



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

BUREAU OF
INVESTIGATION
&
ENFORCEMENT

March 23, 2020

Via Electronic Filing

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

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

Dear Secretary Chiavetta,

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

Copies are being served on parties of record as identified in the attached Certificate of Service. *Due to the temporary closing of the PUC's offices, I&E is only providing electronic service. I&E has informed all parties it will only provide electronic service, and has received no objections.*

Should you have any questions or concerns, please do not hesitate to contact me.

Sincerely,

John M. Coogan
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JMC/jfm
Enclosure

cc: Honorable Steven K. Haas (*ALJ, PUC Harrisburg – via E-Mail Only*)
Honorable Benjamin J. Myers (*ALJ, PUC Harrisburg – via E-Mail Only*)
Office of Special Assistants (*via E-Mail only RA-OSA@pa.gov*)
Per Certificate of Service

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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

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

John M. Coogan
Prosecutor
PA Attorney ID No. 313920

Bureau of Investigation & Enforcement
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, Pennsylvania 17120

Dated: March 23, 2020

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I. INTRODUCTION

On February 28, 2020, Administrative Law Judges Steven K. Haas and Benjamin J. Myers (“ALJs”) issued a Recommended Decision in the above-captioned proceeding. On March 13, 2020, the Bureau of Investigation and Enforcement (“I&E”), Valley Energy, Inc. (“Valley” or “Company”), the Office of Consumer Advocate (“OCA”), and the Office of Small Business Advocate (“OSBA”) filed Exceptions to the ALJs’ Recommended Decision. In response to Valley’s Exceptions, I&E files these Reply Exceptions, addressing Valley’s Exceptions Nos. 2, 6, 7, and 8. For the reasons fully explained below, I&E respectfully requests the Commission deny these Exceptions.

II. I&E REPLY EXCEPTIONS

A. **I&E Reply to Valley Exception No. 2: The ALJs correctly denied Valley’s proposal to increase its FPFTY O&M expense based on annualization of 9-month FTY expense data**

Valley continues to claim its FPFTY expense claim should simply constitute annualized 9-month FTY actual expenses, increased by a 3% inflation adjustment. I&E avers the ALJs correctly rejected this proposition that individual expense claims not be examined. The ALJs correctly stated Valley has the burden of proof to establish the justness and reasonableness of each claim.¹ Valley’s Exception asserts its burden of proof is satisfied here where it projects most recent available costs for each individual account.² As explained in I&E’s Main Brief, Valley’s proposal presents several serious problems. First, Valley’s position renders non-company parties’ review of O&M

¹ Recommended Decision, p. 25 (citing 66 Pa. C.S. §§ 315(a), 1308(d)).

² Valley Exceptions, pp. 8-9.

expenses in a rate case essentially meaningless. Valley provided updates to essentially all of its O&M expenses in rebuttal testimony.³ Valley then points to the updates as a basis to invalidate non-company parties' O&M recommendations.⁴ Following Valley's practice to its logical conclusion, the Company would simply be allowed to update all of its O&M expenses at hearings and any non-company position to the contrary would be summarily rejected.

Second, introducing new claims after non-company parties have addressed the companies' direct position is a violation of due process principles.⁵ The concern is simple: parties have not and will not have the opportunity to evaluate late-brought claims. To be clear, I&E's position did take into account Valley's rebuttal testimony as it relates to specific claims I&E evaluated in direct testimony.⁶ But to voluminously and constantly change the Company's O&M position leaves non-company parties in a hopeless position as to issues not addressed in non-company direct testimony. Relatedly, there are clear Commission regulations that a party cannot introduce evidence in rebuttal phase that should have been included in the party's case-in-chief or substantially varies from the party's case-in-chief.⁷ Valley's attempt to wholesale revise its O&M position in rebuttal testimony, rather than specifically respond to non-company parties' O&M

³ Valley Errata Statement No. 1-R, p. 5.

