

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of the East)
Ohio Gas Company d/b/a Dominion)
Energy Ohio for Approval of An) Case No. 20-1634-GA-ALT
Alternative Form of Regulation to)
Continue Its Pipeline Infrastructure)
Replacement Program.)

**INITIAL BRIEF FOR CONSUMER PROTECTION
BY
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I. INTRODUCTION

The PUCO¹ should protect consumers by rejecting or modifying the Stipulation and Recommendation (“Settlement”) filed by Dominion Energy Ohio (“Dominion” or “Utility”) on October 12, 2021 regarding Dominion’s Pipeline Infrastructure Replacement Rider (“PIR charge”).² It is unjust and unreasonable to force Dominion’s 1.1 million residential consumers to pay the 13-year-old and excessive 9.91% pre-tax rate of return included in the Settlement.³ The stale rate of return will result in Dominion earning profits that are too high for current financial market conditions and allow the Utility to collect a cost of debt from customers that is nearly three times its actual cost of debt.

Dominion seeks to continue its pipeline infrastructure replacement program and charge for collecting costs from consumers, filing an application for an alternative rate plan. The statutes governing alternative rate plans provide that the PUCO shall approve a program filed under the

¹ Public Utilities Commission of Ohio.

² *In the Matter of The East Ohio Gas Company d/b/a Dominion Energy Ohio for Approval of an Alternative Form of Regulation*, Case No. 20-1634-GA-ALT, Stipulation and Recommendation (October 12, 2021).

³ Direct Testimony of Daniel J. Duann, Ph.D. on Behalf of the Ohio Consumers’ Counsel at 4 (October 25, 2021) (“Duann Direct”).

plan only if it finds the program to be *just and reasonable*.⁴ Using Dominion's inflated and outdated rate of return (for profits and debt), as proposed in the Settlement, harms consumers by making them pay too much, a result that is neither just nor reasonable. The PUCO should protect residential consumers by rejecting or modifying the Settlement as recommended by OCC.⁵

II. RECOMMENDATIONS

The Settlement does not pass the PUCO's three-part test for settlements. Under the three-prong test, the PUCO considers: (1) whether the settlement is the product of serious bargaining among capable, knowledgeable parties representing a diversity of interests; (2) whether the settlement, as a package, benefits consumers and the public interest; and (3) whether the settlement package violates any important regulatory principle or practice.⁶ If the PUCO determines that a proposed settlement does not meet each of the three criteria outlined above, the settlement should be rejected.

This Settlement should be rejected under the three-prong test. The Settlement lacks diversity of interest as there is no signatory party that represents the interests of residential customers who will pay the PIR charge. The Settlement also does not benefit consumers or the public interest. And it violates established regulatory principles and state policies. For these reasons, OCC opposes the Settlement.

The PUCO should modify the Settlement and adopt a lower and more reasonable pre-tax rate of return of 7.20%.⁷ By adopting this lower pre-tax rate of return, consumers will be

⁴ R.C. 4929.05(A)(3) (emphasis added).

⁵ Duann Direct at 4.

⁶ *Consumers' Counsel v. Pub.Util. Comm.*, 64 Ohio St.3d 123,126, 592 N.E.2d 1370 (1992); *AK Steel Corp. v. Pub.Util. Comm.*, 95 Ohio St.3d 81, 82-83, 765 N.E.2d 862 (2002).

⁷ Duann Direct at 11-12.

protected from paying unjust and unreasonable PIR charges, and Dominion will have the opportunity to earn a return (profits) comparable to that available of other similarly situated gas utilities.

A. The PUCO should reject the Settlement given the lack of diversity of those who signed it and given that OCC, the statutory representative of Ohio’s residential consumers, opposes it.

