STATE OF RHODE ISLAND
PUBLIC UTILITIES COMMISSION

IN RE:	**THE NARRAGANSETT ELECTRIC**	**:**	
	COMPANY d/b/a NATIONAL GRID	**:**	
	GAS INFRASTRUCTURE, SAFETY,	**:**	**DOCKET NO. 5210**
	AND RELIABILITY PLAN	**:**	
	FY 2023 PROPOSAL	**:**	

REPORT AND ORDER

I. Introduction

On December 17, 2021 and pursuant to R.I. Gen. Laws § 39-1-27.7.1(d), the Narragansett Electric Company d/b/a National Grid (TNEC or Company)[1] filed its FY 2023 Gas Infrastructure, Safety, and Reliability Plan (ISR Plan) with the Rhode Island Public Utilities Commission (Commission).[2] At an Open Meeting on March 29, 2022, the Commission approved the proposed ISR Plan and conditionally approved the revenue requirement and associated rates subject to refund and further review by the Commission of certain pending issues.[3] One of the pending issues related to the Company's Proactive Main Replacement Program, which was one of the capital investment programs conditionally approved in the ISR Plan that involves replacing leak-prone pipes with new main.[4] With respect to that program, the published vote taken on March 29, 2022 by the Commission specifically stated "[t]hat the Commission shall continue the hearings to a date to be determined to continue its review of the Company's lag in performance regarding the timing of abandoning leak-prone pipes that are intended to be replaced in the Proactive Main Replacement

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[1] Subsequent to the initial filing but prior to the issuance of this order, the assets of the Narragansett Electric Company were acquired by PPL Corporation. *See* Docket No. D-21-09.
[2] This Order refers to the entire "Infrastructure, Safety, and Reliability" program as the "ISR" program.
[3] *In Re: The Narragansett Electric Company d/b/a National Grid Gas Infrastructure, Safety, and Reliability Plan FY 2023 Proposal*, Docket No. 5210, Order No. 24452 (Jul. 27, 2022).
[4] *Id.* at 19-20 (Jul. 27, 2022). The Commission's order also contained other conditions relating to the inclusion of cost recovery for certain heaters associated with Tiverton and Wampanoag Trail take stations. This order does not address the heaters and is only limited to the ratemaking treatment related to the Proactive Main Replacement Program.

Program, including a review of the reasons for the lag, the apparent lack of incentive for timely abandonment, and the ratemaking implications relating to the application of the used and useful standard."[5]

As described in this Order, the Commission conducted further hearings and, for the reasons stated herein, the Commission finds – based on the facts established in the hearings relating to this matter – that an appropriate application of the "used and useful" standard calls for a prospective change in the timing of the inclusion of new main in rate base within the Proactive Main Replacement Program. Specifically, the Commission finds that new mains in the program should not be included in rate base unless and until the old main that is being replaced is fully abandoned, subject to the conditions in this Order. This change shall take effect for all new mains in the program starting with the next fiscal year ISR filing.

II. The ISR and Proactive Main Replacement Program

A. Ratemaking and Rate Base Treatment in the ISR Program

This case arises within the statutory framework for annual regulatory review of capital projects. Specifically, gas distribution companies are mandated by R.I. Gen. Laws § 39-1-27.7.1 to file an annual infrastructure, safety, and reliability (ISR) spending plan. The Gas ISR Plan consists of a number of investment programs or initiatives designed to ensure the safety and reliability of the gas distribution system. Under well-settled ratemaking rules, the utility is compensated for investment in capital projects when such projects are placed into "rate base," upon which the utility earns a return, recovers depreciation expenses over the life of the asset classifications, and is reimbursed for applicable tax effects. It is the rate base treatment of the

[5] Open Meeting Minutes at 5 (Mar. 29, 2022).

capital costs which commences utility cost recovery for the capital investments made by shareholders of the utility.

Prior to the passage of the law which created the ISR process in 2010, the utility could not commence recovery of the costs of its capital projects until it filed a general rate case and the Commission allowed the costs in rate base after the statutory nine-month review process was completed. This created a regulatory lag in cost recovery. The ISR process is a statutory modification of the traditional rate case process, which had been the exclusive regulatory means through which the utility could commence recovery of its costs of investing in capital projects, among recovery of other business expenses. The ISR eliminated the regulatory lag on recovery of the costs for certain prioritized investments, allowing current and annual recovery of the capital costs of eligible projects.[6] While the ISR recovery requires ratepayers to begin paying for the costs sooner, it also provides an important financial incentive for the utility to invest in new plant that is needed for reliable and safe service. A regulatory check on overspending is built into the process whereby the Company must negotiate an investment plan with the Division of Public Utilities and Carriers (Division) after which such plan is filed with the Commission for further review and approval.

