BEFORE THE STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

IN THE MATTER OF THE PETITION OF	**) BPU Docket No. E014080897**
PUBLIC SERVICE ELECTRIC AND GAS	**)**
COMPANY TO CONTINUE ITS ENERGY	**)**
EFFICIENCY ECONOMIC EXTENSION	**)**
PROGRAM ON A REGULATED BASIS	**)**
("EEE EXTENSION II")	**)**

DIRECT TESTIMONY OF ANDREA C. CRANE ON BEHALF OF THE STATE OF NEW JERSEY DIVISION OF RATE COUNSEL

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I. STATEMENT OF QUALIFICATIONS

Q. Please state your name and business address.

A. My name is Andrea C. Crane and my business address is 90 Grove Street, Suite 211, Ridgefield, Connecticut 06877. (Mailing address: PO Box 810, Georgetown, Connecticut 06829)

Q. By whom are you employed and in what capacity?

A. I am President of The Columbia Group, Inc., a financial consulting firm that specializes in utility regulation. In this capacity, I analyze rate filings, prepare expert testimony, and undertake various studies relating to utility rates and regulatory policy. I have held several positions of increasing responsibility since I joined The Columbia Group, Inc. in January 1989. I became President of the firm in 2008.

Q. Please summarize your professional experience in the utility industry.

A. Prior to my association with The Columbia Group, Inc., I held the position of Economic Policy and Analysis Staff Manager for GTE Service Corporation, from December 1987 to January 1989. From June 1982 to September 1987, I was employed by various Bell Atlantic (now Verizon) subsidiaries. While at Bell Atlantic, I held assignments in the Product Management, Treasury, and Regulatory Departments.

Q. Have you previously testified in regulatory proceedings?

A. Yes, since joining The Columbia Group, Inc., I have testified in over 350 regulatory proceedings in the states of Arizona, Arkansas, Connecticut, Delaware, Hawaii, Kansas, Kentucky, Maryland, New Jersey, New Mexico, New York, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Vermont, Washington, West Virginia and the District of Columbia. These proceedings involved electric, gas, water, wastewater, telephone, solid waste, cable television, and navigation utilities. A list of dockets in which I have filed testimony since January 2008 is included in Appendix A.

Q. What is your educational background?

A. I received a Master of Business Administration degree, with a concentration in Finance, from Temple University in Philadelphia, Pennsylvania. My undergraduate degree is a B.A. in Chemistry from Temple University.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony?

A. On August 7, 2014, Public Service Electric and Gas Company ("PSE&G" or "Company") filed a Petition with the New Jersey Board of Public Utilities ("BPU" or "Board") requesting approval to extend three Energy Efficiency programs and to recover the associated costs ("EEE Ext II") through a new component of the Green Program Recovery Charge ("GPRC"). The Company is proposing to invest up to $95 million from 2015 to 2018 in the three electric and gas energy efficiency programs and to recover the associated costs from ratepayers through a regulatory asset that would be amortized over a 15-year period.

The Columbia Group, Inc. was engaged by The State of New Jersey, Division of Rate Counsel ("Rate Counsel") to review PSE&G's filing and to provide recommendations to the BPU with regard to the issue of cost recovery and other financial issues. Kenji Takahashi of Synapse Energy Economics, Inc. is also filing testimony on behalf of Rate Counsel with regard to program design issues.

III. SUMMARY OF CONCLUSIONS

Q. Please summarize your conclusions and recommendations.

A. Based on my analysis of the Company's filing and other documentation in this case, my conclusions are as follows:

1. The BPU should deny the Company's request to implement the EEE Ext II Program as proposed by PSE&G.
2. The cost of the EEE Ext II Program is excessive, especially the Company's proposal to earn a pre-tax return of 11.852% on its investment, resulting in a return requirement of $59.83 million and a windfall for shareholders.
3. If an EEE Ext II program is authorized, carrying charges should be based on a return on equity of no more than 9.75%, on the Company's current debt costs, and on an updated capital structure.
4. The Board should reject the Company's proposal to recover lost revenues through a Participation Fee of 1.5%.
5. Any additional fees approved by the BPU should be used to offset the administrative costs of the program that would otherwise be charged to ratepayers.
6. The Board should continue to utilize a 5-year amortization period for program investment, rather than the 15-year period proposed by PSE&G.

7. The Board should deny the Company's proposal to charge ratepayers $1.17 million for additional Information Technology ("IT") costs associated with EEE Ext II Program.

8. The Company's claim for administrative costs is excessive. Administrative costs charged to ratepayers should be limited to no more than 8% of the total program investment. In addition, all administrative costs should be subject to a review in future annual filings for reasonableness.

IV. DISCUSSION OF THE ISSUES

A. Introduction

Q. Please provide a brief summary of the EEE Ext II Program proposed by PSE&G.

A. In its Petition dated August 7, 2014, PSE&G proposed an EEE Ext II Program as a continuation of energy efficiency programs that had been previously approved by the Board. The BPU first approved the Company's Energy Efficiency Program on July 16, 2009 when it approved a Stipulation in BPU Docket No. EO09010058, authorizing a program of up to $166 million in program investment. On January 24, 2011, the Company requested that the BPU approve extensions to three energy efficiency programs - the Multi-Family Housing Program, Government/Municipal/Non-Profit Direct Install Program and the Hospital Efficiency Program. The BPU approved additional investment of $103.0 million in these programs on July 14, 2011 in BPU Docket No. EO11010030.

In the current Petition, PSE&G is requesting a further extension of these three programs, with a total program investment of $95 million. In addition, PSE&G is requesting authorization to recover up to $13.7 million in administrative and other support costs and $1.17 million in IT system enhancement costs.

Q. Please provide a brief description of the programs that PSE&G is proposing to extend.

A. The Residential Multi-Family Housing sub-program provides owners of multi-family housing with energy audits, along with incentives and up-front funding for the cost of eligible energy efficiency measures. Participating customers repay a portion of the total cost interest-free through their PSE&G bill over a 5-year or 10-year repayment period. The Company states that there is currently a backlog of approximately 45 multi-family projects and it is proposing investment of $30 million for this sub-program. S-PSEG-ENE-6.

The Hospital Efficiency sub-program provides 100% of the costs to install energy-savings measures up-front, with customers repaying a share of the program costs on their PSE&G bills interest-free over a period of up to three years. The Company claims that customer demand has exceeded available funding for this program, and it is proposing a $40 million investment under the EEE Ext II program.

