PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania 17105-3265

Implementation of Act 11 of 2012

Public Meeting held August 2, 2012
2293611-LAW
Docket No. M-2012-2293611

DISSENTING STATEMENT OF COMMISSIONER GARDNER

I believe that the Implementation Order approved today, which allows our jurisdictional fixed utilities to take advantage of a distribution system improvement charge (DSIC),[1] contains a misinterpretation of the DSIC statute. The DSIC statute states, in part, that "the cost of equity shall be the equity return rate approved in the utility's most recent fully litigated base rate proceeding for which a final order was entered not more than two years prior to the effective date of the distribution system improvement charge." 66 Pa. C.S. § 1357(b)(2).

The Commission's Tentative Implementation Order, M-2012-2293611 (May 12, 2012), opined that a stipulated cost of equity would not qualify as being the product of a fully litigated base rate case because the Commission would not have addressed and adjudicated all revenue requirement issues in a final rate order. This led to the Commission's determination in its Tentative Order that a stipulated cost of equity from the settlement of a base rate case would not be acceptable as "fully litigated" for DSIC purposes.

Various utilities and the Office of Consumer Advocate filed comments to the Tentative Order, objecting to this interpretation of the term "fully litigated." The objecting Parties argued that a stipulated cost of equity still qualified as fully litigated for the purposes of a base rate proceeding under Section 1357(b)(2) because a non-settling party in a base rate case has the ability to contest any part of a settlement, and the Commission has the final discretion to approve, modify, or reject a settlement. The majority accepts the objecting Parties' position as valid. I disagree.

A basic tenet of public utility regulation is the commission-made rate doctrine. This doctrine holds that commission-made rates are legislative actions and are "implemented subsequent to an exhaustive evidentiary presentation of the company's expenses and their reasonableness, the fair value of the utility's property used and useful in the public service, and the return on that value." *Pa. PUC v. Columbia Gas of Pa., Inc.*, Docket Nos. R-901873 et al., 1991 WL 338320 at *8 (Pa. P.U.C. Oct. 31, 1991). "The commission-made rate doctrine applies to rates that result from settlement **so long as the record is adequately developed** to allow the Commission to independently review and make determinations . . ." *Id.* at *8 (citing *Equitable Gas Co. v. Pa. PUC*, 526 A.2d 823, 830 (Pa. Cmwlth. Ct. 1987) (emphasis added).

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[1] The DSIC is an automatic adjustment charge that enables utilities to recover certain infrastructure improvement costs between base rate cases through a quarterly surcharge on customers' bills.

The key question for me is: How is the record adequately developed if the cost of equity is stipulated? The Commission is only able to independently review and determine a utility's expenses and their reasonableness, as required by law, when the record has been adequately developed. But, the record cannot be adequately developed when settlement of the revenue requirement issues within a base rate proceeding are accomplished within a "black box." Black box negotiations allow parties to negotiate their way to a base rate dollar amount that is acceptable to a majority of them. As the utilities and OCA point out in their Comments, non-settling parties may contest the settlement, and the Commission has the final discretion to approve, modify, or reject the amount of the rate increase to which the parties stipulate. However, the Commission is not privy to all of the information, compromises, and valuations that comprised that final settled rate.

For example, review of Commission's Quarterly Earnings Report of Jurisdictional Utilities for the period ended March 31, 2012 shows that 12 out of the 21 utilities covered in the report had no authorized return on equity (ROE). This is due to black box settlements of rate cases. Without this authorized ROE, the best the Commission can do is make an educated guess as to whether those utilities are overearning for the services they render to the public. While allowing the Commission to make an educated guess as to whether utilities are overearning for the services they render is a poor idea, allowing utilities that are substantially overearning to implement a DSIC surcharge is an even worse idea and does not serve the public interest.

The Commission and the Legislature have had significant time to learn from the water DSIC enacted in 1997, 66 Pa. C.S. § 1307(g). The term "fully litigated base rate proceeding" was not included in the water DSIC. Yet, the Legislature chose to include the phrase in this newly enacted statute. I believe that this was done to balance the perception that the DSIC process would be subject to little or no oversight by the Commission or that DSIC surcharges would be automatic rate increases given to utilities that are already overearning.

I believe that the DSIC is one of the most important regulatory tools that we have, and I know that it will help us accelerate the replacement of aging and unreliable utility infrastructure. But, without periodic fully litigated, non-settled, base rate cases, it is not possible for the Commission to independently review and make determinations concerning our utilities' expenses and their reasonableness, the fair value of the utilities' property used and useful in the public service, and the return on that value. Therefore, I must respectfully dissent.

August 2, 2012
Date

Wayne E. Gardner, Commissioner