BEFORE THE CORPORATION COMMISSION OF THE STATE OF OKLAHOMA

IN THE MATTER OF THE APPLICATION OF	)	
OKLAHOMA GAS AND ELECTRIC COMPANY	)	
FOR AN ORDER OF THE COMMISSION	)	
AUTHORIZING APPLICANT TO MODIFY ITS	)	CASE NO. PUD 2023-000087
RATES, CHARGES, AND TARIFFS FOR RETAIL	)	
ELECTRIC SERVICE IN OKLAHOMA	)	

Rebuttal Testimony

of

Jeremy K. Schwartz

on behalf of

Oklahoma Gas and Electric Company

May 17, 2024

QUALIFICATIONS, EXPERIENCE, AND PURPOSE

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

A. My name is Jeremy K. Schwartz. My business address is 321 North Harvey, Oklahoma City, Oklahoma 73102.

Q. **By whom are you employed and in what capacity?**

A. I am employed by Oklahoma Gas and Electric Company ("OG&E" or "Company") as Manager of Sales Support and Marketing Analytics. My responsibilities include analysis for new business customers, calculating minimum bills, bill estimates, impact analysis for existing customer requests, (rate changes, fuel impacts, tariff changes, and other programs including, but not limited to, Load Reduction, Day Ahead Pricing ("DAP"), Flex, Solar, wind power), OG&E's Load Forecast, customer segmentation analysis, tracking and reporting.

Q. **Please summarize your educational background and professional qualifications.**

A. I earned my bachelor's degree in economics from Oklahoma State University. Prior to assuming my current position in OG&E, I spent four and a half years with the Oklahoma Corporation Commission's ("Commission") Public Utility Division ("PUD"). During my time with PUD, I was responsible for conducting research and performing comparative analysis of utility applications, reports, financial records, and all work papers. My work focused on the areas of cost of service, rate design, and PUD's Accounting Exhibit. While an employee with PUD, I attended numerous utility industry trainings, most of which were related to retail rate and product pricing. Since January 2018, I have been employed with OG&E in various roles in the Regulatory and Finance business units focusing on rates, tariffs, and customer analysis.

Q. **Have you previously testified before the Commission?**

A. Yes. I have testified and/or participated in over 50 cases before the Commission regarding electric, gas, water, and telecommunication issues.

Q. **What is the purpose of your Rebuttal Testimony?**

A. The purpose of this Rebuttal Testimony is to address Responsive Testimonies of Federal Executive Agency witness Michael P. Gorman, Oklahoma Industrial Energy Consumers ("OIEC") witness Mark E. Garrett, and Oklahoma Association of Electric Cooperatives ("OAEC") witness David W. Hedrick related to OG&E's Allowable Expenditure Formula ("Allowable").

ALLOWABLE BACKGROUND

Q. **Please provide an overview of the Commission rules that guide the Company's implementation of its Allowable.**

A. OAC 165:35-25-2 Extension of distribution systems (a), (b), (c), and (d) states,

> (a) Free extension. The utility shall extend its overhead distribution lines a distance of three hundred feet (300') to provide service to each bona fide application for residential service, without cost to the consumer. The utility may prescribe terms and conditions of extending service to applicants for other types of service, and for extensions for low load service such as wells, security lights, and fence charges, and for extension policy required by law or by the terms of a financing agreement; which provisions, when filed with and approved by the Commission, shall be deemed to constitute compliance with this Section.
> (b) Tariff requirements of extension. A utility shall include in its filed tariffs, terms and conditions of furnishing underground service which shall provide for determining and recovery by the utility for the additional cost of providing underground service, and the responsibility for trenching and backfilling, and the method of calculating costs of construction.
> (c) Extension above free limit. If the extension of the distribution system necessary to furnish service to an applicant or group of applicants is greater than specified in (b) of this Section, the utility shall require payment of the cost of the extension over the free limit before extending the distribution system.
> (d) Extension may be made above free limit when economically justified. In lieu of making an extension pursuant to (a) and (b) of this Section, the utility may make an extension above the free limit upon receipt of a lesser payment or no payment, when the gross anticipated annual revenue from the extension will provide the utility with adequate return upon its investment, pursuant to a formula approved by the Commission or contained in its approved terms and conditions of service.