Finally, the Government/Non-Profit Direct Install sub-program provides energy evaluations and 100% up-front funding for energy-savings measures. Customers repay a portion of their costs over a three year period through their PSE&G bills. The proposed investment for this sub-program is $25 million. The Company is proposing that the targeted customer base be expanded to include small business customers.

Q. What is the total revenue requirement associated with the proposed electric and gas programs?

A. The total projected cost for the proposed electric program is $115.48 million. This includes $64.25 million of program investment, $0.80 in IT investment, $40.51 million of return requirements, and $9.92 million of administrative costs. These costs are partially offset by participant repayments of $18.57 million and capacity revenues of $1.13 million, resulting in a revenue requirement of $95.78 that would be charged to ratepayers.

TABLE 1: Proposed Electric Program

	Costs (Millions $)	Recovery (Millions $)
Program Investment	$64.25	
IT Investment	$0.80	
Return to Investors	$40.51	
Administrative Costs	$9.92	
Paid by Ratepayers		$95.78
Participant Repayments		$18.57
Capacity Revenues		$1.13
Total	$115.48	$115.48

The total projected cost for the proposed gas program is $54.26 million. This includes $30.75 million of program investment, $0.37 in IT investment, $19.32 million of return requirements, and $3.82 million of administrative costs. Participant repayments are estimated to be $8.70 million, resulting in $45.56 million to be funded by ratepayers.

TABLE 2: Proposed Gas Program

	Costs (Millions $)	Recovery (Millions $)
Program Investment	$30.75	
IT Investment	$0.37	
Return to Investors	$19.32	
Administrative Costs	$3.82	
Paid by Ratepayers		$45.56
Participant Repayments		$8.70
Capacity Revenues		$0
Total	$54.26	$54.26

Q. How does the Company propose to recover the costs of the EEE Ext II program?

A. As described in the testimony of Stephen Swetz, the Company proposes to recover the costs of the EEE Ext II program through a new component of the GPRC. Costs to be recovered include program investment, capitalized IT costs, and administrative costs. The EEE Ext II program investments would be recorded as a regulatory asset and amortized over a period of 15 years. As shown on page 2 of Mr. Swetz's direct testimony, the monthly revenue requirement would be calculated as follows:

*Revenue Requirement = (Cost of Capital * Net Investment) + Amortization + Administrative Costs - Program Investment Repayments - Net Capacity Revenues + Tax Adjustments*

Net Investment would include the program investment and capitalized IT costs, less accumulated amortization and accumulated deferred income taxes. The amortization expense would be based on an amortization period of 15 years for program investment and of 5 years for capitalized IT costs.

Administrative costs include costs for the overall administration of the program, as well as costs for training, marketing, and inspections. Program Investment Repayments include that portion of the project costs that is repaid by participants pursuant to the terms of each program. These repayments are credited back to the revenue requirement and used to reduce the amounts that would otherwise be paid by ratepayers. Net Capacity Revenues include any revenues (net of costs) received from bidding eligible measures into the PJM Capacity Market Auction. These revenues will also be credited to the revenue requirement. Finally, tax adjustments relate to timing differences between the IRS treatment and ratemaking treatment for repayments made by participants.

Q. What cost of capital is the Company proposing to utilize for the return on its investment balance?

A. PSE&G is proposing to utilize a weighted average cost of capital ("WACC") of 8.21%, as shown in Schedule SS-EEEXII-2 of Mr. Swetz's direct testimony. In addition, the equity portion would be grossed-up for taxes, resulting in a pre-tax cost of capital of 11.852%. This cost of capital is based on the following capital structure and cost rates:

TABLE 3: Weighted Average Cost of Capital

	Percent	Cost	WACC	Revenue Conversion Factor	WACC Including Tax Effects
Long Term Debt	48.80%	6.0172%	2.9364%		2.9364%
Common Equity	51.20%	10.3000%	5.2736%	1.6906	8.9156%
Total	100.00%		8.2100%		11.8520%

Q. What impact will the proposed program have on customer rates?

A. PSE&G is requesting that the BPU approve initial rates that are sufficient to recover annual electric revenues of $4.8 million and annual gas revenues of $1.8 million, based on the projected revenue requirement from March 1, 2015 through September 30, 2016.[1]

1 Direct Testimony of Mr. Swetz, page 8.

By 2023, the revenue requirements increase to a maximum of $7.89 million for the electric utility and of $3.66 million for the gas utility.[2]

For the initial recovery period, the average electric residential customer using 780 kWh in each summer month and 7,360 kWh annually would initially experience an increase in their annual bill from $1,372.36 to $1,372.92, an increase of $0.66, or 0.04% based on rates and charges effective July 1, 2014. The maximum impact to the typical electric residential customer would occur in the rate period October 2023 through September 2024, when the average residential customer would experience an increase of $1.52 or 0.11%.

For the initial recovery period, the average gas residential customer using 160 therms in a winter month and 1,050 therms annually would initially experience an increase in their annual bill from $1,069.40 to $1,069.88, an increase of $0.48, or 0.04% based on rates and charges effective July 1, 2014. The maximum impact to the typical gas residential customer would occur in the rate period October 2023 through September 2024, when the average residential customer would experience an increase of $1.42 or 0.13%.

Q. Does the Company also propose to charge ratepayers interest on monthly over/under recoveries?

A. Yes, PSE&G's filing includes interest on monthly over/under recoveries based upon the Company's interest rate for commercial paper and/or bank credit lines utilized in the preceding month. If both commercial paper and bank credit lines have been utilized, the weighted average of both sources of capital would be used.

2 Direct Testimony of Mr. Swetz, Schedules SS-EEEXII-3E and SS-EEEXII-3G, Column 19.

Q. Is the Company also proposing to charge a Participation Fee to participants in the EEE Ext II Program?

A. Yes, it is. PSE&G is proposing to charge participants a Participation Fee of 1.5% of the project cost. The Company claims that this fee is intended to compensate PSE&G for margins lost as a result of reduced energy sales. The Participation Fee would be retained by the Company and therefore would enhance shareholder return.

