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Witness: Douglas P. Horton, David L. Gladey, John P. Dipaola-Tromba, Leanne M. Landry and Jeffrey D. Turano
Request from: Office of Education, Outreach, and Enforcement

Question:

(F-FACTOR; TARGETED SYSTEM PERFORMANCE PLAN) Refer to Response to EOE-156, Att.1-Att.2. The Company's F-Factor Excel spreadsheet (PBR-4 F-Factor tab) details monthly Plant Additions, Retirements, and Cost of Removal and cites "Exhibit CLP-ELP-1, Figure 7, annual figure divided by 12 less COR" and "Per Company Financial Forecast". Additionally, the PBR-6 Capital Expense Forecast tab details similar annual information by category. Please provide the underlying information used to derive the cited Figure 7 and the Financial Forecast. As part of the response, provide a detailed listing of all planned capital additions, the anticipated in-service date, the total amount per addition, the category, and any additional details available to assist in understanding the nature and timing of the planned capital additions. This request also attempts to understand the level of information available for parties to assess if the planned capital additions within the TSP are adequately substantiated for both necessity and anticipated cost.

Response:

Please refer to the Company's response to interrogatory OCC-858[i], which describes the capital expenditure forecast as well as plant placed into service. Additionally, OCC-858, Attachment 1, provides additional details of the investments comprising the amounts shown in Figure 7.

For additional discussion of the Company's TSP and proposed F-Factor, please refer to the Company's responses to interrogatories OCC-857[ii], EOE-372[iii], and EOE-374[iv]. As explained therein, the capital forecast presented in this proceeding serves as the foundation of the Company's proposed F-Factor framework.

As the Company explained in response to EOE-374:

> "[…] the Company is proposing a hard cap on core capital investment eligible for the F-Factor based on the capital forecast presented in this proceeding. By doing so, the Company can provide upfront, during this proceeding, indicative revenue increases necessary to support those investments while committing to cap resulting revenue increases during the PBMRP even if actual capital investment exceeds the forecast. Additionally, the downward-only reconciliation of the Company's proposed F-Factor protects customers from theoretically-excessive investment, including even investments unforeseen today."

The information underlying Figure 7 of Exhibit CLP-ELP-1 and the F-Factor calculations reflects the Company's current assessment of the investments necessary to maintain and improve the system over the PBMRP term, based on the operating conditions, planning assumptions, and system objectives known today. Accordingly, the forecast serves two critical purposes in this proceeding: it establishes the maximum level of capital investment eligible for recovery through the F-Factor (excluding AMI and other legislatively mandated capital programs not contemplated today) and provides the basis for the illustrative revenues necessary to support those investments.

Consistent with the structure of the proposed PBMRP, the Company's proposal does not require a determination, in this proceeding, of the prudence of individual capital projects that may ultimately be undertaken during the plan term. Rather, the focus at this stage is appropriately placed on the Company's TSP, including the system needs, operating conditions, and policy objectives currently facing the Company, and the revenues necessary to support the investments intended to address those needs and achieve the objectives of the PBMRP, based on the information available today.

The proposed annual reconciliation and prudence review is the mechanism through which the necessity, reasonableness, execution, and support for specific investments can be evaluated based on actual facts rather than forecasts. By the time of prudence review, stakeholders will have access to the completed investment, project-specific documentation, actual costs, rationale, and the circumstances that existed when the investment decision was made. Accordingly, the annual review process places parties in a substantially better position to evaluate prudence than would be possible in this proceeding, which necessarily relies on forward-looking forecasts and planning assumptions and precedes the investments themselves. This distinction is important because it aligns the review with the information available at each stage of the process. This proceeding necessarily relies on forecasts and planning assumptions to establish prospective investment levels and associated revenue requirements, while the annual reconciliation permits review of actual investment decisions based on a complete factual record available at that time.

