BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	Docket Nos. R-2009-2139884
v.	:	P-2009-2097639
	:	
Philadelphia Gas Works	:	

OFFICE OF TRIAL STAFF
STATEMENT IN SUPPORT OF
JOINT PETITION FOR SETTLEMENT
OF RATE PROCEEDING

TO ADMINISTRATIVE LAW JUDGE CHARLES E. RAINEY JR.

I. INTRODUCTION

The Office of Trial Staff ("OTS") of the Pennsylvania Public Utility Commission ("Commission") respectfully submits that the terms and conditions of the foregoing Joint Petition for Settlement ("Settlement") are in the public interest and represent a fair and just balance of the interests of Philadelphia Gas Works ("PGW" or "Company") and its customers.

II. BACKGROUND

1. OTS is charged with the representation of the public interest in proceedings relating to rates, rate-related services and application proceedings affecting the public interest held before the Commission. Consequently, in negotiated settlements, it is incumbent upon OTS to ensure that the public interest is served and to quantify to what extent amicable resolution of any such proceeding will benefit the public interest. Based upon the OTS analysis of the Company's filing, acceptance of this proposed Settlement is in the public interest and OTS recommends that Administrative Law Judge ("ALJ") Charles E. Rainey, Jr. and the Commission approve the Settlement in its entirety.

2. On November 18, 2009, PGW filed Supplement No. 36 to Tariff Gas-Pa. P.U.C. No. 2, containing proposed changes in rates, rules, and regulations calculated to produce $42,500,000 in additional annual revenues to provide funding for PGW's Other-Post Employment Benefits ("OPEB") liability.

3. By Order entered February 11, 2010, the Commission instituted a formal investigation to determine the lawfulness, justness and reasonableness of PGW's existing and proposed rates, rules and regulations. This proceeding was suspended until September 16, 2010, by operation of law, unless permitted by Commission order to become effective at an earlier date.

4. A telephonic Prehearing Conference convened on March 2, 2010, with ALJ Rainey presiding. During the Prehearing Conference, a procedural schedule was developed establishing testimony, hearing and briefing dates.

5. Five public input hearings were held in the Company's service territory.

6. Hearings were held on May 10 and May 11, 2010 to advise the ALJ of the status of Settlement negotiations.

7. On May 11, 2010, the parties advised ALJ Rainey that a Settlement of all issues had been achieved by the active parties.

8. Extensive discovery was undertaken during this proceeding. The Company's compliance with these discovery requests enabled OTS to thoroughly analyze the rate filing to determine whether the requested rates were just and reasonable. Prior to agreeing to the instant settlement, OTS legal and technical staff conducted a thorough review of the Company's filing and supporting information, discovery responses and submitted filing data, and contributed to forthright discussions among the parties during settlement talks.

9. In accordance with the Commission's policy favoring settlements, 52 Pa. Code § 5.231, the signatory parties achieved a full and complete settlement of all issues. OTS submits that the Settlement satisfies all applicable legal standards and is in the best interest of the Company and its customers.

III. TERMS AND CONDITIONS OF SETTLEMENT

10. This Settlement satisfies the legal standard for approval thereby supporting its adoption. "The prime determinant in the consideration of a proposed Settlement is whether or not it is in the public interest."[1] The Commission has recognized that a settlement "reflects a compromise of the position held by the parties of interest, which,

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1 *Pennsylvania Public Utility Commission v. Philadelphia Electric Company,* 60 Pa. PUC 1, 22 (1985).

arguably fosters and promoted the public interest."[2] The Settlement in the instant proceeding protects the public interest in that a review of the testimony submitted by the parties shows that compromises are evident throughout the Settlement.

11. The Settlement represents a balance of the interests of the Company and its customers. Accordingly, for the reasons articulated below, OTS maintains that the proposed Settlement is in the public interest and requests that it be approved by the ALJ and the Commission without modification.

12. The Settlement provides for a level of additional operating revenues that OTS, as one of the Joint Petitioners, agrees is reasonable and lawful. The proposed rate increase is in the public interest because it allows the Company additional annual revenue while significantly moderating the amount of the increase for PGW ratepayers. The Settlement permits the Company to maintain the $60 million revenue increase it received as part of its emergency rate relief filing and further, to increase its level of annual distribution revenues by $16 million.[3] This $16 million increase represents a $26.5 million decrease from the Company's requested $42.5 million. OTS maintains that the proposed rate increase is in the public interest because it provides the Company with sufficient operating revenue in order to provide safe and reliable service to its customers while maintaining an acceptable cash flow. Furthermore, the agreed upon revenue requirement protects ratepayers from undue and unwarranted increases.

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2 *Pennsylvania Public Utility Commission v. C S Water and Sewer Associates,* 74 Pa. PUC 767, 771 (1991).
3 Settlement, p. 4.