Q. Do you support the EEE Ext II Program as proposed by PSE&G?

A. No, I do not. I believe that the proposed EEE Ext II Program as proposed should be rejected by the BPU, for several reasons. First, the proposed EEE Ext II Program is far too costly for ratepayers and would result in excessive returns for PSE&G shareholders. If the Board adopts a EEE Ext II Program for PSE&G, it should limit the return on equity component of carrying charges to a return on equity of 9.75%. It should also require that carrying charges be updated to reflect the most recent cost of debt and capital structure for the Company. Second, the Board should adopt a five-year amortization period for program investment, instead of the 15-year period proposed by PSE&G. Third, the Board should reject the Company's proposal to charge a Participation Fee to recover lost margins. If any additional fees are collected, these fees should be used to reduce the amount of the revenue requirement that would otherwise be charged to ratepayers, rather than retained by shareholders. Fourth, the BPU should deny the Company's request to recover up to $1.17 million in additional capitalized IT costs. Finally, the BPU should limit recovery of administrative costs to no more than 8% of program investment, subject to a review of the reasonableness of administrative costs in a subsequent true-up proceeding. Each of these recommendations is discussed in detail below.

B. Return on Investment

Q. Do you believe that the Company's currently authorized equity return of 10.3% is appropriate for determining carrying costs for the EEE Ext II Program?

A. No, I do not. The currently authorized return on equity of 10.3% was the result of a complex settlement in a base rate case that reflected compromises by several parties on many different issues. Moreover, that case was filed in May 2009 and new rates were effective in July 2010. Since the Company's last base rate case,[3] market conditions have changed substantially, a fact not reflected in the Company's request to earn its currently authorized WACC on investment made in the EEE Ext II Program.

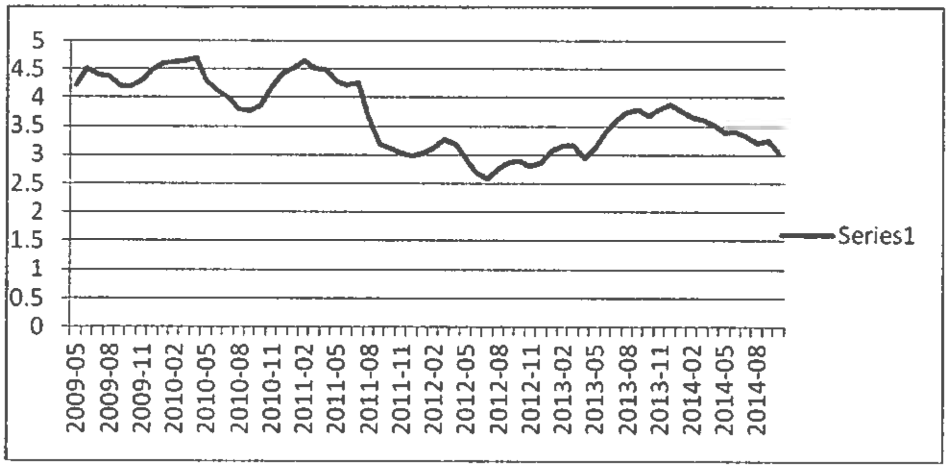
Q. What has generally happened to capital costs since the BPU approved the settlement in BPU Docket No. GR09050422?

A. Capital costs declined between the time that the Company's last base rate case was filed and the issuance of an Order approving a return on equity of 10.3%. In addition, capital costs have continued to decline since that Order was issued in mid 2010. For example, 30-year U.S. Government bonds fell from a rate of 4.23% in May 2009 to 3.99% in July 2010, and continued to decline to a rate of 3.04% in October 2014.[4] As shown below,

3 I/M/O the Petition of Public Service Electric and Gas Company for Approval of an Increase in Electric and Gas Rates and For Changes in the Tariffs for Electric and Gas Service B.P.U.N.J. No. 14 Electric and B.P.U.N.J. No. 14 Gas Pursuant to N.J.S.A.48:2-21 and N.J.S.A. 48:2-21.1 and for Approval of a Gas Weather Normalization Clause, a Pension Tracker and for Other Appropriate Relief, BPU Docket No. GR09050422.
4 All rates are from the Federal Reserve Statistical Releases per www.federalreserve.gov.

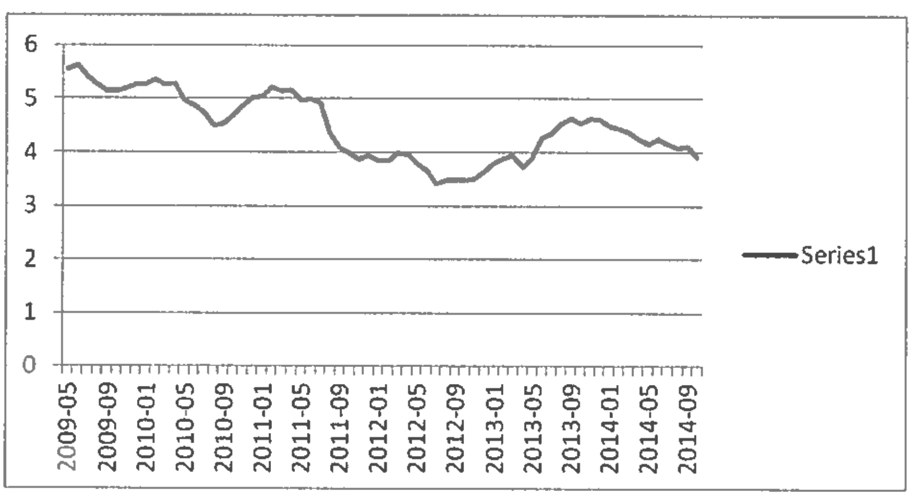
while current rates are slightly above rates reached in mid-2012, they are still well below the market rates at the time of the last PSE&G rate case.

