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

IN REPLY PLEASE
REFER TO OUR FILE

December 31, 2013

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

Re: Pennsylvania Public Utility Commission v.
PPL Electric Utilities Corporation
Docket No. R-2012-2290597

Dear Secretary Chiavetta:

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

Copies are being served on all active parties of record as evidenced in the attached Certificate of Service. If you have any questions, please feel free to contact me at (717) 783-6155.

Sincerely,

Regina L. Matz
Prosecutor
Bureau of Investigation and Enforcement
PA Attorney I.D. #42498

Enclosure
RLM/snc

cc: Honorable Susan D. Colwell
Parties of Record

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2012-2290597
	:	
PPL Electric Utilities Corporation	:	

BUREAU OF INVESTIGATION AND ENFORCEMENT REPLIES TO COMMENTS IN RESPONSE TO THE COMMISSION'S NOVEMBER 15, 2013 ORDER REGARDING PPL ELECTRIC SUPPLEMENT NO. 130

On November 15, 2013, the Commission issued an Order at the above docket providing parties the opportunity to file additional comments on "an alternative funding mechanism to replace the disallowed storm damage insurance"[1] following resolution of PPL's 2012 base rate case. As noted therein, "[b]y Order entered February 28, 2013, the Commission granted the OCA's Petition [for Reconsideration or Clarification] and ordered PPL to include ***both*** a storm damage expense rider and a storm damage reserve account as funding mechanisms within the discussions held in the collaborative process (February 2013 Order)."[2] In the *November 2013 Order*, parties were also specifically requested to respond to nine questions posed by the Commission in Appendix A attached to the Order. Parties were also provided the opportunity to file replies to comments.

[1] *November 2013 Order* at 5 (all acronyms and short form citations identified in full and employed by I&E in its December 16, 2013 Comments continue to be employed in these replies).
[2] *November 2013 Order* at 4 (emphasis added).

On December 16, 2013, additional comments were filed by I&E, OCA, the Industrial Intervenor group, and PPL. I&E hereby files these replies in accordance with the Commission's Order.

I. PPL'S RIDER SDER MUST BE REJECTED

A. Sound Legal And Policy Reasons Compel The Commission's Rejection of PPL's Proposed Section 1307 Rider Either As Proposed Or Modified

The fundamental misconception permeating the comments presented by PPL in this matter is best illustrated by PPL's description of the purpose of this proceeding:

> [I]t must be emphasized that this entire proceeding is for consideration of a SDER under Section 1307 of the Public Utility Code, which authorizes the establishment of automatic adjustment clauses or sliding scales of rates."[3]

This characterization is not only erroneous, but also seriously calls into question the value of PPL's advocacy. PPL's belated Section 1307 rider, even with I&E's proposed modifications offered in the spirit of the failed "collaborative," did not produce a product able to withstand legal and evidentiary scrutiny. It should be rejected.

As I&E has previously noted, at no time did any party on the record below or in advocacy before the Commission raise a Section 1307 rider as an appropriate replacement funding mechanism to address PPL's storm damage expenses. PPL actively ***dismissed*** rider funding on the record and ignored I&E's repeated testimony regarding reserve funding. While in Exceptions PPL accepted the concept of a "reserve/tracker" mechanism to replace its insurance, never did PPL raise a Section 1307 rider.[4] The first

[3] PPL December 2013 Comments at 22.

[4] PPL acknowledged that it proposed a reserve/ tracker in Exceptions and intended to propose a reserve/tracker in its compliance filing. *See e.g.* PPL May 6, 2013 Replies to Comments at 6. It has simply failed ever to do so.

time a Section 1307 rider appeared was in PPL's March 28, 2013 compliance filing. On reconsideration of the Commission's *December 2012 Order*, the Commission expressly directed parties to the collaborative to consider both reserve and rider funding. PPL paid no heed to either the collaborative or alternative funding other than a Section 1307 rider.

