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

IN REPLY PLEASE
REFER TO OUR FILE

July 2, 2018

Secretary Rosemary Chiavetta
Pennsylvania Public Utility Commission
Commonwealth Keystone Building, Second Floor
400 North Street
Harrisburg, PA 17120

Re: Pennsylvania Public Utility Commission v.
UGI Utilities Inc. - Electric Division
Base Rates
Docket No. R-2017-2640058

Dear Secretary Chiavetta:

Enclosed for filing please find the Bureau of Investigation and Enforcement's (I&E) **Main Brief** for the above-captioned proceeding

Copies are being served on all active parties of record. If you have any questions, please contact me at (717) 425-7593.

Sincerely,

Scott B. Granger
Prosecutor
Bureau of Investigation and Enforcement
PA Attorney I.D. No. 63641

SBG/smw
Enclosure

cc: Certificate of Service
ALJ Steven K. Haas
ALJ Andrew M. Calvelli

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	**Docket No. R-2017-2640058**
	:	
UGI Utilities, Inc. – Electric Division	:	

MAIN BRIEF
OF THE
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Dated: July 2, 2018

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I. INTRODUCTION

A. History of the Proceeding

On January 26, 2017, UGI Utilities, Inc. – Electric Division ("UGI Electric" or "Company") filed its proposed Tariff - Electric - PA. P.U.C. Nos. 6 and 2S ("Tariffs 6 and 2S") with a proposed effective date of March 27, 2018. UGI Electric stated that it is requesting an increase in its annual jurisdictional distribution operating revenues by $9.254 million.[1] UGI Electric claimed the $9.254 increase would produce an increase in total revenues (distribution, transmission and generation charges) of approximately 10.4%.[2] UGI Electric's January 26th filing, however, did not address the impact of the Tax Cut and Jobs Act of 2017 ("TCJA") signed into law on December 22, 2017, which significantly reduced the corporate Federal Income Tax rate from 35% to 21%.

Later, on March 12, 2018, UGI Electric filed supplemental direct testimony after its analysis of the TCJA was complete. The Company, in its supplemental direct testimony, revised its filing in consideration of the effects of the TCJA.[3] As a result of the Company's revisions, the Company reduced its revenue increase request from $9,254,354 to $8,491,187.[4]

UGI Electric chose to use the Fully Projected Future Test Year ("FPFTY") as the basis for its requested base rate increase filing. The Company used the twelve months

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1 UGI Electric Statement of Reasons, p. 1.
2 *Id.*
3 I&E St. No. 3, p. 2. *See also* UGI Elec. St. No. 2-SD, p. 1.
4 I&E St. No. 3, p. 2, *citing* UGI Elec. St. No. 2-SD, p. 3.

ended September 30, 2017 as the historic test year (HTY), the twelve months ending September 30, 2018 as the future test year (FTY), and the twelve months ending September 30, 2019 as the FPFTY in this rate case proceeding.[5] To date, the Commission has not adopted final rules or regulations regarding the use of a FPFTY in base rate case filings by regulated utilities. In that regard, the Commission initiated a separate proceeding at Docket No. L-2012-2317273 for adopting final rules and regulations for the use of a FPFTY and that proceeding is ongoing.[6] Several of the issues in this proceeding arise out of differing interpretations regarding the use of the FPFTY in base rate cases in Pennsylvania.

The parties actively participating in this proceeding are I&E; the Office of Consumer Advocate ("OCA"); and the Office of Small Business Advocate ("OSBA").

On March 1, 2018, pursuant to 66 Pa. C.S. § 1308(d), the Commission entered an Order suspending the implementation of proposed Tariffs 6 and 2S by operation of law until October 27, 2018, and opening an investigation to determine the lawfulness, justness, and reasonableness of the rates, rules, and regulations contained in the proposed Tariffs 6 and 2S.

The proceeding was assigned to Administrative Law Judges Steven K. Haas and Andrew M. Calvelli. A telephonic Prehearing Conference was held on March 22, 2018. And, public input hearings were held on April 18, 2018 at 1:00 and 6:00 p.m.

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5 I&E St. No. 1, p. 3.

6 I&E St. No. 1, p. 4. *See Use of Fully Projected Future Test Year, 52 Pa. Code Chapter 53*, Docket No. L-2012-2317273.

Pursuant to the established litigation schedule, I&E filed the following pieces of direct testimony on April 26, 2018; and, I&E filed the following pieces of surrebuttal testimony on June 7, 2018:

Christine Wilson	I&E Statement No. 1 – Non-Proprietary I&E Exhibit No. 1 – Non-Proprietary I&E Statement No. 1 – Proprietary I&E Exhibit No. 1 – Proprietary I&E Statement No. 1-SR Errata Sheet to I&E Statement No. 1-SR I&E Exhibit No. 1-SR – Non-Proprietary I&E Exhibit No. 1-SR – Proprietary
Anthony Spadaccio	I&E Statement No. 2; I&E Exhibit No. 2 I&E Statement No. 2-SR
Ethan Cline	I&E Statement No. 3; I&E Exhibit No. 3 Errata Sheet to I&E Statement No. 3 I&E Statement No. 3-SR; I&E Exhibit No. 3-SR
Brenton Grab	I&E Statement No. 4; I&E Exhibit No. 4 I&E Statement No. 4-SR
Joseph Kubas	I&E Statement No. 5; I&E Exhibit No. 5 I&E Statement No. 5-SR.

During the course of this proceeding the parties held a series of settlement conferences but were unable to amicably resolve the issues presented in UGI Electric's base rate filing. On June 11-12, 2018, at the time and place set for the evidentiary hearing, the parties appeared before ALJ Haas. The parties presented witnesses and pre-served written testimony subject to cross examination; and, also stipulated to the admission of the remaining pre-served written testimony and waived cross-examination. I&E moved the pieces of I&E testimony and exhibits identified above into evidence. A court reporter was present, and Hearing Transcripts ("Tr.") for June 11, 2018, pages 72

through 154, and for June 12, 2018, pages 155 through 169, were prepared and distributed to the parties.

I&E now submits this Main Brief ("I&E MB") in support of the arguments made by the I&E witnesses in the record-evidence presented. I&E also offers support for various arguments propounded by OCA and OSBA.

B. Legal Standards / Burden of Proof

It is axiomatic that the burden of proof in any proceeding involving a utility's existing or proposed rates is on the utility.[7] UGI Electric must satisfy its burden of proof by presenting a preponderance of evidence.[8] A preponderance of the evidence is such evidence that is more convincing, by even the smallest amount, than that presented by another party.[9] If a preponderance of evidence is submitted, the burden of going forward with competing evidence shifts to opposing parties to produce credible evidence of at least equal weight.

While the burden of going forward and producing evidence may shift back and forth between the parties, the ultimate burden of persuasion remains with the Company. Further, the Commission must ensure that any adjudication is supported by substantial evidence. "Substantial evidence" is such relevant evidence that a reasonable mind might accept as adequate to support a conclusion.[10]

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7 *See* 66 Pa.C.S. §§1301, 315(a); *Brockway Glass Co. v. Pennsylvania Public Utility Commission*, 437 A.2d 1067 (Pa. Commw. 1981); *Lower Frederick Twp. v. Pennsylvania Public Utility Commission*, 409 A.2d 505 (Pa. Commw. 1980).

8 *Samuel J. Lansberry, Inc. v. Pennsylvania Public Utility Commission*, 578 A.2d 600 (Pa. Commw. 1990).

9 *Se-Ling Hosiery v. Margulies*, 70 A.2d 854 (Pa. 1950).

10 *Norfolk & Western Ry. Co. v. Pennsylvania Public Utility Commission*, 413 A.2d 1037 (Pa. 1980);

I&E asserts that UGI Utilities, Inc. – Electric Division has failed to meet its burden and therefore I&E respectfully requests that the Administrative Law Judges and the Commission adopt the adjustments and the overall revenue requirement set forth in the record evidence presented by I&E and as asserted in this I&E Main Brief.

II. SUMMARY OF ARGUMENT

UGI Electric has failed to present substantial credible record evidence to support its request for an $8,491,187 revenue requirement increase. Based upon I&E's adjustments following hearings and the creation of a full evidentiary record on all issues, the record evidence proves that only a revenue increase of $863,000 is warranted. This recommendation is based upon the adjustments offered by I&E, as set forth more fully herein and summarized in Table I (Income Summary), Table II (Summary of I&E Adjustments), and Table III (Rate of Return) collectively attached hereto as Appendix "A."

Overall, this base rate proceeding presents the Administrative Law Judges and the Commission with some new and novel issues as well as the tried and true rate base proceeding issues. The new and novel issues include the effect of the Tax Cut and Jobs Act of 2017 on regulated public utilities; the effect of the Tax Cut and Jobs Act of 2017 on the Company's Accumulated Deferred Income Taxes; the application of the average rate base methodology to the Fully Projected Future Test Year; and, the interplay between UGI Electric's Quarterly Earnings Reports and the FPFTY approved for use in base rate cases in Act 11.

I&E recommends the use of the average rate base methodology as opposed to the year-end methodology to calculate the Company's FPFTY utility plant-in-service amount. I&E believes that using the average rate base methodology results in rates that are more just and reasonable because ratepayers are not paying for approximately a year of plant that is only proposed and is not subject to any guarantee of being completed and placed into service. Therefore, I&E recommends that UGI Electric's FPFTY year-end utility plant in service methodology be rejected and that a total utility plant in service amount of $173,871,383 be adopted instead. I&E also recommends an accumulated depreciation level based on the average rate base methodology of $58,992,386. I&E's recommended accumulated depreciation was determined by taking the average of the Company's accumulated for the FTY ending September 30, 2018 and the Company's rebuttal accumulated depreciation for the FPFTY ending September 30, 2019.

I&E recommends an allowance of $6,742,000, or a reduction of $591,000 to the Company's Cash Working Capital claim. I&E's allowance is based on a modification of the Meter Read Lag Day factor from 2.70 days to 1.50 days due to major software system improvements by the Company; modification of other O&M Expense Lag Days from 12.56 days to 15.06 days based on a 12-month average rather than four sample months as used by the Company; and modification of the Company's claim based on I&E's adjustments to O&M expenses.

I&E also recommends that Materials and Supplies be increased by $24,692 up to $1,464,692 based on the 13-month average calculated using updated Materials and Supplies balances provided by the Company.

Regarding deductions from rate base, I&E recommends that the Company's claim for Accumulated Deferred Income Taxes be reduced by $287,500 down to $16,284,500. I&E determined its recommended adjustment to the Company's claim for ADIT by using the average rate base methodology. Further, I&E recommends that the Company be required to reduce rate base in the revenue requirement formula for the excess ADIT balance which resulted as a reclassification of the portion of ADIT associated with the reduction in the federal income tax rate from 35% to 21% due to the enactment of the TCJA. I&E recommends reducing the Company's rate base by the excess ADIT balance at the end of the FPFTY in the amount of $11,483,354. Finally, I&E recommends the Company's customer deposit claim be increased by $76,692 up to $1,495,692 in both the FTY and the FPFTY. I&E determined its recommended level of customer deposits by calculating an average of the most recent 13 months of actual customer deposits balances.

As a result of I&E's application of the average rate base methodology and the resulting recommended adjustments; coupled with the remaining I&E rate base adjustments, I&E reduced the Company's claimed rate base for FPFTY by $25,436,011.

I&E recommends that the Company's total operating revenue under pro forma present rate revenue be decreased by $60,412 down to $87,858,765. Because I&E is recommending the application of an average rate base methodology to calculate the Company's rate base and depreciation expense claims, for purposes of consistency, it is also necessary to calculate the Company's present rate revenue level in the FPFTY using a consistent average rate base methodology. I&E reasoned that when calculating a

revenue requirement in a designated test year, it is vital that the expenses and revenues are assessed using the same time period.

A public utility is entitled to recover all reasonable and normal operating and maintenance expenses incurred by providing regulated services. To the extent that expenses are not incurred, imprudently incurred, or abnormally overstated during the test year, they should be disallowed and found not recoverable through rates.

The following is a summary of I&E's recommendations with regard to the claimed UGI Electric expenses at issue in this proceeding, all of which are represented in Appendix A, Table II. I&E recommends an allowance of $1,912,266 for vegetation management which represents a reduction of $206,235 for the FPFTY. I&E recommends an allowance of $140,000 for Company-Owned Services program expenses which represents a reduction of $314,418 to the Company's proposed service transition program. Regarding environmental remediation expense, I&E agrees with the position presented by OCA that these costs should be removed from the cost of service and instead recovered from the sales proceeds of the associated property thereby removing $139,000 from the Company's revenue requirement claim. I&E recommends an allowance of $253,229 for the Company's storm damage expense claim which represents a reduction of $47,771.

I&E recommends that the Company's rate case expense claim be normalized over a period of 60 months (five years) resulting in an annual expense of $135,000 which represents a reduction of $90,000 to the Company's claim.

There are five claimed employee expenses at issue in this proceeding. First, I&E recommends an allowance for salaries and wages (net of employee additions), of $4,959,000 which is a reduction of $34,000 to the Company's claim. Second, I&E recommends an allowance of $318,000 for employee additions which represents a reduction of $64,000 to the Company's claim. Third, I&E recommends an allowance of $21,000 for outside services employed which represents a reduction of $170,000 to the Company's claim. Fourth, I&E recommends disallowance of the Company's total claim of $11,848 for employee activity costs. And fifth, I&E recommends the disallowance of the Company's total claim for allocated stock options and also recommends the disallowance of the company's total claim for restricted stock awards.

I&E recommends an annual depreciation expense of $5,290,062 based on the application of the average rate base methodology for plant-in-service as it relates to the Company's annual depreciation expense.

The Company noted that it had been over collecting on Other Post-Employment Benefits ("OPEB") expense since the Company's last base rate proceeding dating back to 1996. The Company admitted that the OPEB fund has been generating more income than its expenses and UGI Electric has accumulated an overcollection amount of $7.9 million over the last 22 years. The Company proposal is to refund this overcollection back to ratepayers over 20 years which would result in a return of $395,000 annually to ratepayers.

I&E recommends the Company's claimed power supply expense adjustment be increased by approximately $19,500 up to $1,952,500 as a result of I&E's use of the average rate base methodology adjustment to present rates.

I&E's total expense adjustments of $1,283,000 are shown on the Summary of I&E Adjustments in Appendix A, Table II. Further, I&E's use of the average rate base methodology reduces the annual depreciation expense claim for the FPFTY by $579,062.

Regarding the Tax Cut and Jobs Act of 2017, I&E recommends that the Company be required to flow back to ratepayers, via a reconcilable Section 1307 surcharge mechanism, the net tax savings associated with the reduction in the federal income tax rate for the period January 1, 2018 through the date when the new rates from this proceeding are expected to go into effect. I&E has provided suggested language for the surcharge mechanism in Appendix B.

I&E recommends that the excess Accumulated Deferred Income Tax currently held by the Company be returned to ratepayers over a period of time equal to the remaining life of the affected assets per IRS regulation. In conjunction, I&E also recommends that the Company be required to reduce rate base in the revenue requirement formula for the excess ADIT balance which resulted as a reclassification of the portion of ADIT associated with the reduction in the federal income tax rate due to the enactment of the TCJA.

I&E recommends that UGI Electric be afforded the opportunity to earn an overall rate of return of 6.82%. This recommended overall rate of return is comprised of a weighted average of a 4.69% rate of return on long-term debt and an 8.62% rate of return

on equity. I&E applied the Discounted Cash Flow ("DCF") method and also performed a Capital Asset Pricing Model as a comparison to the DCF results. Further, the parties accepted the capital structure proposed by the company. Finally, I&E performed an investigation into the inclusion of the Company's FPFTY plant into their Quarterly Earnings Reports ("QER"). This investigation resulted in questions being raised as to whether the inclusion of the FPFTY plant ultimately clouded the Company's presentation of their claimed historic return on equity and overall rate of return which permeated throughout the Company's rate of return testimony trying to justify an elevated return on equity and overall rate of return.

Regarding rate structure, I&E did not present testimony regarding the Company's allocated class cost of service study. I&E raise the concept of gradualism with regard to revenue allocation as a well-established ratemaking concept that seeks to limit the large and immediate increases customers receive when rates are increased by seeking to implement significant rate changes on a more gradual basis over time.

Regarding rate design and the residential customer charge, I&E recommends a customer charge for both Rate R and Rate GS-5 of $10.00 per month which is an increase of $4.50 or 81.8%. Further, based on the recommended $10.00 per month customer charge, I&E also recommends single block usage rates for Rate R and Rate GS-5. All of I&E's recommendations for rate design and customer charges take the concepts of rate shock and gradualism into consideration.

I&E further recommends that if the Commission grants less than the Company's requested revenue increase, then the usage rates for the Rate R and GS-5 classes be

scaled back sequentially to produce specific revenue levels for each class first, and then I&E's recommended $10.00 per month customer charge for each class be scaled back if required.

Finally, during the natural course of I&E's investigation into this base rate filing, it became apparent that the Company was alluding to an actual/historic rate of return and return on equity that appeared to be so low as to be a mistake. I&E's investigation uncovered that in the most recent UGI Electric QER provided to the Commission for the 12-month period ending September 30, 2017, the Company appeared to add additional net plant to the actual net plant balance to arrive at the final adjusted net plant in the QER. The adjustments did not appear to be supported by historic data. I&E uncovered that UGI Electric was including proposed FPFTY plant into its QERs filed with the Commission. The effect of the inclusion of the FPFTY plant in the QERs is that it dramatically understates the ROR and the ROE in the reported period and it renders the QERs and the Commission's summary of the QERs meaningless because the reports and summary are based on unsupported projections that do not reflect the current financial position of the utilities being reported.

