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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power to Increase the Deferred EBA Rate through the Energy Balancing Account Mechanism.	Docket No. 18-035-01 **COMMENTS OF UIEC ON THE PUBLIC SERVICE COMMISSION'S 2018 REPORT TO THE PUBLIC UTILITIES AND TECHNOLOGY INTERIM COMMITTEE**

Pursuant to the Scheduling Order issued by the Utah Public Service Commission ("Commission") in this docket on March 29, 2018, the Utah Industrial Energy Consumers ("UIEC") intervention group,[1] hereby submits these Comments relating to the Commission's 2018 Report to the Public Utilities and Technology Interim Committee.

The Commission has requested comments with respect to the Commission report required by S.B. 115 "whether allowing an electrical corporation to continue to recover [100% of the electrical corporation's prudently incurred] costs under Subsection (2)(d) [of the EBA statute] is

[1] In this docket, UIEC is a reference, for convenience only, to Tesoro Refining & Marketing Company LLC, and LafargeHolcim Ltd.

reasonable and in the public interest."[2] The UIEC respectfully submit the following comments, concluding the EBA is not in the public interest whether or not the utility is allowed to recover 100% of its prudently incurred costs, and that it should therefore be completely eliminated.

A. The EBA Is Not in the Public Interest.

The EBA statute requires that for an EBA to be a lawful mechanism for cost recovery, it must initially be found to be, and must remain "in the public interest."[3] At the inception of the EBA pilot program, the Commission identified the criteria necessary for an EBA to be in the public interest:[4]

> To serve the public interest and to ensure just and reasonable rates, most importantly this new mechanism must [1] fairly allocate risk between customers and shareholders, [2] maintain incentives to operate efficiently, both in the long-run and short-run, and [3] satisfy the requirements of the Energy Balancing Account statute.[5]

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[2] *In the Matter of the Application of Rocky Mountain Power to Increase the Deferred EBA Rate through the Energy Balancing Account Mechanism* (Scheduling Order, Notice of Hearings, and Tariff Status, at 3) Docket No. 18-035-01 (Mar. 29, 2018) (quoting Utah Code Ann. § 54-7-13.5(6); § 54-7-13.5(2)(d)).

[3] The EBA statute provides that "[an] energy balancing account shall become effective upon a commission finding that the energy balancing account is: (i) in the public interest; (ii) for prudently-incurred costs; and (iii) implemented at the conclusion of a general rate case." Utah Code Ann. § 54-7-13.5(2) (2010). Once approved, the EBA must be "maintained" in accordance with the requirements of Section 54-13.5 (which includes the "public interest" requirement) to avoid constituting impermissible retroactive ratemaking (*id*. at § 54-7-13.5(4)(c)).

[4] The meaning of the "public interest" must be derived "from the purposes of the regulatory legislation in question." *Ellis-Hall Consultants, LLC v. Pub. Serv. Comm'n*, 342 P.2d 256, 261 (Utah 2014) (*quoting NAACP v. Fed. Power Comm'n,* 425 U.S. 662, 669, 96 S. Ct. 1806, 48 L.Ed.2d 284 (1976)). The Commission has generally required that for the public interest standard to be met, there must be some net benefit to ratepayers. *See, e.g., In the Matter of the Merger of the Parent Corps. of Qwest Comm'ns Corp., LCI Int'l Telecomm. Corp. and US West Comm'ns, Inc.* ("*Qwest Merger*"), Report and Order at 14, Docket No. 99-049-41, 2000 WL 873341 (Utah PSC, June 9, 2000) (applicants must show that the merger "provides a *net positive benefit* to the public") (emphasis added); *see also In the Matter of the Application of PacifiCorp and Scottish Power plc for an Order Approving the Issuance of PacifiCorp Common Stock*, Report and Order at 26-27, Docket No. 98-2035-04 (Utah PSC, Nov. 23, 1999) (The Commission "is to consider [all positive benefits and negative impacts], giving each its proper weight, and determine whether on balance the [proposal] is beneficial or detrimental to the public.").

[5] *In the Matter of the Application of Rocky Mountain Power for Approval of its Proposed Energy Cost Adjustment Mechanism*, Corrected Report and Order (hereinafter, "Corr. Rep. and Order"), Docket 09-035-15 at 67-68 (Mar. 3, 2011).

The Commission rightly recognized that an EBA would by its nature create an unfair allocation of risk which, if left unchecked, would result in harm to ratepayers. Several methods were proposed to ameliorate the unfair allocation of risk inherent in an energy balancing account.[6] In the end, the Commission adopted an EBA design which included "risk sharing during periods of regulatory lag, coupled with prudence review."[7]

The Commission explained why relying solely on prudence review resulted in an unfair allocation of risk to customers:

> As in the past, we will continue to rely on prudence reviews during rate setting proceedings to determine the extent to which the Company is providing least-cost, risk-adjusted service to its Utah customers, consistent with integrated resource planning and competitive solicitation analyses. We recognize, however, *relying solely on prudence reviews will shift too much of the risk for suboptimal planning and operation currently borne by the Company, who is in the best position to manage this risk, to customers, who are not.*[8]

The Commission also explained why a sharing mechanism was the best method to ensure that the EBA would be in the public interest:

> Therefore, the balancing account we adopt requires both Company customers and shareholders to remain at risk for a portion of the actual net power cost which deviates from approved forecasts. This decision recognizes the value of Company management having *meaningful financial incentives* to minimize net power cost in the short-run and long-run, regardless of the extent of net power cost volatility. *We find a sharing mechanism is the best method, at this*

[6] It was suggested the Commission "establish predefined or pre-approved levels of hedging, market purchases, energy efficiency programs, renewable resources or low-cost resource operating characteristics," as well as other methods to provide incentives to the Company's behavior. Corr. Rep. and Order, at 68-69.

