

BEFORE THE STATE OF NEW JERSEY

BOARD OF PUBLIC UTILITIES

IN THE MATTER OF THE PETITION OF)
PUBLIC SERVICE ELECTRIC AND GAS)
COMPANY FOR APPROVAL OF AN)
EXTENSION OF A SOLAR GENERATION)
INVESTMENT PROGRAM)
AND ASSOCIATED COST RECOVERY)
MECHANISM AND FOR CHANGES IN THE)
TARIFF FOR ELECTRIC SERVICE)
("Solar4 All Extension Petition"))

BPU Docket No. E012080721

**SURREBUTTAL TESTIMONY OF ANDREA C. CRANE
ON BEHALF OF THE
NEW JERSEY DIVISION OF RATE COUNSEL**

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1 **I. INTRODUCTION**

2 **Q. Please state your name and business address.**

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

6
7 **Q. Did you previously file testimony in this proceeding?**

8 A. Yes, on January 14, 2013, I filed Direct Testimony on behalf of the State of New Jersey,
9 Division of Rate Counsel. My Direct Testimony addressed cost recovery and other
10 financial issues relating to the Petition filed on August 1, 2012 by Public Service Electric
11 and Gas Company ("PSE&G" or "Company"). In its Petition, the Company requested
12 approval to extend the Solar Generation Investment Program called Solar 4 All™
13 ("Extension Program"). Specifically, the Company proposed a program with a total cost
14 of \$1.864 billion, \$907.3 million of which would be funded by ratepayers. The Company
15 anticipated that the remaining costs would be recovered from sales of Solar Renewable
16 Energy Certificates ("SRECs"), sales of energy and capacity generated by solar facilities,
17 and various tax incentives.

18 In my Direct Testimony, I recommended that the BPU deny the Company's
19 proposed Extension Program, for the reasons fully discussed in that testimony. In the
20 event that the BPU does approve an Extension Program for the Company, I
21 recommended that the BPU approve carrying costs for the program that reflect a return
22 on equity of no higher than 9.75%, consistent with the most recent equity award by the
23 BPU in an electric utility base rate case. I also stated that a lower return may be

1 reasonable, given the significant differences in risk between the Company's proposed
2 program and a utility's traditional recovery of investment in electric plant through base
3 rates. In addition, I recommended that the BPU utilize the Company's current embedded
4 debt cost and current capital structure to calculate carrying costs. In the event that the
5 BPU approves an Extension Program, I also recommended that the BPU deny the
6 Company's request to recover administrative costs from ratepayers, consistent with its
7 May 23, 2012 Order in BPU Docket No. EO11050311V, In the Matter of the Review of
8 Utility Supported Solar Programs.

9
10 **Q. What is the purpose of your Surrebuttal Testimony?**

11 A. The purpose of my Surrebuttal Testimony is to address certain statements contained in
12 the Rebuttal Testimonies of Stephen Swetz, Paul S. Moul, and Terrence J. Moran filed on
13 February 4, 2013. I will also briefly address the Rebuttal Testimony of Lance R. Miller
14 on behalf of Intervenor Wattlots, LLC ("Wattlots") and the Rebuttal Testimony of
15 Anthony Shay on behalf of Intervenor Petra Solar, Inc. ("Petra Solar").

16
17 **II. RESPONSE TO PSE&G**

18 **Q. Please comment on Mr. Swetz's update to the Company's cost of debt, provided on**
19 **page 2 of his Rebuttal Testimony.**

20 A. In his Rebuttal Testimony, Mr. Swetz states that the Company's November 2012
21 embedded cost of debt was 5.3482%, which is higher than the October 2012 embedded
22 cost of 5.05% that I had cited in my Direct Testimony. It is unclear whether Mr. Swetz is
23 recommending that an updated cost of debt be used to determine the carrying costs

1 applied to the Extension Program, in the event that the Extension Program is approved, or
2 whether he is simply providing this update for informational purposes. Regardless of Mr.
3 Swetz's intent, I have no objection to using the most recent embedded cost of debt to
4 determine the appropriate carrying costs.