⁴ Valley's witnesses Howard S. Gorman, Edward Rogers, and Jamie Levering objected to I&E's recommended O&M adjustments generally. I&E Statement No. 1-SR (Errata Version), p. 4 (citing Valley Errata Statement No. 1-R, pp. 4-6; Valley Statement No. 4-R, p. 4; Valley Statement No. 5-R, pp. 2-3).

⁵ *See, e.g., Pa. P.U.C. v. City of Lancaster Sewer Fund*, 2007 WL 517134 (Pa. P.U.C. 2007) (Commission agreed with ALJ "new claims brought in on rebuttal are improper, unfair and a violation of due process").

⁶ *See* I&E Main Brief, pp. 14-22.

⁷ 52 Pa. Code §§ 5.243(c)(2)-(3).

adjustment recommendations, is a prohibited attempt to introduce evidence that should have been introduced in direct testimony.

In addition to being procedurally improper, Valley's position creates factual inaccuracies. In rejoinder testimony, Valley witness Howard S. Gorman confirms presentation of FPFTY O&M costs is based on an escalation of FTY expenses, and does not remove non-recurring costs and plant activities.⁸ But, as Valley witness Gorman also correctly states, "the Company must support each claim made in its rate application."⁹ In direct testimony, I&E recommended adjustments for expenses that were not properly supported by the Company, properly calculated based on information provided by the Company, or were not consistent with sound ratemaking principles on an individual claim basis in the same manner in which the Company states that it is required to support each claim.¹⁰ As I&E witness Brenton Grab appropriately opines, an overall adjustment to O&M expenses is not a more accurate method of determining a Company's allowable O&M expenses.¹¹ Instead, the proper way to analyze a Company's overall O&M expenses is by analyzing individual expense claims. Accordingly, I&E witness Grab recommended disallowance of the total change made to Administrative and General Expense of \$30,096 made by Valley witness Gorman between direct and rebuttal testimony,¹² and instead recommended individual expense adjustments.

⁸ Tr., pp. 104-106.

⁹ Valley Errata Statement No. 1-R, p. 4.

¹⁰ I&E Statement No. 1-SR (Errata Version), p. 6.

¹¹ I&E Statement No. 1-SR (Errata Version), pp. 6-7.

¹² I&E Statement No. 1-SR (Errata Version), p. 9 (citing Valley Errata Statement No. 1-R, p. 5).

It is also important to realize Valley's argument would not be limited to this proceeding only. To the contrary, O&M expenses are a common point of dispute in rate cases. If the Commission allowed this practice here, it will set a very dangerous precedent that would likely be cited by any other utility company where O&M expenses are scrutinized. This will fatally handicap non-company parties' ability to evaluate individual expense accounts. Therefore, the Commission should accept the ALJs' recommendation and reject Valley's attempt to wholesale revise its O&M expenses in rebuttal testimony, and should instead evaluate the merits of the non-company parties' O&M positions.

B. I&E Reply to Valley Exception No. 6: The ALJs correctly approved I&E's Uncollectible Expense adjustment of \$24,201 based on the 3-year average write-off ratio (62%) versus the Company's reliance on the HTY write-off ratio (84%)

Valley repeats its same assertions from briefing, claiming the ALJs erred by adopting I&E's recommended \$24,201 reduction to the Company's claim of Uncollectible Accounts Expense based on three years of historic gross revenues and net write offs (i.e., 2016, 2017, and the HTY (i.e., 2018)). Valley claims actual Uncollectible Accounts Expense in 2014, 2015, and 2018 demonstrate only the write-off ratio from 2018 should be used, i.e., 62%.¹³ I&E avers the ALJs did not err because I&E demonstrated how Valley's write-off history for the HTY shows a much larger net-write off ratio than the previous two years, and, therefore, the Company would be overstating

¹³ Valley Exceptions, pp. 12-13.

