BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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

REPLY BRIEF OF VALLEY ENERGY, INC.

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Pa. PUC v. PPL Electric Utilities Corporation, Docket No. R-2012-2290597, *et al*., (Order entered December 28, 2012 (*PPL 2012 Order*)

Pa. PUC v. UGI Utilities, Inc. – Electric Division, Docket No. R.2017-2640058 (Order Entered October 25, 2018)

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52 Pa. Code § 53.52(a), (b), and (c)

52 Pa. Code § 53.56

52 Pa. Code § 59.48

66 Pa. C.S. § 315(e)

66 Pa. C.S. § 523

Act of February 14, 2012, Pub. L. 72, No. 11

I. INTRODUCTION[1]

On July 1, 2019, Valley Energy, Inc. ("Valley" or "Company") filed with the Pennsylvania Public Utility Commission ("PUC" or "Commission") Supplement No. 49 to Tariff Gas-Pa. PUC No. 2 ("Original Supplement No. 49"), proposing an annual increase in revenue of $1,034,186. In support of this filing, Valley submitted a Statement of Reasons, the supporting information required by 52 Pa. Code § 53.52(a), (b), and (c), and various other information.

On July 29, 2019, Valley filed a revised Supplement No. 49 ("Supplement No. 49") modifying the proposed revenue increase to $834,497. *See* Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1 (R).

In its Rebuttal Testimony, Valley subsequently revised its proposed revenue increase to approximately $745,000, reflecting rate of return, expense, and rate base adjustments to the as-filed request. Valley Statement No. 1-R, Exhibit__(HSG-1R2), Schedule C1 (R).[2]

On January 8, 2020, Valley filed a Main Brief in support of its proposed $745,000 revenue increase. On the same date, Valley received Main Briefs from the Commission's Bureau of Investigation and Enforcement ("I&E"), Office of the Consumer Advocate ("OCA"), and Office of Small Business Advocate ("OSBA").

II. SUMMARY OF ARGUMENT

The Main Briefs received from OCA, I&E, and OSBA generally restate each party's positions on the rate base, revenue, expense, rate design and rate structure issues as addressed in Valley's Main Brief. This Reply Brief will further respond to the arguments advanced in parties'

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[1] A complete procedural history of the case was provided in the Company's Main Brief and is incorporated by reference as if stated herein. Additionally, any terms undefined in this Reply Brief shall be understood to have the meanings defined in the Company's Main Brief.

[2] In its Rebuttal Testimony, Valley provided an updated Schedule C1 showing adjustments to present and proposed revenue, rate base and rate of return. *See* Valley Statement No. 1-R, (Exhibit__HSG-1R2), Schedule C1 (R). At this time, all other schedules remain unchanged from the July 29, 2019 filing.

Main Briefs by referencing the applicable responses in Valley's Main Brief and identifying additional record evidence in support of Valley's positions.

III. ISSUES RESOLVED AMONG ALL PARTIES

Valley's Main Brief reviewed several issues resolved among all parties. The I&E and OCA Main Briefs generally affirmed the agreements recounted in the Valley Main Brief, including parties' agreements on Materials & Supplies, Customer Deposits, and EDIT. *See* I&E Main Brief at 8; *see* OCA Main Brief at 8-10. OCA further accepted the Company's adjustment to increase direct labor and overhead expenses to reflect the hiring of a Corrosion Technician in October 2019. *See* OCA Main Brief at 9-10. Lastly, OCA accepted Valley' adjustment to direct labor expense for an employee short-term disability absence. *See id.* at 10. No other party commented on these adjustments. As such, Valley will not further address these matters in this Reply Brief.

With regard to Construction Work in Progress ("CWIP"), OCA's Main Brief noted a partial agreement among the parties but clarified a remaining point of dispute. OCA recognized that Valley accepted the OCA and I&E proposals to remove CWIP from rate base for the FPFTY. *See* OCA Main Brief at 18; *see also* I&E Main Brief at 9. However, OCA correctly observed that Valley conditioned its removal of CWIP from the FPFTY plant in service instead of the end-of-year plant in service. *See* OCA Main Brief at 18; *see also* Valley Main Brief at 12. OCA argues that CWIP should be removed from rate base regardless of the Commission's resolution of the disputed FPFTY rate base calculation. *See* OCA Main Brief at 18. The merits of OCA's position on CWIP will be addressed in Section IV.D, *infra*.

IV. RATE BASE

A. DISPUTED ISSUES

As indicated above, the parties concur on most rate base items raised in this proceeding. The rate base disputes are limited to OCA's adjustments to reflect plant retirements, OCA's

proposal to calculate FPFTY plant in service and accumulated depreciation using average rate base instead of end-of-year rate base, and the parallel proposal to remove CWIP from the FPFTY. Regarding plant retirements, OCA proposes two parallel adjustments that do not materially impact the rate base calculation developed by the Company. More substantively, OCA continues to defy the Commission's established precedent in arguing that plant in service and accumulated depreciation should be calculated based on the average FPFTY plant-in-service balance. This position ultimately translates into OCA's inability to accept the Company's reasonable condition to remove CWIP from rate base only if the Commission reaffirms its decision to rely on end-of-year plant in service. These positions should be denied for the reasons set forth in the Company's Main Brief and further addressed herein.

B. ORIGINAL COST UTILITY PLANT IN SERVICE

1. Adjustments for Plant Retirements

OCA proposes to adjust the Company's calculations of plant in service and accumulated depreciation to reflect plant retirements. *See* OCA Main Brief at 17. As stated in the Company's Main Brief, these adjustments do not materially impact the Company's rate base claim. *See* Valley Main Brief at 16. Accordingly, the Company recommends approval of its plant in service and accumulated depreciation claims without modification.

2. End-of-Year vs. Average Rate Base Methodology

In its Main Brief, OCA continues to ask the Commission to completely reverse its findings from *Pa. PUC v. UGI Utilities, Inc. – Electric Division*, Docket No. R-2017-2640058 (Order Entered October 25, 2018) ("UGI Order") and calculate the Company's rate base by averaging the beginning-of-test-year and end-of-test-year plant balances. All of the arguments, cases, policies, and analysis presented in support of OCA's position were exhaustively considered by the

Commission in its UGI Order, which has now been affirmed by the Commonwealth Court. Further, OCA's arguments cannot overcome the plain language of the Act of February 14, 2012, Pub. L. 72, No. 11 ("Act 11") explicitly clarifying that Act 11 constitutes an exemption to the general "used and useful" limitation on rate base. Accordingly, the Commission should reject OCA's attempt to re-litigate the precise issue so recently disposed of in the UGI Order.

In its Main Brief, OCA cites to a then-pending appeal to justify its continued opposition to the Commission's determination in the UGI Order. The arguments OCA offers in support of its proposed average rate base methodology mirror the arguments set forth in the UGI Order. These arguments, including the OCA's reliance on an isolated precedent from the Illinois Commerce Commission, were rejected by the Commission. UGI Order at 25-26.

Additionally, on January 15, 2020, the Pennsylvania Commonwealth Court entered an Order affirming the UGI Order and dismissing OCA's appeal. *McCloskey v. Pa. Pub. Util. Comm'n* (Pa. Cmwlth., No. 1549 C.D. 2018, filed January 15, 2020) (a copy of the slip opinion is attached as Attachment A.) The Court concludes:

> The Commission reviewed this language and concluded, within its particular expertise in the complex statutory scheme that is the [Public Utility] Code [citation omitted], that a year-end methodology could be applied to the FPFTY for UGI's rate case. This interpretation is supported by Section 315(e)'s plain language, but also by the purposes of Act 11, which were to mitigate the risks of regulatory lag and to aid in the resolution of the aged and aging nature of Pennsylvania's utility infrastructure.

Id. at 26. As such, there exists no basis for further consideration of OCA's proposed average rate base methodology.

While the Company submits that OCA's proposal should be rejected outright due to affirmation of the UGI Order, Valley alternatively requests that the Commission again deny OCA's proposed average rate base methodology on the merits. The Company's Main Brief reviewed the

myriad of flaws invalidating OCA's proposed methodology for calculating the FPFTY rate base. Valley Main Brief at 18-22. Chief among them is OCA's failure to accept the plain language in the Act. No party to this proceeding disputes that the Commission has historically used end-of-year plant in service to determine rate base for the FTY. *Id*. As a result, the General Assembly's decision to authorize use of the FPFTY by paralleling the language developed to implement FTY contradicts OCA's effort to limit end-of-year plant in service to the FTY and require average plant in service for the FPFTY.

C. ACCUMULATED DEPRECIATION

Consistent with its proposal to adjust the Company's rate base by calculating the average plant in service throughout the FPFTY, the OCA proposed to adjust the Company's claim for accumulated depreciation of $16,499,533 for FPFTY. Valley Main Brief at 21.

As addressed in the Company's Main Brief, the distinction between OCA's position and the Company's position on accumulated depreciation flows directly from the two parties' different approaches to calculating the original-cost plant in service. Consistent with its Main Brief recommendation, as stated above, the Company contends that original-cost plant in service should be calculated based on the FPFTY year-end balance, consistent with the Commission's holding in the UGI Order.[3]

D. CONSTRUCTION WORK IN PROGRESS

As referenced above, Valley accepted OCA's proposal to eliminate CWIP from the FPFTY calculation but conditioned such acceptance on the Commission's rejection of OCA's proposal to

[3] On this basis, the OCA's adjustment to accumulated depreciation also must be rejected. However, if the Commission reduces the Company's claim for original-cost plant in service, there should be a commensurate reduction in accumulated depreciation as well.

calculate rate base and accumulated depreciation based on average FPFTY plant in service instead of the end-of-test-year data. *See* Valley's Main Brief at 12. OCA rejects this condition and alleges that CWIP should be removed from the FPFTY even if the Commission adopts its proposal to use the average FPFTY plant in service to set the Company's rate base and accumulated depreciation. OCA Main Brief at 25-27.

To support this argument, OCA alleges "that it is not appropriate to include CWIP in rate base either using an end of test year or the average rate base test year method because *in either case, the plant item will not be completed and placed in service during the FPFTY*." OCA Main Brief at 19 (emphasis added). This statement reinforces the Company's argument because OCA's proposal to use average plant in service to calculate rate base and accumulated depreciation would exclude the plant that *will be completed and placed in service during the FPFTY*. *See* Valley Main Brief at 12. The same principle underlying OCA's adjustment of CWIP contradicts its proposal to use an average rate base method. Accordingly, the Company's proposal that inclusion of CWIP should be permitted only if the Commission rejects the end-of-test-year method for rate base and accumulated depreciation is reasonable and should be conditionally accepted.

E. CONCLUSION FOR RATE BASE CALCULATION

For the reasons fully explained above, the rate base adjustments proposed by OCA should be rejected.

V. REVENUES

Among the parties, only OCA opposes the Company's revenue projections for the FPFTY. I&E Main Brief at 11; OSBA Main Brief at 5; OCA Main Brief at 19-20. OCA proposes an alternative revenue calculation that increases Valley's projected revenue at present rates by $141,561, thereby decreasing the revenue increase in this proceeding. OCA Main Brief at 20. As

detailed in Valley's Main Brief, OCA offers no support for its proposed departure from Mr. Gorman's revenue analysis. OCA's proposed revenue calculation relies on limited sales data, fails to apply a monthly regression, and provides no explanation for OCA witness Mierzwa declining to weather-normalize sales data for various customer classes. Valley Main Brief at 27. As explained in detail in the Company's Main Brief and summarized below, Mr. Mierzwa failed to fully support his proposed methodology or identify any flaws in the Company's revenue projection. As a result, his unsupported proposal should be rejected by the Commission.

As explained in the Company's Main Brief, Mr. Mierzwa did not identify any flaws in the Company's analysis, which Mr. Gorman described as a "typical regression analysis that you would do for a sales forecast." *Id.* at 27. Rather, Mr. Mierzwa simply substituted his own forecast. *Id.* However, Mr. Gorman identified many flaws in OCA's analysis, including: 1) relying on a single year of sales data; 2) aggregating the usage over the full year instead of the well-supported approach of using a monthly regression; and 3) inexplicably omitting certain classes from weather normalization. *Id.* at 26-27.

OCA provides no explanation for Mr. Mierzwa's rejection of Company witness Mr. Gorman's supported and prudent revenue calculation. *Id.* at 27. The Company's Main Brief reviewed Mr. Gorman's critique that Mr. Mierzwa's reliance on only on a single year of sales data and failure to apply a monthly regression will not capture the customer usage variation necessary to generate reliable data. *See id.* at 27. Additionally, Mr. Mierzwa weather-normalizes sales only for the Residential and Commercial rate classes, but offers no basis for using unadjusted data for the remaining customer classes. *Id.* at 26. To the contrary, Mr. Gorman extensively described the correlation between Heating Degree Data ("HDD") days and gas usage for each and every non-Interruptible gas schedule, to support his weather normalization adjustments. *See id.* at 25-26.

OCA provides no explanation for rejecting Mr. Gorman's prudent and supported weather normalization adjustments for customers other than Residential or Commercial customers. *Id.*

The Company's revenue proposal is reasonable and based on a thorough, well-established methodology. Because OCA has neglected to support its proposed sales and revenue projections or to identify any flaws in the Company's analysis, the Commission should reject OCA's adjustments and approve the Company's proposal.

VI. EXPENSES

As recounted in the Company's Main Brief, Valley developed expense proposals to recover expenses necessary to provide service to its customers and to earn a fair rate of return on the investment and plant used and useful in providing service. *Butler Township Water Co. v. Pa. PUC,* 81 Pa. Cmwlth. 40, 43-44, 473 A.2d 219, 221 (1984) *("Butler Township"). See also T.W. Phillips Gas and Oil Co. v. Pa. PUC,* 81 Pa. Cmwlth. 205, 474 A.2d 355 (1984). In their Main Briefs, I&E and OCA convert the standard into an overly narrow bookkeeping exercise that runs contrary to the practical operations of smaller public utilities. For the reasons set forth in the Company's Main Brief and further discussed below, the Commission should approve the Company's expense claims, including approval of the 3% inflation adjustment for FPFTY O&M expenses.

A. COMPANY PROPOSAL

1. OCA is Incorrect, the Company's Inflation Adjustment is a Reasonable and Appropriate Means of Projecting FPFTY Expenses

OCA's Main Brief asks the Commission to deny the Company's proposed 3% inflation adjustment for FPFTY O&M expenses on the grounds that it is not consistent with Section 315 of the Public Utility Code. *See* OCA Main Brief at 21, 24. OCA also alleges that the 3% inflation

adjustment is an inappropriate calculation and should be modified if the Commission determines any inflation adjustment to be appropriate. *See id.* at 24.

The Company's Main Brief extensively addressed the legal basis for the 3% inflation adjustment, referencing the Commission's prior approval of inflation adjustments in two Pennsylvania-American Water Company rate cases. *See* Valley Main Brief at 38. OCA argues that these cases are not applicable because they predate Act 11 and inflation adjustments were only applied to residual expenses. OCA Main Brief at 22-23. The Company agrees that the circumstances of its proposed inflation adjustment differ due to the intervening passage of Act 11. However, Valley submits that the Commission's prior approval of inflation adjustments for residual expenses in FTY cases supports the Company's proposal to apply a similar adjustment to FPFTY O&M expenses where specific expense increases cannot be determined at the time the rate case is prepared. *See* Valley Main Brief at 38.

With regards to OCA's claim that the 3% calculation is an inappropriate measure of inflation for ratemaking purposes, the Company's Main Brief extensively reviewed the empirical basis for the proposed 3% inflation adjustment developed from the Producer Price Index ("PPI") and supported by the Company's historical year-to-year O&M expense escalations, projected expense increases, and budgeted 2020 expenses. *See id.* at 36-40. All of these indicators support the Company's conservative claim that overall O&M expenses will increase by *at least* 3%. *See id.* at 36-40. However, if the Commission denies the Company's proposed 3% inflation adjustment, the Commission should approve OCA's alternative inflation adjustment of 2.1% based on the Gross Domestic Product-Price Index ("GDP-PI"). *See* OCA Main Brief at 24. To accept OCA's primary position, rejection of any inflation adjustment, would assume no cost increases for

the Company's O&M expenses from the FTY to the FPFTY. This is not only inaccurate and unrealistic; it is contrary to the purpose of the FPFTY as established in Act 11.