Once a capital project is completed, the utility is allowed to include the total capital cost of the project in the ISR rate base, which commences recovery in rates from ratepayers of return on investment, depreciation, and taxes. The capital cost also includes an allowance that addresses the time value of money, referred to as an "Allowance for Funds Used During Construction" (AFUDC). The AFUDC rate is effectively an interest rate that is applied to the total accumulating

[6] Because there is uncertainty of when each capital project will actually be completed in the applicable year, there is a "half-year convention" which is used to allow commencement of rate base treatment for the total estimated capital projects that are forecasted to be completed in the applicable rate year. This is a means of allowing the average of projects to commence rate base treatment, but the costs tied to actual in service dates is later reconciled in a later filing.

project cost until the project is completed.[7] It is a standard convention of ratemaking which allows the utility to be compensated for the cost of capital while the project is pending and before it is eligible for rate base treatment. AFUDC accumulates on the Company's accounts and when the capital cost of the project is included in rate base, the accumulated AFUDC is added to that total cost. Thus, the AFUDC component becomes a part of the capital cost upon which the utility earns a return and is depreciated over the designated life of the asset through depreciation expenses that are recovered from ratepayers.

While the ISR process addresses the annual plan for capital investments, traditional ratemaking principles still apply and were not affected by the ISR law. The initial decision to make an investment is pre-approved by the Commission in the ISR process after being reviewed by the Division. However, there is always a prudency risk for the utility relating to cost over-runs associated with the execution of any utility capital project. In addition to cost over-runs, there also is a prudency risk related to project execution which encompasses the potential that an unreasonable delay in completing a project might unnecessarily extend the period of time upon which the utility would accumulate AFUDC on the capital being expended for the project. In cases where there is evidence that a delay was a result of imprudent management, the Commission has the authority to disallow a portion of the accumulation of AFUDC related to the period of delay.[8] In such case, cost recovery for the investment and the accumulation of AFUDC prior to the delay would be includable in rate base, but there would be a disallowance for the incremental accumulation of AFUDC pertaining to the delay period.

B. The Proactive Main Replacement Program

[7] The current AFUDC rate is 7.41%. Hr'g Tr. at 99 (Jun. 1, 2022). Response to Record Request No. 21 (Jun. 29, 2022).
[8] *See Providence Gas Company v. Malachowski*, 600 A.2d 711, 716-17 (R.I. 1991)(Facts were insufficient to support disallowing AFUDC, but authority to disallow is clear if evidence supports finding.)

The largest component of the ISR Plan is the Proactive Main Replacement Program. This investment program is aimed at replacing leak-prone gas mains and addresses safety concerns relating to the dangers of gas leaks. Under this program, the Company constructs a new main in parallel with the old leak-prone main and, in sequence, abandons the old main.[9] Because ratepayers bear the cost of fugitive gas lost to the atmosphere from leak-prone pipe, it follows that reducing the amount of leak-prone pipe reduces costs to ratepayers. Replacing leak-prone pipe also provides an environmental benefit by eliminating the methane being emitted into the atmosphere from the leak-prone pipe.

In the case of replacements of leak-prone pipes, the old main to be abandoned typically has service connections to customer premises.[10] Thus, an important step in the construction sequence of the project – before the old main can be abandoned – is to transfer or replace each service connection. In each instance, the service connection is removed from the old main and a connection is made to the new main. These customer service connections must be undertaken one connection at a time, after the new main is gassed in. However, the transfer of services takes place while the old main is still providing service and is fully pressurized.[11] During this time, both the new main and the old main have gas flowing at the same pressure.[12]

C. <u>The Ratemaking Issues Arising in this Case</u>

In the instant matter, questions arose about delays that occurred in the abandonment of leak-prone pipes in the Proactive Main Replacement Program after new mains were gassed in

[9] Hr'g Tr. at 47-49 (Mar. 15, 2022); *see also* Docket No. 5165, Hr'g Tr. at 28-35 (October 13, 2021). The Commission has taken administrative notice of the record and transcript of the October 13, 2021 hearings in Docket No. 5165, the testimony of which was referenced in the hearings in this docket.
[10] *Id.*
[11] Docket No. 5165, Hr'g Tr. at 34-35 (October 13, 2021).
[12] *Id*.

during fiscal years 2021 and 2022.[13] According to the Company, the delays were attributable to the challenges the utility faced relating to the COVID pandemic – particularly in how it affected changing out service connections for individual customers – among other effects.

