ORDER NO. 89799

Washington Gas Light Company's Application for Authority to Increase Its Rates and Charges	* * * * * * *	BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND __________ CASE NO. 9651 __________

Issue Date: April 9, 2021

ORDER ON APPEAL OF PROPOSED ORDER

1. Washington Gas Light Company ("Washington Gas" or "WGL"), the Apartment and Office Building Association ("AOBA"), and the Office of People's Counsel ("OPC") have appealed the Proposed Order of the Public Utility Law Judge ("PULJ"), setting new rates for Washington Gas customers. For the reasons outlined below, the Proposed Order is affirmed with one modification.

Background

2. On August 28, 2020, Washington Gas filed an Application for Authority to Increase its Existing Rates and Charges and to Revise Its Terms and Conditions for Gas Services.[1] On August 31, 2020, the Commission delegated the matter to the PULJ Division to conduct evidentiary proceedings. On February 12, 2021, the PULJ issued its

[1] Maillog No. 231646.

Proposed Order.[2] Washington Gas,[3] AOBA,[4] and OPC[5] each filed appeals from that Proposed Order. Subsequently, Washington Gas,[6] AOBA,[7] OPC,[8] and Commission Staff ("Staff")[9] filed Reply Memoranda.

3. On March 17, 2021, Washington Gas filed a stipulation (the "Stipulation"), providing that "for the sole purpose of extending the deadline for the Commission to issue its Final Order as required under PUA § 4-204(b)(2), the Application will be deemed filed on September 28, 2020" and that "[s]hould the Commission issue its order on or before April 25, 2021, Washington Gas will not assert in any forum that the Application is approved by operation of law under PUA § § 4-204(b)(2)."[10]

4. On March 23, 2021, Washington Gas filed a Motion for Clarification and or Authorization.[11] That motion requested, in light of the Stipulation, that the Commission authorize Washington Gas to recover the otherwise-resulting difference in operating revenue from that approved in this Order, as if it were effective March 26, 2021, through its Commission-approved Revenue Normalization Adjustment ("RNA").

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[2] Maillog No. 233744. The PULJ issued an Errata to the Proposed Order on February 19, 2021. Maillog No. 233832. This Order will treat Maillog No. 233832 as the Proposed Order for reference purposes.
[3] Maillog No. 233953 ("WGL Appeal").
[4] Maillog Nos. 233955 and 233956 ("AOBA Appeal").
[5] Maillog No. 233954 ("OPC Appeal").
[6] Maillog No. 234083 ("WGL Reply").
[7] Maillog No. 234087 ("AOBA Reply").
[8] Maillog No. 234088 ("OPC Reply").
[9] Maillog No. 234111 ("Staff Reply").
[10] Maillog No. 234236.
[11] Maillog No. 234300, subsequently amended on March 24, 2021 in Maillog No. 234316.

Issues on Appeal

I. Washington Gas's Appeal

5. Washington Gas raises three issues in its appeal: (1) challenging the PULJ's denial of Washington Gas's proposed non-labor inflation adjustment; (2) challenging the PULJ's denial of Washington Gas's proposed alternative capital structure, based on its "actual test-year-ending capital structure"; and (3) challenging the Proposed Order's approved Rate of Return ("ROR"), arguing that it contained a rounding error.

A. Washington Gas's proposed non-labor inflation adjustment

6. In its Application, Washington Gas proposed Adjustment 21, which would have added a non-labor inflation adjustment based on the Consumer Price Index ("CPI").[12] Adjustment 21 was opposed by AOBA, which argued that CPI was not an appropriate measure of inflation, and by Staff, which argued that an inflation adjustment was not necessary due to customer growth, and the Proposed Order found that the adjustment was unwarranted.[13]

7. Washington Gas now appeals that decision. It argues that the requested adjustment is below the 7.7% annual growth rate in the company's non-labor operation and maintenance ("O&M") expenses from 2015 to 2020.[14] It also argues that the Commission allowed Baltimore Gas and Electric Company ("BGE") and Potomac Electric Power Company ("Pepco") to make similar adjustments in prior rate cases, Case Nos. 9484, 9645, and 9602.[15] It also argues that Staff's argument regarding customer growth rates was rejected by the Commission in Case No 9484. It also argues that

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[12] Proposed Order at 10; WGL Appeal at 3.
[13] Proposed Order at 10.
[14] WGL Appeal at 3.
[15] *Id*. at 3-5.

AOBA's concerns with the CPI were rejected in Case No. 9602, where an adjustment based on CPI was approved.

8. Washington Gas's position on this issue is opposed by AOBA and Staff.

1. AOBA's opposition

9. In its Reply, AOBA states that its witness, Bruce Oliver, presented multiple substantive grounds for why the treatment of non-labor costs in this proceeding should be differentiated from that of BGE: (1) In Washington Gas's five prior proceedings, it has never requested a non-labor inflation adjustment; (2) Washington Gas has failed to show that inflation is a major driver of its non-labor distribution O&M expenditures; (3) Washington Gas has failed to address the influences on its non-labor distribution expenses of several factors; (4) Washington Gas has not shown that the mix of goods and services reflected in the CPI is comparable to the mix of goods and services that have been or will be purchased by Washington Gas; and (5) Washington Gas has not addressed the extent to which its proposed generalized application of a non-labor inflation adjustment might serve to offset cost savings that it has previously indicated would flow to ratepayers as a result of its BPO 2.0 outsourcing activities.[16]

10. AOBA also states that its cross-examination of Washington Gas witness Tuoriniemi established that: (1) Washington Gas's actual non-labor O&M costs for the test year were down $2.7 million (3.0%) below those of the immediately preceding 12-month period; (2) the decline in Washington Gas's non-labor O&M costs was three times larger than the upward adjustment it seeks in Adjustment 21; and (3) the preceding 12-month period followed a 12-month period where non-labor O&M costs increased by

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[16] AOBA Reply at 4.

nearly 30%, for which Washington Gas has offered no explanation.[17] AOBA also states that witness Tuoriniemi acknowledged in cross-examination that "the test year unadjusted in this circumstance is representative of the level cost going forward."[18]

11. AOBA concludes that the record supports the rejection of Adjustment 21 contained in the Proposed Order and that Washington Gas's request to reverse that decision should be denied.

2. Staff's opposition

12. In its Reply, Staff reiterates its opposition to Washington Gas's Adjustment 21. Staff argues that Adjustment 21 is "one-sided" and ignores additional revenues that will be realized during the rate-effective period from new customer additions and anticipated earnings, resulting in an unjustified upward impact on rates.[19] Staff states that WGL data shows that revenues from customer additions exceed the potential impact of inflation on Washington Gas's expenses.[20]

13. Staff also states that, in Case No. 9484, the Commission approved an inflation adjustment for BGE but noted that such adjustments are to be examined on a case-by-case basis.[21] Staff states that Washington Gas witness Touriniemi's Exhibit RET-6 demonstrated that costs are in a downward trend.[22] Staff also argues that the CPI tracks a very different basket of goods from those comprising Washington Gas's O&M expenses and is not an accurate reflection of inflation for those expenses.[23]

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[17] *Id*. at 5.
[18] *Id*. at 5-6.
[19] Staff Reply at 10-11.
[20] *Id*. at 11.
[21] *Id*.
[22] *Id*.
[23] *Id*. at 11-12.

