

R-850152

PENNSYLVANIA  
PUBLIC UTILITY COMMISSION  
Harrisburg, PA 17120

Public Meeting held February 11, 1988

Commissioners Present:

- Bill Shane, Chairman
- William H. Smith, Vice Chairman (dissenting)
- Linda C. Taliaferro, Commissioner
- Frank Fischl, Commissioner

**DOCUMENT  
FOLDER**

Pennsylvania Public Utility Commission      Docket No. M-880183

Philadelphia Electric Company

ORDER ESTABLISHING TEMPORARY RATES

BY THE COMMISSION:

On March 31, 1987, the Nuclear Regulatory Commission (NRC) issued a plant shutdown order applicable to Philadelphia Electric Company's (PECO) Peach Bottom nuclear generating facility. The NRC's order was based on evidence that certain station operators had been asleep or otherwise inattentive while on duty. After it became apparent that the Peach Bottom facility was going to be out of service more than a short period of time, the Pennsylvania Public Utility Commission, by a Secretarial Letter dated June 26, 1987, set PECO's energy cost rate at negative 10.457 mills. This action by the Commission results in the removal of the excess purchased power costs due to the shut down of the Peach Bottom facility. The "excess" purchased power cost is equal to the difference between the cost of the replacement power and the cost of power produced by the Peach Bottom plant had Peach Bottom not been shut down.

The Company is presently contesting the methodology and assumptions used by the Commission to calculate the excess purchased power costs in the investigation initiated August 20, 1987 and docketed at I-870051, P-870230, and M-870140. The Company has not contested the imprudence of the outage. Indeed, the Company has stipulated that "PECO hereby reaffirms that it

does not and will not claim replacement power costs attributable to outage periods solely and proximately caused by the NRC Shutdown Order affecting the Peach Bottom Station." Joint Stipulation filed November 23, 1987. Hearings concerning the purchased power issues commenced on February 1, 1988 before ALJ Smolen.

When the Commission issued its June Secretarial Letter, it was not unreasonable to expect that the plant would be back on line in the foreseeable future. Seven months later, it is now clear that to imagine a return to service date for Peach Bottom is to engage in a highly speculative exercise at best. It appears that the problem currently preventing Peach Bottom from restarting is not mechanical or technical in nature, but is the apparent inability of PECO's management to reorganize itself in a manner sufficient to convince the NRC that PECO can safely operate the plant.

Since the March 31, 1987 shutdown of Peach Bottom, information has appeared in the public record that aggravates the apparent seriousness and scope of that event. In addition to incidents of control room operators sleeping on the job, there have been allegations of harassment of safety personnel, improper or illegal handling of plant contamination incidents, drug use and sales within the facility by employees, use of plant computers for video games by on duty personnel, paper airplane and rubber band fights by control room operators and a near total breakdown of management discipline and control of safety related operations. On August 7, 1987, PECO submitted its so-called "Commitment to Excellence Action Plan" to the NRC, hoping thereby to gain approval for restart. On September 14, 1987, NRC Chairman Lando Zech, addressing the top management of PECO, including Chairman James L. Everett and former Chief Operating Officer J. H. Austin, Jr. stated:

Let me just say from my standpoint, this is one of the most serious meetings we have had since I have been on this commission for the past three years. It is troubling, very troubling, at least to me, to realize that we could have such a breakdown in discipline and the respect for authority and understanding of their commitment to safety as you have had, Mr. Everett, at your Peach Bottom plant. . . Part of the problem, as far as I can see, is leadership, right from the top down. I mean that. You've had a serious situation go on for a number of years, it looks like. There has been a concern about it and now we find complete inattention to duty, as you have acknowledged yourself. It's just not acceptable.

The NRC rejected the "Commitment to Excellence Action Plan" as a basis of restart on October 8, 1987. NRC regional Administrator William T. Russell, in rejecting the plan stated:

[T]here is very little in your (plan) which addresses concerns about the capabilities of corporate management to identify problems at the nuclear (facility) promptly and independent of plant line management reporting, to analyze and address such problems quickly and to assess and evaluate the results of such actions. . . . Our concerns have been heightened by the quality of your September 28, 1987 response.

The NRC announced on the same date that it was suspending consideration of plant restart until such time as PECO was able to submit a plan which satisfactorily addressed its concerns.

In September, the NRC released its latest Systematic Assessment of Licensee Performance report (SALP report) for the period February 1, 1986 through May 31, 1987 for Peach Bottom. The plant was rated unacceptable in the important categories of plant operations and weak or minimally acceptable with regard to quality assurance programs, and fire protection and housekeeping. No rating was given the Peach Bottom training program, since it appears to have been a central factor in the causes of the 1987 shutdown and was still under review.

