**ORDER NO. 92541**

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| Washington Gas Light Company's Application for Authority to Increase Rates and Charges for Natural Gas Services | * * * * * * | BEFORE THE PUBLIC SERVICE COMMISSION OF MARYLAND<br>Case No. 9849 |

ORDER ON APPLICATION TO INCREASE RATES AND CHARGES FOR NATURAL GAS SERVICES

Before: Kumar P. Barve, Chair, Chair
Frederick H. Hoover, Jr., Commissioner
Bonnie A. Suchman, Commissioner
Odogwu Obi Linton, Commissioner
Ryan L. "Chuck" McLean, Commissioner

Issued: July 27, 2026

APPEARANCES

Spencer Nichols, Regina Speed-Bost, Megan Roberts-Satinsky, Vishwa B. Link, Katherine C. Creef, Charlotte A. Mitchell, and Kristin M. Athens for Washington Gas Light Company

Kenneth Albert, Jennifer Purvis, and Richard S. Gratz for Technical Staff of the Public Service Commission of Maryland

Juliana Bell, Ryan Hsu, Diamond Hawkins, and Portia Oduro for the Maryland Office of People's Counsel

Frann G. Francis, Erin B. McAuliffe, and Joshua M. Greenberg for the Apartment & Office Building Association of Metropolitan Washington

David Shapiro, Michele Honick, Steven Talson, and Sondra Simpson McLemore for Maryland Energy Administration

Diane Kilcoyne for Montgomery County, Maryland

Susan Stevens Miller, Timothy R. Oberleiton, and Kevin Breiner for Chesapeake Climate Action Network

Richard Owen Hughes for The U.S. General Services Administration

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## I. EXECUTIVE SUMMARY

Washington Gas Light Company ("WGL," "Washington Gas," or "the Company") is a regulated domestic corporation that provides natural gas retail sales and delivery service to Maryland customers in Calvert, Charles, Frederick, Montgomery, Prince George's, and St. Mary's Counties. On December 29, 2025, the Company filed an application pursuant to *Annotated Code of Maryland*, Public Utilities Article ("PUA") §§ 4-203 and 4-204, seeking authority for an $82.5 million increase in annual base rate revenues,[1] and to make certain other changes to its terms and conditions of service.[2]

The Commission has reviewed the evidence and testimony presented, including the comments received at the public hearings, in reaching the decisions in this Order. Based on the record, the Commission has determined that a total revenue increase of $38,134,000, reflecting an adjusted rate base of $1,645,079 thousand and an adjusted operating income of $92,031 thousand, with an overall rate of return ("ROR") of 7.22% based on return on equity ("ROE") of 9.40% is warranted. The residential customer gas usage bill impacts—as shown in Table 11 herein—reflects a $4.01 increase per month for average residential heating customers.

[1] On rebuttal the Company indicated that certain corrections were made such that the requested revenue should have been approximately $88.1 million (*see* Nguyen Rebuttal at Exhibit PTN-1 at 2). Company witness Fang indicated the Company was not seeking the additional revenue (*see* Fang Rebuttal at 4-5).

[2] Notice of the Commission's Pre-Hearing Conference was published by Washington Gas in various newspapers in Montgomery, Prince George's, Southern Maryland, Anne Arundel, Howard and Frederick Counties from January 2, 2026 through January 13, 2026 as noted in WGL's Certificate of Publication, which was filed with the Commission on January 23, 2026 (Maillog No. 326501).

## II. BACKGROUND

On December 29, 2025, Washington Gas filed an Application for Authority to Increase its Existing Rates and Charges and to Revise its Terms and Conditions for Gas Service ("Application") with the Commission in accordance with §§ 4-203 and 4-204 of the PUA and in accordance with Code of Maryland Regulations ("COMAR") 20.07.04.07, seeking to increase its rates and charges for the retail distribution of natural gas in its Maryland service territory.[3] The Application's proposed rates and charges would increase the Company's Maryland annual base rate revenues by $82.5 million; however, this included $15.4 million of revenue requirements associated with the Company's Strategic Infrastructure Development and Enhancement ("STRIDE") Plan, for a net increase in revenues of $67.1 million.[4] The Application is based on a test year consisting of the twelve months ended September 30, 2025, comprising twelve (12) months of actual information. The Company presents the test year as *normalized, annualized, and adjusted* for known and measurable changes to reflect conditions expected to prevail during the rate effective period.[5]

WGL noted several factors that have contributed to its request for an increase in base rates, including the growth in rate base (including the transfer of STRIDE related revenue requirements to base rates, which accounts for $15.4 million of the proposed total revenue increase), employee-related costs, depreciation, and an increased cost of capital,

[3] Maillog No. 325684. Application of Washington Gas Light Company (December 29, 2025).
[4] Application at 1-2. As previously summarized, the Company on rebuttal indicated that certain corrections were made such that the requested revenue should have been approximately $88.1 million (*see* Nguyen Rebuttal at Exhibit PTN-1 at 2). Company witness Fang indicated the Company was not seeking the additional revenue (*see* Fang Rebuttal at 4-5).
[5] *Id*. at 3.

all of which have led to what the Company considers to be inadequate current rates.[6] Washington Gas further claimed that its overall ROR for the test year on a *pro forma* basis will be 4.66%, which is below the overall ROR of 7.04% approved by the Commission in Case No. 9704, Order No. 90943, as well as below the return necessary for the Company to attract capital on reasonable terms.[7] In its Application, Washington Gas requests the Commission's approval to earn an overall ROR of 8.07% and an ROE of 10.85%.[8]

Several parties filed written testimony in this proceeding. Unless otherwise noted, direct testimony was filed on March 31, 2026,[9] rebuttal testimony was filed on April 28, 2026,[10] and surrebuttal testimony was filed on May 13, 2026.[11]

Washington Gas filed Direct[12] and Rebuttal[13] Testimonies sponsored by Donald "Blue" Jenkins, President, Washington Gas, providing an overview of the need for additional revenue and expected cost to the customers as well as an introduction to the Company's witnesses and the issues addressed by each (WGL Direct and Rebuttal, Jenkins): Kevin Murphy, Vice President, Asset Management, Engineering & Supply,

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[6] *Id*. at 3.
[7] *Id*. at 3-4.
[8] *Id*.
[9] Direct Testimony of MEA (Maillog No. 328518), CCAN (Maillog No. 328531), OPC (Maillog Nos. 328533 and 328534), AOBA (Maillog No. 328520), and Staff (Maillog No. 328543). OPC filed an errata to their direct testimony on April 6, 2026 (Maillog No. 328765). WGL filed an errata to their direct testimony on May 14, 2026 (Maillog No. 330128)
[10] Rebuttal Testimony of WGL (Maillog No. 329502). WGL filed an errata to their rebuttal testimony on May 14, 2026 (Maillog No. 330105) and an errata to their rebuttal exhibit on May 19, 2026 (Maillog No. 330286).
[11] Surrebuttal Testimony of MEA (Maillog No. 330065), OPC (Maillog No. 330071), AOBA (Maillog No. 330068), and Staff (Maillog No. 330072). CCAN wrote a letter in lieu of surrebuttal testimony (Maillog No. 330070). Staff filed an errata to their surrebuttal testimony on May 17, 2026 (Maillog No. 330205) and on May 19, 2026 (Maillog No. 330272).
[12] WGL Application for Authority to Increase Rates and Charges for Natural Gas Services. Case No. 9849 (Public and Confidential) (Maillog No. 325684). WGL Errata to Direct Testimony. Case No. 9849 (Maillog No. 330128).
[13] WGL Rebuttal Testimony. Case No. 9849 (Public and Confidential) (Maillog No. 329502).

supporting the reasonableness and prudence of the Company's capital investments, inclusive of its STRIDE Projects and the Company's operation and maintenance ("O&M") expenses (WGL Direct and Rebuttal, Murphy); Andrew Lawson, Director of Regulatory Affairs, addressing affordability of the Company's service and Lost and Unaccounted for Gas ("UFG") (WGL Direct and Rebuttal, Lawson); Phuong T. Nguyen, Manager of Regulatory Accounting, addressing Revenue Requirement and the Per Book Jurisdictional Cost of Service Study ("PBJCOSS" or "JCOSS") (WGL Direct and Rebuttal, Nguyen); Katina L. Banks, Manager of Utility Revenue Accounting, regarding the Company's test year revenue Adjustments 1 through 5 (WGL Direct and Rebuttal, Banks); Mark Shaver, Chief of Staff and Vice President, Strategic Priorities, addressing the Short-Term Incentive ("STI") expense by explaining the Company's STI Scorecard and how it reflects categories, metrics, and weightings that incentivize all Company employees to help the Company achieve its overarching strategic objective of delivering safe, reliable, and affordable energy for the benefit of customers (WGL Direct and Rebuttal, Shaver); Janet Burrows, Vice President and Treasurer of AltaGas Ltd., regarding the Company's proposed capital structure, financing strategy, credit quality, cost of capital, and access to capital markets (WGL Direct and Rebuttal, Burrows); Joshua C. Nowak, Vice President, Concentric Energy Advisors, Inc., addressing the appropriate ROE for Washington Gas in Maryland (WGL Direct and Rebuttal, Nowak); Kimberly Bell, Senior Manager of Tax Technology, Special Projects and Systems, Regulatory Liaison, describing the Company's proposed tax-related adjustments as appropriate (WGL Direct and Rebuttal, Bell); Mark Kelly, Partner, PricewaterhouseCoopers LLP (PwC), describing the policy support for the Company's net operating loss carry forward deferred tax asset ("NOLC-DTA") adjustment

(WGL Direct and Rebuttal, Kelly); Ghislaine Quenum, Manager, Corporate Accounting, discussing shared services between Washington Gas and its affiliates, specifically outbound services provided by the Company to its affiliates (WGL Direct and Rebuttal, Quenum); Ned W. Allis, Depreciation Consultant (Gannett Fleming Valuation and Rate Consultants, LLC), regarding the depreciation rates as reflected in its Depreciation Study (WGL Direct and Rebuttal, Allis); Paul H. Raab, Independent Economic Consultant, regarding the Company's development of its weather normalized throughput/billing determinants and estimates of weather normalized test year volumes (WGL Direct and Rebuttal, Raab); Cyndee Fang, Director, Atrium Economics, LLC, presenting the Company's class cost of service studies ("CCOSS"), revenue apportionment, and proposed rate designs (WGL Direct and Rebuttal, Fang); and Marc Simone, Senior Vice President, Capital Delivery, regarding the Company's proposed Contract Generation Services ("CGS") tariff (WGL Direct and Rebuttal, Simone).[14]

The Commission's Technical Staff ("Staff") sponsored the Direct[15] and Surrebuttal[16] Testimonies of James Garren, Senior Manager of the Firm NewGen Strategies and Solutions LLC, addressing the depreciation parameters and depreciation expenses for WGL's Maryland assigned plant and WGL's Maryland allocated plant (Staff Direct Testimony and Surrebuttal, Garren); Alden Manka, Regulatory Economist in the Telecommunications, Gas, and Water Division at the Commission, regarding the ROE and capital structure testimony provided by witnesses Nowak and Burrows on behalf of WGL

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[14] WGL Rebuttal Testimony. Case No. 9849 (Public and Confidential) (Maillog No. 329502).
[15] Staff Direct Testimony. (Public and Confidential) Case No. 9849 (Maillog No. 328543).
[16] Staff Surrebuttal Testimony. (Public and Confidential) Case No. 9849 (Maillog No. 330072). Errata to Staff Surrebuttal Testimony and Staff Surrebuttal exhibit, Case No. 9849 (Maillog Nos. 330205 and 330272).

(Staff Direct Testimony and Surrebuttal, Manka); Drew McAuliffe, Director of the Commission's Electricity Division, discussing the CGS rate schedule testimony (Staff Direct Testimony and Surrebuttal, McAuliffe); Negussie Tesfaye, Pipeline Safety Engineer, commenting on WGL's current STRIDE Plan, non-STRIDE capital expenditures, activities related to O&M, and safety related conditions in this proceeding (Staff Direct Testimony and Surrebuttal, Tesfaye); Lillian Tiska, Regulatory Economist, addressing WGL's CCOSS (Staff Direct Testimony and Surrebuttal, Tiska); Kamren Walton, Regulatory Economist, providing an analysis of WGL's rate design (Staff Direct Testimony and Surrebuttal, Walton); and David Valcarenghi, Assistant Director of the Accounting Investigations Division, responding to the proposed revenue requirement (Staff Direct Testimony and Surrebuttal, Valcarenghi).

The Office of People's Counsel ("OPC") sponsored the Direct and Surrebuttal Testimonies of: David J. Garrett, a consultant specializing in public utility regulation, addressing proposed depreciation rates from the 2025 Depreciation Study (OPC Direct Testimony and Surrebuttal, Garrett); Justin Brant, Senior Manager at Current Energy Group, analyzing the CCOSS, cost allocation, and rate design proposals in this proceeding (OPC Direct Testimony and Surrebuttal, Brant); Albert Lin, economic and financial consultant for the OG Finance Lab, providing assistance in determining an appropriate ROE (OPC Direct Testimony and Surrebuttal, Lin); James A. Leyko, Senior Consultant of Brubaker & Associates, Inc., energy economic and regulatory consultants, addressing the revenue deficiency that WGL claims in its Application (OPC Direct Testimony and Surrebuttal, Leyko); and Asa S. Hopkins, Senior Vice President for Consulting at Synapse Energy Economics, Inc, reviewing WGL's proposed additions to gas plant in service, with particular emphasis on WGL's replacement activities conducted under the rubric of the STRIDE program (OPC Direct Testimony and Surrebuttal, Hopkins).[17]

Maryland Energy Administration ("MEA") sponsored the Direct and Surrebuttal testimony of Steven Kihm, regulatory finance consultant, supporting his recommended ROE of 9.0% for WGL's regulated utility operations in Maryland (MEA Direct Testimony and Surrebuttal, Kihm); and Joyce Lombardi, Energy Policy Manager at MEA, addressing policy issues raised by the Application (MEA Direct Testimony and Surrebuttal, Lombardi).[18]

The Apartment and Office Building Association of Metropolitan Washington ("AOBA") sponsored the Direct and Surrebuttal testimonies of Bruce R. Oliver, Chief Executive Officer, Chief Financial Officer, and Chairman of the firm of Revilo Hill Associates, Inc., discussing WGL's requested rate increase, CCOSS, and rate design (AOBA Direct Testimony and Surrebuttal, B. Oliver), and Timothy Oliver, President, Chief of Operations, and Director of New Business at Revilo Hill Associates, Inc., discussing WGL's capital structure, cost of capital, ROR, and ROE (AOBA Direct Testimony and Surrebuttal, T. Oliver).[19]

Chesapeake Climate Action Network ("CCAN") filed Petitions to Intervene in this matter but did not submit written testimony. CCAN filed letters in lieu of direct, rebuttal, and surrebuttal testimony.[20]

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[17] Maillog Nos. 328533, 328534, and 330072. OPC also filed an errata to their direct testimony on April 6, 2026 (Maillog No. 328765).
[18] Maillog No. 328518 and 330065.
[19] Maillog Nos. 328520 and 330068.
[20] Maillog Nos. 328531, 329498, and 330070.

The United States General Services Administration ("GSA") Maryland filed a Petition to Intervene in this matter but did not submit written testimony.

Montgomery County, Maryland ("Montgomery County") filed a Petition to Intervene in this matter but did not submit written testimony. Montgomery County filed a letter in lieu of rebuttal testimony.[21]

The Commission conducted virtual public hearings the evenings of March 24, 2026 and April 7, 2026, at which members of the public spoke to their respective positions on WGL's Application.

On May 21, 2026, Staff filed a Comparison of Revenue Requirement Positions by Party Chart reflecting the positions of the parties with regard to the Company's alleged revenue deficiency.[22] On May 22, 2026, Staff filed a Revised Comparison of Revenue Requirement Positions by Party Chart ("Comparison Chart").[23] The Comparison Chart reflects WGL's purported revenue deficiency of $88.1 million. Staff's final position reflects a revenue deficiency of $48.4 million, and AOBA's final position reflects a revenue deficiency of $14.3 million. OPC's final position reflects a $1.8 million surplus.

The Commission conducted evidentiary hearings on the Application on May 18, 2026, May 19, 2026, and May 20, 2026. On June 22, 2026, Initial Briefs were filed by

[21] Maillog No. 330194.
[22] Maillog No. 330355.
[23] Maillog No. 330378.

Washington Gas,[24] Staff,[25] OPC,[26] AOBA,[27] MEA, [28]and CCAN.[29] Montgomery County filed Post-Hearing Comments in lieu of a brief.[30]

On July 2, 2026, Reply Briefs were filed by Staff,[31] Washington Gas,[32] MEA,[33] AOBA,[34] CCAN[35] and OPC.[36]

## III. DISCUSSION AND FINDINGS

Pursuant to PUA § 4-203, a public service company may not change its rates or establish new rates unless authorized to do so by the Commission. In accordance with PUA § 4-201, a public service shall charge "just and reasonable" rates for the regulated services that it provides. A "just and reasonable rate" is defined as a rate that (1) does not violate the Public Utilities Article, (2) fully considers and is consistent with the public good, and (3) will result in an operating income to the public utility that yields, after reasonable deduction for depreciation and other necessary and proper expenses and reserves, a reasonable return on the fair value of the public service company's property "used and useful" in providing service to the public.

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[24] Maillog No. 331359.
[25] Maillog No. 331373.
[26] Maillog No. 331368.
[27] Maillog No. 331365.
[28] Maillog No. 331358.
[29] Maillog No. 331364.
[30] Maillog No. 331360.
[31] Maillog No. 331773.
[32] Maillog No. 331752. Washington Gas filed an errata to their reply brief on July 8, 2026 (Maillog No. 331886).
[33] Maillog No. 331759.
[34] Maillog No. 331746.
[35] Maillog No. 331760.
[36] Maillog No. 331769.

In a proceeding involving a temporary or permanent new rate, or a temporary or permanent change in rate, the burden of proof is on the proponent of the new rate or change in rate.[37] In rate proceedings, in meeting its burden of proof, the applicant must show by a preponderance of the evidence that the criteria in PUA § 4-201 are satisfied and that the proposed rates are just and reasonable. Additionally, as it relates to infrastructure investments, recently adopted PUA § 4-214 requires utility companies to demonstrate:

> (1) the customer benefits of the investment;
> (2) that the company analyzed cost-effective options available to defer reduce, or eliminate the need to replace, upgrade, or construct new components, including an analysis of:
> (i) for new investments unrelated to safety, nonpipeline alternatives; and
> (ii) leak detection and repair; and
> (3) the estimated risk reduction associated with a safety-related investment, if applicable.[38]

### A. Adjustments to Rate Base and Operating Income

Rate base represents the investments a utility makes in plant and equipment to provide safe and reliable utility service to its customers. Operating income is derived based upon the revenues the utility receives for utility service less the cost it incurs in providing service to customers. In its Application, Washington Gas put forth 41 adjustments proposing to make the test year representative of the rate year, *i.e.*, the 12 months ending September 30, 2025.[39] The parties proposed various modifications to WGL's unadjusted rate base and operating income. The Commission has reviewed the record and accepts the

[37] PUA § 3-112(b).
[38] PUA § 4-214(c).
[39] Nguyen Direct at 7.

uncontested rate base adjustments and operating income adjustments, and resolves the disputed adjustments as discussed below.

Briefly stated, the Commission finds based on the evidence in this case: (1) Washington Gas failed to justify the $88.1million revenue increase requested in its Application, and (2) at this time the Commission finds that a revenue increase in the amount of $38,134,000, with a 9.40% ROE and an overall 7.22% ROR reflecting WGL's appropriate cost of capital is just and reasonable and supported by the record.

As noted above, while Washington Gas only requested a revenue requirement of $82.5 million, the Company on rebuttal updated its adjusted rate base to $1,673.1 million and net operating income to $73.5 million which would justify a revenue requirement of $88.1 million.[40] It was this adjusted rate base and net operating income Staff and OPC relied upon to make adjustments.

1. <u>WGL Distribution Investment</u>

<u>WGL</u>

The Company is requesting approval of a total of $342.9 million in capital investment projects inclusive of STRIDE and Non-STRIDE projects.[41] WGL witness Kevin Murphy argued that these investments "are used and useful both in providing natural gas service to customers directly (*e.g.*, piping, valves, meters, regulators, and other appurtenances), as well as to support the gas distribution business (*e.g.*, fleet facilities, information technology, *etc.*).[42] WGL presented the chart below showing the Company's

[40] Nguyen Rebuttal Exhibit PTN-1.
[41] WGL Initial Brief at 30.
[42] Murphy Direct at 4-5.

Gas Plant In Service ("GPIS") by category and the total dollar amount of investment. The Company represented that the capital projects were all placed into service between January 1, 2023 and September 30, 2025.[43]

*Table 1:*
*GPIS by Category*[44]

| Class | Category | Functional Class | GPIS ($ Million) |
|---|---|---|---|
| Accelerated Pipe Replacement | STRIDE | Distribution | $139.0 |
| | | Transmission | $4.2 |
| System Betterment | Safety/Compliance/ Reliability | Distribution | $70.9 |
| | | Transmission | $46.0 |
| | | Storage | $1.3 |
| | IT Software | Intangible | $17.3 |
| | OT*/Communication Equipment | General Plant | $15.0 |
| | Fleet/Facilities/IT** Hardware/Tools/Misc. Equip. | | $9.4 |
| Customer | New Business | Distribution | $39.6 |
| | | Transmission | $0.2 |
| | TOTAL | | $342.9 |

Table 1 shows that the projects associated with the Company's pipeline replacement program (*i.e.* STRIDE) represents a total of $143 million (41.7%) of the total capital investment, System Betterment represents a total of $160 million (46.6%), and New Business represents a total of $40 million (11.7%).[45] Concerning the STRIDE transfer, WGL witness Preston testified that the Company has been collecting STRIDE-related revenues through the STRIDE surcharge and proposes in this proceeding to transfer certain

[43] WGL Initial Brief at 30.
[44] Murphy Rebuttal at 4 showing the amended chart.
[45] *Id*.

in-service STRIDE projects, which totals approximately $15,415,201 related to these STRIDE projects to base rates.[46]

*A. Overview of the Company's System*

Providing an overview of the Company's distribution system, WGL witness Murphy testified that WGL has owned and operated a natural gas distribution system and has furnished natural gas retail service in the National Capital Region since 1848.[47] The Company receives natural gas from interstate transmission pipelines at various delivery points (or "gate stations") on its system and transports it through the Company's pipeline network to end-use customers, adding odorant and reducing pressure as necessary for safety along the way. WGL's pipeline is an interconnected system across three jurisdictions (Maryland, Virginia and the District of Columbia) consisting of transmission pipelines, high-, medium- and low-pressure distribution mains, related services and other facilities needed to provide safe and reliable gas service to the Company's customers in accordance with all applicable federal, state and local laws and regulations.[48]

As of September 30, 2025, Washington Gas serves approximately 518,000 residential, commercial, and industrial customers in Maryland (Calvert, Charles, Frederick, Montgomery, Prince George's, and Saint Mary's Counties).[49] Mr. Murphy noted that approximately 35% of the Company's transmission assets and distribution mains in Maryland are more than 50 years old. Further, he noted that the Company's peak-shaving facilities were originally constructed more than 60 years ago, and contended that while age

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[46] Preston Direct at 4.
[47] Murphy Direct at 7.
[48] *Id*. at 8.
[49] *Id*.

does not necessarily correlate directly to condition, it offers important context to understand the Company's capital planning and system management.[50]

### *B. WGL's Capital System Planning*

WGL witness Murphy described the Company's approach to capital and system planning as "a structured, iterative process that ensures system integrity, public safety, and cost-effective investment while aligning with federal and state compliance obligations and policies for gas pipeline operators."[51] He claimed that the capital system planning process supports the projects that the Company is requesting to move into rates.[52] Mr. Murphy also indicated that the Company's capital system planning process implements a proactive Distribution Integrity Management Program ("DIMP") and DIMP Plan required by PHMSA "to enhance safety by identifying and reducing pipeline integrity risks."[53]

Mr. Murphy testified that, for the distribution projects addressed in this proceeding, "the Company's DIMP Plan together with a probabilistic risk model (specifically, the JANA Lighthouse ("JANA") model beginning in 2023, and before that, Optimain) were relied upon to prioritize assets for replacement."[54] He noted that beginning in 2020, PHMSA identified the use of a probabilistic risk model as a best practice to evaluate the likelihood of an individual pipe segment failing, the scenarios that may occur due to a failure (*e.g.*, a Grade 1, 2, or 3 leak), and the potential consequences associated with those scenarios (health and safety implications, property damage, repair costs, and others).

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[50] *Id*. at 8-9.
[51] *Id*. at 10.
[52] *Id*. at 13.
[53] *Id*. at 14, referring to the U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration ("PHMSA.")
[54] Murphy Direct at 14.

Results from the JANA risk model, combined with non-specific per unit cost estimates, allow the Company to prioritize assets as candidates for replacement by using a 'risk reduced per dollar spent' metric during its risk mitigation planning."[55] He further asserted that ranking alternatives using this model maximizes the effectiveness of the dollars spent on projects to deliver the most benefit to customers and that the Company intends to expand the use of JANA to the extent possible to include this type of risk analysis for all assets.[56]

Mr. Murphy outlined all of the key considerations and components involved in the Company's capital system planning process including its alleged incorporation of new items required under the Next Generation Energy Act ("NGEA") and the Commission's recent directives in Order Nos. 90943 and 91079 issued in Case No. 9704.[57]

Mr. Murphy noted that the NGEA became law on June 1, 2025 and requires, pursuant to PUA § 4-214, that the Company demonstrate that it has considered customer benefits, cost-effective alternative options related to replacements, upgrades and new components, and that, for safety related investments, the Company has estimated risk reduction.[58] He also pointed out that Commission Order No. 90943, issued in Case No. 9704, "directed the Company to consider: (1) "the likely contraction in gas consumption" in all capital expenditure plans intended to maintain required levels of system safety; and (2) "all cost-effective non-pipeline alternative options available to defer, reduce, or remove the need to construct or upgrade components of [the Company's] natural gas system[], and not solely pursue infrastructure replacement in order to prudently justify [the Company's]

[55] *Id*. at 14-15.
[56] *Id*. at 15.
[57] *Id*. at 19.
[58] *Id*.

system safety and reliability spending." Both requirements were reaffirmed by the Commission in Order No. 91079.[59]

Mr. Murphy argued that the NGEA considerations are addressed in the Company's Capital System Planning process, which is grounded in engineering best practices and standards to determine appropriate materials and components based, in part, on their expected useful life, design options, cost, and assessment of available alternatives.[60] He also claimed that throughout the planning process "the Company continuously analyzes cost-effective options to defer, reduce, or eliminate the need to replace, upgrade, or construct new system components, including an analysis of non-pipeline alternatives, as appropriate."[61]

In his Direct Testimony, Mr. Murphy explained that, taking into account both PUA § 4-214(a) and PUA § 4-210(e)(6),[62] the Company considers energy efficiency, demand response, interruptible rates, local supply/storage, discontinuation of gas service, and proactive abandonments, plastic lining of high-risk pipes, cured-in-place-liners, and "CISBOT" Robotic Internal Cast Iron Joint Remediation and Joint Encapsulation as examples of Non-Pipeline Alternatives ("NPAs").[63] Regarding plastic lining for high-risk pipes, WGL stated lining is a pipe rehabilitation technique that forms a gas-tight barrier

[59] *Id*. at 19-20.
[60] *Id*. at 20.
[61] *Id*.
[62] *Id*. at 21. PUA § 4-214(a) defines non-pipeline alternative as "an investment or activity that defers, reduces or eliminates the need to construct a new gas pipeline. In addition to the accelerated replacement of leak prone pipe and reduction of associated greenhouse gases ("GHGs"), the Company relocates inside meters to outside, where feasible as a part of service replacements that are part of STRIDE projects." PUA § 4-210(e)(6) contemplates consideration of "cost-effective options to defer, reduce, or remove the need to replace, construct, or upgrade components of the gas company's distribution infrastructure, including leak detection and repair[.]"
[63] Murphy Direct at 21-24.

within an existing pipe and relies on the existing pipe for structural support. Mr. Murphy represents that this method is used in certain, limited circumstances when it is found to be a cost-effective solution that offers a limited extension of the assets' life, thereby deferring the need to replace it. Mr. Murphy testified that "the Company's experience has shown that liners are most applicable when installed in large diameter (16" and greater), medium-pressure mains with minimal to no services attached and in locations where the direct replacement is costly or challenging (such as pipelines underneath railroad crossings). Mr. Murphy stated, "These large diameter medium pressure assets generally have thicker remaining wall, offering more structural support for the liner. This approach was last used within the Company's distribution system in the District of Columbia in 2017."[64]

### *C. Capital Investment Cost Recovery—STRIDE, System Betterment, Customer*

STRIDE Investment

As shown in Table 1 above, WGL is seeking approval to move into base rates STRIDE-related distribution and transmission projects, capital investments related to System Betterment, and customer-related new business capital investments. These investments span both the Company's STRIDE 2 Plan that began on January 1, 2018, and extended through December 31, 2023, and the Company's STRIDE 3 Plan that commenced on January 1, 2024, and is ongoing.[65] Accordingly, the Company claims it is seeking approval to move the STRIDE 2 and 3 projects that went into service between January 1, 2023 and September 30, 2025 (the end of the Test Year) into rate base in this case. The

[64] *Id*. at 24.
[65] *Id*. at 30.

projects the Company is seeking to move into rate base are identified in Exhibits KMM-02 and KMM-04 within witness Murphy's Direct Testimony;[66] a revised list is provided in his Rebuttal Testimony.[67] Mr. Murphy noted that each project marked for inclusion in base rates was presented as part of the annual project lists that the Commission has reviewed and approved in the Company's STRIDE Plan proceedings.[68]

The Company has five STRIDE Transmission programs included in the STRIDE project list for moving into base rates in this proceeding. Together those projects represent approximately $4.1 million of gas plant in service total additions.[69] Regarding the STRIDE distribution projects included in Exhibit KMM-02, Mr. Murphy highlighted that among other things, the Company replaced 20.88 miles of higher-risk main, remediated 6,395 higher risk services, and installed 4,345 excess flow valves, and in calendar year 2024, the Company met or exceeded replacement targets while maintaining overall expenditures at planned levels.[70]

To support the reasonableness of the STRIDE capital investments to be placed in base rates, Mr. Murphy highlighted that Exhibit KMM-02 provides project-specific information for each STRIDE project that the Company represents went into service between January 1, 2023 and the end of the Test Year with a capital investment greater than $380,000.[71] The information provided for each STRIDE project includes the project name, type (distribution or transmission), STRIDE Program, project description (location,

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[66] *Id*.
[67] Murphy Rebuttal at 2.
[68] Murphy Direct at 30.
[69] *See id*. at 29 for a description of each transmission project.
[70] *Id*. at 31.
[71] *Id*. at 33.

scope) and the risk mitigation customer benefits. He noted that, because the costs of these STRIDE projects are now known, the Company has also provided actual STRIDE project costs as compared to STRIDE project estimates provided in the STRIDE filing that were used to develop the STRIDE rider. Additionally, the Company also provided an explanation of the difference between the actual cost and the STRIDE filing estimated cost if the difference is greater than 20%.[72]

In addition to customer benefits from the accelerated replacement of leak prone pipe, Mr. Murphy contended that STRIDE projects reduce greenhouse gas emissions ("GHGs") and indicated that certain customers have been able to participate in a meter relocation program (moving inside meters to the outside).[73] Mr. Murphy also testified that "other safety benefits to customers provided through STRIDE projects include the installation of excess flow valves ("EFVs"), thermal safety valves, updated as-built drawings, and improved reliability (*e.g.*, uprating low pressure systems which can reduce water infiltration into pipelines causing outages, *etc*.)."[74]

<u>System Betterment Investments</u>

Mr. Murphy noted that "System Betterment investments cover several categories and functional classes of non-STRIDE capital investments, encompassing a broad set of assets."[75] These projects are identified in Exhibit KMM-03 within Mr. Murphy's Direct Testimony[76] and later revised in his Rebuttal Testimony.[77] Mr. Murphy testified that these

[72] *Id*. at 33-34.
[73] *Id*. at 34.
[74] *Id*. at 35.
[75] *Id*. at 36.
[76] *Id*. at 37.
[77] Murphy Rebuttal at 2.