By ignoring the proper scope of this proceeding and avoiding addressing fully the issue of reserve funding, PPL has failed to contribute substantively to the Commission's consideration of an appropriate resolution of a proper funding mechanism to replace PPL's self-serving affiliated insurance purchases. PPL's Section 1307 rider should be rejected as unsound and unsupported.

PPL's incalcitrance is further demonstrated in PPL's most recent round of comments in which PPL has, again, avoided the Commission's direction to address reserve funding. In its April 2013 Comments, I&E provided a thorough discussion of actions taken in other jurisdictions that address the variability of storm damage expenses. As stated therein and again in I&E's December 16, 2013 comments, a wide variety of jurisdictions within the context of a base rate case establish a reserve account for storm expenses and establish an appropriate rate to fund that reserve.

Though provided an opportunity to reply substantively to I&E's legal discussion in its April 2013 Comments, PPL chose instead to dismiss the discussion out of hand. Stating that I&E's modification to PPL's SDER to assimilate reserve accounting "raises concerns of legality under the Pennsylvania Public Utility Code," PPL avoided

responding to other jurisdictions' actions by concluding, without analysis, that "actions in other states under different laws do not provide support for [I&E's] proposal."[5]

PPL reached this conclusion notwithstanding I&E's identification of reserve accounting in several jurisdictions, at least one of which concluded, with the affirmation of its Supreme Court, that the ability to approve reserve funding has its basis in the regulatory commission's general ratemaking authority.[6] As that regulatory commission noted, "[t]he Mississippi Supreme Court has upheld the establishment of a storm reserve noting that '***it is common practice for public service commissions to permit as an item of expense chargeable to ratepayers the establishment of a reserve for storm damage and to authorize, as a legitimate expenses of operation, annual contributions to those storm reserves***.'"[7]

Notably, nowhere does PPL contend that the Pennsylvania Commission lacks authority under its general ratemaking authority to institute reserve accounting. To the contrary, as stated above, PPL has never opposed the concept of a reserve, and specifically included it in its Exceptions. Rather than substantively addressing the issue, however, PPL dismisses it, implying that only when accompanied by a comprehensive survey of each jurisdictions' regulatory laws would another state's authority have any value. This argument unnecessarily attaches a complex prerequisite to any legal analysis and consideration of reserve accounting rendering it virtually useless, precisely the result PPL seeks.

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[5] PPL May 6, 2013 Replies to Comments at 23.
[6] *See* I&E April 2013 Comments at 19-21.
[7] *In Re: Notice of Intent of Entergy Mississippi, Inc. to Change Rates by Implementing Storm Damage Rider Schedule SD-8 to Supersede Storm Damage Rider Schedule SD-7 (Entergy Mississippi)*, 2012 WL 3265080 (Miss.P.S.C.), slip opinion at 1, note 1 (citation omitted; emphasis added).

The fallacy of that argument is similar to PPL's contention that any storm reserve authorized in another jurisdiction that allows recovery of capitalized costs is equally useless because that is automatically per se illegal in Pennsylvania.[8] Indeed, it is not that PPL is not authorized to recover capitalized costs in any storm expense funding mechanism, it is simply that the recovery of capital costs *in a Section 1307 rider* previously has been found to be improper by the courts because, among other reasons, such recovery lacked the thorough review of a base rate case.[9] Should PPL's storm reserve including an appropriate funding level and mechanism be decided within a base rate case, as I&E contends, reserve accounting would not be "illegal" simply because it included capitalized costs.

I&E also questions the value of PPL's efforts to comply with the Commission's direction to address regulatory precedent for reserve funding both within and outside Pennsylvania by citing pages from an Edison Electric Institute (EEI) report that was neither previously introduced nor assessed by the parties.[10] If intending to fully air the issue, PPL would have better served the Commission by citation to and discussion of these jurisdictions' actual regulatory and judicial decisions. PPL's efforts to address reserve accounting strike I&E as uncooperative and uninstructive as its collaborative.