TABLE 4: 30-Year U.S. Government Bonds



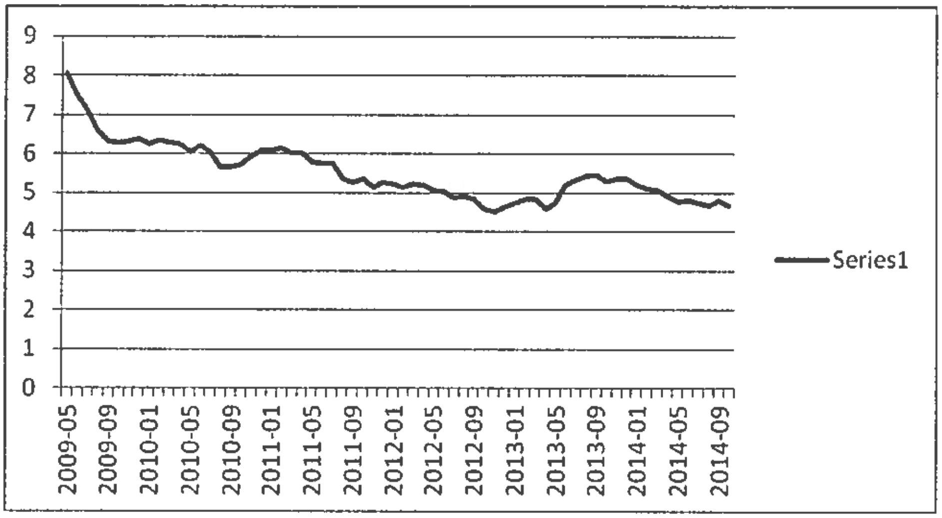
A similar trend can be found with corporate bonds. AAA-rated corporate bonds fell from a rate of 5.54% at May 2009 to 4.72% at July 2010. Rates for AAA-rated corporate bonds have declined further since 2010, and averaged 3.92% for October 2014:

TABLE 5: Corporate Moody's AAA-Rated Bonds



These interest rate trends can also be found with other corporate bonds. Baa-rated bonds declined from 8.06% in May 2009 to 6.01% in July 2010, and to 4.69% by October 2014:

TABLE 6: Corporate Moody's Baa-Rated Bonds



Finally, dividend yields have generally declined as stock prices have increased since the Company's last rate case. The Dow Jones Industrial Index increased from 8,212.41 on May 1, 2009 to 9,732.53 on July 1, 2010. Since the last rate order was issued, the stock market has strengthened significantly with record levels being achieved. The Dow Jones Industrial Index had increased to 17,390.52 by October 31, 2014, more than doubling the index in May 2009. The Dow Jones Utility Index has also increased significantly over this period, from 343.03 on May 1, 2009 to 356.46 by July 1, 2010, and to 596.93 on October 31, 2014. These increases in stock prices have generally outpaced increases in utility dividends, resulting in lower dividend yields and an overall decline in equity returns evaluated based on the Discounted Cash Flow ("DCF") model.

Q. Has the Company's embedded cost of debt declined as well?

A. Yes, it has. The Company's embedded cost of debt has fallen from 6.21%, which was the embedded cost of debt claimed by PSE&G in its last base rate case filing, to 4.60%.[5] Moreover, the current embedded cost of debt is a weighted average that includes some debt incurred at rates that are higher than current market rates. Thus, the substantial fall in the Company's embedded cost of long-term debt is indicative of an even greater decline in the marginal costs of more recently-incurred debt.

Q. What is the significance of these declines in capital costs since the last case?

A. The message is clear. While the parties can debate the specific impact of these reductions on the Company's overall cost of capital, the fact is that capital costs have declined substantially since the decision in BPU Docket No. GR09050422. Regardless of how a party chooses to determine the cost of capital, it is clear that the 10.3% cost of equity reflected in the WACC from the last rate case is no longer appropriate. It is also clear that a reduction to the cost of debt approved in the last base rate case is also warranted. These reductions in capital costs alone provide sufficient rationale for rejecting the Company's proposed EEE Ext II Program as currently structured, which would require ratepayers to pay returns based on a WACC that no longer reflects the Company's actual cost of capital.

Q. Have there been lower returns on equity approved by the BPU since the Order in the last PSE&G rate case?

5 See Petition, Attachment 1, Schedule SS-ESAM-3 in the Company's Energy Strong Filing made on September 30, 2014 (BPU Dkt. No. ER14091074).

A. Yes, there have. Since PSE&G's last base rate case, the BPU has approved a 9.75% return on equity in several base rate cases, for companies such as Rockland Electric Company ("RECO"), the Atlantic City Electric Company ("ACE"), and South Jersey Gas Company.[6] In addition, it has approved a return on equity of 9.75% in PSE&G's Energy Strong proceeding[7] and in several cases involving energy efficiency programs offered by other electric and gas utilities. Therefore, the return on equity of 10.3% requested by PSE&G in this proceeding is clearly excessive and should be rejected by the BPU.

Q. If the BPU approves a EEE Ext II Program, what return on equity would you recommend be utilized to determine the overall return on investment?

A. I recommend a return on equity of no higher than 9.75%, consistent with the most recent equity awards by the BPU. In addition, I recommend that the BPU update the Company's return on debt to reflect the current embedded debt cost, as well as the current capital structure.

C. Amortization Period

Q. What amortization period did the Company utilize for program investments in its proposal?

A. PSE&G is proposing that program investments be amortized over a period of 15-years. The Company has utilized a 5-year amortization period for its proposed capitalized IT investment.

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6 Rockland Electric Company, BPU Docket No. ER13111135; Atlantic City Electric Company, BPU Docket No. ER14030245; South Jersey Gas Company, BPU Docket No. GR13111137.
7 Public Service Electric and Gas Company, BPU Docket Nos. EO13020155 and GO13020156.

Q. Are you recommending any adjustment to the amortization periods proposed by the Company?

A. Yes, I am recommending that program investment be amortized over a period of 5 years instead of over the 15-year period proposed by PSE&G. The Company argues that a 15-year period is reasonable, given the expected life of the measures that are being installed. However, the use of a 15-year period will significantly increase the total cost to ratepayers. As shown in the response to RCR-A-13, the 15-year amortization period will increase the electric revenue requirement paid by ratepayers from $68.77 million to $95.78 million, an increase of $27.01 million or almost 40%. Much of this increase will flow directly to shareholders through increased profits. The use of a 15-year amortization period will similarly increase the gas revenue requirement charged to ratepayers from $32.68 million to $45.66 million, an increase of $12.98 million. Thus, the overall increase charged to ratepayers is approximately $40.0 million if a 15-year amortization period is used instead of a 5-year period. Following are the components of the return requirements under both 15-year and 5-year amortization periods:

TABLE 7: Total Electric and Gas Programs

	15-Year Amortization	5-Year Amortization	Difference
Debt Return	$14.82	$4.94	$9.88
Equity Return	$26.62	$8.87	$17.75
Taxes on Equity Return	$18.39	$6.12	$12.27
Total	$59.83	$19.93	$39.90

Approximately 25% of the return requirement relates to the cost of debt. The remaining 75% relates to return on equity and the associated income taxes. Thus, ratepayers will pay approximately $30 million more for shareholder return and related taxes if the 15-year amortization period is utilized. Approximately 60% of this amount, or approximately $17.75 million, relates to return on equity and approximately $12.27 million to the associated taxes. Therefore, shareholders have a direct benefit of approximately $17.75 million if the 15-year amortization period is utilized instead of a shorter amortization period.