The rate increase achieved in the Settlement provides PGW with solid financial footing. As stated by the Company in PGW Statement No. 1, it was important for PGW to retain the $60 million because that would allow PGW to maintain investment grade bond rating, renew its short term borrowing facility and sell its bonds to finance capital programs.[4] The $16 million increase is also in the public interest as it helps to ensure PGW's $18.5 million OPEB obligation is funded. The combination of the $16 million, along with retaining the $60 million will give PGW the tools to significantly improve their debt structure and credit rating.

13. The Settlement provides that PGW will establish an Irrevocable Trust prior to any effective date for the rate increase to fund OPEBs. This was a critical factor in the OTS evaluation of the Settlement as we provided testimony rejecting OPEB funding because the Company had not yet established an irrevocable trust.[5] Consistent with the recommendation found in OTS Statement No. 1, the Settlement prohibits PGW from collecting any funding for OPEBs until the trust is put in place and approved by the Commission.[6] This is in the public interest because it ensures that this Trust will be set up and that the funds will be used for their intended purpose. Setting up the Trust also provides PGW with a benefit because it ensures funding for the OPEB obligation will be provided. This is important because as stated in PGW Statement No. 2, this will improve PGW's debt to capitalization ratio[7]; this is something credit rating agencies will look favorably upon. PGW will make monthly deposits into the Trust amounts necessary to

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4 PGW St. No. 1, p. 3.
5 OTS Statement No. 1, p. 36.
6 OTS St. No. 1, p. 37.
7 PGW St. No. 2, p. 12.

fund the OPEB obligation. Further the Company will be required to provide a copy of the Irrevocable Trust Agreement to the parties and the Commission to inform them that the Trust has been established.[8]

14. PGW is required by the Settlement to make monthly deposits into the Irrevocable Trust. This is in the public interest as it provides levelized payments. The revenues collected will match the deposit made into the Trust and PGW will not have the opportunity to "sit" on the funds for any period of time.

15. Further, the Settlement states that PGW will not be able to divert the monthly deposits it must make into the OPEB Trust unless PGW files for Emergency Rate Relief. The date that PGW must resume OPEB funding will be set by Commission Order. This is in the public interest for several reasons. First, this provision ensures that safety of PGW ratepayers because PGW will not be allowed to indiscriminately divert funds from this Trust. Should PGW wish to divert funds, it must be in a financial crisis serious enough to warrant Emergency Rate Relief.[9] Additionally, once funds are diverted, ratepayers are assured that PGW will not be able to permanently divert the funds unless permitted by the Commission. Further, PGW is protected by this provision because it gives them the option of diverting the funds when they are facing disastrous financial situations. Therefore, there is some flexibility to the provision should PGW be in dire need of the funds.

8 Settlement, p. 6.
9 Settlement, p. 6.

16. The Settlement provides that the Company will refrain from filing a distribution rate increase for at least 24 months after Commission approval of this Settlement.[10] This stay out provision benefits PGW ratepayers because it provides for a period of rate stability. The stay out period also enables the Company to conduct its operations without the expense and time consumption involved in organizing and filing a rate case.

17. The Settlement addresses the OTS concerns regarding PGW's currently in-force interest swap agreements. Over the course of this proceeding, OTS extensively researched the benefits and risks of municipal organizations entering into interest rate swaps. OTS believes that interest rate swaps carry enormous risk and noted in testimony that Pennsylvania Auditor General, Jack Wagner, has called on the General Assembly to prohibit governments and municipal authorities from entering onto swaps due to the risk.[11]

18. In testimony, OTS argued that PGW's currently in-force interest rate swap agreements carry many risks.[12] However, OTS believes that the Settlement provides appropriate ratepayer safeguards from the risk of interest rate swaps by requiring PGW to give 60 days notice before entering into any new swaps, implementing reporting requirements and encouraging PGW to terminate the swap agreement when favorable economic conditions emerge.[13] Further, PGW has agreed that no one-time termination/cancellation/unwinding or exit fee(s) will be included in any request for

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10 Settlement, p. 5.
11 OTS Statement No. 2, p. 29.
12 *Id.*
13 Settlement, pp. 7-8.

future rate relief.[14] These terms of the Settlement insulate ratepayers from future risk related to interest rate swaps.

19. The Settlement reflects a balance between the benefits of energy efficiency and the accompanying financial burden upon ratepayers. In commenting on PGW's as-filed DSM Plan, OTS relied upon the precedents established by Commission Orders approving Energy Efficiency and Conservation Plans for electric distribution companies. Accordingly, the Settlement provides spending budgets for the first two years of the Plan and a firm commitment to fully fund the Enhanced Low Income Retrofit Program within the initial spending budgets.[15] The Settlement also contains important restrictions, such as prohibiting PGW from recovering lost revenues during the Stay Out period and preventing duplicative conservation efforts by limiting any CFL delivery programs to those where PECO finances or delivers the devices and requiring coordination with other local conservation programs.[16]

20. With the modifications adopted in the Settlement, PGW can implement a DSM Plan that recognizes the financial constraints of its revenue base. The commitment to fully fund the Enhanced Low Income Retrofit Program ensures a broad public benefit as low income customers can benefit from improved conservation and non-low income customers can benefit from reduced subsidies paid to the low income customers. Overall the DSM Plan, as modified by the Settlement, represents a well reasoned solution to conserving gas costs and lowing customer bills.

