

COMMONWEALTH OF PENNSYLVANIA



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September 7, 2018

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Bldg.
400 North Street
Harrisburg, PA 17120

Re: Pennsylvania Public Utility Commission
v.
PECO Energy Company – Electric Division
Docket No. R-2018-3000164

Dear Secretary Chiavetta:

Attached for electronic filing please find the Office of Consumer Advocate's Main Brief in the above-referenced proceeding.

Copies have been served per the attached Certificate of Service.

Respectfully Submitted,

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cc: Honorable Christopher P. Pell, ALJ
Honorable F. Joseph Brady, ALJ
Certificate of Service

*257296

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Pennsylvania Public Utility Commission :
 :
 v. : Docket No. R-2018-3000164
 :
 PECO Energy Company :

I hereby certify that I have this day served a true copy of the following document, the Office of Consumer Advocate’s Main Brief, upon parties of record in this processing in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

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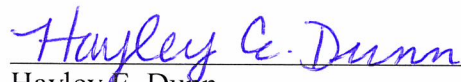
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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission :
v. : Docket No. R-2018-3000164
PECO Energy Company :

MAIN BRIEF OF THE
OFFICE OF CONSUMER ADVOCATE

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Dated: September 7, 2018

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I. INTRODUCTION AND PROCEDURAL HISTORY

A. Background

PECO is engaged in the business of providing electric distribution service to approximately 1.6 million residential, commercial, and industrial customers in southeastern Pennsylvania in all or parts of Bucks, Chester, Delaware, Montgomery, Philadelphia, and York Counties. On March 29, 2018, PECO Energy Company (PECO or the Company) filed with the Pennsylvania Public Utility Commission (Commission) Tariff Electric – Pa. P.U.C. No. 6 (Supplement No. 6) to become effective on May 28, 2018. In its filing, PECO proposed to increase its electric distribution rates by \$81.9 million, or 6.7% on a distribution revenue basis and 2.2% over its total revenues, including distribution, transmission, and generation revenues. PECO also proposed to increase its customer charge from \$8.45 to \$12.50. Additionally, if the Company's proposal were approved in its entirety, PECO would have been permitted to recover a 7.79% overall rate of return on its original cost rate base, including a 10.95% return on common equity. PECO also proposed, *inter alia*, to recover investments and expenses associated with new programs, including an Electric Vehicle Pilot Rider and a new smart street lighting rate for outdoor lighting for any governmental agency. Through the course of discovery, testimony, evidentiary hearings, and settlement negotiations, all but one issue raised by the Company's base rate filing have been resolved. Accordingly, the Office of Consumer Advocate (OCA) addresses a single contested issue in this Main Brief.

B. Burden of Proof

In general, PECO bears the burden of proof to establish the justness and reasonableness of every element of its requested rate increase. In this regard, Section 315(a) of the Public Utility Code, 66 Pa. C.S. § 315(a), provides as follows:

Reasonableness of rates – In any proceeding upon the motion of the Commission, involving any proposed or existing rate of any public utility, or in any proceedings upon the 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). The Commonwealth Court has interpreted this principle in stating that:

Section 315(a) of the Public Utility Code, 66 Pa. C.S. § 315(a), places the burden of proving the justness and reasonableness of a proposed rate hike squarely on the utility. It is well-established that the evidence adduced by a utility to meet this burden must be substantial.

Lower Frederick Twp. v. Pa. PUC., 409 A.2d 505, 507 (Pa. Commw. 1980) (citations omitted); see also Brockway Glass v. Pa. PUC., 437 A.2d 1067 (Pa. Commw. 1981).

The Pennsylvania Supreme Court has stated that the party with the burden of proof has a formidable task to show that the Commission may lawfully adopt its position. Even where a party has established a prima facie case, the party with the burden must establish that “the elements of that cause of action are proven with substantial evidence which enables the party asserting the cause of action to prevail, precluding all reasonable inferences to the contrary.” Burleson v. Pa. P.U.C., 461 A.2d 1234, 1236 (Pa. 1983). Thus, a utility has an affirmative burden to establish the justness and reasonableness of every component of its rate request.

II. STATEMENT OF THE CASE

A. Parties

As noted in Section I.A above, PECO filed Supplement No. 6 on March 29, 2018. Subsequently, on April 4, 2018, the Commission's Bureau of Investigation and Enforcement (I&E) entered its appearance in this matter. On April 9, 2018, the Office of Small Business Advocate (OSBA) filed a Formal Complaint. On April 10, 2018, the Coalition for Affordable Utility Services and Energy Efficiently in Pennsylvania (CAUSE-PA) filed a Petition to Intervene. On April 12, 2018, the OCA filed a Formal Complaint. On April 17, 2018, the International Brotherhood of Electric Workers, Local 614 (IBEW) filed a Petition to Intervene. On April 23, 2018, the Community Action Association of Pennsylvania (CAAP) also filed a Petition to Intervene. On April 26, 2018, the Philadelphia Area Industrial Energy Users Group (PAIEUG) filed a Formal Complaint. On April 27, 2018, the Delaware Valley Regional Planning Commission (DVRPC) a filed a Petition to Intervene.¹ On May 2, 2018, the Trustees of the University of Pennsylvania (UPENN) filed a Formal Complaint.² On May 3, 2018, the Tenant Union Representative Network and Action Alliance of Senior Citizens of Greater Philadelphia (TURN), Tesla, Inc. (Tesla), and Wal-Mart Stores East, LP and Sam's East, Inc. (collectively, Walmart) filed separate Petitions to Intervene. On May 4, 2018, NRG Energy, Inc. (NRG) and the Retail Energy Supply Association (RESA) filed separate Petitions to Intervene.³ On May 18, 2018, Laborers International Union of North America, Local 57 (LiUNA) filed a

¹ On May 16, 2018, the DVRPC filed a Petition for Leave to Withdraw, which was granted on July 3, 2018.