Q. **Please describe how the Company complies with the Commission rules on extension of service mentioned in this Testimony.**

A. In its Commission approved Terms and Conditions of Service, specifically Part IV, the Company provides compliance with these rules. Part IV, Section 408, provides the definition and calculation of the Allowable for the Company. If at any time the Company wishes to make changes to the Allowable formula, the revisions must be provided to the Commission in the form of a letter to the Director of the Public Utility Division of the Commission no later than forty-five days prior to the effective date of the change to the formula and the change to the Allowable shall be subject to the approval of the Director of the PUD. The formula has not substantively changed in 15 or more years. Non-substantive changes include updates to inputs such as tax rate, capital structure, etc. based upon the most recent Commission order.

Q. **What is the purpose of the Allowable?**

A. The purpose of the formula is to calculate the Allowable for when "the utility may make an extension above the free limit upon receipt of a lesser payment or no payment, when the gross anticipated annual revenue from the extension will provide the utility with adequate return upon its investment…"[1] In simple terms, the Allowable ensures the incremental impact of a new project is covered either by the gross annual revenue, or gross annual revenue plus a contribution in aid of construction ("CIAC"). The Allowable is designed to protect all other customers and the Company as new projects are added to the system. Customers and shareholders are protected by ensuring the Company has a high likelihood of receiving the revenues necessary to cover the project. As described further in this Testimony, the Company may also require additional provisions – such as a minimum bill requirement – to provide additional surety for customers.

Adding a customer in a manner in which the incremental revenue (including any applicable CIAC) does not provide an adequate return on investment would be poor business practice and obviously will not result in a competitive advantage. The determination of prudence related to the incremental impact to bring on a project is addressed as part of a rate proceeding such as this Case.

[1] OAC 165:35-25-2 (d).

Q. **Is this the same Allowable that was used to determine what contribution would be required for the projects included in the response to OAEC data request 1-2 in this Case?**

A. Yes.

Q. **Is the same Allowable used if a project is 1 MW competitive or is within OG&E's territorial boundaries?**

A. Yes. The Allowable treats customers equally whether they are subject to 17 O.S. § 158.25(E) or not.

Q. **Does OG&E's Allowable include additional requirements that provide an additional layer of cost recovery assurance on 1 MW competitive projects?**

A. Yes. Every contract for electric service for customers served pursuant to 17 O.S. § 158.25(E) (Exclusive Rights within Territory - New Electric-Consuming Facilities) shall include a provision such as a minimum monthly bill or performance guarantee agreement to address the possibility of early termination of service and recovery of allowable expenditure costs from the customer. This provision currently contained in OG&E's tariffs goes above and beyond what is typically required for customers within OG&E's territorial boundaries which already calculates an adequate return on investment for the Company and thereby protects other customers from those incremental impacts.

RESPONSE TO FEA

Q. **Please address the comments from FEA witness Gorman found on page 14, lines 1-23 page 15, lines 1-2 and page 16, lines 1-12.**

A. In these sections, Mr. Gorman asserts that the Company has not provided any evidence that its Allowable calculation complies with its Commission approved Terms and Conditions of Service.

Q. **Is Mr. Gorman correct in this instance?**

A. No. In response to data request OAEC 2-1, the Company provided examples of its Allowable calculation that demonstrate these calculations comply with its Commission approved Terms and Conditions of Service. As with all data requests, this response was provided to all parties in this Case. To preserve the confidentiality of customer specific information, these examples included redactions. Additionally, unredacted versions of these records were available for all parties to view on site, but only one party requested to view the unredacted versions. While it was not necessary to see the unredacted files to verify the calculation complies with tariff requirements, as with any party in this case, FEA has equal opportunity to view both the redacted and unredacted Allowable examples and the Company has provided evidence of how it calculates Allowable for customers in compliance with the tariff.

