

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF)
DELMARVA POWER & LIGHT COMPANY FOR A) PSC DOCKET NO. 12-546
CHANGE IN NATURAL GAS BASE RATES)
(Filed December 7, 2012))

TESTIMONY OF STAFF WITNESS

BRIAN KALCIC

Regarding
Cost of Service and Rate Design

June 3, 2013

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I. QUALIFICATIONS AND OVERVIEW

Q. Please state your name and business address.

A. Brian Kalcic, 225 S. Meramec Avenue, Suite 720, St. Louis, Missouri 63105.

Q. What is your occupation?

A. I am an economist and consultant in the field of public utility regulation, and principal of Excel Consulting. My qualifications are described in the Appendix to this testimony.

Q. On whose behalf are you testifying in this case?

A. I am testifying on behalf of the Delaware Public Service Commission Staff (“Staff”).

Q. What is the subject of your testimony?

A. Staff requested that I review the cost of service and rate design analysis sponsored by Delmarva Power & Light Company (“Delmarva” or the “Company”) in this proceeding, and to develop an appropriate rate design that would recover Staff witness David E. Peterson’s recommended increase in delivery revenues of \$3.584 million.

In addition, I will review certain revisions to Delmarva’s proposed tariff, and sponsor alternative recommendations, where appropriate.

1 **Q. How is your testimony organized?**

2 My testimony is organized as follows. Section I of my testimony contains my
3 qualifications and an overview of my testimony. Section II reviews the Company's
4 cost-of-service study. Section III examines the Company's proposed class revenue
5 allocation and presents Staff's recommended revenue allocation. Section IV
6 discusses Staff's recommended rate design. Finally, Section V examines certain
7 revisions to Delmarva's proposed tariff.

8

9 **Q. Please summarize your primary recommendations.**

10 A. Based upon my review of the Company's filing and interrogatory responses, I
11 recommend that the Delaware Public Service Commission ("Commission"):

12

- 13 • adopt Delmarva's proposed cost-of-service methodology;
- 14 • adopt Staff's recommended class revenue allocation;
- 15 • adopt Staff's recommended rate design which includes non-uniform rate
- 16 increases to individual rate schedule tariff components; and
- 17 • approve Staff's modifications to Delmarva's proposed penalty charges for
- 18 unapproved overruns.
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23 The specific details associated with Staff's recommendations are discussed below.

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II. COST-OF-SERVICE STUDY

Q. Mr. Kalcic, please provide a brief description of the type of class cost-of-service analysis submitted by the Company in this proceeding.

A. The Company’s cost-of-service study (“COSS”) is sponsored by Mr. Michael T. Normand. Mr. Normand states that the COSS is based on the Company’s test year ended June 30, 2012, as adjusted for certain expense, sales and revenue changes identified by the Company, such that only *base-rate* related revenues and costs remain.

In general, the Company’s cost-of-service methodology reflects the traditional three-step process of functionalization, classification and allocation. *Functionalization* refers to the process whereby utility plant and related expenses are assigned to functions, such as transmission, distribution or customer service. *Classification* refers to the process where the functionalized costs are broken down into three primary cost categories: 1) demand-; 2) commodity-; 3) and customer-related costs. Finally, the *allocation* step refers to the process whereby the utility’s classified costs are assigned to rate classes, based upon a factor that reflects relative cost responsibility (for each type of cost incurred).

The functionalization, classification and allocation steps combine to produce a measure of total cost of service, by rate class. By comparing allocated cost responsibility to class revenue levels, one can determine whether a given rate class is contributing above or below its cost-of-service indications.

1 **Q. Mr. Kalcic, how many different rate classes are included in the Company's**
2 **current tariff?**

3 A. At present, the Company's tariff contains (16) rate schedules.¹ However,
4 approximately 99.9% of the Company's customers are served on just two rate
5 schedules, i.e., Service Classifications ("Rates") RG and GG.

6 Rate RG is available to residential (heating and non-heating) customers
7 only. Rate GG is available to non-residential customers with less than 2,000 Mcf of
8 monthly gas use, and a maximum daily use (i.e., Maximum Daily Quantity or
9 MDQ) of less than 500 Mcf.

