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HAND DELIVERED

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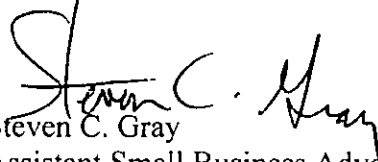
**Re: Petition of UGI Utilities, Inc. – Electric Division for Approval of its Energy
Efficiency and Conservation Plan
Docket No. M-2010-2210316**

Dear Secretary Chiavetta:

Enclosed for filing are the original and nine (9) copies of the Main Brief, on behalf of the Office of Small Business Advocate, in the above-docketed proceeding. As evidenced by the enclosed certificate of service, two copies have been served on all active parties in this case.

If you have any questions, please contact me.

Sincerely,


Steven C. Gray
Assistant Small Business Advocate
Attorney ID #77538

Enclosures

cc: Parties of Record
Robert D. Knecht

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Petition of UGI Utilities Inc. - Electric :
Division For Approval of its Energy : **Docket No. M-2010-2210316**
Efficiency and Conservation Plan :

**MAIN BRIEF
ON BEHALF OF THE
OFFICE OF SMALL BUSINESS ADVOCATE**

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Dated: June 2, 2011

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I. INTRODUCTION

The act of October 15, 2008 (P.L.1592, No. 129) (“Act 129”) required each electric distribution company (“EDC”) with at least 100,000 customers to develop and file an Energy Efficiency & Conservation Plan (“EE&C Plan”) with the Pennsylvania Public Utility Commission (“Commission”) for approval. Moreover, Act 129 required that each EE&C Plan include a variety of EE&C measures to reduce overall and peak load consumption and that each measure be financed by the customer class that receives the direct energy and conservation benefit of that measure. *See* Section 2806.1 of the Public Utility Code, 66 Pa. C.S. § 2806.1.

EDCs with fewer than 100,000 customers are specifically exempted from the requirements of Act 129. *See* 66 Pa. C.S. § 2806.1(l). However, on December 23, 2009, the Commission issued a Secretarial Letter at Docket No. M-2009-2142851 (“*Secretarial Letter*”) addressing the question of the filing of EE&C Plans by those small EDCs on a voluntary basis. *See Voluntary Energy Efficiency and Conservation Program*, Docket No. M-2009-2142851 (*Secretarial Letter* of December 23, 2009).

In a statement that accompanied the *Secretarial Letter*, Commissioner Robert F. Powelson (now the Chairman) observed that “these EDCs should only file plans if, after careful scrutiny, it is determined that doing so is in the best interest of their customers.” Statement of Chairman Robert F. Powelson, Docket No. M-2009-2142851 (Dated December 17, 2009) (“*Powelson Statement*”).

II. HISTORY OF THE PROCEEDING

On November 9, 2010, UGI Utilities, Inc. – Electric Division (“UGI Electric” or the “Company”) filed a Petition for Approval of its Energy Efficiency and Conservation Plan (“*Petition*”) with the Commission at Docket No. M-2010-2210316.

On November 29, 2010, the OSBA filed a Notice of Intervention and an Answer to the *Petition*.

On January 5, 2011, a prehearing conference was held before Administrative Law Judge (“ALJ”) Susan D. Colwell.

On March 17, 2011, the OSBA served the direct testimony of its witness, Robert D. Knecht.

On April 7, 2011, the OSBA served the rebuttal testimony of Mr. Knecht.

On April 21, 2001, the OSBA served the surrebuttal testimony of Mr. Knecht.

On May 4, 2001, an evidentiary hearing was held before ALJ Colwell.

The OSBA submits this Initial Brief pursuant to the procedural schedule in this case.

III. SUMMARY OF ARGUMENT

A. Revenue Decoupling

UGI Electric’s *Petition* includes a proposed Conservation Development Rider (“CD Rider”) that would allow the Company to implement a revenue decoupling mechanism, *i.e.*, a mechanism to recover distribution revenue margins presumed to have been lost because of a conservation-related decline in sales. Although Section 2806.1(k)(1) provides for an EDC’s full recovery of the “reasonable and prudent” costs of its EE&C Plan, Section 2806.1(k)(2) prohibits revenue decoupling. Section 2806.1(k)(3) does allow an EDC to seek to avoid such losses prospectively by reflecting any anticipated conservation-related sales decline in the forecast used

to calculate the revenue requirement in its next distribution base rate case. Consequently, if UGI Electric were required to file an EE&C Plan, the proposed CD Rider would be unlawful.

The fact that the Company submitted its *Petition* on a voluntary basis does not resolve the unlawfulness of its CD Rider. In the *Secretarial Letter*, the Commission recognized that small EDCs such as UGI Electric might file EE&C Plans that would vary somewhat from the mandates set forth in Act 129. Nevertheless, the Commission envisioned a voluntary EE&C Plan that would closely follow Act 129, not depart from Act 129 on such a fundamental principle as the prohibition on revenue decoupling.

However, even assuming *arguendo* that revenue decoupling is not unlawful for EDCs with fewer than 100,000 customers, the Commission should reject the proposed CD Rider and the Company's alternative of recovering the assumed decline in distribution revenue margins as a deferred regulatory asset.

Under UGI Electric's EE&C Plan, customers not participating in an EE&C measure would be required to subsidize customers that are participating. Revenue decoupling would compound the financial burden on the non-participating customers. Not only would they be forced to pay for the subsidies, but they would also be forced to pay for the *deemed* decline in distribution revenue margins resulting from the conservation incentivized by those subsidies.¹

Furthermore, the combination of UGI Electric's proposed CD Rider and the Company's fuel switching proposal would provide a significant financial benefit to UGI Electric and its affiliated interests, and would impose a significant financial burden on the Company's

¹ The OSBA recognizes that both participating and non-participating customers would eventually be required to pay for lost margin related to conservation activities, when the load reductions are reflected in a base rate proceeding. However, a base rate proceeding would likely rely on *observed* conservation effects based on actual customer load data, rather than *deemed* conservation savings as measured using the Technical Resource Manual ("TRM"). Moreover, a base rate proceeding would allow for evaluation of all factors affecting customers' loads, in contrast to the CD Rider which makes automatic rate adjustments subject to only limited regulatory scrutiny.

customers. Specifically, the customers that would be able to take advantage of fuel switching would reduce UGI Electric's sales of electricity and (in most instances) increase the sales of gas by UGI Electric's affiliate, UGI Penn Natural Gas ("PNG"). Because of revenue decoupling, UGI Electric's customers would be required to pay for margins lost because of the decline in electric sales despite PNG's financial gain on gas distribution margins. The net effect would be increased income for the totality of UGI Electric and its affiliated interests.

