DELMARVA POWER & LIGHT COMPANY
TESTIMONY OF W. MICHAEL VONSTEUBEN
BEFORE THE DELAWARE PUBLIC SERVICE COMMISSION
CONCERNING AN INCREASE IN NATURAL GAS BASE RATES
PSC DOCKET NO. 10 - ___

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1. Q: Please state your name and position, and business address.

A: My name is W. Michael VonSteuben. I am Manager, Revenue Requirements and Regulatory Accounting, in the Regulatory Affairs Department of Pepco Holdings, Inc. (PHI), which is located at P.O. Box 9239, Newark, DE 19714. I am testifying on behalf of Delmarva Power & Light Company (Delmarva or the Company).

2. Q: Please state your educational background and professional qualifications.

A: I received a Bachelor of Science Degree in Business Administration from the University of Delaware in 1976. In December 1978, I joined Delmarva in the Payroll section of the Accounting Department. In 1980, I was promoted into the Plant Accounting Department with responsibility related to the book and tax treatment of the Company's utility plant.

In September 1984, I was promoted to Senior Analyst in the Regulatory Practice Department. I was promoted to Staff Analyst in June 1987 and to Supervisor in March 1998. I was designated a Senior Regulatory Leader in 2000 and promoted to my current position in November 2004. My responsibilities include the coordination of revenue requirement determinations in Delaware, Maryland, New Jersey and the District of Columbia as well as coordinating various other regulatory compliance matters.

3. Q: Have you previously presented testimony before a regulatory body?

A: Yes, I have. I have previously presented testimony numerous times as a witness before the Delaware Public Service Commission (DPSC or the Commission) including the Company's two most recent base rate proceedings, Docket Nos. 06-284 and 09-414/09-276T, as well as presenting testimony before the Maryland Public Service Commission, the New Jersey Board of Public Utilities, the Public Service Commission of the District of Columbia and the Virginia State Corporation Commission.

4. Q: <u>What is the purpose of your testimony?</u>

A: The purpose of my testimony is to present the per-book Earnings and Rate Base for use in this filing along with the quantification and support of certain adjustments. I summarize the adjustments being proposed by all the witnesses as well as the revenue requirement request of the Company. I sponsor certain adjustments which are both described in my testimony and have supporting detail that can be found in Schedules WMV 1 – 16, which accompany this filing. I am also sponsoring certain Minimum Filing Requirements (MFR).

<u>FILING REQUIREMENTS</u>

5. Q: <u>What MFR are you sponsoring?</u>

A: I am sponsoring the following filing requirements:

Schedule 1	Financial Summary
Schedule 2	Rate Base Summary
Schedule 2A	Used and Useful Utility Plant
Schedule 2B	Intangible Assets
Schedule 2C	Accumulated Depreciation & Amortization, and Customer Advances
Schedule 2D	Accumulated Deferred Income Taxes &

	Investment Tax Credit
Schedule 2E	Materials and Supplies
Schedule 2F	Other Elements of Property and CWIP
Schedule 3	Summary of Net Operating Income
Schedule 3A	Revenues
Schedule 3B	Operating Expenses
Schedule 3C	Payroll Costs
Schedule 3E	Sales Promotion and Advertising
Schedule 3F	Contributions
Schedule 3G	Association Dues
Schedule 3H	Rate Case Expense
Schedule 3I	Income Taxes and Provisions
Schedule 3J	Federal and State Income Taxes
Schedule 3K	Deferred Federal and State Income Taxes
Schedule 3L	Investment Tax Credit
Schedule 3M	Other Taxes
Schedule 3O	Other Income
Schedule 5	Revenue Conversion Factor

6. Q: <u>What are the test year and the test periods presented in this filing?</u>

A: The test year is the actual twelve months data ending December 2009. The test period is the six months actual – six months forecast ending June 2010. The test period will be updated to the twelve months of actual information ending June 2010 during the course of this proceeding.

7. Q: <u>Is this a reasonable test period?</u>

A: Yes. The test period, with the adjustments proposed, represents a reasonable basis for establishing the Company's revenue requirements for the rate effective period, the 12 months ending January 2012. With the adjustments presented in this filing, this test period provides a matching of revenues, expenses and rate base consistent with Commission regulations and represents a reasonable basis for establishing the Company's revenue requirements for the rate effective period.

