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PSEG Services Corporation

July 27, 2017

In the Matter of the Petition of
Public Service Electric and Gas Company
for Approval of the Next Phase of the
Gas System Modernization Program and
Associated Cost Recovery Mechanism
("GSMP II")

BPU Docket No. GR17070776

VIA E-FILING & OVERNIGHT MAIL

Irene K. Asbury, Secretary
Board of Public Utilities
44 South Clinton Avenue, 9th Floor
Post Office Box 350
Trenton, New Jersey 08625-0350

Dear Secretary Asbury:

Enclosed please find an original and two copies of Public Service Electric and Gas Company's (PSE&G, the Company) filing in the above-referenced matter.

Please be advised that workpapers are being provided via electronic version only.

CMS
LEGAL
DAG] LTR
RPA] ONLY
ENERGY

Very truly yours,

Matthew Weissman

C Attached service list (via e-mail)

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BOARD OF PUBLIC UTILITIES
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STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

In the Matter of the Petition of Public Service Electric and Gas Company for Approval of the Next Phase of the Gas System Modernization Program and Associated Cost Recovery Mechanism ("GSMP II")

BPU DOCKET NO. ________________

VERIFIED PETITION

Public Service Electric and Gas Company (PSE&G, the Company, Petitioner), a corporation of the State of New Jersey, having its principal offices at 80 Park Plaza, Newark, New Jersey, respectfully petitions the New Jersey Board of Public Utilities (Board or BPU) pursuant to N.J.S.A. 48: 2-21, or any other statute the Board deems applicable, as follows:

INTRODUCTION AND OVERVIEW OF THE FILING

1. Petitioner is a public utility engaged in the distribution of electricity and the provision of electric Basic Generation Service (BGS), and distribution of gas and the provision of Basic Gas Supply Service (BGSS), for residential, commercial and industrial purposes within the State of New Jersey. PSE&G provides service to approximately 2.2 million electric and 1.8 million gas customers in an area having a population in excess of 6.2 million persons and which extends from the Hudson River opposite New York City, southwest to the Delaware River at Trenton and south to Camden, New Jersey.

2. Petitioner is subject to regulation by the Board for the purposes of setting its retail distribution rates and to assure safe, adequate and reliable electric distribution and natural gas distribution service pursuant to N.J.S.A. 48:2-21 *et seq.*

3. PSE&G is filing this Petition seeking Board approval of the next phase of its Gas System Modernization Program and associated cost recovery mechanism (GSMP II or Program) for a five-year period. The Program is an extension of PSE&G's current Gas System Modernization Program (GSMP), which was approved by the Board pursuant to an Order dated November 16, 2015. PSE&G anticipates that GSMP II will be conducted over the five-year period 2019 through 2023, as further described herein, and will commence on January 1, 2019, following Board approval.

4. The GSMP II program is comprised of gas utility projects designed to replace cast iron (CI) mains and unprotected steel (US) mains and services; address the abandonment of district regulators associated with this cast iron and unprotected steel plant; rehabilitate large diameter elevated pressure cast iron; upgrade utilization pressure (UP) portions of the system to elevated pressure (EP); replace limited amounts of protected steel and plastic mains; and relocate inside meter sets.[1]

5. The proposed Program would result in the replacement of approximately 250 miles of main per year, with estimated investment of approximately $2.68 billion for the full five years, or approximately $536 million per year.[2] At this time, the Company anticipates these expenditures will result in the replacement of approximately 870 miles of UPCI main (of PSE&G's current inventory of 3,294 miles), 130 miles of EPCI main, 200 miles of unprotected/bare steel main, 50 miles of UP cathodically protected steel and plastic main, and reinforcement of approximately 4,000 EPCI bell joints. This main replacement will result in

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1 For purposes of this petition, "unprotected steel" is steel that is not cathodically protected and includes both bare steel and coated steel.

2 Work required to complete the Program will continue into the first six months of a sixth year of this Program, i.e., through June 30, 2024. The $2.68 billion cost of this Program includes this work.

approximately 266 abandoned district regulators, replacement of approximately 99,200 unprotected steel services, and the relocation of approximately 70,900 inside meter sets to the outside. Where appropriate, services will have excess flow valves installed for improved safety.

6. PSE&G is in the second year of a program that would take 30 years to address all cast iron main and unprotected steel in the distribution system. The Company has demonstrated that it has the capacity to increase the mileage replaced safely and cost-effectively. With this GSMP II filing, PSE&G proposes to accelerate the pace of replacement to 20 years. As discussed in the accompanying testimony, this is the optimal time to accelerate this work given low gas prices, the availability of labor and the corresponding economic stimulus of a continued and expanded program, and the more rapid reduction of greenhouse gas emissions by eliminating leak-prone materials from the system.