² On June 20, 2018, UPENN filed a Petition for Leave to Withdraw, which was granted on July 3, 2018.

³ On May 16, 2018, PECO filed Answers to the Petitions to Intervene of NRG and RESA. On May 23, 2018, NRG filed a Response to PECO's Answer. On May 24, 2018, NRG filed a Response to PECO's Answer. On June 1, 2018, the ALJs granted the Petitions to Intervene in Prehearing Order No. 2. On July 17, 2018, RESA filed a Petition for Leave to Withdraw, which was granted on August 3, 2018.

Petition to Intervene.⁴ On May 24, 2018, ArcelorMittal USA, LLC (ArcelorMittal) also filed a Petition to Intervene. On June 26, 2018, West Norriton Township filed a Formal Complaint.⁵ Lastly, on July 3, 2018, ChargePoint, Inc. (ChargePoint) filed a Petition to Intervene.

B. Proceedings

On April 19, 2018, the Commission entered an Order suspending Supplement No. 6 until December 28, 2018, pursuant to Section 1308(d) of the Public Utility Code, 66 Pa. C.S. Section 1308(d), and initiated an investigation into the lawfulness, justness, and reasonableness of the proposed and existing rates, rules, and regulations. The Company's filing was assigned to the Office of Administrative Law Judge and further assigned to Administrative Law Judges (ALJs) Christopher P. Pell and F. Joseph Brady. A Prehearing Conference was held on May 8, 2018. A series of Public Input Hearings were held on June 6, 7, 12, 14, and 18, 2018 in Media, Norristown, Newtown, Philadelphia, and Oxford, Pennsylvania respectively.⁶

On June 12, 2018, PECO submitted Supplement Direct Testimony.⁷ On June 26, 2018, the OCA submitted the Direct Testimony of its witnesses: David Efron, OCA Statement No. 1; David Habr, OCA Statement No. 2; Clarence Johnson, OCA Statement No. 3; and Roger Colton, OCA Statement No. 4. The following parties also submitted Direct Testimony: I&E, OSBA, CAUSE-PA, IBEW, PAIEUG, TURN, Tesla, Walmart, NRG, LiUNA, and ArcelorMittal. On July 24, 2018, the OCA filed the Rebuttal Testimony of Clarence Johnson, OCA Statement No. 3R. The following parties also submitted Rebuttal Testimony: PECO, OSBA, CAAP, PAIEUG,

⁴ On August 15, 2018, LIUNA filed a Petition for Leave to Withdraw. This Petition is pending.

⁵ On July 18, 2018, West Norriton Township filed a Petition for Leave to Withdraw, which was granted on August 3, 2018.

⁶ Two Public Input Hearings were held in different locations in Philadelphia, Pennsylvania on June 14, 2018.

⁷ PECO also filed a Motion for Leave to File Supplemental Direct Testimony on this date. On June 26, 2018, the ALJs granted PECO's Motion in Prehearing Order No. 3.

TURN, and ChargePoint. On August 8, 2018, the OCA submitted the Surrebuttal Testimony of: David Effron, OCA Statement No. 1S, David Habr, OCA Statement No. 2S, Clarence Johnson, OCA Statement No. 3S, and Roger Colton, OCA Statement No. 4S. The following parties also submitted Surrebuttal Testimony: PECO, I&E, CAUSE-PA, PAIEUG, TURN, Tesla, and NRG. On August 2, 2018, an Evidentiary Hearing was held.

C. Partial Settlement

On August 15, 2018, the parties informed the ALJs that a Partial Settlement in principle had been reached. The parties submitted a Joint Petition for Partial Settlement, including Statements in Support, on August 28, 2018. The OCA now submits this Main Brief, which addresses a single remaining contested issue in this proceeding: NRG's proposed allocation of indirect costs to default service generation.

III. SUMMARY OF ARGUMENT

In this proceeding, NRG proposes an unprecedented and unsupported reallocation of indirect distribution costs to default service generation. The stated purpose of NRG's proposal is to force an "apples-to-apples" comparison of the Price-to-Compare (PTC) and electric generation supplier (EGS) offerings. As discussed in this Main Brief, the OCA submits that that NRG's proposed allocation ignores PECO's role as a default service provider, shifts costs that are not avoidable by customer shopping, and is otherwise flawed. Further, NRG's proposal results in the recovery of costs from default service customers that is not supported by Commission policy or Pennsylvania law. Therefore, the OCA respectfully requests that the Commission reject NRG's proposal and approve the August 28, 2018 Joint Petition for Partial Settlement without modification.

