

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. R-00049255

PPL Electric Utilities Corporation

Statement No. 4-R

Rebuttal Testimony of Douglas A. Krall

1 Q. Please state your full name and business address.

2 A. My name is Douglas A. Krall. My business address is Two North Ninth Street,
3 Allentown, Pennsylvania, 18101.

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

5 A. I am employed by PPL Electric Utilities Corporation (“PPL Electric” or the
6 “Company”) a subsidiary of PPL Corporation. I work in the Asset Management
7 Department of PPL Electric and my title is Manager – Regulatory Strategy.

8 Q. Have you provided testimony previously in this proceeding?

9 A. Yes, I have. I provided written direct testimony that was designated as
10 Statement No. 4. I also provided Exhibit DAK1.

11 Q. Please describe the purpose of your rebuttal testimony.

12 A. The purpose of my rebuttal testimony is to address issues raised by other parties
13 regarding the following:

- 14 • The inclusion of plant held for future use in base rates.
- 15 • PPL Electric’s proposal to establish a Distribution System Improvement
16 Charge (“DSIC”).
- 17 • Issues related to PPL Electric’s proposed Transmission Service Charge
18 (“TSC”).
- 19 • PPL Electric’s proposed allocation of distribution revenue requirements.
- 20 • PPL Electric’s request to amortize and recover from customers costs
21 associated with Hurricane Isabel.
- 22 • Costs and benefits associated with the Automated Meter Reading (“AMR”)
23 system.

1 • Proposals offered by Strategic Energy to promote retail competition.

2 Q. Are you sponsoring additional exhibits as part of your rebuttal testimony?

3 A. Yes, I am. Exhibits DAK2, DAK3 and DAK4 are attached.

4 **Plant Held for Future Use**

5 Q. Please describe PPL Electric's request in this proceeding for plant held for future
6 use.

7 A. In my direct testimony, I stated that PPL Electric is making a claim to include in
8 rate base \$2,212,678 related to distribution plant held for future use. I further
9 stated that if this claim is not approved by the Commission, PPL Electric, in the
10 alternative, is requesting approval to accrue a return equivalent to the applicable
11 AFUDC rate on these investments and to include the accrued amount as part of
12 its distribution plant in-service at the time such plant is placed into service.

13 Q. OCA witness Lafayette Morgan has recommended that the Commission accept
14 PPL Electric's alternative request and allow the Company to accrue AFUDC on
15 those specific parcels of land subject to normal regulatory oversight at the time
16 the Company requests such plant be placed into service. Does the Company
17 accept this proposal?

18 A. Yes, the Company does. An appropriate adjustment to rate base is reflected in
19 Revised Exhibit Future 1.

20 **Distribution System Improvement Charge**

21 Q. Please describe PPL Electric's proposal to establish a DSIC.

22 A. The DSIC that PPL Electric has proposed is a rate mechanism that would allow
23 the Company to recover, between formal rate cases, the carrying costs on

1 certain capital investments in distribution facilities. In the absence of DSIC, PPL
2 Electric can not collect any money from customers to support these investments
3 in facilities until they are recognized as additions to rate base in the context of a
4 formal rate proceeding. This situation can go on for years and is becoming
5 increasingly critical as distribution facilities built in the high growth 1960s, 1970s,
6 and 1980s are nearing the end of their useful lives. The DSIC will enable PPL
7 Electric to begin collecting money to cover the carrying costs of these facilities
8 shortly after the facilities are completed and begin providing service to
9 customers. As a result, PPL Electric will be better able to finance the
10 construction of facilities that are required to maintain safe and reliable service
11 without the immediate need to file a formal base rate case.

12 Q. Please describe the issues raised by other parties relative to this proposal.

13 A. OCA witness Thomas Catlin and OTS witness Michael Gruber argue that PPL
14 Electric's proposed DSIC is illegal under the Pennsylvania Public Utility Code
15 and represents improper single-issue rate-making. PPLICA witness Stephen
16 Baron, DOD witness Thomas Prisco, and OSBA witnesses Robert Knecht and
17 Mark Ewen echo the criticism that DSIC represents improper single-issue rate-
18 making. OCA witness Catlin and OSBA witnesses Knecht and Ewen also argue
19 that verification is problematic. OTS witness Gruber also questions the inclusion
20 of substation equipment and security improvements as DSIC-eligible property.
21 PPLICA witness Baron also questions the need for DSIC and, along with DOD
22 witness Kenneth Kincel and OSBA witnesses Knecht and Ewen, the
23 appropriateness of a kWh-based recovery mechanism. OSBA witnesses Knecht

1 and Ewen also question the necessity for DSIC. Witness Eric Epstein argues
2 that DSIC is illegal, discriminatory, and should not address security
3 improvements.

4 Q. How do you respond to the argument that DSIC constitutes improper single-issue
5 rate-making?

6 A. That argument is not correct. Although PPL Electric will respond fully to such
7 legal arguments in its briefs, counsel has provided me with a brief overview of
8 PPL Electric's position on the legality of its proposed DSIC.

9 The contentions of other parties, that the DSIC is unlawful, ignore the fact
10 that Section 1307(a) of the Public Utility Code, 66 Pa.C.S. § 1307(a), expressly
11 authorizes automatic adjustment clauses, subject to the Commission's approval.
12 The parties who contend that single issue ratemaking is unlawful are incorrectly
13 reading Section 1307(a) out of existence. Of course, PPL Electric must
14 demonstrate to the Commission that the proposed DSIC is in the public interest,
15 but there is no blanket rule that automatic adjustment clauses governing recovery
16 of an expense or class of expenses are unlawful.

17 Q. Certain parties contend that PPL Electric's proposed DSIC is not proper because
18 there is no specific authority for it similar to Section 1307(g) which authorizes
19 DSICs for water utilities. Do you agree with those comments?

20 A. No, I do not. PPL Electric will explain fully in its briefs why the absence of a
21 specific authorization for its proposed DSIC, such as Section 1307(g) for water
22 utilities, does not preclude the Commission from approving PPL Electric's DSIC.
23 I note, however, that the Commission approved a DSIC for a water utility before

1 Section 1307(g) of the Public Utility Code was enacted. Section 1307(g) was
2 enacted into law under the Act of December 18, 1996, P.L. 1061, No. 156, § 1,
3 effective on February 16, 1997. Previously, in an Order entered on August 26,
4 1996, the Commission approved a form of DSIC in *Re: Pennsylvania-American*
5 *Water Company*, Docket No. P-00961031, 86 Pa. PUC 415 (1996). The
6 Commission obviously concluded that a specific statutory authorization to create
7 a DSIC for water utilities was not required and concluded also that DSICs meet
8 the requirements of Section 1307(a) of the Public Utility Code.

9 Further, since the enactment of Section 1307(g), the Commission has
10 approved a similar tariff provision, a Collection System Improvement Charge
11 (“CSIC”), for a wastewater company despite the absence of any specific statutory
12 authorization for such an automatic adjustment clause.

13 Specifically, the CSIC for Pennsylvania-American Water Company’s
14 sewer divisions was implemented pursuant to the Commission’s approval in *Pa.*
15 *P.U.C. v. Pennsylvania-American Water Co.*, Docket No. R-00027982
16 (November 9, 2003). There, the Commission approved the CSIC despite the
17 facts that wastewater or sewer utilities are not mentioned in Section 1307(g) and
18 that there is no other statutory provision specifically authorizing a CSIC for sewer
19 or wastewater utilities. I should note that the OCA has appealed the
20 Commission’s approval of the CSIC. The appeal is presently pending before the
21 Pennsylvania Commonwealth Court at Docket No. 2497 C.D. 2003.

22 Q. How do you respond the criticism that verification of DSIC will be problematic?

1 A. PPL Electric knows of no reason why an electric DSIC should be more difficult to
2 administer and verify than a water DSIC or a sewer utility CSIC.

3 Initially, I note that water and sewer companies are subject to the same
4 alleged “incentives” to classify as many property additions as possible as being
5 subject to the DSIC or CSIC. Nevertheless, the water and sewer companies and
6 the Commission have not experienced, to my knowledge, substantial controversy
7 with regard to these matters. It is my understanding that the Commission’s
8 Bureau of Audits periodically reviews the plant additions of water utilities that are
9 reflected in the water utilities’ DSICs and that there has not been substantial
10 controversy with regard to these matters.

11 Further, PPL Electric’s proposed DSIC explicitly specifies the categories of
12 property that are eligible for the DSIC as follows:

- 13 • Poles (Account 364) oil circuit reclosures (Account 365), underground
14 cable (Account 367) and underground services (Account 369) installed as
15 in kind replacements,
- 16 • Area supply substation equipment (Account 362) replacements due to
17 deterioration, failure, or obsolescence to maintain reliability,
- 18 • Unreimbursed costs related to capital projects that relocate Company
19 facilities due to highway relocation work,
- 20 • Distribution line circuit capital replacements to maintain reliability, and
21 security improvements.

