Rethinking Ratemaking:
from settlement culture to public interest

Written testimony for the

Joint Public Hearing:
Oversight of the Public Service Commission's processes related to
rate case and generic proceedings

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INTRODUCTION

I'm Irene Weiser, coordinator of Fossil Free Tompkins (FFT), an all volunteer organization in Tompkins County that works to effect local and state policies and practices to end reliance on fossil fuels and enable a just and affordable transition to renewable energy resources. Since 2012, FFT has been an active party in many PSC proceedings including three NYSEG rate cases.

The purpose of this testimony is to raise concerns about the way confidential settlement negotiations have come to dominate our rate cases. Confidential negotiations are supposed to be an efficient method of ratemaking. But in practice, they undermine transparency, accountability, and fairness and can result in higher costs to ratepayers.

Below I provide an overview of the rate case process, the history of using confidential settlement in that process, and the problems that arise including the impact on affordability. Next, I identify both some quick fixes to improve the fairness as well as discuss pros and cons of some alternative approaches to ratemaking. I conclude with a recommendation to commission a "Blue Ribbon Panel" to evaluate best practices and chart a path forward in this complex and important area.

OVERVIEW OF THE RATE CASE PROCESS

A rate case starts when a utility company files a revenue request with the Public Service Commission (PSC) asking to raise or change the rates customers pay. That filing is built around a test-year, a 12-month lookback at the company's costs, revenues, and operations. Using this baseline, the utility projects how much money it will need in the coming year to cover expenses and earn its allowed rate of return. The test-year links past performance to the new 12-month forward revenue request, giving regulators and stakeholders a common reference point for evaluating whether the proposed rates are just and reasonable.

Once the utility makes that filing, the Department of Public Service (DPS) staff and stakeholder groups - consumer advocates, public interest and environmental non-profits, commercial and large load customers, unions, trade associations and municipal governments - review the company's request. Parties can ask the utility for detailed information, challenge its assumptions, and present their own testimony about whether the utility's proposed revenue increase is justified.

In theory, the case could then go to trial-like hearings, where an administrative law judge (ALJ) would hear testimony, weigh the evidence and recommend a decision for a one-year rate increase to the PSC Commissioners. But in practice, that almost never happens. Instead, after discovery, nearly all parties agree to enter into confidential settlement negotiations. Behind closed doors, the utility, DPS staff, and other parties hammer out a multi-year compromise agreement - called a Joint Proposal (JP) - that the ALJs and, ultimately, the Commissioners are asked to approve.

HISTORY OF THE USE OF SETTLEMENT IN NEW YORK

Before the 1980s, rate cases were litigated, not negotiated. The utility filed their one-year rate case, and after a period of discovery, DPS and consumer advocates challenged the details in trial-style evidentiary hearings. The ALJ overseeing the trial evaluated the evidence, and wrote a recommended decision that laid out the facts and rationale that Commissioners would review and rule on. That model assumed open evidence, cross-examination, and, when needed, separate prudence reviews of larger infrastructure projects that the utility had invested in for which reimbursement was sought. The process would take 11 months and in the 12th month, a year after the filing was submitted, a one-year rate increase would take effect. Immediately following, the utility would file a rate case for the following year. While effective at tightly regulating utility activities and costs, it was a very demanding and costly process.

By the late 1970s and early 1980s, parties began experimenting with negotiating compromises to avoid unnecessary litigation and perhaps most importantly, to develop muliti-year agreements, thereby reducing demand for financial and human resources. Seeing more of these deals, the PSC issued its first Procedural Guidelines for Settlements in January 1983 to give structure and guardrails.[1]

As settlements became increasingly common, the Commission opened a generic proceeding in 1990 to rethink the rules. That led to Opinion 92-2[2] (issued March 24, 1992), which adopted updated Settlement Procedures and Guidelines. From that point forward, settlement has no longer been ad-hoc; the guidelines define procedures for formal notice, participation, confidentiality, and review standards. Notably these 1992 settlement guidelines are still in effect, and codified in NYCRR[3] without revision, today.

