ML 225871

ORDER NO. 89170

IN THE MATTER OF THE APPLICATION OF WASHINGTON GAS LIGHT COMPANY FOR AUTHORITY TO INCREASE EXISTING RATES AND CHARGES AND TO REVISE ITS TERMS AND CONDITIONS FOR GAS SERVICE	* * * * * * * *	BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND CASE NO. 9481

Issue Date: June 25, 2019

ORDER ON REHEARING

On January 10, 2019, pursuant to Section 3-114(c) of the Public Utilities Article ("PUA") of the Maryland Code, and Code of Maryland Regulations ("COMAR") 20.07.02.08(C), Washington Gas Light Company ("WGL" or "the Company"), the Maryland Office of People's Counsel ("OPC"), and the Apartment and Office Building Association of Metropolitan Washington ("AOBA"), filed respective Petitions for Rehearing of the Maryland Public Service Commission's ("Commission") Order No. 88944, which authorized WGL to increase its Maryland natural gas distribution rates by $28,602,000.[1] For the reasons discussed below, WGL's Petition for Rehearing is granted in part. The Petitions for Rehearing of OPC and AOBA are denied.

A. WGL Petition for Rehearing

WGL raises two issues in its Petition for Rehearing. First, it claims that the Commission erred in accepting Staff Adjustment BCO-9,[2] which disallowed payroll costs

[1] Case No. 9481, *In re Wash. Gas Light Co*., (Dec. 11, 2018) ("Order 88944") at 2.

[2] In its Petition for Rehearing, WGL referred to this adjustment as BCO-9-S, because of the modifications Staff witness Ostrander made to it in his Surrebuttal Testimony—a convention that Staff adopted in its Response. *See* WGL Petition for Rehearing at 3, n. 6.

related to employee overtime. Second, WGL argues that the Commission's Order erroneously accepted Staff Adjustment BCO-16, which removed amortization expense for software and associated assets.

1. BCO-9: (Payroll Costs Related to Overtime)

WGL notes that it proposed Company Adjustment 19 (Wages and Salaries) to reflect several payroll-related adjustments, including: (i) annualization of pay increases that occurred in the test year; (ii) wage increases for union employees pursuant to current contracts; (iii) wage increases for management employees that occurred in December 2017 and were planned to occur in December 2018; (iv) average employee count in the rate effective period; and (v) non-recurring merger related work.[3] WGL states that its test year overtime expense was $9,565,214—representing "actual, stand-alone test year expense for utility employees, compiled from the Company's books."[4] WGL argues that it is entitled to rates that reflect the full $9,565,214 in payroll overtime costs incurred in the test year, and disputes Staff witness Ostrander's Adjustment BCO-9 (accepted by the Commission), which caused a $1,139,000 reduction in the Company's revenue requirement.[5]

WGL further argues that Order No. 88944 did not materially address BCO-9. Instead, according to WGL, the Commission granted BCO-9 summarily as part of a package of adjustments proposed by Staff to Company Adjustments 19 and 27, which are related to labor expense and leak management. Nevertheless, WGL claims that the central reason articulated by the Commission for denying certain costs related to Adjustments 19

[3] WGL Petition for Rehearing at 3.
[4] WGL Petition for Rehearing at 5.
[5] WGL Petition for Rehearing at 2.

and 27 was to adhere to a traditional test year and to base new rates on actual, not projected, data.[6] Because the overtime expense related to BCO-9 "is actual, not estimated or forecasted," WGL concludes that the Commission erred in accepting BCO-9 and that the Company is entitled to an increase in its revenue requirement in the amount of $1,139,000.

In its Response to the Petition for Rehearing, Staff contends that record evidence supports the Commission's decision regarding BCO-9. Staff states that the $9,565,214 base level test period overtime amount does not represent all of the overtime included in WGL's payroll adjustment. Instead, WGL's payroll adjustment also includes a component of test year and forecasted post-test year period payroll increases for union and management employees in addition to a forecasted headcount ratio for all employees.[7] Staff argues that Mr. Ostrander provided substantive ratemaking rationale for disallowing actual test year overtime costs. Specifically, Mr. Ostrander reduced the $9,615,000 payroll costs by the O&M factor of 73.14%, the Maryland factor of 40.76%, and he offset the remainder by an allowance for Leak Management payroll costs, to arrive at his overtime adjustment of $1,104,000.[8]

