



COMMONWEALTH OF PENNSYLVANIA  
PENNSYLVANIA PUBLIC UTILITY COMMISSION  
COMMONWEALTH KEYSTONE BUILDING  
400 NORTH STREET, HARRISBURG, PA 17120

BUREAU OF  
INVESTIGATION  
&  
ENFORCEMENT

January 22, 2020

*Via Electronic Filing*

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

Re: Pennsylvania Public Utility Commission v.  
Valley Energy, Inc. –  
Supplement No. 49 to Tariff Electric – Pa. PUC No. 2  
Docket No. R-2019-3008209  
**I&E Reply Brief**

Dear Secretary Chiavetta,

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

Copies are being served on active parties of record as evidenced in the attached Certificate of Service. Should you have any questions or concerns, please do not hesitate to contact me.

Sincerely,

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JMC/ac  
Enclosure

cc: Honorable Steven K. Haas (*ALJ, PUC Harrisburg*)  
Honorable Benjamin J. Myers (*ALJ, PUC Harrisburg*)  
Per Certificate of Service

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2019-3008209
	:	
Valley Energy, Inc.	:	

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**REPLY BRIEF  
OF THE  
BUREAU OF INVESTIGATION AND ENFORCEMENT**

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Dated: January 22, 2020

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## **I. INTRODUCTION**

### **A. History of the Proceeding**

On January 8, 2020, the Bureau of Investigation and Enforcement (“I&E”) filed a Main Brief in this proceeding. The history of the proceeding was addressed in I&E’s Main Brief.<sup>1</sup> On January 8, 2020, Valley Gas, Inc. (“Valley” or “Company”), the Office of Consumer Advocate (“OCA”), and the Office of Small Business Advocate (“OSBA”) also filed Main Briefs. The issues addressed in this I&E Reply Brief are limited to matters raised in the Company, OCA, and OSBA Main Briefs that relate to recommendations made in the I&E Main Brief.

### **B. Burden of Proof**

I&E fully addressed the Burden of Proof in its Main Brief.<sup>2</sup>

## **II. SUMMARY OF ARGUMENT**

Valley maintains it should be awarded a rate increase of \$745,000.<sup>3</sup> However, the Company’s Main Brief fails to demonstrate its rate increase proposal is just and reasonable. Specifically, Valley’s claim continues to include an inflated rate base; unjustified Operating and Maintenance expenses; an excessive rate of return; and refusal to follow modest reporting recommendations. Therefore, I&E maintains Valley’s proposal should be adjusted so it only receives a rate increase of no more than \$345,049 and its rate structure be scaled-back as explained below and fully in I&E’s Main Brief.

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<sup>1</sup> I&E Main Brief, pp. 1-2.

<sup>2</sup> I&E Main Brief, p. 3.

<sup>3</sup> Valley Main Brief, p. 7.

Additionally, I&E continues to recommend the Commission order the Company to provide reports on actual capital expenditures, plant additions, and retirements for the FTY and FPFTY.

### **III. ISSUES RESOLVED AMONG THE PARTIES**

The issues resolved among the parties are described in I&E's Main Brief.<sup>4</sup> I&E notes Valley is correct I&E withdrew its pension claim adjustment in surrebuttal testimony; however, Valley is not correct that I&E calculated a \$773,767 pension expense for Valley in direct testimony.<sup>5</sup> Instead, based on the most recent invoice provided by Valley, I&E calculated a \$45,003 total pension expense for Valley.<sup>6</sup> However, after direct testimony, Valley provided further clarifying information, satisfying I&E's concerns that Valley's pension expense should be adjusted downwards.<sup>7</sup>

### **IV. RATE BASE**

As explained in the Main Brief, I&E recommended adjustments to rate base for Construction Work in Progress ("CWIP") and Cash Working Capital ("CWC").<sup>8</sup> In its Main Brief, Valley confirms it removed its claim for CWIP.<sup>9</sup> However, Valley incorrectly claims I&E did not dispute any other rate base component.<sup>10</sup> As explained in

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<sup>4</sup> I&E Main Brief, p. 8.

<sup>5</sup> Valley Main Brief, pp. 13-14; *see* I&E Statement No. 1, pp. 21-22.

<sup>6</sup> I&E Statement No. 1, pp. 21-22.

<sup>7</sup> *See* I&E Statement No. 1-SR (Errata Version), pp. 28-31.

<sup>8</sup> I&E Main Brief, pp. 8-10.

<sup>9</sup> Valley Main Brief, p. 12.

<sup>10</sup> Valley Main Brief, p. 15.

I&E's Main Brief, Valley's Operating and Maintenance expense claims should be reduced by \$103,405, which reduces the Company's CWC allowance by \$12,925.<sup>11</sup>

## **V. REVENUES**

As explained in I&E's Main Brief, I&E recommends a reduction to Valley's revenue increase request for the FPFTY as a result of its various adjustments. However, I&E has no recommendations regarding Valley's specific revenue claims for the FPFTY that support its overall revenue increase request.