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[8] *See e.g.* PPL December 16, 2013 Comments at 18, 19, 20.

[9] *Popowsky v. Pa. PUC*, 869 A.2d 1144, 1156 (Pa. Commw 2005) (contrasting surcharge recovery versus base rate review and disallowing surcharge recovery because, inter alia, it "involves, at most, a 'preliminary and cursory' review" and that "the 'cursory' review undertaken for a surcharge is not a substitute for the review undertaken in a base rate case to determine whether a rate is just and reasonable.").

[10] In the base rate case below, I&E witness Morrissey also relied on an EEI publication to support her recommended disallowance of PPL's affiliated storm insurance. The pertinent document was addressed in I&E's testimony and provided as an exhibit, was distributed to parties in discovery as part of I&E's workpapers, was addressed by PPL's witness in responsive testimony, and was available as a subject for cross-examination. *See* I&E Statement No. 2 at 33; I&E Exhibit No. 2, Sch. 20; PPL Statement No. 14-R at 4-5; I&E Statement No. 2-SR at 31-32; I&E Exhibit No. 2-SR, Sch. 5.

B. PPL's Rider SDER As Proposed And Modified Does Not Adequately Address Funding Either In Level Or Manner Of Recovery

In its most recent comments, PPL has proposed several modifications to its Section 1307 Rider. These multiple last-minute revisions are by themselves further reason to reject PPL's Rider. A matter of this import and precedent should not be set "on the fly." Further, some of PPL's adjustments and descriptions are erroneous and would benefit greatly from comprehensive review in PPL's upcoming base rate case.

Among other changes proposed by PPL, the Company now requests one-year recovery of all qualified reportable storm expenses no matter their level or degree. From PPL's perspective, having a fully reconcilable annual rate rider eliminates the need to amortize extraordinary storm expenses because "[t]he concept of amortization simply does not apply to a Section 1307 automatic adjustment clause" and the rate impact on whole is not volatile.[11] For the reasons described in I&E's December 16, 2013 Comments, however, the standards for rider recovery are not synonymous with the standards for deferred accounting and amortization of extraordinary storm expenses and they may not be interchanged. That PPL was previously afforded retroactive recovery of extraordinary and unanticipated storm expenses through deferred accounting petitions does not support approval of the Company's prospective dollar-for-dollar recovery of all reportable storm-related expenses under Section 1307.

In further defense of its Section 1307 structure to include interest on both over and undercollections, rather than allowing interest to accrue to fund the reserve, the Company also describes its method as applying interest in "an even-handed, symmetrical manner to

[11] PPL December 16, 2013 Comments at 14.

both under and over recoveries."[12] However, based on the method PPL used to develop the embedded base rate expense level relative to what the SDER is designed to cover, this is patently inaccurate.

PPL states that "[t]he amount of $14.7 million was based upon a study of PPL Electric's actual storm damage expenses over an extended period of time, and does not include extraordinary storm damage expenses previously or currently amortized in base rates."[13] This, in essence, means that the Company established a rider budget amount based on a level of storm costs that *excluded* extraordinary storm costs, yet proposes a rider that is intended, prospectively, to recover *all* storm costs – *including* extraordinary storms, and to recover all in a one-year period. The method PPL used to develop the base rate budget relative to the storm costs purportedly included in its proposed Section 1307(e) rider, therefore, is inherently established so that PPL will underrecover its costs, consistently placing the Company in the position of collecting interest from ratepayers. This approach is neither even-handed nor symmetrical. Indeed, such a design could substantially reward the Company.

