**PENNSYLVANIA**

**PUBLIC UTILITY COMMISSION**

**Harrisburg, PA 17105-3265**

Public Meeting held March 14, 2013

Commissioners Present:

Robert F. Powelson, Chairman

John F. Coleman, Jr., Vice Chairman

Wayne E. Gardner

James H. Cawley

Pamela A. Witmer

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| Petition of Columbia Gas of Pennsylvania, Inc. forApproval of its Long-Term Infrastructure Improvement Plan Petition of Columbia Gas of Pennsylvania, Inc. forApproval of a Distribution System Improvement Charge |  Docket Number: P-2012-2338282 P-2012-2338282 |

**OPINION AND ORDER**

**BY THE COMMISSION:**

Before the Commission for consideration are the Petitions for approval of the Long-Term Infrastructure Improvement Plan (LTIIP) and the Distribution System Improvement Charge (DSIC) of Columbia Gas of Pennsylvania (Columbia or Company).

**HISTORY OF THE PROCEEDING**

Columbia is a corporation organized and existing under the laws of the Commonwealth of Pennsylvania. Columbia is in the business of selling and distributing natural gas to retail customers within the Commonwealth, and is therefore a “public utility” within the meaning of Section 102 of the Public Utility Code, 66 Pa. C.S. §§ 102, subject to the regulatory jurisdiction of the Commission. Columbia, as an NGDC, provides natural gas service to approximately 415,000 residential, commercial, and industrial customers in portions of 26 counties throughout its greater York and Western Pennsylvania service territories. Columbia provides service through approximately 7,350 miles of mains and 400,000 services that it owns, operates and maintains.

The LTIIP was filed on December 7, 2012, and the DSIC was filed on January 2, 2013. Copies of the LTIIP Petition were served on the statutory advocates as well as the active parties in Columbia’s current base rate case proceeding, docketed at R‑2012‑2321748 and M‑2012‑2323645, in accordance with *Implementation of Act 11 of 2012*, Docket No. M‑2012-2293611 (August 2, 2012) (Final Implementation Order). Columbia’s DSIC Petition includes proposed Supplement No. 194 to Tariff Gas – Pa. P.U.C. No. 9 to introduce the DSIC Rider into the Company’s tariff with an effective date of March 3, 2013. The filing was made pursuant to 66 Pa. C.S. § 1353 and the Final Implementation Order.

Columbia Industrial Intervenors (CII) filed comments on December 27, 2012. CII does not object to Columbia’s proposed LTIIP at this time. However, CII indicates that, if the Commission was to approve Columbia’s proposal to replace customer-owned gas service lines as part of the LTIIP, then that proposal should be addressed in the LTIIP proceeding, and CII would request that the LTIIP be referred to the Office of Administrative Law Judge (OALJ) for a full evidentiary hearing on the merits. In addition, CII calls for a thorough review of the scope of investment in capital improvements in the LTIIP to ascertain that they are limited to DSIC-eligible assets. On January 22, 2013, CII filed a Petition to Intervene and Answer.

The Office of Consumer Advocate (OCA) filed comments on January 4, 2013, but did not initially request hearings. On January 22, 2013 OCA filed a Notice of Intervention, a Formal Complaint and Public Statement, and an Answer to Columbia’s DSIC Petition. In its Answer to the Columbia DSIC Petition, OCA states that the Commission should deny Columbia’s Petition as filed, suspend the proposed Tariff Supplement No. 194 to Tariff Gas – Pa. P.U.C. No. 9, and order a full hearing and investigation pursuant to OCA’s complaint. (OCA Answer, p. 1).

On January 22, 2013 the Office of Small Business Advocate (OSBA) filed a Notice of Intervention and an Answer. OSBA requested hearings and such relief as may be necessary or appropriate. OSBA also filed an Answer. OSBA did not allege that any particular provision or relief requested by Columbia should be denied.

On January 22, 2013, Penn State University (Penn State) filed a Petition to Intervene but did not allege any specific opposition to the Columbia petitions. Penn State affirmatively asserted that it had no issues with Columbia’s LTIIP.

G. Thomas Smeltzer, an individual customer, filed a Formal Complaint on January 30, 2013. Mr. Smeltzer asserted that Columbia has a rate case pending before the Commission and that the DSIC seems to be a way for a utility to receive money before customers receive service. He questions how the elderly on fixed incomes will be able to pay higher bills. Letters expressing opposition to the Columbia DSIC were received from four other individual customers. On January 18, 2013, Henry Senatore questioned whether it is truly necessary to accelerate repair and recovery and whether Columbia actually needs more revenue. On January 18, 2013, Eugene D. Dellinger asserted that utility profits should be used to repair utility lines and equipment that should have been maintained over prior years. On January 28, 2012, Bonnie Smith asserted the request is excessive and should be denied. On February 13, 3013, Alex Barna asserted that Columbia should have been setting aside funds in an escrow account to pay for infrastructure repairs and replacement. All four asserted that a DSIC will have a detrimental effect on person who are elderly, retired, and/or on fixed incomes.

Columbia filed reply comments on January 22, 2013, in response to the OCA’s comments to Columbia’s LTIIP petition

 No objections or comments were received from federal, state or local governmental agencies.

**BACKGROUND**

On February 14, 2012,Governor Corbett signed into lawAct 11 of 2012, (Act 11),[[1]](#footnote-1) which amends Chapters 3, 13 and 33 of Title 66. Act 11, *inter alia*, provides jurisdictional water and wastewater utilities, electric distribution companies (EDCs), and natural gas distribution companies (NGDCs) or a city natural gas distribution operation with the ability to implement a DSIC to recover reasonable and prudent costs incurred to repair, improve or replace certain eligible distribution property that is part of the utility’s distribution system. The eligible property for the utilities is defined in 66 Pa. C.S. §1351. Act 11 states that as a precondition to the implementation of a DSIC, a utility must file a LTIIP with the Commission that is consistent with 66 Pa. C.S. §1352.

On April 5, 2012, the Commission held a working group meeting for discussion and feedback from stakeholders regarding its implementation of Act 11. On May 10, 2012, the Commission issued a Tentative Implementation Order addressing and incorporating input from the stakeholder meeting. Stakeholders filed comments to the Tentative Implementation Order on June 6, 2012. On August 2, 2012, the Commission issued the Final Implementation Order, at Docket Number M-2012-2293611, establishing procedures and guidelines necessary to implement Act 11.

**COLUMBIA’S LTIIP PETITION**

**Columbia’s Petition**

 Columbia has been identifying and repairing or replacing its distribution infrastructure on an accelerated basis since 2007. Through this process, Columbia was able to ascertain that most leaks in its system occur in areas with a high concentration of aging pipe. According to Columbia, 85 percent of all the leakage that occurs annually on mains in the Columbia distribution system is a result of corrosion on first generation mains and service lines. This is because bare steel and cast iron mains are 16 times more likely to experience leakage than plastic or cathodically protected mains.

 Columbia indicates that between 2002 and 2006, it retired 1,070,310 feet of bare steel or cast iron pipe or approximately 214,000 feet of pipe annually. Since 2007, as Columbia began to accelerate the replacement rate of bare steel and cast iron pipe, it has invested over $400 million to replace approximately 2,595,167 feet of pipe or approximately 432,528 feet of pipe annually. According to Columbia, in 2011 alone, it spent approximately $92 million and replaced 533,765 feet of bare steel and cast iron pipe, which equates to an annual replacement of over 5.2 percent of Columbia’s remaining first generation pipes. Columbia avers that it replaced 586,113 feet of main in 2012.

 Columbia states that since starting the major distribution infrastructure replacement program in 2007, it has reduced open Class 2 leaks by nearly 50 percent. In addition to decreasing the number of leaks, the main replacement program will also allow the distribution system to operate at higher pressures which will in turn substantially reduce the current need for pressure regulators in the system, thereby making the system safer, easier and more reliable to operate.

 For new and replacement mains and service lines, Columbia is using plastic or cathodically protected steel throughout its system. Coated steel pipe continues to be used when higher distribution pressures are required; however, such pipe is cathodically protected with an electric current. Cathodically protected steel has all the advantages of steel in terms of strength, and because of its impressed electric current, is highly corrosion resistant. Columbia indicates that currently, approximately 10 percent of the existing priority pipelines are operating at high pressure (greater than 60 psig), which generally requires the installation of coated steel pipe instead of plastic. In essence, as these system replacements are designed, a large portion of the existing high pressure pipelines will be replaced with coated steel; the percentage of steel pipelines installed each year will depend on the projects selected for replacement for that year.

