

ORDER NO. 88641

IN THE MATTER OF THE APPLICATION
OF CHOPTANK ELECTRIC
COOPERATIVE, INC. FOR AUTHORITY
TO REVISE ITS RATES AND CHARGES
FOR ELECTRIC SERVICE

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BEFORE THE
PUBLIC SERVICE COMMISSION
OF MARYLAND

CASE NO. 9459

Issue Date: April 10, 2018

On February 27, 2018, the Public Utility Law Judge (“PULJ”) issued a Proposed Order in this case, finding that Choptank Electric Cooperative, Inc. (“Choptank”) should be authorized a revenue increase of \$5,573,573 and a Modified Debt Service Coverage (“MDSC”) ratio of 1.85. On March 9, 2018, Choptank and the Public Service Commission Staff (“Staff”) filed Notices of Appeal and Memoranda on Appeal. Choptank, Staff, and the Office of People’s Counsel (“OPC”) filed Reply Memoranda on March 20, 2018. The issues on appeal are related to Choptank’s rate design.

Choptank appeals the decision of the PULJ to grant an increase of only \$0.50 to both Choptank’s fixed residential customer charge and its Minimum Monthly Charge (“MMC”). Staff appeals the PULJ’s approval in the Proposed Order of Choptank’s proposal to allocate the cost of Advanced Meter Infrastructure (“AMI) meters to customer classes through a direct assignment of the cost of meters installed for each

customer class. Instead, Staff maintains that AMI costs should be allocated based on the three-factor allocation method the Commission endorsed in prior cases.¹

In reply to Choptank’s appeal, Staff recommends that the Commission affirm and adopt the Proposed Order’s findings and decisions regarding Choptank’s customer charge and MMC, or modify the decision to eliminate any increase in these charges as Staff had originally proposed. OPC requests that Choptank’s appeal be rejected, which would leave the authorized increase of \$0.50 to the customer charge and MMC in place.

In reply to Staff’s appeal, Choptank submits that the Potomac Electric Power Company (“Pepco”) rate case on which the three-factor allocation is based is distinguishable. Choptank states that its legacy meters were failing at an alarming rate and had to be replaced, and that additional investment will be necessary before all of the benefits of the AMI meters can be fully realized.² Choptank therefore requests that the Commission affirm the Proposed Order on this issue.

I. APPLICABLE LAW

Section 4-201 of the Public Utilities Article of the Annotated Code of Maryland (“PUA”) provides:

In accordance with the provisions of this article, a public service company shall charge just and reasonable rates for the regulated services that it renders.

A just and reasonable rate is defined in PUA §4-101:

In this title, “just and reasonable rate” means a rate that:

- (1) does not violate any provision of this article;
- (2) fully considers and is consistent with the public good; and

¹ Staff Memorandum on Appeal (“Staff Memo”), p. 1.

² Reply Memorandum on Appeal of Choptank Electric Cooperative, Inc. (Choptank Reply Memo”), p. 5.

- (3) except for rates of a common carrier, will result in an operating income to the public service company that yields, after reasonable deduction for depreciation and other necessary and proper expenses and reserves, a reasonable return on the fair value of the public service company's property used and useful in providing service to the public.

PUA § 4-102(b) provides:

The Commission shall have the power to set a just and reasonable rate of a public service company, as a maximum rate, minimum rate, or both.

Lastly, PUA § 3-112(b) establishes the burden of proof in rate case proceedings:

In a proceeding involving a temporary or permanent new rate, or a temporary or permanent change in rate, the burden of proof is on the proponent of the new rate or change in rate.

II. CUSTOMER CHARGE AND MMC³

In its Memorandum on Appeal, Choptank submits that the Commission should set Choptank's customer charge and MMC to the levels requested in its application – \$17.30 and \$32.45, respectively. Choptank proposes three alternative minimum levels – a similar \$1.25 increase to the customer charge as the Commission granted in Choptank's most-recent prior rate case (Case No. 9368, Order No. 86994) to \$12.50; a similar 12.5% increase to its customer charge/MMC to \$12.66; or an increase that does not significantly change the proportion of revenue derived from the current customer charge (keeping the proportion of revenue at 16.77% would equate to a customer charge of \$12.52). Choptank's primary argument is that the PULJ incorrectly applied the term "gradualism" in increasing the customer charge from \$11.25 to \$11.75, a 4.4% increase.