[7] *Id*. at 69.

[8] Corr. Rep and Order at 69-70 (emphasis added).

> *point, to ensure customer and shareholder interests are aligned and the public interest is maintained.*[9]

Thus, the Commission concluded the 70/30 sharing mechanism was essential to ensure that the EBA fairly allocated risk between customers and shareholders by creating financial incentives for the public utility to operate efficiently with respect to net power costs.

Senate Bill 115 ("SB 115"), enacted in 2016, removed the 70/30 sharing mechanism,[10] eviscerating one of the two safeguards – prudence review and risk sharing – that the Commission concluded were essential to finding that an EBA is in the public interest. Moreover, it has become starkly evident since the enactment of SB 115, that the Commission was right in finding that the remaining safeguard – prudence review – is ineffective to curb the risk to ratepayers or to incentivize the utility to be efficient. Despite expending substantial time, effort and resources over the past several years in performing audits of Rocky Mountain Power's ("RMP" or "Company") power costs, the Division has concluded that its reviews of the Company's power costs, especially its daily power transactions (of which the Division reviews less than 1%),[11] have been insufficient

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[9] *Id.* (emphasis added).

[10] SB 115 states:

> (d) Beginning June 1, 2016, for an electrical corporation with an energy balancing account established before January 1, 2016, the commission shall allow an electrical corporation to recover 100% of the electrical corporation's prudently incurred costs as determined and approved by the commission under this section.

SB 115 at lines 558-61, codified at Utah Code Ann. § 54-7-13.5(2)(d).

[11] *See Comments of UAE,* Docket No. 17-035-01 (Sept. 15, 2017) at 4 (during 2016, the Company engaged in more than 11.8 million MWh of long-term, intermediate-term and short-term firm purchase transactions, and more than 12.4 million MWh sales transactions). Despite its substantial effort, the Division is able to review a very small fraction of those transactions. *Division of Public Utilities' Final Evaluation Report of PacifiCorp's EBA Pilot Program* ("Pilot Rep."), Docket No. 09-035-15 (May 20, 2016) at 5, 22, 41-45; *see also* Hr'g Transcript, Docket No. 09-035-15 (Jan. 17, 2017) ("Hr'g Transcript") at 44:2-14 (out of "tens of thousands" daily transactions involved in an EBA review, the Division's audit typically includes a review of "about 60.")

to meaningfully assess the accuracy or prudence of those power costs.[12] The Division, consequently, felt compelled to warn of the "moral hazard" that would result "should the Company perceive that it is essentially guaranteed recovery of costs."[13] Yet, given the Division's experience, the Company likely already perceives that the EBA is a guarantee of cost recovery because it understands that prudence reviews are largely ineffective to reveal inaccuracy or imprudence. The 70-30 sharing band might have provided some marginal incentive to the Company by placing it partially at risk for its decisions. But no sharing mechanism can sufficiently incentivize prudent action.[14] The Company must be placed fully at risk for its decisions so that its own economic interest compels it to prudence and efficiency in managing its power costs.

It is not in the public interest to continue to allow the Company to collect power costs from ratepayers through a process that does not place the Company at risk and does not afford regulators the ability to effectively audit the Company's decisions for accuracy or prudence. Without the sharing mechanism, the EBA has gone from bad to worse as the Company has now been relieved of virtually all risk of efficiently forecasting and managing power costs. Ratepayers, have *no* means to control any of that risk, yet now bear *all* of it. By eliminating the 70/30 sharing bands, SB 115 has caused the EBA to devolve into the same mechanism that the Commission concluded

[12] *Id*. at 17. In its Pilot Report, the Division stated it that it is "virtually impossible" to meaningfully assess the prudence of the Company's daily transactions, nor would it be able to do so even with improved documentation. Pilot Rep. at 43. At hearing on the Pilot Program, held on January 17, 2017, the Division testified that it could not attest to the audit results as being "a statistically accurate representation of the universe of [net power costs]." *See* Report and Order, 09-035-15 at 4 (Feb. 16, 2017) (quoting Hr'g Transcript at 13:9-11). The Division stated it has no evidence to reasonably believe that reported net power costs are materially inaccurate (*id.*), but neither could it confirm accuracy. In short, it is unknown whether the Company's reported net power costs are accurate.

[13] Pilot Rep. at 44.

