THE STATE OF NEW HAMPSHIRE
before the
PUBLIC UTILITIES COMMISSION

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

Public Service Company of New Hampshire's
Reconciliation of Energy Service and Stranded Costs for 2012
Docket No. DE 13-108

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE'S BRIEF RE: USED AND USEFUL

In New Hampshire, public utilities are entitled to a just and reasonable rate base and a just and reasonable return of and on that rate base. *Legislative Utility Consumers' Council v. Public Service Company of New Hampshire*, 119 N.H. 332, 341 (1979). Utility rates are to be set in a manner and at a level that balances the interests of customers and investors and satisfies the utility's revenue requirement. *Appeal of Conservation Law Foundation*, 127 N.H. 606, 633 (1986). The just and reasonable rate base to which a utility is entitled has been described as the cost, less depreciation, of the property that is used and useful in providing service to the public. *Id.* at 634. This is consistent with long settled law that:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding, risks and uncertainties . . ..

Bluefield Waterworks & Improvement Co. v. Public Serv. Comm'n. of W. Va., 262 U.S. 679, 692 (1923); *see also Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944).

In the instant case, the Office of Consumer Advocate ("OCA") has proposed a new ratemaking standard – one involving a determination of whether Public Service Company of New Hampshire's ("PSNH") fossil generating stations are "fully" used and useful and so

whether and to what extent PSNH may actually earn the return to which it is entitled on that property. The OCA's proposal turns on a comparison of those stations' recent and historic capacity factors in periods selected by the OCA. Such a proposal: (1) is inconsistent with the plain language of New Hampshire law; (2) represents a significant departure from existing Commission practice; (3) leads to increased and asymmetrical risk to PSNH; (4) singles out, without justification, discrete individual assets of a single utility for disparate rate treatment; and (5) continues to be open to further, unspecified, changes. Accordingly, the OCA's proposal must be rejected.

As a first matter, PSNH notes that Mr. Eckberg testified that the OCA's proposal was based upon a reading of RSA 378:27 and RSA 378:28 and that the term "fully" does not appear in either law, but that he added it on his own.[1] Additionally, the OCA has not identified any other law or rule in New Hampshire that creates a requirement for assets to be "fully" used and useful. Accordingly, this proposal is not based upon any existing law in New Hampshire. Furthermore, in its closing the OCA contended that PSNH's fossil generating stations may be the only assets to which this concept would ever be applied, without ever making clear why such "one-time" treatment was proper or appropriate. Under such circumstances, the OCA's proposal goes beyond even the single issue ratemaking the Commission disfavors,[2] and veers into single asset ratemaking. In that this concept has no basis in New Hampshire law, and that, contrary to

---

[1] *See Lambert v. Belknap County Convention,* 157 N.H. 375, 381 (2008) ("We will not insert words that the legislature did not see fit to include.")

[2] As the Commission has previously noted:

> Single-issue rate cases are frowned upon in utility ratemaking because the objective of ratemaking is not to ensure recovery dollar for dollar of every expenditure made by a utility, but rather to ensure that the company has a reasonable opportunity to earn a reasonable overall return on investments dedicated to public utility functions. In order to make this ultimate determination, it is necessary to match ordinary and necessary expenses with income from the same period, and determine whether the net income is sufficient to provide a reasonable return on allowable rate base.

Connecticut Valley Electric Company, Order No. 23,887 (December 31, 2001) at 15-16.

established policy, it has been proposed to apply to only a few assets of a single company, the Commission must reject the concept and the proposal.

