

Exhibit #2
Philadelphia Gas Works
Capital Budgets - Principles

Principle #1

- 1.1. These principles of capital budgeting shall apply to the Philadelphia Gas Works. Adherence to these principles is required unless strict compliance would cause detriment to PGW ratepayers. Any non-compliance with these principles must be approved by the Philadelphia Gas Commission or its designee.
- 1.2. The Philadelphia Gas Works capital budget is a line item financial budget. The term “line item” includes any and all components related to identifying a program within the capital budget as well as the derivation of total projected capital cost for such program. The term “capital budget category” shall be synonymous with the term “line item”.

Principle #2

- 2.1. A line item will have a definite lifespan indicated by spending years referenced in spending authorizations approved by the City Council.
- 2.2. The numerical code used to identify line items in approved capital budgets (e.g., “#52-20-1-01, Distribution Department, High Pressure Load Addition”) shall remain unchanged throughout the life of the capital budget to which the line item belongs and shall be traceable to its assigned work order(s).
- 2.3. Line items of a “miscellaneous” or “contingency” denomination or nature shall be work ordered only for an identified project. Further, the specific project shall be work ordered in a manner that traces such project to the “miscellaneous” or “contingency” line item in an approved capital budget.
- 2.4. The total capital budget spending authorization approved by City Council for a specific line item shall not be exceeded. Further, the total capital budget spending authorization approved by the City Council for all line items in the aggregate shall not be exceeded, without further authorization by City Council. If PGW is in danger of exceeding a spending authorization for a line item, a departmental capital budget or for a PGW-wide capital budget, PGW must notify the Gas Commission of this possibility as soon as possible with justification for the potential overrun prior to the spending authorization’s being exceeded.
- 2.5. PGW shall propose an amendment to the Capital Budget for which any overspending on a capital budget spending authorization is anticipated; provided, however, that the proposed amended Capital Budget shall be transmitted to the Gas Commission and the Finance Director for their recommendations thereon, and the Gas Commission shall transmit such proposed amended Capital Budget together with both recommendations thereon to City Council for final action.

Principle #3

- 3.1. Capital budget line items are to be developed so that the projected timing of the expenditures realistically matches the budget year.
- 3.2. Multi-year capital projects will be divided into phases. Each phase shall be submitted as a line item for the capital budget applicable to the fiscal year when funds will be required.
- 3.3. Where spending is expected to occur across multiple fiscal years and the indivisible nature of the capital project defining a line item necessitates the approval of the total program authorization proposed, spending approval will be granted on an individual fiscal year to fiscal year basis.

Principle #4

- 4.1. Where capital work related to an approved line item has not adequately progressed, such line item must be reviewed as to whether or not it is still necessary and shall be closed if it is determined that the line item is not necessary. If a closed line item is determined to be necessary at a later date, a line item shall be resubmitted as part of a future capital budget proposal.

Principle #5

- 5.1. If the nature or cost of capital work for an approved line item has changed significantly, the line item shall be resubmitted to the Gas Commission as part of a future capital budget proposal or as a modification to a proposed or approved capital budget.
- 5.2. A “significant change” to an approved line item shall include instances where the scope and requirements of a project have changed materially.
- 5.3. Principles 5.1. and 5.2. shall not apply where the total projected cost of a line item is lower than approved.

Principle #6

[RESERVED]

Principle #7

- 7.1.** Capital budget line items when proposed to the Gas Commission shall be accompanied by explanatory project detail whereby such line items are fully and meaningfully described and explained. Project Detail shall substantiate line items by incorporating applicable documentation, calculations, and any other related derivational parameters so as to leave the reader reasonably informed as to the justification for the project.
- 7.2.** Questions as to whether items of information should logically be included in Project Detail shall be resolved in favor of inclusion. PGW is encouraged to work with the Gas Commission's staff and the Public Advocate to minimize redundancy or arguable irrelevance in Project Detail disclosure.

Principle #8

- 8.1.** Priority 1 Projects (Safety)
 - 8.1.1.** Such projects will reflect capital investment critical to ensuring public safety, the integrity of PGW's facilities, and/or the safety of PGW's employees.
 - 8.1.2.** No cost/benefit analysis is required to satisfy any safety consideration associated with such projects. However, a cost/benefit justification is required for that part of a project which exceeds minimum requirements to achieve an acceptable level of risk.
- 8.2.** Priority 2 Projects (Reliability)
 - 8.2.1.** Such projects will reflect capital investment essential to maintaining the reliability of PGW's facilities in proper working condition as defined by accepted engineering practices. Included in this priority category is the replacement of facilities approaching the end of their useful life (and which need to be upgraded or replaced for reliability considerations).
 - 8.2.2.** Such projects require cost/benefit or risk assessment of potential impact.
- 8.3.** Priority 3 Projects (Enforced Relocations)
 - 8.3.1.** Such projects reflect capital investment that is based upon forecasted city, state, or federal mandated projects as well as those of other agencies or utilities that have a direct impact on PGW facilities. Such projects include the replacement of facilities resulting from enforced relocations.
 - 8.3.2.** Such projects require documentation (obtained through a due diligence effort) of the reason(s) for relocation.

8.4. Priority 4 Projects (Load Growth)

8.4.1. Such projects reflect capital investment required to provide new or additional facilities to customers.

8.4.2. Such projects require a payback-oriented cost/benefit analysis.

8.5. Priority 5 Projects (Improved Efficiency and Discretionary)

8.5.1. Such projects reflect capital investment that offers opportunity to improve efficiency of operations and subsequent reduction in future operating costs.

8.5.2. Such projects require cost/benefit analysis and the identification of consequences from delaying such project.