[14] Rocky Mountain Power confirms: "the reality is that sharing bands have no effect on the operations of the Company." *Comments of Rocky Mountain Power*, Docket No. 17-035-01 (Sept. 15, 2017) at 6.

was not in the public interest. The EBA is not in the public interest, with or without the sharing mechanism, and it should be eliminated.

While not directly connected to the elimination of sharing bands under SB 115, the UIEC offer the following comments on two additional concerns that warrant elimination of the EBA – the practice of setting interim rates in EBA proceedings, and the problem of adjusting RMP's rate of return to reflect the decreased risk it faces because of the EBA.

B. Interim Rates.

Beginning with the 2017 EBA, at the urging of the Division,[15] the Commission started ordering "interim" EBA rates to become effective on May 1 of each year, accepting the Company's allegation of the net power cost deficiency (or over-collection, as the case may be) upon a showing that the Company's filing "does not depart from prior years' EBA filings."[16] Such interim rates are subject to "true-up" after the Division has performed its audit and after an adjudicative hearing before the Commission, usually in January of the following year. The UIEC recognize that EBA audits place a significant burden on the Division's time and resources, and that setting a hearing in January gives the Division additional time for a prudence review. The UIEC also understand that the question of whether interim rates may be ordered in an EBA proceeding is now on appeal to the Utah Supreme Court.

The UIEC, nevertheless, continue to maintain that there exists no process for "interim" rate relief to recover a deficiency in net power costs through the EBA, and that no shortfall in power costs can be incorporated into rates until after the Company has demonstrated by substantial

[15] Pilot Rep. at 7, 49; *Dir. Test. Charles E. Peterson*, Docket No. 09-035-15 (Sept. 21, 2016) at 2:42-44, 7:162-163.

[16] *In the Matter of the Application of Rocky Mountain Power to Decrease the Deferred EBA Rate through the Energy Balancing Account Mechanism*, Order, Docket No. 17-035-01 (April 25, 2017) at 3.

evidence that the costs were prudently incurred.[17] Elimination of the EBA will allow regulators to determine power costs in general rate cases, ensuring that rate increases do not go into effect until there has been a Commission finding that the power costs were prudently incurred.

C. **RMP's Rate of Return.**

Even though SB 115 has saddled ratepayers with 100 percent of the risk of the Company's power costs, there has been no adjustment to the Company's rate of return to account for the decreased risk it faces because of the EBA. The EBA allows the Company to fully recover its power costs from year to year, even during periods of overearning,[18] without having to file a general rate case, the only proceeding in which the Company's rate of return can be examined and adjusted to account for the decreased risk.[19] Thus, the EBA not only creates an inequitable situation where the Company's authorized rate of return is not reflective of its risk, it also perpetuates that inequity by making it unnecessary for the Company to regularly file general rate cases to fully recover its costs. Eliminating the EBA and requiring the Company to seek power cost recovery through a general rate case would not only place the Company at risk again for its power costs but would also allow regulators to set a rate of return commensurate with that risk.

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[17] Arguably, a hearing may not be necessary before decreasing rates when RMP proposes a refund to customers. *See* Utah Code Ann. § 54-7-12(5)(A) (*Notwithstanding any other provisions of this title …* any schedule that does not result in a rate increase shall take effect 30 days after the filing … subject to [the commission's] authority to suspend, alter, or modify that schedule …"); *id.* § 54-7-12(6).

[18] *See* Pilot Rep. at 29-31 (Company earning its authorized rate of return even with the 70/30 bands in place, yet the EBA had not resulted in any reduction in energy rates, rate volatility, or the need for annual rate increases). The Division states, "If the Company can earn its allowed rate of return with the 70-30 sharing band, then it will over-earn without the sharing bands with everything else held constant." *Id*. at 31.

[19] RMP filed its most recent general rate case on January 3, 2014 (Docket No. 13-035-184), setting net power costs in base rates for purposes of future EBA cases.

CONCLUSION

Since inception, the EBA has benefited only the Company, with little or no benefit to ratepayers.[20] Even with the 70/30 sharing mechanism in place, the EBA provided inadequate incentive to RMP to act prudently, largely because of the obvious impracticality of auditing the Company's transactions. With SB 115's elimination of the sharing mechanism, 100 percent of the risk of the Company's power cost recovery has shifted to ratepayers, worsening the inequity. After more than six years' experience with the EBA, it has become abundantly apparent that, even if the sharing mechanism were to be reinstated, the EBA would still not be in the public interest for all of the reasons discussed above. The EBA, therefore, should be eliminated.

Respectfully submitted this 18th day of September, 2018.

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[20] See *Comments of the Division of Public Utilities*, Docket No. 17-035-01 (Sept. 15, 2017) at 3.

CERTIFICATE OF SERVICE
(Docket No. 18-035-01)

I hereby certify that on this 18th day of September 2018, I caused to be e-mailed, a true and correct copy of the foregoing COMMENTS OF UIEC ON THE PUBLIC SERVICE COMMISSION'S 2018 REPORT TO THE PUBLIC UTILITIES AND TECHNOLOGY INTERIM COMMITTEE to:

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