

ORDER NO. 88324

IN THE MATTER OF THE PETITION OF *
WASHINGTON GAS LIGHT COMPANY *
FOR APPROVAL OF REVISED TARIFF *
PROVISIONS TO FACILITATE ACCESS TO *
NATURAL GAS IN THE COMPANY’S *
MARYLAND FRANCHISE AREA *
CURRENTLY WITHOUT NATURAL GAS *
SERVICE *
_____ *

BEFORE THE
PUBLIC SERVICE
COMMISSION
OF MARYLAND

CASE NO. 9433

Issue Date: August 1, 2017

On December 7, 2016, the Washington Gas Light Company (“WGL” or “Company”) filed with the Maryland Public Service Commission (“Commission”) a Petition for Approval of Revised Tariff Provisions to Facilitate Access to Natural Gas in Areas within the Company’s Maryland Franchise Area that are Currently without Natural Gas Service (hereinafter the “Petition”).¹ In its Petition, and as amended by subsequent filings, the Company asks the Commission to approve changes to its tariff provisions² that would authorize three independent, proposed service initiatives: 1) a Contribution Payment Plan (“CPP”) to facilitate the financing of extending gas facilities to homes and businesses; 2) a Targeted Conversion Plan (“TCP”) to lower the customer commitment threshold for converting groups of customers to natural gas; and 3) a Gas Access Program (“GAP”) to facilitate the extension of backbone infrastructure into unserved areas

_____ ¹ Case Item No. 1.

² The proposed changes to WGL’s tariff – General Service Provision (GSP) No. 14 – are found in Petition Exhibit 1.

designated by counties and municipalities for certain types of development, and permit WGL to establish a regulatory asset for certain associated transmission and main expenditures. For the reasons that follow, the Commission denies each of the three proposed service initiatives in WGL’s Petition, without prejudice.

I. BACKGROUND

A. Procedural History

On December 22, 2016, the Commission initiated this proceeding, setting an intervention deadline of January 18, 2017, ordering discovery to commence immediately for WGL, Commission Staff (“Staff”), and the Office of People’s Counsel (“OPC”), suspending the proposed tariff for 150 days under § 4-204 of the Public Utilities Article of the Maryland Annotated Code (“PUA”), and directing WGL to provide certain notices concerning these proceedings and how to intervene.³ On February 1, 2017, the Commission established further procedures and deadlines for discovery as well as a procedural schedule and ordered a 30-day extension of the suspension period for the tariff under § 4-204(b)(2)(ii).⁴ The parties to the matter are WGL, Staff, OPC, the Apartment and Office Building Association of Metropolitan Washington (“AOBA”), and jointly the Mid-Atlantic Petroleum Distributors Association, Inc. and the Mid-Atlantic Propane Gas

³ Case Item No. 2.

⁴ Case Item No. 12.

Association, Inc. (“MAPDA-MAPGA”) (collectively, the “Parties”).⁵

In support of its Petition, WGL filed the direct testimony of Paul S. Buckley, Director of Regulatory Strategy and Advocacy for WGL, as Exhibit 2, and the direct testimony of Paul H. Raab, an independent economic consultant, as Exhibit 3.⁶

On March 1, 2017, MAPDA-MAPGA submitted the direct testimony of James S. Wilson, an economist and independent consultant; AOBA submitted the direct testimony of Bruce R. Oliver, President of Revilo Hill Associates, Inc.; and OPC submitted the direct testimony of Allen R. Neale, a consultant working in conjunction with Daymark Energy Advisors.⁷ On March 2, 2017, Staff submitted the direct testimony and exhibits of: Jason A. Cross, Assistant Director of the Division of the Telecommunications, Gas and Water Division; Jamie A. Smith, Director of the Accounting Investigations Division; and Matthew Bonikowski, a Regulatory Economist in the Energy Analysis and Planning Division.⁸

On March 17, 2017, WGL filed a Motion to Compel MAPDA-MAPGA to respond to data requests relating to MAPDA-MAPGA members’ propane and fuel oil storage and delivery costs and their cost recovery methods, including basic fuel storage

⁵ On February 9, 2017, MAPDA-MAPGA filed a petition to intervene out-of-time, to which the Commission afforded an opportunity to respond. Case Item Nos. 13 and 14. On February 23, 2017, WGL opposed MAPDA-MAPGA’s petition to intervene in part, stating that although they should not be allowed to participate as a representative of commercial customers or a separate class of commercial customers, WGL would not oppose their participation as a “competitive party.” Case Item No. 16. On February 24, 2017, MAPDA-MAPGA responded, arguing that they should be granted full party status on all issues relevant to the instant proceeding. Case Item No. 17. On March 7, 2017, the Commission granted MAPDA-MAPGA’s petition to intervene out-of-time, without limitation. Case Item No. 24.

⁶ Case Item No. 1.

⁷ Case Item Nos. 18, 19, and 20.