7. GSMP II targets all UPCI main diameters, and work prioritization will be based on grid hazard index calculations. UPCI systems will be replaced with EP systems that have improved reliability. EPCI mains will be prioritized by break or leak history, condition, diameter, pressure, and vintage, as well as consideration of EPCI main replacement associated with UPCI and unprotected steel projects. Unprotected steel mains will be prioritized by age, diameter, pressure, and leak history. EPCI joint reinforcement will target large diameter cast iron mains that are not prone to breaks and are not currently planned for replacement but are prone to joint leaks. The reinforcements will reduce the possibility of future joint leaks and reduce potential methane emissions.

8. GSMP II is designed to run for five years, as further described herein, and focuses on modernization of the gas distribution system. These investments will enable the Company to

focus on enhancing the reliability and safety of its gas distribution system in a cost effective manner, and to continue to provide economic stimulus currently being provided by the GSMP program. Although not part of the request in this Petition, the Company anticipates that additional gas distribution system modernization will need to be undertaken beyond this five year Program. The Company anticipates returning to the BPU prior to the expiration of this Program to address continued action of this nature.

9. PSE&G currently performs well with regard to addressing leaks in its system. When compared to companies that operate over 1,000 miles of cast iron, PSE&G is the best in terms of having the least number of main leaks per mile. (PHMSA report data: 2016 F7100.1-1). PSE&G responds to over 80,000 gas emergency calls on an annual basis at a rate of 99.9% within one hour. This ranks within the top decile of peer companies. Since 2014, PSE&G has reduced methane emissions 2.9% annually or a total of 65,000 metric tons of CO_2 equivalent (calculated using EPA Greenhouse Gas Reporting Program: Subpart W – Petroleum and Natural Gas Systems methodology (EPA Subpart W)).

10. Replacement of cast iron and unprotected steel as proposed in this Program builds upon the NJBPU's longstanding proactive approach to addressing aging infrastructure for PSE&G and other utilities. Systematic, long-term replacement allows for greater economies of scale, less municipal disruption, and more efficient execution. Methane emission reduction from this Program is estimated at approximately 199,000 metric tons of CO_2 equivalent per year as of the completion of the Program (calculated using EPA Subpart W), which would be equivalent to removing approximately 42,000 vehicles from the road.

11. The Program includes upgrading of low pressure systems to elevated pressure, which enables the installation of smaller size material, the installation of excess flow valve safety devices, and the use of high efficiency and other appliances by customers. The efficiencies of cost effective construction to replace cast iron mains, unprotected steel mains, and services in this proposed Program and the increased long-term reliability and safety that will result will benefit PSE&G ratepayers and the State for several decades. Proceeding with this Program will also continue PSE&G's support of economic development and enhanced employment opportunities in New Jersey.

12. It is reasonable and prudent to provide for the modernization of the PSE&G gas distribution system to advance the long-term reliability and safety of that system through the Program proposed herein. Accordingly, PSE&G requests that the Board approve this Program, to provide an investment of up to $2.68 billion.

BACKGROUND – ESTABLISHMENT, IMPLEMENTATION AND STATUS OF GAS CAPITAL INFRASTRUCTURE PROGRAMS (CIP I AND CIP II), THE GAS INFRASTRUCTURE PORTION OF ENERGY STRONG, AND GSMP

13. A Capital Infrastructure Program (CIP I) for PSE&G was established in April 2009, with the cooperation and assistance of the Board Staff, the New Jersey Division of Rate Counsel (Rate Counsel), and the Board. The program helped mitigate the negative impacts of poor economic conditions and stimulate the State's economy through investment in additional capital projects, creating new employment opportunities in the state while enhancing service and reliability throughout PSE&G's electric and gas service territories.

14. In CIP I PSE&G proposed to undertake, and the BPU subsequently approved, a program to spend $694 million in capital infrastructure investments, of which $273 million was for

gas infrastructure to be invested over a 24 month period. The results of the accelerated investment in CIP I resulted in the replacement of 200 miles of cast iron and unprotected steel mains and achieved the Board's and PSE&G's job creation and economic growth goals.

15. In July 2011 the Board approved PSE&G's request for an extension of CIP I, to enable the Company to continue that construction program and enhance the reliability of its gas distribution system under a program generally referred to as CIP II. A similar request to extend the electric portion of CIP I was reviewed in parallel with the gas extension. CIP II resulted in the replacement of 47 miles of cast iron and unprotected steel mains.