5
6 **Q. Please comment on Mr. Swetz's statement at page 2 of his Rebuttal Testimony that**
7 **in each of PSE&G's programs conducted pursuant to N.J.S.A. 48:3-98.1, "the Board**
8 **has approved cost recovery mechanisms providing that the utility will earn a return**
9 **at a rate equal to the weighted average cost of capital approved in its most recent**
10 **base rate case."**

11 **A.** Mr. Swetz suggests that just because the BPU approved a stipulation for a program that
12 included carrying costs at the weighted average cost of capital, the BPU is now required
13 to include carrying costs at the weighted average cost of capital ("WACC") in all
14 subsequent cases. Mr. Swetz ignores the fact that each of the prior programs was
15 resolved by a Stipulation and, as in any settlement, there was give and take among the
16 parties with regard to the various issues. Moreover, each of these Stipulations included
17 language that the provisions contained in each of the Settlement Agreements was for the
18 purpose of resolving only the program that was at issue in that particular proceeding, and
19 was not intended to set any precedent for future cases. I am not aware of any Stipulation
20 or BPU Order in which the parties agreed, or the BPU ordered, that the WACC approved
21 in the most recent base rate case would be used for all future programs that may be
22 proposed by PSE&G. In addition, Mr. Swetz's Rebuttal Testimony also ignores the fact
23 that the Company's last base rate case was resolved almost three years ago. As one

1 moves further away from the date of the Order in that case, it becomes less and less likely
2 that the rate of return found to be appropriate at that time is still reasonable. In fact, as
3 demonstrated in my Direct Testimony and in the Surrebuttal Testimony of Rate Counsel
4 witness Matthew I. Kahal, the 10.3% return on equity that the parties agreed to in the
5 Stipulation resolving the Company's last base rate case is excessive given current market
6 conditions, and given subsequent returns on equity approved by the BPU.
7

8 **Q. Please comment on Mr. Swetz's statement on page 3 of his Rebuttal Testimony that**
9 **PSE&G is not guaranteed recovery of 100% of its costs under the Extension**
10 **Program.**

11 A. Mr. Swetz is correct that the BPU could disallow a cost incurred pursuant to the
12 Extension Program, if it found that such a cost was imprudent. However, as noted in the
13 response to RCR-ROR-17, the BPU has never disallowed a cost incurred by the
14 Company for any of its energy efficiency or renewable energy programs on the basis that
15 such a cost was imprudent. More importantly, Mr. Swetz ignores the significant
16 differences between base rate recovery and the recovery of costs through a surcharge
17 mechanism, as is proposed here. First, between base rate case proceedings, utilities are at
18 risk for recovering all costs that have not been previously included in base rates. This
19 includes investment made since the Company's last base rate case as well as new or
20 increased operating expenses. These costs are recovered between base rate cases only if
21 sales have increased or other costs have declined relative to the level of revenues and
22 expenses included in the utility's last base rate case.

1 Second, with base rate recovery, the Company and its shareholders are at risk for
2 actually recovering costs even if those costs have been found to be prudent and included
3 in rates. This is because base rate recovery does not include a true-up process. Rather,
4 rates are determined based on an approved revenue requirement and shareholders bear the
5 risk of recovery between base rate cases. During this period, if revenues exceed
6 expectations or if actual expenses are less than those reflected in rates, then the Company
7 may earn more than its authorized return and shareholders would retain any such benefit
8 between base rate cases. However, the converse is also true. If revenues are less than
9 anticipated or if expenses are higher than those reflected in rates, then the Company and
10 its shareholders will not earn their authorized rate of return in any given year. Thus,
11 shareholders bear considerably more risk when costs are recovered through base rates
12 than when recovery is essentially guaranteed on a dollar-for-dollar basis through a rate
13 rider. It is in recognition of this risk that shareholders are awarded an authorized return
14 on equity that reflects a premium over a risk-free rate.