³ Chairman Hughes and Commissioner Herman dissent from this part of the Commission's decision.

Although the PULJ accepted Choptank’s Cost of Service Study (“COSS”)⁴, the Proposed Order discusses Staff’s concern regarding the COSS’ reliance on the minimum intercept method. The minimum intercept method classifies a portion of distribution plant as customer-related, which results in the residential class being allocated more plant because it is the largest class (approximately 90% of Choptank’s customers, while representing only 69% and 77% of the primary and secondary demand).⁵ The Proposed Order further notes that, with the exception of the proposed AMI meter allocation, Staff found Choptank’s COSS to be reasonable⁶, to be used *as a guide* in calculating rates. [emphasis added].

Indeed, the Proposed Order recites the long-standing premise that cost of service studies are useful tools and can serve as a benchmark to determine whether individual classes of customers are making fair and equitable contribution to the total cost of service.⁷ The Proposed Order continues, “COSSs are rate design tools and consequently appropriate judgment and discretion are required in the final design of customer class rates.”⁸ Thus, the Proposed Order properly concludes that Choptank’s COSS, though accepted, was accepted as a guide for setting rates in this case, and is not a mandate that must be blindly followed.⁹ We reiterate the PULJ’s finding that Choptank has not provided a convincing argument or sufficient evidence that warrants disregarding the Commission’s long-standing approach of using COSSs as rate setting guides.

⁴ No alternative cost of service study was submitted by any other party.

⁵ Direct Testimony of Drew M. McAuliffe (“McAuliffe Direct”), p. 15.

⁶ Proposed Order at. 22.

⁷ Proposed Order at 29, *citing Re Washington gas Light Co.*, 77 Md. P.S.C. 30, 33-34 (1986).

⁸ Proposed Order at. 29-30, *citing Re Delmarva Power & Light Co.*, 103 Md. P.S.C. 377, 421 (2012).

⁹ Proposed Order at. 30.

Thus, Choptank's COSS, which Choptank argues supports a customer charge of \$32.45, is only a guide. Moreover, regardless of what the COSS reflects as total fixed costs, nothing dictates that the fixed customer charge must be equal to total fixed costs. OPC in particular disagrees with Choptank's assertion that all fixed costs should be recovered through a fixed customer charge. OPC's Witness Watkins testified that fixed costs recovered through fixed charges should be limited to "those direct customer costs required to connect and maintain a customer's account."¹⁰ Using this approach, corporate overhead expenses and any indirect costs are collected through energy charges, resulting in a residential direct customer cost of \$10.90 based on Choptank's requested rate of return.¹¹ There is also evidence in the record that the \$32.74 in fixed costs reflected in Choptank's COSS would be reduced to \$22.22 if the minimum intercept method is not used, a method that, as Staff explains, inflates customer-related costs.¹²

From the parties' various calculations of customer-related costs, Choptank proposed a customer charge of \$17.30 and a MMC of an additional \$15.15 or \$32.45; OPC and Staff proposed no increase to the existing customer charge/MMC of \$11.25. From the range of evidence as to fixed costs and opinion as to appropriate customer charges based on those fixed costs, we are tasked with using our judgment and discretion

¹⁰ Surrebuttal Testimony of Glenn A. Watkins ("Watkins Surrebuttal"), p. 4.

¹¹ Direct Testimony of Glenn A. Watkins ("Watkins Direct"), p. 11.

¹² McAuliffe Direct, p. 12.

to arrive at the fixed customer charge authorized in this case.¹³

As the PULJ notes, in Pepco’s last rate case, the Commission rejected a proposed customer charge increase, stating “we place emphasis on Maryland’s public policy goals that intend to encourage energy conservation,” and that lower customer charges provide customers with more control over their bill by increasing the volumetric charges.¹⁴ The Commission in that case also noted the value of lower customer charges to net metering customers.¹⁵ Similarly, as the Proposed Order further notes, more recently, on an appeal of the proposed order in Delmarva Power & Light Company’s (“DPL”) last rate case, the Commission, *sua sponte*, reversed an increase to the residential customer charge finding the increase “could interfere with important Commission policy goals that have been consistently emphasized in Commission decisions.”¹⁶ The Commission again referenced policy goals, including conservation and efficiency, that lower customer charges provide customers greater control over their bills, and the potential impact on low-income customers and net metering customers.¹⁷

