

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE ADOPTION OF)
REGULATIONS GOVERNING THE TRANSFER)
OF PUBLIC UTILITY PROPERTY FROM) PSC REGULATION DOCKET 22
PLANT IN SERVICE OR FROM PLANT)
HELD FOR FUTURE USE OR SIMILAR)
ACCOUNTS WITH COMMISSION APPROVAL)

ORDER 3117

AND NOW, to wit, this 16th day of January, 1990;

WHEREAS, the Public Service Commission of Delaware having received, considered and adopted the Report of the Hearing Examiner in the above-captioned matter, attached to the original hereof as Exhibit "A"; and

WHEREAS, by such adoption, the Commission has determined it appropriate, pursuant to 26 Del.C. §§201 and 208, to enact a regulation to govern accounting practices of regulated utilities regarding the transfer of items of plant and equipment from utility plant in service accounts and from plant held for future use accounts, or similar accounts which are or may be Included in the determination of the utility rate base under 26 Del.C. §102(3); now, therefore,

IT IS ORDERED:

1. That the Commission hereby adopts by affirmative vote (Chairman Norling, Commissioners Twilley, McClelland and Phillips voting aye; Vice Chairman Lester voting no) a regulation designated as "REQUIREMENTS FOR CONTEMPORANEOUS NOTICE OF TRANSFERS FROM PUBLIC UTILITY PLANT SERVICE ACCOUNTS OTHER THAN

NORMAL RETIREMENTS", which reads as follows:

"No public utility may, without giving contemporaneous written notice to the Commission explaining the details of the transaction, reclassify property from a plant-in-service account or plant held for future use account, of any similar account which is normally used in the determination of the utility rate base into non-utility property accounts except for normal retirements in the usual course of business. Such notice shall include the estimated fair market value of all transferred properties, and if the property is more than \$100,000 in value, the notice shall be accompanied by an independent appraisal of said property."

2. That the effective date of the foregoing regulation shall be March 1, 1990.

3. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

BY ORDER OF THE COMMISSION:

/s/ Nancy M. Norling
Chairman

/s/ Earle J. Lester
- Vice Chairman

/s/ Donald D. Phillips
- Commissioner

/s/ Joshua M. Twilley
Commissioner

/s/ John R. McClelland
- Commissioner

ATTEST:

/s/ Bettiann Scott
Secretary

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REPORT OF THE HEARING EXAMINER

DATED: NOVEMBER 13, 1989

G. ARTHUR PADMORE

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REPORT OF THE HEARING EXAMINER

G. Arthur Padmore, having been duly appointed Hearing Examiner in this docket by Commission Order No. 3064, dated April 11, 1989, and pursuant to 26 Del. C. §502 and 29 Del. C. Ch. 101, reports to the Public Service Commission of Delaware as follows:

I. BACKGROUND

1. By Order No. 3064, dated April 11, 1989, The Public Service Commission of Delaware ("the Commission") established this Docket as a rulemaking proceeding to consider the enactment of a regulation to govern accounting practices of regulated utilities regarding the transfer of items of plant and equipment from utility plant in service accounts and from plant held for future use accounts, or similar accounts, which are or may be included in the determination of the utility rate base under 26 Del. C. §102(3).

2. By the same Order, the Commission directed its Secretary to cause the publication of notice, which invited all interested persons to pre-file written comments and other pertinent material for consideration at a public hearing to be held on June 28, 1989.

The Commission's Order also designated this Hearing Examiner to conduct such public hearing and, thereafter, to make recommendations to the Commission concerning all written submissions made in response to its Order.

3. Notice of the proceeding and the scheduled hearing was timely published. (Exhibit 1.)¹ Comments were filed by Chesapeake Utilities Corporation ("Chesapeake"), Delaware Electric Cooperative, Inc. ("DEC" or "the Co-op"), Delmarva Power and Light Company ("Delmarva"), and The Diamond State Telephone Company ("Diamond State").

4. By letter dated June 26, 1989, Staff Counsel requested, and was granted, a postponement of the scheduled hearing so that the Staff would have an opportunity to file comments responsive thereto. On August 1, 1989, Staff filed the comments of Mr. Edwin R. Carlson, the Commission's Chief of Finance and Accounting.