expenditures serve a number of purposes, including acting as corrective and preventative measures, delivering improved performance, mitigating risk, and maintaining compliance.[78] He also noted that WGL uses the same capital system planning process for system betterment projects as is used for the STRIDE-related projects (discussed above).[79] Of these projects, there are 17 large non-STRIDE transmission projects of which 12 are located outside of Maryland.[80] Mr. Murphy noted:

> System Betterment projects provide similar benefits to customers as those provided by STRIDE projects in that they often replace or address higher risk assets, and where applicable, may act to reduce consequences of a failure. For example, projects such as installation of remote-control valves or replacement of valve risers serve to improve valve operations, a capability that is critical to limiting the consequences of pipeline failures, thereby materially enhancing system safety and reliability.[81]

Through these System Betterment projects, the Company states that it has made many improvements between January 1, 2023 and September 30, 2025 including installing or replacing approximately 5.4 miles of main and remediating 3,584 services and associated EFVs.[82] Witness Murphy states that these cost-effective replacements not only eliminated the poorest performing parts of the Company's system, but they also reduced GHG emissions from associated leaks on the Company's system and improved safety and reliability through the addition of safety enhancements and industry advancements.[83]

To support the reasonableness of the System Betterment capital investments being placed in base rates, Mr. Murphy offered Exhibit KMM-03, which provides project-

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[78] Murphy Direct at 37.
[79] *Id*. at 38.
[80] WGL Initial Brief at 32.
[81] Murphy Direct at 38.
[82] *Id*. at 42.
[83] *Id*.

specific information for System Betterment capital investments made by the Company since the last rate case through the end of the Test Year with GPIS above $380,000.[84] He noted that similar to the STRIDE-related exhibits, Exhibit KMM-03 provides project-specific information to support the reasonableness and prudence of these investments, including, among other things, the amount of the investment, a description of the project, an explanation of the project's purpose, and how it benefits customers.[85]

Customer/New Business Investments

Mr. Murphy noted that customer (new business) investments "are capital projects that are responsive to customer requests. This category includes work to connect and supply new customers with natural gas service or to allow for increased use of natural gas by customers."[86] Mr. Murphy represents that between January 1, 2023 and September 30, 2025, the Company completed and placed into service $39.6 million of new business projects.[87] Mr. Murphy asserted that the Company uses the same capital planning process for these projects as was discussed above and considers the cost-effective options available to defer or reduce the need to install piping to serve customers, but states that there is no alternative that avoids the need to install piping because WGL has an obligation to provide natural gas service.[88] Mr. Murphy testified that capital investments made to connect new customers offer those customers all the benefits of natural gas service, which he describes

[84] *Id*. at 39.
[85] *Id*.
[86] *Id*. at 46.
[87] *Id*. at 49.
[88] *Id*. at 47.

as “hot meals, warm showers and comfortable homes via an energy network that is highly reliable, safe, and affordable.” [89]

OPC Direct

OPC witness Hopkins recommended the Commission find that WGL failed to demonstrate its STRIDE distribution investments were prudently incurred, and disallow all associated projects.[90] OPC also recommended a refund of collected surcharges if further evidence of prudence is not provided.[91]

Mr. Hopkins argued that WGL acted imprudently by (a) selecting services for replacement based solely on projected leaks per 100 services and (b) using a mis-calibrated JANA risk model to select projects with costs exceeding their benefits.[92] Mr. Hopkins contended that WGL’s use of JANA means that the Company overstates risk to ratepayers by including “reputational loss to WGL investors” as a risk and by using the maximum consequence for each type of potential cost rather than average cost.[93]

Regarding JANA, OPC witness Hopkins indicated that WGL retained only summary-level documentation of the process used to determine model input parameters, “which required the input of dozens of experts and are key to its argument that tens of millions of dollars of investments were selected prudently.”[94]

OPC argued that WGL also failed to evaluate whether alternatives (*e.g*., re-lining and non-pipe alternatives) could have reduced cost of risk-reduction activities, and also

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[89] *Id*.
[90] Hopkins Direct (PUBLIC) Errata at 75.
[91] *Id*. at 36 and 75.
[92] *Id*. at 6.
[93] *Id*. at 74 and 43-44.
[94] *Id*. at 41.

failed to revisit decision to execute projects when costs increased, even when accurate cost information would have resulted in the project not being selected.[95]

In addition to disallowance, OPC recommended that the Commission direct that investor-oriented benefits be excluded from benefit-cost analyses going forward and require WGL to use its average consequence costs for common events.[96]

As an alternative to disallowing all STRIDE project costs, OPC recommends (a) limiting recovery of main replacement costs to the cost per foot of relining with a cured-in-place liner if the replacement is otherwise deemed prudent and (b) disallowing or limiting recovery for projects where WGL failed to evaluate feasible alternatives.[97]

<u>MEA Direct</u>

MEA witness Lombardi expressed concern that the record developed by WGL in the present proceeding "highlights the need for the Commission to issue clear and swift guidelines that direct utilities to demonstrate full consideration of non-pipeline alternatives and better insight into how their new risk-ranking process works for all Washington Gas capital investments."[98] Ms. Lombardi stated that she is not recommending specific disallowances but expresses general concern about WGL's full consideration of non-pipeline alternatives.[99]

Ms. Lombardi argued that WGL did not adequately adhere to the Commission's directive in WGL's last rate case for gas utilities to consider "all cost-effective non-pipeline alternative options available to defer, reduce, or remove the need to construct or upgrade

[95] *Id*. at 5-6.
[96] *Id*. at 6.
[97] *Id*. at 6-7.
[98] Lombardi Direct at 4.
[99] *Id*. at 5.

components of their gas system."[100] Neither did WGL consider the enactment of the NGEA requiring gas utilities to produce an "analysis that compares the costs of proposed replacement projects with alternatives to replacement, including leak detection and repair…"[101] In the absence of such guidelines, Ms. Lombardi indicates that WGL is not giving the Commission's directive or Maryland law proper weight, *i.e.,* is continuing to interpret the directive and law in a way that lacks transparency and details about its NPA process.[102]

MEA cautioned that WGL's NPA analysis for all capital projects lacked sufficient detail for meaningful review, even though WGL witness Murphy stated that "the Company continuously analyzes cost-effective options to defer, reduce or eliminate the need to replace, upgrade or construct new system components, including an analysis of non-pipeline alternatives, as appropriate."[103]

Ms. Lombardi particularly found Mr. Murphy's explanation about the Company's use of pipe relining technology inadequate. For example, Ms. Lombardi highlighted Mr. Murphy's claim that "[t]he Company's experience has shown that liners are most applicable when installed in large diameter (16" and greater), medium pressure mains with minimal to no services attached and in locations where the direct replacement is costly or challenging (such as pipelines underneath railroad crossings)."[104] Ms. Lombardi argued that Mr. Murphy's statement on its face "pre-disqualifies candidate projects for cured-in-

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[100] *Id*. at 4.
[101] *Id*.
[102] *Id*. at 5.
[103] *Id*. at 5-6.
[104] *Id*. at 6.

place pipe liner technology."[105] MEA witness Lombardi discovered that WGL has used cured-in-place pipe liner technology including in Washington, D.C., but not in Maryland.[106]

Regarding WGL risk-ranking methods, MEA found the Company's process opaque, specifically regarding the choice of data points and how numerical values are assigned to risk factors.[107]

MEA is also concerned that Washington Gas does not adequately consider or proactively identify segments where customers have elected to electrify.[108] Washington Gas only plans for abandonment once all electrifications on a segment are complete, which can lead to replacing pipe that becomes unused shortly thereafter. MEA suggests a better targeted retirement program would balance risk mitigation with pending electrifications.[109]

MEA recommended that the Commission direct WGL in this proceeding or all gas utilities in future proceedings to: (a) provide detailed cost-benefit analyses comparing replacement versus repair, (b) identify criteria and comparative costs for cured-in-place pipe liners, (c) document the reasoning for deeming repairs infeasible, and (d) explain risk-ranking factor selection and data conversion methodologies.[110]

Staff

Staff witness Tesfaye recommended no changes to WGL's proposal regarding the STRIDE expenditures that it proposes to include in base rates in this proceeding, except

[105] *Id*.
[106] *Id*.
[107] *Id*. at 9.
[108] *Id*. at 8.
[109] *Id*.
[110] *Id*. at 9.

the Company's expenditures on Transmission Program 2, ID No. FPT0000050 and Transmission Program 5, ID No. FPT0000082.[111] Staff did not find that WGL justified recovery of the cost of FPT0000050 and recommended rejection of the cost. Staff recommends the approval of the actual cost of $747,654 for FPT0000082, instead of the $1,040,750 expenditure the Company proposed in this filing.[112] Staff witness Tesfaye wanted to review the Company's amended Exhibits KMM-1 through KMM-4 before making his final recommendation regarding the System Betterment and New Business expenditures.[113] On Surrebuttal, Staff recommended full approval of the two projects previously recommended for disallowance or partial disallowance, finding that projects' names had changed over time and that the Company's additional justification was sufficient.[114]

Montgomery County

In its Initial Brief, Montgomery County stated that it continues to be concerned about the ratepayer impacts associated with Washington Gas's planned infrastructure investments, both within and beyond this case. The County questioned the prudency "to authorize continued ratepayer-funded investments that would have the effect of expanding the gas network and locking in long-term future gas consumption."[115] It also asserted that expansion of the gas network unnecessarily saddles future ratepayers with significant and inequitable costs to cover additional expenses associated with potentially stranded

[111] Tesfaye Direct at 2.
[112] *Id*.
[113] *Id*.
[114] Tesfaye Surrebuttal at 6.
[115] Montgomery County Initial Brief at 2.

assets.[116] Regarding WGL's STRIDE request, the County supports OPC witness Hopkins' position that the Company has not met its burden to show that its STRIDE distribution investments were prudently incurred and thus recovery of this spending should be disallowed."[117]

WGL Rebuttal

WGL witness Murphy testified that he amended Exhibits KMM-1 through KMM-4 after the Company discovered that it inadvertently included $24 million of STRIDE projects within the System Betterment category.[118] The revised numbers are reflected in Table 1 above. The overall GPIS addition remains unchanged at $342.9 million, as no projects were added or removed. After further review, Mr. Murphy also clarified details around STRIDE Transmission Projects FPT0000050 and Projects FPT0000082 addressing the issues pointed out by Staff witness Tesfaye.[119]

Contending with OPC arguments on the prudency of WGL's STRIDE investments, Mr. Murphy argued that the Company's STRIDE plans should not be re-litigated. Mr. Murphy described the STRIDE application process and the Company's obligation to make annual filings each November. He also noted that "the Commission, as a statutory condition of approval, found the Company's STRIDE 2 and 3 Plans, to be reasonable and prudent and 'designed to improve public safety or infrastructure reliability over the short term and long term[.]'"[120] He pointed out that the Company's STRIDE Plans explain how the

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[116] *Id*.
[117] *Id*. at 4.
[118] Murphy Rebuttal at 2.
[119] *Id*. at 12-14.
[120] *Id*. at 18-19.

Company evaluates risk and "chooses" its replacement projects in its STRIDE Programs, including the STRIDE projects at issue in this proceeding.[121] Moreover, Mr. Murphy stated that "the Commission has already found the Company's STRIDE Plans and each STRIDE project in this rate case to be reasonably and prudently designed to improve public safety or infrastructure reliability over the short and long term."[122]

Additionally, Mr. Murphy defended WGL's Capital System Planning Process and risk management as critical for safe and reliable service, arguing that witness Hopkins's benefit-cost analysis is flawed for safety-related investments.[123] Witness Murphy contends that Mr. Hopkins's reliance on benefit-cost analysis examples from electric infrastructure and energy efficiency programs is irrelevant to safety-driven gas infrastructure replacements. Mr. Murphy also indicated that Mr. Hopkins understates the benefits of avoided failures by focusing solely on avoided repair costs and ignoring full consequences of failure. Mr. Murphy asserted that the JANA Lighthouse model is intended strictly for risk ranking and integrity management, making it unsuitable for the benefit-cost analysis attempted by witness Hopkins.[124] Mr. Murphy argues that Mr. Hopkins's recommendation to reject projects based on his benefit-cost analysis should be dismissed as it is inconsistent with federal safety requirements and prudent utility management.[125]

In response to OPC witness Hopkins's and MEA witness Lombardi's arguments about NPA analysis, Mr. Murphy maintained that WGL's programmatic-level NPA

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[121] *Id*. at 19.
[122] *Id*. at 20.
[123] *Id*. at 46-51.
[124] *Id*. at 44-45.
[125] *Id*. at 46.

planning was appropriate.[126] Mr. Murphy also argued that a cured-in-place pipe liner is more expensive per foot than replacement after accounting for risk reduction and all project costs.[127]

**Commission Decision**

As discussed in WGL witness Murphy's testimony, the Company properly submitted its applications for STRIDE Plan 2 and STRIDE Plan 3 pursuant to PUA § 4-210 and received approval from this Commission to pursue the projects listed in those respective applications. This proceeding is not a re-litigation of the Commission's decisions approving each of those STRIDE Plans. Nonetheless, the Commission reminds the Company that under PUA § 4-210(1),[128] it retains the right to review previously approved plans and determine whether an investment continues to meet the statutory requirements. Specifically, PUA § 4-210(l) states:

> (1) The Commission may review a previously approved plan.
>
> (2) If the Commission determines that an investment of a project or cost of a project no longer meets the requirements of subsection (f)(3) of this section, the Commission may:
>
> (i) reduce future base rates or surcharges; or
>
> (ii) alter or rescind approval of that part of the plan.

There is no more opportune time for the Commission to exercise its right to review a previously approved plan than during a utility rate case proceeding where the Company

[126] *Id*. at 61-66.
[127] Murphy Direct at 69.
[128] This Order references the current version of PUA § 4-210 which was updated to include provisions reflecting the Next Generation Energy Act. The Commission recognizes that most of the Company's investments in this proceeding were made before the current version of the statute took effect. However, the specific language highlighted here was included in the previous version of the statute under PUA § 4-210(j).

seeks to recover STRIDE expenses and argues that such expenses have been reasonably and prudently incurred. Such is the present case.

The Commission finds that while the Company presented a substantial amount of documentation supporting its position, the Company failed to adhere to the Commission's directive in Order No. 90943, issued in Case No. 9704, which directed the Company to consider:

> (1) "the likely contraction in gas consumption" in all capital expenditure plans intended to maintain required levels of system safety; and
>
> (2) "all cost-effective non-pipeline alternative options available to defer, reduce, or remove the need to construct or upgrade components of [the Company's] natural gas systems, and not solely pursue infrastructure replacement in order to prudently justify [the Company's] system safety and reliability spending in the future."[129]

As recognized by Mr. Murphy, both of these requirements were affirmed in Order No. 91079. Additionally, the recent statutory enactment of the NGEA also reinforces the importance of all utilities examining non-pipeline alternatives.

While Mr. Murphy testified that WGL's Capital System Planning process was iterative and examined alternatives multiple times and at each planning phase, there was little documentation for this, and no documentation demonstrating what NPAs were examined at the project level. The Commission believes that the Company should have provided some level of information documenting what NPAs were considered or why they were truly infeasible for each project. For example, the Company could consider including an additional column where appropriate in Mr. Murphy's Exhibits documenting what NPAs were considered for each project, and the reason for rejection. Therefore, the

[129] Order No. 90943 at 135.

Commission disallows the STRIDE costs associated with projects which began construction after January 1, 2024 (the calendar year beginning after the Commission's directive in Order No. 90943 was issued) according to the Company's STRIDE 3 plan documentation in Case 9708.[130]. Although these STRIDE 3 Plan costs are disallowed from going into base rates at this time, the Commission will allow the Company to maintain the capital in the STRIDE surcharge and the Commission will not preclude the Company from seeking recovery at a future date of these disallowed costs.

Additionally, the Commission notes OPC's concerns that WGL retained little documentation to support parameter selection for JANA analysis, and that "'reputational risk" appears to play a significant part in risk percentile assignments. The Commission requests that the rationale behind such parameters, including how each parameter provides customer benefit, be laid out clearly alongside parameters in WGL's next rate case.

2. Remove Unamortized Costs Related to Network Geothermal

WGL

WGL seeks recovery of a regulatory asset associated with the network geothermal pilot program established pursuant to the Working for Accessible Renewable Maryland Thermal Heat Act,[131] and in accordance with Order No. 91221 in Case No. 9749.[132]

[130] As previously stated, the Company has indicated that it is seeking approval to move into rate base the STRIDE 2 and 3 projects that went into service *between* January 1, 2023, and September 30, 2025 (the end of the Test Year). While this was not raised by any party to the case, the Commission finds it troubling that projects which are represented in STRIDE dockets to have not completed construction until *after* September 30, 2025 are being included in the Company's request in the instant case. *See e.g.*, BCA 310087, (which is included with an amount of $377,514 in WGL witness Murphy's Exhibit KMM-1 on Rebuttal Exhibits at 4), which has a "construction completion date" of Oct 2025 and a closeout date of "TBD" in Case 9708 Maillog No. 327951, Attachment A at 7 of 8.
[131] H.B. 397, 446th Md. Gen. Assembly Ch. 564 (2024) (codified at PUA §§ 7-703, 7-1001-1006; Env't § 1-701; Housing and Community Development § 4-1801).
[132] Nguyen Direct at 10.

Witness Nguyen testified that the balance of the regulatory asset at the end of the Test Year was $418,520 and the Company proposes a three-year amortization of this balance, which would result in an annual amortization of $139,507.[133] Ms. Nguyen indicated that the associated carrying cost of $28,142 calculated based on the Company's proposed rate of return and the 13-month average regulatory asset balance is included in the revenue requirement calculation.[134] WGL proposes to include the regulatory asset balance in subsequent base rate case filings.[135]

Staff

Staff witness Valcarenghi argued that it was not appropriate for WGL to begin recovering pursuant to the pilot. Mr. Valcarenghi noted that the Commission "denied WGL's pilot in its present form but directed the Company to modify its program with the goal of receiving proposals that are more cost effective, limit ratepayer impacts and increase[] learning opportunities."[136] Further, he argued that it was unclear when WGL would submit another proposal and that Commission Order No. 92095 stated that the appropriate recovery mechanism for WGL's pilot required further examination.[137] Initially, WGL contemplated recovering its costs as a surcharge assessed to customers. Given the unresolved issues regarding WGL's pilot program, Mr. Valcarenghi believed that "it is premature to allow WGL to begin recovering costs that were invested in the development of the pilot program." Therefore, Mr. Valcarenghi recommended that WGL continue to defer costs to a regulatory asset without a return until the Commission can fully evaluate

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[133] *Id*.
[134] *Id*.
[135] *Id*.
[136] Valcarenghi Direct at 10.
[137] *Id*.

WGL's modified proposal and determine the cost recovery mechanism.[138] Mr. Valcarenghi noted that WGL's Adjustment 11 includes an amortization of $139,507 that reduces Operating Income to recover costs incurred over a three-year period and his recommendation would remove these costs.[139]

WGL Rebuttal

In her Rebuttal, WGL witness Nguyen argued that Order No. 92095 "does not prevent the Company from seeking cost recovery of the Company's proposed Network Geothermal Pilot Program."[140] Instead, Ms. Nguyen stated that the Commission evaluated the pilot program and requested substantial revisions to the proposal. Ms. Nguyen contends that the Company is seeking recovery of costs incurred during pilot development in its base rate case following the approval of the Company's regulatory asset treatment of these costs in Order No. 91538.[141]

OPC Surrebuttal

In Surrebuttal, OPC witness Leyko recommended that the network geothermal regulatory asset be excluded from the rate base. Mr. Leyko noted that WGL's proposal is not only to recover the regulatory asset over three years but also to earn a return on the regulatory asset. Mr. Leyko pointed out that the Company includes $139,507 of amortization expense and a return on the regulatory asset of $28,142 (at the Company's weighted average cost of capital ("WACC")).[142] Contrary to Ms. Nguyen's view of Order

[138] *Id*.
[139] *Id*. at 11.
[140] Nguyen Rebuttal at 13.
[141] *Id*. at 13-14.
[142] Leyko Surrebuttal at 18.

No. 91538, Mr. Leyko noted that the Commission deferred all "further decisions, including those pertaining to carrying costs, amortization, and cost recovery" to this rate case and pointed out that the Commission in Order No. 91538 also denied Baltimore Gas and Electric Company's ("BGE") request to immediately include its regulatory asset in rate base.[143]

Further, OPC argued that WGL has not explained why it should be allowed to earn a return on costs related to developing a pilot that the Commission has yet to approve.[144] Mr. Leyko contends that WGL has not shown that there is any infrastructure, capital, or anything used or useful that has resulted from the pilot process. Additionally, Mr. Leyko recommended that "[r]ather than earn a return, it is more reasonable to allow WGL a *return of* but not a *return on* the regulatory asset."[145] Mr. Leyko asserted that removing the regulatory asset from rate base as he recommends would lower the Company's revenue requirement by $16,297 (at OPC's recommended WACC).[146]

**Commission Decision**

The Commission agrees with Staff that these costs are not ripe for recovery at this time. The Commission denied the original proposal and required substantial revisions to the Company's Network Geothermal Pilot proposal that have not been made. As a result, the Commission finds that WGL's request for recovery of the expenses incurred during pilot development are not recoverable at this time. However, the Commission accepts Staff's recommendation that WGL can continue to defer these costs to a regulatory asset

[143] *Id*.
[144] *Id*. at 19.
[145] *Id*. (emphasis in original).
[146] *Id*.

without a return until such time that the Company presents a revised proposal addressing the gaps pointed out in Commission Order No. 92095. The Commission at this time declines to accept OPC's recommendation of allowing the Company recovery of costs incurred and removal of the regulatory asset from the rate base.

### 3. Cash Working Capital

WGL

WGL witness Nyugen testified that the Company's cash working capital ("CWC") allowance for this proceeding is developed based on the Company's lead lag study consistent with the method used in previous rate cases before the Commission.[147] Ms. Nyugen explained that the CWC "is calculated by multiplying the average daily amount of expenses in the cost of service that give rise to a CWC capital requirement by their respective net lead lag days (revenue lag days minus expense lead lag days)."[148] She noted that the Company updates the revenue lag and gas purchase lead quarterly, and the study conducted for this proceeding reflects the most recent updates for those two items as of September 30, 2025.[149] Based on the Company's lead lag study performed for the present proceeding, WGL determined that a CWC allowance of $53,678,599 is required. Further, Ms. Nguyen discussed how the Company computes revenue lag, which is a key driver for determining the daily cash resources used in operations. Specifically, Ms. Nyugen explained that revenue lag "represents the average number of days between the time the Company provides service and the time it collects payment for service rendered and is

[147] Nyugen Direct at 22.
[148] *Id*.
[149] *Id*. at 23.

comprised of three components: the meter read lag (15.21 days), the billing lag (4.51 days), and the payment lag (40.52 days) which results in 60.24 revenue lag days."[150] She noted that since the Company's last base rate case, the revenue lag has declined from 65.39 revenue lag days in Case No. 9704 to 60.24 revenue lag days in the current proceeding.[151]

Ms. Nyugen testified that the decline in revenue lag days is primarily due to the lower aged receivables balance of $73,699,781 in this proceeding compared to $86,352,381 in Case 9704.[152] Further, she noted that Maryland revenue lag is driven by the Company's billings and collections and reflects the WGL's actual experience and ability to timely collect payment in Maryland, in compliance with COMAR.[153]

In addition to revenue lag, Ms. Nyugen discussed the calculation of expense leads for certain O&M expense categories.[154] Ms. Nyugen stated, "The expense lead days is calculated by subtracting the average service date (average of beginning service date and invoice date) from the invoice payment date and multiplying the weighted average percentage of the invoice total over the invoice sample total."[155] Ms. Nyugen pointed out that using the Company's proposed methodology for calculating expense lead lag in this case would be lower than the adjusted 45-day formula adopted in Case No. 9704. She argued that the previous formula would result in a calculation of 45.05 days for the lead lag CWC factor, rather than the 34.77 days proposed by the Company.[156]

[150] *Id*.
[151] *Id*. at 24.
[152] *Id*.
[153] *Id*.
[154] *Id*. at 25.
[155] *Id*.
[156] *Id*. at 26.

Finally, Ms. Nyugen indicated that the Company updated its CWC calculation to add:

> a net lag for both depreciation and deferred income taxes to represent that, while customers fund the reserve for depreciation and the reserve for Accumulated Deferred Income Taxes ("ADIT"), they do so on a lagged basis. The Company does not collect depreciation or deferred tax expense on the first day of the month following when the Company records these expenses on its books. Thus, there is a mismatch between the recordation and the funding through collection of rates from customers, which necessitates the application of the lead lag.[157]

Staff

Staff witness Valcarenghi noted that WGL's inclusion of $53.678 million results in approximately $6.2 million of its requested revenue increase in this proceeding.[158] Mr. Valcarenghi disagreed with the methodology WGL used to calculate CWC; namely the Company's calculation of: (1) revenue lag; (2) the inclusion of several non-standard non-cash components; and (3) staff operating adjustments.[159] Mr. Valcarenghi argued that while the revenue lag of 60.24 days in the lead lag calculation is lower than the 65 days used in WGL's last rate case, it still appears to be higher than it was in a rate case prior to Case No. 9704 where a lag of 55 days was utilized.[160]

Mr. Valcarenghi pointed out that WGL's revenue lag days are significantly different between the three jurisdictions of Washington, D.C., Maryland and Virginia.[161] He noted that for each jurisdiction, the lag days used for (a) lag in number of days between service and reading of the meter, (b) lag in number of days between meter read date and

[157] *Id*.
[158] Valcarenghi Direct at 11-12.
[159] *Id*. at 13.
[160] *Id*.
[161] *Id*.

bill date reflect the same number of days: 15.2 days between service and meter read date and 4.51 days from meter read to bill date. He noted that the difference between jurisdictions is related to the revenue derived from the service period, which represents 40.52 days for Maryland, 62.74 days for D.C., and 27.29 days for Virginia.[162] Mr. Valcarenghi pointed out that it is unclear what is driving the significant difference in the lag days between jurisdictions. Due to this unexplained difference, he recommended that the CWC calculation use a revenue lag reflective of a lag of 55 days, which is similar to what was used in Case No. 9704.[163]

Additionally, Mr. Valcarenghi opposed WGL's inclusion of non-standard items that do not involve the outlay of cash in the CWC calculation. Specifically, Mr. Valcarenghi argued that "non-cash, charges such as depreciation expense, are already reflected in the development of operating income, so to also reflect it in the development of CWC is a non-standard approach since the components do not involve an outlay of cash."[164] Mr. Valcarenghi pointed out that no other Maryland utility includes non-cash items such as depreciation expense in the development of its CWC, and WGL did not include such items in its last rate case.[165]

Finally, Mr. Valcarenghi testified that making the CWC adjustments consistent with Staff's recommendation reduces WGL's CWC requirement from $53.6 million to $40.2 million.[166]

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[162] *Id*. at 13-14.
[163] *Id*. at 14.
[164] *Id*.
[165] *Id*. at 15.
[166] *Id*.

OPC

OPC witness Leyko testified that WGL's proposed CWC should be adjusted to capture the proper level of cash that the Company actually needs in its daily operations.[167] OPC argued that WGL's CWC is inflated by adding non-cash items (such as depreciation and amortization) to CWC, as well as WGL's inclusion of a revenue lag, without a corresponding expense lag on income taxes, which means that WGL's rate base is overstated.[168] On Surrebuttal, Mr. Leyko noted that he updated his CWC adjustment to include WGL's corrections on Rebuttal. Mr. Leyko stated that, by further removing non-cash items (depreciation and amortization) from the CWC calculation, the Company's CWC expense is lowered by approximately $11.779 million with a total revenue requirement reduction of about $887,000 at OPC's recommended ROR, grossed up for income taxes.[169]

WGL Rebuttal

Witness Nyugen testified that the Company reduced its revenue lag days downward from 60.24 days to 51.48 days, resulting in a $1.7 million decrease in the revenue requirement. Ms. Nyugen noted that this change in the revenue lag days to 51.48 days closely aligns with Staff witness Valcarenghi's recommendation to reduce the revenue lag days to 55 days.[170]

[167] Leyko Direct at 11.
[168] OPC Initial Brief at 44.
[169] Leyko Surrebuttal at 10-11.
[170] Nguyen Rebuttal at 6.

Ms. Nyugen rejected Staff's and OPC's recommendation to remove non-cash items from the CWC calculation.[171] She argued that "[c]lassifying depreciation as a non-cash item is a convention to conform to generally accepted accounting principles ('GAAP') for financial reporting purposes. However, for utility ratemaking, deferred taxes and depreciation are included as components of the revenue requirement, which is collected from customers and hence is a cash flow source for the Company."[172] She noted that while the Company does not experience an expense lag for these items, there is a revenue lag due to the timing of when customers pay their bills versus when depreciation and deferred taxes are recorded as reductions to the rate base.[173] Ms. Nyugen argued that "the inclusion of depreciation and deferred taxes in cash working capital synchronizes rate base, regulatory treatment for ADIT, and Reserve ('Accumulated Depreciation') with deferred tax expense and depreciation expense, respectively."[174] She indicated that the rate base complement for deferred taxes is an ADIT rate base credit balance and the rate base complement for depreciation is a Reserve credit balance that reduces the Company's rate base and consequently overall return on rate base. This is also a cash flow item for the Company.[175]

Ms. Nyugen argued that the parties' recommendation to remove from the CWC calculation depreciation and deferred taxes "would cause a misalignment in regulatory treatment for the associated components of capital investments" and "would require realignment of the regulatory treatment of the related components, necessitating removal

[171] *Id*. at 7.
[172] *Id*.
[173] *Id*.
[174] *Id*.
[175] *Id*.

of ADIT and Reserve from rate base."[176] She also contended that such a removal, based only on test year ADIT and Reserve balances, would increase rate base by $1,482.4 million, which would in turn significantly increase the revenue requirement in this case.[177]

Additionally, Ms. Nyugen opposed OPC witness Leyko's recommendation that WGL apply lag days according to statutory tax payment schedules. She argued that the recommendation is flawed because the federal and State Income Taxes included in the CWC calculation are deferred income tax amounts. Also, the Company is currently in a net operating loss position and therefore does not have a current tax expense on which to compute an expense lag.[178]

OPC Surrebuttal

OPC witness Leyko argued that witness Nyugen's assertion that OPC's and Staff's adjustments would require removing a large portion of WGL's rate base "is simply false."[179] Mr. Leyko contended that removing depreciation expense and accumulated deferred income tax from CWC does not require removing it from rate base as WGL claims. Rather, Mr. Leyko explained that those are two separate calculations where rate base represents the amount of investment and other capital the utility needs to provide safe and reliable service and CWC is the amount of cash necessary to finance the day-to-day operations of the utility.[180]

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[176] *Id*. at 8.
[177] *Id*.
[178] *Id*. at 9.
[179] Leyko Surrebuttal at 10.
[180] *Id*.

## **Commission Decision**

The Commission agrees with Staff's position in this instance. The Company's lead lag study was updated with a correction to the revenue lag days from 60.24 days to 51.48 days. Staff has adopted this change and points out it better aligns with the revenue lag adopted in Case No. 9074.

