

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

**In the Matter of the Petition of
Public Service Electric and Gas Company
for Approval of an Increase in Electric and Gas Rates
and for Changes in the Tariffs for Electric and Gas Service,
B.P.U.N.J. No. 14 Electric and B.P.U.N.J No. 14 Gas
Pursuant to N.J.S.A. 48:2-21 and N.J.S.A. 48:2-21.1
and for Approval of a Gas Weather Normalization Clause;
a Pension Expense Tracker and for other Appropriate Relief**

BPU Docket No. _____

DIRECT TESTIMONY

OF

**MARK G. KAHRER
VICE PRESIDENT-FINANCE**

P-7

1 **PUBLIC SERVICE ELECTRIC AND GAS COMPANY**

2 **DIRECT TESTIMONY**
3 **OF**
4 **MARK G. KAHRER**
5 **VICE PRESIDENT-FINANCE**
6

7 My name is Mark G. Kahrer and I am an employee of Public Service
8 Electric and Gas Company (PSE&G, Public Service, the Company, Petitioner). My
9 business address is 80 Park Plaza, Newark, New Jersey.

10
11 **QUALIFICATIONS**

12 A summary of my qualifications is attached as Schedule MGK-1.
13

14 **PURPOSE OF TESTIMONY**

15 In this PSE&G electric and gas distribution rate case, I am serving as
16 the Company's witness to support financial policy. My testimony addresses:

- 17 • The overall need for the regulatory relief being sought in this filing;
18 • The Company's capital structure;
19 • The growth in the Company's investment in rate base. This filing includes net
20 utility plant investment that has increased \$452.80 million for electric and has
21 increased \$350.46 million for gas since November 2006, when current electric
22 and gas rates were last reset. In addition, my testimony will describe the

1 capital expenditure review process. The testimonies of Messrs. Daly and
2 Cardenas will support the increases in electric and gas distribution plant in
3 service which resulted from capital expenditures for necessary replacements
4 and upgrades of the distribution system to ensure the continuation of safe,
5 adequate, proper and reliable service and expansion to serve new customers.

- 6 • Establishment of a gas weather normalization clause;
- 7 • Changes to the Capital Adjustment Charge (CAC), established by the Board of
8 Public Utilities' (BPU or Board) approval of the Company's Capital Economic
9 Stimulus Infrastructure Investments (CESI) Program, including the
10 establishment of a pension expense tracker and the inclusion of all non-
11 revenue producing electric and gas capital expenditures.
- 12 • Revenue requirements based upon electric and gas operating income for the
13 proposed test year and pro-forma adjustments that are necessary to properly
14 determine a normalized operating year along with adjustments to reflect the
15 levels of activity for the period of time when new rates are expected to be in
16 effect.

17
18 **THE TEST YEAR**

19 The test year in this proceeding is the twelve-month period ending
20 December 31, 2009. The filing consists of three months actual (actual through March

1 31, 2009) and nine months estimated data. I believe the use of a partially forecasted
2 test year is reasonable in that it will facilitate moving this case forward in an
3 expeditious and timely manner. Actual data is supported based upon the Company's
4 accounting records while projected data is based upon the Company's financial and
5 capital budget for the period ending December 31, 2009. The Company will update
6 for actual information during the proceeding to insure that the Board will have as
7 much actual information available as possible when it makes its determination.

8

9 **DESCRIPTION OF SCHEDULES PROVIDED**

10 Schedule MGK-4 presents the electric and gas distribution revenue
11 requirements of \$133.72 million and \$96.92 million, or 1.93% and 2.95%
12 respectively, over existing revenues. The request represents the additional electric
13 and gas distribution revenues the Company requires to meet its obligation to safely
14 and properly serve its customers. Schedule MGK-5 summarizes the electric and gas
15 rate bases, and Schedule MGK-17 reflects electric and gas operating income.

16 Schedules MGK-17 through MGK-44 provide the details of operating
17 income and the pro-forma adjustments, which I discuss later in my testimony.
18 PSE&G's capitalization and the electric and gas revenue factors are presented in
19 Schedules MGK-6 to MGK-8 and MGK-9, respectively.

1 The schedules are based on the books and records of the Company
2 which are maintained in accordance with the Uniform System of Accounts prescribed
3 by the Board and the Federal Energy Regulatory Commission (FERC).

4
5 **OVERVIEW—THE NEED FOR REGULATORY RELIEF**

6 In the approximately three years since Public Service’s rates were
7 changed, the Company has provided safe, adequate, proper, reliable and high quality
8 service to our customers and is committed to providing the same in the future. Over
9 those years, the Company has invested \$904 million in capital dollars in our electric
10 operations and \$606 million in our gas operations to provide that high quality service.
11 Also, over that period, the Company faced the impacts on expenses of “normal”
12 inflation that ran approximately 3.5%, plus the extraordinary increases in benefit costs
13 provided to employees, while the growth in weather-normalized sales has increased at
14 an annual rate of 0.1% for electric and decreased 0.7% for gas. Over the last year,
15 weather-normalized sales for both electric and gas have, in fact, declined, putting
16 more financial pressure on the utility.

17 In addition to the normal challenges of running the business over the
18 past three years, the Company must also deal with the Country’s economic crisis that
19 has unfolded over the past year. This will be more fully described in the testimony of
20 Dr. Michael J. Vilbert. Financial integrity and strength are keys to the Company’s

1 ability to attract the funding needed to maintain our distribution systems and to
2 continue to provide safe, adequate, proper, reliable and high-quality service to our
3 residential, commercial, and industrial customers. Our priorities are aligned with our
4 customers' demands for improvements in reliability to provide electric and gas
5 distribution service, compliance with State and Federal safety requirements, and the
6 installation of appropriate infrastructure so that the State's economy can not only
7 recover in the near term but also flourish in the longer term. The Company's
8 commitment to its customers, the safety of its employees, and support of State
9 initiatives are our top priorities and must not be compromised.

10

11 ***Financial Integrity and Strength***

12 Over the three years since rates were last set, the combination of the
13 items below converged to necessitate this filing:

- 14 • capital expenditures to meet customer needs;
- 15 • impacts of inflation;
- 16 • no/or declining load growth;
- 17 • challenges put forward by the State to address its energy needs in an
18 environmentally responsible fashion; and,
- 19 • collapse of the economy in general.

1 The Company has reached the point where its (1) investments in
2 facilities and the costs of operations to serve our customers, (2) support for the State's
3 initiatives with regards to the Energy Master Plan (EMP) and economic recovery, and
4 (3) ability to provide the Company's owners with a fair and compensatory return are
5 out of step with current rate levels. Absent action now to enhance the Company's
6 financial strength and stability, PSE&G will not be able to meet its goals as described
7 above.

8 Projected earnings are clearly inconsistent with the concepts of financial
9 integrity and financial flexibility. Faced with these difficult economic times and a
10 myriad of goals to achieve, the Company requests that the Board look at the multiple
11 prongs that are part of this filing and give careful consideration to an end result that
12 provides the opportunity to earn a fair, reasonable, and equitable return on our electric
13 and gas utility investments.

14

15 ***For Financial Integrity: The Specific Issues to be Addressed***

16 To provide the financial strength and flexibility needed to run the
17 Company going forward, PSE&G is seeking a new level of rates that provide the
18 financial strength in the near term, and also a level of stability and predictability in the
19 longer term. More specifically, the Company is requesting the following:

- 1 • Base electric and gas distribution rates set at a level such that the Company
2 has the ability to earn an 8.86% return on its invested capital—reflecting an
3 11.50% return on the 51.20% of capital that represents common equity. My
4 testimony discusses, in more detail, the capital structure included in this filing.
5 The testimony of Dr. Michael J. Vilbert supports the need for an 11.50%
6 return on common equity.
- 7 • The creation of a gas weather normalization clause for a level of earnings
8 stability, namely by avoiding dramatic fluctuations due to the vagaries of
9 weather. Creation of such a clause is consistent with the treatment provided to
10 the other gas utilities in the State and recognizes the dramatic impacts weather
11 has on the earnings of gas operations, which are highly seasonal and
12 dependent on the impacts of weather on heating load. PSE&G’s proposed
13 weather normalization clause is similar to those approved by the BPU for the
14 other New Jersey gas utilities and is designed to maintain a level of earnings
15 based on normal weather. If weather is abnormally cold, credits would be
16 granted to customers. If weather is abnormally warm, revenues would be
17 granted to the Company. The testimony of Mr. Stephen Swetz will explain in
18 detail the mechanics of this clause. In this filing, there is no impact reflected
19 from the operations of this clause since this filing reflects “normal weather.”

- 1 • Adjustments to the CAC, which was established in the CESI Program, will
2 allow for longer term financial stability. My testimony will describe the
3 nature and timing of the adjustment to the CAC. The testimony of Mr. Steven
4 Swetz provides the impact on customers' rates.
- 5 • The Company is also proposing the establishment of a mechanism to account
6 for fluctuations in pension expenses to provide financial stability to the
7 Company and ultimately its' customers. The details of this pension expense
8 tracker are described further on in my testimony.

9

10 **CAPITAL STRUCTURE**

11 I am sponsoring a capital structure in this case as presented on Schedule
12 MGK-6 and shown below.

	Amount (\$ Million's)	Percent	Embedded Cost	Weighted Cost
Long-Term Debt	\$3,531	46.60%	6.21%	2.90%
Preferred Stock	80	1.05	5.03	0.05
Customers' Deposits	87	1.15	2.34	0.03
Common Equity	<u>3,879</u>	<u>51.20</u>	11.50	<u>5.89</u>
Total	<u><u>\$7,576</u></u>	100.00%		<u><u>8.86%</u></u>

13

14

15

In general, a company's capital structure is indicative of what the financial community is expecting in order for the Company to be able to raise funds at

1 the best possible rates and whenever the need arises. Raising funds at reasonable
2 costs is dependent upon both the existing market conditions and on the credit-
3 worthiness or credit rating of the company. For PSE&G, it has been some three years
4 since rates were last set reflecting a weighted average cost of capital (WACC)
5 premised on a capital structure with a 47.40% common equity component. Since
6 then, there have been changes in our business that have resulted in increases in our
7 capital requirements coupled with extreme volatility in the financial markets.

8 The need to be able to raise capital is greater than ever. The Company's
9 current petition before the BPU to approve the issuance of up to \$1.3 billion of debt
10 financing is driven by the expectation of a substantial capital program for the years
11 2009 through 2011. This capital program encompasses not only normal replacement
12 expenditures, but also includes meeting the demands of our changing business,
13 including:

- 14 • Supporting the State's initiative to stimulate the economy—the \$694 million
15 CESI program.
- 16 • Supporting the State's goals surrounding the Energy Efficiency Economic
17 Stimulus Program and Carbon Abatement Program—totaling approximately
18 \$215 million.

- 1 • Helping the State achieve its Renewable Portfolio Standards (RPS)
2 requirements through solar-related initiatives requiring capital outlays totaling
3 approximately \$550 million by 2011.

4 The increase in business risk created by these large capital investments beckons for a
5 reexamination of the financial risk of the Company and whether it must reduce that
6 risk in response to the increasing capital requirements. The obvious response to these
7 capital needs has been to strengthen our balance sheet. This thought was voiced
8 earlier this year by James Hempstead, Moody's Investors Service Senior Vice
9 President, who stated:

10 For the long term, the biggest risk could come from new
11 environmental legislation. Although such new laws may
12 be introduced sooner rather than later, it could take some
13 time before the details of implementation are fully worked
14 out. But given the sheer magnitude of the implications for
15 the sector, we remain befuddled as to why utilities are not
16 more aggressive with their balance-sheet strengthening
17 programs.¹

18
19 It was in fact Moody's Investors Service that raised a concern about the
20 cash coverages of PSE&G relative to the level of debt financing employed by the
21 Company. Over the last two years, PSE&G has been in regular contact with Moody's
22 and the Company's other rating agencies to ensure that they understood the strategies
23 for investment decision making. Despite the regular contact, it took PSE&G some

¹ SNL article entitled "Moody's: Electric IOUs Stable in 2009, but Concerns Growing" (dated January 12, 2009)

1 time before it had re-established “stable” outlooks at all three rating agencies. I
2 believe that the achievement of these stable outlooks position the Company
3 appropriately and coupled with improved cash flow from this rate case and the
4 increased equity in the capital structure, will help PSE&G maintain its “stable”
5 ratings. The financial markets today are very different compared to one year ago and
6 are dramatically different than three years ago. An “energybizinsider” article entitled
7 “Attracting Equity” dated February 6, 2009 stated:

8 With September's and October's turmoil, utilities found
9 themselves cut off from some of the lower-cost debt
10 capital available until 2008. They now are paying about 2
11 percent more for borrowed money...

12
13 The result is an increase in investors’ risk aversion. To address this increase in
14 investors risk requires a reduction in the level of financial risk that the Company takes
15 on, which is accomplished by reducing the relative level of debt on its balance sheet.
16 PSE&G has responded to the demands of funding large capital requirements in a
17 volatile financial market place by strengthening its balance sheet via increasing the
18 percent of common equity in its capital structure. The Company’s capital structure is
19 projected to include common equity of 51.20% by December 31, 2009. This equity
20 ratio is required in order for the Company to reasonably finance the needed
21 commitments to meet its obligations to provide safe, adequate, proper and reliable
22 service.

1 **THE CAPITAL EXPENDITURE REVIEW PROCESS**

2 The electric and gas distribution businesses are capital intensive and
3 PSE&G's capital process involves multiple layers of analysis, review, approval and
4 monitoring.

5 • Engineers determine where investment is most needed to keep the distribution
6 system functioning at a safe, adequate, proper and reliable level.

7 • Project managers oversee the engineers and monitor spending and progress.

8 • Vice Presidents, working with planning groups, ensure that PSE&G is
9 allocating resources optimally and perform high-level reviews.

10 • PSE&G Finance coordinates funding requests, ensures proper documentation
11 is prepared and monitors plan versus actual spending.

