BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of Northern States Power Company, a Wisconsin Corporation, for Authority to Adjust Electric and Natural Gas Rates	))))	Docket No. 4220-UR-121

SURREBUTTAL TESTIMONY OF JONATHAN WALLACH
ON BEHALF OF THE CITIZENS UTILITY BOARD OF WISCONSIN
October 27, 2015

I. Introduction

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

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

Q: Are you the same Jonathan F. Wallach that filed direct and rebuttal testimony in this proceeding?

A: Yes.

Q: On whose behalf are you testifying?

A: I am testifying on behalf of the Citizens Utility Board of Wisconsin (CUB).

Q: What is the purpose of your surrebuttal testimony?

A: This surrebuttal testimony responds to rebuttal testimony by Company witnesses Gerald W. Marx and Donald F. Reck and by WIEG witness Richard A. Baudino.

Q: Do you have any preliminary comments regarding the Company's rebuttal testimony?

A: Yes. First, Mr. Marx suggests in his rebuttal testimony that the Commission abandon its long-standing practice of basing its revenue allocations on a range of results from diverse cost of service studies. Instead, Mr. Marx would have the Commission consider only those studies which produce what he considers to be "moderate" cost allocations and reject other studies that yield what he considers to be "extreme" or "outlier" results.

The Commission should reject Mr. Marx's attempt to impose subjective and unreliable standards of review on the Commission's deliberations. After all, one party's "moderate" study is another party's "outlier." For example, one could validly characterize the Method 3 COSS as an "outlier" because this is the only one of the five studies conducted by NSPW where the large C&I class has a lower percentage revenue increase than the residential class. As the Commission has long held, no one study perfectly captures cost-causation, no matter how strongly any one party's belief to the contrary. Mr. Marx has not offered a reasonably compelling argument for why the Commission should hold otherwise.

Second, Mr. Marx's rebuttal testimony misrepresents both CUB's and Commission staff's positions regarding which cost of service studies each party relied on to develop their respective revenue-allocation proposals. Mr. Marx incorrectly suggests that each party supports one particular study (Method 5 COSS for CUB and Method 2 COSS for Commission staff), when in fact both parties explicitly recommended relying on all five studies for revenue-allocation purposes.[1] The Company should revise its evidence to correct for these mischaracterizations of CUB's and Commission staff's testimony.[2]

[1] I describe CUB's position at Direct-CUB-Wallach-19. At Direct-PSC-Shannon-3r, Commission staff witness Sam Shannon refers to the Method 4 COSS as "a good starting point" for

II. Response to Mr. Marx

Q: In his rebuttal testimony, how does Mr. Marx respond to your conclusion that the 12CP allocator more reasonably reflects cost-causation than the 4CP allocator?

A: Mr. Marx disagrees with my finding that the Company's capacity obligation is driven by its load throughout the year because "MISO reserve requirements planning guidelines have shifted emphasis to the summer peaks."[3]

Mr. Marx apparently mistakes the *measure* MISO uses to express the Company's planning reserve requirement for the *method* MISO uses to determine that requirement. The measure MISO uses to express the Company's reserve requirement is a simple percentage margin above summer peak demand.[4] However, the method MISO uses to determine the amount of capacity required for planning reserve is an LOLP analysis that considers the daily contribution of the Company's demand to annual loss of load expectation. In other words, contrary to Mr. Marx's claim, the Company's annual capacity obligation is determined based on the Company's demand throughout the year, not just by its summer peaks.

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revenue allocation, but then goes on to say that his proposed revenue allocation "incorporates aspects of various models."

[2] These corrections should include removing the reference in Table 2 at Rebuttal-NSPW-Marx-5 to Commission staff's position regarding production capacity cost allocators. This table incorrectly indicates that Commission staff supports the classification and allocation approach used in the Method 2 COSS.

[3] Rebuttal-NSPW-Marx-7.

[4] MISO calculates the reserve margin as the ratio of capacity required for planning reserve to summer peak demand minus one.

Q: What is Mr. Marx's response to your finding that Northern States Power of Minnesota (NSPM) considers only customer-related distribution costs to be fixed?

A: In his rebuttal testimony, Mr. Marx claims that I misinterpreted the NSPM testimony that I relied on as the basis for my finding. Essentially, Mr. Marx's argument is that it is not reasonable to infer from the testimony that NSPM does not consider costs other than customer-related distribution costs to be fixed because the testimony does not explicitly discuss these other costs.

Needless to say, I disagree that such an inference is unreasonable. Nonetheless, regardless of whether my inference was warranted, the NSPM testimony explicitly states that customer-related distribution costs (i.e., customer-service and customer-related distribution plant costs) are the only allegedly fixed costs that are appropriately recovered through a customer charge. Thus, NSPM in its last rate case took a different position than the Company in this proceeding on which types of fixed costs should be recovered through the customer charge.

III. Response to Mr. Reck

Q: How does Mr. Reck respond to your testimony regarding the Company's proposal to increase customer charges for residential and small C&I customers?

A: At Rebuttal-NSPW-Reck-8, Mr. Reck claims that I am recommending rejection of the Company's proposal in this proceeding because the Minnesota Public Utilities Commission rejected a smaller increase proposed by NSPM in its last rate case. This claim is simply not true. Nowhere in my direct testimony do I

argue for rejection of the Company's proposal on the basis of the rejection of NSPM's proposal or even discuss the increase proposed by NSPM.