Q. But won't a shorter amortization period result in a larger annual rate impact?

A. Yes, it will. As stated above, the largest annual revenue requirement under the Company's proposal occurs from October 2023 to September 2024, when the revenue requirement is $7.89 million for electric and $3.66 million for gas. If a 5-year amortization period is utilized, the highest annual electric revenue requirement is $12.30 million, which occurs in 2017, and the highest annual gas revenue requirement is $6.27 million in 2018.

The reduction from a 15-year amortization period to a 5-year amortization period will increase the maximum annual residential electric rate impact from an average increase of $1.52 to an average increase of approximately $2.36, or approximately 0.17%. For the average residential gas customers, the reduction from a 15-year amortization period to a 5-year amortization period will result in a maximum increase of approximately $2.56, or approximately 0.23%. These impacts all reflect the Company's proposed WACC so the annual impacts would be even less if the BPU utilizes a 9.75%

cost of equity and updates the debt costs and capital structure. Therefore, while annual impacts will increase under my proposal, I believe that the resulting revenue requirements charged to ratepayers will still be reasonable, especially when the reduction in the cost of capital discussed above is also taken into account.

Q. Are there other benefits of adopting a shorter amortization period?

A. Yes, there are. Another benefit of adopting a shorter amortization period is that it will limit the amount of "pancaking" of rates as new energy efficiency programs are introduced. Under the Company's proposal, ratepayers would continue to pay for costs associated with the EEE Ext II program through 2033. However, all of the program investment will have been invested by 2018. It is likely that PSE&G will seek to implement additional energy efficiency programs after that date. If so, ratepayers will find themselves paying for multiple programs at the same time. I understand that a certain amount of overlap is unavoidable. For example, ratepayers are currently being charged rates for the Company's Carbon Abatement program, Energy Efficiency Program, and Energy Efficiency Extension Program. However, this overlap will be exacerbated if PSE&G is permitted to utilize a 15-year amortization period for the EEE Ext II Program and future energy efficiency projects.

In addition, the use of a 5-year amortization period is more consistent with the repayment periods for project costs paid by participants in the energy efficiency programs than the 15-year period proposed by the Company.

Finally, the use of a 5-year amortization period is also consistent with the amortization periods used for the previous PSE&G Economic Energy Efficiency and

Economic Energy Efficiency Extension Programs, as well as with the amortization periods authorized by the Board for other New Jersey energy efficiency programs. For all these reasons, I recommend that the BPU continue to utilize a 5-year amortization period for program investment if an EEE Ext II program is approved.

D. Participation Fee

Q. Please describe the Participation Fee that the Company is proposing in this case.

A. As described on page 13 of Mr. Melanson's direct testimony, the Company is proposing to charge participants a Participation Fee of 1.5% of the cost of each participant's overall project cost. This fee would be billed to the participants and repaid over the project repayment period. Mr. Melanson states that the Participation Fee "is intended to allow the Company to recover a limited portion of the decline in distribution sales attributable to energy efficiency programs....".[8] PSE&G proposes that the Participation Fee be retained by the Company and its shareholders, and not used to offset program costs charged to ratepayers.

Q. How did the Company determine the magnitude of the Participation Fee?

A. As shown in the response to RCR-A-7, PSE&G estimated its lost margins over the life of the projected energy measures, assuming that a base rate case would be filed in November 2017 and that new rates would be effective in March 2019. The resulting lost margins of $1.71 million were then compared to the proposed program investment of $95

8 **Page 13 of Mr. Melanson's direct testimony.**

million, resulting in a ratio of 1.8%. The Company then rounded this ratio down to 1.5% for its proposed Participation Fee.

Q. Do you support the Participation Fee as proposed by the Company?

A. No, I do not. The Company's proposed Participation Fee is based on a very limited view of operating margins. PSE&G's approach assumes that shareholders should be compensated for margins lost as a result of the energy efficiency programs being proposed. However, PSE&G has not considered other factors that could increase shareholder margins over this period. On October 30, 2014, Public Service Enterprise Group ("PSEG") released its third quarter earnings report, showing that utility earnings for the first nine months of 2014 increased by $97 million over 2013 results. On a per share basis, PSE&G's earnings increased from $0.92 per share for the first nine months of 2013 to $1.11 per share for the first nine months of 2014. Thus, there are many factors that impact utility earnings. In addition, there are factors that can change the BPU's determination of what constitutes a reasonable level of rates. For example, as noted above, capital costs have declined significantly since the Company's last base rate case, yet base distribution rates still reflect a 10.3% return on equity. The BPU has traditionally utilized the base rate case process as the appropriate mechanism for determining pro forma sales levels. The Company has not demonstrated that it is necessary or appropriate for the BPU to deviate from this practice in this case by permitting the Company to recover lost margins. The BPU has not adopted a policy with regard to compensation for lost margins. If the Board believes that some compensation is appropriate, then it should open a generic proceeding to investigate this issue. Lost margins should not be awarded on a piecemeal basis as PSE&G is proposing this case. Accordingly, the BPU should deny the Company's request to charge a Participation Fee to recover lost margins.

Q. If the BPU determines that some additional fees should be paid by program participants, how should any such fees be reflected for ratemaking purposes?

A. If the BPU determines that additional fees should be paid by participants, then revenues received from any such fee should be included in the Company's revenue requirement as an offset to the amount that would otherwise be charged to ratepayers. As demonstrated above in TABLE 1 and TABLE 2, the vast majority of program costs are being paid by the Company's ratepayers. Electric ratepayers would be responsible for $95.78 million of the total electric costs while participants would pay $18.57 million in repayment fees. With regard to gas projects, ratepayers would be responsible for $45.56 million, while program participants would contribute $8.7 million. In both cases, shareholders are paying <u>none</u> of the costs of the programs and in fact, stand to earn additional profits of $26.62 million if the Company's proposed amortization period and WACC are adopted. Even if a shorter amortization period and a lower return are adopted as proposed by Rate Counsel, shareholders still stand to earn millions of dollars in additional profits from these programs. It is irresponsible to reward shareholders further with an additional Participation Fee, when ratepayers are bearing the overwhelming majority of the costs of these programs. Accordingly, if the BPU believes that participants should be charged a Participation Fee, revenues from the fee should be credited to the revenue requirement instead of being used to increase shareholder returns.