12 • Senior management at PSE&G, through its Utility Review Board (URB),
13 reviews, approves and monitors the capital investments of PSE&G.

14 • Senior management at PSEG, through its Capital Review Committee (CRC)
15 performs a similar function as the URB.

16 Below I describe in more detail the review and approval process while Messrs. Daly
17 and Cardenas discuss the process supporting project selection and analyses.

1 ***Capital Project Classification***

2 Capital investments are classified into:

- 3 • Three categories by need: (1) tariff/legal, (2) minimum, or (3) priority.

4 Tariff/legal projects are generally non-discretionary and identified through
5 external parties (e.g., to support new service, dictated by environmental or
6 regulatory requirements, or moving distribution lines for road widening).

7 Minimum projects are those that need to be done sooner to avoid distribution
8 network impacts. Priority projects are those that keep the distribution network
9 at peak performance.

- 10 • Five work types: (1) new business, (2) environmental/regulatory, (3) system
11 reinforcement/reliability enhancements, (4) facility replacement, and (5)
12 support facilities.

- 13 • Two project types: (1) blankets and (2) specifics. “Blankets” encompass
14 projects that are small, routine and/or repetitive and that individually cost less
15 than \$1 million to complete. “Specific projects” are those that have clearly
16 identified design parameters.

17

18 ***Capital Expenditure Review, Approval and Monitoring***

19 Because the electric and gas distribution businesses are capital asset
20 intensive, PSE&G’s capital spending process involves multiple layers of analysis,

1 review, approval and monitoring. Each line of business identifies the projects they
2 want to pursue in the coming year and proposes these projects to the URB, which is
3 composed of the President of PSE&G and the Vice Presidents that report directly to
4 him. The projects approved by the URB are then sent to the CRC for funding
5 authorization. The CRC is composed of the CFO of PSEG, subsidiary Presidents,
6 and the Executive Vice President – Planning and Strategy. Also, the PSE&G Board
7 of Directors approves projects that will exceed \$100 million. Project Managers, Vice
8 Presidents, and PSEG Planning and Strategy work in concert to evaluate project
9 validity, coordinate funding requests, ensure proper documentation, monitor project
10 spending and progress, and ensure adherence to spending targets.

11

12 **ADJUSTMENTS TO THE CAPITAL ADJUSTMENT CHARGE**

13 *CAC Reset and Inclusion in Rate Base:* A CAC was established for
14 both electric customers and gas customers effective with the Board's April 16, 2009
15 decision approving the Stipulation of Settlement regarding the CESI. A filing will be
16 made by the Company in October 2009 that would be the basis for establishing new
17 electric and gas CACs effective January 1, 2010 such that costs would be fully
18 recovered over the period January 1 through December 31, 2010. With new base
19 electric distribution and gas distribution rates expected to go into effect on March 1,
20 2010, the CAC effective on January 1, 2010 will be changed effective March 1, 2010

1 to reflect the impacts of rolling the net un-recovered CESI out of the CAC and into
2 the rate base for recovery through the new base distribution rates. This adjustment to
3 the CAC is per the Board's April 16, 2009 decision approving the CESI.

4 *Infrastructure Tracker:* A common theme among the financial
5 presenters at the 2009 National Association of Regulatory Utility Commissioners
6 (NARUC) Winter Committee Meetings was that we are in the midst of slow growth,
7 uncertain and volatile capital markets and a heightened focus on liquidity by
8 investors. The expected reaction in the industry has been a reduction in discretionary
9 investment to enhance current liquidity positions. New Jersey, though, has taken a
10 different direction. The creation of the CESI Program was in support of the State's
11 initiative to proactively grow our way out of the economic problems we are now
12 facing in New Jersey.

13 As Richard McMahon, Jr., Executive Director of Edison Electric
14 Institute (EEI), pointed out in his presentation entitled "Wall Street Turmoil: Impacts
15 on Electric Utilities" (dated February 17, 2009) at the NARUC 2009 Winter Meeting,
16 "The utility industry is at the beginning of a major investment cycle...As one of the
17 most capital-intensive industries, reduced access to capital markets at higher cost,
18 means that enhanced liquidity and financial flexibility is important." The industry
19 and the Company face a difficult decision, to invest or not to invest. If investment is
20 insufficient at this time, electric and gas reliability could be impacted when the

1 economy and demand rebound. The Company must be able to maintain its financial
2 strength and have the flexibility to take advantage of opportunities to access capital
3 markets. An approach to provide the longer term financial stability and flexibility
4 required and to conserve liquidity was suggested by Mihoko Manabe, Vice
5 President/Senior Credit Officer Moody's Investors Service, at the NARUC 2009
6 Winter Committee Meeting. His suggestion was the implementation of an
7 infrastructure tracker that enables a more timely recovery of capital outlays than is
8 normally permitted under rate base / rate of return regulation.²

9 In order for the Company to be able to provide safe, adequate, proper
10 and reliable service to its customers, it must be able to not only recover its operating
11 expenses but also be able to recover its investment in necessary capital facilities. The
12 ability to make capital investments is dependent on our ability to finance the
13 investments. The ability, in turn, to raise the financing in a cost-effective manner is
14 dependent on the ability to recover the return of and on that investment in a
15 predictable and timely manner. The best way to accomplish this is through a clause
16 mechanism that would avoid the need for more frequent full base rate cases. The
17 Company, therefore, is proposing that the CAC, which will be reset concurrently with
18 base rates on March 1, 2010, also reflect a level that allows for the return of and on

² Presentation made by Mihoko Manabe entitled "Credit Trends in the Gas Section Amidst the Financial Crisis" dated February 16, 2009 [slide entitled "Credit Perspective on ROE"].

1 the expected capital expenditures to be made for electric and gas distribution services
2 for the period March 1, 2010 through December 31, 2010.

3 The expected capital expenditures to be recovered through the reset
4 CAC would represent expenditures to support environmental and regulatory
5 requirements, provide reliability enhancements and replace distribution and support
6 facilities. None of these expenditures would support revenue enhancements such as
7 the connection of new customers. As under the current Board-approved CAC, rates
8 would continue to be reset annually to ensure the return of and on these and future
9 capital expenditures on a prospective basis based upon the latest approved WACC.
10 There would continue to be an annual true-up and a review of expenditures at the time
11 of the next base rate case. Any capital expenditures over that period necessary to
12 meet new business needs would not be recovered through the CAC but would be
13 addressed at the time of the next base rate case.

14 *Pension Tracker:* The collapse of the financial markets has resulted in a
15 substantial increase in the Company's pension expense. Pension expense for PSE&G
16 was \$8.3 million in 2008. Based upon the latest actuarial report, test year pension
17 expense has risen to \$73.70 million. PSE&G's analysis shows that the annual
18 expense will increase to approximately \$82 million at the time new base rates go into
19 effect. A significant driver of future pension cost is asset performance, which is
20 subject to the uncertainty of the financial markets. I believe it is important to

1 maintain financial stability for the Company by providing revenues for full collection
2 of pension costs. At the same time, I believe that it is equally important not to over
3 collect these revenues if pension costs fall. The Company is therefore proposing a
4 pension expense tracker to ensure proper cost recovery through the CAC. Such a
5 tracker would ensure timely recognition of increases or decreases in pension expenses
6 through annual rate adjustments in a manner analogous to the way a base distribution
7 rate adjustment would be charged, as described in further detail in the testimony of
8 Stephen Swetz. The proposed pension expense tracker in the CAC would operate in
9 the following way:

- 10 1. The current distribution base rate case will establish revenue sufficient to
11 recover the level of pension expense to be incurred by the Company's electric
12 and gas operations for the twelve-month rate year ending February 28, 2011
13 (which assumes that rates requested in this case go into effect nine months
14 after the date of this filing). This will represent the base upon which the
15 adjustment to be collected through the CAC will be determined.
- 16 2. Any difference between the actual expense and the expense currently in base
17 rates will be deferred each month and included in the CAC over/(under)
18 recovered balance.
- 19 3. CAC rates being reset on January 1st, based on the filing 60 days prior, will
20 reflect revenue requirements associated with this component of the CAC that

1 adjusts for any over/(under) recovery and reflect the differential between the
2 actual pension expense level for the prior calendar year and the level of
3 pension expense reflected in base rates (i.e., new CAC rates set on January 1
4 will represent the prior year's actual expense level with a true-up for the
5 difference between actual expense and what is being collected in base
6 distribution rates).

7 4. At the next and all subsequent distribution base rate cases, after the
8 implementation of this change to the CAC, pension expense levels to be
9 recovered in base rates will be reset thereby resetting the base upon which the
10 adjustment to be collected through the CAC will be determined going forward.

11 There is no impact of the proposed change to the CAC associated with the pension
12 expense tracker as of this time. The first such impact on the CAC would be when the
13 CAC rate is reset on January 1, 2012. See Schedule MGK-2 which lays out a time
14 line for the implementation of this proposed new component of the CAC.

15 *CAC Readjustment:* Schedules MGK-E3 and MGK-G3 present the
16 monthly revenue requirements calculation for the CAC for the period March 1, 2010
17 through December 31, 2010 for electric and gas, respectively. Mr. Swetz's testimony
18 provides the expected impact on the CAC at March 1, 2010 for the items described
19 above.

1 **REVENUE REQUIREMENTS--ADJUSTMENTS TO BASE ELECTRIC AND**
2 **GAS DISTRIBUTION RATES**
3

4 The adjustment to electric distribution base rates and gas distribution
5 base rates is expected to be effective March 1, 2010—nine months after the filing of
6 this Petition. The determination of revenue requirements is premised upon a calendar
7 year 2009 test year with appropriate pro forma adjustments. The Petition reflects a
8 test year with three months of actual data and nine months of projected data. The
9 Company will update the test period information as more actual data becomes
10 available.

11 Pro forma adjustments to the test year have been proposed to reflect the
12 expense level of those items for the twelve months ending February 28, 2011. The
13 costs to be covered include expenses of running the business (including operation and
14 maintenance (O&M) expenses and taxes) as well as return of and on the capital
15 invested that is necessary to run the business (i.e., depreciation and amortizations,
16 interest expense, cost of preferred stock and a fair return on equity invested).

17 Plant additions that are expected beyond the end of the test year but
18 prior to the beginning of the rate year have been included in rate base and I have
19 reflected the impacts of rolling the un-recovered investments made under the CESI
20 program into rate base as described previously. Plant related pro forma adjustments
21 which reflect plant additions during the course of the rate year are not included

1 because those additions are addressed by the adjustment to the CAC described
2 previously.

3 The following is an outline of the supporting schedules included in my
4 testimony:

- 5 • Schedule MGK-4: Determination of Revenue Requirements
- 6 • Schedule MGK-5: Rate Base
- 7 • Schedule MGK-6: Weighted Average Cost of Capital
- 8 • Schedules MGK-7 and 8: Support for WACC components
- 9 • Schedule MGK-9: Revenue Factor
- 10 • Schedules MGK-10 through 16: Support for components of rate base
- 11 • Schedule MGK-17: Income Statement
- 12 • Schedules MGK-18 through 26: Support for components of the income
13 statement
- 14 • Schedule MGK-27: Pro-forma Distribution Operating Income
- 15 • Schedules MGK-28 through 44: Support for pro-forma adjustments to test
16 year operating income

17 Each schedule, where appropriate, will reflect information for both electric
18 distribution and gas distribution.

1 ***Determination of Revenue Requirements—Schedule MGK-4***

2 Schedule MGK-4 shows the determination of the revenue requirement
3 increase being requested in this Petition. Based upon rate bases of \$3.83 billion and
4 \$2.39 billion for electric distribution and gas distribution, respectively, pro-forma
5 operating income of \$260.82 million and \$155.48 million for electric and gas,
6 respectively, and a required rate of return of 8.86%, the increase in required revenue
7 requested is \$133.72 million for electric distribution and \$96.92 million for gas
8 distribution.

9

10 ***Utility Rate Base—Schedule MGK-5***

11 Schedule MGK-5 presents projected total electric and gas utility rate
12 bases at December 31, 2009 and February 28, 2010. Electric rate base is expected to
13 be \$3.69 billion by year end 2009 and \$3.83 billion at the beginning of the rate year.
14 Similarly, gas rate base is expected to be \$2.32 billion by year end 2009 and \$2.39
15 billion at the beginning of the rate year. The rate bases consist primarily of the
16 utility's investment in distribution plant, net of the accumulated provision for
17 depreciation of utility plant plus distribution working capital, reduced by accumulated
18 deferred income taxes. Rate base represents the investment necessary to provide safe,
19 adequate, proper and reliable service to our customers and is therefore a crucial factor
20 in setting future distribution rates. The adjusted rate bases as of February 28, 2010

1 also reflect the inclusion of the then un-recovered investments in capital
2 infrastructure, currently collected through the CAC. The amount included in rate base
3 as of the date new base rates will go into effect is \$120.22 million for electric
4 distribution and \$75.21 million for gas distribution. The components of the
5 Company's distribution rate bases are supported by Schedules MGK-10 through 16
6 and will be addressed below.

7

8 ***Revenue Factor—Schedule MGK-9***

9 The electric revenue factor utilized by the Company in this proceeding
10 is 1.6944. The factor includes the 9% State of New Jersey Corporate Business Tax,
11 the 35% Federal income tax, and the assessments for the Board (0.1853%) and the
12 Division of Rate Counsel (Rate Counsel) (0.0359%). The gas revenue factor is
13 1.7138. The higher factor for gas reflects the inclusion of a rate for uncollectibles of
14 1.13%. Electric uncollectibles are recovered through the Societal Benefits Charge
15 (SBC) and are not in distribution base rates.

16

17 ***Utility Plant In Service—Schedule MGK-10***

18 The electric utility and gas utility plant in service, as shown on Schedule
19 MGK-10, is estimated to be \$6.05 and \$4.72 billion at February 28, 2010,
20 respectively. From November 2006 through December 31, 2008, net electric plant in

1 service has increased by approximately \$452.80 million and net gas plant increased
2 by \$350.46 million. The growth in electric plant investments is discussed in the
3 testimony of Mr. David M. Daly. The investments in gas plant are discussed in the
4 testimony of Mr. Jorge Cardenas.