In reviewing the evidence of what transpired during these two fiscal years, however, it became clear to the Commission that principles of ratemaking were being implicated because the prevailing practice employed by the Company was to place the total project cost in rate base *before* the old main is actually abandoned. Specifically, when the first service connection is made, the Company has historically treated the new main as being "in service" for purposes of including the total project costs in the ISR rate base calculation for ratemaking purposes.[14] Once the project is included in ISR rate base for ratemaking purposes, the delay in abandonment has no negative financial implications for the utility, as the Company earns a return on the total investment and commences the recovery of depreciation expenses.

During the hearings on March 15, 2022 the Company's main witness testifying about the projects stated that the risks of leaks on the yet-to-be abandoned old pipe remain the same, even though the new main is connected to the system.[15] In other words, the leakage risks which the main replacement program is designed to address remain unchanged until the old pipe is actually abandoned.[16] In the case of the Proactive Main Replacement Program, all safety issues associated with the old main continue and methane leaks still occur at the same rate, because the pressure in

[13] The fiscal years ran from April 1, 2020 through March 31, 2021 (FY 2021) and April 1, 2021 through March 31, 2022 (FY 2022).
[14] Hr'g Tr. at 91 (Jun. 1, 2022).
[15] Hr'g Tr. at 47-49 (Mar. 15, 2022).
[16] *Id.* ("CHAIRMAN: Until the old main is replaced the risk of leaks on the yet-to-be abandoned main remain at the same level of risk that we had prior to putting in the new pipe next to it? MS. SMITH: The risks associated with leaks on those segments of mains would remain, yes."); *see also* Docket No. 5165 Hr'g Tr. at 33-38 (Oct. 13, 2021).

the old main remains at the level as the pressure in the new main while the old main remains in service.[17]

During the course of these proceedings, it became apparent that the Commission might need to reconsider whether it is appropriate to treat the new main as being "in service" for ratemaking purposes when the old leak-prone pipe which the new main is replacing remains in service. The ratemaking principle is referred to as the used and useful standard. The Rhode Island Supreme Court previously described this ratemaking principle:

> "We have defined 'rate base' as 'the utility's total investment in, or the fair market value of, the used and useful property necessarily devoted to the rendering of regulated service. . . . The elements of the value may be either tangible or intangible but the traditional test is whether the questioned property is 'used and useful.' A horse and buggy might conceivably be used in a modern facility, but it may not be very useful because of other modern-day modes of transportation. On the other hand, property ordered and purchased but for other reasons not placed into service might be useful but not used."[18]

The question addressed in this case is whether it is appropriate to consider the new main as "used and useful" when the old leak-prone pipe which is being replaced by the new main has not yet been abandoned. It is the prospective application of this ratemaking principle to the Proactive Main Replacement Program which is addressed by the Commission in this Order, based on the evidence in this case.

III. <u>Travel of the Case</u>

The issue of delays in abandonment was first addressed during the hearings on the Distribution Adjustment Charge on October 13, 2021.[19] In that case, the Commission discovered that there was a significant lag in the Proactive Main Replacement Program between when new

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[17] Hr'g Tr. at 28-35 (October 13, 2021).
[18] *Newport Electric, v. Public Utilities Commission*, 624 A.2d 1098, 1101 (R.I. 1993)(citations omitted).
[19] Docket No. 5165. As noted, *supra*, the Commission has taken administrative notice of the record and transcript of the October 13, 2021 hearings in Docket No. 5165, the testimony of which was referenced in the hearings in this docket.

gas mains were installed and the date when the associated leak-prone pipe to be replaced was abandoned. The Commission questioned the Company on whether the new pipe was accomplishing its purpose in eliminating risk while the leak-prone pipe continued to be in service. In response, a Company witness responded that risk of leaks on the main would remain the same, confirming that in order to eliminate the risk, the main would have to be abandoned.[20] Subsequent to that proceeding, the Company filed its annual ISR Plan in the instant docket for fiscal year 2023.