8. Q: <u>Please describe how the Company plans on providing updated Test Period data to the Commission as required by the Minimum Filing Requirements.</u>

A: The test period is the six months actual and six months of forecasted data ending June 30, 2010. The MFR require that three additional months of total Company data be provided 60 days after the quarter closes. While the Company is only required to update that actual total Company data for the period January 2010 through March 2010, the Company will provide a complete updated fully adjusted test period based on all actual data for the twelve months ending June 30, 2010 to the Staff and all parties in September 2010. This will allow the Staff and parties adequate time to perform discovery and complete their analysis.

9. Q: <u>Please describe the development of per books rate base and earnings.</u>

A: The rate base for the test year and test period is comprised of average balances and is summarized on Schedule WMV-1. Earnings for the test year and test period is are also summarized on Schedule WMV-1.

The source of the data for the test year and test period consists of the Company's actual books and records provided by Company Witness Kathleen White. The forecasted data has been similarly assembled and organized to provide the monthly data for the parties in this proceeding. Detail for the test year and test period can be found in the workpapers contained in Book 4 that accompanies the Company's Application.

Earnings include Operating Revenues less Operating Expense and Interest on Customer Deposits plus the Allowance for Funds Used During Construction (AFUDC), as shown on Schedule WMV-1. A number of pre-cost study adjustments have been made to the books to allow the resulting cost of service returns by class to be representative for rate design purposes. As discussed in Company Witness Janocha's testimony, the basis for designing rates was the class returns resulting from the cost of service. The pre-cost study earnings adjustments are detailed in the workpapers contained in Book 4. The following are the pre-cost study adjustments:

- Removal of the effect of the Texas Eastern Transmission Company (TETCO) pipeline;
- Removal of the effect of Environmental Surcharge Revenues and Expenses;
- Maximum Daily Quantity (MDQ) Annualization Adjustment;
- Weather Normalization Adjustment;
- Removal of the effects of Utility Tax;
- Bill Frequency Adjustment;
- Removal of the effect of Unbilled Revenues;
- Removal of the effect of Gas Cost Recovery Fuel Revenues and Expenses;
- Removal of Gas Cost Rate Margin Sharing; and
- Restatement of the Investment Tax Credits and Federal and State Deferred Income Taxes.

The per book rate base is detailed by component on Schedule WMV-1. Additions to rate base are included as they represent investment in facilities used to serve the Company's customers as well as investor-supplied working capital necessary for the Company's day-to-day operations. Certain items are deducted from rate base as they represent funds supplied by customers (or at least not investor-provided). Rate base includes Net Plant, Construction Work in Progress (CWIP), Materials and Supplies and Working Capital, less Accumulated Deferred Income Taxes, Unamortized Investment Tax Credits, Customer Advances and Customer Deposits.

10. Q: Do the Company's proposed rate base and earnings conform to the Commission's last detailed decision, Docket No. 05-304?

A: Yes, although there are two items that differ from the Commission's decision in Docket No. 05-304. The Commission did not include CWIP in rate base but indicated that it was within their discretion in future cases to determine whether CWIP should be included in rate base. I have included CWIP in rate base with the corresponding accrued AFUDC in earnings and I discuss detail related to CWIP later in my testimony.

The Commission also denied the inclusion of incentive compensation payments that are primarily triggered by the achievement of a financial threshold. The Commission did allow the incentives that are triggered by the achievement of safety, reliability and goals of that nature. The Commission's Order also noted that this was a difficult issue for the Commission and they recognized that they have allowed incentive plan payments to be included in rates in the past. I have removed executive incentive compensation in this filing but, as I explain later in my testimony, I am requesting that the Commission include in rates the incentive compensation that includes items such as safety, customer satisfaction and reliability for non-executive employees.

In this case, I have included the 13 month average of CWIP in the Company's rate base claim. Of this $2,556,979 Gas specific CWIP on the Company's book as of December 31, 2009, $1,593,597 has been closed to plant in service as of May 31, 2010. $442,024 of the year-end 2009 total continues to accrue AFUDC and $313,739 is capital accruals recorded in CWIP. Only $207,619 of the Company's $2,556,979 year-end CWIP balance currently does not accrue AFUDC because it is below the $25,000 threshold to accrue AFUDC. I will provide an update during the course of this proceeding of the $963,382 not yet closed to plant. This will support the Company's position that the test period level of CWIP is used and useful and providing value to customers during the rate effective period.