## **VI. EXPENSES**

### **A. Total O&M Expenses**

In Main Brief, the Company reiterates its position that the Commission should reject I&E and OCA's individual expense adjustment recommendations in favor of accepting the Company's full expense claim as stated in rebuttal testimony.<sup>12</sup> By contrast, Valley characterizes I&E and OCA's individual expense adjustments as a "mix and match" approach that "penaliz[es] to Company for its effective budget management."<sup>13</sup>

For the same reasons stated in Main Brief, I&E continues to oppose this deeply flawed method for determining Operating and Maintenance ("O&M") expenses.<sup>14</sup> Valley has the burden of proof in this proceeding and I&E has presented evidence that certain specific, individual expense claims for the FPFTY are unjust and unreasonable. Valley

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<sup>11</sup> I&E Main Brief, pp. 9-10. The Company does agree CWC should be recalculated if the Commission orders any changes to Valley's claimed O&M expenses. Valley Main Brief, p. 23.

<sup>12</sup> Valley Main Brief, pp. 28-40.

<sup>13</sup> Valley Main Brief, p. 35.

<sup>14</sup> I&E Main Brief, pp. 11-14.

claims these individual expense adjustments should be rejected because “the Company is effectively managing to its budget”.<sup>15</sup> However, to support its position, the Company primarily relies on vague and unquantifiable statements, e.g., “projections cannot account for all contingencies”, “the adjustments for the FPFTY are conservative expense adjustments”, and “the Company’s FPFTY expense claims are reasonable, well-grounded, and are supported”.<sup>16</sup> Such statements do not provide substantial evidence justifying the individual expense claims that I&E recommended adjustments to on specific, quantifiable bases. Additionally, they do not justify the wholesale revision to O&M expenses Valley provided in rebuttal testimony. To the extent Valley’s Main Brief actually addressed I&E’s recommended adjustments, they will be discussed in the specific expense sections below.<sup>17</sup>

Valley claims it “has managed its expenses close to budget” and that Valley’s expenses are “tracking approximately very close to projections for 2019”, and therefore, its expense claims should be approved in their entirety.<sup>18</sup> Valley further contends I&E does not dispute these general claims. This assertion is incorrect. I&E’s recommendations pertain to whether individual expense claims in the FPFTY are just and reasonable. Reference to historical costs are only relevant as to whether they justify expense claims for the FPFTY. As explained in Main Brief, I&E recommended individual expense adjustments, taking into account the Company’s rebuttal position, but

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<sup>15</sup> Valley Main Brief, p. 10.

<sup>16</sup> Valley Main Brief, pp. 30-31.

<sup>17</sup> Valley claims any resolution of an individual dispute “should be grossed up by the inflation adjustment”. Valley Main Brief, p. 41. However, I&E did not dispute the Company’s 3% inflation adjustment and therefore, any recommendations made by I&E should not be further inflated without specific justification.

<sup>18</sup> Valley Main Brief, p. 41.



only as it related to claims he had analyzed in direct testimony.<sup>19</sup> As explained in I&E's Main Brief, to the extent the Company's position now updates expense claims, whether upwards or downwards, not subject of non-company parties' direct testimony, the Commission should reject them as a prohibited attempt to raise late-brought claims.<sup>20</sup>

Valley also asks the Commission to not weigh the prudence of managerial discretion based on information discovered after the fact.<sup>21</sup> It is unclear to I&E how this statement relates to I&E's recommendations or supports Valley's position.<sup>22</sup>

Nonetheless, I&E contends its position regarding expenses is not based on "information discovered after the fact", but instead is largely based on historical and projected analysis of expense trends as is appropriate for each individual expense adjustment at issue as it relates to the FPFTY. Additionally, the Commonwealth Court just recently held "[t]he Commission does have the authority, pursuant to [66 Pa. C.S. § 315(e)] to make after-the-

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<sup>19</sup> I&E Main Brief, p. 12. I&E further notes, although it did reject Valley's wholesale \$30,096 reduction to O&M expenses in rebuttal testimony, I&E did not dispute Valley's \$96,000 claim reflected in rebuttal testimony for employee medical leave or a Corrosion Technician. See I&E Statement No. 1-SR (Errata Version), pp. 6, 9.

<sup>20</sup> I&E Main Brief, pp. 15-17.

<sup>21</sup> Valley Main Brief, p. 28.