10

11 **Q. Does Delmarva propose to change and/or consolidate any of its current rate**
12 **classes?**

13 A. No, it does not.

14

15 **Q. What classes are included in Delmarva's COSS?**

16

¹ The current rate schedules include: Residential Gas Sales Service (**RG**), General Gas Sales Service (**GG**), Medium Volume Gas Sales Service (**MVG**), Large Volume Gas Sales Service (**LVG**), Large Volume Gas Sales Service-Qualified Fuel Cell Provider-Renewable Capable Power Production (**LVG-QFCP**), Peak Management Rider (**PM**), General Volume Firm Transportation Service (**GVFT**), Medium Volume Firm Transportation Service (**MVFT**), Large Volume Firm Transportation Service (**LVFT**), Stand-By Gas Supply Service (**SBS**), Gas Lighting Sales Service (**GL**), Quasi-Firm Transportation Service (**QFT**), Medium Volume Interruptible Gas Transportation Service (**MVIT**), Large Volume Interruptible Gas Transportation Service (**LVIT**), Flexibly Priced Gas Supply Service (**FPS**), and Negotiated Contract Rate Service (**NCR**).

1 A. The COSS allocates Delmarva's claimed revenue requirement to the following firm
2 service customer classes: Residential (non-heating portion of Rate RG), Residential
3 Heating (space-heating portion of Rate RG), General Service (Rates GG and
4 GVFT), Medium Volume General (Rates MVG and MVFT), Large Volume
5 General (Rates LVG and LVFT), Large Volume QFCP (Rate LVG-QFCP) and
6 Lighting (Rate GL).

7

8 **Q. Why are Delmarva's non-firm (or non-core) service classes excluded from the**
9 **Company's COSS?**

10 A. The Company's non-core service classes include Rates QFT, MVIT, LVIT, FPS
11 and NCR. At the present time, Delmarva is permitted to retain 20% of all margins
12 contributed by the Company's non-core classes on a below-the-line basis, while
13 ratepayers' (80%) share is applied as a credit to the Demand Cost Rate portion of
14 the Gas Cost Rate that is charged to firm sales customers.

15 Since no portion of the margins contributed by non-core customers is
16 available to offset Delmarva's claimed (base rate) revenue requirement, the
17 Company's COSS excludes all non-core rate classes (i.e., allocates costs *only* to the
18 firm sales and transportation classes).

19

20 **Q. Mr. Kalcic, do you agree that it is reasonable to exclude non-core classes from**
21 **the Company's COSS?**

1 A. I do, as long as the approved non-firm margin revenue-sharing mechanism remains
2 in place.

3

4 **Q. Has Delmarva provided any corrections to its filed COSS in this proceeding?**

5 A. Yes, it has. In its response to AG-COS-1, Delmarva corrected an error (related to
6 an incorrect cell reference in its COSS model) in its filed COSS. The class rates of
7 return from Delmarva's filed and corrected COSSs are shown in Table 1 below.

8

9

Table 1

<i>Customer Class</i>	<i>Filed Rate of Return</i>	<i>Corrected Rate of Return</i>
Residential	5.92%	5.80%
General Service	7.41%	7.55%
Medium Volume General	9.79%	10.43%
Large Volume General	3.25%	3.63%
QFCP	-15.92%	-15.92%
Lighting	6.03%	6.96%
Total Company	6.21%	6.21%

10

Source: Delmarva's response to AG-COS-1, Attachment 10.

11

12 **Q. Did Delmarva deem the above differences in its filed versus corrected class**
13 **rates of return significant enough to affect the Company's rate design**
14 **proposals in this case?**

15 A. No.

16

17 **Q. Do you recommend that any changes to the Company's COSS methodology at**
18 **this time?**

1 A. No, I do not.

2

3 **Q. What does Delmarva's corrected COSS indicate with respect to the relative**
4 **contribution toward allocated cost of the Company's firm delivery service**
5 **classes?**

6 A. Table 1 shows that the Medium Volume General, General Service and Lighting
7 classes contribute revenues in excess of their respective cost-based revenue levels at
8 present rates. Conversely, the Residential, Large Volume Service and QFCP
9 classes are under-contributing – the QFCP class remarkably so. Stated differently,
10 the Company's COSS indicates that Residential, Large Volume Service and QFCP
11 customers are being subsidized at present rates.