15 Assuming that all of the Company's estimates are correct, the proposed Extension
16 Program will cost ratepayers \$907.3 million, while providing the Company with a
17 guaranteed income stream (pre-tax) of \$587.7 million. However, while PSE&G would
18 be virtually guaranteed to recover its approved return, ratepayers would be at risk for any
19 changes in the revenues or costs reflected in the filing. Therefore, if SREC prices are
20 lower than the \$200 assumed by PSE&G, or if capacity and energy prices are less than
21 the prices contained in the Company's forecasts, the costs to ratepayers could be even
22 higher than those reflected in the filing. Ratepayers would also be responsible for all
23 operating, maintenance and administrative costs associated with the specific solar

1 projects. To the extent that these costs exceed the costs estimated in PSE&G's filing, it is
2 ratepayers, and not shareholders, that would bear 100% of these cost increases if the
3 Company's Extension Program was approved as proposed. Moreover, ratepayers would
4 also be responsible for any shortfalls in recovery due to lower than projected sales, as
5 well as interest on any under-recovery. Given the mechanism proposed by PSE&G, there
6 is virtually no chance that shareholders would earn less than the 10.3% proposed by
7 PSE&G, while the actual costs borne by ratepayers could vary significantly from those
8 estimated in the Company's filing.

9
10 **Q. Please comment on Mr. Swetz's statement on page 4 of his Rebuttal Testimony that**
11 **surcharge mechanisms provide the parties "with a regular opportunity to pursue a**
12 **detailed review of the Company's activity within each program" and that**
13 **ratepayers "can actually benefit from these types of reviews."**

14 **A.** Mr. Swetz's statement ignores the fact that in a base rate case, the parties have the
15 opportunity to undertake a comprehensive review of the Company's revenues, expenses,
16 investment and return requirements. No such opportunity exists for cost recovery filings
17 made pursuant to surcharge mechanisms. Instead, such filings constitute single-issue
18 ratemaking with the examination limited to only those revenues and costs relating to a
19 particular program. Thus, it is possible for the BPU to approve an increase in the rates
20 for a program whose costs are recovered through a surcharge mechanism, such as the
21 Extension Program proposed in this case, even if PSE&G is earning more than its
22 authorized return on equity.

1 Given the fact that ratepayers bear all of the risk for recovery with a surcharge
2 mechanism, and given the fact that the surcharge process does not entail a comprehensive
3 review of the Company's overall earnings, ratepayers are unlikely to "benefit" from a
4 surcharge mechanism as alleged by Mr. Swetz.

5
6 **Q. Please comment on Mr. Swetz's criticism on page 5 of his Rebuttal Testimony of**
7 **your statement that surcharge mechanisms are "big business for the electric and gas**
8 **utilities in New Jersey."**

9 **A.** First, I note that Mr. Swetz does not dispute my statement, although he claims that I have
10 ignored the fact that such programs have been approved by the Board and are consistent
11 with New Jersey's energy and environmental policies. While this is not the forum to
12 debate the impact of previously-approved surcharge programs, it is non-controvertible
13 that such programs provide shareholders with a virtually guaranteed regulated revenue
14 stream. Mr. Swetz did not address the conclusion in my Direct Testimony that PSE&G's
15 parent company, Public Service Enterprise Group, Inc. ("PSEG"), has the ability to
16 undertake solar investment programs on an unregulated basis if it believes that the risks
17 of such programs warrant this investment. Apparently, PSE&G's parent is not willing to
18 undertake such investment on an unregulated basis, at least not in New Jersey, and hence
19 it is attempting to obtain approval for regulated solar programs that provide shareholders
20 with assurance of cost recovery, including assurance of recovery of a return on equity of
21 10.3%. Since such surcharge programs are particularly lucrative for shareholders, it is
22 not surprising that PSE&G recently announced a \$3.9 billion program for which it is

1 seeking similar guaranteed ratemaking treatment.¹ While one can debate the merits of
2 any particular investment in renewable energy programs, in my opinion ratepayers have
3 clearly been harmed, not helped, by the proliferation of surcharges that now appear on the
4 customers' bills.

5
6 **Q. Does the proliferation of surcharge mechanisms also make it easier for utilities to**
7 **over-recover their costs?**

8 **A.** Yes, they do. The potential for over-recovery can occur in at least two ways. First, while
9 theoretically costs recovered through surcharge mechanisms are intended to be
10 incremental to those recovered in base rates, it is virtually impossible for any party to
11 verify that employees (and other costs) originally included in base rates are not also being
12 allocated to one or more surcharge riders. This is because employees are not strictly
13 identified as being either "base rate" employees or "surcharge" employees, but instead
14 may charge costs to both base rates and one or more riders. Employees are also
15 continuously joining and leaving the company, making it difficult to track movement
16 between base rate cases.