Additionally, the Commission agrees with Staff and OPC that non-cash items including depreciation and deferred income taxes should not be included in the CWC calculation. Both Staff and OPC point out that these items do not involve an outlay of cash and are already reflected in the development of operating income. As pointed out by OPC, removing the non-cash items from the CWC is consistent with how the Commission treated this issue previously and we are not persuaded that a change is necessary based on the record.[181]

### 4. Remove Non-Protected EDITs

Staff

Staff witness Valcarenghi testified that the Maryland jurisdictional share of the balance of excess deferred income taxes ("EDIT") includes $97.5 million of protected EDIT and $46 million of non-protected EDIT.[182] Mr. Valcarenghi explained that EDIT refers to income taxes that were collected from taxpayers but that are no longer payable to the U.S. Government due to a change in the prevailing corporate tax rate that is applied to

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[181] *Id*. at 12, referencing *In the Matter of the Application of the Chesapeake and Potomac Tel. Co. of Maryland to Continue and Revise the Alternative Regulations Plan and to Revise and Restructure Its Rates and Charges*, Order No. 70324 (Case No. 8462, Jan. 22, 1993) 1993 Md. PSC LEXIS 6 at *34.
[182] Valcarenghi Direct at 16.

taxable income in the computation of federal income taxes.[183] Mr. Valcarenghi noted that the change in the corporate tax rate from 35 percent to 21 percent as a result of the Tax Cuts and Jobs Act ("TCJA") gave rise to the balance in the tax payments previously collected that are above the now prevailing income taxes rate, which are held in ADIT as a component of rate base.[184] He also testified that the EDIT falls into two categories: protected and non-protected. Protected EDIT relates to federal income taxes that were attributable to deductions for tax depreciation and the balance of which is disbursed in accordance with regulations that require income taxes to be refunded pursuant to a strict rotation schedule to avoid normalization violations.[185] Non-protected EDIT refers to all other income taxes previously collected that do not relate to deductions for depreciation and does not have to adhere to a strict disbursement schedule.[186]

Mr. Valcarenghi recommended that the balance of the non-protected EDIT be disbursed as a credit to ratepayers in order to mitigate rate impacts on customers and in general to address affordability.[187] Mr. Valcarenghi indicated that "[b]etween 2006 and 2025 an average residential customer using 55 therms per month has experienced an increase in their bills for service from $28.83 to $68.66–a 138 percent increase."[188] He argued that the expedited return of the balance of the EDITs would provide measurable relief to customers.[189] Therefore, Mr. Valcarenghi recommended that WGL's revenue requirement associated with the $46 million balance in non-protected EDITs be disbursed

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[183] *Id*. at 15-16.
[184] *Id*. at 16.
[185] *Id*.
[186] *Id*.
[187] *Id*. at 17.
[188] *Id*.
[189] *Id*. at 17-18.

by removing that balance from rate base and then distributing the revenue requirement to customers by way of a special tariff which would distribute monthly credits for a one-year period then terminate.[190]

Mr. Valcarenghi asserted that a special time-focused tariff is a more appropriate means to deliver the EDIT (rather than by embedding the impact in this proceeding's revenue requirement) because it ensures that only the precise level of refunds subject to disbursal is delivered to customers.[191] Mr. Valcarenghi noted that he anticipates that "[t]he residential revenue requirement associated with the refund of the EDITs should provide targeted credits of approximately $5.00 per month for residential customers which should provide targeted relief to customers in an effort to make bills more affordable."[192] He testified that this recommendation would increase the rate base by the balance of the non-protected EDITs, or $46 million.[193]

*WGL Rebuttal*

WGL witness Bell delineated the Commission's prior acceptance of WGL's proposed methods to reflect the impact of TCJA in rates (in Letter Orders from January, 2018).[194] This included the following amortization rates for unprotected EDIT:

(a) unprotected plant-related EDIT: Average Rate Assumption Method ("ARAM"), consistent with protected plant-related EDIT (approximately 33 years);

(b) unprotected federal NOL DTA EDIT: 15 years; and

(c) unprotected other, non-plant-related EDIT: 10 years.

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[190] *Id*. at 18-19.
[191] *Id*. at 18.
[192] *Id*. at 19.
[193] *Id*. at 21.
[194] Maillog Nos. 218520 and 218665.

WGL witness Lawson testified that after the passage of the TCJA, the Commission accepted WGL's proposal to disburse non-protected EDIT balance using the average rate assumption method ARAM and the plan to return the excess balance to customers over the next 25 years to leverage the cost-free financing it provides for the customers' benefit.[195] Mr. Lawson argued that Staff witness Valcarenghi's proposal would impact the Company and the customers in the following ways.

First, it would add a surcredit to customers' bills for one year, reducing residential customer monthly bills by approximately $4.73.[196] Second, this surcredit would happen over the first year when the Company's base rates would increase.[197] Third, Mr. Lawson noted that Staff's recommendation would mean that rate base and WGL's revenue requirement will increase immediately and in the long-term put upward pressure on rates long after the surcredit rolls off.[198] Fourth, returning the EDIT balance as suggested by Staff would cause the Company to take on additional debt to provide surcredits over the one year period since WGL will lose the cost-free financing afforded by EDIT.[199] Mr. Lawson referenced Company witness Burrows' Rebuttal testimony which further explained that deferred tax balances are a recognized component of utility capitalization and are evaluated by credit rating agencies when assessing financial risk, funds from operations ratios, and capitalization stability.[200]

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[195] Lawson Rebuttal at 4.
[196] *Id*. at 6.
[197] *Id*.
[198] *Id*.
[199] *Id*.
[200] Burrows Rebuttal at 18. *See also* WGL Initial Brief at 60.

Mr. Lawson argued that Staff's recommendation for removing non-protected EDIT has two main drawbacks in addition to the real impact on the Company's credit rating. First, it would generate the type of "volatility the Commission has historically sought to avoid in favor of an approach that has a lower impact on customers."[201] Second, he pointed out that the Commission recognized in Case No. 9645 that rapid return of EDIT is costly to ratepayers. Specifically, Mr. Lawson noted that "the Commission recognized that such an action was costly, that offsetting rates using an accelerated credit created correspondingly higher bills in future periods, undermined principles of transparency of the Company's rates, and raised intergenerational equity concerns."[202]

Mr. Lawson recommended that the Commission reject Staff's recommendation for the one-year surcredit. He testified that while the Company believes continuing its present method is the best it recognizes the affordability challenges that customers are facing. Therefore, Mr. Lawson offered an alternative to Staff's approach for the Commission's consideration. Namely, WGL proposed to shorten the current amortization for the remaining non-protected EDIT from the remaining period of ARAM which is approximately 25 years to straight line amortization of 10 years.[203] Mr. Lawson indicates that, "[b]y moving to a 10-year amortization of this unprotected EDIT, customers will continue to receive an offset in rate base...[h]owever, the shortened amortization period effectively lowers the Company's overall proposed revenue requirement by an additional $2.8 million, when considering all associated tax implications."[204] Mr. Lawson asserts that

[201] Lawson Rebuttal at 8.
[202] *Id*.
[203] *Id*. at 9.
[204] *Id*.

compared to Staff's approach, the Company's 10-year alternative using the current ARAM "provides a comparatively much lower annual revenue requirement offset, but for a much longer period of time."[205]

Staff Surrebuttal

Witness Valcarenghi disagreed with WGL witness Lawson's claim that his proposal ran counter to what the Commission previously approved for WGL's initial non-protected EDITs stemming from the TCJA. Mr. Valcarenghi pointed out that in the Commission's initial approval for WGL's non-protected EDITs, the amount of time proposed by WGL and accepted by the Commission for the return of non-protected, non-plant EDITs to ratepayers was 10 years, not 25 years.[206] Next, he noted that the amount of the non-protected EDITs specified in the Company's 2018 filings requesting approval of its plan to return those EDITs to ratepayers was $39.8 million versus the $45.2 million balance of non-protected EDITs held at the end of the test year in this proceeding."[207]

Mr. Valcarenghi argued that the Staff proposal is consistent with the Commission's TCJA Letter Order. However, he stated that if the Commission opts for an alternative timeframe for disbursing non-protected EDITs, then a five-year amortization would be acceptable. He added that under this five-year amortization proposal, WGL's rate base would decrease by $29.9 million and income taxes would need to be adjusted to reflect the removal of the current amortization of EDITs and deferred income taxes.[208] During the

[205] *Id*. at 10.
[206] Valcarenghi Surrebuttal at 19 and fn. 26; *see also* Staff Brief at 26 for a complete discussion; plant-related non-protected EDITs were accepted to be on an ARAM amortization schedule, while non-plant, non-protected EDITs were accepted under a 10-year amortization schedule.
[207] Valcarenghi Surrebuttal at 20.
[208] *Id*. at 24.

evidentiary hearing, Mr. Valcarenghi argued that returning the funds to customers through a special tariff more immediately is best and would provide benefits to customers. He posited "... is it better to have the Company hold the cash or let the customers decide how they want to spend that money that's rightfully theirs?"[209]

**Commission Decision**

After considering the testimony in the case, the Commission finds it appropriate to reduce the current timeframe for returning a portion of non-protected EDITs to ratepayers over 25 years to 5 years. As WGL witness Bell stated, at least some of the customers that paid into the non-protected EDITs before 2018 may not still be WGL customers in 2051 when the ARAM amortization period ends.[210] This would mean that some ratepayers may never receive a full return of the money they contributed if the Company is permitted to maintain the ARAM amortization schedule.

The Commission also finds that Staff's original proposal to return the money to customers over a one-year time period could cause significant rate volatility and undermine the principle of gradualism. Additionally, the Commission finds that further examination would be required to determine how this shortened time period would impact the financial posture of the Company and impact ratepayers in the future.

The Commission accepts Staff's alternative counter proposal of a five-year amortization period as striking the right balance and ensuring that ratepayers receive the benefit of the EDITs that should flow back to them sooner rather than later. In WGL's Initial Brief, the Company stated that it recognized the affordability challenges facing

[209] Hr'g Transcript Vol. 3 at 736, lines 19-22.
[210] Staff Initial Brief at 31. *See also* Hr'g Transcript, Vol. 1 at 250, lines 1-22.

customers and in the spirit of compromise "would not oppose a five-year amortization period if the Commission believes that it is appropriate."[211] Additionally, WGL noted that either a ten-year amortization or a five-year period would provide near term relief while preserving some of the long term benefits of cost free capital and avoiding rate volatility, capital structure harm and intergenerational inequity that would follow from adopting a one year return period.[212] Therefore, the Commission accepts the Staff-proposed five-year amortization schedule which would require an increase in rate base by $29.9 million and corresponding income tax adjustments to reflect the removal of the current amortization of EDITs and deferred income taxes.[213]

5. Net Operating Loss Carryforward ("NOLC")

WGL

WGL witness Bell proposes an adjustment which adds $65.5 million[214] to rate base to correct what the Company identifies as an inadvertent tax normalization violation.[215] Ms. Bell noted that WGL witness Kelly's Direct Testimony explained that tax normalization rules require that the balance of NOLC-DTA generated by accelerated depreciation "must not be reduced for ratemaking purposes by any amount unrelated to accelerated depreciation or retirement of the property. Specifically, it cannot be reduced by tax sharing payments."[216]

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[211] WGL Initial Brief at 61.
[212] *Id*.
[213] Staff Initial Brief at 32.
[214] Bell Direct at 9.
[215] *Id*. at 3.
[216] *Id*. at 3-4.

Ms. Bell testified that continuing the Company's current practice of reducing the NOLC-DTA by the amount of tax sharing payments from affiliated companies constitutes violation of the normalization rules.[217] Therefore, Ms. Bell argued that the Commission must approve the adjustment "to remedy this violation during this proceeding, in order to satisfy the IRS Safe Harbor Provisions outlined in Revenue Procedure ('Rev. Proc.') 2017-47 for the correction of an inadvertent normalization violation" and to continue the Commission's practice of recognizing the normalization method of accounting which allows customers to continue to receive the benefit of accelerated tax depreciation.[218]

Ms. Bell indicated that the Company became aware of the potential for an inadvertent normalization violation as a result of the public release of certain public letter rulings ("PLR") in 2024. She testified that upon review of these PLRs, the Company recognized that the facts detailed were substantially the same as its own and that the IRS's application of the law was proper, and therefore determined that an inadvertent normalization violation had occurred.[219]

WGL witness Kelly explained that the IRS Rev. Proc 2017-47 requires that an inadvertent normalization violation, once identified, must be corrected at the taxpayer's next available opportunity–meaning either the taxpayer's next base rate proceeding or during a current open proceeding if the Commission's rules permit.[220] Additionally, IRS rules require that the taxpayer disclose the violation on its tax return the year in which the violation was identified and on subsequent tax returns until the violation is corrected.[221]

[217] *Id*. at 4.
[218] *Id*. at 4. *See also* WGL witness Kelly Direct at 16-18.
[219] Bell Direct at 4.
[220] *Id*. at 7.
[221] *Id*.

Ms. Bell testified that WGL disclosed the inadvertent normalization violation on its 2023 tax return filed in October 2024 and on its 2024 tax return filed in October 2025.[222] Ms. Bell argues that the current proceeding is the first available opportunity for the Company to remedy the violation and she cautioned that not doing so could mean that WGL's actions could fall outside the Safe Harbor Provisions of Rev. Proc. 2017-47 and become an intentional violation, resulting in the Company requesting a significant increase to rate base and a corresponding negative impact to customers.[223]

<u>Staff</u>

Staff witness Valcarenghi testified that the NOLC-DTA adjustment was a "necessary adjustment designed to correct the flow of depreciation deductions taken in the computation of federal income taxes."[224] He found that "the adjustment properly contemplates necessary adjustments in prior positions taken that are designed to ensure income taxes used for ratemaking are aligned with federal tax deductions…"[225] He noted that he understood WGL sought a PLR with the IRS during the pendency of a WGL rate case in the District of Columbia and requested that the Company provide the results to the Commission once received from the IRS.[226]

<u>OPC</u>

OPC witness Leyko pointed out that WGL's NOLC-DTA adjustment is in response to PLRs issued to Indiana Michigan Power Company, Public Service Company of

[222] *Id*.
[223] *Id*. at 7-8.
[224] Valcarenghi Direct at 8.
[225] *Id*.
[226] *Id*.

Oklahoma, and Southwestern Electric Power Company (all three affiliates of American Electric Power Company), not WGL itself.[227] Mr. Leyko argued that WGL is seeking a material change to its cost of service and rate base before confirming with the IRS whether the change is even needed.[228] Mr. Leyko acknowledged that, through discovery, the Company confirmed that it had filed for its own PLR on January 16, 2026 about the issue but had not yet received a response.[229] Mr. Leyko contended that the Company should have waited until it received a response from the IRS before implementing the adjustment. He also argued that if the IRS finds that WGL's current accounting of deferred tax is not allowed under normalization rules, then WGL can file for the ratemaking adjustment at that time.[230]

Mr. Leyko recommended that the Commission reject WGL's NOLC-DTA adjustment which would have the effect of lowering the Company's revenue requirement by approximately $4.780 million.[231] Mr. Leyko supported his position based on language in Commission Order No. 91768 where the Commission elected to deny OPC's request to remove the NOLC adjustment in Case Nos. 9692 and 9681 and hold the matter in abeyance pending the IRS response to the Exelon Utilities' PLRs.

<u>WGL Rebuttal</u>

WGL witness Kelly reiterated his argument that the Company would experience negative tax treatment which would be detrimental to the Company's ratepayers.[232] Mr.

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[227] Leyko Direct at 21-22.
[228] *Id*. at 22.
[229] *Id*. at 22-23.
[230] *Id*. at 23.
[231] *Id*.
[232] Kelly Rebuttal at 3.

Kelly also argued that OPC mischaracterizes the decision in Order No. 91768 from Case Nos. 9692 and 9681.[233] He stated that "[t]he Orders indicate that the NOLC DTA will be included in rate base pending the receipt of the IRS ruling, and if the IRS ruled the NOLC DTA inclusion is improper, refunds would be provided to customers."[234] Mr. Kelly ultimately recommended that the Commission allow the Company to maintain the NOLC DTA adjustment in rate base for establishing rates in the current case, provide the PLR to the Commission when received and provide refunds only if the IRS rules unfavorably.[235] He argued that this approach is consistent with Rev. Proc. 2017-47 and previous Commission Order No. 91768, and allows the tax payer to come into compliance with IRS normalization rules.[236]

<u>OPC Surrebuttal</u>

OPC witness Leyko continued to recommend that WGL wait until the IRS issues a Company-specific response confirming that WGL's proposed NOLC-DTA is appropriate before making such a material change to rates.[237] He also points out that Company witness Kelly acknowledged that "determinations made in a PLR are only directed to the taxpayer requesting them and not binding on the IRS as to another taxpayer."[238] Additionally, Mr. Leyko noted that under Rev. Proc. 2017-42, Section 4.07(3), a taxpayer with a pending PLR can maintain safe harbor by having the regulator set rates subject to future adjustment once the private letter ruling is issued.[239] He asserted that this approach would allow the

[233] *Id*. at 2.
[234] *Id*.
[235] *Id*. at 6.
[236] *Id*.
[237] Leyko Surrebuttal at 15.
[238] *Id*.
[239] *Id*. at 16.

Commission to avoid an immediate inclusion of $65 million of NOLC-DTA in the rate base while ensuring eventual compliance with IRS normalization requirements.[240]

**Commission Decision**

The Commission finds that WGL's NOLC-DTA adjustment raises complex regulatory and tax issues. Given that none of the parties have provided a definitive analysis of the associated tax consequences of a NOLC-DTA inadvertent normalization violation, the Commission will err on the side of caution and accept, for now, WGL's NOLC-DTA adjustment subject to future adjustment pending the issuance of the Company-specific IRS PLR response addressing the NOLC issues raised in this proceeding. Further, should WGL fail to support its position with a PLR within three years from the date of this order or should the Company-specific IRS PLR be unfavorable to the Company's position, whichever event occurs first, then the Commission will make an appropriate adjustment in its subsequent rate case to remove the revenue impact of the NOLC-DTA, including carrying costs at the authorized rate of return, in this proceeding. Additionally, the Commission directs the Company to separately account for the NOLC-DTA so that it can be more readily tracked and monitored for changes prospectively. The approach is consistent with previous decisions including Order No. 91768 from Case Nos. 9692 and 9681 (as pointed out in Rebuttal by WGL witness Kelly), as well as Order No. 85724 in Case No. 9311 and Order No. 86441 in Case No. 9336.

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[240] *Id*.

6. Wages & Salary Expenses

Staff

Staff witness Valcarenghi testified that WGL segments its wages into union and management groups. The union group is comprised of employees affiliated with Frederick and Shenandoah unions, or affiliated with the Teamsters and Local 2 unions.[241] He noted that the Frederick/Shenandoah unions received a 3% wage increase effective August 2025, and the Teamsters/Local 2 unions received the same 3% wage increases effective June 2025 and April 2025, respectively.[242] Mr. Valcarenghi agreed that the Test Year ending September 2025 only reflects a portion of these increases and therefore it is necessary to include an adjustment designed to capture the full impact of wage increase on an annualized basis.[243] Mr. Valcarenghi pointed out that the annualization of wage increases applicable to the management group is done in a similar manner as the union group, except management was afforded a higher percentage increase of 4.58% effective April 2025.[244]

Mr. Valcarenghi recommended that the management group wage increase be limited to the 3% increase afforded to union employees. Mr. Valcarenghi argued that WGL did not provide any information to evaluate the reasonableness of the differentiated percentage wage increase that resulted in higher percentage increase provided to the management group.[245] He further argued that it is incumbent on WGL to provide data demonstrating the reasonableness of costs sought. He noted that in prior WGL rate proceedings, the level of increase between the employees' groups has been similar. He

[241] Valcarenghi Direct at 22.
[242] *Id*.
[243] *Id*.
[244] *Id*. at 22-23.
[245] *Id*. at 23.

indicated that if the management group's wage increase was reduced to align with the union group that would result in an annualization of $1.2 million instead of the $1.8 million recommended by WGL.[246]

Additionally, Mr. Valcarenghi noted that WGL also included pro forma wage increases for projected wage increases to be granted post-test year that are applicable to the union groups. WGL included a 3% increase in wages applicable to the Frederick/Shenandoah group effective in August 2026, and a 3% wage increase effective in June 2026 for the Teamster Local 2 group and April 2026 for Local 2 group.[247] Although the wage percentage increases are based on the union contracts, Mr. Valcarenghi pointed out that the actual amount is an estimate that varies based on the employment levels when the increases become effective. Regarding post-test year wage increases, Mr. Valcarenghi agreed with WGL's pro forma wage increase at the percentage increase sought, but recommended including six months of the wages applicable to the proffered employee groups instead of a full year.[248] This would result in a $1.5 million reduction to operating income.[249]

Mr. Valcarenghi noted that while WGL removed $10 million of severance payments in the development of its Operating Wages, he recommended that an additional $326,728 of severance payments which remain in the Test Year should be removed.[250]

Mr. Valcarenghi testified that wages submitted by the Company for its Adjustment No. 20 does not correlate to the level of monthly wages submitted for the Test Year and

[246] *Id*.
[247] *Id*. at 24.
[248] *Id*.
[249] *Id*. at 28.
[250] *Id*. at 27.

the Company sought to increase Adjustment No. 20 by $5.9 million. Mr. Valcarenghi rejected this adjustment arguing that the Company has not provided any rationale or explanation for the change.[251]

In total, Mr. Valcarenghi recommended a downward adjustment of $2.3 million to WGL's Operating Wages on a pre-tax basis.[252]

<u>OPC</u>

OPC witness Leyko pointed out that WGL proposes to have customers pay rates beginning around July 27, 2026 that include costs that might not be incurred and if they are incurred, will be incurred at least 10 months after rates are approved, and 20 months after the end of the test year.[253] He argued that this was "an unreasonable expansion beyond the test year and these costs should be rejected as not known and measurable."[254] OPC contended that the Commission should adopt Mr. Leyko's adjustment and remove all 2027 wage increases from WGL's cost of service. This results in a revenue requirement reduction of $125,126.[255]

<u>WGL Rebuttal</u>

WGL witness Berti opposed Staff's recommendation to limit the management group wage increase to 3% and testified that the Company used actual payroll data that captured the 4.58% increase that occurred in the test year on April 1, 2025 to annualize test year payroll amounts based on known and measurable input.[256] He argued that Staff's

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[251] *Id*.
[252] Valcarenghi Errata to Surrebuttal Exhibit DLV-S3 at 10.
[253] Leyko Direct at 7.
[254] *Id*.
[255] OPC Initial Brief at 49.
[256] Berti Direct at 4.

proposal artificially lowers the management pay increase based on an incorrect comparison to union employee contractual pay increases.[257] He also argued that witness Valcarenghi offered no objective reason why using a hypothetical pay increase of 3% is more reasonable than using the actual pay increase amount the Company incurred to annualize test year labor expense for the management group.[258]

Mr. Berti also disagreed with both Staff's and OPC's proposals regarding the Company's post-test year union contractual pay increase for union employees. He argued that these increases are contractual obligations of the Company that it is required to honor and that should be included to accurately reflect scheduled increases that are known and measurable.[259]

Mr. Berti disagreed with Staff's adjustment to remove $326,728 in severance. He argued that severance expense is a "normal cost of doing business" and that the Commission in prior orders has allowed recovery of these expenses.[260] He asserted that "Staff's proposal to remove all severance expenses fails to recognize that normal-course employee separations–apart from extraordinary programs like the ISP and Voluntary Separation Program–are an ordinary and ongoing part of the Company's operations…"[261] He also noted that Mr. Valcarenghi's adjustment was calculated incorrectly and the correct amount to be removed would be $360,278.[262]

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[257] Berti Rebuttal at 4.
[258] *Id*.
[259] *Id*. at 5.
[260] *Id*. at 7.
[261] *Id*.
[262] *Id*. at 7-8. *See also* WGL witness Phong Nyugen's Exhibit PTN-R02 for corrected additional severance amount.

Mr. Berti also pointed out that if the Commission were to accept OPC's proposal to remove 2027 union pay increases, a corresponding payroll tax adjustment would be required for internal consistency.[263]

**Commission Decision**

The Commission agrees with Staff's proposal and corresponding argument that wage and salary increases occurring six months beyond the Test Year should not be allowed for cost recovery in the current proceeding.

Regarding Staff's proposal to limit the management wage increase percent to the same level as the union employee wage increase of 3%, the Commission recognizes that in Rebuttal testimony, witness Berti testified that the management group wage increase percent of 4.58% was based on actual payroll data which occurred in the test year on April 1, 2025. However, WGL failed to provide supporting documentation that would justify the differentiated wage percentage increase between the employee level groups. Therefore, the Commission accepts Staff's limit for the wage percentage increase for management employees at 3% at this time and notes this percentage is similar to the 2026 cost of living adjustment.

The Commission accepts Staff's proposal to remove the additional severance expenses and accepts the Company's correction of the total amount for removal as $360,278. While WGL points out that the Commission has in prior orders allowed severance expenses, the Company in the present proceeding has failed to provide sufficient documentation demonstrating why the expense is recoverable.

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[263] *Id*. at 6.

7. Normalize Overtime Compensation

Staff

Staff witness Valcarenghi testified that the Company's overtime compensation expense reflects an amount that is above the 5-year average level of the compensation component.[264] Mr. Valcarenghi noted that the 5-year average of this component is approximately $15 million or $1.880 million less than the amounts incurred in the Test Year.[265] Mr. Valcarenghi recommended that the overtime compensation be normalized to reflect the 5-year average of this wage component to reflect a more appropriate balance of the current spending.[266] Mr. Valcarenghi presented a table showing that overtime compensation has increased from $12 million to $17 million from 2021 to 2025 and noted that WGL instituted a severance program during 2024 and 2025. Staff asserted that "it cannot be considered reasonable for overtime compensation to increase as a consequence of the severance program implemented by the Company."[267]

WGL Rebuttal

In Rebuttal, WGL witness Berti disagreed with Staff, arguing that overtime compensation should not be normalized when costs had been increasing year-by-year before flattening in 2025.[268] He noted that over the last five years the vast majority of overtime was worked by union employees and the Company's separation programs did not affect their headcount.[269] He also noted that witness Valcarenghi's overtime adjustment is

[264] Valcarenghi Direct at 29.
[265] *Id*.
[266] *Id*.
[267] *Id*.
[268] Berti Rebuttal at 9.
[269] *Id*. at 8.

incorrect because he does not properly have the O&M factor applied to it.[270] Mr. Berti testified that, if anything, overtime expense should have been adjusted up to match the additional overtime compensation anticipated in the rate effective period; but the Company did not seek that adjustment.[271]

Staff Surrebuttal

Witness Valcarenghi continued to recommend normalizing this wage component, contending first that it is difficult to estimate this wage component with any degree of precision because it requires prediction of expected work that might require overtime in future months. Mr. Valcarenghi also notes that it is typical to normalize such costs reflected in development of operating income.[272] The effect of Staff's proposed adjustment is a reduction in Operating Income by $0.8 million.[273]

**Commission Decision**

The Commission accepts Staff's recommendation to normalize overtime compensation using a 5-year average and agrees that it is impossible for the Company to predict with certainty the associated workload levels. Additionally, the Commission finds, as pointed out by Staff, that using a 5-year average is a standard tool used in this process.[274]

[270] *Id*. at 10.
[271] *Id*. at 9.
[272] Valcarenghi Surrebuttal at 6.
[273] *Id*., Exhibit DLV-S3 at 11.
[274] *Id*. at 6.

8. Short Term Incentive & Long-Term Incentive

Washington Gas

WGL witness Berti represents that, based on precedent, he removed 5% of the Company's short-term incentive ("STI") expenses and 100% of its long-term incentive ("LTI") expenses.[275]

Staff

Staff witness Valcarenghi recommended removing all STI expenses because his review "suggests that costs are related in some measure to financial performance" and that "WGL has not demonstrated that the costs benefit ratepayers."[276]

OPC Direct

OPC witness Leyko recommended an additional disallowance of cost related to the STI above the 5% that was already removed by the Company.[277]

WGL Rebuttal

In response to Staff and OPC proposals to eliminate some or all of STI expenses, WGL witness Berti argued that the Company has taken a reasonable approach to incentive compensation recovery in eliminating 100% of LTI expense and removing 5% of STI expense associated with engaging in regulatory and legislative affairs issues in Maryland because it may be tied to financial performance.[278] Mr. Berti contends that Staff's position that STI's appear to be tied to financial performance and therefore should be disallowed

[275] Berti Direct at 8-9.
[276] Valcarenghi Direct at 32.
[277] Leyko Direct at 30.
[278] Berti Rebuttal at 11.

appears to be based in part on an inference from the fact that STI expense accounts include "ROE" in the title. Witness Berti clarifies that this naming convention "does not reflect the structure or purpose of the current STI programs" and notes that the Company will change the names of the accounts to avoid any future confusion.[279]

Additionally, WGL witness Shaver addressed the parties' recommendations. Mr. Shaver argued that WGL's STI Plan is an integral component of the Company's total compensation program and is necessary to attract, retain, and motivate a skilled workforce in a competitive labor market.[280] Mr. Shaver explained that the STI Scorecard reflects categories, metrics, and weightings that incentivize all Company employees to help the Company achieve its overarching strategic objective of delivering safe, reliable, affordable energy for the benefit of customers.[281] Under the STI Plan, all employees of the Company–including non-supervisory personnel, administrative personnel and union employees–are eligible to receive incentive compensation commensurate with Company and individual performance outcomes outlined in the Company's Value Drivers.[282] He also discussed the STI Scorecard categories, metrics and weightings for each Key Performance Indicator ("KPI"). The KPIs are split into four major categories that are designed to benefit customers: Operational Effectiveness (50% weighting); Safety (20% weighting); Environmental, Social and Governance (10% weighting); and, Support Energy Future (20% weighting).[283] In response to Staff and OPC, Mr. Shaver testified that "it is important to keep in mind that customer growth–such as the addition of new meters–can directly

[279] *Id*. at 10-11.
[280] Shaver Rebuttal at 4.
[281] *Id*. at 7.
[282] *Id*. at 4.
[283] *Id*. at 4-5.

benefit existing customers by improving the utilization of a utility's largely fixed infrastructure and spreading fixed costs over a broader customer base."[284] Mr. Shaver asserted that when new customers are added fixed costs are shared more widely, which can reduce the average cost of service and helps mitigate upward pressure on rates for existing customers.[285] Mr. Shaver contended that the "Support Energy Future" set of metrics incentivizes employees to pursue the kind of sustainable growth that keeps rates affordable for all customers.[286]

Staff Surrebuttal

Staff witness Valcarenghi maintained his position that STI expenses should be removed in full and noted that scorecard data provided by the Company does not reflect the Company's actual performance in any of the specified functional areas and therefore does not demonstrate that short-term incentives provided ratepayer benefit.[287]

OPC Surrebuttal

OPC witness Leyko explained that his recommended disallowance represents 20% of STI costs associated with customer growth (the "Support Energy Future" metric constitutes 20% of the STI scorecard weighting).[288] He explained that they did not disagree with the premise that customer growth can spread fixed costs but challenged that "WGL did not show any customer benefits tied to achieving the targeted customer growth

[284] *Id*. at 6.
[285] *Id*.
[286] *Id*. at 7.
[287] Valcarenghi Surrebuttal at 10.
[288] Leyko Surrebuttal at 13.

incentivized by STI is included in this rate case via lower rates, or verifiable reductions to cost of service."[289]

Generally, Mr. Leyko contended that this metric has not yielded any verifiable benefits to current ratepayers. He further argued that these STI costs are generally self-funding for the Company, since achievement of the goal will increase the Company's revenue while existing customers are forced to bear expenses regardless of whether targets are achieved or benefits actually accrue.[290]

**Commission Decision**

The Commission accepts OPC's 20% reduction in WGL's STI expenses. The Commission agrees that customer growth is a definitive benefit to the Company and shareholders, whereas the benefit to existing customers is not clear. While, on its face, customer growth can lead to spreading out of fixed costs, the Commission finds that the Company should have provided more quantifiable information supporting how its "Support Energy Future"–which is the customer growth KPI category–benefits ratepayers, and why any related expenses should be passed on to them. The Commission reiterates that it will continue to disallow costs associated with financial-related goals not benefiting ratepayers.

9. Leak Detection

WGL

In Direct Testimony, WGL witness Nyugen proposed Adjustment 21 to normalize leak detection expenses over a four-year period, consistent with an adjustment made in

[289] *Id*.
[290] *Id*. at 13-14.

Order No. 90943.[291] Adjustment 21 adjusted the Test Year leak detection expense of $1,021,017 by $397,566 to reflect a four-year average cost of $1,418,583.[292]

Staff

Staff witness Valcarenghi recommended that WGL's leak management costs be based on a 5-year average instead of the 4-year average recommended by the Company. Staff's recommendation using the 5-year average would reduce operating income by $0.4 million.[293] Staff argued that the 5-year average is more appropriate because it better captures a normal level of leak events expected to occur going forward.[294] Mr. Valcarenghi testified that the Company has reported that the number of leaks have declined substantially during the twelve-month period ending December 2021.[295]

OPC

OPC witness Leyko argued that WGL's calculation is not consistent with the Commission's decision in Case No. 9704, as the calculation ignores the reason that the Commission used a 4-year average in that rate case.[296] In that case, the Commission found that WGL did not support their proposed increase in leak detection expense and settled on normalizing adjustments to offset the unjustified increase in these costs.[297] OPC recommends that instead of using a 4-year average, a 3-year average be used that excludes 2023. This would lower WGL's revenue deficiency by $47,227.[298]

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[291] Nyugen Direct at 11.
[292] *Id*.
[293] Valcarenghi Errata to Surrebuttal Exhibits DLV-S3 at 9.
[294] Valcarenghi Direct at 36.
[295] *Id*.
[296] Leyko Direct at 18.
[297] *Id*. at 19.
[298] Leyko Surrebuttal at 5.