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14 Settlement, p. 7.
15 Settlement, p. 10.
16 Settlement, p. 10-11.

21. The Settlement improves PGW's financial outlook by maintaining adequate debt service coverage ratios and improving liquidity. OTS submitted testimony stating that PGW must meet all of its bond covenants and maintain debt service ratios within a range determined to be acceptable by rating agency standards.[17] The same testimony noted that funding the OPEB obligation through an irrevocable trust would signal a reduction to PGW's future liabilities and improve future liquidity.[18] The Settlement ensures that PGW will make monthly principal debt repayments in amounts sufficient to meet the annual forecasts projected in the Revised Exhibit JRB-2A.[19] As discussed above, PGW will fund its OPEB obligation through monthly deposits to an irrevocable trust.

22. These Settlement provisions, designed to reduce PGW's debt obligations and liabilities, will improve the Company's financial outlook. Three rating agencies, Standard and Poor's, Moody's Investors Service and Fitch Ratings, have identified PGW's debt service coverage as a going forward concern.[20] If the PGW improves its debt/equity ratio, the rating agencies may upgrade the Company's credit rating.[21] An improved credit rating will facilitate lower cost borrowing, increase internally generated funds and continue stabilizing PGW's financial condition.

23. In addition to ensuring adequate debt service and increasing liquidity, the Settlement provides measures designed to improve PGW's collection practices. Standard

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17 OTS Statement No. 2, p. 19.
18 OTS Statement No. 2, p. 22.
19 Settlement, p. 5.
20 OTS Statement No. 2, pp. 12, 16, 17.
21 OTS Statement No. 2, pp. 12-18.

and Poor's, Moody's and Fitch identified strong collections as a positive factor in their analysis of PGW's credit rating.[22] The settling parties have agreed to increase the scope of documents which PGW may use to identify individuals with arrearages who apply for service at the same resident at which the arrearage was accrued.[23] This measure should improve collections and further stabilize PGW's financial condition.

24. The Settlement implements limited employee benefit expense reporting requirements targeted to improve PGW's future financial outlook. In testimony, OTS recommended that the Company explore revisions to its current employee benefit programs so as to retain important employee benefits without incurring excessive operating expenses.[24] This Settlement encourages financial prudence by requiring the Company to report on its efforts to provide reasonable employee benefits that do not unduly burden the Company and its ratepayers.[25]

25. The Settlement reflects the principals of cost based rates. Throughout this proceeding, OTS has advocated for rate design that moves the rate of return toward the system average rate of return.[26] While the Settlement rate design differs from that presented in OTS's testimony, it fulfills the goal of moving PGW's rate class allocations closer to their respective cost of service.[27]

26. OTS represents that all issues have been satisfactorily resolved through discovery and discussions with the Company and are incorporated in the Settlement. The

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22 OTS Statement No. 2, pp. 12, 14, 16.
23 Settlement, p. 12.
24 OTS Stmt No. 1, p. 29-30.
25 Settlement, p. 12.
26 OTS Statement No. 4, p. 5.
27 Settlement, p. 8.

very nature of a settlement requires compromise on the part of all parties. This particular agreement exemplifies this principle as the large number of intervening parties and complexity of the issues involved did not preclude open and diligent settlement discussions. The active parties have partnered with PGW in a vigorous attempt to improve PGW's current financial situation. The balance of the issues have been carefully discussed and negotiated in this agreement. Line by line identification of the ultimate resolution of the disputed issues is not necessary as OTS represents that the Settlement maintains the proper balance of the interests of all parties. OTS is satisfied that no further action is necessary and considers its investigation of this rate filing complete.

27. The Settlement is conditioned upon the Commission's approval of all terms and conditions contained therein and should the Commission fail to grant such approval or otherwise modify the terms and conditions of the Settlement, it may be withdrawn by the Company or OTS as provided therein.

28. OTS' agreement to settle this case is made without any admission or prejudice to any position that OTS might adopt during subsequent litigation in the event that the Settlement is rejected by the Commission or otherwise properly withdrawn by any other parties to the instant proceeding.

29. If the ALJ recommends that the Commission adopt the Settlement as proposed, OTS agrees to waive the filing of Exceptions. However, OTS has not waived its right to file Reply Exceptions with respect to any modifications to the terms and conditions of the Settlement, or any additional matters, that may be proposed by the ALJ

in the Recommended Decision. OTS also reserves the right to file Reply Exceptions to any Exceptions that may be filed by the Company.

IV. CONCLUSION

The Commission's Office of Trial Staff represents that it has thoroughly analyzed the instant base rate filing and has actively participated in settlement discussions, which resulted in the foregoing Joint Petition for Settlement. OTS supports the Settlement as being in the public interest and respectfully requests that Administrative Law Judge Charles E. Rainey, Jr. recommend, and the Commission approve, the terms and conditions contained in the Joint Petition for Settlement.

Respectfully submitted,

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