2. The Company's Primary Proposal to Approve the Claimed FPFTY Expenses Based on the Annualized FTY Data Should be Approved

I&E characterizes the Company's use of annualized FTY data to support the FPFTY expense claim as an attempt to "wholesale revise its O&M position in rebuttal testimony." *See* I&E Main Brief at 13. This argument grossly misconstrues the Company's testimony. The Company reviewed the YTD FTY expenses both at the 6-month mark (as of June 30, 2019) and at the 9-month mark (as of September 30, 2019) and provided the annualized information in Rebuttal Testimony to show support for its O&M expense claim. *See* Valley Main Brief at 31. It is incorrect for I&E to state this information should have been introduced in direct testimony when the updated 9-month data was not available when the Company filed its Direct Testimony on August 2, 2019.

Moreover, the Company's rationale does not render intervenor challenges meaningless as claimed by I&E, but instead addresses the operations of smaller utilities. For smaller utilities, labor and overhead comprise the majority of the Company's O&M expenses. *See* Tr. 201. Mr. Rogers explained that Valley's labor and overhead costs compose 65% of its total O&M expenses. *See id.*

The Company's Main Brief described the significant differences in staffing between smaller public utilities and their larger counterparts, as smaller public utilities generally do not have a specific team of employees assigned to tasks in specific accounts, but rather allocate work for all O&M accounts across a small base of employees. *See* Valley Main Brief at 35. As a result, employee activities and costs are incurred to support a variety of accounts or portions of accounts that can differ from the accounts anticipated when the budget was prepared based on operational needs. *See id.* at 41. If the Company were to manage every expense to meet the line item budget,

the unintended consequence would be to remove operational flexibility. If the I&E's proposals are accepted, it would penalize the Company for efficient and effective workforce management.

I&E is also incorrect that the Commission's approval of the Company's proposal would handicap intervenor review of rate proposals from larger public utilities. *See* I&E Main Brief at 14. As the entire basis of the Company's proposal derives from the Company's smaller size, approval of the Company's O&M recommendation would not be precedential for larger public utilities. The evidence submitted by Valley is Company-specific.

The Commission's role in evaluating a rate case is <u>not</u> to ensure that it achieves a desired percentage decrease to the as-filed request. The Commission's role is to set rates that allow the utility to recover its reasonable and prudently incurred expenses. *Pa. PUC v. National Fuel Gas Distribution Corp.,* 54 Pa. PUC 401, 416-417, 40 (1980). This requires the Commission to evaluate the circumstances of the particular utility, which may vary from the other utilities that the Commission regulates. It is contrary to the public interest to reduce a small utility's O&M expense claim because costs shift between O&M expense accounts during the year in comparison to original allocations or because expenses may be concentrated in particular quarters (like the 3rd or 4th). Valley is providing ratepayers with the benefit of reducing its ROE claim based on the most up-to-date financial data. It should be afforded the flexibility to support its O&M expense claim as it has done.

The Company submits that under the circumstances presented in this proceeding, its proposal to approve the FPFTY expense claim based on annualized O&M FTY expense and the 3% inflation adjustment is reasonable and should be approved.

B. COMPANY RESPONSE TO SPECIFIC EXPENSE ADJUSTMENTS

As stated above, the Company believes its primary proposal to approve its FPFTY expense claim based on annualized FTY O&M expense plus the 3% inflation adjustment is reasonable. To the extent the Commission disagrees, the Company responds to the specific expense adjustments proposed by the Advocates as set forth below.

1. Rate Case Expense – Normalization Period

I&E and OCA proposed adjustments to the Company's recommended rate case normalization period based on pure historical rate case filing dates. I&E proposed a normalization period of 48 months based on the Company's last three base rate case filings and OCA proposed 60 months, based on the average time between the Company's last four rate case filings including the present case. I&E Main Brief at 24; OCA Main Brief at 31.

The Company's Main Brief provided clear evidence that a filing gap since the Company's 2010 rate case is an anomaly due to revenues from a very large contract customer. *See* Valley Main Brief at 41-43.[4] It is extremely unlikely that this situation will recur, *i.e.* that another similarly sized large customer will enter the service territory. *See id.* Consistent with the Commission's recent affirmation in the UGI Order that rate case expense normalization period "may be based on future expectations," the Company's proposed 36-month normalization period should be approved. *See* Valley Main Brief at 42 *citing* UGI Order at 59-60.

[4] Valley witness Gorman explained that Valley's filing intervals for the last three rate cases have been "33 months, 36 months, and 110 months." Valley Statement No. 1-R at 7. Valley CEO Rogers explained the abnormal circumstances contributing to the extended 110-month stay out since the 2010 rate case, which are "not likely to recur following this rate case." Valley Main Brief at 43.

(cont'd footnote)

2. Industrial/Commercial Meters and Regulators Operations Expense (Account No. 876)

The Company's claim for Account No. 876 is $73,475. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 at 2. OCA proposed to disallow $9,429 of the Company's claim based on the Company's annualized FTY costs as of September 30, 2019.[5] OCA Main Brief at 25-26.

As explained in the Company's Main Brief, Valley typically incurs approximately 30% of its expense for Account No. 876 in the 4th quarter of each year, which means that even if the Company annualizes the actual FTY costs incurred as of September 30, 2019, the Company's expense would be understated. *See* Valley Main Brief at 43. The Commission should, therefore, approve the Company's claim without modification.

3. Meters and House Regulators Operating Expense (Account No. 878)/Meter Reading Expense (Account No. 902)

Company projects total cost of Account No. 878 will be $172,563 and projects the total cost of Account No. 902 will be $99,668. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 2, 4.

For Account No. 878, OCA recommends disallowance of $33,736 based on a 3-year average for 2016 to 2018, resulting in a recommendation of $138,827. OCA Main Brief at 27. For Account No. 902, OCA points to June 30, 2019 YTD information to argue that Account No. 902 was not on track to reach projections; consequently, OCA proposes a disallowance of $12,847 for a total $86,821. *Id.* at 30.

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[5] OCA initially proposed a $15,730 adjustment claiming that Valley provided no evidence showing that higher materials and labor expenses occurring over the HTY would recur in the FTY of FPFTY. Valley Main Brief at 43. Later, OCA revised its proposed adjustment to $9,429 based on the Company's annualized FTY costs as of September 30, 2019. *Id.*

Although OCA generally acknowledges that the Company's explanation that employee hours are shifted between accounts to work on various projects, OCA proposed adjustment does not recognize the direct connection between Account Nos. 878 and 902. *Id.* at 27-28. As explained in the Company's Main Brief and in Rebuttal Testimony, work shifted from Account No. 878 to Account No. 902. However, OCA proposes significant adjustments to *both* Account No. 878 ($33,746) and Account No. 902 ($12,847) with inconsistent methodologies – essentially creating a double disallowance. *Id.* at 27, 30.

As of September 30, 2019, Account No. 902 was tracking $15,272 below FTY projections. Valley Main Brief at 44-45; Valley Statement No. 1-R at 5. This closely parallels the increased costs observed for Account No. 878, which was tracking $14,010 above FTY projections as of September 30, 2019. *See id*. Read together, both accounts are tracking closely to the Company's projected FTY expenses. Accordingly, the Commission should deny the OCA's proposed adjustments to both accounts.

4. Customer Installations (Account No. 879)

The Company projects an FPFTY expense of $132,269 for Account No. 879. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 2. OCA acknowledges that overhead cost can vary from year to year and recommends a 3-year average of Account No. 879 expenses to take into account increased maintenance cost that may occur. *Id.* at 27. Based on the 3-year average of 2016-2018, OCA recommends a reduction of $17,933 for a total allowance of $117,396 for customer installations. *Id.*

OCA's recommendation should be rejected as unsupported. First, in Direct Testimony, OCA witness Sherwood acknowledged that the vast majority of the HTY to FTY increase – $13,352 – is due to a 3% increase in wages effective January 1, 2019. However, OCA does not

explain why this $13,352 should be disallowed. Additionally, the actual expenses for Account No. 879 are tracking *ahead* of projections for the FTY, based on FTY costs as of September 30, 2019. Valley Main Brief at 33.

For these reasons, OCA's adjustment should be denied, and the Company's expense claim should be accepted.

5. Mains Operating Expense (Account No. 887)

The Company's filing included a claim of $98,308 for Mains expense. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 2. In its Main Brief, OCA proposes an adjustment of $1,219 based on an expense Valley witness Rogers indicated may be related to a single purchase. OCA Main Brief at 29.

As stated on Main Brief, if the Commission declines to accept Valley's expense claim based on annualized the FTY total O&M expense based on September 30, 2019 data, Valley will accept this adjustment. Valley Main Brief at 45.

6. Customer Records & Collection Expense (Account No. 903)

The Company projects total Account No. 903 expenses to be $513,237, a 10% increase over the two years from the HTY to the FPFTY. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 4; OCA Main Brief at 30-31. Valley cites increasing benefits and payroll expenses as the basis for this increase. OCA Main Brief at 31. OCA proposes to disallow $32,977 of this claimed expense by allowing only 3% overhead cost increases from the HTY to the FTY and removing the 3% inflation adjustment from FTY to FPFTY. *Id.* at 31. OCA argues that YTD overhead data as of June 30, 2019 supports its adjustment.

Company-wide overhead expenses will increase during 2019 and particularly in 2020 due to the Corrosion Technician hired in October 2019, as that position was not accounted for in the

FTY budget. Valley Main Brief at 3, 32, 34. OCA did not oppose the expense adjustments to reflect the hired Corrosion Technician. OCA Main Brief at 9-10. While overhead YTD data within Account No. 903 is tracking lower than projected as of the first half of 2019, any adjustment should be made in conjunction with the increased FPFTY expense of the Corrosion Technician. Accordingly, the Company submits that OCA's adjustment to Account No. 903 be accepted only on the condition that the FPFTY expense adjustment for the Corrosion Technician is also accepted.

7. Miscellaneous Customer Expense (Account No. 905)

The Company's claim for Account No. 905 is $24,449, a 17% reduction from the HTY to the FPFTY. OCA Main Brief at 32-33. OCA proposes an $8,267 adjustment for an IT backup system expense in 2018 that it claims should have been accepted. *Id.* OCA's adjustment should be rejected.

First, OCA has provided no evidence that the $8,267 expense is non-recurring in future years. Even assuming that the HTY $8,267 expense should have been capitalized in 2018, OCA's proposal fails to consider that Account No. 905 is running *ahead* of budget for 2019. The Company respectfully requests that the Commission deny OCA's adjustment to Account No. 905.

8. Administrative and General Salaries (Account No. 920)

For Account No. 920, the Company projects an expense of $536,697. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 4. OCA disagrees with the projected increase to the overhead portion of this expense. OCA Main Brief at 33. Valley cites increasing benefits costs for this increase. *Id.* OCA proposes to disallow $76,645 of this claimed expense by allowing only 3% overhead cost increases from the HTY to the FTY and removing the 3% inflation adjustment from FTY to FPFTY. *Id.* OCA argues that YTD overhead data as of June 30, 2019 supports its adjustment. *Id.*

Even if the Company's claim is adjusted to reflect YTD FTY expenses, OCA's proposal would still understate the allowance for Account No. 920. OCA Main Brief at 33-34. The YTD expense as of September 30, 2019 is tracking $56,277 below the Company's original projection (inclusive of the 3% inflation adjustment). Valley Main Brief at 33. It is unclear why OCA relies on June 30, 2019 data when September 30, 2019 data is available. There is no basis for OCA's reliance on stale expense data to support its $76,645 adjustment.

Additionally, as explained above in Section VI.B.6, *supra*, Company-wide overhead expenses are projected to increase beyond the annualized numbers due to the Corrosion Technician hired in October 2019, a position that was not in the FTY budget. Valley Main Brief at 3, 32, 34. OCA did not oppose the expense adjustments to reflect the hired Corrosion Technician. OCA Main Brief at 9-10. Therefore, any adjustment to the Company's claim for Account No. 903 should be based on the annualized FTY YTD expense as of September 30, 2019, and accepted and only on the condition that the FPFTY expense adjustment for the Corrosion Technician is also accepted, to account for general increases to overhead expense that were not accounted for in the FTY budget.

9. Office Supplies and Expense (Account No. 921)

The Company's claim for Account No. 921 is $74,701. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 4. In its Main Brief, OCA proposes a $19,510 adjustment based on a claim that the travel and training component of total Account No. 921 costs are projected to increase by 54% from the HTY and that the actual costs incurred through the first 6 months of the FTY. OCA thus proposes that the travel and training costs within Account No. 921 should be adjusted based on HTY costs and the remainder of the costs should be adjusted based on FTY levels.

OCA's adjustment should be denied for several reasons. First, Valley witness Rogers explained that the Company's claim is reasonable because Valley will incur ongoing training costs both to onboard new employees and "to address increasing regulatory obligations for certified Operators and employee training for continually evolving human resources issues." Valley Main Brief at 46; Valley Statement No. 4-R at 9. Second, OCA's proposal reflects only FTY expense as of June 30, 2019, with no recognition of the Company's updated FTY expenses as of September 30, 2019, which track significantly closer to budget. OCA Main Brief at 34-35; *see* Valley Main Brief at 46. At a minimum, even using OCA's own methodology, OCA's $19,988 adjustment should be reduced to $12,969 to reflect more recent YTD projections. *See* Valley Main Brief at 46.

Accordingly, the Commission should approve the Company's claim, or alternatively, modify OCA's adjustment as set forth above.

10. Regulatory Commission Expense (Account No. 928)

The Company's claim for Regulatory Commission Expense was $172,563. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 4. I&E proposes to disallow this claim, averring that Valley claims the Regulatory Commission Expense both as expense and taxes other than income taxes. I&E Main Brief at 14-15.

If the Commission denies the Company's primary proposal to accept its FPFTY expense claim based on the FTY annualized expense, the 3% inflation factor and the additional expense adjustments described in Ms. Levering's testimony, the Company will accept this adjustment. Valley Statement No. 5-R at 4-5.

11. General Advertising Expense (Account No. 930)

Valley's filing included a claim for General Advertising Expense of $73,373. Valley Statement No. 1, Exhibit__(HSG-1), Schedule C1-1 (R) at 4. OCA proposes a disallowance of $3,889 of the Company's claim on grounds that Valley's claimed expense improperly included volunteer labor costs. OCA Main Brief at 35.

As explained in the Company's Main Brief, volunteer expenses benefit Valley's customers by contributing to a productive and engaged workforce. Valley Main Brief at 47; Valley Statement No. 4 at 10. Valley CEO Rogers testified to the benefit to ratepayers in Direct Testimony, stating that the programs "foster happy, healthy, and fulfilled employees, which helps to reduce turnover and to increase employee productivity." *Id.* Mr. Rogers testified that this increased productivity "benefits ratepayers through better service." *Id.* OCA's adjustment should be denied.

12. C&T Allocation Expense

The Company's FPFTY expense claim includes $233,608 for allocated expenses for shared services from C&T. *See* I&E Statement No. 1, Exhibit No. 1, Schedule 9, at 1.[6] In its Main Brief, I&E recommends a disallowance of $44,429 of the Company's claim because the projected increase from the HTY to the FTY exceeds the historical annual increases for this expense item.

I&E's recommendation should be rejected. First, the Company's historical annual expense exceeds the annualized YTD data for 2019. *See* I&E Statement No. 1, I&E Exhibit No. 1, Schedule 9, at 1. Second, anticipated future trends also support approval of the Company's claim for C&T Allocation Expense. As discussed by Company witness Levering, the C&T Allocation is based on the revenue and meter counts for Valley and its affiliated operating companies. *See* I&E

[6] Notably, the Company's C&T Allocation Expense claim for the FPFTY represents an exception from the Company's proposal to increase FTY expense by the 3% inflation adjustment, as Valley applied a 1% increase from FTY costs based on historical increases to its C&T allocation. Valley Main Brief at 47; *see also* I&E Statement No. 1, Exhibit No. 1, Schedule 9 at 1.

