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July 26, 2004

Honorable Pat Miller, Chairman
c/o Sharla Dillon, Docket and Records Manager
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

Re: *Petition of Chattanooga Gas Company for Approval of Adjustment of its Rates and Charges and Revised Tariff*
Docket No. 04-00034

Dear Chairman Miller:

Enclosed please find the original and fourteen (14) copies of the Direct Testimony of Alan Chalfant, Earl Burton, Tim Spires, Ray Childers, and Dan Nuckolls filed on behalf of Chattanooga Manufacturer's Association

Very truly yours,

BOULT, CUMMINGS, CONNERS & BERRY, PLC

By: Henry Walker
Henry Walker KG

HW/krg

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7/26/2004

CERTIFICATE OF SERVICE

I hereby certify that I have on this 26th day of July, 2004, served the foregoing pleading either by fax, overnight delivery service or first class mail, postage prepaid, to all parties of record at their addresses shown below:

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Before the

Tennessee Regulatory Authority

Docket No. 04-00034

Chattanooga Gas Company

Direct Testimony and Exhibits of

Alan Chalfant

On Behalf of

Chattanooga Manufacturers Association

July 26, 2004

BRUBAKER & ASSOCIATES, INC.
ST LOUIS, MO 63141-2000

Chattanooga Gas Company

Before the

Tennessee Regulatory Authority

Docket No. 04-00034

Direct Testimony of Alan Chalfant

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Alan Chalfant, 1215 Fern Ridge Parkway, Suite 208, St. Louis, Missouri 63141-2000.

Q WHAT IS YOUR OCCUPATION?

A I am a consultant in the field of public utility regulation with Brubaker & Associates, Inc , energy, economic and regulatory consultants

Q PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A My qualifications are stated in Appendix A to this testimony

Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A I am appearing on behalf of the Chattanooga Manufacturers Association (CMA) Members of the CMA include customers of Chattanooga Gas Company (CGC or Company)

Q WHAT IS THE SUBJECT OF YOUR DIRECT TESTIMONY?

A I will address issues concerning the Company's proposed allocation of revenues to the classes including the allocation of the proposed Bare Steel and Cast Iron Pipeline Replacement Program (PRP) tracker and certain proposed tariff changes

REVENUE ALLOCATION

Q HOW HAS THE COMPANY PROPOSED TO SPREAD ITS REQUESTED REVENUE INCREASE AMONG THE VARIOUS CUSTOMER CLASSES?

A The Company has actually presented two proposals The first, reflected in its Exhibit SL-1 tariff proposal, I will refer to as its "basic proposal" The second, reflected in its Exhibit SL-2 tariff proposal, I will refer to as the Company's "preferred alternative proposal" Under its basic proposal, the Company increases the base margin revenue of all classes by approximately 15 3% Under its preferred alternative proposal, it would increase the base margin revenue responsibility of all classes by about 8 2% and recover the remainder through its PRP tracker and, in the case of stored gas inventory costs, as a gas cost

Q DO YOU AGREE WITH THE GENERAL CONCEPT OF INCREASING THE MARGIN REVENUES OF ALL CLASSES BY THE SAME PERCENTAGE?

A Not unless such an approach is justified on the basis of a cost of service study

Q HOW SHOULD THE INCREASE BE SPREAD?

A Any allowed increase should be spread so that the rates charged to each customer class reflect the actual cost of providing service as closely as practicable The movement to cost should only be constrained by gradualism Gradualism means that no class should receive an overly large increase or decrease in its rates relative to the overall average percentage change

Q WHY SHOULD THE RESULTS OF THE COST OF SERVICE STUDY BE THE PRIMARY FACTOR IN DETERMINING CLASS REVENUE REQUIREMENTS?

A Cost-based rates will send the proper price signals to customers Sending proper price signals is especially important in a competitive environment, where customers can choose their commodity supplier Cost-based rates are essential for the development of competitive retail markets because such rates eliminate cross-subsidies and provide unfettered access to competitive suppliers The other reasons for adhering to cost of service principles are *equity*, *engineering efficiency* (cost-minimization), *stability*, and *conservation*

Q WHY ARE COST-BASED RATES EQUITABLE?

A Rates which reflect primary cost of service considerations are *equitable* because each customer pays what it costs the utility to serve them, no more and no less If rates are not based on cost, then some customers must pay part of the cost of providing service to other customers, which is inequitable

Q HOW DO COST-BASED RATES PROMOTE ENGINEERING EFFICIENCY?

A With respect to *engineering efficiency*, when class revenues are established reflective of the demand and commodity cost components, customers are provided with the proper incentive to minimize their costs, which will, in turn, minimize the costs to the utility

Q **HOW CAN COST-BASED RATES PROVIDE STABILITY?**

A When rates are closely tied to cost, the utility's earnings are stabilized because changes in customer use patterns would result in parallel changes in revenues and expenses

Q **DO COST-BASED RATES ENCOURAGE CONSERVATION?**

A Yes By providing balanced price signals against which to make consumption decisions, cost-based rates encourage *conservation* (of both capacity and commodity), which is properly defined as the avoidance of wasteful or inefficient use (and not just less use) If rates are not based on costs, then the choices are distorted

Q **HOW CAN THE TENNESSEE REGULATORY AUTHORITY (TRA) DETERMINE WHETHER CHATTANOOGA'S RATES REFLECT COST OF SERVICE?**

A A properly designed and executed class cost of service study can reveal the extent that rates reflect costs for each of the various customer classes

Q **WHAT IS A CLASS COST OF SERVICE STUDY?**

A A class cost of service study is an analysis used to determine each class' responsibility for the costs incurred by the utility to provide service

Q **HAS THE COMPANY FILED A CLASS COST OF SERVICE STUDY IN THIS DOCKET?**

A No

Q **IS THE ALLOCATION OF PRESENT RATES BASED ON COST?**

A No It is my understanding that the allocation of present rates was established in Docket No 95-02116 as part of a settlement The method for determining class revenue requirements was to spread the increase so as to produce an equal percent increase in gross margin revenues for each class (See the Company's Response to CMA Discovery Request No 6, attached hereto as Exhibit ___(AC-1))

Q **WAS THAT A REASONABLE METHOD?**

A Assuming class revenues were reasonably aligned with cost prior to that increase it could preserve that relationship

Q **IS THAT THE SAME METHOD THAT THE COMPANY CLAIMS TO BE PROPOSING IN THIS CASE?**

A Yes The Company makes this claim in its Response to CMA Discovery Request No 6 (Exhibit ___(AC-1))

Q **DOES THAT METHOD CONTINUE TO BE REASONABLE?**

A Not necessarily It appears that it has been nearly 10 years or more since the revenue responsibility of the classes has been compared to cost of service During that time there may have been, and most likely were, dramatic changes in class cost responsibility and present rates may now be far from cost If this is the case, and it would be surprising if it were not, the Company's proposed allocation method will only exacerbate the extent to which rates depart from cost

Q WHAT IS YOUR SPECIFIC PROPOSAL REGARDING THE ALLOCATION OF REVENUES?