⁸ Case Item No. 21.

data⁹ and more granular cost recovery data.¹⁰ On March 21, 2017, MAPDA-MAPGA filed a reply opposing WGL's Motion, on the grounds that the information sought was not relevant and was overly burdensome, and that the information responsive to the data requests was not in the possession, custody or control of either party -- MAPDA or MAPGA -- but rather was in the possession of their members, over which they had no authority to demand the information.¹¹ On April 3, 2017, the Commission issued Order No. 88102, granting WGL's request for the more basic fuel storage data, because it "should be discernable by MAPDA-MAPGA and is the type of information that persons knowledgeable about the propane and fuel oil business should be able to supply."¹² But the Commission denied the requests for more granular, member-specific data, finding that the information sought was not within MAPDA or MAPGA's possession, custody, or control, and that the burden of collecting it outweighed the information's likely probative value.¹³

On March 24, 2017, WGL filed the rebuttal testimony and exhibits of Paul S. Buckley and Paul H. Raab,¹⁴ and OPC filed the rebuttal testimony of Allen R. Neal.¹⁵ On April 13, AOBA filed the surrebuttal testimony of Bruce R. Oliver;¹⁶ OPC filed the

⁹ The more basic data requests asked that "for each of the supplied addresses, below, please provide a confirmation that the large tanks are fuel storage facilities, the size of each container, the type of fuel stored." Case Item No. 29 at 3.

¹⁰ Case Item No. 25. The more granular data requests were for information "regarding the original cost and remaining net book value and how the cost is recovered from customers" and propounded eleven specific factual inquiries directed at individual members, "such as number of customers, number of trucks, and specific financial information." Case Item No. 29 at 2-4.

¹¹ Case Item No. 26.

¹² Case Item No. 29 at 3.

¹³ *Id.* at 3-4.

¹⁴ Case Item No. 28.

¹⁵ Case Item No. 27.

¹⁶ Case Item No. 30.

surrebuttal testimony of Allen R. Neale;¹⁷ and Staff filed the surrebuttal testimonies of Jason A. Cross, Jamie A. Smith, and Matthew J. Bonikowski.¹⁸

On April 28, 2017, under § 3-104 of the PUA, the Commission designated a panel of Chairman Hughes, Commissioner Richard, and Commissioner O'Donnell to conduct all further proceedings, including the evidentiary hearings.¹⁹ On May 1 and 2, 2017, the evidentiary hearings were held for cross-examination of witnesses. The Parties filed initial post-hearing briefs on June 9, 2017,²⁰ and post-hearing reply briefs on June 30, 2017.²¹

B. Summary of WGL's Proposed Tariff Changes

WGL requests Commission approval to revise one of its tariffs – GSP 14 – to authorize three programs designed to expand natural gas access to unserved or underserved parts of WGL's Maryland service territory. WGL's tariff GSP 13 states that for requested new gas service facilities, WGL will install gas service pipe and connections from the main to the meter, and that the service applicant must pay for any contribution determined after an economic test under GSP 14. The economic test evaluates the difference in net present value (“NPV”) between the life cycle revenue over 30 years and the life cycle cost over 30 years. If the difference is negative, the customer pays it; if it is positive, no payment is required. WGL owns all of the assets that are installed.

¹⁷ Case Item No. 32.

¹⁸ Case Item No. 31.

¹⁹ Case Item No. 34.

²⁰ Case Item Nos. 39-43.

²¹ Staff filed a letter in lieu of a reply brief. Case Item No. 45. MAPDA-MAPGA did not file a reply brief.

1. CPP

To establish the first program, the Contribution Payment Plan, WGL proposes to revise GSP 14 to allow new residential customers to "finance" line extensions, in lieu of paying a customer contribution up-front, by paying a fixed amount of \$40 per month for up to 20 years, with the right to pay the balance in full at any time. The new customer would still have to pay up-front any contribution amount in excess of the amount that may be recovered over 20 years. New commercial customers would be eligible to participate under the same terms, except that the fixed monthly contribution would be \$100. For all CPP customers, WGL would assess the service address, and all future customers at that address would be required to acknowledge and accept this obligation (in advance) in order to receive service. Notice of the CPP obligation would be provided to future customers via three forms: (1) disclosure on the Maryland Realtor standard Sales Contract (aka "Zip Form"); (2) notification in the Company's tariffs; and (3) customer educational materials.²² CPP costs would go into WGL's rate base and remain there unless and until they are offset by contributions received from CPP customers.²³ WGL also indicated that it would be willing to limit the size of the CPP program to \$2.5 million of residential customer contributions annually, and \$2 million of commercial customer contributions annually, as well as limit the duration of the initial CPP program to a certain number of years.²⁴

²² WGL Initial Brief at 7.

²³ *Id.*

²⁴ *Id.* at 7-8.

2. TCP

WGL's second proposed program is a Targeted Conversion Plan that would allow customers in certain "target areas" to more easily obtain new service for their areas through lower customer contribution amounts.²⁵ To authorize the TCP, WGL would revise the economic test under GSP 14 to allow WGL to assess anticipated life cycle revenues once twenty percent (20%) of a target area commits to convert to natural gas, but the test would assume that sixty percent (60%) of the area's customers had committed, meaning that the customers could commit the area to natural gas by making a lower contribution.²⁶ WGL expects that, once service is extended for an area, over a long-term period, a "60% penetration rate for conversions is realistic and achievable."²⁷ The unpaid contribution for the portion of the project that is not assessed to customers would go into rate base.²⁸ WGL indicated its willingness to cap the size of the TCP at \$2 million in annual capital expenditures, which would allow the conversion of approximately 500 homes per year.²⁹ WGL also supports limiting the duration of the initial TCP program to a certain number of years.³⁰

3. GAP

WGL's third proposal would amend GSP 14 to authorize WGL to extend backbone infrastructure into unserved areas without using the economic test if the infrastructure terminates in a Tier 1 or Tier II area as set forth in § 1-508 of the Land Use

²⁵ Direct Testimony of Jason A. Cross ("Cross Direct") at 23-24.