During the March 15, 2022 hearing in this docket, the Company was asked numerous follow-up questions about the delay in abandonments that had occurred in the prior two fiscal years, including the ratemaking implications under the used and useful standard. Specifically, the Commission questioned why ratepayers should be paying for new main before it was achieving its purpose of safety and reliability.[21]

On March 23, 2022, the Commission held an Open Meeting during which it discussed the use and useful standard at length. Later, on March 29, 2022, the Commission unanimously approved the ISR plan and proposed budget, subject to refund on issues relating to the main replacement program and specifically noted in the motion that application of the used and useful standard would be reviewed. Specifically, the Commission voted to "continue the hearings to a date to be determined to continue its review of the Company's lag in performance regarding the timing of abandoning leak-prone pipes that are intended to be replaced in the Proactive Main Replacement Program, including a review of the reasons for the lag, the apparent lack of incentive for timely abandonment, and ***the ratemaking implications relating to the application of the used and useful standard.***"[22] Following that Open Meeting, the Commission issued additional

[20] Docket No. 5165 Hr'g Tr. at 37-38 (Oct. 13, 2021).
[21] Hr'g Tr. at 84 (Mar. 15, 2022).
[22] Open Meeting Minutes at 5 (Mar. 29, 2022)(emphasis added).

discovery to continue its investigation. The Commission then issued a Notice of Public Hearing on May 23, 2022 scheduling a hearing for June 1, 2022. The notice specifically identified that the Commission would continue to examine the ratemaking implications relating to the used and useful standard.

At the June 1 hearing, the Commission engaged in considerable questioning of the Company regarding the abandonment process and the associated rate making issues. The Commission queried whether the Company or the ratepayers should bear the financial risk of the delay in abandoning the leak-prone pipe.[23] The Commission also asked the parties for comment regarding potential ratemaking changes, including a change in how the used and useful standard would be applied to the Proactive Main Replacement Program.[24] The Company and the Division provided responses to the request for comments.

After the final evidentiary hearings on June 1, 2022, the Commission held two Open Meetings to deliberate. The first was on August 30. During the initial deliberations, the Chairman addressed two pending issues: 1) application of the used and useful standard and 2) whether a service quality metric should be developed that would further incentivize the Company to abandon the leak prone pipes within a reasonable time after the new main is gassed in. The Chairman expressed that he was not prepared to rule on any service quality metric issue, which was a matter that could be taken up in the next ISR filing. Regarding the used and useful standard, however, he stated that he had prepared a detailed memorandum for use in deliberations. It consisted of his analysis of the used and useful standard as applied to the evidence presented in the case that he wished to share as a part of the discussions leading to a decision. It included an explanation why he believed it was appropriate to change the Company's practice of including the new main in rate

[23] Hr'g Tr. at 158 (Jun. 1, 2022).
[24] For administrative convenience the request for comments was identified in as Record Request 23 (Jun. 1, 2022).

base prior to the time it had abandoned the leak-prone pipe which the new main was intended to replace.

Rather than reading the draft aloud, he provided a copy of his draft to the Commissioners at the meeting to allow the other Commissioners the opportunity to read and consider his analysis as a part of the deliberations. The memorandum was emailed to the parties and immediately posted on the Commission's website to address open meeting considerations. The Commission continued the Open Meeting to a date in the future when the details of the memorandum could be discussed and a decision be made as to whether the new main should be considered used and useful prior to the old main being abandoned.

The Commission then noticed a second Open Meeting for September 13, 2022 to continue deliberations on the matter. On September 13, 2022, a few hours prior to the commencement of the Commission's continued deliberations, the Division filed a motion or request which essentially asked the Commission to halt its deliberations.[25] The Division's request alleged that "the Commission *generally mentioned* some of its concerns" (emphasis added) prior to the June 1, 2022 hearing and that it was not until after the June 1 hearing through a response to the Commission's request for comments that the Division had the opportunity to respond to the ratemaking issues. The Division claimed it was not given the opportunity to "retain expert consultant(s), to prepare and submit direct testimony, or to be heard on the precise issues framed by [the Commission's request for comments]…." The Division argued that the record was not well-developed and that Commission action will result in a "momentous change of regulatory precedent." Lastly, the

[25] Division of Public Utilities and Carriers' Request for the Commission to Postpone its Open Meeting Deliberation and Vote in Docket No. 5210 Scheduled for September 13, 2022, and for the Commission to Conduct Evidentiary Hearings on the Issues Framed in Record Request 23 and Discussed in the August 30, 2022 Memorandum (Sept. 13, 2022).