17 Second, it is my understanding that all costs, both those recovered through base
18 rates and those recovered through surcharge mechanisms, are allocated overhead costs.
19 Moreover, not only do overhead costs include direct employee-related benefit costs, but
20 they may also include costs of entire administrative departments that are deemed
21 "overhead" by PSE&G. To the extent that these overhead costs were included in base
22 rates and are now being allocated to new surcharge mechanisms, there is a potential for

1 See PSE&G's February 20, 2013 press release, available at:
<http://www.pseg.com/info/media/newsreleases/2013/2013-02-20.jsp>

1 over-recovery, which again is very difficult to track between base rate cases. In my
2 view, the potential for double-recovery of labor costs and overhead costs is another
3 reason why ratepayers are unlikely to “benefit” from surcharge mechanisms.
4

5 **Q. How many surcharges are currently being recovered in a typical residential**
6 **customer’s bill?**

7 A. A review of the Company’s tariff indicates the following are currently being recovered
8 through surcharge mechanisms: Social Programs, Energy Efficiency and Renewable
9 Energy Programs, Manufactured Gas Plant Remediation, Universal Service Fund
10 Programs, Lifeline Programs, Non-Utility Generation Charges, Securitization Transition
11 Charges, Solar Pilot Recovery Charges, the Carbon Abatement Program, Energy
12 Efficiency Economic Stimulus Program, Demand Response Program, Solar Generation
13 Investment Program, Solar Loan II Program, the Energy Efficiency Economic Extension
14 Program, and Capital Adjustment Program Charges.² These are in addition to the Basic
15 Generation Service charges that are recovered by the Company on a dollar-for-dollar
16 basis and which constitute a significant portion of the customer’s overall bill.
17

18 **Q. Please comment on Mr. Moul’s statement on page 2, lines 22-23 of his Rebuttal**
19 **Testimony that you ignore “the reality that the utility can choose between**
20 **alternative investments.”**

21 A. This fact is not ignored in my Direct Testimony, rather, it is one of the critical points of
22 my Direct Testimony. If the BPU approves a return on equity of 10.3% for Extension
23 Program projects, the Company will have an overarching incentive to invest as much as

2 PSE&G Tariff for Electric Service, B.P.U.N.J. No. 15 Electric, Tariff pages 57-59, 60, 62, 64, 65 and 66-68.

possible in the Extension Program, or in other programs where its return on equity is essentially guaranteed. It is not surprising that PSEG does not want to undertake solar investment projects on an unregulated basis, if it can earn an assured return on equity of 10.3% by undertaking such projects on a regulated basis through its New Jersey utility.

Approving a virtually guaranteed 10.3% return on equity for the Extension Program will also make this program substantially more attractive than investments in the distribution system that are recovered through base rates. If the Company truly has a "finite amount of capital that the Company can commit to its rate base and renewable investments" as suggested by Mr. Moul on page 3 at line 6 of his Rebuttal Testimony, and if the BPU awards the same cost of capital for both investments recovered through surcharges and investments recovered through base rates, then PSE&G will have a clear incentive to direct investments to those programs that have the greatest likelihood of earning their authorized rate of return, i.e., those recovered through the surcharge mechanisms.

Q. Please comment on Mr. Moul's statement on page 4 at lines 20-22 of his Rebuttal Testimony that today's low interest rates should be viewed relative to the long recovery period for the solar programs that the Company has proposed.

