

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Joint Petition of Citizen Power and Pennsylvania:  
Steel and Cement Manufactures Coalition for a :  
Declaratory Order to Investigate Stranded Cost :       Docket No.  
Mitigation Efforts, to Investigate Stranded Cost :  
Over Collection and to Refund Stranded Cost :  
Over Collections :**

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**JOINT PETITION OF  
CITIZEN POWER AND  
PENNSYLVANIA STEEL & CEMENT MANUFACTURERS COALITION  
FOR A DECLARATORY ORDER**

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Dated: August 24, 2010

## I. EXECUTIVE SUMMARY

Between 1998 and 2001, at various Dockets, the Pennsylvania Public Utility Commission (“Commission”) approved stranded cost calculations and recovery mechanisms for each Pennsylvania Electric Distribution Company (“EDC”).<sup>1</sup> These stranded cost calculations essentially looked at each EDC’s existing rate based generation and power supply costs which would have been recoverable under regulation but, based upon long range price forecasts, may not be recovered in a competitive environment. These long range electricity price projections looked out more than ten years in some instances. At the time these electricity price projections were done, most stakeholders expected a robust competitive wholesale electricity supply market to develop, and for that reason these projections assumed significantly lower prices than the EDC’s existing generation supply costs.

This expectation of robust wholesale competition and lower prices meant that Pennsylvania EDC’s would be harmed by competition and therefore needed a mechanism to recover their *expected* uneconomic generation and supply costs or “stranded costs”. Since these were merely the expected stranded costs based upon long range electricity price projections and not anything that the Commission at the time could accurately calculate, it is entirely possible that some EDCs have over or under collected significant actual dollars from their customers. Indeed, it is highly likely there was a substantial difference between the projected stranded costs and the actual stranded costs, i.e., costs based on the difference between expected wholesale power prices and actual prices in the intervening years.

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<sup>1</sup> Restructuring docket numbers: R-00973975 (UGI-Electric Utilities, Inc.), R-00973981 (West Penn Power Co.), R-00974101 (Duquesne Light Co.), R-00973953 (PECO Energy), R-00973954 (PP&L), R-00974008 (Metropolitan Edison Co.), and R-00974009 (Pennsylvania Electric Company).

PA Title 66, Chapter 28, Section 2808 (c)(4), “Competitive Transition Charge” (CTC) requires stranded cost mitigation efforts by utilities **throughout the entire transition period**.<sup>2</sup>

To the extent that EDCs complied with Section 2808(c)(4), their actual stranded costs would necessarily change from the projected stranded costs. Now that the transition periods are ending, the Commission is obligated to compare the projected stranded costs to the actual stranded costs and adjust the recovery of such.

The Commission approved nearly \$12 billion in transition charges or stranded cost recovery for Pennsylvania utilities that it deemed just and reasonable.<sup>3</sup> Since the EDCs were required to then mitigate those very costs *during the transition period*, the Commission must review the just and reasonableness of the actual mitigated transition costs incurred against the projected transition or stranded costs recovered. The Joint Petitioners request that now, at the end of the stranded cost collection window, the Commission undertake that review and under 52 Pa. Code §5.42:

**1. Determine whether each EDC fully mitigated stranded costs to the extent practicable as required under 66 Pa.C.S.A. 2808(c)(4),**

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<sup>2</sup> “During the transition period, electric utilities shall have the duty to mitigate generation-related transition or stranded costs to the extent practicable. Efforts may include the following:

- (i) Acceleration of depreciation and amortization of existing rate base generation assets.
- (ii) Minimization of new capital spending for existing rate base generation assets.
- (iii) Reallocation of depreciation reserves to existing rate base generation assets.
- (iv) Reduction of book assets by application of new proceeds of any sale of idle or underutilized existing rate base generation assets.
- (v) **Maximization of market revenues from existing rate base generation assets.**
- (vi) Issuance of securitized debt pursuant to the provisions of section 2812 (relating to approval of transition bonds).”

PA Title 66, Chapter 28, Section 2808, paragraph (c) (4), (emphasis added).