Statement No. 1, Exhibit No. 1, Schedule at 1. As revenue and meter counts determine the C&T Allocation Expense, the Commission should consider that the first phase of the East Athens Main Extension project was not scheduled for completion until November 2019. *See* I&E Statement No. 3, Exhibit No. 3, Schedule 2 at 4 (showing 2019 East Athens Main Extension projects to be completed between November 2019 and June 2020). Accordingly, the YTD expense as of September 30, 2019 for C&T Allocation Expense does not reflect additional customers in East Athens anticipated to begin service before the end of the FTY and throughout the FPFTY.

Considering the Company's historical C&T Allocation Expense and the anticipated increased allocation due to expansion in East Athens, I&E's disallowance should be denied.

13. Uncollectible Expense

Valley claims $55,430 for Uncollectible Expense, which reflects the Company's total projected Uncollectible Expense for the FPFTY of $100,799 minus the commodity portion of Uncollectible Expense ($45,369) to be unbundled for recovery through the GCR. Valley Main Brief at 49; *see also* Valley Statement No. 1, Exhibit__(HSG-1), Schedule C4 (R) at 4.

I&E proposes to disallow $24,201 of Valley's claim for an approved amount of $31,229. I&E Main Brief at 17-18. I&E calculated the three-year average of Valley's write-off percentage (0.62%) and multiplied it by the FPFTY present rate revenues, proposing to apply the 0.62% write-off ratio to any final base rate increase approved in this proceeding. *See id.* I&E's methodology likely understates the Company's write-off percentage in the FPFTY, for two reasons. First, the Company's recent experience for the HTY was a 0.83% write-off percentage. *See* Valley Main Brief at 49. Second, while I&E looks only at the prior 3 years, I&E's Uncollectible Accounts Expense in the two years immediately prior – 2014 and 2015 – were also higher than I&E's

proposed average. *See* I&E Statement No. 1, Exhibit No. 1, Schedule 6 at 1. For these reasons, the Company's Uncollectible Expense claim is prudent, and I&E's adjustment should be denied.

OCA recommends that uncollectible accounts (bad debt reserve) be adjusted based on the Company's approved revenue requirement and projected sales at the conclusion of this case. As a placeholder, OCA witness Sherwood used the Company's requested revenue requirement and calculated an adjustment of $51,403 to Account No. 904. OCA Main Brief at 32; OCA Statement No. 1, Schedule SLS-10. OCA's uncollectible calculation is based on the erroneous premise that the Company claimed $100,799 of uncollectible expense. *See* OCA Main Brief at 31. As explained above, the $100,799 reflects both commodity and distribution uncollectible expense, prior to the unbundling of commodity related uncollectible expense ($45,369). *See* Valley Statement No. 1, Exhibit__(HSG-1), Schedule C4 (R) at 4. As such, the Company's FPFTY claim for uncollectible expense of $55,430 is appropriate and should be accepted by the Commission.

C. CONCLUSION

For the reasons identified above, the various disallowances to the Company's expenses proposed by the other parties in this proceeding should be rejected, and the Company's total expenses should be accepted and included in base rates.

VII. FAIR RATE OF RETURN

A. RATE OF RETURN STANDARDS

In their respective Main Briefs, both OCA and I&E continue advocating for Commission approval of returns on common equity that would eviscerate the principal benchmarks for a fair rate of return set forth in *Bluefield Water Works & Improvement Company v. P.S.C. of West Virginia*, 262 U.S. 679 (1923) (*"Bluefield"*) and affirmed by *Federal Power Commission v. Hope Natural Gas.,* 320 U.S. 591, 603 (1944) (*"Hope")* and *Duquesne Light Co. v. Barasch,* 488 U.S.

299 (1989). The Advocates' efforts to drive Valley's return to industry-wide lows should be rejected.

The Commission should also note that the Company's proposed ROE reflects updated market data available as of September 30, 2019. While OCA and I&E vehemently criticize the Company for updating O&M expense data, neither party expressed such concerns with regards to the Company's updated ROE, presumably because the updates reduced the Company's recommended ROE from 11.35% to 10.60%. *See* Valley Main Brief at 56. The Company's willingness to proactively adjust its recommended ROE to reflect the most current available market data irrespective of the result should be considered in assessing the reasonableness of the Company's overall ROE/rate of return recommendations and the Company's overall recommended revenue requirement.

B. GAS PROXY GROUP

OCA accepted Company witness Mr. D'Ascendis' updated gas proxy group of 6 companies. OCA Main Brief at 50. However, I&E applied different selection criteria than Mr. D'Ascendis. As discussed below, I&E's objections do not merit modification of Mr. D'Ascendis' selection criteria or results. The Commission should accept the 6-company proxy group ("Gas Utility Proxy Group") set forth on page 4 of Mr. D'Ascendis' Rebuttal Testimony. *See* Valley Main Brief at 51.

To support its proposed proxy group, I&E alleges in its Direct Testimony that it uses more current information than Mr. D'Ascendis. I&E Main Brief at 34. However, as noted in Valley's Main Brief, Mr. D'Ascendis updated his proxy group in Rebuttal testimony based on data available as of September 30, 2019. *See* Valley Main Brief at 51; *see also* Joint Statement No. 2, Exhibit__(HSG-1R), Schedule DWD-1R. Accordingly, Mr. D'Ascendis' proxy group is based on the most current data and should be accepted by the Commission.

C. COST OF COMMON EQUITY

1. The Opposing Parties' Unprecedented and Unreasonable Common Equity Recommendations Must Be Rejected

In their Main Briefs, both I&E and OCA request Commission approval of demonstrably unreasonable ROEs of 8.46% and 8.34% respectively. I&E Main Brief at 26; OCA Main Brief at 39. In doing so, both Advocates attempt to discredit the Company's application of other ROE models to address limitations of the DCF model under current market conditions. These arguments conflict with Commission precedent affirming the DCF as the Commission's preferred model but also acknowledging the Commission's willingness to consider other models when the DCF produces unreasonable results. Additionally, both I&E and OCA ignore evidence from the Company demonstrating that consideration of DCF-only results would require higher ROEs than the 8.46% and 8.34% recommendations.

a. The I&E and OCA ROE Proposals are Objectively Unreasonable

The Company's Main Brief reviewed various objective benchmarks illustrating the unreasonableness of the I&E and OCA ROE recommendations. The Company pointed to Mr. D'Ascendis testimony comparing the I&E and OCA recommendations to historic utility ROEs, noting that Commission approval of either I&E's or OCA's proposed ROE would subject Valley to an allowed ROE below any ROE awarded to a major electric utility in the nation according to Regulatory Research Associates ("RRA"), a division of Standard and Poor's ("S&P"). Valley Main Brief at 69. The ROEs recommended by the Advocates also fall well below ROEs granted to investor-owned public utilities by the Commission in recent years, including the 9.85% ROE approved for UGI Utilities, Inc. – Electric Division in October 2018. *See Id.* at 69-70. As further discussed below, the I&E and OCA recommended ROEs also fall below the ROE developed by the Commission in calculating the 10.00% ROE applicable for the gas Distribution System

Improvement Charge ("DSIC") if the NGDC's last rate case settled without an explicit ROE. *Id.* at 53.

The benchmarks collectively reveal the critical flaw in the Advocates' ROE position to be a lack of judgment and market awareness. While both I&E and OCA commit technical errors as well, their results suffer from an unwillingness to observe the core tenet of *Bluefield,* which is that Valley is entitled to a fair return based on what investors would demand from an enterprise of similar risk.

b. <u>I&E and OCA Place Undue Reliance on DCF Results</u>

Both the I&E and OCA Main Briefs emphasize the Commission's historic reliance on the DCF model as the primary analysis for determining utility ROEs in support of their ROE recommendations. *See* I&E Main Brief at 35-36; *see also* OCA Main Brief at 46-47. In doing so, I&E and OCA fail to appropriately consider the Commission's clarification that the DCF is not an immutable model. As detailed in the Company's Main Brief, Mr. D'Ascendis presented thorough evidence affirming that DCF results in the current market environment will understate the return demanded by investors, which the Advocates failed to credibly rebut. *See* Valley Main Brief at 66-68. Accordingly, Mr. D'Ascendis' reliance on multiple models is appropriate for this proceeding.

The Company acknowledges the Commission's historical preference for the DCF model but avers that the arguments from OCA and I&E unreasonably downplay flaws affecting the reasonableness of DCF results and overstate flaws impacting other models. I&E and OCA reference various Commission precedents and aver that the Commission relies on DCF results over other models. *See* I&E Main Brief at 35-36; *see* OCA Main Brief at 46-47. While the Commission has expressed a preference for reliance on the DCF, it has not hesitated to reference other

methodologies where a DCF-only analysis would produce unreasonable outcomes. As stated in the Valley Main Brief, the Commission declared in its UGI Order that "where evidence based on other cost of equity models indicates that the DCF-only results may understate the utility's cost of current equity capital, we will consider those other methods, to some degree, in evaluating the appropriate range of reasonableness for our equity return determination." Valley Main Brief at 66.

In addition to reiterating its responsibility to consider other models where a DCF-only analysis would produce unreasonable results, the Commission has issued ROE determinations developed in reliance on multiple models. I&E attempts to deny this reality and claims Valley witness Mr. D'Ascendis is incorrect in claiming the Commission relied on multiple ROE models in the recent *Columbia Water* and *Emporium Water* rate cases.[7] *See* I&E Main Brief at 37. A review of the cases belies I&E arguments. For example, in *Columbia Water* OCA recommended an ROE of 9.10% based on the midpoint of its DCF and CE analyses, I&E recommended an 8.89% return based on its DCF analysis, and the company recommended a 10.30% ROE based on its DCF, RP, and CAPM analysis and a 0.75% size adjustment. *Columbia Water* at 35. The Commission noted its consideration of "cost models presented" and awarded a 10.00% ROE. *See id.* Both the Commission's language and the end result strongly indicate that the Commission gave considerable weight to the company's multiple-model analysis in that case.

In this case, the Company offered compelling evidence showing that the DCF results will understate the appropriate ROE in the current market environment. Valley witness Mr. D'Ascendis relies on both his own analyses and corroborative financial literature affirming that relationship between market-to-book ratios and DCF results, including the following analysis from Dr. Morin:

[7] *See Pa. PUC v. Emporium Water Company,* Docket No. R-2014-2402324 (Order Entered January 28, 2015); *see also The Columbia Water Company,* Docket No. R-2013-2360798 (Order Entered January 23, 2014).

> *The third and perhaps most important reason for caution and skepticism is that application of the DCF model produces estimates of common equity cost that are consistent with investors' expected return only when stock price and book value are reasonably similar, that is, when the M/B is close to unity.* As shown below, application of the standard DCF model to utility stocks understates the investor's expected return when the market-to-book (M/B) ratio of a given stock exceeds unity. This was particularly relevant in the capital market environment of the 1990s and 2000s where utility stocks were trading at M/B ratios well above unity and have been for nearly two decades. The converse is also true, that is, the DCF model overstates that investor's return when the stock's M/B ratio is less than unity. *The reason for the distortion is that the DCF market return is applied to a book value rate base by the regulator, that is, a utility's earnings are limited to earnings on a book value rate base.*

See Joint Statement No. 2 at 10-11 (emphasis added). I&E does not dispute the underlying premise that market-to-book ratios for electric utilities significantly exceed unity, (*i.e.* a market-to-book ratio of 1.0) but alleges that this relationship should not impact the Commission's analysis because investors are aware that regulators assess utility returns based on book value. *See* I&E Main Brief at 44-45. Other than a conclusory statement from its witness with no reference to financial literature or empirical analysis, I&E offers no support for its assertion that the Commission should disregard the impact of higher market-to-book ratios on the reasonableness of DCF results.

OCA responds to the Company's market-to-book analysis by presenting a litany of caselaw addressing leverage adjustments.[8] OCA Main Brief at 64-66. Notably, as confirmed at the evidentiary hearing, Mr. D'Ascendis has not proposed a leverage adjustment in this proceeding. Tr. 48. Rather, Mr. D'Ascendis proposed that the Commission acknowledge the current environment where market-to-book ratios significantly exceed unity as a limitation on the reasonableness of DCF results. This is consistent with the Commission's finding in the 2012 PPL

[8] OCA cites to various caselaw from other jurisdictions addressing the relationship between market to book ratios in the context of proposed leverage adjustments. OCA Main Brief at 65-66. The Company submits that the Commission has addressed market to book ratios and leverage adjustments in numerous dockets such that the OCA's non-contextual references to decisions from other state regulatory commissions are of questionable persuasive value and should be given no weight.

rate case cited by OCA, where the Commission declined to grant a leverage adjustment to compensate for risk related to PPL's market-to-book ratio, but also clarified that this decision was made "in the context of our determination, *supra,* of a reasonable return of equity for PPL of 10.28%." *See* OCA Main Brief at 65. The 10.28% ROE set in the 2012 PPL case was *higher* than the 8.38% - 9.69% range of DCF results calculated by I&E, OCA, and the utility in that proceeding. *Pennsylvania. Pub. Util. Comm'n v. PPL Electric Utilities Corp,* Docket No. R-2012-2290597 (Order entered December 28, 2012) at 82 ("PPL 2012 Order"). Similarly, Mr. D'Ascendis references the current market-to-book ratios not as support for a leverage adjustment to his DCF results, but as evidence of the necessity to reference other models due to the potential for DCF results to produce unreasonable results when market-to-book ratios exceed unity.

c. **<u>Even Consideration of DCF-Only Results Would Not Support the I&E and OCA ROE Recommendations</u>**

In criticizing the Company's reliance on multiple ROE methods and supporting their historically low proposed ROEs, I&E and OCA overlook the fact that their recommendations are unreasonable even under a DCF-only analysis. I&E's ROE recommendation is based on the average growth rates of its proxy group while OCA uses a median growth rate. *See* I&E Main Brief at 30; *see* OCA Main Brief at 53. As discussed in the Company's Main Brief, the Commission's calculation of the DSIC ROE supports the Company's contention that I&E and OCA significantly understate the appropriate ROE. *See* Valley Main Brief at 77, 81. Specifically, in the most recent Quarterly Report publishing the DSIC ROE on November 14, 2019, the Commission considered results within a standard deviation of the midpoint and set the DSIC ROE at the higher end of that range. *See id.; see also* Tr. 45. While this result would understate the risk profile of the Company due to its size and overlook consideration of management effectiveness, it serves as yet another objective indication that the I&E and OCA recommendations are untenable

and would severely understate the ROE necessary to ensure the Company has an opportunity to earn a reasonable return.

d. <u>I&E's Criticisms of the Company's Non-DCF ROE Models Have Been Thoroughly Rebutted</u>

I&E offers numerous critiques of the CAPM, RP/PRPM, and non-price regulated proxy group ROE analyses performed by the Company. I&E Main Brief at 34-45. The factual assertions underlying I&E's arguments were addressed and rebutted in the Company's Main Brief. *See* Valley Main Brief at 70-77. Additionally, the Company will address certain points herein.

I&E criticizes the CAPM model as generally subject to manipulation and further rejects the Company's CAPM analysis for reliance on growth projections through 2030, use of the 30-year Treasury Bond as the applicable growth rate, and reliance on an ECAPM analysis.[9] I&E Main Brief at 34-45. With regards to I&E's position that the CAPM is uniquely subject to manipulation, the Company's Main Brief explained that all ROE models can be manipulated by poor inputs, including the DCF. *See* Valley Main Brief at 71-72. The Company's Main Brief also noted that I&E's observation that projections out to 2030 are unreliable is completely arbitrary. *See id.* at 73. I&E provides no empirical analysis explaining why its 5-year projection should be deemed reliable, but the Company's 10-year projection should be rejected. *See* I&E Main Brief at 40-41. To the contrary, the Company supported its position by explaining that the source relied on by both I&E and the Company, Blue Chip Financial Forecasts, projects interest rates out to 2030. *See* Valley Main Brief at 73. As this information is available to investors, I&E's assumption that this published interest rate data is not relevant to the CAPM growth forecast conflicts with basic

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[9] I&E's Main Brief references the Company's use of growth rate projections extending out to 2029. *See* I&E Main Brief at 40. This forecast was updated in the Company's Rebuttal Testimony to extend out to 2030, consistent with the available forecast data. *See* Valley Main Brief at 61.

economic principles assuming that investors rely on all publicly available information. *See* Valley Main Brief at 73-74.

