

STATE OF MARYLAND
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of the Review of the)
Delmarva Power and Light Company) **Case No. 9226**
Standard Offer Service Administrative Charge)

In the Matter of the Review of the)
Potomac Electric Power Company) **Case No. 9232**
Standard Offer Service Administrative Charge)

SURREBUTTAL TESTIMONY OF
JONATHAN WALLACH
ON BEHALF OF
THE OFFICE OF PEOPLE’S COUNSEL

Resource Insight, Inc.

MAY 6, 2014

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1 **I. Introduction**

2 **Q: Please state your name, occupation, and business address.**

3 A: I am Jonathan F. Wallach. I am Vice President of Resource Insight, Inc., 5
4 Water Street, Arlington, Massachusetts.

5 **Q: Are you the same Jonathan F. Wallach that filed reply testimony in this**
6 **proceeding?**

7 A: Yes.

8 **Q: On whose behalf are you testifying?**

9 A: I am testifying on behalf of the Office of People's Counsel.

10 **Q: What is the purpose of your surrebuttal testimony?**

11 A: On April 18, 2014, the staff of the Public Service Commission ("Staff") filed
12 rebuttal testimony by Phillip E. VanderHeyden. On that same day, the
13 Companies filed rebuttal testimony by Susan A. DeVito and RESA filed rebuttal
14 testimony by Richard J. Hudson, Jr.

15 This surrebuttal testimony responds to these parties' rebuttal testimony
16 regarding the Administrative Adjustment for the residential Administrative
17 Charge.

18 **Q: Are you revising any of the conclusions or recommendations from your**
19 **reply testimony in light of parties' rebuttal testimony?**

20 A: No. Nothing in parties' rebuttal testimony would lead me to alter my conclusion
21 that the 2014 Stipulation is contrary to the public interest. Specifically with
22 respect to the Administrative Adjustment for the residential Administrative
23 Charge, I continue to conclude that the Administrative Adjustment bears no
24 relation to actual SOS-related costs and serves no purpose other than to

1 arbitrarily and unreasonably increase the price paid by residential customers for
2 Standard Offer Service. I therefore continue to recommend that the Commission
3 reject the Settling Parties' request for approval of the 2014 Stipulation and
4 instead adopt the following changes to the current Administrative Charge for
5 residential SOS:¹

- 6 • As provided under the 2014 Stipulation, replace the fixed rate for the
7 incremental-cost component with a rate set to recover actual, verifiable,
8 prudently incurred incremental costs. Establish an annual proceeding to:
9 (1) review and assess the prudence of the prior year's spending on
10 incremental costs; (2) reconcile incremental-cost revenues against actual
11 costs; and (3) reset the rate for the upcoming year.
- 12 • Limit the return component to recovery of the return on SOS-related cash
13 working capital. Allow no other costs or other deemed return to be
14 recovered through the return component.
- 15 • Replace the fixed rate for the return component with a rate set to recover
16 the return on SOS-related cash working capital. As part of the annual
17 proceeding for incremental costs, update the return rate as appropriate to
18 reflect changes in wholesale SOS supply costs, revised estimates of net lag
19 days, or approved changes to the assumed finance rate.
- 20 • As provided under the 2014 Stipulation, continue to set the rate for the
21 uncollectible-cost component as part of distribution rate cases.
- 22 • Eliminate the Administrative Adjustment.

¹ I also continue to recommend that the initial rates for each component of the Administrative Charge for residential SOS customers be set as shown in Table 1 of my reply testimony.

1 **II. Response to Staff Witness VanderHeyden**

2 **Q: What is Mr. VanderHeyden's position on the Administrative Adjustment?**

3 A: Mr. VanderHeyden alleges that the Companies recover through base distribution
4 rates certain customer-service costs that should be functionalized as SOS-related
5 and instead recovered through SOS rates.² Specifically, Mr. VanderHeyden
6 claims that SOS-related costs are currently recorded in FERC accounts for
7 Customer Accounts Expense, Customer Service Expense, and Administrative
8 and General Expense. Mr. VanderHeyden further contends that the
9 Administrative Adjustment reasonably approximates the portion of the
10 Companies' customer-service costs that would be classified as SOS-related if
11 such costs were functionally unbundled in a base rate proceeding:

12 The use of the Administrative Adjustment does not precisely allocate
13 customer service costs, but it provides a reasonable facsimile of costs that
14 would have been allocated, had it been possible to set base rates and SOS
15 rates simultaneously and continue to adjust costs over time.³

16 **Q: What is the basis for Mr. VanderHeyden's assertion that SOS-related costs
17 are currently being recovered through distribution rates?**

18 A: Mr. VanderHeyden fails to offer any evidence that: (i) a portion of the costs
19 recorded in the FERC accounts in question are due to the provision of standard
20 offer service; (ii) the portion of the costs he believes to be SOS-related are in
21 fact recovered through distribution rates; or (iii) the portion of the costs he
22 believes to be SOS-related are not already recovered through the incremental-
23 cost component of the Administrative Charge.

