

**STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION**

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**Proceeding on Motion of the Commission as to  
the Rates, Charges, Rules and Regulations of  
National Fuel Gas Distribution Corporation for  
Gas Service.**  
-----X

**Case 13-G-0136**

**RESPONSE OF PUBLIC UTILITY LAW PROJECT OF  
NEW YORK, INC. TO NATIONAL FUEL GAS  
DISTRIBUTION CORPORATION POSITION ON THE  
APPLICABILITY OF PUBLIC SERVICE LAW § 66(20) IN  
THIS PROCEEDING**

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**Introduction**

The Commission commenced this proceeding on April 19, 2013 to examine and revise the rates of National Fuel Gas Distribution Corporation ("National Fuel"). After reviewing Department of Public Service Staff reports that National Fuel's earnings may exceed the 9.1% contemplated by its last order setting rates in 2007, the Commission stated

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. 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.<sup>1</sup>

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<sup>1</sup> 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) ("OTSC") at 4.

In the OTSC, the Commission specifically asked the Administrative Law Judges ("ALJs") to examine "the applicability and appropriateness of PSL §66(20) as a potential remedy in addition to temporary rates."<sup>2</sup> The statute provides

Notwithstanding any general or special law, rule or regulation, the commission shall have the power to provide for the refund of any revenues received by any gas or electric corporation which cause the corporation to have revenues in the aggregate in excess of its authorized rate of return for a period of twelve months. The commission may initiate a proceeding with respect to such a refund after the conclusion of any such twelve month period.

*PSL §66(20)*. On August 26, 2013, ALJs Kevin J. Casutto and David L. Prestemon issued a Ruling on Scope and Schedule for considering the applicability of the statute in this case. In accordance with that schedule, on September 13, 2013 the Company filed a brief stating its position.<sup>3</sup> In support of its basic position that it should be able to keep any earnings above the 9.1% return intended when rates were set, National Fuel argues that the situation PSL §66(20) was intended to remedy no longer exists, refund of any excess earnings would be contrary to Commission policy goals, National Fuel's earnings, though above 9.1%, are not so high as to require refunds, and the Commission should not look back more than one year to determine the amount of earnings in excess of the allowed return.

The Public Utility Law Project of New York, Inc., submits this response to the position of National Fuel. In the OTSC and in its Temporary Rates Order, the Commission observed that National Fuel has been deferring costs to be paid in the future by consumers during the period in which it appears that National Fuel has been overearning. In this brief, PULP examines in detail how the deferred costs for pension and other postretirement employee benefits ("OPEB") increased while National Fuel realized earnings in excess of the allowed return. PULP argues

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<sup>2</sup> *Id.*, at 7.

<sup>3</sup> National Fuel also commenced an Article 78 proceeding in Erie County challenging constitutionality of the PSL § 66(20). *National Fuel Gas Distribution Company v. New York State*

that the plain language of the law gives the Commission power to require National Fuel to disgorge excess earnings and that, although the power is rarely invoked, the circumstances of this case amply warrant the exercise of that power.

**A. PSL § 66(20) Plainly Applies, and Commission Exercise of Its Power to Require Refunds is Not Limited to Circumstances when Gas Company Earnings are Inflated by Increased Deliveries in Abnormally Cold Weather**

The plain language of the statute gives the Commission “the power to provide for the refund of any revenues received by any gas or electric corporation which cause the corporation to have revenues in the aggregate *in excess of its authorized rate of return.*” PSL § 66(20) (*emphasis added*). This clearly gives the Commission discretionary power to order refunds if the utility return on equity exceeded the return allowed when rates were last calibrated. In an effort to justify its legislative history argument that the law should be read to mean something other than what it says, National Fuel attempts to spin ambiguity into the statute by suggesting that the statutory phrase “*in excess of its authorized rate of return*” refers not to the ROE but to another concept. National Fuel states:

A utility's "rate of return," however, is not its ROE but is, rather, composed of the cost of its equity, short and long-term debt and customer deposits. Given that the rate of return changes over time from that set in the utility's rate case (due to debt cost rate changes as well as equity costs), *the authorized rate of return is likely to be a completely meaningless number* for purposes of estimating a utility's real earnings.<sup>4</sup>

National Fuel’s strained effort to twist the plain statutory language requiring refund of earnings above the authorized return into a confusing reference to a “meaningless number” should be

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*Public Service Commission*, (Erie Co. Sup. Ct. Index No. 20130015148).

<sup>4</sup> National Fuel September 13, 2013 Brief at 7. (*Emphasis added*).

rejected. National Fuel gives no citation for its alternative definition of “authorized rate of return”. The Commission in the OTSC discussed and used the terms “ROE”, the “equity return,” and the “allowed rate of return” interchangeably:

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 ... 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.<sup>5</sup>

The terms “ROE” and “authorized rate of return” are not defined in the Public Service Law. In the absence of statutory definitions, it is basic that “we construe a statutory term in accordance with its ordinary or natural meaning.” *FDIC v. Meyer*, 510 U.S. 471, 476 (1994). It is well known that in rate cases there is usually heated controversy and discussion and determination of the appropriate return on equity to be authorized by the Commission. The ordinary or natural meaning of the “authorized rate of return” language in the statute, as is reflected by the Commission’s discussion and use of the terms in the OTSC, is the same as the ROE and the “allowed rate of return.” Accordingly, there is no reason to resort to legislative history to find different circumstances when § 66(20) gives the Commission has power to require a refund. These circumstances are manifestly clear from a plain reading of the law: the power arises when a gas or electric utility earns “revenues in the aggregate in excess of its authorized rate of return for a period of twelve months.” *PSL § 66(20)*.

National Fuel cites legislative history of § 66(20) in a strained effort to limit the plainly worded reach of the statute. National Fuel claims the law is intended only to apply to situations

where abnormally cold weather periods might enable a gas utility without a weather normalization clause in its rate plan to realize windfall profits. Obviously that is far afield from the language of the statute. But even if the history establishes that the sponsor's stated motive for introducing the legislation was spurred by such an incident, the actual statute enacted by the legislature and approved by the Governor was far broader: it confers upon the Commission general power to require a refund when the predicate for corrective action – earnings of a gas or electric corporation in excess of the authorized return for a period of twelve months – exists.