The Company's Main Brief also addressed I&E's opposition to using the 30-year Treasury Bond as the CAPM growth rate. *See* Valley Main Brief at 72-73. The Company acknowledged that the Commission previously accepted the 10-year Treasury Note as the appropriate CAPM growth rate in its UGI Order, but encouraged the Commission to reconsider this finding based on the extensive financial literature cited by Mr. D'Ascendis in support of matching the long-term risk-free rate to the long-term nature of utility operations. *See* Valley Main Brief at 72. I&E's representation that the September 18, 2019, Federal Open Market Committee reduction to the target range for the federal funds rate only underscores I&E's misconception that the risk-free rate for utility investments should reflect short-term market conditions. *See* I&E Main Brief at 41-42. Rather, as evidenced by the Company's review of financial literature, "[b]ecause common stock is a long-term investment and because the cash flows to investors in the form of dividends last indefinitely, the yield on very long-term government bonds, namely, the yield on 30-year Treasury bonds, is the best measure of the risk-free rate for use in the CAPM…" *See* Valley Main Brief at 72. Additionally, Mr. D'Ascendis' updated analysis, incorporating data available as of September 30, 2019, would have reflected the Federal Open Market Committee meeting. *See* Joint Statement No. 2-R at 3.

I&E's final critique of the Company's CAPM analysis rejects any reliance on the ECAPM based on a completely unsupported assertion that the ECAPM "merely adds a measure of subjectivity" to the CAPM. *See* I&E Main Brief at 43. I&E presents no coherent analysis to which Valley can respond. By way of contrast, the Company reviewed financial literature explaining

that the traditional CAPM assumes an overly steep predicted Security Market Line that is corrected by the empirical Security Market Line in the ECAPM. *See* Valley Main Brief at 65-66.

The Company also rebutted I&E's criticism of the PRPM model. I&E opposes any reliance on the PRPM for being: (1) an indirect measure of the cost of equity; and (2) available only through proprietary software. *See* I&E Main Brief at 37-38. As confirmed in the Company's Main Brief, both claims are false. Company witness Mr. D'Ascendis explained that the PRPM model directly measures the risk-return relationship and cited to financial literature explicitly stating the PRPM estimates risk "*directly* from asset pricing data." *See* Valley Main Brief at 74-75 citing Joint Statement No. 2-R at 39 (emphasis added). The Company's Main Brief also clarified that while Mr. D'Ascendis used proprietary software, he also made his workpapers available to all parties in this proceeding. *Id.* at 75. Mr. D'Ascendis also confirmed that the PRPM model can be run on free software. *See Id.*

Similarly, the arguments offered by I&E in opposition to the Company's analysis of non-price regulated companies ignores the record evidence presented in the Company's Main Brief. I&E argues that the Company has not demonstrated that the non-price regulated companies have risk profiles similar to Valley solely because the ROE models show higher returns when applied to the non-price regulated proxy group. *See* I&E Main Brief at 38-39. This is a textbook Catch-22 as the only way this standard could be met is if the non-price regulated companies showed returns equal to the Company's Gas Utility Proxy Group, which would also render the analysis superfluous. While the Commission has expressed concerns that comparisons to non-price regulated companies involves a degree of judgment, the selection criteria employed by Mr. D'Ascendis are highly specific, targeting companies with beta-coefficients and residual standard errors within plus or minus two standard deviations of the Gas Utility Proxy Group. *See*

Valley Main Brief at 76. As the selection criteria narrowly defines the proxy group risk profiles, these non-price regulated companies are similar in risk to the Gas Utility Proxy Group.

e. OCA's Proposed DCF and Hybrid CAPM/Risk Premium Models are Flawed

OCA's Main Brief presents its recommended 8.34% ROE based on the FERC 2-step DCF model, while additionally conducting flawed CAPM/Risk Premium analyses. OCA has failed to offer persuasive evidence supporting its proposed departure from the Commission's application of a traditional DCF analysis in favor of the FERC 2-step DCF model. Further, as observed in Valley's Main Brief, OCA's CAPM and Risk Premium analyses suffer from numerous flaws and are unsupported by financial literature.

As discussed in the Company's Main Brief, OCA conducts a reasonable constant growth analysis, but distorts these results by incorporating a FERC-2-step DCF designed to address the theory that company growth rates cannot sustainably exceed GDP. *See* OCA Main Brief at 51-52. Mr. D'Ascendis provided an example illustrating that any adjustment to the traditional DCF to account for GDP growth is a solution in search of problem as even the fastest growing industry sector would require thousands of years of sustained growth to overcome GDP. *See* Valley Main Brief at 78.

Additionally, FERC's ROE analysis relies on a CAPM model incorporating size adjustments and also applies a low-end outlier that eliminates DCF and CAPM proxy group results that fall below the yields of generic corporate Baa bonds + 20% of the CAPM risk premium. *See Ass'n of Bus. Advocating Tariff Equity, v. Midcontinent Indep. Sys. Operator, Inc.*, Opinion No. 569, 169 FERC ¶ 61,129 (2019) ("Opinion No. 569") at 52. To the extent the Commission considers OCA's proposal to incorporate FERC's 2-step DCF model, it should also reflect FERC's clear signal that DCF results alone are insufficient to determine just and reasonable ROEs.

The Company's Main Brief also observes that the CAPM analysis conducted by OCA is highly unorthodox and should be denied. While not evidently clear through OCA's references to use of a "time frame that includes the time frame he used in his DCF analysis," OCA's witness proposes to determine the CAPM risk-free rate based on the six-month average ending August 2019 instead of a forecast. *See* OCA Main Brief at 56. This proposal is contrary to the forward-looking nature of ROEs and should be rejected. *See* Joint Statement No. 2 at 56.

Mr. D'Ascendis also highlights numerous errors in the risk premium calculations applied to OCA's CAPM/Risk Premium model. Valley's Main Brief recounts that Mr. D'Ascendis identified several flaws invalidating Dr. Habr's reliance on two historical and two projected risk premiums. *See* Valley Main Brief at 79. First, Dr. Habr's historical market premium contradicts established financial literature disfavoring shorter term data series by calculating a historical risk premium based on U.S. Treasury bill returns from 1983 to 2018, compared to the Company's reliance on data from 1926 to 2018. *See* Joint Statement No. 2-R at 59. Second, the remaining three market risk premiums all rely on the S&P 500 index, but manipulate the data to remove non-dividend paying companies. *See id.* at 60. This adjustment excludes 19% of the S&P's market capitalization and thus distorts the results of these analyses. *See id.* at 61. At minimum, Dr. Habr should have removed the S&P non-dividend paying companies from the index used to calculate the beta-coefficients for the proxy group to preserve an appropriate correlation between the risk premiums and the proxy group companies. *See id.* at 61.

Finally, in attempting to defend its DCF and CAPM/Risk Premium models, OCA argues the Company's DCF, CAPM, and non-price regulated proxy group models are inappropriate. Specifically, OCA claims the Company's DCF model fails to account for long-term GDP growth, that the CAPM model incorrectly relies on a 30-year Treasury Bond growth rate, and non-price

regulated proxy group presents differing risk profiles compared to the Gas Utility Proxy Group. Other than long-term GDP growth, which is addressed in this Section, these arguments are addressed throughout the above responses to I&E's arguments. As set forth above, OCA's arguments have no merit and should be denied.

f. <u>Size Adjustment</u>

The I&E and OCA Main Briefs oppose the Company's proposed size adjustment. *See* I&E Main Brief at 45-48; *see* OCA Main Brief at 61-63. The Company fully addressed the concerns raised by the Commission in its UGI Order regarding utility-specific support for a size adjustment by presenting both technical literature and independent analysis affirming the reality that smaller utilities face considerable size risk. Valley Main Brief at 85-91.

Per the Company's Main Brief, I&E's efforts to discredit the existence of a size risk, the relevance of the size risk analysis from Dr. Zepp, and Mr. D'Ascendis' independent size risk analysis are not credible and should be disregarded. I&E first references an Ibbotson *Stocks, Bonds, Bills Inflation: 2015 Yearbook* ("SBBI Yearbook") showing year-to-year variance in returns for large and small-capitalization stocks listed on the NYSE, AMEX, and NASDAQ and argues that the fact that large capitalization stocks outperform small capitalization stocks at times refutes the existence of size risk. I&E Main Brief at 45-46. However, the very analysis cited by I&E also invalidates I&E's characterization of the study as a conclusive rebuttal to the existence of size risk, noting that the findings merely "led some market observers to *speculate* that there is no size premium." *See* I&E Main brief at 46 note 165 (emphasis added). More substantively, Mr. D'Ascendis points to the fact that Duff and Phelps bought the SBBI Yearbook from Ibbotson and continued publishing size premiums, which were referenced in this proceeding by both OCA and Company witnesses. *See* Tr. 51; *see* OCA Main Brief at 62; *see also* Joint Statement No. 2,

Exhibit__(DWD-1), Schedule DWD-8. The Company's reliance on published industry data affirming continued acceptance of size risk far outweighs I&E's reference to speculation among some unquantifiable observers in the industry.

I&E's suggestion that Dr. Zepp's study is irrelevant must also fail. The Company's Main Brief presented arguments affirming Dr. Zepp's study as an authoritative and utility-specific rebuttal to the flawed study conducted by Dr. Wong.[10] *See* Valley Main Brief at 88-89. With that argument addressed, I&E pivots to arguing that the Zepp article is not *electric utility* specific because it relies on data from water utilities. *See* I&E Main Brief at 47-48. This argument directly conflicts with I&E's reliance on the Commission's *City of DuBois – Bureau of Water* case to support its proposed ROE methodology. I&E Main Brief at 35. Rate of return fundamentals are uniform among water and natural gas utilities, as even the seminal *Bluefield* case addressed rate of return for a water utility. Accordingly, the Zepp article is a relevant and credible rebuttal to Dr. Wong's study.

Lastly, I&E's criticism of Mr. D'Ascendis' size study as having limited explanatory power ignores Mr. D'Ascendis' comments explaining his findings. Mr. D'Ascendis' utility size study produced an R-Squared value of 0.09, meaning that 9% of the change in risk is explained by size. *See* Valley Main Brief at 90. Mr. D'Ascendis' readily acknowledged that an R-Squared value of 0.09 would not ordinarily have strong explanatory power, but in this case, it exceeds the R-Squared value of the beta-coefficients used by the I&E and OCA in their CAPM analyses. *See* Tr. 50; see also Joint Statement No. 2-R at 36. In other words, Mr. D'Ascendis' study has significantly more explanatory power than commonly accepted risk measures, such as beta coefficients. I&E

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[10] The Commission should also note that I&E's claim that only utility-specific analyses are relevant to assessing size risk is entirely undercut by I&E's failed effort to refute the Company's size adjustment by referencing the non-utility specific 2015 Ibbotson SBBI. *See* I&E Main Brief at 46.

improperly emphasizes only Mr. D'Ascendis' general observation without reference to the context explaining that his study confirms the inverse relationship between utility size and risk.

OCA's criticism of the Company's market capitalization analysis based on the size premiums reported by Duff and Phelps is similarly misguided. *See* OCA Main Brief at 62-63. The Company's Main Brief reviewed Mr. D'Ascendis' market capitalization study, which calculated the market capitalization of the Company and the Gas Utility Proxy Group. Valley Main Brief at 87-88. Mr. D'Ascendis then referenced 2019 data from Duff and Phelps that calculates size premiums for ten deciles, each defined by a market capitalization range. Valley Main Brief at 90-91. Under this analysis, Valley ranked in the tenth size decile while the proxy group ranked in the fourth size decile, resulting in a size premium spread of 4.37%. Valley Main Brief at 87-88.

OCA claims that OLS (ordinary least squares) betas are the more relevant indicator of company size than the market capitalization referenced by Mr. D'Ascendis. *See* OCA Main Brief at 58. OCA presents 2017 data from Duff and Phelps that includes both the market capitalization and OLS betas for each of the ten size deciles. *See id.* at 62. OCA then finds that the gas proxy group has a similar OLS beta to the first size decile, which has a negative size premium.[11] *See id.* at 62-63. On that basis, OCA argues that any size adjustment should be negative. As stated in the Company's Main Brief, this argument defies logic since the relevant size premium justifying Mr. D'Ascendis' 100 basis point adjustment is not simply the size premium for the gas proxy group decile, but rather the *spread* between the size premiums for the Company's size decile and the gas proxy group size decile. *See* Valley Main Brief at 90-91. Even under OCA's analysis, the spread well exceeds 100 basis points and thus supports Mr. D'Ascendis' size adjustment.

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[11] The size premiums differ between the 2017 and 2019 data cited by OCA and the Company, but in both cases, only the first size decile is assigned a negative size premium. *See* OCA Main Brief at 62 *but see* Joint Statement No. 2, Exhibit__(DWD-1), Schedule DWD-8.

g. **<u>Performance Adjustment</u>**

I&E and OCA both oppose the Company's proposed performance adjustments based on nothing more than disagreement with the General Assembly's recognition that effective utility management merits a rate premium. I&E emphasizes that Section 523 of the Public Utility Code requires the Commission to consider a performance adjustment but does not compel the Commission to award one. *See* I&E Main Brief at 48-49. The Company agrees with this premise but notes that I&E and OCA also contradict the statute by averring that management effectiveness is its own reward and should not be recognized in rates. *See* I&E Main Brief at 48-49; *see also* OCA Main Brief at 63. This position is not consistent with the statute or Commission precedent.

The Commission has recognized the validity of performance adjustments and previously granted a 22-basis point performance adjustment to Aqua, Pennsylvania Inc., citing water quality and customer service among the qualifying factors. *See Pa. PUC et al. v. Aqua Pennsylvania Inc., Docket No.* R-00072711 (Order entered July 31, 2018) at 50. Accordingly, the Commission should dismiss the arguments of I&E and OCA opposing the principle of a performance adjustment and proceed to address the merits of whether Valley has performed above and beyond its regulatory obligations to merit a performance adjustment. For the reasons detailed in the Valley Main Brief, this question should be answered in the affirmative and the proposed 25-basis point performance adjustment should be accepted.

D. CONCLUSION AS TO RATE OF RETURN

The Company is entitled to the opportunity to earn a fair and reasonable return consistent with *Bluefield*. The ROE recommendations from I&E and OCA reflect both technical errors and misguided judgment. Determination of a reasonable rate of return requires not just review of the financial models, but also an understanding and appreciation for the economic signals impacting

investors and markets. Accordingly, the Commission should be wary of the I&E and OCA ROE recommendations falling below all objective ROE benchmarks, including its own DSIC ROE calculated simultaneously with the development of the record in this proceeding. Rather, the Commission should award ROEs that facilitate access to capital and support the Company's efforts to continue accelerating replacement of aging infrastructure and providing safe and adequate public utility service. To that end, the Commission should adopt the Company's proposed cost of common equity of 10.60%, which results in an overall rate of return of 7.72% after adjusting for the Company's unopposed capital structure and debt cost rate.

VIII. RATE STRUCTURE

A. REVENUE ALLOCATION

Valley proposed an across-the-board increase to all tariff rate schedules. The across-the-board increase reflects the unbundling of certain GCR-related costs. *See* Valley Main Brief at 92, 99.

No party opposes Valley's proposed revenue allocation. I&E Main Brief at 50-51; OCA Main Brief at 67; OSBA Main Brief at 6. Therefore, Valley requests that the Commission approve the Company's revenue allocation.

B. RATE DESIGN

Valley's proposed rate design reflects the across-the-board revenue allocation. *See* Valley Main Brief at 92. As with the revenue allocation, no party opposes Valley's proposed rate design. I&E Main Brief at 51; OCA Main Brief at 68; OSBA Main Brief at 6.[12] Therefore, Valley requests that the Commission approve the Company's revenue allocation.

