BEFORE THE STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

IN THE MATTER OF THE VERIFIED) **PETITION OF ROCKLAND ELECTRIC)** **COMPANY FOR APPROVAL OF A LOW)** **INCOME AUDIT AND DIRECT INSTALL)** **ENERGY EFFICIENCY PROGRAM AND)** **ASSOCIATED RATE RECOVERY)** **MECHANISM (LOW INCOME AUDIT III))**	**BPU DOCKET NO. ER17080869**

DIRECT TESTIMONY OF ROBERT J. HENKES
ON BEHALF OF THE
STATE OF NEW JERSEY
DIVISION OF RATE COUNSEL

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IN THE MATTER OF THE VERIFIED PETITION OF ROCKLAND ELECTRIC COMPANY FOR APPROVAL OF A LOW INCOME AUDIT AND DIRECT INSTALL ENERGY EFFICIENCY PROGRAM AND ASSOCIATED RATE RECOVERY (LOW INCOME AUDIT III PROGRAM)

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DIRECT TESTIMONY OF ROBERT J. HENKES

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I. STATEMENT OF QUALIFICATIONS

Q. WOULD YOU STATE YOUR NAME AND ADDRESS?

A. My name is Robert J. Henkes and my business address is 7 Sunset Road, Old Greenwich, Connecticut 06870.

Q. WHAT IS YOUR PRESENT OCCUPATION?

A. I am Principal and founder of Henkes Consulting, a financial consulting firm that specializes in utility regulation.

Q. WHAT IS YOUR REGULATORY EXPERIENCE?

A. I have prepared and presented numerous testimonies in rate proceedings involving electric, gas, telephone, water and wastewater companies in jurisdictions nationwide including Arkansas, Delaware, District of Columbia, Georgia, Kentucky, Maryland, New Jersey, New Mexico, Pennsylvania, Vermont, the U.S. Virgin Islands and before the Federal Energy Regulatory Commission.

Q. WHAT OTHER PROFESSIONAL EXPERIENCE HAVE YOU HAD?

A. Prior to founding Henkes Consulting in 1999, I was a Principal of The Georgetown Consulting Group, Inc. for over 20 years. At Georgetown Consulting, I performed the same type of consulting services as I am currently rendering through Henkes Consulting. Prior to my association with Georgetown Consulting, I was employed by the American Can

Company as Manager of Financial Controls. Before joining the American Can Company, I was employed by the management consulting division of Touche Ross & Company (now Deloitte & Touche) for over six years. At Touche Ross, my experience, in addition to regulatory work, included numerous projects in a wide variety of industries and financial disciplines such as cash flow projections, bonding feasibility, capital and profit forecasting, and the design and implementation of accounting and budgetary reporting and control systems.

Q. WHAT IS YOUR EDUCATIONAL BACKGROUND?

A. I hold a Bachelor degree in Management Science received from the Netherlands School of Business, The Netherlands in 1966; a Bachelor of Arts degree received from the University of Puget Sound, Tacoma, Washington in 1971; and an MBA degree in Finance received from Michigan State University, East Lansing, Michigan in 1973. I have also completed the CPA program of the New York University Graduate School of Business.

II. SCOPE AND PURPOSE OF TESTIMONY

Q. WHAT IS THE SCOPE AND PURPOSE OF THIS TESTIMONY?

A. On August 8, 2017, Rockland Electric Company ("RECO" or "Company") filed a Petition with the Board of Public Utilities ("Board" or "BPU") to implement a Low Income Audit III Program and receive rate recovery for the associated program costs through the Company's existing RGGI Surcharge.

Henkes Consulting was engaged by the New Jersey Division of Rate Counsel ("Rate Counsel") to conduct a review and analysis of the filing and present recommendations to the Board with regard to the issue areas of revenue requirements and cost recovery. Ezra D. Hausman, Ph.D. is also filing testimony on behalf of Rate Counsel in this proceeding regarding program design issues.