Were PPL to experience a substantial storm with expenses requiring financing through long or short-term debt, the Company could subject ratepayers to the payment of interest twice, once through the recovery of interest from ratepayers on the undercollection recovered through the Section 1307 rider and a second time through the recovery of the interest associated with the debt presented in the Company's subsequent

[12] PPL December 16, 2013 Comments at 2.
[13] PPL December 16, 2013 Comments at 2.

rate case. The facts that PPL obtains its financing from its affiliate,[14] was not allowed interest on deferred regulatory assets under current Commission practice but seeks interest now, and has designed a rider that mismatches revenues to expenses such that underrecovery with associated ratepayer interest charges are likely all raise to I&E the same serious concerns about PPL's financial dealings with its affiliates that led to I&E's recommendation that PPL terminate its affiliated storm insurance purchases in the first place.

Moreover, PPL never provides the historical data it used to develop its $14.7 million base rate expense budget. I&E, however, on the record below did develop a five-year recommended budget amount, which included the 2011 extraordinary storms submitted for deferral, to arrive at an annual storm expense budget amount of $23.875 million.[15] For PPL's proposed Section 1307(e) rider to resemble an even-handed and symmetrical approach to interest, a budget amount closer in magnitude to that developed by I&E should be established in base rates to fund the reserve (or, as PPL prefers, better approximate a rider funding level). To exclude extraordinary storms from the budget calculation yet include those costs in a 1307(e) rider, however, as PPL has done, positions ratepayers constantly to be paying interest, which is simply inappropriate.

Any viable option, most particularly one intended to fund expenses outside a base rate case through a Section 1307 rider, should include costs that are easily identifiable and subject to a simple mathematical calculation. By excluding extraordinary storms in its budget calculation, however, PPL has created a mismatch between the storms subject

[14] *See* I&E Main Brief at 83; I&E Reply Brief at 61.
[15] *See* OCA December 16, 2013 Comments at 6, citing relevant I&E evidentiary sources.

to recovery under its rider and those included in the calculation of its proposed funding level. This is not sound accounting on any level, presenting a complication in PPL's proposal from the initiation that jeopardizes the accuracy of precisely the funding the rider is intended to provide. This would be mere unsound budgeting practices were it not for the fact that a rider with a design flaw that will assuredly result in undercollection of expenses will guarantee a continual stream of interest revenue from ratepayers. Any extraordinary storm not currently subject to amortization, e.g., Sandy, and any prospective extraordinary storms would have to be excluded from rider recovery and subject to deferred accounting petitions until the storm expense budget could be appropriately sized in a subsequent base rate case or ratepayers very likely will constantly be called upon to pay interest.

While this complication further supports rejection of PPL's proposed SDER in any form, I&E continues to recommend that the $14.7 already accrued by PPL in base rate revenues as a result of the experienced "blue sky" 2013 storm year be considered "seed money" in a reserve that PPL should be compelled to account for as proposed by I&E and recommended for adoption by the ALJ. PPL's newly proposed January 2014 effective date would conveniently eliminate this potential reserve starting funding that would be realized as a result of PPL's 2013 "blue sky" storm year. If I&E's storm reserve account proposal is accepted, PPL should be required to establish a starting reserve account balance reflecting the expense and revenue results of 2013.

II. CONCLUSION

The Bureau of Investigation and Enforcement appreciates the Commission's continued commitment to consideration of reserve accounting as a more appropriate funding mechanism for PPL's recovery of storm damage expenses to replace PPL's disallowed affiliate insurance. Based upon the advocacy provided by the parties to this proceeding, I&E believes that the Commission should reject PPL's efforts to implement a Section 1307 rider, compel PPL to implement reserve accounting effective January 1, 2013, and defer addressing the matter further until PPL files its next base rate case "during 2014 or before."[16]

Respectfully submitted,

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Dated: December 31, 2013

[16] *See* I&E December 16, 2013 Comments at 7, citing PPL's Main Brief below at 76.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
v.	:	
	:	**Docket No. R-2012-2290597**
PPL Electric Utilities Corporation	:	
	:	

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing **Replies to Comments** dated December 31, 2013, in the manner and upon the persons listed below, in accordance with the requirements of § 1.54 (relating to service by a party):

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