<sup>3</sup> The PaPUC final restructuring orders approved \$11.88 billion in stranded cost recovery as follows (in billions of dollars): PECO \$5.26, PPL \$2.97, Duquesne \$1.33, Med Ed \$1.00, West Penn \$0.67, Penelec \$0.43, and Penn Power \$0.22. Testimony of Tyrone J. Christy, Vice Chairman, Pennsylvania Public Utility Commission before the Pennsylvania House of Representatives Environmental Resources and Energy Committee January 20, 2010, p. 14.

- 2. Compare the projected/expected stranded costs to the actual stranded costs after accounting for mitigation efforts and changes in the PJM Market for each EDC and,**
- 3. In the event that any utility has an egregious difference, for example, in excess of \$50 million, between their expected stranded costs that have been collected from ratepayers and the actual stranded costs that a utility experienced, implement a mechanism to refund the over collection back to those EDC customers.**

The Joint Petitioners consist of Citizen Power and the Pennsylvania Steel & Cement Manufacturers Coalition (“PSCMC”). Citizen Power is a nonprofit, public policy research, education and advocacy organization based in Pittsburgh. As such, Citizen Power has been actively involved in the restructuring of the Pennsylvania electricity generation industry since 1996. The PSCMC is an ad hoc coalition of steel and cement manufacturers across Pennsylvania. Steel and Cement manufacturing are the heart and soul of Pennsylvania industry in that Pennsylvania is the birthplace in North America of both the portland cement and the modern steel industries. Joint Petitioners include many of the largest electricity consumers in Pennsylvania and smaller commercial and residential customers who may be our suppliers, employees or retirees in every Pennsylvania EDC service territory. Joint Petitioners consume almost two billion kWh annually in Pennsylvania and thus represent a substantial percentage of Pennsylvania’s electricity consumption.

## II. PETITION

In 1996, under the *Electricity Generation Customer Choice and Competition Act* (“Competition Act”), Pennsylvania became one of the first states in the United States to experiment with retail electric industry restructuring. At the core of that experiment was a trade off under which Pennsylvania retail electricity consumers would have the right to buy electric generation service from suppliers other than their local full service electric utility. In exchange, the local utilities were allowed to collect their generation costs that were expected to become uneconomic or “stranded” as competition lowered electricity prices for Pennsylvania consumers. Central to this trade was an assumption by the Pennsylvania Legislature and the Commission that robust competition would lower electricity prices for consumers and that because retail prices would fall, Pennsylvania utilities needed to be fairly compensated for costs they had incurred under the old regulatory paradigm. This Petition is the result of those assumptions not coming to fruition. Robust competition did not occur and prices didn’t in fact actually fall as expected. The Joint Petitioners recognize that the Commission has limited ability to re-structure the electricity supply industry within Pennsylvania. As a result, eventually all Pennsylvania consumers will bear the burden of an experiment gone awry because the underlying wholesale market that supports retail competition has failed to produce the necessary robust competition. However, the Commission can partially mitigate the impact to consumers in the Commonwealth by determining whether there has been an over-collection of stranded costs and requiring that EDCs refund the excess amounts.

Joint Petitioners are concerned that they may have substantially over paid Pennsylvania EDCs for stranded costs since actual regional electricity prices have been substantially higher than the electricity price forecasts used to determine the stranded costs of Pennsylvania EDCs.

Joint Petitioners do not blame the Commission for the inaccurate long range electricity price forecasts. The Commission relied upon expert forecasts which looked at the way electricity was priced *at that time* in the PJM regional electricity market. However, in April 1999, shortly after the long range price projections were performed, PJM, at the request of the PJM member utilities, implemented market changes to allow energy offers to not be cost based. This was the first of many significant PJM market changes that generation owning entities, including the PJM voting affiliates of most Pennsylvania EDCs, implemented during the stranded cost recovery period. During the window of the long range price projections, Pennsylvania generation owning EDCs have requested and supported several additional substantial revisions to PJM's electricity pricing algorithms, including the Reliability Pricing Model ("RPM") and the creation of multiple layers of ancillary services markets, that lack any level of competitiveness, yet cascade into wholesale energy prices, plus the implementation of a litany of adders to cost based offers when PJM's rules deem the markets to be uncompetitive and trigger cost based offers.<sup>4</sup> The end result of all of these changes to PJM pricing mechanisms is that *actual market prices have greatly exceeded the long range price forecasts used by the Commission to estimate the stranded costs*. Because some Pennsylvania utilities have been among the chief architects of the market changes that have been implemented after the stranded cost estimates were performed, Joint Petitioners believe that Pennsylvania consumers have been subjected to "bait and switch" scams at the hands of Pennsylvania utilities. The Commission should rectify this by first comparing the