A If the approach used in the basic proposal is adopted, I recommend, as a provisional expedient, using the Company's allocation method with one important adjustment which I will describe If the preferred alternative proposal is accepted I also recommend a variant of the Company's proposed revenue allocation

In either case, I recommend that the TRA order the Company to conduct a cost of service study either in its next rate filing or, preferably in a second phase of this proceeding

Q PLEASE DESCRIBE THE COMPANY'S PROPOSED REVENUE ALLOCATION BASED ON ITS FULL REQUESTED INCREASE.

A The Company proposes to increase the base rate revenue requirement of all customer classes by approximately 15 3% in order to recover its requested increase of $4 6 million

Q IS THIS A REASONABLE METHOD?

A As discussed above, the allocation of an equal percentage increase to base rates is reasonable on a provisional basis until a cost of service study is available However, in this case there is one obvious movement toward cost that can, and should be, made immediately This relates to the allocation of the stored gas inventory costs These costs are used to serve only sales customers and should not be recovered from transportation customers In fact, the Company properly proposes to recover these costs only from sales customers under its preferred alternative proposal This same allocation should be reflected in the allocation of revenues under the basic proposal

Q WHY SHOULD THESE COSTS BE RECOVERED ONLY FROM SALES CUSTOMERS?

A CGC witness Richard Lon explains the need for stored gas inventory costs at page 7 of his direct testimony "In order to insure an adequate supply of gas during the winter heating season, Chattanooga purchases and stores gas that it can withdraw and utilize when needed"

Q HAVE YOU DETERMINED HOW THE REQUESTED REVENUES SHOULD BE ALLOCATED UNDER THE BASIC PROPOSAL OF THE COMPANY?

A Yes This is shown on Exhibit ___(AC-2) I have removed the revenue impact of the gas storage inventory costs from the remainder of the increase and allocated it to the classes on the basis of sales volumes As a result of removing the allocation of these gas costs from transportation customers who do not utilize storage gas the increase to the base rates of industrial classes is decreased from 15 3% to 11 9% The percentage increases to the other classes range from 15 7% to 16 4% reflecting the fact that these sales customers do utilize the stored gas

Q HOW HAS THE COMPANY PROPOSED TO ALLOCATE ITS REQUESTED INCREASE UNDER ITS PREFERRED ALTERNATIVE PROPOSAL?

A The Company proposes to allocate approximately $2 5 million or a little more than one-half of its total increase on an equal percent of margin basis Approximately

$1 7 million will be recovered as gas costs as described above and the remainder is recovered through the PRP tracker

Q **PLEASE DESCRIBE THE PROPOSED PRP TRACKER.**

A The PRP tracker is designed to recover the costs that the Company will incur over the next 10 years to replace 100 miles of bare steel and cast iron main and related services with new pipe

Q **HOW DOES THE COMPANY PROPOSE TO RECOVER THESE PRP COSTS FROM CUSTOMERS?**

A It proposes to recover these costs from all customers on a volumetric basis, i e , it will charge all customers an equal amount per therm of throughput

Q **IS THIS A FAIR WAY TO RECOVER THESE COSTS?**

A No This proposed recovery is not related to the way the costs are incurred and is detrimental to industrial customers

Q **WHY IS THE PROPOSED ALLOCATION OF THE PRP DETRIMENTAL TO INDUSTRIAL CUSTOMERS?**

A Industrial customers tend to use gas on a year round and sometimes around the clock basis As a result, the pipes and facilities that serve them are used much more efficiently than those that serve customers whose use is very seasonal This more efficient use is usually summarized by a calculation of the class load factor which is the ratio of the actual usage of a customer of a given size with its potential use without expanding the system The load factors for industrial customers are typically much higher than that of other classes

Q WHAT IMPACT DOES LOAD FACTOR HAVE ON REVENUE ALLOCATION?

A High load factor classes are allocated a greater portion of costs under volumetric allocations than under any other method This may be reasonable for the allocation of variable costs but it is not reasonable for the allocation of fixed costs In fact, the allocation of fixed costs to customers on a volumetric basis is a penalty for efficient use of the system.

Q ARE THE COSTS RECOVERED UNDER THE PROPOSED PRP TRACKER FIXED OR VARIABLE?

A They are fixed costs The amount that will be incurred to replace the pipes will be no different if they are fully used every day or if most of the use occurs in the winter The Company has confirmed that these are fixed costs in its Response to CMA Discovery Request No 12

Q WHY DOES CGC PROPOSE TO RECOVER ITS PRP FROM CUSTOMERS ON A VOLUMETRIC BASIS?

A No explanation was provided in the Company's testimony CMA asked the Company to explain the basis for this proposed recovery method in Discovery Request No 13 to the Company The Company provided the following terse and conclusory response "Recovering the cost on an equal cents per therm basis is a fair and equitable method of allocating the cost of the program to all customers that utilize the system" A copy of this Request and the Company's Response are attached as Exhibit ___(AC-3)

Q **IS THIS CONSISTENT WITH OTHER PROPOSALS OF THE COMPANY IN THIS FILING?**

A No A recurring theme of CGC witness Philip Buchanan's testimony is the need to recover fixed costs through fixed charges For example, at page 4 of his direct testimony he states, "In general, the proposed changes are designed to recover more of the fixed costs of providing delivery service through fixed charges In operating and maintaining the distribution system, the Company incurs substantial <u>fixed costs, which are independent of normal daily usage</u>" (Emphasis supplied)

Basic fairness as well as cost causation principles require that this important distinction also be reflected in the allocation of fixed costs to customer classes It is not reasonable, fair nor efficient to recover these costs which are independent of daily usage on the basis of daily usage But that is exactly what the Company has proposed

Q **HOW DO YOU RECOMMEND THAT THE PRP TRACKER COSTS BE RECOVERED?**

A I recommend that for purposes of this case responsibility for these costs be allocated to the classes in proportion to present base rates This is the same way they are allocated under the Company's proposal under its basic filing Charges for each class can be established by dividing the class revenue responsibility by the appropriate billing units When rates are next revisited and a cost study is available, class revenue responsibility for PRP costs should be determined on the basis of relative class demands

Since the Company proposes to reset and true up the PRP costs on an annual basis this should not introduce any administrative problems

Q HAVE YOU DETERMINED THE IMPACT OF THIS APPROACH AS COMPARED TO THE COMPANY'S PROPOSAL BASED ON ATTRITION YEAR FIGURES?

A Yes This comparison is shown on Exhibit ___(AC-4) As this Exhibit shows, the Company's proposed recovery on an equal cents per therm basis overcharges industrial customers by approximately $115,000 per year Since the Company's proposal is for approximately equal replacements annually, the total overcharge would be more than one million dollars

Q DO YOU HAVE COMMENTS ON ANY PROPOSED TARIFF CHANGES?

A Yes I have comments concerning the proposed changes to the treatment of transportation imbalances and the unauthorized use penalties

Q HOW DOES CGC CURRENTLY HANDLE IMBALANCES?