This structure also provides important customer protections. Customer rates ultimately reflect only prudent investments, not merely the projected investments and associated revenue requirements presented today. Recovery remains subject to review through the annual reconciliation process, and only investments found prudent are eligible for recovery through the F-Factor. At the same time, the Company's proposed hard cap ensures that recoverable capital investment cannot exceed the forecasted level of investment presented and approved in this proceeding. Taken together, these features protect customers from recovery of imprudent investments, recovery of capital investment above the level forecast and approved in this proceeding, and the rate shock commonly experienced with traditional ratemaking.

Prior Referenced Responses:

[i] OCC-858 Question:

Refer to Exhibit CLP-ELP-1, figure 7. Please explain whether the amounts shown in Figure 7 are capital expenditures versus plant additions. Please explain any differences in the nature, or timing of the amounts shown in Figure 7 and the amounts of plant addition that would be used in comparing [i.e., determining "lessor of"] annual plant addition costs in the annual reconciliation filings.

a. Please identify, in disaggregated table form, all of the component costs included in each category of the amounts shown in Figure 7.

[i] OCC-858 Response:

Plant additions and capital expenditures represent two different ways of viewing the same underlying investment. Capital expenditures are generally organized and managed around specific business objectives, programs, projects, or asset installation efforts, such as substation expansions, feeder rebuilds, pole replacement programs, or other distribution system investments. Capital expenditures are incurred over the course of project execution and may span multiple months or years depending on project scope, complexity, and construction schedules.

Plant additions, by contrast, are recognized when utility assets are placed in service and meet the applicable accounting criteria for recording as utility plant. Accordingly, a plant addition is generally recorded at a specific point in time, whereas the associated capital expenditures may have been incurred over an extended period.

The Company develops its forecast of plant additions using its capital investment plans, project schedules, anticipated in-service dates when possible, and historical experience. However, actual in-service dates may differ from forecasted in-service dates (where available) due to changes in project scope, construction sequencing, permitting, material availability, operational considerations, weather, or other factors. Consequently, the timing of annual plant additions may differ from the timing of annual capital expenditures.

While such timing differences may occur in any given year, over a multi-year period it is reasonable to expect that plant additions, together with associated cost of removal, will generally track with capital expenditures.

The amounts shown in Figure 7 are forecasted capital expenditures associated with the Company's planned investment programs. As stated in its response to OCC-423i and other interrogatories, the Company's annual F-Factor reconciliation would consider specifically the plant additions actually placed in-service through the calendar year-end prior to a given annual filing.

For subpart (a) of this request, please refer to OCC-858, Attachment 1.

[ii] OCC-857 Question

(Capital Support Mechanism) On p. 101 of Exhibit CLP-ELP-1, the Company states that, "As part of the Company's annual RAM compliance filing, actual plant additions placed in service during the applicable plan year will be reconciled against the approved forecast." In the Company's response to EOE-156, Witness Horton states that prudence reviews would be included in the annual reconciliation process.

a. Provide a detailed plan for how the Company envisions the annual reconciliation process would proceed and how long the process would take both as a whole, and for each step. Please identify what filings would be made, whether and how discovery would be allowed, and what types of determinations would be required by the Authority.
b. Where in the reconciliation process will the distinction and differences be identified between realized annual plant addition costs and the associated rate base, and the return, taxes, and deprecation on rate base that are included in the going-in revenues?
c. Will the annual PBR reconciliations be assessments of the whole Company's rate base with calculations of commensurate return, tax and depreciation, or will it be an incremental adjustment based on annual plant additions? Please explain.
d. Provide one or more examples, as appropriate, showing how the annual capital recovery process, including reconciliation, would function, including detailed calculations in the form to be used in the annual adjustment filings.
e. Provide a list of all types of costs that will be included in the capital recovery reconciliations.