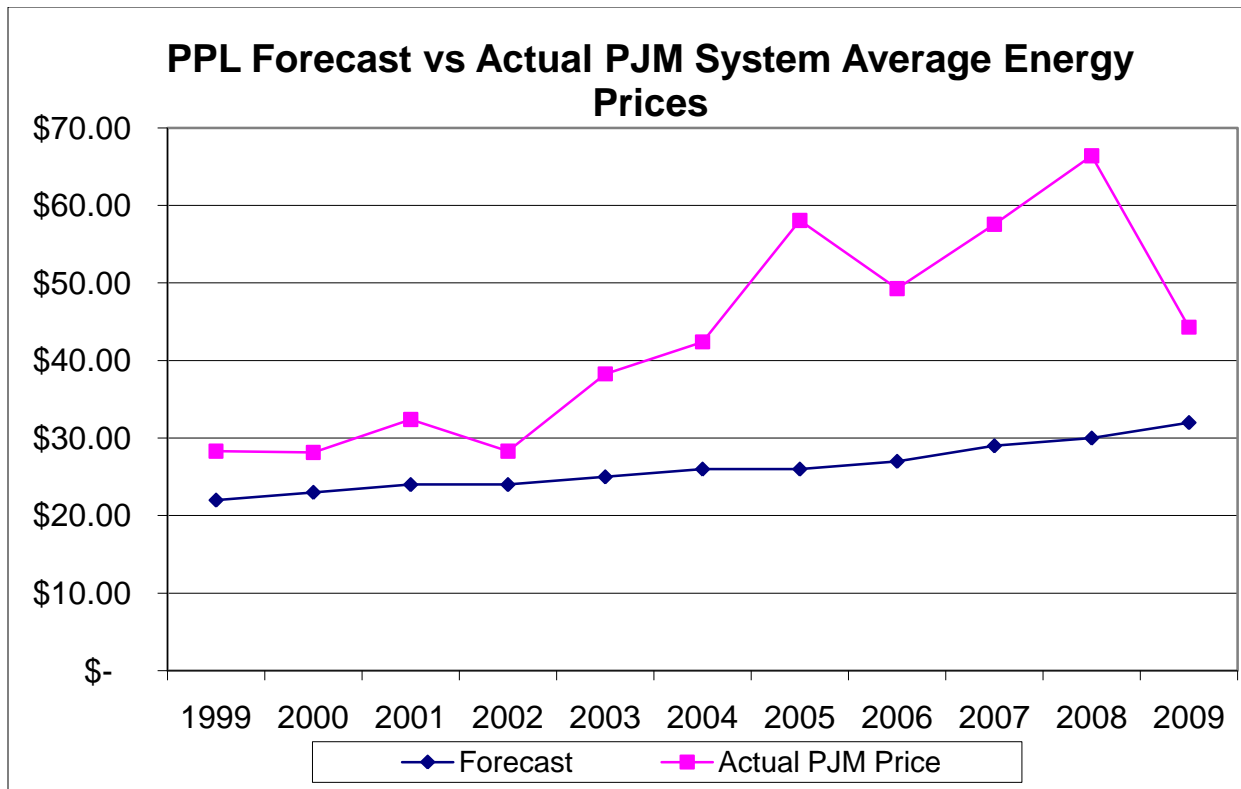
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<sup>4</sup> PJM modified the basis for energy offers in April, 1999 (Docket ER97-3729), restricted competition in the capacity markets in 1999 (Docket ER99-2663) introduced a Day-Ahead Energy market and bid based ancillary service markets 2000 (Dockets ER00-298 and ER97-1082 respectively) introduced and then increased scarcity pricing in 2003 and 2004 (Dockets EL03-236 and EL04-121), the Reliability Pricing Model was added in 2006 (Dockets ER05-1410 and EL05-148), and the RPM prices were substantially increased in 2008 and 2009 (Dockets ER08-232 and ER09-412) and has recently proposed to more than double energy market prices during periods of short supply (Docket ER09-1063). All of these changes had the effect of raising the wholesale price above the levels originally contemplated in the long-term forecasts determining stranded costs.