22 By tying the eligibility of most plant additions to specific distribution plant
23 accounts, PPL Electric has minimized its discretion with regard to eligibility for

1 the DSIC because these accounts are clear and well-defined under the Uniform
2 System of Accounts.

3 Q. Are there any problems with including security improvements in the DSIC eligible
4 property?

5 A. No, there are not. OTS witness Gruber and Witness Epstein take exception to
6 the Company's proposal to include security improvements under the definition of
7 DSIC-eligible property. Both argue that security improvements are more likely to
8 involve the transmission system, and the Company does not disagree. In such a
9 circumstance, however, costs related to security for transmission facilities would
10 be included in the PJM Open Access Transmission Tariff (OATT) and collected
11 from entities purchasing transmission service from PJM. However, the Company
12 does not preclude the possibility that a governmental authority with appropriate
13 jurisdiction might order security improvements to Company buildings or
14 information systems that are defined as distribution property. The Company
15 believes that recovery of such costs through a DSIC is consistent with the
16 provisions of the Commission's Order regarding "government-imposed
17 requirements." *Re: Pennsylvania-American Water Co.*, 86 Pa. PUC, *supra*, pp.
18 419.

19 Further, as I made clear at page 36 of my direct testimony, PPL Electric
20 Statement No. 4, security improvements would be limited to those recommended
21 by a governmental authority with appropriate jurisdiction. There would be little, if
22 any, discretion for PPL Electric with regard to security investments because the
23 decisions would be made pursuant to governmental recommendations or

1 requirements. For this reason, there should be minimal controversy with regard
2 to the eligibility of specific property additions for the DSIC.

3 Q. How do you respond to the assertion that substation equipment improvements
4 should not be DSIC-eligible property?

5 A. OTS witness Gruber asserts that electric substation equipment is analogous to
6 water pumping stations and, in reliance on a Commission Order in *Petition of the*
7 *Columbia Water Company for Approval to Implement a Tariff through*
8 *Supplement Establishing a Distribution Improvement Charge*, Docket No.
9 P-00021979 (April 17, 2003) (“*Columbia*”), recommends that substation
10 equipment not be eligible for recovery under DSIC. The Company initially
11 responds that, regardless of whether water pumping stations are an appropriate
12 analogy for electrical substations, the Commission’s order in the cited case is not
13 relevant because it addresses the proposed construction of a new water pumping
14 station whereas the Company’s proposal is for the recovery of costs related to
15 the replacement of existing, deteriorated or failed substation equipment and not
16 the installation of new substations. Indeed, the Company’s proposal is consistent
17 with the Commission’s *Columbia* Order which states that the intent of DSIC “is to
18 allow cost recovery for distribution system improvement projects requiring
19 immediate implementation due to risk imposed by aging infrastructure or to
20 government-imposed requirements.” (*Columbia* Order, p. 14)

21 Furthermore, with regard to the inclusion of the pumping station, the
22 Commission explained at pages 11 – 12 of the *Columbia* Order, the particular
23 pumping station at issue there was an integral part of the facilities for providing

1 emergency water storage and treatment; it was not an integral part of the
2 distribution system. At page 15 of the *Columbia* Order, the Commission
3 explained that this was the basis for its decision that the pumping station be
4 excluded from the DSIC. The Commission did not adopt any rule that pumping
5 stations should never be included in a water utility's DSIC. The decision was
6 instead based upon the unusual circumstances of that particular pumping station.
7 The *Columbia* Order does not support the OTS' proposed exclusion of substation
8 plant additions from PPL Electric's DSIC.

9 Unlike the pumping station at issue in *Columbia*, an electric substation is
10 an integral part of PPL Electric's distribution system. Initially, I note that a small
11 portion of PPL Electric's substations are related to transmission, not distribution,
12 functions. By restricting substation equipment eligible for the DSIC to Account
13 362, however, PPL Electric has restricted DSIC eligible substation additions and
14 replacements to distribution operations and excluded transmission-related
15 substations.

16 As I noted, such substations are an integral part of PPL Electric's
17 distribution system. Electricity is delivered to PPL Electric's distribution system
18 from electric generation stations at high transmission voltages. At substations,
19 voltage levels are reduced to distribution voltage levels so that electricity can be
20 safely provided to the public. Indeed, all electricity distributed by PPL Electric to
21 customers (excluding customers who take service at transmission voltages) flows
22 through substations. The argument that substations are not an integral part of
23 PPL Electric's distribution system is erroneous.

1 Q. Have parties raised other issues with regard to the DSIC?

2 A. Yes, certain parties have indicated that approval of PPL Electric's proposed
3 DSIC would create the possibility that PPL Electric could over achieve its allowed
4 rate of return as a result of other revenue requirement reductions or increases in
5 revenues that are not reflected in the proposed DSIC (OSBA Statement No. 1,
6 p. 5; OCA Statement No. 2, pp. 6-7; DOD Statement of T. Prisco, p. 11; PPLICA
7 Statement No. 1, pp. 46-50; Pa EC Statement No. 1, p. 11). Such concerns are
8 unrealistic. Specifically, I note that, despite the many efficiencies and savings
9 that PPL Electric has implemented since its last base rate case in 1995, PPL
10 Electric's return on equity has continued to erode. In 2003, PPL Electric
11 achieved a return on equity of less than 2 percent. Return on equity is expected
12 to decline to about 1 percent in 2004 (PPL Electric Statement No. 1, p. 3).

13 Added to PPL Electric's history of declining returns on equity is the
14 substantial nature of its construction budget. As set forth in Exhibit DAK-1, PPL
15 Electric plans to spend on average almost \$200 million annually on construction
16 through 2008. Only a small portion of these expenditures would be reflected on
17 the DSIC, but this additional investment in new plant will drive increases in
18 revenue requirements particularly with regard to depreciation, return and income
19 taxes. The combination of the history of PPL Electric's declining returns on
20 equity and its substantial and growing construction budgets suggest strongly that
21 there is no realistic likelihood that PPL Electric will be able to achieve more than
22 its allowed rate of return in the foreseeable future.

1 Further, PPL Electric submits to the Commission quarterly earnings
2 reports pursuant to the requirements of 52 Pa. Code Ch. 71, regarding financial
3 reports. Thus, the Commission has available for its review – four times each
4 year – reports to determine whether PPL Electric is achieving more than its
5 allowed rate of return. Such reports are available to the public. Therefore, any
6 party who believes that PPL Electric is achieving more than its allowed rate of
7 return can raise such matters for review in proceedings before the Commission.

8 Q. Certain parties have objected to PPL Electric's proposed DSIC on the grounds
9 that certain of the plant additions eligible for the DSIC may reduce operation and
10 maintenance expenses (OCA Statement No. 2). Are those concerns justified?

11 A. No, they are not. Initially it must be noted that only a small portion of PPL
12 Electric's plant additions will be eligible for the DSIC. As I explained at page 38
13 of my direct testimony, PPL Electric Statement No. 4, in a typical year, only about
14 \$26 million of plant additions annually would be eligible for the DSIC. This
15 amount should be contrasted with the totality of PPL Electric's construction
16 program which is expected to be about \$200 million per year over the five years
17 ending 2008. Thus, only about 13 percent of PPL Electric's construction and
18 plant additions will be eligible for the DSIC. An investment of this magnitude will
19 not have a substantial effect upon total operation and maintenance expenses.

20 The plant additions eligible for the DSIC will not cause PPL Electric's
21 operation and maintenance expense to be reduced. It must be recalled that,
22 each year, PPL Electric's distribution system is another year older. The small
23 portion of the distribution system that will be replaced by property additions

1 eligible for the DSIC will not materially alter that process. The original cost of
2 PPL Electric's total depreciable plant as of December 31, 2004, is
3 \$4,398,361,788 (Exhibit JJS-1, p. III-5). Thus, DSIC eligible plant additions
4 constitute only about 0.6 percent of PPL Electric's total original cost of plant (\$26
5 million ÷ \$4,398 million). Although it is possible that operation and maintenance
6 expense may be reduced for the particular distribution system component being
7 replaced, there is no reason to believe that PPL Electric's overall operation and
8 maintenance expenses will be reduced as a result of property additions eligible
9 for the DSIC.

10 Q Certain parties have objected to the inclusion of depreciation on qualifying plant
11 additions for recovery under the DSIC on the grounds that existing rates already
12 have a provision for depreciation on the plant being replaced (OSBA Statement
13 No. 1). Are these concerns well-founded?

14 A. No, they are not. Providing for depreciation recovery on qualifying plant
15 additions is necessary to avoid having the Company experience attrition as a
16 result of the qualifying plant addition.