5
6 ***Plant-In-Service Additions from December 31, 2008 Through the Beginning of the***
7 ***Rate Year—Schedule MGK-11***

8
9 Schedule MGK-11 provides the direct additions to plant in-service from
10 the actual year end 2008 projected through the beginning of the rate year. Additions
11 are expected to total \$385.64 million for electric and \$246.61 million for gas. The
12 additions are primarily distribution plant.

13

14 ***Accumulated Depreciation—Schedule MGK-12***

15 Electric and gas plant in service have estimated useful lives, which
16 normally extends over many operating periods. The systematic recovery of these
17 investments is accomplished by the recognition in rates of annual depreciation
18 charges, with the accumulated depreciation used to reduce rate base utility plant
19 investments. This has been, and continues to be, an acceptable principle in
20 developing rate base since the accumulated depreciation balance infers that these
21 amounts have already been charged to our customers.

1 The accumulated depreciation balance reflects the recognition of annual
2 depreciation charges projected through February 28, 2010 based upon the current
3 BPU-approved electric and gas distribution depreciation rates.

4

5 ***Customer Advances for Construction—Schedule MGK-13***

6 Because the costs of construction related to advances made by the
7 Company's electric and gas utility customers are capitalized and included in the
8 distribution rate bases, it is appropriate to reduce distribution plant costs for these
9 advances. As shown on Schedule MGK-13, I have reduced electric and gas
10 distribution rate base by \$5.45 million and \$4.50 million, respectively, based upon a
11 13-month average of the most current available actual advances—the period March
12 2008 through March 2009. This schedule will be updated for actual test year data, as
13 it becomes available.

14

15 ***Working Capital***

16 Working Capital is the average amount of capital over and above
17 investments in plant and other separately identified rate base items provided by investors
18 of PSEG, to bridge the gap between the time expenditures that are required to provide
19 service and the time collections are received for that service. The Company's proposed
20 working capital allowance is \$206.05 million for electric and \$133.36 million for gas

1 rate base. Each rate base working capital requirement consists of three components:
2 materials and supplies (\$50.63 million for electric and \$12.08 million for gas),
3 prepayments (\$6.71 million for electric and \$4.05 for gas), and cash (Lead/Lag)
4 (\$148.71 million for electric and \$117.23 for gas). The cash working capital
5 requirements are supported by the testimony of Mr. Daniel M. Furlong, Assistant
6 Controller.

7

8 ***Materials and Supplies—Schedule MGK-14***

9 I have included \$50.63 million and \$12.08 million of materials and
10 supplies necessary for ongoing utility electric and gas operations, respectively, in rate
11 base. This is a representative balance of general store items held in inventory for
12 operating and maintenance and capital purposes. It is derived by taking a 13-month
13 average of the most current available actual balances—the period March 2008 through
14 March 2009. This schedule will be updated for actual test year data as it becomes
15 available.

16

17 ***Prepayments—Schedule MGK-15***

18 The Company is also required to make advance payments for certain
19 operating costs, such as insurance and the BPU and Rate Counsel assessments, prior to
20 their being charged to operating expenses. Such prepayments occur every year and

1 therefore require a permanent, ongoing investment by the Company to fund them.
2 Accordingly, I have included the average electric and gas utility prepayment
3 requirements of \$6.71 million and \$4.05 million, respectively, in rate base. These levels
4 are based upon a 13-month average.

5

6 ***Cash (Lead/Lag) Working Capital***

7 The cash (Lead/Lag) working capital allowances reflected on Schedule
8 MGK-5 of \$148.71 million and \$117.23 million that I have included in the electric
9 and gas rate bases, respectively, are the result of detailed Lead-Lag studies supported
10 by Mr. Furlong, in separate testimony and supporting schedules.

11

12 ***Accumulated Deferred Taxes—Schedule MGK-16***

13 Deferred taxes represent the accumulated tax effect of the timing
14 differences between when an item is recognized as a deduction for tax purposes and
15 when it is charged to the customer and included in base rates. Deferred taxes affect the
16 timing of tax payments but not the total amount paid. Since the accumulated deferred
17 tax balances shown on Schedule MGK-16 relate either to electric/gas utility assets
18 included in rate base, or to electric/gas expenses, both of which are utilized in setting
19 customer rates, a rate base deduction is appropriate. The accumulated deferred taxes
20 amount to a \$619.05 million reduction to electric rate base and a \$584.84 million

1 reduction to gas rate base. The reductions are based upon the plant in service balances
2 reflected in the respective rate bases as of February 28, 2010.

3

4 ***Electric and Gas Distribution Operating Income***

5 Schedules MGK-17 through MGK-26 present a complete picture of
6 PSE&G's electric and gas distribution operations. These schedules contain sales,
7 distribution operating revenues, and number of billed customers by class of business
8 for the electric and gas distribution businesses of the Company. Also included are
9 O&M expenses by primary function, depreciation and amortization, taxes other than
10 income taxes, and current and deferred income taxes. Schedule MGK-17 presents the
11 income statements for these business segments. This information has been provided
12 for the calendar year 2008 and twelve-months ending December 31, 2009 which is the
13 test year based on three months actual and nine months estimated.

14

15 ***Pro-forma Distribution Operating Income—Schedule MGK-27***

16 Schedule MGK-27 is a summary of pro-forma adjustments to the test
17 year electric and gas utility operating income. These pro-formas adjust test period
18 operating income for known or measurable changes to expense and income levels so
19 as to reflect the expected expense and income levels for the rate year, which is the
20 first twelve months after new rates are set as a result of this proceeding. Adoption of

1 these adjustments by the Board will provide the Company with a realistic opportunity to
2 earn the reasonable return on its electric and gas investment when the rates are in affect.

3 The Company's revenue requirements determination includes 15
4 adjustments to its test period electric distribution operating income. The pro-forma
5 adjustments lower the test period operating income by \$18.42 million after-tax. On the
6 gas distribution side there are 17 adjustments lowering the test period operating income
7 by \$20.29 million. Each of the pro-forma adjustments will be discussed in more detail
8 below.

9

10 ***Adjustment No. 1: Wages—Schedule MGK-28***

11 These adjustments to operating income of a reduction of \$3.30 million and
12 \$3.71 million for electric and gas, respectively, represent the adjustment to the 2009 test
13 year to reflect wage increases applicable to the rate year. These increases are to the
14 labor costs applicable to Bargaining Unit employees; Management, Administrative,
15 Secretarial and Technical (MAST) employees; and Service Company employees
16 charged to PSE&G. The increases are based on the employee levels during the 2009 test
17 year.

18 In February 2005, the Company and its Unions reached agreement on a
19 six-year contract that expires April 30, 2011, which contains agreed-upon annual
20 increases of 3.25% each year. The wage increases are effective on May 1st. For

1 bargaining unit employees, this pro-forma adjusts the test year's wages through
2 February 28, 2011 to reflect union contract increases of 3.25%.

3 Similar to the adjustment made for bargaining unit employees, MAST and
4 Service Company employees' wages are also adjusted. These adjustments reflect a two
5 percent increase effective annually on April 1st.

6 I urge the Board to continue its consistent practice of recognizing the
7 importance of test year labor adjustments. The Company's employees are a critical
8 element in meeting the service and reliability needs of our customers and this
9 adjustment to the test year insures that the Company's rates will reasonably reflect the
10 cost of this workforce when rates are in effect.

11

12 ***Adjustment No. 2: Payroll Taxes—Schedule MGK-29***

13 The reductions to operating income of \$247,000 and \$278,000 for electric
14 and gas, respectively, result from the increase to operating expense associated with
15 payroll taxes consistent with the wage adjustments made above. This adjustment
16 reflects increases in the Federal Insurance Contribution Act Tax (FICA) for increases in
17 taxable wages and taxable wage ceiling levels. Based on the Company's historic
18 average, additional payroll taxes for the wage adjustment in Schedule MGK-28 are
19 calculated utilizing a composite 7.49% tax rate. This schedule will be updated for actual
20 test year data as it becomes available.

1 ***Adjustment No. 3: Interest Synchronization (Tax Savings) Schedule—MGK-30***

2

3

4 The Board, in the past, has adopted an adjustment to synchronize the
5 Federal income tax savings associated with interest in the test year with the tax
6 savings based on interest calculated using the weighted cost of debt in the capital
7 structure utilized to support rate base.

8

9 As can be seen on the Schedule MGK-30, the interest-bearing components
10 of our capitalization supporting rate base produces synchronized interest expenses of
11 \$299,000 and \$7.46 million more than the test year for electric and gas, respectively,
12 resulting in a tax savings of \$122,000 and \$3.05 million. This adjustment increases
13 operating income.

14

15 ***Adjustment No. 4: Pension and Fringe Benefits—Schedule MGK-31***

16

17 The adjustments to the test year operating income for pension costs and
18 fringe benefits amount to a reduction of \$357,000 for electric and \$4.77 million for
19 gas reflecting the expected increase in these costs over the test period amounts. The
20 adjustment encompasses expenses associated with pensions, OPEB, medical, dental,
21 thrift, long-term disability, insurance and workers compensation for employees
providing support services to PSE&G.

22

23 The pension and OPEB adjustments reflect the expected increase in the
expenses between the rate year and the test year reflecting funding requirements based

1 on actuarial estimates. Other fringe benefit costs are escalated based upon estimates
2 provided by the Company's human resources group derived from research of
3 projections available and past experience.

4 It is widely recognized that the cost of benefits have risen, and are
5 expected to continue to rise, at a pace that outstrips the general rate of inflation. It
6 becomes more important than ever to adjust test year expenses for these items to
7 properly reflect the level of expenses during the time when new rates are in effect.

8 I again urge the Board to continue to recognize that the Company's
9 employees are critical to meeting the service and reliability needs of our customers. The
10 ability to offer a package of wages and benefits will allow the Company to attract and
11 retain skilled employees that are needed. The revenue to cover those costs must be
12 provided.

13

14 ***Adjustment No. 5: Electric / Gas Company Owned Life Insurance (COLI) Interest***
15 ***Expense—Schedule MGK-32***

16

17 In an effort to reduce a portion of the expenses associated with certain
18 employee benefit plans, PSE&G has invested in COLI policies. COLI is a corporate
19 owned investment in cash value life insurance, which provides an income stream to the
20 Company.

21

22 A portion of the Company's workforce is covered by policies with the
Company as owner and beneficiary. The cash value of the insurance contracts earn a

1 return, which the Company utilizes to offset benefit expenses. The Company, as owner,
2 is permitted to borrow against the policy during its life without interfering with the
3 policy's accumulation of earnings. The policy provides life insurance proceeds upon the
4 death of the insured sufficient to settle any outstanding loans.

5 The earnings associated with the growth in the policy's cash surrender
6 value have produced a net credit to benefits expense. For the test year, the credit to
7 Administrative and General Expense combined with tax savings is \$11.95 million for
8 electric distribution and \$3.28 million for gas distribution. Interest expense on funds
9 borrowed from the policy are directly related to the \$15.23 million in benefits
10 attributable to the policy. My adjustments to the test year is to include the gross interest
11 cost of \$8.78 million for electric and \$2.77 million for gas thereby reducing operating
12 income to properly account for all aspects, both benefits and costs, of the COLI.

13

14 ***Adjustment No. 6: Postage—Schedule MGK-33***

15 This adjustment reflects the United States Postal Services rate increase of
16 May 2009 and an expected increase in 2010. The increase per bill was applied to
17 electric and gas customer bills and annualized over a twelve-month period which
18 produced the proposed respective \$623,000 and \$510,000 electric and gas increases to
19 test year operating expenses shown in Schedule MGK-33. Test year operating income is
20 therefore reduced by \$369,000 and \$302,000 for electric and gas, respectively.

1 ***Adjustment No. 7: BPU and Rate Counsel Assessments—Schedule MGK-34***

2 In accordance with the New Jersey statutory requirements (N.J.S.A.
3 48:2-60 (Board) and N.J.S.A. 52:27E-61 (Rate Counsel)), the Company provides the
4 State of New Jersey annual assessments associated with the operations of the Board and
5 Rate Counsel. These assessments are predicated on rates established by the State of
6 New Jersey and are applied to each revenue dollar recorded by the Company for the
7 preceding year. The estimated assessment rates are 0.1853% for the Board and 0.0359%
8 for Rate Counsel. By applying this rate to 2009 test year electric and gas revenues, the
9 Company has estimated the assessment at \$12.74 million and \$7.10 million for electric
10 and gas, respectively. The adjustment of \$2.48 million for electric and \$980,000 for gas,
11 increases test period operating expenses to that level, and is appropriate to be adopted by
12 the Board. It places the test year expense for this item at a level that the Company will
13 incur while the new rates are in effect, thereby reducing test year operating income by
14 \$1.47 million and \$579,000 for electric and gas, respectively.

15

16 ***Adjustment No. 8: Weather Normalization—Schedule MGK-35***

17 This pro-forma adjusts test year actual results to reflect normal weather
18 based on weather patterns over a 20-year period as measured at Newark Liberty
19 International Airport. Because actual weather patterns during the time the rates will
20 be in effect are assumed to be normal, this adjustment to the test year is an appropriate

1 rate setting procedure. The use of unadjusted weather-related actual sales levels
2 would result in overstating or understating the revenue requirement compared to
3 normal. The plan data included in our test year is based on a weather normalized
4 sales forecast and requires no adjustment. However, as we move toward the
5 conclusion of the case and provide updates for actual data, the Company will weather-
6 normalize the additional months of actual data as required.