5. The public hearing was rescheduled and conducted in the Commission's Dover office on the afternoon of August 14, 1989.

6. Participating in the hearing were Chesapeake Utilities Corporation ("Chesapeake"), represented by its Controller, Mr. Michael P. McMasters; Delaware Electric Cooperative, Inc. ("DEC"), represented by Paul E. Bilodeau, Esquire and its General

¹References to the exhibits admitted into evidence will be referred to as "(Ex. __ at __)" or "(Ex. __)". References to the transcript of the public hearing will be referred to as "(Tr. at __)".

Manager, Mr. E. Paul Bienvenue; Delmarva Power and Light Company ("Delmarva"), represented by Peter F. Clark, Esquire and Mr. David G. Dougher, Manager of Reports and Budgets; The Diamond State Telephone Company ("Diamond State"), represented by Judith Dean, Esquire and two of its accountants, Messrs. Robert McGonagle and Thomas J. Slavinski; and the Commission Staff, represented by Rate Counsel James McC. Geddes, Esquire, and Mr. Edwin R. Carlson, the Commission's Chief of Finance and Accounting. Neither the Office of the Public Advocate nor any member of the public appeared or participated in the proceeding.

7. At the conclusion of the hearing, I closed the record, which consists of seven (7) exhibits and a transcript of thirty-nine (39) pages. The participants were afforded an opportunity to meet informally with Staff to discuss their concerns with the regulation as proposed and, thereafter, to file post-hearing submissions if they so chose.

8. By letter dated September 8, 1989, Staff Counsel Geddes informed me that Staff and the participants had met informally and, as a result of that informal meeting, Staff had concluded that a further modification to the proposed regulation was appropriate. The modified regulation was set forth in Mr. Geddes' letter; and all participants timely responded to the Staff proposal. Based upon a consideration of the record evidence and the post-hearing submissions, I submit this report with recommendations for the Commission's consideration.

II. COMMENTS

9. The Order establishing this Docket expresses the Commission's intention to consider the adoption of a regulation designated as "REQUIREMENTS FOR PRIOR APPROVAL OF TRANSFERS FROM PUBLIC UTILITY PLANT SERVICE ACCOUNTS OTHER THAN NORMAL RETIREMENTS". The proposed regulation reads as follows:

"No public utility may, without prior Commission approval, reclassify property from a plant in service account or plant held for future use account or any similar account which is normally used in the determination of the utility rate base into non-utility property accounts except for normal property retirements in the usual course of business."

10. As previously noted, comments concerning the proposed regulation were filed by several Commission regulated utilities to which the Commission Staff responded with the prefiled testimony of Mr. Edwin R. Carlson. The prefiled testimony and comments are summarized below.

Chesapeake Utilities Corporation

11. In comments submitted by its Controller, Mr. Michael P. McMasters, Chesapeake asserted that 26 Del. C. §215 clearly provides the Commission the authority to "pre-approve transfers and sales of essential public utility plant, equipment or other property." (Ex. 4 at 1; emphasis in original.)

12. Mr. McMasters noted that Chesapeake routinely transfers "small plant or rate base items" (such as personal computers, vehicles, etc.) among its operating divisions or subsidiaries. He contended that requiring Commission approval of such transactions

would "cause frequent and numerous filings by Chesapeake." (Id.)

In addition, Mr. McMasters argued that the proper place for the Commission to review such transfers was in base rate proceedings.

13. In summary, Chesapeake believes that the proposed regulation is unnecessary.

Delaware Electric Cooperative, Inc.

14. In its comments, DEC argued that it is not the "cause" of the proposed regulation, therefore, it requested that, pursuant to 26 Del. C. §208(a), DEC be classified out of or removed therefrom. (Ex. 3 at 1.) DEC also asserted that the proposed regulation is unduly onerous and burdensome because although it foresaw no need in the near future to make any of the transfers which the regulation anticipates, the regulation, nonetheless, could potentially cost the Co-op several thousand dollars in various fees merely to obtain Commission approval should the need to make such transfers arise. (Id. at 1-2.)

