Senate Energy & Telecomm.Comm.
Exhibit No. 2
Date 2.10.05
Bill No. SB 321

Memorandum

To: Energy & Telecommunications Committees

From: Commissioner Tom Schneider, PSC

Date: February 10, 2005

Re: **SB 321 PSC Authority to Order Utilities to File Periodic Rate Case**

The Montana Public Service commission unanimously supports SB 321 and an amendment to exclude "rural telecommunications" utilities from the provisions of this section.

Background

Historically, the PSC asserted the implicit authority under its general supervisory powers to require regulated public utilities to file financial information consistent with minimum rate case filing requirements. (38.5.101 et sec & 38.5.2801 et sec).

In recent cases where the Montana PSC asserted its authority to require utilities to file such financial rate case, the utility concerned challenged the assertion as being without clear statutory authority. Clarification of the PSC's authority over these fundamental financial rate case filing requirements is advisable and necessary to avoid future disputes and litigation regarding PSC authority. PSC review under clear statutory authority will streamline the process and assure ongoing ability to assure just and reasonable utility rates.

The current arrangement produces substantial uncertainty about authority to require the essential financial data necessary to assure that the level of existing rates continues to be just and reasonable. The uncertainty produces weaker results for all concerned. A recent example illustrates the ongoing lack of symmetry and unacceptable imbalance accruing to the likely benefit of utilities in the form of excessive earnings under the utilities' legal position on lack of PSC authority. Qwest has not had a comprehensive rate case or revenue requirement case since 1990. The allowed rate of return in the 1990 commission Order was 10.44 %. In its 2001 Annual Report to the PSC, Qwest provided a Montana intrastate rate of return on rate base of 21% or nearly 2 times the last allowed return. The PSC ordered Qwest to confirm and update its Montana earnings level via a minimum rate case filing. Qwest objected and challenged the PSC's authority to Order such financial filing. Qwest's legal position further argued that the only way the PSC or others, including the Montana Consumer Counsel, can investigate or challenge existing rate levels (approved in 1990) is to file a Complaint and carry the "burden of proof". A recent District Court opinion substantially affirmed Qwest's position. The PSC has appealed that decision to the Montana Supreme Court.

Such a standard shifts the burden and responsibility away from the beneficiary of the likely excess profits and the entity with the underlying financial data and regulatory/financial reporting capability to the state agencies. *It is a practical impossibility for entities(PSC, MCC) other than the subject utilities to perform a comprehensive rate case review and burden of proof for major utilities—the utilities themselves have argued that it takes them about six months to prepare a general rate case, and they have all the underlying information, technical and legal resources as well as financial incentive.* **That result is simply not acceptable.**

Utility ratepayers **must** be assured that rate levels can be periodically re-examined by the MCC and PSC to determine whether they are just and reasonable. The asymmetry is readily demonstrated. Utilities which do not earn adequate returns are free to file a rate case to increase rates at their convenience. In fact during the inflationary period from the late 70's – mid 80's utilities filed regular rate increase cases to cover rising costs and achieve increased returns. The PSC was continuously criticized by utilities and even the legislature for regulatory lag in processing such cases, for using historic test years, for not allowing CWIP in rate base, etc., etc. Special ratemaking procedures (trackers, rapid interim rates and shortened periods for PSC decisions) were adopted to accommodate the financial concerns of utilities.

Since the mid-late 80's when the last rate cases for both Qwest and MDU occurred, inflation rates have been relatively moderate and productivity increase related to technology have certainly offset or mitigated cost increase. Furthermore customer growth, expanded products, increased consumption/sales likely flowed to increased earnings. It is essential that clear authority exist to require ongoing review and periodic re-examination and resetting of rate levels. Surely, sound public policy and regulatory oversight would not allow this unbalanced rate regime to continue. While there may be reasonable arguments (1) against expensive, frequent reviews and (2) certain regulatory lags provide some "upside potential" for increased earning through productivity improvements, capital investment, innovation and cost control—it is unreasonable that shareholders are the sole beneficiaries on a permanent basis. **Periodic cost and rate reviews are essential to assure both credibility and a sound regulatory basis for rates--fundamental equity requires no less.**

Proposed statutory authority

Establish specific PSC authority to require utilities to make a general rate case filing, including comprehensive financial information consistent with minimum rate case filing requirement rules, if a utility had not done so five (5) years from the service date of the last PSC general rate case or revenue requirements Order. SB 321 effectively provides the essential authority to address the existing vacuum.