17 On PPL Electric's books, under the Uniform System of Accounts, when old
18 plant is retired and replaced by new plant, the plant balance and the accumulated
19 reserve for depreciation both are adjusted by equal amounts to reflect the
20 retirement of the old plant. Thus, there is no change in net plant as a result of
21 retirement. Similarly, because PPL Electric's depreciation accrual rate applicable
22 to the plant account in which the retired plant was recorded does not change as a
23 result of any specific retirement, PPL Electric's depreciation accrual does not

1 change as a result of the retirement. The annual accrual per books is the result
2 of applying the accrual rate to the net plant balance, and neither changes as a
3 result of a retirement. Therefore, there should be no adjustment to depreciation
4 expense due to the retirement of DSIC eligible property.

5 As a result of the plant addition, however, the plant balance to which the
6 accrual rate is applied increases, and therefore, PPL Electric's annual
7 depreciation accrual, per books, increases as a result of the plant addition. The
8 treatment of depreciation related to replacement of plant eligible for the DSIC
9 proposed by PPL Electric reflects PPL Electric's depreciation accounting per
10 books, and it is appropriate for ratemaking to follow plant accounting in these
11 matters. I note also that PPL Electric's DSIC proposal in this regard follows
12 exactly procedures employed by water and sewer utilities in their Commission-
13 approved DSICs or CSICs.

14 Q. How do you respond to the assertion that the Company has failed to demonstrate
15 a need for DSIC?

16 A. PPLICA witness Baron asserts that the Company has failed to identify any
17 "changed circumstances" that would necessitate the establishment of a DSIC.
18 The Company responds that, in fact, circumstances have changed and, although
19 the consequences of those changes have yet to be experienced, the Company's
20 DSIC proposal is designed to avoid future adverse consequences that may be
21 experienced by the Company and its customers. The "changed circumstances"
22 that the DSIC proposal responds to are the aging of the Company's distribution
23 infrastructure.

1 In analyzing its distribution plant, the Company has identified concerns
2 regarding the age of plant and the fact that a significant amount of plant will need
3 to be replaced in the not too distant future. Records show that 106,050 poles
4 were installed during the 1950's, but with increased demand for electricity, that
5 number grew to 184,104 installed during the 1960s and 234,046 installed during
6 the 1970s before dropping to 157,424 during the 1980s and 136,530 during the
7 1990s. As the large numbers of poles installed during the 1960s and 1970s age,
8 the number of poles that will require replacement will grow dramatically.

9 Other plant accounts show similar results. This is not surprising because
10 other areas of our nation's infrastructure including highways, bridges, water
11 systems, and sewer systems also are aging. PPL Electric sees this as a
12 "changing condition" and has proposed DSIC as a proactive measure to
13 anticipate an increasing need for capital to address the issues associated with
14 aging infrastructure and to manage that issue so that it does not adversely
15 impact customers.

16 Q. How do you respond to the criticism that collecting DSIC on a kWh basis is
17 inappropriate?

18 A. The Company believes that such a collection mechanism is appropriate based on
19 the following considerations:

- 20 • As proposed, DSIC would be limited to not more than 5% of distribution
21 charges. This safeguard limits the amount of additional usage-based
22 charges that can be reflected in rates.

- 1 • As proposed, the DSIC would be reset to zero in base rate proceedings so
2 there would, in fact, be no usage-based charges for up to a year following
3 a base rate proceeding.
- 4 • The annual review and reconciliation of a kWh mechanism is much
5 simpler and more reliable than a reconciliation of a demand-based charge,
6 the most likely other alternative, because residential demand is
7 determined by load survey whereas usage is measured directly. The
8 Company believes that this improves the auditability of DSIC.

9 Q. OSBA, DOD, PEC and PPLICA have argued that recovering the DSIC on a
10 uniform amount per kWh basis caused a greater portion of DSIC costs to be
11 recovered from large customers. Are these concerns valid?

12 A. These criticisms are arithmetically correct to the extent that recovery of DSIC
13 expenses based upon a uniform amount per kWh would tend to recover
14 proportionately more DSIC costs from large customers. In order to address
15 these concerns, PPL Electric, as an alternative, is willing to calculate the DSIC as
16 a percentage to be applied to distribution rates. In that way, DSIC recoveries
17 would follow the Commission's allocations of plant in this proceeding as reflected
18 in rates for distribution service. Use of a uniform percentage would reduce
19 overall DSIC charges to large customers. I note that the DSICs of water
20 companies are expressed as a percentage, and not as an amount per thousand
21 gallons or hundred cubic feet of water. *Re. Pennsylvania-American Water Co.*,
22 86 Pa. PUC, *supra*, p. 424. Thus, use of a uniform percentage applied to
23 distribution rates would make PPL Electric's proposed DSIC similar to the DSICs

1 that the Commission has approved for water utilities and the CSICs that have
2 been approved for sewer utilities.

3 Q. Witness Epstein asserts that the proposed DSIC is discriminatory because it
4 would only be applied to customers taking service at 12,470 volts or below. How
5 do you respond to the assertion that DSIC is discriminatory?

6 A. The Company proposes to exclude customers taking service above 12,470 volts
7 because those customers are not served by the distribution system (other than
8 metering, billing, and other common costs) and, therefore, do not benefit from the
9 investments in the distribution system designated as eligible for collection under
10 the proposed DSIC. The Company does not view its proposal as discrimination
11 toward customers served at lower voltages, but rather as an issue of being fair to
12 the customers who take service at the higher voltage levels.

13 Q. Some parties have argued that the annual process proposed by PPL Electric for
14 its DSIC is unrealistic (OCA Statement No. 2, pp. 5, 9-10). Are such concerns
15 valid?

16 A. No, they are not. Initially I note that the DSICs of water utilities and the CSICs of
17 sewer utilities are filed quarterly, effective upon one month's notice. Re:
18 *Pennsylvania-American Water Co.*, 83 Pa. PUC 415, 423 (1986). I am not aware
19 of any procedural problems caused by these filings. PPL Electric also proposes
20 to file its DSIC on one month's notice, but it will be filed only once each year,
21 thereby imposing far less burden on the Commission than the DSICs of water
22 utilities.

1 Given the fact that water DSICs have been in effect for approximately
2 eight years, with rates changing four times each year upon one month's notice,
3 there is no reason to believe that a similar process proposed by PPL Electric
4 would be as difficult as has been suggested.

5 Further, PPL Electric itself has experience with changes of rates upon
6 exactly the same schedule as the Company has proposed for the DSIC in this
7 proceeding. This schedule has worked for the reconciliation and annual
8 adjustment of PPL Electric's Intangible Transition Charges ("ITCs") and
9 Competitive Transition Charges ("CTCs").

10 Q. Certain parties have contended that the DSIC is inappropriate because it would
11 permit rate changes without regulatory review of rates (OCA Statement No. 2,
12 pp. 5, 10; PPLICA Statement No. 1, pp. 46-50). Are such concerns justified?

13 A. No, they are not. Initially, I note that the rates would not change without
14 Commission approval. Supplement No. 38 to Tariff – Electric Pa. P.U.C. No.
15 201, p. 19Z.3. Further customers will have a full and fair opportunity to challenge
16 the DSIC in general or the specific charge that is in effect at any time. If any
17 customer affected by the DSIC wishes to challenge it, such issues could be
18 raised in a standard complaint. PPL Electric's DSIC will not escape regulatory
19 review.

20 Q. Certain parties have contended that the DSIC is inappropriate because PPL
21 Electric will need to implement accounting and information systems to track costs
22 and identify specifically plant additions eligible for the DSIC (OCA Statement No.
23 2, p. 9). Are these contentions justified?

1 A. No, they are not. Upon the Commission's approval of the DSIC, PPL Electric will
2 implement all accounting and information systems that are needed to track DSIC
3 plant additions, costs and revenues. PPL Electric will submit to the Commission
4 information preserved through such systems in its annual filings and annual
5 reconciliations. Again, as I have noted with regard to the water utility DSIC and
6 the sewer utility CSIC, they present the same implementation issues as does
7 PPL Electric's proposed DSIC, but substantial problems have not materialized
8 with regard to the water utility DSICs or sewer utility CSICs.

9 Q. Are there any other points raised by other parties that you wish to address?

10 A. Yes. On page 17 of his testimony, Witness Epstein states, "Additionally, the '\$26
11 million in property additions' that PPL believes is 'eligible' under DISC surcharge
12 should be rejected in its entirety." If by this statement Witness Epstein means
13 that no property additions should be eligible for recovery under DSIC, then I
14 believe that I have already provided rebuttal testimony on that point. However, if,
15 by his statement, Witness Epstein is saying that such additions should never be
16 reflected in rate base, then the Company responds as follows:

- 17 1. The \$26 million represents the Company's estimate of plant additions in
18 2005 that would meet its eligibility definition. Those additions are not being
19 claimed as additions to rate base in this proceeding.
- 20 2. The Company believes that property additions that meet its eligibility
21 definition represent prudent investments necessary to provide reliable
22 service to customers that should be included in rate base.

