PECO ENERGY COMPANY
STATEMENT NO. 4

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

ENERGY EFFICIENCY AND CONSERVATION PROGRAM

DOCKET NO. M-2015-

DIRECT TESTIMONY
SUPPORTING PECO'S PETITION FOR APPROVAL
OF ITS PHASE III EE&C PLAN

WITNESS: RICHARD A. SCHLESINGER

SUBJECT: COST RECOVERY

DATED: NOVEMBER 30, 2015

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DIRECT TESTIMONY
OF
RICHARD A. SCHLESINGER

I. INTRODUCTION AND PURPOSE OF TESTIMONY

1. Q. Please state your full name, professional position, and business address.

A. My name is Richard A. Schlesinger. I am Manager of Retail Rates in the Regulatory Policy and Strategy Department for PECO Energy Company ("PECO" or the "Company"). My business address is PECO Energy Company, 2301 Market Street, Philadelphia, Pennsylvania 19103.

2. Q. Please describe your educational background.

A. I have a Bachelor of Science Degree in Engineering from Widener University. In addition, I have a Master's Degree in Business Administration from Saint Joseph's University.

3. Q. Please describe your work experience in the energy industry.

A. I was hired in 1986 by PECO as a System Engineer in the Plant Operations group supporting the Limerick Nuclear Generating Station. From 1988 to 1991, I held several positions of increasing responsibility supporting plant operations, management, and quality assurance. In 1992, I transferred into the position of Rate Engineer in the Rates and Regulatory Affairs Group. In 1997, I was appointed to the position of Project Manager, Customer Choice Implementation, and was responsible for many regulatory activities related to the phase-in of electric and gas retail choice for all of PECO's two million electric and gas distribution customers. In 2000, I transferred to the Company's Customer and Marketing Services Department and served as e-Commerce Manager and then as Project Manager, overseeing various Business/Information Technology system implementations. In 2004, I returned to the Regulatory and External Affairs Department, where I served as Principal Rate Administrator. In 2009, I was promoted to my current position – Manager of Retail Rates. In this role, I have primary management and oversight responsibility for PECO's electric and gas service tariffs, as well as overseeing numerous filings with the Pennsylvania Public Utility Commission (the "Commission").

4. Q. Mr. Schlesinger, have you submitted testimony previously before the Commission?

A. Yes. I submitted testimony in support of PECO's Phase I Energy Efficiency and Conservation ("EE&C") Plan[1] and PECO's Phase II EE&C Plan.[2] In addition, I submitted testimony in support of the Company's Market Rate Transition Energy Efficiency Package[3] and its Residential Real-Time Pricing Program.[4] Finally, I recently submitted testimony in support of PECO's 2015 Electric Distribution Rate Case.[5]

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1 *Petition of PECO Energy Company for Approval of its Act 129 Energy Efficiency and Conservation Plan and Expedited Approval of its Compact Fluorescent Lamp Program*, Docket No. M-2009-2093215.

2 *Petition of PECO Energy Company for Approval of its Act 129 Phase II Energy Efficiency and Conservation Plan,* Docket No. M-2012-2333992.

3 *Petition of PECO Energy Company for Approval of its Market Rate Transition Energy Efficiency Package*, Docket No. P-2008-2062740.

4 *Petition of PECO Energy Company for Approval of Phase I of its Residential Real-Time Pricing Program*, Docket No. P-2008-2032333.

5 *Pa. P.U.C. v. PECO Energy Company – Electric Division*, Docket No. P-2015-2468981.