7 Schedule MGK-35 shows the adjustments necessary to reflect normal
8 weather for the period January through March 2009. This schedule shows a comparison
9 of the margin revenue for the first three months actual to that based upon normal
10 weather. Margin revenue represents the revenue from the sale of a kWh or therm less
11 the variable revenue associated with the commodity, SUT, TEFA and SBC. In order to
12 adjust the actual results to a normal sales level, a decrease to test period revenue of \$1.10
13 million and \$11.10 million, for electric and gas respectively, is required since the first
14 three months of the test year, January to March 2009, were colder than normal. The
15 adjustment to revenue reduces operating income by \$648,000 and \$6.56 million for
16 electric and gas, respectively.

17

18 ***Adjustment No. 9: Gains/Losses on Sales of Property—Schedule MGK-36***

19 This adjustment allocates one-half of the gain on sales of property, net of
20 associated income taxes, to the customer based on a five-year average. The use of a

1 five-year average provides a representative amount of gains for ratemaking purposes
2 avoiding the distortion that would occur if an abnormally high or low level of gains are
3 recognized in the test period. The Company has included the five-year average for the
4 years 2005 through 2009 as representative and appropriate for this proceeding. As
5 detailed in Schedule MGK-36, the adjustment to operating income for the customers'
6 share of the five-year average gain is an increase of \$88,000 for electric and \$27,000 for
7 gas.

8

9 ***Adjustment No. 10: Management/Affiliated Standards Audit—Schedule MGK-37***

10 The Board performs audits of the utilities which it regulates. Affiliated
11 Standards audits are to take place approximately every three years. Management
12 audits are conducted every five years. At this time the BPU is beginning a combined
13 Management and Affiliated Standards audit of PSE&G. As of the time of this filing,
14 the Board has issued a Request for Proposal (RFP) to retain a firm to conduct the
15 audit. PSE&G has retained the firm of Huron Consulting Group to assist the
16 Company in this process. The Company expects the cost of the entire audit process to
17 be \$3.1 million, reflecting the cost of the Company's consultant and an estimate,
18 based on past history of similar audits, of the cost of the consultant to be retained by
19 the Board. For purposes of the pro-forma adjustment, the expected total cost is
20 amortized over four years. That normalized cost is compared to the dollars reflected

1 in the test year of \$2.1 million. The difference between the normalized cost and the
2 expense reflected in the test year results in an adjustment lowering the expense and
3 thereby increasing the operating income by \$778,000. This adjustment is allocated
4 55% to electric and 45% to gas—the allocation reflecting the relative number of
5 customer accounts.

6

7 ***Adjustment No. 11: Customer Information System Amortization—Schedule MGK-***
8 ***38***

9

10 In the Company's efforts to provide safe, adequate, proper and reliable
11 service to its customers and to enhance customer satisfaction by reducing response
12 time and facilitating customer contact through its customer operations function, it has
13 invested approximately \$111.13 million of its capital to develop a new customer
14 information system (CIS) to replace its existing system, which dates back over 20
15 years. The new system was placed into service in April 2009. The capital investment
16 is reflected in the electric and gas rate bases. In order to make the CIS operational,
17 the Company incurred considerable expenses principally associated with training
18 customer service representatives in its use. Those expense dollars (\$28.72 million)
19 were deferred pending recovery in this rate proceeding. Consistent with treatment of
20 other deferred items (e.g., accumulated restructuring costs and repair allowance) this
21 pro-forma adjustment is an increase in test year amortization expense to allow for a
22 ten-year levelized amortization of \$4.34 million annually, which includes a carrying

1 charge at the after-tax rate of return of 8.86% in lieu of including the unamortized
2 balance in rate base. This amortization adjustment is allocated 55% to electric and
3 45% to gas, which reflects the relative number of customer accounts. The impact is a
4 reduction in test year operating income of \$1.41 million and \$1.16 million for electric
5 and gas, respectively and will be updated for year-end depreciation as the amounts
6 become known.

7

8 ***Adjustment No. 12: Real Estate Taxes—Schedule MGK-39***

9 This adjustment of \$118,000 for electric and \$49,000 for gas increases
10 the test year operating expense to be representative of the level of property tax
11 expense that is expected to be accrued in the twelve-month period following the date
12 new base rates go into effect. The increase in property tax expense between the rate
13 year and the test year is consistent with actual experience. The increase reflects an
14 estimate of an increase in the property tax rate based upon the Company's experience
15 over the last two years. Accordingly, electric and gas operating income is reduced
16 \$70,000 and \$29,000, respectively.

17

18 ***Adjustment No. 13: Capital Stimulus—Schedule MGK-40***

19 Through the April 16, 2009 BPU decision approving the CESI program
20 and the associated cost recovery mechanism or CAC; the Company must reflect the

1 impacts of rolling the un-recovered in-service CESI out of the CAC and into rate base
2 for recovery through the new distribution base rates. This adjustment is to reflect the
3 impact on expenses and therefore operating income of moving that investment into
4 rate base. Specifically, the adjustment is to allow for recovery of the depreciation
5 expense associated with the investment through the new base rates. To arrive at the
6 pro-forma adjustment to expenses, the depreciation expense being recovered through
7 the CAC in the month prior to when new base rates go into effect, is annualized by
8 multiplying by twelve. The result is an increase to depreciation expense of \$2.53
9 million for electric and \$1.49 million for gas. Accordingly, test year operating
10 income is reduced \$1.50 million for electric and \$879,000 for gas.

11

12 ***Adjustment No. 14: Insurance—Schedule MGK-41***

13 There are items for which PSE&G carries outside insurance policies
14 (i.e., Corporate Property, Excess Liability Insurance and Director’s & Officers
15 Insurance) for which it pays premiums of approximately \$3.90 million for electric and
16 \$2.54 million for gas. This adjustment of \$587,000 for electric and \$384,000 for gas
17 increases the test year operating expense to be representative of the level of insurance
18 expense that is expected to be accrued in the rate year. The increase in insurance
19 expense between the rate year and the test year is estimated to be 15% and reflects
20 input from our insurance carriers and actual experience.

1 ***Adjustment No. 15: EMP Clauses—Schedule MGK-42***

2 Today, as part of its business, PSE&G is investing capital and incurring
3 expenses to provide safe, adequate, proper and reliable services to its electric and gas
4 customers as well as supporting other initiatives developed by the State. Among
5 those initiatives is support for New Jersey's EMP. Return of and on the investments
6 developed in support of the EMP and recovery of associated expenses is
7 accomplished from receipt of revenue collected through the RGGI Recovery Charge
8 (RRC). Within the test year operating income are revenue, depreciation/amortization
9 expenses, O&M costs and expenses associated with over/(under) recovery for
10 programs which are currently reflected in the RRC. This adjustment is required to
11 remove those items from the test year operating income to arrive at an operating
12 income for purposes of setting distribution base rates. The adjustment for gas reflects
13 those items associated with the Company's Carbon Abatement Program approved by
14 the Board. The adjustment for electric is for both the Carbon Abatement Program and
15 the Solar Loan Program which was also approved by the Board. The adjustment to
16 remove the items described above results in a decrease in test year operating income
17 of \$560,000 for electric distribution and \$83,000 for gas distribution.

1 ***Adjustment No. 16: Cost of Removal—Schedule MGK-43***

2 The BPU decision in the Company’s most recent gas base rate case,
3 Docket No. GR05100845, adopted the Stipulation of Settlement whereby the cost of
4 removal (COR) recoverable through rates for gas distribution was set at \$6.38 million on
5 an annual basis reflecting the average actual annual expenditure on COR for the five-
6 year period 1999 through 2003. Consistent with that methodology for establishing the
7 COR recoverable through rates, an adjustment is made to operating income for gas
8 distribution to reflect an increase in COR from the \$6.38 million currently in rates to
9 \$10.37 million based upon the average actual annual expenditure on COR for the five
10 year period 2004 through 2008. This adjustment results in a reduction to the test year
11 operating income of \$2.36 million for the gas distribution business. The electric
12 depreciation rates do not reflect this COR methodology as the Company does not
13 believe that methodology is appropriate.

14

15 ***Adjustment No. 17: TSG-NF Margin—Schedule MGK-44***

16 The Company currently retains a portion of the margins from gas service
17 to new TSG-NF customers that commenced after the Company’s base rate cases in 2001
18 and 2005, in accordance with the Settlements and Board Orders in Docket Nos.
19 GR01050297 and GR05100845. The annual amounts retained by the Company include
20 a 20% carrying charge on the cost of the new facilities required to serve all such

1 customers, net of any customer contribution. Also, the Company retains the margins
2 (total revenue less commodity revenue, SUT, TEFA, SBC, RGGI and CAC) from
3 customers who switch from Rate Schedule LVG to TSG-NF. Conversely, the margins
4 from customers who switch from TSG-NF to LVG are credited to the Margin
5 Adjustment Charge (MAC) in lieu of being retained by the Company. The balance of
6 the margin is credited to the MAC. These retained amounts are reset to zero in each
7 succeeding base rate case. Therefore, this adjustment, a reduction to gas operating
8 income in the amount of \$6,000, is being made. This issue is further discussed in the
9 testimony of Mr. Swetz.

10

11 **SUMMARY**

12 I would like to emphasize that our Company has not reset electric or gas
13 distribution rates since 2006. Since that time, the Company has continued its
14 commitment to safety and reliability in fulfilling its obligation to provide safe,
15 adequate, proper and reliable electric and gas services to its customers. It has further
16 committed to support the State's initiatives with regards to the EMP and economic
17 recovery. The Company has now reached the point where the cost of operations and
18 the investments made to serve our customers and support initiatives vital to New
19 Jersey need to be updated from those reflected in our current rates. Our employees
20 and management have worked prudently and diligently and with great success to

1 provide safe, adequate, proper, and reliable electric and gas service at reasonable
2 rates. New requirements are being incurred, especially in the area of activities and
3 costs related to the infrastructure of the electric and gas distribution system, which
4 directly address the needs of our customers across the State. Necessary expenditures
5 to serve our customers render the Company's current electric and gas base rates
6 inadequate. I request that the Board and the parties in this proceeding perform their
7 duties in a timely and efficient manner and that the Board approve the rate relief as
8 requested by the Company.

9 As discussed in detail in Messrs. Daly's and Cardenas' testimonies, the
10 Company has consistently made efforts in all areas of its operations to provide service
11 to our customers in the most efficient and cost-effective ways possible. The
12 Company's requested base rates are just and reasonable, and afford the Company an
13 opportunity to earn a fair rate of return. The requested rates provide for the financial
14 flexibility needed to accomplish the Company's goals while at the same time enabling
15 it to provide safe, adequate, proper and reliable cost-based service to customers.
16 Without timely and adequate rate relief the Company will be financially weakened,
17 resulting in the loss of its financial flexibility, and impairing our ability to serve
18 current and future customers, thereby threatening a basic driver of New Jersey's
19 economic well being.

1 I trust that the Board, its Staff, the Division of Rate Counsel and any
2 other parties will give this case their focused attention so that rate relief will be
3 approved expeditiously.

4 This concludes my testimony at this time.

1 **PUBLIC SERVICE ELECTRIC AND GAS COMPANY**
2 **PROFESSIONAL QUALIFICATIONS**
3 **OF**
4 **MARK G. KARHER**
5 **VICE PRESIDENT-FINANCE**

6 I have been employed at PSEG for more than 25 years, serving in a
7 number of financial positions in the company including Director – Corporate
8 Accounting, Director – Financial Risk Management, Assistant Treasurer and, most
9 recently, Vice President – Finance and Development of PSEG Power LLC, prior to
10 my appointment as Vice President – Finance for PSE&G. In those roles, I was
11 responsible for closing the corporation’s books of record, filing compliance reports
12 with the Securities and Exchange Commission and the Federal Energy Regulatory
13 Commission, establishing a risk governance framework and policies, overseeing the
14 administration of more than \$4.5 billion in pension, 401(K) and nuclear
15 decommissioning trust funds, implementing the corporation’s insurance programs and
16 leading the corporate finance group, which was responsible for issuing more than \$7
17 billion in debt and equity securities during my tenure. In addition, I was also
18 responsible for managing PSE&G’s relationships with financial rating entities such as
19 Fitch Ratings, Moody’s Investors Service and Standard and Poor’s.

20 I have a Bachelor of Science degree in accounting from St. Peter’s
21 College, a Masters in Business Administration with a concentration in finance from
22 Seton Hall University, and I am a Certified Public Accountant licensed in the State of
23 New Jersey.

**ILLUSTRATIVE TIME-LINE
CAPITAL ADJUSTMENT CHARGE**

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- October 2009 Filing to reset the CAC effective January 1, 2010. Reflects revenue requirements for Capital Economic Stimulus Investments (CESI) to date plus projected for calendar year 2010.
- January 1, 2010 New CAC implemented.
- March 1, 2010 New electric and gas distribution rates set. Reflects cost recovery of in-service CESI and pension expense at level to be incurred for the 12-months ending February 28, 2011.
- March 1, 2010 CAC reset for the period March 1, 2010 through December 31, 2010. Reflects removal of in-service CESI (rolled into base rates) and inclusion of electric and gas distribution capital expenditures (excluding revenue producing new business related) for the period March 1, 2010 through December 31, 2010.
- October 2010 Filing to reset the CAC effective January 1, 2011. Reflects revenue requirements for CESI and electric and gas distribution capital expenditures to date being recovered in the CAC plus projected for calendar year 2011.
- January 1, 2011 New CAC implemented.
- March 2011 Company establishes pension expense for 2011 based upon latest actuarial report and funding plan.
- Monthly in 2011 Difference between 2011 pension expense and level of pension reflected in base rates is added to the CAC over/(under) recovered balance.
- October 2011 Filing to reset the CAC effective January 1, 2012. Reflects revenue requirements for CESI and electric and gas distribution capital expenditures to date being recovered in the CAC plus projected for calendar year 2012, recovery of over/(under) recovered balance, and the differential between the Company's 2011 pension expense level and the pension expense level in base rates.
- January 1, 2012 New CAC implemented.