Transmission Service Charge

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Q. Please describe the Company’s proposal in this case regarding the establishment of a Transmission Service Charge (“TSC”).

A. PPL Electric’s current tariff permits it to charge all of its Provider of Last Resort (“POLR”) customers for FERC-approved transmission charges. The Company has proposed a transmission rate tracking mechanism that would function in a manner similar to the former Energy Cost Rate. The proposed tracker would be reset annually to (1) reflect the current level of transmission charges and forecast of POLR sales and (2) a reconciliation of prior year collections to costs.

Q. Have other parties criticized PPL Electric’s proposed TSC?

A. Yes. Several parties have opposed various portions of PPL Electric’s proposed TSC. However, no party has opposed PPL Electric’s recovery of its transmission service costs.

Q. Can you summarize those criticisms and respond to them?

A. Yes, I can. Several parties have indicated that, in their view, recovery of transmission service expenses should not be subject to reconciliation (OTS Statement No. 5, p. 13; PPLICA Statement No. 1, p. 28; Pennsylvania Energy Consortium Statement No. 1, p. 11). Such contentions are based, in part, on such parties’ interpretations of various provisions of the Public Utility Code. PPL Electric will respond fully to such legal arguments in its briefs. My previous discussion of the legality of automatic adjustment clauses with regard to PPL Electric’s proposed DSIC substantially applies also to the proposed TSC.

1 These parties contend also that, in their view, recovery of transmission
2 service charges should not be subject to reconciliation as a matter of public
3 policy. Such contentions are erroneous. Reconciliation of recovery of
4 transmission service costs through an automatic adjustment clause is
5 appropriate because the expenses are substantial, the expenses are subject to
6 substantial variation and the variation is beyond the control of the utility.

7 Clearly, transmission service charges are substantial. As shown on
8 Exhibit Future 1, Schedule D-3, page 1, projected transmission revenues to be
9 collected from POLR customers during 2004 are approximately \$143 million,
10 which is substantial especially when compared to PPL Electric's projected
11 distribution revenues for the same period of \$500 million. For 2005, with the
12 expiration of the rate cap, transmission service revenues are expected to
13 increase by approximately \$57 million to match the actual amounts charged to
14 PPL Electric by PJM. Thus, total transmission service charges for 2005 are
15 expected to be approximately \$200 million (\$143 million + \$57 million) which is
16 approximately 29 percent of PPL Electric's distribution revenues at proposed
17 rates (\$200 million ÷ \$688 million.) For distribution revenues at proposed rates,
18 see Exhibit Future 1, Schedule D-1.

19 Although increases in transmission service charges may not be of this
20 magnitude in the years immediately after 2005, the Company expects substantial
21 annual changes in the levels of transmission service charges in the future.
22 History supports this belief as transmission costs to serve POLR load have been
23 \$139,950,000 in 2000, \$178,406,000 in 2001, \$170,329,000 in 2002, and

1 \$194,350,000 in 2003. Levels of transmission charges will vary in the future
2 based upon the total amounts of transmission costs incurred by members of the
3 PJM Interconnection, Inc. ("PJM"), changes in procedures under the PJM's Open
4 Access Transmission Tariff ("OATT") by which transmission expenses are
5 apportioned among the load serving members of the PJM such as PPL Electric
6 and changes in the amount and seasonality of the peak and annual load of PPL
7 Electric's POLR customers. PPL Electric's POLR customers' load data are the
8 input from PPL Electric for the PJM transmission allocation procedures set forth
9 in the OATT.

10 Further, PPL Electric's transmission service charges are not subject to its
11 control. As indicated above, such charges are imposed under PJM's OATT.
12 PPL Electric does not control PJM. Although PPL Electric is a voting member of
13 the PJM, it casts only one vote among over 200 voting members. Furthermore,
14 in accordance with PJM bylaws, the vote of the membership is simply a
15 recommendation to the PJM Board which has ultimate decision-making authority.
16 Thereafter, any change to PJM's OATT must be proposed to the Federal Energy
17 Regulatory Commission ("FERC") for its consideration. It cannot be contended
18 that PPL Electric controls the procedures under which transmission expenses are
19 allocated to it.

20 Nor does PPL Electric control the basis on which these transmission
21 expenses are allocated. The principal data which are used to allocate
22 transmission expenses among load serving entities in the PJM are their
23 contributions to the coincidental peaks of the PJM and their annual kWh usage.

1 Such factors are simply the accumulation of usage by all of PPL Electric's POLR
2 customers. PPL Electric gathers the data and provides the data, but PPL Electric
3 does not control the data. The data reflect customers' usage, and customers
4 control their usage, not PPL Electric. Thus, PPL Electric cannot control any
5 element of the process by which transmission service expenses are charged to it.

6 Q. Should PPL Electric's recovery of transmission expenses be subject to a
7 prudence review, as suggested by the OTS (OTS Statement No. 5, p. 15)?

8 A. No, it should not. The OTS refers to the Commission's annual investigations of
9 recovery of purchased gas costs by large local natural gas distribution
10 companies under Section 1307(f) of the Public Utility Code as an example of an
11 appropriate prudence review. OTS' analogy is flawed. In fact, when the annual
12 reviews of purchased gas cost decisions are analyzed, they demonstrate why no
13 prudence review is appropriate for transmission expenses.

14 As explained above, PPL Electric cannot control its charges from the PJM
15 for transmission services under the OATT, which is part of a FERC-approved
16 tariff. Total charges are based entirely upon procedures established by the PJM
17 subject to FERC approval and by PPL Electric's POLR customers' usage. Nor
18 can PPL Electric "shop around" for transmission services. PJM provides the
19 transmission services and the cost of those services is governed by PJM's
20 OATT. Therefore, there is no opportunity for transmission shopping on the PJM.

21 In contrast, local natural gas distribution companies, which are subject to
22 annual Section 1307(f) investigations, can control many aspects of their
23 purchased gas costs. Local natural gas distribution companies control the levels

1 of pipeline transportation and storage capacity for which they contract. It is
2 possible for a local natural gas distribution company to contract for more capacity
3 than needed to meet its customers' requirements. In addition, depending on the
4 pipeline system, a local natural gas distribution company may be able to obtain
5 pipeline capacity or storage capacity from any of several suppliers. Shopping for
6 pipeline and storage capacity may be available.

7 Further, local natural gas distribution companies may choose among a
8 wide variety of suppliers of natural gas for the commodity. Natural gas
9 distribution companies also choose the type of contract under which they
10 purchase natural gas. Natural gas may be purchased in the spot market or
11 under longer term contracts and at variable or fixed rates. There is no equivalent
12 for electric distribution companies with regard to transmission expenses on the
13 PJM.

14 Local natural gas distribution companies make all of these decisions, and
15 each of these decisions can have substantial impacts on customers. Because
16 local natural gas distribution companies exercise substantial discretion over their
17 natural gas purchases and transportation, it is reasonable for the Commission to
18 review their use of such discretion to make certain that it was exercised for the
19 benefit of the public.

20 Unlike local natural gas distribution companies, there is, as a practical
21 matter, nothing for the Commission to review with regard to transmission service
22 charges. PPL Electric realistically has no discretion with regard to the level of
23 transmission expenses that it incurs on the PJM; there is no exercise of

1 discretion for the Commission to review. Therefore, a prudence review of PPL
2 Electric's transmission expenses would be unnecessary and wasteful.

3 Q. OTS also contends that PPL Electric's present tariff does not provide for
4 automatic pass through of transmission costs (OTS Statement No. 5, p. 15). Do
5 you agree with that contention?

6 A. No, I do not. OTS correctly acknowledges that all rate schedules of PPL
7 Electric's presently-effective tariff contain the following language:

8 "The Company will provide and charge for transmission service
9 consistent with the PJM Open Access Transmission Tariff approved
10 or accepted by the Federal Energy Regulatory Commission for
11 customers who receive Basic Utility Supply [POLR] Service from
12 the Company unless such customers obtain transmission service
13 from another provider."

14 This tariff language became effective pursuant to the Commission's approval of
15 the "Joint Petition for Full Settlement of PP&L, Inc.'s Restructuring Plan and
16 Related Court Proceedings" in the Final Order entered on August 27, 1998, in
17 *Application of Pennsylvania Power & Light Company for Approval of its*
18 *Restructuring Plan under Section 2806 of the Public Utility Code,*" at Docket No.
19 R-00973954. All parties to that proceeding joined in the settlement. Pursuant to
20 this tariff language, PPL Electric has charged POLR customers an unbundled
21 rate for transmission service since January 1, 1999.