In this case, we again consider Maryland’s energy policy goals of encouraging efficiency and conservation. We believe that lower customer charges provide customers

¹³ OPC argues in its Reply Memorandum that there is no record evidence to support an increase to an amount other than those proposed by the parties. To clarify, evidence in the record includes testimony as to customer costs, and party opinion, based on those calculated costs and various policy considerations, as to appropriate customer charge. The Commission is not limited by opinion testimony as to appropriate customer charges. Rather, the Commission begins its analysis with the evidence of customer costs that was submitted, and considers opinion testimony as to appropriate customer charges, then uses appropriate judgment and discretion in setting rates including customer charges.

¹⁴ *Re Potomac Electric Power Company*, Case No. 9418, Order No. 87884, 107 MD P.S.C. 701, 759 (November 15, 2016).

¹⁵ *Id.*

¹⁶ *In the Matter of the Application of Delmarva Power & Light Co. for Adjustments to Its Retail Rates for the Distribution of Electric Energy*, Case No. 9424, Order No. 88033, *slip op.* at 26 (February 15, 2017), *citing* 106 Md. P.S.C at 205-206.

¹⁷ *Id.* at 27.

with more control over their bill; with more of their bill comprised of volumetric charges, the correlation between a customer's energy usage and the total bill is more apparent and efforts to be more efficient and conserve energy where possible are more readily managed. Additionally, we are concerned about the impact of high customer charges on low-income customers,¹⁸ and we note the value of lower customer charges to net metering customers. For all of these reasons, we adopt the \$0.50 increase authorized in the Proposed Order. Any increase in customer charge is relative to the overall rate increase and thus comparisons of percentage increases in customer charges between different utilities' rate cases provides an incomplete frame of reference. The resulting 4.4% increase in customer charge does not represent a significant deviation from the overall rate increase authorized in this case.¹⁹ Moreover, this \$0.50 increase will not significantly change the proportion of revenue derived from the customer charge, which the Commission deemed to be an appropriate measure in Baltimore Gas Electric Company's ("BGE") most recent rate case.²⁰ Currently, Choptank's existing rates recover 16.77% of revenues through the fixed charge of \$11.25. The authorized customer charge of \$11.75 will correspond to 15.74% of revenues. We do not find the change from 16.77% to 15.74% of revenues to be significant.

¹⁸ Choptank Witness DeSantis claimed that low-income customers would not be disproportionately impacted by a higher fixed charge as many EUSP customers use the same amount of electricity as non-EUSP customers. Rebuttal Testimony of Lisa H. DeSantis ("DeSantis Rebuttal"), p. 9-10. However, as Staff Witness Hoppock explained, customer impacts should be analyzed based on distribution of actual consumption, not average consumption levels. Surrebuttal Testimony of David Hoppock ("Hoppock Surrebuttal"), p. 2.

¹⁹ The average residential customer (1,000 kWh her month) will see a total bill increase of 4.9%, with a 10.8% increase in the distribution portion of their bill. Proposed Order at 78-79.

²⁰ *Re Baltimore Gas and Electric Company*, Case No. 9406, Order No. 87591, 107 MD P.S.C. 206, 298 (June 3, 2016).

We recognize that the \$.50 increase we authorize equates to a smaller percentage increase than we authorized in Choptank's previous rate case, but the 12.5% increase we authorized in Choptank's last rate case does not bind us to approve a similar increase in this case, or to approve any increase at all. The Proposed Order notes that the increase in the customer charge from \$11.25 to \$11.75 is consistent with the gradualism principle,²¹ *i.e.*, the change is gradual and will not be shocking to ratepayers. Choptank attempts to characterize this statement as a holding "that any increase over 4.4% *would* violate the principles of gradualism."²² Choptank is misguided in this attempt, as well as in its suggestion that the Commission has somehow restricted its definition of a gradual increase to 12.5% based on Order No. 86994. As Staff correctly points out, there cannot possibly be a "hard and fast rule as to what constitutes a gradual increase in a customer charge" given "the myriad variations of evidence and circumstances that are presented to the Commission in rate cases."²³ Moreover, a statement that an authorized increase is consistent with the principle of gradualism does not, as Choptank argues, equate to a finding that any amount over that increase would be inconsistent with the principle; it is simply recognizing that the increase that is being authorized does not constitute a rapid or shocking increase.