**EXHIBIT P-7
SCHEDULE MGK-E3**

PSE&G Capital Stimulus Infrastructure Investment Program
Electric Revenue Requirements Calculation - Monthly

					Prior Month + Col 3	Col 2 - Col 4		(Col 6 - Col 7) * [Income Tax Rate]	Prior Balance + Col 8	Col 5 - Col 9	(Prior Col 10 + Col 10) / 2 * Monthly Pre Tax WACC	Program Assumption	Col 7+ Col 11 + Col 12	
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Month	Year	<u>Program Investment</u>	<u>Gross Plant</u>	<u>Depreciation Expense</u>	<u>Accumulated Depreciation</u>	<u>Net Plant</u>	<u>Tax Depreciation</u>	<u>Book Deprec Tax Basis</u>	<u>Deferred Tax Exp</u>	<u>Accumulated Deferred Tax</u>	<u>Net Investment</u>	<u>Return Requirement</u>	<u>O&M Expense</u>	<u>Calendar Revenue Requirements</u>
1	Jan	2009	-	-	-	-	-	-	-	-	-	-	-	-
2	Feb	2009	-	-	-	-	-	-	-	-	-	-	-	-
3	Mar	2009	-	-	-	-	-	-	-	-	-	-	-	-
4	Apr	2009	-	-	-	-	-	-	-	-	-	-	-	-
5	May	2009	300,000	300,000	-	-	300,000	-	-	-	300,000	1,626	-	1,626
6	Jun	2009	500,000	800,000	-	-	800,000	-	-	-	800,000	5,961	-	5,961
7	Jul	2009	700,000	1,500,000	-	-	1,500,000	-	-	-	1,500,000	12,464	-	12,464
8	Aug	2009	3,195,000	4,695,000	-	-	4,695,000	-	-	-	4,695,000	33,570	-	33,570
9	Sept	2009	3,495,000	8,190,000	-	-	8,190,000	-	-	-	8,190,000	69,823	-	69,823
10	Oct	2009	3,695,000	11,885,000	-	-	11,885,000	-	-	-	11,885,000	108,785	-	108,785
11	Nov	2009	4,395,000	16,280,000	-	-	16,280,000	-	-	-	16,280,000	152,625	-	152,625
12	Dec	2009	5,395,000	21,675,000	-	-	21,675,000	-	-	-	21,675,000	205,676	-	205,676
13	Jan	2010	5,895,000	27,570,000	-	-	27,570,000	-	-	-	27,570,000	266,856	-	266,856
14	Feb	2010	6,995,000	34,565,000	-	-	34,565,000	-	-	-	34,565,000	336,707	-	336,707
15	Mar	2010	39,878,647	74,443,647	93,524	93,524	74,350,123	639,071	93,524	224,132	224,132	74,125,990	588,991	1,282,516
16	Apr	2010	41,378,647	115,822,294	189,124	282,648	115,539,646	1,281,267	189,124	448,696	672,829	114,866,817	1,024,143	1,813,267
17	May	2010	42,578,647	158,400,941	285,761	568,409	157,832,532	1,925,026	285,761	673,476	1,346,304	156,486,227	1,470,449	2,356,210
18	Jun	2010	42,728,647	201,129,588	386,444	954,853	200,174,735	2,574,878	386,444	899,096	2,245,401	197,929,334	1,920,561	2,707,005
19	Jul	2010	41,627,647	242,757,235	494,180	1,449,033	241,308,202	1,645,853	494,180	473,153	2,718,554	238,589,648	2,365,476	3,259,656
20	Aug	2010	40,327,647	283,084,882	624,326	2,073,360	281,011,522	3,924,610	635,428	1,355,888	4,074,442	276,937,080	2,793,615	3,817,941
21	Sept	2010	38,477,647	321,562,529	718,264	2,791,623	318,770,906	4,564,303	729,365	1,580,107	5,654,549	313,116,357	3,197,472	4,315,736
22	Oct	2010	40,727,647	362,290,176	814,380	3,606,003	358,684,173	5,207,277	825,481	1,804,778	7,459,327	351,224,846	3,600,034	4,814,414
23	Nov	2010	42,277,647	404,567,823	911,015	4,517,018	400,050,805	5,851,033	922,116	2,029,557	9,488,884	390,561,921	4,019,708	5,530,722
24	Dec	2010	41,827,647	446,395,470	1,015,431	5,532,449	440,863,021	6,506,507	1,031,097	2,255,954	11,744,838	429,118,184	4,441,808	6,057,239

**EXHIBIT P-7
SCHEDULE MGK-G3**

PSE&G Capital Stimulus Infrastructure Investment Program
Gas Revenue Requirements Calculation - Monthly

					Prior Month + Col 3	Col 2 - Col 4		(Col 6 - Col 7) * [Income Tax Rate]	Prior Balance + Col 8	Col 5 - Col 9	(Prior Col 10 + Col 10) / 2 * Monthly Pre Tax WACC		Col 7+ Col 11 + Col 12	
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Month	Year	Program Investment	Gross Plant	Depreciation Expense	Accumulated Depreciation	Net Plant	Tax Depreciation	Book Deprec Tax Basis	Deferred Tax Exp	Accumulated Deferred Tax	Net Investment	Return Requirement	O&M Expense	Calendar Revenue Requirements
1	Jan	2009	-	-	-	-	-	-	-	-	-	-	-	-
2	Feb	2009	-	-	-	-	-	-	-	-	-	-	-	-
3	Mar	2009	-	-	-	-	-	-	-	-	-	-	-	-
4	Apr	2009	-	-	-	-	-	-	-	-	-	-	-	-
5	May	2009	-	-	-	-	-	-	-	-	-	-	-	-
6	Jun	2009	50,000	50,000	-	50,000	-	-	-	-	50,000	271	-	271
7	Jul	2009	50,000	100,000	-	100,000	-	-	-	-	100,000	813	-	813
8	Aug	2009	50,000	150,000	-	150,000	-	-	-	-	150,000	1,355	-	1,355
9	Sept	2009	50,000	200,000	-	200,000	-	-	-	-	200,000	1,897	-	1,897
10	Oct	2009	100,000	300,000	-	300,000	-	-	-	-	300,000	2,709	-	2,709
11	Nov	2009	100,000	400,000	-	400,000	-	-	-	-	400,000	3,793	-	3,793
12	Dec	2009	700,000	1,100,000	-	1,100,000	-	-	-	-	1,100,000	8,128	-	8,128
13	Jan	2010	50,000	1,150,000	-	1,150,000	-	-	-	-	1,150,000	12,193	-	12,193
14	Feb	2010	50,000	1,200,000	-	1,200,000	-	-	-	-	1,200,000	12,735	-	12,735
15	Mar	2010	15,695,185	16,895,185	41,920	16,853,265	313,515	41,920	111,582	111,582	16,741,683	97,225	100,996	240,141
16	Apr	2010	15,822,010	32,717,195	83,541	32,591,734	626,306	83,541	222,990	334,572	32,257,162	265,522	100,996	450,059
17	May	2010	24,894,338	57,611,532	136,719	57,349,353	1,037,090	136,719	369,908	704,480	56,644,873	481,756	201,991	820,466
18	Jun	2010	29,544,741	87,156,274	195,579	86,698,515	1,496,112	195,579	534,311	1,238,791	85,459,724	770,058	252,489	1,218,126
19	Jul	2010	33,615,433	120,771,707	260,992	120,052,956	2,004,741	260,992	716,402	1,955,193	118,097,763	1,103,068	302,987	1,667,047
20	Aug	2010	31,851,177	152,622,883	323,826	151,580,307	2,490,238	323,826	890,049	2,845,242	148,735,065	1,445,955	277,738	2,047,518
21	Sept	2010	34,096,876	186,719,760	389,267	185,287,916	3,000,698	389,267	1,072,880	3,918,122	181,369,794	1,788,823	302,987	2,481,077
22	Oct	2010	36,196,796	222,916,555	457,464	1,889,308	221,027,248	3,534,691	457,464	1,264,248	215,844,878	2,152,488	328,236	2,938,188
23	Nov	2010	29,413,010	252,329,565	522,384	2,411,692	249,917,873	4,013,075	522,384	1,434,115	6,616,485	2,488,092	252,489	3,262,965
24	Dec	2010	33,538,343	285,867,908	586,940	2,998,632	282,869,276	4,523,515	586,940	1,617,303	8,233,788	2,806,676	302,987	3,696,602

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

DETERMINATION OF REVENUE REQUIREMENTS
(\$000)

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Rate Base	\$ 3,833,261	\$ 2,392,426	\$ 6,225,687
Rate of Return	<u>8.86%</u>	<u>8.86%</u>	<u>8.86%</u>
Operating Income Requirement	\$ 339,735	\$ 212,036	\$ 551,772
Pro-Forma Operating Income	<u>\$ 260,816</u>	<u>\$ 155,483</u>	<u>\$ 416,299</u>
Operating Income Deficiency	\$ 78,919	\$ 56,553	\$ 135,472
Revenue Factor	<u>1.6944</u>	<u>1.7138</u>	
Revenue Requirements	<u><u>\$ 133,720</u></u>	<u><u>\$ 96,921</u></u>	<u><u>\$ 230,641</u></u>

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ELECTRIC RATE BASE
(\$000)

	Balance at December 31, 2009*	Balance at February 28, 2010	Capital Infrastructure Per Stipulation February 28, 2010	Adjusted Balance at February 28, 2010
Plant In Service	\$ 6,004,951	\$ 6,053,872	\$ 136,059	\$ 6,189,931
Plant Held for Future Use	3,580	3,580	-	3,580
Accumulated Depreciation Reserve	(1,907,960)	(1,925,958)	(904)	(\$1,926,862)
Customer Advances	(5,449)	(5,449)	-	(5,449)
Net Plant	<u>\$ 4,095,121</u>	<u>\$ 4,126,044</u>	<u>\$ 135,155</u>	<u>\$ 4,261,199</u>
Working Capital:				
Cash (Lead/Lag)	148,705	148,705	-	148,705
Materials and Supplies	50,633	50,633	-	50,633
Prepayments	6,711	6,711	-	6,711
Net Working Capital	<u>\$ 206,049</u>	<u>\$ 206,049</u>	<u>-</u>	<u>\$ 206,049</u>
Deferred Taxes	(612,611)	(619,052)	(14,935)	(633,986) ⁽¹⁾
Total Electric Rate Base	<u>\$ 3,688,559</u>	<u>\$ 3,713,041</u>	<u>\$ 120,221</u>	<u>\$ 3,833,261</u>

GAS RATE BASE
(\$000)

	Balance at December 31, 2009*	Balance at February 28, 2010	Capital Infrastructure Per Stipulation February 28, 2010	Adjusted Balance at February 28, 2010
Plant In Service	\$ 4,703,729	\$ 4,722,211	\$ 93,559	\$ 4,815,770
Accumulated Depreciation Reserve	(1,936,887)	(1,949,016)	(661)	(1,949,677)
Customer Advances	(4,499)	(4,499)	-	(4,499)
Net Plant	<u>\$ 2,762,343</u>	<u>\$ 2,768,696</u>	<u>\$ 92,898</u>	<u>\$ 2,861,594</u>
Working Capital:				
Cash (Lead/Lag)	\$ 117,231	\$ 117,231	\$ -	\$ 117,231
Materials and Supplies	12,078	12,078	-	12,078
Prepayments	4,049	4,049	-	4,049
Net Working Capital	<u>\$ 133,358</u>	<u>\$ 133,358</u>	<u>\$ -</u>	<u>\$ 133,358</u>
Deferred Taxes	(578,565)	(584,839)	(17,688)	(602,527) ⁽¹⁾
Total Gas Rate Base	<u>\$ 2,317,137</u>	<u>\$ 2,317,215</u>	<u>\$ 75,211</u>	<u>\$ 2,392,426</u>

* 3 Months Actual - 9 Months Estimated

(1) The Deferred Taxes for the Capital Stimulus Investment have been modified from the Stipulation to account for the federal bonus depreciation.