22 The OTS interpretation of the above-quoted provision of PPL Electric's
23 tariff is inconsistent with its plain language. PPL Electric can "provide and

1 charge” for transmission service consistent with the PJM OATT only if PPL
2 Electric can pass through its actual charges from the PJM to its POLR customers
3 on a timely basis as the OATT is changed from time to time subject to FERC’s
4 regulatory review. Although the above-quoted tariff provision does not set forth
5 the precise mechanics by which such results are to be accomplished, it does
6 make clear that PPL Electric is to charge for transmission service consistent with
7 the PJM OATT. OTS’ proposal would render the above-quoted provisions of
8 PPL Electric’s tariff meaningless.

9 In essence, PPL Electric’s TSC proposal in this proceeding merely
10 provides specific procedures for implementation of the tariff provision established
11 in PPL Electric’s restructuring proceeding that permits PPL Electric to charge
12 POLR customers for transmission service consistent with the PJM OATT.

13 Q. OTS contends that transmission service charges incurred by PPL Electric should
14 be recovered as “an unbundled transmission rate that is non-reconcilable” (OTS
15 Statement No. 5, p. 13). Do you agree with this proposal?

16 A. No, I do not. The proposal is incorrect for the reasons which I have explained
17 previously. If, however, the Commission were to determine that the OTS
18 proposal should be adopted, and that PPL Electric should recover transmission
19 expenses as an unbundled transmission rate that is not reconcilable, then the
20 appropriate level of transmission service expenses to be recovered by PPL
21 Electric based upon the best available information in this proceeding would be
22 0.564 cents per kWh. This amount reflects the total amount of annual
23 transmission service charges projected to be incurred by PPL Electric during the

1 2004 test year of \$198,973,679 divided by projected retail kWh sales of
2 35,342,287,000 kWh. These figures reflect adjustments for price response and
3 contract customers who pay for transmission service through those rates and the
4 dollar amount reflects gross receipts tax at the rate of 59 mills. This information
5 is contained in Exhibit DAK2.

6 Q. Is this also the rate PPL Electric proposes to charge in 2005 if the TSC is
7 approved?

8 A. Yes. While PPL Electric's proposal for TSC involves end-of-year filings, that
9 process must be modified this year in light of the expectation that the
10 Commission will not issue a Final Order in this proceeding until December 2004.
11 In order to address this situation, the Company wishes to establish in this
12 proceeding that the transmission costs to be collected from POLR customers
13 during 2005 are \$198,973,679 and that the associated rate, consistent with the
14 Company's proposed collection mechanism, is 0.564 cents per kWh.

15 Q. Do you agree with OCA witness Morgan's comments regarding changes in PPL
16 Electric's projections for revenues from Point-to-Point (PTP) service for 2004?

17 A. No. First it must be understood that the projected \$3.4 million dollar reduction in
18 PTP revenues between the 2003 historic test year and the 2004 future test year
19 was based on the assumption that the FERC order to eliminate regional through
20 and out rates (RTORs) would be effective April 1, 2004 (not April 4, 2004 as
21 stated by Mr. Morgan). The subsequent settlement (at FERC Docket No. EL01-
22 111) postponed the elimination of RTORs until December 1, 2004. PPL Electric's
23 update of its 2004 projected revenues from PTP service is \$4.1 million, which is

1 \$2.9 million, not \$3.4 million, lower than the 2003 historic test year revenues of
2 \$7.0 million.

3 Q. Does the updated \$2.9 million decrease in the projected PTP revenues change
4 the projected \$57.2 million increase in transmission service charges projected by
5 PPL Electric?

6 A, No. The transmission revenue requirement which is projected to increase by
7 \$57.2 million is based on the transmission service charges that PPL Electric
8 expects to be billed by PJM under the PJM Open Access Transmission Tariff
9 (OATT) as a Load Serving Entity (LSE) providing service to POLR customers.
10 The revenues PPL Electric receives from PJM as its share of other parties' PTP
11 reservations on the PJM system are recovered pursuant to FERC jurisdictional
12 PJM agreements and consistent with PPL Electric being a transmission owner in
13 PJM. The revenue PPL Electric receives as a transmission owner is separate
14 and distinct from the transmission service charges PPL Electric incurs as a Load
15 Serving Entity providing service to POLR customers. Revenues that PPL Electric
16 receives as a transmission owner are reflected in Exhibit Future 1, Statement D-3
17 on the line "Other Electric Revenues" under the heading "Transmission Rate
18 Revenue." Both the costs and revenues associated with PPL Electric's provision
19 of transmission service as a transmission owner have been removed from the
20 distribution revenue requirement in this case. Thus, any adjustment would be to
21 these figures and would not affect the Company's distribution revenue
22 requirement or the transmission service charges it incurs as an LSE under the
23 PJM OATT.

1 Q. Wouldn't the reduction in revenues to transmission owners ultimately reduce the
2 amount paid by LSEs?

3 A. In theory, yes, but not for PPL Electric as a POLR provider. The adjustment
4 identified by witness Morgan relates to PTP service, not Network Integration
5 Transmission Services. PPL Electric, as an LSE, does not purchase PTP service
6 to supply its POLR load. The change in PTP revenues, therefore, would not
7 affect the costs it incurs as an LSE.

8 Q. Several parties have criticized PPL Electric's proposed allocation of transmission
9 service charges among classes of customers based upon POLR energy sales,
10 that is, a uniform amount per kWh, regardless of the customer class. Do you
11 agree with such criticisms?

12 A. In my direct testimony, PPL Electric Statement No. 4, I explained that PPL
13 Electric's proposed allocation of transmission service charges among rate
14 classes and customers within each rate class based on kWh of POLR sales is
15 desirable for two important reasons. First, the proposed allocation is simple in
16 that it is easily understood by customers and easily applied. Second, such
17 allocation helped PPL Electric to meet its rate allocation objective of having no
18 single rate class, as a whole, experience increases in its total bills in excess of
19 10 percent. For these reasons, PPL Electric continues to believe that its initial
20 proposed allocation of transmission service charges is preferable to alternatives
21 suggested by other parties.

22 Having said that, however, it must be acknowledged that pursuant to the
23 PJM OATT, approximately 70 percent of transmission service charges incurred

1 by PPL Electric are allocated on the basis of POLR customers' contributions to
2 coincident peaks on the PJM system; although, because only 27% of the load is
3 recorded on interval meters, about 73% of this component is distributed to rate
4 schedules and customers on a pro rata basis consistent with their kWh usage –
5 not their actual demand. The remaining 30 percent of transmission service
6 charges are allocated by PJM among load serving entities based upon kWh of
7 sales.

8 In considering whether to re-allocate transmission charges, the
9 Commission should be aware that allocations of transmission service expenses
10 among customer classes or rate schedules based upon principles of cost
11 causation could vary substantially from year to year. The reason for such
12 substantial variation is that PPL Electric has experienced both winter and
13 summer peaks. For example, over the last four years, PPL Electric has been a
14 winter peaking company in 2000 and 2003 and a summer peaking company in
15 2001 and 2002. Whether PPL Electric's load peaks in the summer or in the
16 winter can change from year to year, and there is no clear trend that either
17 summer peaking or winter peaking will become dominant in the near future.

18 If the Commission were to determine that transmission charges should be
19 allocated based upon principles of cost causation, PPL Electric would reallocate
20 charges annually, consistent with PJM OATT procedures, based upon its actual
21 peak – either winter or summer – during the prior year ended November 30.
22 Allocations among customer classes based upon summer peaks produces
23 substantially different results from allocations based upon winter peaks.

1 To illustrate the effect of peaks in different seasons, I have calculated, for
2 illustrative purposes, the allocations of transmission expenses and rates among
3 the rate schedules based upon the winter peak in 2003 and the summer peak in
4 2002. Exhibit DAK3 shows rates based upon allocations reflecting the 2003
5 winter peak. Exhibit DAK4, in contrast, shows rates based upon allocations
6 reflecting the 2002 summer peak. To make the rates comparable, these two sets
7 of rates are designed to recover the same total amount of transmission charges.
8 As can be seen by comparing the two schedules, the allocations among rate
9 schedules and customer classes vary substantially based upon whether the 2002
10 summer peak or 2003 winter peak is used to allocate transmission service
11 charges. I note that this variability of the allocations among rate classes is a
12 further reason why PPL Electric should recover transmission service charges
13 based upon annual rate adjustments with reconciliation.

14 The rates in Exhibit DAK3 are illustrative of the rates that would go into
15 effect on January 1, 2005, for recovery of transmission expenses if the
16 Commission determines that PPL Electric should recover transmission charges
17 through an unbundled transmission rate under which transmission charges are
18 allocated among the rate schedules based upon principles of cost causation.
19 The exact rates would be determined as part of PPL Electric's compliance filing.
20 Under this proposal, the charges are allocated among rate schedules based
21 upon the procedures set forth in the PJM OATT. Transmission charges would
22 then be recovered within each rate schedule based upon a uniform rate per kWh.