WGL Rebuttal

The Company identified an inadvertent omission of a leak detection cost department that led to understated leak detection expenses in the adjustment calculation.[299] After correcting for this omission, the normalization adjustment changed from a $398,000 increase to a decrease of ($1,000), demonstrating that the test year's expense is already representative of an average over four years.[300] The Company therefore revised its recommendation to remove its adjustment normalizing this expense.[301]

**Commission Decision**

Staff and OPC continued to recommend adjustments based on different normalization approaches, the Company testified after correcting the inadvertent error that no material variance arises and therefore eliminated its proposed adjustment. The Commission accepts Staff's approach and finds that their normalization method most accurately reflects the Company's costs.

10. Informational Advertising Expenses

CCAN Initial Brief

In its Initial Brief, the Chesapeake Climate Action Network ("CCAN") recommended that the Commission disallow the Company's request to recover $262,224 in informational costs.[302] CCAN argued that the Company has not met its burden to show

[299] WGL Initial Brief at 46.
[300] Nguyen Rebuttal at 13.
[301] *Id*.
[302] CCAN Initial Brief at 16.

that these costs are just and reasonable and presented three reasons supporting its disallowance.[303]

First, it argued that the Company's print advertisements "contain at least some clearly promotional content, and the Company has failed to produce a witness with knowledge sufficient to demonstrate that it properly characterized all of its informational advertising."[304] Specifically, CCAN pointed out that the Company did not offer a witness who could testify with personal knowledge of the Company's process for reviewing advertisements, and therefore the "Commission cannot determine that the advertisements at issue are all informational pursuant to the definition set forth in COMAR 20.07.04.08(E)(2)."[305]

Second, CCAN claims that the Company's final list of allocable advertising expenses contains material and unresolved errors.[306] CCAN pointed out that in discovery the Company sponsored an itemized list of "Total Company allocable expenditures" with an allocation of Maryland costs, yet on cross examination WGL witness Nguyen "acknowledged that the list was 'not all advertising' and some of the allocable expenditures actually referred to overhead costs that are 'not directly [related] to advertising' at all."[307] CCAN acknowledged that on rebuttal, Ms. Nguyen corrected the mis-categorization of $200,000 of promotional expenses as informational, but CCAN objected to "the fact that

[303] *Id*.
[304] *Id*.
[305] *Id*. at 17.
[306] *Id*.
[307] *Id*. at 17-18.

its updated list of expenses continues to contain material errors," suggesting a significant degree of unreliability in the Company's review process."[308]

Third, CCAN argued that although the Company submitted information on the advertising expenses from one of its employees, it chose not to call that employee as a witness during the hearing, which denied the Commission and other parties an opportunity to examine the witness about the information submitted or resolve questions. CCAN claims that without further testimony "it is impossible to determine whether the Company is properly seeking the recovery of costs necessary to convey information to ratepayers."[309]

WGL Response

In its Reply Brief, WGL opposed CCAN's recommendation for disallowing advertising expenses related to informational materials.[310] The Company argued that the record in the proceeding is more complete than CCAN alleges and it supports the Company's recovery of these costs.[311] Specifically, WGL noted that "all informational communication material the Company now seeks cost recovery for is included in the record of this case, along with an explanation of the Company's evaluation process."[312] Second, the Company argues that to the extent CCAN desired to evaluate the record evidence materials relative to the informational definition found in COMAR, it could have done so.[313] "The Company reviewed the communications expenditures, corrected the amount requested in rebuttal, and provided the materials supporting the informational

[308] *Id*. at 18.
[309] *Id*. at 19.
[310] WGL Reply Brief at 46.
[311] *Id*.
[312] *Id*.
[313] *Id*.

communications costs it seeks to recover."[314] Therefore, the Company recommended that the Commission reject CCAN's request for total disallowance and approve the amount supported by the Company's rebuttal testimony.[315]

**Commission Decision**

The Commission notes that WGL submitted additional documentation supporting its revised advertising expenses with Company witness Nguyen rebuttal testimony, and like any party, CCAN had the right to challenge the record evidence through filed testimony or during the evidentiary hearing. Here, after WGL filed revised advertising expenses in rebuttal, CCAN's counsel chose not to submit surrebuttal testimony requesting the Company demonstrate that the remaining informational advertisement expenses met the COMAR definition and further elected not to do so during cross-examination[316] of Ms. Nguyen. Therefore, the Commission denies CCAN's request to disallow an additional $262,224 in informational advertising costs and approves the corrected advertising expenses supported by the Company's rebuttal testimony and accepted by both Staff[317] and OPC[318] in Surrebuttal.

11. Depreciation

WGL

WGL completed its 2025 Depreciation Study, which included the following:[319]

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[314] *Id*.
[315] *Id*. at 46-47.
[316] Hr'g. Transcript at 448-457.
[317] Valcarenghi Surrebuttal at 16.
[318] Leyko Surrebuttal at 2-4.
[319] WGL Direct Allis at 4. Table 2 above has been adapted from Table 1 in Witness Allis' testimony to show Maryland rates only.

Table 2:
Summary of Original Cost, Accrual Rates, and Amounts (Maryland Only)

| FUNCTION | ORIGINAL COST | EXISTING ANNUAL DEPR. ACCRUALS | EXISTING ANNUAL DEPR. RATE | PROPOSED ANNUAL DEPR. ACCRUALS | PROPOSED ANNUAL DEPR. RATE | INCREASE/ (DECREASE) |
|---|---|---|---|---|---|---|
| ***MARYLAND*** | | | | | | |
| INTANGIBLE | $ 44.5 | $ 3.8 | 8.53 | $ 3.8 | 8.54 | $ 0.0 |
| STORAGE | 39.8 | 1.3 | 3.15 | 1.6 | 3.99 | 0.3 |
| TRANSMISSION | 472.1 | 7.6 | 1.61 | 11.7 | 2.48 | 4.1 |
| DISTRIBUTION | 2,054.2 | 33.5 | 1.63 | 54.4 | 2.65 | 20.9 |
| GENERAL | 139.5 | 5.9 | 4.22 | 6.4 | 4.55 | 0.5 |
| ***TOTAL MARYLAND*** | ***2,750.1*** | ***52.0*** | ***1.89*** | ***77.8*** | ***2.83*** | ***25.8*** |

Witness Allis testified that WGL's proposed depreciation rates, as outlined in its 2025 Depreciation Study, should be approved because the Company's current rates materially under-recover the cost of its assets over their service lives, particularly with respect to net salvage.[320] WGL proposed an overall increase in depreciation expense of $25.8 million, as a result of changes in plant and reserve balances, service life and net salvage estimates, and changing to the Traditional, or straight line, Method for the recovery of net salvage.[321]

Over the past five years, WGL calculated approximately $36 million in costs associated with the retirement of gas infrastructure, while recovering only a fraction of those costs through depreciation.[322] WGL argued that this persistent mismatch—where annual net salvage costs exceed recovery—resulted in current customers paying for assets that no longer provide service, thereby creating significant intergenerational inequity.[323] WGL proposed that this mismatch should be resolved by returning to the use of the straight

[320] WGL Initial Brief at 47.
[321] *Id*. at 48. *See also* WGL Direct Allis at 5.
[322] WGL Initial Brief at 47. *See also* WGL Direct Allis at 5.
[323] WGL Initial Brief at 47.

line method, in which "costs are allocated ratably, or in an equal amount, to each period that the asset is in service."[324]

In contrast, the Present Value Method ("PVM") reflects a deferred cost methodology, where future net salvage costs are significantly discounted when calculating annual depreciation.[325] Due to PVM's discounting approach, future ratepayers pay more in net salvage costs–in both real and nominal dollars–towards the end of an asset's useful life than they did during the earlier years, the burden of which is compounded by higher discount rates under PVM. In calculating the PVM, a credit-adjusted risk-free rate ("CARFR") is utilized, which is used to calculate the current value of future costs, and defined as "an interest rate that equates to a risk-free interest rate adjusted for the effect of its credit standing."[326] Mr. Allis explained that this definition of CARFR has three components: (1) determining the risk-free rate as compared to the U.S. Treasury bonds; (2) adjusting for the impact on a company's credit standing; and (3) the duration to which the interest rate applies.[327] In the event the Commission rejects the Company's request to return to the straight line method, WGL proposed the adoption of a CARFR discount rate of 5.0%. However, WGL remained adamantly opposed to Staff's assertion that PVM's failures can be eliminated through revised initial net salvage estimates.[328] WGL concluded that modifying the estimates would lead to significantly higher accruals than those proposed in the instant case.[329]

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[324] WGL Direct Allis at 10.
[325] *Id*. at 10 and 24.
[326] *Id*. at 32.
[327] *Id*. at 33.
[328] WGL Initial Brief at 48.
[329] *Id*.

Furthermore, in analyzing depreciation and net salvage, WGL argued that a more reasonable service life was necessary moving forward.[330] WGL adopted FERC's definition of "service life," which states:

> Service life means the time between the date gas plant is includible in gas plant in service, or gas plant leased to others, and the date of its retirement. If depreciation is accounted for on a production basis rather than on a time basis, then service life should be measured in terms of the appropriate unit of production.[331]

Additionally, WGL stated the definition of "net salvage" as "the salvage value of property retired less the cost of removal." WGL proposed that in order to facilitate "intergenerational equity," defined as the "concept that customers should pay their share of the costs of the assets that provide service to them," costs must be fairly apportioned throughout the asset's service life.[332] However, Mr. Allis concluded that the current PVM fails to recover net salvage costs over the asset's service life, which results in service life expenses being disproportionately paid by later generations, resulting in intergenerational inequality.[333]

WGL noted that Staff witness Garren proposed an increase in depreciation expense of approximately $13.2 million, including updated net salvage estimates and service life changes, but continued to rely on the Maryland present value method.[334] WGL argued that this approach perpetuates under-recovery and does not reflect the Company's actual cost

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[330] Allis Direct at 6.
[331] *Id*. *See also* FERC Uniform System of Accounts (Definition 36). Service life and useful life have been used as interchangeable terms.
[332] *Id*. at 9. This concept is also similar to the accounting principle referred to as the "matching principle," under which costs of an asset are matched with the revenues generated during its service life.
[333] *Id*. at 38.
[334] WGL Initial Brief at 48-49.

experience.[335] WGL also opposed Staff's recommendation to extend service lives for certain accounts, asserting that sufficient historical data do not support such proposals and fail to account for ongoing infrastructure replacement programs and evolving policy considerations.[336]

In response to OPC, WGL argued that OPC's witness Garrett's proposal significantly understated appropriate depreciation expense by extending service lives and retaining the Maryland PVM, resulting in a depreciation expense increase of $2.2 million.[337] The Company further asserted that OPC's analysis contains multiple computational and methodological errors, including improper application of the present value method and use of an incorrect discount rate.[338] According to WGL, these errors produce artificially low depreciation rates that are inconsistent with Commission precedent and the evidentiary record.[339]

Finally, WGL rejected AOBA's position, whose witness recommended no change to current depreciation rates.[340] The Company argued that maintaining the status quo would exacerbate existing under-recovery, particularly for net salvage, and contribute to continued growth in rate base.[341] WGL emphasized that inadequate depreciation has already resulted in a substantial shortfall in accumulated depreciation—estimated at approximately $180 million—which in turn increases rate base and customer costs.[342] Accordingly, the Company maintained that its proposed depreciation study and rates

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[335] *Id*. at 49.
[336] *Id*.
[337] *Id*. at 49-50.
[338] *Id*. at 50.
[339] *Id*.
[340] *Id*.
[341] *Id*.
[342] *Id*. *See also* WGL Reply Brief at 22-23.

represent the most accurate and equitable approach and should be adopted by the Commission.[343]

OPC

OPC witness Garrett recommended reducing Washington Gas's proposed annual depreciation accrual by approximately $23.7 million.[344] Two primary factors drove this adjustment: ensuring better-fitting service lives for plant accounts and the retention of Maryland's PVM for calculating net salvage.[345]

On net salvage, OPC opposed WGL's proposal to abandon the Maryland PVM, under which future removal costs are discounted to present value.[346] OPC highlighted that the PVM has been effectively utilized for years and ensures that customers do not overpay for net salvage.[347] Furthermore, Mr. Garrett emphasized that this method protects intergenerational equity by preventing current ratepayers from bearing a disproportionate share of costs that will be incurred decades in the future.[348] OPC argued that the present value approach appropriately reflects the time value of money and ensures more equitable cost allocation between current and future customers.[349]

Mr. Garrett proposed longer service lives than the Company for five disputed accounts–Account 367.1, Account 369, Account 376.2, Account 380.2, and Account 390. For his analysis, he utilized the retirement rate method, which organizes assets by vintage and develops observed life tables ("OLTs") reflecting actual retirement patterns by

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343 WGL Initial Brief at 50.
344 OPC Initial Brief at 53.
345 *Id*. at 53-54.
346 *Id*. at 55.
347 OPC Reply Brief at 33.
348 OPC Initial Brief at 55-56.
349 *Id*. at 56.

showing the amounts of property surviving at age intervals.[350] These OLTs were then fitted to Iowa curves to estimate average service lives.[351] Mr. Garrett proposed that WGL's Iowa curves were systematically too short and did not accurately reflect observed data.[352] Mr. Garrett asserted that service lives in this case are best estimated from an objective analysis of the Company's actual retirement data and argued that its selected curves provide a closer mathematical fit to the empirical record, as evidenced by significantly lower sum-of-squared-differences metrics.[353] For each account in dispute, Mr. Garrett asserts that the Company's service life estimates are "unreasonably short and unsupported" and risk high depreciation rates. Furthermore, Mr. Garrett rejected WGL reliance on speculative "dynamic factors" of electrification risks to justify shorter lives, emphasizing that such claims lack evidentiary support.[354]

Finally, Mr. Garrett recommended that the Commission use WGL's authorized ROR as the discount rate within the present value framework, rather than the CARFR proposed by WGL.[355] He explained that using the authorized ROR promotes regulatory consistency and creates a natural offset mechanism: higher authorized returns result in lower depreciation expense, and vice versa.[356] OPC contended that this approach enhances rate design balance and administrative efficiency, and therefore should be adopted in conjunction with retaining the Maryland present value method.[357]

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[350] *Id*. at 54.
[351] *Id*.
[352] *Id*. at 54-55.
[353] *Id*. at 55.
[354] *Id*.
[355] *Id*. at 56.
[356] *Id*.
[357] *Id*.

Staff

Staff recommended depreciation rates that are lower than those proposed by WGL, amounting to composite depreciation rates of 2.64% for Maryland-assigned plant and 2.34% for Maryland-allocated plant, compared to WGL's proposed 2.92% and 2.63%, respectively.[358] Based on these rates, Staff recommended a decrease to the annual depreciation accruals proposed by WGL of approximately $12.4 million[359]—approximately half of WGL's proposed $25.8 million increase.[360] Staff attributed this lower revenue requirement primarily to its continued use of the PVM for net salvage and modest extensions of service lives for select plant accounts.[361] Furthermore, Staff argued that the U.S. Supreme Court defined depreciation as "the loss, not restored by current maintenance, which is due to all factors causing the ultimate retirement of the property," which includes factors such as wear and tear, decay, inadequacy, and obsolescence.[362] In establishing this standard, Staff observed the U.S. Supreme Court was primarily concerned with depreciation expenses not being excessive, and not merely an evaluation of the Company's mathematical general accounting.[363]

Staff recognized that the calculation of net salvage reflected a core issue between the parties, and explained net salvage as the "difference between the predicted market value of an asset at retirement, or gross salvage, and the predicted expenses the utility would

[358] Staff Initial Brief at 2. *See also* Staff Reply Brief at 2.
[359] Valcarenghi Errata to Surrebuttal at 2.
[360] Staff Initial Brief at 2. *See also* Staff Reply Brief at 2.
[361] Staff Initial Brief at 2-3. *See also* Staff Reply Brief at 2.
[362] Staff Initial Brief at 3. *See also Lindheimer v. Illinois Bell Tel. Co.* ("*Lindeheimer*"), 292 U.S. 151, 167 (1934); *cited* and *quoted* in *Potomac Elec. Power Co.'s Application for Adjustments to its Retail Rates for the Distribution of Electric Energy*, Case No. 9702, Order No. 91181 at 147 (Jun. 10, 2024) (Maillog No. 310182) Errata (correcting details regarding a different subject) (Jun. 18, 2024) (Maillog No. 310314).
[363] Staff Initial Brief at 3. *See also Lindeheimer*, 292 U.S. at 169.

incur for the cost of removal."[364] Staff noted that WGL requested to use PVM in calculating net salvage, whereas other parties recommended the Straight-Line Methodology ("SLM") method. Staff observed that the Commission began utilizing PVM in 2007 through Case No. 9092.[365] Staff explained that the methodologies differ in that SLM "calculates a recovery of net salvage costs by allocating the original asset cost, less accumulated depreciation, less future net salvage estimates in equal amounts over the remaining service lives of the utility's assets by account."[366] However, by contrast the PVM "calculates recovery of net salvage by taking the estimates of future net salvage costs and applying a discount rate on a vintage basis for each depreciable account to reflect the time value of money, in order to determine the present value of future net salvage costs," which "results in a lower level of net salvage collections in depreciation rates."[367]

Staff opposed WGL's proposal to abandon the PVM in favor of the SLM, concluding that WGL failed to demonstrate sufficient justification to depart from nearly two decades of Commission precedent. Staff argued that WGL's criticisms of the PVM rely largely on unsupported assertions, including claims that recent under-accruals of net salvage indicate a systemic and permanent recovery failure, and that all Maryland utilities are similarly affected.[368] Staff maintained that these claims are unsubstantiated and reflect a misunderstanding of both the methodology and the appropriate evaluation period for depreciation performance.[369]

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[364] Staff Initial Brief at 5.
[365] *Id*. at 5. *See also In the Matter of the Application of Potomac Elec. Power Co. for Authority to Revise Rates and Charges for Electric Service and Certain Rate Design Changes*, Case No. 9092, Order No. 81517.
[366] Staff Initial Brief at 6.
[367] *Id*. at 6-7.
[368] *Id*. at 12-15. *See also* Staff Reply Brief at 3-5.
[369] Staff Initial Brief at 15-16. *See also* Staff Reply Brief at 5.

Staff further explained that temporary under- or over-accruals of net salvage are not unique to the PVM and may occur under either methodology, depending on the accuracy of underlying cost estimates.[370] Staff emphasized that the remaining life procedure ensures full recovery of an asset's service value over time, thereby preventing permanent under-recovery.[371] Accordingly, Staff concluded that any observed short-term discrepancies—such as those identified by WGL over a limited five-year period—do not justify abandoning the PVM.[372] Instead, Staff and supporting witnesses asserted that the appropriate remedy for under-accrual concerns is to refine net salvage cost estimates, which are determined prior to application of the depreciation methodology, rather than replacing the PVM itself.[373]

Staff further rejected WGL's broader criticisms of PVM, finding that WGL failed to substantiate several key assertions underlying its proposed shift to the SLM. Staff noted that WGL's claim that all Maryland utilities are under-recovering net salvage is unsupported by verifiable evidence, relying only on a reference to a single SEC filing.[374] Similarly, Staff found that WGL did not substantiate its assertion that accumulated depreciation is understated by approximately $180 million, as no supporting calculations, empirical data, or defined time horizon were provided.[375] Staff also refuted WGL's intergenerational equity argument, explaining that while the PVM may appear to shift costs in nominal terms, it promotes equity when evaluated in real dollars by accounting for the

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[370] Staff Initial Brief at 12.
[371] *Id*. at 8.
[372] *Id*. at 9.
[373] *Id*. at 12-13.
[374] *Id*. at 15-16.
[375] *Id*. at 17. *See also* Staff Reply Brief at 4.

time value of money—whereas the SLM produces inequitable outcomes when measured on that basis.[376]

Staff additionally proposed that several of WGL's concerns reflect misunderstandings of fundamental depreciation principles. Staff emphasized that temporary mismatches in cost recovery, including instances where assets are retired before full recovery, are expected outcomes within group depreciation and are designed to balance over time.[377] Staff further found that WGL's arguments regarding accelerated asset retirements due to energy policy are speculative and unsupported by quantifiable evidence.[378] Instead, Staff recommended that the Commission adhere to established precedent by continuing to apply the PVM with a CARFR-based discount rate of 5.0%, rejecting proposals to base the discount rate on the Company's rate of return.[379] Staff explained that in Case No. 9754, the Commission concluded that an excessively high discount rate is not beneficial to all customers as this would result in intergenerational equity by concentrating expenses to later customers, instead of spreading net salvage recovery more equally over time.[380] Staff also recommended that net salvage continue to be calculated on a vintage basis, consistent with prior Commission decisions, finding that this approach produces more accurate and reasonable results than account-level composite calculations.[381]

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[376] *Id.*at 17-18.
[377] *Id*. at 19-20.
[378] *Id*. at 20.
[379] *Id*. at 20-21. *See also* Staff Reply Brief at 5.
[380] Staff Initial Brief at 22.
[381] *Id*. at 22-23. *See also* Staff Reply Brief at 5.

AOBA

Witness Oliver testified that AOBA opposed the depreciation proposals advanced by WGL's witness Allis, arguing that the proposed changes would result in a substantial and unwarranted increase in rates at a time of heightened affordability concerns.[382] Specifically, AOBA noted that the Company's proposal would increase annual depreciation expense from approximately $52 million to $77.8 million—an increase of roughly 50 percent—and represents the largest single component of WGL's requested revenue increase in this proceeding.[383]

AOBA further contended that Mr. Allis's analysis fails to adequately account for evidence within the Company's own data showing that significant portions of WGL's plant are remaining in service longer than the assumed service lives used to calculate depreciation rates.[384] According to Mr. Oliver, this demonstrated divergence between actual and assumed plant lives supports lower, not higher, depreciation rates.[385] AOBA speculated that where assets remain in service beyond their projected lives, current depreciation rates may already be overstated, resulting in customers being overcharged for depreciation expense.[386] Furthermore, AOBA argued that WGL should provide greater evidence to substantiate the reasonableness of the Company's plant removal costs.[387] Here, AOBA concluded that WGL's plant removal costs were unsupported by evidence in the record.[388]

382 AOBA Initial Brief at 19-20. *See also* AOBA Reply Brief at 10.
383 *Id*. at 20. *See also* AOBA Reply Brief at 10.
384 AOBA Initial Brief at 20.
385 *Id*.
386 *Id*.
387 AOBA Reply Brief at 11.
388 *Id*.

With respect to net salvage, AOBA rejected WGL's criticism of Maryland's PVM, asserting that the Company's proposal is primarily concerned with accelerating cost recovery rather than ensuring full recovery.[389] AOBA emphasized that WGL has not shown that it will be unable to recover prudently incurred net salvage costs under the existing methodology.[390] Instead, Mr. Oliver argued that any mismatch between estimated and actual net salvage costs is largely attributable to inaccuracies in initial estimates and the inherent uncertainty in forecasting removal costs at the time assets are placed in service.[391]

Finally, AOBA maintained that if any intergenerational inequity exists, it lies between past and future customers and is not correctable through changes to depreciation methodology.[392] Witness Oliver emphasized the need for greater scrutiny of WGL's claimed: (1) net salvage costs regardless of the methodology employed, and (2) plant removal costs.[393] Accordingly, AOBA concluded that the Company's proposed depreciation changes—and the associated increase in revenue requirement—are unnecessary, unsupported by the record, and should be denied.[394]

**Commission Decision**

The Commission has carefully reviewed the record evidence and the arguments presented by the parties regarding appropriate depreciation rates, service lives, and net salvage methodology. Based on that review, the Commission finds that Staff's proposed composite depreciation rates—2.64% for Maryland-assigned plant and 2.34% for

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[389] AOBA Initial Brief at 21.
[390] *Id*.
[391] *Id*. at 22.
[392] *Id*. at 23-24.
[393] *Id*. at 24. AOBA Reply Brief at 12.
[394] AOBA Initial Brief at 24.

Maryland-allocated plant—more accurately reflect the expected consumption of utility plants than the higher rates proposed by WGL. Staff's recommendation is to decrease the annual depreciation expense proposed by WGL by approximately $12.4 million. The Commission is persuaded that Staff's use of modest service life extensions for certain plant accounts, its treatment of net salvage, and continuation of the PVM for net salvage produce a more measured and supportable revenue requirement.

As concluded by the U.S. Supreme Court and prior Commission decisions, depreciation is defined as "the loss, not restored by current maintenance, which is due to all factors causing the ultimate retirement of the property. These factors embrace wear and tear, decay, inadequacy, and obsolescence."[395] Furthermore, precedent has established that:

> [T]he company has the burden of making a convincing showing that the amounts it has charged to operating expenses for depreciation have not been excessive. That burden is not sustained by proof that its general accounting system has been correct. The calculations are mathematical, but the predictions underlying them are essentially matters of opinion.[396]

In applying this principle, the Commission is mindful that depreciation rates must be reasonable and not excessive, and must be supported by credible evidence rather than solely by mathematical and mechanical adjustments.

A central issue in this proceeding is the appropriate methodology for calculating net salvage. The Commission finds that all parties have provided thorough and persuasive explanations discussing the PVM and SLM, which the Commission has employed since Case No. 9092.[397] The record demonstrates that PVM endeavors to effectively account for

[395] *Baltimore Gas and Elec. Co.'s Application for an Electric and Gas Multi-Year Plan*, Case No. 9692, Order No. 90948 (Dec. 14, 2023). *See also Lindheimer*, 292 U.S. at 151 and 167.
[396] *Id*. at 52. *See also Lindheimer*, 292 U.S. at 169.
[397] Order No. 81517 at 31.

the time value of money by discounting future net salvage costs and passing on savings to ratepayers. However, WGL raises valid concerns about the creation of intergenerational inequities from discounting rates of current customers at the expense of later customers.

As such, the Commission acknowledges that its adoption of the PVM departed from the traditional method. While the Commission chooses to retain the PVM at this time, the Commission has noted the Company's concerns related to the PVM under-recovering the cost of removal and contributing to intergenerational inequities.[398] As the PVM has been used for a significant number of years by all Maryland utilities, the Commission believes now is an appropriate time for an assessment of its effectiveness. Consequently, within six months of this Order, the Commission directs Staff to submit a Report that reviews the performance of the PVM. The Report should address the following: utilities' historic under-/over-recovery of all net salvage; utilities treatment of any under-recovered net salvage costs; the status of utilities' net salvage recovery in other jurisdictions employing PVM, and the estimated rate impacts of adopting the SLM or net salvage recovery.

The parties disagree about the appropriate service lives to estimate for several accounts. Staff proposes changes to the Company service life estimates for two accounts, Account 376.2 and Account 380.2,[399] while OPC extends the Company's service life estimates for five accounts: Account 367.1, Account 369, Account 376.2, Account 380.2, and Account 390.[400] As the Company noted, the retirement data for the accounts in question is limited.[401] Therefore, the Commission believes Staff's modest service life adjustments

[398] Allis Direct at 38.
[399] Garren Direct at 21.
[400] Garrett Direct at 12-22.
[401] Allis Rebuttal at 20.

are reasonable and conservative based on the observable data and adopts their proposed service lives in the calculation of the depreciation expense.

Additionally, the Commission accepts the CARFR discount rate of 5.0%, which was the proposed rate by both WGL and Staff. The Commission has previously approved the use of CARFR as the discount rate[402] and observes that WGL's depreciation study raised concerns that a higher discount rate may not favor all customers, and could result in intergenerational inequity to the disadvantage of future customers.

Therefore, as summarized above, the Commission concludes that Staff's recommended depreciation rates, service life assumptions, and net salvage methodology represent the most reasonable and well-supported approach in this proceeding and should be adopted in full. However, the Commission remains committed to a thorough review of the Staff report discussing PVM and related customer impacts.

## B. Cost of Capital

The cost of capital for a company is calculated using the rate base, capital structure, cost of debt, and ROE. The utility recovers its ROE and return on debt through charges paid by ratepayers. The ROE requires analysis, as it is typically estimated based on market conditions and different analytical approaches. The cost of debt can be directly observed, as bonds are issued subject to specific interest rates, though the appropriate cost may still require examination. Once the cost of debt and ROE are determined, they are weighted according to the percentage of debt and equity in the utility's capital structure. The sum of the weighted cost of debt and ROE is the utility's overall ROR.

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[402] Order No. 91181 at 112, Case No. 9702.

Although WGL is a subsidiary of AltaGas, and thus its stock is not publicly traded, the Commission must still examine WGL's level of risk and its capital structure to determine its cost of capital. Generally, a determination of appropriate ROE is calculated by a comparison to "proxy" companies and investments of comparable risk. The parties submitted varying analyses based on differing methodologies and models. In assessing the various proposals, the Commission must, in accordance with PUA § 4-201, determine "just and reasonable" rates for the regulated service that it provides.

1. <u>Return on Equity</u>

WGL, Staff, OPC, and AOBA each proposed a different ROE as summarized below:

Table 3:
Return on Equity as Recommended by Parties

| | WGL[403] | Staff[404] | OPC[405] | AOBA[406] | MEA[407] |
|---|---|---|---|---|---|
| ROE Recommendation | 10.85% | 9.50% | 7.07% | 9.40% | 9.00% |

<u>WGL</u>

WGL asserted that the authorized ROE must satisfy the standards established in *Bluefield* and *Hope*, specifically that it: (1) enables the Company to attract capital; (2) maintains the Company's financial integrity; and (3) is comparable to returns on

[403] WGL Direct Nowak at 4.
[404] Staff Surrebuttal Manka at 2.
[405] OPC Surrebuttal Lin at 6.
[406] AOBA Direct T. Oliver at 16.
[407] MEA Direct Kihm at 2.

investments of similar risk.[408] Moreover, WGL explained that the ROE should be consistent with the long-term expectations of equity investors in utility industries.[409] However, WGL mentioned that while the cost of debt and preferred stock can be directly observed, the cost of equity cannot and must be analyzed by various financial models.[410]

The Company further emphasized that ROE represents a component of the cost of service—*i.e.*, the cost necessary to attract common equity—and is therefore recoverable in rates.[411] As a result, WGL witness Nowak recommended that the Commission authorize an ROE of 10.85% (corresponding to an overall ROR of approximately 8.07%) based on several analytical models, including the Discounted Cash Flow ("DCF") model, the Capital Asset Pricing Model ("CAPM"), and the Risk Premium Model ("RPM").[412] The DCF and CAPM models were based on a proxy group of 7 companies.[413]

To calculate his DCF model, witness Nowack used earnings per share estimates from S&P Capital IQ, Zacks, and Value Line, annualized dividend per share, and three different averages for stock prices based on 30, 90, and 180 days.[414] To calculate the CAPM Mr. Nowack used three different risk-free rates (representing different estimates of 30-year U.S. Treasury bonds), betas from Value Line and Bloomberg, and two different estimates of market returns based on a DCF estimate of each company in the S&P 500 where one is based on all companies and the other excludes companies with growth rates over 20%.[415]

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[408] WGL Initial Brief at 15.
[409] WGL Rebuttal Nowak at 15.
[410] *Id*.
[411] WGL Initial Brief at 15.
[412] *Id*. CAPM is an estimate of return and is a function of adding a risk-free rate to an estimated market risk premium adjusted by beta, which is a measure of a particular company's volatility of returns relative to the market as a whole. Order No. 90943 at 80, fn. 280. *See also* WGL Direct Nowak at 1.
[413] WGL Direct Nowak at 24.
[414] *Id*. at 28-29.
[415] *Id*. at 33-34.