IV. ARGUMENT

A. Overview of NRG Proposal

In this proceeding, NRG proposes a major reallocation of what NRG witness Peterson refers to as “indirect” distribution service costs to PECO’s PTC. NRG’s proposal marks a dramatic shift in the allocation of the Company’s costs and must be rejected. See gen’ly OCA St. 3R, PECO St. 9R. NRG witness Chris Peterson erroneously claimed that PECO improperly allocated approximately \$101 million of indirect expense and proposed to reallocate these indirect costs from distribution service to default service generation. OCA St. 3R at 2; PECO St. 9R at 2. OCA witness Clarence Johnson⁸ described the proposal as follows:

Mr. Peterson contends that \$101 million of indirect expense in PECO’s class cost of service study (CCOSS) should be allocated to default service generation. The result of his recommendation is to reduce the distribution expense allocated to Residential (R) and Residential Heating (RH) classes, accompanied by a concomitant increase in the cost of default service purchased by customers in those classes. As a result of his recommendation, the Price to Compare would increase by 1.25 cents per kWh, or 17.5% from 7.11 cents per kWh to 8.40 cents per kWh. Based on his recommendation, the Company’s proposed distribution energy rate would decrease by 0.7 cents per kWh, an 11% reduction in the Company’s requested kWh charge.

OCA St. 3R at 2-3.

OCA witness Johnson concluded that NRG’s proposal should be denied as “Mr. Peterson has not identified any avoidable distribution costs that should be unbundled from PECO’s distribution rates” and “his methodology is inconsistent with . . . other ratemaking principles.”

OCA St. 3R at 8. Similarly, PECO witness Alan B. Cohn concluded that NRG’s proposal should

⁸ OCA witness Johnson is a consultant providing technical analysis, advice, and expert testimony regarding energy and utility regulatory issues. Mr. Johnson’s clients include state consumer advocate offices, customer groups, and coalitions of municipalities in Texas. Mr. Johnson has over 30 years of experience as a utility regulatory expert, including 25 years as Director of Regulatory Analysis for the Texas Office of Public Utility Counsel. A more detailed description of Mr. Johnson’s qualifications is included in OCA Statement No. 3, Appendix A.

be denied as it “reflects a misunderstanding of PECO’s default service program as well as utility cost accounting principles applied by this Commission and does not support any reallocation of distribution service costs.” PECO St. 9R at 2.

B. PECO’s Provision of Default Service and Applicable Law

PECO’s default service is required under the Electric Generation Customer Choice and Competition Act, 66 Pa. C.S. §§ 2801, *et seq.*, as confirmed and modified by Act 129 of 2008 (Act 129). Pursuant to Act 129, PECO is obligated to serve under standards designed to meet the policy goal of ensuring “adequate, reliable, affordable, efficient and environmentally sustainable electric service at the least cost, taking into account any benefits of price stability over time.” Preamble to Act 129, 2008 Pa. Laws 129; 66 Pa. C.S. § 2807(e).

OCA witness Johnson explained that Act 129 subjects PECO to certain requirements.

OCA St. 3R at 3-4. OCA witness Johnson stated:

In its role as default service provider, PECO must be prepared to meet the requirements of serving 100% of residential customers at any time. **As such, PECO’s costs are not avoidable as PECO must stand ready to serve at all times.**

In addition, the default service provider acquires power through open auctions, is required to procure a diverse set of long and short term power, may not advertise default service or include value added services, or earn a profit on providing the service. PECO does not own or operate the generation which provides default service, but instead acquires power through Commission approved solicitations. The law permits PECO to recover its reasonable costs of providing default service.

OCA St. 3R at 3-4 (footnote omitted) (emphasis added); see also 66 Pa. C.S. § 2807(e).

Of critical importance, it is the default service provider, PECO, that must stand ready to service 100% of residential customers’ power needs on a moment’s notice. OCA St. 3R at 4. Accordingly, PECO’s costs are built for that type of service.

PECO witness Cohn emphasized that default service exists for all customers, both shopping and non-shopping. PECO St. 9R at 9-10. PECO witness Cohn stated:

PECO makes no profit from providing default service to its distribution customers or standing ready to serve those customers who return to default service after shopping with an EGS. The Company is required to be able to provide default service to all its distribution customers under Pennsylvania law and the Order of the Commission, regardless of whether the customer shops or does not shop for electricity.

PECO St. 9R at 9-10 (emphasis in original).

Additionally, PECO witness Cohn clarified that default service is part of PECO's distribution service; it is not a separate "operating division" as NRG witness Peterson claims.

PECO St. 9R at 10. PECO witness Cohn stated:

PECO is an electric distribution company in the business of distributing electricity to its customers. Default service is not a separate "operating division," but a service to distribution customers in the form of electric generation provided by wholesale suppliers under Commission-approved contracts with PECO to meet the electricity needs of those customers who have not chosen an EGS or whose EGS decides to cease providing service to such customers. PECO customers are not distribution customers or default service customers; they are distribution customers who may or may not receive default service, which PECO provides at its cost and without profit in accordance with the requirements of the Commission.

PECO St. 9R at 10 (emphasis in original).

As discussed below, NRG witness Peterson's allocation proposal is based on a misunderstanding of the requirements of Act 129 and PECO's distribution service.