A As explained by CGC witness Steve Lindsey at page 19 of his testimony

> "The current tariff provides that when a customer uses more gas than it has delivered, the customer pays the rate applicable to the Interruptible L-1 Rate Schedule When the customer delivers more gas than used the Company purchases the excess gas ' at the Consumer's average commodity cost of gas purchased, including all applicable transportation costs (excluding penalties) during said month, except that the average commodity cost paid to Consumer by Company shall not exceed the Company's lowest priced commodity cost of gas in effect during said month '"

Q **WHY IS CGC PROPOSING TO CHANGE THIS PROVISION?**

A That is not clear Mr Lindsey's testimony simply states that either shortfalls or excesses cause CGC "problems" in managing its gas supply and that the greater the difference, the greater the problem His only description of the "problems" is a sentence stating that the "current process is confusing and a problem to administer and does not recognize the problems that occur as the amount of the over or under supply increases "

Q **DOES CGC LOSE ANY MONEY UNDER THE CURRENT PROCEDURES?**

A No In fact, because of the limitation on the amount paid for gas purchased under the present rules it makes money on customer imbalances

Q **DID CMA REQUEST INFORMATION CONCERNING ANY COSTS INCURRED BY CGC REGARDING IMBALANCES?**

A Yes CMA Discovery Request No 15 asked the Company to "Please provide any calculation of costs imposed on the Company by customer imbalances and show the derivation and workpapers supporting that derivation "

Q **WHAT WAS THE COMPANY'S RESPONSE?**

A The Company initially refused to respond to that request When it was compelled to respond it was unable to identify or quantify any cost it has incurred as a result of transportation customer imbalances

Q WHAT IS THE COMPANY'S PROPOSED METHOD OF HANDLING CUSTOMER IMBALANCES?

A Under the Company's proposal, when a customer uses more gas than it has delivered, the customer purchases the shortfall from the Company at a spot market index price that is not tied to what the Company actually pays for gas plus a penalty When the customer delivers more gas than it uses the Company purchases the excess gas from the customer at a fraction of the index price for spot market gas

Q HOW LARGE ARE THE PENALTIES THE COMPANY PROPOSES?

A First, it should be recognized that the use of a spot market index as the point of reference is, in itself, a penalty since it will almost always exceed the price that both the customer and CGC are paying In addition to that penalty, imbalances in excess of 5% would pay a penalty of 15% Imbalances in excess of 10% would pay a penalty of 30% Imbalances in excess of 15% would pay a penalty of 40% and imbalances in excess of 20% would pay a penalty of 50%

By way of example, if the index price were $6.00 per Dth, the 15% penalty applicable to customers with imbalances as low as 5% would be $0 90 per Dth This is higher than the proposed transportation rate A customer that incurs unusual imbalances of 20% during a particular month because of operating problems beyond its control would be charged a penalty of $3 00 per Dth These penalties are in addition to paying the gas cost of $6 00 per Dth

Q ARE THERE ANY OTHER FACTORS THAT MITIGATE ANY "PROBLEMS" THAT IMBALANCES CAUSE THE COMPANY?

A Yes The only imbalances that can have any effect on the Company's gas supply management are the <u>net</u> imbalance of all transportation customers, not the sum of individual imbalances For example, consider two customers that each nominate 500 Dth per day Customer A may actually use 550 Dth on a particular day while Customer B uses only 450 Dth Both customers have 10% imbalances but the Company sees no imbalance whatever on its pipeline deliveries as a result of these imbalances Nevertheless, CGC would charge each customer penalties of approximately $2 00 per Dth Moreover, even if there is a net imbalance on the part of transportation customers it might be used by the Company to offset an opposite imbalance caused by a difference between the Company's pipeline nomination for sales customers and the actual usage of sales customers

Q HOW SHOULD THIS CUSTOMER DIVERSITY BE RECOGNIZED IN THE COMPANY'S TARIFFS?

A Under existing tariffs the imbalance charges are approximately cost based so that a diversity adjustment is not necessary However, if the TRA were to accept the Company's proposed imbalance scheme it should also order the Company to establish a customer balancing pool The Company would then impose its penalties on the net imbalance of the pool and apportion it among customers based on relative individual imbalances

Q DOES THE COMPANY RECOGNIZE THIS DISTINCTION?

A Apparently so CMA Discovery Request No 16 asked

> "Has the Company considered any proposals that would allow for the pooling of customer imbalances so that only net imbalances are penalized? If yes, please provide copies of all studies and/or reports "

In its response, the Company noted

> "The Company has discussed this briefly, but details have not been developed and there are no studies or reports. This is something the Company would consider implementing to calculate imbalance charges There is no reference to penalty charges in this provision "

Q DOES THE COMPANY'S PROPOSAL CHARGE FOR NET IMBALANCES?

A No It charges for total undiversified imbalances

Q ONE OF THE PROBLEMS THAT THE COMPANY MENTIONED CONCERNING THE PRESENT SYSTEM WAS CONFUSION. DO YOU HAVE ANY SUGGESTIONS CONCERNING THAT PROBLEM?

A Yes First, I would note that Mr Lindsey does not explain if it is customers or the Company that is confused In either case, the proposal would replace the present method with one that is much more complex and difficult to understand so it certainly will not solve the asserted problem with the current method

Q IS IT POSSIBLE TO MAKE THE CURRENT PROCEDURES SIMPLER WITHOUT TOTALLY ABANDONING THEM?

A Yes The apparent confusion is related to the need to know what the customer is paying for gas and what is the "lowest price commodity cost of gas" in the Company's portfolio during a given month Both of these determinations would be unnecessary if the Company simply paid customers for excess gas at the weighted average cost of gas (WACOG) experienced by the Company during the month If there is some problem calculating this, any reasonable and objective determination of a price could be used as long as it does not include a penalty

Q **PLEASE SUMMARIZE YOUR PROPOSAL CONCERNING BALANCING.**

A The TRA should reject the Company's proposed balancing penalties and maintain the present tariff with the following change The price that CGC pays customers that deliver excess gas should be equal to the system WACOG for the month the imbalance occurred

If, on the other hand, the TRA does allow the Company to implement its proposed matrix of imbalance charges and penalties, it should be applied only to the net imbalance of transportation customers and apportioned among all transportation customers in proportion to the absolute values of each customer's imbalance

Q **WHAT IS YOUR CONCERN REGARDING THE OVERRUN PENALTY?**

A The Company is proposing to double the overrun penalty The present penalty is the higher of $15 per Dth or the actual cost to the Company that results from the customer's overrun The proposal is to increase the penalty to the higher of $30 per Dth or actual cost

Q **WHAT CAUSES A CUSTOMER TO INCUR THE OVERRUN PENALTY?**

A An overrun is defined as a situation in which a customer takes gas in excess of its daily contract amount or does not comply with a curtailment order

Q **WHY DOES THE COMPANY ISSUE A CURTAILMENT ORDER?**

A It does so when it determines that the "supply and capacity services contracted by the Company are not sufficient to meet the full requirements of Customers desiring sales services from the Company"

Q **HAS THE COMPANY EXPLAINED WHY IT IS PROPOSING TO INCREASE THIS PENALTY?**

A No Mr Lindsey's testimony simply states that it is doing so

Q **IS A $30 PER DTH PENALTY LIKELY TO DISCOURAGE OPERATIONS ON THE PART OF CUSTOMERS THAT WERE NOT DISCOURAGED BY A $15 PER DTH PENALTY?**

A No If a customer was unable to correct the situation leading to an overrun at a cost of $15 per Dth, it is not likely that it could do so for $30 per Dth Incurring such a punitive penalty suggests that the customer, like CGC, was encountering serious operating problems at the time

Q **IS IT POSSIBLE THAT THE COMPANY COULD INCUR COSTS IN EXCESS OF $15 PER DTH TO PROVIDE GAS TO A CUSTOMER IN AN OVERRUN SITUATION?**

A Yes Although such circumstances would be rare it is possible that the costs, which include the cost of gas, could exceed $15 per Dth for short periods of time.

