



COMMONWEALTH OF PENNSYLVANIA  
PENNSYLVANIA PUBLIC UTILITY COMMISSION  
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE  
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May 31, 2017

Via E-Filing

Secretary Rosemary Chiavetta  
Pennsylvania Public Utility Commission  
P.O. Box 3265  
Harrisburg, PA 17105-3265

Re: Alternative Ratemaking Methodologies  
Docket No. M-2015-2518883

Dear Secretary Chiavetta:

Enclosed please find the Bureau of Investigation and Enforcement's (I&E) **Comments** in the above-captioned proceeding.

Copies are being served on parties as identified in the attached certificate of service. If you have any questions, please contact me at (717) 783-6156.

Sincerely,

Carrie B. Wright  
Prosecutor  
Bureau of Investigation and Enforcement  
PA Attorney I.D. #208185

Enclosure  
CBW/sea

cc: Kriss Brown  
Marissa Boyle  
Andrew Herster

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Alternative Ratemaking Methodologies : Docket No. M-2015-2518883**

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**COMMENTS OF THE  
BUREAU OF INVESTIGATION & ENFORCEMENT**

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**I. INTRODUCTION**

Pursuant to a Secretarial Letter dated December 31, 2015, the Pennsylvania Public Utility Commission (“PUC” or “Commission”) held an *en banc* hearing on Alternative Ratemaking Methodologies on March 3, 2016. At that hearing the interested parties testified to their views on the efficacy and appropriateness of the alternative ratemaking methodologies. The specific topics addressed were: (1) whether revenue decoupling or another similar rate mechanism would encourage energy utilities to better implement energy efficiency and conservation programs; (2) whether such rate mechanisms are just, reasonable, and in the public interest; and (3) whether the benefits of implementation of these types of rate mechanisms outweigh the costs associated with their implementation.

Following the *en banc* hearing the Commission solicited written comments from interested parties by no later than March 16, 2016. This culminated in the Commission

issuing a tentative Order on March 2, 2017. In that tentative Order, the Commission sought further comments on “...the reasonableness and efficacy of employing certain rate methodologies specifically for electric, natural gas, and water and wastewater utilities.”<sup>1</sup> As a result of that Order, the Bureau of Investigation and Enforcement (“I&E”) now provides the following comments.

## II. COMMENTS

As a result of the testimony heard at the *en banc* hearing, as well as the Comments received from interested Parties, I&E believes that the Commission’s current practice which allows each utility to propose fully or partially decoupled rates through a base rate proceeding as the utility sees fit, is still the most appropriate practice. As stated in the Commission’s Tentative Order “...there is a consensus among these utilities and several of the advocacy organizations that the current Act 129 programs are working, and they find it difficult to determine the value of an alternative ratemaking methodology reform.”<sup>2</sup>

Traditional cost of service/rate of return regulation, such as is practiced by the Commission, is based on the analysis of a utility’s cost of doing business in a selected historical period, known as a test year, to determine the appropriate level of revenues necessary to allow the utility an opportunity to earn a fair rate of return in that historical period. Decoupling, on the other hand, is a rate setting mechanism that separates a utility’s revenues from its unit sales volumes without affecting the design of the rates.

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<sup>1</sup> Tentative Order at 14.

<sup>2</sup> Tentative Order at 5.

Decoupling is commonly established after the revenue requirement and rate design is established through a traditional base rate case. In these situations, regulators can use regular, small adjustments in rates to ensure that the utility recovers its authorized fixed cost, thereby, breaking the link between revenues and sales by either restoring to the utility, or giving back to customers, any money over or under collected as a result of fluctuations in retail sales.

In Pennsylvania, utility rates have historically been largely tied to volumetric throughput with few exceptions. As a result, when consumption decreases, whether by the choice of the customer or through a mandated energy efficiency and conservation (“EE&C”) program as mandated by Act 129, the utilities revenues also decrease. In recognition of this reality, the Commission and Legislature have, over time, worked to craft different options that are already forms of alternative ratemaking. These include mechanisms such as cost trackers, or reconcilable cost recovery riders, the expansion of the applicability of the distribution system improvement charge (“DSIC”) to energy utilities, the option of using a fully projected future test year (“FPFTY”), and employing weather normalization clauses that decouple the effects of weather on firm gas sales load. However, having utility rates that are largely tied to volumetric usage is also very beneficial to the utility customers because it allows them a measure of control over their bill; if a customer wants to lower their bill, they can simply conserve usage. That said, the potential impacts of implementing new rate mechanisms must be carefully assessed in the context of Pennsylvania’s overall regulatory framework. General regulatory theories and the experience of other states, while informative, do not provide sufficient basis for

overturning Pennsylvania's existing regulatory structure. The approach taken must serve both the utility and its customers well. I&E will be addressing the following alternative rate making methodologies: revenue decoupling, straight fixed variable pricing, and cost trackers.