In considering the first prong of the PUCO’s three-part test for settlements, the PUCO has at times considered the diversity of the signatory parties. Diversity is not required, and no single party can veto a settlement, but “the diversity of the signatory parties may be a consideration in determining whether a settlement is a product of serious bargaining among capable, knowledgeable parties under the first prong of the Commission’s test.”⁸

The Settlement was signed by Dominion, PUCO Staff, Industrial Energy Users-Ohio and Ohio Partners for Affordable Energy. However, OCC, the statutory representative of Ohio’s residential consumers,⁹ opposes the Settlement. No other signatory party truly represents residential customers, who will be forced to pay the rates others agreed to. Oftentimes, the signatory parties to a settlement are predominantly the utility and other parties who do not pay for the costs proposed in the settlement, while the representative for all residential consumers—whose constituents pay the costs proposed in the settlement—is on the outside. This matters. When the representatives of those who bear the costs of a settlement oppose the settlement, the PUCO should give those representatives’ views substantial weight in considering whether the

⁸ *In re Application of Ohio Edison Co., the Cleveland Elec. Illuminating Co., & the Toledo Edison Co. for Approval of their Energy Efficiency & Peak Demand Reduction Program Portfolio Plans*, Case No. 16-743-EL-POR, Opinion & Order ¶ 61 (November 21, 2017).

⁹ R.C. Chapter 4911.

settlement in fact benefits customers and the public interest, whether the settlement is consistent with regulatory principles, and whether the settlement was the product of serious bargaining.

The PUCO should give substantial consideration to OCC's opposition to it and conclude that it fails the first prong due to lack of diversity.

B. To protect consumers, the PUCO should reject or modify the Settlement because using Dominion's outdated and inflated rate of return harms consumers and is not in the public interest.

1. The Settlement, by requiring consumers to pay a pre-tax rate of return of 9.91%, results in too high profits for Dominion, and will substantially harm consumers and the public interest.

The Settlement fails the second prong because requiring consumers to pay a too-high pre-tax rate of return of 9.91% substantially harms consumers and is not in the public interest.

Dominion wants consumers to continue pay an unjust and unreasonable pre-tax rate of return of 9.91% that was set in a rate case 13 years ago and does not include major changes to tax law.

The stale rate of return proposed in the Settlement will result in Dominion earning profits that are too high for current financial market conditions and allow the Utility to collect a cost of debt from customers that is nearly three times its actual cost of debt.

Dominion proposes to use a pre-tax rate of return of 9.91% in calculating the PIR charge revenue requirement that consumers would pay. The proposed Settlement uses the same pre-tax rate proposed in Dominion's PIR Application. This pre-tax rate of return reflects the gross-up of current federal income tax rate (21%) and the rate of return components (a cost of equity of 10.38%, a cost of debt of 6.50%, and capital structure of 48.66% debt and 51.34% equity) from its last rate case *decided in 2008* in Case No. 07-829-GA-AIR et al.¹⁰

¹⁰ Duann Direct at 6.

The issue in this case is not just if Dominion should or should not continue the PIR program. The more important issue is how much PIR charges Dominion can reasonably collect from consumers. Dominion can (and most certainly would) continue the PIR program with either a 9.91% or a 7.20% pre-tax rate of return.¹¹ Dominion has provided no evidence that the PIR program will not be able to continue in the absence of a 9.91% pre-tax rate of return.

And as explained throughout the testimony of OCC witness, Daniel J. Duann, Ph.D., the 9.91% rate of return is unjust, unreasonable, and inflated.¹² And since the PIR program could continue with a reasonable return of 7.20%, there is absolutely no basis to conclude that the proposed Settlement (with a 9.91% pre-tax rate of return) will provide a benefit of continuing the PIR program.

The only benefit of the Settlement's stale and inflated pre-tax rate of return goes to Dominion, not to consumers. Among other things, as an alternative form of regulation, the PIR program accelerates the charges to consumers as compared to traditional regulation. The Settlement further harms consumers due to Dominion's excessive rate of return, at consumer expense, resulting in unreasonably high profits, and consumers paying a cost of debt well in excess of Dominion's actual debt costs.