[ii] OCC-857 Response

a. The Company has given this process a lot of thought based on discussions throughout the PBR dockets. Based on input from those sessions, the Company's proposal is to align the Performance Based Multi-Year Rate Plan (PBMRP) with the Rate Year, and as much as possible, aligns with the existing annual RAM ratemaking process. As such, the Company proposes that PBMRP adjustments occur on each July 1, starting with July 1, 2027, and annually thereafter. For each year that the PBMRP mechanism is in effect, the Company would submit an Annual PBR Plan Compliance Filing to PURA in the annual RAM proceeding. The annual compliance filing would include, among other things:

(1) the calculation of the annual revenue-cap adjustment;

(2) the new proposed rate using the PBR formula;

(3) an earnings-sharing computation;

(4) cost documentation for the Company's capital investments;

(5) the calculation and reconciliation of the annual capital-cap adjustment;

(6) documentation of metric performance and resulting penalties or incentives; and

(7) bill impacts of the new rate by rate class.

(8) as applicable, any request for exogenous cost recovery.

With respect to the capital-support mechanism or "F" factor in the formula, the Company proposes a mechanism based on a fixed annual capital investment level for each year of the PBMRP, with reconciliation through PURA's annual RAM proceedings. The fixed annual investment level would initially be set at the Company's capital forecast, as approved in this proceeding, and would be subject to downward-only reconciliation[1] in the event that either i) the Company's actual plant in service is lower than projected and utilized in establishing the initial F-Factor for that Rate Year or ii) PURA ultimately denies as imprudent a level of investment that was initially included in the F Factor

allowance. In this way, customers are assured that rates ultimately reflect the costs of system investments that are actually in service, and have been found prudently incurred by PURA.

[1] The Company notes that the revenue decoupling mechanism (RDM) will continue to operate and reconcile actual revenues to the target revenues, as adjusted by the PBMRP. The Company's reference to a 'downward only' reconciliation is meant to reflect that the revenue target utilized in the RDM will not be adjusted upward in the event actual plant additions exceed the level originally reflected in the F-Factor allowance. In that circumstance, the F-Factor allowance is capped at the fixed level projected in this proceeding. Capital that is placed in service above the cap would not be included in rates until a future rate case proceeding, and only then on a prospective basis.

As described in its Exhibit CLP-ELP-1 testimony, the Company has presented different investment trajectories in the Company's 5-Year targeted system performance (TSP) and is proposing to establish the capital support mechanism of the PBR adjustment consistent with the annual capital funding requirements presented in Figure 7 of the Exhibit CLP-ELP-1 testimony. As part of the Company's annual RAM compliance filing, actual plant additions placed in service during the applicable plan year would be reconciled against the approved forecast that would have been utilized in the prior PBMRP filing to establish the F-Factor initially.

Following PURA's determination that the Company's actual plant additions are prudent, used and useful, the Company's allowed rate base and associated revenue requirement for that year will be limited to the lesser of (1) the total revenue requirement for the forecasted capital approved in this proceeding; or (2) the total revenue requirement for the actual plant in service. As described previously, if the Company's actual capital additions exceeds the forecasted amount approved in this proceeding, the Company would not be permitted to seek recovery of the incremental investment during the initial four-year PBMRP Term. Any such investment would instead remain subject to review and consideration in a subsequent base rate proceeding or successor PBMRP Term.

The Company's proposed capital funding mechanism sets a defined cap on capital recovery during the plan term, providing customers with greater rate certainty and placing the risk (and cost) of increased capital spending on the Company during the course of the PBMRP. The annual reconciliation further protects customers by blocking recovery of investments that are delayed, deferred, canceled, or not placed in service, since those costs would not be reflected in the "F" factor upon reconciliation, which is based on plant in service. For these reasons, the proposal aligns cost recovery with prudent investment and incentivizes efficient execution of the capital program, all while minimizing customer over-collection.

Based on the above framework, an exhibit that demonstrates a revenue requirement consisting of: (1) a reconciliation of actual plant additions placed in service during the previous calendar year against the approved forecast (also referred to as the F-factor allowance) for that calendar year, and (2) the F-factor allowance for the new Rate Year beginning July 1st, would be filed on or about March 1st of each year consistent with the timing of all other RAM component reconciliations. Concurrent with that timing, all plant additions documentation for the previous calendar year included in the above reconciliation will also be filed on or about March 1st as part of the same filing.