²⁶ *Id.*

²⁷ WGL Initial Brief at 9.

²⁸ Cross Direct at 25-26.

²⁹ WGL Initial Brief at 10.

³⁰ *Id.* at 7-8.

Article of the Maryland Annotated Code.³¹ All customers would pay for the costs of the backbone infrastructure, and WGL would create, with Commission approval, a regulatory asset to defer the future collection of associated property taxes, carrying costs and depreciation of qualifying expenditures in rates. The amount of GAP investment that could be deferred each year would not exceed one half of one percent (0.5%) of the Company's net rate base as determined in its last rate case, which under the current rate base would amount to approximately \$3.3 million annually.³² This means that the total GAP program expenditures would be capped at \$23.3 million per year.³³ WGL also supports limiting the duration of the initial GAP program to a certain number of years.³⁴ The amended GSP 14 also would require annual reports for GAP projects that describe constructed projects and summarize costs.

C. Positions of the Parties

1. AOBA's Position

AOBA opposes all three of WGL's proposals to expand its natural gas service -- as full scale or pilot programs -- because it asserts the proposals each allegedly contain material deficiencies that warrant rejection. AOBA argues that the instant Petition procedurally amounts to a back-door attempt by WGL to resuscitate legislative proposals that were previously rejected by the Maryland General Assembly. Substantively, AOBA contends the proposals unfairly and unnecessarily transfer the risks associated with the Company's efforts to expand its gas service system from its shareholders to its Maryland

³¹ State and local officials target Tier 1 and 2 communities for promoted, planned growth. *Id.* at 11.

³² *Id.* at 11-12.

³³ *Id.* at 12.

³⁴ *Id.* at 7-8.

customers.³⁵ AOBA objects to WGL insulating its shareholders in this manner, especially when substantial risks arise from financially questionable projects.³⁶ Thus, AOBA recommends that the Commission reject all three proposals.

AOBA specifically disapproves of WGL's CPP proposal on the basis of a number of infirmities.³⁷ First, AOBA states the CPP incorporates comparatively high costs of financing over the entire period in which new customers would make monthly CPP payments. AOBA argues that while most creditworthy customers can find lower costs of financing through banks or other lending sources, allowing less creditworthy customers to take advantage of the CPP plan will shift the cost recovery risks associated with default from the Company to ratepayers.³⁸ Additionally, whereas WGL proposes to include CPP costs in the Company's rate base, AOBA argues that this would effectively increase the overall costs paid by all of WGL's existing Maryland customers.³⁹ Second, AOBA argues that the CPP fails to properly assess the economics of conversion to natural gas service, omitting the consideration of any behind-the-meter costs that a residential customer would have to incur in order to convert. Third, AOBA criticizes WGL for failing to provide the terms of its CPP customer commitment agreement for Commission review. Fourth, AOBA finds problematic the attachment of the CPP payment obligation to the service address and not to the customer who initiates the program with WGL.⁴⁰ According to AOBA, there is no assurance that a subsequent

³⁵ AOBA Initial Brief at 3.

³⁶ *See id.*; Direct Testimony of Bruce R. Oliver ("Oliver Direct") at 5.

³⁷ AOBA Initial Brief at 8-9.

³⁸ Oliver Direct at 12.

³⁹ *See* AOBA Initial Brief at 10.

⁴⁰ *Id.* at 11-14.

property owner will be aware of any outstanding CPP obligation let alone agree to take on the remaining payment obligations.⁴¹ Lastly, AOBA objects to the Company's "one-size-fits-all" approach to structuring its CPP proposal for commercial customers where, unlike residential accounts, gas use- and billed-charges are much greater.⁴²

AOBA objects to WGL's TCP proposal because the Company fails to provide any assurance that it will actually achieve the assumed 60% "targeted customer group" participation. AOBA further argues the TCP proposal fails to identify a timeframe for achieving the required 60% participation, which calls into question the calculations on which approval of a TCP project would be premised.⁴³ Furthermore, AOBA challenges the reasonableness of WGL's 60% conversion forecast, arguing that an analysis of WGL's conversion data reveals a substantial lag in the achievement of the Company's assumed penetration level in prior conversion projects.⁴⁴

Finally, AOBA recommends rejection of the GAP proposal because contrary to traditional ratemaking principles for regulatory asset treatment, WGL has not specified the costs that the Company will incur to expand its gas distribution system. Furthermore, the Company has not provided any economic criteria for assessing the reasonableness of those undecided costs.⁴⁵ AOBA contends that before GAP costs can be accepted for regulatory asset treatment, the Commission should: 1) first review the economics of each GAP project in advance of construction; 2) determine the dollar amount that is economically justified based on its review; and 3) address any uncertainties regarding

⁴¹ *Id.* at 13.

⁴² *Id.* at 14-15.

⁴³ *Id.* at 15-17.

⁴⁴ *Id.* at 17 (citing Surrebuttal Testimony of Bruce R. Oliver at 9).