Q WILL THE COMPANY LOSE MONEY IN SUCH CIRCUMSTANCES?

A No The customer would be required to pay the full cost in those circumstances which would also exceed $15 per Dth

Q WHAT IS YOUR RECOMMENDATION CONCERNING THE PENALTY PROVISION?

A I do not believe the Company has justified a change from the present level of $15 per Dth

Q IF THE TRA DETERMINES THAT IT IS NECESSARY TO REVISE THE PENALTY DO YOU HAVE AN ALTERNATIVE TO SUGGEST?

A Yes The real problem is the combination of an arbitrary high number and the "greater of" language I would recommend that the overrun charge be set at the actual cost to the Company that results from the customer's overrun plus a reasonable penalty to provide an incentive for avoiding such situations This penalty should be no more than $2 00 per Dth This would eliminate the need for a "greater of" provision and ensure that customers always have a disincentive to incur overruns

It is also important to specify in the Tariff that all revenues in excess of costs be returned to customers through the PGA

Q DO YOU HAVE ANY OTHER CONCERNS WITH SERVICE TO COMMERCIAL AND INDUSTRIAL CUSTOMERS ON THE CGC SYSTEM?

A Yes The ability of customers to choose their own suppliers and use CGC only as a transporter of their gas is unduly limited

Q PLEASE DESCRIBE THE PRESENT AVAILABILITY OF TRANSPORTATION SERVICE ON THE CGC SYSTEM.

A Under the present tariffs, transportation service is unavailable to customers that use less than 100 Dth per day or 36,500 Dth per year

Q HAS CGC PROPOSED ANY CHANGES TO ITS MINIMUM REQUIREMENT FOR TRANSPORTATION IN THIS CASE?

A No

Q WHY IS THE AVAILABILITY OF TRANSPORTATION SERVICE TO CUSTOMERS OF A LOCAL DISTRIBUTION COMPANY (LDC), SUCH AS CGC, IMPORTANT?

A The availability of transportation service allows customers to seek their own suppliers of natural gas The existence of this option provides benefits to the customers choosing that option as well as customers that continue to purchase both gas supply and delivery service from the LDC The customers that take advantage of the opportunity to transport their own supplies are able to lower their costs by finding competitive sources of supply and by structuring supply arrangements to meet their specific needs The fact that customers are able to shop for competitive supplies also provides a check on the purchasing practices of the distribution company

Q WHY SHOULD THE THRESHOLD FOR CUSTOMERS TO TAKE ADVANTAGE OF TRANSPORTATION SERVICE BE LOWERED AT THIS TIME?

A The only arguments I am familiar with for not making transportation service available to all customers are administrative It is often suggested that it is important for the

LDC to first gather experience with a relatively few large accounts before expanding availability to smaller accounts

Regardless of the importance of such concerns, CGC has been offering transportation service to its largest customers for some time now and should have completed its "learning" In any event, it is clearly time to expand the availability of this service to much smaller customers The size of individual customer accounts should not be the determining factor in the availability of transportation service, but rather the willingness of the customer to assume responsibility for purchasing its own gas supply

Q IS IT LIKELY TO BE ECONOMIC FOR SMALLER CUSTOMERS TO TRANSPORT THEIR OWN SUPPLIES?

A It probably will be for some, but will not be for others Customers that do purchase their own gas supplies bear any risks associated with this decision Since the customers bear the risks, they should be allowed to make their own decisions rather than having it made for them by CGC

Q DOES NASHVILLE GAS COMPANY HAVE A SIMILAR LIMITATION?

A Yes However, the minimum limitation in the Nashville Gas Company Tariffs is 50 Dth per day or only one-half as much as CGC's

Q WHAT IS THE MINIMUM REQUIREMENT FOR ATLANTA GAS LIGHT COMPANY, CGC'S SISTER COMPANY IN GEORGIA?

A Transportation service is available to all customers of Atlanta Gas Light Company, including small commercial and residential customers

Q **WOULD CGC LOSE ANY PROFIT IF IT EXPANDED ITS TRANSPORTATION SERVICE AVAILABILITY?**

A No CGC does not profit from its sales of gas Thus, it should be indifferent as to whether it delivers sales gas or transportation gas, as long as the utility's cost of service is fully recovered CGC's transportation tariffs assure that it has the opportunity to fully recover its cost of service

Q **HOW DOES THE 100 DTH PER DAY THRESHOLD OF CGC GENERALLY COMPARE WITH THE MINIMUM REQUIREMENTS OF OTHER LDCS?**

A While I have not prepared a detailed survey concerning this question, I have reviewed the tariffs of numerous other LDCs as part of my preparation for this and other proceedings In general, I have found the minimum volume requirements to be much less than those of CGC In fact, on several systems like Atlanta Gas Light Company even residential customers are able to shop for their own gas and have it delivered by the LDC

Q **DO YOU HAVE A SPECIFIC RECOMMENDATION CONCERNING AN EXPANSION OF THE AVAILABILITY OF TRANSPORTATION SERVICE AT THIS TIME?**

A Yes I recommend that transportation service be made available to all customers that use at least 50 Dth per day as does Nashville Gas I also recommend that the TRA order CGC to expand the availability of transportation further in the near future

Q **DOES THIS COMPLETE YOUR DIRECT TESTIMONY?**

A Yes, it does

Qualifications of Alan Chalfant

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Alan Chalfant My business mailing address is P O Box 412000, 1215 Fern Ridge Parkway, Suite 208, St Louis, Missouri 63141-2000

Q WHAT IS YOUR OCCUPATION?

A I am a consultant in the field of public utility regulation and am a principal in the firm of Brubaker & Associates, Inc (BAI), energy, economic and regulatory consultants

Q PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A I hold a Bachelor's Degree in Mathematics from Northern Illinois University and the degree of Master of Arts in Economics from Washington University From 1968 to 1973, I was Assistant Professor of Economics at California State University at Northridge, California Among other courses in economics and statistics, I taught courses in the economics of antitrust and regulation at both the graduate and undergraduate levels I have also taught courses at both graduate and under-graduate levels at California Lutheran College

In 1973, I accepted a position with the Public Service Commission of Wisconsin in the Utility Rates Division While at the Commission, I designed the rates for electric and natural gas utilities and aided in the preparation for cross-examination of witnesses representing utilities and intervenors before the Commission

I joined the firm of Drazen-Brubaker & Associates, Inc in September 1974 and became a Principal in that firm in 1988 In April 1995 the firm of Brubaker & Associates, Inc was formed It includes most of the former DBA principals and staff and currently has its principal office in St Louis, Missouri, with branch offices in Denver, Colorado, Chicago, Illinois, Corpus Christi, Texas, and Plano, Texas

Since 1974, I have been engaged in the preparation of studies relating to utility rate matters and have participated in numerous electric and gas rate cases In total, I have participated in cases involving more than 60 electric utilities, 30 gas distribution utilities and 20 interstate pipelines

Q HAVE YOU PREVIOUSLY TESTIFIED BEFORE A REGULATORY COMMISSION OR A PUBLIC AUTHORITY?