B. Subsidization

UGI Electric's non-residential customers should not be required to subsidize the EE&C measures proposed in the *Petition*. Every dollar a non-residential customer must pay in subsidies is a dollar not available to expand a business, to hire more employees, or to increase pay and benefits.

Non-residential customers do not require a subsidy if they could save more in lower electric bills than they would spend if they had to bear the entire cost of an EE&C measure. They simply need to have those savings opportunities brought to their attention.

C. Cost-Effectiveness of the EE&C Plan

UGI Electric is not subject to the mandatory targets and penalties that Act 129 imposes on larger EDCs. Nevertheless, UGI Electric should be required to demonstrate that the overall cost-effectiveness of its load reductions is comparable to that achieved by the larger EDCs. Therefore, in the absence of targets and penalties, the Commission should require an *ex post* prudence review.

An *ex post* prudence review of the EE&C costs would be especially appropriate if the Commission approves UGI Electric's proposal to require non-participating customers to pay subsidies to participating customers.

D. OSBA's Alternative

The OSBA would support the *Petition* if: revenue decoupling were eliminated and the subsidies to non-residential customers for participating in the EE&C measures were eliminated. However, if the Commission approves subsidies for participating non-residential customers, the OSBA respectfully submits that an *ex post* prudence review process for EE&C costs should be adopted.

IV. ARGUMENT

A. Burden of Proof/Applicable Legal Standard

Section 332(a) of the Public Utility Code, 66 Pa. C.S. § 332(a), states in pertinent part, as follows:

Except as may be otherwise provided in section 315 (relating to burden of proof) or other provisions of this part or other relevant statute, the proponent of a rule or order has the burden of proof.

66 Pa. C.S. § 332(a).

Similarly, Section 315(a) of the Public Utility Code, 66 Pa. C.S. § 315(a), states in pertinent part, as follows:

In any proceeding upon the motion of the commission, involving any proposed or existing rate of any public utility, or in any proceedings upon complaint involving any proposed increase in rates, the burden of proof to show that the rate involved is just and reasonable shall be upon the public utility.

66 Pa. C.S. § 315(a).

Consequently, as the party proposing the EE&C Plan and the resulting rate increases, UGI Electric bears the burden of proving that the Plan is just, reasonable, and in conformance with the *Secretarial Letter*.

Once UGI Electric has presented evidence sufficient to satisfy the burden of proof initially, the burden of going forward to rebut that evidence shifts to the OSBA and the parties aligned with the OSBA. If the evidence presented by UGI Electric and the OSBA (and those other parties) is of co-equal weight, UGI Electric has not satisfied its burden of proof. In order to rebut the OSBA (and those other parties), UGI Electric must provide some additional evidence. *Burleson v. Pennsylvania Public Utility Commission*, 443 A.2d 1373 (Pa. Cmwlth. 1982), *affirmed*, 501 Pa. 433, 461 A.2d 1234 (Pa. 1983).

Even though the burden of going forward may shift throughout this proceeding, the burden of persuasion never shifts. The burden of persuasion always remains on the party seeking affirmative relief from the Commission, *i.e.*, on UGI Electric. *Milkie v. Pennsylvania Public Utility Commission*, 768 A.2d 1217 (Pa. Cmwlth. 2001).

B. Filed Plan

1. Position Regarding Approval of the Plan as Filed

The *Petition* contains a revenue decoupling mechanism, *i.e.*, the CD Rider, both as originally filed and as advocated throughout this proceeding by the Company. This decoupling mechanism is a fatal flaw in the *Petition* and a violation of both Act 129 and the direction provided by the Commission in the *Secretarial Letter*. OSBA witness Mr. Knecht summarized the decoupling mechanism, as follows:

The Company proposes that an adjustment mechanism, termed the Conservation Development Rider ('CDR'), would automatically increase the Company's distribution rates for revenues that are theoretically lost as a result of deemed reductions in consumption associated with the EE&C Plan proposed in this proceeding. I refer to these reductions in consumption as 'deemed' reductions, because they would not be directly measured. Deemed reductions would be determined based on the specific conservation measures adopted, and the technical parameters embedded in the Technical Reference Manual ('TRM') or other sources. The CDR is a partial

‘revenue decoupling’ mechanism, in that the Company’s revenues would be independent (decoupled) from one form of volume variation.

OSBA Statement No. 3, at 1.

Section 2806.1(k)(1) provides for an EDC’s full recovery of the “reasonable and prudent” costs of its EE&C Plan. However, Sections 2806.1(k)(2) prohibits revenue decoupling. Section 2806.1(k)(3) allows an EDC to reflect any anticipated conservation-related sales decline in the forecast used to calculate the revenue requirement in its next distribution base rate case. In short, the statute allows EDCs to seek to avoid the future loss of distribution revenue margins but prohibits them from recovering those losses retroactively.

UGI Electric’s proposed CD Rider is an unlawful revenue decoupling mechanism. Consequently, the *Petition*, as filed, should be rejected by the Commission. The fact that the Company submitted its *Petition* on a voluntary basis does not resolve the unlawfulness of its CD Rider. In the *Secretarial Letter*, the Commission recognized that small EDCs such as UGI Electric might file EE&C Plans that would vary somewhat from the mandates set forth in Act 129. Nevertheless, the Commission envisioned a voluntary EE&C Plan that would closely follow Act 129, not depart from Act 129 on such a fundamental principle as the prohibition on revenue decoupling.

In addition, the *Petition*, as filed, requires the Company’s non-residential customers to subsidize the proposed EE&C measures. Imposing the cost of subsidization on non-participating customers is unreasonable. Non-residential customers should not need a subsidy if they are alerted to the opportunity to save more on their electric bills than the total cost of the particular EE&C measure they select.

Furthermore, the *Petition*, as filed, does not include an *ex post* prudence review of EE&C costs. Because the Company is not subject to the mandatory targets and penalties that Act 129 imposes on larger EDCs, UGI Electric lacks the financial incentive to assure that the overall cost-effectiveness of its EE&C Plan is comparable to what has been achieved by the larger EDCs. Subjecting recovery of EE&C costs to an after-the-fact prudence review would provide UGI Electric with such an incentive.