Division opined that the consequences of a change could be “detrimental to ratepayers,” but gave no indication of how or why that might be the case.

At the September 13 Open Meeting, the Commission addressed (i) the pending question regarding the delays in abandoning the old leak-prone pipe during the pandemic, (ii) the Division’s motion to halt deliberations, and (iii) the question relating to the application of the used and useful standard to the Proactive Main Replacement Program. Each of the decisions are addressed below.

IV. Decision

A. The Delays Regarding Abandonments During the Pandemic

As described above, one of the pending issues in this docket involved a review of the reasons why the Company experienced significant delays between the installation of new mains and the abandonment of old leak-prone mains which the applicable new mains were designed to replace. The Company testified that the COVID pandemic was the cause of the delays and provided additional data supporting the position.[26] The Division concurred with the Company’s claim that the delays were reasonable under the circumstances.[27] Based on the evidence, the Commission has accepted the prudency of the management of the main replacement projects that were undertaken in fiscal years 2021 and 2022, even though the pace of abandonments fell well below the pace of new main installations. The Commission finds no basis for concluding that the Company acted in an imprudent manner which would justify a disallowance of cost recovery from the periods in fiscal years 2021 or 2022. Accordingly, the Commission approves the revenue requirement related to the forecasted recovery of main replacements which were conditionally approved by the Commission in its prior order.

[26] Hr’g Tr. at 25-29 (Jun. 1, 2022).
[27] Hr’g Tr. at 143-145 (Jun. 1, 2022).

B. The Division of Public Utilities and Carriers' Request to Halt the Commission's Open Meeting Deliberations

As described above, the Division requested that the Commission essentially halt its deliberations and give the Division a new opportunity to address the used and useful ratemaking rule which had been under consideration since the hearings of March 15, 2022 and the Commission's Open Meeting on March 23, 2022. For the reasons explained below, the request was denied.

The Division's assertion that the Commission "generally mentioned some of its concerns" regarding the Company's practice of including new main in rate base prior to the old main being abandoned is not only inaccurate, but leaves out important procedural steps in the sequence of events of what had actually transpired. As described above, the Commission's inquiry on the ratemaking implications of the Proactive Main Replacement Program was precipitated from testimony in another docket during the October hearing on the Distribution Adjustment Charge in Docket No. 5165. Approximately six months later in this docket, the Commission continued its questioning on this issue including more questions about the ratemaking implications under the used and useful standard. Specifically, and as set forth above, the Commission questioned why ratepayers should be paying for new main before it was achieving its purpose of safety and reliability[28] and considered what steps might be appropriate to incentivize the Company to prioritize the transfer of services once the new main is in place.[29]

The Commission then discussed the ratemaking issue relating to the used and useful standard during two Open Meetings. On March 23, 2022, the Commission discussed in detail the

[28] Hr'g Tr. at 84 (Mar. 15, 2022).
[29] *Id.* at 299-300, 303-306.

used and useful standard and the question of whether it was appropriate to include new main in rate base when the old main has not been fully abandoned.[30]

On March 29, 2022, the Commission then unanimously passed a motion

> "to continue its review of the Company's lag in performance regarding the timing of abandoning leak-prone pipes that are intended to be replaced in the Proactive Main Replacement Program, including a review of reasons for the lag, the apparent lack of incentive for timely abandonment, and ***the ratemaking implications relating to the application of the used and useful standard***." (emphasis added).[31]

On April 1, 2022, the Commission issued further data requests to the Company regarding the Company's past performance in abandoning leak-prone pipes. Between March 25 and June 1, the Division did not retain an expert, file testimony, offer any written legal analysis on the application of the used and useful standard, or explain why in its role as the ratepayer advocate, the Division believed it was in the best interests of ratepayers to leave the timing of the current cost recovery in place.

Despite the fact that the Commission's vote and notice clearly indicated that the Commission would be addressing the application of the used and useful standard, the Division chose not to present any witnesses at the June 1 hearings to address the ratemaking rule. The Division's testimony focused solely on the Company's past lag in performance, stating no position on the used and useful standard.[32] The only comment offered by the Division was from counsel for the Division at the close of the hearing, briefly referencing the March 23, 2022 Open Meeting when the Commission referred to a Supreme Court case[33] on the used and useful standard which

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[30] Open Meeting Minutes at 5 (Mar. 23, 2022).
[31] Open Meeting Minutes at 3 (Mar. 29, 2022).
[32] Hr'g Tr. at 135-145 (Jun. 1, 2022).
[33] *Newport Electric Corporation v. Public Utilities Commission*, 624 A.2d 1098, 1101 (R.I. 1993)(citations omitted).

had been discussed at that Open Meeting.[34] No further elaboration of the Division's position was provided at the hearing.