I&E submits that the totality of its adjustments demonstrates that UGI Electric is only entitled to receive a revenue requirement increase of $863,000 to I&E's adjusted present rate revenue of $89,032,00 in order for UGI Electric to have the opportunity to earn a fair return on and of its investments while providing safe and reliable service at just and reasonable rates. For the reasons, and as more fully discussed below, I&E contends that the record evidence presented by UGI Electric does not substantiate a

revenue increase of $8,491,187; instead, based upon the evidence of record, the Commission should only grant UGI Electric the I&E recommended revenue increase of $863,000.

III. STIPULATION OF PARTIAL SETTLEMENT

A. Capital Structure

Pursuant to the Partial Stipulation agreed to by the parties, the parties except the capital structure proposed by the company in the direct testimony of Paul R Moul, UGI Electric St. No. 5.

B. Depreciation Rates

Pursuant to the Partial Stipulation agreed to by the parties, the parties have agreed that UGI Electric's as-filed depreciation rates are accepted.

C. EV Rider

Pursuant to the Partial Stipulation agreed to by the parties, rate EV is withdrawn at this time without prejudice to the companies right to refile the EV rider in a future rate case or in a separate proceeding at the company's discretion.

D. Storm Damage Expense Rider

Pursuant to the Partial Stipulation agreed to by the parties, the Company will withdraw the proposed Storm Expense Rider without prejudice to its right to refile the Storm Expense Rider in a future rate case or to file with the Commission for deferral of any major storm expenses incurred on or after June 1, 2018.

E. Pennsylvania Public Utility Realty Tax ("PURTA")

Pursuant to the Partial Stipulation agreed to by the parties, base rates established in this proceeding shall reflect $97,000 for PURTA obligations. Any future recalculations of the State Tax Adjustment Surcharge after the effective date of new rates in this proceeding shall also reflect this base amount unless and until a different tax obligation is established by the Pennsylvania Department of Revenue.

F. Universal Service Programs

Pursuant to the Partial Stipulation agreed to by the parties, UGI Electric's Universal Service Programs issues, including the Customer Assistance Program (CAP); Self-certification; Rider C; Budget Billing; and Payment Plans, are all resolved as fully set forth in the Partial Stipulation filed by the parties in this proceeding.

G. Miscellaneous Accounting Issues

Pursuant to the Partial Stipulation agreed to by the parties, the parties have agreed to resolve certain accounting issues presented by the Company in the direct testimony of UGI Electric witness Megan Mattern, which include, the Cloud Based program and the UNITE Phase 2 Costs, as fully set forth in the Partial Stipulation filed by the parties in this proceeding.

IV. RATE BASE

A. Original Cost Utility Plant in Service

Utility plant-in-service comprises all the utility's intangible assets (i.e., organization costs, franchise and consents costs, and land and land right costs) and

tangible assets (i.e., facilities and equipment). Moreover, for a utility plant to be included in rates, the plant must be used and useful in the provision of utility service to the customers. Therefore, by definition, only plant currently providing or capable of providing utility service to customers is eligible to be reflected in rates.[11]

UGI Electric has selected the year ended September 30, 2017 as the HTY, the year ending September 30, 2018 as the FTY, and the year ending September 30, 2019 as the FPFTY.[12]

1. Average Rate Base Methodology vs End of Year

In the absence of clear guidance regarding the application of the FPFTY to base rate proceedings in Pennsylvania, I&E recommends that the Company use an average rate base methodology to calculate UGI Electric's FPFTY utility plant-in-service amount.[13] I&E recommended the use of an average rate base methodology rather than the year-end rate base methodology used by the Company.[14] I&E believes that using the average rate base methodology results in rates that are more just and reasonable because ratepayers are not paying for approximately a year of plant that is only proposed and is not subject to any guarantee of being completed and placed into service.[15] Therefore, I&E recommends that UGI Electric's FPFTY year-end utility plant-in-service be rejected and that a total utility plant-in-service amount of $173,871,383 be adopted instead.[16]

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11 I&E St. No. 3, pp. 4-5.
12 UGI Elec. St. No. 1, p. 8.
13 I&E St. No. 3, pp. 4-13. I&E St. No. 3-SR, pp. 2-12.
14 I&E St. No. 3, p. 5-6.
15 I&E St. No. 3, p. 6.
16 I&E St. No. 3-SR, pp. 11-12. *citing* I&E Exh. No. 3-SR, Sch. 1, ln 4.

I&E's recommendation regarding the use of an average rate base methodology is also supported by OCA witness Lafayette K. Morgan, Jr.[17]

Again, in the absence of clear guidance regarding the application of the FPFTY to base rate proceedings in Pennsylvania, the Company relied on the FPFTY year-end plant-in-service as described in its filing to support its FPFTY plant-in-service claim of $188,423,130.[18]

In support of I&E's recommendation to use the average rate base methodology, I&E offers the following. Under the FPFTY, the traditional interpretation of the "used and useful" requirement for rate base inclusion of investments is unclear because when a company employs the use of a FPFTY in a base rate case, the new rates go into effect before the end of the Company's FPFTY.[19] The inclusion of rate base added in a FPFTY necessarily means that customers will be paying a return on and a return of a utility's plant investment that has not yet been placed in service.[20] By using an average of the rate base that is projected to be in service by the end of the FPFTY, rather than the full year-end amount, the impact of the necessary customer overpayment at the beginning of the year is mitigated.[21] This results in rates that are more just and reasonable because ratepayers are not paying for approximately a year of plant that is not yet in service.[22]

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17 *See* OCA St. No. 1, pp. 6-9; OCA St. No. 1S, pp. 3-4.

18 I&E St. No. 3-SR, p. 11, *citing* UGI Elec. Exh. JFW-1, p. 2.

19 I&E St. No. 3, pp. 5-6.

20 I&E St. No. 3, p. 6.

21 *Id.*

22 *Id.*

In this instance, UGI Electric is requiring ratepayers, in essence, to pre-pay a return on its projected investment in future facilities that are not only NOT in place and providing service at the time the new rates take effect, but also that are NOT subject to any guarantee of being completed and placed into service.[23] As a result, ratepayers will begin paying for expenses and plant when new rates become effective on October 27, 2018, but those projected expenses and plant may not be incurred or placed into service until September 30, 2019 or even later.[24]

UGI Electric's new rates are expected to become effective on October 27, 2018, which is approximately eleven months before the end of the Company's FPFTY of September 30, 2019.[25] However, none of the Company's capital projects included in the 2019 fiscal year have an in-service date and are merely "planned".[26]

Accordingly, customers would pay rates in October 2018 that are calculated to recover depreciation expense and a return on investment at the end of the FPFTY, which are in excess of the rates that are necessary to provide the revenue requirement that allows the Company the opportunity to earn its authorized rate of return ("ROR") on the plant and expenses that are used and useful when the new rates become effective.[27] Requiring customers to pay a return of and on plant investments that are only proposed to occur in the FPFTY does not produce just and reasonable rates for ratepayers.[28] Instead,

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23 *Id.*
24 *Id.*
25 I&E St. No. 3, p. 7.
26 *Id.*, *citing* I&E Exh. No. 3, Sch. 2.
27 I&E St. No. 3, p. 8.
28 *Id.*

if all projects are completed as proposed, ratepayers reach the projected "just and reasonable" rate point on the final day of the FPFTY or more specifically on the first day of the year after the FPFTY.[29]

Furthermore, as I&E notes, an average rate base would yield an average annual return on rate base throughout the FPFTY equal to the authorized ROR.[30] Whereas, under the Company's proposed methodology, as illustrated in I&E witness Cline's direct testimony, only the end-of-year point at Day 365 would coincide with the authorized ROR, which would shift the entire graph upwards with the entire ROR line shifted above the authorized rate of return for every point.[31]

I&E also notes, the Company's proposed use of the FPFTY year-end methodology has additional negative effects.[32] As I&E witness Cline points out, the return of investment, or depreciation expense, which is recovered on a dollar for dollar basis, will also be overstated to reflect an amount greater than the Company's actual recorded depreciation expense in the FPFTY.[33] Because the plant is added at different dates throughout the year, the Company will not record a full-year of depreciation expense for plant that is added variably throughout the year, which results in a greater revenue requirement result than necessary when the full end-of-year depreciation expense is included in the Company's FPFTY claim.[34]

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29 *Id.*
30 I&E St. No. 3, p. 8-9.
31 I&E St. No. 3, p. 9.
32 I&E St. No. 3, pp. 9-11.
33 I&E St. No. 3, pp. 9-10.
34 *Id.*

Additionally, the Company's projected usage declines and customer count adjustments projected to the end of the FPFTY will not accurately reflect the actual FPFTY usage, nor will annualized expenses for which a full year's expense is not realized in the FPFTY accurately reflect the actual FPFTY expenses.[35] Both will impact the revenue requirement through the ratemaking equation on a dollar for dollar basis and overinflate the Company's FPFTY revenue needs.[36] These items will all serve to shift the return graph even further upward, which would result in an end of FPFTY ROR that is even higher than the authorized ROR.[37]

And, while the reduction in revenue requirement associated with using the average rate base methodology may impact rate case frequency, Companies should file rate cases on the frequency demanded by revenue needs and should not unnecessarily inflate customer rates beyond what is just and reasonable for the sole purpose of decreasing rate case frequency.[38] Imposing rates on customers that are excessive and unreasonable to alleviate a single issue does not comport with a utility's obligation to provide service at just and reasonable rates.

With regard to the application of a utility company's DSIC, utilizing the average rate base methodology could allow earlier implementation of a DSIC if a company demonstrated that the plant-in-service used to establish rates had been added to rate

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[35] I&E St. No. 3, p. 10.

[36] *Id.*

[37] *Id. See also* I&E St. No. 1 (expenses) and I&E St. No. 2 (rate of return) for the domino effect of the FPFTY year-end methodology.

[38] I&E St. No. 3, pp. 10-11.

base.[39] Implementation of the DSIC earlier would mitigate the impact of the rate increase that would result from assuming a year-end rate base in establishing rates and still provide a company the opportunity to recover later DSIC-eligible plant investments, potentially within the FPFTY.[40] Earlier implementation of the DSIC could also limit any increase in rate case frequency presumed to be associated with usage of the average rate base method.[41]

I&E recognizes that it is asking the Commission to approve a methodology that has not yet been adopted by this Commission. Nevertheless, I&E is aware of at least one other state utility commission that is utilizing the average rate base methodology.[42] The Illinois Commerce Commission ("Illinois Commission") concluded, in a recent proceeding, that an average rate base is more appropriate than a year-end rate base, given a future test year.[43] The Illinois Commission's decision is relevant and can provide guidance in Pennsylvania because the Illinois Administrative Code[44] allows a utility to propose a "future" test year that is "[a]ny consecutive twelve month period of forecasted data beginning no earlier than the date new tariffs are filed and ending no later than 24 months after the date new tariffs are filed."[45] Accordingly, the Illinois 24 month period includes the 12 month period that comprises Pennsylvania's FPFTY. Further, 83 Ill. Admin. Code Section 285.2005(e) implies that average data should be used, imposing

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39 I&E St. No. 3, p. 11.
40 *Id.*
41 *Id.*
42 I&E St. No. 3, pp. 12-13.
43 I&E St, No. 3, pp. 12-13, *citing Re North Shore Gas Company*, 2013 WL 3762292 (Ill. C. C.), pp. 28-29 (Order entered June 18, 2013).
44 *See* 83 Ill. Adm. Code 287.20.
45 I&E St. No. 3, p. 12, *quoting* 83 Ill. Adm. Code 287.20. *See also* I&E Exh. No. 3, Sch. 3.

additional specific reporting and calculation requirements if the average rate base methodology is not used.[46]

In response to the recommendation to use the averages rate base methodology for the FPFTY by both I&E and OCA, UGI Electric argues that it does not agree that using an average rate base more accurately reflects the period during which rates in this proceeding will be in effect.[47] The Company argues, because the rates set in this proceeding would be in effect for three or more years thereafter, that the use of average rate base methodology does not accurately reflect plant investment during the time rates will be in effect.[48]

I&E argues that UGI is incorrect in its assumption that the entire three or more year period that rates are in effect should be utilized to set base rates in this proceeding.[49] Projection of revenues and expenses beyond the FPFTY has not been permitted by the Commission.[50] Rates are not meant to be set so that the Company can recover the cost of projects outside of the FPFTY that were not included in base rates.[51] Further, should the Company require additional rate relief due to the addition of plant in service for the safe and reliable provision of service, the Company can and should acquire funding for those projects through the use of a Distribution System Improvement Charge ("DSIC"), should those projects be eligible, or through the filing of future base rate cases.[52]

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46 I&E St. No. 3, p. 13. *See also* I&E Exh. No. 3, Sch. 4, p. 2.
47 I&E St. No. 3-SR, p. 3.
48 I&E St. No. 3-SR, p. 4, *citing* UGI Elec. St. No. 4-R, p. 3.
49 I&E St. No. 3-SR, p. 4.
50 *Id.*
51 *Id.*
52 *Id.*

UGI Electric also argues[53] that end of test year plant balances were routinely accepted prior to the passage of Act 11 and that Section 315(e) of Act 11 states that "the Commission may permit facilities which are projected to be in service during the fully projected future test year to be included in the rate base."[54]

I&E asserts while the language of Act 11 as provided by UGI Electric does permit inclusion of plant proposed to be placed into service throughout the FPFTY to be included in rates, it does not indicate a specific or preferred methodology for recovery in rates.[55] I&E's recommendation does not preclude the Company from projecting plant additions throughout the FPFTY.[56] In fact, the average is based upon the full proposed FPFTY level of plant additions and the level of plant additions projected in the FTY.[57] Instead, I&E's recommendation lowers the amount of return on and of the Company's investment that customers are required to pay for through rates on plant that is merely proposed but is not yet and may never be used and useful in the provision of service.[58] Additionally, the ratemaking treatment of plant-in-service prior to and after the passage of Act 11 are not comparable.[59]

Further, the Company did not provide an in-service date for any of the projects it has projected to be in service during the FPFTY.[60] The use of the average rate base methodology that both I&E and OCA recommend mitigates the risk to customers that the

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53 I&E St. No. 3-SR, p. 5
54 66 Pa. C.S. § 315(e).
55 I&E St. No. 3-SR, p. 5.
56 *Id.*
57 I&E St. No. 3-SR, pp. 5-6.
58 I&E St. No. 3-SR, p. 6.
59 *See* I&E St. No. 3-SR, p. 7.
60 I&E St. No. 3-SR, p. 7, *citing* I&E Exh. No. 3, Sch. 2.

vague "planned" projects proposed by the Company in the FPFTY, which will be included in customer rates at the beginning of the FPFTY, will not be placed into service, as proposed, by the end of the FPFTY.[61]

UGI Electric also claims that the use of the average plant in service complicates the alignment of test year plant with test year accumulated deferred income tax (ADIT), accumulated depreciation, annualized depreciation expense, and the annualization of revenues and expenses.[62]

UGI Electric simply makes this claim but provides no further explanation as to how or why the average rate base methodology complicates the alignment of the components of the revenue requirement formula.[63] Further, I&E disagrees that using the average plant in service complicates the alignment of the components of the revenue requirement formula.[64] I&E witness Cline made adjustments throughout his direct testimony using the average rate base methodology to ensure that each component is aligned with the mid-point of the FPFTY.[65] Any complications in this alignment would be generated more from the budget method the Company used in its base rate filing in which the FTY and FPFTY are based on separate and unconnected budgets for the FTY and FPFTY rather than a clear continuation of data starting from actual revenues,

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61 I&E St. No. 3-SR, p. 7.
62 I&E St. No. 3-SR, p. 7.
63 I&E St. No. 3-SR, p. 8.
64 *Id.*
65 *Id.*

expenses, and plant additions experienced in the HTY and the first half of the FTY and projecting through the second half of the FTY and into the FPFTY.[66]

Fourth, the Company argues that the Illinois Administrative Code referenced in I&E direct testimony permits the use of a year-end rate base.[67] The Illinois Commission concluded in the recent *Re North Shore Gas Company* decision that an average rate base is more appropriate than a year-end rate base.[68] The year-end rate base method may be permitted by the Illinois Commission, but the average rate base methodology has been determined by that Commission to be more appropriate in determining rates.[69]

Finally, UGI Electric argues the fact that the statutory advocates have made the recommendation of the average rate base methodology has no probative value in determining whether the year-end rate base is consistent with the language and intent of Act 11.[70] I&E argues to the contrary, in the absence of clear guidance regarding the application of the FPFTY to base rate proceedings in Pennsylvania, it is incumbent upon the statutory parties to raise issues, present well-reasoned arguments, and seek guidance from the Commission on a going forward basis.

Therefore, in consideration of all of the above and the record evidence presented by I&E, I&E recommends that the Company use an average rate base methodology to calculate UGI Electric's FPFTY utility plant-in-service amount. I&E recommends the

66 *Id.*
67 *Id.*
68 I&E St, No. 3-SR, p. 9, *citing Re North Shore Gas Company*, 2013 WL 3762292 (Ill. C. C.), pp. 28-29 (Order entered June 18, 2013).
69 *Id.*
70 I&E St. No. 3-SR, p. 9.

use of an average rate base methodology rather than the year-end rate base methodology used by the Company.

2. Electrical Engineering and Operations Center

I&E takes no position regarding the Company's rate base claim for its electrical engineering and operations center.

B. Accrued Depreciation

I&E recommends an accumulated depreciation level based on the average rate base methodology, advocated for by I&E and OCA, of $58,992,386.[71] I&E's recommended accumulated depreciation was determined by taking the average of the company's accumulated depreciation for the FTY ending September 30, 2018 and the Company's rebuttal accumulated depreciation for the FPFTY ending September 30, 2019.[72] ($58,179104 + $59,805,668) / 2 = $58,992,386.[73]

UGI Electric's accumulated depreciation claim for the FTY is $58,179,104 and for the rebuttal FPFTY is $59,805,668.[74] UGI Electric rejected I&E's use of the average rate base methodology, and therefore, UGI Electric recommended that I&E's accumulated depreciation based on the use of the average rate base methodology be similarly rejected.[75]

In surrebuttal, I&E adjusted its original accumulated depreciation recommendation set forth in its direct testimony based on adjustments to the plant-in-service made by the

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71 I&E St. No. 3-SR, p. 15.
72 I&E St. No. 3-SR, pp. 15-16. I&E Exh. No. 3-SR, Sch. 1, ln. 7.
73 I&E St. No. 3-SR, p. 16.
74 I&E St. No. 3-SR, pp. 15-16.
75 I&E St. No. 3-SR, p. 15, *citing* UGI Elec. St. No. 4-R, pp. 14-15.