National Fuel also argues that regulatory practices which evolved subsequent to passage of the statute, such as the weather normalization clause and revenue decoupling mechanisms, reduce the possibility a gas company will earn windfall profits from cold weather, and so the statute is no longer needed and should be ignored.<sup>6</sup> The statute has not been repealed. Subsequent ratemaking trends do not eliminate the power of the Commission to require refunds for the benefit of consumers when the conditions are satisfied.

National Fuel invokes a nostalgic model of good old fashioned filed rate regulation with regulatory lag, suggesting that it gives results superior to the multi-year rate plans with earnings sharing agreements in vogue at the Commission for two decades or more. National Fuel overlooks, however, that the 2007 National Fuel rate plan still in force is hardly an example of the traditional fixed rates model. It includes numerous rate adjustment provisions under which utility risk is reduced. For example, it allows National Fuel to reconcile its actual costs for the gas commodity, to adjust rates for weather variations, to adjust the bulk of revenues to a predetermined target with revenue decoupling, and to defer certain major new costs and rising

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<sup>5</sup> *OTSC* at 2.

<sup>6</sup> The existence of weather normalization and true-up mechanisms to adjust rates actually cuts against National Fuel's argument that it is unfair to refund excess earnings under § 66(20),

liabilities incurred during the rate plan. These features diverge from a classic filed rate regime by allowing for retroactive adjustments that often mean additional recovery from customers of new costs arising while the “fixed” rates were in place. All of these mechanisms can work to limit the risks for the utility. When a gas or electric utility over-earns and there is reason to trim the over earnings in a proper case such as this one, there is no injustice in using the refund remedy created by § 66(20).

**B. Applying § 66(20) in this Case to Disgorge National Fuel’s Excess Returns is Warranted Because National Fuel Used Excess Earnings to Increase Dividends to Shareholders While Simultaneously Deferring Burgeoning Liabilities for Pension Costs that will Otherwise Burden Consumers in Future Years**

As National Fuel points out, the Commission can and usually does allow utilities to earn and keep revenues in excess of the return authorized by a prior rate order. But it does so when it deems it to be reasonable, for example, when there is a long term rate plan with sharing provisions to benefit customers if earnings exceed the level identified in the rate plan. This furthers the Commission goals of promoting long term rate setting, reduces costly litigation, and arguably promotes settlements where both the utility and consumers benefit when earnings exceed the level intended to be achievable when rates were set.

In this case the rate plan was approved in 2007 before the Great Recession, and it has no mechanism to address situations when National Fuel’s earnings exceed a 9.1% return. Unanticipated results flowed from the working of other features of the rate plan. In particular, much higher pension and OPEB plan unfunded liabilities were identified, because the value of assets in pension and OPEB trusts did not rise sufficiently to offset future plan benefit obligations. These increased obligations were not met by National

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because these mechanisms work to protect the company by reducing the risk of under earning.

Fuel, but instead were deferred as regulatory assets, to be recovered in the future from its customers. Thus, “good” developments following 2007 (e.g., lower interest on debt and lower labor costs due to cost cutting) increased National Fuel’s earnings to levels above 9.1%, while major “bad” developments (higher unfunded pension and OPEB liabilities) were parked in accounting deferrals to be paid by customers in future years. Instead of using excess revenues to fund and defray the soaring pension liabilities, National Fuel paid increased dividends to its holding company parent. In its OTSC, the PSC stated:

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. . . . [W]e 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 . . . .

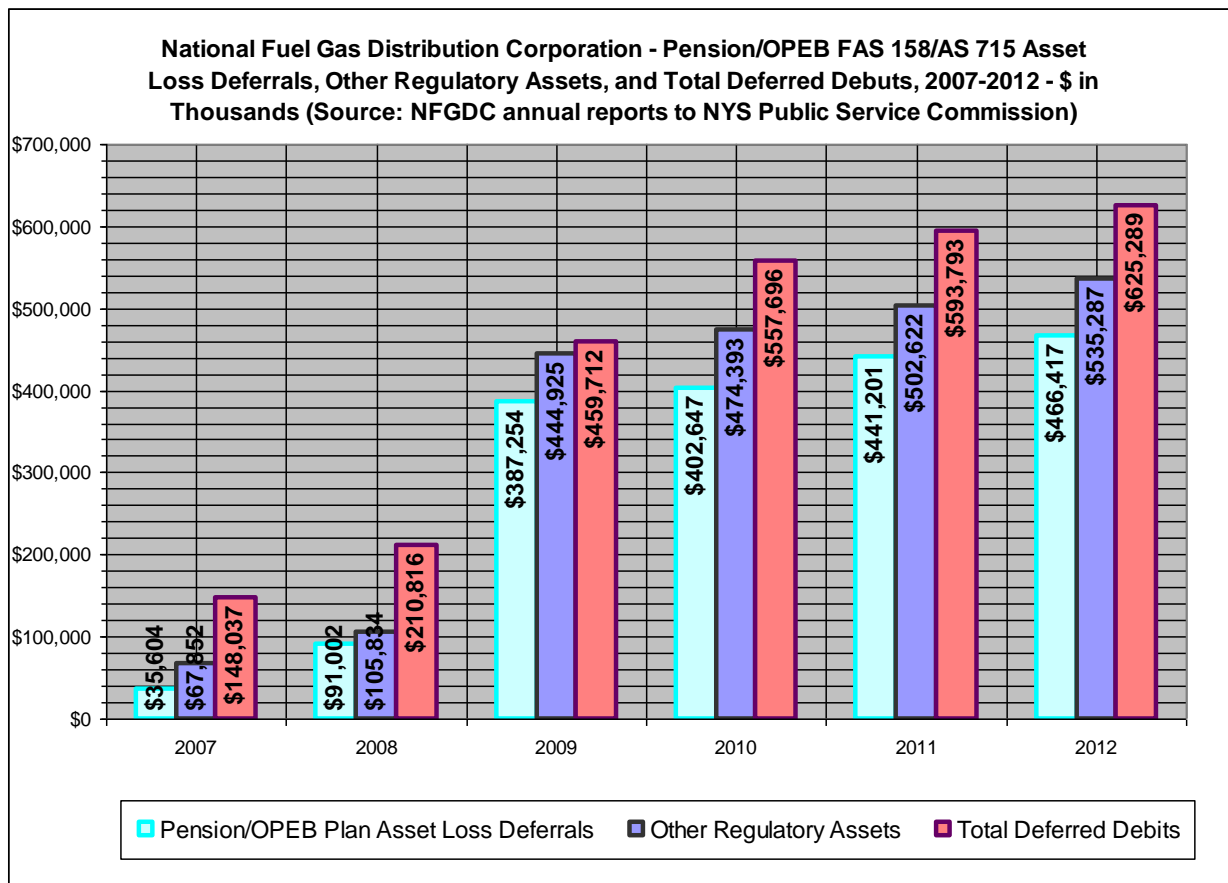
*OTSC* at 4.