2. Filed Plan's Adherence to the Commission's December 23, 2009, Secretarial Letter Guidelines

In the *Secretarial Letter*, the Commission stated, as follows:

While the provisions of Act 129 are not directly applicable to voluntary EE&C plans, certain elements of the Act 129 EE&C Program are instructional and applicable to any prudent and cost-effective EE&C program.

Secretarial Letter, at 1.

Furthermore, Chairman Powelson observed as follows:

I am extremely cognizant of the fact that the Legislature specifically exempted these companies from the requirements set forth in Act 129, which mandated EE&C plans for EDCs with 100,000 customers or more. I wish to make it clear that, by today's action, we are in no way mandating that the smaller EDCs file EE&C plans of the scope mandated by Act 129, or even file EE&C plans at all.

I believe these EDCs should only file plans if, after careful scrutiny, it is determined that doing so is in the best interest of their customers. Further, companies filing plans should determine the proper scale and scope of the measures in their proposed plans; in many cases it may be prudent to file plans that are less expansive, with lower reduction targets, than those filed by the larger EDCs.

Powelson Statement, at 1.

OSBA witness Mr. Knecht summarized the ways in which the *Petition* differs from the requirements of Act 129:

There are three fundamental differences between UGI Electric's Plan and the EE&C plans approved for the larger EDCs:

- First, counsel advises that UGI Electric is not required under Act 129 to implement an EE&C plan. Therefore, UGI Electric must demonstrate that its Plan is economically reasonable, and cannot rely on a legislative mandate as a justification for either the Plan itself or for the cross-subsidies proposed within the Plan.
- Second, counsel advises that UGI Electric is not subject to the penalties specified in Act 129 which apply to EDCs that do not meet certain energy and peak demand reduction targets specified in the legislation. Counsel further advises that UGI Electric also is not subject to the spending limits of Act 129. As such, UGI Electric has little incentive to be efficient with program costs, particularly if its proposed cost recovery mechanism is adopted.
- Third, counsel advises that the CDR mechanism proposed by the Company for recovery of margin associated with lost load is explicitly banned by Act 129, and therefore is not used by any other EDC EE&C plan in Pennsylvania.

OSBA Statement No. 1, at 3-4.

As summarized by Mr. Knecht and as discussed in the preceding section of this brief, the *Petition* contains an unlawful revenue decoupling mechanism. As a result, the *Petition* is not in conformance with either Act 129 or the *Secretarial Letter*.

Other elements of the *Petition* will be addressed throughout this brief. However, the OSBA views the Company's proposed CD Rider mechanism as a violation of Act 129. If the Company believes that it cannot operate the EE&C Plan set forth in the *Petition* without the CD Rider, then the OSBA respectfully submits that UGI Electric should withdraw the *Petition*. As Chairman

Powelson pointed out, the size of an EDC matters, and it may simply be prudent for UGI Electric to have no EE&C Plan whatsoever.

3. The Plan's Cost Effectiveness

In the *Secretarial Letter*, the Commission provided the following specific guidance to small EDCs such as UGI Electric:

To begin with, the Commission will adopt the Act 129 definition of an energy efficiency and conservation measure and apply it to all voluntary EE&C plan filings. Furthermore, as the cost effectiveness and verification of energy savings is prudent and essential for any such program, the evaluation, verification and measurement (EM&V) of energy savings are to be evaluated using the Technical Reference Manual established under Docket No. M-00051865. In addition, the Total Resource Cost test ["TRC Test"] as defined in Act 129 and applied by this Commission pursuant to any order at Docket No. M 2009 2108601 will also apply to all voluntary EE&C plans to determine whether each proposed EE&C plan is cost effective.

Secretarial Letter, at 1-2 (footnotes omitted).

Furthermore, Mr. Knecht observed as follows:

The fundamental principle of the TRC Test is that the total costs that are avoided by the conservation program exceed, in present value terms, the total program costs incurred. Economic principles dictate that this evaluation be made on a marginal or incremental cost basis, rather than on an average cost basis. In practice, a number of methodological assumptions must be adopted to determine the costs avoided. It is my understanding that the methods and assumptions used by UGI Electric are generally consistent with the Commission's rules for the EE&C plans required by Act 129.

OSBA Statement No. 1, at 4 (footnote omitted).

Therefore, the OSBA does not take issue with the *Petition's* use of the TRC Test for the Plan's various EE&C measures. However, as Mr. Knecht pointed out, UGI Electric has less

incentive than a larger EDC to design and operate its Plan in a cost-effective manner because the Company is not subject to the mandatory targets and penalties that Act 129 imposes on larger EDCs. Therefore, in the absence of targets and penalties, the Commission should require an *ex post* prudence review of the Plan's costs. OSBA Statement No. 1, at 9. An *ex post* review of the EE&C costs is necessary if the Commission approves UGI Electric's proposal to require non-participating customers to pay subsidies to participating customers.

4. Filed Plan's Voluntary Nature/Company's Ability to Withdraw Plan If Commission Removes Revenue Recovery Mechanism

As set forth above, and as addressed in the *Powelson Statement*, an EE&C Plan may be an expense that is unaffordable for a small EDC. Nevertheless, the OSBA opposes the Company's proposal to implement the CD Rider. If the Commission were to approve the *Petition*, but agree with the OSBA and deny the Company the use of the CD Rider, UGI Electric has implied that it might withdraw the *Petition*. See UGI Electric Statement No. 3RJ, at 7.

If the Company were to withdraw its *Petition* under those circumstances, the OSBA would not object.

C. Proposed Modifications to the Filed Plan

1. Elimination of Any Revenue Recovery Mechanism

As set forth above, the OSBA opposes the Company's proposed CD Rider mechanism as a violation of Act 129 and the *Secretarial Letter*.