The Division's assertion that it did not have ample notice to address the issue raised by the Commission is without merit. The used and useful standard was discussed numerous times and reflected in the hearing notice.[35] The Division was aware since the Commission discussed the matter at length on March 23, 2022 and then voted at the March 29, 2022 Open Meeting that the Commission had a keen interest in the issue and would be ruling on the same at a later date. The Division was given ample opportunity to present a detailed argument but chose not to do so when it filed its response to the June 1, 2022 request for comments. The deliberations commenced on August 30. Yet, it was not until the morning of the September 13, 2022, only 3½ hours prior to the continuation of deliberations that the Division sought to stop the Commission's decision-making process, requesting a continuance to further investigate, research, or hire a consultant.

In summary, the request was out of order and denied for the following reasons:

(i) the ratemaking issue was unambiguously identified five months earlier in March,

(ii) the notice for the June 1, 2022 hearing clearly identified the ratemaking issue,

(iii) the evidentiary hearings directly addressing the issue took place in early June, two full months before deliberations at Open Meeting commenced,

(iv) the Division was asked to comment in June and never directly addressed the used and useful standard in its comments,

[34] Hr'g Tr. at 163-164 (June 1, 2022).

[35] When the Division made its filing requesting the Commission halt its deliberations, the Division did not explain why the notice for the hearing in June was inadequate, which contained language similar to the vote that was taken on March 23, 2022: "At this hearing, the Commission will continue examination of the Company's lag in performance regarding the timing of abandoning leak-prone pipes that are intended to be replaced in the Proactive Main Replacement Program, including a review of the reasons for the lag, the apparent lack of incentive for timely abandonment, ***and the ratemaking implications relating to the application of the used and useful standard***." (emphasis added).

(v) the deliberations by the Commission had already commenced on August 30, 2022, two weeks before the request to halt deliberations was filed,

(vi) no new evidence was provided to justify the request to halt deliberations, and

(vii) the Division waited until approximately 3 hours before the final open meeting to file its request.

Accordingly, the Commission denied the request.

C. The Timing of Rate Base Treatment: Applying the Used and Useful Standard with the "Act on Climate" in View

During the June 1, 2022 hearings, the Commission asked the parties to comment upon two potential ratemaking rules relating to the Proactive Main Replacement Program which arose from considering the testimony in the evidentiary hearings. The inquiry for comments stated:

> Given the high degree of importance that the Act on Climate places on reducing greenhouse gas emissions, please provide comment on the reasonableness of the Commission adopting a revised ratemaking rule for the Gas ISR for the purpose of incentivizing the Company to complete each project all the way through to abandonment of the old leak-prone main. The proposal would have two parameters:
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> (i) New gas mains under the Company's main replacement program would not be considered to be "in-service" for ratemaking purposes until the old main with which the new replacement main is associated is abandoned; and
>
> (ii) The Company would be directed to stop the charging of AFUDC as of the date that the Company connects the first customer to the new main or, if it is a gas main that would not be expected to have any service connections, the date the main is "gassed-in."[36]

Except for making a legal argument that the Act on Climate did not contain a provision to override the Rhode Island Supreme Court precedent with respect to the used and useful standard, the Company's response did not make any attempt to address the Act on Climate.[37] Contrary to the Company's perception, however, the Commission was not proposing to override the used and

[36] Record Request 23 (Jun. 1, 2022).
[37] TNEC Response to Record Request 23 at 4 (Jun. 29, 2022).

useful standard. Rather, the Commission was proposing to apply the used and useful standard based on a finding that until the old main is abandoned, it is not reasonable to treat the new main as being "useful." This was supported by the evidence in the record provided in testimony from Company witnesses, the significance of which is amplified by the objectives and directives of the Act on Climate to reduce greenhouse gas emissions.[38]