PULP agrees with the Commission that there is a significant risk that the Company’s deferral balances may continue to escalate. PULP’s review finds that most of these deferrals (over 80% of “Other Regulatory Assets” as of September 30, 2012) relate to deferrals for losses in National Fuel’s pension and OPEB plans, which are required to be recorded by accounting standards FAS 158 / ASC 715.<sup>7</sup> The following chart illustrates both the large increase of deferrals during the period of over earning, and that the bulk of deferrals consist of those for pension and OPEB:

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<sup>7</sup> Accounting Standards Codification (ASC) 715 codifies former FASB Statement 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R). ASC 715 requires that the funded status of defined benefit postretirement plans be recorded as an asset or liability on its balance sheet. Funded status is computed as the difference between plan assets and the





In order to understand how liabilities to be paid in the future by National Fuel customers grew while the Company over earned and increased its dividends, a brief summary of the mechanisms for determining, adjusting, and deferring expenses for pension contributions is necessary.

**i. The Mechanisms for Determining, Deferring and Amortizing Actuarial Losses on Pension and Other Postretirement Plan Assets.**

The pension and OPEB plans generated actual returns over the years from 2002-2012 that, annually, varied positively or negatively from each plan’s “Expected Return on Plan Assets”. For New York regulatory purposes, the impact of such annual variances is buffered using a deferral and amortization process set forth in the Commission’s *Statement of Policy and Order Concerning the Accounting and Ratemaking Treatment for Pensions and Postretirement*

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postretirement benefit obligation.

*Benefits Other Than Pensions*, (issued and effective September 7, 1993) (“the PSC Guidance”).

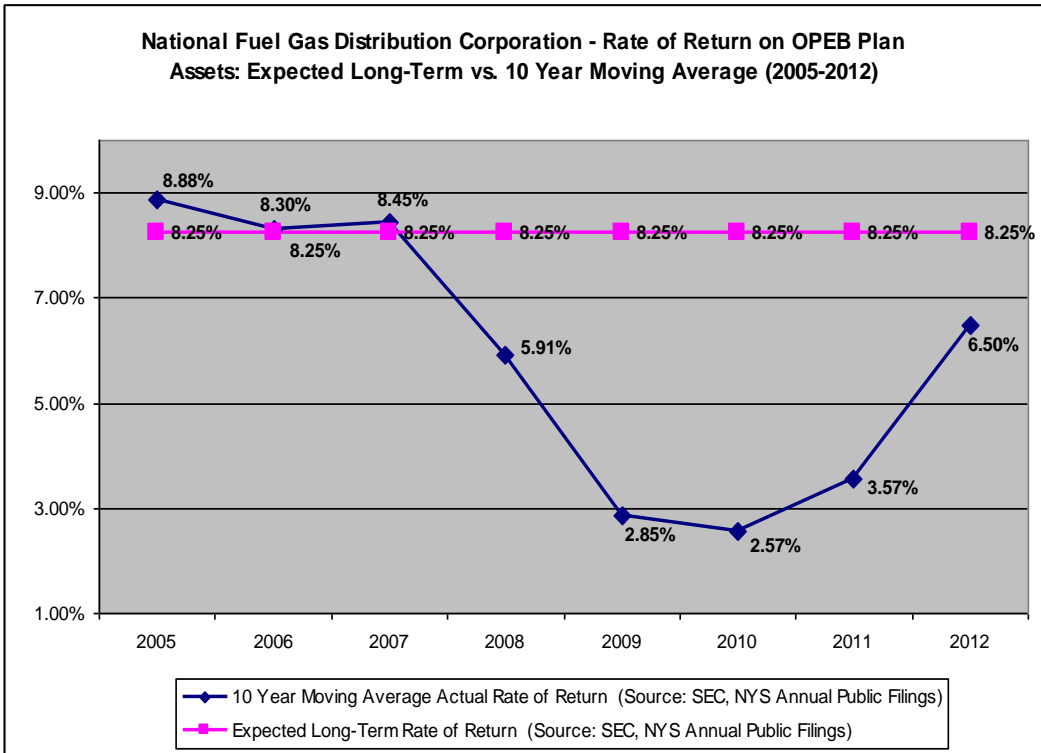
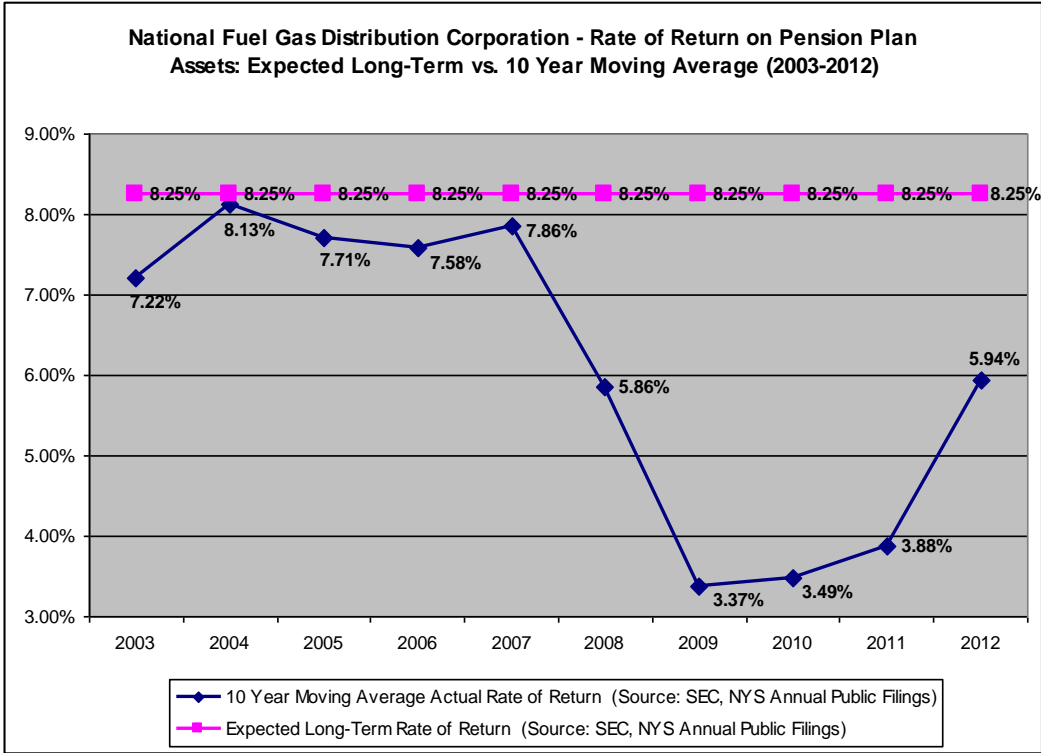
The PSC Guidance utilizes a two-step procedure, which we summarize as follows:

Step 1 - Under FAS 158 / ASC 715, differences between expected and actual plan returns are deferred and amortized on a straight-line basis over the future working period of current plan participants. However, the PSC Guidance requires that these deferrals be amortized on a ten-year “vintage year” basis. This method is acceptable under GAAP because it tends to result in a shorter amortization period.

Step 2 – FAS 158 / ASC 715 amortizations become a component of net periodic (actual) pension/OPEB expense. The PSC Guidance further requires that companies defer the difference between 1) the rate allowance for pension/OPEBs (in the case of pensions, less any rate allowance the company is directed to use for OPEB purposes), and 2) actual pension/OPEB expense. This effectively “re-defers” any excess of FAS 158 / ASC 715 amortization that causes actual pension/OPEB expense to exceed the rate allowance for pension.

**ii. The Company’s Assumed Rate Of Return On Plan Assets From 2003 To 2012 Was Unrealistic, And A Significant Cause Of The Growth In Pension/OPEB Plan Asset Loss Deferrals During This Period.**

National Fuel assumed in each year from 2003 to 2012 that its pension and OPEB plans would grow at the rate of 8.25%. The 8.25% rate, however, was unrealistically high for the pension plan throughout these years, as it was from 2008-12 for the OPEB plan. This resulted in excessive and unnecessarily high asset loss deferrals. The following charts compare the actual ten-year moving average growth of National Fuel’s pension and OPEB plan assets with the unrealistic assumed level of 8.25%:



If, instead of adhering to the unrealistic 8.25% pension and OPEB plan asset growth level, the annual expected rate of return were set at the moving average of actual returns over the prior ten

years (the same time period used for the PSC Guidance ten-year vintage amortization requirement), this would have reduced net pension and OPEB loss deferrals for the Company's New York division alone by at least \$73 million from 2003-12. See Exhibit 1 to this brief. PULP asserts that National Fuel's New York Division amortization (even before considering the rate allowance limitation) could have been \$7.3 million lower annually - likely eliminating most of the now-needed re-deferrals caused by the rate allowance limitation of net periodic pension/OPEB costs.

PULP notes that, beginning with the Company's fiscal year ended September 30, 2010, FAS 158 / ASC 715 required it to at least *consider* its prior returns on plan assets when setting the expected rate of return prospectively:

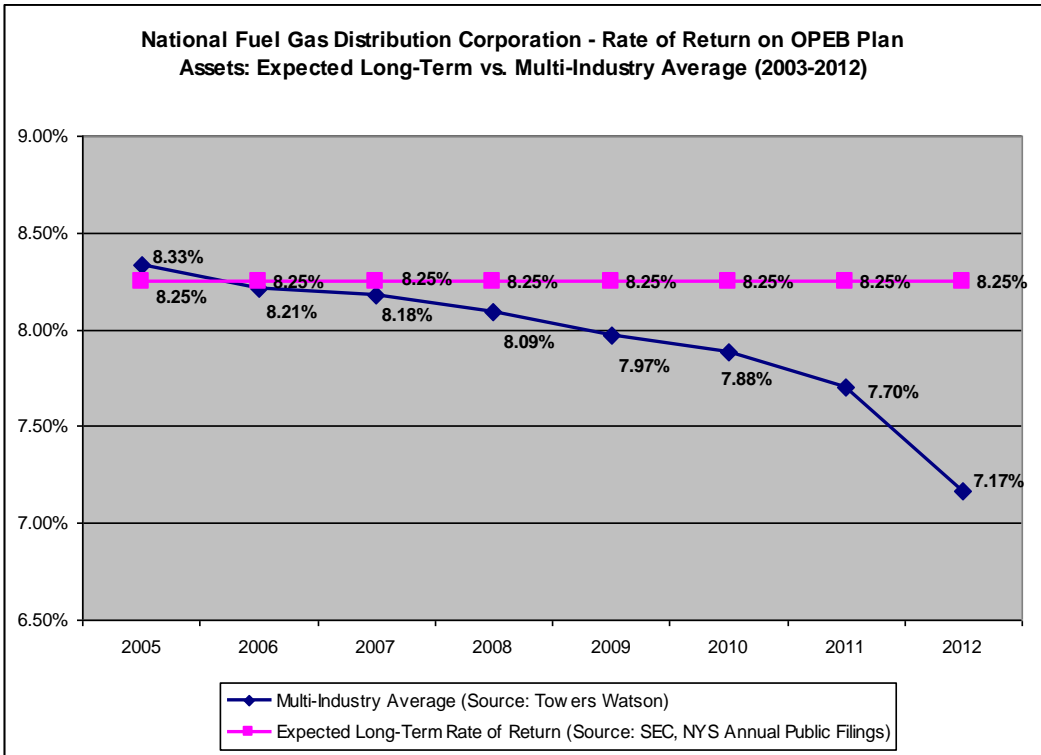
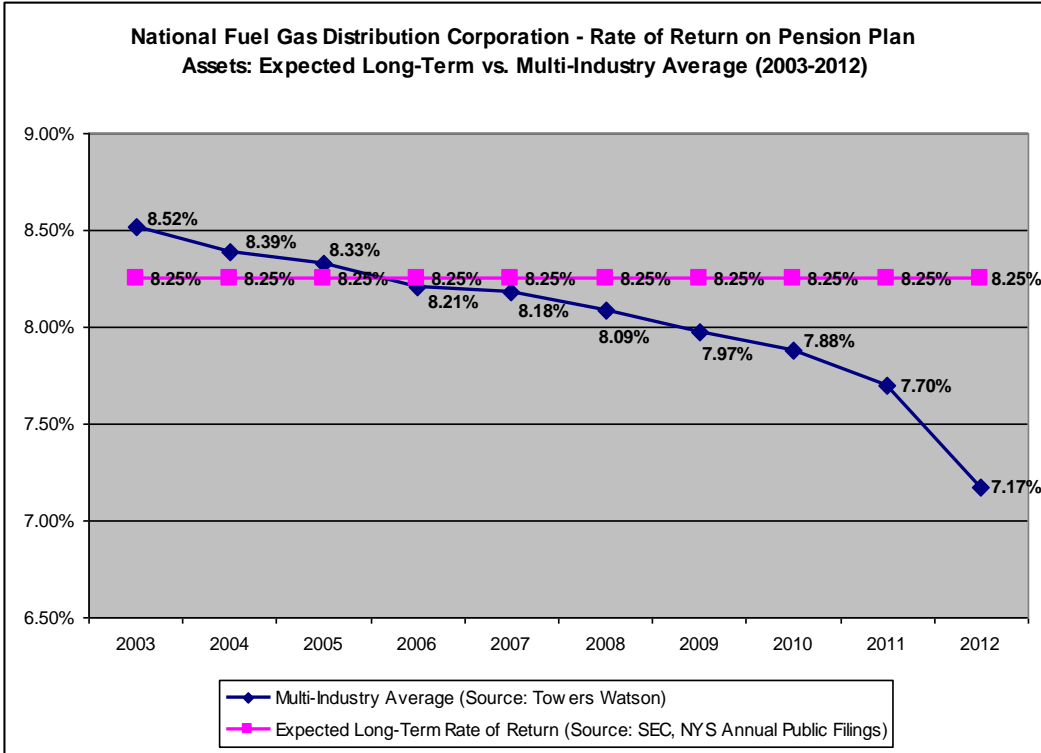
The expected long-term rate of return on plan assets shall reflect the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the projected benefit obligation. *In estimating that rate, appropriate consideration shall be given to the returns being earned by the plan assets in the fund and the rates of return expected to be available for reinvestment.\** The expected long-term rate of return on plan assets is used (with the market-related value of assets) to compute the expected return on assets. In the context of its use in this paragraph, funds to be invested refers only to the reinvestment of returns on existing plan assets.<sup>8</sup>