A I have testified before the Federal Energy Regulatory Commission and more than 30 state public utility regulatory commissions In addition, I have appeared before a number of municipal regulatory bodies and courts

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Chattanooga Gas Company
Chattanooga Manufacturer's Association
Discovery Request No. 6
Docket Number 04-00034
April 30, 2004
Page 1 of 2

Data Request No. 6

Please provide the basis for the Company's decision to allocate the requested increase equally across all customer classes.

Response:

Chattanooga Gas Company (the Company) does not propose to allocate the requested increase equally across all customer classes. The Company is requesting rate relief of $4.56M. As described in Exhibit PGB-7 Page 1 of 1, the Company is requesting $2.02M of the increase from the residential customer class, $0.003M from the Multi-Family Housing customer class, $1.75M from the commercial customer class, and $0.70M from the industrial customer classes. The allocation of the requested increase can be summarized as follows:

Customer Class	Proposal of Rates as Filed		Proposal of The Company's Preferred Rates	
	Increase	% of Total Increase	Increase	% of Total Increase
Other Revenue	$0.09M	2.0%	$0.08M	3.1%
Residential	$2.02M	44.4%	$1.08M	43.8%
Multi-Family Housing R-4	$0.003M	0.1%	$0.002M	0.1%
Commercial	$1.75M	38.3%	$0.93M	37.9%
Industrial	$0.70M	15.3%	$0.37M	15.1%
Total Requested Increase	$4.56M	100.0%	$2.46M	100.0%

The Company proposes to increase rates to each customer class proportional to the class' contribution to total attrition year gross margin under current rates. The amount of the proposed increase, less Other Revenue and Special Contract Revenue, is allocated to each customer class so that the percent of increase in the attrition year from current rates to proposed rates would be the same for each class. Thus, for example, even though residential rates will be increased by $2.02M and industrial rates will be increased by only $0.70M, rates for the residential and industrial customer classes will each be increased by 15.3% over current rates.

The allocation of the proposed increase to each customer class proportional to its contribution to total attrition year gross margin under current rates resulting in an equal percentage increase for the customer classes is consistent with the agreement of the Chattanooga Manufacturers Association, the Consumer Advocate Division, and Chattanooga Gas Company at the time of Chattanooga Gas Company's last rate increase in Docket No. 95-02116. In that docket the parties agreed: "Any rate increase awarded in this case will be spread equally, on a percentage basis as applied to the gross margin, among the residential, commercial and industrial classes." [1]

[1] Joint Settlement Among Chattanooga Gas Company, the Consumer Advocate Division, and Associated Valley Industries/Chattanooga Manufacturers Association Intervention Group Concerning Rate Design Issues filed in Docket 95-02116, paragraph 1.

Chattanooga Gas Company

Recommended Allocation of the Requested Increase Under the Basic Proposal

Line		Present Base Revenue	Proposed Base Revenue	Increase Amount	Increase Percent	Storage Inventory Costs	Total Increase Amount	Total Increase Percent	Sales Volumes	Percent of Sales
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1	Other Revenue	$ 973,248	$ 1,062,197	$ 88,949	9.1%		$ 88,949	9 1%		
2	Special Contract Revenue	$ 80,286	$ 80,286	$ -	0 0%		$ -	0 0%		
3	Residential	$ 13,183,382	$ 15,206,266	$ 1,233,124	9.4%	$ 830,170	$ 2,063,294	15 7%	42,636,106	47.55%
4	Multi-Family Housing	$ 22,528	$ 25,985	$ 2,107	9 4%	$ 1,459	$ 3,566	15 8%	74,918	0.08%
5	Commercial	$ 11,383,796	$ 13,130,549	$ 1,064,797	9.4%	$ 796,509	$ 1,861,307	16 4%	40,907,371	45 62%
6	Industrial	$ 4,553,227	$ 5,251,883	$ 425,892	9 4%	$ 117,692	$ 543,584	11.9%	6,044,467	6 74%
7	Total	$ 30,196,467	$ 34,757,166	$ 2,814,869	9 3%	$ 1,745,830	$ 4,560,699	15.1%	89,662,862	100 00%

Exhibit ___(AC-2)

Data Request No. 13

Please explain the basis, if any, for recovering all costs on an equal cents per therm basis in the proposed Chattanooga assisted rate for energy services tracker.

Response:

Recovering the cost on an equal cents per therm basis is a fair and equitable method of allocating the cost of the program to all customers that utilize the system.

Chattanooga Gas Company

Comparison of CGC and CMA Recommended Allocation of PRP

Line		Annual Volumes Therms	Annual Volumes Pct of Total	Present Base Revenue Amount	Present Base Revenue Pct of Total	CGC Allocation of PRP Revenue	Recommended Allocation of PRP Revenue	Difference
		(1)	(2)	(3)	(4)	(5)	(6)	(7)
1	Residential	42,636,106	26 62%	$ 13,183,382	45 24%	$ 95,563	$ 162,401	$ 66,838
2	Multi-Family Housing	74,918	0.05%	$ 22,528	0.08%	$ 168	$ 278	$ 110
3	Commercial	40,907,371	25.54%	$ 11,383,796	39 06%	$ 91,688	$ 140,232	$ 48,544
4	Industrial	76,552,390	47 79%	$ 4,553,227	15 62%	$ 171,581	$ 56,089	$ (115,492)
5	Total	160,170,785	100.00%	$ 30,196,467	100.00%	$ 359,000	$ 359,000	$ -

Exhibit ___(AC-4)

Direct Testimony of Earl Burton

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

A. Earl Burton
Tennessee Energy Consultants
100 E. 10th Street Suite 401
Chattanooga TN 37402

Energy Consultant

Q. **Please outline your education, professional training and experience**

A. I graduated from the Georgia Institute of Technology with a degree in Mechanical Engineering in 1984. I also earned a Masters Degree in Business Administration from University of Tennessee Chattanooga in 2003. I began working for Atlanta Gas Light Company in 1984 and transferred to Chattanooga Gas Company in 1989 where I worked until 2003. My responsibilities and positions with Chattanooga Gas Company included Manager of Marketing, Commercial Representative, and Manager of Rates and Marketing where I was very involved marketing natural gas, working with industrial accounts and natural gas billing. As owner of Tennessee Energy Consultants, I assist industrial customers with managing natural gas and electric costs.

Q. **Have you previously submitted testimony for the Chattanooga Manufacturer's Association Intervention Group to this Authority?**

A No

Q. **What is the subject of your testimony?**

A. I will provide expert testimony related to interstate pipeline tariffs and related gas distribution balancing costs.

Q. **Have you prepared any exhibits to accompany your testimony?**

A. Yes

Q. **Are you familiar with related balancing costs incurred by gas distribution companies as it relates to providing supply and transportation options to industrial endusers?**

A. Yes, One of my clients is a large carpet manufactures that has contracted for my services to work with several municipalities in Tennessee and Alabama to secure a transportation rate behind their system. One of the issues we have addressed is the costs of balancing that the gas distribution company would incur. As part of my services, I have assisted these municipalities with drafting a transportation rate tariff that will safeguard the integrity of their gas system and ensure that their other customers are not adversely impacted by transportation customers.