Mr. Knecht also explained how the CD Rider would be inconsistent with normal *ratemaking principles*:

In addition to this apparent legislative proscription [under Act 129], other basic ratemaking principles also argue against the adoption of the CDR. Under current rate design principles in Pennsylvania, load changes related to conservation, weather, or economic fluctuations are not subject to automatic adjustment mechanisms. Adopting such a mechanism that applies to only one type of conservation program (but excludes all other conservation programs, including those undertaken by customers themselves) is inconsistent and represents single-issue ratemaking. For example, any load growth experienced by UGI Electric related to new customers, or to existing customers, is not subject to a similar reconciliation mechanism. To the extent that UGI Electric desires to adopt a rate 'decoupling' mechanism to reduce the impact of load fluctuations on its bottom line, it should make such a proposal in the context of a base rates proceeding.

OSBA Statement No. 1, at 10 (footnote omitted).

As an alternative to the CD Rider, the Company proposed the use of a regulatory asset to recover the assumed lost distribution revenue margins instead of the CD Rider. UGI Electric Statement No. 3R, at 2. Mr. Knecht responded to the Company's alternative, as follows:

The regulatory asset proposal suffers from the same single-issue ratemaking problem as the CDR. The regulatory asset would compensate UGI Electric for any deemed loss of revenues associated with the EE&C Plan, but would not permit offsetting adjustments to be considered. Moreover, as UGI Electric's current rates appear to exceed its costs based on its financial filing, deferring costs in a regulatory asset would be doubly inequitable, in that it would require future generations of UGI Electric's ratepayers to pay for the Company's over-recovery of costs today.

OSBA Statement No. 3, at 3.

In response to the OSBA's opposition to the CD Rider, as well as the OSBA's opposition to the regulatory asset proposal, UGI Electric asserted that the assumed loss of distribution revenue margins would cause the Company to file a base rate case sooner rather than later. *See* UGI Electric Statement No. 3R, at 3.

Mr. Knecht addressed the Company's assertion in his surrebuttal testimony, as follows:

First, it is not obvious that a rate case for UGI Electric is imminent, or would become imminent as a result of adopting the proposed EE&C Plan. To my knowledge, UGI Electric has not filed a base rate case since 1995 (adjudicated in 1996), at Docket No. R-00953534. However, according to its March 31, 2011 Financial Report to the Commission, attached to this testimony as Exhibit IEc-S1, the Company's reported return on common equity was 13.08 percent for the 12 months ending December 31, 2010, a value well in excess of recent return on equity awards from this Commission or from other U.S. regulatory authorities. In addition, the \$308,000 first year deemed reduction in revenues cited by Mr. McAllister (adjusted for income tax effects) would reduce that equity rate of return by no more than 40 to 50 basis points. Even after three years, the deemed annual revenue reduction of \$1.0 million would reduce UGI Electric's return on equity by about 144 basis points. All other factors being equal, the effects of the EE&C Plan would leave UGI Electric's return on equity above 11 percent.

Moreover, all other factors are not necessarily equal. Load growth or cost reductions unrelated to the EE&C Plan could produce increases in net income which offset the effect of deemed revenue losses from the EE&C Plan.

OSBA Statement No. 3, at 2 (footnotes omitted).

In his rejoinder testimony, UGI Electric witness William J. McAllister disputed certain elements of Mr. Knecht's financial analysis of the Company. Mr. McAllister claimed that the correct "ROE is 11.55%, not the 13% referenced by Mr. Knecht." The basis for Mr. McAllister's contention is that Mr. Knecht performed his return on equity ("ROE") calculations from the "per books" data the Company is required to file with the Commission rather than from the "adjusted" data that the Company is also required to file. UGI Electric Statement No. 3RJ, at 3. Mr. McAllister continued:

Mr. Knecht states the Company's approximately \$1,000,000 in lost revenue would reduce UGI Electric's ROE by 80 basis points (0.8%). This is simply not correct. A \$1,000,000 erosion in revenues would cause UGI Electric's ROE to fall by approximately 150 basis points, or 1.5%. Measured against UGI Electric's adjusted ROE of 11.55%, the impact of the margin

erosion due to the lost revenue from the EE&C Programs alone, causes the adjusted ROE to fall to 10%.

Id.

For the sake of argument, assume that Mr. McAllister is correct that the calculation of the Company's ROE should be based on the "adjusted" data rather than on the "per books" data. Under Mr. McAllister's calculations, at the end of the Company's three-year EE&C Plan, a loss of distribution revenue caused by conservation would reduce UGI Electric's ROE to 10%. However, as Mr. McAllister admitted during cross examination, if the Company's ROE did drop to 10%, that decline in ROE would *not* be sufficient to trigger a base rate case filing:

Q: What level of return on equity would trigger, and presumably a lower level of return of cost of common equity, would trigger the filing of a UGI base rate case, if you have the expertise to respond to that question? And the authority and the ability.

A: As far as I know, we won't have any set predetermined rate. But if the return on equity on a ratemaking basis would drop in the neighborhood of drop two, roughly around nine and a half percent, all else being equal.

That would send a strong signal for us to begin really considering moving forward with, analyzing all the details and setting up the historic test year future test year, etcetera, to see what indeed the return on equity barometer would be when one factors in all the detailed ratemaking adjustments for rate base revenue expenses.

So once, in my opinion, you get to that nine and a half percent ROE level, that would send a strong signal to start seriously considering the base rate case process.

Transcript, page 109, line 12 to page 110, line 5.

Two salient points are evident from Mr. McAllister's cross examination. First, a 9.5% ROE would be the trigger for the Company's taking action to initiate its next base rate case. However, under Mr. McAllister's worst case scenario, as set forth above, UGI Electric's ROE would only drop to 10%. Second, Mr. McAllister stated that the 9.5% ROE would only cause

the Company “to start seriously considering the base rate process.” *Id.* Considering a base rate case is far from actually making a formal base rate filing. Thus, there is no basis for accepting the Company’s assertion that, without a revenue decoupling mechanism of some type, UGI Electric would have to file a base rate case sooner rather than later.

The Commission should deny the proposed CD Rider, deny UGI Electric any regulatory asset treatment of the reduction in distribution revenues.

2. Elimination or Modification to Fuel Switching Program

The OSBA does not oppose the Company’s proposed fuel switching program *per se*. However, the OSBA is concerned about the use of the Company’s proposed CD Rider coupled with the fuel switching proposal. OSBA witness Mr. Knecht explained the problem, as follows:

UGI Electric’s EE&C Plan contains certain programs which involve fuel switching, including conversion from electric to gas appliances. Such conversions may indeed be consistent with the TRC Test requirements, and may indeed result in net reductions in energy consumption. As such, I do not believe that such programs should be necessarily excluded from an overall EE&C plan.

