



USAID
FROM THE AMERICAN PEOPLE



National
Association of
Regulatory
Utility
Commissioners

Performance Based Ratemaking: Pennsylvania

Robert Eckenrod

23 July 2008



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- “Chapter 30” Telecommunications Price Cap Regulation
 - In 1993, Pennsylvania Legislature adopted legislation adopted an alternative regulatory framework for telecommunications providers
 - Intended to
 - Provide a framework to ensure deployment of broadband capable infrastructure (such as fiber optics) in a timely manner
 - Ensures deployment of broadband services to areas that otherwise may not have access to such services (rural areas)
 - Attract new commerce to the state by providing a technologically friendly atmosphere



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- How was this to be achieved?
 - The law provided regulatory flexibility incentives to telecommunications companies who submitted network modernization plans to the Commission for review and approval
 - Upon approval of such plans, the companies were allowed to move to price cap regulation, with an annual inflationary adjustment which allowed rate to be adjusted annually up or down depending on changes in inflation less a productivity offset.
- Original law was to expire on December 31, 2003, but new law passed in 2004 which removed the productivity offset



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Therefore, in exchange for certain broadband service milestones over the life of the plan, a participating telecommunications provider could raise, or lower, its rates annually based on the rate of inflation.
- Must also meet minimum service quality benchmarks to ensure quality of service is not endangered in an effort to reduce costs.
- As a result of Chapter 30
 - All but several Pennsylvania telecommunications providers have elected this alternative form of regulation
 - Commitments to have 100% broadband deployment in place by 2015 for all providers electing alternative regulation



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Performance Based Ratemaking for the Electric Industry
 - Commission workgroup has considered how PBR could potentially be applied as a useful framework for cost recovery of Demand Side Response mechanisms deployed by electric distribution companies.
 - Demand Side Response mechanisms have been identified as a tool to enhance retail market competition in electricity within Pennsylvania
 - PBRs considered to provide incentives or disincentives to encourage regulated electric companies to meet Demand Side Response related objectives



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Three basic steps in designing and evaluating a PBR mechanism to apply
 - Articulating the goals to be achieved
 - Selecting the right structure to meet the goals
 - Getting the “numbers” right



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Articulating the goals to be achieved
 - PBR in this instance would involve providing incentives or disincentives to encourage regulated electric companies to meet Demand Side Response related objectives
 - The Commission would need to define specific objectives as part of any Demand Side Response related guidelines
 - Policy statement
 - Regulation



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Appropriate Structure
 - The structure of the PBR mechanism determines what incentives will be given
 - Broad based
 - Covers all or most costs under single structure
 - » Price caps generally better structure to utilize where there is a strong correlation between costs and volume
 - » Revenue caps generally appropriate where costs do not vary much with volume
 - Narrowly targeted
 - Covers the marginal cost to serve higher costs areas



USAID
FROM THE AMERICAN PEOPLE



N A R U C
National Association of Regulatory Utility Commissioners

Case Study: Performance Based Ratemaking in Pennsylvania

- Getting the numbers “right”
 - Essential to prevent windfall gains or losses
 - Assure long term viability of the PBR
 - Define what “right” means
 - What is the starting point?
 - How to measure inflation and productivity offset