5. Q. What is the purpose of your direct testimony?

A. I am sponsoring a supplement to PECO's Electric Service Tariff bearing a proposed effective date of June 1, 2016, which contains provisions designed to implement PECO's proposed Phase III EE&C Plan Charge ("Phase III EEPC"). Accordingly, my testimony: (1) describes PECO's Phase III EEPC, which is the rate adjustment mechanism the Company proposes to establish under Section 1307 of the Pennsylvania Public Utility Code[6] to recover the costs associated with the Company's Phase III EE&C Plan; (2) identifies the categories of PECO's Phase III EE&C Plan costs that the Phase III EEPC will recover; and (3) provides the Company's current estimates of its Phase III Plan costs. In addition, I will describe how PECO's rates will be adjusted annually over the term of its Phase III EE&C Plan to reflect over-or under-recoveries and how PECO's currently-effective EEPC, which recovers the costs of PECO's Phase II EE&C Plan ("Phase II EEPC"), and its proposed Phase III EEPC will be combined into a single surcharge.[7] I will also discuss how PECO will transition from its Phase II EEPC to its proposed Phase III EEPC and how it proposes to reconcile costs and revenues. Finally, I will describe how the Company will separate costs incurred and EEPC revenues billed with respect to its Phase III EE&C Plan from costs incurred and EEPC revenues billed with respect to its Phase I EE&C Plan and its Phase II EE&C Plan.

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[6] Hereafter, unless specifically stated otherwise, all section references are to the Pennsylvania Public Utility Code.

[7] As required by the Commission's Final Order in *Petition of PECO Energy Company for Approval of its Act 129 Phase II Energy Efficiency and Conservation Plan* entered on February 28, 2013, at Docket No. M-2012-2333992 (p. 45), PECO's currently-effective Phase II EEPC also recovers the remaining balances of PECO's unrecovered Phase I EE&C Plan costs.

6. Q. Have you prepared any exhibits to accompany your testimony?

A. Yes, I have prepared four exhibits, which consist of the following:

Exhibit RAS-1 –	Proposed supplement setting forth revisions to PECO's Electric Service Tariff (Clean and Redline).
Exhibit RAS-2 –	Program costs by rate class.
Exhibit RAS-3 –	Calculations of the cost recovery charges by rate class for the first year of PECO's Phase III EE&C Plan.
Exhibit RAS-4 –	Responses to the Commission's filing requirements at 52 Pa. Code § 53.52.

II. PECO'S PROPOSED METHOD OF COST RECOVERY

7. Q. Do the EE&C provisions of Act 129 of 2008 ("Act 129")[8] and the Commission's Phase III Implementation Order[9] grant an electric distribution company ("EDC") the right to recover the costs of its EE&C plan?

A. Yes, they do. Act 129 added Section 2806.1, which provides that EDCs are entitled to recover all reasonable and prudent EE&C plan costs, on a full and current basis, through a cost-recovery mechanism established under Section 1307.[10] The Commission previously directed EDCs to develop separate cost recovery mechanisms for their Phase II EE&C Plans and also required that the cost recovery mechanism be non-bypassable and that it not affect the EDCs' prices-to-compare.[11]

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8 66 Pa. C.S. § 2806.1, et seq.

9 Implementation Order, *Energy Efficiency and Conservation Program*, Docket No. M-2014-2424864 (Order entered June 19, 2015) ("*Phase III Implementation Order*").

10 66 Pa. C.S. § 2806.1(k).

11 *See* Implementation Order, *Energy Efficiency and Conservation Program*, Docket No. M-2012-2289411 (Order entered August 3, 2012) ("*Phase II Implementation Order*")

8. Q. Please explain the mechanism that PECO is proposing to recover Phase III Plan costs.

A. Consistent with the authority granted by Section 2806.1(k) and the *Phase II Implementation Order*, PECO's Phase III EEPC will be a fully reconcilable, non-bypassable charge. The Phase III EEPC is designed to adjust customers' distribution rates by the amount of the charge calculated for each rate class and, as a result, PECO's price-to-compare will not be affected by the recovery of Phase III EE&C Plan costs. The Phase III EEPC follows the same format the Company used for its currently-effective, Commission-approved Phase II EEPC, which, as previously noted, recovers costs associated with PECO's Phase II EE&C Plan.

Exhibit RAS-1 is a pro forma supplement, in both clean and redlined versions, to PECO's Electric Service Tariff that sets forth the revisions to PECO's currently effective Electric Service Tariff needed to implement PECO's Phase III EEPC and, therefore, reflects changes with respect to the cost recovery method, the formula for calculating the Phase III EEPC charge and the Phase III EEPC charges specific to each rate class. All of the rate schedules setting forth distribution rates that would have to be adjusted to reflect the Phase III EEPC are also included in the proposed tariff supplement provided as Exhibit RAS-1. However, PECO will submit the final distribution rates in a compliance filing after its Phase III EE&C Plan and Phase III EEPC are approved.