On November 20, 1987 the Commonwealth of Pennsylvania formally requested hearings prior to the authorization of restart. On January 29, 1988, PECO released to the NRC a recently completed report by the Institute of Nuclear Power Operators (INPO), an industry organization founded by the nation's nuclear utilities to insure operating excellence at the nation's nuclear power plants. PECO released the report to the public and to this Commission on February 2, 1988. The report dated January 11, 1988, consisting of a summary cover letter and numerous attachments, indicates that the cause for the outage apparently extends beyond the personnel at Beach Bottom, and includes the very top levels of corporate management. In its January 11 summary, INPO states:

The situation that existed at Peach Bottom in the months preceding the March 31, 1987 shutdown was worse than had been conveyed to the Industry Panel and to INPO by PECO management. . . . The grossly unprofessional behavior by a wide range of shift personnel, involving all shifts, and condoned by the shift superintendents reflects a major breakdown in the management of a nuclear facility. It is an embarrassment to the industry and to the nation.

The INPO report went on to note that under present circumstances, the Company's Peach Bottom operation is so poorly rated that restart is not recommended.

After taking into account the uncertain operational status of the Peach Bottom facility, NRC reports concerning the cause of the Peach Bottom outage, the NRC reactions to PECO's abortive attempts to respond to NRC concerns, and the allegations of ineffective top management raised by INPO in its January 11 report, it is time for this Commission to initiate further action concerning the outage at Peach Bottom. Presently the Peach Bottom facility can not be described as used and useful in the public service and continued ratemaking consideration is inappropriate. PECO's present rates, established by the Commission at the conclusion of the Company's last rate case in 1986, include allowances for operating and maintenance expenses, depreciation, income taxes, interest on long-term debt, dividends for preferred shareholders, and a profit return to common equity shareholders, all associated with the Peach Bottom station.

While our previous disallowance of Peach Bottom-related excess purchased power costs is authorized by 66 Pa. C.S. §1322(a), that provision does not exhaust the Commission's ability to formulate additional regulatory remedies where appropriate and in the public interest. Indeed, 66 Pa. C.S. §1322(e) states clearly that notwithstanding the authority to disallow purchased power costs due to an outage, that provision "shall not be construed to diminish the powers and duties of the Commission under any other provision of law to reduce rates in the event of an outage. . . ." In our judgment, the circumstances surrounding this particular outage require that the Commission take additional action to protect the public interest.

It is a fundamental principle of Pennsylvania public utility law that a utility may earn a return only on that portion of its property which is used and useful in the public service. Barasch v. Pa. P.U.C., Pa. \_\_\_\_\_, 532 A.2d 325, 334 (1987). Therefore, if the Commission reasonably finds that certain property is no longer used and useful, it may exclude the value of that property from the computation of just and reasonable rates. Philadelphia Electric Co. v. Pa. P.U.C., 61 Pa. Commonwealth Ct. 325, 329, 433 A.2d 620, 623 (1981).

Peach Bottom 2 and 3 have been out of service since March 31, 1987; they have provided no electric service to the public for nearly one year and, under present circumstances, the prospect for a return to service in the near term future is remote. All indications point to management imprudence as the root cause of the outage, and PECO has not contested the Commission's regulatory actions to date on that basis. The Commission has removed from consumer rates the additional

purchased power costs due to the Peach Bottom outage but, as noted earlier, consumer rates still contain allowances for a return on the investment in these idle facilities. Given the duration of this outage and the apparent serious management deficiencies that lead to the outage, we believe that it would be inappropriate and contrary to the public interest to continue to allow PECO to earn a full return on Peach Bottom. This property is no longer used and useful in the public service and, absent further Commission action to address this situation, the Commission is of the opinion that PECO's current rates will produce an excessive return on the fair value of PECO's remaining used and useful property.

Therefore, based upon our review of the reports and records pertaining to the outage, our determination that Peach Bottom is not used and useful and our opinion that current rates are producing an excessive return, the Commission will exercise its power pursuant to 66 Pa. C.S. §1310(d) to set temporary rates for PECO for an initial trial period of six months. In the opinion of this Commission, PECO's consumer rates would produce a fair return if they were reduced to reflect disallowance of the equity return associated with Peach Bottom. Based upon our examination of the test-year data presented in PECO's last rate case at R-850152, the annual revenue requirement associated with the equity return on Peach Bottom is \$30,393,000. See Table I. We shall, therefore, order the Company to calculate and apply a negative surcharge or credit to all customer bills that, given current usage patterns, will accomplish a \$30,393,000 annual reduction in base rates. The negative surcharge shall remain in force until the Peach Bottom facility returns to service, and the Commission is satisfied that commercial operation has been achieved and the facility is once again used and useful in the public service.