11. Q: <u>Please summarize the Company's overall revenue deficiency.</u>

A: Schedule WMV-2, page 1, provides a listing of each adjustment supported by the Company. Schedule WMV-2, page 2, displays the calculation of the Company's revenue deficiency of $11,915,000. This calculation includes the effect of all of the pro-forma adjustments to the test period level of earnings and rate base and uses Company Witness Hanley's recommended rate of return of 8.10 %.

Proforma Adjustments

12. Q: Please list the pro forma adjustments that you are sponsoring in this proceeding.

A: The pro forma adjustments that I am sponsoring are as follows:

- Adjustment No. 1 - Removal of Employee Association Expense;
- Adjustment No. 2 – Amortization of Regulatory Commission Expense;
- Adjustment No. 3 - Reflect price changes associated with the Company's Wage and FICA Expense;
- Adjustment No. 4 – Removal of Executive Incentive Compensation Expense;
- Adjustment No. 5 – Normalize Non-Executive Non-Safety Incentive Compensation Expense;
- Adjustment No. 6 – Normalize Non-Executive Safety Incentive Compensation Expense;
- Adjustment No. 10 – Benefits Expense Adjustment;
- Adjustment No. 13 – Energy Expert Expense;
- Adjustment No. 14 – Gas Decoupling Customer Education Expense;
- Adjustment No. 15 – Non-Operating Consulting Expense Reclassification;
- Adjustment No. 16 – Test Period Reliability Plant Closings Adjustment;
- Adjustment No. 17 – Proforma Forecasted Reliability Plant Closings from July 2010 to October 2010;
- Adjustment No. 22 – Common Depreciation Expense Reclassification;
- Adjustment No. 25 – Interest on Customer Deposits Adjustment;
- Adjustment No. 28 – Effects of Interest Synchronization; and

- Adjustment No. 29 – Cash Working Capital related to all proforma adjustments.

13. Q: <u>Why are you making these adjustments?</u>

A: These adjustments are being made to establish a level of earnings and rate base representative of the rate effective period as a basis for providing just and reasonable rates. Many of these adjustments reflect previously approved ratemaking treatment by the Commission. Other adjustments have been made to assure that the rate effective period reflects a matching of all elements of the ratemaking formula for known and measurable changes. Workpapers supporting each of these adjustments are included in Book 4 of this filing.

14.Q: <u>Please describe Adjustment No. 1, the Removal of Employee Association Expense.</u>

A: Consistent with the treatment included in Docket Nos. 94-22, 03-127 and 05-304, the amounts charged to expense for support of the Employee's Association were removed for ratemaking purposes. This adjustment is detailed on Schedule WMV-3.

15. Q: <u>Please describe the adjustment made to restate Regulatory Commission Expense, Adjustment No. 2.</u>

A: Consistent with the treatment included in Docket Nos. 94-22, 03-127 and 05-304, the amount expensed in the test period was adjusted for two items. The first is to normalize the test period level of expense using a three-year average. The second item is to adjust the test period level of expense to reflect the cost of this filing, including the costs of Staff and the Division of Public Advocate (DPA), amortized over a three-year period with the unamortized amount of these costs being included as a rate base item. Also included is an estimated amount of $ 50,000 related to DPA now being able to charge the Company for certain regulatory activities. This adjustment results in a $175,245 decrease to test year operating income and is detailed on Schedule WMV-4.

16. Q: <u>Please describe Adjustment No. 3, the adjustment made to reflect the Company's Proposed Wage and FICA expense.</u>

A: Consistent with the treatment included in Docket Nos. 94-22, 03-127 and 05-304, the Company's test period wage and FICA levels of expense were adjusted for the known price changes required to be made to be reflective of the rate effective period. These include:

- the actual non-union wage increase of 3.09% effective March 2010 for 8 months,
- an estimated wage increase of 1.50% for IBEW Local 1238 effective in February 2010 for 7 months,
- an estimated wage increase of 1.50% for IBEW Local 1307 effective in June 2010 for 12 months,
- an estimated non-union wage increase of 3.00% effective March 2011 for 11 months,
- an estimated wage increase of 1.50% for IBEW Local 1238 effective in February 2011 for 12 months, and
- an estimated wage increase of 1.50% for IBEW Local 1307 effective in June 2011 for 7 months.