Q **What interstate pipelines serve these municipalities?**

A East Tennessee Natural Gas (Duke Energy) and Southern Natural Gas Company which are the same pipelines that serve Chattanooga Gas Company.

Q. **Have you performed research on the penalty costs on both of these pipelines if a gas distribution uses unauthorized overrun gas over their contract entitlements.**

A. Yes, The penalty rate on both East Tennessee and Southern Natural Gas Company's FERC approved tariff is $15.00 per dekatherm. "See Exhibit A."

Q. **Please explain**

A. An gas distribution company such as Chattanooga Gas Company would pay a charge of $15.00 per dekatherm if they used natural gas over and beyond their contract entitlements whenever the pipeline effectuated a MAD or Type 3 Operational Flow Order.

Q. **In designing transportation/industrial tariffs for other gas companies served by East Tennessee Pipeline and Southern Natural Gas Company, what penalty rate did you recommend for unauthorized consumption interruptible endusers?**

A I recommended the interstate pipeline rate of $15.00 per dekatherm. This rate was established based on the interstate pipeline rate and recovers the potential penalty exposure for the local distribution company.

Q. **What is the penalty rate proposed for Chattanooga's L-1, I-1, T-1, and T-2 Rate tariffs?**

A The penalty rates proposed in Chattanooga's rate tariffs are $30.00 per dekatherm.

Q **What other aspects of penalty rates are relevant to distribution actual penalty cost exposure?**

A. Both interstate pipelines offer a bandwidth tolerance before the penalty rate would be charged. In East Tennessee's tariff, the bandwidth tolerance is 50 dekatherms or 2% before actual penalty charges would apply. This allows for some flexibility given the variability of gas flows which are unpredictable with many customers.

Q **What is your opinion regarding the proposed cashout and monthly imbalance tariff proposed by Chattanooga Gas Company, and how the tariff compares with Chattanooga Gas Company's cost of balancing through their interstate pipeline suppliers?**

A The potential balancing costs will be much higher for industrial end-users relative to Chattanooga Gas Company's actual costs Let me explain. Most gas utilities are part of a pool of other utilites, and their cumulative delivery points are pooled together and served under an Operating Balance Agreement with East Tennessee Pipeline. Therefore, there is a netting effect on the cumulative imbalance that mitigates much of the cashout and balancing costs. Chattanooga Gas Company would also benefit from the netting effect of transport customers because some will be long and short, thus the cumulative imbalance for the utility would be considerably less than the sum of imbalances. Another issue for industrials is the variability of their gas consumption load profile. Some industrials operate on a five day work week, or may have a random gas load profile that makes balancing difficult The average variability for an industrial customer would be considerably higher than the variability of Chattanooga Gas Company. Thus, the forecasting and balancing required for industrial end-users is more difficult than a typical gas distribution company. Another issue is the price used for cashout and imbalance costs. Chattanooga Gas Company proposes to use the highest daily index, and their pipeline supplier, East Tennessee Natural Gas Company uses the highest weekly price published. Given the volatile spikes with daily natural gas pricing, I would be concerned with this pricing methodology and additional cost impact to industrial endusers. Given the above issues addressed above, the balancing costs for industrial endusers served by Chattanooga Gas Company will be considerably higher than Chattanooga Gas Company's costs, furthermore, will result in additional administrative costs to industrial end-users to accurately forecast and predict gas nominations and consumption.

Q. **Is the reference to Nashville Gas Company's tariff a fair comparison relative to cashout and imbalance costs?**

A. No. Nashville Gas Company's market is a firm transportation market. The costs of firm interstate service is the norm for the Nashville market. The market for interstate transportation to Chattanooga is mostly interruptible given the higher costs of interstate transportation and capacity constraints on Southern Natural and East Tennessee. Therefore, balancing is much more difficult if interstate transportation is subject to interruption when the pipeline issues an operational flow order. Nashville Gas Company's transportation customers receive firm service through most of their providers, thus enabling them to better manage balancing without the costs of capacity interruptions

Q. **Are you aware of some of the gas management issues that prompted Chattanooga Gas Company to propose amendments to tariff?**

A. Yes, Chattanooga Gas Company needs to modify the existing tariff to close some loopholes and ensure that the integrity of their system is maintained and firm ratepayers do not subsidize the gas costs of industrial endusers. However, this can be accomplished with some simple modifications to the tariff that will not penalize Chattanooga's industrial customers.

Q. **Do you have a tariff recommendation?**

A. Yes, I would propose the following language, Exhibit B. for the L-1 Rate Tariff.

Q. **Please explain.**

A. Chattanooga Gas Company could ensure that the full costs of gas service are recovered through the rates by issuing a supply restriction provision on Chattanooga's L-1 customers. This would allow Chattanooga to recover the actual costs of gas supply whenever Chattanooga Gas Company felt is was necessary implement. By implementing a supply restriction, Chattanooga would be able to eliminate any subsidy that the firm ratepayers would incur with this service. It would also be an incentive for the L-1 customers to nominate sufficient gas supplies to meet their requirements. On the other hand, Chattanooga Gas Company may elect during certain times to make L-1 supply available for competitive purposes or to use storage gas to soften the impact of natural gas volatility. Chattanooga's industrial end-users would desire to receive some benefits from storage assets whenever possible.

Q. **Are you familiar with Chattanooga's industrial billing system?**

A Yes, as Manager of Rates and Marketing for Chattanooga Gas Company, I was in charge for implementing the new system back in 1998.

Q. **Can this functionality of a supply restriction rate be added to the existing billing system?**

A. Yes, with a few changes the billing system could be modified to bill this proposal Furthermore, the complexity of billing would be greatly reduced relative to Chattanooga Gas Company's tariff proposal.

Q **What is your opinion regarding the proposed Semi-Firm Sales Service SF-1.**

A. I would applaud Chattanooga Gas Company for this rate offering An important issue with industrial endusers is managing gas volatility. I believe access to gas storage for all customers will be of increasing importance especially if we have as severe gas pricing spikes. Given the complexity of this tariff, and ambiguity of service reliability, I would be concerned on how this rate is implemented and managed from Chattanooga's perspective. I would suggest that Chattanooga Gas Company work closely with the Chattanooga's industrial endusers to fine tune this rate offering to achieve a quality service offering that will be beneficial to industrial end-users.

Q. **Does this conclude your testimony**

A. Yes

Rate Schedule LMS-MA
Load Management (Market Area) Service

6. BALANCING OBLIGATION

Based upon the best information available, a Balancing Party shall take action to correct any imbalances occurring during the month by making adjustments in nominations or deliveries. If Balancing Party fails to take such corrective action, then Transporter may, upon 48 hours notice, adjust Balancing Party's scheduled deliveries over the remainder of the calendar month in order to maintain a balance of deliveries and nominations, provided Transporter determines that such action is necessary to maintain the operational integrity of the system or to enable Transporter to meet its firm obligation to its other shippers.

7 UNAUTHORIZED OVERRUN

7.1 On any day, Transporter may, based on a good faith belief that such action is necessary and appropriate to protect system integrity and ensure firm deliveries, upon 8 hours prior notice via LINK®, invoke its right to assess Unauthorized Overrun Charges in accordance herewith Transporter shall provide fax or telephone notification of its intent to invoke its right to assess Unauthorized Overrun Charges, for all customers that have provided Transporter with a 24 hour telephone or fax number. Transporter shall have the right to assess an Unauthorized Overrun Charge of fifteen dollars ($15) per DTH on quantities taken in excess of a Balancing Party's Maximum Allowed Deliveries ("MAD") plus a 2% allowable variation or 50 DTH, whichever is greater. A Balancing Party's MAD shall be calculated as follows:

Exhibit B.