Additionally, Staff observes that Mr. Ostrander testified that WGL's payroll adjustment included an increase in overtime costs in this proceeding, comprised of actual test period overtime of $9,565,214 plus projected pay increases and projected headcount ratio applied to the test period payroll of approximately $900,000.[9] Staff asserts that WGL's projected increase in overtime costs is contrary to the Company's forecasted

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[6] WGL Petition for Rehearing at 8, citing Order No. 88944 at 11.
[7] Staff Response at 5.
[8] Staff Response at 7.
[9] Staff Response at 7-8.

reduction in overtime costs to a level of $6.9 million by March 31, 2019.[10] Specifically, Staff highlights Mr. Ostrander's testimony that "WGL forecasts that overtime costs will decrease significantly from $10.9 m in this case (March 31, 2018) to $6.9 m at March 31, 2019…."[11] Finally, Staff states that if it was the Commission's intent not to remove any test period overtime costs, then the Commission "should remove at least $647,000 of overtime costs related to post-test period/projected overtime costs that were included in Case No. 9481 and which were not removed by other Commission-approved payroll adjustments."[12]

Commission Decision

The Commission grants rehearing regarding Staff adjustment BCO-9. As observed by WGL, Order No. 88944 addressed BCO-9 in conjunction with a package of adjustments proposed by Staff that related to labor expense and leak management. The Commission accepted several Staff adjustments on the basis that they removed projected costs outside of the test year. It appears from the Company's Petition for Rehearing and Staff's Response, however, that most of the costs removed in BCO-9 relate to payroll costs the Company actually incurred during the test year. Although Mr. Ostrander testified that WGL forecasted that overtime costs would decrease significantly by March 31, 2019, the Commission finds it would be inconsistent to require removal of costs WGL projected it would incur outside the test year (as Order No. 88944 does), while simultaneously reducing the Company's actual costs due to a forecast also outside the test year (as Staff advocates).

[10] Staff Response at 8, citing Ostrander Surrebuttal at 44.
[11] Staff Response at 8, citing Ostrander Surrebuttal at 44.
[12] Staff Response at 8, citing Ostrander Surrebuttal at 45.

The Commission agrees with WGL that in this case, the Company should recover the actual overtime costs incurred in the test year. Nevertheless, the Commission concurs with Staff that to be fully consistent with the principle of adherence to a test year, it is necessary to remove the $647,000 of overtime costs that are related to post-test period/projected overtime costs that were included in the rate case but not removed by other Commission-approved payroll adjustments.[13] This change increases the revenue requirement approved in Order No. 88944 by $472,000.

2. *BCO-16: (Fully Amortized Software)*

WGL petitioned the Commission to reconsider its acceptance of BCO-16, wherein Staff witness Ostrander recommended removal of the costs of certain software "which has been replaced and is not used and useful [and] is still being maintained on the books and being amortized."[14] WGL argues that its response to a data request issued by OPC (OPC DR 1-99) demonstrates that the software is still in service. Specifically, WGL highlights the portion of its response that states: "All of the items shown are physically being utilized (not retired on an amortization basis, but rather still physically being utilized)."[15] WGL concludes that it is entitled to a fair return on the value of its property used and useful in providing service to the public, and asks that the Commission increase its revenue requirement by $1,667,000 to account for the value of the software in service.[16]

Staff opposes WGL's Petition regarding fully amortized software. First, Staff observes that WGL does not claim that the assets included in BCO-16 are not fully

[13] *See* Staff Response at 8; Ostrander Surrebuttal at 45.
[14] WGL Petition for Rehearing at 4, citing Ostrander Surrebuttal at 48.
[15] WGL Petition for Rehearing at 10.
[16] WGL Petition for Rehearing at 3.