9. Q. What categories of costs will be recovered under the Phase III EEPC?

A. The Phase III EEPC will recover all of the fixed capital costs (depreciation and pre-tax return) and operating expenses, not otherwise recovered in base rates, to design and implement the EE&C programs incorporated in its Phase III EE&C Plan. These costs include, among others, the cost of information technology ("IT") needed to design and implement the EE&C programs; the costs of customer outreach and program promotion; incremental labor costs incurred to manage and administer the EE&C programs on an ongoing basis; the cost to measure and verify EE&C program results; and the cost of incentives offered to customers to participate in the approved EE&C programs.[12]

10. Q. Will the Phase III EEPC recover any capital expenditures?

A. The Company will incur certain IT costs to implement the Phase III Plan that must be capitalized for financial accounting purposes and will be depreciated over the service life of the property, which will correspond to the five-year term of PECO's Phase III EE&C Plan. Accordingly, PECO proposes to include as recoverable costs in its Phase III EEPC the annual depreciation of this property and a pre-tax return on the depreciated original cost at PECO's weighted cost of capital, as permitted by the *Phase III Implementation Order* (p. 132).[13]

12 *See Phase III Implementation Order*, p. 132.

13 PECO proposes to calculate its weighted average cost of capital in the same manner specified by the Commission in the Final Implementation Order, *Implementation of Act 11 of 2012*, Docket No. M-2012-2293611 (Order entered August 2, 2012), pp. 30-31 and Appendix A, Section 2.B.2.

11. Q. What are the Company's budgeted expenditures for its Phase III Plan?

A. As explained in Section 7 of PECO's Phase III EE&C Plan, which is being submitted as PECO Exhibit 1 accompanying the Petition Of PECO Energy Company For Approval Of Its Phase III Energy Efficiency And Conservation Plan, consistent with the cost limitation imposed by Section 2806.1(g), the Company's budgeted Phase III expenditures total $427.4 million for the five-year term of the Plan. The Company projects that its budgeted expenditures by rate class will be as follows:

Residential	$202.3 million
Small Commercial and Industrial ("SC&I")	$70.9 million
Large Commercial and Industrial ("LC&I")	$153.8 million
Municipal Lighting ("ML")	$0.4 million
Total	$427.4 million

Exhibit RAS-2 contains a summary of the projected expenditures by class for all of the programs in the Phase III EE&C Plan.

12. Q. How will Statewide Evaluator ("SWE") costs be handled?

A. The *Phase III Implementation Order* (p. 95) requires PECO to remove the SWE costs from its EE&C Phase III budget. (The same requirement was imposed for purposes of EDCs' Phase I and Phase II EE&C Plans, as well.)[14] Accordingly, PECO has not included SWE costs in its Phase III Plan budget. PECO will track Phase III SWE costs separately from its Phase III EE&C Plan costs and, as permitted by the *Phase III Implementation Order*,[15] will recover both categories of costs through its Phase III EEPC. Because the Phase III SWE has not yet been selected, the Company is using

[14] *See* Implementation Order, Energy Efficiency and Conservation Program, Docket Nos. M-2012-2289411 and M-2008-2069887 (Order entered August 3, 2012) ("*Phase II Implementation Order*")

[15] *See Phase III Implementation Order*, p. 95.

estimated SWE costs for the five-year term of the Phase III EE&C Plan (approximately $4.5 million) as a placeholder for the actual Phase III SWE costs. More up-to-date projected Phase III SWE costs will be included in a compliance filing after the Phase III Plan is approved.

13. Q. What is the cost recovery period and when will it begin?

A. The cost recovery period will begin when bills are sent to customers during July 2016 for June 2016 usage and will continue through bills sent to customers in June 2021 for May 2021 usage. There will be a final "true-up" to the actual EE&C Plan costs at the end of the recovery period, and any over- or under-collection will then be refunded or recouped, as applicable, without interest, over a twelve-month period following the completion of Phase III.

