

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service
Commission held in the City of
Albany on April 18, 2013

COMMISSIONERS PRESENT:

Garry A. Brown, Chairman
Patricia L. Acampora
Maureen F. Harris
James L. Larocca
Gregg C. Sayre

CASE 13-G-0136 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of the National Fuel Gas Distribution Corporation for Gas Service.

ORDER INSTITUTING PROCEEDING AND TO SHOW CAUSE
(Issued and Effective April 19, 2013)

BY THE COMMISSION:

INTRODUCTION AND BACKGROUND

In Case 07-G-0141, the Commission established rates for National Fuel Gas Distribution Corporation (National Fuel or the Company).¹ In the 2007 Rate Order, the rates set for National Fuel were expected, among other things, to permit National Fuel to earn a return on equity (ROE) of 9.10% for the rate year ended December 31, 2008 based on a 44.35% common equity ratio. Under the 2007 Rate Order, there is no ROE earnings sharing mechanism, and, therefore, National Fuel retains all excess earnings when they occur. The rates and other terms prescribed in the 2007 Rate Order remain in effect today.

A review of the Company's more recent financial statements by Department of Public Service Staff (Staff)

¹ Case 07-G-0141, National Fuel - Rates, Order Establishing Rates For Gas Service (issued December 21, 2007)(2007 Rate Order).

indicates that National Fuel may now be earning in excess of the 9.10% ROE envisioned by the 2007 Rate Order, and in excess of a reasonable return. Staff's projection forward suggests that this condition may continue in the future.

Specifically, National Fuel measures its annual earnings on a fiscal year basis that ends September 30th. The latest earnings calculation provided by the Company based on a 50% equity ratio, for the twelve months ended September 30, 2012, showed an earned unadjusted ROE of 12.77%. National Fuel made normalizing adjustments that appear to reduce the ROE to 11.87%. However, after adjusting the Company's calculation for the 44.35% equity ratio allowed in its current rates and removing executive restricted stock and stock option compensation expense not allowed in current rates, Staff calculates that National Fuel earned a 13.15% equity return for the twelve months ended September 30, 2012.

In addition to National Fuel's earning in excess of its allowed rate of return, certain expenses, including Pension, Other Post Employment Benefits (OPEBs), and Site Investigation and Remediation (SIR) expenses, are being deferred by the Company for future recovery from customers. Thus, for fiscal year 2012, which is the same year in which the Company, pursuant to Staff's analysis, earned a 13.15% equity return, the Company recorded net deferrals owed by its customers of \$7.6 million, and the total accumulated deferrals owed by its customers for Pensions, OPEBs and SIR, as of September 30, 2012, was \$13.1 million.²

Staff reports that after an examination of all data to date it expects National Fuel will be earning, with the rates

² This deferral amount does not include the \$6.8 million of SIR expense owed the Company as mandated by The New York State Court of Appeals. National Fuel Gas Distribution Corporation v. Public Service Commission, 16 N.Y.3d 360 (2011).

set in the 2007 Rate Order, at or near the 2012 levels for fiscal year 2013, and deferral levels are expected to likewise continue in 2013.

NATIONAL FUEL PROPOSAL

On March 27, 2013, National Fuel filed a proposal (Proposal) that would allow the Company to share its "...savings with its customers by implementing an earnings sharing and stabilization mechanism and by accelerating its infrastructure modernization program."³ Under the Proposal, the earnings sharing mechanism would be on a cumulative basis for three years beginning on June 1, 2013 and ending on May 30, 2016. Fifty percent (50%) of any cumulative earnings above 9.96% would be placed in a reserve fund. Any annual excess or deficiency would carry forward and the 50/50 sharing of earnings would occur only if National Fuel exceeds the 9.96% ROE in year 3 (June 1, 2015 to May 30, 2016).

Under this Proposal, the ratepayer share would be put into a reserve and used to fund the Company's economic development program (the Area Development Program), and to promote gas expansion in areas where such expansion is economically not feasible. National Fuel would also increase its investment in infrastructure and for storm-hardening upgrades in flood-prone areas, as well as continue to replace its Customer Information System. The Company also proposes to fund a program to apply an existing credit on qualified low-income customer bills, in an amount to be determined, using unspent Low Income Customer Affordability Assistance Program revenues which are currently deferred.

³ Case 07-G-0141, National Fuel Proposal, p. 1.

DISCUSSION AND CONCLUSION

National Fuel's earnings level indicates that its gas rates may be higher than needed to provide safe and adequate service, particularly in light of the recently allowed ROE and earnings sharing provisions established for other utilities.⁴ Further, absent action, National Fuel's deferral balances may continue to escalate during a period of time that the Company is earning a return in excess of its cost of equity. These circumstances may result in National Fuel customers paying higher rates than are just and reasonable.

These results, should they occur, would not be in the public interest and the possibility of their recurring in the coming rate year requires our action. Therefore, we institute this proceeding to examine the need to revise the gas rates of National Fuel and to provide ratepayers with appropriate and concomitant adjustments to the Company's deferred accounts, pursuant to our statutory authority under Public Service Law (PSL) §§66, 72, and 114.