National Fuel, however, adhered to the unrealistic 8.25% growth assumption which worked to increase the divergence between actual and projected results required to be deferred.<sup>9</sup> In doing so, National Fuel was out of step with other companies that modified their pension and OPEB plan asset growth projections over the 2002 - 2012 period. The charts below illustrate that the relationship between the Company's expected rate of return on plan assets diverged from multi-industry averages during the periods 2003-2012 and 2008-12.

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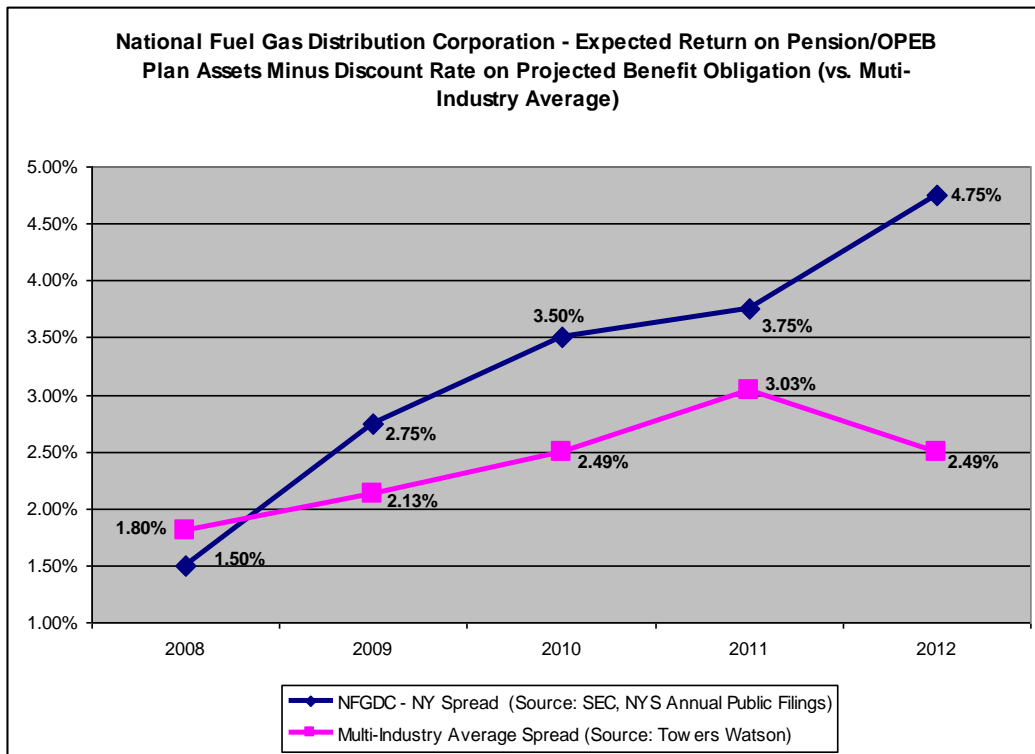
<sup>8</sup> FASB, ASC 715-35-47 (\* *Emphasis added*), available at <https://asc.fasb.org/link&sourceid=SL2308013-114930&objid=29635418>