 According to Columbia, plastic pipe has proven to be very good for distribution-level pressures. It has strength and flexibility, and as a result, is generally immune to the stress of ground movement. Plastic is also less costly to purchase and easier to join and install than steel pipe, does not corrode, and does not require cathodic protection. Columbia states that since 2007, at least 90 percent of the pipelines installed were plastic. As a result, based on current trends, Columbia estimates that it will continue, on average, to install 90 percent or more of plastic pipelines on an annual basis.

Columbia asserts that its LTIIP will allow Columbia to maintain its accelerated main replacement program, with over 500,000 feet of main replacement proposed for each of the plan’s next five years. The LTIIP also has a projected average annual spending of $131,480,000 on infrastructure replacement from 2013 through 2017. This represents a significant increase over the average annual investment of $78,338,500 during the years 2007 through 2012.

 Columbia’s LTIIP addresses the seven elements as required in the Final Implementation Order.[[2]](#footnote-2)

 **(1) TYPES AND AGE OF ELIGIBLE PROPERTY**

**Columbia’s Petition**

Columbia’s LTIIP indicates that portions of its system date back to the 1800s. Columbia’s system comprises many different types of pipes, fittings, and appurtenances. According to Columbia, in the oldest portions of its system, cast iron was used because at the time of construction it was considered relatively strong and easy to install. However, since cast iron is vulnerable to breakage from ground movement, the gas industry transitioned to bare steel and wrought iron piping by the early 1900s up till the 1960s. Columbia states that a significant portion of its system is composed of bare steel which is also subject to corrosion. Nevertheless, the industry moved to the use of plastic piping in the 1970s. Aldyl-A (first generation plastic pipes) is a common plastic material used but is vulnerable to stress propagation cracking. Aldyl-A is currently being replaced with medium density 418 polyethylene pipe.

 Columbia states that in addition to replacing first generation mains made out of the above three identified materials; it is also replacing associated distribution and safety equipment that is compatible with the upgraded design. Columbia indicates that it will also install excess flow valves, install or relocate automated meter reading systems, replace risers, meter bars, and service regulators. Columbia states that all of the facilities included in its LTIIP are considered “eligible property” under 66 Pa. C.S. § 1352.

 Columbia is also currently replacing customer-owned service lines in tandem with its main replacement program. Columbia notes that, in 2008, the Commission approved Columbia’s request to replace customer-owned service lines in conjunction with its main replacement efforts.[[3]](#footnote-3) Columbia books the cost of these customer-owned service line replacements in its mains account just as it would book the cost of other customer-owned property such as driveways that are replaced as part of a main replacement project. Since instituting the main replacement program, Columbia avers that it has increased the number of customer-owned service lines replaced annually from 421 in 2007 to 5,296 in 2011. Columbia anticipates that it will replace 7,000 to 9,000 customer-owned service lines per year over the next five years for a total of approximately 36,000 service lines by the end of 2017. Columbia asserts that gas service lines and insulated and non-insulated fittings are considered eligible property under 66 Pa. C.S. § 1351(2)(iii) of Act 11. Columbia states that the investment in customer-owned service lines is directly and solely driven by its accelerated infrastructure replacement program. Columbia also states that it is appropriate that these investments booked to the mains account be considered DSIC-eligible property as “other related capitalized costs under 66 Pa. C.S. § 1351(2)(x).

**Comments**

 In its Comments, OCA agrees that the Commission’s *Service Line Waiver Order* authorizes Columbia to capitalize customer-owned service line replacement costs in rate base and to recover such costs in base rates. OCA avers, however, that the Commission has not determined that customer-owned service line replacement costs are eligible for recovery through DSIC. OCA therefore recommends that Columbia’s proposal to treat the investment in customer-owned service lines as eligible for recovery through the DSIC, be reviewed and considered as part of Columbia’s DSIC filing rather than the present LTIIP filing.

 CII takes the same position as the OCA. CII states that the eligibility of customer-owned service lines should be more appropriately addressed in Columbia’s DSIC proceeding. CII specifically mentions that if the Commission approves Columbia’s LTIIP prior to the outcome of the DSIC proceeding, it requests that the Order not address replacement of customer-owned service lines as the LTIIP does not seem to be the appropriate venue for full and complete review of Columbia’s proposal. CII indicates that if the Commission does address Columbia’s proposal to replace customer-owned gas service lines in this proceeding, then the LTIIP should be referred to the OALJ for a full evidentiary hearing on the merits.

**Resolution**

The Commission acknowledges OCA and CII’s concerns regarding Columbia’s inclusion of service line work in its LTIIP and the description of the costs associated with customer-owned service lines as DSIC-eligible assets. Because this is a combined LTIIP and DSIC proceeding, we shall address this issue at this point in our consideration of the two Columbia petitions.

Section 1352 of the Public Utility Code specifically requires a utility to submit a LTIIP for Commission approval in order to qualify for DSIC recovery. This provision ensures that quarterly DSIC repairs, improvements, and replacements to eligible property are made consistent with a LTIIP that has been approved by the Commission through careful examination.

Columbia proposes to include customer-owned service lines in its LTIIP. In particular, Columbia proposes to capitalize costs associated with the replacement of customer-owned service lines as part of its accelerated main replacement program. This is consistent with Columbia’s work on customer-owned service lines since 2008. The Commission allows Columbia to pay for the cost of replacing customer-owned service lines and to capitalize those costs. Thus, we find that Columbia’s plan to coordinate customer-owned service line replacement along with its main replacement plans is reasonable, and that Columbia’s LTIIP is the logical vehicle for such coordination. CII and OCA assert no reason to prohibit Columbia from addressing customer-owned service lines in its LTIIP other than their concern that inclusion in the LTIIP would mean that the costs could be recovered through the DSIC mechanism.

OCA and CII are concerned that Columbia’s inclusion of the customer-owned service lines in its LTIIP would lead to classification of the costs associated with customer-owned service lines as DSIC-eligible assets. OCA and CII contend that the cost of customer-owned service lines should not be recoverable through the DSIC surcharge. They assert that this matter should be assigned to the OALJ for evidentiary hearings.

We conclude that such concerns do not warrant exclusion of the customer-owned service lines from Columbia’s LTIIP, especially since it is reasonable to include this work as part of Columbia’s overall infrastructure improvement plans and because customer-owned service line costs can be capitalized by Columbia pursuant to the *Service Line Waiver Order*. The LTIIP is a comprehensive planning document encompassing more than what may be recoverable via the DSIC mechanism. Act 11 requires that, for costs to be DSIC-eligible, the work underlying those costs must have been contemplated within the utility’s LTIIP; it does not specify that all LTIIP work and costs must be DSIC-recoverable or that inclusion of such work would warrant rejection of the LTIIP.

Accordingly, we will approve the inclusion of customer-owned service lines as part of their LTIIP. Inclusion in the LTIIP does not necessarily qualify customer-owned service lines, or any other expenditure, as DSIC-recoverable property. Therefore, we shall refer the matter of DSIC recovery of customer-owned service line expenditures to the OALJ.

Upon review of Columbia’s LTIIP and all supplemental information and explanations filed, the Commission finds that the requirements of element one of the Final Implementation Order of Act 11, types and age of eligible property, has been fulfilled.

 **(2) SCHEDULE FOR PLANNED REPAIR AND REPLACEMENT OF ELIGIBLE PROPERTY**

**Columbia’s Petition**

Columbia’s focus under the accelerated main replacement program in the next five years is replacing existing bare steel and cast iron mains and other related facilities based on the needs driven by the distribution system (condition and age of the pipe, geographical proximity, leak history, the capacity needs of the area, and expected growth in system demand requirements). Columbia annually attempts to identify the highest risk segments and prioritizes those segments each year using the Optimain DS® as a tool to identify the most efficient plan to accomplish this goal.

 Optimain DS® is a comprehensive software solution used by all NiSource Gas Distribution Companies (Columbia’s counterparts) to help assess and prioritize the risk associated with priority mains and allocate capital towards those risks. Optimain DS® utilizes many environmental and pipe condition factors obtained from field reports to develop and calculate the risk for each segment of pipe. Leak history, pipe condition and depth, coating condition, pipe size, and pressure and pipe material are some examples of the factors used. First generation pipes are susceptible to failure from corrosion, cracks and leakage. According to Columbia, if other facilities are located adjacent to the projects that are prone to fail (unprotected coated steel pipe, ineffectively coated steel pipe, Aldyl-A, *etc*.), those facilities will also be replaced.