Company in rebuttal, and therefore, the accumulated depreciation expense recommendation was necessarily revised as well to the final amount.[76] In consideration of the above and the record evidence presented by I&E, I&E recommends an accumulated depreciation level based on the average rate base methodology of $58,992,386.

C. Additions to Rate Base

1. Cash Working Capital

Cash Working Capital, ("CWC"), includes the amount of funds necessary to operate a utility during the interim period between the rendition of service, including the payment of related expenses, and the receipt of revenue in payment for services rendered by the utility.[77]

I&E recommends an allowance of $6,742,000, or a reduction of $591,000 ($7,333,000 - $6,742,000), to the Company's claim based on: (1) modification of the Meter Read Lag Day Factor from 2.70 days to 1.50 days due to major software system improvements by the Company; (2) modification of Other O&M Expense Lag Days from 12.56 days to 15.06 days based on a twelve-month average rather than four sample months as used by the Company; and (3) modification of the Company's claim based on my recommended adjustments to O&M expenses and the recommendations of I&E witnesses Ethan Cline (I&E Statement No. 3) and Brenton Grab (I&E Statement No. 4).[78]

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[76] I&E St. No. 3-SR, pp. 15-16.

[77] I&E St. No. 1, p. 42.

[78] I&E St. No. 1-SR, pp 45-46. *See also* I&E St. No. 1, pp. 43-49.

The Company's original claim for CWC was $7,333,000.[79] The Company calculated its CWC claim by using a lead/lag study.[80] A lead/lag study measures the differences in time between: (1) the time services are rendered until payment of those services is received; and (2) the time between the point when a utility has incurred an expense and the actual payment of the expense.[81] Ultimately, in rebuttal testimony, UGI electric provided an updated CWC claim of $7,180,000.[82]

While I&E agrees, generally, with the Company's use of the lead/ lag method, I&E does not agree with the amount of the Company's CWC claim.[83] Also, I&E does not agree with the Companies claimed meter read lag factor of 2.70 days. Instead, I&E recommends a meter read lag day factor of 1.50 days.[84] I&E notes that the Company has made a major investment in software installation in its UNITE Phase I software implementation.[85] The Company, however, did not modify its meter read lag times and does not have a specific plan to modify them.[86] I&E argues that the Company must realize some reduction in the time it takes to read the meters and process data in its computer system after spending a substantial amount of money on new software.[87] The Company simply stated it has no plan to change the number of its meter read lag days but offered no adequate explanation.[88]

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79 I&E St. No. 1, p. 43, *citing* UGI Elec. Rev. Exh. A – Fully Projected, Sch. A-1 (Revised).
80 I&E St. No. 1, p. 42.
81 *Id.*
82 I&E St. No. 1-SR, p. 46, *citing* UGI Elec. Exh. A – Fully Projected (REBUTTAL), Sch. C-4.
83 I&E St. No. 1, pp. 42-48; I&E St. No. 1-SR, pp. 45-50.
84 I&E St. No. 1, p. 45; I&E St. No. 1-SR, pp. 46-47.
85 I&E St. No. 1, pp. 45-46. I&E St. No. 1-SR, p. 47.
86 I&E St. No. 1, p. 46, *citing* I&E Exh. No. 1, Sch. 13, p. 1.
87 I&E St. No. 1-SR, p. 47.
88 I&E St. No. 1, p. 46. I&E St. No. 1-SR, p. 47.

Regarding Other O&M Expense Lag Days, I&E recommended a factor of 15.06 days for the Other O&M Expense Lag Days factor.[89] The Company claimed Other O&M Expense Lag Days of 12.56 days.[90] Then, in rebuttal testimony, the Company accepted the I&E recommendation in its revised CWC claim.[91] Therefore, I&E recommended a factor of 15.06 days for the Other O&M Expense Lag Days factor.[92]

Ultimately, all O&M expense adjustments that are cash-based expense claims are included when determining the Company's overall CWC requirement and the CWC must be modified to reflect the I&E O&M adjustments. .[93] The I&E recommended O&M expense adjustments are summarized in I&E witness Wilson's surrebuttal.[94] In consideration of the above and the record evidence presented by I&E, I&E's updated recommendation for CWC is an allowance of $6,755,000 or a reduction of $425,000 ($7,180,000 - $6,755,000).[95]

Finally, all adjustments to the Company's claims must be continually brought together in the Administrative Law Judge's Recommended Decision and again in the Commission's Final Order. This process, known as "iteration," effectively prevents the determination of a precise calculation until all adjustments have been made to the Company's claims.[96]

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89 I&E St. No. 1, p. 47.
90 *Id.*
91 I&E St. No. 1-SR, p. 47, *citing* UGI Elec. St. No. 4-R, p. 8.
92 I&E St. No. 1-SR, p. 47.
93 I&E St. No. 1-SR, pp. 48-50.
94 *Id.*
95 I&E St. No. 1-SR, p. 50.
96 *Id.*

2. Materials and Supplies

I&E recommended, based upon the 13-month average calculated using updated Materials and Supplies balances provided by the Company, that Materials and Supplies be increased by $24,692 to $1,464,692.[97]

The Company originally claimed $1,440,000 in Materials and Supplies in its base rate filing.[98]

I&E also notes that because the 13-month average of actual materials and supplies balance was used for both the FTY and the FPFTY, I&E's use of the average rate base did not result in a further adjustment.[99] In consideration of the above and the record evidence presented by I&E and the Company, I&E recommends $1,464,692 for the Companies Materials and Supplies.[100]

D. Deductions from Rate Base

1. Accumulated Deferred Income Taxes ("ADIT")

I&E recommended that the Company's claim for ADIT be reduced by $287,500, from $16,572,000 to $16,284,500.[101] I&E determined its recommended adjustment to the Company's claim for ADIT by using the average rate base methodology.[102]

The Company's claim for ADIT in the FTY is $15,997,000[103] and the claim for ADIT in the FPFTY is $16,572,000. [104]

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97 I&E St. No. 3-SR, p. 16.
98 *Id.*
99 *Id.*
100 *Id.*
101 I&E St. No. 3, p. 22. I&E St. No. 3-SR, p. 17.
102 *Id.*
103 I&E St. No. 3-SR, p. 17, *citing* UGI Elec. REV. Exh. A – Future, Sch. C-1.
104 *Id.*, *citing* UGI Elec. REV. Exh. A – Fully Projected, Sch. C-1.

As noted above, I&E determined its recommended adjustment to the Company's claim for ADIT by averaging the Company's FTY and FPFTY claims.[105] In consideration of the above and the record evidence presented by I&E, I&E recommends $16,284,500 for the Company's ADIT claim.[106]

2. Excess Accumulated Deferred Income Taxes

I&E recommends that the Company be required to reduce rate base in the revenue requirement formula for the excess ADIT balance which resulted as a reclassification of the portion of ADIT associated with the reduction in the federal income tax rate from 35% to 21% due to the enactment of the TCJA.[107] I&E recommends reducing the Company's rate base by the excess ADIT balance at the end of the FPFTY in the amount of $11,483,354.[108] The full argument regarding the excess ADIT is set forth in the Section VII. Taxes, B. Excess Accumulated Deferred Income Taxes *infra.*[109] This same argument applies to I&E's recommendation set forth here.

The Company has identified two FTY components of its excess ADIT: (1) the protected excess ADIT liability of $11,809,611; and (2) the non-protected excess ADIT asset of $2,024,704.[110] These balances are as of January 1, 2018. As of the end of the FPFTY the Company states that the balances will be as follows: (1) the protected excess

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105 I&E St. No. 3-SR, p. 17.
106 *Id.*, *citing* I&E Exh. No. 3, Sch. 1, ln 10.
107 I&E St. No. 1, p. 38; I&E St. No. 1-SR, p. 37.
108 I&E St. No. 1, p. 39, *citing* I&E Exh. No. 1, Sch. 11, p. 5.
109 IE M.B., pp. 61-65 *infra.*
110 I&E Exh. No. 1, Sch. 11, p. 4.

ADIT liability is $11,483,354;[111] and (2) the non-protected excess ADIT asset balance is zero.[112]

The Company reclassified the protected excess ADIT to a regulatory liability, but it did not make a corresponding reduction to its rate base. The Company acknowledged that Commission precedent requires that amounts recorded as ADIT be deducted from rate base.[113] However, the Company argues that the excess deferred taxes are not ADIT; rather they are "excess" deferred taxes[114] and the Company is not aware of any precedent under which excess deferred taxes are treated as a rate base deduction.[115] Further, the Company argues that regulatory assets are not allowed to be added to rate base, thus, the Company believes that the same treatment should apply to regulatory liabilities.[116] In short, the Company believes it should be able to earn a return on the excess ADIT balance.[117]

I&E disagrees. The excess ADIT monies were originally built into the rate formula to cover future income tax payments to the government.[118] The fact that this money (i.e., the excess ADIT) is no longer due in future income tax payments but is now due to ratepayers via a refund over the remaining useful life of affected plant, does not change the fact that the Company has received this money from ratepayers in prior years,

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111 I&E Exh. No. 1, Sch. 11, p. 5.
112 I&E Exh. No. 1, Sch. 11, p. 7.
113 I&E St. No. 1, p 37, *citing* I&E Exh. No. 1, Sch. 11, p. 8.
114 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 4. *See also* I&E Exh. No. 1, Sch. 11, p. 8.
115 I&E St. No. 1, p 37, *citing* I&E Exh. No. 1, Sch. 11, p. 8.
116 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 4.
117 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 5.
118 I&E St. No. 1, p. 38.

which has been available for infrastructure improvements.[119] Each regulatory asset or liability needs to be reviewed based on its own merits to determine whether it should be an addition/reduction to rate base.[120] In this instance, the original intent should be considered, and that is that the funds were an interest-free loan from the government (taxes due at some point in the future), and now due to the reclassification, the money is basically an interest-free loan from ratepayers.[121] I&E asserts that ratepayers should not be required to pay the Company a return on this balance during the time it takes to refund the money to them.

Regardless of whether the account for this balance is entitled ADIT or excess ADIT, the fact remains that the Company over-collected in rates an amount of ADIT based on the pre-January 1, 2018 federal income tax rate of 35%.[122] When classified as ADIT, this was previously the equivalent of an interest-free loan from the government to UGI Electric and should now be considered an interest-free loan from ratepayers until fully refunded over future years using the Average Rate Assumption Method (ARAM).[123] I&E views the Company's argument regarding a lack of precedent as unsupported and incorrect given the infrequency of major tax reform.[124] I&E also disagree with the fact that all regulatory assets and liabilities should be treated in the same manner for rate base purposes.[125] In this instance, the excess ADIT represents monies over-collected for

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119 *Id.*
120 I&E St. No. 1, p. 38. I&E St. No. 1-SR, p. 37.
121 *Id.*
122 I&E St. No. 1-SR, p. 38.
123 I&E St. No. 1, pp. 38-39.
124 I&E St. No. 1, p. 39.
125 I&E St. No. 1, pp. 36-39; I&E St. No. 1-SR, pp. 37-39.

payment of future taxes. In I&E's opinion, it is 100% accurate not to allow the Company to earn its cost of capital on the excess ADIT balance since the monies were over-collected from ratepayers with the intent of paying future tax liabilities, which no long exist due to the lower tax rate.[126] The excess ADIT amount needs to be returned to ratepayers over a period of time equal to the remaining life of the affected assets per IRS regulation.[127] Each year, the balance in the excess ADIT account will be ratably reduced until the entire amount is refunded to ratepayers.[128]

In consideration of all of the above and the record evidence presented by I&E, I&E recommends the Company be required to reduce rate base in the revenue requirement formula for the excess ADIT balance which resulted as a reclassification of the portion of ADIT associated with the reduction in the federal income tax rate from 35% to 21% due to the enactment of the TCJA. I&E recommends reducing the Company's rate base by the excess ADIT balance at the end of the FPFTY in the amount of $11,483,354.

3. Act 40 of 2017

I&E takes no position regarding the reduction of rate base for Act 40 of 2007.

4. Customer Deposits

I&E recommended the Company's Customer Deposit claim be increased by $76,692 from $1,419,000 to $1,495,692 in both the FTY and the FPFTY.[129] I&E

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126 I&E St. No. 1-SR, p. 39.
127 I&E St. No. 1, p. 36.
128 I&E St. No. 1, p. 36.
129 I&E St. No. 3, p. 24. I&E Exh. No. 3, Sch. 1. I&E St. No. 3-SR, p. 18.

determined its recommended level of customer deposits by calculating an average of the most recent 13 months of actual customer deposits balances.[130]

The Company's claim for customer deposits in the FTY and the FPFTY is $1,419,000.[131] The Company claimed that because of the Company no longer being able to collect customer deposits from low income customers, the Company's customer deposits has fallen and subsequently leveled off. [132] The Company therefore used the customer deposits balance at the end of the HTY to determine the rate base offset.[133]

I&E rejects the Company's argument.[134] I&E asserts that based on the actual customer deposit levels from October 2016 through February 2018, the Company's assertion that the customer deposit balance is decreasing or has leveled off is unsupported.[135] In fact, the $1,419,000 balance at September 2017 is actually the lowest balance in the referenced seventeen- month period.[136] In consideration of the above and the record evidence presented by I&E, I&E recommends a customer deposits level of $1,495,692 for both the FTY and the FPFTY.[137]

E. Cloud Based Program

Pursuant to the Partial Stipulation agreed to by the parties, the parties have agreed the Company shall be permitted to record the Cloud Based Implementation Costs as set forth in paragraph 12(a) of the Partial Stipulation Resolving Certain Contested Issues.

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130 *Id.*
131 I&E St. No. 3, p. 23. I&E St. No. 3-SR, p. 18.
132 I&E St. No. 3, p. 23, *citing* UGI Elec. St. No. 4.
133 I&E St. No. 3, p. 23.
134 I&E St. No. 3-SR, pp. 18-19.
135 I&E St. No. 3-SR, p. 18.
136 I&E St. No. 3-SR, p. 18, *citing* I&E Exh. No. 3, Sch. 8.
137 I&E St. No. 3-SR, p. 19.

F. Unite Phase 2 Costs

Pursuant to the Partial Stipulation agreed to by the parties, the parties have agreed the Company shall be permitted to capitalize the UNITE Phase 2 pre-implementation costs as set forth in paragraph 12(b) of the Partial Stipulation Resolving Certain Contested Issues.

G. Conclusions as to Rate Base

I&E notes that its use of the average rate base methodology and the resulting recommended adjustments; coupled with I&E witness Wilson's rate base adjustments; serve to reduce the Company's claimed rate base for the FPFTY by $(25,436,011) as shown on I&E Exhibit No. 3-SR, Schedule 1, line 15.[138] I&E's recommended FPFTY rate base is $93,835,143.[139]

Further, I&E recommended, and the Company agreed, that the Company provide the Commission's Bureau of Technical Utility Services and I&E with rate base updates which should include actual capital expenditures, plant additions, and retirements by months from October 1, 2017 through September 30, 2018 and an additional update for actuals from October 1, 2018 through September 30, 2019; to be provided no later than January 2, 2020.[140]

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138 *Id.*

139 *Id.*

140 I&E St. No. 3, p. 27. I&E St. No. 3-SR, p. 20.

V. REVENUES

A. Present Rate Revenues

I&E recommends that the Company's total operating revenue under pro forma present rate revenue be decreased by $60,412, from $88,919,177 to $87,858,765.[141] I&E reasoned that when calculating a revenue requirement in a designated test year, it is vital that the expenses and revenues are assessed using the same time period.[142] In this case, I&E is recommending the application of an average rate base methodology to calculate the Company's rate base and depreciation expense claims, therefore, for purposes of consistency, it is also necessary to calculate the Company's present rate revenue level in the FPFTY using a consistent average rate base methodology.[143]

The Company's revised claimed Total Operating Revenues under pro forma present rates in the FPFTY are $88,933,177.[144] To determine its claimed present rate revenue in the FPFTY, the Company's process begins with a calculated sales and revenue budget for the FPFTY.[145] The Company then adjusts that budgeted number for customer changes, normalized usage per customer, and annualized revenue from several Riders and the State Tax Adjustment Surcharge.[146] The result of the Company's adjustment is a claimed decrease in sales of 1.73 million kWh.[147]

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141 I&E St. No. 3, p. 21. I&E St. No. 3-SR, p. 21.
142 I&E St. No. 3, p. 30.
143 *Id.*
144 I&E St. No. 3, p. 28, *citing* UGI Elec. REV. Exh. E, p. 1.
145 I&E St. No. 3, p. 29, *citing* UGI Elec. St. No. 8, p. 3.
146 *Id.*
147 I&E St. No. 3, p. 29. *See also* I&E Exh. No. 3, Sch. 10.