C. NRG's Proposal to Reallocate Costs

1. Qualifications of Mr. Peterson

In response to PECO's oral Motion to disqualify NRG witness Peterson as an expert at the Evidentiary Hearing in this proceeding, ALJ Brady stated, "As to his level of expertise, that

will play a factor into our decision.” Tr. at 482. ALJ Brady continued, “We will give it due weight based on that level.” Id. The OCA notes that NRG witness Peterson proposed a reallocation of \$101 million of what he characterizes as indirect expense to default service generation, despite not having ever allocated public utility costs for ratemaking purposes.⁹

2. NRG’s Alternative Cost Allocation

a. NRG’s Proposal Ignores PECO’s Role as a Default Service Provider and Shifts Costs That Are Not Avoidable.

NRG witness Peterson’s reallocation of what he claims are “indirect” costs instead seeks to reallocate direct costs. Only avoidable costs, that is costs that PECO avoids when a customer switches to an EGS, are properly allocated to the PTC. PECO’s default service costs are not avoidable because the Company must stand ready to serve both shopping and non-shopping customers at all times. As such, NRG witness Peterson does not identify any avoidable costs of providing default service. OCA St. 3R at 3-4.

In particular, NRG witness Peterson seeks to re-allocate the following costs: customer service expenses (customer assistance, information advertisement, and miscellaneous customer service), sales expenses (demonstrating & selling), A&G expenses (administrative salaries, office supplies & expense, outside services employed, property insurance, injuries & damages, employee pensions & benefits, regulatory commission, duplicate charges – credit, miscellaneous general, and maintenance of general plant), and depreciation & amortization expense (relating to intangible plant, general plant, and common plant). PECO St. 9R at 13-14.

⁹ Tr. at 476 (Mr. Peterson stated, “I have not done other cost allocations for utility companies.”); see also Tr. at 475 (Mr. Peterson testified that he relied on counsel to explain the following: the Commission’s 1997 restructuring order, what costs the PTC is intended to recover, the Commission’s default service regulations, Commission statements on wholesale market price signals, PECO’s comments in other proceedings on retail market enhancements, PECO’s micro-grid proposal referenced in Mr. Peterson’s testimony, and PECO’s prepaid pilot referenced in Mr. Peterson’s testimony.).

OCA witness Johnson explained that PECO quantifies and collects from default service customers the direct expense of providing default service. OCA witness Johnson stated:

These costs include the acquired power cost, the cost of compliance with the law, transmission and ancillary service costs, and the administration costs of operating the solicitation process. **Mr. Peterson has not identified any avoidable costs of providing default service which are improperly recovered from customers of competitive EGS providers.**

OCA St. 3R at 4-5 (emphasis added). Further, PECO witness Cohn explained that “all PECO customers – whether they receive electric generation supply from EGSs or from PECO – are distribution customers, and responsibility for distribution business costs should not vary based upon receipt of default service.” PECO St. 9R at 14. As PECO witness Cohn stated, “the distribution business costs Mr. Peterson proposed to allocate to default service customer are not a function of the number of distribution customers that receive default service or the amount such customers pay for default service.” PECO St. 9R at 16-17.

In addition, PECO witness Cohn noted that “it would be inappropriate to allocate fixed costs to default service in a manner that would result in the company losing money as more people shop for power.” Tr. at 442. PECO witness Cohn further stated:

Under Mr. Peterson’s allocation method, if all customers became default service customers, large amounts of PECO distribution system costs (including depreciation and amortization for general, common and intangible plant) would need to be recovered from those customers. Alternatively, if all of PECO’s customers decide to shop (which they are free to do), PECO would not recover any distribution business expenses under Mr. Peterson’s allocation method that are allocated to default service even though all the costs would still remain with PECO.

PECO St. 9R at 17.

Accordingly, NRG witness Peterson’s proposal is illogical. PECO must stand ready to serve 100% of customers at all times. PECO’s default service costs are unavoidable and,

therefore, remain the same when customers shop. Distribution costs in rates cannot be added to the PTC as NRG witness Peterson proposes.

b. NRG's Proposal Contains Other Flaws and Inconsistencies.

OCA witness Johnson identified several additional flaws and inconsistencies in his analysis of NRG witness Peterson's proposed allocation. In particular, OCA witness Johnson explained that NRG witness Peterson's proposed allocation is inconsistent with the structure of the CCOSS and the CCOSS classification of indirect costs. OCA St. 3R at 4-6.

OCA witness Johnson explained why NRG witness Peterson's recommendation is inconsistent with the structure of PECO's CCOSS, as follows:

First, Mr. Peterson limits his allocation recommendation to only the R and RH classes. The CCOSS is based on fully allocated costs. PECO's default service has commercial and industrial customers, but Mr. Peterson does not explain why the re-allocation of indirect costs is limited to residential customers. Second, Mr. Peterson's allocation process is not consistent with the classification of indirect costs in the CCOSS. The classification procedure is an intermediate step for determining whether costs should be allocated based on demand, energy, customers, or an internal composition of factors.

OCA St. 3R at 5.