14. Q. How will the Company ensure that its Phase III EEPC recovers the cost of particular programs from the classes of customers that will receive the benefits those programs provide?[16]

A. The programs included in PECO's Phase III EE&C Plan are designed such that the cost of each program is directly assigned to the customer class that will receive the benefits of that program. For programs that provide benefits to more than one class, costs will be allocated using reasonable and generally accepted cost-of-service principles. Support Services costs ("common costs") will be allocated using the same method employed to allocate such costs for purposes of PECO's Phase I and Phase II EE&C Plans. Specifically, that method will allocate Support Service costs to each

[16] *See Phase III Implementation Order*, p. 130.

rate class in proportion to the non-Support Service expenditures for each rate class under the Phase III Plan. The same allocation method will be used for R&D costs. The total projected costs of each program for the five-year Phase III EE&C Plan term, by rate class, are shown in Exhibit RAS-2, page 1 of 2.

15. Q. Have you developed proposed charges for the Phase III EEPC for each customer class?

A. Yes, I have developed charges under the Phase III EEPC based on the total projected program costs to be incurred for each rate class for the first year of the Phase III EE&C Plan ("Program Year 8" or "PY8"). To develop the charge for each rate class, the total projected program costs to be incurred for that class for PY 8 (see Exhibit RAS-2, pages 2 of 2) was divided by the appropriate projected class billing units (e.g. kilowatt hours of energy use or kilowatts of demand) for the period from June 1, 2016 through May 31, 2017. In addition, as described previously, although the Phase III SWE costs will be tracked separately from the Phase III Plan costs, they are included for recovery under the Phase III EEPC. The resulting charges were then grossed up to provide for recovery of Pennsylvania Gross Receipts Tax. This calculation produces a charge designed to recover the total program costs for PY 8. Exhibit RAS-3 contains the detailed calculations for the development of the charges for each class.

16. Q. Are there any differences between the Phase II and Phase III EEPCs?

A. Yes. The *Phase III Implementation Order* requires changes to the EEPC from the terms of the EEPC approved in the *Phase II Implementation Order*. These include:

(1) requiring Phase III charges to be calculated to recover project program costs and be adjusted annually to reflect over- or under-recoveries; (2) requiring the Phase II and III EEPCs to be combined into a single charge set forth in a single tariff provision; and (3) changing the manner in which the transition will occur from the Phase II EEPC to the Phase III EEPC.

17. Q. Please explain the annual calculation and adjustment of Phase III EEPC charges.

A. In the *Phase III Implementation Order* (pp. 146 and 149), the Commission required the charge to be developed using "projected program costs" and not "the authorized budget amount" because "[t]he development of the surcharge using the projected program costs rather than the authorized budget amount would mitigate over- or under-recoveries of costs during the surcharge application period." Additionally, in that Order (p. 149), the Commission required "each EDC to annually reconcile (i.e., 1307(e) Statement) actual expenses incurred with actual revenues received for the reconciliation period." Accordingly, for the first year of the Phase III EE&C Plan (PY8), which runs from June 1, 2016 through May 31, 2017, PECO will develop EEPC-adjusted rates based on projected Plan costs it anticipates will be incurred over that year. Thereafter PECO will reset the charge annually to recover the projected Plan costs for the then-upcoming plan year and the appropriate adjustment to reconcile and true-up revenues and the previous program years' actual costs.

18. Q. How does PECO propose to combine the Phase II and III EEPCs into a single charge?

A. The *Phase III Implementation Order* states that "[t]he Commission agrees with PECO, PPL and FirstEnergy that the Phase II and Phase III surcharges should be combined into a single surcharge and tariff with the Implementation of Phase III" (p. 149). Accordingly, PECO proposes to combine its Phase II EEPC and Phase III EEPC into a single surcharge and a single tariff provision with the implementation of its Phase III EEPC.

19. Q. What does the Phase III Implementation Order provide with regard to the transition from the Phase II EEPC to Phase III EEPC?