I&E argues that the adjustments to present rate revenue claimed by the Company, however, occur in the 11 months after rates go into effect from October 27, 2018 through September 30, 2019.[148] The result is, the rates customers will be paying on October 28, 2018 will be improperly calculated based on a projected revenue requirement for the year ending September 30, 2019.[149] The more reasonable approach is to average the effect of the changes that occur at varying rates and at varying times over the course of the full year to match the average rate base.[150]

In consideration of the above and the record evidence presented by I&E, I&E recommends a decrease of $60,000 to the present rate revenue level in the FPFTY down to $87,858,765. Further, I&E recommends this $60,412 reduction to the present rate revenue level be allocated 100% to the Rate R class.[151]

VI. EXPENSES

It is well settled that a utility is entitled to recover its reasonably incurred expenses.[152] Operating and maintenance expenses, if properly incurred, are allowed as part of the overall rate computation. As such, a public utility is entitled to recover all reasonable and normal operating and maintenance expenses incurred by providing regulated service.[153] To the extent that expenses are not incurred, imprudently incurred, or abnormally overstated during the test year, they should be disallowed and found not

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148 I&E St. No. 3, p. 30.
149 *Id.*
150 *Id.*
151 I&E St. No. 3, p. 31, *citing* I&E Exh. No. 3, Sch. 11.
152 *UGI Corp. v. Pa. P.U.C.*, 410 A.2d 923, 932 (Pa. Cmwlth. 1980).
153 *Western Pennsylvania Water Company v. Pa. P.U.C.*, 422 A.2d 906 (Pa. Cmwlth. 1980).

recoverable through rates. The public utility requesting a rate increase and seeking to recover expenses has the burden of showing that the rate requested, including all claimed expenses, is just and reasonable.[154]

A. Vegetation Management Expense

I&E recommended an allowance of $1,912,266 for vegetation management or a reduction of $206,235 ($2,118,501 - $1,912,266) for the FPFTY.[155]

The Company's expense claim for vegetation management is $2,118,501.[156] The Company based this expense claim on FPFTY budget amounts. Further, the Company is basing a significant FTY increase in claimed vegetation management expense on additional resources needed to address an emergent danger tree issue stemming from the Emerald Ash Borer's devastation of Pennsylvania's ash trees.[157]

I&E based its recommended allowance for vegetation management expense on an average increase between fiscal years ended September 30, 2015, 2016, and 2017 for the non-payroll/other component which is 5.2%.[158] The Company's proposed 14.8% increase for the FTY is unsupported. I&E's methodology minimizes the Company's 14.8% increase to its future test year claim but allows for a trended year-to-year increase in this expense.[159] While the company indicated that this 14.8% issue was due to a relatively new issue with Pennsylvania ash trees, I&E expressed concerns that UGI

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154 66 Pa.C.S. § 315(a); *See also Cup v. Pa. P.U.C.*, 556 A.2d 470 (Pa. Cmwlth. 1989).
155 I&E St. No. 1, p. 13; I&E St. No. 1-SR, p. 12.
156 I&E St. No. 1, p. 12, *citing* I&E Exh. No. 1, Sch. 3, pp. 1-2.
157 I&E St. No. 1, p. 12, *citing* I&E Exh. No. 1, Sch. 3, p. 5.
158 I&E St. No. 1, p. 13. I&E St. No. 1-SR, p. 10.
159 I&E St. No. 1, p. 14. I&E St. No. 1-SR, p. 10.

Electric has not adequately supported this claimed increase. I&E would expect that year-to-year changes in issues, such as types of trees to address, would be captured in an overall historic average of the expense, thus supporting the I&E recommended yearly inflation of the HTY actual expenses.[160]

In consideration of the above and the record evidence presented by I&E, I&E recommends an allowance of $1,912,266 for vegetation management or a reduction of $206,235 ($2,118,501 - $1,912,266) for the FPFTY.

B. Company Owned Services ("COS") Program Expenses

I&E recommended an allowance of $140,000 or a reduction of $314,418 ($454,418 - $140,000) to the Company's claim for the Company-owned service transition program.[161] It is important to note that even though I&E argues strongly against the Company-owned services program expense, I&E is not advocating to eliminate it completely. I&E is recommending that the inspections be made voluntary while trying to balance the claimed expense against the inherent unknowns.[162]

To summarize, the Company currently owns and maintains nearly 5,000 Company-owned service facilities (mainly residential) including service entrance cables, meter sockets, panel boxes, main breakers and 240-volt breakers, of which some equipment is located inside customers' homes.[163] The Company has submitted an

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160 I&E St. No. 1-SR, p. 11.
161 I&E St. No. 1, p. 30.
162 I&E St. No. 1, pp. 29-31. I&E ST. No. 1-SR, p. 24.
163 I&E St. No. 1, p. 29, *citing* UGI Elec. St. No. 3, pp. 14-15.

expense claim of $454,418[164] to fund it's proposed a 10-year plan to transition ownership of these facilities to homeowners.

The Company argues that the services were installed in the 1970's when electrical code requirements were less stringent, and it estimates that a minimum of 90% of existing equipment will require work to bring service up to code and to pass inspection.[165] The Company also argues it's the Company's intention to inspect approximately 500 services a year over the next ten years for a total estimated cost of $4.544 million.[166] Further, the Company references OCA witness Mierzwa's non-opposition to this program as long as the Company does not profit from it and no one is canceled.[167]

I&E argued that the Company admits it is not guaranteed that it will be afforded access to all of the affected homes for maintenance, so there is no reason to believe that all homeowners will all allow access for the proposed final inspections.[168] Secondly, the Company has indicated that it is not required by law to perform these inspections prior to relinquishing ownership of the equipment;[169] therefore, it is more appropriate to make the inspections voluntary, giving homeowners the ability to decide by a certain date whether they wish to have such inspections performed prior to the change in ownership of the equipment. Finally, the true amount of the total cost for either mandatory or voluntary

164 I&E St. No. 1, p. 29, *citing* UGI Elec. Rev. Exh. A – Fully Projected.
165 I&E St. No. 1, p. 29, *citing* I&E Exh. No. 1, Sch. 10, p. 5.
166 I&E St. No. 1-SR, p. 25, *citing* UGI Elec. St. No. 3-R, p. 9.
167 *Id.*
168 I&E St. No. 1, p. 30, *citing* UGI Elec. St. No. 3, p. 15.
169 *Id.*, *citing* I&E Exh. No. 1, Sch. 10, p. 2.

inspections is not accurately known and measurable at this time, particularly not 9.44 years into the future considering that costs will change over time and that it is unknown how many affected homeowners will grant access to the inspectors.[170]

I&E also argues that the Company has the potential to profit from the COS program. In theory, if the Company inflated its 2019 budget amount of $140,000 by $314,418 due to its revised estimate of $454,418 where it reflected increased costs and a period of 9.44 years to complete the project.[171] And if the inflated claimed expenses are built into the revenue requirement equation, even if no portion is capitalized, the Company would over-recover and profit based on the erroneous expense projection.[172]

Finally, the Company's present safety concerns regarding these service facilities appears a bit self-serving.[173] During the 50 years of ownership, the Company was receiving both a return of and a return on the service facilities through rate base inclusion.[174] And, the Company was also logically including a claim in expenses for the repairs and maintenance associated with these Company owned assets.[175] All of which would have been as a result of the Company's obligation to provide safe and reliable service to its ratepayers.

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170 I&E St. No. 1, pp. 30-31.
171 I&E St. No. 1, pp. 29-30, *citing* I&E Exh. No. 1, Sch. 10, p. 4.
172 I&E St. No. 1-SR, pp. 25-26.
173 I&E St. No. 1-SR, pp. 26-29.
174 *Id.*
175 *Id.*

In consideration of the above and the record evidence presented by I&E, I&E recommends an allowance of $140,000 or a reduction of $314,418 ($454,418 - $140,000) to the Company's claim for the Company-owned service transition program.

C. Environmental Remediation Expense

While I&E originally recommended disallowance of the entire $139,000 environmental remediation expense claim, I&E ultimately expressed its agreement with the position propounded by OCA witness Lafayette Morgan. [176] I&E agrees with the OCA recommendation that these costs should be removed from the cost of service, because they should be recovered from the sales proceeds of the associated property.[177]

Explaining further, I&E agrees with the position of OCA witness Lafayette Morgan, that the gain on the sale of the property could be reduced by the cost of remediation and that the revenue requirement should be reduced by the $139,000 claim.[178] However, if the Commission decides to allow this cost to be recovered in the Company's revenue requirement, I&E recommends that it be amortized over a period of five years, which is more in line with the UGI Electric's rate case filing frequency.[179] A five-year amortization would produce a yearly allowance of $83,400, or a reduction of $55,600 ($139,000 - $83,400) to the Company's claim.[180]

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176 I&E St. No. 1-SR, pp. 6-7.
177 I&E St. No. 1-SR, p. 7, *citing* OCA St. No. 1, p. 17.
178 *Id.*
179 I&E St. No. 1-SR, p. 7
180 *Id.*

D. Storm Damage Expense

I&E recommended an allowance of $253,229 for the Company's storm damage expense claim, or a reduction of $47,771 ($301,000 - $253,229).[181] I&E had originally accepted the Company's use of a five-year *historic* average for this expense and the resulting $355,000 claim.[182] The Company however changed its claim in its rebuttal testimony.[183]

In rebuttal, the Company revised its storm damage expense claim to $301,000 (from the Company's original claim of $275,000) based on dropping the oldest year (2013) from its average and replacing it with 2018 in the five-year average.[184]

I&E rejects the Company's replacement of 2013 with 2018 in the five-year historic average.[185] The Company has not provided relevant substantial record evidence to support this claim.[186] Further, the 2018 expense claim is based on estimates as the 2018 FTY ends September 30, 2018.[187] Rather, it is more relevant to include the actual historic expenses from 2013 in the five-year historic average.[188]

In consideration of the above and the record evidence presented by I&E, I&E recommends an allowance of $253,229 for the Company's storm damage expense claim, or a reduction of $47,771 ($301,000 - $253,229).

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181 I&E St. No. 1-SR, p. 43.

182 I&E St. No. 1, p. 41.

183 I&E St. No. 1-SR, p. 43, *citing* UGI Elec. St. No. 8-R, pp. 22-23.

184 I&E St. No. 1-SR, p. 43, *citing* UGI Elec. St. No. 8-R, pp. 22-23.

185 I&E St. No. 1-SR, p. 43-44. I&E did, however, accept the Company's correction of a 2017 error.

186 I&E St. No. 1-SR, p. 43.

187 *Id.*

188 I&E St. No. 1-SR, p. 44

E. Rate Case Expense

I&E recommended that the Company's rate case expense be normalized over a period of 60 months (five years) resulting in an annual expense of $135,000 [($676,000 ÷ 60 months) x 12 months], or a reduction of $90,000 ($225,000 - $135,000) to the Company's claim.[189]

The Company's claim for rate case expense is $225,000.[190] The Company's last base rate case filing was in 1996 (22 years or 264 months).[191] To support its claim, the Company has estimated its total rate case expense amount to be $676,000 and is requesting a normalization period of three years (36 months) which produces a normalized claim of $225,000 [($676,000 ÷ 36 months) x 12 months].[192]

As a rule, the nature and types of individual expenditures that comprise a utility's allowable claim for rate case expense are those directly incurred to compile, present, and defend a utility's request for a base rate increase before the Commission.[193] The actual expenditures and estimated costs typically found in an allowable rate case expense claim include legal fees for outside counsel, fees to outside consultants, and the cost of printing, document assembly, and postage.[194]

The Commission has historically stated that it considers prudently incurred rate case expense as an ongoing expense, occurring at irregular intervals, related to the

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189 I&E St. No. 1, pp. 9-11. I&E St. No. 1-SR, pp. 7-10.
190 UGI Elec. Rev. Exh. A – Fully Projected, Sch. D-10.
191 I&E St. No. 1, pp. 9-11.
192 UGI Elec. Rev. Exh. A – Fully Projected, Sch. D-10.
193 I&E St. No. 1, p. 9.
194 *Id.*

rendering of utility service.[195] The Commission has also cited the importance of considering the involved utility's history regarding the frequency of rate case filings as an essential element to determine the normalized level of rate case expense for ratemaking purposes.[196] In fact, in a recent base rate case filed by *Emporium Water Company*, the Commission adopted the I&E-recommended historic filing frequency.[197]

I&E rejects the Company's claimed 36-month normalization period, because it is not supported by the Company's historic filing frequency.[198] The proposed normalization period fails to properly rely upon the historic data and is speculative in nature.[199] I&E's recommendation is based on an average historic base rate filing frequency of every 103 months when considering all cases filed by the Company since 1992.[200] While the Company's history shows a filing frequency in excess of every five years, I&E recommended a 60-month normalization period that moderates the impact of that longer historic filing frequency.[201]

In consideration of the above and the record evidence presented by I&E, I&E recommends that the Company's rate case expense be normalized over a period of 60 months (five years) resulting in an annual expense of $135,000 [($676,000 ÷ 60 months) x 12 months], or a reduction of $90,000 ($225,000 - $135,000) to the Company's claim.

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195 *Id.*

196 *Id.*

197 *Pa. P.U.C. v. Emporium Water Company*, Docket No. R-2014-2402324, OPINION AND ORDER, p. 50, Order Entered January 18, 2015.

198 I&E St. No. 1, p. 11. I&E St. No. 1-SR, pp. 8-9.

199 *Id.*

200 I&E St. No. 1, p. 11, *citing* I&E Exh. No. 1, Sch. 2.

201 I&E St. No. 1, p. 11. I&E St. No. 1-SR, pp. 7-8.

F. Employees Expenses

1. Salaries and Wages Net of Employee Additions

I&E recommended an allowance for salaries and wages – net of employee additions of $4,959,000 or a reduction of $34,000 ($4,993,000 - $4,959,000) based on the recommended disallowance of FPFTY pay annualizations, to provide a more accurate representation of expenses actually incurred in that twelve-month period.[202]

The Company's claim for salaries and wages expense net of employee additions is $4,993,000 ($4,959,000 budgeted salaries + $34,000 annualization adjustment).[203] The Company has based its claim on budgeted salaries and wages for the FPFTY with an adjustment for annualization of anticipated wage increases.[204] Further, the Company argues that I&E's recommendation is at odds with the use of the FPFTY, that it will not allow recovery for salaries and wages expenses representative of end of FPFTY amounts, and that the Company has consistently used end-of-FPFTY amounts.[205]

I&E rejects the Company's argument and asserts that I&E's recommendation for salaries and wages expense net of employee additions based on disallowance of the annualization of FPFTY pay increases is appropriate.[206] I&E's recommendation more accurately represents salaries and wages that the Company will pay across the twelve months that make up the FPFTY.[207] Annualization of the end-of-year salaries and wages,

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202 I&E St. No. 1, p. 16. I&E St. No. 1-SR, p. 12.
203 I&E St. No. 1, p. 15, *citing* UGI Elec. Rev. Exh. A – Fully Projected, Sch. D-7, p. 1.
204 I&E St. No. 1, p. 16.
205 I&E St. No. 1-SR, p. 13.
206 I&E St. No. 1, p. 16.
207 *Id.*

that include all increases, should not be allowed.[208] The annualization of end-of-year salaries and wages would allow the Company to recover in rates more than it requires for the test year utilized. Allowing only the amount to be incurred in the twelve months making up the FPFTY is more in line with the average rate base methodology employed by I&E witness Ethan Cline in I&E Statement No. 3.[209]

Further, I&E asserts the Company added $494,000 to its budgeted salaries and wages expense for three additional positions not reflected in the FPFTY budget.[210] This amount is addressed below in the Employee Additions section. It should be noted that the $494,000 amount on UGI Electric Revised Exhibit A – Fully Projected, Sch. D-7 is an error because the Company included the entire amount and not that amount attributable to distribution ($382,000).[211]

In consideration of the above and the record evidence presented by I&E, I&E recommends an allowance for salaries and wages – net of employee additions of $4,959,000 or a reduction of $34,000 ($4,993,000 - $4,959,000).

2. Employee Additions

I&E recommended an expense allowance of $318,000 for employee additions or a reduction of $64,000 ($382,000 - $318,000) to the Company's claim.[212] I&E's recommendation for employee additions is based on the removal of the annualization of

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208 I&E St. No. 1-SR, p. 13. *See also* I&E M.B., pp. 15-24 *supra*, and I&E St. No. 3, pp. 3-13 rejecting the Company's year-end methodology.

209 I&E St. No. 1, p. 17.

210 I&E St. No. 1, p. 17, *citing* I&E Exh. No. 1, Sch. 4.

211 I&E St. No. 1, p. 17, *citing* UGI Elec. Rev. Exh. A – Fully Projected Sch. D-9.

212 I&E St. No. 1, p. 19.

compensation for the three positions in the FPFTY, reflecting the actual amount anticipated to be incurred during that period.[213] This recommendation mirrors I&E's recommendation for salaries and wages net of employee additions *supra*.

The Company submitted a claim for employee additions of $382,000.[214] The Company's claim includes salaries, wages, and benefits for three new positions: a general manager, a new business engineer, and a business support engineer.[215] The Company assumes the positions will be filled *by* December 1, 2018; but, its claim is based on a *full year's* worth of expense (salaries, wages, and incentive compensation) for the positions.[216] The Company again argues that the I&E recommendation is at odds with the FPFTY and that end-of-year conditions are appropriate for use in a FPFTY expense claim.[217]

I&E again rejects the Company's argument and asserts that the FPFTY expense allowance be based on the actual amounts incurred across the FPFTY period and not an annualization of the end-of-year inflated projections.[218] I&E also requests that this methodology be reflected in the anticipated Commission FPFTY regulations.[219]

In consideration of the above and the record evidence presented by I&E, I&E recommends an expense allowance of $318,000 for employee additions or a reduction of $64,000 ($382,000 - $318,000) to the Company's claim.

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213 *Id.*
214 I&E St. No. 1, p. 18, *citing* UGI Elec. Rev. Exh. A – Fully Projected, Sch. D-3 and Sch. D-9.
215 I&E St. No. 1, p. 18, *citing* UGI Elec. St. No. 3, pp. 13-14.
216 *Id.*
217 I&E St. No. 1-SR, p. 14, *citing* UGI Elec. St. No. 2-R, p. 8.
218 I&E St. No. 1-SR, p 15.
219 *Id. See also* I&E M.B., pp. 15-24 *supra*, and I&E St. No. 3, pp. 3-13 rejecting the Company's year-end methodology.