In developing this testimony, I have reviewed and analyzed the revenue requirement and cost recovery aspects of RECO's Petition, the testimonies of RECO witnesses Donald E. Kennedy and John de la Bastide, RECO's responses to initial and follow-up data requests submitted by Rate Counsel and BPU Staff; and other relevant documents and data.

III. SUMMARY OF RECOMMENDATIONS

Q. MR. HENKES, PLEASE SUMMARIZE YOUR RECOMMENDATIONS.

A. Based on my review and analysis of the revenue requirement and cost recovery aspects of the previously referenced Low Income Audit III Program filing material and other related documents and data, I am making the following recommendations to the Board:

1) The Company's proposed ten (10)-year amortization period for the Low Income Audit III Program costs should be disallowed by the Board; however, if the Low Income Audit III Program is approved , the Board should permit only a five (5)-year amortization period; and

2) The Company's proposed administrative costs in support of the Low Income Audit III Program should be reduced to exclude the cost component claimed for Evaluation activities.

These recommendations should be considered in conjunction with the recommendations made by Rate Counsel witness, Ezra Hausman, and would only apply in the event the Board approves the Company's proposed Low Income Audit III Program.

IV. CASE OVERVIEW

Q. PLEASE PROVIDE A BRIEF OVERVIEW OF THIS CASE.

A. In this petition, RECO has requested authorization from the Board to implement its proposed Low Income Audit III Program and to recover any costs associated with the program through its RGGI Surcharge. The purpose of the proposed Low Income Audit III Program is to provide free energy efficiency measures, recommended as a result of an energy audit, to the Company's customers that meet specified income criteria. The Low Income Audit III Program would be implemented over a two-year period with program costs of $225,800 in year 1 and $229,600 in year 2, or a total cost of $455,400 over the two-year program period. The Company intends the proposed Low Income Audit III Program to be similar in most material respects to its prior Low Income Audit I Program that was approved by the Board in Docket No. EO09010061 and its current Low Income Audit II Program that was approved by the Board in Docket No. ER13060535.

As shown in Mr. de la Bastide's direct testimony, Low Income Audit III Program's revenue requirement would be calculated as follows:

*Revenue Requirements = (Cost of Capital * Net Investment) + Amortization Expense*
+Administration Costs, Including Program Evaluation Costs - Program Investment Repayments(if applicable)

Net investment represents the gross Low Income Audit III Program costs, less the associated accumulated amortization and accumulated deferred income taxes. The Cost of Capital is RECO's pre-tax overall weighted average cost of capital ("WACC") of 10.77% that was approved by the Board in the Company's last base rate case at Docket No. ER16050428. The amortization costs represent the gross Low Income Audit III Program costs amortized over a 10-year period. The administrative costs to be recovered are proposed to total $132,000, consisting of $41,000 for Vendor Administration, $40,600 for RECO Internal Administration, $20,000 for Direct Mail/Other Outreach/Neighborhood Events, $7,600 for Field Inspections, and $22,800 for Evaluation costs.

The Low Income Audit III Program component of the RGGI Surcharge would be set initially to recover estimated annual expenditures as approved by the Board, which expenditures would be subject to deferred accounting, with interest, and would be reconciled on an annual basis.

Q. DID THE COMPANY INITIALLY PROPOSE TO OFFSET ITS ANNUAL LOW INCOME AUDIT III PROGRAM REVENUE REQUIREMENTS WITH THE

COMPANY'S ANNUAL REMITTANCES TO THE NJCEP FOR CLEAN ENERGY PROGRAM COSTS UNDER THE STATEWIDE COMFORT PARTNERS BUDGET?

A. Yes, this proposal is addressed on page 10, lines 1-5, of the testimony of RECO witness Donald E. Kennedy. However, as stated in its responses to S-RECO-EE-22, S-RECO-23 and INF-3, the Company has subsequently withdrawn that proposal.

V. DISCUSSION OF ISSUES

1. Low Income Audit III Program Cost Amortization Period.

Q. DO YOU AGREE WITH THE COMPANY'S PROPOSAL TO AMORTIZE THE LOW INCOME AUDIT III PROGRAM COSTS OVER A TEN-YEAR AMORTIZATION PERIOD?