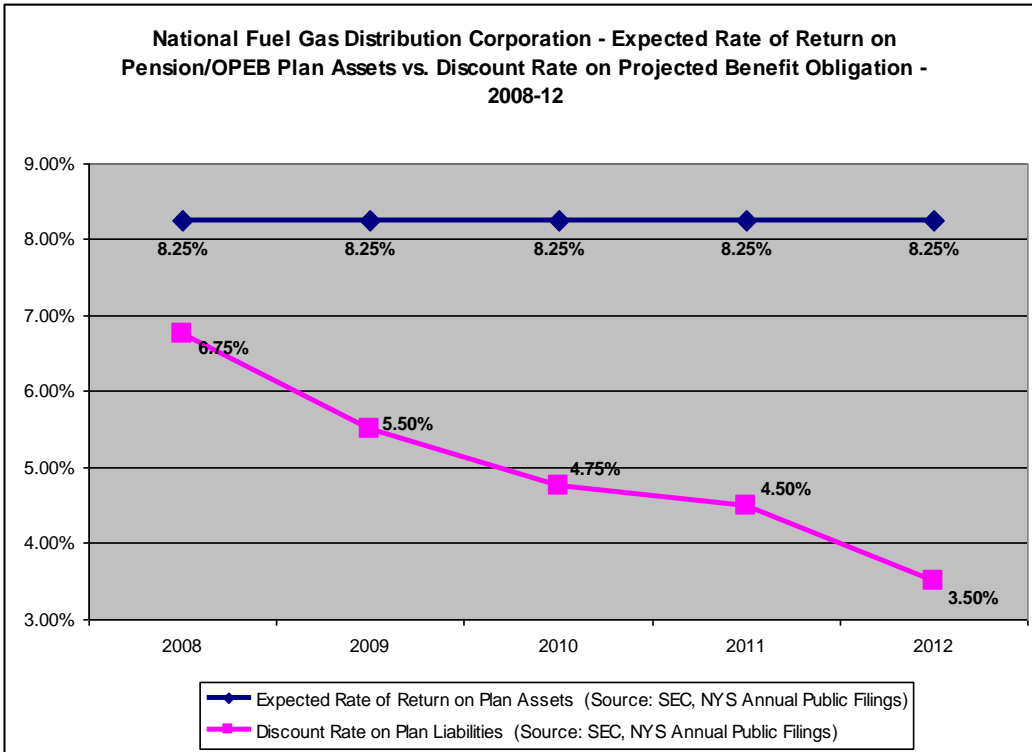
<sup>9</sup> The PSC Guidance does not appear to have been updated for the adoption of FAS 158, or its codification in ASC 715. Had the Guidance been updated for FAS 158 / ASC 715, the Company would have been required for ratemaking purposes to give consideration to the historic returns on its



pension and OPEB plans as it annually reviewed its expected long term rate of return.

Another major factor affecting the major buildup of pension and OPEB plan funding deficiencies is the discount rate used to project growth in future obligations to plan beneficiaries. Generally, changes in the expected rate of return on plan assets and discount rate on plan liabilities are positively correlated. As reported by Towers Watson, from 2003 to 2012, expected rates of return and discount rates declined from 8.52% to 7.17% and 6.17% to 4.00%, respectively; while from 2008-12, they dropped from 8.09% to 7.17% and 6.29% to 4.00%, respectively. With regard to changes in National Fuel’s expected rate of return and discount rates, however, there is no correlation between the assumed return on plan assets and the discount rate selected, a condition that becomes particularly evident in 2012. These anomalies are illustrated in the charts below:





As illustrated by the above charts, since 2008, the spread between National Fuel’s expected return on plan assets and its discount rate has increased to 4.75%, over 200 basis points more than the multi-industry average, clearly an anomalous condition unlikely to be sustained.

PULP notes that the non-cash return provided on the Company’s internal reserve for pension deferrals is based on National Fuel’s expected rate of return on pension assets and therefore would have been reduced by the difference between the reported expected rate of return and the ten-year average rate of return times the balance of the internal reserve for pension for each period that the ten-year average rate was used as an alternative. In 2012 alone this would have reduced the eventual pre-tax recovery of the non-cash return on the pension reserve by at least \$1.7 million.

PULP also notes that the Commission’s Guidance did not anticipate the exceptional circumstances of a national financial crisis such as that which occurred in 2008-9. The dual-

deferral mechanism (steps 1 and 2 described above) may not be capable of absorbing such large losses in so short period of time without raising the possibility that sizeable pension/OPEB losses may have to be deferred indefinitely. The FAS 158 / ASC 715 pension/OPEB deferral balance will likely still exceed \$300 million at September 30, 2013 (down from \$467 million at September 30, 2012). Thus, in contrast to FAS 158 / ASC 715 deferrals of \$36 million at September 30, 2007, the Company will be working to recover from a base *almost ten times greater*. While one might hope to achieve sufficient returns in the next 3-5 years that could have the chance of reducing deferrals to 2007 levels, based on historical experience, such an outcome seems unlikely. Further, during the next 3-5 years, historic FAS 158 / ASC 715 deferrals will continue to amortize into the rate-allowance "re-deferral" (step 2 of the PSC Guidance). Rates and other mechanisms will need to be set to incorporate those costs.

Dealing with these deferrals could become an acute priority for National Fuel and the Commission, perhaps displacing many other worthy ratemaking priorities. Indefinite deferrals would defeat the purpose of the Guidance policy of ten-year vintage amortization of pension/OPEB asset gains and losses. It could also lead to ad-hoc, inconsistent amortization decisions. If the first priority in rate proceedings becomes the amortization of legacy pension/OPEB deferrals, ratepayers would be harmed because new initiatives and even rate design policies may need to move to the back burner in order to deal with hold-over deferred losses.

Most, if not all, parties are likely to agree that it is in their interest to avoid unnecessary deferrals. PULP believes that excessive deferrals generated by inappropriate



asset growth and discount rate assumptions, coupled with insufficient funding, impose an unacceptable burden on low-income customers for two primary reasons:

1. Amortization of excess, unnecessary deferrals – if allowed in rates – would have the effect of increasing customer bills.
2. The need to amortize these deferrals eventually could displace other ratemaking priorities and initiatives. For example, improvement in programs for low-income customers, such as the Company's LICAAP program, or implementation of a broad-based, volumetric low-income reduced rate might be deemed to have too much impact on other customers to implement, if rates must rise in order to meet the priority of amortizing pension/OPEB deferrals.

With PSL § 66(20) refunds to recapture excess earnings reaped while the deferrals were built up, there may be more opportunity to implement important initiatives to improve affordability of service to low-income customers. Other parties may share, for their own reasons, the same concern about higher rates and the displacement of priorities that would be caused by the possible need to amortize excess pension/OPEB deferrals. As indicated above, some of the deferred losses subject to recovery from customers may have been excessive due to the methodologies used. In addition, as discussed below, funds received in excess of the allowed return could be used to reduce rates or mitigate pension and OPEB amortizations.