3. Outside Services Employed

I&E recommended an allowance of $21,000 or a reduction of $170,000 ($191,000 - $21,000) based on a three-year historic average of this expense due to the 2015, 2016, and 2017 expense amounts being substantially less than FTY amount of $171,000 and the FPFTY claim of $191,000, which are not supported by substantial record evidence.[220]

The Company submitted a claim for Outside Services Employed - Miscellaneous of $191,000.[221] This claim includes recruiting and staffing services, certain legal expenses not included elsewhere, various printing and photography services, unclassified IT analytical consulting, and other miscellaneous outside professional services.[222]

I&E rejects the Company's claim, because the Company did not provide a breakdown of this expense, and has therefore, not provided substantial evidence to support this expense.[223] The Company attempted to provide an explanation however the Company's explanation fails to provide adequate support to the Company's original claim.[224] In consideration of the above and the record evidence presented by I&E, I&E recommends an allowance of $21,000 based on the historic average.

4. Employee Activity Costs

I&E recommended disallowance of the company's total claim of $11,848 for employee activity costs.[225] These Company-sponsored employee events are not

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220 I&E St. No. 1, pp. 23-24. I&E St. No. 1-SR, pp. 15-16.
221 I&E St. No. 1, p. 22, *citing* UGI Elec. Book I, Attch. II-D-7(b).
222 I&E St. No. 1, p. 22, *citing* I&E Exh. No. 1, Sch. 5, p. 1.
223 I&E St. No. 1, p. 22.
224 I&E St. No. 1-SR, pp. 16-17.
225 I&E St. No. 1, p. 25.

necessary for the provision of safe and reliable service to UGI electric ratepayers and should be denied.[226]

The Company's claim for employee activity costs in its filing is $11,848. The Company argues that the claimed employee activities are related to business operations in that they provide recognition for hard work and dedication, and they boost morale and engagement of staff.[227]

I&E rejects the Company's argument.[228] I&E reiterates that these expenses are not necessary for the provision of safe and reliable service to ratepayers and that hosting a picnic or a party to boost morale or employee engagement is not justified as a business meeting qualified for recovery from the ratepayers.[229]

In consideration of the above and the record evidence presented by I&E, I&E recommends disallowance of the company's total claim of $11,848 for employee activity costs.

5. Allocated Stock Options and Restricted Stock Awards

I&E recommended the disallowance of the Company's total claim for Allocated Stock Options and also recommended the disallowance the Company's total claim for Restricted Stock Awards.[230] Ratepayers should not be responsible for paying a benefit

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226 *Id.*
227 I&E St. No. 1-SR, p. 18.
228 I&E St. No. 1-SR, pp. 18-19.
229 I&E St. No. 1-SR, p. 19.
230 I&E St. No. 1, pp. 27-28.

available only to high-level executive type positions that are likely based on stock prices and/or earnings targets rather than goals that benefit ratepayers.[231]

The Company's total claim for Allocated Stock Options and the Company's total claim for Restricted Stock Awards are set forth in I&E witness Wilson's proprietary direct testimony.[232] These stock options and stock awards are allocated for high-level UGI employees such as the President and CEO, numerous Vice Presidents, and the Controller.[233] The Company argues that the executive bonus plan and the restricted stock grants are based on the overall financial performance of UGI Utilities. UGI states that good financial performance provides an internal source of capital and can defer the need to file base rate cases and possibly reduce requested dollar increases in rates.[234] Further, UGI characterizes these benefits as a part of the total compensation package and states that the Company would have to raise base salaries if they were not offered.[235] The Company also argues that stock options and awards encourage employees by motivating them to perform at a higher level.[236] Finally UGI argues that it is common in the industry to offer incentive compensation for management and non-management employees.[237]

I&E rejects the Company's arguments.[238] I&E disagrees with the Company's argument that offering stock options and awards will directly correlate to a reduced base

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231 I&E St. No. 1, p. 28.
232 I&E St. No. 1 PROPRIETARY, pp. 27-28.
233 I&E St. No. 1, p. 27.
234 I&E St. No. 1-SR, p. 20.
235 *Id.*, p. 21,
236 *Id.*
237 *Id.*
238 I&E St. No. 1-SR, pp. 22-23.

rate case filing intervals and lower requested revenue increases.[239] I&E also disagrees that the Company would have to raise salaries if it did not continue to offer stock options and awards.[240] To the contrary, it is the Company's discretion as to whether or not to offer these benefits, and the ratepayers should not be required to fund them.[241] Also, the Company's reference to a report regarding plans that exclude executives is not relevant to the executive options and awards offered here.[242] UGI witness Mattern stated during cross examination that for the cash bonus component, there are non-financial metrics built in; but the stock components are primarily based on financial metrics to determine actual payout.[243] Finally, the Company also offers its executives and executive bonus plan of which I&E did not recommend a disallowance.

In consideration of the above and the record evidence presented by I&E, I&E recommends the disallowance of the upper echelon earnings-based benefits for ratemaking purposes identified by the Company as Allocated Stock Options and Restricted Stock Awards.

G. Depreciation Expense

I&E recommended an annual depreciation expense of $5,290,062 based on the average rate base methodology.[244] I&E's adjusted annual depreciation expense recommendation was determined by taking the average annual depreciation expense plus

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239 *Id.*
240 *Id.*
241 *Id.*
242 I&E St. No. 1-SR, p. 23.
243 *See* Tr. pp. 109-110.
244 I&E St. No. 3, p. 13, *citing* I&E Exh. No. 3-SR, Sch. 2.

the average amortization of net salvage less the average amount charged to clearing accounts.[245]

The Company's REVISED claimed annual depreciation expense for the FTY is approximately $4,265,854 and for the rebuttal FPFTY is approximately $5,333,752.[246] The Company determined its annual depreciation expense claim for the FPFTY by taking the calculated annual depreciation expense plus the amortization of net salvage and subtracted an amount charged to clearing accounts.[247] The Company disagrees with I&E's use of the average rate base methodology as used in I&E's calculation of the Company's annual depreciation expense.[248]

I&E rejects the Company's argument and continues to recommend use of the average rate base methodology for plant-in-service and as it relates to the Company's annual depreciation expense.[249] Based on the Company's adjustments to plant-in-service, I&E altered its annual depreciation expense recommendation in surrebuttal.[250]

In consideration of the above and the record evidence presented by I&E, I&E recommends the revised annual depreciation expense level calculated based on the average rate base methodology of $5,290,062.[251]

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245 I&E St. No. 3-SR, pp. 13-14, *citing* I&E Exh. No. 3, Sch. 2, col. F.
246 I&E St. No. 3-SR, p. 13.
247 I&E St. No. 3, p. 14, *citing* UGI Elec. REV. Exh. A, Sch. D-21.
248 I&E St. No. 3-SR, p. 12, *citing* UGI Elec. St. No. 4-R, p. 14.
249 I&E St. No. 3-SR, p. 13.
250 I&E St. No. 3-SR, pp. 13-14.
251 I&E St. No. 3-SR, p. 14, *citing* I&E Exh. No. 3, Sch. 2.

H. Other Post-Employment Benefits ("OPEB")

UGI Electric witness Mattern made an adjustment to the Company's direct case in her rebuttal testimony.[252] The Company revealed that it had been over collecting on an OPEB expense since the Company's last base rate proceeding dating back to 1996. The Company admitted that the OPEB fund has been generating more income than its expenses and UGI Electric has accumulated an over-collection in the amount of $7.9 million over the last 22 years.[253] The Company proposed to refund this over-collection to customers over 20 years. UGI Electric has offered to return $0.395 million annually to its ratepayers with no mention of any interest on the return.[254]

I&E did not present testimony regarding the return of the OPEB over collection to ratepayers. Therefore I&E has no objection to the Company's proposal. Neither would I&E object to returning the over-collection over a shorter period of time, maybe ten or even five years. Logically, it is easier to return over collected monies already in the possession of the Company over a shorter period of time than it took to collect the over-collection over a period of years from the rate payers. Additionally, I&E would not object to the addition of interest to the over-collection.

I. Power Supply Expense

I&E recommended the Company's claimed power supply expense adjustment be increased by approximately $19,500 from $1,933,000 to $1,952,500 as a result of I&E's

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252 UGI Electric, St. No. 4-R, pp. 16-18.

253 *Id.*, p. 17.

254 *Id. See also* UGI Electric Rev. Sch. D-14.

use of the average rate base methodology adjustment to present rates.[255] UGI Electric disagreed with the I&E recommendation on the basis that the Company rejects the use of an average FTY and FPFTY to calculated adjustments.[256] Obviously, I&E continues to recommend using the average rate base methodology, I&E will continue to recommend its adjustment to present rate revenue and power supply expense.[257]

J. Conclusion as to Expenses

I&E's total expense adjustments are $(1,283,000) as shown in the itemized Summary of the I&E adjustments to the Company's claimed expenses in Table II attached to this I&E Main Brief in Appendix A. I&E's use of the average rate base methodology reduces the annual depreciation expense claim for the FPFTY by $(579,062) as shown on I&E Exhibit No. 3-SR, Schedule 2.[258]

Subject to the concept of "iteration," where applicable, I&E's total operation and maintenance expense adjustments are ($1,283k).[259]

VII. TAXES

A. Tax Cuts and Jobs Act of 2017 ("TCJA")

On December 22, 2017, Public Law No. 115-97 was signed into law by the President Trump. The short title of this law is the Tax Cuts and Jobs Act ("TCJA"). Pursuant to the TCJA, effective January 1, 2018, various provisions of the Tax Reform Act of 1986 (the governing tax law in the United States prior to the effective date of the

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255 I&E St. No. 3-SR, p. 22. *See also* I&E St. No. 3, pp. 28-32.
256 I&E St. No. 3-SR, p. 22, *citing* UGI Elec. St. No. 8-R, p. 3.
257 I&E St. No. 3-SR, p. 23.
258 *Id.*, pp. 19-20.
259 *See* I&E M.B. Appendix A, Table II.

TCJA) have been repealed or amended. One of the many modifications to the Tax Reform Act of 1986 resulting from the passage of the TCJA is a reduction in the corporate Federal Income Tax rate. Specifically, the TCJA reduces the corporate Federal Income Tax rate from 35% to 21%.

By Secretarial Letter issued February 12, 2018, the Pennsylvania Public Utility Commission initiated a proceeding at Docket No. M-2018-2641242 to determine the effects of the TCJA on the tax liabilities of Commission-regulated public utilities for 2018 and future years and the feasibility of reflecting such impacts in the rates charged to Pennsylvania utility ratepayers. Ultimately, the Commission issued a Temporary Rates Order[260] on May 17, 2018. The Commission concluded generally that due to the substantial decrease in federal corporate income tax rates and its effect on utility revenue requirements, the existing rates of the identified public utilities are no longer just and reasonable and, indeed, excessive.[261] The Commission added, for utilities with a pending general rate case, the proceedings in regard to their temporary rates will be consolidated with their pending base rate case for hearing and decision.[262]

Further, the Commission stated in its disposition,

> upon review and consideration of the comments and financial data filed in this matter in response to the February 12, 2018 Secretarial Letter, as well as our financial analysis of the TCJA tax effects, the Commission is persuaded that the tax savings and associated reductions in utility revenue requirements should be flowed back to consumers on a current basis.[263] While ratemaking is generally *prospective* in nature, an exception to this

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260 Temporary Rates Order, Docket No. M-2018-2641242, Order Entered May 17, 2018.

261 Temporary Rates Order, p. 22.

262 *Id.*

263 Temporary Rates Order, p. 15.

rule applies in the case of expenses that are extraordinary, substantial and nonrecurring.[264]

The Commission added, "in this regard, we agree with the OCA that the TCJA tax savings represent an extraordinary and substantial, non-recurring reduction in utility expenses that [can and] should be treated outside of a general rate proceeding and flowed back to ratepayers."[265]

The Commission recognized the arguments made by OCA and OSBA and stated:

> The OCA and the OSBA both propose detailed methods for flowing these savings and reductions back to utility customers on an immediate basis by means of a negative surcharge to address the effect of the tax changes due to the TCJA. Citing to *Popowsky v. Pa. Public Utility Commission*, 13 A.2d 583 (Pa. Cmwlth. 2011), the OCA points out that a Section 1307(a) automatic adjustment clause is appropriate "for easily identifiable expenses that are beyond a utility's control, such as tax rate changes …" OCA Comments at 10. In the Commission's judgment, the TCJA tax rate changes are easily identifiable and beyond the utilities' control; and because they are substantial, the effect of these tax rate changes require action by the Commission to ensure that consumer rates remain just and reasonable.[266]

The Commission noted its agreement with these OCA and OSBA that a negative surcharge is both a lawful and appropriate means to recognize the TCJA tax rate changes and their effect on consumer rates.[267] The Commission stated further that it is not persuaded by the arguments of some commenters that utilities be given the option to use any tax savings from the TCJA for utility infrastructure projects or other utility-identified benefits.[268]

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264 Temporary Rates Order, p. 15, *citing Philadelphia Electric Co. v. Pa. Public Utility Commission*, 502 A.2d 722 (Pa. Cmwlth. 1985).

265 Temporary Rates Order, p. 15.

266 Temporary Rates Order, pp. 15-16.

267 Temporary Rates Order, p. 16.

268 *Id.*

And, with regard to the arguments made regarding a perceived risk of possible negative outlooks from credit rating firms and cash flow concerns, the Commission stated:

> Similarly, the Commission does not deem it appropriate to permit utilities to retain TCJA savings due to a perceived risk of possible negative outlooks from credit rating firms. Once again, if a utility's cash flow is of concern, a general rate increase is the appropriate vehicle to address such a concern. But, as pointed out by BI&E, an increased cash flow realized because a utility is permitted to retain revenues resulting from customers paying a "phantom 35%" income tax rate would not be lawful or appropriate. BI&E Comments at 4. Indeed, while utilities are entitled to recover in rates all reasonable and prudently incurred expenses, there is no warrant for the recovery of taxes or other expenses from consumers that are not incurred. *Barasch v. Pa. PUC*, 493 A.2d 653 (Pa. 1985). Accordingly, the Commission declines to allow rates for non-existent tax expenses for the purpose of artificially augmenting a utility's cash flow.[269]

Therefore, in consideration of I&E's investigation and the conclusions reached by the Commission in its investigation regarding the effects of the TCJA on Commission-regulated public utilities; I&E recommends that the Company be required to flow back to ratepayers, via a reconcilable 1307 surcharge mechanism (which could be entitled the Federal Tax Adjustment Credit, or FTAC), the net tax savings associated with the reduction in the federal income tax rate for the period January 1, 2018 through the date when new rates from this proceeding are expected to go into effect.[270] The I&E suggested language for the FTAC is set forth on Appendix B attached hereto. The net amount for this Future Test Year (FTY) over-recovery, as calculated by the Company based on its effective tax rates pre- and post-TCJA, is $212,677.[271] The recommended

269 Temporary Rates Order, pp. 16-17.

270 I&E St. No. 1, pp. 33-34.

271 I&E St. No. 1, p. 34, *citing* I&E Exh. No. 1, Sch. 11, p. 3.

FTAC is necessary to return to ratepayers an amount equal to the excess income tax recovery resulting during the FTY plus interest as noted below.

In its Order, the Commission states that excess income taxes collected from ratepayers for the period January 1, 2018 through June 30, 2018 should be recorded as a deferred regulatory liability that "…shall accrue interest at the residential mortgage lending rate specified by the Secretary of Banking in accordance with the Loan Interest and Protection Law (41. P.S. §§ 101, et seq.)."[272] Therefore, I&E recommends that this amount be refunded with interest at the residential mortgage lending rate specified by the Secretary of Banking in accordance with the Loan Interest and Protection Law.[273]

The Company does not propose to return any of the FTY over-recovery to ratepayers. Instead, the Company makes a veiled argument and portrays that UGI Electric's actual FTY rate of return (ROR) at present rates is 4.83%.[274]

I&E rejects the Company's argument that its actual FTY ROR at present rates is 4.83%. I&E witness Wilson cites to I&E witness Kubas' thorough testimony[275] detailing apparent manipulation by the Company to portray lower historic ROR figures in its Quarterly Earnings Reports.[276] Mr. Kubas' arguments are set forth herein at Section IX - Miscellaneous Issues, A – UGI's Quarterly Earnings Reports, *infra*.[277] Ms. Wilson also identifies necessary FTY adjustments to PURTA and vegetation management expenses,

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272 I&E St. No. 1-SR, p. 36, *citing* Temporary Rates Order, p. 18.

273 *Id.*

274 I&E St. No. 1, p. 32, *citing* UGI Elec. Rev. Exh. A – Future, Sch. A-1. *See also* UGI Elec. St. No. 1, p. 6.

275 *See* I&E St. No. 5; I&E Exh. No. 5; and, I&E St. No. 5-SR for I&E's full detailed explanation.

276 I&E St. No. 1, pp. 32-33.

277 I&E M.B., pp. 80-92.

which would bring the Company's FTY ROR to in excess of 5%, and she mentions the Company's lack of a rate base reduction for excess accumulated deferred income taxes[278] as other factors affecting the inaccurate portrayal of the Company's FTY ROR at 4.83%.

The Company also opines that $212,677 (a Company provided amount) is an incorrect amount but does not offer a corrected amount for the potential flowback of excess 2018 income taxes.[279] If a corrected amount is offered by the Company, it must be supported by substantial record evidence.

The Company also argues that flowing back the 2018 over-recovery of income tax to ratepayers via a surcharge would result in single-issue ratemaking. I&E rejects this argument[280] and the Commission rejected it as well. The Commission stated that in the its judgement, there is no legal impediment (of which, single-issue ratemaking would be one) to the Commission's consideration of the substantial tax savings from the TCJA.[281] The Commission concluded, "a negative surcharge is both a lawful and appropriate means to recognize the TCJA tax rate changes and their effect on consumer rates."[282]

The Company also argues that flowing back the 2018 over-recovery of income taxes to ratepayers via a surcharge mechanism would result in retroactive ratemaking.[283] I&E rejects this argument and the Commission rejected it as well. The Commission stated:

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278 I&E St. No. 1, pp. 32-33.
279 I&E St. No. 1-SR, p. 34.
280 I&E St. No. 1-SR, p. 35.
281 Temporary Rates Order, p. 15.
282 Temporary Rate Order, p. 16.
283 I&E St. No. 1-SR, p. 35.