Additionally, in New Hampshire the evaluation of whether an asset is used and useful, and so may properly be included in the rate base upon which the utility is entitled to earn a reasonable return, takes place at the time the asset is added to the utility's rate base. Said another way, "usefulness judges [the] value [of an investment or expenditure] *at the time its reflection in rate base is under consideration.*" *Conservation Law Foundation*, 127 N.H. at 638 (emphasis added); *see also Public Service Company of New Hampshire*, Order No. 25,213 (April 18, 2011) at 77 (noting that the "used and useful principle acts as a prohibition on what assets are included in rate base"); *see also Public Service Company of New Hampshire*, Order No. 22,841, 80 N.H. P.U.C. 40 (1998). Thus, in New Hampshire, as noted by Mr. Chung in his rebuttal testimony, there is a point at which an asset is determined to be either used and useful or not. The assets at issue here have been included in PSNH's rate base for decades because the Commission has concluded that they are used and useful. Accordingly, there should be no "second bite at the apple" that would permit a disallowance of some ever-shifting portion of the return on PSNH's assets.

Moreover, to change the manner of the Commission's evaluation of the "used and usefulness" of utility assets and to limit the ability of utilities in New Hampshire to earn a return on assets previously found to be both prudent and used and useful, would demonstrate a marked departure from the Commission's prior practice and would be contrary to the principle that a utility is entitled to earn a return on those assets – not some undetermined fraction of the assets. Moreover, to amend the Commission's established practice, especially on the limited basis proposed, would put PSNH and other utilities at risk of substantial uncertainty about what rate

setting methodology would be applied to their assets. As the United States Supreme Court has warned:

> The risks a utility faces are in large part defined by the rate methodology because utilities are virtually always public monopolies dealing in an essential service, and so relatively immune to the usual market risks. Consequently, a State's decision to arbitrarily switch back and forth between methodologies in a way which required investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others would raise serious constitutional questions.

Duquesne Light Company v. Barasch, 488 U.S. 299, 315 (1989).[3] In evaluating whether assets are used and useful, the Commission has established a policy, grounded in New Hampshire law, upon which PSNH, and other utilities, are entitled to rely. To make the arbitrary determination that a specific subset of PSNH's assets are subject to differing treatment whereby a portion of the value of some assets is denied would be akin to a taking and would, as the Supreme Court notes, raise serious constitutional questions.[4]

Furthermore, the Commission's policy is consistent with the traditional application of the used and useful test elsewhere. As noted by one commentator:

> Generally speaking, the case law regards costs incurred and investments made used and useful if: (1) there is a direct and immediate benefit to customers; traditionally, the investment is in a plant that is operational now or in a future test year or in the period during which the rates may reasonably be expected to be in effect; (2) the investment or expense, even if not affording an immediate tangible benefit, meets certain secondary benefit criteria, such as reasonably foreseeable

---

[3] *See also*, Richard Goldsmith, *Utility Rates and "Takings"*, 10 Energy L.J. 241, 274-75 (1989) noting that "where rate regulators apply *any* rate methodology consistently, investors automatically receive a return commensurate with the risks they have assumed, and the end-result cannot offend the Constitution." (emphasis in original).

[4] To be clear, PSNH is not contending that the Commission may never change the aspects of its review or evaluation of utility assets. PSNH is, however, contending that there is no adequate foundation for doing so here and that should the Commission make such a change, it should do so following a thorough and public process and on a going forward basis so that the risks and benefits of the approach may be understood and properly applied. *See, e.g., Re Pricing and Rate-Making Treatment of New Electric Generating Facilities that are not Qualifying Facilities*, 89 P.U.R. 4th 190, 213-15 (Mass. 1987) (concluding, in part, that changes to the traditional used and useful standard would be appropriate for new facilities and recognizing that a new system of review needed to satisfy various criteria including that it appropriately align risks and rewards and provide proper incentives); *see also Re Pricing and Rate-Making Treatment of New Electric Generating Facilities that are not Qualifying Facilities*, 93 P.U.R 4th 313, 336-38 (Mass. 1988) (applying new standard through "pre-approval contract" approach).

> plant completion, a necessary cost of continuing business (including land acquisition to enhance gas reserves or other reasonable plans and commitments to dedicate property to public service), or assets held in reserve to ensure service reliability; or (3) the expenditure is necessitated by the projected immediate needs of the ratepaying public.