14. Staff concludes that Washington Gas's proposed inflation adjustment for non-labor O&M expenses is not supported and that the PULJ was justified in rejecting it.[24]

Commission Decision

15. The Commission finds that the PULJ's decision to reject Washington Gas's proposed inflation adjustment was correct. Although Washington Gas correctly notes that the Commission has in some cases approved inflation adjustments similar to that requested by Washington Gas, such an adjustment is not automatic but depends on a showing by the utility that the adjustment is necessary for resulting rates to be fair, just, and reasonable.

16. The Commission is unpersuaded by Staff's and AOBA's argument that the CPI may not perfectly align with Washington Gas's cost increases for non-labor O&M. Particularly given the Commission's recent approval of increased reliance on forecasting in rate cases,[25] the Commission expects and encourages utilities and interested parties to test other indices and methods of cost forecasting, with an eye toward improving the ratemaking process in Maryland. Nonetheless, until superior methods can be developed, the Commission has and will continue to utilize the CPI and other indices so long as the evidence shows that doing so makes rates more fair, just, and reasonable.

17. Nonetheless, the parties have identified factual disputes in the record over both whether inflation is driving increased non-labor O&M costs and whether increased revenue from forecasted customer growth (not otherwise accounted for) will offset any non-labor O&M inflation. The evidence and testimony identified by Staff and AOBA on

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[24] *Id*. at 12.
[25] *See* Case No. 9618.

those points raise serious concerns with the proposed adjustment, and Washington Gas has not presented persuasive evidence to assuage those concerns. The Commission also observes that while Washington Gas in this case has shown recent customer growth, BGE in Case No. 9645 (the Pilot multi-year rate case upon which Washington Gas chiefly relies) projected flat-to-low customer growth.[26] Additionally and as noted by the Commission in its decision in Case No. 9645, customers in that case are protected from an overestimation of inflation or underestimation of customer growth by the reconciliation process of the multi-year rate plan process.[27] No such protections exist in this case. The Commission therefore finds that in this case the PULJ's rejection of the non-labor O&M inflation adjustment should be affirmed.

B. Washington Gas's proposed alternative capital structure

18. In its Application, Washington Gas proposed a capital structure based on an average of the capital structures from each of the four quarters of financing within the test year. During the rate case, Washington Gas later proposed an alternative capital structure that was adjusted to account for a debt issuance in September 2019 and an equity infusion in March 2020 (the last month of the test year) – a "terminal"[28] or "actual test-year-ending"[29] capital structure.[30] Staff argued against those adjustments and in favor of a capital structure similar to that originally proposed by Washington Gas and based on the average of the actual capital structure during each of the four quarters of the test year – an

[26] Order No. 89678 at 51 - 54.
[27] *Id*. at 54, 61.
[28] A term used by Staff. Staff Reply at 3.
[29] A term used by Washington Gas.
[30] WGL Ex. 8, Bonawitz Direct at 9-24.

"average capital structure."[31]

19. In the Proposed Order, the PULJ noted that the "Commission[] has long stated its strong preference for the use of the actual test-year-ending capital structure"[32] but ultimately rejected Washington Gas's proposed alternative capital structure and instead found that Staff's proposed capital structure was most appropriate.[33]

20. Washington Gas now appeals that decision, arguing that the Commission should approve the Company's proposed alternative capital structure. Washington Gas argues that the capital structure approved in the Proposed Order does "not properly account for recent, test year financing activity."[34] Washington Gas states that the Commission has demonstrated flexibility in establishment of a capital structure but also quotes the Commission's recent decision in Case No. 9645 for the rule that "long-standing precedent in Maryland is that a utility's actual test-year-ending capital structure should be used when determining its authorized rate of return in a base rate proceeding."[35] Washington Gas states that it only offered (in surrebuttal testimony) the alternative capital structure now at issue on this appeal as a result of that decision.[36]

21. Washington Gas's position on this issue is opposed by AOBA, OPC, and Staff.

1. AOBA's opposition

22. In its Reply, AOBA states that this argument by Washington Gas is being raised for the first time on this appeal and was not made before the PULJ, where Washington

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[31] Staff Ex. 21, at 20.
[32] Proposed Order at 12, at para 29, citing Case No. 9645, Order No. 89678, at 348.
[33] Proposed Order at 12, at para 29.
[34] WGL Appeal at 7.
[35] *Id*. at 7.
[36] *Id*. at 8.

Gas proposed a capital structure based on a four-quarter average.[37] AOBA states that Washington Gas's capital structure historically varies and has never been maintained at the level of the test-year ending capital structure throughout the rate effective period.[38]

23. AOBA notes that its recommended capital structure differs from that of Staff in its treatment of preferred stock, which Staff has treated as common equity, while AOBA states that it is more appropriate to treat it as debt.[39] Nonetheless, AOBA states that both its and Staff's capital structures are in line with the capital structure Washington Gas requested in Formal Case No. 1162, before the District of Columbia Public Service Commission, which was based on a test year three months earlier than the test year in this proceeding.[40]

2. OPC's opposition

24. In its Reply, OPC argues that Washington Gas's alternative capital structure should be rejected because it is contrary to Washington Gas's pre-filed testimony and primary case, wherein it argued in favor of a capital structure based on an adjusted average across the test year.[41] OPC argues that the PULJ's decision to accept the four-quarter averaging approach was thus what Washington Gas itself had argued for in its case.[42]

25. OPC also argues that Washington Gas's alternative capital structure is not representative of test year conditions because the impact of an equity infusion in the final

[37] AOBA Reply at 6-8.
[38] *Id*. at 7-8.
[39] *Id*. at 9.
[40] *Id*. at 9.
[41] OPC Reply at 2-4.
[42] *Id*. at 5.

quarter of the test period increased the equity ratio "far beyond" the levels in the two previous quarters.[43]

26. OPC finally argues that Washington Gas's alternative capital structure is not appropriate under the facts of this case.[44] OPC states that, while the Commission's general practice is to use a utility's actual test-year-ending capital structure, the Commission has also said that the practice is not "immutable" and has utilized a hypothetical capital structure when a utility's actual test-year-ending capital structure is too equity heavy.[45] OPC argues that Washington Gas's proposed alternative capital structure is too equity heavy and thus the PULJ correctly applied a hypothetical capital structure in setting rates.[46]

3. Staff's opposition

27. In its Reply, Staff states that Washington Gas's proposed capital structure would, among other things, increase its equity ratio from 51.58% to 54.55% and would impose an undue burden on ratepayers because of the much higher costs of equity compared to debt.[47] Staff argues that utilities have a financial incentive to adopt a capital structure with an excessive equity ratio and cites to a decision of the Washington, DC Public Service Commission (also a Washington Gas rate case) wherein that body noted that "the focus of the Commission's capital structure determination must be placed on achieving

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[43] *Id*.