E. Capitalized IT Costs

Q. Please summarize the Company's claim for capitalized IT costs.

A. PSE&G is proposing to recover capitalized IT costs of $1.17 million from ratepayers. According to page 14 of Mr. Melanson's testimony, PSE&G believes that "...IT system modifications are necessary to improve on-bill customer repayment functionality." The Company projects that these IT improvements will occur in May 2016. It is proposing to amortize these capitalized costs over 5 years and to accrue carrying charges at the pre-tax WACC of 11.852% authorized in the Company's last base rate case.

Q. Do you believe that the Company has justified its proposal to charge ratepayers for an additional $1.17 million in capitalized IT costs?

A. No, I do not. PSE&G has already received authorization for over $2 million of capitalized IT costs.[9] In addition to $1 million authorized in the Carbon Abatement program and $1 million authorized in the EEE filing, PSE&G stated in that response that additional amounts have also been charged to other GPRC Programs as "administrative costs".

The Company has not justified its request for additional expenditures of $1.17 million in this case. Except for a brief description of this claim in Mr. Melanson's testimony, PSE&G did not include testimony explaining how the budgeted IT costs were developed or why the Company had not undertaken the on-bill payment upgrades previously. Nor has the Company demonstrated why any additional IT upgrades could

9 Per the response to RCR-A-22.

not be provided by in-house PSE&G personnel, whose labor costs are already being recovered through base rates.

Q. Do you have additional concerns regarding the timing of these costs?

A. Yes, I do. The Company has indicated that these IT upgrades will not be in-service until May 2016 and that any system upgrades would be used not only by EEE Ext II participants, but also by the Carbon Abatement, EEE, and EEE Extension participants that have repayments remaining at the time the billing system enhancements are complete. Yet the Company seeks to recover the entire cost from ratepayers through the rates established as a result of this proceeding. IT improvements to facilitate on-bill repayments are therefore related to multiple Company programs, and not just to the EEE Ext. II program, in spite of the fact that it is proposing to assign the entire $1.7 million in IT system improvement costs to the programs at issue in this proceeding.

Q. What do you recommend?

A. I recommend that the Board reject the Company's claim for recovery of additional capitalized IT costs at this time. PSE&G has already received authorization for substantial IT expenditures in other filings. In addition, it has not provided sufficient details for its IT claim in this case nor has it shown why additional IT upgrades could not be handled by in-house personnel. Therefore, the Board should eliminate $1.17 million in capitalized IT costs from the Company's budgeted costs in this case.

F. Administrative Cost Recovery

Q. What level of administrative costs is the Company proposing in this case?

A. PSE&G has included administrative costs of $13.7 million in its filing. These costs include administration and program development, sales and marketing activities, training, rebate processing, inspections and other quality control functions, and follow-up evaluation and related research.

Q. How do the administrative costs compare to the program investment costs being claimed in this case?

A. PSE&G's estimated administrative costs of $13.7 million equate to approximately 14.4% of its $95 million program investment budget. Under the Company's proposal, ratepayers would pay 100% of these costs. The Company has claimed that its percentage of administrative costs is relatively high since many of its costs are fixed, especially labor costs. PSE&G claims that employee levels cannot be reduced even as work on existing energy efficiency projects winds down. Instead, PSE&G has implied that a larger percentage of these costs will now be charged to other programs, such as the EEE Ext II Program.

In addition to the percentage of administrative costs, I am also concerned about the salary levels for the personnel being charged to these programs. As shown in the response to RCR-A-20, the personnel assigned to these administrative functions are, for the most part, very highly paid. Salaries for many of these employees exceed $100,000 annually, excluding fringe benefits and overhead costs. Since PSE&G distributes a broad range of overhead costs to all labor costs, the per employee costs allocated to the EEE

Ext II programs would be significantly greater than those shown in this data request response.

The EEE Ext II program, if approved, will follow several other programs implemented by PSE&G, such as the Carbon Abatement Program, Economic Energy Efficiency Program, and Economic Energy Efficiency Extension. While I appreciate the fact that implementation of a new program often requires a concentrated administrative effort, by this time PSE&G should be relatively familiar with the administrative requirements of these programs. Accordingly, I believe that a request for approval of administrative costs comprising 14.4% of program investment is excessive.

Q. What do you recommend?

A. I recommend that the BPU authorize administrative costs of 8% of total program investment for the EEE Ext II program. This recommendation was developed by examining actual administrative costs incurred for the Carbon Abatement, Economic Energy Efficiency, Economic Energy Efficiency Extension programs, which are averaging approximately 7-9% of program investment. All administrative costs should be subject to review in each annual filing to ensure that the actual costs incurred were necessary and that the level of such costs was reasonable. In addition, I recommend that the Company be required to support its administrative cost claims in future filings with information identifying (a) individual employees charging costs to the program, (b) the salary and wage rates for each employee allocating costs to the program, and (c) the total costs per employee including fringe benefits and overhead levels.

Q. Do you have any additional comments?

A. Yes, in addition to my recommendation to limit the Company's recovery of administrative costs to 8% of program investment, the BPU may also want to consider requiring program participants to contribute to the Company's administrative costs. The BPU adopted a similar policy with regard to its solar programs in May 2012. While ratepayers had initially been responsible for paying all of the administrative costs for most of the solar programs that had been introduced, one of the objectives of the BPU's May 2012 Order in BPU Docket No. EO11050311V was to mitigate the cost of solar financing programs on New Jersey ratepayers. In its May 2012 Order in BPU Docket No. EO11050311V, which approved extensions of solar renewable energy certificate ("SREC") financing programs, the BPU found that for new programs "...all administrative fees would be paid for by the solar developer or the generation customer."[10] The BPU may want to adopt a similar policy for future energy efficiency programs.

Q. Does this conclude your testimony?

A. Yes, it does at this time. Rate Counsel reserves the right to present supplemental testimony based on any updated and/or new information.