amortized—rather, the Company simply asserts that they are still in use and that the amortization expense should continue to accrue.[17] Second, Staff argues that WGL's position is untenable because its Petition for Rehearing is the first and only time in the proceeding that the Company has cited OPC DR 1-99 as evidence that software and other amortizable assets in BCO-16 are used and in service. Third, Staff contends that OPC DR 1-99 cannot be wholly relied upon because it provides a mere listing of software assets, while BCO-16 reflects fully amortized expense that has been removed for both "software" assets as well as "other amortizable" assets.[18] Finally, Staff argues that WGL's interpretation of OPC DR 1-99 is completely contrary to WGL's responses to several Staff data requests, including Staff DRs 20-10; 34-4; 28-1; and 20-4 (attached to Staff's Response and referenced in Mr. Ostrander's Direct Testimony at 47-49 and Surrebuttal Testimony at 53-55). For example, in response to Staff DR 20-10, which asked for WGL to identify all software that would be fully amortized by December 31, 2019, WGL provided $39,403,936 of software assets categorized as "Total Software Retirements."[19] Staff DR 20-10(b) inquired why WGL did not exclude amortization expense and related assets that are fully amortized, to which WGL responded: "Fully amortized software was overlooked in the calculation of software amortization expense."[20] Similarly, Staff stated that WGL's response to Staff DR 34-4 identified the smaller subset of retired software that has been replaced. In Staff DR 28-1, WGL was asked to explain whether certain 10-year depreciable software was still in service, and if so, when it would be fully amortized, and

[17] Staff Response at 9.
[18] Staff Response at 10.
[19] Staff Response at 12; Staff Attachment A at 1. The $39,403,936 amount represents software assets ***before*** the Maryland jurisdictional allocation.
[20] Staff Response at Staff Attachment A.

WGL referenced $32,047,247 of software that was retired between August 1, 2017 and January 1, 2018.[21] Finally, Staff states that Staff DR 20-4 requested WGL to provide all other amortizable assets (not software), and WGL provided a list of $4,333,923 of other amortizable assets that were fully amortized as of December 31, 2018.[22]

Commission Decision

The Commission denies rehearing regarding BCO-16 (fully amortized software). Staff correctly notes that WGL does not argue that the assets identified in Staff witness Ostrander's adjustment have not been fully amortized. Moreover, WGL's Petition for Rehearing is the first time that the Company has argued that its response to OPC DR 1-99 provides software and other amortizable assets that are used and in service. For example, the WGL witness who testified regarding software expense (Mr. Tuoriniemi), did not address OPC DR 1-99 in his Direct, Rebuttal, or Rejoinder Testimony. WGL did not cross examine Mr. Ostrander regarding OPC DR 1-99, nor did the Company address it in its post-hearing brief. Most importantly, Mr. Ostrander's testimony regarding fully amortized software was informed by the Company's responses to several Staff data requests. WGL's responses to Staff DRs 20-10, 34-4, 28-1, and 20-4 indicate that the software and other amortizable assets are retired, not in service, and fully amortized. WGL's Petition for Rehearing on this issue is therefore contrary to the preponderance of the evidence and is denied.

[21] Staff Response at 14; Staff Attachment C at 1. Staff states that WGL indicated that only Work Order No. C1000356 remained in the cost of service at March 31, 2018, with all other software retired. Staff Response at 14-15.

[22] Staff Response at 16; Staff Attachment D at 3. Asked why the Company did not exclude amortization expense and related assets that are fully amortized by December 31, 2019,WGL responded: "Fully amortized property was overlooked in the calculation of amortization expense." Staff Attachment D at 2.

B. OPC Petition for Rehearing

OPC petitioned the Commission for rehearing or clarification regarding revenue allocation. Specifically, OPC contends that the Commission should recalculate its two-step allocation process to allocate less of the revenue requirement to the residential class. In support of that argument, OPC observes that in step one, Order No. 88944 allocated 15% to the two customer classes with a current unitized rate of return ("UROR") below 1.0—RES Heat/Cool and Interruptible customers, with the remaining 85% of the revenue requirement allocated to all classes, except C&I Non-Heat/Non-Cool and GMA Non-Heat/Non-Cool, since those classes were significantly over-earning. OPC maintains that the Order is silent as to how the 15% step-one revenue is to be allocated ***between*** the RES Heat/Cool class and the Interruptible class. Claiming that the Commission's approach to revenue allocation does not require step-one increases to be revenue proportional, OPC argues that at least half of the $4,290,300 step-one increase should be allocated to the Interruptible class. In support of that contention, OPC states that the RES Heat/Cool's UROR is nearly 1.0 (at 0.97), while the Interruptible class has a UROR of 0.41.[23] Alternatively, if the Commission decides to make the step-one increase revenue proportional, OPC asks that it base the step-one allocation on total base rate revenues of the RES Heat/Cool and the Interruptible classes.[24]

In its Response, Staff opposes OPC's Petition for Rehearing. Based on the Commission's two-step revenue allocation in previous rate cases, Staff states that the Commission "clearly intended the allocation of revenue increases within both the first and