IV. Response to Mr. Baudino

Q: In his rebuttal testimony, how does Mr. Baudino respond to your conclusion that the Equivalent Peaker method classifies production capacity costs in a manner that reasonably reflects cost-causation?

A: Mr. Baudino disagrees with my conclusion because Equivalent Peaker classifications are not based on analyses of the actual economic trade-offs that lead to plant investment. According to Mr. Baudino, without these historical analyses, "it is impossible to identify the 'cost causation' underlying each unit and the expected fuel savings that a base load coal or nuclear unit was likely to achieve."[5] Mr. Baudino goes on to claim that:

> The additional cost of a base load unit may not have been justified by fuel savings expectations alone. Rather, the decision may also have considered other factors (such as the longer life of a base load unit) that, when combined with fuel savings, justified the higher cost base load unit.[6]

Q: Are historical analyses of fuel savings relevant to the determination of cost-causation for production capacity costs?

A: No. What is relevant is that the decision to invest in baseload or cycling capacity, rather than less-expensive peaking units, was based on the fundamental economic logic underlying least-cost capacity expansion planning. In other words, what is relevant is not the amount of "the expected fuel savings that a base load coal or nuclear unit was likely to achieve," but that under typical

[5] Rebuttal-WIEG-Baudino-8.

[6] *Id.*

capacity expansion planning practice the Company's additional capital investment for baseload or cycling units would have been justified on the basis of fuel savings. As described in the NARUC manual on cost allocation:

> The utility can choose to construct one of a variety of plant-types: combustion turbines (CT), which are the least costly per KW of installed capacity, combined cycle (CC) units costing two to three times as much per KW as the CT, and baseloaded units with a cost of four or more times as much as the CT per KW of installed capacity. The choice of unit depends on the energy load to be served.[7]

Thus, from a cost-allocation perspective, the capital costs incurred for baseload or intermediate capacity over and above that incurred for peaking capacity are appropriately classified as energy-related, since these additional costs are incurred to meet energy requirements at lowest total cost.

Q: Could other factors, such as expected plant life, play a role in determining the type of investment, as Mr. Baudino contends?

A: Expected life, along with a number of other assumptions regarding plant and transmission-system characteristics, are typically factors that are accounted for in economic evaluations of capacity-expansion plans, and these factors, either individually or collectively, may affect the economic trade-offs between different types of plant investments. However, it is unlikely that such factors would prove to be material in the determination of the least-cost capacity additions.

Q: How does Mr. Baudino respond to your criticisms of the minimum distribution system method?

[7] *Electric Utility Cost Allocation Manual*, National Association of Regulatory Utility Commissioners, January 1992, p. 53.

A: Mr. Baudino disagrees with my critique of the minimum distribution system method, and instead believes that the Company's reliance on this approach is "reasonable and appropriate to use for purposes of classifying and allocating distribution costs."[8] In particular, Mr. Baudino argues that:

> … to the extent that the utility incurs a distribution cost simply to connect a customer to its system, regardless of that customer's size, it is appropriate to assign the cost of these minimal facilities to rate schedules on the basis of the number of customers, rather than on the kW demand of the class.[9]

The fallacy in Mr. Baudino's argument is that even if there is a minimum cost to connect customers, the cost of that minimum system does not necessarily vary with the number of customers. For example, if service were extended to a new area using minimum-height poles, the total cost of those poles would likely be the same whether service was being extended to a single industrial customer or to one apartment building with 100 residential customers. If the cost of the minimum system does not vary with the number of customers, it would not be appropriate to allocate such minimum costs to rate classes in proportion to the number of customers in each class.

This fallacy is highlighted by Mr. Baudino's discussion of the examples in Figures 1a and 1b of my direct testimony. In these figures, I show how the minimum distribution system method inappropriately allocates minimum costs for a hypothetical single-feeder system to the residential class in proportion to the number of customers even though such costs do not vary with the number of residential customers. Mr. Baudino alleges that my example shows that the customer allocation of minimum costs is appropriate because the allocated minimum cost per residential customer decreases from $25,000 to $10,000 as

[8] Rebuttal-WIEG-Baudino-11.

[9] Rebuttal-WIEG-Baudino-10.

the number of residential customers served increases from one to four. However, Mr. Baudino fails to recognize that the *incremental* minimum cost to serve the three additional residential customers is zero, so that the allocated minimum cost per residential customer should drop to $6,250, not $10,000. In other words, the share of total minimum cost allocated to the residential class should be the same whether one or four customers are served by the feeder, since the minimum cost of the feeder does not increase as the number of residential customers served by that feeder increases.

This discussion illustrates the fundamental problem with the minimum distribution system approach. Even if one could reasonably estimate the cost of a minimum system to serve the Company's customers, there is no reason to believe that those costs would vary directly with the number of customers. Instead, such costs would more likely vary with such factors as customer density or topography.

Consequently, the Commission should give little weight to Mr. Baudino's finding that the Company's reliance on the minimum distribution system method is reasonable.

Q: Does this complete your surrebuttal testimony?

A: Yes.