Additionally, OCA witness Johnson explained why NRG witness Peterson's recommendation is inconsistent with the CCOSS allocation of indirect costs, as follows:

Administrative & General (A&G) expense is the largest component of indirect cost which Mr. Peterson re-allocates to default service. A&G expense, by definition, is not directly allocable to any particular corporate function. A&G includes upper management salary, general consulting and legal costs, pension and benefits, injuries and damages, and regulatory activities. Most of the A&G expense accounts are classified by PECO's CCOSS as salary and wage (S&W) related, and are therefore, allocated on the basis of salary and wages incurred for direct activities within the CCOSS. For example, A&G costs are assigned to customer accounting based on customer accounting

salaries as a percent of total direct wage and salary expense. The A&G costs assigned in this manner to customer accounting are then allocated on the customer accounting allocation factor (*i.e.*, customer allocation). Mr. Peterson reallocates A&G expense to residential default service without any consideration of the classification of the A&G costs as S&W-related. Based on the logic of PECO's CCOSS, any allocation of this A&G expense to the generation function should follow S&W incurred for the direct costs of providing default service. Because the bulk of direct costs of acquiring default power consists of actual power expense and consultant expense, it is not clear that any direct S&W expense is incurred in the provision of default service, meaning that no S&W-related A&G expense is allocable to the default service program function. Moreover, Mr. Peterson's procedure for re-allocating A&G expense based on customers or revenues assumes a fixed allocation to Rate R and RH which is unaffected by the change in allocation basis. If Mr. Peterson seeks to replace the S&W classification with a hybrid customers-revenue classification, the amount of A&G expense allocated to each customer class should change—but it does not under his method.

OCA St. 3R at 5-6 (footnote omitted).

OCA witness Johnson further explained that PECO's default service is a pure pass through expense. OCA St. 3R at 6. As OCA witness Johnson stated

PECO does not generate the power or own the facilities that produce the power. PECO conducts auctions to procure the power and passes the power costs through to default service customers. Typically, such pass through costs are not included in the calculation of allocation factors for most A&G expense items in the CCOSS. If O&M expense is utilized as the A&G classifier instead of S&W, the O&M allocator generally excludes purchase power and fuel. Given that most of the default service cost is a pure pass through of purchased power, the magnitude of this re-allocation appears to be unreasonable.

OCA St. 3R at 6-7.

As PECO witness Cohn stated, the "primary goal in cost allocation is appropriate recognition of cost causality." Tr. at 442. NRG witness Peterson "has not shown that the costs he allocates are caused by or even vary with his chosen allocators." Tr. at 442. Therefore, as

OCA witness Johnson explained, NRG's proposed allocation is inconsistent with the structure of the CCOSS and the CCOSS classification of indirect costs. OCA St. 3R at 4-6.

c. NRG's Proposal is Not Supported by the Unbundling Proceeding.

NRG witness Peterson referred to the Commission's Order in the 1997 unbundling proceeding, or the restructuring proceeding, as well as the OCA testimony relied upon by the Commission in that proceeding to support his recommendation to allocate indirect costs to default service generation.¹⁰ NRG St. 1 at 9-10, 18, Exh. CP-4. As OCA witness Johnson and PECO witness Cohn testified, neither the unbundling proceeding nor the OCA's testimony in that proceeding support NRG's proposal here. OCA St. 3R at 7.

The unbundling proceeding separated generation from transmission and distribution; it did not divide costs with an understanding of what it would cost to provide default service.

In particular, OCA witness Johnson explained:

First, the unbundling proceeding did not pertain to, or set, default service rates. The proceeding unbundled the utility's unregulated generation service from regulated transmission and distribution service. The purpose of the proceeding was unrelated to Mr. Peterson's objective of allocating distribution costs to the default service rate. Second, PECO was unbundling the full cost of its generation plants for stranded cost determination and an eventual transfer to an unregulated affiliate.

OCA St. 3R at 7. Further, as PECO witness Cohn stated, "the Commission was addressing the actual separation of PECO's generation business which had thousands of employees and generated significant income on a stand-alone basis and the distribution business, not a hypothetical separation of functions PECO performs as a distribution Company." Tr. at 443.

PECO witness Cohn also testified that, in the unbundling proceeding, "the Commission at the time agreed with testimony of a witness for the [OCA] that the unbundling of generation,

¹⁰ Application of PECO Energy Co. for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, Docket No. P-00971265, 1997 Pa. PUC LEXIS 51 (Order entered December 23, 1997)

transmission, and distribution rates in restructuring ‘should produce results that should look like what functional costs would be if PECO were to separate itself into functionally separate divisions.’” PECO St. 9R at 11. PECO witness Cohn explained:

What Mr. Peterson ignores in his discussion of the 1997 Restructuring Order is that at the time, PECO was a very different company – one that included generation operations with twice the employees of its distribution operations. The 1997 Restructuring Order reflects the Commission concern regarding the allocation of administrative expense between two different business groups with significant administrative requirements. Notably, the allocator adopted by the Commission to address the administrative expense of PECO’s generation and distribution operations was neither revenues nor customers, nor some hybrid of the two, as Mr. Peterson proposes in this proceeding; instead, the Commission allocated administrative expense based upon the number of employees working in generation and operations.

Twenty years later, PECO does not have a generation business and is no longer at the beginning of the restructuring era. And PECO’s rates and those of other EDCs have been subject to scrutiny in both default service proceedings and in distribution rate proceedings where the Commission has “strived to address” the need to ensure that the PTC reflects all costs of default service.