Further, under the Company's proposed timeline, the revenue requirement resulting from the reconciliation of the prior year's F-factor allowance and the new Rate Year's F-factor allowance will go into effect on July 1, following the March 1st filing. As part of the RAM process, PURA performed prudence reviews of capital documentation filed for the ESI, including discovery, between March 1st and September 1st, the date on which additional RAM rate changes were made. Even though PBMRP rates would go into effect on July 1st, the Company proposes that this timeline continues to be used for capital prudence reviews under the PBMRP.

To the extent PURA's prudence review warrants any adjustment to the revenue requirement that went into effect on July 1, the Company will calculate the excess revenue collected from customers over the period of July 1 through

August 31 and include this amount, plus carrying costs for those 2 months, in the RDM's allowed revenue target for the July 1 through June 30th Rate Year.

b. Please refer to subpart (d) of this question.

c. Please refer to subpart (d) of this question.

d. Please refer to the example shown in EOE-156, Attachment 1, pages 4 through 12, showing how the annual capital recovery process, including reconciliation, would function, including detailed calculations in the form to be used in the annual adjustment filings. Please note that pages 4, through 12, show an illustrative example for all four Rate Years contemplated for the duration of the PBMRP; however, the annual filing would only be for a single year of the PBMRP. As part of this example, please refer to the differences between realized annual plant addition costs and the associated rate base, and the return, taxes, and depreciation on rate base that are included in the going-in revenues found in EOE-156, Attachment 1, worksheet "PBR-7 Going-In Capital RR", Lines 13-16. Additionally, the detailed calculations shown in EOE-156, Attachment 1, pages 4 through 12, demonstrate that the annual PBR reconciliations will be an assessment of the Company's total accumulated depreciation included in base distribution rates (i.e., customers will be receiving credit for the increase in the Company's accumulated depreciation for all capital included in base distribution rates), as opposed to the Company's entire rate base (the Company considers its entire rate base to include other rate base items such as deferred assets and liabilities, etc.).

e. The revenue requirement for capital recovery will include appropriate recovery of net plant in service, accumulated deferred income taxes ("ADIT") and accumulated depreciation for the cumulative additional plant additions and will include a pre-tax return on investment (i.e. return on rate base including income taxes), return of investment (i.e. depreciation), property taxes, gross earnings tax and uncollectible expense.

[iii] EOE-372 Question:

(TIMING OF ANNUAL FILINGS; F-FACTOR) Provide both a discussion and a visual representation of the timeline detailing key components of the Company's proposed annual filings for each year of the MRP. As part of the response, identify the cutoff date(s) for capital additions, the annual filing date(s), and rate change date(s). This request attempts to understand the amount of time needed for the Company to close its books and prepare the filing, along with the amount of time for the Authority's approval, and the Company's subsequent processing of the rate increases within its system. Additionally, this request attempts to understand relevant cutoff dates whereby the F-Factor capital additions would be applicable from the end of the evidentiary record through the first annual cutoff date.

[iii] EOE-372 Response:

Please refer to the Company's response to OCC-857i which responds to a similar question.

The Company proposes to align the Performance Based Multi-Year Rate Plan (PBMRP) with the Rate Year, with PBMRP adjustments occurring on July 1 each year. For each year that the PBMRP mechanism is in effect, the Company would submit an Annual PBR Plan Compliance Filing to PURA in the annual RAM proceeding. The annual compliance filing would include, among other things: (1) the calculation of the annual revenue-cap adjustment; (2) the new proposed rate using the PBR formula; (3) an earnings-sharing computation; (4) cost documentation for the Company's capital investments; (5) the calculation and reconciliation of the annual capital-cap adjustment; (6) documentation of metric performance and resulting penalties or incentives; (7) bill impacts of the new rate by rate class; and (8) any request for exogenous rate change, if applicable.