> In this regard, we agree with the OCA that the TCJA tax savings represent "an extraordinary and substantial, non-recurring reduction in utility expenses that should be treated outside of a general rate proceeding and flowed back to ratepayers."[284]

I&E agree with the Commission in this instance that the over-recovery of 2018 income taxes is specifically isolated to the period from January 1, 2018 through the effective date of new rates in this proceeding and thus non-recurring and a one-time expense.[285] Further, I&E argues that it is an extraordinary expense in that Tax Reform occurs very infrequently and is beyond the control of the Company.[286]

Finally, I&E disagrees with the Company's assertion that flowing back the over-recovery of 2018 income taxes to ratepayers creates a mismatch in revenues and expenses because the Company has collected an amount for taxes in rates based on an incorrect tax rate.[287] To the contrary, making this correction would create more accurate matching of expenses true to the period in question.[288]

In consideration of all of the above and of the record evidence presented by I&E, I&E recommends that the Company be required to flow back to ratepayers, via a reconcilable 1307 surcharge mechanism (which could be entitled the Federal Tax Adjustment Credit, or FTAC, and using the language set forth on Appendix B attached hereto), the net tax savings associated with the reduction in the federal income tax rate for

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284 Temporary Rates Order, p.15.
285 I&E St. No. 1-SR, p. 35.
286 *Id.*
287 I&E St. No. 1-SR, pp. 35-36.
288 I&E St. No. 1-SR, p. 36.

the period January 1, 2018 through the date when new rates from this proceeding are expected to go into effect.

B. Excess Accumulated Deferred Income Taxes

I&E recommended that the excess accumulated deferred income tax currently held by the Company be returned to ratepayers over a period of time equal to the remaining life of the affected assets per IRS regulation.[289] Each year, the balance in the excess ADIT account will be ratably reduced until the entire amount is refunded to ratepayers. In conjunction, I&E also recommended that the Company be required to reduce rate base in the revenue requirement formula for the excess ADIT balance which resulted as a reclassification of the portion of ADIT associated with the reduction in the federal income tax rate from 35% to 21% due to the enactment of the TCJA.[290] I&E recommends reducing the Company's rate base by the excess ADIT balance at the end of the FPFTY in the amount of $11,483,354.[291] While the full argument regarding the excess ADIT is set forth here in the Tax section, this same argument applies to I&E's recommendation set forth in Section IV. D. Deductions from Rate Base, 2. Excess Accumulated Deferred Income Taxes *supra*.[292]

As a result of the 21% tax rate taking effect as of January 1, 2018, regulated utilities now hold an amount of ADIT that was calculated based on the prior federal income tax rate of 35%. Since the tax rate is now reduced to 21%, the attributable dollar

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289 I&E St. No. 1, p. 36.
290 I&E St. No. 1, p. 38; I&E St. No. 1-SR, p. 37.
291 I&E St. No. 1, p. 39, *citing* I&E Exh. No. 1, Sch. 11, p. 5.
292 IE M.B., pp. 30-33 *supra*.

amount needs to be reclassified to a deferred liability account.[293] This deferred liability account is necessary to track the remaining balance of excess taxes recorded in prior years due to the higher 35% federal income tax rate that was in effect before January 1, 2018.[294]

The Company has identified two FTY components of its excess ADIT: (1) the protected excess ADIT liability of $11,809,611; and (2) the non-protected excess ADIT asset of $2,024,704.[295] These balances are as of January 1, 2018. As of the end of the FPFTY the Company states that the balances will be as follows: (1) the protected excess ADIT liability is $11,483,354;[296] and (2) the non-protected excess ADIT asset balance is zero.[297]

The Company reclassified the protected excess ADIT to a regulatory liability, but it did not make the necessary corresponding reduction to its rate base. The Company acknowledged that Commission precedent requires that amounts recorded as ADIT be deducted from rate base.[298] However, the Company argues that the excess deferred taxes are not ADIT; rather they are "excess" deferred taxes[299] and the Company is not aware of any precedent under which excess deferred taxes are treated as a rate base deduction.[300] Further, the Company argues that regulatory assets are not allowed to be added to rate base, thus, the Company believes that the same treatment should apply to regulatory

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293 I&E St. No. 1, p. 36.
294 *Id.*
295 I&E Exh. No. 1, Sch. 11, p. 4.
296 I&E Exh. No. 1, Sch. 11, p. 5.
297 I&E Exh. No. 1, Sch. 11, p. 7.
298 I&E St. No. 1, p 37, *citing* I&E Exh. No. 1, Sch. 11, p. 8.
299 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 4. *See also* I&E Exh. No. 1, Sch. 11, p. 8.
300 I&E St. No. 1, p 37, *citing* I&E Exh. No. 1, Sch. 11, p. 8.

liabilities.[301] In short, the Company believes it should be able to earn a return on the excess ADIT balance.[302]

I&E disagrees. The excess ADIT monies were originally built into the rate formula to cover future income tax payments to the government.[303] The fact that this money (i.e., the excess ADIT) is no longer due in future income tax payments but is now due to ratepayers via a refund over the remaining useful life of affected plant, does not change the fact that the Company has received this money from ratepayers in prior years, which has been available for infrastructure improvements.[304] Each regulatory asset or liability needs to be reviewed based on its own merits to determine whether it should be an addition/reduction to rate base.[305] In this instance, the original intent should be considered, and that is that the funds were an interest-free loan from the government (taxes due at some point in the future), and now due to the reclassification, the money is basically an interest-free loan from ratepayers.[306] I&E asserts that ratepayers should not be required to pay the Company a return on this balance during the time it takes to refund the money to them.

Regardless of whether the account for this balance is entitled ADIT or excess ADIT, the fact remains that the Company over-collected in rates an amount of ADIT based on the pre-January 1, 2018 federal income tax rate of 35%.[307] When classified as

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301 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 4.
302 I&E St. No. 1-SR, p. 38, *citing* UGI Elec. St. No. 9-R, p. 5.
303 I&E St. No. 1, p. 38.
304 I&E St. No. 1, p. 38.
305 I&E St. No. 1, p. 38.
306 I&E St. No. 1, p. 38.
307 I&E St. No. 1-SR, p. 38.

ADIT, this was previously the equivalent of an interest-free loan from the government to UGI Electric and should now be considered an interest-free loan from ratepayers until fully refunded over future years using the Average Rate Assumption Method (ARAM).[308] I&E views the Company's argument regarding a lack of precedent as unsupported and incorrect given the infrequency of major tax reform.[309] I&E also disagree with the fact that all regulatory assets and liabilities should be treated in the same manner for rate base purposes.[310] In this instance, the excess ADIT represents monies over-collected for payment of future taxes. In I&E's opinion, it is 100% accurate not to allow the Company to earn its cost of capital on the excess ADIT balance since the monies were over-collected from ratepayers with the intent of paying future tax liabilities, which no long exist due to the lower tax rate.[311] The excess ADIT amount needs to be returned to ratepayers over a period of time equal to the remaining life of the affected assets per IRS regulation.[312] Each year, the balance in the excess ADIT account will be ratably reduced until the entire amount is refunded to ratepayers.[313]

In consideration of all of the above and the record evidence presented by I&E, I&E recommends that the excess accumulated deferred income tax currently held by the Company be returned to ratepayers over a period of time equal to the remaining life of

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308 I&E St. No. 1, pp. 38-39.
309 I&E St. No. 1, p. 39.
310 I&E St. No. 1, pp. 36-39; I&E St. No. 1-SR, pp. 37-39.
311 I&E St. No. 1-SR, p. 39.
312 I&E St. No. 1, p. 36.
313 I&E St. No. 1, p. 36.

the affected assets per IRS regulation.[314] Each year, the balance in the excess ADIT account will be ratably reduced until the entire amount is refunded to ratepayers.

VIII. RATE OF RETURN

A. Rate of Return Standards

I&E recommends the following rate of returns[315] for UGI Electric:

Type of Capital	Ratio	Cost Rate	Weighted Cost
Long-Term Debt	45.98%	4.69%	2.16%
Common Equity	54.02%	8.62%	4.66%
Total	100.00%		6.82%

In utility ratemaking, the concept of rate of return enjoys the dubious status of being at once both well-documented legally and highly disputed factually. Simply stated, rate of return is the revenue an investment generates in the form of net income; and is generally expressed as a percentage of the amount of capital invested over a given period of time. It is perhaps the most controversial component of the revenue requirement formula.[316]

A fair and reasonable overall rate of return allows the utility the opportunity to recover those costs prudently incurred by all classes of capital used to finance the rate base during the prospective period in which its rates will be in effect. *Bluefield Water*

[314] I&E St. No. 1, p. 36;

[315] I&E St. No. 2, p. 7; I&E Exh. No. 2, Sch. 1; I&E St. No. 2-SR, p. 28.

[316] For calculation of a utility's base rate revenue requirements, the formula used RR = E + D + T + (RB x ROR), where RR = Revenue Requirement; E = Operating Expense; D = Depreciation Expense; T = Taxes; RB = Rate Base; and ROR = Overall Rate of Return. I&E St. 1 at 4-5.

Works & Improvements Co. v. Public Service Comm. of West Virginia, 292 U.S. 679, 692-93 (1923) ("*Bluefield*"), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 603 (1944) ("*Hope Natural Gas*") are the seminal cases that present the legal standards applicable to regulators calculating utility rates of return.

In *Bluefield,* the Supreme Court stated:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be too high or too low by changes affecting opportunities for investment, the money market and business conditions generally.[317]

Twenty years later, in *Hope Natural Gas,* the Supreme Court reiterated:

> From the investor or company point of view it is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.[318]

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[317] *Bluefield*, 262 U.S. at 692-93.

[318] *Hope Natural Gas,* 320 U.S. at 603.

Restated, the principles generally accepted by state and federal regulators as the appropriate criteria for measuring a fair rate of return are these:

- A utility is entitled to the opportunity of a return similar to that being earned by other enterprises with corresponding risks and uncertainties, but not as high as those earned by highly profitable or speculative ventures;

- A utility is entitled to the opportunity of a return level reasonably sufficient to assure financial soundness;

- A utility is entitled to the opportunity of a return sufficient to maintain and support its credit and raise necessary capital;

- A fair return can change (increase or decrease) along with economic conditions and capital markets.[319]

B. Barometer Group

As is its common practice, I&E selected a proxy group of companies to act as a benchmark for determining UGI Electric's rate of return in this base rate proceeding.[320] The proxy group's cost of equity is used as a benchmark to satisfy the long-established guideline of utility regulation that seeks to provide the subject utility with the opportunity to earn a return similar to that of enterprises with corresponding risks and uncertainties.[321]

As more fully explained by I&E witness Anthony Spadaccio, a proxy group is typically utilized since the use of data exclusively from one company may be less reliable than using a proxy group.[322] The lower reliability occurs because the data for one

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319 I&E St. No. 2, p. 4.
320 I&E St. No. 2, pp. 7-11.
321 I&E St. No. 2, p. 7.
322 I&E St. No. 2, pp. 7-10; I&E St. No. 2-SR, pp. 2-5.

company may be subject to events that can cause short-term anomalies in the marketplace. The rate of return on common equity for a single company could become distorted in these circumstances and would therefore not be representative of similarly situated companies.[323] Therefore, a proxy group has the effect of smoothing out potential anomalies associated with a single company.[324]

UGI Electric witness Paul R. Moul criticized I&E's proxy group stating that using the percentage of revenue as a criterion for a proxy group is incorrect, and that the percentage of electric assets to total assets is a more appropriate criterion.[325]

I&E rejects the Company's argument.[326] Calculating the percentage of utility assets that make up the total assets of a company is not always a reliable way of determining if a business is primarily a regulated utility.[327] Further, the percentage of utility business is not always accurately represented by using the percentage of utility assets to total assets because there are differences between businesses in the amount of capital needed.[328] A utility with all new equipment may need a large level of assets to produce a small level of cash flow while another business may need only a small amount of assets to produce a large level of cash flow.[329] Therefore, comparing the assets of an electric utility segment to the total assets of a company is not an appropriate criterion as it

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323 I&E St. No. 2, p. 8.
324 *Id.*
325 UGI Elec. St. No. 5-R.
326 I&E St. No. 2-SR, pp. 2-5.
327 I&E St, No. 2-SR, p. 3.
328 *Id.*
329 *Id.*

could be misleading.[330] I&E witness Spadaccio concluded there is no reason to change the I&E proxy group.[331]

C. Capital Structure.

In the Partial Stipulation, the parties accepted the Capital Structure proposed by the Company. I&E recommended using the Company's claimed capital structure as presented; Long Term Debt = 45.98%; Common Equity = 54.02%.[332] I&E reasoned further, the Company's claimed capital structure falls within the range of I&E's proxy group's 2016 capital structures.[333] This range contains capital structure ratios from 44.75% to 74.46% debt and 25.54% to 55.25% equity, with a five-year average of 53.44% debt and 46.56% common equity.[334] Although the Company's capital structure is certainly more equity heavy than the proxy group average, I&E does not recommend that it be adjusted given that it falls within the proxy group range.[335]

D. Cost of Long Term Debt

I&E recommends using the Company's claimed long-term debt cost rate of 4.69% for the FPFTY.[336] The Company's claimed cost rate of long-term debt is reasonable, as it is representative of the industry.[337] It falls within I&E's proxy group's implied long-term

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330 *Id.*, pp. 3-4.
331 I&E St. No. 2-SR, p. 5.
332 I&E St. No. 2, pp. 11-12.
333 I&E St. No. 2, p. 12.
334 I&E Exhibit No. 2, Schedule 2.
335 I&E St. No. 2, pp. 12-13.
336 UGI Elec. St. No. 5, p. 16.
337 I&E St. No. 2, p. 13.

debt cost range of 3.91% to 6.30%, with an average implied long-term debt cost of 5.21%.[338]

E. Cost of Common Equity

I&E recommended using the Discounted Cash Flow (DCF) method as the primary method to determine the cost of common equity.[339] Further, I&E recommended using the results of the Capital Asset Pricing Model (CAPM) as a comparison to the DCF results.[340] As a result of I&E's DCF analysis I&E recommended a cost of common equity of 8.62%.[341] The comparable results of I&E's CAPM analysis are 8.00% (forecasted) and 8.98% (historic), placing the DCF result of 8.62% and I&E's recommendation comfortably within the CAPM range.[342]

Further, as recently as *Pa. P.U.C. v. City of DuBois-Bureau of Water (City of DuBois)* the Commission reaffirmed its support for I&E's methodology of basing its recommended cost of common equity on a DCF method analysis with a CAPM analysis solely as a check.[343] The Commission stated, "although there are various models used to estimate the cost of equity, the DCF method applied to a barometer group of similar utilities, has historically been the primary determinant utilized by the Commission."[344] The DCF model assumes that the market price of a stock is the present value of the future

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338 *Id. See* I&E Exh. No. 2, Sch. 3.
339 I&E St. No. 2, p. 16; I&E St. No. 2-SR, p. 6.
340 *Id.*
341 I&E St. No. 2, p. 20; I&E St. No. 2-SR, p. 6.
342 *Id.*
343 *See PA P.U.C. v City of DuBois-Bureau of Water* (*City of Dubois*), Docket No. R-2016-2554150, OPINION AND ORDER, Order Entered March 28, 2017. *See also* RECOMMENDED DECISION (RD), Entered January 9, 2017).
344 *City of DuBois* Order, p. 88.

benefits of holding that stock.[345] These benefits are the future cash flows of holding the stock, *i.e.*, the dividends paid and the proceeds from the ultimate sale of the stock.[346] Because dollars received in the future are worth less than dollars received today, the cash flow must be "discounted" back to the present value at the investor's rate of return.[347]

I&E utilizes the DCF method to determine recommended cost rate of common equity and verified the reasonableness of the cost of equity with the CAPM method and the reasonableness of the overall return by analyzing the Debt Service Coverage.[348] The fundamental concept behind the DCF is that the receipt of dividends in addition to expected appreciation is the total return requirement determined by the market.[349] I&E's DCF analysis utilizes a forecasted growth rate and expected dividend yield, which allows the time-value of money to be considered and causes the results to be forward-looking.[350] The use of a growth rate and dividend yield allows the DCF, unlike alternative methodologies, to measure the cost of equity directly which makes it the superior method for determining rate of return.[351] As noted in *City of Dubois*, this market-based DCF methodology has traditionally been endorsed by the Commission.[352]

The Company also raised other issues regarding the cost of common equity. The Company argues that I&E should apply a 102 basis point CAPM size adjustment and

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345 I&E St. No. 2, pp. 14-16.
346 *Id.*
347 *Id.*
348 I&E St. No. 2, pp. 17-18.
349 *Id.*, p. 18.
350 *Id.*, p. 16.
351 *Id.*, p. 18.
352 *City of DuBois*, RD, p. 67, [*citations omitted*].

cites the article written by Dr. Annie Wong and the Fama/French study.[353] The Company argues enormous changes occurred in the industry since Dr. Wong wrote her article.[354]

I&E rejects this argument. The Company states that enormous changes have occurred in the industry since the 1960s, however, it presents no evidence that these "changes" have caused a size adjustment to be needed.[355] And, Dr. Wong's study demonstrated that a size adjustment does *not* need to be made in the regulated utility industry.[356] Rather, Dr. Wong's article presents evidence that although a size effect may exist for industrial stocks, it does not exist for utility stocks.[357]

Finally, the Company argues that 20 basis points should be included in the cost of equity to recognize that Company's management performance.[358] This recommendation was made by the Company after already recommending a cost of equity of 11.25%.[359]

I&E rejects the Companies argument. If management points are awarded, at all, it should be done on a case-by-case basis. No prior awarding of management points to another company in a previous base rate proceeding is relevant to the next company's claim for management points.[360] Further, I&E does not believe that UGI Electric or any utility company for that matter, should reap additional rewards for programs funded by ratepayers for meeting the Company's obligations to provide safe and reliable service.[361]

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353 *See* I&E St. No. 2, pp. 45-46; I&E St. No. 2-SR, pp. 20-21.
354 *Id.*
355 *Id.*, p. 21.
356 *Id.*
357 *Id.*
358 I&E St. No. 2, pp. 47-49. I&E St. No. 2-SR, pp. 26-27.
359 I&E St. No. 2, p. 47. A cost of equity of 11.25% is already at the high end of the Company's calculated range, and significantly above I&E's recommended 8.62%.
360 I&E St. No. 2-SR, p. 27.
361 I&E St. No. 2-SR, p. 27, *citing* 66 Pa. C.S. § 1501.