These wage increases have been applied to the Company's test period salaries and wages to be reflective of the rate effective period, February 2011 through January 2012. Updates to estimated information will be provided during the course of the proceeding. This adjustment is detailed on Schedule WMV-5.

17. Q: <u>Please describe Adjustment No. 4, which is the adjustment to Remove Executive Incentive Compensation expense.</u>

A: This adjustment removes the test period level of expense associated with executive incentives. As described in Company Witness Jenkins's testimony, these "compensation at risk" payments are an important component of the Company's total executive compensation, and are likely to continue to be so in the future. I am excluding such amounts in light of the current economic environment. As displayed on Schedule WMV-6, the Company is removing $277,198 of test period O&M expense related to executive incentive compensation in this adjustment.

18. Q: <u>Please describe Adjustments No. 5 and No. 6 which provide for the Normalization of Non-Executive Non-Safety and Non-Executive Safety Incentive Compensation Expense.</u>

A: As Company Witness Jenkins describes in his testimony, motivated employees look out for the safety of themselves and the public, serve the needs and expectations of satisfied customers, and do so in a financially responsible way. These incentives motivate employees to work safely, promote efficiency and focus on critical processes such as diversity, reliability and our customers' needs.

For these reasons, I have normalized the non-executive incentive safety expense using a three year average. This treatment follows that recently approved by the Maryland Public Service Commission in Case 9192. Adjustment No. 5, which is detailed on Schedule WMV-7, adjusts the test period level of non-executive non-safety incentive expense of $527,680 to the three-year average of $849,498, or an increase of $321,818 in O&M expense.

Similarly, Adjustment No. 6, which is also detailed on Schedule WMV-7, adjusts the test period level of non-executive safety incentive expense of $123,652 to the three-year average of $85,548, or a decrease of $38,104 in O&M expense.

19. Q: <u>Please describe Adjustment No. 10, which is the adjustment made to reflect price changes related to the Company's employee medical, dental and vision benefits program.</u>

A: I have included an adjustment for increased employee benefit expenses that decreases test year operating income by $180,522 as calculated on Schedule WMV-8. This adjustment reflects increased expense related to medical, dental and vision plan expenses provided by the Company for its active employee population. This adjustment to test period operation and maintenance expense reflects an increase in medical expense by 8%, and dental and vision expense by 5% that Company Witness Jenkins supports in his testimony. Based on the work of the Company's benefit consultant, Lake Consulting, Inc., I have adjusted the test period level of expense to reflect the projected change to medical, dental and vision costs to reflect the level of expense for the rate effective period. A similar benefit adjustment was filed in the Company's last Gas base rate case, Docket No. 06-284.

20. Q: <u>Please describe Adjustment No. 13, the adjustment made to proform Energy Expert Costs.</u>

A: As included in the Company's filing in Docket No. 09-414, the Company has hired 13 additional employees to coach and educate our customers on energy use and to help our customers reduce their bills. These employees constitute the Energy Advisor team handles more advanced inquiries, including helping customers to use the available self service options, learn more about programs being offered, understand their energy usage via ‘My Account’, and by providing energy usage analyses utilizing AMI-sourced data. Additional information about weatherization options and energy efficient appliances can also be provided, although all information will be generic such that no specific manufacturers would be recommended. Due to the length and complexity of these calls, this inquiry type should not be subject to telephone service level target.

While access to this group of experts would not be restricted by user class, we would expect the Energy Specialist Team to be able to address the needs of small to mid-sized commercial customers whose needs are often more complex than residential customers, but lack the resources that large commercial customers may have.

The intent of this expanded effort will be to supplement other resources available to customers, rather than to compete with them. Customers already have the opportunity to call energy services companies for specific services, including energy audits. The Delaware Energy Office, and that Agency’s Sustainable Energy Utility, provides energy audits, renewable rebates and incentives, and energy information. The Delmarva team would supplement these resources available to customers, and if appropriate, refer customers to these resources. Customer visits on-site would be within the scope of the team’s mission, but full scale on-site energy audits would be outside the Company’s scope. The Commission’s Staff recommended acceptance of this adjustment in Docket No. 09-414 for the Delaware Electric allocated portion of this expense. This adjustment is detailed on Schedule WMV-9.