James J. Hoecker, *"Used and Useful": Autopsy of a Rate Making Policy*, 8 Energy L.J. 303, 312 (1987). Each of PSNH's plants are operational now and provide direct and immediate benefits to customers, particularly in the present circumstances where they provide not only energy and capacity benefits and revenues, but also a valuable hedge against exposure to volatile energy costs in the state and region. Therefore, they fit well within the traditional definition of assets that have been found to be used and useful.

PSNH also notes that the attempt to classify certain assets as something less than "fully" used and useful based upon their real or perceived economic value is not new. One commentator notes that this "economic used and useful test" – that is, a test of "used and usefulness" based upon a comparison of the value of the asset to market prices rather than upon an analysis of whether an asset is, in fact, physically providing service to customers – was proposed as far back as the 1980s, primarily by consumer advocates in conjunction with the review of investments in nuclear power plants that were never built. Jonathan A. Lesser, *The Used and Useful Test: Implications for a Restructured Electric Industry*, 23 Energy L.J. 349, 351, 359-60 (2002). According to that analysis, the use of the so-called "economic used and useful" test in evaluating whether certain costs relating to those failed plants could be recovered, at times, outweighed even the prudence standard, such that recovery of prudently incurred costs was disallowed based upon a the contention that the investment turned out, after the fact, to be uneconomic. *Id.* at 360.

Based upon Mr. Lesser's analysis of various cases, including *Jersey Central Power and Light Company v. Federal Energy Regulatory Commission*, 810 F. 2d 1168 (D.C. Cir. 1987) and

Duquesne Light Company v. Barasch, 488 U.S. 299 (1989), he notes that there was, for a time, an "economic used and useful test" that implemented:

> a regulatory policy under which: (1) prudently incurred costs can be disallowed any time in the future; (2) the extent to which a utility will be able to recover prudently incurred costs will be determined using information not available to the utility at the time its decision was made; (3) the determination of "uneconomic" costs will change over time as market conditions change; and (4) the treatment of investments and purchase decisions will be the same, except that a utility will not be allowed to profit from an advantageous purchase decision - at most, it will be able to recover its cost.

Lesser, *supra*, at 360. Thus, in applying this test – a test described as being "fundamentally incompatible with utility efforts to manage market price uncertainty", *id.* at 370 – the traditional used and useful analysis was supplanted by a regulatory policy that sometimes used information that did not or could not have been available to the utility at the time of an investment to place an asymmetrical risk on the utility, and made it so that even entirely prudent costs for assets that were actually in use could be disallowed by a real or perceived shifts in markets.[5] Denying the utility an ability to earn a reasonable return based upon the perceived economics of an asset in some discrete period after the decision-making process had concluded would not only depart from New Hampshire precedent, but would also be inherently inequitable and it would mean that the utility would not, in fact, have the opportunity to earn a return on the property employed for the convenience of the public since that return could be stripped away at any time.[6] *Bluefield*, 262 U.S. at 692.

---

[5] *Cf. Public Service Company of New Hampshire*, Order No. 25,546 (July 15, 2013) at 9 ("PSNH's prudent costs of complying with RSA 125-O must be judged in accordance with the management options available to it at the times it made its decisions to proceed with and to continue installation. The hearing on the merits will therefore not address current market or regulatory conditions but rather those conditions in place at the time of the decision-making under review . . .").

[6] The Illinois Commerce Commission recognized similar potential difficulties in rejecting a similar test for certain generating assets of Consolidated Edison because such a test was a "radical departure" from that commission's practice and required "a needed unit also to be economically beneficial in order to be deemed used and useful." *In re Commonwealth Edison Co.*, 158 P.U.R. 4th 458, 480 (Ill. 1995).