The Company also argued that once newly installed mains are gassed in, they are being devoted to regulated service and, thus, considered used and useful for purposes of including the main in rate base. This argument is simplistic and ignores the principle that a capital project needs to be providing net benefits to ratepayers. A partially completed capital project which is not yet providing a net benefit to ratepayers is not ripe for rate base treatment unless there are clear benefits to ratepayers for allowing it. As stated by a court in neighboring jurisdiction: "The 'used and useful' standard generally requires that a utility plant must be in commercial operation and providing net benefits to customers in order for expenses associated with it to be included in rate base."[39] There also has been scholarly commentary that has emphasized the importance of a capital project providing benefits in order to be given rate base treatment under the used and useful standard.[40] Further, it has been noted that in order for a project to be considered "used and useful," it not only must be "devoted to providing utility service," but also must be "reasonably necessary

[38] The Commission also notes that the Act on Climate contains a directive which states: "Addressing the impacts on climate change shall be deemed to be within the powers, duties and obligations of all…agencies, commissions…" R.I. Gen. Laws § 42-6.2-8. The Act on Climate established enforceable targets for the reduction of greenhouse gas emissions and reflects a policy that prioritizes the reduction of greenhouse gases into the atmosphere. One of the key objectives of the main replacement program is to eliminate the risk of methane being released into the environment from the leak-prone pipes targeted for replacement. This objective is not met by the installation of the new main unless and until the old-leak-prone pipe is replaced.

[39] *Town of Hingham v. Dpt. Of Telecommunications and Energy*, 740 N.E.2d 984, 989 (Mass. 2001).

[40] *See* Baumol, W., "The Pig in the Python: Is Lumpy Capacity Investment Use and Useful?", 23 *Energy L.J.* 383, 385-386 (2002); Hoecker, J., "'Used and Useful': Autopsy of a Ratemaking Policy," *Energy L.J.* 303, 312 (1987). It is important to note that the case of main replacement of leak-prone pipe is not a case of installing excess capacity for a targeted forecasted need to avoid capacity shortages which is economically beneficial when installed, it is a case of main installation projects not yet complete to meet the targeted purpose.

to the provision of utility service."[41] While the main replacement project needs to be sequenced to transfer the services over, the new main is not technically needed for the service connections to customer facilities until the old main is no longer in service. Stated simply, the project is not complete and providing net benefits until all the transfers occur and the old main is abandoned.

It is important to note that the Commission has a considerable amount of discretion when applying ratemaking methods to the decisions it makes. As the Supreme Court has stated, "when reviewing a decision of the commission, [the Court's] concern is not with the method used to attain a particular result but with the fairness and reasonableness of the end result itself. . . . Indeed, keeping in mind the determination of what is fair and reasonable requires a balancing of investor and consumer interests."[42] The Commission's ruling in this case is fair to both the utility that will still recover its costs, and to the ratepayers who are funding those costs and expecting the leaks to be addressed within a reasonable time as a result of the expenditures. Further, it is apparent from the review of sources, that the used and useful standard has been interpreted and applied in different nuanced ways across various jurisdictions and is "not constitutionally mandated."[43]

Similarly, the Division did not adequately address the relevancy of reducing greenhouse gas emissions in applying the ratemaking standards given the Act on Climate. Instead, the Division made only two passing references to the Act and expressed a concern that the proposal would be "tantamount to a denial of cost recovery" for the utility – concluding that the delays that occurred

[41] "'Used and Useful' Rule" 73B *C.J.S. Public Utilities* § 51 (May 2022).
[42] *Michaelson v. New England Tel. & Tel. Co.,* 404 A.2d 799, 809-10 (1979)(Citing *Narragansett Electric Co. v. Harsch,* 117 R.I. 395, 418, 368 A.2d 1194, 1208 (1977((Citing *FPC v. Hope Natural Gas Co.,* 320 U.S. 591, 602, 64 S.Ct. 281, 287-88, 88 L.Ed. 333, 344-45 (1944).
[43] "'Used and Useful' Rule," 73B C.J.S. Public Utilities § 51 (Aug. 2022 Update). The Company also made a passing reference to the Federal Energy Regulatory Accounting Regulations, stating that its current way of applying the used and useful standard "is consistent with" those rules. But this bare statement of consistency asserts nothing binding about the way they have historically applied the ratemaking rule as an accounting convention. Whether an asset is used and useful is a factual determination by the regulatory authority approving the rates.

during the pandemic were now being adequately addressed.[44] However, there is no denial of cost recovery when the project is not treated as "useful" when the abandonment has not yet occurred. A change in how the Commission determines when the new main is used and useful merely provides a more relevant and updated application of the ratemaking standard. The utility would not be deprived of putting the capital cost in rate base. Rather, the change merely shifts the timing of recovery to the point when ratepayers are actually realizing the benefits which the project is set out to achieve. The Commission is simply making a finding, based on the evidence, that the main replacement project has not been sufficiently completed to conclude that it is useful to the wide body of ratepayers.[45] The shifting of the timing of recovery will not deny the utility company cost recovery.