 Columbia posits that the replacement schedule is also consistent with its Distribution Integrity Management Program (DIMP) plan that complies with 49 CFR §192.1007. Columbia avers that it referenced replacement programs as one of the measures to reduce risk in its DIMP plan. Columbia’s pipe replacement program impacts risk and reduces the probability of three threats identified by the DIMP Steering Team (corrosion, natural forces damage, and material or weld failure).

 Columbia anticipates completing the replacement of cast iron and bare steel mains in approximately 17 years, or by the end of 2029. Columbia also anticipates replacing approximately 2,800,000 feet of cast iron and bare steel mains over the next five years. As noted above, Columbia will also install excess flow valves and regulators and also replace risers and meter bars in concert with the service line replacements. The quantities of these additional facilities will be reflective of the number of service line replacements. Columbia also states that it will continue to replace meters and while meter replacement will be driven by conditions found on each service location, it plans on replacing approximately 9,000 to 14,000 meters annually over the next five years.

**Comments**

 In its Comments, OCA indicates that Columbia anticipates replacing its entire unprotected bare steel and cast iron pipe inventory in approximately 17 years without justifying why a 17-year replacement time-frame was selected as being appropriate to provide and maintain safe and adequate service. OCA further calls for Columbia to provide a breakdown of its pipe materials (unprotected bare steel, protected bare steel and cast iron) to be replaced in the next five years. OCA also requests among other things, basic performance information for Columbia’s system, such as leak rates per 1,000 services by material type or leaks per mile of main by pipe material type, types of meters targeted to be replaced, relocation of inside meters (if any), a breakdown of the LTIIP projects showing pipe diameter of the current and replacement pipe so that increased capacity can be evaluated.

**Resolution**

 In response to OCA’s request for data or studies supporting the 17-year geographic replacement program, Columbia provided a study done by Stone & Webster Management Consultants, Inc. (Stone & Webster) dated March 30, 2007, that assesses a 20-year duration for the bare steel and cast iron replacement plan. Columbia indicated that during the period from 2002 to 2006 it reduced its inventory of bare steel and cast iron mains by 97 miles, or 24.25 miles per year. With a remaining inventory of 2,262 miles of mains at the end of 2006, and projecting a continuing replacement/retirement rate of 24.25 miles per year, it would take approximately 94 years to complete the retirement/replacement of first generation facilities. This means at this rate, the last segments of cast iron and bare steel pipes would be replaced in the year 2100, or about 70 years later than Columbia’s currently anticipated replacement program completion date.

 Columbia asserts that, based on current information on leak rates of its mains, this replacement rate was inadequate and unsustainable. The Stone & Webster study proposed a replacement rate of 111 miles per year for Columbia to completely replace/retire its cast iron and bare steel mains in 20 years. Columbia has indicated that with its in-depth knowledge of its system, and as a prudent and cautious operator, it has elected to eliminate most of its leak prone facilities in 17 years.

 Columbia also provided information on leak rates per 1,000 services by material type or leaks per mile of main by pipe material type. In targeting meters for replacement, Columbia identified meters that do not fit the standard 1-inch meter bar that is standard today as one of the reasons for replacing such meters. Other meters targeted for replacement include: damaged or corroded meters, leaking meters, meters not compatible with the ITRON AMR deployment, meters where the capacity needs have changed and meters that are identified by a statistical sampling program as having higher failure rates than the typical meter population. Columbia also routinely relocates all inside meters to an outside location that is served off of facilities that are placed in conjunction with its accelerated infrastructure replacement program.

To the extent that Columbia has relied on its current DIMP plan, prepared pursuant to 49 CFR § 192.1107, in developing its LTIIP, Commission review at this docket of the Columbia DIMP plan is limited to a determination of consistency between the LTIIP and the DIMP plan. With this Order, the Commission makes no determination as to the adequacy of Columbia’s DIMP plan.

Upon review of Columbia’s LTIIP and all supplemental information and explanations filed, the Commission finds that the requirements of element two, schedule for its planned repair and replacement, of the Final Implementation Order, has been fulfilled.

 **(3) LOCATION OF ELIGIBLE PROPERTY**

**Columbia’s Petition**

Columbia states that mains manufactured using cast iron, bare steel, and Aldyl-A are located throughout Columbia’s 26 county certificated service territory in Western and South Central Pennsylvania. Columbia utilizes a systemic approach to determining the property to be replaced based on age, condition, geographical proximity, leak history, and capacity needs of the area. The specific projects identified are then engineered for a calendar year beginning in the fourth quarter of the preceding year in accordance with expected capital budgets. Columbia anticipates using the Annual Asset Optimization Plan (AAO Plan) required by Section 1356 to provide the Commission with current specific annual replacement projects as well as address any changes that were made in the implementation of the prior year’s plan.

**Comments**

No comments were received regarding the location of eligible property.

**Resolution**

Upon review of the LTIIP, the Commission finds that element three, the location of eligible property requirement, of the Final Implementation Order has been fulfilled.

 **(4) REASONABLE ESTIMATES OF THE QUANTITY OF PROPERTY TO BE IMPROVED**

**Columbia’s Petition**

Columbia states that, on an average basis since 2007, it has doubled its bare steel and cast iron retirements/replacement to approximately 430,000 feet per year, compared to the average of approximately 214,000 feet per year retired/replaced between 2002 through 2006. From 2013 through 2017, Columbia intends to maintain its accelerated pace and projects to replace at least 500,000 feet of pipe per year.

As stated under element three (schedule for repair and replacement), Columbia intends to replace approximately 2.8 million feet of pipeline over the five-year plan with yearly breakdown shown in Table 1. Columbia states that in addition to main replacements, it anticipates replacing 7,000 to 9,000 customer service lines per year for the next five years for a total of approximately 36,000 service lines by the end of 2017. While meter replacement will be driven by conditions found at each service location, approximately 9,000 to 14,000 meters will be replaced per year over the next five years. Columbia will also install other related eligible facilities such as risers, meter bars, valves and regulators, *etc*.

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| **Table 1: Columbia’s 2013-2017 Reasonable Estimate of the Quantity of Property to be Improved** |
| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 5 year total |
| Projected annual feet of pipe | 625,000 | 625,000 | 525,000 | 525,000 | 500,000 | 2,800,000 |

**Comments**

No comments were received regarding this aspect.

**Resolution**

Upon review of the LTIIP, the Commission finds that element 4, the reasonable estimate of the quantity of property to be improved requirement, of the Final Implementation Order has been fulfilled.

 **(5) PROJECTED ANNUAL EXPENDITURE AND MEASURES TO ENSURE THAT THE PLAN IS COST EFFECTIVE**

**Columbia’s Petition**

Columbia’s projected annual budget is shown in Table 2. Annual investments in distribution infrastructure replacement will exceed $115 million per year with a total of over $657 million over the next five years. These estimates are based, among other things, on current capital markets, current economic conditions, and Columbia’s projected revenues given its current rate structure.

 Columbia states that it reassesses its system and projects are reprioritized each year based on the most current data available. Columbia characterizes its current list of distribution improvement projects as a dynamic roster that is subject to modification based on emerging conditions. Columbia avers that it maximizes efficiencies and minimizes costs by addressing large segments of the system and carries out replacement on a planned, systemic basis. One way Columbia minimizes cost through systemic approach is by integrating its program work with state and municipal improvements.

 In addition, contractor resources are concentrated and competitive bidding processes are leveraged in order to drive down the cost of time and materials. Competitive bidding allows Columbia to secure long-term lower unit cost contracts with various utility installation contractors. It also allows Columbia to purchase larger quantities of construction materials resulting in lower cost and long-term contracts. This has helped Columbia to reduce cost by moving away from segment by segment approach.