[12] OCA clarified that the final customer charge should be increased by a percentage reflecting the Commission's final rate determination. OCA Main Brief at 68.

C. SCALE BACK

I&E, OCA and OSBA all proposed proportional scale backs. I&E Main Brief at 51-52; OCA Main Brief at 68; OSBA Main Brief at 6. I&E and OCA specified their position that the final customer charge should also reflect the Commission's final rate increase. I&E Main Brief at 52; OCA Main Brief at 68. Consequently, if the Commission approves a revenue requirement for Valley that is less than Valley's full requested increase, the Company proposes that rates for each class shall be scaled back in a proportional manner.

IX. MISCELLANEOUS ISSUES

A. REPORTING REQUIREMENTS

In its Main Brief, I&E accepts the Company's plant-in-service projections for the FTY and FPFTY, but argues that the Company should be ordered by the Commission to submit updates to Schedule C3 by April 1, 2020 (for the year ended December 31, 2019) and by April 1, 2021 (for the year ended December 31, 2020). I&E Main Brief at 52-54. I&E offers two primary arguments in support of its position. First, I&E states that such reporting requirements have been approved in other proceedings. *Id.* at 53-54. Second, I&E argues that lack of regulations, if anything, heightens the need for the reporting requirements. *Id.* at 54. The Company respectfully requests that the Commission reject I&E's arguments and decline to impose additional reporting requirements, for the following reasons.

First, the Commission has undertaken to develop FPFTY regulations through the ongoing FPFTY stakeholder process. Presumably, the ongoing FPFTY stakeholder process will result in a clear set of reporting standards to which the Company (and all EDCs) will be subject. As opposed

to this individual rate case, the stakeholder process is the ideal location for the Commission to gather input from a variety of stakeholders and issue a broadly applicable order.[13]

Similarly, the Company rejects I&E's argument that a lack of regulation should, in fact, result in additional burdens on Valley. As explained in its Main Brief, the Company submits numerous filings to the Commission each year, including Annual Reports that include detailed plant, expense, and sales data that the Commission and I&E can review. *See* Valley Main Brief at 93 *citing* 52 Pa. Code § 59.48. In addition, Commission regulations require quarterly updates while the rate filing is pending. *Id.* at 117 *citing* 52 Pa. Code § 53.56. Thus, year-end balances will be provided through other means. The Company urges the Commission to mitigate the regulatory burden on small utilities by denying I&E's mandatory reporting request.

B. TARIFF CHANGES

1. Valley's Proposed Updates to its Facilities Expansion Policy Benefit Customers and Should be Approved as Consistent with the Public Interest.

As part of the rate filing, Valley proposed several modifications to its Facilities Expansion Policy. Valley Main Brief at 96. I&E and OCA did not oppose Valley's proposed modifications. However, OSBA opposed Valley's proposal to implement a third method for calculating the Company's portion of service line extension costs. OSBA Main Brief at 7-11. OSBA contends that the Company's proposal violates cost causation principles, and also argues that: (1) the possibility of customers qualifying for different allowable investment levels is not inherently inequitable; (2) the proposed additional method for calculating the Company's contribution toward a line extension raises the Estimated Base Annual Revenue ("EBAR") credit; and (3) Valley's

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[13] *See, e.g., Pa. PUC v. Pennsylvania-American Water Co.*, Docket No. R-00932670 et al., 1994 Pa. PUC LEXIS 120 at *158 (Final Order entered July 26, 1994) (adopting the ALJ's conclusion that the issues raised by OCA were outside the scope of rate case and would be better addressed in a statewide rulemaking proceeding).

proposal is discriminatory and shifts costs. *Id.* at 9-11. However, as explained below, OSBA has failed to demonstrate its claims are accurate.

First, the Company's proposal addresses an unnecessary inequity inherent in the current tariff rule. As explained on brief, the average cost for 200 feet of service line or main extension for new installations over the 12-month period ending September 30, 2018 is $6,557. Valley Main Brief at 96. Under the current rule, a customer requiring a 200-foot extension costing $6,557 is entitled to a Company contribution, while a customer requiring a 300 foot extension costing a total of $6,400 is not entitled to receive a full allocated contribution amount for the footage over 200 feet. *Id.*[14] Valley proposes to add a third option addressing this inequity allowing for Company contributions for extensions *up to the average cost of 200 feet of service and/or main extensions.*[15] *Id.* at 96-97.

Second, OSBA offers no empirical analysis supporting the association between the 200 feet of service line or main extension and the EBAR from customers. As explained in its Main Brief, the Company's proposal preserves the same *upper limit on Company contributions*, which is the average cost of a 200-foot extension. Valley witness Rogers explained that, "Valley is proposing a third method that merely allows all customers to access, if needed, the same minimum

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[14] As stated by OCA witness Mierzwa:

> For example, Customer A, with a lower than average unit cost) of installation, may require a total of 250 feet of main/service line investment at a cost of, say, $6,500, or $26 per foot. Customer B, with a greater than average (unit cost) of installation, may require a total of 200 feet of main/service line investment at a cost of, say, $6,800, or $34 per foot. Under the Company's existing service extension policy, Customer B would not be required to pay a CIAC since the service extension does not exceed 200 feet. On the other hand, Customer A would be required to provide a CIAC equal to the cost to install facilities beyond 200 feet. Valley deems this outcome inequitable since Customer A is required to pay a CIAC even though Customer A's total cost of installation ($6,500) is less than the total cost to extend service to Customer B.

OCA Main Brief at 73; OCA Statement 4-R at 7.

[15] Under the Company's proposed tariff language, the average cost of main and/or service line extensions is calculated for each 12-month period ending September 30. *See id.* at 96-97.

dollar investment available to any customer with an average 200-foot extension." Valley Main Brief at 97. Addressing this same topic, OCA witness Mierzwa stated in Rebuttal Testimony that "it is unclear how Valley's proposal would effectively raise its existing EBAR credit." OCA Statement No. 4-R at 9.

Third, OSBA has presented no evidence demonstrating costs are shifted between classes. Clearly, individual new customers benefit by having a portion of their extension covered by other ratepayers. However, this occurs regardless of customer's class and is entirely consistent with the purpose of line extension policies, which provide system-wide benefits to all classes. *See* Valley Statement No. 4-R at 13. Further, it is consistent with policies approved in multiple other proceedings. OCA Main Brief at 74. As explained by OCA, other utilities have received approval for modifications to main extension policies to facilitate expansion of service. *Id.* In summary, the Company agrees with OCA witness Mierzwa's statement that "Mr. Kalcic has presented no evidence to indicate that the additional facility extension projects would not be cost-justified or uneconomic." OCA Statement No. 4-R at 9.

As indicated above, OCA supports Valley's proposal. OCA argues that Valley has met its burden of proof that the Company's proposal will provide a benefit to customers seeking to obtain access to low-cost natural gas in unserved and underserved areas within the Commonwealth. *See* OCA Main Brief at 74. OCA witness Mierzwa opines that Valley's proposal is consistent with the efforts of other NGDCs to promote the availability of natural gas to unserved and underserved areas. OCA Statement No. 4-R at 9.

In summary, OSBA's arguments are not persuasive when weighed against the public interest benefits derived from the Company's proposal. For the reasons set forth above, in the

Company's Main Brief, and in OCA's Main Brief, the Commission should approve Valley's proposed changes to its Facilities Extension Policy.

2. Valley's Proposed Updates to its Disconnection and Reconnection Fees are Reasonable and Should be Approved.

Valley proposed changes to its tariff to update its disconnection and reconnection fees by increasing the current fees by $10. Valley Main Brief at 98. The Company proposes to increase the fee for reconnections/disconnections completed during working hours from $25 to $35 and increase the fee for reconnections/disconnections completed outside of working hours from $30 to $40. *Id.*

OCA opposes Valley's proposed change. OCA Main Brief at 69-70. OCA argues that Valley has presented no evidence to show these fees are cost-based. *Id.* at 70. However, Valley CEO Ed Rogers explained in testimony that the fees were increased to account for 13 years of inflation. Testifying to the cost basis of the fee, Mr. Rogers explained that "an update is necessary to *reflect the reconnection cost in today's dollars*." Valley Statement No. 4 at 15 (emphasis added). Ten dollars is a reasonable increase for an inflation-based adjustment covering nearly 13 years. Consequently, Valley's proposed adjustments to the disconnection and reconnection fees are reasonable.

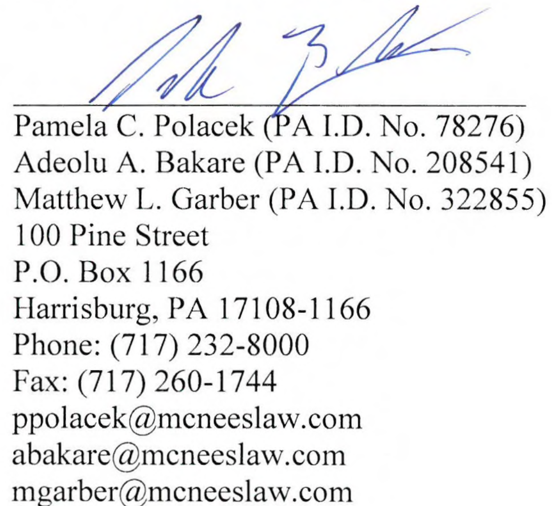
As mentioned on brief, OCA did not inquire further into the cost basis of Valley's proposed updates to these fees and did not present any evidence rebutting Mr. Rogers' testimony. Valley Main Brief at 98-99. Accordingly, the proposed fee updates should be approved.

X. CONCLUSION

WHEREFORE, Valley Energy, Inc. respectfully requests that the Pennsylvania Public Utility Commission approve the rate increase and other proposals set forth in Tariff-Gas PA. PUC No. 2.

Respectfully submitted,

McNEES WALLACE & NURICK LLC

By 

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Dated: January 22, 2020

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

Tanya J. McCloskey, Acting	:	
Consumer Advocate,	:	
Petitioner	:	
	:	
v.	:	No. 1549 C.D. 2018
	:	Argued: December 10, 2019
Pennsylvania Public Utility	:	
Commission,	:	
Respondent	:	

BEFORE: **HONORABLE RENÉE COHN JUBELIRER,** Judge
HONORABLE PATRICIA A. McCULLOUGH, Judge
HONORABLE ANNE E. COVEY, Judge

OPINION BY
JUDGE COHN JUBELIRER **FILED: January 15, 2020**

Before this Court is the petition for review of Tanya J. McCloskey, Acting Consumer Advocate (Office of Consumer Advocate (OCA)), challenging the October 25, 2018 Order of the Pennsylvania Public Utility Commission (Commission) that approved a general rate increase filed by UGI Utilities, Inc.-Electric Division (UGI), which OCA contends results in utility rates that are not just and reasonable. The Commission ultimately approved an annual revenue increase for UGI of $3.201 million, or 3.6%. Although the underlying general rate proceeding involved the litigation or settlement of numerous issues, the only issues remaining for our consideration are: whether Sections 315, 1301, and 1301.1 of the Public Utility Code (Code), 66 Pa. C.S. §§ 315, 1301, 1301.1, support UGI's

calculation of its rate base,[1] rather than OCA's calculation of that rate base, and whether the Commission's acceptance of UGI's calculations is supported by substantial evidence. OCA contends that the approved rates are inconsistent with the Code and the Commission's Decision is not supported by substantial evidence. The Commission, UGI, which has intervened, and the Energy Association of Pennsylvania (EAP), which has filed an *amicus curiae* brief in favor of affirmance, argue the Commission's determinations are supported by the plain language of Sections 315(e) and 1301.1(b) of the Code, the purpose of those statutory provisions, and the record.

I. Background

To better understand the nature of UGI's general rate proceeding, OCA's objections to UGI's proposed rate increase, and the Commission's Decision, we begin with some basic principles of ratemaking, the Commission's role in the ratemaking process, and changes to the ratemaking process made by the General Assembly in 2012 and 2016.

A. Ratemaking Under the Code

1. General Principles

Section 1301(a) of the Code mandates that "[e]very rate made, demanded, or received by any public utility . . . shall be just and reasonable, and in conformity with [the] regulations or orders of the [C]ommission." 66 Pa. C.S. § 1301(a). Pursuant to the just and reasonable standard, a utility may obtain "a rate that allows

[1] A utility's "[r]ate base" is "[t]he value of the whole or any part of the property of a public utility which is used and useful in the public service." Section 102 of the Code, 66 Pa. C.S. § 102.

it to recover those expenses that are reasonably necessary to provide service to its customers[,] as well as a reasonable rate of return on its investment." *City of Lancaster (Sewer Fund) v. Pa. Pub. Util. Comm'n*, 793 A.2d 978, 982 (Pa. Cmwlth. 2002). There is no single way to arrive at just and reasonable rates, and "[t]he [Commission] has broad discretion in determining whether rates are reasonable" and "is vested with discretion to decide what factors it will consider in setting or evaluating a utility's rates." *Popowsky v. Pa. Pub. Util. Comm'n*, 683 A.2d 958, 961 (Pa. Cmwlth. 1996). "Under traditional ratemaking, utilities may not change rates charged to customers outside of a base rate case." *McCloskey v. Pa. Pub. Util. Comm'n*, 127 A.3d 860, 863 n.2 (Pa. Cmwlth. 2015).

At issue here is a general rate filing governed by Section 1308(d) of the Code, which provides the procedures for changing rates, the time limitations for the suspension of the new rates, and the time limitations on the Commission's actions. 66 Pa. C.S. § 1308(d).[2] The Commission is required to investigate all

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[2] Section 1308(d) provides:

> **(d) General rate increases**.--Whenever there is filed with the commission by any public utility described in paragraph (1)(i), (ii), (vi) or (vii) of the definition of "public utility" in section 102 (relating to definitions), and such other public utility as the [C]ommission may by rule or regulation direct, any tariff stating a new rate which constitutes a general rate increase, the [C]ommission shall promptly enter into an investigation and analysis of said tariff filing and may by order setting forth its reasons therefor, upon complaint or upon its own motion, upon reasonable notice, enter upon a hearing concerning the lawfulness of such rate, and the [C]ommission may, at any time by vote of a majority of the members of the [C]ommission serving in accordance with law, permit such tariff to become effective, except that absent such order such tariff shall be suspended for a period not to exceed seven months from the time such rate would otherwise become effective. Before the expiration of such seven-month period, a majority of the members of the [C]ommission serving in accordance with law, acting unanimously, shall make a final decision and order, setting forth its reasons

(Footnote continued on next page…)

general rate increase filings. *Popowsky*, 683 A.2d at 961. Section 315(a) of the Code places the burden of proving the reasonableness of a proposed rate on the utility. 66 Pa. C.S. § 315(a). The evidence necessary to meet that burden must be substantial. *Lower Frederick Twp. Water Co. v. Pa. Pub. Util. Comm'n*, 409 A.2d 505, 507 (Pa. Cmwlth. 1980). To meet this burden of proof, a utility uses a test year, which is a snapshot of time that reflects the typical conditions, revenues, expenses, and capital costs of the utility. *See Green v. Pa. Pub. Util. Comm'n*, 473

(continued…)

> therefor, granting or denying, in whole or in part, the general rate increase requested. If, however, such an order has not been made at the expiration of such seven-month period, the proposed general rate increase shall go into effect at the end of such period, but the [C]ommission may by order require the interested public utility to refund, in accordance with section 1312 (relating to refunds), to the persons in whose behalf such amounts were paid, such portion of such increased rates as by its decision shall be found not justified, plus interest, which shall be the average rate of interest specified for residential mortgage lending by the Secretary of Banking in accordance with the act of January 30, 1974 (P.L. 13, No. 6), referred to as the Loan Interest and Protection Law, during the period or periods for which the [C]ommission orders refunds. The rate in force when the tariff stating such new rate was filed shall continue in force during the period of suspension unless the [C]ommission shall grant extraordinary rate relief as prescribed in subsection (e). The [C]ommission shall consider the effect of such suspension in finally determining and prescribing the rates to be thereafter charged and collected by such public utility, except that the [C]ommission shall have no authority to prescribe, determine or fix, at any time during the pendency of a general rate increase proceeding or prior to a final determination of a general rate increase request, temporary rates as provided in section 1310, which rates may provide retroactive increases through recoupment. As used in this part general rate increase means a tariff filing which affects more than 5% of the customers and amounts to in excess of 3% of the total gross annual intrastate operating revenues of the public utility. If the public utility furnishes two or more types of service, the foregoing percentages shall be determined only on the basis of the customers receiving, and the revenues derived from, the type of service to which the tariff filing pertains.