⁴⁵ *Id.* at 18-19.

anticipated customer additions as well as the risk bearers associated with those uncertainties.⁴⁶

2. MAPDA-MAPGA's Position

In its Initial Brief, MAPDA-MAPGA argues that the Commission should reject all three of WGL's proposed tariff changes because they do not result in just and reasonable rates. MAPDA-MAPGA argues that the programs require subsidies from one group of customers to another and distort inter-fuel competition. Because potential natural gas customers may pay less to obtain natural gas service under the proposed programs, MAPDA-MAPGA maintains that WGL's programs would harm unregulated participants in the competitive fuel industry, who are unable to provide service and then recover costs in the same manner.⁴⁷ MAPDA-MAPGA further emphasizes that the Maryland General Assembly's decision not to pass legislation enabling similar programs is another reason for the Commission to reject the proposed tariff changes.⁴⁸

MAPDA-MAPGA argues that WGL could already proceed with projects that would qualify under the proposed programs, but does not because they are uneconomic and therefore the Company seeks to change Commission policy so that existing ratepayers must bear the associated costs and risks. MAPDA-MAPGA further states that WGL's proposed programs run contrary to principles cited in Order No. 78817, in which the Commission authorized WGL's current tariff and noted the merits of: connecting cost causation and responsibility, preventing cross-subsidies from existing customers,

⁴⁶ See *id.* at 19-20 (citing Oliver Direct at 28-29).

⁴⁷ MAPDA-MAPGA Initial Brief at 4.

⁴⁸ *Id.* at 4-5.

protecting existing ratepayers, and using a realistic and accurate economic test to evaluate proposed extensions.⁴⁹ Specifically, MAPDA-MAPGA points out the high interest rate and return on investment WGL would receive under the CPP, even though the risk of under-collection would be borne by ratepayers.⁵⁰ Moreover, because of that allocation of risk, MAPDA-MAPGA maintains that WGL would have no incentive to ensure that purchasers of houses that are subject to a CPP charge actually pay it.⁵¹ Additionally, MAPDA-MAPGA criticizes the TCP for not conforming to principles of economic expansion, arguing that the TCP: is speculative, could result in uneconomic extensions even when all customers eventually sign up, could result in potential customers minimizing customers contributions, does not incentivize adding customers beyond the threshold 20%, and forces existing customers to bear the risks of those possible shortcomings.⁵² MAPDA-MAPGA also maintains that the GAP would result in existing ratepayers subsidizing the expansion of natural gas, including for uneconomic projects, without receiving their benefit.⁵³ Furthermore, MAPDA-MAPGA observes that Tier I and II areas are not necessarily designated for growth.⁵⁴

3. OPC's Position

In its Initial Brief, OPC recommends rejection of all three amendments to WGL's tariff as well, arguing that current tariff provisions better protect existing ratepayers from uneconomic expansions of service. OPC also opposes the CPP, TCP, and GAP-related

⁴⁹ *Id.* at 7.

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.* at 8.

⁵³ *Id.* at 9.

⁵⁴ *Id.*

tariff changes on a pilot basis, because regardless of the scope of the programs, OPC's underlying concerns remain.

OPC maintains that the CPP imposes an unreasonable rate recovery risk, because if any portion of the customer contribution is not paid in full, WGL customers must (after paying an incremental rate of return throughout the payback period) pay the return and depreciation on it. OPC questions the adequacy of WGL's plans to address obligations on future property owners, as well as WGL's assessment of program participation and the relative risks for existing customers and the Company. OPC emphasizes that the "easy terms" WGL would offer – i.e., a higher interest rate than comparable lenders without a credit check or personal liability on a deferred balance – will attract customers who may not want to commit available credit or have a higher risk of default, which would shift additional program risks onto existing customers.⁵⁵

OPC argues that WGL's TCP proposal imposes an unjustified obligation on existing ratepayers to pay for neighborhood conversions that do not achieve a participation level of at least 60%. Because existing ratepayers, and not WGL, are responsible for build-out costs unless and until a 60% threshold is achieved, OPC maintains that WGL has little incentive to seek conversions beyond the initial 20% participation requirement.⁵⁶ Moreover, OPC notes that there is no deadline for when a 60% threshold must be reached, and that many customers may subsidize outstanding customers and no longer be a customer when the 60% threshold is achieved.⁵⁷

⁵⁵ OPC Initial Brief at 8-9.

⁵⁶ *Id.* at 10.

⁵⁷ *Id.* at 10-11.

OPC opposes WGL's GAP proposal because it comes with even fewer protections for ratepayers, and because under its proposal WGL can undertake backbone infrastructure projects without changing its tariff. OPC observes that although revenues could eventually offset or minimize the costs deferred under a regulatory asset, those outcomes are difficult to predict and dependent on extrinsic factors like population growth around a particular project.⁵⁸ OPC maintains that this is especially problematic because WGL will be entitled to full recovery of its deferred costs by simply showing that its projects end in a Tier I or Tier II area, regardless of whether the plant is fully used and useful.⁵⁹ OPC also questions WGL's need for the GAP because some counties have not adopted a Tier system and will still see system expansion, and because WGL has identified a GAP pilot project that is already NPV-positive under WGL's existing tariff.⁶⁰

OPC supplements its project-specific arguments with several objections to WGL's general case. For instance, OPC claims that WGL overstates the environmental benefits of natural gas, because WGL's analysis does not reflect the benefits of existing and future renewables and cleaner sources of generation, overstates emission reductions levels by pegging natural gas customer use exclusively to "non-baseload" sources of electric generation, and ignores other public policies and cost reduction that will or may lead to future emissions reductions for consumers of electricity.⁶¹ OPC also claims that WGL overstates residential customer savings for natural gas conversions by using outdated and misleading fuel price information, ignoring the costs of new gas appliances

⁵⁸ *Id.* at 12.