There is no question that consumers in Dominion's service area will be harmed substantially by the excessively high and unreasonable pre-tax rate of return of 9.91% included in the Settlement.¹³ A precise calculation of the additional harms to consumers depends on the amount of PIR capital investments added by Dominion and other factors during the 2022 to 2027

¹¹ Duann Direct at 16.

¹² *Id.* at 6-12.

¹³ *Id.* at 15.

period. They are not known at this time.¹⁴ Nevertheless, given the even larger amount of capital investment associated with the PIR program, the harm to consumers from adopting the 9.91% pre-tax rate of return will likely be even greater than what OCC calculated for Dominion's CEP program (approximately \$18.6 million) in Case No. 21-619-GA-RDR.¹⁵ Simply put, an unreasonably high rate of return plus larger capital investment equals higher charges for customers and higher profits for Dominion.

2. The PUCO should reject the proposed pre-tax rate of return of 9.91% proposed by Dominion and instead adopt a pre-tax rate of return of 7.20% to protect consumers.

The 9.91% pre-tax rate of return proposed by Dominion is unreasonable for two reasons. First, it includes a 10.38 percent return on equity that is vastly inflated and will result in much higher than justified charges for consumers and undeserved and unreasonable profits for Dominion.¹⁶ Financial market conditions and the business and financial risks facing Dominion have improved significantly since 2008.¹⁷ And the authorized cost of equity for gas distribution companies nationwide has declined during the same period and is much lower than the 10.38% decided in Dominion's last rate case.¹⁸ Continued use of the 10.38% return on equity for the PIR Program is simply not supported by current market conditions or Dominion's risk. Second, Dominion's current cost of debt is merely 2.29%.¹⁹ That is only about one third of the 6.50% cost of debt the PUCO set for Dominion 13 years ago and that Dominion still wants to charge to consumers now.

¹⁴ *Id.*

¹⁵ *See*, PUCO Case No. 21-619-GA-RDR, Testimony of Daniel J. Duann, Ph.D. at 13 (September 14, 2021).

¹⁶ Case No. 20-1634, Duann Direct at 6-7.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

However, neither Dominion nor the PUCO Staff have provided any factual support for using a high cost of equity of 10.38% and a high cost of debt of 6.50% to charge to consumers.²⁰ Dominion and the PUCO Staff offered no testimony by a rate of return expert to support the use of an unreasonably high cost of equity of 10.38% and a high cost of debt of 6.50% in calculating the 9.91% pre-tax rate of return. The Dominion witness in this proceeding is not a rate of return expert and does not offer any opinion on whether the 9.91% pre-tax rate of return is reasonable or not. Dominion has proposed to charge an outdated rate of return and the PUCO Staff is accepting it without any explanation.

OCC is the only party in this proceeding to present any evidence regarding a reasonable rate of return based on current market condition and Dominion's own business and financial risks. Specifically, OCC's witness, Daniel J. Duann, Ph.D. has reviewed the current financial market conditions and the business and financial risks facing Dominion at this time. He concluded that a pre-tax rate of return of 7.20% (reflecting a cost of equity of 9.36%, a cost of debt of 2.29%, a capital structure of 48.66% debt and 51.34% equity, and a tax-gross-up factor of 1.2658) is reasonable and consistent with established regulatory principles and state policies.²¹ Dominion did not issue any additional long-term debt in 2021 and there are no significant changes in the financial markets or Dominion's risk profile to indicate the need for revision of Dominion's cost of equity and cost of long-term debt.²²

Using a 7.20% pre-tax rate of return, as recommended by OCC, would permit Dominion to continue its PIR program. The 7.20% pre-tax rate of return is reasonable and can provide sufficient profits and debt cost coverage to Dominion based on current market conditions and

²⁰ *Id.*

²¹ Duann Direct at 11-12.