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| **Table 2: Columbia’s Projected Annual Budget for Age and Condition, Upgrade and Mandatory Replacement 2013-2017 (Dollar Figures in Millions)** |
| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 5 year total |
| Projected Annual Budget | $151.6 | $148.0 | $120.6 | $119.4 | $116.9 | $656.5 |

**Comments**

 OCA states that Columbia identifies higher-risk segments of its cast iron and unprotected bare steel mains but plans to mix replacement of the higher-risk segments with its “larger geographic replacement area” approach. OCA alleges that Columbia is not clear about how higher-risk segments would be prioritized in a given year if they do not align with the geographic replacement areas chosen for that year. OCA asserts that Columbia should provide the Commission with more detailed information that highlights how its geographic approach effectively addresses replacement of its higher-risk main segments and is consistent with the risk-reduction goals of its Distribution Integrity Management Plan.

**Resolution**

Columbia asserts that it uses an assessment tool called “Optimain” that uses an algorithm to assess dozens of pre-determined risk factors and scores the resultant risk. In addition, Columbia conducts quarterly meetings at each local Operations Center with its field supervisory, operating, engineering, and pipeline safety personnel to review any segments that are identified by the field maintenance teams as being in very poor condition. Columbia uses the two processes, along with planned state, municipal or utility highway work occurring in that year to determine the ultimate list of segments to be replaced.

Columbia also asserts that a “systematic” geographic replacement strategy is more cost-effective than a “segmented” approach targeting specific poorly-performing targets. Columbia indicates that an examination of NPL Construction Company’s (NPL) annual bid reveals that larger “systemic” projects are less costly on a unit basis than small “segmented” projects. NPL is Columbia’s current largest single new-and-replacement-construction contractor. NPL also accounts for one-third of the blanket construction excavation work carried out in Columbia’s system. Columbia also provided several risks assessment tests it applies to determine “prone to fail” adjacent facilities that will be replaced at the same time it is replacing its mains.

The LTIIP is not a micromanagement tool. As Columbia notes, the decisions must be dynamic. While Columbia has indicated that some of its decision-making will be driven by economics as mandated by Act 11, there no basis to conclude that Columbia plans to sacrifice safety for the sake of cost effectiveness.

Upon review of Columbia’s LTIIP and all supplemental information and explanations filed, the Commission finds that the requirements of element five of the Final Implementation Order, projected annual expenditures and measures to ensure that the plan is cost effective, has been fulfilled.

 **(6) ACCELERATED REPLACEMENT AND MAINTAINING SAFE AND RELIABLE SERVICE**

**Columbia’s Petition**

The FinalImplementation Order noted that utilities should reflect and maintain acceleration of infrastructure replacement. Utilities that have already taken substantial steps towards increasing capital investment to address the issue of aging infrastructure needed to reflect in their LTIIP how the DSIC will maintain or augment acceleration of infrastructure replacement and prudent capital investment.

 Columbia states that it has already taken substantial steps to increase the replacement of its distribution infrastructure. As stated earlier, since starting in 2007, Columbia doubled the rate at which it replaced its aging mains. Columbia, in its LTIIP, proposes to maintain its accelerated main replacement program with more than 500,000 feet of main replacement each year for the next five years. The projected average annual spending of $131,480,000 on infrastructure replacement from 2013 through 2017 represents a significant increase over the average annual investment of $78,338,500 during the years 2007 through 2012.

 Columbia asserts that replacement of aging distribution equipment and facilities will reduce the number of leaks on its system, allow it to install additional safety mechanisms, and generally improve service to customers. Columbia avers that the DSIC will allow Columbia to continue its already accelerated pace for replacing its distribution infrastructure.

Table 3 below shows a comparison of Columbia’s main replacement activity in three periods. Period 1 includes annual footage of cast iron and bare steel (priority) pipe replaced for the six year period prior to the initiation of Columbia’s accelerated replacement program. Period 2 depicts the amount of priority pipe replaced by year since the accelerated program began in 2007, and Period 3 projects the annual footage of pipe to be replaced under the terms of the LTIIP.

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| **Table 3: Priority Pipe Retired/Replaced Per Year (Feet)** |
| **Period 1** | **Period 2** | **Period 3** |
| **Year** | **Ret./Replaced** | **Year** | **Ret./Replaced** | **Year** | **Ret./Replaced** |
| 2002 | 232,320 | 2007 | 355,764 | 2013 | 625,000 |
| 2003 | 179,520 | 2008 | 528,567 | 2014 | 625,000 |
| 2004 | 201,520 | 2009 | 344,488 | 2015 | 525,000 |
| 2005 | 174,240 | 2010 | 322,583 | 2016 | 525,000 |
| 2006 | 282,518 | 2011 | 533,765 | 2017 | 500,000 |
|  |  | 2012 | 510,000 |  |  |
| **Average** | **214,062** | **Average** | **432,528** | **Average** | **560,000** |

Columbia’s annual service lines replacement has also increased during this period from an average of 3,289 feet per year in Period 1 to 6,260 feet year in Period 2. Period 3 is estimated at 8,000 feet per year of service lines replacement.

In terms of capital spending within the same period, Columbia has increased from $107,144,000 for an average of $21,428,800 per year in Period 1 to $470,031,000 for an average of $78,338,500 per year in Period 2. This is an increase of approximately 339 percent from the previous period. For the period of the LTIIP (Period 3), Columbia anticipates spending $657,400,000 or approximately $131,480,000 per year.

**Comments**

In its comments, OCA asserts that Columbia stated that as part of its main replacement program, it will increase pressure across its system and that increasing pressure will increase the deliverability of gas by adding capacity. According to OCA, Columbia’s LTIIP does not specify by what amount capacity will increase or how the additional capacity will be used and useful in the provision of utility service. OCA suggests that Columbia provide a breakdown of its LTIIP projects to show pipe diameter of the current and replacement pipe so that increased capacity can be evaluated.

OCA also indicates that on a going-forward basis, for each main project that increases system pressure or is not a ‘like-for-like” pipe diameter replacement, the Commission should have Columbia provide the results of system network analysis before and after the segment installation to confirm that the project is DSIC-eligible.

**Reply Comments**

Columbia indicates that it will be replacing the current cast iron and bare steel pipes with new plastic pipes and, in some cases, such as bridge attachments, it will be installing cathodically protected coated steel pipes. Columbia stated that time and advances in technology have shown that cast iron and bare steel pipelines are not the best material to ensure a safe and reliable distribution system in the future. Columbia will replace its aging infrastructure with facilities that are capable of handling gas at higher pressures than the current pipelines. According to Columbia, this will increase the capacity of its system, even where existing facilities are replaced with smaller diameter piping. Columbia posits that adopting OCA’s recommendations would require Columbia to provide a system network analysis for virtually every pipe replacement before the pipe would be considered DSIC-eligible. Columbia alleges that this would constitute an unreasonable burden and potentially deter investment by creating an unnecessary question as to cost recovery.

Columbia further indicates that OCA did not provide any legal basis for asserting that only pipes of equal diameter and pressure may be DSIC-eligible. Columbia asserts that, in many cases, it will be installing smaller diameter pipelines when it replaces aging mains. For example, to save costs, Columbia may install smaller diameter plastic facilities to replace larger diameter steel piping by inserting the new pipe through the old pipe. This approach allows Columbia to avoid excavating an entire street for main replacement.

**Resolution**

We conclude that there are sufficient consumer protection mechanisms in place at the Commission to address OCA’s concerns. Section 1356 requires a utility with an approved DSIC to file an AAO Plan. As noted above, Columbia anticipates using its AAO Plan to provide the Commission with current specific annual replacement projects as well as address any changes that were made in the implementation of the prior year’s plan. The elements of an AAO Plan include (1) a description of all eligible property repaired, improved and replaced in the preceding 12 months and (2) a detailed description of all facilities to be improved in the upcoming 12 months. Also, the AAO Plan is expected to demonstrate compliance in meeting the LTIIP and to identify a utility’s near-term construction projects that will be funded by the DSIC, consistent with the LTIIP. The Commission’s Bureau of Audits also conducts periodic review of DSIC related projects.

Columbia, in essence, explains in its Reply Comments that higher pressure pipelines are necessary for the safety and reliability of its distribution system and that using higher pressure pipelines is consistent with the Commission’s determination in its Final Implementation Order. Columbia further highlights on the safety and benefits of using higher pressure and smaller diameter pipelines on certain main replacements, emphasizing that it has no incentive to significantly increase capacity on its system.

Therefore, the Commission concludes that, while it will not specifically require Columbia to submit results of system analysis network before and after the segment installation to confirm DSIC eligibility of related projects, OCA’s concern will be addressed through the AAO Plan review and through other various Commission reviews of DSIC-related projects.