<sup>22</sup> If Valley means to infer I&E is interfering with managerial discretion, I&E's expense adjustments are based on trends and projections to reflect just and reasonable rates, not claimed superior knowledge of day-to-day operations, and therefore clearly do not constitute an attempt to micromanage or act as a super board of directors. See *Bell Tel. Co. of Pa. v. Driscoll*, 21 A.2d 912 (Pa. 1941); *Metropolitan Edison Co. v. Pa. P.U.C.*, 437 A.2d 76 (Pa. Cmwlth. 1981); *Pa. P.U.C. v. Philadelphia Electric Co.*, 501 Pa. 153 (Pa. 1983). Additionally, the cases Valley relies upon to support its position are inapposite to the present case. In *Pa. P.U.C. v. Philadelphia Suburban Water Company*, the Commission denied OCA's recommendation that Philadelphia Suburban Water Company not be allowed to receive a return on meter registers that became obsolete soon after their purchase. 1991 Pa. PUC LEXIS 206, pp. 6-10 (Pa. P.U.C. 1991). Similarly, in *Pa. P.U.C. v. Duquesne Light Co.*, the Commission's discussion of the "prudence standard" was in the context of whether already incurred costs should be allowed into a rate claim. 63 Pa. P.U.C. 337 (Pa. P.U.C. 1987). I&E is not recommending disallowance of a past cost, but refinement to cost *projections* (i.e., the FPFTY) based on past experience.

fact adjustments and to require a utility to support its prior projections in a subsequent rate case.”<sup>23</sup> Parties can clearly rely on a company’s experience in informing its positions in subsequent rate filings.

More appropriately, Valley states “[t]he relevant question in a base rate proceeding is whether the proposed expenses are reasonable and appropriate for furnishing of service to customers.”<sup>24</sup> As explained in Main Brief and further below, I&E has addressed a number of individual expenses that are not reasonable or appropriate for furnishing service to customers.<sup>25</sup> In summary, for the reasons explained above and in I&E’s Main Brief, the Commission should reject the Company’s attempt to wholesale discredit non-company parties’ expense claim recommendations.

## **B. Regulatory Commission Expense**

I&E recommends that the entire \$38,524 claim for Regulatory Commission Expenses be denied because Valley failed to provide an adequate explanation or support for its claim where PUC assessment and Public Utility Realty Tax were double counted.<sup>26</sup> Valley’s Main Brief does not address this adjustment, but simply claims any adjustment must also address the expense adjustments addressed at Valley Statement No. 5-R, pages 4 and 5. However, this citation does not address Regulatory Commission Expense at all, and therefore provides no further support for Valley’s claim.<sup>27</sup> Therefore, the

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<sup>23</sup> *McCloskey v. Pa. P.U.C.*, 2020 WL 215931 (Pa. Cmwlth. 2020).

<sup>24</sup> Valley Main Brief, p. 28.

<sup>25</sup> I&E Main Brief, pp. 14-22.

<sup>26</sup> I&E Main Brief, pp. 14-15.

<sup>27</sup> As explained above, I&E did not dispute Valley’s claim in rebuttal testimony related to employee medical leave or a Corrosion Technician. However, to be clear, the Commission should not further adjust Valley’s claim

Commission should accept I&E's recommended downward adjustment of \$38,524 for the reasons explained in Main Brief.

**C. Miscellaneous General Expense<sup>28</sup>**

I&E recommends that Valley's Miscellaneous General Expense claim be reduced by \$14,415.<sup>29</sup> Valley did not address I&E's recommended adjustment in Main Brief.<sup>30</sup> For the reasons explained in I&E's Main Brief, Valley's claim for Miscellaneous General Expense should be adjusted downwards by \$14,415.

**D. Uncollectible Accounts Expense**

I&E recommends a \$24,201 reduction to the Company's claim of Uncollectible Accounts Expense based on three years of historic gross revenues and net write offs (i.e., 2016, 2017, and the HTY). Further, consistent with the three years' experience, I&E recommends that the Commission use the write-off ratio of 0.62% to determine the additional Uncollectible Accounts Expense attributable to any final base rate increase to be determined in this proceeding.<sup>31</sup>

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upwards as these expenses are already incorporated into the Company's rebuttal position. *See, e.g.*, Valley Errata Statement No. 1-R, p. 2.

<sup>28</sup> In Valley's Main Brief, this expense is under the heading "General Advertising Expense". However, in discovery, Valley stated this expense account was for "Miscellaneous General Expenses", not "General Advertising". I&E Exhibit No. 1, Schedule 6, page 2 of 2.

<sup>29</sup> I&E Main Brief, pp. 15-16.

<sup>30</sup> Valley only addressed OCA's recommendations regarding this expense. Valley Main Brief, pp. 46-47. However, I&E did address similar claims regarding volunteer labor expense in Main Brief. I&E Main Brief, pp. 15-16.

<sup>31</sup> I&E Main Brief, pp. 17-18.

Valley claims the Commission should instead only look to the Company's experience in the HTY.<sup>32</sup> However, I&E demonstrated how Valley's write-off history for the HTY shows a much larger net-write off ratio than the previous two years, and, therefore, the Company would be overstating its claim by using only the HTY.<sup>33</sup> Valley also now claims actual Uncollectible Accounts Expense in 2014 and 2015 undermines I&E's claim.<sup>34</sup> However, Valley raises this discussion for the first time in Main Brief. I&E objects to Valley's raising this claim for the first time in Main Brief, depriving I&E of its ability to scrutinize this contention in surrebuttal testimony. Further, Valley provides no discussion or analysis to explain its contention, or how it relates to or supports its claim. Therefore, I&E continues to maintain the Company's claim for Uncollectible Accounts Expense be limited to \$31,229, and the Commission should use the write-off ratio of 0.62% to determine the additional Uncollectible Accounts Expense attributable to any final base rate increase to be determined in this proceeding.