In its 1992 materials, the PSC explained the assumptions and rationale for settlement proceedings:

- Save time and money vs. full litigation.
- Enable innovative regulatory approaches that parties can craft together.
- Protect participation rights (everyone who should be at the table must be notified and allowed in).

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[1] I am unable to find the original 1983 document referred to as Case 11175 – Procedural Guidelines for Settlement and Stipulations, issued January 19,1983. https://dps.ny.gov/system/files/documents/2023/12/guidance-documents-listing-as-of-11.30.23.pdf, however, the 1992 opinion, linked below, makes detailed references to the original 1983 settlement guidelines.

[2] PSC Opinion 92-2, Cases 90-M-0025 and 92-M-0138, Opinion, Order and Resolution Adopting Settlement Procedures and Guidelines, March 24, 1992 https://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId=%7B4DC4475E-AD4D-4A07-AC26-B7AAE863CEA7%7D

[3] Rules of Settlement Procedure 16 NYCRR Sec 3.9 https://www.law.cornell.edu/regulations/new-york/16-NYCRR-3.9

- Formalize confidentiality of negotiation substance.
- Keep Commission oversight: any deal must be supported by a record and be shown to be in the public interest (balancing ratepayers, investors, and the utility's long-term viability), and it must land within the range of what a litigated outcome could reasonably produce.

The 1992 guidelines also detail the standards by which settlements were to be evaluated. It states that "All Commission decisions, including those pertaining to proposed settlements must be - and appear to be - just, reasonable, and in the public interest."[4]

The elements considered in determining the public interest include:

1. consistency with the law and regulatory economic, social and environmental State and Commission policies;
2. whether the terms of the joint proposal compare favorably with the likely result of a fully litigated case and produce a result within the range of reasonable outcomes;
3. whether the joint proposal fairly balances the interests of ratepayers, investors and the long-term soundness of the utility; and
4. whether the joint proposal provides a rational basis for the Commission's decision.

Additionally, Commissioners are guided in their assessment by two additional factors: the completeness of the record, and whether the settlement is contested.

By the early 1990s, settlements were widespread, and in 1995 the Office of the State Comptroller published an audit that examined if the settlement guidelines were being followed, if the proceedings were sufficiently open to interested parties, and to determine whether settlement reduced the amount of staff time spent on rate proceedings.[5] They concluded that 1) guidelines were followed, that 2) the process was sufficiently open to interested parties and that 3) while there was no system in place to track staff hours, the fact that negotiations resulted in multi-year settlements meant less frequent filings and therefore less burden on staff. The OSC commented that "no generalizations should be drawn from this report about the appropriateness of the resulting negotiated rates."

To our knowledge, no audits have been conducted to determine the extent to which settlement agreements have satisfied the elements of the public interest, nor to evaluate the appropriateness of the resulting negotiated rates. However, there are many critiques in the literature, as well as our own experience in rate proceedings that can inform such analysis.

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[4] *Ibid,* p 30-32

[5] Public Service Commission Use of Negotiated Settlements in the Ratesetting Process. Office of the State Comptroller, Division of Management Audit, Report 94-S-12, https://web.osc.state.ny.us/audits/audits/94s12.pdf

PROBLEMS WITH SETTLEMENT NEGOTIATIONS

There are significant problems that arise with settlement proceedings - even when nothing is confidential - that do not serve the public interest.

Power imbalances. Settlement discussions are not negotiations among equals. Utilities arrive with armies of lawyers, consultants, and technical experts—costs they pass on to ratepayers. DPS Staff have expertise, but they are stretched thin and under pressure to settle quickly. Public-interest groups have very limited resources, limited access to data, and often face intimidation or disparagement. They may have to fight just to get their concerns on the agenda, or be coerced to sign agreements they largely oppose to secure a token win. For many groups, the barriers are so high that participation is effectively closed off. The result: the best-resourced parties wield disproportionate influence.