CMA proposed Tariff Changes. Add below restriction to existing L-1 Tariff Sheet No. 25B

Supply Restriction

Whenever service under this rate schedule would result in an under-recovery of gas costs and higher costs to the Company's firm ratepayers, the Company may issue a supply restriction whenever applicable to recover additional costs of providing gas supplies on these days. The incremental costs of this gas supply would reflect the actual costs to the Company to purchase and deliver gas to their distribution system. The incremental rate charge would reflect the cost premium over the current L-1 tariff required to purchase gas supplies during the supply restriction.

DIRECT TESTIMONY OF TIM SPIRES

Q. Please state your name, business address and occupation.

A. I am Tim Spires, Director of Manufacturing for NA Industries. My business address is 2651 Riverport Rd, Chattanooga, Tennessee.

Q. What are your principal responsibilities as Director of Manufacturing of NA Industries?

A. I am responsible for the overall operation of the company

Q. Is Chattanooga the only area in which NA Industries operates?

A NA Industries in an international company with 2 manufacturing sites in the United States.

Q. Please outline your educational and professional training and experience.

A I received a Bachelor of Chemical Engineering, and 25 years experience in Engineering and Management.

Q. Have you previously submitted testimony for the Chattanooga Manufacturer's Association ("CMA") Intervention Group to this Authority?

A. No.

Q. What is the subject of your testimony?

A I will present information opposing Chattanooga Gas Company's filing for a revised natural gas tariff in the manner submitted to this Authority.

Q. Have you prepared any exhibits to accompany your testimony?

A. No.

Q. Does your company have a facility located in Hamilton County, Tennessee that utilizes fuel supplied by Chattanooga Gas?

A. Yes. NA Industries has one facility located in Hamilton County, Tennessee that employs over 75 people at wages significantly higher than minimum wage. In addition, NA Industries has a goal to expand the number of jobs in and around Hamilton County to support this facility.

Q. Please describe the type of labor that your company uses in its manufacturing and production processes in Chattanooga.

A. Our company directly provides jobs for skill levels ranging from employees with the equivalent a high school education to very technical occupations and careers requiring college and post-graduate degrees.

Q. Does NA Industries intend to expand its facilities in Chattanooga or Hamilton County, Tennessee?

A. We hope to do so.

Q. Does the cost of utility services factor into such expansion plans?

A. Yes. All costs and expenses factor into such plans for any company that seeks to increase capacity and grow jobs in Chattanooga or Hamilton County

Q. What Chattanooga Gas Company Gas Rate Schedule does NA Industries currently subscribe to?

A NA Industries is served under the I-1 Commercial and Industrial Large Firm Sales Service and the T-2 Interruptible Transportation Service with Firm Gas Supply Backup.

Q. Has service under these rate schedules provided NA Industries Inc. options beneficial to your company?

A. Yes. NA Industries, Inc has no backup system so we enjoy the reliability of firm service contracted through Chattanooga Gas Company. We also prefer to manage our own gas procurement by transporting natural gas through the T-2 Interruptible Transportation Rate.

Q. Does NA Industries make a significant contribution to Chattanooga Gas Company in order to guarantee firm service?

A. Yes We make a significant contribution through the I-1 and T-1 Firm Demand Charge that gives NA Industries the right to use natural gas priced at the I-1 tariff rate whenever our transportation is interrupted by our supplier. It is my understanding that the firm demand charges we pay through the I-1 rate reimburses Chattanooga Gas Company for the cost of reserving the necessary interstate pipeline capacity and reserving pipeline storage to meet our gas requirements.

Q. Will the proposed balancing changes to the I-1 and T-2 rate schedules increase costs for NA Industries Inc?

A The balancing costs will increase significantly for NA Industries, and others, and will not be manageable under the current proposed language. This will force NA

Industries to take review all of its options, including but not limited to installing a backup system or subscribing to another rate schedule.

Q. Please explain.

A. For instance, our interstate transportation is delivered to Chattanooga's city-gate on a recallable basis, and if the interstate pipeline issues an Operational Flow Order our natural gas will not be delivered Several days of transportation interruption will result in a significant short position with Chattanooga Gas Company. Chattanooga Gas Company's proposed language would charge us the highest Gas Daily index for the applicable month, plus we would be further penalized by the balancing penalty tiers. Given the volatility of natural gas, especially during the winter with cold weather, this could result in NA Industries paying a *premium* of several dollars per dekatherm. That risk is not acceptable; it would equate to cost penalties in the tens of thousands of dollars to NA Industries.

Q. Did Chattanooga Gas Company confer with NA Industries about the proposed changes or ask for comments relative to the potential impact of this tariff?

A. No. In fact, we are very disappointed that Chattanooga Gas Company did not seek out our company or others and allow input into the tariff change before the rate filing was filed. I am unsure whether they understand the detrimental cost impacts that customers in our rate class will incur.

Q. What other provisions of the tariff changes does NA Industries oppose?

A. NA Industries opposes the annual election requirements proposed in Section 5 of the T-2 Rate Schedule. As I mentioned before, NA Industries is making a significant rate contribution that allows us to use the I-1 tariff gas supply. The proposed balancing changes will eliminate the tariff gas supply option if we elect to transport natural gas. Thus, even though we would still be making a considerable contribution to pay for firm assets and storage, the proposed tariff change removes the value of what N. A. Industries would receive.

Q. Does NA Industries have a recommendation regarding the proposed tariff changes?

A. We believe that the current tariff language for the I-1 and T-2 rate schedules should remain the same. The current tariffs allow NA Industries options that have been and are beneficial to our business. This ensures that the value of pipeline assets we subsidize through the rates are returned in the form of rate supply options that provide us energy cost savings.

Q. Does this conclude your testimony?

A. Yes, it does.

Direct Testimony of Ray Childers

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

A I am Ray Childers I am President of the Chattanooga Manufacturers Association. The address of the Chattanooga Manufacturers Association is now 100 Cherokee Boulevard, Suite 313, Chattanooga, Tennessee, 37405.

Q **What are your principal responsibilities as President of the Chattanooga Manufacturers Association (sometimes referred to as "CMA")?**

A. I am responsible for the daily operations of the Chattanooga Manufacturers Association including, but not limited to, disseminating news and information regarding actions or activities that may impact or affect manufacturers' growth and economic development in Chattanooga, Hamilton County and surrounding areas in Tennessee.

Q. **Please outline your educational and professional training and experience.**

A. I received a Bachelor of Science (Education) degree from the University of Tennessee at Knoxville in 1962 I have completed numerous post-graduate level classes at Middle Tennessee State University. I began my employment with DuPont in 1966 at its Old Hickory facility outside of Nashville, Tennessee. I also worked at DuPont's Chattanooga plant, and was employed by that fine company for 26 years. I have been President of the Chattanooga Manufacturers Association since leaving DuPont in 1992. I am also a registered lobbyist in the State of Tennessee.