#### **E. C&T Allocation**

I&E recommends an allowance of \$189,179 or a reduction of \$44,429 (\$233,608 - \$189,179) to the Company's claim based on the Company's average annual percentage increase of the C&T Allocation to Valley from 2016 to the HTY.<sup>35</sup> In rejoinder testimony, Valley confirmed annualizing FTY data and adding a 1% increase would

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<sup>32</sup> Valley Main Brief, p. 49.

<sup>33</sup> I&E Main Brief, p. 17. Specifically, The Company's three-year net write-off history is 0.49% for 2016, 0.52% for 2017, and 0.84% for the HTY.

<sup>34</sup> Valley Main Brief, p. 49.

<sup>35</sup> I&E Main Brief, pp. 18-19.

result in a FPFTY claim of \$172,967.<sup>36</sup> I&E asserts its \$189,179 recommendation for this expense is in line with this most recent figure.<sup>37</sup> However, Valley claims annualizing the FTY data is inadequate because this amount (i.e., \$172,967) was exceeded in 2016, 2017, and 2018, thereby apparently maintaining \$233,608 is a reasonable claim.<sup>38</sup> Additionally, Valley asserts FTY C&T Allocation does not reflect additional customers in East Athens.

I&E maintains its reduction of \$44,429 is reasonable. First, Valley incorrectly claims I&E's recommended adjustment is based off the Company's FTY data. As I&E witness Brenton Grab explained, his recommendation of \$189,179 is based off escalating the average increase in C&T Allocation between 2016 and 2018 into the FTY and FPFTY, not on simply escalating the current FTY data.<sup>39</sup> Nonetheless, the current FTY data confirms I&E's recommendation is reasonable. Second, Valley, for the first time in Main Brief, raises the contention that additional customers in East Athens validates its \$233,608 claim. As discussed above, I&E objects to Valley's raising this claim for the first time in Main Brief, depriving I&E of its ability to scrutinize this contention through expert witness testimony. Nevertheless, Valley provides absolutely no quantifiable analysis to support its claim. Accepting I&E's recommendation would already provide

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<sup>36</sup> See Valley Main Brief, p. 48. As Valley explains, C&T Allocation represents an exception from the Company's generally-proposed 3% inflation adjustment. *Id.*, p. 47.

<sup>37</sup> I&E Main Brief, p. 19.

<sup>38</sup> Valley's Main Brief does not specifically update a dollar amount it is seeking approval for, simply "the Company's claim should be approved". Valley Main Brief, p. 48. As Valley's tables attached to Main Brief do not include a downward adjustment for C&T Allocation, Valley is apparently maintaining its entire \$233,608 claim.

<sup>39</sup> I&E Statement No. 1, pp. 19-20; I&E Statement No. 1-SR (Errata Version), pp. 24-25. The Company's C&T Allocation amount for 2016, 2017, and 2018 was \$176,426, \$180,703, and \$183,633, respectively. I&E Exhibit No. 1, Schedule 9, p. 1.

Valley \$16,212 above what annualizing and inflating its current FTY C&T Allocation data supports. Therefore, the Commission should reject Valley's inadequate justifications, and accept I&E's recommended downward adjustment of \$44,429 to this expense.

#### **F. Rate Case Expense**

I&E's recommends a 60-month normalization period for Rate Case Expense, resulting in an annual allowance of \$54,200 ( $(\$271,000 \div 60 \text{ months}) \times 12 \text{ months}$ ), which is a reduction of \$36,133 ( $\$90,333 - \$54,200$ ) to the Company's claim.<sup>40</sup> Valley points to the Commission's decision in *Pa. P.U.C. v. UGI Utilities, Inc. – Electric Division*<sup>41</sup> to support its 36-month normalization period for rate case expense.<sup>42</sup>

Comparison to the Commission's decision in *UGI Utilities, Inc. – Electric Division* is inappropriate for several reasons. First, as Valley admits, prior to its 2018 rate case filing, UGI Electric had not filed a base rate case for 22 years. By contrast, Valley's last four rate cases were filed within 33, 36, and 110 months of each other.<sup>43</sup> Additionally, Valley witness Edward Rogers admitted the circumstances allowing 110 months to elapse between the last and present rate cases will likely not occur again.<sup>44</sup> Clearly, Valley has a much more frequent filing history than UGI Electric. Therefore, it is much more reasonable to rely on a historical filing frequency for Valley than UGI Electric.