This imbalance is sharper in New York because we lack a strong, independent Consumer Advocate. At least 40 states and territories have such offices. Unlike DPS Staff—whose duty is to ensure just and reasonable rates *while also safeguarding the utility's fiscal integrity*—a Public Advocate's sole responsibility is protecting the public interest.

New York also fails to provide intervenor funding, which in other states enables public-interest groups to hire consultants and/or attorneys to effectively represent their constituencies in rate cases.

Information Imbalances. Utilities hold a distinct advantage because only they have full knowledge of the conditions and limitations of their systems. While DPS Staff make efforts through discovery to obtain relevant information, utilities can - and sometimes do - withhold or mischaracterize data. This can leave other parties with an incomplete or misleading picture of whether an infrastructure project is truly essential.

Pressures of Time and Resources. Settlement negotiations are also shaped by the law of diminishing returns. The longer negotiations continue, the more pressure parties feel to reach *some* agreement, since shifting to litigation would entail even greater delays and costs. Parties may capitulate simply from financial or human resource exhaustion.

Compromise versus Public Interest. Compromise is often assumed to be a virtue of negotiation, but it is not synonymous with serving the public interest. In settlement discussions, concessions are exchanged to reach agreement—but there is no guarantee that what is given up aligns with ratepayer protections or long-term policy goals.[6] Moreover, strategic overstatement is a well-known tactic: utilities may originally ask for more than they reasonably expect to be awarded in order to create the appearance of compromise, skewing outcomes in their favor.

[6] 2017, Scot Hempling *The Public Interest - Who has a definition*? https://scotthemplinglaw.com/wp-content/uploads/2021/11/The-Public-Interest-Who-Has-A-Definition.pdf

Negotiating Public Policy. Certain issues should not be left to negotiation at all. Public policy—such as the temperature thresholds for utility shutoffs, or the implementation of actions mandated under the Climate Leadership and Community Protection Act—should be determined through transparent rulemaking or legislation, not as bargaining chips in confidential settlement rooms.

PROBLEMS WITH CONFIDENTIALITY

The PSC's Settlement Guideline set strict rules for maintaining confidentiality of settlement negotiations:

> **Confidentiality of settlement discussions**. No discussion, admission, concession or offer to stipulate or settle, whether oral or written, made during any negotiation session concerning a stipulation or settlement shall be subject to discovery, or admissible in any evidentiary hearing against any participant who objects to its admission...The Administrative Law Judge assigned to the case…may impose appropriate sanctions for the violation of this subdivision which may include exclusion from the settlement process.[7]

It is easy to see how such rules of confidentiality exacerbate existing problems in settlement talks. Once discussions are cloaked in secrecy, none of the concerns arising during negotiations can later be raised in evidentiary hearings to demonstrate that the JP may not, in fact, serve the public interest.

Fossil Free Tompkins encountered this very predicament in the 2022 NYSEG/RGE rate case. In our Post-Hearing Brief[8], we highlighted serious problems stemming from the sweeping use of confidentiality in the evidentiary hearing:

- **Burden of proof undermined.** Settlement guidelines require documentation as rigorous as a litigated rate case. Yet the JP lacked cost justifications for hundreds of millions in infrastructure investments. The ALJs ruled that confidentiality barred access to evidence explaining how Staff's original objections were resolved.

- **Discovery gaps concealed.** DPS Staff initially testified that NYSEG/RGE filings were vague and inconsistent. They later claimed confidential negotiations had "cured" these deficiencies, but the details remained hidden under confidentiality rules.

[7] 16 NYCRR 3.9(d)
[8] PSC Case 22-E-0317, NYSEG Rate Case, Fossil Free Tompkins Post Hearing Brief (Aug 4, 2023) https://documents.dps.ny.gov/public/Common/ViewDoc.aspx?DocRefId={A038C289-0000-CC34-AA13-D9BA0B2D14CF}

- **Cross-examination obstructed.** When FFT questioned cost justifications, objections were sustained because responses depended on confidential settlement discussions.