[23] OPC Petition for Rehearing at 2.
[24] OPC Petition for Rehearing at 3.

the second steps to be assigned based on each class's proportion of distribution revenues, consistent with Commission precedent."[25]

Commission Decision

The Commission denies OPC's Petition for Rehearing on the issue of revenue allocation. In Order No. 88944, the Commission cited the Potomac Electric Power Company ("Pepco") rate case[26] to describe how the Commission has traditionally employed a two-step methodology for determining inter-class revenue allocations. As observed by OPC, in Order No. 88944, the Commission cited the following language from the Pepco rate case:

> We have developed a general policy of allocating rate increases using a two-step approach. First, a portion of the increase is allocated to under-earning classes to move their rates of return or URORs closer to the system average. In the second step, the remainder of any increase is apportioned to all customer classes based upon the proportion of their class revenues compared to overall system revenues.[27]

Although OPC implies that the Commission may have intentionally omitted from the step-one allocation increase the language stating that revenue allocations will be based on class proportions of distribution revenues, this is not the case. The Commission intended that revenue allocations be assigned based on class proportions of distribution revenue for both steps of the revenue allocation, consistent with past orders. In Order No. 85028, for example, the Commission specifically directed Pepco to apply a step-one revenue increase "to the three under-earning classes … *in proportion to the class distribution revenues compared to the overall revenues of these three classes*."[28] That order similarly directed

[25] Staff Response at 18.
[26] Case No. 9286, *In Re Potomac Electric Power Co.*, 103 Md. PSC 293 (2012) ("Order No. 85028").
[27] Order No. 88944 at 124, citing Order No. 85028 at 124-25.
[28] Order No. 85028 at 125 (emphasis added).

Pepco to apply a step-two allocation based on each included class's share of distribution revenues. In the instant case, the Commission did not intend to deviate from its long-standing practice of assigning revenue allocations based on class proportions of distribution revenues in each step. Accordingly, OPC's Petition for Rehearing on this issue is denied.

C. AOBA Petition for Rehearing

AOBA petitioned the Commission for rehearing and clarification regarding interruptible margin sharing.[29] Although AOBA states that it is not contesting substantive provisions of Order No. 88944, it argues that WGL's December 21, 2018 compliance filing and revised tariffs (as amended by WGL on January 8, 2019), fail to comply with the requirements of Order No. 88944.[30] Specifically, AOBA observes that in its Order, the Commission accepted the recommendations of AOBA and OPC to eliminate WGL's participation in the sharing of interruptible (non-firm) revenue margin sharing, and found: "There is nothing in the record to suggest that margin pricing provides any tangible incentive for customers to adopt interruptible service…"[31] Despite that directive, AOBA claims that WGL failed to amend its tariff to fully eliminate margin sharing. AOBA states that WGL's tariff provisions "continue to recognize only 90.9% of Interruptible base rate revenue in its determination of class revenue requirements and rates."[32] AOBA further

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[29] AOBA's Petition for Rehearing also addresses issues that were raised in AOBA's January 4, 2019 Motion to Reject the Washington Gas Light Company Compliance Filing of December 21, 2018 ("AOBA Motion to Reject.") Those issues were addressed in the January 30, 2019 Administrative Meeting (Item No. 6) and resolved in the Commission's January 30, 2019 Letter Order addressing Mail Log Nos. 223383, 223466, 223522, and 223651. AOBA and WGL also presented argument regarding margin sharing during the January 30, 2019 Administrative Meeting.

[30] AOBA Petition for Rehearing at 4.

[31] *See* Order No. 88944 at 130-31.

[32] January 25, 2019 Comments of The Apartment and Office Building Association of Metropolitan Washington Pursuant to the Commission's January 14, 2019 Notice of Opportunity to Respond ("AOBA Comments"), at 6.

claims that "the Company is still retaining funds for margin sharing despite the Commission's determination in its Order No. 88944…that it was terminating Interruptible margin sharing."[33] AOBA concludes that the Company's tariff provisions should be amended to recognize 100% of interruptible revenue in the setting of the final base rates, and that interruptible service revenues should be credited to all customers, not just firm customers.[34]

WGL responds that it has fully complied with Order No. 88944.[35] First, WGL states that its January 8, 2019 tariff filing clarified that "any interruptible margins received between the 90.9% and 100% range would be returned to firm customers."[36] The Company asserts that it no longer recognizes margin sharing for itself, in conformity with the Order. Additionally, WGL asserts that Order No. 88944 required the Company to eliminate margin sharing for itself, not to eliminate margin sharing from its Maryland tariff altogether.[37] For example, the results of the annual Interruptible Rate Adjustment ("IRA") should still flow through the Firm Credit Adjustment ("FCA") mechanism to credit interruptible revenues to firm customers.