**C. While Deferrals for Future Recovery of Pension/OPEB Costs from Customers Grew, National Fuel Achieved ROEs above 9.1% with Cumulative Excess Earnings of \$24.0 Million, and Excess in Revenue Equivalent of \$39.2 Million**

National Fuel's authorized return was 9.1% when rates were last set in 2007. In the intervening years it realized earnings higher than the ROE intended by the Commission. In its May, 2013 prepared testimony, the DPS staff's temporary rate panel indicates that in Exhibit TRP-3 to its testimony it has calculated that:

if the Company's actual cost of equity for the twelve months ended September 30, 2012 was 9.0%, an amount that Staff calculates to be a reasonable return on equity authorization at this time, then National Fuel's current gas rates would be approximately \$17.3 million too high on an annual basis.

*Testimony of Staff Temporary Rates Panel, May 2013 (Case #13-G-0136) at 13.* Later in its testimony, staff justifies the use of 9.0% as a reasonable return on equity authorization on the basis that:

The Company's most recent reported return on equity is over 300 basis points higher than the return on equity of 9.10% that was allowed when National Fuel's rates were last established in 2007. Furthermore, it exceeds the cost of equity levels determined reasonable by the Commission in recent proceedings, most notably the authorized ROE, less an estimated stayout premium, established for Niagara Mohawk Power Corporation in Case 12-G-0202 in the Commission's order issued on March 15, 2013.

*Testimony of Staff Temporary Rates Panel, May 2013 (Case #13-G-0136) at 21.*

PULP concurs with the reasonableness of staff's use of a 9.00% return on equity authorization, as well as its calculation of \$10.5 million potential equity earnings above 9.00%, and \$17.3 million excess in revenue equivalent for the historic fiscal year ended September 30, 2012 in TRP-3.

Using staff's methodology in TRP-3 used for 2012, PULP has also calculated the potential equity earnings above 9.10% and excess in revenue equivalent for fiscal years 2010 and 2011, drawing upon the adjusted return on equity calculations used by staff in Exhibit TRP-2 of its temporary rate panel testimony. By PULP's calculation, the potential equity earnings over 9.10% were \$6.5 million and \$7.0 million in 2010 and 2011, respectively; and the excess in revenue equivalent was \$10.8 million and \$11.6 million. PULP believes that staff's methodology for calculating equity over earnings and excess in revenue equivalent is the correct one, and therefore asserts that National Fuel's over earnings from 2010 – 2012 equaled \$24.0 million, with an excess in revenue equivalent \$39.2 million.

In sum, National Fuel has earned significantly more than the return contemplated when rates were set, while increasing dramatically the liabilities in deferral accounts to be paid in the future by customers. These circumstances cry out for correction, to rebalance what up to now has been a one-sided result under the 2007 rate plan. PSL § 66(20) is the right tool to use to ameliorate the situation.

**D. The Commission has Discretion to Use § 66(20) to Refund Earnings Above the Level Authorized in the Rate Plan, and its Use is Appropriate in this Case.**

Given the extraordinary circumstances, where National Fuel received excess earnings even as deferred customer liabilities for pension costs mushroomed, the Commission should use PSL § 66(20) refunds to reduce customer rate burdens. National Fuel argues that the

Commission's "explicit policy goals" will be frustrated if it requires disgorgement of excess earnings. National Fuel, however, cites no official or explicit policy or goal contained in any Commission rule or policy statement which confers any legitimate expectation that the Company will be allowed to earn \$39 million more than the authorized level while recording deferrals of large amounts to be paid later by customers. Rather, it is an "explicit policy goal" of the legislature to empower the Commission to require refunds for the benefit of customers in appropriate cases when a gas or electric utility has excess earnings.

That the Commission has statutory power to act, of course, does not require it to act in every situation where a utility earns more than the return authorized in its last rate plan. The statute does not say that the Commission "shall" require refunds when it learns a gas or electric utility has earned more than the authorized rate of return. On the other hand, the fact that the §66(20) refund tool is rarely unsheathed does not mean that the Commission cannot wield it. Indeed, other sections of Section 66 of the Public Service law are replete with numerous powers of the Commission that are rarely invoked or exercised, as the Commission flexibly draws upon its vast and varied powers and employs different methods to achieve the statutory goal that all rates be just and reasonable.

National Fuel cites discussions about "regulatory lag" contained in the Commission's Order Setting Temporary Rates<sup>10</sup> and in a more than two decade old opinion in a telecom case. These discussions point out that in a period after rates are fixed a utility has the incentive to cut costs below those projected when rates were set, because it will ordinarily keep the cost savings during the "lag" period until the next rate review. National Fuel argues

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<sup>10</sup> CASE 13-G-0136 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of National Fuel Gas Distribution Corporation for Gas Service. ORDER SETTING TEMPORARY RATES, (Issued and Effective June 14, 2013) at 8.

that its incentives to cut costs or grow revenues will be diminished if § 66(20) is used to require refunds of all earnings above the return authorized by the Commission when it set rates. But § 66(20) does not require this in every situation, it only gives the Commission power, in a proper case, to do it. Indeed, if the Commission were to use § 66(20) as National Fuel fears, it would never have approved sharing plans where utilities keep part of any earnings in excess of the authorized return. Why would anyone agree for the utility to share earnings above an allowed return if customers could get it all from the Commission as refunds under § 66(20)? But in fact such agreements are regularly made and regularly approved, and in some instances the shared over earnings are explicitly targeted to reduce deferrals. There will be no injustice in this case if the Commission uses its refund power under § 66(20) to accomplish similar ends.

**E. National Fuel’s Effort to Limit the § 66(20) Refund Period Should be Rejected.**

National Fuel argues in the alternative that if § 66(20) applies and a refund of over earnings is required, the refund should be limited to just a refund of one year’s over earnings. But there is no such limit in the statute. The refund power is triggered when a gas or electric utility has excess earnings for a twelve month period. It clearly is not triggered by high earnings over a shorter period. For example, the Commission could not initiate a refund proceeding based on a single quarterly earnings report, no matter how high the excess earnings.