projected stranded costs to the actual stranded cost experience for each utility. Joint Petitioners have performed several versions of this type of analysis and suspect that Pennsylvania EDC's have collected billions of dollars more in "stranded costs" than the costs that were actually stranded in that time frame. Such an over-collection from all Pennsylvania consumers is clearly not what the Commission had in mind when approving the various Restructuring Settlements.

**Projected Stranded Costs Assumed Much Lower Electricity Prices Than Those That Pennsylvania Consumers Have Experienced Since 1998.**

Joint Petitioners are asking the Commission to perform a simple comparison, to calculate the expected stranded costs to the actual stranded costs, given that electricity prices have been significantly higher than the price forecasts used to calculate the expected stranded costs. The graph below shows the actual PJM Interconnection, LLC ("PJM") system average prices and the projected electricity prices approved in the PPL Restructuring proceeding, that determined PPL Utilities expected stranded costs for the corresponding period. Importantly, in no single year were the actual electricity prices below the expected prices which were used to determine PPL's "expected stranded costs", costs which in fact are what PPL Utilities has charged to customers since 1999.



It is important to note that the comparison above ignores the fact that PPL and other generation owners—who largely make payment rules for generators—receive significantly more revenue from PJM than just these energy prices via PJM’s RPM capacity mechanism and PJM’s various ancillary service markets. These various adders substantially increase PPL revenues, making the potential “over recovery” even larger. PPL Corporation has been, and continues to be, among the most vigorous advocates within PJM for any mechanism that increases prices to consumers, but it is not alone among affiliates of Pennsylvania EDCs. The simple fact is that the long range projections in the graph above were done under substantially different market rules than what has existed during the stranded cost recovery period. The fact that the Pennsylvania EDCs have had a large role in the PJM stakeholder process, and thereby made sure that the long



range electricity price projections proved to be too low, calls for the Commission to revisit those projections.

Simply by taking the difference between the actual load-weighted PJM energy prices and the forecasted “competitive” electricity prices, Joint Petitioners estimate that Pennsylvania consumers were subjected to a multi-billion dollar over recovery of expected EDC stranded costs. If we are correct, this is particularly egregious in this difficult economic environment and comes at a time when electricity customers are facing rate increases due to the expiration of rate caps. In the event that there was any egregious over collection by a particular Pennsylvania EDC, those EDC shareholders have already received this difference in the form of changes in common stock prices and dividend yields. The consumers of any EDC that substantially over collected because the projections turned out to be wrong deserve just and reasonable treatment in the form of refunding the over payments.

An argument has been made that the apparently excess stranded costs recovered by the EDCs are reasonable because consumers have received the benefit of price caps on rates. In fact, a Commission publication states that “[i]n exchange for the recovery of stranded costs, generation, transmission and distribution rates were capped at 1996 levels.”<sup>5</sup> However, this contention overstates the benefits attributed to the price caps, ignores the fact that the rate caps were designed to protect against high electric rates resulting from immature markets, instead of serving as a *quid pro quo* for stranded costs; and also disregards the fact that EDCs are statutorily required to mitigate generation-related stranded costs to the extent practicable.<sup>6</sup>

First, the economic benefit of the price caps is strongly overstated by the Commission because the purported benefits are based on an assumption that prices would be trending upwards

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<sup>5</sup> The Expiration of Electric Generations Rate Caps, pg.1, available at [http://www.puc.state.pa.us/general/consumer\\_ed/pdf/Rate\\_Caps.pdf](http://www.puc.state.pa.us/general/consumer_ed/pdf/Rate_Caps.pdf)