[44] *Id*. at 1.

[45] *Id*. at 6-7, quoting Order No. 87591 at 166, *In the Matter of The Application of Baltimore Gas and Electric Company for Adjustments to Its Electric and Gas Base Rates* (Case No. 9406, June 2016), also citing Order No. 86013 at 5, *In the Matter of the Application of Washington Gas Light Company for Authority to Increase Its Existing Rates and Charges and To Revise Its Terms and Conditions for Gas Service* (Case No. 9322, November 2013).

[46] OPC Reply at 7.

[47] Staff Reply at 4-5.

'the lowest cost of service that is consistent with a sound financial posture' for [WGL's] stand-alone utility operations."[48]

28. Staff also quotes this Commission's 2013 decision in a Washington Gas rate case, wherein the Commission determined that Washington Gas's actual equity ratio of 60.8% would result in excessive rates and instead calculated rates based on an imputed equity ratio of 53.02%, for the rule that the Commission "may modify a Company's capital structure for ratemaking purposes when the actual capital structure would impose an undue burden on ratepayers."[49]

29. Staff also quotes Case No. 9406, in which the Commission found that BGE's proposed equity ratio of 53.7% "impose[d] an undue burden on ratepayers" and instead adopted an imputed capital structure based on a 51.9% equity ratio.[50]

30. Staff also compares Washington Gas's proposed equity ratio to other equity ratios used by Washington Gas and other utilities in other cases, and in some cases other jurisdictions.[51] For example, Staff states that the average equity ratio approved in litigated rate cases before the Commission since 2010 is 51.14%, 341 basis points below Washington Gas's proposed equity ratio.[52] Staff also states that Washington Gas's proposed equity ratio is 181 basis points above the 52.74% equity ratio[53] established in its

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[48] Staff Reply at 5, citing DC PSC, Docket FC 1137, at 13.

[49] Staff Reply at 5-6, quoting *In the Matter of the Application of the Washington Gas Light Company to increase its existing rates and charges and to revise its terms and conditions for gas service*, Case No 9322, Order No. 86013, slip op. at 10 (2013).

[50] Staff Reply at 6, citing *In the Matter of the Application of Baltimore Gas and Electric Company for adjustments to its electric and gas base rates*, Case No. 9406, Order No. 87591, at 169 (2016).

[51] Staff Reply at 6-7.

[52] *Id*. at 6; McAuliffe Direct. Staff Ex. 21, at 22.

[53] Staff calculates this number based on 51.69% common stock and 1.05% preferred stock. Staff Reply at 7.

most recent prior litigated rate case, Case No. 9481.[54]

31. Staff also argues that Washington Gas has obtained its higher equity ratio by leveraging risk from other non-regulated assets owned by its parent company, AltaGas, which has relied, in part, on debt issuance to provide equity infusions to Washington Gas.[55] Staff argues that AltaGas could undo the equity infusion after this rate case by transferring funds back to AltaGas, though Washington Gas has stated that it will not do this.[56]

32. Staff argues that relying on the average capital structure is appropriate in this case because it reflects the fact that there are regular changes in capital structure and an average provides a longer-term view of the capital structure than a snapshot, which may not reflect the normal capital structure.[57]

Commission Decision

33. Although Washington Gas correctly notes that the Commission has historically expressed a preference for using the actual test-year ending capital structure, the Commission's duty to set fair, just, and reasonable rates also requires it to consider whether any proposed capital structure would impose an undue burden on ratepayers due to the impact of capital structure on the utility's overall ROR. Accordingly, it is the Commission's "long-standing policy to base the utility's return on its actual capital structure absent evidence that the actual capital structure would impose an undue burden

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[54] Staff Reply at 7.
[55] *Id*. at 8-9.
[56] *Id*. at 9.
[57] *Id*. at 9-10.

on ratepayers."[58] The Commission's decision in Case No. 9645 does not represent a deviation from that policy, notwithstanding the fact that the Commission did not reference in that case the issue of undue burden caused by excess equity capitalization; that issue was not argued in that case.

34. For example, in Case No. 9322, the Commission considered an appeal from a PULJ proposed order that reduced WGL's equity ratio (among other things), which was "nearly 300 points" higher than that used in WGL's then-prior rate case, stating that WGL's preferred equity ratio was "too high for a company facing as little real risk as WGL."[59] The Commission chose to set WGL's rates based on an imputed equity ratio of 53.02%, noting that to do otherwise would provide WGL an unfair windfall, at the expense of ratepayers.[60] As noted by Staff above, the Commission has consistently followed this practice and utilized imputed equity ratios in cases where excess equity capitalization creates an undue burden on ratepayers.

35. Here, Washington Gas's proposed alternative capital structure calls for an equity capitalization (54.55%) that is significantly higher than both Washington Gas's own recent historical capital structures and the capital structures that the Commission has recently approved for other utilities. In Washington Gas's only other fully litigated rate case in the last five years, the Commission approved a common equity percentage of 51.69% plus 1.05% preferred stock.[61] The Commission-approved equity percentages for

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[58] *In the Matter of the Application of Pepco for Authority to Increase its Rates and Charges for Electric Distribution Service*, Case No. 9311, Order No. 85724 at 109 (2013).
[59] Order No. 86013, at 3 and 8.
[60] *Id*. at 11.
[61] Case No. 9481, Order No. 88944 at 100.

other utilities in fully litigated rate cases begun since 2019 have been 52.00%,[62] 50.53%,[63] and 50.46%.[64]

36. The effect of this increased equity capitalization in this case would be higher customer rates (holding static the Return on Equity ("ROE") and cost of debt); however, Washington Gas has made no argument in this appeal as to why a greater than normal equity capitalization is necessary for its operations. This concern is not alleviated by Washington Gas's representations that it intends to maintain a stable capital structure throughout the rate-effective period because rates would still be unduly elevated based on excessive equity capitalization and the higher returns thereon.

37. The PULJ's decision to set an imputed capital structure based on WGL's average quarterly capital structure (resulting in an equity capitalization of 52.03%, which is in line with prior approved ratios of WGL and other utilities, as noted above and by Staff) was therefore appropriate and consistent with past Commission practice. Washington Gas's request to set rates based on its alternative capital structure is denied.

C. Washington Gas's challenge to the Proposed Order's rounding in its Rate of Return calculation

38. As part of its calculation of Washington Gas's revenue requirement, the Proposed Order set an ROR for Washington Gas's assets of 7.08%.[65] On appeal, Washington Gas argues that the Proposed Order erroneously truncated the fourth digit in the ROR, which Washington Gas states was 7.086%, and requests that the Commission round rather than

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[62] As part of a combined gas and electric case for Baltimore Gas and Electric Company, Case No. 9465, Order No. 89678 at Appendix B.

[63] As part of a combined gas and electric case for Delmarva Power and Light Company, Case No. 9630, Maillog No. 230768.

[64] As part of an electric case for Potomac Electric Power Company, Case No. 9602, Maillog No. 225999.