⁵⁹ *Id.* at 13.

⁶⁰ *Id.* at 13-14.

⁶¹ *Id.* at 15-16.

and associated home improvement work, and failing to consider how electric customers may absorb the costs of maintaining distribution infrastructure amidst a smaller base of customers.⁶² Finally, OPC maintains that existing customers should not have to further cross-subsidize new customers, who benefit from STRIDE investments that provide ongoing benefits paid for by existing customers.⁶³

4. Staff's Position

Staff also recommends rejection of WGL's proposals because as filed, Staff asserts, they would expose existing ratepayers to potentially adverse effects of undue subsidization (of new customers) and excess shifting of risk.⁶⁴ Staff argues that the Commission should reject the CPP proposal because WGL failed to adequately address questions related to transfers in ownership of CPP-bound property. Staff opposes the TCP proposal because the potential TCP-related benefits are insufficient to offset the inherent shifts in cost recovery risk from new customers to existing customers. Staff disapproves of the GAP proposal because the pilot project identified by WGL is NPV-positive and thus already authorized under the Company's tariff.⁶⁵

At the outset, Staff states that while CPP payments would be used to offset the Company's rate base, there remains a potential for default, especially where CPP could be used by customers of limited credit.⁶⁶ Of greater import to Staff, however, is that WGL has not sufficiently addressed concerns raised by the Commission in Order No. 85858, regarding transfers in ownership of encumbered property and the adequacy of

⁶² *Id.* at 17-18.

⁶³ *Id.* at 19-20.

⁶⁴ Staff Initial Brief at 5.

⁶⁵ *Id.*

⁶⁶ *Id.* at 12.

notifying any subsequent purchaser of property of the related payment obligations.⁶⁷ According to Staff, WGL has not adequately resolved those concerns here. Despite WGL's assurance that it would include the CPP proposal in standard Maryland real estate contracts, Staff contends there is no certainty that WGL can accomplish this or that WGL has demonstrated any preliminary work in this regard. Furthermore, Staff argues that mere inclusion of the CPP proposal in the Company's tariff would provide, at most, constructive notice and would not provide sufficient actual notice.⁶⁸

Staff similarly does not support the TCP proposal. Because the TCP assumes that for every two initiating participants WGL incorporates the future income stream of six participants, Staff reasons that the cost of expansion is lowered for each of the two initiating participants. Accordingly, Staff argues that as much as 40% of the allotted costs would shift to existing ratepayers if the remaining four customers are not added.⁶⁹ Staff is further concerned that WGL's 60% targeted conversion rate may not be appropriate. Staff contends that WGL's own 2014 study of conversions achieved in 13 neighborhoods in Virginia and Maryland reveals that 40% of those neighborhoods did not attain 60% conversion and those that reached 60% saturation did so at a slow pace. Staff argues that the Company's proposed 20% test for the TCP would have the undesired effect of driving up rates for existing customers for lack of a sufficient user base over which to spread infrastructure costs.⁷⁰

⁶⁷ See *id.* at 11-12.

⁶⁸ *Id.* at 13.

⁶⁹ *Id.* at 14.

⁷⁰ See *id.* at 14-16.

Lastly, Staff recommends that the Commission reject the GAP proposal insofar as the identified GAP pilot project is already NPV-positive. Staff explains that under the current tariff, WGL is authorized to receive full cost recovery for the identified project.⁷¹ According to Staff, the GAP program would allow WGL to circumvent the economic test under GSP 14 as long as the identified project terminates in a Tier I or Tier II area.⁷² Staff initially supported the GAP proposal as a pilot program -- limited to a single project and subject to certain conditions -- believing that the proposed GAP project would target a “greenfield” site. Staff has since withdrawn its support after discovering that the project identified by WGL is a different project. Staff avers that the total benefits of allowing GAP treatment for this NPV-positive project remains unclear.⁷³ By contrast, Staff states a GAP-like pilot could be an alternative to an NPV-negative project, provided that the project ends in a Tier I area and the targeted conversion is limited to a “greenfield” area.⁷⁴

II. COMMISSION DECISION

A. Washington Gas Must Show that its Tariff Changes Result in Just and Reasonable Rates.

Section 4-201 of the PUA requires the Commission to ensure that WGL charges just and reasonable rates for its services. PUA § 4-101 defines a “just and reasonable” rate as one that is consistent with the PUA, is fully considered by the Commission and consistent with the public good, and will result in a reasonable return on the fair value of

⁷¹ *Id.* at 16.

⁷² *See id.*

⁷³ *Id.* at 17-18.

⁷⁴ *Id.* at 21.

the utility's property found used and useful in providing service to the public. PUA § 3-202 places the burden of proof on the utility to show that its proposed tariff changes result in just and reasonable rates.