With respect to the capital support mechanism or "F" factor in the formula, the Company proposes a mechanism based on a fixed annual capital investment level for each year of the PBMRP, with reconciliation through PURA's annual RAM proceedings. The fixed, annual investment level will be set at the Company's capital forecast, as approved in this proceeding. As described in its Exhibit CLP-ELP-1 testimony, the Company has presented different investment trajectories in the Company's 5-Year targeted system performance (TSP) and is proposing to establish the capital support mechanism of the PBR adjustment consistent with the annual capital funding requirements presented in Figure 7 of the Exhibit CLP-ELP-1 testimony. As part of the Company's annual RAM compliance filing, actual plant additions placed in service during the applicable plan year will be reconciled against the approved forecast. As described in the response to OCC-857, the fixed annual investment level would initially be set at the Company's capital forecast, as approved in this proceeding, and would be subject to downward-only reconciliation in the event that either i) the Company's actual plant in service is lower than projected and utilized in establishing the initial F-Factor for that Rate Year or ii) PURA ultimately denies as imprudent a level of investment that was initially included in the F Factor allowance. In this way, customers are assured that rates ultimately reflect the costs of system investments that are actually in service, and have been found prudently incurred by PURA. If the Company's actual capital spending exceeds the forecasted amount approved in this proceeding, the Company will not be permitted to seek recovery of the incremental investment during the initial four-year PBMRP Term. Any such investment would instead remain subject to review and consideration in a subsequent base rate proceeding or successor PBMRP Term. The Company's proposed capital funding mechanism sets a defined cap on capital recovery during the plan term, providing customers with greater rate certainty and placing the risk of excess capital spending on the Company. The annual reconciliation further protects customers by blocking recovery of investments that are delayed, deferred, canceled, or not placed in service, since those costs would not be reflected in the "F" factor, since, although the F-factor will initially be established based on the capital expenditure forecast presented in this proceeding, it will ultimately be reconciled based on plant in service, but only to the extent actual plant in service is less than (not more than) contemplated in the original F-Factor. For these reasons, the proposal aligns cost recovery with prudent investment, promotes accurate capital forecasting, and incentivizes efficient execution of the capital program, all while ensuring that customers do not provide revenues that support capital that is not in-service and used and useful to customers, and that is not found prudent by PURA.

Based on the above framework, an exhibit that reconciles actual plant additions placed in service during the applicable plan year against the approved forecast will be filed on or about March 1st of each year consistent with the timing of all other RAM component reconciliations. Further, under the Company's proposed timeline, the revenue requirement resulting from the reconciliation of the prior year's F-factor allowance and the new Rate Year's F-factor allowance will go into effect on July 1, following the March 1st filing. As part of the RAM process, PURA performed prudence reviews of capital documentation filed for the ESI, including discovery, between March 1st and September 1st, the date on which additional RAM rate changes were made. Even though PBMRP rates would go into effect on July 1st, the Company proposes that this timeline continues to be used for capital prudence reviews under the PBMRP. To the extent PURA's prudence review warrants any adjustment to the revenue requirement that went into effect on July 1, the Company will calculate the excess revenue collected from customers over the period of July 1 through August 31 and include this amount, plus carrying costs for those 2 months, in the RDM's allowed revenue target for the July 1 through June 30th Rate Year.

Annual reconciliation, including the prudence reviews involved, is a critical element of the Company's PBMRP proposal. As part of each annual PBMRP adjustment effective July 1 each year of the PBMRP1, the Company's actual capital additions for the Prior Year are allowed for inclusion in the calculation of the F factor to the extent that the actual capital additions do not exceed the Forecasted Budget (referred to as the F-factor allowance). To the extent that the cumulative actual capital costs in-service through the Prior Year, in aggregate, exceeds the Forecasted Budget through the Prior Year, then the F Factor allowance is capped at the cumulative Forecasted Budget. This downward-only reconciliation will ensure that, in the end upon reconciliation, customer bills reflect the costs associated only with projects that are in service to customers and no more, and that if the Company invests more than the Forecasted