[65] Proposed Order at 14-15, at para 37.

truncate, resulting in an ROR of 7.09%.[66] Washington Gas argues that this methodology has been previously applied in prior case cases for itself and BGE.[67]

39. Washington Gas's position is opposed by AOBA. OPC and Staff offer no comment or position on this issue.

1. AOBA's opposition

40. In Reply, AOBA cites National Center for Education Statistics Standard 5-3-4 for the following rule: "In multiplying or dividing numbers using data from secondary sources, the resulting precision cannot be more precise than that of any of the component numbers."[68] AOBA states that Washington Gas's own capital structure calculations do not use more than three significant digits.[69] AOBA argues that the rounding requested by Washington Gas is therefore inappropriate.[70] AOBA also states that this request would result in $173,000 in additional annual revenue for Washington Gas.[71]

Commission Decision

41. The Commission finds that Washington Gas's concerns regarding the use of rounding of the ROR to be reasonable and that rates should be set based on an ROR of 7.09%, as a result of rounding to three significant digits. That result is consistent with both the evidence in the record, which shows a consistent minimum of three significant digits, and with Commission historic practice, as noted by the parties above.

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[66] WGL Appeal at 9.
[67] *Id*.
[68] AOBA Reply at 12.
[69] *Id*. at 13.
[70] *Id*.
[71] AOBA Reply at 11.

II. AOBA's Appeal

42. On appeal, AOBA makes three arguments: (1) challenging the allocation of federal income taxes across the jurisdictions where Washington Gas operates; (2) challenging the Proposed Order's approved Return on Equity; and (3) requesting the Commission implement an incentive structure.

A. AOBA's challenge to the allocation of federal income taxes across the jurisdictions where Washington Gas operates

43. AOBA argues that the Proposed Order failed to address AOBA's argument that a disproportionately high share of Washington Gas's federal income tax burden is allocated to Maryland ratepayers.[72] AOBA states that this is caused in part by the fact that the District of Columbia Public Service Commission has awarded Washington Gas a much lower ROR than the Utility's Maryland and Virginia regulators and because income taxes are a function of equity return contributions by each jurisdiction.[73] AOBA recommends that test year revenues should be adjusted for each jurisdiction to reflect Washington Gas's overall average rate of return, which would reduce Maryland's share of the federal income tax expense from approximately $10 million to less than $5 million.[74]

1. Washington Gas's opposition

44. In Reply, Washington Gas argues that AOBA's argument should be rejected. Washington Gas argues that the calculation of Company Adjustment 34 (concerning federal income tax) follows Commission precedent and presents no methodological changes from the study performed in prior cases.[75] Washington Gas states that company

[72] AOBA Appeal at 6.
[73] *Id*. at 7-8.
[74] *Id*. at 8-9.
[75] WGL Reply at 8, citing Case Nos. 9481 and 9605.

witness Gibson explained that income taxes are directly assigned, not allocated, and the difference in effective tax rates is driven in part by ratemaking treatments and in part by regulatory lag.[76] Washington Gas further argues that AOBA's proposal is flawed and out of step with basic ratemaking principles for two reasons: (1) it incorrectly begins with unadjusted test year results; and (2) it inappropriately focuses on a comparison of rate base instead of taxable income.[77]

Commission Decision

45. Adoption of AOBA's approach would result in WGL being unable to recover all of the income tax it actually pays. AOBA's novel proposal is inconsistent with past Commission treatment of income taxes, and the Commission declines to adopt it based on the record presently before it.

B. AOBA's challenge to the Proposed Order's approved Return on Equity

46. As part of its rate calculation, the Proposed Order set an ROE of 9.70%.[78] In so finding, the PULJ considered competing approaches and resulting ROE ranges from Washington Gas, Staff, OPC, and AOBA.[79] The PULJ also noted that Washington Gas's two prior rate cases in Maryland had set an ROE of 9.70% and its current approved ROEs in Virginia and the District of Columbia were 9.2% and 9.25%.[80]

47. On appeal, AOBA disputes the ROE set in the Proposed Order, which AOBA argues was without record evidence or fair comparison to prior ROE determinations.[81]

[76] WGL Reply at 8-9.
[77] *Id*.
[78] Proposed Order at 14-15, at para 37.
[79] *Id*. at 13-15.
[80] *Id*. at 14, at para 35-36.
[81] AOBA Appeal at 10.

AOBA argues in favor of a 9.25% ROE, which it states would be in line with those approved in Virginia and the District of Columbia.[82] AOBA also argues that the Proposed Order's 9.70% ROE failed to account for falling interest rates.[83] AOBA also argues that in the Proposed Order the PULJ offered no indication of the weight given to each of the parties' presentations and did not explain why a continuation of Washington Gas's current ROE was appropriate.[84]

1. Washington Gas's opposition

48. In Reply, Washington Gas argues that the Proposed Order's ROE determination was supported by the record and should be affirmed. Washington Gas argues that the "most compelling" record evidence omitted from AOBA's appeal is the Commission's December 2020 ROE determination of 9.65% for the gas division of BGE in Case No. 9645.[85] Washington Gas states that the Proposed Order compared this case to Case No. 9645 and noted that the MRP Pilot in that case reduced risk and that gas companies should have higher returns than electric companies.[86] Washington Gas also states that the financial and economic data from the Virginia and District of Columbia cases cited by AOBA were based on information from "as long ago as 2017 and 2019" and argues that the Proposed Order "properly characterized" the findings of other jurisdictions as "indirect comparison."[87] Washington Gas also states that AOBA improperly relies on a settlement agreement (to which AOBA was a party) from a District of Columbia case

[82] *Id*. at 10-13.
[83] *Id*. at 11.
[84] *Id*.
[85] WGL Reply at 12.
[86] *Id*. at 13.
[87] *Id*.

where the terms of the agreement expressly precluded citation for any purpose other than to enforce the settlement.[88]

Commission Decision

49. Although AOBA objects to the level of explanation provided in the Proposed Order, the Commission does not set any specific methodology or formula for generating ROE determinations.[89] On this question, the record contains the expert testimonies of WGL witness Dylan D'Ascendis, Staff witness Drew M. McAuliffe, OPC witness David J. Garrett, and AOBA witness Timothy Oliver. Consistent with the Commission's openness to different methodologies, those witnesses each applied multiple methods of financial analysis to the ROE question and then attempted to synthesize those results into a final recommendation, resulting in a wide range of recommended ROEs, from a high of 10.45% to a low of 9.00%.[90] The Commission has reviewed the testimonies of those witnesses and finds that the PULJ's decision to set rates based on an ROE of 9.70% was reasonable and supported by substantial evidence.

50. The PULJ's decision is also in line with recent Commission decisions (most notably the 9.65% used for BGE's gas rates in Case No. 9645). In comparison, AOBA's recommended 9.25% ROE would be a significant outlier, far below any recent ROE approved by the Commission for a gas utility. AOBA's request is therefore denied.

C. Proposal to implement an incentive structure to reduce gas leaks

51. Third, AOBA states that Washington Gas has seen eroding safety and rising numbers of hazardous leaks on its distribution systems, leading to more than four times

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[88] *Id*.

