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July 31, 2017

VIA E-FILED

Ms. Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
2nd Floor, Room-N201
400 North Street
Harrisburg, PA 17120

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

Dear Secretary Chiavetta:

Enclosed please find Duquesne Light Company's Reply Comments in the above-referenced proceeding.

Upon receipt, if you have any questions regarding the information contained in this filing, please contact the undersigned or Audrey Waldock at 412-393-6334 or awaldock@duqlight.com.

Sincerely,

A handwritten signature in blue ink that reads "Shelby A. Linton-Keddie".

Shelby A. Linton-Keddie
Manager, State Regulatory Affairs
And Senior Legal Counsel

Enclosure

c: Kriss Brown (kribrown@pa.gov)
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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Alternative Ratemaking Methodologies

:

Docket No. M-2015-2518883

**REPLY COMMENTS OF
DUQUESNE LIGHT COMPANY**

On March 2, 2017, the Pennsylvania Public Utility Commission (“PUC” or “Commission”) issued an order in this proceeding,¹ “seeking comments on, and potential processes to advance, alternative rate methodologies that address issues each utility industry is facing.”² After reviewing a Motion from the Office of Consumer Advocate (“OCA”) requesting more time for comment and reply comment, the Commission, via Secretarial Letter dated March 23, 2017, extended the comment period until May 31, 2017, with reply comments due on July 31, 2017.³

Consistent with these deadlines, on May 30, 2017, Duquesne Light Company (“Duquesne Light” or “Company”) submitted comments for the Commission’s consideration. Comments were also submitted by more than twenty other interested stakeholders.⁴

In accordance with the schedule in this proceeding, Duquesne Light hereby submits reply comments to highlight areas of disagreement with other parties,⁵ to reiterate specific points of its

¹ Prior to the March 2, 2017, Order, the Commission issued a Secretarial Letter on December 31, 2015, at this docket, announcing its intention to hold an *en banc* hearing and soliciting comments from interested stakeholders. Consistent with that direction, Duquesne Light Company submitted comments in this proceeding on March 3, 2016.

² *Alternative Ratemaking Methodologies Tentative Order*, Docket No. M-2015-2518883, at 1-2.

³ See *Alternative Ratemaking Methodologies*, Docket No. M-2015-2518883, Secretarial Letter (Mar. 23, 2017).

⁴ In addition to Duquesne Light, comments in this proceeding have been filed to date by: AARP, Advanced Energy Economy Institute, Alliance for Industrial Efficiency, American Eagle Paper Mills, Veolia, Arcelor Mittal, *et al.*, Aqua PA, Bureau of Investigation and Enforcement, Columbia Gas of Pennsylvania, Energy Association of Pennsylvania, Industrial Energy User Groups (MEIUG, PICA, PAIEUG, PPLICA and WPPII), Keystone Energy Efficiency Alliance, First Energy, National Fuel Gas Distribution, Natural Resources Defense Fund, Sierra Club and Clean Air Council, Office of Consumer Advocate, Office of Small Business Advocate, PECO, Peoples Natural Gas and Peoples TWP, Philadelphia Gas Works, PPL Electric Utilities, Pennsylvania Utility Law Project, Strata, UGI, and Valley Energy, Citizens’ and Wellsboro.

⁵ Due to the voluminous nature of the comments at this proceeding, these reply comments are limited in nature and should be regarded as addressing only those points which necessitated response. The Company’s silence as to any

proposal, and to encourage the Commission to move in a measured way that preserves flexibility rather than mandate any one specific outcome or methodology.⁶

REPLY COMMENTS

Innovations in energy and information technologies are creating new options for all customers. These new options make it imperative that as use of the electric distribution grid is evolving, so must the rate structures historically used. Alternative ratemaking methodologies allow electric distribution companies (“EDCs”) to better value distribution system infrastructure and recover reasonable costs that ensure the long term reliability, safety, security, availability, and viability of the distribution grid. Not only will the combined use of various alternative ratemaking methodologies for recovery of distribution costs better match cost causation but, if used appropriately, will also retain consumer protections and maintain reliability while incorporating and encouraging the use of new technology by customers.

1. Utilization of Alternative Ratemaking Methodologies Will Not Degrade Either Existing Consumer Protections or Reliability Standards.