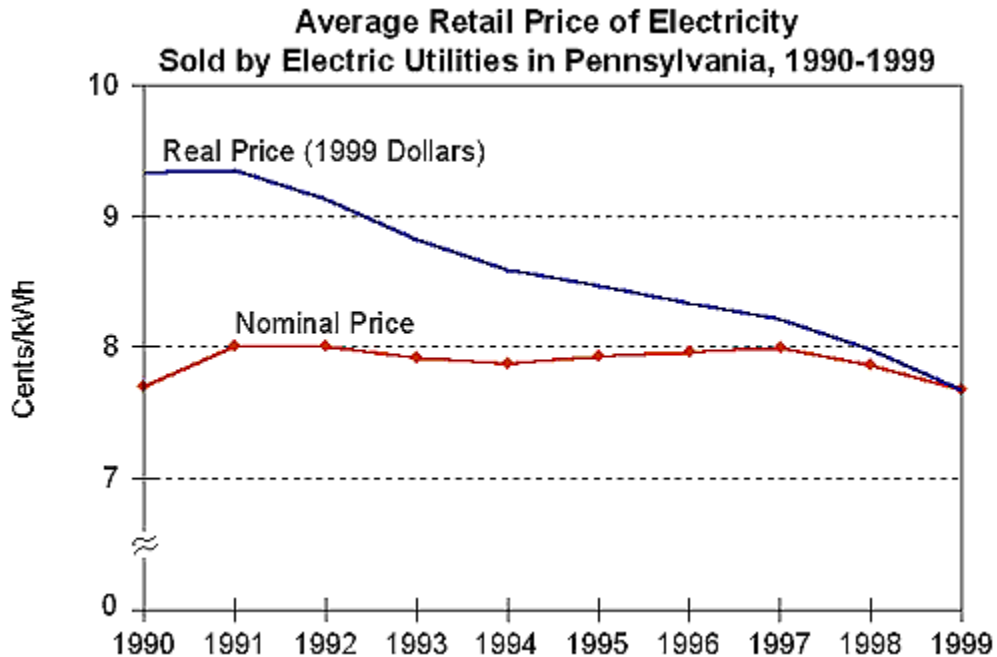
<sup>6</sup> 66 Pa. C.S.A. § 2808(c)(4).

in lieu of caps. In fact, as shown in the graph below, in the decade preceding the institution of the rate caps, electricity prices were trending downward in Pennsylvania. There is no reason to believe that trend would not have continued. Second, the purpose of the rate caps was to protect against price volatility that could occur before sufficient competition developed.<sup>7</sup> However, Pennsylvania electric utility rates were capped at 1996 levels which ranged between 8 and 35% above the national average.<sup>8</sup> So it can be argued that the rate caps actually prevented customers from reaping the benefits of likely price decreases had deregulation not occurred. In addition, while transmission and distribution rates were capped, generation rates increased during the transition period via the Provider of Last Resort (POLR) proceedings. Finally, even if we accept the claim that rate caps saved customers money, the amount of savings claimed is significantly lower than the \$12 billion collected in transition charges. Rate caps were never designed to offset stranded cost over collection, and should not be used as a tool to conflate the separate purposes behind stranded costs and rate caps. Finally, the fact that rate caps are in place should have no bearing on the calculation of stranded costs or any mitigation of stranded costs. The presence of rate caps does not alleviate the statutory requirement to mitigate stranded costs.

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<sup>7</sup> Electricity Deregulation: A Successful Transition, available at [http://www.eeapa.com/about/electricity\\_deregulation](http://www.eeapa.com/about/electricity_deregulation)

<sup>8</sup> Investigation into Electric Power Competition, Statement of Commissioner John Hanger, PaPUC, July 3, 1996.