The RMP was a regression model of awarded ROEs in natural gas rate case minus the 30-year treasury yield against the 30-year treasury yields.[416] Finally, Mr. Nowak used the expected earnings methodology as a benchmark and relied upon the projected 2028 - 2030 ROE for the proxy group as reported by Value Line that witness Nowack adjusted.[417]

Mr. Nowak's analysis resulted in the following:[418]

Table 4:
Summary of Updated Results of ROE Analyses

| | Low | Mean | High |
|---|---|---|---|
| *Primary Analyses* | | | |
| DCF Result | 9.83% | 11.31% | 14.13% |
| CAPM Result | 11.65% | 11.89% | 12.31% |
| Risk Premium | 10.39% | 10.45% | 10.47% |
| **Average** | | **11.21%** | |
| *Benchmark Analysis* | | | |
| Expected Earnings | 10.42% | | |

WGL compared the Company's requested ROE to recent regulatory outcomes, noting that the national mean and median authorized ROEs for gas distribution utilities since January 2024 are 9.70% and 9.75%, respectively.[419] While the Company's requested ROE exceeds these averages, they attributed the difference to WGL's specific risk profile, including its elevated capital expenditure requirements, relatively smaller size, and the regulatory environment in Maryland.[420] The Company contended that setting ROE at or below national averages without accounting for these factors would fail to meet the comparability standard and could impair the Company's ability to attract capital.[421]

[416] *Id*. at 35-37.
[417] *Id*. at 38-40.
[418] *Id*. at 16.
[419] *Id*.
[420] *Id*. at 16-17.
[421] *Id*. at 17.

Furthermore, Mr. Nowak analyzed the relationship between government bond yields and the cost of equity, explaining that higher interest rates necessitate higher equity returns to remain competitive for investment capital.[422] He noted that sustained elevated Treasury yields place upward pressure on utility dividend requirements and, correspondingly, the cost of equity.[423] As a historical benchmark, witness Nowak observed that when Treasury yields were last at similar levels (2006–2007), authorized ROEs for gas distribution utilities ranged from approximately 10.14% to 10.52%.[424]

Washington Gas also argued it has greater business risk due to elevated capital expenditures, small size relative to the proxy group and because Maryland's regulatory environment is one of the most restrictive in the U.S. for investors.[425] Ultimately, Washington Gas "asks the Commission to recognize that Washington Gas's risk profile supports an ROE of 10.85%."[426]

In response to other parties' recommendations, WGL argued that the proposed ROEs are not substantiated by evidence of record and could jeopardize the financial integrity of the Company, resulting in harm to customers.[427] In particular, Mr. Nowak stated that the Commission should reject OPC's recommendation of 6.74% or MEA's recommendation of 9.00% as they "are clearly insufficient to meet the standards for a just and reasonable return."[428] Mr. Nowak asserted that both recommendations would place the Company's ROE as an outlier and substantially below the authorized equity return of other

[422] *Id*.
[423] *Id*.
[424] *Id*.
[425] *Id*. at 26 - 27.
[426] *Id*. at 29.
[427] *Id*. at 18.
[428] WGL Rebuttal Nowak at 3.

gas companies.[429] Witness Nowak emphasized that if accepted by the Commission, these recommendations represented a risk to the financial integrity of the company.[430]

Additionally, WGL claimed that Staff witness Manka excluded many DCF results as outliers, and his CAPM estimates would be closer if both utilized a forward-looking market risk premium rather than a historical one and not using Vasicek-adjusted betas.[431]

Regarding OPC, WGL noted that witness Lin referenced several expected equity market return estimates from financial advisors, asset managers, and academic institutions, which are "forward-looking estimates used for broader portfolio allocation purposes and incorporate a "repricing" component that reflects anticipated changes in asset valuations, reducing the projected return."[432] Additionally, WGL averred that OPC's proposed ROE is insufficient to incentivize private investment when compared to the yield of 30-year Treasury bonds.[433] In response to MEA witness Kihm, the Company criticized the use of a multi-stage DCF as unnecessary for mature companies such as utilities, that dividend growth can only be sustained by earnings growth, and that witness Kihm did not provide analytical support for GDP growth as an indicator of long-run dividend growth.[434] Regarding Mr. Kihm's CAPM analysis, WGL claims it is unreliable and points to analysis conducted by Mr. Nowak that shows if MEA had relied upon the historical equity risk premium in-lieu of the one used that the resulting CAPM would be higher.[435] The Company also took issue with arguments presented by MEA that ROE level does not affect the

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[429] *Id*.
[430] *Id*. at 3.
[431] WGL Initial Brief at 18-19.
[432] *Id*. at 19-20.
[433] *Id*. at 20.
[434] *Id*. at 22-23.
[435] *Id*. at 23.

utilities ability to attract capital and refers to Mr. Nowak's discussion of cases where lower ROEs and concerns with regulatory environments led to credit downgrades and or increased financing costs.[436]

Washington Gas argued that AOBA's DCF and CAPM analyses fail to match the lower recommended ROE of 9.40% without sufficient explanation for the reduction from models' results.[437]

Mr. Nowak argued that separating the authorized ROE from a reasonable interpretation of the cost of equity creates substantial financial uncertainty.[438] He noted that such an action would risk moving the Commission further away from principles of *Hope* and *Bluefield*.[439] Washington Gas highlighted that there have been numerous events that contributed to financial uncertainty and risk to the Company, which need not be compounded.[440] WGL observed that international events including trade tensions between China and Taiwan, wars in the Middle East, "Operation Southern Spear," and "Operation Epic Fury" introduce additional risks in the gas industry and potential strain on gas supply.[441]

<u>OPC</u>

OPC cautioned that WGL's cost of capital should reflect real-world investor expectations and did not result in an excessive transfer of wealth from ratepayers to shareholders.[442] It was argued that WGL's requested rate increase was driven largely by

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[436] *Id*. at 24.
[437] *Id*. at 25.
[438] WGL Rebuttal Nowak at 16.
[439] *Id*.
[440] *Id*. at 9.
[441] *Id*. at 8-9.
[442] OPC Initial Brief at 3.

increased capital spending and an unreasonably high ROE, making it a critical lever for moderating customer rate impacts.[443] OPC advised against the Commission relying on historical ROE levels or outcomes from other jurisdictions and instead was encouraged to base its determination on the evidentiary record and the standards established in *Hope* and *Bluefield*.[444]

Under those standards, OPC asserted that the Commission should adopt witness Lin's recommended ROE of 7.07%, as it satisfied the requirements of maintaining financial integrity, supporting creditworthiness, attracting capital, and ensuring comparability to investments of similar risk.[445] OPC argued that WGL's financial position remained strong and that the Company would continue to attract capital even at the lower ROE, noting that other utilities in more distressed conditions have successfully accessed capital markets.[446]

To develop its ROE methodology relative to WGL, OPC used market pricing data from academic institutions and asset managers, such as BlackRock, Vanguard, State Street and New York University's Stern School of Business.[447] In utilizing data from these institutions and asset managers, OPC argued Mr. Lin's recommended ROE is closer to the returns on the entire stock market anticipated by the world's biggest investment firms.[448] OPC added that investor required returns for the entire stock market are necessarily higher than returns required for extremely low-risk utilities.[449] In further support of the proposed 7.07% ROE, OPC highlighted that WGL had experienced substantial and increasing

[443] *Id*.
[444] *Id*.
[445] *Id*. at 4.
[446] *Id*. at 5.
[447] OPC Direct Lin at 16-18.
[448] OPC Initial Brief at 5.
[449] *Id*.

profitability in recent years, with net income rising consistently from 2020 through 2025.[450] OPC cited these earnings trends as evidence that WGL was financially secure and highly profitable, and that a reduction in ROE would not jeopardize its financial health or ability to operate effectively.[451]

OPC argued that WGL would be able to attract capital at a 7.07% ROE, and that claims to the contrary were unsupported.[452] The position rejected the notion—frequently advanced by utilities—that any reduction in ROE would impair access to capital markets, noting that such outcomes had not been demonstrated in practice.[453] As support, OPC observed that even financially distressed utilities, such as Pacific Gas and Electric following its 2019 bankruptcy, were able to raise substantial amounts of debt and equity capital within a relatively short period.[454]

It was further asserted that Mr. Lin's recommended ROE of 7.07% more accurately reflected the return required by investors for a low-risk, regulated utility such as WGL.[455] Although this recommendation fell below the range of ROEs commonly authorized by regulatory commissions, OPC argued that deviation from prevailing norms was appropriate where supported by the record.[456] OPC urged that the Commission's determination should be based on the specific facts of the case rather than relying on past decisions or outcomes in other jurisdictions.

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[450] *Id*. at 6.
[451] *Id*.
[452] *Id*. at 7.
[453] *Id*.
[454] *Id*.
[455] *Id*. at 8.
[456] *Id*.

Furthermore, OPC argued that WGL erred in its DCF and CAPM modeling that estimates a cost of equity for its proxy group. By using five-year growth rates OPC contended that WGL's DCF models were too short of a timespan to represent a growth rate expected to last in perpetuity.[457] OPC concluded that growth rates cannot exceed the growth rate of the overall economy in which they operate and thus, WGL's DCF calculations create a cost of equity far above what is deemed normal.[458] Similarly, OPC asserts that WGL's CAPM modeling is flawed because it uses the same DCF model as an input to the CAPM and subjects the final figures to the same flaws inherent in the DCF models.[459] Finally, OPC argued that WGL's Risk Premium calculations were inherently unreliable.[460]

Finally, OPC contended that empirical evidence, including analyses from investment firms and academic research, indicated that the appropriate cost of equity for WGL was materially below the typical 9–10% range.[461] Accordingly, setting an ROE above Mr. Lin's recommendation would result in an unjustified transfer of wealth from ratepayers to shareholders.[462] As a result, OPC proposed that the "Commission should set the ROE near the utility's market cost of equity." This, in collaboration with affordability concerns, OPC argued, justified the Commission lowering ROE to better align with market-based expectations and reduce the burden on customers.[463]

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[457] OPC Direct Lin at 42-43.
[458] *Id*. at 43.
[459] *Id*. at 48.
[460] *Id*. at 41-42.
[461] OPC Initial Brief at 10.
[462] *Id*.
[463] *Id*. at 10-11.

Staff

Staff witness Manka proposed a ROE of 9.40%, but on surrebuttal revised his recommendation to 9.50% based on updated inputs into his CAPM model.[464]

To arrive at his recommendation, Mr. Manka relied upon analysis of a proxy group using the constant growth DCF model and the CAPM. As inputs to the DCF model, Mr. Manka used EPS from Value Line, Zacks, and Yahoo Finance, the average stock price over 180 days, dividend growth data from Value Line, and one year of dividend data.[465] As inputs to the CAPM model Mr. Manka relied upon the BlueChip 30-year U.S. Treasury Bond yield average forecast from 2026 through 2030, value line betas based on the Blume adjustment and the S&P betas based on the Vasicek adjustment, and the historical equity risk premium.[466] In both the DCF and CAPM Mr. Manka excluded results below 7% or above 14% over concerns of either being too low to attract investors or too high for an investor to reasonably expect to earn from a regulated utility.[467]

Staff noted a shared reliance on the same proxy group to estimate the Company's ROE with WGL, but Staff expanded the proxy group to include Chesapeake Utilities Corporation ("Chesapeake").[468] Staff observed that WGL opposed Chesapeake's inclusion on the grounds that only slightly more than half of its regulated operating income is derived from gas distribution operations and because it lacked credit ratings from S&P Global and Moody's.[469] Staff, however, responded that because the regulated gas income is above 50%

[464] Staff Surrebuttal Manka at 14-15.
[465] Staff Direct at 15-16.
[466] *Id*. at 17-19.
[467] *Id*. at 17 and 19-20.
[468] Staff Initial Brief at 60.
[469] Staff Surrebuttal Manka at 8. *See also* Staff Initial Brief at 60-61.

and faces similar regulatory risk as WGL in Maryland, it should be included.[470] Staff also argued that a larger proxy group improves analytical reliability by reducing the risk that any single company disproportionately influences the overall ROE results.[471]

Staff supported the use of an 180-day stock price averaging period to calculate the dividend yield, in contrast to WGL's reliance on shorter averaging periods for the DCF.[472] Staff argued that a consistent 180-day period—specifically September 8, 2025 through March 4, 2026—strikes an appropriate balance between mitigating short-term market volatility and avoiding outdated data.[473] Staff further noted that this approach aligns with investor practices, such as reliance on longer-term moving averages, and is particularly appropriate given recent market volatility.[474]

Furthermore, Staff rejected WGL's approach of annualizing the most recent dividend and instead calculated dividend yield based on dividends paid over the prior twelve months, adjusted for expected growth.[475] Staff contended that this method better reflects actual investor experience and captures potential variability in dividend payments, including the possibility of decreases.[476] By incorporating a full year of dividend data and applying a forecasted growth rate, Staff asserted that its approach more accurately reflects forward-looking investor expectations.[477]

Additionally, Staff explained that WGL relied on the same earnings per share ("EPS") growth forecasts in developing the DCF growth component, although they used

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[470] Staff Surrebuttal Manka at 8-9.
[471] Staff Initial Brief at 61.
[472] *Id*.
[473] *Id*.
[474] *Id*.
[475] *Id*. at 62.
[476] *Id*.
[477] *Id*.

slightly different data sources.[478] Staff observed that WGL relied on forecasts from S&P Capital IQ, Zacks, and Value Line, while Staff relied on Yahoo Finance, Zacks, and Value Line.[479] Despite these differences, Staff agreed that the use of EPS growth forecasts is appropriate, as investors routinely rely on such projections when evaluating expected returns.[480]

Mr. Manka noted that the primary difference from the Company's CAPM was due to witness Manka's use of Vasicek-adjusted betas and because WGL witness Nowak used a market risk premium derived from all S&P 500 companies.[481] Also, Mr. Manka noted that Mr. Nowak's CAPM results would have been more similar had they both utilized the FERC methodology for estimating market risk premiums.[482]

Mr. Manka responded to criticism of his CAPM model in surrebuttal regarding the use of Vasicek betas and his historical market risk premium. Regarding the Vasicek betas, Mr. Manka argues that witness Nowak did not provide much support for not using them. He notes that the argument regarding utilities being just as risky as other industries during economic crisis does not apply, as his five-year period did not include a financial crisis. Also, he argued that the Vasicek betas allows for better industry analysis since assuming all betas trend toward 1.0 creates an upward bias and that they should be considered with the Bloom betas.[483] Mr. Manka did update his historic market risk premium to the more recent value identified by the Company but continued to disagree with the projected market

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[478] Staff Direct Manka at 16. *See also* Staff Initial Brief at 62.
[479] *Id*.
[480] *Id*.
[481] Staff Direct Manka at 24-25. Staff Surrebuttal Manka at 12.
[482] Staff Direct Manka at 24-25.
[483] Staff Surrebuttal Manka at 13.

return premised upon all S&P 500 companies, as the included companies that do not pay dividends are not useful for comparison.[484]

Staff emphasized that the CAPM should be applied using well-supported, independent inputs and consistent with prior Commission precedent.[485] With respect to the CAPM beta, Staff supported the use of both the Blume and Vasicek adjustments, while WGL relied only on Blume-adjusted betas developed by Bloomberg and Value Line.[486] Staff explained that the Blume adjustment appropriately reflects the tendency of stock betas to move toward the broader market over time, but argued that the Vasicek adjustment is also necessary to reflect movement toward the industry mean—particularly for utilities, which typically exhibit betas below 1.0.[487] Staff maintained that relying solely on the Blume adjustment biases results upward by pulling utility betas toward 1.0, whereas the Vasicek adjustment better captures the lower-risk profile of regulated utilities.[488] Staff further noted that WGL failed to provide evidentiary support for its claim that utility betas align with the broader market during periods of financial stress.[489]

Regarding the ERP, Staff rejected WGL's use of a forward-looking market return derived from a DCF analysis of S&P 500 companies and instead relied on a historical ERP published by Kroll.[490] Staff argued that the use of a historical ERP is supported by Commission precedent, including its acceptance in a prior Columbia Gas of Maryland ("Columbia Gas") rate case, and provides a more stable and transparent basis for estimating

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484 *Id*. at 13-14.
485 Staff Initial Brief at 63.
486 *Id*.
487 *Id*.
488 Staff Direct Manka at 18. *See also* Staff Initial Brief at 63.
489 Staff Initial Brief at 63.
490 *Id*. at 64.

market returns.[491] Staff further emphasized that the CAPM should not incorporate the DCF model to derive the market return, as WGL's approach effectively applies the DCF methodology twice—once as a standalone model and again within the CAPM—contrary to the Commission's practice of relying on multiple distinct models that capture different financial perspectives.[492]

Furthermore, Mr. Manka argued against Mr. Nowak's RPM.[493] Staff asserted that the RPM is an inferior methodology that depends on authorized ROEs from other jurisdictions rather than market-based data.[494] Staff noted that the Commission has previously rejected this model, including in a Columbia Gas proceeding, where the Commission adopted an ROE based solely on DCF and CAPM analyses.[495] Staff contended that the CAPM already captures the relationship between equity and debt costs in a more rigorous and market-oriented manner, rendering the RPM unnecessary and duplicative.[496]

Finally, Staff rejected any upward adjustment to ROE based on WGL's relatively smaller market capitalization.[497] While WGL argued that its smaller size increases business and credit risk and therefore justifies a higher ROE, Staff pointed to prior Commission decisions rejecting similar size-based adjustments.[498] In particular, the Commission has found that the risks associated with smaller companies in competitive markets do not translate to regulated utilities, which benefit from monopoly service territories and stable

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[491] *Id*.
[492] *Id*.
[493] Staff Direct Manka at 32-34. *See also* Staff Surrebuttal at 15-16.
[494] Staff Initial Brief at 65.
[495] *Id*.
[496] *Id*.
[497] Staff Direct Manka at 27-29. *See also* Staff Surrebuttal Manka at 17-18, and Staff Initial Brief at 66.
[498] Staff Initial Brief at 67.

customer bases.[499] Staff argued that this precedent applies equally here and supports rejection of WGL's proposed size adjustment.[500]

MEA

MEA witness Kihm recommended an ROE of 9.0% for WGL, which was lower than both the Company's requested ROE and its currently authorized level.[501] When arriving at Mr. Kihm's recommended ROE of 9.0%, MEA noted the need to "create an incentive for the utility to invest capital and innovate, but we do not want to burden consumers with an unnecessarily high ROE."[502] Additionally, Mr. Kihm recognized the importance of gradualism and the need for moderate changes.[503]

Mr. Kihm distinguished between ROE and the cost of equity, estimating WGL's cost of equity at approximately 7.8%, and asserted that the Company's criticisms of his analysis were unsupported by evidence.[504] Mr. Kihm argued that the cost of equity represents the "minimum threshold ROE that a company must exceed to create value for its existing investors" and that "setting the ROE at the cost of equity will drive the utility stock price to book value and eliminate the incentive for management to invest more equity capital."[505] Additionally, Mr. Kihm explained his methodology in calculating cost of equity, stating he is "looking for a low number, a figure that if applied as the ROE would drive the utility stock price to book value and would eliminate the incentive for the utility

499 *Id*.
500 *Id*.
501 MEA Initial Brief at 11.
502 MEA Direct Kihm at 29.
503 *Id*.
504 MEA Initial Brief at 11.
505 MEA Direct Kihm at 5.

to invest capital."[506] Furthermore, Mr. Kihm expanded on the theory that a fair ROE is not based on a mathematical formula or equation that can lead to a correct ROE, but rather a public policy matter."[507]

Analytically, to arrive at his cost of equity of 7.8%, Mr. Kihm used a three-stage DCF model and the CAPM model, both based on the proxy group utilized by WGL witness Nowak.[508] For the three-stage DCF model, Mr. Kihm utilized the stock price as of March 13, 2025, ValueLine projected dividends per share ("DPS") for the short-term growth rates, and for the long-term growth rate he used a low and a high scenario of 4% and 5% respectively to represent gross-domestic product ("GDP") growth.[509] MEA stated the average results of this model for the individual companies are 6.5%-8.4% with the median of 7.7%.[510] Mr. Kihm criticized the Company's decision to use a single-stage or "constant growth DCF model" because of its simplistic assumption to use analyst near-term growth rates.[511]

For the CAPM model, Mr. Kihm used a 10-year Treasury yield for the risk-free rate, betas from Value Line and Zacks Investment Research, and a market cost of equity for the S&P 500 of 9.2%.[512] In calculating the 9.2% cost of equity, Mr. Khim added a 2.2% inflation adjustment to the 7% cost of equity, which was based on S&P 500 data.[513] Subsequently, Mr. Khim noted that other expert estimates ranged from 8.3%-9.9%.[514] As

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506 *Id*. at 18.
507 *Id*. at 18, 20 and 28-31.
508 *Id*. at 17.
509 *Id*. at 21.
510 *Id*. at 22 and SK-2.
511 *Id*. at 39.
512 *Id*. at 25.
513 *Id*. at 22-23.
514 *Id*. at 23-24.

a result, Mr. Khim claimed witness Nowak's S&P 500 cost of equity estimate was unreasonable.[515] Mr. Khim argued Mr. Nowak's value artificially inflates the results by 330 basis points.[516]

Mr. Kihm testified that an ROE of 9.0% satisfied the legal standards established in *Bluefield* and *Hope*, including the requirements to maintain financial integrity, attract capital, and ensure comparability with investments of similar risk.[517] Mr. Kihm pointed to strong market indicators—such as gas utility stocks trading above book value—as evidence that investors continued to view the sector favorably and that access to capital was not at risk.[518] Furthermore, he emphasized that maximizing shareholder returns was unnecessary and that an ROE materially above the cost of equity was unjustified.[519]

MEA also rejected WGL's claims that reducing ROE would increase costs to customers or discourage investment.[520] In contrast, Mr. Kihm emphasized that regulated utilities remain obligated to meet demand and cannot withhold necessary investments based on ROE levels.[521] He cited empirical evidence showing that utilities have continued to increase capital spending even after ROE reductions, undermining the Company's assertions.[522]

In addition, MEA addressed concerns regarding potential market value impacts, noting that the U.S. Supreme Court in *Hope* upheld regulatory actions that significantly

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[515] *Id.*at 41.
[516] *Id*. at 37.
[517] MEA Initial Brief at 11.
[518] *Id*.
[519] *Id*. at 11-12.
[520] *Id*. at 12.
[521] *Id*.
[522] *Id*.

reduced utility earnings and could result in stock price declines.[523] Mr. Kihm argued that such outcomes do not invalidate regulatory decisions and, in fact, reflect the proper functioning of capital markets.[524]

Finally, MEA highlighted the distinction between ROE and the cost of equity, cautioning that conflating the two leads to unreasonable ratemaking outcomes.[525] Mr. Kihm explained that while the cost of equity reflects investor expectations, ROE is a regulatory construct, and value is created only when ROE exceeds the cost of equity.[526] MEA concluded that the Commission should adopt an ROE of 9.0% as proposed by Mr. Kihm.[527]

AOBA

AOBA witness T. Oliver proposed the Company be awarded a ROE of 9.40%.[528] Mr. T. Oliver raised concerns that there is a lack of comparable data on which to determine an ROE due to most utilities being part of holding companies.[529] Also, AOBA criticized the objectivity of organizations, rating agencies, and the Security Exchange Commission such that there is a gap in data.[530] As a result, Mr. T. Oliver proposed that "the assessment of the Company's return requirements be guided by commission precedent, common sense, and historical perspective" and that a reliable quantitative analysis does not exist.[531]

Mr. T. Oliver argued the Company's ROE analysis was flawed, due to the small size of the proxy groups, the use of holding companies, availability of data for proxy group

[523] *Id*. at 12-13.
[524] *Id*. at 13.
[525] *Id*.
[526] *Id*.
[527] *Id*. at 16.
[528] AOBA Direct T. Oliver at 16.
[529] *Id*. at 26.
[530] *Id*. at 27.
[531] *Id*. at 28.

ROE analysis, and lack of detailed beta explanations.[532] Additionally, Mr. T. Oliver claimed WGL witness Nowak's Bond Yield Plus Risk Premium model was problematic because there was a change in utility risk profiles over the regression period.[533]

As a result, AOBA argued that WGL's requested ROE of 10.85% was excessive, unsupported, and inconsistent with the Commission's policy of gradualism.[534] AOBA contended that the Company's overall cost of capital proposal—including its equity-heavy capital structure and lack of transparency regarding debt costs—would inappropriately shift financial risks and costs to ratepayers rather than reflect the Company's actual regulated utility operations.[535]

Additionally, AOBA expressed concern that WGL's ROE analysis relied on market data from diversified utility holding companies rather than the risk profile of WGL's regulated gas distribution business.[536] Because WGL was no longer a standalone, publicly traded entity and obtained financing through its parent, AltaGas, AOBA proposed that available market data reflected higher-risk, non-regulated activities and therefore overstated the appropriate cost of equity for the utility.[537] AOBA emphasized that holding companies typically operated with greater leverage and broader business risks, making them inappropriate proxies for a regulated utility with a stable, monopoly service territory.[538]

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[532] *Id*. at 32-37.
[533] *Id*. at 37-39.
[534] *Id*. at 15-16. *See also* AOBA Initial Brief at 11.
[535] AOBA Initial Brief at 11. *See also* AOBA Direct T. Oliver at 45-46.
[536] AOBA Initial Brief at 11-12.
[537] *Id*. at 12.
[538] *Id*.

AOBA further cautioned against mechanical reliance on traditional ROE models—such as the DCF, CAPM, and Risk Premium approaches—when their inputs were derived from non-comparable holding company data.[539] AOBA emphasized that this practice risked inflating customer rates by embedding parent-company financial objectives into utility ratemaking.[540]

To address these concerns, AOBA recommended a 9.40% ROE, which it described as a measured and gradual adjustment that reflected the lower-risk nature of regulated utility operations while maintaining consistency with prior Commission decisions.[541] AOBA also rejected the notion that rates should ensure achievement of specific earnings targets, emphasizing that utilities were entitled only to a reasonable opportunity—not a guarantee—to earn their authorized return.[542]

Finally, AOBA asserted that the *Hope* and *Bluefield* standards must be applied to the regulated utility itself, not to its parent company.[543] Given the limitations of modern market data, AOBA argued that proxy group analyses should be treated with caution, as they no longer reliably reflected the cost of equity for standalone regulated utilities like WGL.[544]

**<u>Commission Decision</u>**

A public utility must charge just and reasonable rates for the regulated services that it provides.[545] Pursuant to well-established regulatory principles, regulated utilities are

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[539] *Id*. at 12-13.
[540] *Id*. at 13.
[541] *Id*.
[542] *Id*. at 13-14.
[543] *Id*. at 14.
[544] *Id*.
[545] A "just and reasonable rate" is one that: (1) does not violate any provision of the Public Utility Article of the Maryland Code; (2) fully considers and is consistent with the public good; and (3) will result in an

allowed the opportunity to recover the costs of prudently incurred debt financing. U.S. Supreme Court precedent, primarily *Bluefield*[546] and *Hope*,[547] established a standard by which the Commission is to consider certain relevant factors when determining whether to allow a change in a utility's rates to allow the recovery of financing costs. In a proceeding involving a change in rate, the burden of proof is on the proponent of the change. Thus, in the instant matter, WGL bears the burden to support every element of its request for a rate increase.[548]

As an initial matter, the Commission reaffirms that the authorized ROE must strike a reasonable balance between investor and ratepayer interests. Specifically, it must provide the Company a reasonable opportunity to attract capital, maintain financial integrity, and ensure comparability with returns on investments of similar risk, while also protecting customers from excessive rates. No single financial model is dispositive; rather, the Commission evaluates the results of multiple methodologies, together with qualitative considerations, in arriving at a just and reasonable ROE. Also, the Commission recognizes that a utility's authorized ROE directly impacts the rates that are ultimately paid by customers. While the Commission is always cognizant of the affordability of rates, in reaching our decision, we must also consider a utility's ability to attract capital. A fair rate of return should balance all interest and ensure a utility is not making speculative profits.

operating income to the public service company that yields, after reasonable deduction for depreciation and other necessary and proper expenses and reserves, a reasonable return on the fair value of the public service company's property used and useful in providing service to the public. PUA § 4-201.

[546] *Bluefield Water Works and Improvement Co. v. Pub. Serv. Comm'n of W. Va*., 262 U.S. 679 (1923).

[547] *Federal Power Comm'n v. Hope Natural Gas Co*., 320 U.S. 591 (1944).

[548] PUA § 3-112.

The Commission has carefully reviewed the record evidence, including the competing ROE recommendations and supporting analyses presented by WGL, Staff, OPC, AOBA, and MEA. These proposals span a wide range—from OPC's 7.07%, MEA 9.0% (based on a range of 7.8% to 9.2%), AOBA 9.40%, Staff 9.50%, and WGL's requested 10.85%—and reflect differing views regarding proxy group composition, model inputs, and the appropriate application of the standards articulated in *Bluefield* and *Hope*. This is a very large range of potential outcomes, even more so once it is recognized that even within a witness's models there are a diverse set of outcomes.[549]

In the instant case, the Commission is persuaded that the recommendations of MEA (9.0%) and Staff (9.5%) set the most reasonable bounds of outcomes in the present case. After weighing the quantitative results and qualitative factors set forth in the record, the Commission concludes that lowering the authorized ROE modestly to 9.40% is justified.

While the Company correctly notes that interest rate conditions and capital market dynamics are relevant considerations, the record does not demonstrate that WGL's risk profile is sufficiently differentiated from its peers to justify an ROE materially different from recent authorized levels for comparable gas distribution utilities which the Company points out since January 2024 on average has been 9.70%.

Arguments were presented that suggest that if ROEs are lowered, this would not improperly harm the utility's ability to attract capital and there are valid measures of ROE on the record that indicate it could be lower. Economic indicators, such as interest rates, do imply an upward pressure and the Commission does not believe it is appropriate to engage

[549] *E.g.,* Staff's DCF model results range from 8.17%–10.35% and CAPM results range from 8.93%–10.20% (*see* Witness Manka Surrebuttal at ATTACHMENT ABM-1S). WGL's DCF results range from 9.83%–14.13%, CAPM results range from 11.65–12.31% and risk premium 10.39–10.47%.

in drastic modifications to the return at this time that may risk a credit downgrade and which would be contrary to the Commission's reliance upon gradualism. Therefore, the Commission finds a modest decrease in the ROE of 10 basis points to 9.40% to be appropriate at this time.

This ROE remains within the range of reasonableness indicated by the record and continues to satisfy the *Bluefield* and *Hope* standards that the ROE provides comparable returns investors expect to earn on investments of similar risk, is sufficient to ensure confidence in Washington Gas's financial integrity, and will enable investors to receive a fair return. Additionally, while this may be below the national average of ROEs awarded to gas companies cited by the Company, the Commission does not believe that this modest reduction will impact capital attraction requirements. Accordingly, the Commission finds that an ROE of 9.40% is just and reasonable and should be retained for purposes of setting rates in this proceeding.

### 2. Capital Structure

The Commission must determine the capital structure that provides a fair ROR and results in just and reasonable rates. In accordance with PUA § 4-201, a public service company shall charge "just and reasonable" rates for the regulated service that it provides.