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<sup>40</sup> See I&E Main Brief, pp. 20-22; I&E Statement No. 1, pp. 4-8.

<sup>41</sup> Docket No. R-2017-2640058 (Order Entered October 25, 2018) ("*UGI Utilities, Inc. – Electric Division*").

<sup>42</sup> Valley Main Brief, p. 42.

<sup>43</sup> See I&E Main Brief, p. 26.

<sup>44</sup> See Valley Main Brief, pp. 42-43. Specifically, Valley witness Rogers stated Valley received a very large new contract customer shortly after the 2010 rate case. *Id.*, p. 43 (citing Valley Statement No. 4-R, p. 5).

Second, Valley has not provided the same level of specificity regarding capital expenses that the Commission found persuasive in granting UGI Electric deviation from the general rule that historic frequency be used to determine rate case expense normalization period. The Commission found that UGI Electric's reference to \$8 million in annual spending for capital projects following the FPFTY would cause a \$3 million shortfall at the end of a three-year period.<sup>45</sup> By contrast, Valley has provided no quantifiable or otherwise reliable bases or projections why its proposed normalization period is appropriate. As explained in I&E's Main Brief, Valley's witnesses' specific bases for a shorter normalization period reflect routine or speculative costs.<sup>46</sup> I&E therefore continues to recommend the Commission approve normalization of Valley's Rate Case Expense with reference to its historical filing frequency only, i.e., a 60-month average, resulting in a \$36,133 reduction to Rate Case Expense.

## **VII. FAIR RATE OF RETURN**

### **A. Return on Common Equity – Methodologies**

I&E agrees with Valley that the primary dispute regarding rate of return is return on equity ("ROE").<sup>47</sup> Unlike I&E, which primarily used the Discounted Cash Flow ("DCF") model, Valley analyzed multiple ROE models to develop an ROE recommendation.<sup>48</sup> Although Valley correctly notes "the Commission has primarily relied on the [DCF] to set ROE", to support its use of multiple models and discount

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<sup>45</sup> *UGI Utilities, Inc. – Electric Division*, p. 60.

<sup>46</sup> I&E Main Brief, pp. 21-22.

<sup>47</sup> Valley Main Brief, p. 52.

<sup>48</sup> Valley Main Brief, p. 52. Valley witness Dylan D'Ascendis used the DCF, Risk Premium ("RP"), and Capital Asset Pricing Model ("CAPM") methods, as well as comparison to non-price regulated companies. *See* Valley Main Brief, pp. 54-55.

primary reliance on the DCF, Valley states “the Commission has also observed [in *UGI Utilities, Inc. – Electric Division*] that DCF-only results may understate the appropriate ROE.”<sup>49</sup> However, in its full context, the Commission stated:<sup>50</sup>

*[W]here evidence based on other cost of equity methods indicates that the DCF-only results may understate the utility’s current cost of equity capital, we will consider those other methods, to some degree, in evaluating the appropriate range of reasonableness for our equity return determination*

The Commission did not hold that the DCF method understates ROE or that multiple methods should be used to determine ROE, but only commented that it will look to other methods if the DCF appears understated by comparison. In this case, I&E justified its DCF analysis by comparison to the Capital Asset Pricing Model (“CAPM”).<sup>51</sup> I&E’s analysis is consistent with the Commission’s decision in *UGI Utilities, Inc. – Electric Division* that the cost of equity should “primarily be based upon the use of the DCF methodology and that the results of the CAPM analysis should be used as a comparison to the DCF results”.<sup>52</sup> As explained in I&E’s Main Brief, I&E calculated a CAPM ROE of 8.04%.<sup>53</sup> Therefore, as endorsed by the Commission, I&E’s CAPM analysis confirms the reasonableness of I&E’s 8.46% DCF calculation. Additionally, in *UGI Utilities, Inc. – Electric Division*, the Commission rejected the other models used by Valley in developing its recommended ROE, i.e., the Risk Premium (“RP”) method and Comparable Earnings (“CE”) method.<sup>54</sup>

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<sup>49</sup> Valley Main Brief, p. 52 (citing *UGI Utilities, Inc. – Electric Division*, p. 105).

<sup>50</sup> *UGI Utilities, Inc. – Electric Division* p. 105 (emphasis added).

<sup>51</sup> See I&E Main Brief, pp. 28-31.

<sup>52</sup> *UGI Utilities, Inc. – Electric Division*, p. 104; See also I&E Main Brief, p. 28, fn. 98 (citation of Commission decisions validating use of the DCF as the primary methodology to determine ROE).

<sup>53</sup> I&E Main Brief, pp. 30-31.

<sup>54</sup> *UGI Utilities, Inc. – Electric Division*, p. 105.