In an attempt to support their opposition to decoupling and alternative ratemaking in general, at least two parties to this proceeding have either questioned or alleged that if more stable, predictable rates were charged for electric distribution, namely through an increase in fixed charges, that reliability will suffer and existing consumer protections could be stripped.⁷ The stated reasoning is that EDCs would be “indifferent to the prospect of extended outages”⁸ and that

particular issue should not be regarded as agreement or endorsement, and Duquesne Light reserves its right to challenge any issue not covered in the scope of these comments going forward.

⁶ Duquesne Light is a member of the Energy Association of Pennsylvania (“EAP”), which is also submitting reply comments in this proceeding. In addition to the positions stated herein, Duquesne Light supports the positions articulated in EAP’s reply comments.

⁷ See Industrial Energy User Group Comments at 7-8; see also OCA Comments at 12, 14, 15.

⁸ OCA Comments at 15.

“such methodology endorses mediocrity and encourages utilities to become indifferent to their fundamental business.”⁹ Both of these conclusions are unsubstantiated, not based on fact or evidence, and should be rejected outright.

The discussion in this proceeding centers on fundamental fairness and equity for both customers and utilities when deciding how best to recover approved revenue requirements. The way a utility collects revenue has no impact on existing reliability benchmarks, consumer protections, or the myriad of other statutory and regulatory requirements to which regulated public utilities must adhere. More critical is that these arguments ignore the inherent problem with the current rate structure for electricity – distribution rates are charged primarily on a volumetric basis, divorced of how they are actually incurred. Moreover, reductions in consumption, which are mandated by the state, are not allowed to be adjusted on a full and current basis. Rather, adjustments to consumption can only be reflected in the course of a base rate proceeding.¹⁰ This outdated and lagging methodology not only gives customers an inaccurate signal as to how their costs are actually incurred, but it also prevents EDCs from recovering the actual costs to serve customers on a full and current basis unless an assumed amount of electricity is consumed by customers.

The Office of Small Business Advocate (“OSBA”) argues, when weighing the concept of decoupling, that “a relevant question is whether utility incentives are misaligned (vis-à-vis the implementation of energy efficiency programs) in Pennsylvania.”¹¹ Duquesne Light counters that any perceived effects on energy efficiency programs once alternative rate structures take effect is only one of many issues that must be considered when choosing an appropriate rate methodology.

⁹ Industrial Energy User Group Comments at 8.

¹⁰ See 66 Pa. C.S. §2806.1(k)(3)

¹¹ OSBA Comments at 3-4.

The Company believes that the more important inquiry is whether cost causation and cost drivers are properly structured so that customers are charged rates in line with how costs are actually incurred by the EDCs that serve them. In today's environment, under the current regulatory construct, there is clearly a mismatch between distribution system cost drivers and revenue recovery that should not be perpetuated any longer.

Further, the argument that fixed charges for distribution would degrade the results and incentive for energy efficiency as a whole are speculative at best. In comments, First Energy clearly demonstrated the fallacy in this argument when stating:

As a point of illustration, even if the Companies were to establish a 100% fixed rate for their commercial and industrial classes, those customers would still see a large percentage of their bill charged under a variable rate due to the proportion of the generation piece of their bills. The same holds true for the residential classes, where approximately 51 to 64% of the total charges for electricity would remain variable in nature if 100% of base distribution charges were collected on a customer charge basis.¹²

Because customers will still see tangible benefits through savings on the generation portion of their bill as they incorporate more efficient measures, there is no basis to believe that higher fixed charges for distribution service, no matter the level, will negate the necessity or success of current or future energy efficiency and conservation programs in the Commonwealth.

Moreover, comments alleging that the use of alternative ratemaking methodologies constitutes single issue ratemaking ignores the possibility that such methodologies for distribution base rates would likely be proposed in the context of a base rate proceeding rather than a stand-alone Petition, thus negating that argument. As explained *infra*, Companies should be free to propose alternative ratemaking mechanisms that work for their size, customer make-up, revenue

¹² First Energy Comments at 9. Duquesne Light believes that similar results would exist for its customers. The weighted averages for transmission and generation portions of its customers' bills range from a low of 48% for residential customers to a high of 77% for Large C&I customers. Accordingly, regardless of the fixed nature of distribution costs, customers in all classes could see tangible benefits through electricity conservation.

requirement, and usage patterns. Other than suggestions by the Industrials and OCA, there has been no evidence that demonstrates EDCs propose to decouple or request any other alternative ratemaking methodology for distribution base rates outside the scope of a base rate proceeding. In the scope of a base rate proceeding, regardless of the methodology proposed, EDCs, stakeholders and the Commission would determine an appropriate revenue requirement based on numerous inputs, not a singular one. The alternative ratemaking methodologies proposed in this proceeding are simply different means by which that revenue requirement could be collected and reconciled. It is only one portion of the process and will not, by itself, turn the current ratemaking process on its head, as some suggest.