WGL's most recently authorized capital structure is 42.81% long-term debt, 5.19% short-term debt, and 52% equity.[550] In this case, WGL has proposed a capital structure of 54.269% common equity and 44.687% long-term debt, and 1.045% short-term debt, which

[550] *In the Matter of Washington Gas Light Co.'s Application for Authority to Increase Rates and Charges for Natural Gas Services*, Order No. 90943 at 95, Case No. 9704 (Dec. 14, 2023).

the Company calculated using the four-quarter average of the Company's actual capitalization during the test year from December 2024 through September 30, 2025. In opposition, Staff, OPC, and AOBA proposed capital structures that reflected lower equity amounts and different long-term versus short-term debt amounts to account for their reductions to equity; these are reflected below:[551]

Table 5:
Capital Structure as Recommended by Parties

| | WGL[552] | Staff[553] | OPC[554] | AOBA[555] |
|---|---|---|---|---|
| Long-Term Debt | 44.687% | 44.99% | 46.955% | 50% |
| Short-Term Debt | 1.045% | 3.21% | 1.045% | 0% |
| Common Equity | 54.269% | 51.80% | 52.00% | 50% |

Washington Gas

WGL witness Burrows argued in favor of the Company's proposed capital structure of 44.687% long-term debt, 1.045% short-term debt, and 54.269% common equity.[556] Per its merger commitments, WGL observed that the Company must maintain an equity ratio between 48-55%.[557] Mr. Burrows explained that WGL sets the capital structure separate from its parent and is based on the need to fund utility operations and maintain efficient access to capital.[558] Mr. Burrows explained that, in the past, the Commission has used the

[551] MEA did not propose any adjustments to WGL's proposed capital structure.
[552] WGL Initial Brief at 9.
[553] Staff Surrebuttal Valcarenghi at 7.
[554] OPC Surrebuttal Lin at 7.
[555] AOBA Initial Brief at 16.
[556] WGL Direct Burrows at 2.
[557] *Id*. at 6.
[558] *Id*.

actual test year capital structure and presented an analysis of a peer group that had a mean equity ratio of 52.13% and a median ratio of 53.06%.[559] However, if only those companies of an A- credit rating were considered, then the ratio would be 54.00% for the mean and 54.86% for the median.[560] Mr. Burrows claimed the increase in equity from the previous case is to maintain favorable credit ratings and that the Company's equity ratio cannot go below a likely downgrade to the Company's credit rating.[561]

Mr. Burrows responded to the capital structure proposals of AOBA witness T. Oliver, OPC witness Lin, and Staff witness Manka. In response to Mr. T. Oliver, Mr. Burrows explained that the Company's proposal reflected the actual capitalization during the test year and aligned with peer utility practice.[562] By contrast, WGL argued that AOBA's proposal weakened cash flow-based credit metrics and could be viewed negatively by rating agencies.[563] Mr. Burrows also claimed AOBA's proposal lacked sensitivity and reflected a misunderstanding of credit market operations that could potentially weaken WGL's financials.[564] Additionally, WGL noted that weakening the Company's financial posture, with the plan to respond once negative consequences materialized, reflected an imprudent method of oversight.[565]

Mr. Burrows objected to Mr. Manka's use of a five-year average of the Company's end-of-year capital structures, instead of an annual test-year average.[566] WGL criticized the five-year average because it did not account for the seasonality of WGL's operations and

[559] WGL Direct Burrows at 12-13.
[560] *Id*. at 13.
[561] *Id*. at 15-16.
[562] WGL Rebuttal Burrows at 5.
[563] *Id*.
[564] *Id*.
[565] *Id*.
[566] *Id*. at 8

included years impacted by COVID within the five-year average.[567] Mr. Burrows also asserted Staff's proposal does not account for forward looking financial risk.[568] Mr. Burrows additionally disagreed with Staff's assessment of peers, noting that some of the peers have equity ratios above those examined by Staff, and if only those with A are considered, then the equity ratio aligns with that of the Companies.[569]

Mr. Burrows argued Mr. Lin's analysis of equity ratio and credit metrics minimizes consequences of regulatory decisions on credit quality.[570] Mr. Burrows claimed Mr. Lin provided no empirical evidence to support his recommendation.[571]

In conclusion, WGL emphasized that its proposed structure utilized established ratemaking methodology and relies on actual financial data, including adjustments to debt balances and a normalized treatment of short-term debt.[572] WGL further highlighted that the Commission has previously accepted this approach in prior cases, finding it to be representative of utility financing.[573] The Company maintained that its proposed capital structure appropriately reflects its cost of capital, supports access to financial markets, and enables the provision of safe and reliable service.[574] WGL also rejected concerns regarding affiliate influence, asserting that its capital structure is determined independently of its parent and remains within previously approved parameters in Case No. 9449, which

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[567] *Id*. at 8 and 11.
[568] *Id*. at 9-10.
[569] *Id*. at 12.
[570] *Id*. at 13.
[571] *Id*. at 15.
[572] WGL Initial Brief at 9-10.
[573] *Id*. at 10.
[574] *Id*. at 9.

required the Company to "maintain a common equity ratio between 48% and 55% under Merger Commitment 35."[575]

OPC

OPC witness Lin evaluated WGL's proposed capital structure, and proposed a competing capital structure of 46.955% long-term debt, 1.045% short-term debt, and 52.00% equity.[576] OPC opposed WGL's proposed capital structure, concluding that it is overly equity-heavy and imposes unjustified costs on ratepayers.[577] OPC noted that WGL's proposed equity ratio of 54.269 percent exceeds levels previously authorized by the Commission, including in WGL's most recent rate case where a lower equity ratio was rejected.[578] OPC explained that higher ROE calculations result in increased customer bills, and WGL's proposed 10.85% ROE is estimated to cost customers $13 million per year.[579] While acknowledging the Commission's general practice of relying on a utility's actual capital structure, OPC emphasized that deviations are warranted, claiming that WGL has not justified its request for a higher equity ratio.[580]

Staff

Staff witness Manka evaluated the Company's capital structure and proposed the Commission impute a capital structure based on "the average of WGL's actual end-of-year capital structure for the past five years."[581] Mr. Manka argued that this aligns with WGL's

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[575] *Id*. at 10.
[576] OPC Direct Lin at 7 and 52-54.
[577] OPC Initial Brief at 11.
[578] *Id*.
[579] OPC Direct Lin at 55.
[580] OPC Initial Brief at 11.
[581] Staff Direct Manka at 13.

typical capital structure instead of the one proposed by the Company and prevents recent or temporary changes in the capital structure from having an outsize impact on the longer-term capital structure.[582] Mr. Manka proposed the Company's equity structure is higher than typical, the result of recent developments, and higher than any awarded capital structure for WGL since 2011.[583] Also, Mr. Manka noted that Pepco's witness Burrows testified that a peer group had a mean equity percentage of 52.13% and a median of 53.06%.[584] He also emphasized that witness Nowak's proxy group had an average equity ratio of 48.89%.[585] Therefore, he recommends a capital structure of 51.80% equity, 44.99% long-term debt, and 3.21% short-term debt.[586]

Mr. Manka recognized that the Commission has previously approved utility capital structures based on the average of the quarterly capital structure in the test year, and the Commission has also deviated when a high equity ratio would put an undue burden on ratepayers.[587] For example, Staff observed that in Case No. 9651, the Commission found the Company's proposed capital structure was higher than its recent structure and those approved for other utilities.[588] Staff noted that the end-of-year equity in 2024 and 2025 was higher than any year since 2015.[589] In response to Mr. Burrow's argument for a higher equity capital structure due to recent market conditions, Mr. Manka argued that the conditions that lead to higher levels of equity (rising interest rates and regulatory lag) were

[582] *Id*.
[583] *Id*. at 14-15.
[584] *Id*. at 14.
[585] *Id*. at 14-15.
[586] *Id*. at 13.
[587] Staff Surrebuttal Manka at 4.
[588] *Id*. *See also In the Matter of Washington Gas Light Co.'s Application for Authority to Increase Its Rates and Charges*, Order No. 89799 at 13, Case No. 9651, (Apr. 9, 2021).
[589] Staff Surrebuttal Manka at 4-5. *See also* Staff Direct Manka, Attachment ABM-2.

not guaranteed to continue in the future.[590] Additionally, Staff proposed it is not guaranteed that the test year will be more similar to future years than the five-year average, noting the recent increase in equity levels.[591]

Also, Mr. Manka disagreed with Mr. Burrow's focus on proxy group companies that have the same credit rating as WGL instead of considering a broader proxy group of companies.[592] Staff noted that the proxy group is supposed to be a group of companies that are at similar risk, and believed Mr. Nowak's use of the entire proxy group instead of a subset with similar credit rating was more appropriate.[593] Staff observed that Mr. Nowak's entire proxy group average was 48.89%, which was below WGL's proposed equity level.[594]

Staff continued to oppose WGL's proposed capital structure methodology, concluding that reliance on a single-year, quarterly average produces an equity ratio that is unreasonably high and not representative of the Company's typical financing practices.[595] Staff emphasized that while the Commission has, in some instances, relied on test-year averages, it has also departed from that approach where an elevated equity ratio would impose undue costs on ratepayers.[596] Staff found that WGL's proposed 54.3% equity ratio is significantly higher than the Company's historical levels, exceeds peer group benchmarks, and reflects a recent upward shift driven in part by affiliate equity infusions.[597] Staff further noted that such infusions—particularly those occurring shortly before a rate case filing—can artificially inflate the equity ratio and, in turn, increase the authorized rate

[590] Staff Surrebuttal Manka at 5.
[591] *Id*.
[592] *Id*. at 6.
[593] *Id*. at 6-7.
[594] *Id*.
[595] Staff Initial Brief at 58.
[596] *Id*.
[597] *Id*. at 59-60.

of return.[598] Given the volatility of WGL's capital structure and the potential for parent-company influence, Staff supported the use of a five-year average capital structure, finding that it better reflects normalized conditions and protects ratepayers from unjustified costs.[599]

AOBA

AOBA witness T. Oliver claimed WGL did not justify the Company proposed capital structure, claiming that the company provided no quantitative basis to assess the cost reasonableness of WGL's financial strategy or analysis of alternate market conditions on financial options.[600] Mr. T. Oliver raised concerns that a capital structure with high equity could have adverse impacts due to: (1) increased revenue requirement, and (2) subsidization of non-regulated affiliates.[601] AOBA argued the Commission "should establish a capital structure that minimizes the capital costs imposed on Maryland ratepayers while preserving reasonable financial flexibility."[602] Furthermore, Mr. T. Oliver compared WGL's credit ratings and capital structure to its parent company AltaGas, and noted WGL has a stronger credit rating and is less leveraged.[603] AOBA postulated that the higher debt in AltaGas's capital structure could be used to leverage cheaper financing at the expense of Maryland ratepayers.[604]

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[598] *Id*. at 60.
[599] *Id*. at 58-60.
[600] AOBA Direct T. Oliver at 18.
[601] *Id*. at 19
[602] *Id*. at 21.
[603] *Id*. at 23-24
[604] *Id*. at 24.

In the interest of protecting Maryland customers, Mr. T. Oliver recommended that the Commission approve a 50% equity and 50% debt structure.[605] He averred that this ratio within WGL's merger commitments, would better protect customers, and has not been shown to impair access to capital.[606] Additionally, AOBA emphasized that the appropriate capital structure must be evaluated within the broader cost of capital framework, with a focus on balancing financing cost minimization, financial stability, and the avoidance of subsidizing non-regulated affiliates.[607] AOBA contended that WGL did not meet its burden of proof, as it provided no quantitative analysis demonstrating that its proposed equity ratio is necessary or results in least-cost financing.[608] AOBA further warned that an elevated equity ratio increases revenue requirements and may enable the Company's parent to benefit from greater leverage in non-utility operations at ratepayer expense.[609]

In conclusion, AOBA emphasized that the recommendation does not require WGL to utilize the proposed capital structure.[610] However, the Company's "management must be responsible for weighing the costs and benefits of deviations from the capital structure on which the Commission's cost of capital determinations and approved rates are based."[611] This is especially true when the proposed capital structure has not been proven to be necessary, and the least costly option for customers.[612]

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[605] *Id*. at 25.
[606] *Id*.
[607] AOBA Initial Brief at 15.
[608] *Id*. at 16.
[609] *Id*.
[610] *Id*.
[611] *Id*.
[612] *Id*.

## **Commission Decision**

The Commission must determine a capital structure that yields a fair ROR while ensuring that resulting rates are just and reasonable, consistent with PUA § 4-201. In making this determination, the Commission balances the utility's need to maintain financial integrity and access to capital with its obligation to protect ratepayers from excessive costs. Generally, the Commission will not impute a capital structure unless there is evidence that the actual capital structure would impose an undue burden on ratepayers. The record supports such action, and the Commission shall impute the Company's proposed capital structure by lowering the equity ratio to 52%.

WGL proposes a capital structure consisting of 54.269% common equity and 44.687% long-term debt, and 1.045% short-term debt, derived from a four-quarter average of its actual capitalization during the test year. The Company asserts that this approach reflects Commission precedent and accurately captures its cost of financing. However, the record demonstrates that WGL's proposed equity ratio is elevated relative to both its historical levels and those of comparable utilities, and is not sufficiently supported by evidence demonstrating that it minimizes costs to customers.[613]

The Commission is not persuaded that strict adherence to a test-year average is appropriate under the circumstances presented here. While the Commission has, in prior cases, relied on a utility's actual capital structure, it has also recognized that departures from this approach are warranted where the resulting equity ratio is unduly high and would impose an unnecessary burden on ratepayers. That concern is present in this case.

[613] Staff Initial Brief at 59-60.

The evidence shows that WGL's proposed equity ratio reflects a recent upward shift that the Commission is not yet convinced will continue into the future. While circumstances in 2024 may have warranted equity infusions, Staff persuasively demonstrated that in this instance a reliance on a single-year, quarterly average captures a period of atypically high equity levels, influenced in part by recent affiliate equity infusions. Such infusions, particularly when occurring proximate to a rate case filing, risk artificially inflating the equity component and, in turn, increasing the authorized ROR. The Commission finds that this volatility undermines the reasonableness of Washington Gas's proposed approach.

Accordingly, the Commission adopts Staff's recommendation to rely on a multi-year average capital structure in the instant case. The use of a five-year average better reflects normalized financing conditions, mitigates the effects of short-term fluctuations, and provides a more balanced and representative measure of the Company's capital structure over time. This approach appropriately protects ratepayers from bearing the costs associated with an inflated equity ratio while preserving the Company's ability to maintain financial stability and access to capital markets.

For these reasons, the Commission finds that Staff's proposed capital structure is just, reasonable, and consistent with the public interest, and it is therefore adopted. The Commission will make one slight adjustment such that the cost of equity represents 52%, long-term debt represents 44.89%, and short-term debt represents 3.11% of the capital structure. This results in a ROR of 7.22% when ROE is set at 9.40%.

The parties' rate base and ROR recommendations and the Commission's findings are reflected in the following table:

Table 6:
Rate of Return Comparison

| (000's) | WGL[614] | Staff[615] | OPC[616] | AOBA[617] | Commission Determined |
|---|---|---|---|---|---|
| Rate of Return | 8.069% | 7.26% | 5.96% | 7.06% | 7.22% |

The Commission believes these ratios fairly compensate Washington Gas and protect ratepayers, while allowing the Company to remain competitive in capital markets. As the Supreme Court stated in *Bluefield*:

> [a utility's] return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market, and business conditions generally.[618]

The Commission concludes that a rate of return of 7.22% satisfies these policy considerations underlying ratemaking.

614 WGL Initial Brief at 9.
615 Staff Surrebuttal Manka at 2.
616 OPC Surrebuttal Lin at 6
617 AOBA Initial Brief at 19.
618 *Bluefield Water Works, 262 U.S. at 693.*

### C. **Cost of Service Study**

The purpose of a cost-of-service study ("COS" or "COSS") is to determine the costs a customer class, or in some cases a jurisdiction, imposes upon a company. Costs may be directly assigned or allocated based upon various allocation methodologies. Once costs are assigned, then class (and jurisdictional) RORs can be developed, which are used to assign customer rates. The Commission uses the results from COS studies as a guide in developing appropriate customer class rates.[619] A Jurisdictional COSS ("JCOSS") is utilized for companies that operate over multiple regulatory jurisdictions and is used to correctly allocate the utility's overall costs to each individual jurisdiction, either through direct assignment or the use of allocators. The Class COSS ("CCOSS") estimates the ROR for each class and further determines the Relative Rate of Return ("RROR") based on the system average ROR for all customer classes. The COSS utilizes the principles of cost causation and gradualism when determining results.

#### 1. Jurisdictional Cost of Service

WGL

Company witness Nguyen prepared a per book jurisdictional cost of service study ("PBCOSA") for WGL's rate case. In her testimony, she described the process of performing the study, stating that the jurisdictional cost allocation study prepared for this case uses the same methods as prior Maryland rate cases, with one exception.[620] Ms. Nguyen noted a change in the jurisdictional allocation methodology since the Company's

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[619] *See BGE* Order No. 87591 at 170, *in Case No. 9406*, *In the Matter of the Application of Baltimore Gas and Electric Company for Adjustments to its Electric and Gas Base Rates*. (Jun. 3, 2016).
[620] Nguyen Direct at 28.

last rate case, changing utility income tax expense to an apportionment methodology to better align attributable income taxes to each jurisdiction.[621] Ultimately, Ms. Nguyen recommended the study be adopted.

Staff

In direct testimony, Staff witness Tiska briefly summarized the Company's PBCOSA but did not raise any issues.

**Commission Decision**

As the Company's PBCOSA is not contested, the Commission accepts the study. However, the Commission is concerned that costs for transmission and other plants outside of Maryland may be unfairly allocated to Maryland ratepayers. OPC raised its concerns in brief about 14 projects in Virginia and the District of Columbia with costs allocated to Maryland but where the benefits to Maryland ratepayers are unclear.[622] The Commission finds the concerns raised by OPC have merit. The JCOSS is a critical tool for evaluating these types of costs, but it must be calibrated appropriately. For WGL's next rate case, the Commission directs the Company to include in its JCOSS more detailed information on whether the plant is addition is intended to address a particular need in a single state or jurisdiction, how the Company identifies costs allocated to Maryland for plant located outside of the state, and how it quantifies the realized or anticipated benefits to Maryland ratepayers in relation to the costs.

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[621] *Id*. at 30.
[622] OPC Initial Brief at 31-36. OPC argued on brief that, because WGL has not shown how the projects bring specific benefits to Maryland ratepayers, the allocated costs for the 14 projects should be removed from WGL's rate base in this case. OPC Initial Brief at 36.

2. Class Cost of Service

Washington Gas

Company witness Fang testified that a CCOS study helps to guide the allocation of costs to serve individual customer classes, and that the development of CCOSSs consists of three steps (1) cost functionalization, (2) cost classification, and (3) cost allocation.[623] She noted that the first step, cost functionalization, identifies and separates plant and expenses into specific categories based on the various characteristics of utility.[624] The second step "cost classification, further separates the functionalized plant and expenses according to the primary factors that determine how costs are incurred." According to the National Association of Regulatory Utility Commission's ("NARUC") Gas Distribution Rate Design Manual, costs can generally be classified into three categories:

(1) Customer-related costs, which vary based on the number of customers served rather than the amount of utility service supplied;

(2) Energy/usage costs, which vary based on the quantity of gas used. Purchased gas cost is an example of an expense that is usage related; and,

(3) Demand/capacity costs, which vary with the size or quantity of plant or equipment.[625]

Regarding the cost allocation process, Ms. Fang testified that "to the extent possible, revenues, operating expenses, and rate base are directly assigned by customer class."[626] She also noted that "[i]n addition to customer sales revenues, the CCOSSs directly assigns forfeited discounts, reconnect revenues, returned check charges, service initiation charges, and field collection charges." Further, she indicated that an estimate of

[623] Fang Direct at 6.
[624] *Id*.
[625] *Id*. at 7.
[626] *Id*. at 8.

the distribution service investment cost applicable to the interruptible and special contract customers has been used to directly assign those costs."[627]

WGL has four broad customer class categories including:

> (1) Residential Service, which is "defined as service to customers for residential purposes by individual meter in a single-family dwelling, or in an individual apartment, or to not over three families served by a single meter (one customer) in a multiple family dwelling, or portion thereof." Residential customers are either Heating and/or Cooling ("H/C") or Non-Heating and Non-Cooling ("Non-H/C").
>
> (2) C&I Service, which is defined as service to commercial and/or industrial customers, including schools, churches, embassies, rest homes, boarding houses, rooming houses, etc., supplied through one meter or a battery of meters. C&I customers are also either H/C or Non-H/C.
>
> (3) Group Metered Apartment ("GMA") Service, which is defined as service applicable to any multiple-dwelling building or project comprised of four or more dwelling units (apartments) supplied through one meter or a battery of meters. GMA customers are either H/C or Non-H/C.
>
> (4) Interruptible Service which is service to any customer on an interruptible basis only where the Company has the right to curtail or interrupt delivery of gas whenever, in the sole judgment of the Company, gas is not available for delivery.[628]

The CCOSSs helps determine whether the rates charged by each class generate sufficient revenue to cover the costs of serving each customer class, including a fair return on capital.[629] Ms. Fang asserted that "[b]y ensuring rates accurately reflect the utility's cost of providing service, the design encourages responsible resource use and conservation, while minimizing cross-subsidies among customer classes."[630]

Ms. Fang testified that the Company filed three CCOSSs in this proceeding as directed by the Commission in Order No. 90943.[631] The three CCOSSs include (1) a

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[627] *Id*.
[628] *Id*. at 9-10.
[629] *Id*. at 13.
[630] *Id*. at 14.
[631] *Id*.

Coincident Peak-and-Annual ("CP&A") COSS which the Company continues to recommend; (2) a Non-Coincident Peak and Annual ("NCP&A") CCOSS; and (3) a "true" Non-Coincident Peak ("NCP") CCOSS.[632] She noted that the Company relied on the Weather Normalization Study sponsored by Company witness Raab for coincident peak ("CP") and NCP information based on Staff's recommendation in Case No. 9704.[633]

Ms. Fang explained that a "composite peak and annual" factor blends a measure of peak demand for each class with annual throughput for each class to allocate costs associated with distribution mains.[634] She stated that CP is a single system-wide peak, while NCP uses each class's individual peak.[635] She noted that in accordance with Staff's recommendations from Case No. 9704, the Company's NCP-CCOSS in this proceeding includes for the allocation of mains a demand only allocation factor, based on NCP, that includes interruptible customers.[636] Moreover, she noted that the major allocators used in previous cases–combination of customers and normal weather throughput and peak usage–were applied in the current proceeding.[637] However, she indicated two proposed changes to the previous allocators with the intention to move to more cost-based allocations factors for the following costs: (1) Distribution House Regulators, and (2) Operations component of Materials and Supplies.[638] She testified that these proposed changes to the allocation factors have no material impact on the CCOSS results.[639] Specifically, she argued that "distribution house regulators and the operations component of materials and supplies

[632] *Id*.
[633] Id.
[634] *Id*. at 15.
[635] *Id*.
[636] *Id*.
[637] *Id*. at 16.
[638] *Id*. at 17.
[639] *Id*. at 18.

represent approximately 1.5% of total rate base addressed in the CCOSS and therefore do not have a material impact on the results for revenue apportionment to customer classes of rate design."[640]

Based on the Company's evaluation of the three CCOSSs, Ms. Fang testified that the Company recommends utilization of the CP&A method in this case for the following reasons. First, CP reflects customer needs. "That is, the Company's customers across all classes are primarily heating customers and therefore winter peaking. As a result, customer needs are well represented by a CP and a NCP is not needed." Second, CP reflects the design of the gas system. Third, "CP&A provides a reasonable allocation to Interruptible customers."[641]

In rebuttal testimony, Ms. Fang updated the Company's recommended CCOSS tables based on updated revenue requirement figures in corrected testimony from Company witness Banks.[642]

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[640] *Id*.
[641] *Id*. at 19.
[642] Fang Rebuttal at 6.

Table 7:
Comparison of Direct and Corrected CCOSS Rate of Return[643]

| | CP&A | | NCP&A | | NCP | |
|---|---|---|---|---|---|---|
| | From Direct | Corrected | From Direct | Corrected | From Direct | Corrected |
| **Earned Return** | | | | | | |
| **Residential** | | | | | | |
| H/C | 4.67% | 4.20% | 4.69% | 4.22% | 4.53% | 4.07% |
| Non-H/C | 3.10% | 2.80% | 3.12% | 2.81% | 3.11% | 2.80% |
| **C&I** | | | | | | |
| H/C <3,000 | 5.59% | 5.04% | 5.66% | 5.10% | 5.24% | 4.73% |
| H/C ≥ 3,000 | 5.23% | 4.54% | 5.10% | 4.42% | 5.51% | 4.78% |
| Non-H/C | 1.56% | 1.07% | 1.63% | 1.13% | 2.10% | 1.53% |
| **GMA** | | | | | | |
| H/C | 3.82% | 3.28% | 3.91% | 3.36% | 4.00% | 3.43% |
| Non-H/C | 6.00% | 5.18% | 6.03% | 5.21% | 8.04% | 6.96% |
| **Interruptible** | 5.43% | 3.89% | 5.43% | 3.89% | 5.98% | 4.34% |
| **Total** | 4.70% | 4.14% | 4.70% | 4.14% | 4.70% | 4.14% |
| **Relative Rate of Return** | | | | | | |
| **Residential** | | | | | | |
| H/C | 0.99 | 1.02 | 1.00 | 1.02 | 0.96 | 0.98 |
| Non-H/C | 0.66 | 0.68 | 0.66 | 0.68 | 0.66 | 0.68 |
| **C&I** | | | | | | |
| H/C <3,000 | 1.19 | 1.22 | 1.20 | 1.23 | 1.11 | 1.14 |
| H/C ≥ 3,000 | 1.11 | 1.10 | 1.08 | 1.07 | 1.17 | 1.16 |
| Non-H/C | 0.33 | 0.26 | 0.35 | 0.27 | 0.45 | 0.37 |
| **GMA** | | | | | | |
| H/C | 0.81 | 0.79 | 0.83 | 0.81 | 0.85 | 0.83 |
| Non-H/C | 1.28 | 1.25 | 1.28 | 1.26 | 1.71 | 1.68 |
| **Interruptible** | 1.15 | 0.94 | 1.15 | 0.94 | 1.27 | 1.05 |
| **Total** | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 |

OPC

OPC generally agrees with WGL's proposal to utilize the CP&A approach.[644] However, OPC witness Brant testified that several key inputs supporting WGL's COSS– including weather normalization methodology, peak demand calculations, and service line

[643] *Id*. at 7.
[644] OPC Initial Brief at 57.

costs allocation methodology–do not accurately reflect current conditions and cost responsibility.[645]

OPC maintained that "the CP&A methodology appropriately recognizes that WGL designs its system to meet peak demand while also accounting for annual throughput to ensure that customers contribute to system costs based on their overall usage."[646] OPC argued that the Commission should approve CP&A but improve it by adopting OPC's recommended modifications to weather normalization, peak demand calculations, and service line cost allocation, better aligning the COSS with actual customer usage and cost-causation.[647]

Staff

Staff recommended that the Commission adopt the NCP CCOSS for class revenue allocation.[648] Staff noted that the NCP methodology is consistent with Commission precedent.[649] Moreover, in Surrebuttal testimony, Staff witness Tiska reiterated that the Company's NCP CCOSS better aligns with the design of the Company's system; allocates distribution mains more fairly and adequately, considering varying peak days between classes; and includes a demand only allocation factor that includes Interruptible customers.[650] For ratemaking purposes, Staff recommended the Commission use the Company's proposed NCP CCOSS as a guide in allocating the revenue requirement among the customer classes and in designing rates in this case.[651] Additionally, Staff found the

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645 *Id*.
646 *Id*. at 58.
647 *Id*.
648 Staff Initial Brief at 71.
649 *Id*.
650 Tiska Surrebuttal at 12.
651 *Id*.

changes WGL made to the allocators for Distribution House Regulators and the Operations component of Materials and Supplies are consistent with the principles of cost causation and should be accepted.[652]

AOBA

AOBA witness B. Oliver recommended that the Commission accept WGL's CP&A method as it reflects the factors that drive the largest components of system planning and plant investment decisions.[653] However, AOBA cautions that WGL's CP&A calculation has a flaw: it applies equal weight to CP demands and Average demands. Because the system's Annual Load Factor (the ratio of average daily use to peak day use) is only 25.7%, applying equal weighting significantly over-weights class contributions to average daily gas use and distorts true cost responsibilities.[654]

*a. Weather Normalization*

WGL

Consistent with the Company's past cases, WGL witness Raab testified that the Company calculates the normal weather throughput by first calculating Normal Weather Heating Days ("HDDs") using a least squares regression of temperature data dating back to 1871 for the Maryland area based on temperature records at Reagan National Airport.[655] Mr. Raab described the Company's process for converting the calendar year Normal Weather HDDs to a billing basis using the most current meter reading schedule, extracting

[652] Staff Initial Brief at 71.
[653] B. Oliver Direct at 44-45.
[654] *Id*. at 45.
[655] Raab Direct at 6.

36 months of usage and actual HDD data from the billing system by customer class, and performing a linear regression analysis to derive the weather sensitivity coefficient and base use factor.[656] He noted that these factors are applied to test year data in order to determine total normal weather throughput by customer class.[657] Regarding the use of 2024 annual versus 2025 monthly HDD estimates, Mr. Raab explained that WGL uses 2024 across jurisdictions. Mr. Raab noted that the Company uses annual estimates to maintain reasonably consistent estimates of weather-normal billing determinants across all jurisdictions it serves for jurisdictional cost of service studies, and that deviating for Maryland could distort the allocation of costs across its service territory jurisdictions.[658]

In Rebuttal, Mr. Raab agreed with OPC's observation regarding the climate trends of warmer weather (discussed below), but argued that OPC witness Brant had not demonstrated that his recommendation would result in a significant change compared to the Company's long-standing approach.[659] For instance, Mr. Raab demonstrated that Mr. Brant's recommended approach would only alter the estimated normal HDDs by 3.8% and shift the Residential Heating and Cooling Class allocation by less than 1%.[660] Therefore, Mr. Raab asserted changing the methodology is not necessary. However, he conducted an independent analysis evaluating shorter periods for weather normalization and found that the best sample size for purposes of determining normal weather is clustered around 20

[656] *Id*. at 7.
[657] WGL Initial Brief at 63.
[658] *Id*. at 64.
[659] Raab Rebuttal at 5.
[660] *Id*.

years—not the 40 years Mr. Brant recommends.[661] The Company indicated that it would not be opposed to presenting its analysis in the next base rate application.[662]

<u>OPC</u>

OPC argued that WGL's weather normalization methodology does not adequately account for the impacts of climate change and therefore overstates normal-weather related gas usage.[663] OPC witness Brant criticized WGL's approach because it relies on more than 150 years of historical weather data, which biases the analysis toward colder temperatures that no longer reflect current climate conditions.[664] Mr. Brant argued that WGL's weather normalization method inflates billing determinants and over-allocates the Company's revenue requirement to weather-sensitive customer classes, such as residential and small commercial heating customers.[665] OPC recommended WGL modify its methodology by using a shorter and more representative weather dataset and by calculating normal weather based on the rate case test year rather than calendar year 2024.[666] OPC argued that "[t]hese changes would better reflect current weather patterns, improve the accuracy of cost allocation, and more closely align rates with cost causation principles."[667]

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[661] WGL Initial Brief at 64.
[662] *Id*. at 63.
[663] *Id*. at 58.
[664] *Id*.
[665] Brandt Direct at 11-12.
[666] OPC Initial Brief at 59.
[667] *Id*.

Staff

Staff recommended that the Commission direct WGL to conduct a detailed analysis of the appropriate length of historical weather data to be used in the regression analysis for the weather normalization study.[668]

AOBA

Witness B. Oliver expressed several concerns with WGL's Normal Weather Study including the following: (1) "comparatively weak correlations developed between weather sensitive gas use and heating degrees day measures for the Company's largest gas users (*i.e.*, its Interruptible Service customers and National Institute of Health ("NIH"), the Company's one very large C&I Non-Heating customer);" (2) the unexplained and loss of over 4 million therms of gas use for NIH in WGL witness Raab's process of converting billed usage to weather gas volumes; and (3) billing data inconsistencies that WGL relied upon to perform its regression analysis in this case and data for identical months used in the Company's regressions for the Normal Weather Study in Case No. 9704.[669]

*b. Peak Demand Calculation*

WGL

As noted in WGL's Initial Brief, the Company's peak demand calculation methodology is based on its system design parameters and engineering judgment of the temperature at which all temperature-sensitive appliances would be operating at full

[668] Staff Initial Brief at 72.
[669] AOBA Initial Brief at 33-34.

capacity.[670] The Company argues this approach ensures reliable system planning and is consistent with the Company's obligation to serve customers under peak conditions.[671]

OPC

OPC argues that the Commission should direct WGL to calculate both CP and NCP using actual load data, because actual customer usage data provides a more accurate measure of cost causation than theoretical design day.[672] OPC witness Brant argued that the allocation of costs based on estimated design day usage assigns costs based on conditions that may never occur during the test year, and can over allocate costs to weather-sensitive classes by assuming higher temperature-dependent usage than is actually experienced.[673]

AOBA

AOBA asserted WGL's design day and peak day assumptions contain flaws. First, AOBA pointed out that for the Interruptible Service class, the Company used a Peak and Annual Sales allocator that AOBA argues does not reflect the interruptible nature of these customers: because interruptible customers are assumed to be curtailed during design peak conditions, their gas load under Design Day Peak conditions should effectively be zero.[674] However, AOBA noted that WGL's methodology assigns them peak day demands, which improperly overstates their responsibility for the costs of distribution facilities.[675]

[670] WGL Initial Brief at 64.
[671] *Id*.
[672] OPC Initial Brief at 60.
[673] *Id*. at 61.
[674] B. Oliver Direct at 47.
[675] *Id*.