However, in the case of UGI Electric, any reduction in electric load as a result of conversion to natural gas will involve an increase in natural gas load. An increase in natural gas load will result in an increase in distribution revenues to UGI Electric’s affiliate, UGI Penn Natural Gas (‘PNG’). In effect, a single-issue ratemaking device would be in place to protect UGI Electric from margin losses associated with its EE&C Plan, but there would be no comparable single-issue ratemaking mechanism in effect to recognize the gain in revenues achieved by the Company’s PNG affiliate from that same Plan. Such a result would be unreasonable and inequitable.

OSBA Statement No. 1, at 10-11.

As Mr. Knecht explained, UGI Electric’s fuel switching program would increase the revenues of an affiliated interest, PNG, and decrease the revenues of UGI Electric. Ratepayers

would then be required to make UGI Electric whole through the CD Rider. Rather than a conservation measure, fuel switching would become a profit-maker for the totality of UGI Electric and its affiliates.

As set forth above, the OSBA strongly opposes any form of revenue decoupling. If revenue decoupling (through the CD Rider or the deferred regulatory asset alternative) is eliminated from the Company's proposed EE&C Plan, the OSBA does not object to the inclusion of the UGI Electric's fuel switching proposal.

3. Inclusion of Peak Load Reduction Targets

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

4. Reduction in Total Plan Expenditure Levels

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

5. Recovery of Plan Costs by Customer Class

The *Petition* originally proposed to aggregate all non-residential customers into a single rate class group for cost recovery purposes under the EEC Rider. Obviously, if the Commission adopts the OSBA's position that no cross-subsidies should apply to the non-residential EE&C programs, there is no need for any cost recovery program. Program costs would simply be recovered from participating customers. However, to the extent the Commission does permit the

socialization of non-residential EE&C program costs, Mr. Knecht explained the OSBA's objections to the Company's cost allocation proposal, as follows:

UGI Electric's only rationale for developing rate class groups on this basis is that it is consistent with how rate classes are grouped for purposes of electric default service charges. There is no particular reason that default service groupings should apply for EE&C costing purposes. For a small EDC such as UGI Electric, it may have been necessary to aggregate all non-residential loads in order to make the load large enough to be attractive to bidders in a default service procurement. Moreover, default service customers have an option to bypass default service rates by shopping; no non-residential customers will be able to bypass the EEC Rider charges.

As the Company's response to OSBA-I-11 demonstrates, there are significant differences between smaller non-residential customers served primarily under Tariff Schedules GS-1 and GS-4 and the larger non-residential customers served primarily under Tariff Schedules LP and IH. The vast majority of GS-1, GS-4 and lighting class customer load is related to customers with peak demand below 100 kW. A very large share of LP and IH load is related to customers with peak demand over 100 kW. In fact a majority of the LP and IH load is related to customers with demand over 500 kW.

In addition, UGI Electric's proposed EE&C Plan contains the potential for substantial costs to be incurred related to a very small number of customers in the CHP fuel-switching program. Because it is likely that this program would be targeted at larger customers, it would be inequitable to require smaller non-residential customers to subsidize it. Similarly, it would be inequitable to require larger customers to subsidize programs targeted at smaller customers, such as the office equipment replacement program.

OSBA Statement No. 1, at 11-12 (footnote omitted).

Mr. Knecht concluded with the following recommendation:

[I]f the Commission requires all non-residential customers to bear the costs of the non-residential programs, [I recommend that] those costs be tracked in at least two non-residential rate class groups. Specifically, a large non-residential rate class group would consist of Rate LP and Rate IH load, while a small/medium non-

residential rate class group would comprise the balance of non-residential customers.

Id., at 12.

In his rebuttal testimony, Company witness Mr. McAllister agreed to adopt Mr. Knecht's recommendation:

We agree it is more precise from a rate design perspective and, given that it will not cause an undue administrative burden, we think it is an improvement to the Plan.

UGI Electric Statement No. 3R, at 10.

6. Expansion or Modification of Customer Education

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

7. Funding Percentage for Residential Lighting

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

8. Modification to Commercial Lighting

OCA witness Geoffrey C. Crandall recommended that the Company's proposed EE&C Plan be modified to include various commercial lighting options. *See* OCA Statement No. 1, at 5-6. Mr. Knecht responded with qualified support for the OCA's proposal:

In my direct testimony, I explained why UGI Electric should not offer incentives to non-residential program participants at the expense of non-participants. Such cross-subsidization would violate the basic principles of utility cost allocation, in that costs would be assigned to customers who do not cause those costs to be

incurred. This logic applies to Mr. Crandall's recommendation as well. Therefore, I have no objection to UGI Electric including commercial lighting in its menu of EE&C options, provided that the incentives for participating customers are set to zero.

OSBA Statement No. 2, at 1.

Mr. Knecht continued, as follows:

However, if the Commission determines that cross-subsidization within the EE&C Plan is appropriate, commercial lighting technologies may provide an opportunity for more cost-effective conservation than some of the other programs in the plan. As such, it may be appropriate for UGI Electric to displace some other programs in favor of commercial lighting, while staying within the plan cost cap. However, because Mr. Crandall has not presented any direct evidence regarding the cost-effectiveness of the commercial lighting programs he proposes compared to the programs in the Company's EE&C Plan, it is not clear at this time whether such programs should necessarily be added to the Plan.

In light of this uncertainty, I do not recommend that the Commission preclude UGI Electric from adding commercial lighting programs to its Plan in lieu of some other programs. Nevertheless, I do recommend that UGI Electric be required to demonstrate that doing so is cost-effective. Specifically, if the Company incurs costs related to commercial lighting programs, it should be required to demonstrate in its cost reconciliation proceedings that the commercial lighting programs were more cost-effective than the EE&C programs which were displaced.

Id., at 1-2.

Consequently, to the extent that the Commission approves cross-subsidization of non-residential EE&C program costs, the OSBA does not oppose the OCA's proposal. However, if UGI Electric selects the commercial lighting programs for inclusion in the Company's EE&C Plan, UGI should be required to demonstrate the cost-effectiveness of those lighting programs in comparison to other measures in its Plan.

9. Notice Period for a Change in Plan Rider Charges

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

10. Necessity for a Prudence Review of Plan

As set forth above, both the *Secretarial Letter* and the *Powelson Statement* make it clear that the Commission expects that a small EDC will follow the basic tenets of Act 129, with certain reasonable exceptions.