12

13 **Q. Have you utilized the corrected cost-of-service results shown in Table 1 as a**
14 **guide when preparing Staff's recommended class revenue allocation in this**
15 **proceeding?**

16 A. Yes, I have.

17

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III. CLASS REVENUE ALLOCATION

2 **Q. Mr. Kalcic, how does Delmarva propose to recover its requested delivery**
3 **revenue increase of \$12.174 million from ratepayers?**

4 A. Schedule BK-1 summarizes Delmarva's proposed revenue allocation to the
5 Company's firm delivery service classes. As shown on lines 1-7 of Schedule BK-1,
6 the Company's proposed base revenue increases range from 9.7% (for Rates MVG
7 and MVFT) to 537.9% (for Rate LV-QFCP). The proposed increase to the
8 Company's Residential class is 17.0% (per line 1).

9 Line 7 of Schedule BK-1 shows that the Company's proposed increase of
10 \$12.174 million equates to an overall system average increase in adjusted test year
11 delivery revenues of 17.4%. As such, Rates LVG, LVFT and LV-QFCP would
12 receive delivery revenue increases in excess of the system average under
13 Delmarva's proposed revenue allocation.

14

15 **Q. How did the Company arrive at the proposed class revenue allocation shown in**
16 **Schedule BK-1?**

17 A. With the exception of Rate LV-QFCP, Delmarva used a two-step process to derive
18 its proposed revenue allocation. In Step 1, the Company determined the class
19 revenue adjustments (if any) necessary to move the relative rate of return (RROR)

1 of each class within a predetermined bandwidth of 0.85 to 1.15 (around the
2 Company's proposed system average rate of return of 7.51%).²

3 In Step 2, Delmarva assigned the *residual* increase, i.e., the Company's total
4 requested increase less the overall net increase assigned in Step 1, to all rate classes
5 on uniform percentage basis (across class delivery revenues). Therefore, the *total*
6 increase assigned to a given class is the sum of the class' Step 1 and Step 2
7 increases.

8

9 **Q. Please explain how Delmarva determined its proposed increase to the LV-
10 QFCP class.**

11 A. In the case of Rate LV-QFCP, Delmarva set the LV-QFCP Step 1 increase at the
12 level necessary to move the class to full cost of service (i.e., provide a RROR of
13 1.00).³

14

15 **Q. Mr. Kalcic, why does Delmarva propose to set the LV-QFCP revenue
16 requirement at full cost of service in this proceeding?**

17

² The RROR of a class is calculated by dividing: 1) the class' rate of return, by 2) the system average rate of return. By definition, a class that provides a rate of return equal to the system average will exhibit a RROR of 1.00.

³ Since the proposed LV-QFCP Step 1 increase is designed to establish a cost-based rate, no Step 2 increase is assigned to the class.

1 A. In compliance with the mandates contained in Delaware's Renewable Energy
2 Portfolio Standard Act, Delmarva established service for LV-QFCP customers in
3 May 2012, with the understanding that the initial LV-QFCP rate would be revisited
4 in the Company's next base rate proceeding. **Consistent with the intent of the**
5 **Company's Fuel Cell Provider Application, PSC Docket No. 11-362, the Rate**
6 **LV-QFCP was to be set at full cost of service in the Company's next base rate**
7 **proceeding .**

8 **Q. Have you prepared a recommended class revenue allocation, similar to that**
9 **shown in Schedule BK-1?**

10 A. Yes. Staff's recommended class revenue allocation is shown in Schedule BK-2.

11

12 **Q. How did you determine Staff's recommended revenue allocation shown in**
13 **Schedule BK-2?**

14 A. Mr. Peterson is recommending an overall revenue increase of \$3.584 million, which
15 equates to a system average increase in adjusted test period delivery revenues of
16 5.1%, as shown on line 7 of Schedule BK-2. Staff's individual class revenue
17 increases, shown in lines 1-6 of Schedule BK-2, are designed to move classes closer
18 to cost of service, as measured by the Company's class cost of service study,
19 subject to the condition that: 1) no rate class receive a base rate decrease in this
20 proceeding; and 2) no class, with the exception of Rate LV-QFCP, receive an
21 increase greater than 1.5 (or 150%) of Staff's recommended system average
22 increase.