RESPONSE TO OIEC

Q. **Please address the comments made by witness Garrett as it relates to the Allowable.**

A. On pages 23-25, Mr. Garrett presents an incorrect argument that CIAC payments are the only method in which incremental investment costs can be offset. This line of reasoning completely ignores the reason for and the application of OAC 165:35-25-2(d) which states, "the utility may make an extension above the free limit upon receipt of a lesser payment or no payment, when the gross anticipated annual revenue from the extension will provide the utility with adequate return upon its investment, pursuant to a formula approved by the Commission…"

Q. **Please summarize the components of the Company's Allowable.**

A. The Company's Commission approved Allowable Expenditure Formula ("AEF") is as follows.

AEF = [EAR – VOC] x SF

Where EAR = Estimated Annual Revenue = Applicable base rate tariff electric revenue inclusive of customer, energy, and demand charges; does not include rider revenues;

VOC = Variable Operating Charge = Operations and Maintenance expenses directly attributable to the line extension, inclusive of fuel, ad valorem taxes, and third-party transmission tap fess (if applicable);

SF = Scaling Factor = The present value of EAR less VOC for each year of the expected years of electric service, net of OG&E corporate taxes, where the present value for each year of the term is discounted to the present by the Company's most recently approved weighted average cost of capital.

Q. **Please explain how Mr. Garretts's arguments do not align with Commission rules and the Company's Allowable.**

A. Mr. Garrett's assertions are not supported by the facts in multiple ways. First, CIAC is required only when the Allowable is insufficient to provide the utility with adequate return upon its investment. This is clearly established in Commission rules. CIAC is not the only mechanism within the Allowable policy to offset these costs. Mr. Garrett is leaving out the actual components of the Allowable formula described above that determine how much expenditure is "allowed" versus what needs to be paid through CIAC. It is inappropriate to assert that if a project does not have a CIAC the "customers have paid virtually none of the costs to extend service."[2] It is also inappropriate to ignore a basic component of the Allowable: the estimated annual revenue used to offset the incremental impact of a project. Additionally, any project that has "gross anticipated annual revenue" above its incremental impact will eventually lower average cost to all customers. Simply stated, when marginal revenue is greater than marginal costs, average cost will be reduced. Mr. Garrett is misrepresenting the purpose and application of the Allowable.

Second, Mr. Garrett attempts to narrow the focus to only 1 MW competitive customers while ignoring the Commission approved formula applies to all OG&E customers, including those OIEC claims to represent. The Allowable is not a "scheme" as Mr. Garrett accuses, it is a Commission approved formula consistent with Commission Rules that is intended to ensure the utility is provided with an adequate return upon its investment, thereby protecting other customers. Additionally, as described above in this Testimony, the Company implements a minimum monthly bill or performance guarantee agreement to address the possibility of insufficient revenue or early termination of service and recovery of allowable expenditure costs from 1 MW competitive customers to further ensure cost recovery protections for existing customers.

Third, Mr. Garrett provides no evidence to support the accusation, and it is not accurate, that the Company "waived the CIAC charges for competitive load outside the

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[2] Responsive Testimony of Mark E. Garrett, Page 23, Lines 16-17.

certified service territory in an attempt to entice those customers onto OG&E's system."[3] The Allowable is a strictly followed formula for all customers. There has been no situation where CIAC is "waived" in an instance where the Allowable shows one is required. Mr. Garrett is incorrect in his accusation that the Allowable is designed to provide a competitive advantage on load outside of OG&E's territorial boundaries. The Allowable applies equally to all applicable customers. As stated previously, basic business theory concludes that adding a customer that does not provide an adequate return on investment will not result in a competitive advantage nor is it a good business practice.

Finally, Mr. Garrett attempts to argue that other customers are paying for the CIAC charges that OG&E failed to collect.[4] This is incorrect and reflects continued misunderstanding of the purpose and application of the Allowable. OG&E has collected CIAC where the Allowable showed one was required. Again, Mr. Garrett is leaving out the actual components of the Allowable formula described previously that determine how much expenditure is "allowed" versus what needs to be paid through CIAC.

RESPONSE TO OAEC

Q. **According to OAEC witness David W. Hedrick, what is the purpose of the Allowable?**

A. On Page 22, lines 19-23 of Mr. Hedrick's Responsive Testimony he states, "the purpose…is to determine the greatest level of plant investment the company can make to provide service to a new customer and recover those cost from that load through current rates."