Finally, I&E offers that UGI Electric management should have proposed a reconcilable surcharge mechanism to flow back the net tax savings from the TCJA to rate payers in its base rate filing.

E. Quarterly Earnings Reports and Rate of Return/Return on Equity

I&E presented the testimony of I&E witness Joseph Kubas[362] regarding the inclusion of the Company's FPFTY Plant in their QERs. This I&E Main Brief contains and extensive discussion of this issue and how the inclusion of the FPFTY Plant in the September 30, 2017 QER severely skewed the Company's presentation of their claimed actual ROE and ROR which permeated throughout the Company's testimony trying to justify their requested ROR and ROE going forward.[363] As a result, the Company's entire testimony regarding their requested ROE and ROR is tainted and not reliable.

F. Conclusion as to Overall Rate of Return

In consideration of the above and the record evidence presented by I&E, I&E recommends that the Company should be afforded the opportunity to earn an overall rate of return of 6.82%. This recommended overall rate of return is comprised of a weighted average of a 4.69% rate of return on long-term debt and an 8.62% rate of return on equity.

IX. RATE STRUCTURE

A utility's rate structure addresses how the Commission's approved revenue increase will be allocated among the utility's various tariffed rate classes. Once a class

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[362] *See* I&E St. No. 5, pp. 1-15; I&E St. No. 5-SR, pp. 1-30.
[363] *See* I&E M.B., Section XI. A. UGI Electric's Quarterly Earnings Reports, *infra*.

revenue allocation is determined, development of a rate design will address how the tariffed rates and rate elements will generate the allocated revenues. A properly designed rate structure will not unduly burden one class of ratepayers to the benefit of another. Under the Public Utility Code, "[n]o public utility shall...make or grant any unreasonable preference to any person, corporation....No public utility shall establish or maintain any unreasonable difference as to rates, either as between localities or as between classes of service."[364] Differences in rates charged to different classes are permissible so long as there is reasonable basis for the discrepancy.[365] "Public utility rates should enable the utility to recover its cost of providing service and should allocate this cost among the utility's customers in a just, reasonable and nondiscriminatory manner."[366]

A. Allocated Class Cost of Service Study

I&E did not present testimony regarding the Company's allocated class cost of service study. I&E did recognize that the Company prepared a customer cost analysis presented in CORRECTED REVISED UGI Electric Exhibit D.[367] Although I&E did not make a specific recommendation regarding the customer cost analysis, I&E did state that I&E's believes the Company's customer cost analysis is overly inclusive.[368]

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[364] 66 Pa. C.S. §1304.

[365] *Peoples Natural Gas Company v. Pa. P.U.C.*, 409 A.2d 446 (Pa. Cmwlth 1979).

[366] *Pa. P.U.C. v. West Penn Power*, 73 Pa. P.U.C. 454, 510, 199 PUR 4th 110 (1990)

[367] I&E St. No. 3, p. 34.

[368] I&E St. No. 3, p. 34. I&E St. No. 3-SR, p. 23.

B. Revenue Allocation

1. Gradualism

Gradualism is a well-established ratemaking concept that seeks to limit the immediate increases customers receive when rates are increased and instead seeks to implement significant rate changes on a more gradual basis over time.[369] In this proceeding, the Company's proposed one-time sudden 155% increase to its residential customer charge is excessive and violates the concept of gradualism. For this reason, I&E has applied the concept of gradualism to its analysis of the Company's proposed customer charge increase.[370]

The Company argues that the concept of gradualism should be applied to the overall rate increase and not individual subcomponents (residential customer charge) of the rate design.[371] The Company also argues that it's last base rate increase was 22 years ago and that a change of 13.6% to overall class revenue appears to be quite gradual.[372]

I&E believes that gradualism concerns, from the standpoint of rate design, must be handled differently than those of the overall rate class.[373] Rate design determines how individual customers will generate revenue allocated to each rate class.[374] However, when a customer looks at their bill, they will only care about how much their own rate has increased and not how much revenue the rate classes generating. This is particularly

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369 I&E St. No. 3, p. 36.
370 I&E St. No. 3, pp. 33-37.
371 I&E St. No. 3-SR, p.24.
372 *Id.*
373 *Id.*
374 *Id.*

true for the customer charge component of rate design, which is a defined, constant amount on the customer's bill that the customer cannot control through usage.[375] Further, the percent increase to the customer charge must be specifically considered because every customer pays a customer charge and the large 155% increase in the residential customer charge proposed by the Company will disproportionately negatively impact low usage customers.[376] Therefore, gradualism and rate shock must be considered for individual components of a customer's bill and the customer charge in particular.[377]

In consideration of the above and the record evidence presented by I&E, I&E urges the Administrative Law Judges and the Commission to apply the concept of gradualism to any increase in the customer charge granted in this proceeding.

C. Rate Design

1. Summary of Rate Design

This base rate proceeding presents some unique challenges in that UGI Electric has not been in for a base rate increase for nearly 22 years. Those challenges will need to be met through careful consideration regarding the ultimately approved rate design and customer charges. Concepts mentioned herein like rate shock, gradualism, and scale back will need to be artfully applied. I&E's recommendations regarding rate design are addressed below under "customer charge." It is worth noting here that I&E agrees with

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375 I&E St. No. 3-SR, p. 25.
376 I&E St. No. 3-SR, p. 25.
377 *Id.*

the Company that, in general, a single block usage rate is preferable to multiple block usage rates.[378]

2. Residential Customer Charge

UGI Electric has proposed a total revenue increase of $8,491,187 with $8,475,717 (99.8%) going to the residential Rate R customer class; and $15,254 (0.2%)[379] going to the general service Rate GS-5 customer class.[380] The proposed distribution rates for Rate R and Rate GS-5 are the same at $0.03169/Mcf.[381] The Company's proposed customer charge for Rate R is $14.00 per month; an increase of $8.50 (155%) form the present charge of $5.50.[382] And, the Company's proposed customer charge for Rate GS-5 is also $14.00 per month; an increase of $8.50 (155%) from the present charge of $5.50.[383]

I&E recommends a customer charge for Rate R of $10.00 per month; an increase of $4.50 (81.8%).[384] For Rate GS-5 I&E also recommends $10.00 per month; an increase of $4.50 (81.8%).[385] Further, based on the recommended $10.00 customer charges, I&E also recommends single block usage rates of $0.036567 per kWh for Rate R and $0.033927 per kWh for Rate GS-5.[386] All of I&E's recommendations for rate design and customers charges take the concepts of rate shock and gradualism into consideration.[387]

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378 I&E St. No. 3, p. 38.
379 Note: $8,491,187 - $8,475,717 = $15,470.
380 UGI Elec. St. No. 8-SD, p. 4.
381 *Id.*
382 I&E St. No. 3, pp. 34-38. I&E St. No. 3-SR, pp. 23-28.
383 *Id.*
384 *Id.*
385 *Id.*
386 I&E St. No. 3-SR, p. 28.
387 I&E St. No. 3, pp. 34-38. I&E St. No. 3-SR, pp. 23-28.

Further, any increases granted should also take the concept of scale back into consideration.

3. Non-Residential Customer Charges

The Company's proposed base rate increase did not include a proposed increase to the following rate classes: Large Power; Lighting; and HTP.[388]

D. Scale Back

I&E recommended that if the Commission grants less than the Company's requested revenue increase, I&E recommends that the usage rates for the GS-5 and Rate R classes be scaled back sequentially to produce specific revenue levels for each class first, and then I&E's recommended $10 customer charge for each class be scaled back if required.[389] Specifically, the GS-5 usage rate should be scaled back to produce $29,078 or the usage rate revenue level under present rates.[390] Then, Rate R usage rates should be scaled back to produce $14,297,208, or the usage rate revenue level under I&E recommended present rate revenue.[391]

The Company argues that any scale back should be based on the Company's originally proposed rates and not the reduced customer charge proposed by I&E and OCA.[392]

I&E rejects the Company's argument. I&E argues that its scale back methodology is based first upon the fact that the recommended decrease to the Company's requested

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388 UGI Elec. St. No. 8-SD, p. 5.
389 I&E St. No. 3, p. 39. I&E St. No. 3-SR, p. 29.
390 I&E St. No. 3, p. 39, *citing* I&E Exh. No. 3, Sch. 14, col E, ln 5.
391 I&E St. No. 3, p. 39, *citing* I&E Exh. No. 3, Sch. 15, col G, ln 31.
392 I&E St. No. 3-SR, p. 29.

customer charge has the effect of increasing the usage rates at the fully requested revenue increase.[393] Therefore, usage rates should be scaled back prior to any scale back of the customer charge.[394] Second, I&E recommends the GS-5 class be scaled back first because the overall increase to that class is minimal.[395] Then, the bulk of the scale back is left for the Rate R class, which will most likely be assessed the majority of the proposed increase.[396] Finally, any scale back methodology used should be based upon the customer charges ultimately granted by the Commission.[397]

In consideration of the above and the record evidence presented by I&E, I&E recommends that the usage rates for the GS-5 and Rate R classes be scaled back sequentially to produce specific revenue levels for each class first, and then I&E's recommended $10 customer charge for each class be scaled back if required.

D. Summary and Alternatives

I&E's proposed monthly customer charge; as well as its gradualism and scale back recommendations, are based on sound Commission ratemaking policies and precedent and should be adopted and implemented as set forth.

X. UNIVERSAL SERVICE

Pursuant to the Partial Stipulation agreed to by the parties, UGI Electric's Universal Service Programs issues, including the Customer Assistance Program (CAP); Self-certification; Rider C; Budget Billing; and Payment Plans, are all resolved as fully

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393 I&E St. No. 3, p. 39.
394 *Id.*
395 *Id.*
396 *Id.*
397 I&E St. No. 3-SR, p. 29.

set forth in the Partial Stipulation filed by the parties in this proceeding. I&E presented no further position regarding Universal Service.

XI. MISCELLANEOUS ISSUES

A. UGI Electric's Quarterly Earnings Reports

I&E asserts that the purpose of a quarterly earnings report is to establish uniform and industrywide financial reporting requirements designed so the Commission can monitor, on a regular basis, the financial performance and earnings of the electric, gas, telephone, water and wastewater public utilities that are subject to commission jurisdiction.[398] During the natural course of I&E's investigation it became apparent that the Company was alluding to an actual rate of return and return on equity that appeared to be so low so as to be a mistake. UGI Electric Chief Regulatory Officer, Paul J. Szykman, stated that:

> as reflected in UGI Exhibit A (Fully Projected), Schedule A-1, the Company's operations are projected to produce an overall return on rate base of 3.20%, which equates to a return on common equity of only 1.92% for the twelve months ending September 30, 2019.[399]

Followed by the statement:

> As explained by Company witness Paul R. Moul (UGI Electric Statement No. 5), these returns are not adequate based on applicable financial data and the risks confronted by UGI Electric. Unless UGI Electric receives the requested rate relief, those returns will continue to decline.[400]

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398 I&E St. No. 5, p.4; I&E St. No. 5-SR, p. 15.

399 UGI Elec. St. No. 1, p. 6.

400 *Id.*

Continuing to follow the natural course of its investigation, I&E conducted a review of UGI Electric's recent Quarterly Earnings Reports looking for confirmation.[401] Instead, I&E found discrepancies between the Company's HTY net plant claim shown on UGI Exhibit A - Historic, Schedule A-1, sponsored by UGI witness Megan Mattern,[402] compared to the Quarterly Earnings Report submitted to the Commission by UGI Utilities, Inc. - Electric Division for the period ending September 30, 2017.[403]

I&E uncovered that in the most recent UGI Electric QER provided to the Commission for the 12-month period ending September 30, 2017, the Company inexplicably added $44,453,000 of net plant to the actual net plant balance of $86,742,000 to arrive at an "adjusted" net plant of $131,195,000.[404] This $44,453,000 of net plant is an increase in actual net plant of **51.2%.** The Company also inexplicably added $1,600,000 of annual depreciation expense to the actual annual depreciation expense of $4,495,000 to arrive at an "adjusted" annual depreciation expense of $6,095,000.[405] These adjustments do not appear to be supported by historic data.[406]

When asked by I&E to explain the discrepancies, the Company offered that Quarterly Earnings Reports, which are submitted pursuant to Commission regulations, provide for, among other criteria, ratemaking adjustments.[407] The Company stated further:

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401 I&E St. No. 5, pp. 1-2.
402 *Id. See also* UGI Elec. St. No. 4.
403 UGI Elec. St. No. 5, pp. 1-2.
404 I&E St. No. 5, p. 3, *citing* I&E Exh. No. 5, Sch. 1, p. 1, ln 3.
405 *Id.*, *citing* I&E Exh. No. 5, Sch. 1, p. 1, ln 18.
406 *Id.*
407 I&E St. No. 5, p. 4, *citing* I&E Exh. No. 5, Sch. 2.

> Act 11 of 2012 provides for ratemaking on the basis of a Future Test Year or Fully Projected Future Test Year, as may be elected by a utility. UGI Electric has elected to use a Fully Projected Future Test Year, and accordingly, the referenced projected plant additions are appropriate.[408]

I&E responded by arguing that the QERs are governed by the regulations found in 52 Pa. Code Chapter 71, Financial Reports ("Chapter 71").[409] Chapter 71 states that the QERs are required to reflect the actual per book "revenues, expenses and investment amounts that reflect the unadjusted results of operations for the 12-month periods ending each March 31, June 30, September 30 and December 31 as recorded in the public utility's financial books of account."[410] Further, annualization, normalization, and ratemaking adjustments are required to bring a public utility's accounts to a 12-month level of activity for changes to the actual per books accounts which occur before the end of the 12-month period ending December 31 of each historic year.[411] It is clear that Chapter 71 is backward looking, as all adjustments are made to the actual per books accounts for the historic period. There is no mention of future or fully projected future accounts or periods in Chapter 71.

Further, Chapter 71 defines "ratemaking adjustments" as "adjustments to a public utility's actual per book amounts to reflect disallowances made in prior cases by the Commission to revenues, expenses and investments which are not reflected in the public utility's financial books of account."[412] Meaning these disallowances have already

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408 *Id.*
409 I&E St. No. 5, p. 4.
410 I&E St. No. 5, p. 5, *citing* 52 Pa. Code § 71.2 - *Actual per books*.
411 *Id.*
412 *Id.*

occurred but are not yet reflected in the utilities books of account for the relevant historic period. Again, there is no mention of future or projected future. Chapter 71 also states, regarding permitted adjustments to financial reports, that a:

> public utility shall make ratemaking adjustments to its intrastate per book amounts to reflect adjustments made in prior cases by the Commission which are not included in the actual per book amounts recorded by the public utility, if these adjustments are still applicable, and adjustments to reflect current Commission ratemaking policy and practices.[413]

I&E asserts that Chapter 71, does not permit projected rate base included in a FPFTY in a current base rate case to be included as an adjustment in a QER as that rate base does not qualify as an adjustment approved by the Commission in a prior case.[414] Nor is I&E aware of the Commission issuing any Secretarial Letters allowing the practice.[415]

The Company, however, continued its argument in rebuttal testimony that Act 11 modified the QER filing requirements set forth in Chapter 71; that FPFTY ratemaking adjustments are permitted; and, that ratemaking adjustments to reflect current Commission ratemaking policy and practices are allowed.[416]

I&E rejects the Company's argument that Act 11 modified the filing requirements of Chapter 71. There is simply no support for the company's position that Act 11 modified Chapter 71.[417] There is no pronouncement in the plain language of Act 11 that it modified Chapter 71, nor is there any pronouncement of any intent to modify Chapter 71. The language of both Act 11 and Chapter 71 are un-ambiguous and their meaning

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413 *Id.*, pp. 5-6, *citing* 52 Pa. Code § 71.6.

414 I&E St. No. 5, p. 6.

415 *Id.*

416 I&E St. No. 5, p. 3, *citing* UGI Elec. St. No. 1-R, p. 5.

417 I&E St. No. 5, pp. 10-12. I&E St. No. 5-SR, pp. 4-9.

and intent is clear. Therefore, there is no need to go beyond a "plain meaning" analysis of Act 11.