Upon review of Columbia’s LTIIP and all supplemental information and explanations filed, the Commission finds that the requirements of element six of the Final Implementation Order of Act 11, manner in which replacement of aging infrastructure will be accelerated and how repair, improvement or replacement will maintain safe and reliable service, have been fulfilled.

 **(7) WORKFORCE MANAGEMENT AND TRAINING PROGRAM**

**Columbia’s Petition**

Columbia’s workforce is comprised of employees who work directly for Columbia and workers who are hired by contractors of Columbia. Columbia utilizes a wide variety of programs and tools to ensure that it has a qualified workforce. Also, Columbia has been developing a strategy to address future workforce planning issues since 2008. In 2009, Columbia hired a full time workforce planning coordinator to help develop a comprehensive, long term strategy to address the challenges of an aging workforce.

 Columbia enhanced its recruiting efforts to address the volume of hiring as well as ensuring a more diverse workforce by reaching out to local minority groups, military sites, and community and technical schools in order to alert them of job opportunities. Columbia also brought the pipeline locating function back in-house in order to hire new employees into the organization and put them into roles that will allow them to learn Columbia’s system, develop new skills and eventually move into jobs that are vacated by promotions or retirements.

 Lastly, to improve workforce planning, Columbia created multi-skilled positions, which offers Columbia the flexibility to utilize workers based on the peak needs of the business. According to Columbia, these multi-skilled employees provide the flexibility to better respond to customer needs and thereby enhance cost effectiveness.

 On the use of contractors, Columbia avers that discussions with its affiliated service entity, NiSource Corporate Services Company, began in early 2011 on the impact of escalating capital improvement program on the supply of construction contractors. This led to the decision to proceed with a Contractor Acquisition Strategy to build longer term relationships with blanket contractors. Columbia stated that from early to mid-2012, meetings were held with incumbent blanket contractors to share Columbia’s plans and begin dialogue around the proposed enhancements to the blanket construction contracts, which included extending the term of some contracts until December 31, 2015, to ensure a sufficient supply of contractors accessible to Columbia.

 Columbia also states that in order to ensure that all employees and contractors are qualified, the NiSource Gas Distribution companies maintain a written Operator Qualification Plan applicable to all Columbia employees, contractors and mutual aid individuals who perform covered tasks on behalf of Columbia. This plan also encompasses all aspects of ensuring a qualified workforce and that its operations comply with relevant Federal Pipeline Safety Regulations. A copy of this plan was filed along with the LTIIP.

**Comments**

 In its comments, OCA acknowledges that Columbia’s LTIIP contains the DOT Operator Qualifications Plan and lists the NiSource gas affiliates that follow the plan. OCA points out that the list, however, excludes the NiSource Massachusetts affiliate, Bay State Gas Company. OCA, therefore, requests Columbia to provide a copy of that plan with an explanation of how it differs from the plan adopted for the Pennsylvania distribution affiliate.

**Resolution**

In response to OCA’s request, Columbia provided a copy of the DOT Operator Qualification Plan for the Bay State Gas Company (d/b/a Columbia Gas of Massachusetts) (CMA). According to Columbia, CMA is covered under the Northeast Gas Association (NGA) Operator Qualification program. Columbia also indicates that the NGA program is used by almost all the New England LDC’s and their contractors. Columbia pointed out task nomenclature as the most obvious difference between the two plans. Columbia avers that both plans have provisions for establishing covered tasks and intervals, non-qualified individuals working under direct observation, questioning and re-evaluating an individual due to an incident or performance of a task, communication of change, training, and record keeping.

 Upon review of Columbia’s LTIIP and all supplemental information and explanations filed, the Commission finds that the requirements of element seven of the Final Implementation Order, a workforce management and training program, have been fulfilled.

**LTIIP SUMMARY**

The Commission has reviewed each of the seven required elements of Columbia’s Petition for Approval of its LTIIIP individually and has taken into account the comments received on this petition.  We have directed that the issue of whether customer-owned service line costs, incurred by Columbia as part of its LTIIP and/or pursuant to the *Service Line Waiver Order*, may be recovered through a DSIC mechanism be assigned to the OALJ for evidentiary hearings.

                        While the Commission’s *Final Implementation Order* stated, at page 18, that the LTIIP “need only address the specific property eligible for DSIC recovery,” the inclusion of arguably non-DSIC-eligible property does not void the LTIIP application, nor is the inclusion of such property in the LTIIP dispositive of whether the cost of that project will be afforded DSIC recovery.  The issues of eligibility and cost recovery, for all property claimed as DSIC-eligible, are to be addressed and resolved in the subsequent DSIC petition and calculation.  Accordingly, Columbia’s LTIIP is approved.

**COLUMBIA’S DISTRIBUTION SYSTEM IMPROVEMENT CHARGE PETITON**

Section 1353 requires utilities to file a petition seeking approval of a DSIC that includes the following:

1. An initial tariff that complies with the Model Tariff adopted by the Commission, which includes:
	1. A description of eligible property;
	2. The effective date of the DSIC;
	3. Computation of the DSIC;
	4. The method for quarterly updates of the DSIC; and
	5. A description of consumer protections.
2. Testimony, affidavits, exhibits, and other supporting evidence demonstrating that the DSIC is in the public interest;
3. A Long Term Infrastructure Improvement Plan (LTIIP) as described in Section 1352, 66 Pa. C.S. § 1352;
4. Certification that a base rate case has been filed within five years prior to the filing of the DSIC petition; and
5. Other information required by the Commission.

Columbia’s petition addresses each of the elements listed in the statute.

 **(1) Tariff Filing**

Section 1353 requires utilities to file an initial tariff that complies with the Model Tariff adopted by the Commission. Columbia’s proposed Supplement No. 194 to Tariff Gas – Pa. P.U.C. No. 9 (Supplement No. 194) closely reflects the language of the Model Tariff. We shall review each item in turn.

 **(a) Eligible Property**

**Columbia’s Petition**

Columbia designates the same property as DSIC-eligible as it included in its LTIIP, including piping, couplings, gas service lines, valves, excess flow valves, risers, meter bars, meters, unreimbursed costs related to highway relocation projects, service lines, and other related capitalized costs. Eligible property for NGDCs is defined in Section 1352, 66 Pa. C.S. § 1351(2).

As noted in the LTIIP discussion above, Columbia proposes to include its investment in customer-owned gas service lines in its DSIC. Replacing these service lines is an integral part of Columbia’s strategy for improving the safety and quality of its distribution system. The bare-steel customer-owned service lines have been subject to the same elements that affect the physical integrity of the Company-owned mains that are being replaced. Columbia could not continue to provide service to these customers without replacing the customer-owned service lines because the lines are incapable of handling the new system pressures and are not up to current code requirements.

While the customer owns these service lines, it is necessary for Columbia to undertake replacement of them on its own in order to maintain the speed and efficiency of its replacement strategy. According to Columbia, the investment in customer-owned service lines is directly and solely driven by Columbia’s accelerated infrastructure program.

The Commission previously approved a petition by Columbia to allow replacement of all customer-owned service lines at the Company’s cost where doing so is necessitated by Columbia’s main replacement and upgrade program. The cost of replacement of customer-owned service lines has been included in all of the Company’s rate cases since such approval; therefore, the Company maintains that inclusion of customer-owned service lines in the DSIC is logical. *See Service Line Waiver Order*.

**Comments**

In its Petition to Intervene and Answer, CII is concerned with Columbia’s proposal to replace customer-owned service lines in conjunction with the Company’s main replacement program and to include these customer-owned lines as DSIC-eligible property. CII notes that although these customer-owned lines may need to be replaced at the same time as Columbia’s pipes, they do not fit clearly within the definition of “eligible property” for purposes of the DSIC. CII Answer at 4-5.

OCA also submits concern over the Company’s proposal to treat the costs associated with replacing customer-owned service lines as DSIC-eligible property. The OCA requests that this should be fully examined by the Commission, as the statute limits DSIC-eligible property to “costs incurred to repair, improve or replace eligible property that is part of the *utility’s*distribution system.” 66 Pa. C.S. § 1351. OCA Answer at 3-4.

OCA and CII have expressed concern that Columbia has proposed treating customer service lines in conjunction with the Company’s main replacement program as DSIC eligible property. This concern was also raised in comments to Columbia’s LTIIP. Both OCA and CII have requested evidentiary hearings to review this matter.