**EXHIBIT P-7
SCHEDULE MGK-6**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

WEIGHTED AVERAGE COST OF CAPITAL
(\$ MILLIONS)

	<u>Amount</u>	<u>Percent</u>	<u>Embedded Cost</u>	<u>Weighted Cost</u>
Long-Term Debt	\$ 3,531	46.60%	6.21%	2.90%
Preferred Stock	80	1.05%	5.03%	0.05%
Customer Deposits	87	1.15%	2.34%	0.03%
Common Equity	<u>3,879</u>	<u>51.20%</u>	11.50%	<u>5.89%</u>
Total	<u>\$ 7,576</u>	100.00%		<u>8.86%</u>

**EXHIBIT P-7
SCHEDULE MGK-7**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**EMBEDDED COST OF LONG TERM DEBT AS OF MARCH 31, 2009
INCLUDING NET UNAMORTIZED PREMIUM - INCLUDING AMOUNT DUE WITHIN ONE YEAR**

		COST OF BOND YIELD BASIS	PRINCIPAL AMOUNT OUTSTANDING	PLUS NET UNAMORTIZED PREMIUM/ (DISCOUNT)	PLUS NET UNAMORTIZED SELLING EXPENSE	PLUS NET UNAMORTIZED PREMIUM/ (DISCOUNT) & SELLING EXPENSE	PRINCIPAL AMOUNT AND UNAMORTIZED PREMIUM/ (DISCOUNT) & SELLING EXPENSE-NET	WEIGHT IN % OF PRINCIPAL AMOUNT AND UNAMORTIZED PREMIUM/ (DISCOUNT) & SELLING EXPENSE-NET	COST IN PERCENT
<u>PSE&G LONG TERM DEBT</u>									
6.750%	SERIES VV DUE 1-1-16	7.354%	\$171,245,000.00	(\$898,265.56)	(\$11,340.00)	(\$909,605.56)	\$170,335,394.44	4.8558%	0.3571%
6.450%	PC SERIES T DUE 10-1-19	7.180%	4,600,000.00	(36,808.59)	(35,028.00)	(71,836.59)	4,528,163.41	0.1291%	0.0093%
9.250%	SERIES CC DUE 6-1-21	9.768%	134,380,000.00	(156,802.07)	(7,008.00)	(163,810.07)	134,216,189.93	3.8261%	0.3737%
5.200%	PC SERIES M DUE 3-1-25	5.736%	23,000,000.00	(188,799.72)	(168,462.00)	(357,261.72)	22,642,738.28	0.6455%	0.0370%
1.755%	PC SERIES Z (2003 B1) DUE 11-1-33	2.029%	50,000,000.00	-	(318,411.60)	(318,411.60)	49,681,588.40	1.4163%	0.0287%
1.480%	PC SERIES AA (2003 B2) DUE 11-1-33	1.745%	50,000,000.00	-	(318,411.60)	(318,411.60)	49,681,588.40	1.4163%	0.0247%
5.450%	PC SERIES O DUE 2-1-32	5.923%	50,000,000.00	(570,751.33)	(155,358.00)	(726,109.33)	49,273,890.67	1.4047%	0.0832%
6.400%	PC SERIES P DUE 5-1-32	6.945%	100,000,000.00	(1,081,115.83)	(473,670.00)	(1,554,785.83)	98,445,214.17	2.8064%	0.1949%
8.000%	SERIES DUE 6-1-37	8.395%	7,462,900.00	-	-	-	7,462,900.00	0.2127%	0.0179%
5.000%	SERIES DUE 7-1-37	5.248%	7,537,800.00	-	-	-	7,537,800.00	0.2149%	0.0113%
2.206%	FRN SERIES B DUE 3-12-10	4.893%	300,000,000.00	-	(509,131.90)	(509,131.90)	299,490,868.10	8.5376%	0.4177%
8.160%	SERIES DUE 5/26/09	8.814%	16,500,000.00	(548.49)	(85.00)	(633.47)	16,499,366.53	0.4703%	0.0415%
8.100%	SERIES DUE 5/26/09	8.752%	43,500,000.00	(1,445.71)	(224.00)	(1,669.77)	43,498,330.23	1.2400%	0.1085%
5.125%	SERIES DUE 9/01/12	5.906%	300,000,000.00	(399,750.00)	(711,610.47)	(1,111,360.47)	298,888,639.53	8.5204%	0.5032%
5.000%	SERIES DUE 1/01/13	5.716%	150,000,000.00	-	(381,157.76)	(381,157.76)	149,618,842.24	4.2652%	0.2438%
5.000%	SERIES DUE 8/15/14	5.770%	250,000,000.00	(532,675.00)	(914,714.13)	(1,447,389.13)	248,552,610.87	7.0855%	0.4088%
7.040%	SERIES DUE 11/06/20	7.622%	9,000,000.00	(33,990.60)	(39,198.00)	(73,188.54)	8,926,811.46	0.2545%	0.0194%
5.375%	SERIES DUE 9/1/13	6.113%	300,000,000.00	(140,747.99)	(860,988.62)	(1,001,736.59)	298,998,263.41	8.5236%	0.5211%
7.180%	SERIES DUE 8/01/23	7.776%	5,000,000.00	(17,908.10)	(34,400.00)	(52,308.13)	4,947,691.87	0.1410%	0.0110%
7.150%	SERIES DUE 8/30/23	7.744%	33,500,000.00	(120,168.52)	(230,652.00)	(350,820.59)	33,149,179.41	0.9450%	0.0732%
5.250%	SERIES DUE 7/1/35	5.659%	250,000,000.00	(689,062.50)	(1,877,531.10)	(2,566,593.60)	247,433,406.40	7.0536%	0.3992%
5.700%	SERIES DUE 12/1/36	6.140%	250,000,000.00	(979,096.63)	(2,008,995.69)	(2,988,092.32)	247,011,907.68	7.0416%	0.4323%
5.800%	SERIES DUE 5/1/37	6.225%	350,000,000.00	(639,665.76)	(2,788,286.79)	(3,427,952.59)	346,572,047.41	9.8797%	0.6150%
5.300%	SERIES DUE 5/1/18	6.034%	400,000,000.00	(289,540.64)	(2,488,240.19)	(2,777,780.83)	397,222,219.17	11.3236%	0.6833%
6.330%	SERIES DUE 11/1/2013	7.660%	275,000,000.00	(79,515.27)	(1,632,278.14)	(1,711,793.41)	273,288,206.59	7.7906%	0.5967%
	TOTAL PSE&G LONG TERM DEBT		\$ 3,530,725,700.00	\$ (6,856,658.31)	\$ (15,965,182.99)	\$ (22,821,841.40)	\$ 3,507,903,858.60	100.000%	6.2126%

**EXHIBIT P-7
SCHEDULE MGK-8**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**ANNUAL COST OF PREFERRED STOCK CAPITAL INCLUDING EXPENSES OF ISSUANCE
AS OF MARCH 31, 2009**

<u>SERIES</u>	<u>DATE OF ISSUE</u>	<u>ORIG. ISSUE NUMBER OF SHARES</u>	<u>ORIG. ISSUE PAR VALUE OUTSTANDING</u>	<u>PREMIUM/ (DISCOUNT)</u>	<u>EXPENSES</u>	<u>ORIG. ISSUE PROCEEDS TO THE COMPANY</u>	<u>ORIG. ISSUE PERCENT OF PAR VALUE</u>	<u>ORIG. ISSUE COST TO COMPANY</u>	<u>CURRENT PAR VALUE OUTSTANDING</u>	<u>WEIGHT IN % OF CURRENT PAR VALUE OUTSTANDING</u>	<u>PRE-TAX COST IN PERCENT</u>	<u>AFTER-TAX COST IN PERCENT</u>
4.08%	10-25-49	250,000	\$ 25,000,000.00	\$ 37,500.00	\$ 115,835.55	\$ 24,921,664.45	99.6867%	4.0928%	\$ 14,622,100.00	18.387167%	0.752554%	0.752554%
4.18%	5-27-54	249,942	24,994,200.00	31,691.30	49,054.24	24,976,837.06	99.9305%	4.1829%	11,695,800.00	14.707369%	0.615195%	0.615195%
4.30%	10-03-55	250,000	25,000,000.00	-	67,061.93	24,932,938.07	99.7318%	4.3116%	14,947,800.00	18.796732%	0.810433%	0.810433%
5.05%	3-12-58	250,000	25,000,000.00	25,000.00	64,244.33	24,960,755.67	99.8430%	5.0579%	10,400,200.00	13.078163%	0.661486%	0.661486%
5.28%	12-21-60	250,000	25,000,000.00	37,500.00	63,235.67	24,974,264.33	99.8971%	5.2854%	11,786,400.00	14.821298%	0.783371%	0.783371%
6.92%	2-03-94	600,000	60,000,000.00	(288,000.00)	55,000.00	59,657,000.00	99.4283%	6.9598%	16,071,100.00	20.209272%	1.406522%	1.406522%
		1,849,942	\$ 184,994,200.00	\$ (156,308.70)	\$ 414,431.72	\$ 184,423,459.58			\$ 79,523,400.00	100.000000%	5.029562%	5.029562%

EXHIBIT P-7
SCHEDULE MGK-9

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

REVENUE FACTOR

	<u>ELECTRIC</u>	<u>GAS</u>
Revenue Increase	100.0000	100.0000
Uncollectible Rate		1.1300
BPU Assessment Rate	0.1853	0.1853
Rate Counsel Assessment Rate	0.0359	0.0359
Income before State of NJ Bus. Tax	99.7788	98.6488
State of NJ Bus. Income Tax @ 9.00%	8.9801	8.8784
Income Before Federal Income Taxes	90.7987	89.7704
Federal Income Taxes @ 35%	31.7796	31.4196
Return	59.0192	58.3508
Revenue Factor	<u>1.6944</u>	<u>1.7138</u>

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ELECTRIC UTILITY PLANT IN-SERVICE

(\$000)

	<u>Test Year 2009*</u>	<u>Period Ending February 28, 2010</u>
Beginning Balance	\$ 5,713,113	\$ 6,004,951
Total Direct Additions	331,204	54,435
Total Transfers to Plant In-Service	940	0
Retirements:		
Distribution	(11,590)	(2,167)
General	(26,145)	(3,084)
Intangible	(1,129)	0
Customer Operations	(1,442)	(264)
Total Retirements	(40,307)	(5,515)
Total Electric Utility Plant In-Service	\$ 6,004,951	\$ 6,053,872

GAS UTILITY PLANT IN-SERVICE

(\$000)

	<u>Test Year 2009*</u>	<u>Period Ending February 28, 2010</u>
Beginning Balance	\$ 4,498,567	\$ 4,703,729
Total Direct Additions	224,291	22,316
Total Transfers to Plant In-Service	(308)	0
Retirements:		
Production - Gas	0	0
Storage	0	0
Transmission	(863)	(192)
Distribution	(4,944)	(1,000)
General	(10,057)	(2,434)
Intangible	0	0
Customer Operations	(2,958)	(209)
Total Retirements	(18,821)	(3,835)
Total Gas Utility Plant In-Service	\$ 4,703,729	\$ 4,722,211

* 3 Months Actual - 9 Months Estimated

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ADDITIONS TO ELECTRIC PLANT IN-SERVICE
(\$000)

	<u>Test Year 2009*</u>	<u>Two-Months Ending February 28, 2010</u>
Distribution	\$ 257,364	\$ 49,198
General	8,882	3,648
Intangible	58,669	(0)
Customer Operations	6,290	1,589
Total Direct Additions	<u>\$ 331,204</u>	<u>\$ 54,435</u>

ADDITIONS TO GAS PLANT IN-SERVICE
(\$000)

	<u>Test Year 2009*</u>	<u>Two-Months Ending February 28, 2010</u>
Production - Gas	\$ 321	\$ 69
Storage	13	0
Transmission	6,445	63
Distribution	159,209	18,361
General	5,469	2,522
Intangibles	47,693	0
Customer Operations	5,141	1,300
Total Direct Additions	<u>\$ 224,291</u>	<u>\$ 22,316</u>

* 3 Months Actual - 9 Months Estimated

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ACCUMULATED DEPRECIATION OF ELECTRIC UTILITY PLANT
(\$000)

	<u>Test Year 2009*</u>	<u>Two-Months Ending February 28, 2010</u>
Beginning Balance	\$ (1,812,921)	\$ (1,907,960)
Distribution	(140,055)	(23,700)
General	(18,526)	(2,845)
Customer Operations	(3,365)	(597)
Total Charge to Depreciation Expense	<u>(161,945)</u>	<u>(27,142)</u>
Amortization of Intangibles	<u>(3,154)</u>	<u>(657)</u>
Total Depreciation Expense	(165,099)	(27,800)
Retirements	40,307	5,515
Cost of Removal (Net)	30,349	4,445
Other	<u>(595)</u>	<u>(158)</u>
Net Increase	<u>(95,039)</u>	<u>(17,998)</u>
Balance - Accumulated Depreciation	<u>\$ (1,907,960)</u>	<u>\$ (1,925,958)</u> ⁽¹⁾

ACCUMULATED DEPRECIATION OF GAS UTILITY PLANT
(\$000)

	<u>Test Year 2009*</u>	<u>Two-Months Ending February 28, 2010</u>
Beginning Balance	\$ (1,866,004)	\$ (1,936,887)
Production - Gas	(1,363)	(228)
Storage	(289)	(48)
Transmission	(2,047)	(339)
Distribution	(68,497)	(11,650)
General	(15,325)	(2,491)
Customer Operations	<u>(2,566)</u>	<u>(433)</u>
Total Charge to Depreciation Expense	<u>(90,088)</u>	<u>(15,190)</u>
Amortization of Intangibles	<u>(2,443)</u>	<u>(536)</u>
Total Depreciation Expense	(92,530)	(15,727)
Retirements	18,821	3,835
Cost of Removal (Net)	2,920	(236)
Other	<u>(94)</u>	<u>-</u>
Net Increase	<u>(70,884)</u>	<u>(12,128)</u>
Balance - Accumulated Depreciation	<u>\$ (1,936,887)</u>	<u>\$ (1,949,016)</u> ⁽¹⁾

* 3 Months Actual - 9 Months Estimated

(1) The Accumulated Depreciation Balances are exclusive of the Capital Infrastructure Program

EXHIBIT P-7
SCHEDULE MGK-13

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

CUSTOMER ADVANCES FOR CONSTRUCTION - ELECTRIC DISTRIBUTION (a)
(\$000)

Extension of Electric Lines	\$ (5,449)
Total Electric Customer Advances for Construction	<u><u>\$ (5,449)</u></u>

CUSTOMER ADVANCES FOR CONSTRUCTION - GAS DISTRIBUTION (a)
(\$000)

Extension of Gas Mains	\$ (4,014)
Deposits for Facilities	<u>(485)</u>
Total Gas Customer Advances for Construction	<u><u>\$ (4,499)</u></u>

(a) 13-month Actual Average Balance (March 08 - March 09)

**EXHIBIT P-7
SCHEDULE MGK-14**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY
WORKING CAPITAL - MATERIALS AND SUPPLIES
(\$000)

	<u>Electric</u>	<u>Gas</u>
Materials and Supplies (a)	\$ 50,633	\$ 12,078
Total Materials and Supplies	<u>\$ 50,633</u>	<u>\$ 12,078</u>

(a) 13-month Actual Average Balance (March 08 - March 09)

EXHIBIT P-7
SCHEDULE MGK-15

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

WORKING CAPITAL - PREPAYMENTS
(\$000)

	<u>Electric</u>	<u>Gas</u>
Insurance (a)	\$ 1,450	\$ 861
BPU & Rate Counsel Assessment	5,261	3,188
Total Prepayments	<u><u>\$ 6,711</u></u>	<u><u>\$ 4,049</u></u>

(a) 13-month Actual Average Balance (March 08 - March 09)

**EXHIBIT P-7
SCHEDULE MGK-16**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ACCUMULATED DEFERRED TAXES - ELECTRIC
(\$000)