66 Pa. C.S. § 1308(d).

A.2d 209, 213-15 (Pa. Cmwlth. 1984) (describing generally items within a test year); *City of Pittsburgh v. Pa. Pub. Util. Comm'n*, 112 A.2d 826, 832 (Pa. Super. 1955) (indicating that a condition to be considered in examining a test year is the weather during that year). A utility could use a historic test year (HTY), the year prior to the filing of the rate case, or a future test year (FTY), the year ending shortly before the date the new rates would go into effect, to determine the amount of the rate base upon which its new rates would be calculated. Historically, in order for certain facility or related costs to be included in a utility's rate base, the facility had to be "used and useful" and "in service to the public" **at the time** the rate base was being calculated. Section 1315 of the Code, 66 Pa. C.S. § 1315.[3] However, the manner in which a utility could meet its burden of proof **changed** in 2012, when the General Assembly enacted a series of amendments to the Code, including to Section 315(e), which addressed the type of test year a utility could use to support its proposed rates.

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[3] Section 1315 provides:

> Except for such nonrevenue producing, nonexpense reducing investments as may be reasonably shown to be necessary to improve environmental conditions at existing facilities or improve safety at existing facilities or as may be required to convert facilities to the utilization of coal, the cost of construction or expansion of a facility undertaken by a public utility producing, generating, transmitting, distributing or furnishing electricity shall not be made a part of the rate base nor otherwise included in the rates charged by the electric utility until such time as the facility is used and useful in service to the public. Except as stated in this section, no electric utility property shall be deemed used and useful until it is presently providing actual utility service to the customers.

66 Pa. C.S. § 1315.

2. Act 11 of 2012 – Section 315(e) of the Code

By the Act of February 14, 2012, P.L. 72, No. 11 (Act 11), the General Assembly amended Section 315(e) to allow a utility to use a "**fully projected future test year**" (FPFTY) to satisfy its burden of proving the reasonableness of its proposed rates. 66 Pa. C.S. § 315(e) (emphasis added). The FPFTY is "the 12-month period beginning with the first month that the new rates will be placed in effect after application of the full suspension period permitted under section 1308(d) [(a period not to exceed seven months)]." *Id.* Section 315(e) requires that:

> Whenever a utility utilizes a [FTY] or a [FPFTY] in any rate proceeding and such [FTY] or a [FPFTY] forms a substantive basis for the final rate determination of the [C]ommission, the utility shall provide, as specified by the [C]ommission in its final order, appropriate data evidencing the accuracy of the estimates contained in the [FTY] or a [FPFTY], and the [C]ommission may after reasonable notice and hearing, in its discretion, adjust the utility's rates on the basis of such data.

Id. As part of the Act 11 amendments to Section 315(e), the General Assembly added the following: "Notwithstanding section 1315 (relating to limitation on consideration of certain costs for electric utilities), the [C]ommission may permit facilities which are projected to be in service during the fully projected future test year to be included in the rate base." *Id.*

In its *Implementation of Act 11 of 2012* Final Order, 299 P.U.R.4th 367 (August 2, 2012), 2012 WL 3249678 (*Final Implementation Order*), issued after holding a working group with stakeholders, the Commission explained the Act 11

amendments were intended "to reduce regulatory lag[4] due to the use of rate case inputs that [were] outdated by the time new base rates bec[a]me effective." *Id.* at 2. The addition of the ability of a utility to use a FPFTY, the Commission indicated, would substantially reduce "the risks associated with regulatory lag" "because the new rates w[ould] be consistent with the test year used to establish those rates for at least the first year." *Id.* at 3. The Commission further noted the exemption to Section 1315's "used and useful" requirement now included in Section 315(e) allowed it discretion in deciding whether to include in a utility's rate base facilities that are not yet used and useful but are projected to be during the FPFTY. *Id.* at 3-4. The Commission indicated that, where a FPFTY is used and a utility is permitted to include a facility that is not yet in service, it "expect[ed] that in subsequent base rate cases, the utility [would] be prepared to address the accuracy of the [FPFTY] projections made in its prior base rate case." *Id.* at 5. OCA "support[ed]" the Commission's interpretation in its comments during the Act 11 implementation process and indicated that the use of the FPFTY could result in fewer rate increases on customers in the future. *Id.* at 4.

The General Assembly did not end its amendments to the ratemaking provisions of the Code in 2012.

3. Act 40 of 2016 – Section 1301.1 of the Code

In 2016, the General Assembly enacted the Act of June 12, 2016, P.L. 332, No. 40 (Act 40), in which it added Section 1301.1 to the Code, 66 Pa. C.S.

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[4] Regulatory lag is "a delay between the imposition of wholesale costs on a utility and state regulatory commission approval of a retail rate increase. Regulatory lag is inherent in many systems of retail rate regulation . . . ." *Kentucky West Virginia Gas Co. v. Pa. Pub. Util. Comm'n*, 862 F.2d 69, 75 (3d Cir. 1988).

§ 1301.1. Act 40 addressed the computation of income tax expenses for ratemaking purposes and eliminated the use of the consolidated tax savings adjustment (CTA). The CTA required a utility to adjust its rate base to account for the amount of tax savings it received by filing its taxes jointly with its parent and/or affiliated entities. In eliminating the use of the CTA, Pennsylvania joined the majority of states, which do not use the CTA. *See* H. 200th Sess., Feb. 8, 2016, at 117.[5] Section 1301.1(a) provides:

> If an expense or investment is allowed to be included in a public utility's rates for ratemaking purposes, the related income tax deductions and credits shall also be included in the computation of current or deferred income tax expense to reduce rates. If an expense or investment is not allowed to be included in a public utility's rates, the related income tax deductions and credits, including tax losses of the public utility's parent or affiliated companies, shall not be included in the computation of income tax expense to reduce rates. The deferred income taxes used to determine the rate base of a public utility for ratemaking purposes shall be based solely on the tax deductions and credits received by the public utility and shall not include any deductions or credits generated by the expenses or investments of a public utility's parent or any affiliated entity. . . .

66 Pa. C.S. § 1301.1(a). However, recognizing that a differential could result between the ratemaking procedures used prior to the effective date of subsection (a) (applying the CTA), and the computation now in effect (excluding the CTA), the General Assembly mandated in subsection (b) how the revenue from that differential should be used. Per that subsection, "the differential shall be used as follows: (1) fifty percent to support reliability or infrastructure related to the rate-base eligible capital investment as determined by the commission; and (2) fifty

[5] Available at https://www.legis.state.pa.us/WU01/LI/HJ/2016/0/20160208.pdf#page=18 (last visited January 8, 2020).

percent for general corporate purposes." 66 Pa. C.S. § 1301.1(b). The General Assembly's restriction on the use of this revenue applies until December 31, 2025. 66 Pa. C.S. § 1301.1(c)(1).

With these principles and statutory provisions in mind, we turn to the facts of UGI's rate case.

B. UGI's Rate Case

"UGI provides electric distribution services to approximately 61,832 residential, commercial[,] and industrial customers." (Commission Opinion (Op.) at 2.) It maintains over 1200 miles of underground and overhead primary distribution lines, 12 distribution substations, and 49 distribution circuits. Its last base rate case was in 1996. On January 26, 2018, UGI filed a new tariff, which was to become effective on March 27, 2018, that UGI later amended to reflect certain changes in federal tax law. "UGI proposed a rate base change that would have increased its annual revenues by $7.705 million, or 8.6%, based on a . . . FPFTY[] ending September 30, 2019." (*Id.* at 1.) The use of September 30, 2019, as the end of the FPFTY reflects the use of a "year-end rate base methodology" (year-end methodology). (*Id.* at 18.) UGI asserted the proposed rate increase reflected the business environment it currently faced, including the "accelerated investment in the repair, replacement or improvement of an aged and aging distribution system; the modernization of core technology systems . . . ; and modest increases in employee wages and salaries since its last base rate case in 1996." (*Id.* at 1-2.) UGI claimed that it was prevented from earning a fair rate of return on its investment at the present rate levels due to the growth in capital and operating costs, as well as stagnation in customer usage and growth trends. (*Id.*)

UGI further asserted that under Act 40, it was required to compute what the CTA would have been, here, $75,400, and then certify that this amount (Act 40 savings) would be used in accordance with Section 1301.1(b). Pointing out that its capital expenditures for reliability and infrastructure projects for the FPFTY exceeded $11 million, which was far greater than 50% of $75,400, and that its general corporate expenses likewise far exceeded the 50% requirement, UGI contended it complied with Section 1301.1(b)'s requirements.

By operation of law, the tariff was suspended, pursuant to Section 1308(d) of the Code, until October 27, 2018. In accordance with the requirement that all general rate cases be investigated, *Popowsky*, 683 A.2d at 961, the Bureau of Investigation and Enforcement (I&E) began an investigation of the proposed general rate increase.

C. Objections to UGI's Rate Case

OCA, along with others including the Office of Small Business Advocate (OSBA) and two UGI customers, filed complaints against UGI's proposed rate increase. (Commission Op. at 3.) I&E also opposed UGI's proposed rates. OCA, OSBA, and I&E particularly objected to UGI's calculation of its rate base using facilities and costs that were projected to be in effect as of the **end** of the FPFTY. They asserted that using this calculation would allow UGI to **overcollect** because the proposed rates included costs that would not be incurred by UGI on the day the rates went into effect, October 27, 2018, but would be incurred throughout various points within the FPFTY, ending September 30, 2019. Instead, they proposed using an "**average rate base methodology**" that would combine the costs listed for the beginning of the FPFTY and the costs listed at the end of the FPFTY and divide the total by two. (*Id.* at 15.) This methodology, they contended, resulted in

a more just and reasonable rate. They also suggested that the same methodology be applied to UGI's depreciation expenses. OCA contended this position was supported by the decision of the Illinois Commerce Commission in *Re North Shore Gas Company*, (Ill. C.C. No. 12-0511/0512, June 18, 2013), 2013 WL 3762292, which rejected the use of year-end methodology in favor of an average rate base methodology.

OCA further sought a downward adjustment to UGI's rate base in the amount of $75,400, UGI's Act 40 savings. OCA contended that UGI did not prove that it would use that $75,400 as required by Section 1301.1(b) because it had not provided an accounting for those funds and, therefore, UGI should not be able to retain those funds. OCA observed that UGI's approach to satisfying this requirement should be rejected as it would not show actual use of the funds for the required purposes.

II. Recommended Decision and the Commission Decision

A. Recommended Decision

Following the receipt of witness testimonies, documentary evidence, other evidentiary filings, and an evidentiary hearing, two Administrative Law Judges (ALJs) issued a Recommended Decision. After providing an overview of the amendments to Section 315(e) of the Code, the ALJs held that, following Act 11, a utility may use the FPFTY in a base rate case to project items such as revenues, operating expenses, and capital expenditures throughout the 12-month period beginning with the first month the rates go into effect. (Recommended Decision (R.D.) at 13.) Noting that while a fundamental principle of regulating utilities is that a public utility be permitted to include projects in a rate base and earn a reasonable return on its investments **only** when the project becomes used and

useful, the ALJs concluded that Act 11 **altered** this principle by allowing the use of the FPFTY to address the risks associated with regulatory lag. Citing the plain language of Section 315(e) and the policy behind its enactment, the ALJs accepted the use of the year-end methodology proposed by UGI. The ALJs were particularly persuaded by the exemption from Section 1315's "used and useful" requirement given to utilities that sought to meet their burden of proof using a FPFTY. (R.D. at 18-19.) However, the ALJs did not approve all of UGI's projected facilities. They rejected UGI's proposed "Electrical Engineering and Operations Center" (Operations Center), which added $17.3 million to UGI's FPFTY, as being in its preliminary planning stages and because there was no "reasonable certainty that it [would] be in operation in the FPFTY." (*Id.* at 22-24.) The ALJs rejected, as not persuasive, the Illinois Commerce Commission's decision in *North Shore Gas Company*, observing that decisions of other jurisdictions were not relevant to Pennsylvania rate cases due to, among other reasons, differences in statutory language and ratemaking principles. (R.D. at 21.) The ALJs acknowledged OCA's concern regarding the possibility of a utility overcollecting based on overstated projections, but indicated such issues could be addressed through protections the Commission could invoke, including verifications in subsequent rate filings or the imposition of an audit. (*Id.* at 22.)

The ALJs likewise agreed that UGI satisfied the requirements of Act 40, the language of which the ALJs found to be clear and unambiguous. (*Id.* at 110.) Reasoning that Act 40 does not state within Section 1301.1(b) any specific requirements for demonstrating the use of funds, the ALJs held that UGI was not required to show exactly where the Act 40 savings would be spent. (*Id.*) The ALJs found that the testimony of UGI's witness explaining how UGI's capital and

general corporate purpose expenditures far exceeded the 50% threshold found in Section 1301.1(b) supported UGI's ability to retain the full $75,400. (*Id.* at 111.) Finding OCA's contrary argument to be unpersuasive and without support in the Code, the ALJs recommended the Commission approve UGI's retention of the full $75,400 to be used in accordance with Act 40.

B. Exceptions and Replies

OCA filed exceptions to the ALJs' acceptance of UGI's proposed rate base calculated using the year-end methodology. OCA contended that because the plain language of Act 11 did not specifically address the type of methodology to be used in conjunction with a FPFTY, the average rate base methodology must be used to ensure the proposed rates would be just and reasonable as required by Section 1301. UGI responded that the use of the year-end methodology was consistent with the plain language of Act 11, the purpose of Act 11 to reduce regulatory lag, and the prior use of that methodology in ratemaking under the FTY process.

OCA also filed an exception to the ALJs' recommendation that the Commission adopt UGI's Act 40 proposal. OCA argued that Section 1301.1(b) requires a utility to provide an accounting for how these funds are being used to benefit ratepayers when rates are being set, at least until December 31, 2025, and the ALJs' interpretation of that provision rendered Section 1301.1(b) meaningless. According to OCA, UGI failed to establish its proper use of these funds and those amounts should be used to offset the rate base in this case. UGI responded that it complied with Act 40's directives and, therefore, the exception should be denied. UGI contended Section 1301.1(b) does not contain any requirement that an accounting be given in order for a utility to retain those amounts.

C. The Commission Decision

Upon its review, the Commission agreed with and adopted the ALJs' recommendation and rationale that UGI be permitted to utilize a year-end methodology for calculating its rate base. Pointing to the purposes of Act 11 to address regulatory lag and to encourage plant investment to counter aging utility infrastructure, the Commission explained these purposes are addressed by allowing the use of the FPFTY. Reviewing the statutory language of Section 315(e), and its exemption from Section 1315 for utilities using the FPFTY, the Commission held that the "used and useful" language in Section 1315 is not a bar to including plants added during the FPFTY. (Commission Op. at 23-24.) According to the Commission, the use of the FPFTY, as authorized by Section 315(e), allows a utility to project revenue requirements and ratemaking components throughout the 12-month period beginning with the first month the new rates would begin and to recover those amounts as part of the rate base. Further, in reviewing the rate base approved by the ALJs, the Commission affirmed their exclusion of the $17.3 million Operations Center from UGI's rate base, agreeing there was insufficient evidence to establish it would be in service during the FPFTY. (*Id.* at 31.)

The Commission found no error in the ALJs' rejection of the Illinois Commerce Commission's decision in *North Shore Gas Company*. The Commission observed, among other things, that it was not bound by such decision and "it would be inappropriate to consider another jurisdiction's statute where there was no indication that the General Assembly based Pennsylvania legislation on [the] legislation adopted in other jurisdictions." (Commission Op. at 25 (citing *Elder v. Orlucky*, 515 A.2d 517, 522 (Pa. 1986)).)