[89] *See* Case No. 9326, Order No. 86060 at 76 ("We find all of these analytical tools helpful and will not rely on any one to the exclusion of the others in making our decision.").

[90] *See* Staff Comparison Chart of Party Positions, Maillog No. 233231.

the national averages of unaccounted-for gas.[91] AOBA asks the Commission to implement an incentive structure to improve these metrics.

1. Washington Gas's opposition

52. In Reply, Washington Gas opposes AOBA's proposal. Washington Gas argues that AOBA's argument does not identify any mistake of law or other error that would form a basis for appeal.[92] Washington Gas also argues that AOBA failed to provide sufficient information with respect to its proposal for it to be evaluated.[93] Washington Gas also argues that AOBA did not propose a specific adjustment based on its analysis.[94]

Commission Decision

53. The Commission notes AOBA's concerns regarding hazardous leaks and its initiative in proposing a performance incentive structure. The Commission has recently established a framework for testing performance incentives as part of PC51 and Case No. 9618. The Commission has reviewed AOBA's proposal and finds that it is premature.

III. Office of People's Counsel's Appeal

54. OPC appeals six issues from the Proposed Order.

A. OPC's argument that the Proposed Order ignored its argument that Washington Gas's corporate costs, under proposed adjustment 20, should be reduced by $4,259,730

55. OPC cites to Commission Order No. 88631 in Case No. 9449 (the "AltaGas Approval Order"), in which the Commission held that synergy savings from the merger would "lower customer distribution rates and thereby help satisfy the benefits prong of

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[91] AOBA Appeal at 13-14.
[92] WGL Reply at 7.
[93] *Id*.
[94] *Id*.

the statute [PUA § 6-105]."[95] The Commission ensured these savings by including two commitments in Appendix A of the AltaGas Approval Order – Commitments 28 and 44.

56. Commitment 28 required Washington Gas to file side-by-side comparisons of corporate and shared-services costs at the end of the second quarter following one year post-merger, using 2016's costs as the baseline. Commitment 44 required WGL to track and account for merger-related savings, as well as the transition costs that enabled those savings, in the Company's next two base rate proceedings in which the test-year in question includes transition costs. This commitment further required Washington Gas to amortize transition costs over five years and provided that the Company could not seek recovery of any amortized transition costs or corporate costs allocated from AltaGas to Washington Gas in excess of merger-related savings. Finally, this commitment required Washington Gas to demonstrate financial benefits of at least $800,000 per year for five years post-merger that would not have resulted had the two companies continued to operate separately.

57. OPC contends that Commitments 28 and 44 are intertwined and that Commitment 44 requires Washington Gas to provide a side-by-side comparison of corporate and shared costs in order to establish that the Company has experienced the annual $800,000 in synergy savings. OPC argues that the Company has failed to meet this burden of proof because Witness Tuoriniemi's testimony regarding these savings does not contain any side-by-side comparison of pre- and post-merger costs as required by Commitment 28. Without such a comparison, OPC claims that it cannot determine whether the Company actually provided the required synergy benefits to Maryland ratepayers.

[95] AltaGas Approval Order at 36.

58. Relying upon Witness Tuoriniemi's Rebuttal Testimony, OPC claims that the record supports the conclusion that Washington Gas's corporate costs for the 2016 baseline year were $59,042,090. Total costs for the test-year (April 2019 – March 2020) in the present case were $77,230,393, which reflects an increase of $18,188,303 in overall annual costs following the merger.[96] OPC contends that such an unexpected increase in costs belies Washington Gas's claim that it has delivered on its commitment to achieve annual synergy savings of at least $800,000.

59. OPC argues the unreliability of Washington Gas's assertion should have caused the PULJ to adopt OPC's analysis of post-merger savings. OPC Witness Coppola proposed an adjustment to Adjustment 20 that reduced those corporate and shared-services functions that saw a significant increase in post-merger costs in excess of what might reasonably be expected post-merger.[97] After adjusting the Company's 2016 costs by an annual 2% for inflation, Mr. Coppola compared these costs with his adjusted costs for the test year. After subtracting one-fifth of the Company's amortized transition costs, Mr. Coppola concluded that the Commission should disallow $4,259,730 from Adjustment 20.[98] OPC appeals the PULJ's refusal to do so.

1. Washington Gas's opposition

60. In response, Washington Gas argues that the Proposed Order did address OPC's argument and clearly stated that the PULJ "duly considered the entire record in this

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[96] Citing Tuoriniemi Rebuttal Testimony at Exhibit R-6.

[97] Coppola Direct at 88. Mr. Coppola included in his adjustment Accounting and Tax, Finance, Human Resources, Information Technology, Legal and Compliance, and Supply Chain. Coppola Surrebuttal at Exhibit SC-SR10.

[98] Coppola Surrebuttal at Exhibit SC-SR10.

proceeding, including all the filed and oral testimony and exhibits, taking into account recent Commission Orders."[99]

61. Washington Gas also contends that OPC improperly conflates Commitments 28 and 44 from the Commission's AltaGas Approval Order. The Company argues that Commitment 28 requires Washington Gas to file its annual report every second quarter, whereas Commitment 44 controls the ratemaking implications of its cost allocations. As support, Washington Gas notes that Commitment 28 is contained under the Commitment Heading "Affiliate Requirements", whereas Commitment 44 falls under the heading "Cost Accounting, Tax and Rate Neutrality." Washington Gas also criticizes Mr. Coppola's "manufactured" adjustment to the Company's corporate and shared services.[100] Washington Gas also argues that Mr. Coppola's reliance on Commitment 28's annual report is misplaced because that report does not include capital cost reductions as well as O&M cost reductions.

62. Finally, Washington Gas asserts that the record contains substantial evidence to support the actual savings and costs provided during the course of proceedings. Washington Gas Witness Tuoriniemi testified regarding Washington Gas's "Synergy Analysis," a report which OPC does not address in its appeal.[101] Specifically, Mr. Tuoriniemi testified that test-year synergy savings were $21,703,998 and test-year synergy costs were $18,774,306, with $1,084,503 of those savings attributable to Washington Gas's Maryland territory. After subtracting $255,440 in amortized

[99] Proposed Order at 68.
[100] WGL Reply Brief at 6. The Company also identified several calculating errors within Mr. Coppola's proposed adjustment, forcing OPC to rely upon WGL's rebuttal testimony for the proper amount of synergy costs.
[101] Tuoriniemi Direct at Ex. RET-6.

transaction costs, Mr. Tuoriniemi testified that the Company had achieved a total test-year synergy savings of $829,603, in excess of the annual savings threshold contained in Commitment 44.[102]

Commission Decision

63. The Commission agrees with Washington Gas's contention that Commitments 28 and 44 in the AltaGas Approval Order are separate commitments, and Washington Gas need not rely upon the same data in its annual report to establish overall synergy savings for purposes of Commitment 44. The commitments are contained in two separate sections of Appendix A to the AltaGas Approval Order, and neither commitment refers to the other.