21. Q: <u>Please describe Adjustment No. 14, which is the adjustment to reflect the expense associated with Gas Decoupling Customer Education expense.</u>

A: As displayed on Schedule WMV-10, this adjustment reflects the additional expense of related to the expense of $106,500 related to Company's customer education program associated with the decoupling program. A comprehensive gas decoupling customer education program will be an important deliverable which will go a long way to help customers understand the new rate design and how it will impact them going forward. The need for a decoupling customer education program has been discussed in Docket No. 09-227T, and a program is being designed and will be rolled out coincident with implementation of the rate design.

22. Q: Please describe Adjustment No. 15, which is the adjustment to remove test period expense associated with a non-Gas related consulting cost.

A: I have included an adjustment to remove $306,901 of expense related to a consulting fee related to an electric tax issue that was recorded during the test period. This adjustment is detailed on Schedule WMV-11.

23. Q: Please explain the adjustment made for the Test Period Reliability Plant Closings, Adjustment No. 16

A: As approved by the Commission in Docket No. 05-304, this adjustment reflects the annualization of reliability plant investment added during the test period. This adjustment also reflects the removal of the associated test period level of CWIP and AFUDC and also reflects the annualization of any retirements to plant that occurred during this period. This adjustment is detailed on Schedule WMV-12.

24. Q: Please describe Adjustment No. 17, the adjustment made to proform Forecasted Reliability Plant Closings, from July 2010 to October 2010.

A: As approved by the Commission in Docket No. 05-304, this adjustment reflects the annualization of reliability plant added to plant for four months past the end of the test period, July 2010 through October 2010. This adjustment also reflects the annualization of any retirements to plant that occurred during this period and is detailed on Schedule WMV-13.

25. Q: Should the Commission acknowledge this Reliability Plant Adjustment in its determination of the Company's revenue requirements?

A: Yes. The inclusion of this item is known and measurable and is precisely the type of adjustment that the Commission should continue to include in its determination of the revenue requirement. The actual reliability plant additions should be included in rate base to properly recognize the value that customers are currently realizing and will realize during the rate effective period.

26. Q: Please discuss the Common Depreciation Expense Reclassification Adjustment No. 22.

A: The Company is removing an out-of-period adjustment included in its test period related to common gas depreciation expense. In December 2009, a reclassification entry was made to correct the amount of common plant depreciation expense related to electric and gas. An adjustment of $965,955 was made between gas and electric for common depreciation for the entire year of 2009 as shown on Schedule WMV-14. The adjustment lowered the 2009 common depreciation expense related to gas. To properly reflect only the amount related to the 6 months of test period information of July through December 2009, the Company has removed $482,766 of depreciation expense associated with January 2009 through June 2009 as an out-of-period adjustment in this case.

27. Q: Please describe the adjustment made to restate Interest on Customer Deposits (IOCD), Adjustment No. 25.

A: This adjustment provides for recalculating the test period level of IOCD expense using the currently effective IOCD rate of 0.36% and is shown on Schedule WMV-15. I have applied this currently effective interest rate to the Customer Deposit Balance as of the end of the test period to determine an appropriate level of interest expense on customer deposits to be reflected in rates.

28. Q: Describe the Interest Synchronization Adjustment that you support in this proceeding, Adjustment No. 28.

A: This adjustment, shown on Schedule WMV-16, synchronizes the interest expense utilized in the per books income tax calculation with the adjusted rate base and the tax deductible component included in the cost of capital.

29. Q: Describe Adjustment No. 29, the Cash Working Capital Adjustment.

A: This adjustment reflects the inclusion of the calculated cash working capital effect of all earning adjustments using the ratios supported in the testimony of Company Witness Timothy J. White. This adjustment is detailed on Schedule WMV-16.

Revenue Requirement

30. Q: Can you summarize the adjustments that are included in this filing?

A: Yes, I can. Schedule WMV-1 displays all of the proforma adjustments included in this filing and the earnings and rate base impact.

31. Q: Please summarize the Company's overall revenue deficiency.

A: Schedule WMV-2 displays the calculation of the Company's revenue deficiency of $11,915,000. This calculation includes the effect of all of the proforma adjustments to the test period level of earnings and rate base and uses Company Witness Hanley's supplied rate of return of 8.10 %.

32. Q: Does this conclude your testimony?

A: Yes, it does.