B. WGL Has Not Demonstrated that the CPP, TCP, and GAP Plans Adequately Protect Existing Ratepayers.

Every party to this proceeding other than WGL opposes each of the three proposed programs, in full as well as in the form of a pilot. Although each of those parties gives varying reasons for rejecting each program, each party argues or at least acknowledges that the Company's proposals place the interests of existing ratepayers at risk, and that the Company has not provided adequate evidence to overcome those concerns. Because the three proposals would force existing ratepayers to bear the risks of a program that primarily benefits a select few, we cannot find that the proposed tariff changes would result in just and reasonable rates.

1. The Contribution Payment Plan Would Require Existing Ratepayers to Back the Extension of Easy Financing without Adequate Protections or Benefits.

The Parties' principal concern regarding the CPP is the same as ours: it will force existing ratepayers to pay for the costs of any defaults by program participants, or their successors. Although WGL maintains that CPP customers will be more likely to pay their bills because they will be paying a lower amount than they would for an alternative energy source (even with the CPP added in),⁷⁵ that assertion is based on fluctuating energy prices and does not appear to factor in the cost of new appliances and other home improvements necessary to accommodate natural gas service. Moreover, by extending

⁷⁵ WGL Reply Brief at 12.

credit to customers at a higher-than-normal rate, but without the same credit checks required by a third-party financier, the CPP runs the risk of attracting a group of new WGL customers who are at a higher overall risk of default than existing ratepayers.⁷⁶ Finally, even if one assumes perfectly executed notice between owners, WGL provides no plan – and appears to establish no incentive – to encourage new residents and business owners who inherit CPP obligations at a service address to pay inherited CPP charges. Simply allowing unpaid contributions to enter the Company’s rate base directly exposes WGL’s other customers to the return and depreciation on the unpaid portion of the CPP. Although existing customers almost always shoulder the non-payment of utility services, WGL does not appear to have taken steps to address the possibility that the CPP will expose existing ratepayers to more risk than normal. Nor has the Company presented any plan or strategy to hedge against CPP payment default. Without additional safeguards, other sources of funding, or efforts to share risks, we are unwilling to approve, even in pilot form, a program that -- for the reasons explained above -- could increase costs to existing ratepayers.

Lastly, we note that while the risk of defaults under the CPP are borne by existing ratepayers, the Company is proposing to earn its full pre-tax rate of return (approximately 12% currently) as the carrying charge customers would have to pay to finance their conversion costs.⁷⁷ Given the long-term financial benefits to the Company of increasing

⁷⁶ WGL maintains in both the Rebuttal Testimony of Witness Buckley and its Reply Brief that “the available evidence from a similar program in Pennsylvania conducted by Columbia Gas of Pennsylvania demonstrates that there is no high rate of defaults.” Rebuttal Testimony of Witness Buckley at 32; WGL Reply Brief at 11 (quoting the Rebuttal Testimony of Witness Buckley). The Commission notes that WGL did not cite further detail to support its assertion.

⁷⁷ Hr’g Tr. 129, May 1, 2017 (Chairman Hughes/Buckley).

its customer base, we question whether shareholders should not also contribute to this proposal in the form of lower and thus more attractive carrying charges.

2. The Targeted Conversion Plan Would Require Existing Ratepayers to Assume the Risk of a Speculative Program without Adequate Contributions from the Company or Future Ratepayers.

We commend WGL for exploring ways to encourage natural gas conversions among small groups of customers, especially by reducing the up-front costs of their conversion. We cannot, however, approve a program that bears a significant chance of increasing the rates of existing customers,⁷⁸ without requiring new customers or the Company to bear any responsibility for ensuring that enough additional users make the program economic and beneficial for all ratepayers. As OPC observes, the TCP program would require existing customers to pay its build-out costs unless and until the 60% threshold is achieved.⁷⁹ Without making any apparent effort to mitigate or spread program risks, WGL maintains instead that its findings suggest that the TCP has at least a reasonable likelihood of success, and that it is willing to cap the program.⁸⁰ WGL, OPC, and Staff, however, disagree on the implications of WGL's 2014 study of neighborhood conversions, and we are not willing to risk the interests of existing ratepayers on a wager that WGL's interpretations are superior to those of all other parties. We are further concerned with the apparent lack of incentives for conversions to occur beyond the initial 20% customer threshold; after crossing that threshold, neither the Company nor its new

⁷⁸ Staff Initial Brief at 16.

⁷⁹ OPC Initial Brief at 10.

⁸⁰ WGL Reply Brief at 13.

customers bear any responsibility to recruit additional customers, while the bearers of the risk – existing ratepayers – will have no means of protecting their interests.⁸¹

Moreover, although we recognize that capping the TCP somewhat mitigates the risk to existing ratepayers, there is no need to authorize such a pilot when a similar program will soon be underway in Virginia.⁸² If, as WGL speculates, “the 2014 results” are in fact “conservative when compared to future activity under an approved, structured and fully supported marketing and education program,” WGL will have ample opportunity to show this to the Commission in future years.⁸³

3. The Gas Access Program Would Require Existing Ratepayers to Bear the Risk of Cost Recovery if Growth Expectations Are Not Met.