Source: Trends in Pennsylvania's Electricity Retail Rates Fact Sheet; available at [http://www.eia.doe.gov/cneaf/electricity/page/fact\\_sheets/pennsylvania.html](http://www.eia.doe.gov/cneaf/electricity/page/fact_sheets/pennsylvania.html)

Joint Petitioners recognize that the Commission has performed reviews of the recovery of stranded costs but notes that those reviews were essentially limited to comparing the forecast vs. actual EDC throughput volumes.<sup>9</sup> The Commission has never compared forecasted electricity prices to actual electricity prices in order to determine if the Commission approved CTCs were in fact within any range of reasonableness of the costs actually stranded. This is not a difficult process. Joint Petitioners are merely asking the Commission to compare the year by year expected electricity price projections to the wholesale market costs actually experienced in each Pennsylvania EDC zone, and thereby calculate the difference between each EDC's expected stranded costs, which were recovered from Pennsylvania consumers, and the costs actually stranded. The actual EDC zonal supply costs are readily available from the regional wholesale

<sup>9</sup> For example see Docket No. M-FACE0212, PPL Electric Utilities Corporation's Competitive Transition Charge (CTC) Section 1307(e) Reconciliation.

electricity market operator, PJM, or independently from the PJM Independent Market Monitor Dr. Joseph Bowring of Monitoring Analytics.

Joint Petitioners believe that it is the Commission's duty to perform this calculation for two reasons. One, the Commission has never evaluated the long range electricity price projections that were used to estimate the stranded costs, yet these long range projections were used to set retail electricity rates. When the Commission relies upon long range forecasts it usually conducts some form of reconciliation. The Commission routinely relies upon shorter term forecasts for adjustment mechanisms but reconciles even one year forward projections to actual experience. Considering the billions of dollars involved in the stranded cost projections, the Commission has an obligation to at least compare the projections to the actually experienced stranded costs. Two, as already mentioned, the Competition Act requires Pennsylvania utilities to lessen the burden that stranded cost charges place on customers through mitigation during the transition to full deregulation. Accordingly, as part of its investigation of stranded cost recovery, the Commission should examine whether in fact the utilities sufficiently mitigated stranded costs. There is in fact no reason to not compare the projections of stranded costs to the actually experienced stranded costs under the relatively straight forward method proposed by the Joint Petitioners, other than that some EDCs probably already know that they have substantially over recovered from customers and therefore prefer that no one ever review the projections to the actual stranded costs. Any EDC opposition to this Petition should in fact be considered as the strongest possible evidential support for the need for just such a comparison, and a high probability of the need for refunds to the consumers of the opposing EDC.

## **The PJM Electricity Market Is Substantially Different Than What It Was When The Stranded Cost Projections Were Performed.**

In 1996, the PJM electricity market was one in which each generation owner actually competed to sell the next incremental Mega-Watt-hour (“MWh”) of electricity. The market at that time was settled by paying the winning offer the midpoint between its cost of generation and the next highest cost of a generation unit. This so-called “split the savings” approach assured consumers in Pennsylvania (and all of PJM) that they could never pay more by having their local utility either buy an incremental MWh via PJM, or produce it from their own generation fleet. In 1996, the PJM operating companies, including most of the Pennsylvania EDCs, began a restructuring of PJM that was not Commission jurisdictional but rather is within the jurisdiction of the Federal Energy Regulatory Commission (“FERC”). Via this and many subsequent FERC processes, PJM utilities substantially altered the pricing mechanisms in PJM. This restructuring of PJM has dramatically affected the resulting market prices in the PJM region, including within Pennsylvania, as seen on the chart above. The Pennsylvania EDCs were 37.5% of the PJM operating and voting companies at the time that they and their regional utility brethren chose to restructure PJM.<sup>10</sup> Importantly, no Pennsylvania EDC opposed eliminating the “split the savings” pricing that had benefitted both utilities and consumers in PJM and Pennsylvania for years<sup>11</sup> (). Nor have they opposed the myriad other changes designed to increase their wholesale electricity revenues. Since Pennsylvania’s EDCs were complicit in the changes in the wholesale electricity market structure, the Commission is not compelled to continue to apply calculations that were performed under the old wholesale market structure. These substantial changes in wholesale market structure that Pennsylvania EDCs often initiated are why Pennsylvania

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<sup>10</sup> When PJM was restructured in 1998, there were 8 initial members and PECO, PPL and GPU represented 37.5% of the vote.