16. In February 2013, Public Service petitioned the Board for approval of a program (Energy Strong) and for the recovery of costs to harden its electric and gas infrastructure to make them less susceptible to damage from wind, flying debris and water damage in anticipation of future Major Storm Events, and to increase the resiliency of PSE&G's electric delivery system. In an Order issued in May 2014, the Board approved a Stipulation to authorize the Energy Strong Program, which includes an investment level of up to $400 million of investment in gas infrastructure designed to harden gas infrastructure to protect it from future storms. The Energy Strong Program also includes $820 million of electric infrastructure investment.

17. Up to $350 million of the gas portion of the Energy Strong program is for a sub-program for PSE&G to replace an estimated 250 miles of utilization pressure cast iron main and associated services with a higher operating pressure system utilizing plastic or cathodically protected steel mains and services in specified areas. The investment in this gas Utilization Pressure Cast Iron subprogram of Energy Strong was completed in July 2016.

18. In November 2015 the Board approved GSMP, which provided for $650 million in total spend, plus $85 million per year in stipulated base investment that would not be recovered through the GSMP cost recovery mechanism. Up to 400 miles of main were to be installed to replace UPCI and unprotected steel mains. The stipulated base investment would include the replacement of cast iron (UP and EP) and unprotected steel mains and associated services, as well as the costs required to uprate the UPCI systems if applicable (including the uprating of associated protected steel and plastic mains and services) to higher pressures and the elimination, where applicable, of district regulators, the installation of excess flow valves associated with the stipulated base investment, and the additional costs associated with the relocation of inside meter sets that is associated with the stipulated base as well as the program main replacements. During the three years 2016 – 2018, the Company would install no less than 110 miles of main to replace cast iron and unprotected steel mains and associated services under the stipulated base.

19. Under GSMP, as of June 2017 YTD, the Company has replaced approximately 157 miles of main and replaced approximately 11,820 services, or an average of 75 services per mile of main replaced. The Company has also abandoned 16 district regulators associated with the replacement areas. Cost to date is approximately $266 million, or approximately $1.7 million per mile.

20. The cost recovery mechanism and rate of return proposed by PSE&G in this GSMP II Petition and supporting materials are aligned with the Board's recently issued Infrastructure Investment Program regulations described below, and otherwise consistent with the 2015 GSMP order.

FEDERAL AND STATE POLICY SUPPORTING THIS GAS MODERNIZATION INVESTMENT

21. In 2011, the Secretary of the Department of Transportation (DOT), and the Pipeline and Hazardous Materials Safety Administration (PHMSA) issued a "Call to Action," which seeks more aggressive actions on the part of pipeline operators to repair and replace infrastructure that is considered high risk. The PHMSA specifically characterizes cast iron and unprotected steel pipe as categories of pipeline infrastructure that require repair, rehabilitation and replacement. The "Call to Action" was followed by an advisory bulletin issued by PHMSA on March 23, 2012, to owners and operators of natural gas cast iron distribution pipelines and state pipeline safety representatives. The bulletin urges operators of natural gas distribution systems to accelerate replacement of aging infrastructure in order to enhance safety and requests state agencies to consider enhancements to cast iron replacement plans and programs. PSE&G's proposed Program, with a focus on gas projects designed to replace cast iron mains, unprotected steel mains and services, and regulators associated with this cast iron and unprotected steel plant, will provide substantial progress in addressing the goals of the "Call to Action", as described in the attached testimony of Wade E. Miller.

22. The most recent update to the State's Energy Master Plan (EMP)[3] emphasizes continued and increased reliance on natural gas and thus investment in natural gas infrastructure overall as a means of lowering energy costs, decreasing carbon emissions, and enhancing energy security. Specifically, the report states that New Jersey has benefitted from the enhancement and expansion of its natural gas distribution system, which "will help further lower the cost of energy to

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[3] See http://nj.gov/emp/docs/pdf/New_Jersey_Energy_Master_Plan_Update.pdf

New Jersey's homeowners and businesses and reduce emissions." The EMP continues to encourage increased use of natural gas for residential and commercial applications, "including the use of high-efficiency natural gas appliances such as replacing distillate oil appliances with natural gas furnaces and hot water heaters." The most recent EMP update specifically notes that "[the] BPU has approved almost $1 billion for natural gas utility infrastructure upgrades and mitigation projects," and that "[a]n additional $280 million in proposed projects is pending." Finally, the report states that New Jersey "will continue to develop policies that remove barriers and expand the use of the entire array of alternative fuel vehicles," including vehicles powered by Compressed Natural Gas (CNG). PSE&G's proposed investment in gas infrastructure modernization is consistent with these EMP policies.