15. Notwithstanding the foregoing, should the Commission adopt the proposed regulation, then DEC suggested that such regulation be modified to include a minimum dollar threshold (or tied to a percentage of plant) which would be required for approval by the Commission. (Id. at 2-3.)

16. In addition, DEC opined that it would be more appropriate if the Commission addressed the regulation of accounting practices on a utility by utility basis during rate-making proceedings. Furthermore, DEC asserted, the proposed

regulation should include standards by which the Commission will exercise its judgment in approving or disapproving such transfers.

(Id. at 3.)

Delmarva Power & Light Company

17. Delmarva took the position that the proposed regulations should apply only to those utilities which are not subject to federal accounting rules² because 26 Del. C. §208(a) clearly acknowledges federal preemption of state regulatory authority in accounting matters "at least to the extent that state and federal systems cannot be made to 'correspond' 'as far as practicable.'" (Ex. 6 at 4.)

18. Delmarva contended that, at least in its own case, there is no justification for the Commission's imposing the proposed prior approval rule because in the past, rate base transfers of the type that the proposed regulation addresses were adequately examined in base rate proceedings, which, supplemented by periodic reports to the Commission Staff, offers an efficient method for considering the proper accounting and rate-making treatment for such transfers. (Id. at 7-8.)

19. Delmarva suggested that to the extent that the Commission finds that its proposed regulation is neither preempted nor unnecessary, the proposed regulation should provide only for improved reporting of significant transactions³ or specify in detail the approval standards for such transactions. (Id. at 9.)

²Delmarva is also subject to regulation by the Federal Energy Regulatory Commission ("FERC").

³Delmarva suggests that "significant transfers" should be transfers involving sums in excess of \$100,000 over the lesser of original cost or fair market value. (See, Ex. 6 at 9.)

20. In addition to the foregoing, at the hearing, Delmarva presented the testimony of David G. Dougher, its Manager of Reports and Budgets (See, Ex. 5), who described the federal accounting regulations to which Delmarva is subject as well as the annual reporting requirements which those regulations prescribe for rate base related accounts. (Tr. at 29.) Mr. Dougher expressed concerns of a potential federal and state conflict on accounting for property transfers and recommended that the proposed regulations be modified so that Delmarva would be required to provide notice to the Commission only of transactions involving transfers of property with an original cost or estimated fair market value over \$100,000. (Id.)

The Diamond State Telephone Company

21. In its prefiled comments, Diamond State opposed the proposed requirement of prior Commission approval for the transfers which the proposed regulation addresses because it is subject to federal accounting rules regarding such transfers.⁴ According to Diamond State, those rules adequately safeguard the assets used to provide service to its ratepayers, therefore, the proposed prior approval regulation would be "unnecessary and unduly cumbersome, and could present conflicts for utilities subject to [both federal and state regulation]." (Ex. 7 at 1-2.)

22. However, Diamond State asserted that it would not oppose

⁴Diamond State is also subject to regulation by the Federal Communications Commission ("FCC").

a requirement that the Commission be provided notice of any such transfers of a "significant level, above a threshold that might be measured in absolute dollar amounts or, for example, as a percentage of rate base." (Id. at 1.)

The PSC Staff

23. In reply comments, Mr. Edwin R. Carlson, the Commission's Chief of Finance and Accounting, testified that although the major utilities do file annual reports based on standards prescribed by federal regulatory bodies, such reports are, in some cases inadequate. Thus, the Staff is seeking more detailed and timely reporting of rate base property transfers. (Ex. 2 at 7.)

24. Mr. Carlson stated that there was no specific practice by any of the regulated utilities which the Staff sought to curb or prohibit; however, he expressed concern about the increasing number of unregulated parent and/or subsidiary relationships, which created a "heightened need for monitoring of rate base property transfers." (Id.) Moreover, Mr. Carlson asserted that in past base rate proceedings the Commission has, due to the lack of readily available information, been unable to deal effectively with this type of transaction. In view of the foregoing, Mr. Carlson concluded that the appropriate remedy may be a "systematic method of reporting rate base transfers to the Commission." (Id. at 8.)