its claim by basing its claim on the HTY.¹⁴ Also, as I&E noted in Reply Brief, Valley only raises use of 2014 and 2015 data for the first time in Main Brief.¹⁵ I&E objects to Valley's reliance on 2014 and 2015 data for the first time in Main Brief, thereby depriving I&E of its ability to scrutinize this contention in testimony. It therefore continues to be inappropriate for Valley to raise this point in Exceptions. Further, as I&E also explained in Reply Brief, Valley provides no discussion or analysis to explain its contention, or how it relates to or supports its claim.¹⁶ Therefore, I&E avers the ALJs did not err by accepting I&E's recommendation, and Valley's Exception should be rejected.

C. I&E Reply to Valley Exception No. 7: The ALJs' correctly declined to accept Valley's market-to-book ratio analysis to establish the ROE

The ALJs correctly declined to consider Valley's market-to-book ratio analysis to determine return on equity ("ROE"), and did not err by relying primarily on a discount cash-flow ("DCF") analysis, as compared to the Capital Asset Pricing Method ("CAPM"). Valley does not dispute the ALJs' finding the Commission has historically relied on the DCF as the preferred method for determining an appropriate ROE, with the CAPM serving as a check.¹⁷ However, Valley's Exception states the ALJs erred because they did not appropriately consider where, in *Pa. P.U.C. v. UGI Utilities, Inc. – Electric Division*, the Commission stated it will consider other methods when the DCF analysis

¹⁴ I&E Main Brief, p. 17. Specifically, The Company's three-year net write-off history is 0.49% for 2016, 0.52% for 2017, and 0.84% for the HTY.

¹⁵ I&E Reply Brief, p. 8.

¹⁶ See Valley Main Brief, p. 49.

¹⁷ Valley Exceptions, p. 13.

appears understated.¹⁸ Valley then claims the record in this proceeding demonstrates DCF results will understate the appropriate rate of return for the Company, and the Commission must consider other methods, specifically, Valley’s market-to-book ratio analysis.¹⁹

I&E asserts Valley’s Exception does not demonstrate DCF results are understated. As the ALJs note, Valley’s standalone CAPM ROE and DCF ROE were within 20 basis points, making Valley’s DCF analysis appear reasonable.²⁰ Likewise, I&E calculated a CAPM ROE of 8.04%, confirming the reasonableness of I&E’s 8.46% DCF calculation.²¹ To support its Exception, Valley wholly depends on its market-to-book ratio analysis.²² I&E avers this analysis is insufficient to show the DCF is understated or the ALJs erred. As explained in I&E’s Main Brief, Valley’s market-to-book ratio analysis is flawed because it has not demonstrated investors expect utility returns to be set on a different basis than book value.²³ Further, the Commission has consistently validated the use of the CAPM method as a check on DCF analysis, including in *UGI Utilities, Inc. – Electric Division*, unlike the market-to-book ratio analysis.²⁴ The ALJs should not be expected to use or equally weight any method offered to check the results

¹⁸ Valley Exceptions, pp. 13-14 (citing *Pa. P.U.C. v. UGI Utilities, Inc. – Electric Division*, Docket No. R-2017-2640058 (Order Entered October 25, 2018) (“*UGI Utilities, Inc. – Electric Division*”)).

¹⁹ Valley Exceptions, pp. 14-17.

²⁰ Recommended Decision, p. 68.

²¹ See I&E Reply Brief, p. 12.

²² Valley Exceptions, pp. 14-17.

²³ I&E Main Brief, pp. 43-45.

²⁴ See Recommended Decision, pp. 51-52. In *UGI Utilities, Inc. – Electric Division*, the Commission found cost of equity should “primarily be based upon the use of the DCF methodology and that the results of the CAPM analysis should be used as a comparison to the DCF results”. *UGI Utilities, Inc. – Electric Division*, p. 104.

of the DCF analysis. Because the ALJs did not err and appropriately considered CAPM analysis as a comparison to DCF results, Valley's Exception should be rejected.