1 Q. PPLICA has proposed that, for those classes of customers with interval meters,
2 transmission rates be developed on a demand/energy basis to follow more
3 precisely the PJM OATT procedures (PPLICA Statement No. 1, pp. 13-18). Do
4 you agree with this proposal?

5 A. No. In my opinion, developing demand/energy rates for recovery of transmission
6 charges within rate schedules for large customers is an unnecessary
7 complication that will make little practical difference given the similar load
8 characteristics of large customers. If the Commission were to approve the
9 PPLICA proposal, however, it is critical that reconciliation be implemented on
10 either a demand basis or an energy basis, but not both. Reconciliation over two
11 rate elements would be extremely difficult to implement and administer.

12 Q. Do you have any other alternatives for consideration by the ALJ, the Commission
13 and the parties?

14 A. Yes. Exhibit DAK3 also contains, as another alternative, illustrative rates for
15 recovery of transmission charges for each of three broad classes of customers.
16 This approach allocates transmission charges based upon principles of cost
17 causation among three broad categories and recovers those transmission
18 charges within each broad class based upon kWh of sales. The use of fewer
19 groupings for recovery of transmission charges would promote rate stability and
20 simplify administration of recovery of transmission expenses.

21 Under this alternative, the first class of customers would be all residential
22 customers. The second class would include smaller commercial, industrial and
23 municipal customers served under Rate Schedules GS-1, GS-3, BL, GH, IS-1.

1 and all lighting rate schedules. The third group of customers would be large
2 customers served under all large power, interruptible and price response rate
3 schedules. These are the same groups that are used for reconciliation of PPL
4 Electric's Competitive Transition Charges ("CTCs") and Intangible Transition
5 Charges ("ITCs"). Again, these rates are for illustrative purposes, only, and exact
6 rates for 2005 would be calculated as part of the compliance filing.

7 Q. If the Commission were to decide that a portion of transmission service charges
8 should be allocated on a demand basis, does PPL Electric have a specific
9 proposal for reconciliation of transmission expenses under these circumstances?

10 A. Yes, PPL Electric does have such a proposal. As an alternative to PPL Electric's
11 preferred method of recovering costs and reconciling recoveries based upon the
12 uniform amount per kWh of sales, PPL Electric would be willing to follow a
13 procedure very similar to those approved by the Commission in PPL Electric's
14 restructuring proceeding for recovery and reconciliation of CTCs and ITCs.

15 PPL Electric would be willing to allocate costs among rate schedules
16 based upon procedures set forth in PJM's OATT, as amended from time to time
17 subject to FERC approval. PPL Electric, however, would reconcile recoveries
18 with expenses not by individual rate schedule, but by the three broad classes of
19 customers identified previously. The three groups of customers for reconciliation
20 would be the same as those for the alternative proposal for recovery of
21 transmission expenses. Reconciliation by large, broad groups, instead of
22 individually by the numerous rate schedules will reduce volatility in rates due to
23 small or variable kWh sales for the smaller, individual rate schedules. Using

1 broad categories for purposes of reconciliation also will reduce substantially the
2 costs of administering the recovery of transmission charges.

3 **Allocation of Distribution Revenue Requirements**

4 Q. Please describe the Company's proposal in this case regarding the allocation of
5 distribution revenue requirements.

6 A. While PPL Electric believes in the principle that customer rates should reflect the
7 costs those customers place on the distribution system, there are certain aspects
8 of this request that would result in significant disruptions to the rates of certain
9 customer classes if that principle is strictly followed. PPL Electric believes that a
10 gradual approach is appropriate and, accordingly, the allocations proposed by
11 the Company are intended as a first step and reflect the following objectives:

- 12 1. Keep the increase on a total-bill basis to all residential rate schedules
13 below 10%. "Total-bill" basis means that the allocation process included
14 both the distribution increase proposed in this case and an estimate of the
15 increase in the transmission service charge pass-through that will also
16 occur on January 1, 2005.
- 17 2. Keep the increase on a total-bill basis to all rate schedules below 10%.
- 18 3. Bring the rate of return for customers taking service at 69,000 volts closer
19 to the system average rate of return.

20 Q. Please describe the issues raised by other parties.

21 A. PPLICA witness Stephen Baron, DOD witness Kenneth Kincel, and OSBA
22 witnesses Robert Knecht and Mark Ewen, while generally acknowledging that
23 cost of service based allocations may be tempered by other factors, argue that

1 PPL Electric's proposal does not go far enough in the direction of cost-based
2 allocations. Although the details of each witness's proposal are different, all
3 recommend some amount of gradualism as evidenced by the fact that none
4 recommends a strict adherence to cost causation principles. The disagreement
5 appears, then, to not be one of approach, but one of degree.

6 Q. Do any parties agree with PPL Electric's proposal?

7 A. Yes. OCA witness Richard Galligan supports PPL Electric's approach. OCA
8 witness Galligan observes, correctly in PPL Electric's opinion, that, when viewed
9 as a whole, electric rates remain in a transitional period until the generation rate
10 cap expires. It is, therefore, unnecessary and inappropriate to move rapidly to
11 "correct" the allocation of distribution revenue requirements when other bill
12 components that remain capped may continue to be "incorrect." PPL Electric
13 agrees with OCA witness Galligan that "considerations such as gradualism,
14 stability, understandability, acceptance, simplicity, etc." are important issues for
15 commissions to factor into the setting of rates.

16 Q. Has the Company's proposal changed in light of the issues raised by PPLICA,
17 DOD, and OSBA?

18 A. No, it hasn't. The Company continues to believe that the combined impact of
19 changes in distribution rates and the transmission service charge pass-through
20 should be considered in the context of their impact on the total bill. The
21 Company also continues to believe that 10% is an important threshold, especially
22 considering that electric rates are in the middle of a transition that will provide
23 other opportunities, such as the completion of stranded recoveries, to achieve

1 additional "corrections" without introducing disruptive distortions of individual
2 unbundled components.

3 Q. Does the Company have an opinion as to how proposed revenue allocations
4 should be adjusted in the event that overall revenue requirements granted in this
5 proceeding are lower than the amount requested by the Company.

6 A. PPL Electric believes that a proportional scale-back across all rate schedules
7 would be the most appropriate approach. The Company acknowledges that the
8 scale-back could be skewed across rate schedules in order to provide additional
9 movement toward cost-based allocations. However, such an approach could be
10 considered unfair from the perspective of a party who successfully advocated a
11 revenue reduction, but then may not benefit from the result of that advocacy.
12 Consistent with the views of OCA witness Galligan regarding gradualism, the
13 Company believes that the incremental movement that might be achieved by a
14 scale-back on a non-proportional basis, a departure from normal Commission
15 practice, would be relatively small. When balanced against other considerations,
16 such an approach would be inappropriate.

17 **Amortization and Collection of Hurricane Isabel Costs**

18 Q. Please describe the Company's request regarding the recovery of costs
19 associated with Hurricane Isabel.

20 A. On October 20, 2003, PPL Electric requested Commission authority to defer, for
21 accounting and financial reporting purposes, losses arising from severe damage
22 caused by Hurricane Isabel and to amortize those losses for recovery from
23 customers in a future base rate proceeding. Hurricane Isabel struck PPL

1 Electric's service territory most heavily during the evening of September 19, 2003
2 and the morning of September 20, 2003. The losses which PPL Electric sought
3 to defer were increases in operation and maintenance, customer, and general
4 administrative expenses incurred by the Company in preparing to respond to the
5 damage from Hurricane Isabel, restoring service to customers, assisting
6 customers during the service interruptions, and repairing facilities damaged by
7 the storm. In its petition, PPL Electric specifically acknowledged that it was not
8 requesting that the Commission decide, at that time, whether its deferred losses
9 were recoverable from customers. PPL Electric stated in its petition that
10 approval to recover such losses as well as the length of the amortization would
11 be determined in a future rate base proceeding. The Commission granted PPL
12 Electric's request to defer storm-related losses for accounting and financial
13 reporting purposes in an order entered on January 16, 2004 at Docket No.
14 P-0032069. In this case, PPL Electric is requesting amortization of \$15 million in
15 costs related to Hurricane Isabel over a period of five years. This request is
16 included as an adjustment to Operating and Maintenance Expense in the future
17 test year.