**Resolution**

As noted above in the LTIIP section, the Commission approved Columbia’s petition at P‑00072337 to pay for the cost of replacing customer-owned service lines and capitalization of these costs. Section 1510 of the Public Utility Code addresses ownership and maintenance of natural gas service lines and prohibits a utility from acquiring or assuming ownership of pipe installed after the section’s effective date in 1984 except to the extent permitted by then existing tariffs. Consequently, we granted that Columbia’s request for limited waivers of the provisions of its tariff to permit Columbia to replace certain customer-owned service lines. We also found that it is in the public interest for Columbia to replace at its expense certain customer-owned service lines when the lines must be replaced as a result of Columbia’s main replacement and upgrade program. *See Service Line Waiver Order.*

As addressed as part of our discussion of Columbia’s LTIIP above, the Commission agrees with Columbia that such service line projects are reasonable to include in Columbia’s LTIIP and that the costs associated with replacing customer-owned service lines that are part of its accelerated main replacement program/LTIIP may qualify as DSIC-eligible projects. However, since the OCA and CII have challenged the recovery of these costs in the DSIC, the Commission will refer the issue of whether the costs associated with customer-owned service lines are recoverable through the DSIC mechanism to the OALJ for hearing and recommended decision.

 **(b) Effective Date**

**Columbia’s Petition**

Columbia’s proposed Supplement No. 194 has an issued date of January 2, 2013 and an effective date of March 3, 2013. Company witness Nancy Krajovic states that Columbia filed its DSIC as early as permitted by Act 11, and that because tariff supplements are filed on sixty days’ notice, the earliest effective date for the DSIC is March 3, 2013. Columbia DSIC Petition at 4.

**Comments**

OCA, OSBA, and CII have filed to intervene. Requests were made to assign some matters to OALJ for evidentiary hearings. However, no specific comments have been filed regarding the effective date of Columbia’s DSIC tariff.

**Resolution**

Given that the parties have raised issues and requested hearing regarding certain elements of Columbia’s DSIC petition, we shall refer those issues to OALJ for hearing and recommended decision. However, consideration of those issues need not delay implementation the DSIC mechanism itself. We shall permit Columbia to implement a **DSIC mechanism**, pursuant to a tariff filed on a 10-day notice and in compliance with the directives in this order, but note that the rates charged pursuant to the DSIC surcharge shall be subject to recoupment and refund after final resolution of the issues brought before the OALJ. Therefore, based on requirements for DSIC quarterly updates, as more fully described below, the Commission directs Columbia to file a tariff no later than March 20, 2013, if Columbia wishes to have an effective date of April 1, 2013.[[4]](#footnote-4) Columbia’s tariff must be modified in a tariff filing as directed by the Commission in this Order.

 **(c) Computation of the DSIC**

**Columbia’s Petition**

With Supplement No. 194, Columbia proposes a DSIC of 1.90%, which the Company avers was calculated consistent with the Model Tariff in the Final Implementation Order. The formula for calculation of the DSIC is as follows:

DSIC = (DSI \* PTRR)+Dep+e

 PQR

Where:

DSI = Original cost of eligible distribution system improvement projects net of accrued depreciation.

PTRR = Pre-tax return rate applicable to DSIC-eligible property.

Dep = Depreciation expense related to DSIC-eligible property.

e = Amount calculated under the annual reconciliation feature or Commission audit.

PQR = Projected quarterly revenues for distribution service (including all applicable clauses and riders) from existing customers plus revenue from any customers which will be acquired by the beginning of the applicable service period.

Columbia’s calculation (in thousands) is:

DSIC = (28,997 \* 3.01%)+150

 53,896

Columbia witness Krajovic pointed to numerous inputs required by Act 11 for the DSIC calculation that were not fully compliant in Columbia’s Petition. She stated that these rates would be updated to reflect the actual capital structure and cost rates as of January 31, 2013 when the filed-for DSIC was submitted on February 19, 2013. In particular, she explained, that by law, DSIC will begin recovery of eligible property placed in service during the three-month period ending one month prior to the effective date of the DSIC. Therefore, for a DSIC effective March 3, 2013, the three-month period is November through January. Columbia’s Petition, however, provided only actual data for eligible property placed into service in November 2012; December 2012, and January 2013 reflected projected data for eligible property placed in service. Additionally, the Company’s current capital structure and cost rates for long-term debt and preferred stock reflected the actual cost rates as of November 30, 2012. Columbia Statement No. 6 at 5.

On February 21, 2013, Columbia filed updated information and calculations reflecting actual data for eligible property placed into service during the entire three-month period, November through January. The result is a proposed DSIC of 2.29% calculated as follows (in thousands):

DSIC = (33,789 \* 3.06%)+175

 52,725

Columbia’s last base rate case was settled without a specified rate of return on equity (ROE); therefore Columbia used an ROE of 10.4% in calculating its DSIC. Columbia avers this ROE was based on the Commission’s decision in *PPL Electric Utilities Corporation*, Docket No. R‑2012‑2290597, which was fully litigated, and is consistent with the DSIC ROE of 10.46% proposed by the Utility Sub-Group in the Commission’s Act 11 ROE Working Group.[[5]](#footnote-5) Columbia states that when the Commission publishes an ROE to be used for DSIC purposes, it will revise its tariff filing to reflect the allowed ROE.

Columbia proposes to use one-fourth of its projected annual distribution revenues to calculate projected quarterly revenues, which, according to the Company, makes the DSIC more simple and reflective of the fixed nature of Columbia’s investments. Columbia witness Krajovic further explains that heating service drives a significant portion of Columbia’s load and since Columbia’s rate design is largely volumetric, its revenue stream is seasonal. The Company has, therefore, chosen to base its quarterly revenues on one-fourth of its projected annual revenues to match the fixed nature of the investment that the DSIC will be recovering. Columbia Statement No. 6 at 6.

**Comments**

OCA claims that Columbia’s DSIC calculation is incorrect because: 1) The DSIC computation does not reflect the impact of accumulated deferred income taxes (ADIT) associated with DSIC investments made by the Company, which in turn permits Columbia to earn a return on an investment balance that exceeds Columbia’s actual investment; 2) The calculation of the state income tax component of the DSIC revenue requirement determination requires further examination to ascertain whether it is consistent with the actual taxes paid doctrine; and 3) The ROE used by Columbia is excessive. OCA Answer at 2.

**Resolution**

Columbia acknowledges in its original DSIC filing that its calculations were not in precise compliance with the law because: 1) The inputs for eligible plant were based on forecasted, not actual, data for two of the three months; 2) The current capital structure and cost rates for long-term debt and preferred stock were as of November 30, 2012, and should be reflective of the capital structure and cost rates as of January 31, 2013; and 3) The ROE was an estimate based on another utility’s rate case and did not reflect that of the DSIC ROE as determined by the Commission. Columbia filed updated information on February 21, 2013, along with a new DSIC calculation. Columbia also provided actual data for plant additions, depreciation, and capital costs and structure.

Based on requirements for DSIC quarterly updates, as more fully described below, the Commission directs Columbia to file a DSIC tariff using actual data for eligible property placed into service during the three-month period of December through February.

In the calculation of its proposed DSIC, Columbia used a quarterly depreciation expense equal to the total monthly depreciation multiplied by three. The Commission directs Columbia to use the actual depreciation expense booked for eligible plant during the specified three month period to calculate its quarterly depreciation expense, which is consistent with what has been allowed for the water utility DSICs as accepted by the Bureau of Audits and approved by the Commission.

The cost of equity determinations in the Commission’s Staff Report on Quarterly Earnings of Jurisdictional Utilities (Quarterly Report) are used for DSIC calculations if more than two years have elapsed since a utility’s last fully litigated base rate case. 66 Pa. C.S. § 1357(b)(3). If, in any quarter, a utility will earn more than the ROE used for the DSIC calculations (which may be the ROE determined in the Staff Quarterly Report), the DSIC will be reset to zero. 66 Pa. C.S. § 1358(b)(3). Accordingly, the DSIC must remain at zero until such time that the utility, in a subsequent quarter, earns less than the ROE used for the purpose of DSIC calculation.