10 I/M/O The Review of Utility Supported Solar Programs, BPU Docket No. EO11050311V, Order at page 27 (May 23, 2012).

APPENDIX A

Company	Utility	State	Docket	Date	Topic	On Behalf Of
Black Hills/Kansas Gas Utility Company	G	Kansas	14-BHCG-502-RTS	9/14	Revenue Requirements	Citizens' Utility Ratepayer Board
Public Service Company of New Mexico	E	New Mexico	14-00158-UT	9/14	Renewable Energy Rider	Office of Attorney General
Public Service Company of New Mexico	E	New Mexico	13-00390-UT	8/14	Abandonment of San Juan Units 2 and 3	Office of Attorney General
Atmos Energy Company	G	Kansas	14-ATMG-320-RTS	5/14	Revenue Requirements	Citizens' Utility Ratepayer Board
Rockland Electric Company	E	New Jersey	ER13111135	5/14	Revenue Requirements	Division of Rate Counsel
Kansas City Power and Light Company	E	Kansas	14-KCPE-272-RTS	4/14	Abbreviated Rate Filing	Citizens' Utility Ratepayer Board
Comcast Cable Communications	C	New Jersey	CR13100885-906	3/14	Cable Rates	Division of Rate Counsel
New Mexico Gas Company	G	New Mexico	13-00231-UT	2/14	Merger Policy	Office of Attorney General
Water Service Corporation (Kentucky)	W	Kentucky	2013-00237	2/14	Revenue Requirements	Office of Attorney General
Oneok, Inc. and Kansas Gas Service	G	Kansas	14-KGSG-100-MIS	12/13	Plan of Reorganization	Citizens' Utility Ratepayer Board
Public Service Electric & Gas Company	E/G	New Jersey	EO13020155 GO13020156	10/13	Energy Strong Program	Division of Rate Counsel
Southwestern Public Service Company	E	New Mexico	12-00350-UT	8/13	Cost of Capital, RPS Rider, Gain on Sale, Allocations	New Mexico Office of Attorney General
Westar Energy, Inc.	E	Kansas	13-WSEE-629-RTS	8/13	Abbreviated Rate Filing	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	E	Delaware	13-115	8/13	Revenue Requirements	Division of the Public Advocate
Mid-Kansas Electric Company (Southern Pioneer)	E	Kansas	13-MKEE-447-MIS	8/13	Abbreviated Rate Filing	Citizens' Utility Ratepayer Board
Jersey Central Power & Light Company	E	New Jersey	ER12111052	6/13	Reliability Cost Recovery Consolidated Income Taxes	Division of Rate Counsel
Mid-Kansas Electric Company	E	Kansas	13-MKEE-447-MIS	5/13	Transfer of Certificate Regulatory Policy	Citizens' Utility Ratepayer Board
Mid-Kansas Electric Company (Southern Pioneer)	E	Kansas	13-MKEE-452-MIS	5/13	Formula Rates	Citizens' Utility Ratepayer Board
Chesapeake Utilities Corporation	G	Delaware	12-450F	3/13	Gas Sales Rates	Attorney General
Public Service Electric and Gas Co.	E	New Jersey	EO12080721	1/13	Solar 4 All - Extension Program	Division of Rate Counsel
Public Service Electric and Gas Co.	E	New Jersey	EO12080726	1/13	Solar Loan III Program	Division of Rate Counsel
Lane Scott Electric Cooperative	E	Kansas	12-MKEE-410-RTS	11/12	Acquisition Premium, Policy Issues	Citizens' Utility Ratepayer Board
Kansas Gas Service	G	Kansas	12-KGSG-835-RTS	9/12	Revenue Requirements	Citizens' Utility Ratepayer Board
Kansas City Power and Light Company	E	Kansas	12-KCPE-764-RTS	8/12	Revenue Requirements	Citizens' Utility Ratepayer Board
Woonsocket Water Division	W	Rhode Island	4320	7/12	Revenue Requirements	Division of Public Utilities

Company	Utility	State	Docket	Date	Topic	On Behalf Of
						and Carriers
Atmos Energy Company	G	Kansas	12-ATMG-564-RTS	6/12	Revenue Requirements	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	E	Delaware	110258	5/12	Cost of Capital	Division of the Public Advocate
Mid-Kansas Electric Company (Western)	E	Kansas	12-MKEE-491-RTS	5/12	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Atlantic City Electric Company	E	New Jersey	ER11080469	4/12	Revenue Requirements	Division of Rate Counsel
Mid-Kansas Electric Company (Southern Pioneer)	E	Kansas	12-MKEE-380-RTS	4/12	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	G	Delaware	11-381F	2/12	Gas Cost Rates	Division of the Public Advocate
Atlantic City Electric Company	E	New Jersey	EO11110650	2/12	Infrastructure Investment Program (IIP-2)	Division of Rate Counsel
Chesapeake Utilities Corporation	G	Delaware	11-384F	2/12	Gas Service Rates	Division of the Public Advocate
New Jersey American Water Co.	W/WW	New Jersey	WR11070460	1/12	Consolidated Income Taxes Cash Working Capital	Division of Rate Counsel
Westar Energy, Inc.	E	Kansas	12-WSEE-112-RTS	1/12	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Puget Sound Energy, Inc.	E/G	Washington	UE-111048 UG-111049	12/11	Conservation Incentive Program and Others	Public Counsel
Puget Sound Energy, Inc.	G	Washington	UG-110723	10/11	Pipeline Replacement Tracker	Public Counsel
Empire District Electric Company	E	Kansas	11-EPDE-856-RTS	10/11	Revenue Requirements	Citizens' Utility Ratepayer Board
Comcast Cable	C	New Jersey	CR11030116-117	9/11	Forms 1240 and 1205	Division of Rate Counsel
Artesian Water Company	W	Delaware	11-207	9/11	Revenue Requirements Cost of Capital	Division of the Public Advocate
Kansas City Power & Light Company	E	Kansas	10-KCPE-415-RTS (Remand)	7/11	Rate Case Costs	Citizens' Utility Ratepayer Board
Midwest Energy, Inc.	G	Kansas	11-MDWE-609-RTS	7/11	Revenue Requirements	Citizens' Utility Ratepayer Board
Kansas City Power & Light Company	E	Kansas	11-KCPE-581-PRE	6/11	Pre-Determination of Ratemaking Principles	Citizens' Utility Ratepayer Board
United Water Delaware, Inc.	W	Delaware	10-421	5/11	Revenue Requirements Cost of Capital	Division of the Public Advocate
Mid-Kansas Electric Company	E	Kansas	11-MKEE-439-RTS	4/11	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
South Jersey Gas Company	G	New Jersey	GR10060378-79	3/11	BGSS / CIP	Division of Rate Counsel
Chesapeake Utilities Corporation	G	Delaware	10-296F	3/11	Gas Service Rates	Division of the Public Advocate
Westar Energy, Inc.	E	Kansas	11-WSEE-377-PRE	2/11	Pre-Determination of Wind Investment	Citizens' Utility Ratepayer Board