<sup>11</sup> at various Dockets in Note 4, Supra

consumers have potentially been subjected to a classic “bait and switch” scam. The Commission is well aware that unlike real competitive markets (such as cement or steel), the rules of PJM’s various administrative pricing mechanisms are largely driven by PJM member input. This input is dominated by the large utility holding companies. As previously mentioned, in addition to the elimination of “split the savings” pricing and cost based offers, PJM has implemented new reserve markets (which lack competition according to the IMM, yet affect wholesale costs directly), the RPM capacity mechanism, several questionable, and in some cases, duplicative cost adders for generation units, and countless other mechanisms and processes that serve only to increase electricity prices. Joint Petitioners request that the Commission at least calculate the difference between the projected stranded costs and the actual stranded costs since Pennsylvania’s EDC affiliates have had a major role in restructuring PJM’s pricing methodology. Pennsylvania EDC affiliates directly changed the market rules, which increased wholesale prices **after** the stranded cost projections that were used to set retail consumer rates were performed.

**The Commission Must Order Refunds If Actually Stranded Costs Are Substantially Different Than The Projected Stranded Costs.**

The Commission approved the various settlements in the restructuring Dockets. However, this does not preclude the Commission from re-evaluating the calculations of stranded costs. Nothing in Title 66 Chapter 28, which governs electric industry restructuring, precludes such a re-evaluation of transition or stranded costs. As previously noted, Section 2808(c)(4) requires stranded cost mitigation efforts by utilities.

Clearly if utilities were required to continue to mitigate their transition or stranded costs “during the transition” period, some level of post transition period re-evaluation is required by the Commission in order to measure how much mitigation took place. Under 66 Pa.C.S. § 1312(a), the Commission has the authority to issue refunds if any rate received by a public utility was unjust or unreasonable. The amounts received by the EDCs may have been unreasonable if the estimated stranded costs collected under the CTCs were significantly in excess of the actual stranded costs during the transition period. In addition, these amounts may also be unreasonable if the EDCs did not mitigate the stranded costs to the extent practicable. If an investigation finds that the rates during the transition period were unreasonable for either of these reasons, for any of the EDCs, the Commission should grant a refund to the customers of those EDCs.

### **III. CONCLUSION**

Pennsylvania electricity consumers have potentially been the victims of a classic “bait and switch” scheme. Actual electricity prices have greatly exceeded the forecasted electricity prices that the Commission, consumers, and even the EDCs relied upon, when projecting the potentially stranded costs. After the stranded cost projections that the Commission relied upon were developed, the underlying wholesale pricing mechanisms for electricity were changed largely at the request and insistence of generation owning companies in PJM. Most Pennsylvania EDCs are owned by affiliates of such entities. In addition to the underlying fairness, the Commission has an obligation to review the actual stranded costs after mitigation efforts by the EDCs “during the transition period” in order to assure that the level of transition or stranded cost recovery is just and reasonable. Joint Petitioners are asking the Commission to

perform the necessary post transition period review now that the transition periods are ending and the mitigated transition costs are known. Joint Petitioners suspect that in some instances the over collection will be egregious, totaling hundreds of millions or even billions of dollars. If the Commission's investigation finds what we suspect, that this level of over collection did indeed occur, it is incumbent upon the Commission to order refunds to customers who paid these costs. Such a public service will be particularly beneficial during the time customers are experiencing substantial price increases as a result of the expiration of the rate caps.

Respectfully submitted,

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**VERIFICATION**

I, David Hughes, hereby state that the facts above set forth in the Joint Petition of Citizen Power and Pennsylvania Steel and Cement Manufactures Coalition are true and correct to the best of my knowledge, information and belief and that I expect to be able to prove the same at a hearing held in this matter. I understand that the statements herein are made subject to the penalties of 18 Pa.C.S. § 4904 (relating to unsworn falsification to authorities).

/s/ David Hughes \_\_\_\_\_

David Hughes  
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2121 Murray Avenue  
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Dated this 24<sup>th</sup> day of August, 2010.

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a true copy of the Joint Petition of Citizen Power and the Pennsylvania Steel and Cement Manufactures Coalition for a Declaratory Order, which was electronically filed today, in accordance with the requirements of § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 24<sup>th</sup> day of August, 2010.

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