

Process for Setting Utility Rates

Background

- Utility ratemaking is the formal State regulatory process by which public utilities set the rates they will charge customers
- While the process is basically the same, there is some **variation from State-to-State**
- Each State's process is **governed by a law** - for example, in Illinois the law is called the Illinois Public Utilities Act (PUA), (220 ILCS 5)
- Ratemaking is carried out by means of a "rate case" before a public utility commission in a **court-like procedure**
- Public utility commissions (PUC) have different names depending on the State, e.g., Public Service Commission, Commerce Commission, Public Utility Commission
- Public utilities have a **natural monopoly for the services they provide** in a particular State
- Examples of public utilities which use ratemaking to set rates are: electricity, natural gas, water, sewer, and (in varying degrees, in some States) telecommunications
- In order for a public utility to increase (or decrease) its rates, it must file a request with its State PUC, proposing and justifying new rates
- When setting rates many PUCs are guided by various **legislative principles**, such as in Illinois where "[t]he General Assembly finds that the health, welfare and prosperity of all Illinois citizens **require the provision of adequate, efficient, reliable, environmentally safe and least-cost public utility services at prices which accurately reflect the long-term cost of such services and which are equitable to all citizens.**" (220 ILCS 5/1-102)
- Of course, public utilities must be allowed to recover a reasonable return on investment used to provide service and their necessary operating expenses
- **In general, rate setting is premised on the rate formula: Revenue Requirement = Operating Expenses + (Investment - Depreciation) x Rate of Return**

Steps in the Ratemaking Process

(varies from State-to-State, using Illinois as an example)

- **Public utility files its rate request** with the Illinois Commerce Commission (ICC) following the Illinois PUA and the standard information requirements in ICC rules (83 Ill. Adm. Code 285, 286, 287)
- In general, the filing **will contain written testimony and financial and accounting schedules**
- For a standard rate case, **the ICC has 11 months** from filing to make its decision; less time for performance-based formula rate cases
- An ICC Administrative Law Judge (ALJ) is assigned; ICC; Staff is assigned various interested parties (e.g., Citizens Utility Board, Attorney General, AARP, consumer groups, industrial customers) file to intervene and participate in the proceeding
- It is ICC Staff's job to be impartial, neutral expert witnesses in areas such as accounting, finance, rates, etc.
- The ALJ has 35 days from the date of filing to **send the utility a list of deficiencies in the materials the utility filed** with respect to the standard information requirements
- A pre-hearing conference is held with the ALJ and all the parties to **set the case schedule**
- **Parties are allowed to file discovery requests (i.e., questions)** upon one another to clarify each other's positions in an effort to narrow the list of contested issues
- **Staff and Intervenors file direct testimony** in response to the Utility's filing; **Utility files rebuttal testimony** in response to Staff/Intervenor direct testimony; **Staff and Intervenors file rebuttal testimony** in response to the Utility's rebuttal position; **Utility files surrebuttal testimony (the party filing the case is entitled to the final say)**
- **An evidentiary hearing is held** with the ALJ presiding (NOT the Commissioners in Illinois); the **parties may cross-examine one another on the contested issues** (for example, a contested issue might be the appropriate amount of the Utility's fixed charge)

- After the hearing, **Initial Briefs**, which summarize and argue the parties' positions on the issues, are filed
- The parties file **Reply Briefs** in response to one another's Initial Brief positions
- The ALJ issues a **Proposed Order (PO)** that sets forth all of the parties' positions and offers **Conclusions (i.e., decisions)** regarding the contested issues
- The parties file **Briefs on Exceptions (BOE)** to the PO, arguing that the PO has incorrectly arrived at certain Conclusions; parties file **Reply Briefs on Exceptions (RBOE)** to the other parties' BOEs. Suggested replacement language to the PO supporting their respective arguments and positions is required.
- After considering the BOEs and RBOEs, the ALJ sends a **Post Exceptions Proposed Order (PEPO)** to the Commissioners
- The Commission may hear oral argument on a specific issue or issues that it wants to hear or issue(s) that a party to the case asks to argue; while oral argument is not mandatory and within the discretion of the Commission, it provides the parties with the unique opportunity to argue directly before the final decisionmakers, (i.e., the Commissioners) instead of the ALJ
- The Commission votes on the Order in an **Open Meeting** (called a Bench Session in Illinois), either approving the ALJ's PEPO or making changes to certain of the PEPO's Conclusions
- A party may file an application for rehearing (i.e., reconsideration) on a specific issue or issues in the Order with which it does not agree, which the Commission may grant or deny
- Appeals may then be taken to an appellate court, in general when a party does not believe the ICC has correctly applied the law to the facts in the case