64. Additionally, Commitment 28 explicitly requires Washington Gas to provide the Company's annual report in its next rate case if that case occurs before the first annual report is due. This language strongly suggests that if Washington Gas does not file a base rate case before its first annual report is due, Commitment 28's report is *not* required in Washington Gas's next rate case. Washington Gas did file the Company's Commitment 28 report in the second quarter of 2020. Therefore, the Commission agrees with Washington Gas that Commitment 44 permits Washington Gas more flexibility than OPC contends, so long as it establishes that Maryland ratepayers received over $800,000 in synergy-related savings during the test-year.

65. Mr. Tuorinemi testified that the Company achieved test-year synergy-related savings in Maryland of $829,603, slightly in excess of the annual savings required by Commitment 44. Therefore, the PULJ had substantial evidence in the record upon which

[102] Tuoriniemi Direct at 47.

to conclude that no downward adjustment was necessary to Adjustment 20. The Commission also notes that Commitment 44 does not prohibit recovery of an increase in post-merger costs, so long as the increase in benefits exceeds those costs by greater than $800,000.

B. OPC's argument that the Proposed Order does not address its prudency challenges to many of Washington Gas's capital projects

66. OPC contends that it provided evidence that Washington Gas repeatedly under-estimated the cost of various capital projects for which the actual costs exceeded the original estimated costs in excess of 20%: (1) two non-STRIDE safety and reliability projects;[103] (2) nine STRIDE projects;[104] and (3) three additional significant projects.[105] As an example, Washington Gas's Newport Mill Road project, which entailed the replacement of 1,475 feet of pipe and 11 service lines, had an original cost-estimate of $2,193,460. However, the actual incurred costs were $3,734,004, reflecting an increase of 70%. In response to a data request regarding this project, Washington Gas stated that the causes of this cost-overrun were: (1) the need to limit the number of hours of work near a school; (2) the need to lease additional space to store materials and equipment; and (3) higher paving costs than anticipated.[106]

67. Mr. Coppola testified that these increased costs should have been anticipated and that Washington Gas failed to explain why it did not foresee these requirements initially.[107] For each of the 14 projects for which OPC seeks the Commission to partially disallow recovery, Mr. Coppola testified that Washington Gas failed to act prudently by

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[103] OPC Post-Hearing Brief at 24-26.
[104] *Id*. at 26-34.
[105] *Id*. at 34-40.
[106] Coppola Direct at 26, and attached Response to OPC Data Request 10-05.
[107] Coppola Direct at 26.

relying upon past project costs rather than proactively identifying unique potential cost issues for each project.[108] After allowing for a 20% variance in cost-overruns, Mr. Coppola concluded that the PULJ should have disallowed $1,524,610 for the two non-STRIDE safety and reliability projects, $2,357,045 for the nine STRIDE projects, and $1,166,469 for the additional three capital projects.[109]

68. Despite noting the lengthy discussion of these issues during the proceedings, the PULJ approved Company Adjustments 6-9 without discussing the issues raised by OPC. Rather, the PULJ briefly stated that "the costs associated with these projects were actual, not estimated costs."[110] OPC did not and does not dispute whether Washington Gas actually incurred these costs, but OPC does dispute whether these costs were prudent in the first place. OPC contends that the Proposed Order therefore ignores their objections to these adjustments in their entirety.

1. Washington Gas's opposition

69. Washington Gas argues that the Proposed Order confirms that the PULJ "thoroughly reviewed the testimony filed by all parties as well as the evidence introduced during the hearings."[111] Additionally, the Proposed Order states that "[t]estimony at length was presented at the hearings in this matter regarding STRIDE projects, prudency, and cost overruns."[112]

70. Washington Gas notes that the Proposed Order describes OPC's proposed 20% cost variance as well as the evidence introduced by Washington Gas regarding the

[108] *Id*. at 47.
[109] Coppola Surrebuttal at Ex. SC-SR2, SC-SR3, SC-SR6, and SC-SR8.
[110] Proposed Order at 8.
[111] *Id*. at 5.
[112] *Id*. at 7.

Company's projects and their actual costs. Therefore, the PULJ rejected OPC's proposed adjustments to these 14 capital projects only after giving full consideration to OPC's alternative. The PULJ did not, as OPC claims, fail to perform a prudency review, as can be inferred from her decision to reject OPC's prudency objections. Additionally, Washington Gas provided cost information for 6,000 projects, the vast majority of which did not result in cost overruns.

71. Washington Gas argues that although the PULJ did not describe the details of each contested capital project, the record contains hundreds of pages of Surrebuttal testimony by Washington Gas witnesses, which describe the costs as well as the reasons why any cost overruns occurred. Therefore, the record contained substantial evidence upon which to conclude that Washington Gas prudently incurred these capital costs. Finally, Washington Gas argues that Witness Coppola's 20% variance is arbitrary and capricious. The Company uses a 20% variance to assist in setting a capital budget, rather than a limitation on any recovery in rates.

Commission Decision

72. OPC does identify what appears to be a systemic issue in Washington Gas's ability to accurately estimate the costs of some its largest projects. Although we deny OPC's appeal, the Commission does expect Washington Gas to address these issues proactively going-forward.

73. However, in the present case, the Commission agrees with Washington Gas that the record contains substantial evidence upon which the PULJ could have concluded that

OPC's proposed disallowances should be rejected.[113] In 2012, the Commission stated that, "unless the project experiences egregious waste, fraud or abuse…we suspect it will be difficult, if not impossible, for us to unpack *post hoc* any imprudence."[114] Additionally, Washington Gas observed below that the Company does not perform on-site inspections due to the high number of capital projects it performs and the additional expense to ratepayers that would result from 6,000 separate site inspections. Washington Gas utilizes historical averages when estimating project costs to avoid incurring these additional capital costs.[115] Washington Gas witness Morrow testified that more specific forms of cost estimates, such as bid pricing or site visits, would likely result in higher estimates but would not lower actual costs.[116] Mr. Morrow also testified as to the reason for cost overruns for each of the projects challenged by OPC. The PULJ need not document the specific reasons for higher actual costs in each of the Company's 14 capital projects.[117] The record clearly provided substantial evidence upon which the PULJ could conclude that the Company prudently incurred the actual costs of these projects.[118]

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[113] Witness Coppola does not contest that these projects are used and useful.

[114] *In the Matter of the Application of Potomac Electric Power Company for Authority to Increase its Rates and Charges for Electric Distribution Service*, Case No. 9286, Order 95028 (2012).

[115] WGL estimates a cost of $100.00 per site visit, which would result in $6 million in additional capital costs. WGL Post-Hearing Brief at 12, n. 63.

[116] Morrow Direct at 24.

[117] Regarding OPC's challenges to the nine specific STRIDE projects, Public Utilities Article, *Annotated Code of Maryland* ("PUA") § 4-203(e)(3) states that "the Commission may approve a plan if it finds that the investments and *estimated* costs of eligible infrastructure replacement projects are: (i) reasonable and prudent" (emphasis added). As WGL observed below, all of the STRIDE-related capital projects challenged by OPC were part of a Commission-approved STRIDE plan, and separately approved.

[118] WGL Post-Hearing Brief at 15-23.