18 Q. Please describe the issues raised by other parties.

19 A. OCA witness Thomas Catlin argues that the costs were incurred during the
20 period that distribution and transmission rates were capped and that, on advice
21 of counsel, recovery of those costs subsequent to the expiration of the rate cap
22 would constitute a de facto exception to the cap in violation of the Electricity
23 Generation Customer Choice and Competition Act ("the Competition Act") and

1 PPL Electric's Restructuring Settlement (Docket No. R-00973954). OCA witness
2 Catlin further argues that, in the event the Commission determines that these
3 costs are recoverable, the portion of the \$15 million associated with regular
4 salaries, wages, and benefits would have been incurred regardless of whether
5 the Hurricane occurred and should, therefore, be excluded. OTS witness
6 Charles Weakley also argues that regular salaries, wages and benefits should be
7 excluded. OTS witness Weakley also argues that a 10 year amortization period
8 is more appropriate. Witness Eric Epstein argues that collection of costs related
9 to Hurricane Isabel would be a violation of the rate cap provisions of the
10 Competition Act. Witness Epstein further argues that if the Company is entitled
11 to rate recovery for extraordinary weather then consumers are also entitled to
12 refunds when the loss of service due to those extraordinary conditions results in
13 quantifiable hardships.

14 Q. How do you respond to the assertion that recovery of these costs would
15 constitute a violation of the rate cap provisions of the Competition Act?

16 A. Counsel advises me that collection of these costs would not be a violation of the
17 rate cap provisions of the Competition Act. The Competition Act specifies, in
18 Section 2804(4)(1)(B), that "the charges of the utility for non-generation services
19 that are regulated as of the effective date of this chapter...shall not exceed the
20 non-generation charges that have been approved by the Commission for such
21 service as of the effective date of this chapter." The Competition Act is silent on
22 the issue of the recovery of costs incurred during the cap period except on the
23 point that charges during the cap period cannot exceed the capped levels. PPL

1 Electric did not request these costs incurred in 2003 be recovered during 2004;
2 i.e., during the cap period. PPL Electric requests that they be recovered starting
3 in 2005; i.e., after the cap period. PPL Electric's request is entirely consistent
4 with the Competition Act.

5 Q. How do you respond to the assertion that regular salaries, wages, and benefits
6 should be excluded from any claim?

7 A. At the start of each year, the Company identifies a scope of work that is
8 necessary to maintain its facilities and to assure an appropriate level of reliability.
9 Activities included in that scope include tree trimming, inspections, testing,
10 preventative maintenance, and repairs. Staffing plans are made consistent with
11 the scope of work. When an event like Hurricane Isabel occurs, all available
12 resources are engaged in storm-related restoration and repair and none of the
13 planned scope of work is done. Nevertheless, that planned work must be
14 completed within a reasonable period of time after storm-related work is
15 completed and overtime and contracting are employed to get the work done.
16 While the Company cannot identify each individual project that incurred
17 contracting and overtime costs as a result of regular time and salaries being
18 devoted to storm-related efforts, the regular salaries accumulated under the
19 storm account provide an estimate of that impact. Such costs are real costs
20 experienced by the Company as a result of the storm.

21 Q. How do you respond to the recommendation that these costs be amortized over
22 a ten year period instead of a five year period?

1 A. OTS witness Weakley's only rationale for a longer recovery period is that "PPL
2 has not experienced a storm the size of Hurricane Isabel for an extended period"
3 and, therefore, should recover allowable costs over an extended period. In fact,
4 the Company acknowledges that it has never in its 80 year history experienced a
5 storm of the magnitude of Hurricane Isabel in terms of the number of cases of
6 trouble. However, this does not mean that it would be appropriate to recover the
7 costs of Hurricane Isabel over the next 80 years. The Company asserts that a
8 five-year period is an appropriate "extended period". In making this assertion,
9 the Company observes that it has not requested to recover a return on amortized
10 amounts not recovered. Consequently, assuming a rate of return of 8.8%
11 consistent with the Company's request in this proceeding, the proposed 5-year
12 amortization will recover \$11.7 million on a present value basis or only 78% of
13 the total amount. If OTS witness Wheatley's 10-year period is used, the recovery
14 will be \$9.7 million or only 65% on a present value basis. The effect is to punish
15 the Company for its efforts to restore customers and to accommodate their needs
16 during this unprecedented event.

17 Q. How do you respond to the assertion that customers should be entitled to a
18 refund as a result of storm-related outages?

19 A. Under the Public Utility Code, PPL Electric is required to maintain safe and
20 reasonable service which shall be reasonably continuous. The Code does not
21 require continuous service, nor does it suggest that utilities bear any liability
22 when the service they provide is reasonably continuous. Consistent with the

1 requirements of the Code, Rule 4 of the Company's Commission-approved tariff
2 (Tariff – Electric Pa. P.U.C. No. 201) states under the heading “F. Continuity”:

3 “(1) The Company uses reasonable diligence to preserve
4 continuity of service, but in the event of interruption or
5 curtailment of service, Company shall not be subject to any
6 liability, penalty or payment for or on account of any such
7 interruption or curtailment...”

8 The Company does not propose any change to this language in this proceeding.

9 The intent of this language is to recognize that the Company cannot
10 anticipate and prevent all possible interruptions to or curtailment of service. The
11 Company's responsibility is to exercise reasonable diligence and, having done
12 so, it should not be liable for the consequences of outages; especially, those
13 caused by Hurricane Isabel as they are beyond the Company's reasonable
14 control. It has not been suggested by any party that the Company failed in any
15 way to exercise reasonable diligence in its efforts to prepare for or restore
16 service following Hurricane Isabel.

17 **Costs and Benefits Associated with AMR**

18 Q. Please describe the Company's request in this proceeding.

19 A. A significant portion of the benefits achieved by the AMR project is the
20 elimination of manual processes associated with the prior metering system. With
21 the elimination of manual processes comes the opportunity to reduce the
22 workforce. PPL Electric estimates that the deployment of AMR will ultimately
23 lead to a substantial reduction in the number of positions from what would have

1 otherwise existed without AMR. The displacement of employees carries with it
2 certain costs. PPL Electric has been able to accommodate most of these
3 displacements through normal attrition within PPL Electric; i.e., employees
4 displaced by AMR have been trained to fill vacancies that arose as a result of the
5 normal course of retirements and severance. However, with a displacement this
6 large, the normal rate of attrition has not been enough. Accordingly, the
7 Company offered enhanced severance benefits to 94 employees in order to
8 capture the payroll and benefits savings of AMR. In this proceeding, the
9 Company requested the authority to amortize the cost of these enhanced
10 benefits over a five-year period and recover the resultant amounts through rates.

11 Q. Please describe the issue raised by other parties in regard to costs and benefits
12 associated with the AMR project.

13 A. Parties raise a number of issues regarding the Company's request including the
14 accounting treatment of these costs and the assertion that recovery of these
15 costs in rates is a violation of the rate cap provisions of the Competition Act. The
16 Company's response to these concerns is included in Statement No. 2-R, the
17 Rebuttal Testimony of Joseph R. Schadt. The issue I wish to address is the
18 assertion by OCA witness Thomas Catlin that "ratepayers would be better off
19 without AMR if the amortization of the \$8,818,000 was allowed."

20 OCA witness Catlin correctly states that PPL Electric has performed an
21 analysis of the total present worth of revenue requirements associated with the
22 AMR system over a 15-year period. That analysis, as described in my direct
23 testimony (PPL Electric Statement No.4), reflected quantifiable economic

1 benefits in the form of reduced expenses. However, Statement No. 4 also
2 describes tangible benefits of a non-economic nature that customers are
3 currently enjoying as well as future economic and non-economic benefits that will
4 be available to customers as the AMR system is enhanced and as generation
5 rate caps expire. Witness Catlin's assertion that ratepayers would be better off
6 without AMR fails to recognize the benefits associated with more accurate billing,
7 more complete usage information, and outage identification and restoration that,
8 although not quantifiable in economic terms, are, nevertheless, of significant
9 value to customers. It is PPL Electric's firm belief that customers are better off
10 for having the AMR system.

11 **Proposals to Promote Retail Competition**

12 Q. Please describe the recommendations of Strategic Energy witness Jim
13 McCormick to promote retail competition.

14 A. Strategic witness McCormick makes five recommendations that he believes will
15 lead to increased retail competition in PPL Electric's service territory. These are:

- 16 1. Accelerate the enhancement of the AMR system and make data derived
17 from that system available to Electric Generation Suppliers ("EGSs").
- 18 2. Make available 12 months of usage data to EGS's for customers that have
19 authorized the release of such data.
- 20 3. Provide an updated of the Eligible Customer list.
- 21 4. PPL Electric should accept an EGS's telephonic representation that the
22 customer has authorized the EGS to obtain historical usage information.

1 5. PPL Electric should commit to having EGS Consolidated Billing available
2 within a specified period after an EGS requests it.

3 Q. Are these issues germane to a rate request involving distribution rates?

4 A. Some of the issues are appropriately addressed in a distribution case. For
5 example, the AMR system is distribution plant so the issue regarding further
6 enhancement of the AMR system is appropriately addressed here. However, the
7 issue of making additional metering data available to EGSs is not appropriate to
8 address because it relates to the generation portion of electric service which
9 remains capped under the terms of the Restructuring Settlement. Nevertheless,
10 the Company is prepared to respond to Strategic witness McCormick's individual
11 points.