	Test Year 2009*	January - February Activity	Balance Ending February 28, 2010
Liberalized Depreciation	\$ (539,480)	\$ (5,145)	\$ (544,625)
Cost of Removal	(17,324)	(861)	(18,185)
Computer Software	(3,598)	(4)	(3,602)
Capitalized Interest	505	(74)	430
NJ Corporate Business Tax	(52,714)	(356)	(53,070)
Total Electric Accumulated Deferred Taxes	\$ (612,611)	\$ (6,441)	\$ (619,052)

ACCUMULATED DEFERRED TAXES - GAS
(\$000)

	Test Year 2009*	January - February Activity	Balance Ending February 28, 2010
Liberalized Depreciation	\$ (533,566)	\$ (6,514)	\$ (540,080)
Cost of Removal	(20,684)	130	(20,554)
Computer Software	(1,050)	(4)	(1,054)
Capitalized Interest	498	(6)	492
NJ Corporate Business Tax	(23,763)	119	(23,644)
Total Gas Accumulated Deferred Taxes	\$ (578,565)	\$ (6,275)	\$ (584,839)

* 3 Months Actual - 9 Months Estimated

**EXHIBIT P-7
SCHEDULE MGK-17**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

INCOME STATEMENT

(\$000)

ELECTRIC (1)	2008	2009*
Electric Operating Revenues	<u>\$5,446,903</u>	<u>\$5,633,761</u>
<u>Electric Operating Expenses:</u>		
Operation Expense	\$4,532,567	\$4,728,309
Maintenance Expense	99,518	98,570
Depreciation Expense	148,546	154,574
Amortization of Limited Term Plant	1,279	2,644
Amortization of Property Losses	144,223	148,806
Taxes Other Than Income Taxes	114,760	115,511
Income Taxes - Federal	117,274	107,001
Accretion Expense-Electric	2	4
Investment Tax Credit Adjustments (Net)	<u>(954)</u>	<u>(889)</u>
Total Electric Utility Operating Expenses	<u>\$5,157,214</u>	<u>\$5,354,530</u>
Electric Utility Operating Income	<u>\$289,689</u>	<u>\$279,232</u>

(1) Electric Distribution only

GAS	2008	2009*
Gas Operating Revenues	<u>\$3,144,537</u>	<u>\$2,863,918</u>
<u>Gas Operating Expenses:</u>		
Operation Expense	\$2,699,272	\$2,426,767
Maintenance Expense	27,094	29,016
Depreciation Expense	89,313	90,813
Amortization of Limited Term Plant	399	2,027
Amortization of Property Losses	11,682	15,460
Amortization of Excess cost of removal	(13,200)	(13,200)
Taxes Other Than Income Taxes	58,715	61,059
Income Taxes - Federal	83,478	77,513
Investment Tax Credit Adjustments (Net)	<u>(911)</u>	<u>(1,311)</u>
Total Gas Utility Operating Expenses	<u>\$2,955,842</u>	<u>\$2,688,145</u>
Gas Utility Operating Income	<u>\$188,695</u>	<u>\$175,774</u>
Net Utility Operating Income	<u><u>\$478,384</u></u>	<u><u>\$455,005</u></u>

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-18

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ELECTRIC DISTRIBUTION SALES BY CLASS OF BUSINESS
(KWh/Therms - 000)

<u>Line</u>	Year Ended December 31, 2009*	
	Electric	Gas
1 Residential	13,774,892	1,432,294
2 Commercial	24,192,267	849,304
3 Industrial	4,612,665	85,607
4 Firm Transportation Service		41,777
5 Non-Firm Transportation Service		570,112
6 Cogeneration Interruptible		52,525
7 Cogeneration Contracts		419,337
8 Street Lighting	552,577	674
9 Total Sales to Customers	43,132,402	3,451,630
10 Interdepartmental	12,691	792
11 Total Sales	43,145,093	3,452,422

* 3 Months Actual - 9 Months Estimated

**EXHIBIT P-7
SCHEDULE MGK-19**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**REVENUE BY CLASS OF BUSINESS
(\$000)**

	Year Ended December 31, 2009*		
<u>Line</u>	<u>Electric</u>	<u>Gas</u>	<u>Total</u>
1 Residential	\$ 2,352,200	\$ 1,953,362	\$ 4,305,563
2 Commercial	2,766,230	606,276	3,372,506
3 Industrial	322,292	48,740	371,032
4 Firm Transportation Service		6,416	6,416
5 Non-Firm Transportation Service		82,136	82,136
6 Cogeneration Interruptible		35,295	35,295
7 Cogeneration Contracts		89,779	89,779
8 Street Lighting	130,210	795	131,005
9 Total Revenue from Sales to Customers	<u>\$ 5,570,932</u>	<u>\$ 2,822,799</u>	<u>\$ 8,393,732</u>
10 Interdepartmental	1,479	595	2,074
11 Total Revenue from Sales	<u><u>\$ 5,572,412</u></u>	<u><u>\$ 2,823,394</u></u>	<u><u>\$ 8,395,806</u></u>

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-20

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

AVERAGE CUSTOMERS BILLED BY CLASS OF BUSINESS

<u>Line</u>	Year Ended December 31, 2009*	
	<u>Electric</u>	<u>Gas</u>
1 Residential	1,843,684	1,590,248
2 Commercial	263,564	150,677
3 Industrial	9,382	6,962
4 Firm Transportation Service		63
5 Non-Firm Transportation Service		257
6 Cogeneration Interruptible		26
7 Cogeneration Contracts		8
8 Street Lighting	22,419	15
9 Total Customers	<u>2,139,049</u>	<u>1,748,256</u>
10 Interdepartmental	1	1
11 Total Customers	<u><u>2,139,050</u></u>	<u><u>1,748,257</u></u>

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-21

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

EXPENSES
(\$000)

Electric	Year Ended December 31 2009*
<u>Production Expenses</u>	
Other Power Supply Expenses:	
Purchased Power	\$ 4,054,041
System Control/Load Dispatch	(461)
Total Other Power Supply Expenses	\$ 4,053,580
 <u>Distribution</u>	
Operation	\$ 53,121
Maintenance	98,570
Total Distribution	\$ 151,690
 Gas	
<u>Production Expenses</u>	
Gas Supply	
Natural Gas City Gate Purchases	\$ 1,899,306
Fuel Gas - Raw Materials	47,222
Other Gas Purchases	(19)
Other Gas Supply Expenses	3,271
Total Gas Supply	\$ 1,949,780
 Gas Production	
Operation	\$ 254
Maintenance	772
Total Gas Production	\$ 1,026
 Other Storage	
Operation	\$ 47
Maintenance	329
Total Other Storage	\$ 376
Total Production Expenses	\$ 1,951,183
 Transmission	
Operation	\$ 11
Maintenance	337
Total Transmission	\$ 348
 Distribution	
Operation	\$ 48,275
Maintenance	27,579
Total Distribution	\$ 75,854

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-22

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

CUSTOMER ACCOUNTS AND INFORMATION

(\$000)

	Year Ended December 31, 2009*		
	Electric	Gas	Total
Customer Accounts Expenses			
Operation:			
Meter Reading Expenses	\$ 17,421	\$ 13,174	\$ 30,595
Customer Records and Collection Expenses	58,834	51,144	109,978
Uncollectible Accounts	56,046	33,132	89,177
Misc. Customer Accounts Expenses	114,211	15,535	129,746
Total Customer Accounts Expenses	\$ 246,511	\$ 112,986	\$ 359,497
 Cust. Service and Informational Expenses			
Operation:			
Supervision	\$ -	\$ -	\$ -
Customer Assistance Expenses	135,331	152,030	287,360
Misc. Cust. Service and Info. Expenses	698	245	943
Total Cust. Service and Info. Expenses	\$ 136,028	\$ 152,275	\$ 288,303
 Sales Expenses			
Operation:			
Demonstration and Selling Expenses	\$ 2,330	\$ 473	\$ 2,803
Misc. Sales Expenses	0	396	396
Total Sales Expenses	\$ 2,330	\$ 869	\$ 3,199
Total Customer Accounts and Information	\$ 384,869	\$ 266,130	\$ 650,999

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-23

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

ADMINISTRATIVE AND GENERAL SALARIES AND EXPENSES
(\$000)

	Year Ended December 31, 2009*		
	<u>Electric</u>	<u>Gas</u>	<u>Total</u>
Salaries & Wages	\$ 8,087	\$ 4,973	\$ 13,060
Supplies & Expenses	4,065	3,292	7,356
Outside Services	53,034	39,478	92,511
Property Insurance	661	150	811
Injuries and Damages	13,058	9,515	22,573
Death Benefit	(229)	(261)	(490)
Group Life	365	413	778
OPEB	72,968	26,039	99,007
Medical Insurance	12,886	14,570	27,455
Dental & Vision Plan	1,206	1,375	2,581
Pensions	28,684	32,325	61,009
PSE&G Thrift/Savings Plan	4,117	4,648	8,766
Benefits Other	11,729	6,024	17,753
Regulatory Expenses	11,685	8,049	19,734
Duplicate Charge	(3,069)	(1,181)	(4,251)
General Advertising	3,528	2,830	6,358
Other Miscellaneous General	3,247	1,990	5,237
Rents	10,724	8,044	18,768
Maintenance	-	(1)	(1)
Total Administrative and General Salaries & Expenses	<u>\$ 236,744</u>	<u>\$ 162,269</u>	<u>\$ 399,013</u>

* 3 Months Actual - 9 Months Estimated

**EXHIBIT P-7
SCHEDULE MGK-24**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**DEPRECIATION AND AMORTIZATION
(\$000)**

ELECTRIC

<u>Line</u>	<u>Depreciation</u>	Year Ended December 31 <u>2009*</u>
1	Electric	<u>\$154,574</u>
	<u>Amortization</u>	
2	High Volume Call Answering (HVCA) System Replacement	\$59
3	Basic Generation Service CIS & ADC System Upgrade-Year 3	157
4	Security Doors - General Office	36
5	Improvements to Customer Service Center Leased Locations	421
6	Customer Information System	1,939
7	Replace Field Collection Handheld System Hardware & Software	32
8	Amort of Property Losses, Unrecov. Plt & Reg Study Costs	6,147
9	Amortization of Securitization-Regulatory Asset	127,608
10	Electric-Amortization of Restructuring Asset	4,941
11	Electric-Amortization-Repair Allowance	10,110
12	Total Electric Amortization	<u>\$151,450</u>
13	Total Electric Depreciation and Amortization	<u><u>\$306,024</u></u>

GAS

<u>Line</u>	<u>Depreciation</u>	Year Ended December 31 <u>2009*</u>
1	Gas	<u>\$90,813</u>
	<u>Amortization</u>	
2	High Volume Call Answering (HVCA) System Replacement	\$48
3	Improvements to Customer Service Center Leased Locations	344
4	Customer Information System	1,609
5	Replace Field Collection Handheld System Hardware & Software	27
6	Amort of Prop Loss, etc.	15,460
7	Amortization of Excess Cost of Removal	(13,200)
8	Total Gas Amortization	<u>\$4,287</u>
9	Total Gas Depreciation and Amortization	<u><u>\$95,100</u></u>

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-25

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

TAXES OTHER THAN INCOME TAXES
(\$000)

Line	Year Ended December 31, 2009*		
	Electric	Gas	Total
1 Real Estate	\$ 10,736	\$ 4,440	\$ 15,176
2 FICA	7,917	11,091	19,008
3 TEFA	96,180	44,607	140,787
4 State Unemployment	332	451	783
5 Federal Unemployment	143	194	337
6 Miscellaneous Municipal and State Taxes	203	275	478
7 Total	\$ 115,511	\$ 61,059	\$ 176,569

* 3 Months Actual - 9 Months Estimated

EXHIBIT P-7
SCHEDULE MGK-26

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

CURRENT AND DEFERRED INCOME TAXES

(\$000)

Year Ended December 31, 2009*

<u>Line</u>	<u>Electric</u>	<u>Gas</u>	<u>Total</u>
1 Current			
2 Federal	\$ 134,309	\$ 5,513	\$ 139,822
3 State	35,244	\$ 10,850	\$ 46,094
4 Total Current	<u>\$ 169,553</u>	<u>\$ 16,363</u>	<u>\$ 185,916</u>
5 Deferred			0
6 Liberalized Depreciation (CLS)	\$ 63,677	\$ 57,931	\$ 121,608
7 Cost of Removal	2,427	4,821	7,248
8 Deferred iPower Costs	1,186	970	2,156
9 Deferred Societal Benefits Clauses	(5,275)	(5,277)	(10,552)
10 Pension Accrual Adjustment	5,155	(2,240)	2,914
11 Contribution in Aid of Construction	(4,322)	2,444	(1,878)
12 Deferred NJ Corp Business Tax (Net of FIT)	8,934	(1,043)	7,892
13 Interest Capitalized (Net)	441	5,582	6,022
14 Environmental Clean-Up Costs (RAC)	2,731	(456)	2,275
15 Unallowable OPEB Amortization	(9,149)	(553)	(9,703)
16 Other	<u>(128,357)</u>	<u>(1,029)</u>	<u>(129,385)</u>
17 Total Deferred	\$ (62,552)	\$ 61,150	\$ (1,402)
18 Investment Tax Credit Amortized	(889)	(1,311)	(2,200)
19 Net Income Taxes	<u>\$ 106,112</u>	<u>\$ 76,202</u>	<u>\$ 182,314</u>

* 3 Months Actual - 9 Months Estimated

**EXHIBIT P-7
SCHEDULE MGK-27**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY
PRO-FORMA DISTRIBUTION OPERATING INCOME
(\$000)