23. On June 30, 2017, the Board announced a proposed set of regulations (Infrastructure Investment and Recovery (Proposed New Subchapter: N.J.A.C. 14:3-2A, BPU Docket Number: AX17050469), encouraging utilities to implement Infrastructure Investment Programs (IIPs). Specifically, this regulation has been proposed by the BPU to "allow a utility to construct, install, or remediate utility plant and facilities related to reliability, resiliency, and/or safety to provide safe and adequate service. The IIP is a regulatory initiative intended to create a financial incentive for utilities to accelerate the level of investment needed to promote the timely rehabilitation and replacement of certain non-revenue producing components that enhance reliability, resiliency, and/or safety." This filing has been designed to be consistent with the Board's proposed regulations. Appendix 1 attached to this Petition sets forth the location in this filing of all requirements per the Board's proposed regulations.

<u>Benefits to Customers and the New Jersey Economy</u>

24. This proposed Program, like the prior PSE&G Capital Infrastructure Programs and Energy Strong and the current GSMP, will produce many benefits for customers, for PSE&G's gas distribution system, and for the environment. Customers will benefit from a safer, more modern system that accommodates newer technologies and appliances. The replacement of mains and services will enhance the safety and reliability of the system through the use of more modern materials and construction. An additional benefit of GSMP II is an accelerated reduction of greenhouse gas emissions from legacy facilities. The long term 20 year elimination strategy is equivalent to removing approximately 127,000 vehicles from the road.

25. Providing for this Program over multiple years will enable PSE&G to plan to construct these facilities in a cost effective manner, and allow PSE&G to coordinate with municipalities in planning construction.

26. Proceeding with this Program will also continue PSE&G's support of economic development and enhanced employment opportunities in New Jersey. This Program will support additional skilled jobs. Proceeding on a multi-year basis will provide stability and permanence in the jobs the Program creates and supports.

<u>Cost Recovery</u>

27. PSE&G is proposing a cost recovery mechanism for GSMP II that is consistent with the recently proposed BPU Infrastructure Investment and Recovery (IIR) regulations (Proposed New Subchapter: N.J.A.C. 14:3-2A, BPU Docket Number: AX17050469) and the existing Gas System Modernization Program (GSMP I) where applicable. As detailed in the attached Direct Testimony of Stephen Swetz, the cost recovery method will involve semi-annual base rate roll-in

filings, consistent with the proposed IIP regulations and the same approach used for PSE&G's Energy Strong program (for electric investments).

28. Consistent with the IIP proposal, PSE&G proposes to limit each base rate roll-in to a minimum investment level of 10 percent of the total program investment. Therefore, based on the proposed capital expenditure forecast, the first base rate roll-in filing will not occur until December 31, 2019, for rates effective June 1, 2020. Following that initial filing in December 2019, filings will be made at the end of June and December of each year, for rate changes related to plant in-service August 31 of the same year and February 28 (or 29) of the subsequent year, respectively. Those filings would be updated through a second filing that would be due September 15 and March 15, respectively, and that would provide actual data through August 31 and February 28 (or 29), respectively. Under this proposal, the rate adjustment following the June filing would be implemented on the first of December, and the rate adjustment following the December filing would be implemented on the first of June.

29. The main replacement work for GSMP II is scheduled to be complete December 31, 2023. However, close out work such as final paving must wait 3 to 6 months following main installation to allow ground to settle. In addition, trailing charges from contractors may lag into 2024. Without a firm date for completion of this close out work, the Company is proposing a rate filing no later than July 15, 2024 with all actual data for rates effective October 1, 2024.

30. Consistent with the Energy Strong program and GSMP, PSE&G proposes that the costs to be included in rates will include: depreciation/amortization expense providing for the recovery of the invested capital over its useful book life; return on the net investment, where net

investment is the capital expenditures less accumulated depreciation/amortization, less associated accumulated deferred income taxes; and the impact of any tax adjustments applicable to the Program. The return on net investment will be based upon a weighted average cost of capital (WACC). The Company's initial WACC for the Program will be based on the ROE, long-term debt rate and capital structure approved in PSE&G's Solar 4 All Extension II filing in Docket No. EO16050412, which was the latest new program approved for the Company by the Board on November 30, 2016. Any change in the WACC authorized by the Board in a subsequent base rate case will be reflected in the subsequent monthly revenue requirement calculations.