Budget, customer bills will not reflect amounts above the Forecasted Budget, until such time as those capital investments are allowed into rates at the time of the Company's next rate case. The prior-period reconciliation will be reflected in the F-Factor, in addition to the revenue requirement associated with the Forecasted Budget for the upcoming Rate Year, effective July 1 annually. The F Factor allowance will be calculated to determine the revenue requirement (inclusive of depreciation expense, property tax expense, return on rate base, and income tax) on actual plant additions (including plant additions, cost of removal, plant retirements, accumulated depreciation, and plant-related accumulated deferred income taxes ("ADIT")) up to the Forecasted Budget amount, and to reflect the revenue requirement for the Prior Year and through the Rate Year on in service capital additions placed in service in the Prior Year, provided that those in service capital additions are not reflected in base rates or in another rate mechanism. In addition, the F Factor allowance will reflect the revenue requirement for Rate Year capital, established at the Forecasted Budget, subject to downward-only reconciliation in the subsequent F Factor filing.

As noted above, annual reconciliation will consider plant-related ADIT on the Company's books through the end of the calendar year, prior to a given annual filing. To the extent the Company has recorded cumulative plant additions in excess of the capital expenditure forecast provided in this docket or supported by a mechanism other than the F-Factor, the plant-related ADIT will be adjusted in the Company's annual reconciliation to avoid overstating the ADIT relevant to the F-Factor.

In total, the Company's proposed F-Factor will provide revenue support for, and ultimately reconcile, the capital investment placed into service from the cutoff date for inclusion in base rates through the effective date of the Company's subsequent rate case at the conclusion of the proposed PBMRP term. Per the Company's proposal the F-Factor would ultimately reconcile capital investments made up to July 1, 2031 (the effective date of the subsequent rate case). Should the subsequent rate case be effective later than the July 1, 2031, illustrative date, the F-Factor would continue to reconcile capital investments placed into service until such time as that rate case does take effect.

[iv] EOE-374 Question:

(F-FACTOR; CAPITAL ADDITIONS) Refer to Response to EOE-156, Att.1-Att.2. Explain how the F-Factor calculation and the Company's Targeted System Performance (TSP) plan accounts for unplanned capital additions.

[iv] EOE-374 Response:

The Company's F-Factor proposal does not make the distinction between "Capital Plan" and "Non-Capital Plan."

As the Company explained in Docket No. 21-05-15RE01, some projects cannot be planned with precision. For example, it would be impossible for the Company to perfectly predict Emergent Failures. The Company cannot predict which specific pole or cross-arm will fail. The Company can, however, reasonably forecast a volume and severity of such failures based on system conditions and recent experience, which is the type of information that the Company uses to develop its forecasted capital plan.

The Company is proposing to (1) set a hard cap on the annual plant additions that may be recovered through the F-Factor; and (2) set that cap on the basis of the Company's forecast annual capital expenditures, as presented in this case. If Emergent Failures were to develop in year beyond what is budgeted, it would not change the cap. The cap would operate to allow a quantity of plant additions into rates, while the rest would have to wait until the next rate case, similar to how the ESI works now with the $300 million annual allowance.

With this perspective in mind, there is no distinction between "Capital Plan" and "Non-Capital Plan" that is necessary for two reasons:

First, the hard cap on core capital investment eligible for the F-Factor is based on the capital forecast presented in this proceeding, but in the end, it will be the actual plant additions that are entered into rates – whether planned or

unplanned. This approach results in the circumstances where the Company is providing upfront, during this proceeding, indicative revenue increases necessary to support those investments while committing to cap resulting revenue increases during the PBMRP even if actual capital investment exceeds the forecast. Additionally, the downward-only reconciliation of the Company's proposed F-Factor protects customers from the bill impacts associated with plant additions over the threshold, including necessary emergent, or unplanned investments unforeseen today.

Second, all capital plant additions, whether planned, unplanned, "Capital Plan" or "Non-Capital Plan," ultimately must pass PURA's prudence review before actual rate recovery of those specific projects costs may commence. This critical gate, successfully demonstrating prudence, is and should remain the ultimate determinant of recovery regardless of whether a particular investment was forecast in advance. Applying this test renders the distinction between Capital Plan and Non-Capital Plan items irrelevant.