²² *Id.* at 12.

Dominion’s current business and financial risks. Dominion would not encounter any difficulty in obtaining funding (both equity and debt) to make the PIR investments, collecting returns on deferrals, and covering operating expenses if the 7.20% pre-tax rate of return were adopted. Neither Dominion nor the PUCO Staff claimed that the PIR program cannot continue under a lower pre-tax rate of return of 7.20%), either.

3. The PUCO should not permit Dominion to add substantial new charges, that are unjust and unreasonable, to consumers’ bills given the challenging economic time experienced by many Ohioans.

As discussed by OCC witness, Dr. Daniel J. Duann, Dominion’s residential consumers are being asked to pay more – a lot more if the proposed Settlement is approved. Dominion’s current PIR Rider rate for residential consumers is \$14.98 per month (\$179.76 per year). And under the Settlement, residential consumers could be paying as much as \$20.27 per month (\$243.24 per year) for the PIR in 2025 by the time that new base distribution rates using an updated rate of return will take effect from the base rate case that Dominion has committed to file in October 2024.²³ This additional burden to consumers from using this outdated and inflated pre-tax rate of return is more alarming now with the very rapid rise in natural gas and other energy costs in recent months and potentially over an extended time into the future.²⁴ The Energy Information Administration recently warned:

“We expect that the nearly half of U.S. households that heat primarily with natural gas will spend 30% more than they spent last winter on average—50% more if the winter is 10% colder-than-average and 22% more if the winter is 10% warmer-than-average.” For the Midwest Region (where Ohio is located), the increase in natural gas expenditure is expected to be even higher at 48.6%, from \$551 to \$818. The unit price (\$/Mcf) of natural gas in the Midwest Region is forecasted to increase by 44.7% from \$7.80 to \$11.28.²⁵

²³ Duann Direct at 11.

²⁴ Duann Direct at 9.

²⁵ Duann Direct at 10.

The PUCO may have little control over the gas commodity prices as they are largely determined in the marketplace. But the PUCO does have the power (and responsibility) to set reasonable profits (authorized return on equity) and debt costs for Dominion's PIR program to protect consumers from paying unreasonable rates. The PUCO should redouble its efforts to lower the costs of gas services, including the PIR charge, to protect consumers, especially those at-risk population.²⁶

The PUCO should reject or modify the Settlement to implement Dr. Duann's recommended rate of return of 7.20% to protect consumers.

C. To protect consumers, the PUCO should reject or modify the Settlement because using an outdated and inflated rate of return violates important regulatory and state principles and practices.

1. Using an outdated and inflated pre-tax rate of return will increase the revenue requirement for the CEP program and lead to rates that are unjust and unreasonable (and too high) for consumers, which violates important regulatory principles.

The Settlement fails the third prong because using an outdated and inflated pre-tax rate of return increases the revenue requirement for the CEP program and leads to rates that are unjust and unreasonable for consumers, violating important regulatory principles and state policies. The regulatory principles used in setting a reasonable rate of return for regulated utilities, including the cost of equity ("return on equity" or "allowed profits") and cost of debt, are well-established.²⁷ The fundamental regulatory principles regarding rate of return are best exemplified in the case of *Bluefield Water Works v. Public Service Comm'n*, 262 U.S. 679 (1923). In that case, the U.S Supreme Court ruled that:

²⁶ *Id.*

²⁷ Duann Direct at 18-19.

A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economic management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.²⁸

Accordingly, for the purpose of this proceeding, the returns on the net rate base (net plant investment and deferrals) included in PIR charges should be commensurate with the current business and financial risks facing Dominion and current financial market conditions. But the pre-tax rate of return included in the Settlement is not commensurate with those current risks and conditions. Instead, the pre-tax rate of return included in the Settlement at 9.91% (and the resulting PIR charges based on the inflated rate of return) far exceed those justified under current risks and market conditions, meaning the Settlement would result in Dominion overcharging consumers for its profit and cost of debt.

