefore, there are occasions where Schedule 30 (small) is included in the large commercial/industrial grouping, and occasions where Schedule 30 (large) is included in the small commercial/industrial grouping to provide better alignment with the customers expected to receive the direct energy and conservation benefits.
4. The costs associated with time-of-use rates and hourly-pricing rates are for EE&C plan management and reporting requirements and are allocated solely to the small commercial/industrial grouping since the large commercial/industrial grouping is already subject to hourly-pricing for default generation service, subject to the terms and conditions contained in the Company's Retail Electric Default Service Program and Competitive Procurement Plan at Docket No. P-00072342.

The allocation of various EE&C Plan programs to the various tariffs and tariff rate schedules is illustrated on a chart in Section 7.5 of the Template.

Q. Are customers precluded from participating in a program if costs from that program are not allocated to the tariff or tariff rate schedule on which they receive service?

A. Generally speaking, the tariff and tariff rate schedule allocation is designed for customers to pay for programs in which they are likely to participate. However, even if costs of a program are not allocated to a particular tariff or tariff rate schedule, it does not preclude a customer from participating in the program. It only means the number of customers likely to participate in a program is so small, the allocation of costs was not deemed to be significant. Of course, Allegheny Power will track the number of customers on a given tariff and tariff rate schedule utilizing a particular program and if a re-allocation of program costs is appropriate, a redesigned allocation methodology will be proposed so that EE&C Plan costs and benefits are best aligned.

Cost Recovery Tariff Mechanism

Q. How does Allegheny Power propose to recover the reasonable and prudent EE&C Plan costs?

A. Consistent with the Act 129 standard, Allegheny Power has proposed a separately stated non-bypassable line-item bill surcharge entitled "EE&C Surcharge" for Tariff No. 37 and

Tariff No. 39 that is reconciled annually, in accordance with Section 1307 of the Public Utility Code.

Q. How will the tariffed surcharge recovery EE&C program costs?

A. Cost recovery will be accomplished via a per kilowatt-hour energy surcharge for Schedules 10, 20, and 22 since the majority of customers on these rate schedules presently do not have demand meters. Since all customers on Schedules 30 (small), 30 (large), 40, 41, 44, 46 and Tariff No. 37 have meters capable of recording demand, cost recovery will be accomplished via a per kilowatt-hour energy surcharge and a per kilowatt demand surcharge (or kilovolt-ampere demand surcharge, as the case may be). The EE&C program costs allocated to each tariff and tariff rate schedule are separated into an energy-related portion and a demand-related portion, based upon the resultant load factor calculated from the energy and demand savings projections for each program. For example, if the resultant load factor from the energy and demand savings projections is one percent, then the program produces greater demand reductions in proportion to energy reductions. Therefore, one percent of program costs are collected in the kilowatt-hour energy surcharge and ninety-nine percent of program costs are collected in the kilowatt (or kilovolt-ampere) demand surcharge.

Q. Has the Company included pro forma tariffs in its filing?

A. Yes, the pro forma tariffs for the EE&C Surcharge are depicted in REV Exhibit 1. The EE&C Surcharge is designed on a levelized basis over the 43-month period beginning on or before November 1, 2009 and running through May 31, 2013. Subject to an annual reconciliation mechanism, the implementation of a levelized surcharge helps mitigate the peaks and valleys that may otherwise occur if the surcharge had not been designed on a levelized basis.

Q. Please describe the annual reconciliation mechanism.

A. Allegheny Power will submit to the Commission by March 31 of each year: (1) a comparison between forecasted revenues billed and actual revenues billed through February, as adjusted for removal of gross receipts tax and the Commission assessment fee; (2) any adjustment to the forecasted revenues anticipated to be billed during March through May, as adjusted for removal of gross receipts tax and the Commission assessment fee; (3) any adjustment to the costs levelized over the 43-month period based upon actual costs incurred through February and any revised estimates for future months, up to the amount permitted to be recovered under Act 129; and (4) the subsequent reconciliation effect to the surcharge adjusted for gross receipts tax and the Commission assessment fee, and levelized over the period of the upcoming June 1 and continuing through the remaining months of the surcharge. A final reconciliation of amounts to be collected or refunded after May 31, 2013, through a further surcharge, should be authorized by the Commission. The purpose of this annual reconciliation mechanism is to mitigate the magnitude of the reconciliation balance. Commission approval of this annual reconciliation mechanism to ensure dollar for dollar recovery of all prudently incurred costs through May 31, 2013, with a projected aggregated cost of $94.25 million, will allow the Company to utilize regulatory accounting to properly match surcharge revenue with the program costs. Allegheny Power is requesting authorization for regulatory accounting to track on a dollar for dollar basis the amounts to be recovered on a deferred basis for any under-collections, or refunded on a deferred basis any over-collections, that may occur throughout the duration of the surcharge, which can arise because of the levelized nature of the surcharge.