Choptank's interpretation of gradualism implies that the Commission determined an appropriate increase to the fixed customer charge in Case 9368, but then authorized only a portion of that increase. Such an interpretation is not supported by the language of

²¹ Proposed Order at 68.

²² Memorandum on Appeal of Choptank Electric Cooperative, Inc. ("Choptank Memo"), p. 6.

²³ Staff's Reply Memorandum on Appeal, p. 10.

Order No. 86994 however.²⁴ Instead, the Commission relies on the record developed in each case and our expertise and judgment to set just and reasonable rates. Using Choptank's COSS as a guide, weighing all of the evidence as to fixed costs and opinion as to appropriate customer charges based on those fixed costs, and taking into account policy considerations as discussed above, we find that a \$0.50 increase in the customer charge is just and reasonable.

With regard to the MMC, we agree with the PULJ that the MMC should not be set higher than the fixed customer charge, *i.e.*, a customer that uses less than 296 kWh per month pays only the fixed customer charge of \$11.75. Choptank conceded that based on Staff Witness Hoppock's bill impact analysis, approximately 7% of residential customers receiving bill assistance would experience an increased bill due to application of the MMC.²⁵ Although Choptank maintains that this represents only a small percentage of residential customers, it cannot deny that low-income customers would be negatively impacted. The proposal would also negatively impact net metering customers.

As the PULJ noted in the Proposed Order, there are other viable options for Choptank that may provide it with revenue stability. OPC offered to work with Choptank and Staff to explore creating a separate rate class for sporadic use customers such as boat docks, vacations homes, hunting cabins, and seasonal poultry houses.²⁶ Additionally, as OPC suggested, Choptank could consider whether to propose a Bill Stabilization

²⁴ See Order No. 86994 at 11.

²⁵ Rebuttal Testimony of Jessica Trump, p. 3.

²⁶ OPC Initial Brief, p. 18.

Adjustment to mitigate the effects on sales (and thus revenue) caused by weather, energy efficiency, and distributed generation.²⁷

III. ALLOCATION OF AMI COSTS

Choptank proposed to allocate AMI costs directly to the customer classes as customer-related costs, resulting in the residential class being allocated a majority of the AMI-related costs.²⁸ Choptank argued that this direct allocation method was the most appropriate allocation because “the primary function that [AMI] replaced is the meter and metering problem that Choptank had” with its legacy meters.²⁹

Staff argues that the functions of obsolete equipment that is replaced by new technology equipment are irrelevant in determining how to allocate the new equipment’s costs. Instead, the proper focus is on the functionality of the new equipment because this is the equipment that the utility is now using.³⁰ In response to Staff’s argument, Choptank claims that “although Choptank’s AMI meters are operational, additional investment will be necessary before the entire panoply of benefits from AMI meters are fully realized.”³¹

In response to Staff Data Requests regarding the benefits that have already been developed through conversion to AMI, Choptank stated that the AMI meters are completely interfaced with Choptank’s outage management system (OMS), so Choptank knows in real time when there is an outage and when service is restored, regardless of

²⁷ OPC Initial Brief, p. 14.

²⁸ McAuliffe Direct, p. 15-16.

²⁹ Transcript, p. 225.

³⁰ Staff Memo, p. 12.