Second, WGL states that Schedule B of its Compliance Filing reflects 90.9% of interruptible revenues "for the sole purpose of supporting the IRA, which the Commission did not revise or remove."[38] According to the Company, any implication by AOBA that the IRA should be further amended or abrogated is incorrect.

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[33] AOBA Motion to Reject at 6.
[34] AOBA Comments at 8.
[35] January 25, 2019 Response of Washington Gas Light Company ("WGL Response") at 3-4.
[36] WGL Response at 4, citing Mail Log No. 223522, Fourth Revised Page No. 77.
[37] WGL Response at 5.
[38] WGL Response at 3-4.

Third, WGL states that pursuant to the IRA, interruptible customers are responsible for the entire interruptible class revenue requirement, such that when interruptible service revenues fall short of 90.9%, WGL will collect the shortfall through the IRA and credit the full amount to firm ratepayers; and when interruptible service revenues exceed the interruptible revenue requirement, the Company will credit interruptible customers through the IRA. That reconciliation takes place in the annual Actual Cost Adjustment, which was established through settlement in Case No. 8990.[39]

Fourth, WGL contends that AOBA's argument that interruptible revenues between 90.9% and 100% should be shared with all classes "flatly contradicts the essential purpose underlying the settlement in Case No. 8990, which was to hold the Company *and firm service customers* harmless from the move to cost-of-service pricing for interruptible service."[40]

Finally, WGL argues that AOBA's contention that the interruptible class should be credited with 100% of its distribution charge revenue rather than 90.9% is contradicted by the settlement language of Case No. 8990, which provides that the interruptible customer class is guaranteed only 90.9% of interruptible margins.[41]

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[39] *In the Matter of the Investigation into Washington Gas Light Company's Regulation of Interruptible Service*, Case No. 8990, Order No. 80130 (2005). WGL states that the current phase of the Actual Cost Adjustment will take place in Case No. 9509(m).

[40] WGL Response at 4 (emphasis in original).

[41] WGL Response at 5.

Commission Decision

The Commission denies AOBA's Petition for Rehearing regarding interruptible margin sharing. The Company has amended its Maryland tariff (through its Fourth Revised Page No. 77, among other revisions), to eliminate margin sharing for WGL. No other tariff revisions are necessary. In particular, the Commission finds that Order No. 88944 does not require that WGL remove or further modify the IRA tariff language, which ensures that the interruptible class covers 100% of its Commission-approved revenue requirement, and which allows the results of the annual IRA calculation to flow through the FCA to credit interruptible revenues to firm customers. It was not the intention of the Commission through Order No. 88944 to eliminate margin sharing entirely from WGL's tariff. The Commission also agrees with WGL that interruptible revenues between 90.9% and 100% should not be shared with all classes, because the settlement in Case No. 8990 established that the Company and firm service customers should be held harmless from the move to cost-of-service pricing for interruptible service. That settlement language further provides that the interruptible customer class is guaranteed only 90.9% of interruptible margins.[42] Because the Commission finds that WGL's compliance filing properly reflects the Commission's intent regarding interruptible margin sharing, AOBA's Petition for Rehearing on that matter is denied.

IT IS THEREFORE, this 25th day of June, in the year Two Thousand Nineteen, by the Public Service Commission of Maryland,

[42] WGL Response at 5.

ORDERED: (1) That the Petition for Rehearing of Washington Gas Light Company is granted in part and denied in part, as explained in the body of this Order;

(2) That Washington Gas Light Company is directed to file revised tariffs in compliance with this Order with an effective date of December 11, 2018, subject to acceptance by the Commission;

(3) That the Petition for Rehearing of the Maryland Office of People's Counsel is denied; and

(4) That the Petition for Rehearing of the Apartment and Office Building Association of Metropolitan Washington is denied.

By Direction of the Commission,

/s/ Terry J. Romine

Terry J. Romine
Executive Secretary