In regards to the effectiveness of a small EDC's EE&C Plan, the Commission stated, as follows:

Additionally, while the Commission will not at this time establish mandatory energy reduction targets for voluntary EE&C plans, the Commission still has the responsibility to track the cost effectiveness and success of any such plan. As such, the Commission encourages those filing voluntary EE&C plans to use the Act 129 targets as guiding principles in establishing energy consumption and peak demand objectives. A voluntary EE&C plan's energy consumption reduction objective ought to be measured against the filing EDC's annual historical load for June 1, 2007 through May 31, 2008. In addition, a voluntary EE&C plan's peak demand reduction objective ought to be measured against the filing EDC's historical peak load for June 1, 2007 through May 31, 2008. In order to track the progress and success of voluntary EE&C plans, the Commission will require all EDCs filing a voluntary EE&C plan to submit an annual report to the Commission detailing the results of its EE&C plan, its cost effectiveness and any additional information required by this Commission.

The Commission will permit the recovery of all reasonable and prudent costs incurred in implementing and managing a voluntary EE&C plan through a reconcilable adjustment clause under section 1307 of the Public Utility Code, 66 Pa. C.S. § 1307. Again, while the cost limits contained in Act 129 are not applicable to a voluntary EE&C plan, an EDC submitting such a plan must justify the level of expenditures it proposes whether they meet the Act 129 cost limits or not. In addition, the costs must be allocated to the customer rate class that receives the benefit of any particular

EE&C plan measure to avoid inter class cost subsidies. As indicated above, any voluntary EE&C plan filing must contain a section 1307 cost recovery mechanism that will be subject to an annual review and reconciliation at the time of the EE&C plan annual report and may be subject to a Commission audit.

Secretarial Letter, at 2.

UGI Electric is not subject to the mandatory targets and penalties that Act 129 imposes on larger EDCs. Consequently, OSBA witness Mr. Knecht recommended that, if the Commission approves the recovery of non-residential EE&C program costs from non-participating customers, a rigorous review of the Company's EE&C Plan performance be required as a substitute for those strictures. Mr. Knecht explained, as follows:

[W]ith respect to penalties, it would be difficult to adopt Act 129 load and peak reduction targets for UGI Electric, due to timing differences between the UGI Electric Plan and the plans of the other EDCs. Therefore, in lieu of penalties, a rigorous *ex post* prudence review should serve as a proxy. Specifically, UGI Electric should be required to demonstrate in each annual review of the Plan's performance that the overall cost-effectiveness of its load reductions is comparable to that achieved by the larger EDCs. To the extent that the programs do not meet this cost-effectiveness standard, excess costs should be subject to exclusion from the EEC Rider cost basis.

OSBA Statement No. 1, at 9.

All of the large EDCs' EE&C Plans are based on spending the money of both participating and non-participating ratepayers in order to provide incentives for a sufficient number of customers to reduce their loads or their peak usage. However, the large EDCs have a financial incentive of their own to spend ratepayers' money prudently. Specifically, if they fail to spend ratepayers' money in a cost-effective manner, the EDCs are at risk of missing the load and peak reduction targets set by Act 129. EDCs that miss those targets are subject to a penalty of a minimum of \$1 million to a maximum of \$20 million. EDCs are explicitly prohibited from

recovering any such penalties from their ratepayers. *See* 66 Pa. C.S. §2806.1(f)(2). In contrast, UGI Electric would spend ratepayers' money but would not be subject to load and peak reduction targets and would not be subject to penalties financed by stockholders. As a result, UGI Electric would not have the same incentive as large EDCs to design and operate the EE&C Plan in the most cost-effective manner possible. *See* OSBA Statement No. 1, at 3-4.

As explained in the following section of this Initial Brief, the elimination of ratepayer-financed subsidies for non-residential customers to participate in specific conservation measures would mitigate the OSBA's concerns about the cost-effectiveness of UGI Electric's EE&C Plan. However, if the Commission approves UGI Electric's proposed reliance on subsidies, the potential denial of recovery of costs which are not reasonable and prudent would provide a financial incentive for the Company to spend ratepayer-provided funds in a cost-effective manner. Therefore, the Commission should order an *ex post* prudence review of costs as part of the annual review and reconciliation of UGI Electric's EE&C Plan contemplated by the *Secretarial Letter*.

In response to Mr. Knecht's recommendation for an *ex post* prudence review, UGI Electric witness Paul H. Raab stated, as follows:

Finally, his third recommendation [Mr. Knecht's *ex post* prudence review] unilaterally imposes an additional burden upon UGI Electric that has not been imposed upon any other EDC and the value of which has not been evaluated by any party or the Commission. If it is the Commission's intention to guarantee that no other EDCs files voluntary plans, then it may be appropriate to impose additional burdens upon them. However, this does not seem consistent with the goal of encouraging broad-based energy efficiency investments by small EDCs.

UGI Electric Statement No. 2R, at 6-7.

Mr. Knecht responded to Mr. Raab, as follows:

The objective of this recommendation was to serve as a substitute for the Act 129 penalties which apply to larger EDCs if they fail to meet targeted load and peak demand reductions. If Mr. Raab is suggesting that UGI Electric would prefer to face the same penalties as other EDCs if it fails to meet the reductions mandated by Act 129, I would understand his complaint. However, as UGI Electric has not proposed that it be subject to the same penalties as other EDCs, it would not be unreasonable for the Commission to require UGI Electric to demonstrate that its Plan is as cost-effective as those of the other EDCs.

Moreover, I am informed by OSBA counsel that Section 2806.1(i)(1)(iii) of the Public Utility Code requires that each large EDC's annual report include an evaluation of the cost-effectiveness of the EE&C expenditures. Since the other EDCs are subject to this requirement, it would not be an unreasonable burden to require UGI Electric to make a similar demonstration, and to compare the effectiveness of its own program with those of the other EDCs.

OSBA Statement No. 3, at 5-6.

Simply put, an *ex post* prudence review would be a reasonable and valuable tool for the evaluation of the effectiveness of any EE&C Plan submitted by a small EDC. The *ex post* prudence review is a reasonable substitute for the penalties which are not imposed upon EDCs like UGI Electric, but which are imposed upon larger EDCs by Act 129.