² *Rebuttal Testimony of Phillip E. VanderHeyden on Behalf of the Staff of the Public Service Commission*, Case Nos. 9226 and 9332, April 18, 2014, p. 2, ll. 7-10.

³ VanderHeyden Rebuttal, p. 7, ll. 11-14.

1 **Q: Has Mr. VanderHeyden offered any evidence to support his claims that the**
2 **amounts recovered through the Administrative Adjustment reasonably**
3 **approximate the amount of SOS-related costs allegedly being recovered**
4 **through distribution rates?**

5 A: No. Mr. VanderHeyden has not offered any evidence that the amounts recovered
6 under the proposed initial rate for the Administrative Adjustment reasonably
7 reflects the SOS-related costs allegedly being recovered through distribution
8 rates. Nor, for that matter, does he offer any evidence that changes to the rate in
9 the future (due to changes in incremental or uncollectible costs) would be
10 consistent with changes in the SOS-related costs allegedly being recovered
11 through distribution rates.

12 **Q: Are you opposed to further separation of customer-service costs into**
13 **distribution and SOS functions?**

14 A: No. However, I am opposed to adoption of an arbitrary and artificial proxy
15 value for SOS-related customer-service costs, as would be the case with the
16 Administrative Adjustment under the 2014 Stipulation. As such, I recommend
17 that the Administrative Adjustment be eliminated.

18 As Mr. VanderHeyden suggests, customer-service costs can be unbundled
19 using a variety of functional allocators.⁴ Whichever allocator the Commission
20 deems appropriate, it is critical that the Companies unbundle only those
21 customer-service costs which have been determined to be incremental, i.e.,
22 potentially avoidable as a result of customers migrating to competitive retail
23 service. For example, certain billing expenses may be avoidable if a customer
24 switches to a retail supplier that offers separate billing for supply. On the other

⁴ VanderHeyden Rebuttal, p. 3, ll. 6-8.

1 hand, metering expenses are not avoidable, since such expenses would be
2 incurred whether a customer takes standard offer or competitive service. If non-
3 incremental costs were recovered through the Administrative Charge, those
4 customers who switch to retail supply would be able to avoid paying their fair
5 share of such costs, while customers remaining on SOS would be obligated to
6 subsidize switching customers for such costs.

7 It is also critical that the Companies charge retail suppliers for the full
8 amount of supply-related incremental costs associated with any customer
9 services provided to those retail suppliers. For example, retail suppliers whose
10 receivables are purchased by the Companies should be charged for all supply-
11 related credit and collection expenses associated with those purchased
12 receivables.⁵ If not, then SOS customers would inappropriately subsidize retail
13 suppliers for such costs.

14 **Q: What process do you recommend for determining the amount to be**
15 **recovered through the residential Administrative Charge for SOS-related**
16 **customer-service costs?**

17 A: As with the rate for the uncollectible-cost component of the residential
18 Administrative Charge, the charge for SOS-related customer-service costs
19 should be determined through a full evidentiary review in a distribution rate case
20 of the Company's proposed functional unbundling of customer-service costs
21 into distribution-related and SOS-related cost categories. This process would
22 provide a record for the Commission to rely on to ensure that:

⁵ The supplier fee in this case would be in addition to any discount applied to purchased receivables to account for the risk that such receivables will be uncollectible.

- 1 • The only customer-service costs classified as SOS-related and recovered
2 through the Administrative Charge are those incremental costs incurred as
3 a result of providing standard offer service.
- 4 • Customer-service costs are unbundled in a reasonable and consistent
5 manner and that the distribution and SOS-related portions are appropriately
6 reflected in base distribution rates and the Administrative Charge,
7 respectively.
- 8 • Supplier fees are set at appropriate amounts to reflect supply-related
9 customer-service costs attributable to the provision of customer services to
10 retail suppliers.