C. OPC's argument that the Proposed Order improperly allowed recovery for post-test-year projects unrelated to safety or reliability

74. OPC challenges six post-test-year projects for which the PULJ allowed recovery. All six projects are "advance of paving" ("AOP") projects. Washington Gas conducts these projects at the request of a state or local government when it is necessary to relocate a gas main during road construction.

75. OPC acknowledges that the Commission allowed post-test-year recovery in Washington Gas's last fully litigated rate case for base additions and reliability spending.[119] However, OPC points to language in the Commission's Order that "emphasized that recovery of post-test-year rate base additions and reliability spending is not guaranteed and should not be expected."[120] OPC contends that the Commission created an exception in Case No. 9481 due to Washington Gas's increasing leak rate problem.

76. OPC argues that the Company's AOP projects are not safety-related and therefore should be removed from rate base because they were not performed during the relevant test-year. OPC points to Mr. Morrow's admission during the hearings that the AOP projects did not have the primary purpose of addressing leaks.[121] Because the issue of increased leak rates did not affect the Company's AOP projects, OPC claims the Commission should enforce the general rule against post-test-year recovery and disallow $6,048,495 in total capitalized costs associated with the six AOP projects.[122]

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[119] *In re Washington Gas,* Case No. 9410 (December 2018).
[120] Order No. 88944 at 73-74.
[121] Tr. 404-05.
[122] Coppola Direct at Att. 1 (OPC DR 10-5.

1. Washington Gas's opposition

77. Washington Gas contends that its AOP projects are safety-related because the Company must relocate its gas mains when requested by state and local government or "there is a significant chance of damage to them, which could range from minor to catastrophic. Thus, the essential purpose of the relocation activity is safety-related; relocation is intended to avoid damages and damage consequences."[123]

78. Washington Gas also points to language in Case No. 9481 in which the Commission stated that it would "continue to address this issue on a case-by-case basis, with post-test-year recovery viewed as an exception to the rule, and not intended to be deemed as guaranteed or automatic."[124] Therefore, Washington Gas argues, the PULJ properly performed a case-specific analysis, and properly used her discretion to allow cost-recovery for the Company's AOP projects.

Commission Decision

79. The Commission affirms cost recovery for Washington Gas's six post-test-year AOP projects. The Commission will continue to evaluate this issue on a case-by-case basis. In the present case, the Commission agrees with Washington Gas that these projects are related to overall infrastructure safety, even if not as directly related to gas leaks as in Case No. 9481.

80. Additionally, the AOP projects at issue have already been performed, even if post-test-year, and the record contains no evidence that they were not necessary to reduce the risk of a future gas leak. Therefore, the record supports the PULJ's conclusion to allow recovery of the capital costs associated with these projects.

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[123] Murrow Direct at 15-16.
[124] Order No. 88944 at 75.

D. OPC's argument that the Proposed Order failed to address Washington Gas's workforce reduction initiative

81. OPC notes that Washington Gas witness Gibson testified that the Company's "workforce reduction initiative" saved Washington Gas $792,227 in O&M costs in 2020.[125] Because these cost savings are known and measurable, OPC witness Coppola testified that they should be removed from Washington Gas's proposed pre-tax operating expense in Adjustment 19 in this case.

1. Washington Gas's opposition

82. Washington Gas contends that the Proposed Order did properly consider the impact of its workforce reduction initiative. Washington Gas notes that the PULJ adopted Staff's proposed adjustment to Adjustment 19.[126] Staff's proposed adjustment incorporated the impact of Washington Gas's workforce reduction initiative based upon the testimony of Staff witness Valcarenghi. Therefore, OPC incorrectly contends that the Proposed Order ignores Mr. Coppola's proposed adjustment to Washington Gas's pre-tax operating income.

83. Additionally, Washington Gas contends that the record is unclear as to whether OPC's proposed income tax reduction results in any actual adjustment to rates since that reduction is not included in OPC's proposed revenue requirement or OPC's adjustments to the Company's cost-of-service.

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[125] Gibson Direct at 14.

[126] Proposed Order at 8 ("I find Staff's argument compelling and accept Staff's proposed adjustment at this time").

Commission Decision

84. The Commission agrees with Washington Gas. The Proposed Order accepted Staff's recommendations regarding Adjustment 19. Staff witness Valcarenghi addressed this initiative in his surrebuttal testimony, and it appears Staff incorporated Mr. Valcarenghi's testimony into its recommended adjustments to Adjustment 19. Therefore, the record contains substantial evidence that the PULJ properly evaluated all evidence related to Washington Gas's "Wages and Salaries," including the Company's "workforce reduction initiative."

E. OPC's argument that the Proposed Order does not address whether Washington Gas's assumptions regarding pension and other post-employment benefits ("OPEB") are too low

85. OPC contends that Washington Gas employed improperly low return rates when calculating its OPEB and pension expenses for purposes of Adjustments 14 and 15. For 2020, Washington Gas used return rates of 4.50% for the union portion of its benefit plan and 3.25% for the non-union portion of its plan. To support OPC's argument, OPC witness Coppola noted that in 2019, Washington Gas used 5.75% and 3.75% as rates of return on its union and non-union plans respectively. Mr. Coppola testified that these return rates should serve as the floor in evaluating the appropriate rates in the current case.[127] Additionally, Mr. Coppola noted that Washington Gas's OPEB plan averaged an annual return of 13.6% between 2012 and mid-2020, and the Company's average annual return on its pension investments was 9.5% for the same period.[128] Based on his previous experience handling OPEB and pension plans for two separate energy companies, Mr. Coppola testified that Washington Gas would "have wide discretion to determine the

[127] Coppola Direct at 67.
[128] *Id*. at 67, 70.

appropriate expected return rate based on multiple factors including the actual return it has achieved historically over multiple years."[129]

86. In discovery, Washington Gas admitted that its OPEB expenses would have declined by $2.7 million had the Company employed the same return rate it used in 2019.[130] Therefore, OPC requests the Commission to disallow $1,061,199, the portion of the Company's OPEB expense savings applicable to Maryland. OPC makes a similar argument regarding Washington Gas's pension expense. If Washington Gas employed the same return rate as it used in 2019, pension expense would have declined by $3.9 million, of which $1,208,792 applies to Maryland. OPC asks the Commission to reduce Washington Gas's pension expenses by this amount.

1. Washington Gas's opposition

87. Washington Gas contends that the Proposed Order's adoption of Adjustments 14 and 15 was proper and consistent with Commission precedent. Washington Gas states that it based its proposed return rates on a 2020 actuarial study by Willis Towers Watson using Generally Accepted Accounting Procedures.[131] Finally, Washington Gas witness Gibson testified that the Company's proposed return rates were consistent with its outside auditor as well as its internal accountants.[132] Washington Gas asks the Commission to affirm the Proposed Order's finding that Adjustments 14 and 15 were consistent with Commission precedent and based upon substantial evidence in the record.