Valley criticizes I&E for “maintain[ing] an unreasonably narrow focus on replying primarily on the DCF and considering only the CAPM as a check”.<sup>55</sup> However, as explained above, this methodology has been expressly endorsed by the Commission. Instead, Valley’s Main Brief reiterates the methods Company witness Dylan D’Ascendis used to develop his DCF, CAPM, RP and CE positions.<sup>56</sup> As explained above, and fully in I&E’s Main Brief, use of these rejected RP and CE methodologies,<sup>57</sup> in addition to unorthodox modifications to DCF and CAPM analyses,<sup>58</sup> should be disregarded as inaccurate, unreliable, and inconsistent with Commission precedent.<sup>59</sup>

Abandoning a methodological ROE analysis completely, Valley points to non-jurisdictional and irrelevant metrics for other companies’ ROEs to support its claim. First, Valley claims I&E’s recommended ROE is below any major electric utility followed by Regulatory Research Associates since at least 1980.<sup>60</sup> This statement is completely unsupported by any evidence in the record. Valley ROE witness D’Ascendis

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<sup>55</sup> Valley Main Brief, p. 70.

<sup>56</sup> Valley Main Brief, pp. 54-64. Valley goes on to criticize I&E for not adopting its various methodologies, which, as explained in I&E’s Main Brief, were rejected. Valley Main Brief, pp. 65-77; See I&E Main Brief, pp. 31-45.

<sup>57</sup> See I&E Main Brief, pp. 34-40. Valley incorrectly asserts the Commission’s decision in *UGI Utilities, Inc. – Electric Division* validated use of a Comparable Earnings analysis. Valley Main Brief, p. 76. To the contrary, the Commission expressly rejected UGI Electric’s use of the CE method. *UGI Utilities, Inc. – Electric Division*, p. 105.

<sup>58</sup> Specifically, use of an inappropriate risk-free rate and ECAPM for the CAPM analysis, and reference to market-to-book ratios with regard to the DCF analysis. See I&E Main Brief, pp. 40-45. Additionally, I&E objected to the proxy group Valley used for its DCF analysis. See I&E Main Brief, pp. 32-34.

<sup>59</sup> The Company again claims the Commission incorporated multiple models into its authorized ROEs in *Pa. P.U.C. v. Emporium Water Company*, Docket No. R-2014-2402324 (Order Entered January 28, 2015) (“*Emporium Water*”) and *Pa. P.U.C. v. The Columbia Water Company*, Docket No. R-2013-2360798 (Order Entered January 23, 2014) (“*Columbia Water*”). See Valley Main Brief, p. 66. As explained in I&E’s Main Brief, in *Columbia Water*, the Commission specifically states that it used the DCF method as the foundation in determining the cost of equity, and in *Emporium Water*, the Commission simply summarized the recommendations presented by OCA, I&E, and Emporium Water and did not comment on which model(s) it relied on for its ROE determination. I&E Main Brief, p. 37.

<sup>60</sup> Valley Main Brief, p. 53.

simply cites “Source of Information: Regulatory Research Associates” for this claim.<sup>61</sup> There is no specific cite or data attached to Valley witness D’Ascendis’s testimony. Second, Valley cites past higher ROE awarded to various Commission regulated companies.<sup>62</sup> However, Valley has provided absolutely no analysis why these ROEs are germane to Valley’s ROE claims here. As Valley recognizes, “market conditions may change”<sup>63</sup> and comparison to ROEs awarded to companies a decade ago should not be allowed to carry weight without any analysis. Although UGI Electric was awarded a 9.85% ROE in 2018, this amount also included a 1.20% downward adjustment to remove a size adjustment completely and a five basis points performance factor adjustment. If a similar adjustment was made to the Company’s ROE claim, Valley would only be awarded a 9.40% return on equity (10.60% - 1.20%).

Last, Valley cites the Commission-approved 10.00% Distribution System Improvement Charge (“DSIC”) ROE for gas utilities as a reason why I&E’s recommended return on equity is deficient.<sup>64</sup> I&E avers comparison to the Commission’s standard DSIC ROE for gas utilities is inappropriate for several reasons. First, citation to this standard is completely divorced from any of the various analyses parties have used in developing their respective positions. The Commission should not abandon parties’ analyses just to look at a generic standard that has no relevance to the specific facts in this record. Second, the 10.00% ROE is developed in a different context than Valley’s

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<sup>61</sup> Valley Statement No. 2-R, p. 5.

<sup>62</sup> Valley Main Brief, pp. 69-70. Specifically, 11% to Aqua Pennsylvania, Inc. in 2008; 10.40% to PPL Electric Utilities Corporation in 2011; and 9.85% to UGI Electric in 2018.

<sup>63</sup> Valley Main Brief, p. 70.

<sup>64</sup> Valley Main Brief, p. 53.