It is clear that Columbia’s cost of equity used in the calculation of the estimated DSIC does not comply with these regulations. Since Columbia’s last base rate case was settled without a specified ROE, Columbia estimated an ROE. Columbia used 10.4% as its ROE which appears to be taken from the recent PPL base rate case at Docket No. R‑2012‑2290597. Additionally, Columbia attempted to justify its proposed ROE of 10.4% by citing a 10.46% ROE proposed by the Utility Sub-Group in the Commission’s Act 11 ROE Working Group. Columbia’s ROEs of 10.4% and 10.46% are not obtained according to 66 Pa. C.S. § 1357(b)(3). Therefore, consistent with Section 1357(b)(3), the current Staff Quarterly Report for the quarter ending September 30, 2012 (3rd Quarter Report) contains appropriate ROE calculations.

The Staff Quarterly Report uses the DCF model, CAPM, and informed judgment to determine the ROE used for water utility industry DSIC purposes. The Staff Quarterly Report contains similar information for the gas utility industry with the exception of an explicit gas utility DSIC ROE. The gas industry market indicated ROE range is calculated and can be used to attain a DSIC ROE for Columbia. The DCF model indicates an ROE range of 7.75% to 9.66% and the CAPM ROE range is 4.69% to 5.70%. Using these calculations and informed judgment, the Staff Quarterly Report indicates a recommended **ROE of 9.70%** for an NGDC DSIC filing at this time.[[6]](#footnote-6)

The Model Tariff makes available to utilities two options for calculating projected quarterly revenues: 1) The summation of projected revenues for the applicable three-month period; or 2) One-fourth of projected annual revenues. Because of the seasonal nature of its revenue stream, Columbia chose to use one-fourth of its projected annual distribution revenues as its projected quarterly revenues. The Model Tariff permits the use of one-fourth of annual revenues and the Final Implementation Order recognized the seasonality of revenues issue. Therefore, Columbia’s use of one-fourth of its projected annual distribution revenues as its projected quarterly revenues is appropriate.

OCA opines that Columbia’s DSIC calculation should be adjusted to reflect the impact of ADIT associated with DSIC investments made by the Company; otherwise Columbia will earn a return on an investment balance that exceeds Columbia’s actual investment. That is, ADIT can be viewed as a source of zero cost capital. OCA Answer at 3. The Commission in its Implementation Order has determined that the “adjustment, which was not previously used in the DSIC by the water industry, would add unnecessary complexities to the DSIC and, accordingly, will not be included in the model tariff.” Final Implementation Order, p. 39.

Additionally, OCA is reviewing the calculation of the state income tax component of the DSIC revenue requirement determination to ensure that ratepayers receive the full benefit of the tax deductions consistent with the actual taxes paid doctrine. OCA Answer at 3.

We will refer OCA’s issues related to the impact of ADIT associated with DSIC investments, the calculation of the state income tax component of the DSIC revenue requirement, and, appropriate ROE,[[7]](#footnote-7) to the OALJ for further disposition. To the extent that Columbia may be permitted to implement a DSIC pending the OALJ proceeding and chooses to do while these matters are pending in the OALJ, the DSIC recovery shall be subject to recoupment and refund after final resolution.

 **(d) Quarterly Updates**

**Columbia’s Petition**

A utility’s DSIC is subject to quarterly updates to reflect eligible plant additions placed in service during the three-month period ending one month prior to the effective date of any DSIC update. Proposed Supplement No. 194 includes a chart of the effective dates of Columbia’s proposed DSIC updates, and the corresponding period for eligible plant additions that will be reflected in each update. The Company states that once its DSIC is implemented, customers will receive notice of quarterly changes in the DSIC through bill messages, consistent with Act 11 and the Final Implementation Order.

**Comments**

No comments were filed regarding this aspect.

**Resolution**

In accordance with 66 Pa. C.S. § 1358(e)(2), the revenue received under the distribution system improvement charge for the reconciliation period shall be compared to the utility's eligible costs for that period. The difference between revenue and costs shall be recouped or refunded, as appropriate, in accordance with section 1307(e), over a one-year period or quarterly period commencing April 1 of each year. Based on the statute mandating over/under collections be refunded commencing April 1 of each year, the Commission directs the Company to modify the effective dates of Columbia’s proposed DSIC updates, and the corresponding period for eligible plant additions that will be reflected in each update. The quarterly updates shall be scheduled for April, July, October, and January.

 **(e) Consumer Protections**

**Columbia’s Petition**

In accordance with the Model Tariff and consistent with Section 1358, Columbia’s proposed Supplement No. 194 also includes the following customer safeguards:

1. A 5.0% cap on the total amount of revenue that can be collected by Columbia as determined on an annualized basis;
2. Annual reconciliations performed by Columbia;
3. Audits conducted by the Commission;
4. Customer notice of any changes in the DSIC;
5. A reset of the DSIC to zero as of the effective date of new base rates that include the DSIC-eligible plant; and
6. Provisions for the charge to be set at zero if, in any quarter, Columbia’s most recent earnings report shows that Columbia is earning a rate of return that exceeds the allowable rate of return used to calculate its fixed costs under the DSIC.

As a customer safeguard, the Model Tariff states that the DSIC shall be applied equally to all customer classes. Columbia added to this a provision that specifies that the Company may reduce or eliminate the Rider DSIC to any customer with competitive alternatives or potential competitive alternatives and customers having negotiated contracts, which is consistent with the Final Implementation Order. Columbia has excluded the Rider DSIC charge from tariffs for customers with competitive alternatives and negotiated contracts. Testimony submitted by Columbia states “a provision has been added that specifies that the DSIC will not be applied to any customer with competitive alternatives or negotiated contracts.” Columbia Statement No. 6 at 3-4.

**Comments**

CII notes that although Columbia’s Petition indicates that the DSIC will not apply to customers with negotiated rates, the language in proposed Supplement No. 194 suggests that the Company will retain discretion regarding whether to apply the DSIC to these customers. CII asserts that this creates uncertainty for these customers regarding if, or when, the DSIC will be applied to their service, and suggests that Columbia modify the tariff language to clarify its intent to exclude these customers. CII Answer at 4-5.

OCA also claims that the language in Columbia’s proposed tariff relating to customers with competitive alternatives is not consistent with Act 11 and the Final Implementation Order. Columbia’s proposed language would allow the Company to reduce or eliminate the DSIC for customers with “potential competitive alternatives.” OCA submits that this is overly broad and not consistent with the Commission’s intent. OCA Answer at 2 and 4.

**Resolution**

Columbia’s proposed Supplement No. 194 is consistent with the Model Tariff and complies with the customer safeguards required by 66 Pa. C.S. § 1358. Additionally, the Company has provided language in its tariff which excludes those customers with competitive alternatives or negotiated contracts that is consistent with the Final Implementation Order. Prior to such a change going into effect, the Commission must review any future tariff change that would exclude and/or include any customer class. Therefore, the current language as provided which excludes customers with competitive alternatives or negotiated contracts will be allowed.

 **(2) Public Interest Considerations**

**Columbia’s Petition**

According to the Company, implementing the proposed DSIC and allowing proposed tariff Supplement No. 194 to go into effect is in the public interest because the DSIC will ensure that customers continue to receive safe and reliable service in the future as required by Section 1501, 66 Pa. C.S. § 1501.

In 2007, Columbia began a significant distribution system infrastructure evaluation, repair and replacement program that is focused primarily on those portions of its system that were constructed using cast iron and bare steel pipe. Cast iron is vulnerable to breakage from ground movement and bare steel is subject to corrosion. Columbia has determined that there are an increasing number of leaks in areas with a high concentration of aging pipe. The Company avers that the DSIC will allow for the continuation of the infrastructure improvement process without the risk of uncertainty or delay.

Columbia has replaced approximately 2.6 million feet of pipe since the beginning of 2007. The Company avers that as a result of its program, open Class 2 leaks have been reduced by nearly 50% since 2007. Columbia avers that the proposed DSIC will allow the Company to continue its already accelerated pace for replacing its distribution infrastructure, resulting in fewer leaks, the installation of additional safety mechanisms, and improved service to customers.

Columbia further avers that its infrastructure replacement program will allow the distribution system to operate at higher pressures. According to the Company, higher pressures will substantially reduce the current need for pressure regulators, making the system safer, easier and more reliable to operate. A distribution system operating at these higher pressures also will enable Columbia to install additional new safety devices in areas to be upgraded. This includes excess flow valves, which will shut off gas to a residence or business in the event of a large pressure differential, which is typically indicative of a major gas leak or a service damaged by excavation. Columbia avers that the DSIC will allow it to remove deteriorating portions of its system, ultimately leading to enhanced safety and better service for its customers.