A. In the *Phase III Implementation Order* (pages 146-149) the Commission adopted a plan for the transition from the cost recovery methodology utilized during Phase II, ending May 31, 2016, to the cost recovery methodology to be utilized during Phase III, beginning on June 1, 2016. The plan requires that each EDC reconcile its total actual recoverable EE&C Plan expenditures incurred through March 31, 2016, with its actual EE&C Plan revenues received through March 31, 2016. In addition, each EDC should include, as part of the calculation of the Phase III rates to become effective June 1, 2016, as clearly identified separate line items, projections of the: expenses to finalize any measures installed and commercially operable on or before May 31, 2016; expenses to finalize any contracts; and other Phase II administrative obligations. The Phase II rate that became effective June 1, 2015 will remain effective through May 31, 2016. Consistent with the transition requirements, for PY8

(June 1, 2016 through May 31, 2017), PECO's cost recovery rates will be calculated based on the projected total program expenditures for each rate class for PY8 plus the reconciliation amount for PY7 (June 1, 2015 through March 31, 2016) and any costs remaining from previous periods. As previously explained, for each subsequent Plan year, PECO will develop annual Phase III recovery rates based on its projected program expenditures for that plan year plus amounts necessary for the reconciliation of costs and revenues from prior periods.

20. Q. What has the Commission directed regarding the application of interest to any Phase II and Phase III over- and under-recoveries?

A. In the *Phase III Implementation Order* (pages 146-149), the Commission addresses the application of interest to Phase II and to Phase III over- and under- recovered amounts. They concluded that interest should not be included on any Phase II or Phase III net over- or under-recovery amounts. The Phase III EEPC as described in Exhibit RAS-1 does not include the application of interest. In addition, the EEPC reflects the other provisions that I previously explained (i.e., annual calculation and adjustment, the application of a single charge and the transition plan) in order to ensure that the EEPC complies with the Commission's directives on cost recovery.

III. SEPARATE ACCOUNTING FOR COSTS INCURRED AND EEPC REVENUES BILLED FOR PHASE III AND PREVIOUS PHASES

21. Q. What has the Commission directed regarding accounting for costs to be incurred and EEPC revenues to be billed for Phase III and such costs and revenues associated with prior Phases?

A. On September 22, 2015, the Commission issued a Secretarial letter captioned *Re: Implementation of Act 129 of 2008 – Phase III Energy Efficiency and Conservation Plan Template* at Docket No. M-2014-2424864. In that Secretarial letter, the Commission stated that EDCs must account for Phase III costs and revenues separately from the costs and revenues associated with prior Phases.

22. Q. Please explain how the Company intends to comply with the Commission's accounting requirements.

A. PECO will comply with the Commission's directive to separately account for Phase III costs and revenues by setting up new general ledger accounts for Phase III costs and revenues. Phase I and Phase II costs and revenues are currently tracked through similar, separate accounting measures. Thus, there will be no comingling of Phase III and prior Phase costs or revenues in PECO's accounting records. Phase I and Phase II costs and revenues will also be clearly identified and tracked separately for purposes of the EEPC. This will allow Phase III costs to be reconciled against Phase III revenues billed under the EEPC as explained in the pro forma tariff supplement provided as Exhibit RAS-1.

23. Q. How will any Phase I and Phase II over- or under-collection balances be treated with the start of Phase III?

A. In accordance with the reconciliation method approved for use in conjunction with PECO's Phase I EE&C Plan, over- and under-recoveries from the period January 1, 2009 through May 31, 2013 were trued-up (i.e., refunded or recouped, as applicable) during the period June 1, 2013 through April 30, 2014. However, a small balance remained after the Phase I reconciliation, which PECO still needs to refund to or recoup from customers. This will be accomplished as part of the charges to be implemented during the first year that PECO's Phase III EEPC is in effect (PY8). In addition, in accordance with the Commission-approved method for reconciling costs and revenues for PECO's Phase II EE&C Plan, PECO will refund or recoup, as applicable, over- or under-recovery balances from Phase II as part of the EEPC charges to be implemented during PY8. The Phase I and Phase II balances are included as separate line items in the calculation of the cost recovery rates, as shown in Exhibit RAS-3.

IV. CONCLUSION

24. Q. Does this conclude your direct testimony?

A. Yes, it does.