11. Applicability of the Plan to Small Business Customers

All of the EDC EE&C Plans submitted to date have included incentive plans to get the EDC's customers to adopt the various conservation measures. OSBA witness Mr. Knecht explained the rationale for these incentives, as follows:

It is conventional wisdom that customers will not make conservation investments without such incentives, even if such investments are in their economic interests as determined by the specific economic parameters in the TRC Test and the Commission's Technical Resource Manual ('TRM'). Many factors may contribute to this observed result, including customer

ignorance, customer inability to finance equipment replacement, a higher cost of capital for customers than for the utility, landlord-tenant issues, and customer skepticism about the actual effectiveness of various conservation measures.

OSBA Statement No. 1, at 7.

In regard to this proceeding, Mr. Knecht recommended that no subsidies be provided for the non-residential customers of UGI Electric. Mr. Knecht stated, as follows:

It must be recognized that a subsidy program conflicts with the most basic principle of utility cost allocation and rate design, namely that the customer who causes the cost to be incurred should pay for the cost. In this case, the customer who desires to implement an energy conservation measure, and who in fact receives a very attractive benefit from that conservation measure, should pay for it.

* * *

I recommend that the cost of the non-residential programs be fully borne by program participants, and that the non-residential EEC Rider charge be set to zero. Based on the calculations prepared by the Company, the participants in the programs should obtain benefits that exceed their costs; there is no need for customers who either cannot adopt these efficiency measures or have already done so to provide subsidies.

Id.

Removing the subsidies from the non-residential customers would have a positive effect on the cost-effectiveness of UGI Electric's EE&C Plan. Mr. Knecht observed, as follows:

For non-residential customers, the approach I am recommending would certainly establish an incentive for UGI Electric to be efficient with its plan expenditures. Because it could recover costs only from plan participants, UGI Electric would surely strive to focus on the most cost-effective plan options, and to keep program and administrative costs to a minimum.

Id., at 7-8.

Eliminating the subsidies for the non-residential EE&C measures would leave UGI Electric with a viable EE&C Plan for its non-residential customers. As Mr. Knecht pointed out, the Company's own calculations demonstrate that any non-residential participants in the various EE&C programs should see benefits that are greater than their costs. OSBA Statement No. 1, at 7. In addition, Mr. Knecht observed, as follows:

UGI Electric's filing did not indicate that the Company already has an EE&C Plan targeted at non-residential customers, and my proposal would not stop the Company from implementing such a Plan. As the incumbent utility, UGI Electric would certainly have advantages over other energy service companies, in that it has established business relationships with its customers and it has strong name recognition, which presumably inspire confidence on the part of customers. I propose only that UGI Electric operate under the same restrictions that other energy service companies face, namely that it not be allowed to cross-subsidize energy conservation programs. As I demonstrate in my direct testimony, I make this recommendation because these programs need no cross-subsidy to be economically beneficial for the Plan participant.

OSBA Statement No. 3, at 5.

Furthermore, the Company has a variety of options without providing a subsidy for its non-residential EE&C Plan measures. Mr. Knecht stated:

To the extent that UGI Electric believes that the factors I identify above preclude customers from 'doing the right thing,' there are a variety of approaches other than a cross-subsidy that could mitigate these problems, such as utility loans, appliance rental programs, etc.

OSBA Statement No. 1, at 7.

Therefore, the OSBA recommends that the Company's EE&C Plan be modified to remove the program subsidies for the non-residential customer classes. Simply put, those non-residential customers who can pay for (and will benefit from) the conservation measures should do so. The other non-residential customers should not be forced to subsidize those participants.

12. Expansion to include solar thermal and/or other Tier I resources

The OSBA takes no position on this issue. The OSBA reserves the right to respond to other parties in regards to this issue in its Responsive Brief.

13. Other Modifications

The OSBA has no additional modifications to propose at this time. The OSBA reserves the right to respond to other parties' proposals in its Responsive Brief.

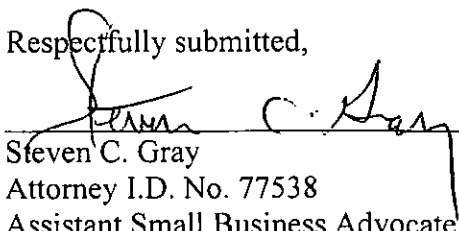
V. CONCLUSION

For the reasons set forth herein, the OSBA respectfully requests that the Commission deny the *Petition* unless revenue decoupling, *i.e.*, both the CD Rider and the alternative of deferred regulatory asset treatment, is eliminated from the EE&C Plan.

If the Commission approves the Company's EE&C Plan (with or without revenue decoupling), the OSBA respectfully requests that the Plan be modified to eliminate the ratepayer-funded subsidies for participating non-residential customers.

If the Commission approves the socialization of costs related to non-residential EE&C programs by allowing recovery of those costs from non-participants (which it should not do), the OSBA respectfully requests that the Commission impose an *ex post* prudence review of the Plan's costs.

Respectfully submitted,



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Dated: June 2, 2011

Appendices

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Proposed Findings of Fact

1) UGI Electric is an EDC with 62,000 customers. *Petition*, at 2, paragraph 4.

2) UGI Electric voluntarily filed this *Petition*. *Petition*, at 1.

3) UGI Electric proposed the CD Rider, which is an adjustment mechanism that would automatically increase the Company's distribution rates for margins that are theoretically lost as a result of deemed reductions in consumption associated with the proposed EE&C Plan. OSBA Statement No. 3, at 1.

4) The reductions in consumption would be determined by UGI Electric based on the specific conservation measures adopted, and by the technical parameters embedded in the TRM or other sources. OSBA Statement No. 3, at 1.

5) Because UGI Electric is not subject to the penalties set forth in Act 129 which apply to EDCs that do not meet certain energy and peak demand reduction targets and because UGI Electric is not subject to the spending limits set forth in Act 129, the Company has an inadequate incentive to be efficient with program costs, particularly if its proposed CD Rider mechanism is adopted. OSBA Statement No. 1, at 3-4.

6) The fundamental principle of the TRC Test is that the total costs that are avoided by the conservation program exceed, in present value terms, the total program costs incurred. OSBA Statement No. 1, at 4-6.

