



Testimony for Public Hearing on House Bill 1294

before the

Pennsylvania House Consumer Affairs Committee

April 28, 2011

Good morning. My name is Nancy Krajovic and I am here on behalf of Columbia Gas of Pennsylvania. Columbia appreciates the opportunity to talk with you today about the benefits and sensibility of the alternative regulatory mechanisms that House Bill 1294 would enable.

The primary and overarching goal of Columbia Gas is to deliver gas to our customers safely and reliably. Cast iron and bare steel pipe comprise over 1,900 miles or 26% of Columbia's local distribution system. As those facilities now approach the end of their useful lives, we must move from a maintenance focus to a replacement focus for aging infrastructure in order to remain consistent with our goal of safe and reliable service. These circumstances are the backdrop for the long-term accelerated pipe replacement effort that Columbia undertook several years ago. The costs associated with this effort are staggering. For instance, over only the next six years, Columbia anticipates investing more than \$625 million to replace over 700 miles of pipe and associated services. Along with that investment come hundreds of good-paying jobs that will contribute to the Commonwealth's economy.

As you know, utilities do not have the ability to just raise their rates to recover increased expenses or investments in new or upgraded facilities. Instead, we must file a base rate case with the Public Utility Commission. A base rate case is a complex, time-consuming and expensive process that involves the review of all aspects of a utility's business, not just new expenses or investments that generate the need for adjusted rates. Columbia Gas can incur \$1,000,000 in costs in litigating a base rate case –

which is about the same amount it costs to replace more than a mile of old pipe. Of course the difference is the \$1,000,000 invested in replacing pipe will be providing useful service for the next 100 years, whereas the \$1,000,000 spent on litigating a rate case is simply charged to customers without providing any comparable benefit. I also note that the million dollars doesn't include the resources spent on these cases by the PUC and the Consumer Advocates, and those offices are supported by assessments on the utilities, which are in turn recovered from our customers.

At the end of a base rate case, the rates that are approved will only reflect the pipe in the ground at that point in time. As Columbia continues to make additional investment in these facilities, those rates quickly become insufficient to recover our incremental costs and provide the authorized rate of return on the company's assets. The inability to earn on and recover on investments made between rate case filings is called regulatory lag. That financial indicator impacts the company's ability to attract reasonably priced capital to finance its ongoing pipeline replacements. In order to mitigate that degradation of earnings as much as possible it is currently necessary for Columbia to file frequent rate cases. Failure to do so means that the pipe replacement will be more expensive than necessary because of higher cost borrowings. Those higher costs are ultimately passed on to our customers. Since our infrastructure replacement began, Columbia has filed three base rate proceedings with the Public Utility Commission – the first one in 2008, 13 years after the most recent base rate case at the time. Since the 2008 case, we filed again in January of 2010 and most recently in January of this year. Under the current regulatory construct, as long as Columbia remains committed to replacing its aging infrastructure – and we will remain so

committed – these frequent cases will continue. The provision in HB 1294 permitting the use of a fully projected test year in a base rate proceeding will address the regulatory lag that results in insufficient cost recovery as soon as new rates are effective. In years gone by, this lag could be offset by growth in customer base and consumption, but the past decade has seen decreases in consumption in the gas industry due to more efficient appliances and processes and conservation efforts. That shift in consumption demands that the regulatory process be modified to continue to allow utilities an opportunity to collect enough revenues to cover costs and earn a return that will facilitate investment at the least cost of capital available. Passage of HB 1294 will provide that correction.

As I mentioned before, base rate proceedings are complex, time-consuming, and labor intensive. They require the exchange of an enormous amount of detailed information, the vast majority of which has very little to do with capital investment or pipe replacement. In the discovery phase of our current rate case, Columbia has received nearly 600 data requests, most with several questions within each, from the other parties in the case and only about 20 are relevant to the driving issue behind the filing of the case.

In its current rate case, as in the two preceding it, Columbia has proposed to implement a Distribution System Improvement Charge Rider, commonly referred to as DSIC, similar to the mechanism that has been in place in the water industry. Recognizing that the water DSIC is a creature of statute, in each case where Columbia has proposed a DSIC, we have acknowledged that we cannot implement such a charge in the absence

of legislation that permits a gas DSIC. The passage of HB 1294 would enable Columbia to proceed with its DSIC proposal. This Rider would allow the Company to earn a return on invested dollars and begin to recover from customers the dollars that it has invested in pipe replacement in a more timely fashion through quarterly rate changes approved outside of a base rate case. Under this proposed scenario, the customers would benefit by seeing a gradual increase in rates reflective of the ongoing investment in the system rather than significantly larger increases every year or two. And because the revenue stream would more closely match the investment schedule, the Company would be in a better position to attract lower cost financing. This benefit ultimately means that the sum of those gradual increases the customer sees will be less than the increases that would occur every year or two.