25. Mr. Carlson observed that, in his opinion, adoption of

the proposed regulation should not adversely affect a utility's ability to provide adequate service because, if there is a reasonable basis for the transfer of rate base property, Commission approval should be routinely granted. (Id.)

26. In light of the comments filed by the utilities, Mr. Carlson expressed a willingness to modify the proposed regulation as follows:

- "(1) To expedite approval and curtail costs, prior approval could be delegated to the Chief Accountant rather than the Commission as a whole.
- (2) If after one year's experience this regulation is determined to be burdensome on the utilities, the Commission could consider setting a threshold level below which prior approval is not required.
- (3) Transfers of property which federal regulatory agencies have approved could be granted automatic approval by this Commission, subject only to prior reporting." (Id.)

III. DISCUSSION

27. As previously noted, at the conclusion of the public hearing, the participants were afforded an opportunity to meet with the Staff informally to discuss utility concerns with, and to attempt to resolve their differences over, the proposed regulation. The participants met in Wilmington on August 31, 1989, and, by letter dated September 8, 1989, Staff Counsel Geddes

reported the results of that meeting.

28. According to Mr. Geddes, at the conference, Staff indicated its intent that the proposed regulation "should not be construed to confer anything other than authority to consider the proposed accounting treatment" for transactions involving the transfer of property from rate base accounts to non-utility accounts. Mr. Geddes reported that the utilities raised questions as to the appropriate methodology for reporting the value of a transaction (e.g., whether or not the transaction should be reported at original cost or fair market value). However, realizing that the Commission traditionally observes the principle that accounting follows ratemaking, Staff concluded that "since there appear to be situations where the proper accounting for a transaction may indeed be dependent upon the regulatory treatment to be afforded," it would be appropriate to require only contemporaneous notice reporting of rate base property transactions.

29. Thus, the proposed regulation was further modified to read as follows:

"No public utility may, without giving contemporaneous written notice to the Commission explaining the details of the transaction, reclassify property from a plant-in-service account or plant held for future use account, or any similar account which is normally used in the determination of the utility rate base into non-utility property accounts except for normal retirements in the usual course of business."

30. I have reviewed the proposed regulation, and it appears to be a reasonable compromise because it adequately addresses the

concern expressed by Mr. Carlson about the "heightened need" to monitor transfers of property from rate base accounts. Moreover, since none of the utilities which participated in this proceeding have opposed the proposed regulation as modified, it appears that their initial concerns about the regulation have been allayed. However, in its post-hearing comments, Delmarva indicated that although it would have preferred that the proposed regulation established a threshold below which there would be no reporting requirement, it, nonetheless, would not oppose Commission adoption of the proposed regulation as set forth in Mr. Geddes' September 8, 1989 letter. Delmarva noted, however, that if experience shows that the reporting requirement creates compliance problems, it may request further changes in the provisions of the regulation.

31. In my view, Commission adoption of any regulation would not preclude any entity affected thereby from requesting, at any time, the Commission's reconsideration or modification of such regulation. I recommend that the regulation as modified be approved and promulgated. Obviously, the designation of the regulation should reflect the change that contemporaneous notice rather than prior approval is required for certain transfers of property from rate base accounts.

IV. RECOMMENDATIONS

32. In summary, I recommend that the Commission approve and adopt, effective not less than thirty (30) days from the date of its Order, a regulation designated as "REQUIREMENTS FOR

CONTEMPORANEOUS NOTICE OF TRANSFERS FROM PUBLIC UTILITY PLANT SERVICE ACCOUNTS OTHER THAN NORMAL RETIREMENTS", which reads as follows:

"No public utility may, without giving contemporaneous written notice to the Commission explaining the details of the transaction, reclassify property from a plant-in-service account or plant held for future use account, of any similar account which is normally used in the determination of the utility rate base into non-utility property accounts except for normal retirements in the usual course of business."

33. A proposed form of Order which will effect the foregoing recommendation is attached for the Commission's consideration.

Respectfully submitted,

/s/ G. Arthur Padmore
G. Arthur Padmore
Hearing Examiner

Dated: November 13, 1989