A. No, I do not. There are several reasons why this proposed amortization period should be rejected by the Board. Petition Exhibit C, Schedule JD-1, page 1 and the response to data request S-RECO-EE-14 show that the total revenue requirements to be charged to the ratepayers would be as follows under RECO's proposed 10-year amortization period as compared to the use of alternative 7-year and 5-year amortization periods:

10-year amortization period:	$559,837
7-year amortization period:	$525,026
5-year amortization period:	$501,817

Thus, the first reason for adopting a shorter amortization period than the proposed ten years is that it is more economical from the ratepayer's point of view.

Second, the proposed 10-year amortization period is inconsistent with the program cost amortization periods agreed to by the parties and adopted by the Board for RECO's prior Low Income Audit I Program and currently effective Low Income Audit II Program. Specifically, while I understand that in its Low Income Audit I Program filing RECO proposed a 3-year program cost amortization period, the parties eventually stipulated, and the Board approved, the use of a 5-year amortization period. Similarly, for RECO's currently existing Low Income Audit II Program the Board again approved a 5-year program cost amortization that was stipulated by the parties. The Company has advanced no reason why in this case this should be changed to a 10-year amortization period, particularly since this is a relatively small program.

Finally, it is my understanding that the proposed 10-year amortization period is also inconsistent with what has been allowed by the Board for the energy efficiency programs of other New Jersey utilities. For example, Elizabethtown Gas Company's most recent energy efficiency program approved by the Board in Docket No. GR16070618 in April 2017 uses a 4-year amortization period; New Jersey Natural Company's 2014 energy efficiency program approved by the Board in Docket No. GO14121412 in July 2015 uses a 5-year amortization period; while PSE&G's most recent energy efficiency program approved by the Board in Docket No. EO17030196 (involving very large program costs) uses a 7-year amortization period.

Q. WHAT IS YOUR RECOMMENDATION WITH REGARD TO THIS ISSUE?

A. Based on the foregoing findings, I recommend that a 5-year amortization period continue to be used for RECO's proposed Low Income Audit III Program costs if this program were to be approved by the Board in this case.

2. <u>Program Evaluation Costs</u>

Q. DO YOU AGREE THAT THE COMPANY'S PROPOSED CHARGES FOR PROGRAM EVALUATION COSTS SHOULD BE INCLUDED AS A COST COMPONENT IN THIS CASE?

A. No, I do not. The program evaluations in RECO's prior Low Income Audit Programs have always been performed by the Center for Energy, Economics, and Environmental Policy ("CEEEP") at Rutgers University. The response to S-RECO-EE-16 shows that while the Company had projected to incur Evaluation costs in its prior Low Income Audit I and Low Income Audit II Programs ($7,500 in the Low Income Audit I Program and $30,600 in the Low Income Audit II Program), in actuality no Evaluation costs were charged to RECO. The reason for this is explained as follows in the response to S-RECO-EE-16:

> "the Center for Energy, Economics, and Environmental Policy (CEEEP) at Rutgers performed the benefit/cost analysis at no cost to the Company so no evaluation expenses were incurred."

In the instant proceeding, RECO has apparently taken the position that it will actually incur Evaluation costs. Not knowing how much these costs will actually amount to, RECO has simply assumed that they may be equal to 5% of the overall Low Income Audit III Program costs, or $22,800. Response to RCR-A-4.

Q. WHAT IS YOUR RECOMMENDATION WITH REGARD TO THE THIS ISSUE?

A. I recommend that the Company's proposed Administrative Costs for the Low Income Audit III Program be reduced to remove the $22,800 cost component for Evaluation costs. The Company has provided no reasons or any written evidence showing that the evaluation activities of CEEEP will no longer continue to be rendered free of charge. It should also be noted that even if the Company will actually incur Evaluation costs, they have the opportunity to charge the ratepayers for these expenses through the annual reconciliation mechanism when actual Low Income Audit III Program costs are compared to the projected Low Income Audit III Program costs, if the Low Income Audit III Program is approved.