12 Q. How do you respond to the request to accelerate enhancements of the AMR
13 system?

14 A. PPL Electric has stated in its direct case its expectation that the functionality of
15 its AMR system can be enhanced and that the Company expects to pursue
16 appropriate enhancements in anticipation of the end of the generation rate cap
17 on December 31, 2009. The Company is currently an active participant in both
18 the Commission's Demand-Side Response Working Group and Provider of Last
19 Resort (POLR) Roundtable – two collaborative efforts wherein future metering
20 and data requirements will be defined. The Company believes it is important to
21 work within collaboratives such as these so that the needs of all stakeholders can
22 be properly recognized in Commission orders and policies. The Company is
23 concerned about the possibility that it might undertake enhancements that would,

1 in the end, be inconsistent with whatever direction the Commission might
2 establish.

3 Currently, PPL Electric makes available to EGSs metering information
4 consistent with its Restructuring Settlement and Commission-approved supplier
5 tariff. PPL Electric intends to continue providing that information through at least
6 the term of the Settlement (currently December 31, 2009) consistent with and in
7 support of the billing, load scheduling, and load reconciliation processes
8 established in the Restructuring Settlement.

9 PPL Electric does not offer POLR service in competition with EGSs as
10 suggested by Strategic witness McCormick. POLR service is default service
11 available, consistent with the Competition Act, to customers who elect not to
12 seek supply from an EGS and to customers whose EGS fails to provide
13 contracted for supply. The price that PPL Electric charges for POLR service is
14 established by the Restructuring Settlement and cannot change, regardless of
15 the capabilities of AMR, during the term of the Restructuring Settlement.

16 In summary, PPL Electric is encouraged by the support offered by
17 Strategic witness McCormick for the Company's AMR system and for further
18 development of that system, but believes that there is no need for an accelerated
19 development and that such a development might, in fact, result in unnecessary
20 and inappropriate expenditures.

21 Q. How do you respond to the request that PPL Electric make available 12 months
22 of usage data to EGS's for customers that have authorized the release of such
23 data?

- 1 A. PPL Electric currently does provide EGSs with twelve (12) months of usage and
2 demand data for customers who have agreed to allow EGS's access to their
3 account data. For customers that are billed using non-interval meters, 24 data
4 points are sent per request. There are twelve (12) usage and twelve (12)
5 demand data points sent per request. For customers that are billed using interval
6 meters, one year of hourly data is sent per request. PPL Electric's standard
7 method of providing historical usage data to EGSs is through standardized
8 electronic data transactions called Electronic Data Interchange (EDI)
9 transactions. These EDI transactions are exchanged between the EGS and PPL
10 Electric according to standards established by the Commission's Electronic Data
11 Exchange Working Group (EDEWG). EGS's sends an EDI 814 historical usage
12 (HU) request to PPL Electric. The Company sends back to the supplier an EDI
13 814 HU response that PPL Electric either accepted or rejected the EGSs
14 historical usage request. Requests may be rejected because they don't match
15 an active customer account number or because the customer has indicated that
16 his usage information is not to be made available. When PPL Electric accepts
17 the EDI 814 HU, the Company sends the EGS an EDI 867 HU transaction that
18 contains the customer usage and demand information.
- 19 Q. How do you respond to the request that PPL Electric send "opt-out" cards to
20 customers biannually (or at some other regular interval) in order to update its
21 Eligible Customer list?
- 22 A. During the pilot-program and phase-in of customer choice, the number of
23 customers eligible to participate was limited and EGSs had a need to know which

1 specific customers were participating so they could market to those customers.
2 Orders implementing pilot programs and restructuring orders required utilities to
3 establish and maintain Eligible Customer Lists to address this need. PPL Electric
4 established such a list and maintained it through the completion of the phase-in,
5 which for PPL Electric was January 2, 2000. As of that date, all customers were
6 eligible for choice and there was no longer a need to identify eligible customers
7 separate from ineligible customers. PPL Electric still solicits information from
8 new customers for the purpose of responding to 814 HU requests (such as the
9 customer's willingness to release its usage to EGSs). However, PPL Electric no
10 longer maintains the Eligible Customer List.

11 Strategic witness McCormick recommends the periodic dissemination
12 of "opt-out" cards which were the mechanism by which existing customers
13 indicated whether they wished to withhold information from the Eligible Customer
14 List. Given that the need addressed by the Eligible Customer List no longer
15 exists and that the list is no longer maintained, the sending of "opt-out" cards is
16 unnecessary. Witness McCormick may, instead, be pointing to another need –
17 that being the desire of EGSs to have customer usage information to identify the
18 customers that can be served most profitably and to develop proposals for those
19 customers. Because the Eligible Customer List included historical usage
20 information, for those customers willing to allow it to be published, EGSs came to
21 rely on the List for that information. However, EDEWEG rules established the
22 historical usage request process described above as a more efficient and lower
23 cost means by which EGSs could obtain customer usage information. PPL

1 Electric assumes that the remaining issue in this regard is an individual
2 customer's willingness to make his usage information available. PPL Electric has
3 established Web-based procedures to address this issue that it believes are
4 more appropriate and less costly than the option of periodically sending 1.3
5 million post cards to customers asking them if their prior election regarding
6 confidentiality has changed.

7 Q. How do you respond to the request that PPL Electric should accept an EGS's
8 telephonic representation that the customer has authorized the EGS to obtain
9 historical usage information?

10 A. Customers' right to privacy and the confidentiality of customer information are
11 important issues that are recognized by PPL Electric and the Commission. The
12 Commission went to great lengths to establish rules regarding customer choice
13 that attempted to protect customer rights while providing EGSs reasonable
14 opportunities to bring potentially beneficial proposals to customers. An additional
15 and important concern that the Commission was attempting to address through
16 these rules was that the availability of customer information could facilitate
17 slamming. In this regard, PPL Electric is reluctant to accept a telephonic
18 representation by an EGS because the customer's intent cannot be verified.

19 Aside from choice, PPL Electric has a standing practice of requiring
20 the use of verifiable means to evidence a customer's desire to have its usage
21 information provided to any third party. PPL Electric, responding to the concerns
22 of a significant number of customers, is concerned that consultant's may
23 represent that they have the customer's approval to obtain usage information

1 when, in fact, they are acting in their own interest or in the interest of a client that
2 may be a competitor of the customer. That practice in the past required the use
3 of customer letterhead but has been since updated to accept e-mail with
4 appropriate safeguards. These practices have never included the acceptance of
5 telephonic requests.

6 Q. How do you respond to the request that PPL Electric should commit to having
7 EGS Consolidated Billing available within a specified period after an EGS
8 requests it?

9 A. At the start of the phase in of competition in 1999, PPL Electric was replacing its
10 customer information and billing system because the existing system was not
11 Y2K-compliant and because it could not be cost effectively modified to
12 accommodate the functionality necessitated by customer choice. In part
13 because the choice rules were not finalized until late in the system's design, PPL
14 Electric experienced a number of billing problems in early 1999 with choice
15 accounts. There was also some functionality that simply was not available at the
16 outset. One functionality that was not available was the ability to support EGS
17 Consolidated Billing. The Company worked closely with the Commission's Office
18 of the Executive Director during 1999 and 2000 as the Company corrected the
19 problems and deficiencies. As part of that effort it was agreed that, as long as no
20 EGSs were seeking to perform EGS Consolidated Billing, providing that
21 functionality could be a lower priority. It was agreed that if an EGS made known
22 that it wished to employ that functionality, PPL Electric would work with the
23 EGS to (1) identify interim alternatives, and (2) design and install the

1 modifications necessary to support that functionality. While no EGS has
2 indicated a need for EGS Consolidated Billing, PPL Electric has done much of
3 the design work and has completed some of the necessary modifications. The
4 Company estimates that of the originally estimated 6.700 manhours of work,
5 about 3.000 manhours of work remain. PPL Electric estimates that it will require
6 about ten months to complete the remaining work and test the modifications.
7 Because the necessary modifications affect the fundamental structure of the
8 customer support system and because they are so extensive, PPL Electric
9 anticipates that other system enhancements, including ones that may be
10 beneficial to customers, be placed on hold during the period in which EGS
11 Consolidated Billing modifications are being made.

12 Strategic witness McCormick's comments don't indicate a need for
13 this functionality, only that it works in Texas where customers appear, unlike in
14 Pennsylvania, to have no option regarding bill presentment. PPL Electric stands
15 by its original commitment to complete EGS Consolidated Billing upon a
16 reasonable demonstration that ratepayer money would be spent on functionality
17 that would be useful to customers. PPL Electric also is prepared to work with
18 any EGS to explore lower cost alternatives that may be available to achieve an
19 equivalent functionality.

20 Q. Does this conclude your rebuttal testimony?

21 A. Yes, it does.