Q. Besides over/under collections, are there other factors that could impact the annual reconciliation process?

A. Yes. In addition to actual costs and revenues deviating away from the projections, the surcharge could change due to factors such as an update of forecasted billing determinants, re-evaluation or re-design of programs, and re-allocation of program costs to Tariff No. 39 rate schedules and Tariff No. 37. These factors are listed in the pro forma tariffs as part of the surcharge mechanism. It is our expectation that these adjustment factors would also be addressed in the annual reports submitted as part of the monitoring/evaluation process.

Q. Do the EE&C Plan costs, as filed, include capital costs?

A. No. However, as the portfolio of EE&C programs morph over time from lessons learned and actual implementation experience, at some point EE&C Plan costs could include capital costs. If such a situation occurs, this adjustment will be reflected in the annual reconciliation mechanism.

Q. When is the surcharge effective date?

A. Allegheny Power respectfully requests Commission approval to begin the EE&C Surcharge effective on one day's notice on the portions of the plan the Commission has approved within 120 days of the EE&C Plan submission date.

Q. What are the anticipated customer bill impacts from the proposed surcharge?

A. The table at the end of Section 7.5 of the Template shows estimated customer bill impacts based upon average customer energy and demand consumption. In my view, these impacts are small and reasonable and should not negatively impact any customer rate schedule.

Q. Does this conclude your testimony?

A. Yes, it does.

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ENERGY EFFICIENCY AND CONSERVATION ("EE&C") SURCHARGE

In addition to the charges provided in this Tariff and in accordance with 66 Pa. C.S.A. §2806.1, there shall be a surcharge as set forth below to recover the costs associated with Company-sponsored programs for energy efficiency and conservation programs as approved by the Commission. This surcharge is applied to designated Rate Schedules to recover costs allocated to that Rate Schedule. This surcharge will be applied each month until changed by the Commission. The resulting surcharge is in addition to any minimum charge set out in the Rate Schedule and is added to the Customer's bill before any tax surcharge is levied against the Customer's total bill. Amounts billed hereunder shall be subject to late payment charges.

CALCULATION OF SURCHARGE

The EE&C Surcharge is calculated as a levelized surcharge for the 43-month period of November 2009 through May 2013. The surcharge is calculated by dividing the Program Costs allocated to each Rate Schedule by an allocated portion of forecasted distribution energy and, if applicable, distribution demand sales for the same Rate Schedule. The calculation includes an Annual Reconciliation Factor adjustment, and an adjustment for gross receipts tax and the Commission assessment factor. The Annual Reconciliation Factor adjustment will be filed by March 31 to become effective the forthcoming June 1. Upon determination that the surcharge, if left unchanged, would result in a material over/under-collection, the Company may file a proposed interim revision of the surcharge for Commission approval.

Bills shall include an amount equal to the surcharge rate times the number of distribution energy and capacity sales as follows:

EE&C SURCHARGE

Schedule	Rate per kWh	Rate per kW / kVA
10	$0.00222	
20	$0.00112	
22	$0.00099	
30 (small)*	$0.00071	$0.34
30 (large)*	$0.00050	$0.25
40	$0.00017	$0.13
41	$0.00017	$0.13
44	$0.00017	$0.13
46	$0.00017	$0.13

*Schedule 30 (small) defined as Customers receiving service under Schedule 30 with a Kilowatt Demand less than 500 kilowatts, and Schedule 30 (large) defined as Customers receiving service under Schedule 30 with a Kilowatt Demand greater than or equal to 500 kilowatts. The Company will categorize Customers as those with Kilowatt Demands less than 500 kilowatts and those with a Kilowatt Demand greater than or equal to 500 kilowatts.

(C) Indicates Change

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ENERGY EFFICIENCY AND CONSERVATION ("EE&C") SURCHARGE (Concluded)

ELIGIBLE COSTS

Costs eligible for recovery through the EE&C Surcharge are approved by the Commission and include:

Program Costs -- Program Costs are the estimated costs for research, development, implementation, and operation of programs to be incurred by the Company and approved by the Commission. Program costs include, but are not limited to, Company labor, rebates and incentives, payments to third parties for program administration and implementation, direct marketing and advertising costs incurred by the Company, market research costs, program development, monitoring and evaluation, consultant and contractor fees, applicable software and software licenses, program measurement and monitoring hardware, and all other administrative activities associated with program development and implementation.