We are further troubled by the risk-shifting that may occur under the GAP program if WGL does not fully realize the anticipated growth in new customers and the development of greenfield (or brownfield) sites. WGL proposes the GAP program as a means of extending gas service to areas that would otherwise fail the Company’s traditional economic test. As proposed, the GAP would allow WGL to bypass the traditional economic test altogether, proceed with a GAP-eligible project and seek cost recovery through rate base. While the Company is quick to point out that Staff supports the concept of the GAP, we note that Staff does not advocate for a program completely devoid of any economic consideration.⁸⁴

⁸¹ Additionally, as MAPDA-MAPGA notes, the TCP program could incentivize customers beyond the threshold 20% to decline service initially and avoid a customer contribution, which would shift costs to existing customers. MAPDA-MAPGA Initial Brief at 8.

⁸² *Id.*

⁸³ WGL Initial Brief at 9.

⁸⁴ As discussed in a later section of this Order, Staff has consistently maintained through these proceedings that the NPV test should be used to evaluate the project preliminarily whether it is NPV-positive or negative, with the latter qualifying as GAP-eligible. Cross Direct at 33; Staff Initial Brief at 20-21.

Traditional ratemaking principles presume that, to the extent possible, costs should be assigned in rates to those responsible for the costs. However, the proposed GAP program does not simply target the Company's new customers. Company Witness Buckley testified plainly that "a portion of the cost of common infrastructure used by multiple customers would be spread across all customers."⁸⁵ To justify this cost-spreading, WGL argues that revenues from new customers will cover some of the fixed costs of extending its main lines. WGL also claims additional benefits, such as minimizing excessive infrastructure and overlap, avoiding conversion costs, and achieving environmental efficiency in connection with extending lines into Tier I and Tier II areas.⁸⁶

While it is true that WGL would not recover any costs of any GAP-eligible projects through rate base until such projects are demonstrably used and useful, the fact that there is no guaranteed cost recovery, by itself, does not justify authorizing the regulatory asset. We note with particular relevance Staff's statement that "GAP projects might not become fully useful until the greenfield parcel it is designed to serve is fully developed and established."⁸⁷ Under our current line extension policy, the ratepayers' cost-sharing responsibility triggers when: 1) the potential customers' projected long-term revenues exceed the project's estimated costs; or 2) the projected revenues fail to exceed the costs, but the potential customers pay the difference up front. In either case, the existing customers do not bear the impact of any costs that exceed projected revenues.

⁸⁵ Direct Testimony of Paul S. Buckley at 15.

⁸⁶ See WGL Initial Brief at 37.

⁸⁷ Cross Direct at 34.

We find the same cannot be said for the proposed GAP. The Company has not provided any assurance that it will attract the new customers necessary to offset the spreading of GAP-related costs across all customers. And while the Company proposes to terminate a GAP project in a Tier I or Tier II growth area, the Company has not indicated how it will achieve its growth expectations. At best, there remains uncertainty whether WGL can realize the claimed material benefits to sustain a future prudency review. Accordingly, we are reluctant to gamble on a prospect that may or may not produce sufficient benefits to offset any risk-shifting to WGL's entire customer base.

4. WGL Has Not Proposed a Suitable Project for Pilot Study under the GAP Plan.

We are further persuaded by Staff's objection to the GAP proposal on the grounds that the project proffered for the GAP pilot is NPV-positive, which as Staff correctly notes is already authorized under the Company's current tariff. Staff Witness Cross initially supported approving the GAP proposal as a pilot, based on a discrete project described by WGL in a confidential data response to Staff.⁸⁸ In his surrebuttal testimony, however, Witness Cross reversed his position upon discovering that the intended GAP project was not the one envisioned by Staff but, rather, the same gas expansion project WGL previously submitted to the Commission under its existing tariff.⁸⁹ Furthermore, Mr. Cross could not discern from the Company whether the proposed GAP project would include greenfield land or be strictly limited to natural gas conversions at existing premises. Even so, he believed the proposed project would "mainly result in conversions

⁸⁸ Cross Direct at 34.

⁸⁹ See Surrebuttal Testimony of Jason A. Cross at 3.

to natural gas service from existing customers,” which could diminish the environmental and societal benefits of the GAP.⁹⁰

WGL disputes Staff’s assertion that the proposed GAP project is NPV-positive. While WGL agrees that a more discrete project would not be appropriate for GAP treatment, Company Witness Buckley testified on rejoinder that the expansion potential of the “full project” would not pass the NPV test.⁹¹ Furthermore, WGL contends that the Company is investigating other potential GAP projects—at least 10-12 areas that would provide extension work for “a couple decades” if we were to approve the GAP program on a permanent basis.⁹²

The Company attempts to assure us that its GAP program can be approved “given the prospect of likely qualifying areas aside from the project Staff identified.”⁹³ Notwithstanding this assertion, the Company has not provided us, Staff, or any of the parties with an alternative pilot project. While we appreciate the Company’s indication that it is investigating other potential GAP projects, we must take the record as it stands.

Presently, the project before us in connection with the GAP is the one identified by Staff as NPV-positive. We agree with Staff that it would be unreasonable and inappropriate to use the GAP to fund a project the Company is already authorized to proceed with under its current tariff.⁹⁴ WGL has already determined that the project in question is economically feasible. We do not see how the Company would be better

⁹⁰ See *id.* at 6–7.

⁹¹ WGL Reply Brief at 15.

⁹² Hr’g Tr. 137, May 1, 2017 (Chairman Hughes/Buckley).

⁹³ WGL Reply Brief at 15.