Finally, in response to OCA's concerns that UGI may have overstated its projections, the Commission agreed with the ALJs that this issue is addressed through other available protections. In addition to requiring verification through a subsequent rate filing, Section 315(e) specifically authorizes the Commission to **audit** a utility that uses a FPFTY to determine whether such projections are accurate and to **adjust** the utility's "rates to reflect material differences." (*Id.* at 26.) For these reasons, the Commission denied OCA's exception to the use of the year-end methodology.

Next, after reviewing the language of Section 1301.1 and the purpose of Act 40, which "was to move away from Pennsylvania's past practice of requiring a CTA to a public utility's tax expenses when setting rates in a base rate proceeding," the Commission agreed with the ALJs that this language was clear and unambiguous and supported UGI's position. (*Id.* at 152.) The Commission explained:

> Section 1301.1(a) specifies how income tax expense is to be computed for ratemaking purposes in base rate cases, while Section 1301.1(b) specifies how utility operating income generated by the operation of Section 1301.1(a) must be used by the affected public utilities until December 31, 2025. Based on a plain reading of the statute, Section 1301.1(b) requires that 50% of the Act 40 savings be used for reliability or infrastructure purposes, and the other 50% of the Act 40 savings be used for general corporate purposes. The statute does not require public utilities to provide specific information concerning how the amounts would be used.

(*Id.*) The Commission found that UGI had presented substantial evidence to show its compliance with Act 40's requirements. This evidence, the testimony of its witness, was that UGI's *pro forma* capital additions for reliability or infrastructure for its FPFTY were over $11 million, far greater than 50% of $75,400, and that

UGI's general corporate purpose expenses also far exceeded that threshold. (*Id.*) The Commission accepted that evidence and approved UGI's retention of the $75,400 for the purposes UGI stated they would be used. Thus, the Commission denied OCA's exception.

OCA now petitions this Court for review.

III. OCA's Appeal

OCA is challenging the Commission's interpretation of the Code and acceptance of UGI's calculations and retention of the Act 40 savings. The Commission argues its determinations are supported by the Code and the record and should be affirmed. UGI has intervened in OCA's appeal, providing argument in support of affirming the Commission's Order.[6] EAP filed an *amicus curiae* brief also providing argument in support of affirming. Before setting forth and addressing these arguments, we lay out the standards by which this Court reviews Commission decisions generally, as well as Commission decisions related to ratemaking. Further, as this matter involves statutory construction, we set forth those standards of review as well.

A. Standards for Reviewing Commission Decisions and Engaging in Statutory Construction

Our standard of review of a Commission decision is limited to determining whether substantial evidence[7] supports the findings of fact, whether the Commission committed an error of law, and whether constitutional rights were

[6] The OSBA participated in the proceedings before the ALJs and the Commission and filed a notice of intervention in OCA's petition for review. However, due to its failure to file a timely brief, OSBA was precluded from further participation.

[7] "Substantial evidence is such evidence that a reasonable mind might accept as adequate to support a conclusion." *McCloskey*, 127 A.3d at 866 n.16.

violated. *McCloskey*, 127 A.3d at 866 n.16. We defer to the Commission's interpretation of the Code and its own regulations unless the Commission's interpretations are clearly erroneous. *Coal. for Affordable Util. Servs. & Energy Efficiency in Pa. v. Pa. Pub. Util. Comm'n*, 120 A.3d 1087, 1095 (Pa. Cmwlth. 2015). We are not to substitute our judgment for that of the Commission "when substantial evidence supports the [Commission's] decision on a matter within the [C]ommission's expertise." *Id.* (internal quotation marks and citation omitted). Such "deference is even more necessary when the statutory scheme is technically complex." *Id*. (internal quotation marks and citation omitted). However, on issues of law, "our standard of review is de novo and our scope of review is plenary." *Id*.

"The [Commission] has broad discretion in determining whether rates are reasonable" and "is vested with discretion to decide what factors it will consider in setting or evaluating a utility's rates." *Popowsky*, 683 A.2d at 961. We are not to "indulge in the processes of weighing evidence and resolving conflicting testimony." *Popowsky v. Pa. Pub. Util. Comm'n*, 706 A.2d 1197, 1201 (Pa. 1997) (citations omitted). Where "[t]he decision at issue[] involve[s] complex financial determinations and weighing and interpreting statistical and economic evidence, [it] is within the [Commission's] area of expertise." *Id.* Further, "[a]s long as there is a rational basis for the [Commission's] methodology [in establishing the rate structure], such decisions are left entirely up to the discretion of the" Commission, "which, using its expertise, is the only one which can properly determine which method is most accurate given the particular circumstances of the case and economic climate." *Id.* (third alteration in the original) (citations omitted). "[T]he establishment of a rate structure . . . is an administrative function peculiarly within the expertise of the [Commission]." *Id.* (citation omitted).

Finally, because this matter involves statutory construction, we are guided by the principles of Section 1921 of the Statutory Construction Act of 1972, which dictate that the object of statutory construction is to ascertain and effectuate legislative intent. 1 Pa. C.S. § 1921(a). Thus, "[w]hen the words of a statute are clear and free from all ambiguity, the letter of it is not to be disregarded under the pretext of pursuing its spirit." 1 Pa. C.S. § 1921(b). "The best indication of legislative intent is the plain language of the statute." *Slippery Rock Area Sch. Dist. v. Pa. Cyber Charter Sch.*, 31 A.3d 657, 663 (Pa. 2011). We are to construe the statutory language, if possible, to give effect to all of its provisions. 1 Pa. C.S. § 1921(a). It is "[o]nly when the words of the statute are not explicit" that the court should resort to statutory construction to ascertain the legislature's intent. 1 Pa. C.S. § 1921(c).

B. *Use of the Year-End Methodology – Section 315(e) of the Code*

1. The Parties' Arguments

a. OCA's Arguments

OCA argues the Commission erred in calculating UGI's rate base using the FPFTY that included any facility that was **projected** to be in service by the end of that year for the following reasons. Section 315(e), which does not expressly set forth what methodology may be used to calculate a utility's rate base when a FPFTY is utilized, must be read consistently with Section 1301(a) of the Code, which requires that all rates be just and reasonable. OCA does not dispute that when Sections 315(e) and 1315 are read together, the use of a FPFTY permits an electric utility "to include in its rate base projected plant[s] and investments that are not used and useful on the day that rates go into effect." (OCA Brief (Br.) at 32.) But, allowing the use of the year-end methodology, rather than the average

rate base methodology, permits a utility to collect rates for facilities or costs **before** the facilities are operational or the costs incurred and creates a rate that is not just or reasonable in contravention of Section 1301. OCA's witnesses, along with the witnesses of I&E, explained why the year-end methodology was not an appropriate form of ratemaking because it allowed for overcollection by a utility, for which OCA contends the utility will not be held to account. This conclusion is supported by the Illinois Commerce Commission's decision in *North Shore Gas Company*, which the Commission erred in not considering. Further, while the year-end methodology was used in conjunction with a FTY, such did not result in overcollection because the FTY ended at approximately the same time the new rates became effective. Thus, the facilities projected to be in service by the end of the FTY would be in service (used and useful) when the ratepayers began to pay the new rates.

OCA further argues the Commission's decision is not based on substantial evidence, citing evidence in the record that supports the use of the average rate base methodology rather than the year-end methodology. In contrast, UGI presented no evidence to demonstrate that Act 11 and the use of the FPFTY authorized the use of the year-end methodology.

b. The Commission's Arguments

The Commission responds that its interpretation of Section 315(e) is entitled to deference, particularly given the complexity of the Code, and should not be reversed because that interpretation is not clearly erroneous for the following reasons. The Commission's approval of the year-end methodology is supported by the plain language of Section 315(e) and the purpose of the Act 11 amendments, which was intended to encourage plant investment by mitigating, among other

things, the risks associated with regulatory lag. OCA's use of the average rate base methodology results in a utility being unable to recover costs for all facilities projected to be in service during the FPFTY, which is contrary to the plain language of Section 315(e). The plain language of Section 315(e) likewise does not support OCA's argument that the only way the rates calculated using the FPFTY can be just and reasonable as required by Section 1301 is to use the average rate base methodology. The General Assembly was aware of Section 1301's just and reasonable requirements when it amended Section 315(e) to allow usage of the FPFTY without the restrictions of the used and useful requirements of Section 1315 in a general rate case. Thus, including in a rate base facilities not yet in service but projected to be during the relevant time period is permitted and does not result in an unjust and unreasonable rate. As for *North Shore Gas Company*, that decision may have supported OCA's position on its face, but the Commission examined that decision and found it not to be persuasive, as is its prerogative.

In response to OCA's concerns about a utility not being accountable for its projections or collections, the Commission asserts every utility has the burden of presenting an evidentiary record that supports the additions to its rate base and why such additions are needed to provide service to its customers. The Commission does have the authority, pursuant to Section 315(e), to make after-the-fact adjustments and to require a utility to support its prior projections in a subsequent rate case. Thus, contrary to OCA's contentions, there are safeguards that the Commission may use to hold a utility to account if the use of the year-end methodology results in overearning.

c. UGI's and EAP's Arguments

UGI and EAP both argue, like the Commission, that the use of the year-end methodology is supported by substantial evidence and the plain language and purpose of the Act 11 amendments to Section 315(e). They contend OCA's evidentiary arguments are not relevant because this issue involves a legal question and, if relevant, are merely a request for the Court to reweigh the evidence. UGI presented substantial evidence to support that its proposed rate was just and reasonable and that OCA's proposed methodology was flawed, which the Commission accepted. That evidentiary determination is not subject to appellate review.

As for OCA's legal arguments, UGI and EAP assert as follows. OCA's arguments are inconsistent with the statutory language as amended by the General Assembly via Act 11, and the Commission's interpretation of those provisions, as well as its setting of UGI's rate, are entitled to deference. The Act 11 amendments reflect the General Assembly's intent to reduce regulatory lag and support the need to replace Pennsylvania's aging utility infrastructure. By permitting a utility to use a FPFTY to meet its burden of proof in a rate case, the General Assembly authorized utilities to include, without limitation, all facilities projected to be in service **during** the FPFTY in its rate base. The use of the term "during" supports the use of the year-end methodology approved by the Commission in this matter, as does the use of that methodology to calculate a utility's rate base prior to the Act 11 amendments. OCA's average rate base methodology also allows a utility to earn returns on facilities not yet in service, but only for a portion of the FPFTY, a position not supported by Section 315(e)'s language. Although OCA raises concerns about utilities overearning through the use of the year-end methodology, utilities are not overearning when they comply with the plain language of Section

315(e), which authorized the use of the FPFTY and projected costs that would be incurred during that test year.

UGI, individually, argues the following. Section 315(e) does **not** speak in terms of partially projected future test years or of averaging the costs of plants projected to be in service in the test year for inclusion in the rate base, which is what OCA proposes. This methodology also eviscerates the concept of prospective rate making by designing a rate year that will recover only one-half of the total costs a utility will incur in a prospective test year. Using year-end methodology is appropriate because rates are established on an annual basis, are prospective in nature, and will be in effect for more than a year. The use of the FPFTY coupled with year-end methodology has the effect of not only reducing regulatory lag more than the average rate base methodology proposed by OCA but also reducing how frequently a utility must return to the Commission to seek an increase in its rates. OCA's arguments reflect its position that the used and useful requirement of Section 1315 should continue to be utilized, at least in part, in calculating UGI's rate base. However, the General Assembly was aware of this requirement and **exempted FPFTYs** from Section 1315, thereby choosing to **allow** rates based on facilities not yet in service but projected to be sometime during that test year. OCA's argument that rates proven under Section 315(e)'s FPFTY process are not permissible because they do not meet Section 1301's general just and reasonable requirement is not supported by the principles of statutory construction. According to UGI, OCA seeks to impose a general statutory provision (Section 1301) on a specific statutory provision (Section 315(e)), which is also the later enacted provision. Rather, Section 315(e) should be read as a refinement of Section 1301's general just and reasonable requirement. In short, if

a rate base is calculated using the FPFTY and year-end procedures authorized by the General Assembly in Section 315(e), the corresponding rate is just and reasonable.

EAP argues, individually, as follows. There is no single way to arrive at a just and reasonable rate and the methodology used by the Commission in determining a utility's rate base is a sub-determination within ratemaking that falls distinctly in the Commission's expertise. The use of the year-end methodology provides the most current and foreseeable financial information for the purpose of setting a utility's rates. According to EAP, as long as there is evidence to support the numbers used by the Commission to set a utility's rate, the Commission did not err or abuse its discretion. Using any point earlier than the end of the FPFTY would result in an understated rate base, and OCA's average rate base methodology effectively eliminates one-half of the benefits of using the FPFTY. In reviewing UGI's proposed rate base, the Commission excluded certain claimed facilities UGI projected to be in service during the FPFTY, demonstrating the Commission's exercise of its expertise in ratemaking.

d. OCA's Reply

In its reply brief, OCA reiterates many of the arguments made in its initial brief, including that the plain language of Section 315(e) does not support the Commission's determination and that the use of its proposed average rate base methodology is the only way to ensure just and reasonable rates when a FPFTY is used. OCA contends the Commission's interpretation of Section 315(e) as allowing the use of year-end methodology is clearly erroneous and not entitled to deference because it does not give effect to Section 1301's requirement that rates must be just and reasonable. These two provisions must be read together and using

OCA's average rate base methodology harmonizes the two. Neither the mere existence of the FPFTY, nor the use of the word "during" in Section 315(e), implies the General Assembly intended that a rate base be calculated using the year-end methodology. Finally, OCA asserts that using the average rate base methodology also addresses regulatory lag when compared to the use of the HTY or FTY to set new rates.

2. Discussion

Due to the high level of deference this Court gives to the Commission, particularly in rate making decisions, in order to reverse the Commission's Order in this case, the Court would have to conclude that the Commission's interpretation of Section 315(e) of the Code is **clearly erroneous** and that there is **no rational basis for the Commission's methodology** in approving UGI's rate structure. *Popowsky*, 706 A.2d at 1203. Although OCA asserts the Commission's decision is not supported by substantial evidence, the question before the Court on this issue is one of law – whether the statutory language supports the use of a year-end methodology when a utility chooses to utilize a FPFTY to calculate its rate base. Reviewing the statutory language of Section 315(e), we cannot say the Commission's interpretation of that provision in this rate case is clearly erroneous. Nor can we say there is no rational basis for the Commission's approval of that methodology under the plain language of Section 315(e) and the purposes of Act 11.

Section 315(e) of the Code states, in relevant part:

> In discharging its burden of proof the utility may utilize a future test year or a **[FPFTY], which shall be the 12-month period beginning with the first month that the new rates will be placed in effect after application of the full suspension period permitted under**

> **section 1308(d) (relating to voluntary changes in rates).** . . . Whenever a utility utilizes a future test year or a [FPFTY] in any rate proceeding and such [FTY] or a [FPFTY] forms a substantive basis for the final rate determination of the [C]ommission, the utility shall provide, as specified by the [C]ommission in its final order, appropriate data evidencing the accuracy of the estimates contained in the [FTY] or a [FPFTY], and the [C]ommission may after reasonable notice and hearing, in its discretion, adjust the utility's rates on the basis of such data. **Notwithstanding section 1315 (relating to limitation on consideration of certain costs for electric utilities), the [C]ommission may permit facilities which are projected to be in service during the [FPFTY] to be included in the rate base.**

66 Pa. C.S. § 315(e) (emphasis added).

By its terms, Section 315(e) authorizes a utility to meet its burden of proof in a general rate case by using a FPFTY, which is "the 12-month period **beginning with the first month** that the new rates will be placed in effect." *Id.* (emphasis added). While ordinarily a facility must be in service to the public, or used and useful, for its associated costs to be included in a utility's rate base and the rates charged by the utility, 66 Pa. C.S. § 1315, the General Assembly granted the Commission the discretion **not to impose** this requirement for those utilities seeking to meet their burden of proof using the FPFTY. It did so by allowing a utility to include in its **rate base**, upon which customer rates are calculated, "facilities which are **projected** to be in service **during** the" FPFTY "[n]otwithstanding [S]ection 1315." 66 Pa. C.S. § 315(e) (emphasis added). Thus, under Section 315(e)'s plain language, a utility can include in its rate base, if permitted by the Commission, the costs of facilities that are not yet in service, but that are projected to be in service **during the 12-month period beginning with the first month** the new rates will be in effect. Section 315(e) does not speak in terms of averages or partially projected test years – it says facilities that are projected to be in service during the 12-month period that is statutorily defined as

the FPFTY can be included in the rate base. This 12-month period includes day 1, as well as day 365.