ROE in this proceeding. As Valley witness D'Ascendis correctly recognizes, DSIC is only designed to recover costs on specifically defined capital improvements between rate cases.<sup>65</sup> The Commission's most recently performed Quarterly Earnings Summary Report states the current market indicated ROE ranges between 7.90% and 10.63% for gas utilities.<sup>66</sup> I&E suggests the Commission sets the DSIC rate at a higher level of market indicated returns to incentivize utilities to undertake critical infrastructure projects.<sup>67</sup> By contrast, simply awarding the DSIC rate at the high end of the Commission's DCF analysis<sup>68</sup> in a base rate proceeding would provide an elevated ROE to all elements of the rate base, not just critical infrastructure projects.<sup>69</sup> Therefore, utilities should not simply expect the DSIC rate to serve as a substitute for a base rate ROE analysis. Further, as PUC Commissioner Andrew Place recently stated regarding the Quarterly Earnings Report of Jurisdictional Utilities,<sup>70</sup> the standard DSIC ROE for gas utilities suffers flaws. Specifically, although the DSIC ROE for gas utilities is 10.00%, the DCF analysis for gas utilities only indicates a ROE of 9.27%, with one

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<sup>65</sup> Tr. 57-59.

<sup>66</sup> *Bureau of Technical Utility Services Report on the Quarterly Earnings of Jurisdictional Utilities for the Year Ended June 30, 2019*, Docket No. M-2019-3013392, p. 14 (November 14, 2019) ("Quarterly Earnings Summary Report").

<sup>67</sup> 66 Pa. C.S. §§ 1350, et seq.

<sup>68</sup> The Quarterly Earnings Summary Report explains "[t]he Commission consistently uses the DCF model to determine the appropriate cost of equity for utilities". Quarterly Earnings Summary Report, p. 16.

<sup>69</sup> Relatedly, although the Public Utility Code mandates a utility's DSIC cost of equity match its litigated cost of equity within a two-year period, the reverse is not true. 66 Pa. C.S. § 1357(b)(2). In a base rate proceeding, a company can demonstrate why its proposed ROE is justified, including by reference to any infrastructure projects. I&E avers Valley has not provided any particular evidence why any of its infrastructure projects justify an elevated ROE.

<sup>70</sup> *Statement of Commissioner Andrew G. Place*, Docket No. M-2019-3013392 (November 14, 2019) ("Commissioner Place Statement").

standard deviation of 7.90% to 10.63%.<sup>71</sup> A 10.00% ROE is at the upper end of the Commission's DCF analysis, and Commissioner Place recommended its adjustment downwards. Additionally, the CAPM analysis only produces a 8.46% ROE.<sup>72</sup> Commissioner Place also cites a decline to national rate case ROEs and a "financially supportive, low risk regulatory environment in Pennsylvania" to indicate the Commission's DSIC rate for gas utilities is overstated. In summary, Valley reliance on the Commission's DSIC rate to support its separate ROE analysis should be disregarded as irrelevant and unreliable, and the Commission should accept I&E's specific DCF analysis, as checked by a CAPM analysis.

## **B. Return on Common Equity – Equity Adjustments**

### **1. Size Adjustment**

Valley maintains the Commission "must" include a size adjustment of 100 basis points and claims a body of evidence supports its position.<sup>73</sup> To support its position, Valley cites one Commission Order from 2007 where a size adjustment was allowed.<sup>74</sup> Valley then reiterates its position, including reference to non-utility specific technical literature.<sup>75</sup> However, as explained in I&E's Main Brief, in *UGI Utilities, Inc. – Electric Division* the Commission recently rejected use of technical literature not specific to the

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<sup>71</sup> Commissioner Place Statement, p. 1.

<sup>72</sup> Commissioner Place Statement, p. 1.

<sup>73</sup> Valley Main Brief, p. 85.

<sup>74</sup> Valley Main Brief, pp. 85-86 (citing *Pa. P.U.C. v. PPL Gas Utilities Corp.*, Docket No. R-00061398, p. 105 (Order Entered February 8, 2007)). In this one proceeding, the Commission awarded a 31 basis point upwards adjustment to PPL Gas Utilities Corporation's ROE. *Id.*, pp. 107-108.

<sup>75</sup> Valley Main Brief, pp. 86-88.

regulated utility industry to support a size adjustment.<sup>76</sup> Additionally, I&E presented technical literature demonstrating a size effect for utilities does not exist,<sup>77</sup> and Valley did not provide sufficient evidence to the contrary. As explained in I&E's Main Brief, the study Valley presented to rebut I&E's technical literature is speculative and, at best, applicable only to water utilities. Valley witness D'Ascendis also admits his own study has limited explanatory power.<sup>78</sup> Therefore, for the reasons stated herein and in I&E's Main Brief, the Commission should find Valley has not justified its claim for a size adjustment to its return on equity.

## **2. Management Performance**

Valley maintains its management performance merits a 25 basis point increase to return on equity.<sup>79</sup> As explained in I&E's Main Brief, Valley should not be awarded additional basis points simply for performing what is required to provide adequate, efficient, safe, and reasonable service.<sup>80</sup> Therefore, I&E continues to recommend a 25 basis point performance factor increase be disallowed.