Q. MR. HENKES, DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

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

ATTACHMENTS

STATE OF NEWJERSEY
BOARD OF PUBLIC UTILITIES

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S-RECO-EE-14 In reference to Page 12 (Paragraph 29) of the Petition, RECO indicates that the Low Income Audit III Program expenditures will be recovered over a ten (10) year period beginning in the billing period commencing after the expenditure is made. In this regard, please provide the following:

a) As shown on Exhibit C, Schedule JD-1, the projected annual revenue requirements and the total program revenue requirement amount using a seven (7) year amortization.

Response: Please see Exhibit A.

b) Please provide the information requested in (a) above in excel format with all formulas intact.

Response: Please see Exhibit B.

c) As shown on Exhibit C, Schedule JD-1, the projected annual revenue requirements and the total program revenue requirement amount using a five (5) year amortization.

Response: Please see Exhibit C.

d) Please provide the information requested in (c) above in excel format with all formulas intact.

Response: Please see Exhibit D.

Exhibit A 5-year

ROCKLAND ELECTRIC COMPANY
LOW INCOME AUDIT III PROGRAM
FINANCIAL SUMMARY

Amortization Period	5 years
Equity Component	49.70%
Equity Return	9.60%
Before -Tax WACC	10.77%
Effective Tax Rate	40.85%
Interest Expense	2.70%

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	Cumulative
Expenditures													
Energy Efficiency Programs	$ 180,300	$ 184,100											$ 364,400
Cumulative Expenditures	$ 180,300	$ 364,400											
Amortization - 2017 Expenditures	36,060	36,060	$ 36,060	$ 36,060	$ 36,060								
Amortization - 2018 Expenditures		36,820	36,820	36,820	36,820	36,820						-	
Cumulative Amortization	$ 36,060	$ 108,940	$ 181,820	$ 254,700	$ 327,580	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	
Gross Expenditures	$ 180,300	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	
Accumulated Amortization	36,060	108,940	181,820	254,700	327,580	364,400	364,400	364,400	364,400	364,400	364,400	364,400	
Net Expenditures	$ 144,240	$ 255,460	$ 182,580	$ 109,700	$ 36,820	$ -	$ -	$ -	$ -	$ -	$ -	$ -	
Accumulated Deferred Tax	58,922	104,355	74,584	44,812	15,041	-	-	-	-	-	-	-	
Under/(Over) Recovery Balance	$ 85,318	$ 151,105	$ 107,996	$ 64,888	$ 21,779	$ -	$ -	$ -	$ -	$ -	$ -	$ -	
Return Requirement	$ 9,187	$ 16,270	$ 11,628	$ 6,987	$ 2,345	$ -	$ -	$ -	$ -	$ -	$ -	$ -	
Pre-Tax Equity Portion	$ 6,882	$ 12,189	$ 8,711	$ 5,234	$ 1,757	$ -	$ -	$ -	$ -	$ -	$ -	$ -	
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	
Revenue Requirement	$ 90,747	$ 134,650	$ 84,508	$ 79,867	$ 75,225	$ 36,820	$ -	$ -	$ -	$ -	$ -	$ -	
Expenses:													
Amortization	$ 36,060	$ 72,880	$ 72,880	$ 72,880	$ 72,880	$ 36,820	$ -	$ -	$ -	$ -	$ -	$ -	
Administrative	20,300	20,300	-	-	-	-	-	-	-	-	-	-	
Marketing & Sales	10,000	10,000	-	-	-	-	-	-	-	-	-	-	
Evaluation	11,400	11,400	-	-	-	-	-	-	-	-	-	-	
Inspections	3,800	3,800	-	-	-	-	-	-	-	-	-	-	
Interest Expense	2,305	4,082	2,917	1,753	588	-	-	-	-	-	-	-	
Taxable Income	6,882	12,189	8,711	5,234	1,757	-	-	0	0	0	0	0	
Federal and State Taxes	2,811	4,979	3,559	2,138	718	-	-	-	-	-	-	-	
Net Income	$ 4,071	$ 7,210	$ 5,153	$ 3,096	$ 1,039	$ -	$ -	$ -	$ -	$ -	$ -	$ -	