PECO St. 9R at 12 (footnotes omitted).

Further, OCA witness Johnson noted that the OCA’s testimony in the unbundling proceeding is **not** applicable to this proceeding as NRG witness Peterson suggests. OCA St. 3R at 7. OCA witness Johnson explained:

Unlike purchase power acquired for default service, these generation plants incurred significant labor costs, which in turn requires significant indirect costs for employee benefits and supervision. The OCA’s testimony in that case proposed a labor allocation for A&G expense, which is comparable to the S&W allocation method used for most A&G expense in the current CCOSS. Because the generation plants were labor intensive, 66% of direct labor expense was associated with generation at the time. However, as previously noted, little if any wage cost is incurred for default service.

OCA St. 3R at 7 (footnote omitted).

Accordingly, neither the Commission's Order in the 1997 unbundling proceeding nor the OCA's testimony in that proceeding support NRG witness Peterson's proposal to allocate indirect costs to default service generation in this proceeding.

3. Effects of NRG's Proposal

a. NRG's Proposal Results in the Recovery of Costs From Default Service Customers That Is Not Supported By Commission Policy or Pennsylvania Law.

NRG witness Peterson's recommendation to allocate indirect costs to default service generation would increase the PTC by 1.25 cents per kWh, or 17.5%, from 7.11 cents per kWh to 8.40 cents per kWh. OCA St. 3R at 3. This significant increase in the PTC does not reflect PECO's cost of providing default service. OCA St. 3R at 2-3.

Pursuant to the Customer Choice Act, PECO is permitted "to recover on a full and current basis . . . all reasonable costs incurred under this section and a commission-approved competitive procurement plan." 66 Pa. C.S. § 2807(e)(3.9). The costs "under this section" are the costs of providing default service. In addition, as PECO witness Cohn explained, PECO is not permitted to earn a profit for providing default service. PECO witness Cohn stated:

Under the Pennsylvania Public Utility Code, PECO is entitled to recover all reasonable costs of providing default service under its approved procurement plan. The Commission has not authorized PECO (or any other electric distribution company) ("EDC") to earn a profit on the provision of default service.

PECO St. 9R at 4.

PECO witness Cohn also discussed the Commission's policy statement regarding default service and retail electric markets, 52 Pa. Code § 69.1808. PECO St. 9R at 5. As PECO witness Cohn explained:

In a Policy Statement regarding default service and retail electric markets (52 Pa. Code § 69.1808), the Commission identified the types of costs that should be recovered from default service customers. As the Policy Statement explains:

(a) The PTC should be designed to recover all generation, transmission and other related costs of default service. These cost elements include:

(1) Wholesale energy, capacity, ancillary, applicable RTO or ISO administrative and transmission costs.

(2) Congestion costs will ultimately be recovered from ratepayers. Congestion costs should be reflected in the fixed price bids submitted by wholesale energy suppliers.

(3) Supply management costs, including supply bidding, contracting, hedging, risk management costs, any scheduling and forecasting service provided exclusively for default service by the EDC, and applicable administrative and general expenses related to these activities.

(4) Administrative costs, including billing, collection, education, regulatory, litigation, tariff filings, working capital, information system and associated administrative and general expenses related to default service.

(5) Applicable taxes, excluding Sales Tax.

(6) Costs for alternative energy portfolio standard compliance.

PECO St. 9R at 5. PECO witness Cohn further explained that PECO' PTC includes each of these types of costs. See PECO St. 9R at 5-8

In addition, PECO witness Cohn testified that the costs NRG witness Peterson proposed to reallocate were “properly functionalized and assigned to distribution customers.” PECO St. 9R at 14. As discussed in Section IV.C.2.a above, “all PECO customers – whether they receive electric generation supply from EGSs or from PECO – are distribution customers, and responsibility for distribution business costs should not vary based upon receipt of default

service.” PECO St. 9R at 14. PECO witness Cohn noted that Mr. Peterson’s allocation inflates the PTC by allocating hypothetical costs to default service generation. Mr. Cohn explained:

In effect, Mr. Peterson is assuming that a separate default service division is appropriate and that it would have many of the same costs PECO has as a distribution company without determining the costs PECO actually incurs in providing default service. By choosing to then allocate the **hypothetical costs** of a separate default service division based on default service revenue and number of default service customers, he creates an artificially high PTC.

PECO St. 9R at 14-15 (emphasis added).

As discussed in Section IV.B above, PECO is permitted only to recover the cost of providing default service and is not permitted to earn a profit on default service. In this regard, the Commonwealth Court has provided: “[A] utility may pass along to its customers only those expenses or costs it actually incurs. Any other approach would permit the utility, by charging higher rates than necessary, to gain a profit from its customers under the guise of recovering operating expenses.” Cohen v. Pa. PUC, 468 A.2d 1143, 1150 (Pa. Commw. 1983) (citations omitted). Similarly, the Pennsylvania Supreme Court has similarly stated that, “the Commission has no authority to permit, in the rate-making process, the inclusion of **hypothetical expenses** not actually incurred.” Barasch v. Pa. PUC, 493 A.2d 653, 655 (Pa. 1985) (emphasis added).

Therefore, NRG’s proposal to allocate indirect costs to default service generation is inconsistent with sound ratemaking principles and PECO should not be permitted to artificially inflate the PTC and recover hypothetical costs under NRG’s proposal.