In ascertaining and effectuating the General Assembly's intent, we are mindful that "when the words of a statute are clear and free from all ambiguity, the letter of it is not to be disregarded under the pretext of pursuing its spirit." 1 Pa. C.S. § 1921(b). OCA's arguments appear to urge the Court to disregard the letter of Section 315(e), which, it acknowledges, when read with Section 1315 permits a utility "to include in its rate base projected plant[s] and investments that are not used and useful on the day the rates go into effect." (OCA's Br. at 32.) However, it is OCA's preferred methodology that does not give effect to the plain language of Section 315(e) because it essentially redefines the key term "FPFTY" and limits the language excluding FPFTYs from Section 1315's used and useful requirement. We may not disregard the General Assembly's intent when it is clearly stated within the statutory language in question. 1 Pa. C.S. § 1921(b). The Commission reviewed this language and concluded, within its particular expertise in the complex statutory scheme that is the Code, *Coalition for Affordable Utility Service*, 120 A.3d at 1094, that a year-end methodology could be applied to the FPFTY for UGI's rate case. This interpretation is supported not only by Section 315(e)'s plain language, but also by the purposes of Act 11, which were to mitigate the risks of regulatory lag and to aid in the resolution of the aged and aging nature of Pennsylvania's utility infrastructure. (Commission Decision at 23); *Final Implementation Order* at 1-3; *see also* H. 195th Sess., Oct. 4, 2011, at 1954-56; S. 196th Sess., Jan. 25, 2012, at 71-72; H. 196th Sess., Feb. 7, 2012, at 156-57.[8]

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[8] These materials are available, respectively, at https://www.legis.state.pa.us/WU01/LI/HJ/2011/0/20111004.pdf#page=10; https://legis.state.pa.us/WU01/LI/SJ/2012/0/Sj20120125.
(Footnote continued on next page…)

OCA once recognized that a benefit of using this methodology was the reduction in the need for future rate increases as reflected in its comments set forth in the *Final Implementation Order*, but now OCA seeks to reduce the benefit of using the FPFTY by one half, which would, ironically, require the need for future rate increases sooner. *Id.* at 3. That the Illinois Commerce Commission came to a different result in *North Shore Gas Company* under that state's statutory and ratemaking scheme does not mean the Commission erred in its interpretation of the Code's language.

We are also mindful that there is **no single way** to arrive at just and reasonable rates and that the Commission enjoys "**broad discretion** in determining whether rates are reasonable." *Popowsky*, 683 A.2d at 961 (emphasis added). While OCA claims the Commission's interpretation does not give effect to Section 1301 and results in a rate that is not just and reasonable, that provision does not require a different result. When enacting Act 11 and amending Section 315(e), the General Assembly was aware of the requirement that all rates must be just and reasonable. *Marcellus Shale Coal. v. Dep't of Envtl. Prot.*, 216 A.3d 448, 501 (Pa. Cmwlth. 2019) ("[W]hen the General Assembly enacts a statute, it is presumed to know the current state of the law."). Exercising its legislative and policy making authority, the General Assembly chose to allow, under certain circumstances, a utility to include in its rate base the costs associated with not-yet-in-service facilities, and authorized the Commission, within its discretion, to calculate the utility's rate so as to include such as-of-yet incurred costs. In allowing such costs

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Pdf#page=3; and https://www.legis.state.pa.us/WU01/LI/HJ/2012/0/20120207.pdf#page=23 (last visited January 8, 2020).

to be included in the rate base, the General Assembly authorized a utility to include those costs in what it charges its customers for their utility service. Accordingly, we agree with UGI that Section 315(e) is a refinement of Section 1301 and that a rate approved by the Commission in accordance with Section 315(e) is one that is just and reasonable under both provisions.

However, both the General Assembly and the Commission were cognizant of the potential of a utility to overproject its rate base when using a FTY or FPFTY, one of OCA's main concerns in this matter.[9] Notably, all parties agree that the year-end methodology was used in the FTY process. Given the potential for overprojection, the General Assembly incorporated certain protections in Section 315(e) by authorizing the Commission to require a utility to provide the Commission with "appropriate data evidencing the accuracy of the estimates" used to calculate the rate base via either the FTY or the FPFTY and to adjust a "utility's rates on the basis of such data" after reasonable notice and a hearing. 66 Pa. C.S. § 315(e). Similarly, in its *Final Implementation Order*, the Commission advised that it "expect[ed] that in subsequent base rate cases, the utility" using the FPFTY would "be prepared to address the accuracy of the [FPFTY] projections made in its prior base rate case." *Id.* at 3. Thus, while OCA's concerns are not lightly taken, there is recourse if a utility does overproject and overcollect because there are means by which the Commission can address a utility's overprojections and any

[9] Moreover, while OCA's arguments could be viewed as suggesting that the Commission did not fully review UGI's projected facilities to determine whether they should be included in the rate base, which allows for improper overcollection, it is apparent the Commission reviewed the evidence to determine what facilities should be included in the FPFTY. For example, the Commission specifically excluded the proposed Operations Center from the rate base on the basis that there was insufficient evidence to support that it would be in service during the FPFTY. This exclusion reduced the rate base by over $17.3 million.

related overcollection that could occur as a result of the use of the FPFTY and year-end methodology.

For all these reasons, we cannot say that the Commission's interpretation of Section 315(e) is clearly erroneous or that its ratemaking decision lacks a rational basis such that the Commission's determinations are not entitled to deference from this Court.

C. *Use of the Act 40 Savings – Section 1301.1(b) of the Code*

1. <u>The Parties' Arguments</u>

a. OCA's Arguments

OCA argues the Commission erred in allowing UGI to retain the Act 40 savings because UGI failed to establish that the $75,400 was actually used or will be used in accordance with Section 1301.1(b). Beyond relying on its *pro forma* calculations, UGI presented no evidence specifically showing how or for what these funds were used: on reliability or infrastructure-related projects or general corporate purposes. Further, the Commission's interpretation of Section 1301.1(b) as not requiring a specific accounting of where or how the Act 40 savings are used does not give effect to the statutory language and renders both that subsection and subsection (c), requiring that restricted use of those savings until December 31, 2025, inoperative. For these same reasons, OCA asserts that the Commission's determination is not supported by substantial evidence. Because UGI did not meet its burden of proof under Section 1301.1(b) with substantial evidence, UGI's rate base should be reduced by $75,400.

b. The Commission's Arguments

The Commission argues its interpretation of Section 1301.1(b) is entitled to deference as it is supported by the section's plain language and the purpose of Act 40 and, therefore, is not clearly erroneous. OCA's assertion that the Act 40 savings should be used to reduce the rate base is contrary to Section 1301.1(a)'s language and purpose, which was to eliminate the use of the CTA such that any savings a utility obtains by filing its taxes with a parent and/or affiliated companies are not used in calculating the utility's rate base. 66 Pa. C.S. § 1301.1(a). Section 1301.1(b) clearly and unambiguously sets out how a utility is to use the Act 40 savings, 50% toward capital investments relating to reliability or infrastructure and 50% toward general corporate purposes, but does not require that a utility provide specific or detailed information as to how those amounts are used. All the utility has to do is show that it is using or expending the threshold amounts in the required category, and UGI presented such evidence by establishing that its capital expenditures for reliability and infrastructure and general corporate expenditures for the FPFTY each far exceeded 50% of $75,400 UGI had in Act 40 savings. The Commission accepted this evidence as showing compliance with Section 1301.1(b), and this determination should be upheld.

c. UGI's and EAP's Arguments

UGI and EAP argue that the Commission's interpretation of Section 1301.1(b) is supported by the plain language of that provision and the purpose of the Act 40 amendment. Act 40 was enacted to end the use of the CTA in Pennsylvania, consistent with a majority of other states, and OCA's arguments disregard the plain language of the statute and seek, essentially, to reinstate the CTA by requiring a reduction of UGI's rate base by $75,400. There is no

requirement in Section 1301.1(b) that UGI specifically identify or state with particularity where the Act 40 savings are used. Rather, UGI was required to, and did, establish that the Act 40 savings will be used for the designated statutory purposes.

d. OCA's Reply

In its reply brief, OCA acknowledges Act 40 abolished the use of the CTA in ratemaking, but argues that the Commission's interpretation does not require a utility to prove that the Act 40 savings are actually used in accordance with Section 1301.1(b). OCA asserts the Commission's interpretation does not give effect to the term "use" in that section and, therefore, is not entitled to deference. Moreover, the Commission's acceptance of the *pro forma* evidence does not show how UGI used or will use the $75,400 as required by Section 1301.1(b).

2. Discussion

On this issue the Court is reviewing both the Commission's interpretation of Section 1301.1(b) and the Commission's determination that UGI's evidence established that its use of the Act 40 savings was or would be in accordance with Section 1301.1(b). OCA does not dispute that the General Assembly's intent in enacting Act 40 and adding Section 1301.1 to the Code was to eliminate the use of the CTA in the ratemaking process. Nor does OCA dispute that the Act 40 savings at issue are $75,400, 50% of which is $37,700. Instead, OCA challenges the Commission's reading of Section 1301.1(b) as not requiring UGI to present specific evidence of exactly how UGI actually used or will use the Act 40 savings. OCA further contends the evidence UGI presented did not show the actual use of those savings for the requisite purposes.

Section 1301.1(a) sets forth the treatment of certain income tax deductions and credits a public utility may have for ratemaking purposes. As acknowledged by OCA, this section eliminates the use of the CTA for ratemaking purposes and, therefore, only "the tax deductions and credits received by the public utility" and not the "deductions or credits generated by the expenses or investments of a public utility's parent or any affiliated entity" shall be included in the utility's rate base. 66 Pa. C.S. § 1301.1(a). Because the change in treatment of tax deductions and credits would result in a utility accruing additional revenues, the General Assembly placed restrictions on the use of that additional revenue until December 31, 2025. 66 Pa. C.S. § 1301.1(b), (c). That restriction requires a utility to use its Act 40 savings as follows: "(1) fifty percent to support reliability or infrastructure related to the rate-base eligible capital investment as determined by the commission; and (2) fifty percent for general corporate purposes." 66 Pa. C.S. § 1301.1(b).

In its Decision, the Commission held that the plain language of Section 1301.1(b) "**does not require** public utilities to provide **specific information** concerning how the amounts would be used." (Commission Decision at 152 (emphasis added).) While OCA contends this interpretation is inconsistent with that provision's language, reviewing the language supplied by the General Assembly, we cannot say the Commission's interpretation is clearly erroneous. Section 1301.1(b) sets forth the categories to which the Act 40 savings must be applied, but the General Assembly **did not expressly** impose any particular manner in which a utility had to establish its compliance. Instead, the General Assembly indicated that those savings had to be used to support reliability or infrastructure capital investment and general corporate purposes, but does not require an accounting of those funds. "When the words of a statute are clear and

free from all ambiguity, the letter of it is not to be disregarded under the pretext of pursuing its spirit." 1 Pa. C.S. § 1921(b). Even if this provision was ambiguous as to what a utility had to do to establish its compliance, because the Commission's interpretation is not clearly erroneous, it is entitled to deference. *Popowsky*, 706 A.2d at 1203.

Finally, we turn to OCA's substantial evidence challenge. The Commission is the fact finder in these matters, and we may not "indulge in the process of weighing evidence and resolving conflicting testimony." *Id.* at 1201. In performing a substantial evidence review, we must consider the record in the light most favorable to the party that prevailed before the Commission, giving that party the benefit of all inferences that can be logically drawn from the evidence. *United Transp. Union, Pa. State Legislative Bd. v. Pa. Pub. Util. Comm'n*, 68 A.3d 1026, 1032 (Pa. Cmwlth. 2013).

Here, UGI's witness Stephen F. Anzaldo testified regarding UGI's Act 40 savings and Section 1301.1(b). When asked whether UGI's rate case supported the conclusion that UGI was "using at least 50 percent of [Section 1301.1(b)'s] revenue requirement . . . to support reliability or infrastructure related to capital investment," Anzaldo stated yes, it did, because UGI's "*pro forma* capital additions for reliability or infrastructure for projects for the . . . FPFTY is $11.770 million," which was "greater than 50% of the amount of what would have been consolidated tax savings adjustment under the prior ratemaking principles." (Reproduced Record at 23a.) When asked the same question regarding the use of the Act 40 savings to support general corporate purposes, Anzaldo explained that UGI "anticipated an operating expense budget of more than $81 million" and that "50[%]of the consolidated tax adjustment revenue requirement would equate to

only $37,700." (*Id.* at 23a-24a.) Anzaldo further acknowledged that he understood Section 1301.1(b)'s requirement that the $75,400 in Act 40 savings had to be used by UGI as set forth in that provision. (*Id.* at 23a.)

Considering this testimony, accepted by the Commission, and all inferences logically drawn therefrom in favor of UGI, we cannot say that a reasonable mind would not accept it as adequate to support the conclusion that UGI's use of the Act 40 savings was or would be in accordance with Section 1301.1(b). It is a reasonable inference that UGI will use the $75,400 in Act 40 savings as mandated by Section 1301.1(b) because it is aware of that requirement and it is otherwise expending more than $11 million in capital additions related to reliability and infrastructure and has an $81 million budget for its operating expenses. Thus, there is substantial evidence to support the Commission's conclusion that UGI satisfied the requirements of Section 1301.1(b). While OCA cites to evidence disagreeing that UGI's evidence met its burden of proof under Section 1301.1(b) and explaining that UGI had not used the Act 40 savings as required, the fact that there is evidence in the record to support a contrary finding does not matter where the findings made are supported by substantial evidence. *Energy Conservation Council of Pa. v. Pub. Util. Comm'n*, 995 A.2d 465, 486 n.19 (Pa. Cmwlth. 2010).

Because the Commission's interpretation of Section 1301.1(b) is not clearly erroneous and its conclusion that UGI met its burden of proof under that provision is supported by substantial evidence, there is no basis to reverse that decision.[10]

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[10] Moreover, we question whether the relief requested by OCA, the reduction of UGI's **rate base for ratemaking purposes** would be consistent with the plain language of Section 1301.1(a) or the purpose of Act 40. The General Assembly was clear that Act 40 savings, which reflect the former CTA, **are not** to be included in a utility's rate base. 66 Pa. C.S. § 1301.1(a) ("**[T]he rate base** . . . shall be based solely on the tax deductions and credits received by the
(Footnote continued on next page…)

IV. Conclusion

As the United States Supreme Court has explained, "[t]he economic judgments in rate proceedings are often hopelessly complex and do not admit of a single correct result." *Duquesne Light Company v. Barasch*, 488 U.S. 299, 314 (1989). And, in reviewing these complex matters, the Commission is given broad discretion in interpreting the Code and in setting rates. *Popowsky*, 706 A.2d at 1203. Those determinations will not be overturned unless clearly erroneous or they lack a rational basis. Because the Commission's determinations in this complex matter are consistent with Sections 315(e) and 1301.1 of the Code, and are supported, where required, by the accepted evidence, we cannot say the Commission's Decision was clearly erroneous or lacked a rational basis. Accordingly, we affirm.

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RENÉE COHN JUBELIRER, Judge

Judge Fizzano Cannon did not participate in the consideration of this matter.

(continued…)
public utility and **shall not include any deductions or credits generated by the expenses or investments of a public utility's parent or any affiliated entity**." (emphasis added)).

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

Tanya J. McCloskey, Acting Consumer Advocate, Petitioner	:	
v.	:	No. 1549 C.D. 2018
Pennsylvania Public Utility Commission, Respondent	:	

O R D E R

NOW, January 15, 2020, the Order of the Pennsylvania Public Utility Commission, entered in the above-captioned matter, is **AFFIRMED**.

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RENÉE COHN JUBELIRER, Judge