Exhibit C 7-year

ROCKLAND ELECTRIC COMPANY
LOW INCOME AUDIT III PROGRAM
FINANCIAL SUMMARY

Amortization Period	7 years
Equity Component	49.70%
Equity Return	9.60%
Before -Tax WACC	10.77%
Effective Tax Rate	40.85%
Interest Expense	2.70%

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	Cumulative
Expenditures													
Energy Efficiency Programs	$ 180,300	$ 184,100											$ 364,400
Cumulative Expenditures	$ 180,300	$ 364,400											
Amortization - 2017 Expenditures	25,757	25,757	$ 25,757	$ 25,757	$ 25,757	$ 25,757	$ 25,757						
Amortization - 2018 Expenditures		26,300	26,300	26,300	26,300	26,300	26,300	26,300				-	
Cumulative Amortization	$ 25,757	$ 77,814	$ 129,871	$ 181,929	$ 233,986	$ 286,043	$ 338,100	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	
Gross Expenditures	$ 180,300	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	$ 364,400	
Accumulated Amortization	25,757	77,814	129,871	181,929	233,986	286,043	338,100	364,400	364,400	364,400	364,400	364,400	
Net Expenditures	$ 154,543	$ 286,586	$ 234,529	$ 182,471	$ 130,414	$ 78,357	$ 26,300	$ -	$ -	$ -	$ -	$ -	
Accumulated Deferred Tax	63,131	117,070	95,805	74,540	53,274	32,009	10,744	-	-	-	-	-	
Under/(Over) Recovery Balance	$ 91,412	$ 169,515	$ 138,724	$ 107,932	$ 77,140	$ 46,348	$ 15,556	$ -	$ -	$ -	$ -	$ -	
Return Requirement	$ 9,843	$ 18,252	$ 14,937	$ 11,621	$ 8,306	$ 4,990	$ 1,675	$ -	$ -	$ -	$ -	$ -	
Pre-Tax Equity Portion	$ 7,374	$ 13,674	$ 11,190	$ 8,706	$ 6,222	$ 3,739	$ 1,255	$ -	$ -	$ -	$ -	$ -	

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue Requirement	$ 81,100	$ 115,810	$ 66,994	$ 63,679	$ 60,363	$ 57,048	$ 53,732	$ 26,300	$ -	$ -	$ -	$ -
Expenses:												
Amortization	$ 25,757	$ 52,057	$ 52,057	$ 52,057	$ 52,057	$ 52,057	$ 52,057	$ 26,300	$ -	$ -	$ -	$ -
Administrative	20,300	20,300	-	-	-	-	-	-	-	-	-	-
Marketing & Sales	10,000	10,000	-	-	-	-	-	-	-	-	-	-
Evaluation	11,400	11,400	-	-	-	-	-	-	-	-	-	-
Inspections	3,800	3,800	-	-	-	-	-	-	-	-	-	-
Interest Expense	2,469	4,579	3,747	2,915	2,084	1,252	420	-	-	-	-	-
Taxable Income	7,374	13,674	11,190	8,706	6,222	3,739	1,255	0	0	0	0	0
Federal and State Taxes	3,012	5,586	4,571	3,556	2,542	1,527	513	-	-	-	-	-
Net Income	$ 4,361	$ 8,088	$ 6,619	$ 5,150	$ 3,681	$ 2,211	$ 742	$ -	$ -	$ -	$ -	$ -

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S-RECO-EE-15 Please refer to Exhibit C at page 3, line 5 to page 4, line 2 and JD-1 at page 1. The witness identifies the "internal administrative expense" as $40,600 over the two years of the proposed program. Over the same two-year period, the witness also identifies marketing and sales expenses of $20,000; evaluation expenses of $22,800; and inspection expenses of $7,600. Please confirm that the total administrative expenses for the proposed Low Income Audit III Program are $91,000.