Absent Peach Bottom's return to service, the temporary rates established pursuant to this order shall become permanent at the conclusion of the trial period, unless PECO files a complaint alleging that the rates prescribed by this order are unjust and unreasonable. Upon complaint, the matter will be assigned to an Administrative Law Judge for such hearings as may be necessary to resolve the relevant issues and to determine the permanent level of just and reasonable rates. Such a proceeding has the potential of involving the full gamut of rate case issues, including a determination of the Company's allowed rate of return.

The Commission would note, however, that the rate reduction ordered herein will reduce the Company's annual revenues by only 1.1% from the level of base rate revenues

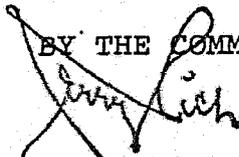
authorized in its last rate case, \$2,852.8 million. Assuming no change to the allowed rate base, the revenue reduction ordered herein will reduce the Company's overall rate of return from 12.26% to 11.95%, see Table II, and the Company's rate of return on equity from 14.75% to 13.95%, see Table II. In our judgment, these rates of return are more than compensatory given the current cost of capital for electric public utilities. Furthermore, it should be noted that our actions to date will have removed from consumer rates only the excess purchased power costs due to the outage and the equity return associated with the Company's investment in Peach Bottom. Consumer rates will still contain substantial revenue allowances for operating and maintenance expenses, depreciation charges, income tax expenses, interest on long-term debt and dividends to preferred stockholders. See Table IV. Nevertheless, the non-used and useful status of the Peach Bottom facility compels us to act promptly to insure that consumer rates will no longer include any allowance for an equity (or profit) return on those idle facilities and to communicate to the Company the seriousness with which we view the management deficiencies that have lead to this outage; THEREFORE,

IT IS ORDERED:

1. That, pursuant to our authority under 66 Pa. C.S. §1310(d), the Commission hereby establishes temporary rates for PECO equivalent to a \$30,393,000 annual reduction in consumer rates.
2. That PECO shall file, within five days of the entry date of this order, a tariff supplement which implements a negative surcharge applicable to all customer bills that, based on current usage patterns, will accomplish a \$30,393,000 reduction in its gross annual operating revenues. Said tariff supplement shall be accompanied by a proof of revenues.
3. That the tariff supplement described in ordering paragraph 2 shall be effective for service rendered on and after March 1, 1988.
4. That if PECO files a complaint alleging that the rates established by this order are unjust and unreasonable, the Office of Administrative Law Judges shall assign this matter to an Administrative Law Judge and shall schedule such hearings as may be necessary to resolve the relevant issues.
5. That a copy of this order shall be served on PECO, the Office of Trial Staff, the Office of Consumer Advocate and

the parties of record in the Company's last rate case at R-850152.

BY THE COMMISSION,

  
Jerry Rich  
Secretary

(SEAL)

Order Adopted: February 11, 1988

Order Entered: February 23, 1988

TABLE I

COMPUTATION OF PEACH BOTTOM 2 & 3  
EQUITY RETURN REMOVAL

	REFERENCE	\$000
	R-850152	
PB 2 & 3 PLANT IN SERVICE	TPH 2A C-2C	\$513,351
PB 2 & 3 ADDITIONAL AFDC	TPH 2A C-2G	\$1,468
PB 2 & 3 CWIP CA408526	TPH 2A C-8	\$20
PB 2 & 3 CWIP CA408301	TPH 2A C-8	\$3,960
PB 2 & 3 CWIP CA408301	TPH 2A C-8	(\$2,518)
PB 2 & 3 DEP. RESERVE	TPH 2A C-2C	(\$126,528)
PB 2 & 3 AFDC DEP. RES.	TPH 2A C-2G	(\$481)
PB 2 & 3 ACC. DEF. INC. TAX		(\$64,215)
PB 2 & 3 INTEREST OFFSET		(\$1,785)
NET RATE BASE IN SERVICE		\$323,272
EQUITY RETURN RATE	FINAL ORDER	14.75%
EQUITY CAPITAL STRUCTURE	FINAL ORDER	38.40%
EQUITY RETURN	FINAL ORDER	5.66%
PB 2 & 3 EQUITY INCOME		\$18,310
FIT 34 % RETURN TO REVENUE FACTOR		0.6024412
PB 2 & 3 EQUITY ELIMINATION REVENUE		\$30,393

TABLE II  
 INCOME SUMMARY  
 PHILA. ELECT.