### *c. Service Line Allocator*

OPC

OPC recommended that the Commission revise the Company's service line cost allocation methodology by limiting the customer component of service lines to facilities measuring 0.75 inches or less.[676] OPC argued that treating larger service lines as customer-related facilities improperly assigns demand-related costs to all customers regardless of their usage characteristics and understates the cost responsibility of customers that require larger facilities. Thus, OPC asserted that by limiting the customer components to service lines of 0.75 inches or less, the Commission can ensure that service line costs are allocated more accurately and, in a manner, consistent with established cost allocation principles.[677]

WGL Rebuttal

WGL witness Fang's argued that the Company uses 1.25 inches lines to serve residential customers. Further, she asserted OPC's recommendation fails to recognize that residential customers are not allocated any portion of the higher-cost, demand related service lines greater than 1.25 inches.[678]

### *d. National Institutes of Health Customer Class*

WGL

WGL's CCOSS results were impacted by a significant reclassification of one customer during the test year. Witness Fang testified that the C&I Non-H/C class experienced a significant change in cost of service since the last rate case "due to the recent

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[676] OPC Initial Brief at 62.
[677] *Id*.
[678] Fang Rebuttal at 14.

migration of a large customer under a special contract to tariffed service as a C&I Non-H/C customer under Schedule 2/2A as of March 2025."[679] The large customer was identified as NIH. As discussed below in the section on rate design, moving NIH into the C&I Non-H/C class caused the class to go from over-earning relative to its own cost of service to significantly under-earning.[680] Rather than reclassify NIH and complete a COSS reflecting its costs separately, WGL proposes to address this intra-class issue by limiting the amount of revenue increase apportioned to that class.[681]

OPC

OPC witness Brant discussed WGL's inclusion of NIH into the C&I Non-H/C customer class and argued the Company's proposed limits to the revenue increase for that class would be inappropriate.[682] Mr. Brant asserts that the NIH issue is "a fundamental issue with the structure of the company's class definitions."[683] According to Mr. Brant, the Company's CCOSS shows the C&I Non-H/C class is heavily subsidized by other customer classes, and limiting its revenue increase to be less than increases to other low-performing classes would perpetuate inter-class cross-subsidization.[684] Mr. Brant argued that, to the extent the changes to the C&I Non-H/C CCOSS affect existing customers, the issue of intra-class cross-subsidization should be addressed through rate design and not revenue allocation.[685]

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679 Fang Direct at 23.
680 Fang Rebuttal at 21.
681 Fang Direct at 23. This revenue apportionment proposal is discussed in the section below.
682 Brant Direct at 31.
683 *Id*. at 31 and 38.
684 *Id*. at 31.
685 *Id*. at 26.

If the Commission cannot create a new rate schedule for NIH that accurately reflects its costs of service and ROR in this rate case–which witness Brant opines would be an appropriate solution–then intra-class cost-shifting should be addressed by rate design specifically within the C&I Non-H/C class.[686]

Staff

In Direct testimony, Staff witness Tiska analyzed the inclusion of NIH in the C&I Non-H/C class and found that the results suggest a material change in the class composition compared to the previous rate case.[687] She detailed a substantial decline in the class's RROR.[688] Ms. Tiska recommended that the Commission direct WGL to conduct a detailed analysis of customer class definitions and characteristics, with a focus on the C&I Non-H/C class.[689] She asserted that such analysis would be helpful to determine if it is appropriate to require WGL to change the rate classification for NIH. Staff agreed with WGL that this issue should be addressed in a future rate case to allow for consideration of customer impacts and understanding, and the collection and evaluation of customer usage data needed to support the analysis.[690]

AOBA

AOBA witness B. Oliver expressed great concern about the inclusion of NIH in the C&I Non-H/C class and argued that it distorts class cost results. He recommended the Company be required to create a separate rate class for NIH.[691] Mr. B. Oliver noted that

[686] *Id*. at 40.
[687] Tiska Direct at 29.
[688] *Id*. at 28.
[689] Staff Initial Brief at 72.
[690] *Id*.
[691] B. Oliver Surrebuttal at 20.

there are stark differences in usage characteristics between NIH and the other Maryland C&I Non-H/C customers, as summarized in the table below.

Table 8:
Comparison of C&I Non-H/C Class Usage Characteristics[692]

| | All Others | NIH |
|---|---|---|
| **Annual Therms per Customer** | 9,990 | 13,419,675 |
| **Peak Day Therms per Customer** | 944 | 224,409 |
| **Percent of Usage that is Base Gas** | 87.7% | 0.0% |
| **Percent of Usage that is Weather Gas** | 12.3% | 100.0% |
| **Annual Load Factor** | 62.0% | 16.4% |

As discussed further in the rate design section below, Mr. B. Oliver computed that the Company's test year revenues for NIH under the C&I Non-H/C rates under-recovered the Company's cost of service for NIH by $3.3 million, and he argued this was an avoidable result caused knowingly by WGL.[693] AOBA argues that the Commission must hold WGL accountable for its decision[694] and that other customers in the C&I Non-H/C class should not bear the burden of subsidizing NIH.

**Commission Decision**

The Commission accepts Staff's recommendation to maintain the NCP CCOSS methodology in the current proceeding. This method is consistent with the Commission's decision in the previous two rate cases for the Company where the Commission accepted the Company's NCP COSS and directed WGL to continue to provide both a CP and an

[692] B. Oliver Direct Table 1 at 30.
[693] B. Oliver Surrebuttal at 12-13.
[694] AOBA Initial Brief at 25-29.

NCP in future rate cases.[695] The Commission continues to maintain this same direction and ensure continuity with previous precedent that has found that this methodology best aligns with how customers use the system.

Regarding the weather normalization issue presented in this proceeding, the Commission accepts WGL's position maintaining the 2024 calendar year as OPC has not demonstrated that changing to the 2025 test year calendar would have a material impact on the allocation. However, recognizing present global climate changes, the Commission finds that conducting a regression analysis for a shorter period of time such as 20 years is appropriate at this time and directs WGL to present a detailed analysis of appropriate timeframes for its next rate case.

Regarding the peak demand calculation, the Commission accepts the Company's design day method which is consistent with the Commission's previous rate cases and reflects as argued by WGL the long-term system needs versus Actual CP and NCP advanced by OPC.

The Commission's decision regarding NIH is in the Rate Design section below.

### D. Rate Design

Rate Design involves two functions: (1) the design of inter-class rates, which involves the allocation of the utility's revenue requirement between the various customer classes, and (2) the design of intra-class rates, which involves the manner in which the apportioned class revenue requirement will be collected from customers. In order to

[695] Order No. 90943, Case No. 9704, *Washington Gas Light Company's Application for Authority to Increase Rates and Charges for Natural Gas Services,* (Dec. 14, 2023); Prop'd Order of the Pub. Util. Law Judge, Case No. 9651, *Washington Gas Light Company's Application for Authority to Increase its Rates and Charges* , 2021).

determine how much of any rate increase (or decrease) should be assigned to a particular customer rate class, the Commission first looks at the actual RORs for each class reflected in the CCOSS, expressed as a ratio of the class's operating income to its share of the distribution rate base. These results are then translated into a unitized ROR ("UROR", sometimes used interchangeably with RROR), expressed as a factor calculated by dividing the class ROR ratio by the utility's system average or overall ROR ratio.

The Company's system average ROR serves as the baseline for comparison of the class URORs, and thus is represented by a UROR of 1.0. A UROR greater than 1.0 signifies that a rate class has a return that is greater than the system average–*i.e.*, the class's income contribution exceeds its respective COS. A UROR that is lower than 1.0 indicates a class return that is less than the system average, indicating that the class's income contribution does not cover its respective COS. Customer rate classes with a UROR of 1.0 are contributing their "fair share" of income to the utility's overall ROR based upon their respective calculated COS.

The Commission uses the calculated URORs for each class to determine a just and reasonable apportionment of the overall revenue increase to each class. As a matter of policy, the Commission aims to bring all classes closer to a UROR of 1.0 in each rate case to ensure rates that better reflect the cost causation from each class. However, this goal must be tempered by the policy of gradualism in order to avoid rate shock to the customers of any particular rate class.

Once the revenue requirement is apportioned among the various classes, intra-class rates may be assigned. Almost all rate classes have a service charge, which is designed to recover fixed utility costs, such as the cost of meters. Additionally, Washington Gas customers have a distribution charge, which is designed to cover variable costs. That is, each customer's bill has a fixed, monthly customer charge and a volumetric, per-therm charge. Intra-class rate design is guided by important policy considerations, including gradualism, energy conservation, economic impacts, as well as cost causation.

### 1. Revenue Allocation Methodology

WGL

WGL witness Fang stated that the Company's proposed revenue allocation methodology is informed by fairness, cost-causation, stability, and understandability.[696] She discusses that while apportioning revenue on an equal percent basis is simple and understandable, it does not consider the costs of serving each class and may lead to cross subsidization.[697] However, Ms. Fang also found that a revenue apportionment based solely on achieving equal rates of return for all classes would result in wide disparities in rate impacts, with marginal revenue allocations by class ranging from one half to two times the system average increase.[698] In order to move towards parity in class rates of return without causing rate shock to any class, the Company proposes an allocation that moves classes towards an equalized rate of return but that limits the revenue increase to any one class to no more than 25% higher than the system average increase.[699] The Company's proposed

[696] Fang Direct at 19-20.
[697] *Id*.
[698] Fang Direct, Table 2 at 20-21. The system average increase depends on the CCOSS methodology and the total increase in revenue. WGL's initial application would have resulted in a system average increase in margin revenue of 20.2%.
[699] *Id*. at 23. Based on WGL's calculated system average, the increase cap would have been 25.25%.

moderation approach results in all classes–with the exception of C&l Non-H/C–achieving a parity ratio of no less than 5% below and no more than 3% above a 1.0 UROR.[700]

For the C&I Non-H/C class specifically, WGL proposes to further limit the apportioned revenue increase to no more than 5% above the system average.[701] As discussed in the CCOSS section above, Ms. Fang explained that this class has experienced a significant change to its cost of service since the last rate case due to the addition of NIH.[702] Until March 2025, NIH was being served under a special contract with a take-or-pay contract minimum therms per year. When NIH could no longer meet the terms of this contract, it expressed interest in moving to Interruptible service.[703] Instead, the Company determined that NIH met the definition of a C&I Non-H/C customer and opted to move NIH to tariffed service in that class.[704] WGL's decision to serve NIH in this class rather than Interruptible was driven by the stated desire to maintain system revenue and impose non-negotiated rate increases.[705]

Without NIH, WGL's CCOSS indicated that the C&I Non-H/C class was over-earning relative to its cost of service with a UROR of 1.63. On the other hand, when NIH was evaluated on its own it had a UROR of -0.55, showing significant under-earning relative to its cost of service.[706] When NIH is added to the C&I Non-H/C class, WGL's CCOSS yields a class UROR of 0.33–the lowest of any class–suggesting the class as a whole is underearning.[707] The Company's proposal to specially limit the revenue allocated

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[700] *Id*. at 24.
[701] *Id*. at 23.
[702] *Id*.
[703] WGL Response to Staff DR 16-3 and Tiska Direct Attachment Lt-1 at 39-40.
[704] Fang Rebuttal at 29.
[705] WGL Response to Staff DR 16-3 and Tiska Direct Attachment Lt-1 at 39-40.
[706] WGL Revised Response to AOBA Data Request 1-3 and B. Oliver Surrebuttal Exhibit BRO-SR2.
[707] Fang Rebuttal at 21.

to the C&I Non-H/C class intends to soften the blow to other customers caused by NIH, which is the "primary driver" of the class's total allocated revenue increase.[708]

The Company's proposed moderated approach in the current proceeding differs from the two-step 15/85 apportionment method used in Case No. 9704.[709] Ms. Fang explained that the 15/85 methodology focuses on incremental revenue allocations based on parity under current rates rather than parity under the updated CCOSS.[710] She argued that the Company's proposal in this case provides more transparency, brings all customer classes closer to parity, and applies appropriate moderation to mitigate customer impacts as needed.[711]

<u>Staff</u>

Staff witness Walton enumerated similar rate design goals to those of WGL witness Fang, with some notable differences. Mr. Walton testified that the primary criteria to be satisfied in rate design are fairness, simplicity, stability, and economic efficiency.[712] These goals add a focus on optimal usage of resources and reduction of waste.[713] Overall, Staff found WGL's allocation methodology flawed because it did not target under-earning classes, leading to unacceptably high inter-class subsidization.[714] Instead, Staff proposes the same two-step allocation methodology that was approved by the Commission in WGL's previous rate case, Case No. 9704.[715]

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[708] *Id*. at 23.
[709] *Id*. at 25.
[710] *Id*. at 27.
[711] *Id*.
[712] Walton Direct at 3.
[713] *Id*.
[714] *Id*. at 12.
[715] *Id*.

In the first step of Staff's proposed two-step allocation process, 15% of the total approved revenue increase is apportioned to under-earning classes based on their share of total revenues.[716] Staff includes in this category "the most under-earning classes", which witness Walton identifies in his Direct Testimony as C&I Non-H/C, RES Non-H/C, and GMA H/C,[717] with the addition of C&I RES H/C shown in his surrebuttal attachments.[718] In the second step, Staff distributes the remaining 85% of the revenue increase across all customer classes based on their share of total revenues, with the exception of any classes that already have an elevated UROR. On Direct, Mr. Walton's narrative testimony indicated that the GMA Non-H/C and Interruptible classes were excluded;[719] but in his updated surrebuttal attachment, witness Walton shows only GMA Non-H/C as excluded.[720] Staff concludes that this two-step allocation best addresses under-earning classes while also being consistent with the principle of gradualism.[721]

Notably, while WGL proposes to specially limit the revenue apportioned to the C&I Non-H/C class because of the NIH migration, Staff targets the C&I Non-H/C class for additional revenue allocation because of its low UROR. Staff acknowledges that NIH impacts the class's ROR and cost of service, but believes that the full extent of those impacts cannot be determined at this time.[722] Staff recommends that the Commission approve WGL's placement of NIH into the C&I Non-H/C class but that no allocation adjustments be made until additional analyses by WGL are performed.[723] As stated in the

[716] *Id*. at 13.
[717] *Id*.
[718] Walton Errata Surrebuttal at KW-S1.
[719] Walton Direct at 13-14.
[720] Walton Errata Surrebuttal at KW-S1.
[721] Walton Direct at 13.
[722] *Id*. at 11.
[723] *Id*. at 11-12.

CCOSS section above, Staff additionally recommends that the Commission order WGL to conduct a detailed study before its next rate case to determine the correct treatment for NIH.[724]

AOBA

Contrary to Staff's approach to NIH, AOBA witness B. Oliver's rate design puts front and center what he believes to be "the proverbial 'elephant in the room.'"[725] AOBA asserts that WGL's entire proposed allocation methodology is fundamentally flawed because NIH should not be classified as a C&I Non-H/C customer.[726] Mr. B. Oliver argues that NIH's usage characteristics, as summarized above in Table 8, differ so substantially from all of the other customers in the class that it was unreasonable to put them in that class in the first place.[727] Further, AOBA points out that WGL had more than adequate opportunity to analyze the issue and devise a solution for NIH through its "Study Reviewing Current Non-Residential Customer Class Definitions 2025"[728]–which was ordered by the Commission in WGL's previous rate case–but did not do so.[729]

Based on NIH's usage characteristic disparities and known cost of service data–which was provided by WGL to AOBA–AOBA asserts that WGL knew or should have known that including NIH in the C&I Non-H/C class would result in inadequate revenue recovery.[730] AOBA concludes that WGL's proposal results in substantial intra-class

[724] Tiska Surrebuttal at 12.
[725] B. Oliver Direct at 28.
[726] *Id*. at 28-29.
[727] Witness B. Oliver states that WGL provided no documentation justifying its classification, and that its determination was driven solely by potential loss of revenue if NIH was placed on interruptible service. Mr. B. Oliver Surrebuttal at 19.
[728] Fang Direct, Exhibit CSF-12.
[729] B. Oliver Direct at 26-28 and Surrebuttal at 18-19.
[730] B. Oliver Surrebuttal at 12.

subsidization of NIH by other members of the class, and would result in rates that are not just and reasonable.[731]

To ensure WGL's customers do not bear the costs of WGL's classification decisions, AOBA recommends that the Commission impute a level of base rate revenue to WGL's test year sufficient to raise NIH's ROR to the system average. As stated above in the CCOSS section, Mr. B. Oliver concludes that this would result in counting an additional $3.33 million towards test year base rate revenues, which would in turn lower the Company's revenue increase request by $2.4 million, adjusted for income taxes.[732]

In addition to AOBA's recommendation detailed above that the Commission reject NIH's classification in the C&I Non-H/C class and require WGL to establish a separate rate class for NIH,[733] AOBA states that until WGL is able to develop rates for NIH and obtain Commission authorization to charge them, NIH should be charged interim rates equal to those approved for other C&I Non-H/C customers, with WGL responsible for any costs attributable to serving NIH that it does not recover in that time.[734]

For purposes of revenue allocation across all classes, AOBA proposes that once adjustments are made for NIH and the C&I Non-H/C class, increases for all rate classes should be adjusted to achieve UROR parity ratios similar to those proposed by WGL.[735]

<u>OPC</u>

OPC also takes issue with WGL's treatment of NIH for the purposes of revenue allocation, as indicated above in the discussion on CCOSS. OPC witness Brant states that

[731] B. Oliver Direct at 28.
[732] B. Oliver Surrebuttal at 12-13.
[733] *Id*. at 20.
[734] *Id*. at 20-21.
[735] B. Oliver Direct at 51 and Direct Exhibit BRO-5.

by classifying NIH as a C&I Non-H/C customer and then artificially capping the percent of revenue increase allocated to that class, WGL perpetuates issues of class cross-subsidization.[736] Essentially, WGL's revenue allocation design makes what should be strictly an *intra*-class issue into an *inter*-class issue, forcing other classes to bear the burden of NIH's cost of service.[737] Mr. Brant asserts that the proper way to address the issues caused by NIH is through rate design, not revenue allocation.[738] As such, for purposes of revenue allocation, OPC proposes that the Commission adopt WGL's apportionment method without limiting the increase to the C&I Non-H/C class.[739]

WGL Rebuttal

WGL reiterates its position that a modified equalized ROR allocation methodology best achieves the goals of fair and efficient rate design. WGL says that Staff's proposed two-step allocation methodology, while providing some movement towards parity, does not achieve system-wide improvements that are as good as WGL's proposal without introducing offsetting distortions elsewhere.[740]

In response to AOBA's and OPC's separate but related concerns about WGL's treatment of NIH, witness Fang indicates that the Company stands by its classification of NIH because, disparate usage patterns notwithstanding, NIH meets the current definition of a C&I Non-H/C customer.[741] WGL asserts that it would need to carefully study NIH's usage characteristics, costs, and revenues in order to reclassify or create a new rate class,

[736] Brant Direct at 26-27.
[737] *Id*. at 38.
[738] *Id*. at 31 and 38.
[739] *Id*. at 34.
[740] Fang Rebuttal at 26.
[741] *Id*. at 28-29.

which it has not done for this rate case.[742] The Company thus recommends that the Commission approve its proposed treatment of NIH in the present case, and allow for the matter to be revisited in a future rate case after WGL has had the opportunity to conduct an appropriate study.[743]

As to OPC's recommendation that revenue increase allocated to the C&I Non-H/C not be limited, WGL responds that OPC's proposal would cause other customers in that class to be unfairly impacted by costs that they did not cause.[744] Further, WGL states that AOBA's recommendation that the Commission impute base rate revenue to cover NIH's cost of service is not consistent with any Commission policy or precedent,[745] and is "unsupported as a matter of fact and law."[746] The Company further suggests that imputing revenue would violate the "known and measurable" standard for test year adjustments because the revenues reflected in the Company's workpapers for NIH and for the C&I Non-H/C class are already based on actual data.[747]

**Commission Decision**

The Commission agrees with Staff that the two-step allocation methodology does a better job of addressing underearning classes than other proposals. The two-step allocation method approved in WGL's previous rate case provides a fair and

[742] *Id*. at 33.
[743] *Id*.
[744] *Id*. at 22.
[745] Banks Rebuttal at 8.
[746] WGL Reply Brief at 43.
[747] Banks Rebuttal at 8. On rebuttal, witness Banks also details a correction to NIH's test year revenue numbers necessitated by inaccurate calculations related to the Montgomery County Fuel Energy Tax, and states that this adjustment to the test year revenues addresses witness B. Oliver's concerns. Banks Rebuttal at 6-7. However, witness B. Oliver points out that the correction makes the difference between the rates of return for NIH and all other C&I Non-H/C customers during the test period even larger, so AOBA maintained its proposal. B. Oliver Surrebuttal at 17-18.

straightforward way for ensuring that underearning classes progress towards the system average rate of return without causing rate shock.

The Commission believes that the specific determinations documented in witness Walton's *narrative* Direct Testimony as to which customers should be included in step one and which customers should be excluded from any increase at all would create unreasonably high bill impacts for certain small classes. For example, under the proposal that the bottom three earning classes be included in step one and that two over-earning classes not be included in either step, the RROR for the RES Non-H/C class would almost double.

However, as indicated above, the Commission notes that witness Walton's surrebuttal workpapers–upon which Staff's proposed bill impacts are calculated– indicate a different revenue allocation. Attachment KW-S1 to Mr. Walton's Surrebuttal shows the four classes with a UROR less than 1.0 included in step one, and only one over-earning class receives no apportionment of the revenue increase at all. In the Commission's view, these differences lead to a much more equitable distribution of the revenue increase while still moving under-earning classes closer to the system average rate of return.

The Commission therefore adopts Staff's proposed allocation methodology as indicated in Attachment KW-S1 of Mr. Walton's Errata Surrebuttal Testimony, with one alteration. At a time when Maryland ratepayers are struggling with increasing household expenses across the board, the Commission finds it appropriate to prioritize the mitigation of customer bill impacts over other rate design goals to the extent that it is just and reasonable to do so. At this time, including all classes in step two in order to spread the revenue increase to a wider customer base still moves the highest over-earning class closer to a UROR of 1.0, though to a slightly smaller degree, and would lead to improved bill impacts for most classes. Though relatively small, these bill impact changes may make a meaningful difference to customers for whom every dollar counts. As such, the Commission approves a two-step allocation methodology materially similar to Staff's which apportions 15% of the overall revenue increase to the Res-H/C, RES Non-H/C, C&I Non-H/C, and GMA-H/C classes based on their proportion of overall revenue, and the remaining 85% of the overall revenue increase to all classes based on their proportion of overall revenue.

With respect to WGL's treatment of NIH, the Commission shares the concerns voiced by AOBA and OPC about NIH's classification in the C&I Non-H/C class and the resultant potential revenue allocation issues. While it may be technically true that NIH "took tariffed service for which it qualified,"[748] the validity of WGL's reliance on that statement is undermined by the fact that WGL completed a study on the appropriateness of its current non-residential class definitions that did not address NIH's circumstances, despite the issue being salient at the time the study was conducted.[749] Staff and AOBA each opined that WGL's study was deficient for this reason.[750]

The Commission finds this particularly problematic when viewed in the context of the Commission's order in Case No. 9704 that gave rise to the class definition study. The Commission ordered WGL to "conduct an analysis of current non-residential customer

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[748] WGL Reply Brief at 43.

[749] WGL knew NIH was not going to renew its special contract before January 2025 and moved NIH to the C&I Non-H/C tariff in March 2025. The study was published in December 2025.

[750] Tiska Surrebuttal at 10 and B. Oliver Direct at 27-28. Though OPC does not address the quality of WGL's non-residential class definition study, witness Brant does state his opinion that the NIH issue is fundamentally one of classification, and that no additional study is necessary to prove that it is an issue that should be addressed in the instant case. Brant Surrebuttal at 15-16.

classes to determine if they still adequately represent the customer base."[751] This order was in response to a concern raised by Staff about intra-class subsidies in the context of declining block rates–specifically that larger customers were being subsidized by smaller customers within rate classes.[752] Despite NIH's inclusion in the C&I Non-H/C potentially being an even more exaggerated version of this type of issue, WGL opted not to include a substantive examination of–and justification for–NIH's classification in this rate case. Instead, WGL leaned on the study results that did not contemplate NIH to conclude generally that there is no support for redefining customer classes at this time, and that further study that includes potential rate impacts would be necessary before any classification changes could be made.[753]

The Commission agrees with AOBA that WGL knew, or should have known, at the time it moved NIH to tariffed service in the C&I Non-H/C class that rates charged would be inadequate to cover the costs of serving NIH. Even so, it was not necessarily inappropriate for WGL to move NIH to that class at the time that it did so. At the time, WGL was not able to adjust its base rates and it was in the process of studying its non-residential class definitions, necessitating a business decision about the best way to handle NIH until it had the information necessary to adjust rates and/or class definitions.

However, given the obvious usage and cost of service disparities between NIH and the rest of the C&I Non-H/C class that are documented in the record, it is not acceptable that WGL did not conduct additional analysis and provide either justification for its current

[751] Order No. 90943 at 117, Case No. 9704, *Washington Gas Light Company's Application for Authority to Increase Rates and Charges for Natural Gas Services* (Dec. 14, 2023).
[752] *Id*. at 110-111.
[753] Fang Direct at 28-29 and Rebuttal at 33.

treatment of NIH or an alternative rate design by the time it filed this rate case. WGL had time and opportunity to do so. The Commission finds that WGL failed to sufficiently prove that maintaining its classification of NIH without incorporating any rate design measures specific to NIH would yield a just and reasonable rate for all customers.

The record is replete with recommendations from parties for how to address this issue, including moving NIH into its own class and setting separate rates; imputing base revenue to the test year to compensate for NIH's significant under-recovery; and implementing rate design measures designed to allocate costs specifically to NIH. What the record lacks, though, is sufficient data and information necessary for the Commission to determine the actual scope of the issue and independently craft a rate design with confidence that it is accurate and best-suited to provide a just and reasonable resolution.[754]

Finding an insufficient record upon which to base a solution, and also finding it unacceptable to defer consideration of this issue to a future rate case, it is the Commission's decision that the question of how to appropriately deal with NIH be addressed in a Phase II proceeding of this case. WGL will be required to produce a CCOSS which shows NIH in its own category using the true NCP methodology as proposed by Staff. WGL must also conduct an evaluation of whether NIH should reasonably be included in the C&I Non-H/C class given its usage characteristics and costs of service. Based on these analyses, WGL must either definitively demonstrate that its current treatment of NIH allows for just and

[754] Although the Commission is aware that a CCOSS showing NIH in a separate category was produced by WGL, for example, only portions of that document have been entered into the record. Further, the Commission understands that the referenced CCOSS used the CP&A methodology rather than the true NCP, which would also render it inaccurate for the Commission's purposes.

reasonable rates for all customers, or propose a reasonable alternative rate design to address the myriad issues raised in this case.

Staff is directed to evaluate WGL's conclusions and proposals and provide its own rate design proposal supported by sufficient data. Other parties may also file responses to WGL and make alternative proposals supported by sufficient data.

Until Phase II is concluded, the Commission finds it reasonable for distribution rates based on WGL's current customer classifications to go into effect. Though the Commission is concerned about the possibility of undue cross-subsidization, it notes the following: (1) by adopting Staff's allocation methodology that targets the C&I Non-H/C class in step one, OPC's concerns about inter-class subsidization are minimized; and (2) the Commission's decisions related to customer charge and the C&I declining block rate structure–discussed later in this order–provide a rate design mechanism that ostensibly places more of the revenue allocation burden on higher users within a class, which may serve to at least partially address AOBA's concerns of intra-class subsidization.[755]

As part of their responses, parties should address whether and how rates charged to and paid by customers during the pendency of Phase II should be adjusted based on the results of the proceeding, should it reveal that changes to any aspects of the interim rate design are necessary to produce just and reasonable rates. A Phase II procedural schedule will be forthcoming.

[755] As discussed in more detail below, changes to the declining block rate structure within the C&I Non-H/C class specifically will result in decreased rates for usage below 300 therms and increased rates for usage above 300 therms. Because the average non-NIH customer in the class uses approximately 825 therms per month and NIH averages over 1 million therms per month, bill impacts for NIH should, in theory, be greater than the other members in the class.

The table below summarizes the results of the Commission's approved revenue allocation methodology:

Table 9:
Commission Approved Allocation Results

| Customer Class | Current Dist. Revenue | Current UROR | Step 1 Allocation | Step 2 Allocation | Overall Revenue Change | New UROR |
|---|---|---|---|---|---|---|
| RES - H/C | $234,898,719 | 0.98 | $5,184,655 | $22,269,765 | $27,454,420 | 1.01 |
| RES - Non H/C | $1,320,715 | 0.68 | $29,151 | $125,211 | $154,362 | 0.78 |
| C&I- H/C < 3K | $12,242,668 | 1.14 | $0 | $1,160,676 | $1,160,676 | 1.09 |
| C&I- H/C > 3K | $57,739,440 | 1.16 | $0 | $5,474,035 | $5,474,035 | 1.08 |
| C&I- Non H/C | $6,907,343 | 0.37 | $152,458 | $654,856 | $807,314 | 0.45 |
| GMA - H/C | $16,031,093 | 0.83 | $353,836 | $1,519,841 | $1,873,677 | 0.84 |
| GMA- Non H/C | $2,259,221 | 1.68 | $0 | $214,187 | $214,187 | 1.57 |
| Interruptible | $10,498,596 | 1.05 | $0 | $995,328 | $995,328 | 0.96 |
| *Total* | *$341,897,795* | *1.00* | *$5,720,100* | *$32,413,900* | *$38,134,000* | *1.00* |

2. System Charges

WGL

The goal of fixed-system charges in a rate design regime is to effectively and fairly collect non-variable customer-related costs. WGL witness Fang states that cost-based rates promote efficiency and fairness, ensuring that all customers "pay their fair share for energy services."[756] Ms. Fang opines that WGL's current system charges are not cost-based. Based on her analysis of the CCOSS, WGL's current system charges recover less than 50% of customer related fixed costs.[757]

Because of this, WGL believes that substantial increases to customer charges for most customer classes are necessary. The Company proposes that, at a minimum, system charges increase by 30.2%, which is their calculated system average increase plus 10%.[758] Further, to help manage bill impacts for certain non-residential customers caused by the transition away from declining block rates, WGL proposes to further increase fixed-customer charges ranging from an *additional* increase of 30% to 130%.[759] The Company believes definitive movement towards cost-based customer charges at this time is necessary for bill stability and efficient price signals that do not overvalue energy efficiency and conservation.[760]

<u>Staff</u>

Staff finds WGL's proposed customer charge increases to be untenably high. While Staff generally supports cost-based rates, Staff witness Walton points out that WGL's proposal in this case would yield customer charge increases that deviate significantly from Commission precedent.[761] Mr. Walton calculates that WGL's proposal would cause

[756] Fang Direct at 32-33.
[757] *Id*. at 33.
[758] *Id*. at 34-35.
[759] *Id*. at 35 and 44. This proposal is part of WGL's comprehensive recommendation for gradual elimination of declining block rates, discussed further below.
[760] *Id*. at 34.
[761] Walton Direct at 18.

customer charge increases ranging from 30.2% at the minimum to 158.3%; whereas the increases to the customer charge in WGL's last four rate cases have not exceeded 5.14%.[762]

Staff proposes instead that customer charge increases for each class equal the percent increase of the revenue allocated to the class.[763] This would result in charges that make progress towards being cost-based but at a more moderate and incremental pace.[764] Staff indicates that this moderation is necessary because large increases to fixed rates can cause rate shock, particularly for customers who have lower usage because a larger proportion of their bill becomes unavoidable.[765] As justification for its proposal to exceed the trend of the Commission's relatively low historical customer charge increases, Staff states that the higher amounts are necessary to help support the transition away from declining block rates, and that increased fixed charge can help smooth seasonal bill fluctuations for customers.[766]

AOBA

AOBA also finds WGL's proposed customer charge increases to be inappropriately high and inconsistent with the principle of gradualism.[767] AOBA does not oppose a reasonable increase to fixed customer charges for non-residential customers, but also argues that system charges should not be fully cost-based.[768] AOBA witness B. Oliver points out that the Company's costs to serve customers within the same rate class are not uniform; as such, an effective rate design should allow for customers who cause more of

[762] *Id*.
[763] *Id*.
[764] *Id*.
[765] *Id*. at 18-19.
[766] *Id*. at 19-20.
[767] B. Oliver Direct at 61.
[768] *Id*.

the Company's fixed costs to bear a greater portion of those costs.[769] AOBA recommends that no customer charge increase should exceed 1.5 times the overall system average increase percentage.[770]

OPC

OPC does not support WGL's customer charge proposals for residential customers. OPC witness Brant finds that WGL's customer-related unit cost calculations are inflated, which results in a proposal that is not actually consistent with cost-causation.[771] OPC states that WGL classified service lines and house regulator costs as fully customer-related, whereas WGL's CCOSS accurately reflects those expenses as partially based on demand.[772] OPC argues that WGL has an incentive to inflate customer charges because those fixed charges represent assured income for WGL.[773] OPC also states that such large customer charge increases contradict State policy goals that necessitate energy efficiency and decarbonization.[774] Higher fixed charges provide less incentive for customers to consume less gas to save money on their energy bills, which negatively impacts progress towards electrification and decarbonization.[775] OPC recommends that the Commission maintain current residential customer charges and reject WGL's proposal.[776]

[769] *Id*. Witness B. Oliver's rate design solution for this issue is to maintain the declining block rate system.
[770] *Id*. at 61-62.
[771] Brant Direct at 41-42.
[772] *Id*. at 42.
[773] *Id*.
[774] *Id*. at 43.
[775] *Id*. at 44.
[776] *Id*. at 45.