7) Because the rates paid by UGI Electric's customers for generation, transmission and distribution are primarily based on per-kWh energy charges, it is likely

that the benefit to a program participant is actually greater than that implied by the TRC Test. OSBA Statement No. 1, at 4-6.

8) The CD Rider represents single-issue ratemaking because it applies to only one type of conservation program (but excludes all other conservation programs, including those undertaken by customers themselves) and excludes the impact from all other types of load changes. OSBA Statement No. 1, at 10.

9) UGI Electric's regulatory asset proposal has the same single-issue ratemaking problem as the CDR. The regulatory asset proposal would compensate UGI Electric for any deemed loss of distribution revenue margins associated with the EE&C Plan, but would not permit offsetting adjustments to be considered. OSBA Statement No. 3, at 3.

10) UGI Electric has not filed a base rate case since 1995 (adjudicated in 1996), at Docket No. R-00953534. OSBA Statement No. 3, at 2.

11) UGI Electric's reported per books return on common equity was 13.08 percent for the 12 months ending December 31, 2010. OSBA Statement No. 3, at 2.

12) Under UGI Electric's proposed fuel switching plan, any reduction in electric load as a result of conversion to natural gas will involve an increase in natural gas load to UGI Electric's affiliate, UGI Penn Natural Gas. OSBA Statement No. 1, at 10-11.

13) The OCA proposed to add commercial lighting programs to UGI Electric's EE&C Plan in lieu of some other programs. OSBA Statement No. 2, at 1-2.

14) An *ex post* prudence review of UGI Electric's EE&C Plan is a reasonable substitute for the mandated load reductions, penalties, and budget cap that Act 129 applies to large EDCs. OSBA Statement No. 1, at 9.

15) The elimination of the proposed subsidies to non-residential customers for participating in EE&C measures would require UGI Electric to focus on the most cost-effective plan options and to keep program and administrative costs to a minimum. OSBA Statement No. 1, at 7-8.

16) UGI Electric's non-residential EE&C Plan measures do not require subsidies in order to make those measures economically attractive to participating customers. OSBA Statement No. 1, at 7.

17) On December 23, 2009, the Commission issued a Secretarial Letter at Docket No. M-2009-2142851 addressing the question of the filing of EE&C Plans by small EDCs on a voluntary basis. *Voluntary Energy Efficiency and Conservation Program*, Docket No. M-2009-2142851 (*Secretarial Letter* of December 23, 2009).

18) In a statement that accompanied the *Secretarial Letter*, Commissioner Robert F. Powelson (now the Chairman) observed that "these EDCs should only file plans if, after careful scrutiny, it is determined that doing so is in the best interest of their customers." Statement of Chairman Robert F. Powelson, Docket No. M-2009-2142851 (Dated December 17, 2009).

19) UGI Electric has agreed that if the Commission requires all non-residential customers to bear the costs of the non-residential programs, those costs shall be tracked in two non-residential rate class groups. One group would consist of Rate LP and Rate IH customers, while another group would consist of the remaining small/medium non-residential customers. UGI Electric Statement No. 3R, at 10.

Proposed Conclusions of Law

- 1) Act 129 requires each EDC with at least 100,000 customers to develop and file an EE&C Plan with the Commission for approval.
- 2) Section 2806.1 of the Public Utility Code, 66 Pa. C.S. § 2806.1, requires that each EE&C Plan include a variety of EE&C measures to reduce overall and peak load consumption. Section 2806.1 also requires that each measure be financed by the customer class that receives the direct energy and conservation benefit of that measure.
- 3) Section 2806.1(1) of the Public Utility Code, 66 Pa. C.S. § 2806.1(1), specifically exempts EDCs with fewer than 100,000 customers from the requirements of Act 129.
- 4) As set forth in the *Secretarial Letter*, voluntary plans filed by small EDCs are to be consistent with Act 129.
- 5) Section 2806.1(k)(1) of the Public Utility Code, 66 Pa. C.S. § 2806.1(k)(1), provides for an EDC's full recovery of the "reasonable and prudent" costs of that EDC's EE&C Plan.
- 6) Section 2806.1(k)(2) of the Public Utility Code, 66 Pa. C.S. § 2806.1(k)(2), prohibits the recovery of distribution revenue margins lost because of a conservation-related decline in sales, *i.e.*, revenue decoupling..
- 8) Section 2806.1(k)(3) of the Public Utility Code, 66 Pa. C.S. § 2806.1(k)(3) allows an EDC to seek to avoid distribution revenue margin losses prospectively by reflecting any anticipated conservation-related sales decline in the forecast used to calculate the revenue requirement in its next distribution base rate case.

9) Section 332(a) of the Public Utility Code, 66 Pa. C.S. § 332(a), and Section 315(a) of the Public Utility Code, 66 Pa. C.S. § 315(a), place the burden of proving that the EE&C Plan is just, reasonable, and in conformance with the *Secretarial Letter* upon UGI Electric.

10) UGI Electric has failed to meet its burden of proving that its EE&C Plan, as filed, is just, reasonable, and in conformance with the *Secretarial Letter*.

Proposed Ordering Paragraphs

IT IS RECOMMENDED:

- 1) That UGI Electric's *Petition* shall be approved with the following modifications:
 - a. That no revenue decoupling mechanism, including the proposed CD Rider and the alternative regulatory asset proposal, shall be part of UGI Electric's EE&C Plan; and
 - b. That the non-residential customers of UGI Electric shall not subsidize any EE&C measures provided for in UGI Electric's EE&C Plan.
- 2) If the Commission requires all non-residential customers to bear the costs of the non-residential programs:
 - a. That the Commission shall conduct an annual *ex post* prudence review of UGI Electric's EE&C Plan; and
 - b. That the non-residential program costs shall be tracked in two non-residential rate class groups. One group would consist of Rate LP and Rate IH customers, while another group would consist of the remaining small/medium non-residential customers.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

UGI Utilities, Inc. - Electric Division :
Energy Efficiency and Conservation Plan : Docket No. M-2010-2210316

CERTIFICATE OF SERVICE

I certify that I am serving two copies of the Main Brief, on behalf of the Office of Small Business Advocate, by e-mail and first-class mail (unless otherwise noted) upon the persons addressed below:

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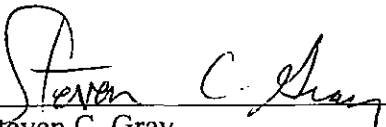
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