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[129] *Id*. at 67.
[130] *Id*. at attached Response to OPC DR 8-15.
[131] Gibson Direct at 21-25.
[132] *Id.*

Commission Decision

88. The Commission affirms the Proposed Order regarding the appropriate return rates for Washington Gas's OPEB and pension plans. As Washington Gas argues, the Company derived its rates of return from a 2020 actuarial study. Washington Gas is also correct that the Commission has frequently approved return rates that were based upon an actuarial study. In fact, Washington Gas cites multiple occasions in which the Commission rejected departures from actuarial expenses.[133] Washington Gas witness Gibson substantiated that the return rates proposed by Washington Gas were consistent with internal and external Company accountants. Therefore, both Commission precedent and the record provide substantial evidence to support return rates of 4.50% and 3.25% proposed by the Company and adopted by the PULJ.

F. OPC's argument that the Commission should eliminate Washington Gas's declining block rate structure

89. Washington Gas employs a declining block rate structure, which OPC contends undermines Maryland's stated conservation goals. OPC witness Watkins testified that the Commission should abolish this rate structure because discounting energy prices the more a customer consumes directly encourages more energy usage. Therefore, a declining rate structure undermines both stated Maryland policy as well as the conservation policies contained in PURPA.[134] Additionally, the majority of states and commissions have switched to flat or inverted block rates.[135]

[133] *See e.g.,* Case No. 8959, Proposed Order at 19-25; Case No. 9322, Proposed Order at 61-62.
[134] Watkins Direct at 21-28.
[135] *Id*.

90. OPC witness Watkins testified that his research revealed that high-usage customers place a greater cost on the system than low-usage customers.[136] For this reason, he noted, the Virginia State Corporation Commission recently ordered Washington Gas to transition to a single volumetric rate to reduce subsidies among the residential class. Mr. Watkins recommended a gradual elimination of the declining block rate structure by moving the second usage block one-third of the way to the first usage block and moving the third usage block halfway to the second usage block. Mr. Watkins testified that this would avoid rate shock to large-volume residential customers, and the Commission can then eliminate the declining block rate structure in Washington Gas's next rate case.[137]

91. OPC contends that the Proposed Order wrongly adopts Staff's Rate Design methodology without explaining how the elimination of the declining rate block structure (recommended by Staff) will be eliminated in Washington Gas's next rate case.

1. Washington Gas's opposition

92. In response to OPC, Washington Gas points to a study performed by Washington Gas witness Raab on whether the declining block structure disincentives conservation. This study incorporated load data from Non-Coincident and Coincident Peak Class Cost of Service Studies ("CCOSS") from Case No. 9322's Working Group. Mr. Raab's study also incorporated data from the Company's proposed CCOSS in the present case.[138] Based on the results of his study, Mr. Raab concluded:

[136] *Id*. at 25.
[137] *Id*. at 26-27.
[138] Raab Rebuttal at 8-12.

> (1) As volumetric consumption increases, average cost decreases for both high- and low-usage classes of customers;
>
> (2) Neither the existing declining block rate nor OPC's proposed flat rate is superior in matching cost of service to customers' charge. The primary issue is that the Proposed System Charge is too low; and
>
> (3) Contrary to OPC's contention, Mr. Raab's intra-class cost study showed that the relative cost to serve the lowest volume users exceeds any other identified customer grouping as reflected in Washington Gas's current rate design.[139]

93. Generally, Mr. Raab also cited a 2015 Energy Information Administration report that revealed a 36% increase in homes using electric heat rather than natural gas as their main source of energy between 2009 and 2015. Mr. Raab testified that switching from natural gas to electricity is increasingly common.[140]

94. Based upon these conclusions, WGL argued that the record contained substantial evidence to support the PULJ's decision not to eliminate the declining block rate structure in the Company's next rate case.

Commission Decision

95. The Commission affirms the PULJ's decision to adopt Staff's Rate Design methodology in the present case, and OPC does not contend that the record does not support this decision. However, the Commission recognizes that the majority of states as well as PURPA have expressly concluded that declining block rate structures do incentivize increased energy consumption, as Mr. Watkins testified. The Commission also notes that the Virginia State Corporation Commission has ordered WGL to switch its rate structure to a flat rate for the reasons set forth in Mr. Watkins' testimony and

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[139] *Id*. at 14.
[140] Raab Direct at 25-26.

described in the Proposed Order. [141] The Commission has previously stated that it "places emphasis on Maryland public policy goals that encourage energy conservation and efficiency."[142]

96. To further this Maryland policy, the Commission notifies WGL that it intends to eliminate the declining block rate structure in its next rate case. When Washington Gas files its next rate case, its application shall include the elimination of this rate structure in its proposed rate design. Washington Gas may also file alternative rate design proposals within its application.

IV. Washington Gas's Motion for Clarification

97. Washington Gas's Motion for Clarification is granted, and Washington Gas is authorized to utilize its RNA to correct any deficiency between actual and authorized operating revenue that was caused by the delay in issuance of this Order and the resulting difference in rates. WGL is further directed to specify how customer classes not subject to the RNA will be accounted for.

IT IS THEREFORE, this 9th day of April, in the year of Two Thousand Twenty One, by the Public Service Commission of Maryland;

ORDERED: (1) Except as stated above, the Proposed Order of the Public Utility Law Judge Division is hereby affirmed;

(2) Washington Gas is hereby authorized, pursuant to § 4-204 of the Public Utilities Article, Annotated Code of Maryland, to file tariffs that shall increase natural

[141] Proposed Order at 17-18.
[142] *In Re DPL*, Case No. 9424, Order No. 88033 at 27 (2017).

gas distribution rates for service rendered on or after April 9, 2021, subject to acceptance by the Commission, and which shall otherwise be consistent with the findings in the Proposed Order, as modified herein and in Appendix A[143] hereto; and

(3) Washington Gas's Motion for Clarification is granted.

/s/ Jason M. Stanek

/s/ Michael T. Richard

/s/ Anthony J. O'Donnell

/s/ Odogwu Obi Linton

/s/ Mindy L. Herman
Commissioners

[143] Appendix A contains updated financials in light of the Commission's decision above to revise the approved ROR.

Appendix A

Washington Gas Light Company
Case No. 9651

Revenue Requirement
($000's)

Adjusted Rate Base	$1,212,272
Rate of Return	7.09%
Required Income	$85,950
Adjusted Operating Income	$76,714
Operating Income Deficiency	$9,236
Conversion Factor	1.4266
Revenue Requirement *	$13,146

* less Project C1002415 $29,718 revenue

Rate Base
($000's)

Per Books Balance	$1,205,241
Uncontested Adjustments	($48,665)
Total Uncontested	$1,156,576
Contested Adjustments	
Additional Plant in Service - STRIDE & Safety Plant	$55,696
Reduce Post Year Plant	
Safety-Related Project Cost Overruns	
STRIDE Projects Cost Overruns	
Other Capital Projects Cost Overruns	
Adjusted Rate Base	$1,212,272

Operating Income
($000's)

Per Books Balance	$79,959
Uncontested Adjustments	($4,110)
Uncontested Balance	$75,849
Contested Adjustments	
Non-Labor Inflation	$0
Wages and Payroll Taxes	$538
Leak Management	$580
Interest Synchronization	($253)
Adjusted Operating Income	$76,714