While Duquesne Light affirms, regardless of the ratemaking methodology used, that its obligation to deliver electricity safely and reliably will remain paramount as it is our core mission, any fear around reliability or energy efficiency concerns could be addressed through use of performance incentives tied to these measures. Rather than the Commission mandating performance incentives, however, EDCs should be free to propose these mechanisms on their own.

2. Utilization of Alternative Ratemaking Methodologies Should Not Require Degradation of Companies' Return on Equity.

OSBA argues that if full decoupling is approved, “the Commission should implement a commensurate reduction in each utilities’ allowed return on equity (“ROE”),” arguing that it would eliminate the largest risk utilities face – the risk of sales variability.¹³ Similarly, OCA states that “the ROE levels of utilities must be considered as risk is greatly reduced with the implementation of any alternative ratemaking methodology.”¹⁴ Duquesne Light agrees that when determining the ROE in a base rate proceeding numerous factors should be considered, including risk, but disagrees

¹³ See OSBA Comments at 5.

¹⁴ OCA Comments at 65.

that simply because an alternative ratemaking methodology is used that there should automatically be a lower ROE.

As recognized by Commissioner Robert F. Powelson, “[r]ate of return on common equity is frequently the most material and most contested item in a base rate proceeding.”¹⁵ This is, in part, because ROE is a measure of financial health and stability, which utilities use to attract capital investment that is used to maintain and upgrade its distribution system. Moreover, if a company is using a Distribution System Improvement Charge (“DSIC”), the ROE is especially important, because if a utility earns more than its stated DSIC ROE, the DSIC resets to zero.¹⁶ In order to provide utilities with a fair return, as well as encourage accelerated infrastructure investment and maintain the ability to attract capital, Duquesne Light agrees with Commissioner Powelson that ROEs, including when a DSIC is utilized, should be at levels that simultaneously effectuate all these goals.¹⁷

The conclusion that simply because an alternative ratemaking methodology is used that the ROE should automatically be lowered ignores the fact that ratemaking, especially the setting of the ROE, is a complicated financial exercise, sometimes described as part art, part science. ROE is made up of components such as expenses, revenue, debt and capitalization. Notably, risk is not listed, but is taken into account. While Duquesne Light agrees that risk should be considered when setting an ROE, the Commission should be cognizant that risk is only one of numerous factors to be considered when setting an appropriate ROE. No one input should be elevated to the exclusion of all others.

¹⁵ See *Pennsylvania Public Utility Commission, et al. v. The Columbia Water Company*, Motion of Chairman Robert F. Powelson (Jan. 9, 2014). (hereinafter “Powelson Motion”)

¹⁶ See 66 PA C.S. §1358(b)(3). In practice, the range of DSIC ROEs per industry typically mirror both the ROEs approved by the Commission in litigated distribution rate cases and the ROEs set in the TUS Quarterly Reports.

¹⁷ See Powelson Motion, supra n. 13; see also *Bureau of Technical Utility Services Report on the Quarterly Earnings of Jurisdictional Utilities for the Year Ended June 30, 2016*, Statement of Commissioner Robert F. Powelson (Oct. 27, 2016).

3. Specific Issues Related to Standby Rates and Combined Heat and Power Should be Addressed as Part of the PUC’s Existing CHP Policy Statement Proceeding.

