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Witness: Douglas P. Horton, Matthew Nelson and Michael Goldman
Request from: Public Utilities Regulatory Authority

Question:

(CONSUMER DIVIDEND) Exhibit CLP-ELP-1. The Consumer Dividend is capped so that it does not exceed the applicable I-Factor for the year. Explain how the cap operates when the Consumer Dividend resulting from the ratchet exceeds the I-Factor (e.g., is it temporarily blocked, does it disappear, etc.). Provide an illustrative calculation and identify the Consumer Dividend used as the starting point for the following year's ratchet. Provide the results in an unlocked Excel workbook with all equations, calculations, links, and underlying assumptions/workpapers unhidden, unprotected, and in a reproducible format.

Response:

The Consumer Dividend has two values in any year, which are: (1) the ratchet level; and (2) the applied Consumer Dividend. The Consumer Dividend is 30 basis points. The Consumer Dividend ratchet level is set by the Company's performance against the Core Operating Expense per customer benchmark. Combined, the value starts at 0.30 percent, increases by 0.10 percentage points for a year in which Core Operating Expense per customer is below the benchmark, decreases by 0.05 percentage points for a year in which it is at or above the benchmark, and never falls below 0.30 percent (Exh. CLP-ELP-1, at 94, line 2–9; 96, line 3–13). The applied Consumer Dividend is the amount deducted in that year's PBR adjustment and it equals the Consumer Dividend ratchet level unless the PBR cap applies.

The PBR cap ensures that the annual O&M revenue adjustment is never negative. Under the PBR formula, the O&M revenue requirement is adjusted each year by I − X − CD (Ex. CLP-ELP-1, at 86, line 11–21). If the Consumer Dividend could exceed the inflation adjustment net of the productivity offset, the formula would reduce the Company's O&M revenue in nominal terms in a year of very low inflation. That result would be inconsistent with the purpose of the PBMRP, which is to provide predictable rate changes for customers and revenue support for the Company's operating costs over a multi-year term, while also enabling a multi-year rate case stay-out and the performance commitments provided for in the PBMRP (Exh. CLP-ELP-1, at 92, line 1–8). The PBR cap therefore limits the applied Consumer Dividend to I − X for the year, so that the total adjustment is not negative.

When the Consumer Dividend ratchet level exceeds I − X for a year, the PBR cap operates as follows.

1. The applied Consumer Dividend for that year equals I − X, and the PBR adjustment for that year is zero percent.

2. The portion of the Consumer Dividend ratchet level above I − X is not applied in that year. It is temporarily blocked, not eliminated; the Consumer Dividend ratchet level itself is unchanged. The blocked portion is not deferred, banked, or recovered in a later year, and no regulatory asset or liability is created (Exh. CLP-ELP-1, at 93, line 16–18).

3. The following year's Consumer Dividend ratchet starts from the Consumer Dividend ratchet level, not from the capped amount applied. Adjustments to the level accumulate over the plan term (Exh. CLP-ELP-1, at 96, line 10–12). If I − X in a subsequent period increases such that the PBR cap is not triggered, the full Consumer Dividend ratchet level is applied again prospectively in the applicable PBR rate change.

The table below illustrates the PBR cap using the third performance year, assuming the Company has been below the benchmark in each year and the Consumer Dividend ratchet level has reached 0.60 percent. This is an illustrative example (not a forecast) to show how component works together. In every scenario, the starting point for the following year's Consumer Dividend ratchet is the 0.60 percent level.

(*) Illustrative scenario (percent)	**I – X (presented at different levels for illustration)**	**Consumer Dividend ratchet level, Y3**	**Applied Consumer Dividend**	**Portion not applied**	**PBR-O adjustment**
(a) Inflation above the dividend range	2.20	0.60	0.60	0.00	1.60
(b) Inflation inside the dividend range	0.45	0.60	0.45	0.15	0.00
(c) Inflation below the 0.30 percent starting level	0.20	0.60	0.20	0.40	0.00
(d) Inflation at the zero floor	0.00	0.60	0.00	0.60	0.00

(*) For a full illustration of the operation of the S Factor please see Attachment 1, to response UPA – 71.

Under inflationary conditions that the Company expects over the plan term, the PBR cap is not expected to be triggered. Thus, Scenario A is the most likely outcome. Scenarios B through D have the potential to occur only when inflation falls below the Consumer Dividend ratchet level, which is at most 0.60 percent.

The PBR cap matters only when I − X falls below the Consumer Dividend ratchet level (Scenarios B through D). In those years, customers receive the full available adjustment; the Company's O&M revenue is held flat rather than reduced; and the Consumer Dividend ratchet level is preserved so that the full dividend resumes when inflation recovers.

Lastly, the PBR cap and the Consumer Dividend ratchet operate independently year over year. The Consumer Dividend ratchet level moves only on the Company's performance against the benchmark; the PBR cap limits only the amount applied in a year's rate adjustment. In a year of low inflation, the Company's performance is still measured, the Consumer Dividend ratchet level still steps up or down, and the capped amount is applied. When I − X returns above the Consumer Dividend ratchet level in the following year, the full Consumer Dividend ratchet level is applied in that year. There is no catch-up adjustment for the amount blocked in the prior year and no reset of the level.