1

2 **Q. Please explain how you determined Staff's recommended class increases shown**
3 **in column 3 of Schedule BK-2.**

4 A. Staff's recommended class increases were developed via the following steps. First,
5 I set the Rate LV-QFCP increase at the level needed to move the class to full cost of
6 service (i.e., so as to provide a class rate of return equal to Staff's overall
7 recommended rate of return of 7.15%).⁴ Second, I assigned no increase to the
8 MVG class, in recognition of the fact that MVG customers currently provide a
9 present rate of return in excess of 10.0%. Third, I assigned the LVG class a
10 maximum increase of 1.5 times the system average or 7.6%, since LVG customers
11 currently provide the lowest present rate of return of any class on Delmarva's
12 system (excluding Rate LV-QFCP). Fourth, I assigned the Residential class a
13 system average increase, since residential customers provide a present rate of return
14 that is just slightly below the system average. Fifth, I assigned the General Service
15 and Lighting classes the residual increase (i.e., 4.5%) needed to implement Staff's
16 overall recommended revenue requirement.

17

18 **Q. Mr. Kalcic, what are the present and recommended class rates of return that**
19 **result from Staff's recommended revenue allocation?**

20 A. Table 2 below provides a summary of class rates of return at present and Staff
21 recommended revenue levels.

⁴ See Exhibit__(DEP-1), Schedule 1 at line 4.

1

2

Table 2

<i>Customer Class</i>	<i>Present Rate of Return</i>	<i>Recommended Rate of Return</i>
Residential	5.81%	6.74%
General Service	7.57%	8.41%
Medium Volume General	10.45%	10.45%
Large Volume General	3.64%	4.73%
QFCP	-15.96%	7.15%
Lighting	6.97%	8.00%
Total Company	6.23%	7.15%

3

Source: Delmarva's COSS adjusted for Staff's revenue levels.

4

5 **Q. Mr. Kalcic, have you designed a set of rates to implement Staff's recommended**
6 **class revenue allocation shown in Schedule BK-2?**

7 A. Yes, I have. Staff's recommended rate design is discussed in the following section
8 of my testimony.

9

1

IV. STAFF RATE DESIGN

2 **Q. Mr. Kalcic, does Staff recommend any changes to the Company's rate**
3 **structure?**

4 A. With the exception of Rate LV-QFCP (where Staff's recommends implementing a
5 new demand charge), it does not. Staff's recommended rate design and proof of
6 revenue for the Company's firm delivery service classes are shown in Schedule
7 BK-3.

8

9 **Q. Please describe your recommended rate design for the Residential class shown**
10 **on Schedule BK-3, page 1 of 7.**

11 A. Staff assigned an 8.75% increase to the residential customer charge, consistent with
12 the cost-based customer charge increase suggested by Delmarva's COSS. The
13 residual increase of 3.42% (necessary to implement Staff's overall recommended
14 Residential increase) was applied on an across-the-board basis to the Company's
15 existing volumetric charges.

16

17 **Q. Please describe your recommended rate design for Rates GG and GVFT**
18 **shown on Schedule BK-3, page 2 of 7.**

19 A. Staff assigned an overall increase of 6.90% to General Service customer charges,
20 consistent with the overall cost-based customer charge increase suggested by
21 Delmarva's COSS. At the same time, Staff's rate design implements a \$75.00 per

1 month differential in the customer charges applicable to Rate GG and Rate GVFT
2 customers, as proposed by Delmarva.

3 The residual increase of 3.89% (necessary to implement Staff's overall
4 General Service increase) was applied on an across-the-board basis to the
5 Company's existing volumetric charges.

6

7 **Q. Please describe your recommended rate design for Rates MVG and MVFT**
8 **shown on Schedule BK-3, page 3 of 7.**

9 A. Since Staff is recommending no increase to the MVG class, Staff's rate design is
10 limited to implementing the Company's proposed \$75.00 per month differential in
11 the customer charges applicable to Rate MVG and Rate MVFT customers, *on a*
12 *revenue neutral basis*. In other words, Staff's recommended rate design contains no
13 change in Delmarva's existing MVG/MVFT demand or commodity charges.