- **Public interest compromised.** Information critical to evaluating project costs, justifications, and Staff's shift from opposition to support was inaccessible, preventing any transparent assessment of the JP.

In short, confidentiality allowed settlement deals to bypass evidentiary scrutiny, making it impossible for outside parties—or the public—to test whether the agreements truly served the public interest.

Once a JP is published, DPS Staff and ALJs regard it as *de facto* in the public interest. During evidentiary hearings, stakeholders are warned that they cannot challenge individual elements because the JP is considered a carefully crafted interdependent whole. The effect is unmistakable: the hearing becomes largely performative, and the agreement stands. Similarly Commissioners are reluctant to alter JPs, since modifications would trigger the need for renewed settlement negotiations with all parties to seek consent to the new agreement.

Scott Hempling terms this hands-off approach "regulation by settlement". His warnings about it are worth quoting in their entirety:

> A settlement culture can induce regulatory passivity: the less they get into the parties' business, the less they (a) engage mentally, (b) learn about the regulated businesses, (c) gain confidence, and (d) lead objectively. A stance of "let's see what the parties say" leads to "let's see what the parties want" and, ultimately, "who are we to stand in the way of their deal?" There is a risk of atrophy: muscles unused become muscles less able. This spiral points downward: as the commission becomes less engaged and less alert, it becomes less respected and less relied upon, leading to more settlements and more atrophy.[9]

Settlement Agreements and Affordability

Finally, and perhaps not surprisingly in light of the foregoing discussion, there is evidence that confidential settlement agreements are more profitable for utilities. A January 2023 S&P Global Market Intelligence review of over 1350 rate case settlements across the country found that settled cases achieved 6% higher returns than did litigated cases. Similarly, settled cases resulted in 0.35% higher ROE paid to the utilities.

[9] Scott Hempling, *Regulatory Settlements: When do private agreements serve the public interest?* Energy Regulation Quarterly, Volume7, Issue 3, 2019

Quick, Necessary Reforms

Certain improvements can and should be implemented as soon as practical to help restore level the playing field and ensure that proceedings more effectively serve the public interest:

- **Restore an independent Office for Utility Public Advocacy.** New York once had a consumer protection board to represent the interests of ratepayers, but today relies on the Department of State's Utility Intervention Unit, which lacks the resources required to handle the amount and complexity of the work[10]. At least forty states and territories maintain well-funded consumer advocate offices. New York should do no less.

- **Provide intervenor funding.** Many states offer intervenor compensation so that public-interest organizations can secure the technical and legal expertise needed to participate effectively in rate cases. Without it, the playing field remains tilted toward utilities with far greater resources.[11]

- **Hire and train more DPS staff.** Over the past two decades, DPS has faced significant staffing cuts even as its workload has grown. Today's rate cases are more complex than ever, involving not only traditional revenue needs but also climate planning, electrification, and grid modernization. The Department must be properly resourced to carry out its statutory responsibilities.

- **Require DEC participation in rate cases.** To ensure that New York's Climate Leadership and Community Protection Act is not undermined in the ratemaking process, the Department of Environmental Conservation should participate directly in relevant proceedings.

- **Take ROE off the negotiating table.** Return on Equity should be determined through a transparent formula or an evidentiary hearing—not through closed-door negotiations. ROE goes to the heart of utility profits and public costs and should be subject to independent scrutiny.

- **Use independent mediators in settlement talks.** Rather than leaving settlement negotiations under the control of the Utility, a neutral mediator should be appointed to manage discussions and ensure fairness among parties.