### **A. Revenue Decoupling**

There are a number of design and implementation issues that would need to be considered in the development of an effective revenue decoupling mechanism. These include, but are not limited to: (1) whether the mechanism is applied to all or only some customer classes; (2) whether allowed revenues are calculated on a per customer basis (i.e., encourage economic development by allowing utilities to collect revenues for new customers); (3) which indices (e.g., inflation, productivity), if any, are incorporated in the mechanism; and (4) whether to include or exclude weather related sales fluctuations. The frequency and allowed level of true-up would also need to be considered to avoid amassing significant revenue deferrals.

With respect to the different customer classes and whether the rate design impacts are more prominent for certain classes than others, it must be recognized that decoupling mechanisms affect the different rate classes in quite different ways because certain rate classes are more price responsive than others. More movement toward fully cost-based rates traditionally has been and can more easily be accomplished within the larger commercial and industrial classes, thereby largely breaking the link between utility sales and profits attributable to these customers. On the other hand, lost revenue and profits due

to reduced sales can be significant for residential and small commercial classes. Careful consideration must be given to these issues.

In its Tentative Order, the Commission lists three different ways revenues can be determined when decoupling rates, and three different types of decoupling rate adjustment mechanisms. As noted above, I&E believes the utility is best suited to examine these and determine which, if any, to propose on a case-by-case basis. Absent the utility actually proposing one of these methods and providing all supporting information to review, it is impossible to determine which, if any, would be appropriate to implement in Pennsylvania.

#### **B. Straight-Fixed Variable Pricing**

Under the straight fixed variable (“SFV”) approach all of the utilities fixed costs are recovered through the fixed monthly charge, while any variable costs would be recovered through usage rates. In general, under this approach, a greater portion of the customer’s bill is allocated to the fixed charge than what is typically contained in the customer charge as developed under current ratemaking methodologies.

There has been some suggestion from parties such as the Office of Consumer Advocate (“OCA”) that a rate redesign that shifts fixed costs into fixed charges could be harmful to low usage or low income customers. This is because it is expected that a person living in a small apartment would use less energy than a person living in a large house; however, the person in the small apartment would still be expected to pay the same high fixed cost as the person living in a large house. Further, low income customers who already potentially struggle to pay their utility bills would also be expected to pay the

higher fixed cost. However, other parties, such as Columbia, point out that these customers concerns could be addressed through the low income programs that are already in place. While the answer is not clear, I&E would agree that a rapid shift of fixed costs from volumetric to fixed customer charges could potentially harm low usage and low income customers. While a targeted approach to addressing potential bill impacts on low income customers would help mitigate those impacts, I&E does not recommend pursuing such a rapid shift of fixed costs from volumetric to customer charges. A more gradual shift would allow the customer to better prepare for the higher bill and mitigate the rate shock experienced from a significant increase to their bill. I&E recognizes, however, that low income programs may need to be expanded and energy efficiency programs further targeted to help mitigate the impact on these customers.

A SFV approach also may serve to dilute any conservation efforts on the part of the customer as well. When a customer is presented with a lower fixed charge there is more incentive to conserve energy because the customer can see more of an impact on their bill. A higher fixed charge serves to lessen that impact of conservation on a customer's bill.

**C. Cost Trackers (also known as Surcharges or Riders)**

Today, reconcilable riders predominate, utility revenues are very stable, and the opportunity to earn a return is more assured. As such, I&E does not believe that it would be necessary or proper to expand the use of riders and surcharges at this time.