14

15 **Q. How did you derive Staff's recommended rates for Rates LVG and LVFT**
16 **shown on Schedule BK-3, page 4 of 7?**

17 A. Since the Company's only remaining LVG customer will be migrating to Rate
18 LVFT over the course of this proceeding (and therefore subject to the higher LVFT
19 customer charge), Delmarva proposes to implement an across-the-board increase to
20 all LVG/LVFT tariff charges, so as to mitigate the rate impact experienced by the
21 migrating LVG customer.

1 Staff's recommended rate design mirrors that of the Company. First, I
2 assigned Staff's recommended class increase of 7.59% to the LVFT customer
3 charge. However, since the remaining LVG customer will be subject to the higher
4 LVFT charge of \$1,064.61 per month, the effective increase in LVG/LVFT
5 customer charge *revenue* is slightly higher, i.e., approximately 8.6%. Second, I
6 assigned the (resulting) residual increase of 7.5% to all remaining LVG/LVFT
7 charges.

8

9 **Q. Please describe Staff's recommended rate design for the Gas Lighting class**
10 **shown on Schedule BK-3, page 5 of 7.**

11 A. Since there is only one rate element applicable to lighting customers, I implemented
12 Staff's recommended class increase of 4.5% by assigning that increase to the
13 customer charge.

14

15 **Q. How did you develop Staff's recommended rates for the LVG-QFCP class**
16 **shown on Schedule BK-3, page 6 of 7?**

17 A. At the present time, Rate LVG-QFCP consists solely of a customer charge of
18 \$3,166.67 per month. Like the Company, Staff recommends employing a customer
19 and *demand* charge to recover the LVG-QFCP class' revenue requirement.

20 In particular, Staff's recommended rate design: a) sets the LVG-QFCP
21 customer charge at \$1,064.61 per month (which is the same level as Staff's

1 recommended LVFT customer charge); and b) recovers the balance of the class'
2 revenue requirement in the new demand charge.

3

4 **Q. What is shown on Schedule BK-3, page 7 of 7?**

5 A. Page 7 of Schedule BK-3 contains Staff's recommended rate design for the MVIT
6 and LVIT classes. At the present time, MVIT and LVIT customers pay the
7 corresponding customer charges applicable to MVFT and LVFT customers,
8 respectively. Accordingly, Staff's recommended MVIT and LVIT rate design
9 consists solely of updating Delmarva's current interruptible tariff charges to reflect
10 Staff's recommended MVFT and LVFT customer charges.

11

12 **Q. Mr. Kalcic, are any of the interruptible delivery revenues shown on Schedule**
13 **BK-3, page 7 of 7 applied toward the recovery of Staff's overall recommended**
14 **revenue requirement in this proceeding?**

15 A. No. As previously discussed in Section II, no portion of the margins contributed by
16 interruptible customers is available to offset Delmarva's base rate revenue
17 requirement at this time.

18

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V. PROPOSED TARIFF REVISIONS

2 **Q. Mr. Kalcic, do you have any preliminary comments on the Company's**
3 **proposed tariff revisions?**

4 A. Yes, I do. First, I would note that the primary revisions to the Company's proposed
5 tariff pertain to Delmarva's proposals to: 1) implement a Utility Facility Relocation
6 Rider (Rider UFRC); and 2) modify its existing policy with respect to main
7 extensions. Second, I find that most of the remaining revisions to the Company's
8 tariff are generally non-substantive in nature, except for those related to Delmarva's
9 proposed revisions to penalties for unauthorized (usage) overruns.

10

11 **Q. Which of the above topics (that involve substantive changes to Delmarva's**
12 **tariff) do you wish to address at this time?**

13 A. I will limit my comments to Delmarva's proposal to revise its unauthorized overrun
14 penalties. Staff's recommendations with respect to Delmarva's proposed Rider
15 UFRC and main extension policies are presented in the testimony of Staff witnesses
16 Malika Davis and Michael McGarry, respectively.

17

18 **Q. Mr. Kalcic, what is an "unauthorized overrun"?**

19 A. An unauthorized overrun is defined as any quantity of gas taken for service on any
20 day of the month in excess of 110% of the maximum daily quantity specified in a
21 customer's service contract (i.e., Contract MDQ). Similarly, the associated overrun

1 deliveries are defined as “unauthorized overrun volumes” for the day on which the
2 overrun occurred.