³¹ Choptank Reply Memo, p. 5.

whether the member is at home.³² Choptank also included in its response the benefit of AMI being able to predict service failures and transformer failures when/if the voltage drifts out of the allowable range.³³ The AMI is “capable of alarming when the voltage goes above or below acceptable levels. Choptank has been able to investigate these voltages and repair the cause during business hours (rather than at night or on weekends) and often before an outage actually occurs.”³⁴ Although Choptank argues that these benefits are consumer-related, as Staff pointed out, Choptank Witness Miranda cited the operational benefits of AMI as justification for the use of additional cost allocations that are not only customer-related.³⁵ On cross examination, Mr. Miranda acknowledged that the reliability benefits of AMI enhance Choptank’s entire distribution system.³⁶

We agree with Staff that AMI provides important operational benefits that increase the reliability of service on Choptank’s distribution system for all customers. We also agree that by measuring consumption throughout the day, AMI will facilitate conservation programs as well as adoption of time-of-use pricing, which will reduce peak load and lead to further improvement in reliability. Thus, although additional investment in software is required to utilize the benefit of, *e.g.*, Demand Voltage Reduction (“DVR”), operational benefits of AMI are likely already being realized with the meter investment accepted by the Proposed Order.

Staff’s proposed allocation, however, is based on the allocation methodology approved by the Commission in Case No. 9418. In that case, Pepco submitted a detailed

³² McAuliffe Surrebuttal, Exhibit DMM-1.

³³ *Id.*

³⁴ *Id.*

³⁵ McAuliffe Surrebuttal, p. 3.

³⁶ Transcript, p. 211.

cost benefit analysis, for cost recovery purposes, that included estimated future energy and demand management benefits to all customer classes. Only 25% of the benefits Pepco presented were exclusive to classes receiving AMI meters. Accordingly, the Commission rejected Pepco's proposed 100% allocation as customer-related. Instead, the Commission adopted Staff's recommendation to allocate Pepco's AMI costs 25% as customer-related, 37.5% as energy-related, and 37.5% as demand-related, finding that such allocation more equitably distributes the AMI costs across all rate classes receiving benefits from AMI.³⁷

Although the AMI Choptank has installed likely already provides system-wide benefits, unlike in the Pepco case, these benefits have not been quantified. We know that the 100% allocation as customer-related does not reflect those operational benefits, but we can only speculate as to the percentage of benefits that are customer-related. As was the situation in the most recent DPL rate case, Case No. 9424, there is no data in the record to support Staff's recommendation.³⁸

In its Memorandum on Appeal, Staff opines that the use of both peak and average usage as allocators for AMI costs is supported by Choptank's use of both peak and average use allocators for other facilities.³⁹ Staff argues on brief that Choptank, in its COSS, allocated the cost of substations and primary distribution facilities based on the Average and Excess Demand ("AED") method, which recognizes that facility costs should be allocated in a manner that reflects the extent to which each customer class

³⁷ *Re Potomac Electric Power Company*, Case No. 9418, Order No. 87884, 107 MD P.S.C. 701, 757 (November 15, 2016).

³⁸ *In the Matter of the Application of Delmarva Power & Light Company for Adjustments to Its Retail Rates for the Distribution of Electric Energy*, Case No. 9424, Proposed Order, p. 173.

³⁹ Staff Memo, p. 9.

relies on the distribution system as measured by average and peak usage.⁴⁰ Staff asserts that allocating AMI costs based on average usage and peak usage would be consistent with allocating the cost of substations and primary distribution facilities under the AED method. However, Staff's Memo does not reference any witness testimony in support of this assertion. Thus, although we find Staff's alternative hybrid allocation of 25% as customer-related, 37.5% as energy-related, and 37.5% as demand-related logical, we cannot adopt such allocation given the lack of data or evidence in the record to support it.

Choptank offered to review additional future AMI investments "to determine what the best allocation method is for that portion of the plant."⁴¹ As set forth above, we find that the AMI meters already provide system-wide benefits, without the additional investment Choptank plans. We direct Choptank, prior to its next rate case, to determine the best allocation method for its entire AMI investment (including these meters) in accordance with that finding. As part of Choptank's next application for a rate increase, we expect Choptank to submit an allocation for AMI costs that aligns with the current and future customer-related and system-wide benefits associated with AMI. The quantification of benefits can be an estimate; indeed, Pepco's cost benefit analysis in Case No. 9418 was based on estimates of benefits years into the future.

For the reasons set forth herein, the Proposed Order is hereby affirmed.

IT IS THEREFORE, this 10th day of April, in the year Two Thousand and Eighteen, by the Public Service Commission of Maryland,

ORDERED: (1) That, as more fully detailed herein, the Proposed Order of

⁴⁰ Staff Memo, p. 9-10.