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[10] 2020, *The increasingly complex role of the Consumer Advocate*, Elin Swanson Katz and Tim Schneider, Energy Law Journal, Volume 41:1
https://www.eba-net.org/wp-content/uploads/2023/02/5.-Katz-SchneiderFinal1-21.pdf .
[11] NARUC State Approaches to Intervenor Funding, Dec 2021
https://pubs.naruc.org/pub/B0D6B1D8-1866-DAAC-99FB-0923FA35ED1E

- **Review and update PSC Settlement Guidelines.** The current framework, issued decades ago, no longer reflects the complexity of modern utility regulation or the requirements of the Climate Act. A thorough update is overdue.

- **Require commissioner attendance at evidentiary hearings.** At least three Commissioners should attend evidentiary hearings to hear testimony directly. Reliance on transcripts strips away tone, emphasis, and off-the-record clarifications, weakening the Commission's ability to judge credibility and weigh the public interest.

Rethinking the Ratemaking Process

Before turning to specific reforms, I want to emphasize caution. Ratemaking is an extraordinarily complex undertaking, involving billions of dollars of ratepayer costs and it is deeply intertwined with our state's economic, social, and climate objectives. The temptation to respond quickly with legislative "fixes" should be resisted. As Alvarez, et. al., caution:

> utility regulation through state legislation too often results in a reduction of regulator authority and independence … typically ending badly for both customers and shareholders.[12]

When legislatures bypass regulators or dictate investment structures, they often unintentionally eliminate cost disallowance risk, shift financial burdens to customers, and encourage uneconomic spending. Further, Alvarez notes, it is difficult to undo legislation once it is enacted.

However, the real challenge is larger than simply adjusting the mechanics of settlement negotiations. As Scott Hempling argues in *The Regulatory Mission*[13] Utility regulation is not just about balancing interests within the existing framework, but about redefining the regulator's role itself: moving from passive arbiter toward active architect of the public-interest outcomes our economy and climate demand. This broader rethinking should be part of any serious reform process.

Notwithstanding this advice, here are some options that might be considered:

- Keep settlement but end most confidentiality (except for trade secrets). This would improve transparency and allow more meaningful evidentiary review, though it could reduce parties' willingness to compromise.

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[12] Alvarez, P., Stephens, D., & Ericson, S. (2021). Utility Regulation Through Legislation: A Cautionary Tale for Legislators, Regulators, Stakeholders, and Utilities: Article No. 107005. *Electricity Journal*, *34*(8). https://doi.org/10.1016/j.tej.2021.107005

[13] Hempling, S. The regulatory mission. November 2008 https://scotthemplinglaw.com/wp-content/uploads/2021/11/The-Regulatory-Mission.pdf

- End settlement negotiations and rely on evidentiary hearings (annual or multiyear). Annual hearings create a clear, testable record but are resource-intensive. On the other hand, there are financial risks with multiyear rate plans.

- Reintroduce prudence reviews (as used before the 1980s as part of ratemaking), where utilities spend first and must prove expenditures were necessary and cost-effective before rate recovery. This shifts risk to shareholders instead of ratepayers.[14]

- Adopt a hybrid model, litigating routine costs over multi-year horizons while subjecting large infrastructure projects to annual prudence reviews. This targets scrutiny where it is most needed but adds procedural complexity.

- Explore performance-based ratemaking (PBR), tying earnings to policy outcomes rather than capital investment. This aligns incentives with climate and customer goals, but requires careful metric design to avoid gaming.

Final Recommendation

Given the magnitude of ratepayer exposure, the growing complexity of utility responsibilities under the Climate Act, and the risks of unintended consequences, I recommend convening a blue-ribbon panel of experts—as New York did after Superstorm Sandy. This panel should not only weigh the relative merits of different forms of ratemaking, but also examine the broader question of regulatory mission: how to design institutions that ensure affordability, accountability, climate compliance, and reliable service in our rapidly changing energy ecosystem.

[14] Paul J. Alvarez, Dennis Stephens, Kenneth W. Costello, Sean Ericson, Alternative ratemaking in the US: A prerequisite for grid modernization or an unwarranted shift of risk to customers?, The Electricity Journal, Volume 35, Issue 9, 2022, https://doi.org/10.1016/j.tej.2022.107200