			<u>Electric</u>	<u>Gas</u>	<u>Total</u>
Test Year Distribution Operating Income			\$ 279,232	\$ 175,774	\$ 455,006
Adjustment #	Pro-Forma Adjustments:	Schedule #			
1	Wages	MGK - 28	\$ (3,302)	\$ (3,714)	\$ (7,015)
2	Payroll Taxes	MGK - 29	(247)	(278)	(525)
3	Interest Synchronization (Tax Savings)	MGK - 30	122	3,049	3,171
4	Pension & Fringe Benefits	MGK - 31	(357)	(4,767)	(5,123)
5	COLI Interest Expense	MGK - 32	(8,780)	(2,772)	(11,552)
6	Postage	MGK - 33	(369)	(302)	(670)
7	BPU/RPA Assessments	MGK - 34	(1,468)	(579)	(2,047)
8	Weather Normalization	MGK - 35	(648)	(6,562)	(7,210)
9	Gains/Losses on Sales of Property	MGK - 36	88	27	114
10	Management/Affiliated Standards Audit	MGK - 37	428	350	778
11	Customer Information System Amortization	MGK - 38	(1,412)	(1,155)	(2,567)
12	Real Estate Taxes	MGK - 39	(70)	(29)	(99)
13	Capital Stimulus	MGK - 40	(1,495)	(879)	(2,374)
14	Insurance	MGK - 41	(347)	(227)	(574)
15	EMP Clauses	MGK - 42	(560)	(83)	(644)
16	Cost of Removal	MGK - 43		(2,364)	(2,364)
17	TSGNF Margin Sharing	MGK - 44		(6)	(6)
Total Pro-Forma Adjustments			\$ (18,416)	\$ (20,291)	\$ (38,707)
Total Pro-Forma Distribution Operating Income			\$ 260,816	\$ 155,483	\$ 416,299

**EXHIBIT P-7
SCHEDULE MGK-28**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 1

**Wages
(\$000)**

	ELECTRIC	GAS	TOTAL
Bargaining Unit Employees	\$ 3,950	\$ 4,701	\$ 8,652
MAST Employees	808	962	1,770
Service Company Employees Charged to PSE&G	823	615	1,438
Operating Expense Increase before Taxes	\$ 5,582	\$ 6,278	\$ 11,860
Income Taxes @ 40.85%	2,280	2,565	4,845
Operating Income Increase (Decrease) After Taxes	\$ (3,302)	\$ (3,714)	\$ (7,015)

EXHIBIT P-7
SCHEDULE MGK-29

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 2
Payroll Taxes
(\$000)

	ELECTRIC	GAS	TOTAL
Bargaining Unit Employees	\$ 296	\$ 352	\$ 648
MAST Employees	61	72	133
Service Company Employees Charged to PSE&G	62	46	108
Operating Expense Increase before Taxes	\$ 418	\$ 470	\$ 888
Income Taxes @ 40.85%	171	192	363
Operating Income Increase (Decrease) After Taxes	\$ (247)	\$ (278)	\$ (525)

**EXHIBIT P-7
SCHEDULE MGK-30**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 3
Interest Synchronization (Tax Savings)
(\$000)**

Electric Rate Base			\$ 3,833,261
	Percent	Embedded Cost	Weighted Cost
Debt Components:			
Long Term Debt	46.60%	6.21%	2.90%
Customer Deposits	1.15%	2.34%	0.03%
Total Weighted Cost of Debt			2.92%
Annualized Interest Expense			\$ 112,011
Less: Test Period Interest Expense			111,712
Net Interest Expense Increase/Decrease			\$ 299
Income Tax Rate			40.85%
Operating Income Increase (Decrease) After Taxes			\$ 122
Gas Rate Base			\$ 2,392,426
	Percent	Embedded Cost	Weighted Cost
Debt Components:			
Long Term Debt	46.60%	6.21%	2.90%
Customer Deposits	1.15%	2.34%	0.03%
Total Weighted Cost of Debt			2.92%
Annualized Interest Expense			\$ 69,909
Less: Test Period Interest Expense			62,445
Net Interest Expense Increase/Decrease			\$ 7,464
Income Tax Rate			40.85%
Operating Income Increase (Decrease) After Taxes			\$ 3,049

EXHIBIT P-7
SCHEDULE MGK-31

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 4
Pension and Fringe Benefits
(\$000)

		<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Rate Year	Pension	\$ 39,061	\$ 42,498	\$ 81,559
	OPEB	75,663	28,350	104,013
	Medical	17,923	18,976	36,899
	Dental	1,488	1,582	3,070
	Thrift	5,899	6,052	11,951
	Long Term Disability	222	221	444
	Group Life Insurance/Death Benefit	243	226	468
	Workers Compensation	2,243	2,472	4,714
	Other	1,641	1,817	3,458
		<u>\$ 144,382</u>	<u>\$ 102,194</u>	<u>\$ 246,576</u>
Less:				
December 31, 2009	Pension	\$ 35,952	\$ 37,748	\$ 73,700
	OPEB	73,849	26,699	100,548
	Medical	15,137	15,954	31,091
	Dental	1,379	1,505	2,884
	Thrift	5,416	5,623	11,039
	Long Term Disability	199	199	398
	Group Life Insurance/Death Benefit	233	225	458
	Workers Compensation	1,559	1,634	3,194
	Other	10,055	4,548	14,604
		<u>\$ 143,779</u>	<u>\$ 94,136</u>	<u>\$ 237,915</u>
Increase in Test Year Operating Expenses		603	8,059	8,662
Income Taxes @ 40.85%		<u>\$ 246</u>	<u>\$ 3,292</u>	<u>\$ 3,538</u>
Operating Income Increase (Decrease) After Taxes		<u><u>\$ (357)</u></u>	<u><u>\$ (4,767)</u></u>	<u><u>\$ (5,123)</u></u>

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 5
COLI Interest Expense
(\$000)

	<u>Electric</u>	<u>Gas</u>	<u>TOTAL</u>
Net Credit in Test Year			
Administrative & General Expenses	\$ (11,615)	\$ (3,071)	\$ (14,686)
Tax Savings on COLI	(330)	(213)	(543)
Interest Charges	<u>8,780</u>	<u>2,772</u>	<u>11,552</u>
Net Benefit	\$ (3,165)	\$ (512)	\$ (3,677)
Reclassification of Test-Year COLI Interest	<u><u>\$ (8,780)</u></u>	<u><u>\$ (2,772)</u></u>	<u><u>\$ (11,552)</u></u>

EXHIBIT P-7
SCHEDULE MGK-33

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 6

Postage
(\$000)

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Postage Expense	\$ 5,903	\$ 4,830	\$ 10,733
Test Year Postage Expense	<u>5,280</u>	<u>4,320</u>	<u>9,600</u>
Operating Expense Increase Before Taxes	\$ 623	\$ 510	\$ 1,133
Income Taxes @ 40.85%	255	208	463
Operating Income Increase (Decrease) After Taxes	<u>\$ (369)</u>	<u>\$ (302)</u>	<u>\$ (670)</u>

**EXHIBIT P-7
SCHEDULE MGK-34**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 7
BPU/Rate Counsel Assessment
(\$000)**

Electric

	BPU	Rate Counsel	Total
Year 2009 Revenues	\$ 5,760,340	\$ 5,760,340	
Estimated Assessment Rate	0.1853%	0.0359%	
Estimated Assessment	\$ 10,675	\$ 2,066	\$ 12,741
Less: Assessment Included in Test Year Operating Expenses	8,669	1,590	10,259
Operating Expense Increase Before Taxes	\$ 2,006	\$ 476	\$ 2,482
Income Taxes @ 40.85%	819	195	1,014
Operating Income Increase (Decrease) After Taxes	\$ (1,186)	\$ (282)	\$ (1,468)

Gas

	BPU	Rate Counsel	Total
Year 2009 Revenues	\$ 3,211,620	\$ 3,211,620	
Estimated Assessment Rate	0.1853%	0.0359%	
Estimated Assessment	\$ 5,952	\$ 1,152	\$ 7,104
Less: Assessment Included in Test Year Operating Expenses	5,175	949	6,124
Operating Expense Increase Before Taxes	\$ 777	\$ 203	\$ 980
Income Taxes @ 40.85%	317	83	400
Operating Income Increase (Decrease) After Taxes	\$ (459)	\$ (120)	\$ (579)

**EXHIBIT P-7
SCHEDULE MGK-35**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 8
Weather Normalization
(\$000)**

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Actual Distribution Margin Revenues (1st Quarter)	\$ 204,380	\$ 289,241	\$ 493,621
Weather Normalized Margin Revenues (1st Quarter)	<u>203,285</u>	<u>278,147</u>	<u>481,432</u>
Decrease in Test Year Margin Revenue	\$ 1,095	\$ 11,094	\$ 12,189
Income Taxes @ 40.85%	<u>447</u>	<u>4,532</u>	<u>4,979</u>
Operating Income Increase (Decrease) After Taxes	<u><u>\$ (648)</u></u>	<u><u>\$ (6,562)</u></u>	<u><u>\$ (7,210)</u></u>

**EXHIBIT P-7
SCHEDULE MGK-36**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 9
Gains/Losses on Sales of Property
(\$000)**

		<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
2005	Book Gain/(Loss)	\$ 22	\$ -	\$ 22
2006	Book Gain/(Loss)	573	34	607
2007	Book Gain/(Loss)	-	184	184
2008	Book Gain/(Loss)	504	230	734
2009	Book Gain/(Loss)	-	-	-
		<hr/>	<hr/>	<hr/>
Five-Year Average - Book Gain/(Loss)		\$ 220	\$ 89	\$ 309
Income Taxes		44	36	80
		<hr/>	<hr/>	<hr/>
	Net Income/(Loss)	<u>\$ 176</u>	<u>\$ 53</u>	<u>\$ 229</u>
	Operating Income Increase (Decrease) After Taxes	<u>\$ 88</u>	<u>\$ 27</u>	<u>\$ 114</u>

**EXHIBIT P-7
SCHEDULE MGK-37**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 10
Management/Affiliated Standards Audit
(\$000)**

	ELECTRIC	GAS	TOTAL
Management/Affiliated Standards Audit Expense	\$ 1,725	\$ 1,411	\$ 3,137
Amortization Period	4	4	4
Normalized Test Period Management/Affiliated Standards Audit Expense	\$ 431	\$ 353	\$ 784
Management/Affiliated Standards Audit Expense Included in Test Period	(1,155)	(945)	(2,100)
Test Period Normalization	\$ (724)	\$ (592)	\$ (1,316)
Income Taxes @ 40.85%	(296)	(242)	(538)
Operating Income Increase (Decrease) After Taxes	\$ 428	\$ 350	\$ 778

EXHIBIT P-7
SCHEDULE MGK-38

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 11
Customer Information System Amortization
(\$000)

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Annual Amortization (E - \$23.87 million - 10 years; G -\$19.53 million - 10 years)	\$ 2,387	\$ 1,953	\$ 4,339
Income Taxes @ 40.85%	<u>975</u>	<u>798</u>	<u>1,773</u>
Operating Income Increase (Decrease) After Taxes	<u>\$ (1,412)</u>	<u>\$ (1,155)</u>	<u>\$ (2,567)</u>

**EXHIBIT P-7
SCHEDULE MGK-39**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 12
Real Estate Taxes
(\$000)**

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Increase in Property Taxes	<u>\$ 118</u>	<u>\$ 49</u>	<u>\$ 167</u>
Operating Expense Increase Before Taxes	\$ 118	\$ 49	\$ 167
Income Taxes @ 40.85%	48	20	68
Operating Income Increase (Decrease) After Taxes	<u><u>\$ (70)</u></u>	<u><u>\$ (29)</u></u>	<u><u>\$ (99)</u></u>

EXHIBIT P-7
SCHEDULE MGK-40

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 13
Capital Stimulus
(\$000)**

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Annualized Depreciation Expense	\$ 2,527	\$ 1,486	\$ 4,014
Operating Expense Increase Before Taxes	\$ 2,527	\$ 1,486	\$ 4,014
Income Taxes @ 40.85%	1,032	607	1,640
Operating Income Increase (Decrease) After Taxes	<u><u>\$ (1,495)</u></u>	<u><u>\$ (879)</u></u>	<u><u>\$ (2,374)</u></u>

EXHIBIT P-7
SCHEDULE MGK-41

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

Adjustment No. 14
Insurance
(\$000)

	<u>ELECTRIC</u>	<u>GAS</u>	<u>TOTAL</u>
Insurance Premium Expense	\$ 4,490	\$ 2,928	\$ 7,418
Test Year Insurance Premium Expense	<u>3,903</u>	<u>2,544</u>	<u>6,447</u>
Operating Expense Increase Before Taxes	\$ 587	\$ 384	\$ 971
Income Taxes @ 40.85%	240	157	397
Operating Income Increase (Decrease) After Taxes	<u>\$ (347)</u>	<u>\$ (227)</u>	<u>\$ (574)</u>

**EXHIBIT P-7
SCHEDULE MGK-42**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 15
EMP Clauses
(\$000)**

	ELECTRIC	GAS	TOTAL
Operating Revenues	\$ 3,346	\$ 1,295	\$ 4,641
Operating Expenses	2,399	1,154	3,553
Net Income (Expense)	\$ 948	\$ 141	\$ 1,088
Income Taxes @ 40.85%	387	57	444
Operating Income Increase (Decrease) After Taxes	\$ (560)	\$ (83)	\$ (644)

**EXHIBIT P-7
SCHEDULE MGK-43**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 16
Cost of Removal - Gas
(\$000)**

Operating Income Decrease Before Taxes (2004-2008)	\$ 3,997
Income Taxes @ 40.85%	<u>1,633</u>
Operating Income Increase (Decrease) After Taxes	<u><u>\$ (2,364)</u></u>

**EXHIBIT P-7
SCHEDULE MGK-44**

PUBLIC SERVICE ELECTRIC AND GAS COMPANY

**Adjustment No. 17
TSG-NF Margin - Gas
(\$000)**

Operating Income Decrease Before Taxes	\$ 10
Income Taxes @ 40.85%	<u>4</u>
Operating Income Increase (Decrease) After Taxes	<u><u>\$ (6)</u></u>