⁴¹ Transcript, p. 207.

the Public Utility Law Judge is affirmed;

(2) That the Application filed by Choptank Electric Cooperative, Inc. on September 12, 2017 is hereby denied;

(3) That Choptank Electric Cooperative, Inc. is hereby authorized, pursuant to § 4-204 of the Public Utilities Article, *Annotated Code of Maryland*, to file tariffs for Commission review and acceptance that shall increase electric distribution rates by no more than \$5,573,573, with an effective date of April 10, 2018, consistent with this Order.

(4) That the appeal of Choptank is rejected and a \$0.50 increase in the residential customer charge and MMC is adopted for the reasons set forth herein;

(5) That the appeal of Staff is rejected and the costs of AMI will be allocated as set forth in the Proposed Order;

(6) That Choptank Electric Cooperative, Inc. shall submit an allocation for AMI costs that aligns with the current and future customer-related and system-wide benefits associated with its AMI as part of its next base rate case application; and

(7) That any motions or requests not granted herein are denied.

W. Kevin Hughes

Michael T. Richard

Anthony J. O'Donnell

Odogwu Obi Linton

Mindy L. Herman

Commissioners

**Dissenting Statement, In Part, Of
Chairman W. Kevin Hughes and Commissioner Mindy L. Herman**

We respectfully dissent from the Commission's Order approving the \$0.50 increase in the residential customer charge and the monthly minimum charge (MMC) on the grounds of gradualism and Commission precedent. The Commission's prior order in the most recent Choptank rate case increased the residential customer charge by \$1.25 and we would support an increase to both the customer charge and the MMC at that level in this proceeding. The Proposed Order of the Public Utility Law Judge in this proceeding cites gradualism as the basis for his decision to limit the increase in the customer charge,¹ but acknowledges that the \$0.50 increase will in fact *reduce* the percent of recovery of fixed charges from 16.77 percent to 15.74 percent.² Unfortunately, this fails to even maintain the level of fixed costs being recovered through a fixed charge, much less modestly increase it as proposed by the Company in its appeal.

Due to the unique aspects of Choptank's service territory, we do not agree that an increase of \$1.25 would impact conservation or energy efficiency measures, nor adversely impact or discriminate against low income customers.³ Choptank's service territory is relatively rural and populated with hunting sheds, barns, and other separately metered facilities that increase fixed costs without providing a corresponding increase in volumetric revenue. The proposed \$0.50 increase in the customer charge requires

¹ Proposed Order at 68-69.

² *Id.* at 68.

³ The majority opinion argues that because approximately 7% of residential customers receiving bill assistance could see an increased bill under a higher MMC and thus, low-income customers would be negatively impacted. We note that 93% of low-income residential customers would actually see their bills lowered (or unaffected) by an increase in the MMC.

Choptank to recover additional revenues through volumetric rates,⁴ which disproportionately impacts typical residential consumers who do not own separately metered facilities.⁵

There is evidence in the record that low income customers who rely on EUSP in the Choptank service territory do not use less energy than the average residential customer, and therefore a very modest increase in the customer charge will not adversely impact such customers.⁶ Similarly, given that average residential customers will see an overall monthly bill increase of \$6.74, the \$1.25 customer charge (about 18 percent of the total increase) is unlikely to materially impact a customer's incentive to reduce their energy usage.⁷ As noted by the Company, customers are more likely to respond to subsidies and tax incentives that encourage conservation and efficiency than a very modest increase in the fixed costs of service from the Cooperative.⁸

In summary, we believe an increase in the residential customer charge of \$1.25 maintains the proper balance between fixed charges and volumetric charges in the context of the overall monthly bill increase of \$6.74 for the average residential customer. For the reasons discussed above, we dissent from the Majority Opinion regarding the increased customer charge and MMC.

W. Kevin Hughes

Mindy L. Herman

Commissioners

⁴ As noted in the Proposed Order, Choptank's revenues are also more susceptible to fluctuations in demand, because it does not have a Bill Stabilization Adjustment mechanism.

⁵ This disproportionate impact is most acute in more rural territories like Choptank's.

⁶ Proposed Order at 38.

⁷ *Id.* at 79. We note that Choptank does not participate in the Commission's EmPOWER Maryland program.

⁸ *Id.* at 51.