Further, during the hearing on June 1, 2022, the Commission was clear when it asked who should be bearing the financial risk of delay in the abandonment. Specifically, the Chairman stated: "And I think if your conclusion is the ratepayer should bear the risk, then we need to understand there must be some offsetting reason why it's good for the ratepayers to bear that risk. . . . So, in your response it would be important to say we're okay with the ratepayers bearing that risk because it provides this other benefit . . . ."[46] The Commission, however, was not provided with any answer to this inquiry from either the Company or the Division.

Given these considerations, the Commission is changing the timing of inclusion of new main in the ISR rate base. The Commission finds that the leak-prone main replacement projects should no longer be treated as having been completed for ratemaking purposes at the time of the

[44] Division Response to Record Request 23 (Jun. 29, 2022).
[45] While the service connections to the new main may be benefitting those certain customers that have been connected, it is illogical to believe that the benefit of those service connections to a few customers in these specific instances is what is intended as "benefit to ratepayers" for purposes of including the entire new main in rate base. A more logical interpretation is that benefit to customers includes those customers that are contributing to the utility's return on equity, depreciation expense, and taxes, in other words, the wide body of ratepayers.
[46] Hr'g Tr. at 156 (Jun. 1, 2022).

first customer service connection. The Commission finds that while the new main is being used, it is not yet "useful" until the associated leak-prone pipe is abandoned. Accordingly, subject to the conditions in this Order, the new main is includable in ISR rate base when the old main associated with the specific project has been taken out of service.[47] The Commission is confident that application of this ratemaking principle should cause the Company to act expeditiously in abandoning leak-prone mains. It is important to note that the Company's dual operation of both pipes does not fulfill the objective of the ISR law to achieve both safety and reliability until the abandonment occurs. In that context, this finding of the Commission can stand on its own, even if there were no directives arising out of the Act on Climate to reduce greenhouse gas emissions.

This change in ratemaking rules will be prospective only. Because the Company has already undertaken projects during fiscal year 2023, the Commission will not apply this rate accounting rule for projects that were approved for the ISR 2023 fiscal year, or projects still pending from prior years. The new rule will take effect for all projects approved in the Company's next ISR filing.

Accordingly, it is hereby

(24541) ORDERED:

1. With respect to the Proactive Main Replacement Program, commencing with all leak-prone pipe replacement projects proposed and constructed pursuant to the next ISR Plan filed before the end of calendar year 2022, new main that is constructed to replace the applicable

[47] The Commission does note that there may be unusual circumstances where it would be beneficial to ratepayers to install the new main even though it is clear at the time of planning that the abandonment is not likely to take place within a reasonable period of time. The Company may seek an exception to the rule for individual projects at the time it is seeking approval of its ISR plan. However, the Company carries a high burden of proof to show the benefits to ratepayers of going forward with the particular replacement project are important to obtain even though the Company knows that abandonment of the leak-prone main is likely to be materially delayed. One hypothetical example might be a bridge project when the opportunities for doing a crossing will be limited, even though it means that a portion of the old main will have to remain in service for a longer period of time.

leak-prone pipe will not be considered used and useful and therefore eligible for rate base treatment until the date that the leak-prone pipe is actually abandoned.

2. The revenue requirement category provided in the FY 2023 ISR Plan relating to the forecasted recovery of main replacements which was conditionally approved in ordering paragraph (b) of Order No. 24452 is approved.

EFFECTIVE AT WARWICK, RHODE ISLAND ON SEPTEMBER 13, 2022 PURSUANT TO AN OPEN MEETING DECISION ON SEPTEMBER 13, 2022. WRITTEN ORDER ISSUED NOVEMBER 18, 2022.

PUBLIC UTILITIES COMMISSION

Ronald T. Gerwatowski, Chairman

Abigail Anthony, Commissioner

John T. Revens, Jr., Commissioner

NOTICE OF RIGHT TO APPEAL: Pursuant to R.I. Gen. Laws § 39-5-1, any person aggrieved by a decision or order of the PUC may, within seven days from the date of the order, petition the Supreme Court for a Writ of Certiorari to review the legality and reasonableness of the decision or order.