D. I&E Reply to Valley Exception No. 8: The Commission should reject Valley's Exception to adjust its ROE to 10.60%

At the outset, as explained in I&E's Exceptions, the ALJs did not conclude a size risk exists for utilities, and therefore, because the Company has the burden of proof, any size adjustment should be rejected.²⁵ However, Valley's Exceptions asks that the Commission apply a further size adjustment to the ALJs' initial size adjustment, specifically, the Commission should "apply a size adjustment to the [ROE] result of the standard deviation method approved by the [Recommended Decision]", subject to a 10.60% cap, i.e., Valley's proposed ROE.²⁶ I&E initially notes the ALJs' size adjustment already effectively awards a 122 basis points size adjustment to Valley.²⁷ Valley's claim was only for a 100 basis points upward adjustment. However, Valley's Exceptions now claim the ALJs' recommendation to award an ROE at the upper end of a standard deviation of DCF results is not truly a size adjustment. Instead, this only reflects the Commission's practice regarding calculating natural gas utility Distribution System Improvement Charge ("DSIC") ROEs for larger companies, and therefore does not truly reflect an adjustment for size.²⁸

²⁵ I&E Exceptions, pp. 8-9.

²⁶ Valley Exceptions, pp. 17-18.

²⁷ See Recommended Decision, p. 74. The average of I&E's DCF results is 8.46%, and the upper end of one standard deviation is 9.68%.

²⁸ Valley Exceptions, pp. 17-19.

Valley's Exception essentially asks the Commission to completely abandon any methodological analysis, whether it be DCF, CAPM, market-to-book ratios, etc., and simply conclude that the ALJs' recommended ROE is similar to DSIC ROEs from which a further adjustment is needed. However, Valley provides no specific reason why it should be awarded at the upper end of one standard deviation of its DCF analysis other than simply stating that's how the Commission sets its DSIC ROE. By comparison, although the average of I&E's DCF analyses only supports an 8.46% ROE, the ALJs at least specifically stated they relied on a size adjustment as the reason to award an ROE at the upper end of one standard deviation. As explained in I&E's Reply Brief, Valley's reliance on the standard DSIC ROE for electric utilities is misplaced because it does not account for any of the specific facts or analyses in this case.²⁹ Although I&E disagrees with the ALJs regarding a size adjustment,³⁰ by comparison no evidence in the record exists to demonstrate why Valley should simply be awarded at the upper end of one standard deviation of its DCF analysis other than the conclusory finding the Commission does the same for DSIC ROEs. Therefore, Valley has not demonstrated the ALJs erred by not further adjusting its size adjustment, and its Exception should be rejected.³¹

²⁹ I&E Reply Brief, pp. 14-16.

³⁰ Specifically, the ALJs erred by finding evidence for a generic size effect merits a size adjustment when they did not conclude utility size effect exists. *See* I&E Exceptions, pp. 8-9.

³¹ However, as mentioned above, I&E opposes any size adjustment.

III. CONCLUSION

I&E respectfully requests the Commission reject the Exceptions of Valley Energy, Inc. discussed above, and approve the ALJs' Recommended Decision as modified consistent with I&E's Exceptions.

Respectfully submitted,

A handwritten signature in black ink, consisting of a large, stylized loop followed by a horizontal line extending to the right.

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Dated: March 23, 2020

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Pa. PUC No. 2	:	

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing **Reply Exceptions** dated March 23, 2020, in the manner and upon the persons listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a party):

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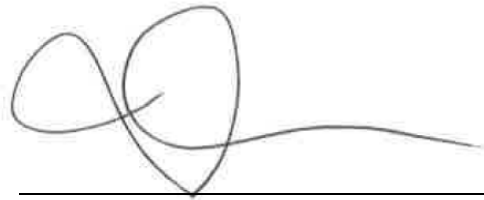
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