TEST YEAR: 12 MONTHS ENDING JUNE 30, 1986

	PRESENT RATES	STAFF ADJUSTMENTS	PRO FORMA RATES	RECOMMENDED ALLOWANCE	RECOMMENDED TOTALS
	\$	\$	\$	\$	\$
OPERATING REVENUE	2,852,790	0	2,852,790	-30,393	2,822,397
DEDUCTIONS:					
O&M EXPENSES	1,431,356	0	1,431,356		1,431,356
DEPRECIATION	234,332	0	234,332		234,332
TAXES, OTHER	94,280	0	94,280	-608	93,672
INCOME TAX	357,207	0	357,207	-11,475	345,732
TOTAL DEDUCTION	2,117,175	0	2,117,175	-12,083	2,105,092
INCOME AVAILABLE	735,615	0	735,615	-18,310	717,305
COMPANY RATE BASE	6,000,125		6,000,125		6,000,125
RATE OF RETURN	12.25999%		12.26%		11.95483%
STAFF RATE BASE			6,000,122		6,000,122
RATE OF RETURN			12.26%		11.95483%

TABLE III  
RATE OF RETURN

PHILA. ELECT.

	STRUCTURE	COST		WEIGHTED COST
LONG TERM DEBT	50.90Z	10.76Z	5.47480Z	
SHORT TERM DEBT	0.00Z	0.00Z	0.00000Z	
PREFERRED STOCK	10.70Z	10.50Z	1.12311Z	
COMMON STOCK	38.40Z	13.95Z	5.35692Z	
TOTAL	100.00Z			11.95483Z

PHILA. ELECT. PHILA. ELECT. PHILA. ELECT.

TABLE IV

COMPONENT COST OF PEACH BOTTOM 2 & 3  
 CONTAINED IN THE RATES OF PHILADELPHIA ELECTRIC COMPANY  
 FROM DOCKET R-850152

	BASE	REVENUE
NET RATE BASE	\$323,272	
NON-FUEL OPERATING EXPENSES	\$23,768	\$24,243
DECOMMISSIONING	\$3,288	\$3,354
SPENT FUEL COSTS	\$4,789	\$4,885
COST OF DEBT	\$17,705	\$18,059
COST OF PREFERRED	\$3,632	\$6,029
COST OF EQUITY	\$18,310	\$30,393
DEPRECIATION	\$17,481	\$29,017
		\$115,980
NEW OVERALL RETURN	11.95%	
NEW EQUITY RETURN	13.95%	

PUBLIC MEETING OF FEBRUARY 11, 1988

STATEMENT OF VICE CHAIRMAN WILLIAM H. SMITH

RE: PHILADELPHIA ELECTRIC COMPANY,  
PEACH BOTTOM NUCLEAR GENERATING  
STATION OUTAGE  
FEB-88-C-4

In reaching my position with regard to Chairman Shane's Motion, I reviewed prior Commission action involving outages at other nuclear plants to see what action was taken to protect ratepayers.

In the case of Philadelphia Electric Company's Salem #1 Unit, the Commission investigation included an outage that lasted from February 22 to May 21, 1983. That investigation started after the outage ended and was initiated by a Petition filed by the Office of Consumer Advocate (OCA) which relied upon, among other things, a finding by the NRC that the shutdown was due to inadequate, unreasonable and improper operation by Public Service Electric and Gas of New Jersey, which operated the Salem plant for PECO and three other utilities. According to one part of that Commission Order, the NRC reviewed operation and maintenance practices at Salem and the managerial competence of the Salem management and, it concluded that the outage was caused by inadequate maintenance and supervisory practices. In that case, this Commission determined that PECO should not be permitted to recoup the \$26 million related to the Salem #1 1983 outage. This disallowance was effected through the denial of excess replacement power costs related to the Salem #1 generator outage.

Another Commission investigation involved outages at Duquesne Light Company's Beaver Valley 1 plant in 1979 which, it was alleged, was due, in part, to an NRC Order to Show Cause issued because of the NRC's concern about an incorrect seismic analysis used in the design of the plant.

Although the Duquesne outages case culminated in a settlement, one of the principal issues addressed was the question of the proper level of replacement power costs.

Our 1986 "Sunset" legislation deals specifically with "Outages of electric generating units", and provides that when a base load unit, "is out of service for more than 120 consecutive days, a utility owning a share of that unit shall not be permitted to recover...the excess energy costs incurred to generate or purchase replacement power". [Section 1322(a)]

As Chairman Shane's motion states, the Commission's action on June 26, 1987 setting a negative ECR for PECO removed the "excess" replacement power costs due to the Peach Bottom shutdown.

And, as his footnote indicates, that action ensured that PECO's ratepayers were protected from sharing in the added cost of replacement power.

Accordingly, I believe the Commission has properly moved to protect PECO's ratepayers by making the adjustment it made in June; and one mandated by law.

I'm not convinced that any further burden against the Company and its common equity shareholders will materially contribute to resolution of the problems at Peach Bottom.

2-11-88

DATE

*William H. Smith*

WILLIAM H. SMITH  
VICE CHAIRMAN