The law does not limit the time in which a refund proceeding may be commenced. It simply provides that the “commission may initiate a proceeding with respect to such a refund *after* the conclusion of any such twelve month period.” *PSI § 66(20)*. Thus, the commission

in 2013 can initiate a refund proceeding for the twelve month period in 2012. Equally clearly, this proceeding can seek refunds for overearnings in the twelve month period in 2011, etc., because it is commenced “after the conclusion” of 2011. PULP recommends that in this case, where there has been a buildup over several years of very large deferrals, the look-back period should reach at least to 2010.

## CONCLUSION

National Fuel's arguments that PSL § 66(20) does not give the Commission power to grant refunds, and that the Commission should not exercise that power in this case should be rejected. The statute plainly gives the Commission power to order refunds of excess earnings for any twelve month period. PULP has shown that while the company received earnings in excess of its allowed return, there was a buildup of major new liabilities for pension and OPEB expense, \$73 million of which could have been avoided if reasonable asset growth projections had been used. PULP asserts that National Fuel's over earnings from 2010 – 2012 equaled \$24.0 million, with an excess in revenue equivalent \$39.2 million. Under these unusual circumstances, it is just and reasonable for the Commission to correct these anomalies by requiring refunds of excess earnings since at least 2010 for the benefit of customers under PSL § 66(20).

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Respectfully submitted,



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Public Utility Law Project of New York, Inc. - Case #13-G-0136, Exhibit 1  
National Fuel Gas Distribution Corp. (New York Division) Pension/OPEB Asset Gain/Loss Deferrals and Amortization - 2003-11  
Reported Expected Rate of Return vs. 10 Year Moving Average Actual Return

**Pension**

**Deferrals and Amortization \*\*\***

Plan Year	Expected Rate of Return	Actual Return Years**		+/- Expected Rate	At Reported Expected Rate of Return		At Actual 10 Moving Average Rate of Return		Difference	
					Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization
2002	8.50%	N/A	1993-2002	N/A	N/A	N/A	N/A	N/A	N/A	N/A
2003	8.25%	N/A	1994-2003	N/A	N/A	N/A	N/A	N/A	N/A	N/A
2004	8.25%	8.13%	1995-2004	-0.12%	20,199	-2,020	27,867	-2,787	7,668	-767
2005	8.25%	7.71%	1996-2005	-0.54%	3,994	-399	7,712	-771	3,719	-372
2006	8.25%	7.58%	1997-2006	-0.67%	11,224	-1,122	15,081	-1,508	3,857	-386
2007	8.25%	7.86%	1998-2007	-0.39%	41,056	-4,106	44,630	-4,463	3,574	-357
2008	8.25%	5.86%	1999-2008	-2.39%	-58,318	5,832	-55,825	5,583	2,493	-249
2009	8.25%	3.37%	2000-2009	-4.88%	-91,590	9,159	-83,380	8,338	8,210	-821
2010	8.25%	5.86%	2001-2010	-2.39%	6,197	-620	22,524	-2,252	16,327	-1,633
2011	8.25%	3.88%	2002-2011	-4.37%	-28,716	2,872	-13,642	1,364	15,074	-1,507
Total (2004-11)					-95,955	9,595	-35,032	3,503	60,923	-6,092

\* Based on 10 year moving average.

\*\* Moving average rate determined at end of each 10 year period is applied as Expected Rate of Return for the following year For example, the moving average rate for the 2002-11 period of 3.88% is used for 2012.

\*\*\* Deferrals and amortizations are for GAAP only. GAAP amortizations are included in net periodic pension expense, which is limited by a second deferral based on the rate allowance for pension/OPEB.

2012 Rate To Use For Calculation Of 'Expected Return on Plan Assets' And 'Amortization of Actuarial Gains/Losses' Components of Net Periodic Pension Expense (Actual Cost)	
<b>8.25%</b>	<b>3.88%</b>



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**OPEB**

**Deferrals and Amortization \*\*\***

Plan Year	Expected Rate of Return	Actual Return Years**		+/- Expected Rate	At Reported Expected Rate of Return		At Actual 10 Moving Average Rate of Return		Difference	
					Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization
2002	8.50%	N/A	1993-2002	N/A	N/A	N/A	N/A	N/A	N/A	N/A
2003	8.25%	N/A	1994-2003	N/A	N/A	N/A	N/A	N/A	N/A	N/A
2004	8.25%	7.75%	1995-2004	-0.50%	14,437	-1,444	14,936	-1,494	498	-50
2005	8.25%	9.57%	1996-2005	1.32%	1,029	-103	-833	83	-1,862	186
2006	8.25%	8.88%	1997-2006	0.63%	7,490	-749	6,399	-640	-1,091	109
2007	8.25%	8.30%	1998-2007	0.05%	23,155	-2,316	23,122	-2,312	-33	3
2008	8.25%	8.45%	1999-2008	0.20%	-54,661	5,466	-54,791	5,479	-130	13
2009	8.25%	5.91%	2000-2009	-2.34%	-57,711	5,771	-58,193	5,819	-481	48
2010	8.25%	2.85%	2001-2010	-5.40%	1,821	-182	6,432	-643	4,611	-461
2011	8.25%	2.57%	2002-2011	-5.68%	-18,510	1,851	-7,173	717	11,338	-1,134
Total (2004-11)					-82,950	8,295	-70,101	7,010	12,849	-1,285

\* Based on 10 year moving average.

\*\* Moving average rate determined at end of each 10 year period is applied as Expected Rate of Return for the following year For example, the moving average rate for the 2002-11 period of 2.57% is used for 2012.

\*\*\* Deferrals and amortizations are for GAAP only. GAAP amortizations are included in net periodic OPEB expense, which is limited by a second deferral based on the rate allowance for pension/OPEB.

2012 Rate To Use For Calculation Of 'Expected Return on Plan Assets' And 'Amortization of Actuarial Gains/Losses' Components of Net Periodic OPEB Expense (Actual Cost)	
<b>8.25%</b>	<b>2.57%</b>

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 National Fuel Gas Distribution Corp. (New York Division) Pension/OPEB Asset Gain/Loss Deferrals and Amortization - 2003-11  
 Reported Expected Rate of Return vs. 10 Year Moving Average Actual Return

**Pension & OPEB**

**Deferrals and Amortization \*\*\***

	At Reported Expected Rate of Return		At Actual 10 Moving Average Rate of Return		Difference	
	Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization	Deferral Amount	10 Yr. Vintage Amortization
Grand Total - Pension and OPEB (2004-11)	-178,904	17,890	-105,133	10,513	73,772	-7,377