## **VIII. TAXES**

As explained in I&E's Main Brief, I&E's various recommendations have a flow-through impact on the Company's taxes for the FPFTY as depicted in Table I attached therein.

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<sup>76</sup> *UGI Utilities, Inc. – Electric Division*, p. 100.

<sup>77</sup> *See* I&E Main Brief, p. 46.

<sup>78</sup> *See* I&E Main Brief pp. 47-48.

<sup>79</sup> Valley Main Brief, pp. 81-84.

<sup>80</sup> I&E Main Brief, p. 53.

## **IX. CUSTOMER RATE STRUCTURE**

### **A. Allocated Cost of Service Study**

Valley did not provide a cost of service study.<sup>81</sup>

### **B. Revenue Allocation**

As explained in Main Brief, I&E accepts Valley's proposed revenue allocation.<sup>82</sup>

### **C. Rate Design**

I&E has no tariff structure recommendations.

### **D. Scale Back**

In Main Brief, Valley accepted I&E's proportional scale back recommendation.<sup>83</sup>

### **E. Summary**

As explained in Main Brief, the Company's revenue allocation and I&E's scale back proposals are based on sound Commission ratemaking policies and precedent and should be adopted.

## **X. MISCELLANEOUS ISSUES**

### **A. Reporting Requirements**

The Company opposes I&E's recommendation that it provide updated schedules to the Commission reflecting actual capital expenditures, plant additions, and retirements for the FTY and FPFTY.<sup>84</sup> The Company states the information can already be found in

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<sup>81</sup> As explained in I&E's Main Brief, only rate filings proposing increases in excess of \$1 million must be accompanied by a cost of service study. 52 Pa. Code § 53.53.

<sup>82</sup> I&E Main Brief, pp. 50-51.

<sup>83</sup> Valley Main Brief, p. 92; See I&E Main Brief, pp. 51-52.

<sup>84</sup> Valley Main Brief, pp. 93-94.

the Annual Reports and quarterly updates while the rate case is pending.<sup>85</sup> As a threshold matter, I&E notes Valley is raising this point for the first time in Main Brief, thereby depriving I&E of its ability to provide an expert witness response on the factual basis for its contention. Therefore, the Commission should disregard Valley's late-brought assertion that other filing requirements address I&E's recommendation. Nonetheless, I&E avers its recommendation aligns with the test year of the Company in a form consistent with the rate filing, providing an apples-to-apples comparison of what the Company is projecting and what actually will be in the plant. Additionally, if Valley contends that its Annual Reports provide similar information, I&E avers it is therefore even less of a burden to repurpose this information into a form directly corresponding to a schedule provided in the rate filing.<sup>86</sup>

Additionally, the Company reiterates its position that it should not be required to provide reporting while rules and regulations regarding use of the FPFTY are pending.<sup>87</sup> As explained in I&E's Main Brief, current lack of detailed standardized rules and regulations regarding use of the FPFTY should support, rather than discourage, this sort of reporting requirement.<sup>88</sup> Indeed, many other utilities have agreed to the exact same reporting requirements under consideration.<sup>89</sup> Therefore, I&E continues to recommend the Company provide the reporting requirements as outlined in Main Brief.<sup>90</sup>

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<sup>85</sup> Valley Main Brief, p. 93.

<sup>86</sup> Quarterly reports end upon close of a rate case proceeding, and therefore would not satisfy I&E's reporting recommendation. *See* 52 Pa. Code § 53.56.

<sup>87</sup> Valley Main Brief, pp. 93-94.

<sup>88</sup> I&E Main Brief, pp. 71-72.

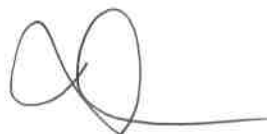
<sup>89</sup> *See* I&E Main Brief, p. 71, fn. 242.

<sup>90</sup> I&E Main Brief, pp. 69-70.

## XI. CONCLUSION

For the reasons explained herein and in I&E's Main Brief, Valley has failed to bear its burden of proof with respect to each and every element of its proposed rate increase. The Company's proposal must be amended to reflect the necessary and appropriate adjustments proposed by the Bureau of Investigation & Enforcement fixed utility financial analyst and engineer witnesses. Therefore, the Bureau of Investigation & Enforcement respectfully requests the Administrative Law Judges and the Commission to adopt its recommendations in this proceeding, which include adjustments and modifications as supported herein and in I&E's Main Brief, and as reflected in I&E's tables attached to I&E's Main Brief.

Respectfully submitted,



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Dated: January 22, 2020



**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket No. R-2019-3008209
	:	
Valley Energy, Inc. –	:	
Supplement No. 49 to Tariff Electric – Pa.	:	
PUC No. 2	:	

**CERTIFICATE OF SERVICE**

I hereby certify that I am serving the foregoing **Reply Brief** dated January 22, 2020, 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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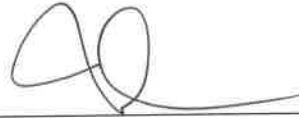
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