Company	Utility	State	Docket	Date	Topic	On Behalf Of
Delmarva Power and Light Company	G	Delaware	10-295F	2/11	Gas Cost Rates	Attorney General
Delmarva Power and Light Company	G	Delaware	10-237	10/10	Revenue Requirements Cost of Capital	Division of the Public Advocate
Pawtucket Water Supply Board	W	Rhode Island	4171	7/10	Revenue Requirements	Division of Public Utilities and Carriers
New Jersey Natural Gas Company	G	New Jersey	GR10030225	7/10	RGGI Programs and Cost Recovery	Division of Rate Counsel
Kansas City Power & Light Company	E	Kansas	10-KCPE-415-RTS	6/10	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Atmos Energy Corp.	G	Kansas	10-ATMG-495-RTS	6/10	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Empire District Electric Company	E	Kansas	10-EPDE-314-RTS	3/10	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Delmarva Power and Light Company	E	Delaware	09-414 and 09-276T	2/10	Cost of Capital Rate Design Policy Issues	Division of the Public Advocate
Delmarva Power and Light Company	G	Delaware	09-385F	2/10	Gas Cost Rates	Division of the Public Advocate
Chesapeake Utilities Corporation	G	Delaware	09-398F	1/10	Gas Service Rates	Division of the Public Advocate
Public Service Electric and Gas Company	E	New Jersey	ER09020113	11/09	Societal Benefit Charge Non-Utility Generation Charge	Division of Rate Counsel
Delmarva Power and Light Company	G	Delaware	09-277T	11/09	Rate Design	Division of the Public Advocate
Public Service Electric and Gas Company	E/G	New Jersey	GR09050422	11/09	Revenue Requirements	Division of Rate Counsel
Mid-Kansas Electric Company	E	Kansas	09-MKEE-969-RTS	10/09	Revenue Requirements	Citizens' Utility Ratepayer Board
Westar Energy, Inc.	E	Kansas	09-WSEE-925-RTS	9/09	Revenue Requirements	Citizens' Utility Ratepayer Board
Jersey Central Power and Light Co.	E	New Jersey	EO08050326 EO08080542	8/09	Demand Response Programs	Division of Rate Counsel
Public Service Electric and Gas Company	E	New Jersey	EO09030249	7/09	Solar Loan II Program	Division of Rate Counsel
Midwest Energy, Inc.	E	Kansas	09-MDWE-792-RTS	7/09	Revenue Requirements	Citizens' Utility Ratepayer Board
Westar Energy and KG&E	E	Kansas	09-WSEE-641-GIE	6/09	Rate Consolidation	Citizens' Utility Ratepayer Board
United Water Delaware, Inc.	W	Delaware	09-60	6/09	Cost of Capital	Division of the Public Advocate
Rockland Electric Company	E	New Jersey	GO09020097	6/09	SREC-Based Financing Program	Division of Rate Counsel
Tidewater Utilities, Inc.	W	Delaware	09-29	6/09	Revenue Requirements Cost of Capital	Division of the Public Advocate
Chesapeake Utilities Corporation	G	Delaware	08-269F	3/09	Gas Service Rates	Division of the Public Advocate

The Columbia Group, Inc., Testimonies of Andrea C. Crane

Company	Utility	State	Docket	Date	Topic	On Behalf Of
Delmarva Power and Light Company	G	Delaware	08-266F	2/09	Gas Cost Rates	Division of the Public Advocate
Kansas City Power & Light Company	E	Kansas	09-KCPE-246-RTS	2/09	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Jersey Central Power and Light Co.	E	New Jersey	EO08090840	1/09	Solar Financing Program	Division of Rate Counsel
Atlantic City Electric Company	E	New Jersey	EO06100744 EO08100875	1/09	Solar Financing Program	Division of Rate Counsel
West Virginia-American Water Company	W	West Virginia	08-0900-W-42T	11/08	Revenue Requirements	The Consumer Advocate Division of the PSC
Westar Energy, Inc.	E	Kansas	08-WSEE-1041-RTS	9/08	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Artesian Water Company	W	Delaware	08-96	9/08	Cost of Capital, Revenue, New Headquarters	Division of the Public Advocate
Comcast Cable	C	New Jersey	CR08020113	9/08	Form 1205 Equipment & Installation Rates	Division of Rate Counsel
Pawtucket Water Supply Board	W	Rhode Island	3945	7/08	Revenue Requirements	Division of Public Utilities and Carriers
New Jersey American Water Co.	W/WW	New Jersey	WR08010020	7/08	Consolidated Income Taxes	Division of Rate Counsel
New Jersey Natural Gas Company	G	New Jersey	GR07110889	5/08	Revenue Requirements	Division of Rate Counsel
Kansas Electric Power Cooperative, Inc.	E	Kansas	08-KEPE-597-RTS	5/08	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Public Service Electric and Gas Company	E	New Jersey	EX02060363 EA02060366	5/08	Deferred Balances Audit	Division of Rate Counsel
Cablevision Systems Corporation	C	New Jersey	CR07110894, et al..	5/08	Forms 1240 and 1205	Division of Rate Counsel
Midwest Energy, Inc.	E	Kansas	08-MDWE-594-RTS	5/08	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board
Chesapeake Utilities Corporation	G	Delaware	07-246F	4/08	Gas Service Rates	Division of the Public Advocate
Comcast Cable	C	New Jersey	CR07100717-946	3/08	Form 1240	Division of Rate Counsel
Generic Commission Investigation	G	New Mexico	07-00340-UT	3/08	Weather Normalization	New Mexico Office of Attorney General
Southwestern Public Service Company	E	New Mexico	07-00319-UT	3/08	Revenue Requirements Cost of Capital	New Mexico Office of Attorney General
Delmarva Power and Light Company	G	Delaware	07-239F	2/08	Gas Cost Rates	Division of the Public Advocate
Atmos Energy Corp.	G	Kansas	08-ATMG-280-RTS	1/08	Revenue Requirements Cost of Capital	Citizens' Utility Ratepayer Board