**Commission Decision**

The Commission agrees with Staff, AOBA, and OPC that WGL's requested customer charge increases are disconcertingly high. While cost causation is a factor to consider when setting fixed customer charges, it is not the *only* factor to consider. WGL's proposed customer charge increases that range from 30% to over 150% are based only on the pursuit of a more cost-reflective rate, without regard for affordability or policy considerations. As Staff points out, even modest increases to fixed charges could represent an affordability concern for some customers.[777] While many Maryland residents served by WGL are experiencing economic hardship, the Commission does not find it appropriate at this time to diminish a residential customer's ability to control a bill by reducing usage, which may at times be a critical tool available to a customer to be able to make ends meet. The Commission also agrees with OPC that WGL's proposal is not consistent with Maryland's goals for energy efficiency. For these reasons, the Commission adopts OPC's recommendation to leave residential customer charges at their current levels.

These concerns are also generally applicable to non-residential rate classes and weigh in favor of limiting customer charge increases for those classes as well. However, the Commission understands that the process of moving towards the elimination of non-residential declining block rates presents a unique rate design consideration for these classes. The Commission agrees with WGL and Staff that increases in customer charges can somewhat cushion the impact of declining block rate changes on customers–

[777] Staff references public comments made in WGL's prior rate case, Case No. 9704, *Washington Gas Light Company's Application for Authority to Increase Rates and Charges for Natural Gas Services* (Dec. 14, 2023), in which residential customers express concern over a proposed customer charge increase of only around 5%.

particularly high-use customers–by limiting further increases to volumetric rates. The Commission does not agree that customer charge increases that exceed 30%, as proposed by WGL, are necessary to achieve this goal. The Commission generally agrees with the range of increases proposed by Staff, but finds that a 10% customer charge increase for each non-residential rate class is a more equitable approach. The table below summarizes the Commission's findings with respect to customer charges.

Table 10:
Commission Approved System Charge Increases

| Customer Class | Current System Charge | Approved System Charge | Change (%) | Change ($) |
|---|---|---|---|---|
| RES - H/C | $11.85 | $11.85 | 0% | $0.00 |
| RES - Non H/C | $11.85 | $11.85 | 0% | $0.00 |
| C&I- H/C < 3K therms | $21.50 | $23.65 | 10% | $2.15 |
| C&I- H/C > 3K therms | $43.00 | $47.30 | 10% | $4.30 |
| C&I- Non H/C | $15.75 | $17.33 | 10% | $1.58 |
| GMA - H/C | $55.85 | $61.44 | 10% | $5.59 |
| GMA- Non H/C | $19.80 | $21.78 | 10% | $1.98 |
| Interruptible | $136.50 | $150.15 | 10% | $13.65 |

With the findings in this section, the final residential bill impacts are as follows:

Table 11: Commission Approved Monthly Residential Bill Impact Summary Based on Average Use[778]

| Customer Class | Current Dist. Bill | Dist. Change ($) | Dist. Change (%) | Current Total Bill | Total Change ($) | Total Change (%) |
|---|---|---|---|---|---|---|
| RES - H/C | $46.30 | **$4.01** | **8.66%** | $92.08 | **$4.01** | **4.36%** |
| RES - Non H/C | $30.64 | **$2.16** | **7.04%** | $56.51 | **$2.11** | **3.73%** |

Table 12: Monthly Residential Distribution Bill Impact Comparison Based on Average Use

| Customer Class | WGL Proposed Increase | | Staff Proposed Increase | | Commission Approved Increase | |
|---|---|---|---|---|---|---|
| RES - H/C | $7.87 | 8.5% | $4.82 | 5.24% | $4.01 | 4.36% |
| RES - Non H/C | $6.17 | 10.9% | $2.64 | 4.67% | $2.11 | 3.73% |

3. Declining Block Rate Structure

The Commission ordered WGL to begin moving away from declining block rates in Case No. 9651 to support Maryland's policies related to climate change and energy

[778] As discussed in the Commission's decision related to the Company's STRIDE investments above, the Commission ordered that certain STRIDE expenses remain in the STRIDE surcharge because the Company did not sufficiently justify its request to move them into rate base at this time. The Commission's estimated bill impacts in Tables 11 and 12 reflect that decision and are calculated using an estimated surcharge value, which is not included in the bill impacts that were presented by WGL and Staff earlier in this case.

efficiency.[779] WGL complied by eliminating declining block rates for residential classes in Case No. 9704, but deferred changes to non-residential class rate structures to a later rate case due to concerns of rate shock. The Commission ordered WGL to study the amount of rate shock that would result from the elimination of declining block rates and propose a total elimination in its next base rate case.[780]

<u>WGL</u>

Now arriving at WGL's next base rate case, WGL has complied with the Commission's Order and presented an analysis which contemplates full elimination of declining block rates for non-residential customers.[781] However, WGL witness Fang's analysis of the bill impacts that would result from this change indicates substantial rate shock would occur for most customer classes.[782] For this reason, WGL proposes that steps be taken in this rate case towards elimination of declining block rates, with the goal of gradually transitioning to total elimination in the future. WGL proposes to achieve this gradualism by eliminating one of the three blocks in the rate structure, and by decreasing the rate differential between those two blocks.[783]

<u>Staff</u>

Staff agrees with WGL's gradual approach to transitioning away from declining block rates and also proposes to go from a three block to a two-block design. To move more decisively towards the goal of elimination, however, Staff recommends modifications

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[779] Order No. 89799 at 36-37.
[780] Order No. 90943 at 117-118, Case No. 9704, *Washington Gas Light Company's Application for Authority to Increase Rates and Charges for Natural Gas Services* (Dec. 14, 2023).
[781] Fang Direct, Exhibit CSF-9.
[782] Fang Direct at 39.
[783] *Id*. at 40-41.

to the relative level of volumetric rates within each block, and a further decrease in the differential between blocks.[784] Additionally, Staff recommends that the Commission require WGL to establish a clear and defined timetable for full elimination over the course of its next two rate cases.[785]

AOBA

AOBA does not support the elimination–gradual or otherwise–of declining block rates. AOBA witness B. Oliver finds WGL's study to be flawed because it did not address price elasticity, the impacts of higher tail block rates on other existing rate mechanisms, and the cost-basis for WGL's existing declining block rate structure.[786] AOBA requests that the Commission be more sensitive to the greater diversity in usage characteristics among non-residential rate classes, which necessitates a declining block rate structure in order to equitably price service to differently-sized customers within a class.[787] Mr. B. Oliver also states that the Commission should be primarily concerned with fair and equitable rates rather than energy efficiency policies.[788]

**Commission Decision**

Consistent with its previous orders, the Commission finds that the elimination of declining block rates is congruent with Maryland's public policy goals that encourage energy conservation and efficiency. Promoting energy efficiency policies is not incompatible with setting fair and equitable rates.[789] AOBA's concern about equitable

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[784] Walton Direct at 27.
[785] *Id*. at 28.
[786] B. Oliver Direct at 52-53.
[787] *Id*. at 53.
[788] B. Oliver Surrebuttal at 31.
[789] In fact, such considerations are a *requirement* of the Commission's supervision and regulation of public service companies pursuant to PUA § 2-113, which includes conservation of natural resources, preservation

intra-class pricing could be addressed in a manner that does not sacrifice efforts towards conservation–by segmenting classes where usage characteristics are so diverse as to cause a perceived imbalance of impacts to customers within the class. AOBA–or any party–is invited to propose segmented rate classes in Phase II or any other future proceedings if there are intra-class subsidization concerns.[790]

Although the Commission expressed its intention that declining block rates be fully eliminated in this case, the Commission agrees with WGL's assessment that doing so at this time could result in serious rate shock to some customers. The Commission therefore approves a gradual approach towards full elimination and adopts the Company's proposed design to be effective until the conclusion of Phase II. The Commission notes that it is unclear whether Staff's workpapers on the record demonstrate that its proposed rates would function effectively to collect its total proposed revenue requirement. For this reason, the Commission did not find that it could appropriately evaluate Staff's proposal in comparison to the Company's. Because the Phase II proceeding may result in changes to revenue allocation and rates for the C&I classes, the issue of declining block rate design can be further addressed then. In any case, the Commission finds that the Company's proposal should move rates closer to the goal of eliminating the declining blocks without causing significant adverse impacts to any class.

of environmental quality, protection of the global climate, and achievement of the State's greenhouse gas emissions reduction targets as necessary concerns in every matter before the Commission.

[790]As discussed above, this was the driver of the Commission's order to WGL in its previous rate case to study whether existing commercial customer classes still appropriately represent their respective customer bases. AOBA criticized this study in testimony, including in relation to the Company's treatment of NIH. As a result, the Commission is ordering today a Phase II proceeding to address the issue, which will allow for stakeholder input to consider the matter further.

The Commission also agrees with Staff that WGL should be prepared with a clear and defined plan to fully eliminate declining block rates. Consistent with its past orders, the Commission orders WGL to prepare such a plan, which outlines how WGL will eliminate declining block rates in that rate case without harming its customers, and share it with Staff and other stakeholders for review and comment *prior* to filing its next rate case.

### E. <u>Lost and Unaccounted for Gas</u>

In WGL's last rate case, Case No. 9704, the Commission rejected AOBA's recommendation to reduce the Company's revenue requirement by $12 million for unaccounted-for-gas ("UFG").[791] The Commission found that the issue was more appropriately addressed in proceedings involving the Company's Purchased Gas Costs and directed the Company to file testimony addressing UFG standards, reasonable volume of UFG, costs of its UFG and the Company's efforts to reduce its UFG, in its next Purchased Gas Adjustment case.[792] In Case No. 9509(r) in 2024, UFG was raised. WGL included a discussion of the topics requested.

<u>AOBA</u>

In his Direct Testimony, AOBA witness B. Oliver criticized WGL's handling of UFG, arguing that the Company's UFG levels are exceptionally high, mismanaged, and unfairly burden Maryland ratepayers.[793] Specifically, Mr. B. Oliver pointed out that WGL's

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[791] Order No. 90943 at 74-76.
[792] *Id*.
[793] B. Oliver Direct at 13-18.

UFG percentage of over 4% as reported in Case No. 9704 and Case No. 9509(r) is an industry outlier.[794] Mr. B. Oliver noted that based on the data presented by WGL witness Waller in Case No. 9509(r), the Company's UFG percentage is an outlier for gas distribution utilities having more than 500,000 customers.[795] He stated that WGL's UFG rate is three to four times higher than the industry average of approximately 1%.[796]

Mr. B. Oliver commented that UFG is primarily an operational and maintenance issue caused by leaks, metering errors, theft, and third-party damage.[797] He criticized WGL for failing to take definitive action despite knowing about these issues. For example, he noted WGL acknowledged that a metering pressure mismatch existing since 2008 contributes 1.28% to the Company's UFG, yet he stated WGL has provided no evidence of implementing a fix to align the base pressures.[798]

Mr. B. Oliver also expressed concern that WGL applies a single, uniform UFG percentage across its Maryland, Virginia, and District of Columbia service territories.[799] However, U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration ("PHMSA") data shows the leak rate on distribution mains in D.C. is roughly three times greater than in Maryland and Virginia.[800] Mr. B. Oliver argued that by using a blended system-wide rate, WGL is effectively forcing Maryland customers to subsidize the much higher leak rates and costs driven by WGL's D.C. system.[801]

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794 *Id*. at 14.
795 *Id*.
796 *Id*.
797 *Id*. at 15.
798 *Id*. at 15-16.
799 *Id*. at 17.
800 *Id*.
801 *Id*. at 17-18.

Mr. B. Oliver asserted that WGL lacks an economic incentive to fix these issues and recommended that the Commission establish strict UFG targets:

> In the absence of identifiable industry standards for acceptable UFG performance, this Commission should require WG to target the achievement of annual UFG percentages not greater than twice the average for investor/privately-owned gas distribution utilities serving over 500,000 customers in a single service territory (based on the Annual Gas Distribution Utility reports that such utilities are required to file with PHMSA). That target can be pursued gradually by ratcheting the allowed UFG rate for Washington Gas for ratemaking purposes downward to the Company's UFG percentage in this case by 50 basis points and making similar downward adjustments in each of the Company's next two rate cases.[802]

He further commented in footnote 1 of his Direct Testimony that the UFG rate Washington Gas has used for ratemaking purposes in this proceeding is 3.53%.

> Lowering that rate by 50 basis points in this case and in each of the Company's next two cases would yield an acceptable UFG of slightly over 2.0%. In the Company's third subsequent rate case, the acceptable UFG rate for Washington Gas for ratemaking purposes could be re-examined. Costs associated with Unaccounted for Gas volumes in excess of the level established by the Commission in the Company's most recent rate case would not be recoverable from its Maryland ratepayers.[803]

<u>WGL Rebuttal</u>

WGL witness Lawson noted UFG can arise from leaks, theft, third-party damage, and inexact volumetric corrections, but he also emphasized the role of metering conventions and correction factors. Specifically, he pointed to mismatched base pressures, varying pressure levels within WGL's meters, and the installation of slightly higher delivery pressure regulators beginning in 2008.[804]

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[802] *Id*. at 8-9.
[803] *Id*. at 9, *citing* fn. 1.
[804] Lawson Rebuttal at 11-12.

Mr. Lawson argued that the Company is actively working to address UFG through system improvements and implementation of the identified metering correction factors. Specifically, he highlighted that WGL is:

> (1) continuing to install or adjust standard regulators to a delivery pressure of 7” Water Column (“WC”);
>
> (2) evaluating additional correction factors to consider for implementation based on system information being gathered and how to implement changes to billing correction factors; and
>
> (3) working to identify which customers have received a new regulator or pressure adjustment since 2008 (changing from 5.5” WC to 7” WC), as each pressure requires a different correction factor for accuracy.[805]

Mr. Lawson also acknowledged that correcting these metering factors will increase the volumes of gas billed to customers across most rate classes. However, he argued this change should be revenue-neutral. Because the overall cost of service would remain unaffected by the upward adjustment in billed therms, the actual per-therm rate would correspondingly decrease.[806] He stressed that these metering corrections must be implemented simultaneously and in the context of a base rate case so that the normal weather therms underlying base rates can be properly adjusted and to minimize disruption from multiple instances of adjustments to billing factors.[807]

Mr. Lawson recommended that the Commission reject AOBA witness Oliver's proposal to establish strict, descending UFG percentage targets and penalties.[808] He argued that implementing such targets would not be useful because much of the UFG stems from the metering conventions he outlined and reiterated the Company’s efforts to work on UFG

[805] *Id*. at 12-13.
[806] *Id*.
[807] *Id*.
[808] *Id*. at 13-14.

as it replaces standard regulators along with other system improvements. Mr. Lawson recommended that WGL provide a comprehensive update on the status of its UFG reduction efforts during its next base rate case. He anticipates that by the next rate case, the Company will be able to provide differentiated correction factors for customers with 5.5" WC versus 7" WC regulators, along with any necessary tariff changes and corresponding adjustments to normal weather therms.[809]

AOBA Surrebuttal

AOBA witness B. Oliver commented that WGL witness Lawson's suggestion that WGL will provide an update on UFG efforts in its *next* base rate case was merely a way of "kicking the can down the road."[810] He pointed out that, in the Company's last PGA proceeding, it indicated it would be appropriate to take up UFG issues in the next rate case, which is the current proceeding.[811]

**Commission Decision**

While the Commission recognizes that the Company's UFG rate of 4.53% cited in its last rate case in 2022 has decreased to 3.53% in the present proceeding, the Commission finds that AOBA raises legitimate concerns regarding the persistent high rate of WGL UFG compared to other natural gas utilities. The Commission is concerned that the Company's use of a uniform UFG percentage for all three of its jurisdictions (Maryland, the District of Columbia, and Virginia) may be causing inter-jurisdictional subsidization where WGL's customers in Maryland and Virginia are subsidizing the Company's District of Columbia

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[809] *Id*. at 14.
[810] B. Oliver Surrebuttal at 5.
[811] *Id*. at 4-5.

service. The Commission directs the Company to report on its ability to separate MD's UFG from the other jurisdictions. Additionally, the Commission finds the Company's explanation about the metering conventions questionable and directs the Company to continue addressing the underlying factors causing its rate to be two to three percent higher than industry average. The Company is directed to include an updated analysis of UFG in Maryland, including a detailed description of its efforts to reduce UFG to align more closely the industry average, in its next rate case. The Commission finds that should the Company fail to make measurable progress to bring its UFG closer to industry average, then the Commission will consider a reduction in basis points in a future rate case.

### F. Mercury Service Regulators

Staff witness Tesfaye continued to support the Commission's directive in Rate Case No. 9704 directing the Company to remove all mercury service regulators on its system, to work with Commission Staff and Consumer Affairs Division in this process and to file quarterly progress reports. Staff recommended that the Company complete its removal efforts and continue to adhere to the directives provided by the Commission in Case No. 9704.

#### Commission Decision

As no party is contesting Staff's recommendation, the Commission directs the Company to continue to remove all mercury service regulators on its system and to adhere to the Commission's directive related to this issue in Order No. 90943 issued in Case No. 9704.

## G. **Contract Generation Service Rate Schedule**

WGL

WGL witness Simone proposed a new Contract Generation Service Tariff ("CGS") rate schedule, Rate Schedule 9, to serve as a mechanism for serving C&I loads that seek to generate power locally on-site.[812] Based on prospective customer inquiries, WGL proposed requiring prospective customers to use between 8,400 and 168,000 therms per day to qualify for the CGS rate schedule, which is the equivalent of 5MW to less than 100MW of electricity generation.[813] WGL stated it has received interest over the last several years from potential customers with large energy demand, such as data centers, quantum computing campuses, and biotechnology firms, who have expressed a need to secure reliable power and self-generate.[814] WGL stated the new tariff will help attract new businesses. Under the proposed tariff, WGL indicated that it would negotiate with a prospective customer a Service Agreement specifying the rate, terms and conditions, and the type of service (firm vs interruptible). WGL would also have the discretion not to supply gas, in which case the customer could contract for third-party supply.[815]

OPC

OPC witness Brant recommended that the Commission reject the Rate Schedule 9 tariff at this time.[816] He argued the proposal lacks necessary details to protect existing customers from the significant risks of stranded assets and cost increases and pointed to

[812] Simone Direct at 5.
[813] *Id*.
[814] *Id*. at 3.
[815] *Id*. at 4.
[816] Brant Direct at 3.

uncertainty surrounding actual future energy demand and project completion rates for AI data centers.[817] He expressed concern that the tariff gives WGL total discretion to negotiate bespoke contracts, allows the Company alone to determine a CSG customer's incremental costs, and does not explicitly establish minimum provisions for contract terms, minimum bills, exit fees, security deposits, and cancellation penalties.[818]

Rather than approving a new tariff at this time, OPC witness Brant recommended that the Commission open a statewide rulemaking to establish minimum terms and consumer protections for contract generation tariffs, or require WGL to refile the tariff in a standalone proceeding.[819]

Staff

Staff witness McAuliffe also recommended rejecting the proposed tariff without prejudice because he considers it premature.[820] He pointed out that under Commission proceeding Public Conference 72 ("PC 72"), the Large Load Work Group is currently discussing similar large load issues (such as minimum bills, contract terms, and exit fees) for electric utilities.[821] He recommended WGL wait until the Commission issues its decisions regarding electric Large Load tariffs before refiling the CGS schedule.[822]

Mr. McAuliffe also expressed concern that WGL's proposal relies too heavily on special, customized contracts. He preferred that standardized terms and conditions be explicitly listed in the tariff to apply to all similarly situated customers equally, warning

[817] *Id*. at 47-49.
[818] *Id*. at 47 and 51-53.
[819] *Id*. at 3.
[820] McAuliffe Direct at 6.
[821] *Id*.
[822] *Id*. at 7.

that bespoke agreements could lead to illegal rate discrimination or fail to meet Commission requirements.[823] He also recommended that all CGS customers be required to take interruptible service so they can be curtailed during extreme cold weather events to ensure reliable service for firm customers.[824]

Montgomery County

In its Initial Brief, Montgomery County stated that it agrees with Staff witness McAuliffe and OPC witness Brant that the Commission should reject the proposed CGS rate schedule at this time.[825] Specifically, the County noted that "[t]he proposed rate schedule would be more appropriately considered once PC 72 is completed. Such an approach can safeguard that utility efforts to serve Large Load customers are aligned and consistent with legislative intent to safeguard other ratepayers."[826]

WGL Rebuttal

WGL witness Simone defended the CGS tariff against the recommendations of Staff and OPC, maintaining that the Commission should approve the tariff immediately in this proceeding.[827] Mr. Simone argued gas utilities are fundamentally different from electric utilities, so PC 72 (in which electric companies are participating) should not apply, and a rulemaking process will be too long and would not be specific to WGL customer needs. He reiterated the Company's belief that the CGS tariff would attract economic development to the state.[828]

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[823] *Id*. at 8.
[824] *Id*. at 8-9.
[825] Montgomery County Initial Brief at 5.
[826] *Id*.
[827] Simone Rebuttal at 1, 4, and 11.
[828] *Id*. at 4 and 5.

Mr. Simone also rejected the recommendation to establish standardized terms and conditions in the tariff, arguing that contractual flexibility is essential. He opposed requiring formal Commission approval for underlying service agreements, arguing it would thwart the "speed to market" that the tariff is designed to facilitate.[829] Further, Mr. Simone stated WGL would agree to file a General Service Provision ("GSP-14") analysis with underlying CSG service agreements.[830]

Additionally, he argued against the recommendation to limit CGS customers exclusively to interruptible service, stating that while interruptible service is an option if requested, mandating it would undermine the core goal of providing reliable service to these customers.[831]

OPC and Staff Surrebuttal

OPC witness Brant maintained his previous position and noted that while he appreciates WGL's offer to conduct a GSP-14 analysis, this does not assuage other concerns.[832]

Staff witness McAuliffe maintained there is no need for consideration of the CSG tariff to be limited to a rate case.[833] He pointed out that there is no urgency for this tariff, as indeed WGL has already signed a contract with a data center without it.[834] McAuliffe also noted the Large Load Work Group utilities are scheduled to file their Large Load tariffs this September, so any delay will be minimal, and the PC Large Load tariff work

[829] *Id*. at 6-9.
[830] *Id*. at 9-10.
[831] *Id*. at 10.
[832] Brant Surrebuttal at 17-18.
[833] McAuliffe Surrebuttal at 5-6.
[834] *Id*. at 4-5.

includes aspects that are similar in some respects to the CGS.[835] Mr. McAuliffe reiterated his argument that the CGS tariff should not be approved until PC 72 Large Load tariff process concludes, and his other recommendations regarding contract terms are adopted. Mr. McAuliffe disputed Simone's argument that limiting the CSG tariff to interruptible customers would undermine reliability for CSG customers.[836] On the contrary, Mr. McAuliffe testified that requiring these massive facilities to be curtailed on peak days will help ensure reliability for the entire system.[837]

**Commission Decision**

The Commission agrees with Staff and OPC that WGL's proposed new CSG Rate Schedule 9 tariff would be premature at this time given the current work of PC 72 which may be able to address many of WGLs goals. The Commission also reminds the Company of its ability to enter into special contracts outside of the proposed tariff. Therefore, the Commission rejects the tariff without prejudice.

The Commission directs WGL to review the findings of PC 72 and, if it chooses, to submit a revised proposed tariff considering the applicable results of PC 72. The Commission also agrees with Staff that any revised tariff must include as many contract requirements as possible that would apply to all similarly situated customers, on issues such as contract lengths, exit fees, collateral requirements, *etc*.

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[835] *Id*. at 5.
[836] *Id*. at 8.
[837] *Id*.

### H. <u>WGL's Gas Odor Response</u>

Staff witness Tesfaye reviewed the Company's gas odor response trend from 2021 to 2025 and found that "the average response time, calls over one hour, and the percentage of calls answered within one hour fluctuated with shifting upward and downward trends between 2021 and 2025."[838] Mr. Tesfaye's evaluation concluded that the average odor response time in 2025 increased by more than 38% and that the percentage of calls within one hour did not show any improvement and decreased by three percentage points from 77.3 in 2021 to 74.3 in 2025.[839] Therefore, witness Tesfaye recommended that the Commission direct the Company to work toward improving its odor response time.

<u>WGL Response</u>

WGL witness Murphy agreed that Staff raises focus to an important metric and correctly observes the Company's response times.[840] He further commented that the Company is committed to improving its response time for all odor calls and evaluating how its internal odor call response processes can be improved. Mr. Murphy proposed that the Company conduct a technical conference with Staff later in this calendar year to reassess current reporting and develop targets that support action planning.[841]

**<u>Commission Decision</u>**

The Commission appreciates and agrees with Staff shedding light on such an important metric and topic. The Commission does not agree that a technical conference is

[838] Tesfaye Direct at 24.
[839] *Id*.
[840] Murphy Rebuttal at 17.
[841] *Id*.

necessary at this time as it is unclear if other utilities have similar issues. Therefore, the Company is directed to work with Staff and other interested parties to address odor response time concerns identified by Staff. If Staff believes other utilities have similar odor response time concerns or believe that universal standards in Maryland are warranted, then Staff may petition the Commission to expand the scope or initiate a technical conference.

### I. Phase II Proceeding Considering the Utility RELIEF Act and Other Continued Matters

OPC

In its Initial Brief, OPC noted that during the 2026 Legislative Session, the General Assembly passed the Utility RELIEF Act which, in relevant part, restricts recovery of supervisor compensation that exceeds 110% of the Chair of the Public Service Commission maximum annual salary.[842] Under the new statute, "Supervisor" is defined as meaning an employee "employed in a bona fide executive capacity under the Federal Fair Labor Standards Act," or an employee of a public service company who is delegated certain authorities over personnel, including hiring, promotion, firing and discipline, assignment of work, and responding to complaints.[843] Also "compensation" is broadly defined to mean "a form of payment or consideration to or for the benefit of" an employee of a public service company, its parent, or any affiliate "in connection with the employee's work for a public service company."[844]

[842] 2026 Session Laws, Ch. 353. *See also* OPC Initial Brief at 51.
[843] 2026 Session Laws, Ch. 353 (codified at PUA § 4-504 (a)(4).
[844] 2026 Session Laws, Ch. 353 (codified at PUA § 4-504 (a)(3).

OPC pointed out that it is likely WGL's revenue requirement in this proceeding includes costs that the recently enacted law now prohibits WGL from recovering.[845] OPC observed that the present WGL proceeding did appear to have sufficient records to identify all compensation amounts covered by the new law that must be removed. Therefore, WGL requested the Commission establish a Phase II proceeding limited to identifying and removing the published compensation costs from WGL's revenue requirement.[846]

<u>WGL Response</u>

In its Reply Brief, WGL opposes OPC's recommendation for a Phase II proceeding related to Utility RELIEF Act requirements. WGL argues that OPC does not base its assertion that WGL's rates likely include costs prohibited by the law on any record evidence.[847] Thus, the Company states a Phase II would be "speculative" and not properly supported by the evidence in this case.[848]

<u>Staff Response</u>

Staff supports OPC's proposal for a Phase II proceeding in this case to apply the new requirements of the Utility RELIEF Act. Staff argues that the Commission must apply the law as it exists at the time of decision, not at the time of application.[849] To support its argument, Staff points to the holdings in several cases, including those of the U.S. Supreme Court and Maryland Supreme Court, as well as prior Commission orders that align with those holdings. In one such order where the Commission applied a law that took effect

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[845] OPC Initial Brief at 51.
[846] *Id*. at 53.
[847] WGL Reply Brief at 50-51.
[848] *Id*. at 51.
[849] Staff Reply Brief at 17-18.

during the pendency of a CPCN case, Staff indicates that the Commission quoted case law which concluded that a "statute which affects…a matter still in litigation when it became law will be applied by the court reviewing the case at the time the statute takes effect…"[850]

Because application of the Utility RELIEF Act would require additional information-gathering beyond the scope of the current record, Staff recommends that the Commission adopt OPC's proposal for a Phase II.

**Commission Decision**

The Commission agrees that a Phase II proceeding is appropriate given the Utility RELIEF Act was signed into law during the pendency of this proceeding, and the relevant section became effective on May 12, 2026. None of the parties nor the Commission have had an opportunity to determine its impact on WGL's revenue requirement, if any, in this proceeding.

WGL's argument that the Commission should reject OPC's proposal because it is not supported by the evidence on the record belies the purpose of a Phase II proceeding. As WGL itself states in another section of its reply brief, the Commission has appropriately ordered Phase II proceedings in cases in which "there was not an opportunity to fully develop the record on an issue."[851]

In this case, the Commission is required by the statute to ensure a utility does not recover certain expenses through rates. The Commission's approved rates will go into effect prospectively, and thus are logically subject to the requirements of the statute.

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[850] *Id*. at 17.

[851] WGL Reply Brief at 29, *citing In the Matter of the Application of Washington Gas Light Co. for an Increase in Rates and Charges for Gas Service and to Implement a Performance-Based Rate Plan,* Case No. 9104, Order No. 81715 at 22, (Nov. 16, 2007).

Therefore, the Commission finds that a Phase II proceeding that is specifically tailored to ensure compliance with the law is appropriate and necessary. This issue will be included in the Phase II proceeding set forth above related to the classification of NIH, and a procedural schedule to resolve both issues will be established accordingly.

## IV. <u>CONCLUSION</u>

The goal of any ratemaking proceeding is for the Commission to ensure that the rates approved for a public utility to charge customers for regulated service are just and reasonable. Having duly considered the entire record in this proceeding, including all of the filed and oral testimony and exhibits, as well as public comments, and taking into account recent Commission decisions, the Commission hereby authorizes an increase in rates of **$38,134,000,** with an overall ROR of **7.22%** based on a ROE of **9.40%** on an adjusted rate base of **$1,645,079 thousand**. The Commission finds that these terms, along with the decisions stated elsewhere in this Order, encompass just and reasonable rates that will not induce rate shock and will not unduly burden any one class of customers.

**IT IS**, **THEREFORE**, this 27th day of July, in the year Two Thousand Twenty-Six, by the Public Service Commission of Maryland, **ORDERED**:

(1) that the Application filed by Washington Gas Light Company on December 29, 2025 (as supplemented by the Company over the course of this proceeding), seeking an increase in its Maryland distribution rates of $82.5 million, is hereby denied, as discussed in the body of this Order;

(2) that Washington Gas Light Company is hereby authorized to increase its Maryland distribution rates by no more than $38,134,000 for service rendered on or after July 27, 2026, consistent with the findings in this Order;

(3) that Washington Gas is directed to file tariffs in compliance with this Order with the effective dates prescribed herein, subject to acceptance by the Commission;

(4) that the Commission will initiate a Phase II proceeding for the limited purposes of addressing the rate design issue regarding declining block rates, Washington Gas' class cost of service classification of the National Institute of Health as discussed herein, and evaluating the impact of the compensation provision in PUA § 4-504 on Washington Gas's revenue requirement in this proceeding; and

(5) that any motions or requests not granted herein are denied.

*/s/ Kumar P. Barve*

*/s/ Frederick H. Hoover, Jr.*

*/s/ Bonnie A. Suchman*

*/s/ Odogwu Obi Linton*

*/s/ Ryan C. McLean*
Commissioners