A. Mr. Moul seems to suggest that whatever carrying costs are approved in this case would remain in effect during the entire recovery period of the Extension Program, which is currently projected through 2037, or approximately 25 years. He therefore states that it is necessary to consider if the low interest rate environment will prevail over the entire recovery period and also states that it is necessary to understand why interest rates are

1 currently so low. However, it is unreasonable to suggest that any carrying cost
2 established today, by whatever measure, should prevail for the entire recovery period,
3 unless carrying costs were limited solely to debt costs related to project financing. In fact,
4 Mr. Moul acknowledged that carrying costs are likely to change over the recovery period
5 in his response to RCR-A-51, where he stated that “[t]he rate of return will remain fixed
6 up to the point when the Board resets the Company’s weighted average cost of capital in
7 the next base rate case.” This response recognizes that capital costs change over time,
8 and that such changes should be reflected in the Company’s carrying costs if the BPU
9 approves carrying costs based on a weighted average cost of capital. This position is also
10 consistent with my recommendation that the cost of capital utilized for recovery of
11 surcharge program costs should be updated between base rate cases if it is no longer
12 reasonable. Otherwise, the Company could continue to recover excessive carrying costs
13 by delaying the filing of a base rate case. Given the proliferation of surcharge
14 mechanisms, and the Company’s continued attempt to recover more and more costs
15 through such surcharges, it is reasonable to assume that the Company may not have the
16 need to file a base rate case in the foreseeable future, especially if its capital costs have
17 declined and the Company fears that this decline would be reflected in new base rates.

18 As to the Company’s second point, that it is necessary to determine why interest
19 rates are so low at the present time, I disagree with Mr. Moul’s position that this factor is
20 relevant to the determination of an appropriate carrying cost for the Extension Program.
21 Regardless of the reason for the current low capital cost environment, the fact is that
22 capital costs have declined since the Company’s last base rate case and that this decline
23 should be recognized in any carrying costs approved for the Extension Program.

Moreover, as discussed in Mr. Kahal's Surrebuttal Testimony, it is likely that low interest rates will continue for some time. This does not mean to suggest that low interest rates will prevail until 2037 or over the entire recovery period, only that any carrying cost approved in this case should reflect the currently low capital costs. In the event that the Board approves the use of a weighted average cost of capital as an appropriate carrying cost, it is my understanding that Rate Counsel does anticipate that any such WACC would be updated periodically, either through base rate case filings or through some other review mechanism, to ensure that the costs being charged to ratepayers reflect reasonable capital costs.

Q. Please comment on Mr. Moul's statement on page 7, lines 1-9 of his Rebuttal Testimony, that the Blue Chip Financial Forecasts provide "evidence that the trend of interest rates is upward...."

A. In support of his statement, Mr. Moul referenced the December 1, 2012 Blue Chip Financial Forecasts for 30-Year Treasury Bonds, Aaa-rated Corporate Bonds and Baa-rated Corporate Bonds, all of which he states are projected to increase significantly in the 2014-2018 and 2019-2023 periods. However, a review of prior Blue Chip Financial Forecasts suggests that these "consensus" forecasts can deviate greatly from actual results. For example, in the response to RCR-A-54, Mr. Moul provided the December 1, 2010 forecasts for 2012-2016 and 2017-2021. As shown in that response, the December 1, 2010 consensus forecasts for 2012 interest rates for 30-year Treasury Bonds, Aaa-rated Corporate Bonds and Baa-rated Corporate Bonds were significantly overstated. For example, in December 2010, the 2012 consensus forecast for 30-year Treasury bonds was

1 4.8% while actual rates for 30-year Treasury Bonds were below 3.0% for most of 2012,
2 declining to 2.88% in December 2012 as stated in my Direct Testimony. Similarly, the
3 2010 Blue Chip consensus forecast for Aaa-rated Corporate Bond rates during 2012 was
4 5.4%, while actual interest rates for Aaa-rated Corporate Bonds were below 4.0% in 2012
5 and declined to 3.65% by December 2012. Finally, the December 2010 Blue Chip
6 consensus forecast for 2012 interest rates for Baa-rated Corporate Bonds was 6.4%, while
7 actual Baa-rated Corporate Bond rates were under 5.0% for most of the year and declined
8 to 4.63% by December 2012. As demonstrated, the December 2010 consensus forecasts
9 were not a good indicator of 2012 interest rates and such forecasts are likely to be even
10 less accurate when projecting interest rates even further in the future.

11 Moreover, even if the BPU believed that these long-term projections were valid, it
12 would still be inappropriate to utilize those future rates to determine the Company's
13 carrying charges in this case. Projections about future interest rates are speculative and
14 should not be used to set regulated utility rates. Rather, the BPU should base its carrying
15 costs on current capital costs, and should state its intention to update these costs in the
16 future as the Company's capital costs change.