Q. **Is Mr. Hedrick's description of the purpose of the Allowable, correct?**

A. No. As clearly laid out in Commission rules and the Company's Terms and Conditions of Service, the purpose of the Allowable is to calculate the amount of extension costs that may be made above the free limit when economically justified. This is clearly explained in the formula and complies with OAC 165:35-25-2. It is important to note that there is no effort to maximize the level of potential investment made in these calculations and the Allowable determines the amount of CIAC that may be applicable.

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[3] *Id. Lines 20-21.*
[4] *Id. Page 24, Lines 4-11.*

Q. **Does Mr. Hedrick try to address embedded vs marginal costs within the Allowable?**

A. Yes. Mr. Hedrick states, "The calculation of the allowable investment that a utility can support is not based on marginal costs. Marginal costs are defined as the incremental cost of providing service to a new customer. The rates billed to a customer are designed to recover the embedded costs of providing service as reflected in the utility's cost of service study. Those costs are largely a function of the level of plant investment that has been made to provide service." [5]

Q. **Do the Commission rules reference the inclusion of any embedded costs in the Allowable?**

A. No. The rules specifically reference the costs of the extension of the system itself as necessary to furnish service to a customer. The rules are clear in their intent - the incremental cost, the extension, to serve a new customer is what should be considered in the Allowable. Once connected, the customer is charged its tariff applicable rates based on their classes applicable embedded costs like any other customer.

Q. **Is Mr. Hedrick correct in his opinion of embedded vs marginal costs as they apply within the Allowable?**

A. No. The Allowable is essentially a risk calculator used to ensure that the incremental impact of a project to extend service to a new customer is offset with revenues that will provide the utility with adequate return upon its investment which helps hold existing customers harmless by that addition. If the "rates billed to a customer"[6] in the Allowable are sufficient, or in excess, to cover the new incremental impact of a project, then no CIAC is required. Embedded costs, or total system costs – rate base, are addressed for recovery through cost allocation steps in a rate case proceeding such as this Case. The prudence review of costs associated with projects that have an Allowable are considered in this process. In simple terms, Commission rules guide that Company's Allowable to address the incremental impact of a project whereas a rate case addresses both the embedded costs

5 Responsive Testimony of David W. Hedrick, Page 23, Lines 6-10.
6 *Id.*

and the prudence/inclusion of these new marginal costs in rate base. Mr. Hedrick acknowledges[7] that embedded costs should be addressed during a rate case through the use of a cost of service study. In this instance, OAEC is attempting to implement an anticompetitive practice by inflating the cost side of the Allowable by including costs outside of what is prescribed by Commission rules.

Under Mr. Hedrick's belief, he would include total system costs that overstate the impact of extending service to a new customer. Mr. Hedrick would allocate existing/embedded costs to the new customer even if the expenses associated with extending service to that customer are not associated. His belief assumes all customers should be treated the same as the applicable system average customer. For example, Mr. Hedrick's Responsive Testimony implies that administrative and general expenses would increase by adding a new customer. A counter to this would be that administrative and general expenses would decrease if the project did not come online, which is false. It would not be appropriate to inflate costs considered in the Allowable that would not reasonably occur.

Q. **Please address the statements made by Mr. Hedrick on page 25, lines 3-7.**

A. In this instance, Mr. Hedrick is referencing the Company's response to data request OAEC 2-1 and he states, "…the non-variable operations and maintenance expense was set at zero for the first six years. In this example, the costs recognized in the calculation are even less than the marginal cost of providing service." While Mr. Hedrick is correct that a specific project may not have had variable expenses included for the first six (6) years, he is leaving out a key aspect of the analysis to better fit his narrative. In the example Mr. Hedrick is referencing, those expenses occur on a rolling schedule and maintenance on that equipment would not be expected to be performed within the first six (6) years of the new plant in service. As stated previously, it would be inappropriate to artificially inflate costs considered in the Allowable that would not reasonably occur in a given time.

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[7] *Id. Page 24, Lines 1-5.*

RECOMMENDATIONS

Q. **What are your recommendations to the Commission?**

A. I respectfully request that the Commission reaffirm the more than a decade's worth of approval and precedence of the Company's Allowable policy and find that the accusations made, and approaches suggested, by FEA, OIEC, and OAEC are inappropriate.

Q. **Does this conclude your Rebuttal Testimony?**

A. Yes.