**III. CONCLUSION**

In general, the current rate making methodology employed by the Commission adequately protects the interest of both the utilities and their customers, as evidenced by

the Comments received to date on this issue. The public benefits resulting from energy efficiency programs, renewable technologies and distributed generation could potentially be substantial. Nevertheless, a link continues to exist between utility sales and delivery service revenues, due to the current design of utility delivery rates. This could influence utility behavior by providing disincentives that impede their promotion of these initiatives because, essentially, the lower usage means that the utilities are collecting less revenue. Rate design changes can potentially reduce such utility disincentives, but are often effectuated gradually due to potential impacts on customers' bills. While the eventual implementation of more cost-based rate designs remains an important long-term objective, especially for larger more price responsive customers, the question exists as to whether or not properly designed revenue decoupling mechanisms are needed at this time to address disincentives that may still exist, given present delivery service rate designs, for the less price responsive customers. Therefore, should the General Assembly and the Commission determine changes to the current regulatory model to accommodate revenue decoupling are needed, I&E would recommend that many of the consumer protections as outlined by OCA<sup>3</sup> in addition to the following issues and comments:

- Identify the statutory and regulatory barriers associated with alternative rate mechanisms in Pennsylvania.
- Identify the impact of alternative ratemaking approaches on a utility's cost of capital.
- Identification of bill impacts on a wide variety of households, including low usage customers, low income customers, renters, and customers with inelastic usage due to health needs.

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<sup>3</sup> OCA Comments pp. 22-24 at Docket M-2015-251883 (March 16, 2016).

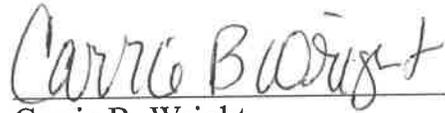
- Issues associated with the impact of net metering.
- Any alternative method that is proposed would have to be studied and implemented carefully to avoid conflict of recovery incentives with the current mechanisms in place.
- The mechanism should be designed to true-up forecast and actual utility delivery service revenues for a given time period.
- The mechanism should be designed to prevent gaming by the utility (e.g., shifting customers to different classes).
- The recovery of any net lost revenues component of the mechanism should not, in and of itself, produce inter-class revenue reallocations between customer classes (such reallocations should only be made purposefully after considering a current fully-allocated cost of service study).
- All remaining design and implementation issues should be addressed in individual rate proceedings.
- The Commission can continue its current practice of allowing each utility to propose fully decoupled rates or partially decoupled rates through base rate proceedings as they see fit. In addition, the Commission, when it suspends a 1308 rate filing and initiates an investigation of the rate filing, could direct the parties to address decoupled rates in the rate hearings. This practice gives maximum flexibility to allow utilities and ratepayer representatives to craft acceptable rates.
- If the Commission chooses to encourage more widespread use of decoupled rates or encourage a particular decoupled rate design, it could issue a policy statement that directs the utilities to investigate such decoupled rate designs in subsequent 1308 base rate filings. This could be targeted to specific utility types, sizes or address certain situations, such as when an EDC hits a specific threshold of interconnected distributed generation in a rate class. It could also encourage different types of decoupled rates for NGDCs and EDCs. A policy statement would provide some parameters around what the Commission finds are acceptable decoupled rate designs and under what circumstances they would be acceptable.

- If the Commission chooses to require utilities to implement rate decoupling or a specific form of rate decoupling, regulation(s) will be required. Such a regulation would dictate when a utility would implement rate decoupling, what type of rate decoupling it could implement, and which rate classes it would apply to. While this would reduce utility flexibility in rate design, it would ensure that decoupled rates are implemented.
- If the Commission chooses to provide performance incentives or to provide revenue recovery directly related to decreased sales resulting from the Act 129 EE&C Program for those EDCs required to comply with that program, than legislative changes would be needed. Such legislative changes would provide the Commission, the EDCs, ratepayers and interested stakeholders with certainty as to Commission authority to provide such incentives and rate relief, and what form such incentives and rate relief is permitted.

I&E continues to believe revenue decoupling is unique to the particular circumstances of each utility. Therefore, the determination of whether a utility should decouple its rates needs to be made on a case-by-case basis. Therefore, I&E believes that the design and implementation of any revenue decoupling mechanism should take place in the context of individual base rate proceedings. I&E does not believe, at this point, that a broad, general decoupling approach would be appropriate for either the utility, or its customers.

**WHEREFORE**, for the reasons state herein, the Bureau of Investigation & Enforcement respectfully requests that the Pennsylvania Public Utility Commission consider the above comments regarding alternative ratemaking methodologies.

Respectfully submitted,



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Dated: May 31, 2017