17
18 **Q. Please comment on Mr. Moran's statement on page 33 of his Rebuttal Testimony**
19 **that the Board's May 23, 2012 Order, which directed that "all administrative fees**
20 **would be paid for by the solar developer or the generation customer", did not apply**
21 **to the Company's original Solar Generation Investment Program and should not**
22 **apply to the proposed Program Extension.**

1 A. While I acknowledge that the May 23, 2012 Order did not specifically apply to the
2 Company's original Solar Generation Investment Program or to the Program Extension
3 that was filed on August 1, 2012, one of the objectives of the BPU Staff in formulating
4 the positions that the BPU adopted in its Order was to "wean the solar industry from
5 ratepayer subsidies", as stated in my Direct Testimony at page 22. This remains a valid
6 objective for any future programs approved by the BPU. The BPU recognized in the
7 May 23, 2012 Order that ratepayers have contributed significant subsidies to the
8 development of the solar industry. In order to begin to mitigate these subsidies, it is
9 appropriate to require other parties to share in the burden of financing solar investment in
10 the State of New Jersey. One way of achieving some sharing is to require that
11 administrative costs be recovered from parties other than the New Jersey ratepayers. In
12 addition, as stated in my Direct Testimony, permitting PSE&G to recover administrative
13 costs from ratepayers but requiring solar developers or generators to absorb
14 administrative costs associated with SREC Financing programs would provide an unfair
15 advantage to PSE&G in the solar energy market. Accordingly, if the BPU approves the
16 proposed Extension Program, it should not permit PSE&G to recover administrative costs
17 from ratepayers.

18
19 **III. RESPONSE TO INTERVENORS**

20 **Q. Please comment on Mr. Lance Miller's statement at page 5, lines 8-10 of his Direct**
21 **Testimony on behalf of Wattlots that the proposed Extension Program provides "a**
22 **degree of certainty in the solar market...."**

1 A. While I agree with Mr. Miller that the proposed program would provide a degree of
2 certainty to solar developers and to PSE&G shareholders, it would not provide such
3 certainty to ratepayers. The only "certainty" provided to ratepayers is the knowledge that
4 they would be responsible for all costs that are not covered by revenues from the sale of
5 SRECs, energy or capacity, or by tax incentives. Under the Company's proposal, all such
6 costs would be the responsibility of ratepayers. Moreover, the extent of such costs is
7 unknown and will depend on fluctuating market prices for SRECs, energy and capacity as
8 well as on the Company's ability to control expenditures associated with the facilities.
9 Therefore, the Extension Program shifts uncertainty from solar developers and utilities to
10 the ratepayers, without providing ratepayers with any reduction in capital costs to
11 recognize this shifting of risk.

12
13 **Q. Please comment on Mr. Anthony Shay's statement on page 3 of his Rebuttal**
14 **Testimony on behalf of Petra Solar that "Petra Solar innovation, BPU forward**
15 **thinking, and PSE&G project success has established New Jersey as a technology**
16 **and market leader."**

17 A. It is unfortunate that Mr. Shay has apparently forgotten the one principal factor that has
18 made this leadership possible – the New Jersey ratepayer. While the solar developers and
19 the utilities are applauding themselves for being such innovators and market leaders, it is
20 the ratepayers of New Jersey who are once again left holding the short straw. If the
21 Extension Program is approved as proposed, it is the ratepayers who will be responsible
22 for hundreds of millions of dollars of new charges and who will bear all of the risk of
23 fluctuating market prices and cost overruns while shareholders will earn a virtually

1 guaranteed rate of return for the next 25 years. It is time that New Jersey ratepayers were
2 given the recognition and consideration they deserve. For this reason, and for all the
3 other reasons discussed above and in my Direct Testimony, I recommend that the BPU
4 deny the Company's proposed Extension Program as filed. If the BPU approves an
5 Extension Program for PSE&G, then it should modify the Company's proposal to (1)
6 reflect reasonable carrying costs and (2) to prohibit the recovery of administrative costs
7 from ratepayers.

8
9 **Q. Does this complete your testimony?**

10 **A. Yes, it does.**