And, while I&E recognizes that Act 11 permits utilities to set rates based on a FPFTY; including FPFTY Plant in rate cases is perfectly appropriate.[418] It, however, does not follow that FPFTY Plant should be reflected in the QERs, as the purpose of the QERs is to provide the Commission a snapshot of the utility's current financial performance and earnings at that point in time.[419] Therefore, only verifiable, current data should be included in the QER.[420] I&E urges, the Commission cannot monitor the financial performance and earnings if future plant is included in the QER as it dramatically understates the ROR and ROE in the reported period as evidenced by the testimony and the exhibits submitted by UGI Electric.[421]

To illustrate the very real effect and substantial benefit gained by UGI Electric as a result of its unilateral inclusion of the additional Net Plant and Annual Depreciation Expense in its September 30, 2017 QER, I&E offers the following.[422] The inclusion of the $44,453,000 of Net Plant and the $1,600,000 of Annual Depreciation Expense related to the FTY and the FPFTY years in the September 30, 2017 QER dramatically reduces the overall rate of return and return on equity in its September 30, 2017 QER.[423] As shown on I&E Exhibit No. 6, Schedule 1, page 1, line 26, the Company determined that

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418 I&E St. No. 5-SR, p. 5.
419 *Id.*
420 *Id.*
421 *See* I&E St. No. 5-SR, pp. 5-6.
422 *See Id.*, pp. 6-7.
423 *Id.* p. 6.

the overall rate of return earned by UGI in the Quarter Ending September 30, 2017 was **4.94%**.[424] Further, as shown on I&E Exhibit No. 6, Schedule 1, page 2, line 15, the Company determined that the return on equity earned by UGI Electric in the Quarter Ending September 30, 2017 was **5.22%**.[425]

Now, compare the above to the following. If you remove the projected plant and corresponding annual depreciation expense that were unilaterally added to the September 30, 2017 QER by UGI Electric, as shown on I&E Exhibit No. 6, Schedule 3, Page 1, line 26, the overall rate of return would have been **10.17%**.[426] Further, removal of the projected plant and corresponding annual depreciation expense, as shown on I&E Exhibit No. 5, Schedule 3, Page 2, line 15, results in a return on equity of **14.9%**.[427]

It is I&E's contention that the overall rate of return claimed by the Company for the Quarter ending September 30, 2017 should have been 10.17% and not 4.94%; and, that the return on equity should have been 14.9% and not 5.22%.[428]

To provide further explanation and a summary of I&E witness Joseph thorough discussion of this issue, I&E offers, including future test year and fully projected future test year plant and corresponding annual depreciation expense drastically lowers the overall rate of return and return on equity because the investments that have yet to be made or are outside the reporting period. This inclusion gives UGI "credit" for investments in plant additions that have yet to be made. It is illogical to include plant

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424 *Id.*

425 *Id.*

426 *Id.*, p. 7.

427 *Id.*

428 *See* I&E St. No. 5, pp. 1-15; I&E St. No. 5-SR, pp. 1-30.

additions that may be made in 2019 when determining the actual historic rate of return and return on equity at September 30, 2017. Any future test year and fully projected future test year plant additions and annual depreciation expense claims are only projections that may or may not occur two years beyond September 30, 2017. It is I&E's position that QERs should be based on verifiable current data, not speculation.[429] Including future test year and fully forecasted future test year plant and annual depreciation expense renders the QERs and the Commission's summary of the QERs meaningless because the reports and summary are based on unsupported projections that do not reflect the current financial position of the utilities being reported.[430]

It is patently obvious that the Company's projections made in the September 30, 2017 QER were overly optimistic at best and woefully inaccurate at worst.[431] The over optimism and inaccuracies became obvious during the course of I&E's investigation and comparison of the September 30, 2017 QER with the information filed by UGI Electric as part of its base rate filing.[432] The projected plant addition time periods in this rate case overlap and align with the projected plant addition time periods in the QER for September 30, 2017. I&E was compelled to compare the two as the logical next step after the Company claimed the very low ROR and ROE as discussed supra.[433]

To illustrate further, I&E's investigation found that the Company is not projecting it will add the same amount of net plant in the FTY and the FPFTY in this base rate case

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[429] I&E St. No. 5, p. 9.
[430] *Id.*
[431] I&E St. No. 5, pp. 9-10.
[432] *Id.*
[433] *See* I&E St. No. 5, pp. 6-7; I&E St. No. 5-SR, pp. 5-6. *See also* UGI Elec. St. No. 1, p. 6.

filing as it did in the September 30, 2017 QER. In this case, the Company is projecting it will add only $32,729,000 in net plant during the same time-period of October 1, 2017 to September 30, 2019 as opposed to the $44,453,000.[434] Subtracting the $90,893,000 in net plant shown on UGI Book 5, Schedule A-1, Historic, from the $123,622,000 shown on UGI Book F, Schedule A-1, Fully Forecasted, leaves the $32,729,000.[435] The difference in projected net plant between these two projections covering the same time period is $11,724,000, or 35% less than projected in the September 30, 2017 QER ($44,453,000 - $32,729,000 = $11,724,000).[436]

The $11,724,000 difference reveals that in just the four months from the filing of the September 30, 2017 QER to the filing of this base rate case, the Company's projected plant additions became 35% "less optimistic." For the September 30, 2017 QER, the Company was overly optimistic in its projected plant additions. This large difference in net plant indicates that the Company's projected net plant additions in the QER for September 31, 2017 were unreasonable and also supports I&E's contention that the Company's projections were and are highly speculative.[437] It also supports I&E's recommendation that the Commission not permit projected plant additions to be included in the QERs.[438]

In response to I&E witness Kubas' testimony, UGI Electric's raised various arguments, all of which I&E rejects. In addition to the Company's arguments regarding

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434 I&E St. No. 5, pp. 9-10.
435 I&E St. No. 5, p. 10.
436 *Id.*
437 *Id.*
438 *Id.*

the alleged modification of Chapter 71 by Act 11 that I&E rejected *supra*, the Company argues that the I&E testimony discussing the Company's September 30, 2017 desire to present a dire financial picture is without merit.[439] The Company rationalized that at the time the Company was compiling a base rate case, the Company had no regarding the possibility of an overearning investigation as the Company was certain rate relief was justified. [440]

This argument fails however because while I&E understands the Company was compiling a base-rate case during the time of the September 30, 2017 QER filing, the I&E testimony was not tied specifically to that time period.[441] I&E was presenting a more general comment that reducing the ROR and ROE, as was done in the September 30, 2017 QER, and would likely be done in future QERs, reduces the likelihood of an overearning investigation generally.[442] I&E understands that an overearning investigation can occur at any time, therefore, it is important that the Company's practice of improperly including future plant not continue so that the QERs accurately reflect the company's actual financial picture for the identified quarter.[443] With or without a pending rate case, the Company's September 30, 2017 QER presents a more direr financial picture than it would have if the proposed fully FPFTY Plant were not

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439 I&E St. No. 5-SR, p. 3.
440 *Id.*
441 I&E St. No. 5-SR, pp. 9-10.
442 I&E St. No. 5-SR, p. 10.
443 *Id.*

included.[444] Furthermore, UGI Electric's September QER was used in the Commission's analysis on the earnings of utilities, making the commission's analysis less reliable.[445]

The Company also argued, the Company believes that the I&E testimony concerning the Distribution System Improvement Charge ("DSIC") is without merit because the Company currently does not have a DSIC.[446] Further, the Company believes that Act 11 permits utilities to move forward and utilize their Long-Term Infrastructure Improvement Plans ("LTIIP"), and if I&E's recommendation is accepted, utilities will reevaluate their LTIIP commitments, and file more base rate cases.[447] The Company's rationale is that I&E's recommendation lessens the effectiveness of the DSIC and creates regulatory inefficacies.[448]

I&E rejects these arguments. The Company's statement "since UGI electric does not currently have a disk" is misleading.[449] Rather, the Company has filed for its LTIIP, which will pave the way for the Company to initiate its DSIC.[450] I&E also noted that the inclusion of the FPFTY Plant that dramatically reduces the overall ROR and ROE in the Company's September 30, 2017 QER also allows UGI electric to be eligible for a DSIC.[451] Further, the Company does have a financial incentive to report lower ROR and ROE results in the future to be eligible for the DSIC or not subject to an overearning

444 *Id.*
445 *Id.*
446 I&E St. No. 5-SR, p. 3.
447 I&E St. No. 5-SR, p. 4.
448 I&E St. No. 5-SR, p. 4.
449 I&E St. No. 5-SR, pp. 12-13.
450 I&E St. No. 5-SR, pp. 12-14.
451 I&E St. No. 5, pp. 6-7. I&E St. No. 5-SR, pp. 10-11.

investigation.[452] A lower ROR allows UGI Electric to be eligible for a DSIC.[453] Utilities that earn more than the authorized ROR would have their DSIC reset to zero.[454] It is critical for the QERs to not include the additional FPFTY Plant, which serves to artificially lower the ROR and ROE, thus not triggering a disk reset to zero which has the effect of invalidating the important customers safeguard built into the DSIC statute.[455] Therefore, the Commission should also consider the customer protections of the DSIC statute and not permit the inclusion of the FPFTY Plant in future QERs because it significantly impacts the ROR and ROE, which are the determining factors of whether the DSIC must be reset to zero.[456]

The Company also argues that it believes FPFTY Plant should be in the QER because the numbers are not speculative as they are based upon budgeted and planned projects, including the Company's projected DSIC eligible plant included in its LTIIP.[457]

I&E rejects the Company's argument.[458] The Commission cannot rely on the Company's claim that the FPFTY Plant additions are budgeted, and therefore, not speculative.[459] The simple fact is that budgeted amounts do not always result in actual plant in service.[460] The Company admits that there can be, and recently were, changes totaling $11,724,000 in the Company's budgeted amounts, changes in allocation factors

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452 I&E St. No. 5-SR, p. 12.
453 *Id.*
454 I&E St. No. 5, p. 7. I&E St. No. 5, p. 12.
455 I&E St. No. 5-SR, pp. 12-14.
456 I&E St. No. 5-SR, p. 13.
457 I&E St. No. 5-SR, p. 14.
458 *See* I&E St. No. 5-SR, pp. 14-17.
459 I&E St. No. 5-SR, p. 15.
460 *Id.*

and changes in depreciation rates between the September 30, 2017 QER and this base rate filing.[461] Therefore, while a budget may reflect projections, there is no guarantee that plant will be installed at the projected budgeted amount; be depreciated at the projected rate; or be allocated using the projected methodology[462]. With so many variables admitted to by the Company, it is not reasonable to include those projections in the QER, which is designed to give the Commission a current actual financial snapshot of the utilities it regulates.[463] The Company's explanation for the 35% difference in such a short time period supports I&E's recommendation to not allow any FPFTY Plant in the QERs.[464] As previously noted, the purpose of the QER is to establish uniform and industry-wide financial reporting requirements designed so the Commission can monitor on a regular basis, the financial performance and earnings of the electric, gas, telephone, water and wastewater public utilities that are subject to Commission jurisdiction.[465]

Finally, the Company argues that other utilities, including affiliates of UGI Electric, include FPFTY Plant in their QERs.[466]

I&E rejects this argument.[467] I&E strongly believes that Chapter 71 is unambiguous and does not allow the inclusion of FPFTY plant in the utilities QER reports to the Commission. The fact that another company besides UGI Electric is doing the same thing does not change I&E's belief that the inclusion of the FPFTY Plant in the

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461 *Id.*
462 *Id.*
463 *Id.*
464 *Id.*
465 I&E St. No. 5, p. 4. I&E St. No. 5-SR, p. 15.
466 I&E St. No. 5-SR, p. 3.
467 I&E St. No. 5-SR, pp. 18-22.

QERs is impermissible.[468] Chapter 71 was not modified nor amended by Act 11, and therefore, there is no need for a rulemaking proceeding to determine the meaning of the clear and unambiguous language of Chapter 71.[469]

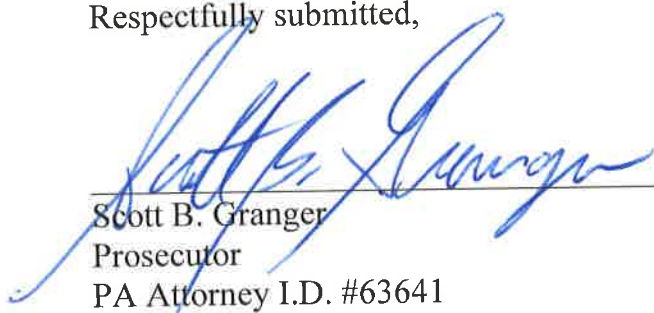
B. Public Input Hearings

Public Input Hearings were held on April 18, 2018 in Hearing Room 1 of the Commonwealth Keystone Building using the Commission's Smart Hearing technology. I&E did not incorporate any of the on-the-record testimony into its testimony in this proceeding.

XII. CONCLUSION

I&E respectfully submits that for all the reasons presented in this I&E Main Brief, UGI Electric has not met its burden of proof; and, there is substantial evidence of record to support Your Honors issuing a Recommended Decision accepting all of the positions presented on the record by I&E.

Respectfully submitted,



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PA Attorney I.D. #63641

Dated: July 2, 2018

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468 I&E St. No. 5-SR, p. 21.
469 *Id.*

APPENDICES

Appendix A

I&E TABLE I

($ in '000)
R-2017-2640058

TABLE I
INCOME SUMMARY

	9/30/19 Proforma Present Rates	INVESTIGATION & ENFORCEMENT Adjustments	Present Rates	Allowances	Proposed
	$	$	$	$	$
Operating Revenue	89,092	-60	89,032	824	89,856
Deductions:					
O&M Expenses	72,027	-1,283	70,744	9	70,753
Depreciation	5,869	-579	5,290		5,290
Taxes, Other	6,514	-356	6,158	48	6,206
Income Taxes:					
Current State	-317	270	-47	77	30
Current Federal	-460	511	51	145	196
Deferred Taxes	981	0	981		981
ITC	0	0	0		0
Total Deductions	84,614	-1,437	83,177	279	83,456
Income Available	4,478	1,377	5,855	545	6,400
Measure of Value	119,272	-25,436	93,836	0	93,836
Rate of Return	3.75%		6.24%		6.82%

I&E TABLE II

($ in '000) R-2017-2640058	Rate Base	Revenues	Expenses	Depr.	Taxes Other	Current FIT	Current PACNI	Combined Deferred Inc Taxes	ITC
		Table II - Summary Of I&E Adjustments							
MEASURE OF VALUE:									
Excess ADIT	-11,483								
CWC	-425								
Rate Base (net of CWC/Excess ADIT)	-13,528								
Revenues:									
Average revenues		-60	0		-4	-11	-6		
Expenses:									
Uncoll. Accts. Exp.			-6			1	1		
Environmental Remediation			-139			26	14		
Rate Case Expense			-90			17	9		
Vegetation Management			-206			39	21		
Salaries & Wages-net of Additions			-34			7	3		
Employee Additions			-64			12	6		
Outside Services-Miscellaneous			-170			32	17		
Employee Activity Costs			-12			2	1		
Stock Options/Awards			-189			36	19		
Co-owned Svc. Transition Program			-314			59	31		
Storm Damage Expense			-48			9	5		
Purchased Power			-11			2	1		
Depreciation:									
Depreciation Expense				-579		109	58		
Taxes Other:									
PURTA					-352	67	35		
Interest Synchronization						104	55		
Total Additions / Deductions	-25,436	-60	-1,283	-579	-356	511	270	0	0
Company Measure of Value	119,272								
I&E Measure of Value	93,836								

I&E TABLE III

Table III
Rate of Return

Per Company	Structure	Cost	Weighted Cost
Total Debt	46.00	0.0470	2.1600
Long Term Debt	46.00	0.0469	2.1600
Short Term Debt	0.00	0.0000	0.0000
Preferred Stock	0.00	0.0000	0.0000
Common Equity	54.00	0.1125	6.0800
TOTAL	100.00		8.24

Per Staff	Structure	Cost	Weighted Cost
Total Debt	45.98	0.0470	2.1600
Long Term Debt	45.98	0.0469	2.1600
Short Term Debt	0.00	0.0000	0.0000
Preferred Stock	0.00	0.0000	0.0000
Common Equity	54.02	0.0862	4.6600
TOTAL	100.00		6.82

Appendix B

Federal Tax Adjustment Credit (FTAC)

A credit value of x.xx% will apply to all Pennsylvania Public Utility Commission jurisdictional distribution charges during the period xxx x, xxxx through xxx x, xxxx to pass the January 1, 2018 through September 30, 2018 effects of the Tax Cuts and Jobs Act (TCJA) to customers. The FTAC will be computed annually, will be effective ten days after filing, and will continue until the effect of the change in tax rates resulting from the TCJA has been refunded to customers.

The FTAC will be based on the difference in total annual revenue requirement before and after implementing the 2018 effects of the TCJA and the calculation will reflect the reduction in required revenues. The reduction in required revenues will be divided by estimating annual applicable base revenues to develop the FTAC to be applied to customers' bills for service rendered during the twelve-month period beginning on the effective date of new rates. The difference between the actual reduction in required revenue and the reduction in revenues produced by the FTAC as applied will be subject to refund or recovery in an annual revision to the FTAC. The interest rate on the over or under collection will be applied using the residential mortgage lending rate specified by the Secretary of Banking in accordance with the Loan Interest and Protection Law (41. P.S. §§ 101, et seq.). For any over/under credit balance that remains after the twelve-month refund period elapses, the Company shall propose a final additional FTAC adjustment in the thirteenth month to ensure the balance is eliminated.

A reconciliation statement will be submitted to the Commission at the end of the twelfth month. A final reconciliation statement will be filed with the Commission within 30 days after the final over/under balance has been eliminated in the thirteenth month after the effective date of new rates. The FTAC revenues and reconciliation will be subject to audit by the Commission's Bureau of Audits.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2017-2640058
	:	
UGI Utilities Inc. – Electric Division	:	
Base Rates	:	

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing **Main Brief** dated July 2, 2018, in the manner and upon the persons listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party):

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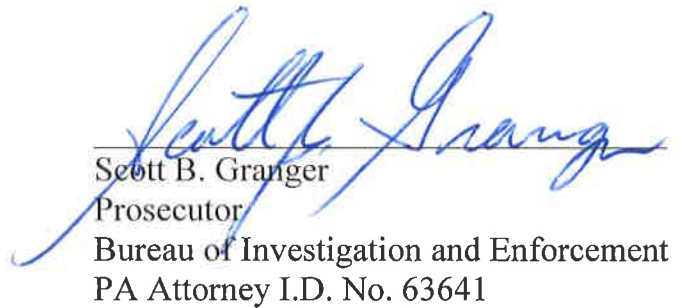

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