Further, given that the authorized rate of return (for profits and cost of debt) for gas utilities have declined significantly during the period of 2008 to 2020, the continued use of a rate of return based on the market conditions and risk profiles of Dominion as 2008 is unreasonable.²⁹ Doing so does not comport with the fundamental regulatory principle that the rate of return authorized for a regulated utility should be based on current market conditions and for giving

²⁸ *Bluefield Water Works v. Public Service Comm'n*, 262 U.S. 679, 692 (1923)

²⁹ *Id.*

shareholders investors of the regulated utility an opportunity to earn a fair return when compared to the return that they might obtain were they to invest their money elsewhere.³⁰

2. Using an outdated and inflated pre-tax rate of return will increase the revenue requirement for the CEP program and lead to rates that are unjust and unreasonable (and too high) for consumers, which violates Ohio law and policies.

The proposed Settlement violates important regulatory principles and practices by using an outdated and inflated pre-tax rate of return that will increase the revenue requirement for the PIR program and lead to rates that are unjust and unreasonable (and too high) for consumers.³¹ This violates the fundamental regulatory principle that all rates for monopoly utility services should be just and reasonable for consumers.³² Ohio law also requires all utility rates to be just and reasonable.³³ Consequently, the proposed Settlement is contrary to the policy of the state in Revised Code 4929.02(A)(1) for natural gas service to be “reasonably priced.”³⁴ And, specifically, R.C. 4929.05(A)(3) provides that the PUCO may only approve an alternative rate plan if the utility has shown and the PUCO finds that the alternative rate plan is just and

³⁰ *Id.* Specifically, in the case of *Bluefield Water Works v. Public Service Comm'n*, 262 U.S. 679, 692 (1923), the U.S Supreme Court ruled that “A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties.”. *See In re Application of Columbus S. Power Co.*, Case No. 11-346-EL-SSO, Opinion & Order (Aug. 8, 2012) (while the utility “should have the opportunity to earn a reasonable rate of return, there is not a right to a guaranteed rate of return”); *In re Application of Dayton Power & Light Co.*, Case No. 78-92-EL-AIR, Opinion & Order (Mar. 9, 1979) (“It is not the function of this Commission to guarantee a particular rate of return to an applicant utility but merely to afford the company an opportunity to earn a fair rate of return.”) (quoting Case No. 76-704-GA-CMR (June 29, 1977)).

³¹ Duann Direct at 17.

³² This regulatory principle is also referred as cost-based regulation. In other words, the rates of utility services that consumers pay should be based on the prudently-incurred costs of providing these utility services to consumers, which includes a reasonable and fair rate of return on the capital invested. *See*, for example, James C. Bonbright, *Principles of Public Utility Rates*, Columbia University Press, New York (1961) at 240-241.

³³ *See* R.C. 4905.22.

³⁴ Duann Direct at 17-18.

reasonable.³⁵ The Settlement's use of an outdated and inflated pre-tax rate of return leads to rates that are unjust and unreasonable for consumers, thus violating Ohio law.

The Settlement violates important regulatory principles and Ohio law. The PUCO should either reject Settlement or modify it consistent with OCC's recommendations for consumer protection.

III. CONCLUSION

The PUCO can approve Dominion's Application to continue the PIR for a new five-year period only if the PUCO finds the program to be just and reasonable. Dominion's proposal to continue to use the outdated and inflated rate of return set more than 13 years ago, as proposed in the Settlement, is neither just nor reasonable. The PUCO should reject or modify the Settlement to adopt a fair and reasonable pre-tax rate of return of 7.20%, instead of the 13-year-old 9.91%, for PIR charges to consumers.

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³⁵ *Id.*

CERTIFICATE OF SERVICE

I hereby certify that a copy of this Initial Brief was served on the persons stated below via electronic transmission, this 22nd day of November 2021.

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