⁹⁴ As stated earlier in this Order, the GAP is intended to facilitate the extension of natural gas service into areas where it would otherwise be uneconomical to do so.

situated by deferring cost recovery of this NPV-positive project into a regulatory asset, when our regulatory structure has allowed utilities the opportunity to earn a return of (and a return on) such projects through rates. Whereas the Company has failed to articulate a justifiable reason for giving GAP treatment to its proposed NPV-positive project, we decline to establish such a broad-sweeping precedent today for all future NPV-positive projects terminating in Tier I or Tier II areas. To do so would allow WGL to change the way it funds expansion projects.

C. The NRRI and the FERC Disapprove of Unwarranted Cost-Recovery Risk Shifting onto Customers.

We generally support the concept of improving customer access to natural gas as an alternative to higher cost electricity. Nevertheless, the case before us plainly highlights a complexity of issues attendant to such a request. The concerns expressed herein are in accordance with the views espoused by the National Regulatory Research Institute (“NRRI”) and by the Federal Energy Regulatory Commission (“FERC”). As MAPDA-MAPGA Witness Wilson noted in his direct testimony, the NRRI published a report in 2013, reviewing state policies on natural gas line expansion (the “NRRI Report”), observing that many states require an economic test for new expansions.⁹⁵ This is true for Maryland and certainly reflected in WGL’s current tariff. Notably, the NRRI Report found that “most commissions adhere to the principle that any line extensions should not burden existing customers.”⁹⁶ The NRRI is not alone in this regard. Similarly, the FERC requires that any pipeline company seeking approval for new construction “must be prepared to financially support the project without relying on

⁹⁵ Direct Testimony of James S. Wilson at 6.

⁹⁶ *Id.*

subsidization from its existing customers.”⁹⁷ This is, in fact, a threshold requirement for pipelines proposing new projects. According to the FERC, “subsidization by existing ratepayers will mask or distort the true costs of a project . . . leading to inefficient investment and contracting decisions.”⁹⁸ The FERC, like the NRRI, disfavors placing unwarranted burdens on existing customers, which is consistent with the fundamental cost causation principle we recited earlier. While we agree with this principle, we also acknowledge that expanding natural gas service to underserved and unserved areas may require unconventional or innovative approaches.

D. The Commission Will Benefit Further From the NARUC Gas Expansion Study.

Just prior to the May hearings in this case, the National Association of Regulatory Utility Commissioners (“NARUC”) established a new Presidential Natural Gas Access and Expansion Task Force charged with developing best practices and recommendations regarding expanding natural gas service to underserved and unserved areas of the country. The Task Force has an eight-month term, and is expected to produce an analytical report that will:

study current access, expansion and service extension policies for underserved and unserved areas; examine the need for access and expansion including case studies and review of the barriers and obstacles to such access; recommend potential mechanisms to address the benefits and opportunities for access and expansion and identifies alternative or unconventional approaches to reaching unserved and underserved areas; and compile a national

⁹⁷ *Id.* (quoting Certification of New Interstate Natural Gas Pipeline Facilities, 88 FERC ¶ 61,227 (1999) (“FERC 1999 Policy Statement”).

⁹⁸ FERC 1999 Policy Statement at 17.

“best practices” collection on natural gas access and expansion to underserved and unserved areas.⁹⁹

We would encourage Staff, the Maryland Energy Administration, OPC, the State’s natural gas companies, and other stakeholders to use the Task Force report for the purpose of considering and developing future proposals to expand natural gas access.

III. CONCLUSION

Expanding natural gas access in Maryland has the potential to provide benefits to the State and its ratepayers, including environmental benefits when gas replaces electricity, increased efficiencies when natural gas is used directly rather than as a fuel source for electricity, lower energy costs, and greater convenience.¹⁰⁰ While we commend WGL for designing three discrete proposals to expand access to natural gas in Maryland, we cannot approve WGL’s Petition at this time. For the above-stated reasons, we find that none of the three programs, as proposed in full or in pilot form, would result in just and reasonable rates. We are looking forward to the results of the NARUC gas expansion study, and we encourage further efforts to discuss these issues among interested parties. The Commission remains open to future proposals to expand natural gas access. It will be imperative, however, that future proposals more appropriately share risks between affected stakeholders, not the least of which are the existing customer ratepayers. Accordingly, we deny the Petition as filed. This denial is without prejudice

⁹⁹ NARUC Establishes Natural Gas Access and Expansion Task Force (2017), <https://www.naruc.org/about-naruc/press-releases/naruc-establishes-natural-gas-access-and-expansion-task-force/> (last visited July 17, 2017).

¹⁰⁰ Staff Letter in Lieu of a Reply Brief at 1.

to WGL's ability to submit a different proposal(s) to expand access to natural gas, as discussed above.

IT IS THEREFORE, this 1st day of August, in the year Two Thousand and Seventeen, by the Public Service Commission of Maryland,

ORDERED: (1) That the Washington Gas Light Company's Petition for Approval of Revised Tariff Provisions to Facilitate Access to Natural Gas in Areas within the Company's Maryland Franchise Area that are Currently without Natural Gas Service is hereby denied without prejudice;

(2) That WGL's proposed changes to its tariff, General Service Provision No. 14, are hereby rejected; and

(3) That all motions not granted herein are denied.

/s/ W. Kevin Hughes _____

/s/ Michael T. Richard _____

/s/ Anthony J. O'Donnell _____

Commissioners