National Fuel's Proposal recognizes that its various cost saving and control measures have reduced "... the cost of operating the Company's business in New York to a level below what it was when rates were last set ... in 2007."⁵ We have, in the past, and will continue to commend National Fuel for cutting costs and increasing productivity. In addition, we regard

⁴ Case 12-G-0202, Niagara Mohawk Power Corporation d/b/a National Grid - Rates, Order Approving Electric and Gas Rate Plans In Accordance with Joint Proposal (issued March 15, 2013) (9.3% ROE and earning sharing in excess of 9.3%); Case 11-E-0408, Orange and Rockland Utilities, Inc. -Rates, Order Adopting Terms of Joint Proposal, With Modifications, And Establishing Electric Rate Plan (issued June 15, 2012) (Three year rate plan ending June 30, 2015 - ROE RYE June 2013 (9.4%), June 2014 (9.5%) and June 2015 (9.6%) - annual sharing thresholds 80 basis points above the ROE).

⁵ Case 07-G-0141, National Fuel Proposal, p. 4.

positively the Company's recent proposals to dedicate some portion of over earning to customer interests. However, the Company's current Proposal does not yet describe an adjustment to existing rates large enough to fully compensate for the imbalance between ratepayer and shareholder interests that has developed since the 2007 Rate Order.

We also note that while National Fuel has been reducing its costs of providing service during this period it has achieved the service and safety performance standards that we established in the 2007 Rate Order. In the most recent Staff report provided to us concerning customer service performance of major energy utilities for 2011, National Fuel demonstrated better than average performance in most of the metrics used to measure customer service.⁶ However, as noted in the 2011 Gas Safety Performance Measures Report,⁷ Staff recommended that National Fuel conduct a self assessment in the areas of Damage Prevention and Leak Management performance. Our safety targets for National Fuel were established from statewide performance information in 2006. Given this length of time, there may be areas that require review and future improvement.

In this case, a process will be developed to examine the resetting of the Company's rates going forward. The results of this process will not be final for months, at a minimum. The Company's Proposal makes no provision to fully protect ratepayers while this case is moving toward that conclusion. In the absence of a Company proposal to fully and fairly adjust current rates on a permanent basis, and in the further absence of a proposal to fully protect ratepayer interests while appropriate permanent rates are being determined, we must

⁶ Case 12-M-0170, Staff Report on 2011 Energy Utility Service Quality Performance, July, 2012.

⁷ Case 12-G-0222, 2011 Gas Safety Performance Measures Report, May 31, 2012.

consider the establishment of temporary rates, pursuant to PSL §114, at their current levels subject to refund.⁸

Accordingly, unless National Fuel within seven days of the issuance of this order, agrees to make its current gas rates and charges temporary subject to refund, effective June 1, 2013,⁹ it is directed to show cause, on or before May 8, 2013, why we should not direct the Company to immediately file tariff revisions to establish temporary rates subject to refund pursuant to PSL §114 (Show Cause Filing). If the Company declines to voluntarily make rates temporary, but instead makes the Show Cause Filing, interested parties, including Staff, shall have ten days from the date of the Company's filing to respond. All parties, including National Fuel, will then have three days to reply to the parties' responses.

Further, regardless of which above option the Company elects, the Company shall also file on or before May 8, 2013, at a minimum, detailed cost of service, rate base, and capitalization schedules, sales forecast and work papers to support calculations of earnings for the period ending May 31, 2014 (COS Filing).

Our evaluation of the need for temporary rates will be conducted on an expedited basis and consistent with the filing dates in this order. We direct that an Administrative Law Judge be immediately assigned and, upon assignment, assume the management of this case so that we may make a timely and fully informed decision on the establishment of temporary rates at our

⁸ Case 06-E-1433, Orange and Rockland Utilities - Temporary Rates, Order Making Temporary Rates Subject To Refund (issued March 1, 2007); Case 00-G-1495, National Fuel- Rates, Order To Show Cause (issued August 31, 2000).

⁹ Such an agreement would represent National Fuel's consent to establish temporary rates without a hearing or further process.

June 2013 session. The Administrative Law Judge will also be tasked with examining the applicability and appropriateness of PSL §66(20) as a potential remedy in addition to temporary rates. A fuller examination of the case, including the establishment of permanent rates, can proceed thereafter.

The Commission orders:

1. A proceeding is instituted under this case number to examine the rates, charges, rules and regulations of National Fuel Gas Distribution Corporation.

2. Unless National Fuel Gas Distribution Corporation files a statement within seven days of the issuance of this order agreeing to make its gas rates temporary subject to refund effective June 1, 2013, and consenting to establish such temporary rates without a hearing or further process prior to our temporary rate determination, it shall show cause, on or before May 8, 2013, why its gas rates and charges should not be set on a temporary basis subject to refund, as discussed in the body of this order.

3. National Fuel Gas Distribution Corporation shall file on or before May 8, 2013 all information addressing the issues raised in this order, including, but not limited to, the specific information requested herein.

4. This Order will be served on all parties to Case 07-G-0141 and all other known interested parties.

5. The Secretary is authorized to extend deadlines stated in this order.

6. This proceeding is continued.

By the Commission,

(SIGNED)

JEFFREY C. COHEN
Acting Secretary