11 **Q: Has the Commission used the process you recommend to explicitly**
12 **unbundle customer-service costs in the past?**

13 A: Yes. As Mr. VanderHeyden notes, the Commission approved as part of a
14 settlement agreement an explicit unbundling of Baltimore Gas and Electric
15 Company's gas credit and collection expenses in Case No. 8950.⁶ In contrast
16 with the arbitrary proxy mechanism proposed under the 2014 Stipulation, credit
17 and collection expenses in Case No. 8950 were explicitly unbundled into
18 distribution-related and commodity-related portions. The amount determined to
19 be commodity-related was then removed from recovery through gas base rates
20 and instead included as part of the commodity-related costs recovered through
21 the gas administrative charge.

22 Consistent with the process used in Case No. 8950, the Commission should
23 set the amount to be recovered through the residential Administrative Charge for

⁶ VanderHeyden Rebuttal, p. 7, ll. 18-20.

1 SOS-related customer-service costs based on an explicit functional unbundling
2 of customer-service costs in a distribution rate case.

3 **III. Response to Companies Witness DeVito**

4 **Q: Please comment on Ms. DeVito's rebuttal testimony regarding the**
5 **Administrative Adjustment.**

6 A: Ms. DeVito admits that the Administrative Adjustment is a proxy for costs other
7 than the verifiable and prudently incurred costs allowed under Public Utilities
8 Article §7-510(c)(3)(ii)(2).⁷ In fact, Ms. DeVito cites marketing expenses as an
9 example of the type of cost that is not incurred by the Companies, but for which
10 the Administrative Adjustment would act as a proxy in order to level the playing
11 field for retail suppliers. As I discussed in my reply testimony, artificially
12 increasing the rate for the Administrative Charge beyond that required to
13 recover actual, verifiable, and prudently incurred costs in an attempt to level the
14 playing field would be contrary to statute.

15 **IV. Response to RESA Witness Hudson**

16 **Q: Please comment on Mr. Hudson's rebuttal testimony regarding the**
17 **Administrative Adjustment.**

18 A: Mr. Hudson believes that I claimed in my reply testimony that the Companies
19 do not recover any SOS-related costs in distribution rates.⁸ Mr. Hudson is

⁷ *Rebuttal Testimony of Susan A. DeVito on Behalf of Delmarva Power and Light Company and Potomac Electric Power Company*, Case Nos. 9226 and 9232, April 18, 2014, p. 8, ll. 17-20.

⁸ *Rebuttal Testimony of Richard J. Hudson, Jr. on Behalf of Retail Energy Supply Association*, Case Nos. 9226 and 9232, April 18, 2014, p. 2, ll. 15-17.

1 mistaken in this regard, since I made no such claim in my reply testimony.
2 Instead, I asserted that neither the Companies nor RESA had offered any
3 evidence to support their allegations that SOS-related costs are currently
4 recovered in distribution rates or in support of their claims that the proposed rate
5 for the Administrative Adjustment reasonably approximates the SOS-related
6 costs allegedly recovered through distribution rates.

7 Mr. Hudson did not take the opportunity to offer any such evidence on
8 rebuttal.⁹ Instead, Mr. Hudson claims that Staff is already on record in this case
9 supporting recovery of allegedly SOS-related costs through Staff's proposed
10 Allocated Cost component of the residential Administrative Charge.¹⁰ Mr.
11 Hudson further concludes that the Administrative Adjustment proposed under
12 the 2014 Stipulation is reasonable, because the rate for the Administrative
13 Adjustment would be lower than the rate implied by Staff's Allocated Cost
14 proposal.¹¹

15 The Commission should give no weight to Mr. Hudson's conclusion, since
16 he judges the reasonableness of the proposed Administrative Adjustment solely
17 in relation to a deeply flawed proposal by Staff. As I discussed in my August 23,
18 2010 rebuttal testimony in this proceeding, Staff failed to show that SOS-related
19 costs were being recovered through distribution rates, that such SOS-related
20 costs were not already being recovered through the incremental-cost component
21 of the residential Administrative Charge, or that its proposal to unbundle
22 customer-service costs in proportion to revenues was reasonable. It is no
23 wonder, then, that the rate that would have been charged under Staff's Allocated

⁹ Nor did any of the other parties to the 2014 Stipulation.

¹⁰ Hudson Rebuttal, p. 2, line 25 through p. 3, line 1.

¹¹ Hudson Rebuttal, p. 3, ll. 1-6.

1 Cost proposal is many times higher than the proposed rate for the
2 Administrative Adjustment under the 2014 Stipulation. However, that fact alone
3 does not imply the proposed Administrative Adjustment is itself reasonable.

4 **Q: Does this conclude your surrebuttal testimony?**

5 A: Yes.