31. BPU Staff and Rate Counsel will have an opportunity to review each roll-in filing to ensure that the revenue requirements and proposed rates are being calculated in accordance with the BPU Order approving the Program. The changes to base rates made through these roll-in filings would be subject to refund based solely upon a Board finding that PSE&G imprudently incurred capital expenditures. The actual prudence of the Company's expenditures in GSMP II will be reviewed as part of PSE&G's subsequent base rate case(s) following the roll-ins. Again, this is identical to the approach under the Energy Strong program and GSMP. Following the base rate case to be filed no later than November 1, 2017, the Company proposes that it will file its next base rate case no later than five years after the commencement of work for GSMP II, anticipated to be December 31, 2023.

32. In addition to limiting the base rate roll-ins to a minimum investment level of 10 percent of the total program investment, PSE&G is also proposing to limit the amount of investment to be included in the rate base roll-ins by an earnings test. Consistent with the IIP, if the Company exceeds the allowed ROE from the utility's last base rate case by fifty (50) basis

points or more for the most recent twelve (12) moth period, the pending base rate roll-in shall not be allowed for the applicable filing period. Details regarding application of the earnings test are set forth in the direct testimony of Stephen Swetz, submitted herewith.

33. This Petition does not propose any rate increase and, for that reason, no public comment hearings are required. Nevertheless, PSE&G proposes public comment hearings similar to those that are held when rate increases are proposed. Thus, a proposed form of public notice of filing and public hearings, including the proposed rates and bill impacts attributable to the proposed implementation of the Program, is attached to the testimony of Stephen Swetz as Schedule SS-GSMPII-7. PSE&G proposes that this Form of Notice will be placed in newspapers having a circulation within the Company's gas service territory upon receipt, scheduling and publication of public hearing dates. As with petitions that propose rate increases, PSE&G proposes that public hearings will be held in each geographic area within the Company's service territory, i.e., Northern, Central, and Southern. A Notice will be served on the County Executives and Clerks of all municipalities within the Company's gas service territories upon receipt, scheduling and publication of public hearing dates.

ATTACHED DIRECT TESTIMONY AND PROPOSED PROCEDURAL SCHEDULE

34. The attached Direct Testimonies of Wade E. Miller and Stephen Swetz provide support for the forgoing and the requests herein.

35. Given the expiration of the Energy Strong main replacement program in July 2016, the anticipated expiration of the GSMP main replacement work in 2018, and the importance of maintaining the support for jobs through PSE&G infrastructure programs and continuity in those programs, it is important for PSE&G to receive Board approval in the first quarter of 2018 to begin

planning for, designing and making the capital investments described herein. Therefore, the Company respectfully requests that the Board retain this matter and utilize a schedule similar to the following procedural schedule:

• Petition and Direct Testimony filed	July 27, 2017
• Prehearing Conference	Week of August 21, 2017
• Discovery on PSE&G Filing	July-September, 2017
• Non-Petitioner Direct Testimony Due	October 15, 2017
• Discovery Requests on Non-Petitioner Testimony	October 16 – November 30, 2017
• Rebuttal Testimony – All Parties	November 20, 2017
• Discovery Requests on Rebuttal Testimony	November 21- December 5, 2017
• Settlement Conferences	Week of December 11, 2017
• Hearings	December 18-22, 2017
• Initial Briefs	January 15, 2018
• Reply Briefs	January 29, 2018
• BPU Decision and Order	1st Quarter 2018

<u>COMMUNICATIONS</u>

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<u>CONCLUSION AND REQUESTS FOR APPROVAL</u>

For all the foregoing reasons, PSE&G respectfully requests that the Board issue an Order approving this Petition no later than the first quarter of 2018 and specifically finding that:

1. The Gas System Modernization Program Extension is in the public interest;

2. The Gas System Modernization Program Extension as described herein is reasonable and prudent;

3. PSE&G is authorized to implement and administer the Program under the terms set forth in this Petition and accompanying Attachments;

4. The cost recovery proposal and mechanism set forth in this Petition will provide for implementation of just and reasonable rates and is approved; and

5. PSE&G may recover all prudently-incurred Program costs, on a full and timely basis, under the cost recovery mechanism set forth herein.

Respectfully submitted,

PUBLIC SERVICE ELECTRIC
AND GAS COMPANY

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DATED: July 27, 2017

STATE OF NEW JERSEY)
:
COUNTY OF ESSEX)

Wade E. Miller of full age, being duly sworn according to law, on his oath deposes and says:

1. I am the Director – Gas Transmission and Distribution Engineering Gas Company, the Petitioner in the foregoing Petition.

2. I have read the annexed Petition, and the matters and things contained therein are true to the best of my knowledge and belief.

Wade E. Miller

Sworn and subscribed to)
before me this 27th day)
of July, 2017)

MICHELE D. FALCAO
Notary Public, State of New Jersey
My Commission Expires
November 14, 2021