



STATE OF RHODE ISLAND

Public Utilities Commission

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Chairman Ronald T. Gerwatowski
Commissioner Abigail Anthony
Commissioner John C. Revens, Jr.

MEMORANDUM

To: Legal Counsel to the Parties in Docket Nos. 22-53-EL and 22-54-EL
From: Cynthia Wilson-Frias, Esq. and Patricia S. Lucarelli, Esq.
Date: March 10, 2023
Re: PUC Docket Nos. 22-53-EL Proposed FY 2024 Electric Infrastructure Safety and Reliability Plan and 22-54-NG Proposed FY 2024 Gas Infrastructure Safety and Reliability Plan

At the Electric ISR hearing (Docket No. 22-53-EL) on March 9, 2023 the Chairman requested the parties file briefs addressing certain legal issues relating to the interpretation of the statutory provisions in Rhode Island General Laws which established the regulatory process for the Infrastructure, Safety and Reliability program (ISR) for both Rhode Island Energy's electric and gas distribution businesses.¹ The legal question at issue implicates the rate recovery provisions of the applicable statutory provisions. Specifically, if there are capital projects and associated expenses occurring in a given ISR fiscal year that were not approved by the Commission in the ISR filing pertaining to the that ISR fiscal year affect, to what extent does the absence of pre-approval affect the right and/or timing of recovery of the associated revenue requirement in the ISR-related rates?

The Chairman informally summarized the issues on the record, indicating that the issues for briefing would be communicated to the parties in a clearer and more precise manner to provide guidance for the parties in briefing. The purpose of this memorandum is to provide such guidance.

Because the legal issue is directly relevant to both the Electric ISR Docket No. 22-53-EL and the Gas ISR Docket No. 22-54-NG, **the Commission is requesting that the briefs be filed in both dockets on or before 4:00 p.m. March 23, 2023.**²

The Relevant ISR Statutory Provision

The relevant provision of Rhode Island law pertaining to the ISR issue appears in R.I. General Laws § 39-1-27.7-1(c). The chapter in which it appears requires the utility to file certain proposals with the Commission which are specified in paragraph (c). The second of the two proposals relates to the ISR. The paragraph states in pertinent part:

¹ R.I. Gen. Laws § 39-1-27.7.1

² The parties in both the electric and gas ISR proceeding are identical: Rhode Island Energy, the Division of Public Utilities and Carriers, the Attorney General, and the Office of Energy Resources.

(c) The proposals shall contain the following features and components:

- (1) [a “revenue decoupling” mechanism not relevant to the ISR]; and
- (2) An annual infrastructure, safety, and reliability spending plan for each fiscal year and an annual rate-reconciliation mechanism that includes a reconcilable allowance for the anticipated capital investments and other spending pursuant to the annual pre-approved budget as developed in accordance with subsection (d) of this section. (emphasis added)

Ratemaking Background

As noted above, the question arises as to what happens when a capital project or program for which cost recovery is later sought is implemented by the Company without the requisite pre-approval. In the absence of an ISR, traditional ratemaking principles would require the utility to wait until the next distribution rate case to commence recovery of the revenue requirement for a given capital project. Between the time when the project is placed in service and when new distribution rates from the rate case go into effect, the utility would experience what is referred to as “regulatory lag” in recovery. This meant that for each year prior to new rates going into effect, the revenue requirement associated with the capital project would not be recovered from ratepayers and would be absorbed in expenses by the utility. However, once the project was placed into rate base, prospective recovery of the revenue requirement would commence (with the utility having lost the opportunity for recovery of any revenue requirement for the time prior to the rate case decision).

Further, there is a long-standing principle that prohibits retroactive ratemaking. “The central principle is that ratemaking must be prospective and, although subject to narrow exceptions, the PUC may not engage in retroactive ratemaking that results in future payments for past expenses.”³ The Commission has approved many tariff provisions for the utility which allow the reconciliation of specifically defined eligible costs against revenues collected in rates that relate to expenses that occur prior to approval of the rate recovery.⁴ The approval of such a reconciliation tariff provision avoids the application of the prohibition. However, in the absence of a statute or specific tariff provision that allows the recovery retroactively through a pre-approved reconciliation tariff, the prohibition against retroactive ratemaking stands.

The ISR provisions in the law were intended to limit or eliminate regulatory lag for certain capital projects that relate to safety and reliability, as expressed in statute. To comply with the statute, tariff provisions were approved for both the electric and gas ISRs consistent with the statute that contemplates a reconciliation of expenses against revenue for the applicable fiscal year. However, those tariff provisions arise out of the expressed statutory requirements which specify how it is to be implemented, as stated in paragraph (c) quoted above. It was not a policymaking decision of the Commission.

³ *In Re Providence Water Supply Board’s Application to Change Rate Schedules*, 989 A.2d 110, 115 (R.I. 2010).

⁴ Typically, when the reconciliation of prior costs is not statutory, the costs are those outside of the utility’s reasonable control. For example, the Rhode Island Supreme Court has found there may be exceptions to the prohibition when the utility is faced with extraordinary expenses flowing from unexpected events (i.e., ice storm or supplemental tax increase during the rate year). See *Narragansett Electric Company v. Burke*, 415 A.2d 177 (R.I. 1980). For example, this is the basis for the pension related reconciliation factors.

Legal Questions to Be Addressed

In both the pending electric and gas ISR dockets, the Company has identified certain projects or investments that were not expressly approved in the ISR filing for the relevant fiscal year and indicated an expectation that the Company would be able to utilize the ISR reconciliation to recover the revenue requirement retroactively for projects going into service during the fiscal year. This has given rise to the legal questions raised in this memorandum which are set forth below, along with some simplifying assumptions.

Simplifying Assumptions

In order to simplify the briefing of these legal issues, please make the following assumptions. (These assumptions are not to be construed as necessarily being applicable to the projects at issue. They are only being given to facilitate exploration of the legal issue.)

- (a) The capital investment was not included in the initial ISR filing for the applicable year and, therefore, was never pre-approved;
- (b) The capital investment decision was made after the ISR plan was approved;
- (c) The capital investment was made during the fiscal year to which the initial ISR filing applied;
- (d) The capital project relating to the investment was placed in service during that fiscal year;
- (e) The capital investment was prudent and addressed safety and reliability (and no party disputes the reasonableness of the investment); and
- (f) The capital investment would have been approved by the Commission if it had been timely included in the initial ISR filing for the applicable fiscal year.

Questions to Be Briefed

- (1) If a capital investment is made in a project during a given fiscal year which was not approved by the Commission in the relevant ISR filing pertaining to that same fiscal year, is the utility entitled to or prohibited from recovering the first fiscal year revenue requirement for such investment through the reconciliation, or must the utility experience regulatory lag for at least the first year's revenue requirement recovery?
- (2) Is the utility entitled to obtain recovery in the subsequent fiscal year ISR filing for the prospective revenue requirement for such project which was implemented in the prior fiscal year if it is disclosed and included in the spending plan, or does the utility have to experience regulatory lag until the next distribution rate case before seeking recovery of any prospective revenue requirement because it was never pre-approved in an ISR plan filing?
- (3) Does the Commission have the discretion (but not the obligation) to allow recovery of the revenue requirement prospectively or retroactively through the reconciliation if the Commission finds it reasonable to allow it?
- (4) Does the Commission have the discretion (but not the obligation) to allow recovery of the revenue requirement prospectively or retroactively through the approval of an ISR spending plan in the following fiscal year if the Commission finds it reasonable to allow it?