Furthermore, as was noted by Mr. Chung in his testimony, and during the OCA's testimony at hearing, the additional risk placed upon the utility from the uncertainty of potential disallowances would likely result in higher costs to the utility, and ultimately to customers. Being subject to ongoing and changing disallowances would make the utility less able to borrow money at attractive or competitive rates and less able to service its debt. Further, the perception of risk of potential disallowances in the future would drive investors to demand a higher return on equity to account for that possibility. Lesser, *supra*, at 375-76; Goldsmith, *supra*, at 272-73. In the end, the costs for PSNH and other utilities in New Hampshire to operate their businesses would rise, which would translate to an increase in the costs to customers. In that the OCA repeatedly stated that there were additional potential amendments or refinements to its proposal, but that it did not have them available at present, it remains unclear what potential risks might actually be imposed upon PSNH or other utilities in New Hampshire by adoption of this proposal.

Similarly, as was noted at hearing, under the OCA's proposal, there is no ability for PSNH to reap the benefits of advantageous decisions or circumstances. As was discussed, for example, PSNH's Schiller Unit 5 actually performs significantly better today under the OCA's arbitrarily selected metric than it did in the base period the OCA decided to select. Yet, PSNH would have no ability to benefit from such a circumstance. Further, if there was to be an increase in the capacity factor of PSNH's other units, it would serve only to decrease the amount of the loss, but would not provide any benefit to PSNH, at least until that metric reached the same level that the OCA has decided is the appropriate benchmark (and even then the average proposed by the OCA would mask any actual benefit). "[E]valuating a utility company as if it were in a competitive industry, while constraining its behavior as a fully regulated firm, is

inconsistent with promoting economic efficiency." Lesser, *supra*, at 378. The OCA has proposed a lopsided "all risk and no reward" system that is inconsistent with the Commission's role in balancing the interests of utilities and customers. *See* RSA 363:17-a; *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,972 (May 29, 2009) at 48.

Finally, in its closing the OCA stated that the underlying reason for its proposal was that under the current system, PSNH has no incentive to view the economics of its facilities differently than it had previously because its rate of return would not change. Staff's witness stated, however, that PSNH has adapted the operation of its facilities to meet the market conditions and to make them as economic as possible. Furthermore, the OCA's witness agreed that if its proposal was adopted, it may actually create perverse incentives regarding the use of PSNH's facilities. PSNH has responded appropriately to market pressures under the current system, and adopting the OCA's proposal would actually work to undermine those enhancements to PSNH's operations. Thus, the underlying basis for the OCA's proposal is unsupported.

The OCA's proposal is not in line with existing New Hampshire law or Commission practice. In addition, the proposal it advocates would raise questions of constitutional dimension and the OCA has not provided an adequate justification for the amendments it supports. Further, adopting the proposal would place undue risk on PSNH, and other utilities, and would eventually result in cost increases to customers. In addition, the OCA has admitted its proposal is subject to additional changes making it essentially impossible to truly evaluate the potential risks or consequences of the proposal. PSNH's facilities have been determined by the Commission to be used and useful, and they are providing real and immediate benefits to customers.[7] There is

[7] The OCA's plan would be further complicated by situations where the utility itself did not make the investment decision, but was mandated to do so by force of law. *See e.g., Re Conversion of Schiller Station,* Order No. 13,711,

nothing in New Hampshire law that would permit or require a partial disallowance of the return on PSNH's assets and the OCA's proposal must be rejected.

Respectfully submitted,

Public Service Company of New Hampshire

February 4, 2014
Date

By: _____
Matthew J. Fossum
Senior Counsel
780 North Commercial Street
Post Office Box 330
Manchester, New Hampshire 03105-0330
(603) 634-2961
Matthew.Fossum@nu.com

CERTIFICATE OF SERVICE

I hereby certify that, on the date written below, I caused the attached Brief to be served pursuant to N.H. Code Admin. Rule Puc 203.11.

February 4, 2014
Date

_____
Matthew J. Fossum

64 N.H. P.U.C. 195 (1979); Order No. 14,131, 65 N.H. P.U.C. 127 (1980) (Commission's decision mandating the conversion of Schiller Station from oil to coal, rather than natural gas); RSA 125-O:13 mandating the installation of scrubber technology at Merrimack Station.