The Office of Consumer Advocate has opposed the enactment of a gas DSIC and similar alternate regulatory mechanisms, assailing them as examples of prohibited "single issue ratemaking" in that not all of the revenues and expenses of a utility would be considered in total in the decision to grant a rate increase. The consumer advocate's strong opposition to AMR creates barriers for infrastructure investment and jobs for the Commonwealth.

The reality for Columbia is that, in light of our accelerated pipeline replacement effort, our rate cases are largely driven by the single issue of recovering the investment in those facilities. Our specific circumstances aside, eliminating the need for base rate cases to recover capital investment in facilities, as contemplated by HB 1294, will not remove, reduce or in any way impact the Commission's existing ability to oversee or

regulate the rates that are billed to customers in Pennsylvania. Nor will passage of HB 1294 create a windfall or unchecked opportunity for excessive earnings by the utilities in Pennsylvania. Current statutes and the regulations that implement them already include provisions to safeguard against that.

- Title 66 of the Pennsylvania Code requires, in § 1301, that “every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with the regulations or orders of the commission.”
- § 1309 provides that “Whenever the commission, after reasonable notice and hearing, upon its own motion or upon complaint, finds that the existing rates of any public utility for any service are unjust, unreasonable, or in anywise in violation of any provision of law, the commission shall determine the just and reasonable rates, including maximum or minimum rates, to be thereafter observed and in force, and shall fix the same by order to be served upon the public utility, and such rates shall constitute the legal rates of the public utility until changed as provided in this part.”
- Current statutes at § 505 and § 506 of Title 66 guarantee the Commission authority to request and examine any information, data, records or property of a utility that the Commission wants to see.
- Furthermore, the stated purpose of current regulations in Title 52 - Public Utilities at Chapter 71 is “to improve the Commission’s ability to monitor on a regular basis the financial performance and earnings of the electric, gas, telephone, water and wastewater public utilities subject to Commission jurisdiction.” Under that chapter fixed utilities are required to file quarterly

- Any party has the opportunity to monitor these reports and the utilities' earnings and to file a complaint requesting investigation to determine whether a utility's rates are indeed just and reasonable.

It is against this backdrop that I would like to address the concerns raised by Donald C. Siegel, International Vice President of the IBEW in his April 19, 2011 letter to the Committee.

*The letter opens with "House Bill 1294 appears to be a blank check for the utilities. It opens the door for utilities to propose any sort of cost-recovery mechanism they can come up with and does not provide the PUC with any standards or guidance. It would be left up to the PUC to decide whether there should be any standards, limits, etc."*

In reality, utilities have never been prohibited from proposing anything, so HB 1294 does not "open the door" in that respect. Rather the proposed legislation will give the PUC the authority to approve, not the requirement to approve, alternative ratemaking provisions to allow for more timely recovery of capital investments in infrastructure.

The letter goes on to say *"Read literally, the bill would dramatically change the regulatory process which has developed over more than a century."*

Key here is the statement that the process “has developed.” Indeed, public utility statutes have developed in that they have been modified, amended, and otherwise altered over the past many decades to best ensure safe and reliable service at just and reasonable rates as the environment in which utilities serve the public has changed.

Mr. Siegel’s letter states “In fact, it could be argued that this bill would effectively repeal all of Chapter 13 of the Public Utility Code (the ratemaking provisions).” Actually, that cannot be argued, specifically because HB1294 constitutes an addition to Chapter 13, which demands in its opening passage that “Every rate made, demanded or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable and in conformity with regulations or orders of the commission.”

While HB 1294 would grant the Commission the authority to approve alternative regulatory mechanisms filed by utilities, it would not grant utilities the ability to adjust rates without the oversight and approval of the Commission.

### Conclusion

- HB 1294 would allow utilities to increase the efficiency of their capital investment by mitigating regulatory lag and supporting the acquisition of least cost borrowing – that benefit accrues to the customers in the form of least cost rates.
- HB 1294 would increase the efficiency of the ratemaking process by eliminating redundant and excessive processes, while maintaining the Commission’s ability to ensure just and reasonable rates.

- HB 1294 recognizes that the current ratemaking model in Pennsylvania no longer encourages the efficient deployment of capital resources, which runs counter to least cost rates. It therefore sensibly provides the Public Utility Commission with regulatory alternatives to align its processes with the realities faced by the companies it regulates. Columbia Gas respectfully requests your support of the passage of HB 1294.