3

4 **Q. To what class(es) do overrun penalties apply?**

5 A. Overrun penalties apply to all rate classes that require a *contract* as a condition of
6 service. Therefore, overrun penalties are applicable to: 1) all sales customers take
7 service under Rates MVG or LVG; and 2) all transportation service customers.

8

9 **Q. Does the Company’s tariff permit “authorized overruns”?**

10 A. Yes. In those instances where a customer has requested and received advance
11 authorization from the Company, that customer may use in excess of 110% of the
12 Contract MDQ without an overrun penalty.⁵

13

14 **Q. Please describe the Company’s proposed changes to its overrun penalties.**

15 A. As shown in Table 3 below, the Company is proposing to increase its unauthorized
16 overrun penalties from \$20.00 to \$50.00 per Mcf during non-Operational Flow
17 Order (OFO) periods, and from \$35.00 to \$60.00 per Mcf during any period in
18 which an OFO is in effect.

19

⁵ Advance notification is required in order for Delmarva to determine whether or not a requested overrun is feasible, i.e., will not cause any operational/system delivery issues.

1

2

Table 3

<i>System Conditions</i>	<i>Current Penalty (\$/Mcf)</i>	<i>Proposed Penalty (\$/Mcf)</i>
No Operational Flow Order	\$20.00	\$50.00
With Operational Flow Order	\$35.00	\$60.00

3

Source: Delmarva's proposed tariff.

4

5 **Q. Why is Delmarva proposing to revise its overrun penalties at this time?**

6 A. In response to PSC-RD-17, Delmarva states that its existing overrun penalties are at
7 the low end of the range of penalties charged by gas utilities in neighboring states.

8 In particular, the Company notes that its existing penalties are much lower than the
9 \$50.00 per Mcf penalty approved for Chesapeake Utilities Corporation

10 (Chesapeake). In order to bring its overrun penalties in line with the "benchmark"
11 penalty levels used by neighboring utilities, Delmarva proposes to adjust its overrun
12 penalties to the levels shown in Table 3.

13

14 **Q. Do you agree with Delmarva's proposed revisions to its overrun penalties?**

15 A. In part. I agree that Delmarva's proposed \$50.00 per Mcf overrun penalty is
16 reasonable, in as much as Chesapeake currently charges that amount for

17 unauthorized overruns in either non-OFO or OFO periods. However, the

18 Company's proposed \$60.00 per Mcf penalty for unauthorized overruns in OFO

19 periods is not supported by the Company's benchmark analysis. In other words,

Direct Testimony of Brian Kalcic

1 none of the gas utilities used in the Company's benchmark analysis charges a
2 penalty for unauthorized overruns in excess of \$50.00 per Mcf.

3

4 **Q. What do you recommend?**

5 A. I recommend that the Commission approve a \$50.00 per Mcf penalty for
6 unauthorized overruns during Delmarva's OFO periods.

7

8 **Q. Does this conclude your direct testimony?**

9 A. Yes.

SCHEDULES BK-1 THROUGH BK-3

APPENDIX

APPENDIX

Qualifications of Brian Kalcic

Mr. Kalcic graduated from Benedictine University with a Bachelor of Arts degree in Economics in December 1974. In May 1977 he received a Master of Arts degree in Economics from Washington University, St. Louis. In addition, he has completed all course requirements at Washington University for a Ph.D. in Economics.

From 1977 to 1982, Mr. Kalcic taught courses in economics at both Washington University and Webster University, including Microeconomic and Macroeconomic Theory, Labor Economics and Public Finance.

During 1980 and 1981, Mr. Kalcic was a consultant to the Equal Employment Opportunity Commission, St. Louis District Office. His responsibilities included data collection and organization, statistical analysis and trial testimony.

From 1982 to 1996, Mr. Kalcic was employed by the firm of Cook, Eisdorfer & Associates, Inc. During that time, he participated in the analysis of electric, gas and water utility rate case filings. His primary responsibilities included cost-of-service and economic analysis, model building, and statistical analysis.

In March 1996, Mr. Kalcic founded Excel Consulting, a consulting practice that offers business and regulatory analysis.

Mr. Kalcic has previously testified before the state regulatory commissions of Delaware, Kansas, Kentucky, Maine, Massachusetts, Minnesota, Missouri, New Jersey, New York, Ohio, Oregon, Pennsylvania, and Texas, and also before the Bonneville Power Administration.