In addition to comments about the scope and use of alternative ratemaking methodologies for distribution base rates, two commenters expressed concern over the current level of combined heat and power (“CHP”) or waste heat to power (“WHP”) in the Commonwealth, as well as perceived inequities over current standby rates, purportedly demonstrated by a study that compared the standby rates of PPL and PECO.¹⁸ Both groups argued over what they perceive as excessive standby rates and suggest that current rate structures are inequitable, thereby preventing further CHP and WHP development in the Commonwealth. In an effort to cure this perceived inequity, both groups suggest adoption of a model tariff that purportedly contains a number of “best practice principles.”¹⁹

Duquesne Light does not oppose CHP in its service territory or the proposed expansion of CHP (or WHP), provided it is based on sound concepts of economics, safety, and appropriate cost allocation for utilization of the distribution system paid for by other customers over time. What concerns the Company, however, is the implication that the perceived lag in CHP development in the Commonwealth is due, in large part, to utility policies and standby charges that create barriers to such development.²⁰ As stated in Comments in the proceeding titled *Proposed Policy Statement on Combined Heat and Power*, Docket No. M-2016-2530484, and reiterated here, Duquesne Light simply does not find this to be the case. Rather than a lack of utility policies and standby charges to make CHP more viable, the Company believes that, even with low to moderate natural gas prices, the economics remain challenging for installing baseload generation, obtaining air emission permits, building onsite distribution and disposing of waste heat.

¹⁸ See generally Alliance for Industrial Efficiency Comments; see also American Eagle *et al.* Comments.

¹⁹ See Alliance for Industrial Efficiency Comments at 3-4, Appendix A.

²⁰ See Alliance for Industrial Efficiency Comments at 3; see also American Eagle *et al.* Comments at 1.

It is the Company's experience that CHP projects, when in either planning or discussion stages, often do not come to fruition. Final investment decisions on whether to construct these projects are largely dependent on factors completely outside an EDC's ability to control: gas expansion costs, project payback periods, borrowing rates, current and forecasted market power prices, air permitting issues, construction costs and timelines, etc. To that end, the Company asks that the Commission be mindful of these realities prior to invoking any specific requirements on EDCs, including adopting the proposed CHP policy statement as currently written, or considering the model tariff format put forward in this proceeding.

Rather than make any wholesale changes through this proceeding on standby rates, including consideration of the model tariff, Duquesne Light believes that any consideration should either be done in the course of the existing CHP docket, referenced *supra*, or on a case-by-case basis. Regardless of which path the Commission chooses to follow, the Company disagrees with the suggestion of the Alliance for Industrial Efficiency to initiate a rulemaking on this subject.

4. The Commission Should Not Mandate Any One Methodology To the Exclusion of Others.

Upon review of the submitted comments, there are numerous suggestions of how the Commission should move forward. While some parties suggest that nothing needs to be done, others cite the need for legislation, a request for a stakeholder working group or that, if anything, the Commission should draft a Policy Statement that contemplates a number of potential ratemaking methodologies.²¹

Duquesne Light continues to believe that legislation that specifically names and authorizes certain methodologies is the clearest way to settle any ambiguities around PUC authority and the

²¹ See e.g., OCA Comments, NRDC, Sierra Club and CAC Comments, Duquesne Light Comments.

ability of EDCs to use these methodologies.²² With that said, however, the Company agrees that any methodologies chosen should be incorporated over time, through study, and when impacts are visible.²³ Duquesne Light further agrees that absent an actual proposal rather than theoretical discourse, neither the Commission nor stakeholders will be able to determine which methodology/methodologies will work best for implementation.²⁴ To that end, untested rate designs must be vetted and supported by empirical evidence before spread among an entire customer base.²⁵

Regardless, a “one size fits all” approach should be avoided, and utilities should be free to propose preferred methodologies through base rate cases, as is the current practice.²⁶ To suggest that one can, in 2017, determine a singular methodology that is best for all situations going forward, without actual information on customer and EDC effects, is ill-advised. It is more likely that it will take pilots of small test groups using different methodologies before determining the best option for customers, EDCs and the Commission. Upon review of other parties’ comments, Duquesne Light remains convinced that utilities should be given options and flexibility to determine what is appropriate for their size, revenue requirement, customer make-up and usage.

²² See Duquesne Light Comments at 8.

²³ See OCA Comments at 19.

²⁴ See I&E Comments at 5.

²⁵ See NRDC, Sierra Club and CAC Comments at 15.

²⁶ See I&E Comments at 2.

CONCLUSION

Duquesne Light appreciates the opportunity to further comment on the important issues raised when considering the use of alternative ratemaking methodologies and requests that the Commission consider the suggestions and clarifications herein before issuing a Final Order in this proceeding.

Respectfully submitted,



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DATE: July 31, 2017