Annual Reconciliation Factor -- The Annual Reconciliation Factor corrects for over/under-collection of Program Costs and may reflect items such as an update of forecasted billing determinants, re-evaluation or re-design of EE&C programs, and re-allocation of Program Costs to the designated Rate Schedules. The Company will submit to the Commission by March 31 of each year: (1) a comparison between forecasted revenues billed and actual revenues billed through February, as adjusted for removal of gross receipts tax and the Commission assessment fee; (2) any adjustment to the forecasted revenues anticipated to be billed during March through May, as adjusted for removal of gross receipts tax and the Commission assessment fee; (3) any adjustment to the Program Costs levelized over the 43-month period of November 2009 through May 2013 based upon actual costs incurred through February and any revised estimates for future months, subject to this Tariff's allocation portion of the maximum aggregated cost of $94,250,408; and (4) the subsequent reconciliation effect to the EE&C Surcharge adjusted for gross receipts tax and the Commission assessment fee, and levelized over the period of the upcoming June 1 and continuing through the remaining months of the surcharge. There shall also be a final reconciliation of amounts to be collected or refunded after May 31, 2013.

(C) Indicates Change

WEST PENN POWER COMPANY

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Electric-Pa. P. U. C. No. 37
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ENERGY EFFICIENCY AND CONSERVATION ("EE&C") SURCHARGE

In addition to the charges provided in this Tariff and in accordance with 66 Pa. C.S.A. §2806.1, there shall be a surcharge as set forth below to recover the costs associated with Company-sponsored programs for energy efficiency and conservation programs as approved by the Commission. This surcharge is applied to this Tariff to recover costs allocated to this Tariff. This surcharge will be applied each month until changed by the Commission. The resulting surcharge is in addition to any minimum charge set out in the Tariff and is added to the Customer's bill before any tax surcharge is levied against the Customer's total bill. Amounts billed hereunder shall be subject to late payment charges.

CALCULATION OF SURCHARGE

The EE&C Surcharge is calculated as a levelized surcharge for the 43-month period of November 2009 through May 2013. The surcharge is calculated by dividing the Program Costs allocated to this Tariff by an allocated portion of forecasted distribution energy and distribution demand sales. The calculation includes an Annual Reconciliation Factor adjustment, and an adjustment for gross receipts tax and the Commission assessment factor. The Annual Reconciliation Factor adjustment will be filed by March 31 to become effective the forthcoming June 1. Upon determination that the surcharge, if left unchanged, would result in a material over/under-collection, the Company may file a proposed interim revision of the surcharge for Commission approval.

Bills shall include an amount equal to the surcharge rate times the number of distribution energy and capacity sales as follows:

EE&C SURCHARGE

Rate per kWh	Rate per kVA
$0.00035	$0.18

ELIGIBLE COSTS

Costs eligible for recovery through the EE&C Surcharge are approved by the Commission and include:

Program Costs -- Program Costs are the estimated costs for research, development, implementation, and operation of programs to be incurred by the Company and approved by the Commission. Program costs include, but are not limited to, Company labor, rebates and incentives, payments to third parties for program administration and implementation, direct marketing and advertising costs incurred by the Company, market research costs, program development, monitoring and evaluation, consultant and contractor fees, applicable software and software licenses, program measurement and monitoring hardware, and all other administrative activities associated with program development and implementation.

Annual Reconciliation Factor -- The Annual Reconciliation Factor corrects for over/under-collection of Program Costs and may reflect items such as an update of forecasted billing determinants, re-evaluation or re-design of EE&C programs, and re-allocation of Program Costs to this Tariff The Company will submit to the Commission by March 31 of each year: (1) a comparison between forecasted revenues billed and actual revenues billed through February, as adjusted for removal of gross receipts tax and the Commission assessment fee; (2) any adjustment to the forecasted revenues anticipated to be billed during March through May, as adjusted for removal of gross receipts tax and the Commission assessment fee; (3) any adjustment to the Program Costs levelized over the 43-month period of November 2009 through May 2013 based upon actual costs incurred through February and any revised estimates for future months, subject to this Tariff's allocation portion of the maximum aggregated cost of $94,250,408; and (4) the subsequent reconciliation effect to the EE&C Surcharge adjusted for gross receipts tax and the Commission assessment fee, and levelized over the period of the upcoming June 1 and continuing through the remaining months of the surcharge. There shall also be a final reconciliation of amounts to be collected or refunded after May 31, 2013.

(C) Indicates Change

Issued

Effective