D. Summary

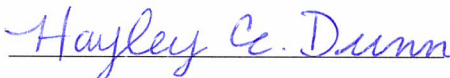
NRG proposes an unprecedented and unsupported reallocation of indirect distribution costs to default service generation. The OCA submits that NRG’s proposed allocation ignores PECO’s role as a default service provider, shifts costs that are not avoidable by customer

shopping, and is otherwise flawed. Further, NRG's proposal results in the recovery of costs from default service customers that is not supported by Commission policy or Pennsylvania law. Therefore, the OCA respectfully requests that the Commission reject NRG's proposal and approve the Joint Petition for Partial Settlement without modification.

V. CONCLUSION

For the reasons set forth in this Main Brief, the OCA respectfully requests that the Commission reject NRG's proposal to reallocate indirect costs to default service generation and approve the August 28, 2018 Joint Petition for Partial Settlement without modification.

Respectfully Submitted,



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Dated: September 7, 2018

Appendix A

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2018-3000164
	:	
PECO Energy Company	:	

PROPOSED FINDINGS OF FACT, CONCLUSIONS OF LAW,
AND ORDERING PARAGRAPHS
OF THE OFFICE OF CONSUMER ADVOCATE

PROPOSED FINDINGS OF FACT

1. PECO is an electric distribution company engaged in the business of providing electric distribution service to its customers. PECO St. 9R at 10.
2. Default service is a part of PECO’s distribution service and is not an operating division of PECO separate from its distribution function. PECO St. 9R at 10.
3. Default service is a “service to distribution customers in the form of electric generation provided by wholesale suppliers under Commission-approved contracts with PECO to meet the electricity needs of those customers who have not chosen an EGS or whose EGS decides to cease providing service to such customers.” PECO St. 9R at 10.
4. PECO customers are “distribution customers who may or may not receive default service, which PECO provides at its cost and without profit in accordance with the requirements of the Commission.” PECO St. 9R at 10.
5. The default service provider must stand ready to service 100% of customers’ power needs on a moment’s notice. OCA St. 3R at 3-4.
6. Default service exists for all customers, both shopping and non-shopping. PECO St. 9R at 10.
7. PECO makes no profit from providing default service to distribution customers or from standing ready to serve customers who return to default service after shopping with an EGS. PECO St. 9R at 9-10.
8. Avoidable costs are those that do not occur when a customer leaves default service. OCA St. 3R at 3.

9. The indirect costs NRG witness Peterson seeks to allocate to default service are not avoided by PECO when a customer switches to an alternative supplier. OCA St. 3R at 3-4.

10. The direct costs of default service include the acquired power cost, the cost of compliance with the law, transmission and ancillary service costs, and the administration of operating the solicitation process. OCA St. 3R at 4-5; PECO St. 9R at 5.

11. NRG witness Peterson seeks to re-allocate \$101 million of expense in PECO's Class Cost of Service Study (CCOSS) as indirect and proposes to reallocate these costs from distribution service to default service. OCA St. 3R at 2; PECO St. 9R at 2.

12. NRG witness Peterson seeks to re-allocate the following categories of costs: customer service expenses (customer assistance, information advertisement, and miscellaneous customer service), sales expenses (demonstrating & selling), A&G expenses (administrative salaries, office supplies & expense, outside services employed property insurance, injuries & damages, employee pensions & benefits, regulatory commission, duplicate charges – credit, miscellaneous general, and maintenance of general plant), and depreciation & amortization expense (relating to intangible plant, general plant, and common plant). PECO St. 9R at 13-14.

13. The costs NRG witness Peterson proposed to reallocate were properly functionalized and assigned to distribution customers. PECO St. 9R at 14.

14. Mr. Peterson limits his allocation recommendation to only the R and RH classes, even though commercial and industrial customers also receive default service. OCA St. 3R at 5.

15. Mr. Peterson has not identified any avoidable distribution costs that should be unbundled from PECO's distribution rates. OCA St. 3R at 8.

16. The Commission's Policy Statement provides the types of costs that should be recovered from default service, including the following:

(a) The PTC should be designed to recover all generation, transmission and other related costs of default service. These cost elements include:

(1) Wholesale energy, capacity, ancillary, applicable RTO or ISO administrative and transmission costs.

(2) Congestion costs will ultimately be recovered from ratepayers. Congestion costs should be reflected in the fixed price bids submitted by wholesale energy suppliers.

(3) Supply management costs, including supply bidding, contracting, hedging, risk management costs, any scheduling and forecasting service provided exclusively for

default service by the EDC, and applicable administrative and general expenses related to these activities.

(4) Administrative costs, including billing, collection, education, regulatory, litigation, tariff filings, working capital, information system and associated administrative and general expenses related to default service.

(5) Applicable taxes, excluding Sales Tax.

(6) Costs for alternative energy portfolio standard compliance.

52 Pa. Code § 69.1808.

17. PECO's PTC includes each of the costs identified in 52 Pa. Code § 69.1808. 52 Pa. Code § 69.1808; see PECO St. 9R a 5-8.

18. All PECO customers are distribution customers, and responsibility for distribution business costs does not vary based upon receipt of default service. PECO St. 9R at 14.