**Comments**

No comments were received regarding the supporting evidence that Columbia’s DSIC is in the public interest.

**Resolution**

Section 1353 requires testimony, affidavits, exhibits, and other supporting evidence to be submitted demonstrating that the DSIC is in the public interest. Based on Columbia’s submitted direct testimony by the Company’s Director of Rates and Regulatory Affairs and exhibits demonstrating how the proposed DSIC supports accelerated infrastructure improvement, the Commission concludes that the DSIC filing is in the public interest and that the Company has met its obligation under Section 1353.

 **(3) Long Term Infrastructure Improvement Plan**

Section 1353 requires that the utility have an approved Long Term Infrastructure Improvement Plan (LTIIP). Columbia filed a LTIIP with the Commission on December 7, 2012, which is recommended for approval concurrently with the DSIC.

 **(4) Base Rate Case**

Section 1353(b)(4) requires a utility to certify that it has filed a base rate case within the five years prior to the date of its DSIC petition. Columbia has provided the required certification that its last base rate case, under which Columbia’s current base rates were established, was filed on January 14, 2011.[[8]](#footnote-8) Columbia has a base rate case currently pending before the Commission at Docket No. R‑2012‑2321748, which was filed on September 28, 2012.

 **(5) Other Information Required by the Commission**

**Section 1354 - Customer Notice**

Pursuant to Section 1354, a utility is required to provide customer notice of: 1) Submission of the DSIC petition; 2) Commission’s disposition of the DSIC petition; 3) Any quarterly changes to the DSIC rate; and 4) Any other information required by the Commission. Columbia has verified that it will provide customer notice of the proposed DSIC, Commission action thereon, and quarterly updates through bill inserts, consistent with Act 11 and the Final Implementation Order.

Columbia will provide a bill insert to all customers informing them of the filing, the estimated impact of a DSIC on their bills and their rights to intervene in the proceeding. The language on the bill insert was circulated to, and reflects comments provided by, the Commission’s Communications Office and Bureau of Consumer Services, and OCA.

The Commission agrees that this is consistent with the notice requirements set forth in the Model Tariff, Act 11, and the Final Implementation Order.

**Bills Rendered or Service Rendered**

The Final Implementation Order directed utilities to bill customers for the DSIC on a bills rendered basis versus a service rendered basis[[9]](#footnote-9), based on current practice and procedure for water companies. (*See* 66 Pa. C. S. § 1358). Columbia’s proposed tariff did not specify whether billing for the DSIC would be on a bills rendered or a service rendered basis. Therefore, in accordance with the Final Implementation Order, we direct Columbia to modify the language in the proposed tariff to specify that customers would be billed for the DSIC on a bills rendered basis.

**Section 1355 – Commission Review**

Section 1355 provides that the Commission shall, after notice and opportunity to be heard, approve, modify or reject a utility’s proposed DSIC and initial tariff. The Bureau of Technical Utility Services has reviewed Columbia’s proposed DSIC and proposed tariff Supplement No. 194 and has determined that the filing contains all necessary items identified in Section 1353.

**DSIC SUMMARY**

We will approve the proposed DSIC calculation and tariff subject to the modifications consistent with this Order, including the following:

1. A tariff filed on ten days’ notice with an effective date no earlier than April 1, 2013;
2. A three-month period of December through February for eligible plant additions;
3. A quarterly depreciation expense based on actual booked depreciation expense;
4. A return on equity of 9.70%.

Section 1355 also states that the Commission shall hold evidentiary and public input hearings as necessary to review the petition. As noted above, OCA, OSBA, CII, and Penn State have petitioned to intervene in Columbia’s DSIC proceeding, and there were requests to hold evidentiary hearing on several aspects of the DSIC.

Accordingly, in addition to referring the matter of DSIC recovery of costs associated with customer-owned service lines to OALJ as provided in our discussion of Columbia’s LTIIP, we shall also refer the impact of ADIT associated with DSIC investments, the calculation of the state income tax component of the DSIC revenue requirement, and the question of an appropriate ROE to OALJ for evidentiary hearings and preparation of a recommended decision. To the extent that Columbia elects to implement a DSIC mechanism prior to resolution of these matters, any recovery will be subject to refund or recoupment consistent with final determinations on these matters referred to OALJ.

We note the filings by of Penn State, OSBA, Mr. Smeltzer, Mr. Senatore, Mr. Dellinger, Ms. Smith, and Mr. Barna. We conclude that they have not articulated a basis for denying Columbia the opportunity to implement a DSIC mechanism, consistent with our discussion above.

**CONCLUSION**

Upon review, the Commission finds that the Columbia Long-Term Infrastructure Improvement Plan and manner in which it was filed conforms to the requirements of Act 11 and our Final Implementation Order.

Additionally, the Commission finds that the Petition of Columbia for a Distribution System Improvement Charge complies with the requirements of Act 11 and our Final Implementation Order. Moreover, the Commission has reviewed the filing and does not find it to be inconsistent with the applicable law or Commission policy. Subject to recoupment and/or refund pending final resolution of the matters referred herein to the OALJ, Columbia may elect to implement a DSIC mechanism consistent with this order on ten days’ notice; **THEREFORE,**

**IT IS ORDERED:**

1. That the Petition for approval of a Long-Term Infrastructure Improvement Plan (LTIIP) filed by Columbia Gas of Pennsylvania is approved, consistent with this Order.

2. That the Petition for approval of a Distribution System Improvement Charge (DSIC) filed by Columbia Gas of Pennsylvania is approved, consistent with this Order.

3. That Columbia Gas of Pennsylvania shall file a tariff, consistent with this Order, on ten days’ notice to be effective April 1, 2013. Revenues collected pursuant to said tariff will be subject to refund and recoupment based on the Commission’s final resolution of the matters referred herein to the Office of Administrative Law Judge for hearing and recommended decision.

4. That the following issues be assigned to the Office of Administrative Law Judge for hearing and preparation of a recommended decision:

* 1. DSIC-recovery of costs related to customer owned service lines;
	2. Impact of accumulated deferred income taxes associated with DSIC investments;
	3. Calculation of state income tax component of the DSIC revenue requirement; and
	4. Return on equity, to the extent not resolved herein.

5. The Complaint of G. Thomas Smeltzer is dismissed.

**BY THE COMMISSION,**

 Rosemary Chiavetta

 Secretary

(SEAL)

ORDER ADOPTED: March 14, 2013

ORDER ENTERED: March 14, 2013

1. <http://www.legis.state.pa.us/WU01/LI/LI/US/HTM/2012/0/0011..HTM>. [↑](#footnote-ref-1)
2. The Final Implementation Order requires the inclusion of the following seven elements in the LTIIP:

	1. Types and age of eligible property;
	2. Schedule for its planned repair and replacement;
	3. Location of the eligible property;
	4. Reasonable estimates of the quantity of property to be improved;
	5. Projected annual expenditures and measures to ensure that the plan is cost effective;
	6. Manner in which replacement of aging infrastructure will be accelerated and how repair, improvement or replacement will maintain safe and reliable service; and
	7. A workforce management and training program. [↑](#footnote-ref-2)
3. *Petition of Columbia Gas of Pennsylvania, Inc. for Limited Waivers of Certain Tariff Rules Related to Customer Service Line Replacement*, P-00072337 (May 19, 2008) (*Service Line Waiver Order*). [↑](#footnote-ref-3)
4. The quarters are fixed by statute. If Columbia does not have an effective date of April 1, 2013, the next earliest effective date would be July 1, 2013. [↑](#footnote-ref-4)
5. *See Act 11 ROE Working Group*, M-2012-2317272. [↑](#footnote-ref-5)
6. We note here that, based upon the input provided by the ROE Working Group, the Commission may authorize changes in the Staff Quarterly Report protocols on a going-forward basis. [↑](#footnote-ref-6)
7. If the parties agree on the ROE designated herein, based on the current Quarterly Earnings Report, there will be no need to address ROE in the OALJ proceeding. [↑](#footnote-ref-7)
8. Docket No. R-2010-2215623 (October 14, 2011). [↑](#footnote-ref-8)
9. “Bills rendered” bills are computed based on the effective tariff rate at the time of the bill. “Service-rendered” bills are prorated based on service rendered before and after a tariff rate change. [↑](#footnote-ref-9)