Response: The total administrative expenses for the two year program are $132,000 including evaluation. Exhibit C, Schedule JD-1, page 4 of 6 provides the detailed cost categories above.

S-RECO-EE-16 Please provide a breakdown, by category, of the administrative costs budgeted and actually spent on each previously approved Low Income Audit Programs.

Response: Below are the budgeted and actual spending tables for the Low Income I (2010-2014) and Low Income II (2015-2016) Programs. The administration costs include both vendor implementation and Company administration expenses. Actual administration costs were higher than expected in the Low Income I program since the program was extended to four years or two years beyond its initial two year program period. In addition, the Center for Energy, Economics, and Environmental Policy (CEEEP) at Rutgers performed the benefit/cost analysis at no cost to the Company so no evaluation expenses were incurred.

Low Income I (2010-2014)	Budget	Actual
Administration	$112,500	$139,440
Rebates	$650,000	$608,757
Evaluation	$7,500	$0
Total	**$770,000**	**$748,197**

Low Income II (2015-2016)	Budget	Actual
Administration	$112,780	$106,907
Rebates	$506,250	$186,478
Evaluation	$30,600	$0
Total	**$649,630**	**$293,385**

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Board Staff's Discovery Requests S-RECO-EE-17 to S-RECO-EE-23 Directed to Petitioner

S-RECO-EE-17 Please explain the great disparity in participation between 2015 and 2016 evidenced in the response to S-RECO-EE-2.

Response: While the contract was signed in early 2015, Honeywell did not begin installations until May 2015.

S-RECO-EE-18 Please refer to the response to RCR-RECO-EE-2. No participants are shown for 2014. Was this inadvertent or did no customers participate in that year? If so, please explain.

Response: There was no participation in 2014 because there was a gap between the end of the Low Income Audit I program, and the commencement of the Low Income II program.

S-RECO-EE-19 Please refer to the table provided in response to S-RECO-EE-4. Please break out the actual and budgeted expenses in each category for Low Income Audit Program I and Low Income Audit Program II.

Response: Please refer S-RECO-EE-16 response.

S-RECO-EE-20 The response to S-RECO-EE-4 shows that actual expenses fell far below the budgeted amounts in every category but administrative. Please account for this discrepancy.

Response: Administration expenses are associated to the monthly administration of the program and do not vary based on the level of participation. Therefore, the administration expenses were in line with the budget.

S-RECO-EE-21 The response to S-RECO-EE-4 indicates that nothing was spent on evaluation. Please explain why no expense is shown. If all evaluations were performed by RECO personnel and that cost is captured separately, please state where it is captured and provide a sample showing how the costs of one evaluation are reflected in the RECO budget.

Response: No evaluation expenses were incurred since no process or impact evaluations were performed. In addition, CEEEP conducted the benefit cost analysis at no charge to the Company.

S-RECO-EE-22 Please reference RECO's response to S-RECO-EE-12. If RECO plans to deduct its program expenditures from the amount it remits to the NJCEP for Clean Energy Program costs, why does RECO also seek rate recovery of all costs of LIAP III?

Response: RECO no longer plans to deduct program expenditures from the amount it remits to OCE and withdraws that proposal.

S-RECO-EE-23 The response to S-RECO-EE-12 states that RECO plans "to deduct the program expenditures from the amount it remits to the OCE . . . for Clean Energy Program costs and <u>for the historical LIAP I and II program expenses</u>." (Emphasis added). Please clarify the meaning of the emphasized language. Does RECO intend to deduct the costs of the historical LIAP I and II programs also? If not, what is the meaning of this phrase?

Response: Please refer to S-RECO-EE-22.

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INF-2

Please describe the process of retaining Honeywell as the Low Income Audit II program vendor.

Response: The Company issued an RFP in 2014 for the Low Income Audit II program implementation vendor. Three companies responded to the RFP. Honeywell was the lowest bidder and was selected.

INF-3

Please explain in more detail the Company's proposal to reduce its contributions for the Clean Energy budget.

Response: The Company is withdrawing this proposal.