19. As a result of NRG's proposal, the Price to Compare would increase by 1.25 cents per kWh, or 17.5% from 7.11 cents per kWh to 8.40 cents per kWh. OCA St. 3R at 3.

20. Based on Mr. Peterson's proposal, the Company's proposed distribution energy rate would decrease by 0.7 cents per kWh, an 11% reduction in the Company's requested kWh charge. OCA St. 3R at 3.

21. Mr. Peterson's allocation inflates the PTC by allocating hypothetical costs to default service generation. PECO St. 9R at 14-15.

22. The Class Cost of Service Study (CCOSS) is based on fully allocated costs. OCA St. 3R at 5.

23. Administrative & General (A&G) expense is the largest component of indirect costs that Mr. Peterson re-allocates to default service. OCA St. 3R at 5.

24. A&G, by definition, is not directly allocable to any particular corporate function. OCA St. 3R at 5.

25. A&G includes upper management salary, general consulting and legal costs, pension and benefits, injuries and damages, and regulatory activities. OCA St. 3R at 5.

26. Most of the A&G expense accounts are classified by PECO's CCOSS as salary and wage (S&W) related, and are therefore, allocated on the basis of salary and wages incurred for direct activities within the CCOSS. OCA St. 3R at 5.

27. PECO acquires power through open auctions, is required to procure a diverse set of long and short term power, may not advertise default service or include value added services, or earn a profit on providing the service. OCA St. 3R at 4; see also, 66 Pa. C.S. § 2807(e).

28. PECO does not own or operate the generation that provides default service, but instead acquires power through Commission approved solicitations. OCA St. 3R at 4; see also, 66 Pa. C.S. § 2807(e).

29. The unbundling proceeding separated generation from transmission and distribution; it did not divide costs with an understanding of what it would cost to provide default service. OCA St. 3R at 7.

30. The purpose of the unbundling proceeding was unrelated to NRG witness Peterson's objective of allocating distribution costs to the default service rate. OCA St. 3R at 7.

PROPOSED CONCLUSIONS OF LAW

1. A public utility seeking a rate increase has the burden of proof to establish the justness and reasonableness of each element of its request. 66 Pa. C.S. § 315(a).

2. The utility requesting the rate increase has the burden of proving that the rate involved is just and reasonable. 66 Pa. C.S. §§ 315(a), 1301, and 1308(e).

3. PECO has met its burden of proof and demonstrated that the costs at issue are direct costs and are appropriately assigned to distribution service.

4. PECO's default service is required under the Electric Generation Customer Choice and Competition Act, 66 Pa. C.S. §§ 2801, *et seq.*, as confirmed and modified by Act 129 of 2008 (Act 129).

5. Pursuant to Act 129, as default service provider, PECO is obligated to serve under standards designed to meet the policy goal of ensuring "adequate, reliable, affordable, efficient and environmentally sustainable electric service at the least cost, taking into account any benefits of price stability over time." Preamble to Act 129, 2008 Pa. Laws 129; 66 Pa. C.S. § 2807(e).

6. Act 129 allows PECO to recover its reasonable costs of providing default service. 66 Pa. C.S. § 2807(e).

7. NRG's proposal is not supported by the law or sound ratemaking principles. Preamble to Act 129, 2008 Pa. Laws 129; 66 Pa. C.S. d§ 2807(e).

8. NRG's proposal is not supported by the Commission's 1997 Order in PECO's restructuring, or unbundling, proceeding. Application of PECO Energy Co. for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, Docket No. P-00971265, 1997 Pa. PUC LEXIS 51 (Order entered December 23, 1997).

PROPOSED ORDERING PARAGRAPHS

It is hereby ORDERED THAT:

1. NRG's proposal to reallocate indirect costs to default service generation is rejected.
2. The August 28, 2018 Joint Petition for Partial Settlement is approved without modification.
3. PECO Energy Company shall be permitted to file tariffs, tariff supplements or tariff revisions containing proposed rates, rules and regulations to increase annual revenues consistent with the Joint Petition for Partial Settlement and this Commission's Opinion and Order.
4. PECO Energy Company's tariffs, tariff Supplements or tariff revisions may be filed on less than statutory notice, and pursuant to the provisions of 52 Pa. Code §§ 53.31 and 53.101, may be filed to be effective on at least one day's notice after entry of the Commission's Final Order, for service rendered on and after the date of entry of the Commission's Final Order in this matter.
5. The Complaints filed by the various parties to this proceeding at Docket No. R-2018-3000164 are granted in part and denied in part, to the extent consistent with this Commission's Opinion and Order.
6. Upon acceptance and approval by the Commission of the tariff supplements and proof of revenues filed by PECO Energy Company consistent with this Order, this proceeding shall be marked closed.

DATE: _____

Christopher P. Pell
Deputy Chief Administrative Law Judge

F. Joseph Brady
Administrative Law Judge

Appendix B

- OCA Statement No. 2S Surrebuttal Testimony of David S. Habr, including Exhibit DSH-S1, Verification
- OCA Statement No. 3S Surrebuttal Testimony of Clarence L. Johnson, including Appendix A, Schedules CJ-S-1 through CJ-S-4, Verification
- OCA Statement No. 4S Surrebuttal Testimony of Roger D. Colton, including Verification