Q. **Have you previously submitted testimony for the Chattanooga Manufacturers Association Intervention Group to this Authority?**

A. Yes, I have. I recall submitting testimony last year in conjunction with the Tennessee American Water Company's request to change tariffs and increase rates involving water and fire hydrants. I do not recall whether I have filed testimony in any other cases before this Authority (or its predecessor).

Q. **What is the subject of your testimony in this case?**

A I oppose Chattanooga Gas Company's petition to revise their natural gas tariff so as to implement higher rates. I wanted to provide information about the negative impact that the proposed changes would have on CMA member companies and, also, those companies that rely upon or supply to such companies as part or all of their business

Q **What impact, if any, do you believe the Company's proposed rate increase will have to economic development in the production, manufacturing and industrial sectors of the Chattanooga economy?**

A. I said this last year, and it remains true today, -- Chattanooga, and the State of Tennessee for that matter, is struggling to retain current production, industry and manufacturing jobs; jobs that pay at a much greater scale on average than the typical service industry employment (and other minimum wage sectors). Chattanooga and the State of Tennessee also are struggling in their efforts to attract new industrial and manufacturing jobs. While this is true for a variety of reasons, if the proposed rate increase is implemented, it will cause our manufacturers to be less competitive precisely at a time when becoming *more competitive* is essential In addition, it will drive away long-term capital investment used for expansion and increasing production from some Chattanooga plants.

Q. **Is the potential increase in rates the only concern that you have?**

A No.

Q **What other concerns do you have about the petition filed by Chattanooga Gas Company as it affects the manufacturing sector?**

A. I have many concerns. First, I am concerned that this local monopoly called Chattanooga Gas, is being directed by persons out-of-state to undertake actions in Tennessee that may not be consistent with the best interests of Tennessee residents, employers and manufacturers, especially since the parent company in Atlanta continues to grow. The primary staff influence in Chattanooga has dwindled over the past decade. Communication with affected ratepayers now is essentially non-existent. I was not asked for any input, comment or feedback prior to Atlanta's pronouncement of this petition and, to my knowledge, none of CMA's manufacturing member ratepayers were asked in advance of the submission how such an increase might adversely affect them.

Q. **Please continue.**

A In addition to concerns expressed by others, I fear that the penalty and balancing provisions are unfair and not reasonable as currently written. I also question whether benefits from the system assets flows down to the Company's ratepayers in and around Chattanooga, but due to the number of interventions in the recent past we cannot afford to investigate that issue in a manner that we believe would be adequate -- especially as to affiliate transactions. We would like to respectfully request and encourage the Authority to assist us in ensuring that this is happening, since we cannot even get questions of that nature answered by the Company. *See Company's responses dated July 15, 2004 to CMA Data Requests Nos 26 through 33.*

Q. **Is it your understanding that a portion of the Company's recent proposal constitutes an effort by the Company to make a profit off of penalties it imposes on customers?**

A. In trying to understand what it is the Gas Company seeks from its penalty provisions, it appears that they want to impose the highest penalty and biggest burden they possibly can against industrial customers, and to do so without regard to any actual penalty imposed by the pipeline That would appear to be an unacceptable practice for a regulated monopoly, but even if it is not, that is not the type of business practice which will help to bring jobs to Chattanooga and Hamilton County.

Q **How would the Authority's acceptance of Chattanooga Gas Company's petition as currently submitted affect the manufacturing sector in Chattanooga and Hamilton County?**

A. When companies seek to locate in a city, county or state, they oftentimes closely evaluate the possible expenses and costs that may be involved in operating a facility. While one significant factor certainly is those hard costs, economic prospects also consider the regulatory environment and relationships. All of that factors into whether a company will choose to locate a plant here and employ Tennessee residents. To the extent there appears to be an unfavorable climate surrounding regulated utilities servicing the manufacturing sector, the various persons charged with marketing to economic development prospects and growing Chattanooga and Tennessee's tax base is made that much more difficult

Q. **Does this complete your testimony in this rate increase proceeding?**

A. Yes.

<u>**Direct Testimony of Dan Nuckolls**</u>

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

A. I am Dan Nuckolls, Director of Operations and Maintenance for Koch Foods, LLC. My business address is 1835 Kerr Street, Chattanooga, Tennessee 37401

Q. **What are your principal responsibilities as Director of Operations and Maintenance of Koch Foods, LLC?**

A I am responsible for all plant operations, plant maintenance, export logistics and special projects involving my company's production facility in Chattanooga and feed mill in Hamilton County, just outside of the Chattanooga city limits.

Q. **Please outline your educational and professional training and experience.**

A. I received a Bachelor of Business Administration degree with an emphasis in management from West Georgia State University. I also have an Associates degree in Architectural Engineering Technology from Southern Tech in Marietta, Georgia I have worked in the poultry industry for 22 years with the following companies· Con-Agra, Seaboard Farms and Koch Foods. I have been with my present company, Koch Foods, for almost 7 years. I have been Director of Operations and Maintenance at Koch Food's Chattanooga facility since 2002.

Q. **Have you previously submitted testimony for the Chattanooga Manufacturer's Association ("CMA") Intervention Group to this Authority?**

A. Yes I recall submitting testimony last year in conjunction with the Tennessee American Water Company's request to change and increase rates involving water and fire hydrants, TRA Docket No. 03-0018 I do not recall whether I have filed testimony in any other cases before this Authority or its predecessor.

Q. **What is the subject of your testimony?**

A. I will present information opposing Chattanooga Gas Company's filing for a revised natural gas tariff submitted to this Authority where the gas company asks to impose higher costs and additional burdens on ratepayers such as Koch Foods while at the same time moving their services from being handled in Chattanooga to being handled out of Atlanta.

Q. **Have you prepared any exhibits to accompany your testimony?**

A No.

Q. **Does your company have a facility located in Hamilton County, Tennessee that utilizes fuel supplied by Chattanooga Gas?**

A. Yes. Koch Foods has two facilities located in Hamilton County, Tennessee that employ over 275 people at wages significantly higher than minimum wage In addition, Koch Foods has a goal to expand the number of jobs in and around Hamilton County to support this facility Also, we help employ others that contribute to our facility through farming and raising chickens or feed. The production facility in an area of downtown Chattanooga that is currently being revitalized has been in operation by Koch Foods since March, 1996, and the Chattanooga facility has been in existence for over 40 years (as Koch or a predecessor).

Q **Is Chattanooga the only area in which Koch Foods operates?**

A. No; our company has facilities in five states other than Tennessee. The Tennessee operations generate about $300 million per year in economic impact for the state economy.

Q. **Please describe the type of labor that your company uses in its manufacturing and production processes in Chattanooga.**

A. Our company directly provides jobs for lower skill levels requiring a high school education or less, as well as very technical occupations and careers requiring college and post-graduate degrees.

Q **Does Koch Foods intend to expand its facilities in Chattanooga or Hamilton County, Tennessee?**

A. We hope to do so.

Q. **Does the cost of utility services factor into such expansion plans?**

A. Of course, all costs and expenses factor into such plans for any company that seeks to increase capacity and grow jobs in Chattanooga or Hamilton County. It is frustrating and increasingly troubling that we now are seeing rate increases almost annually proposed by the utilities serving our Chattanooga facilities. It requires us to review and justify our attempts to expand with our headquarters and, due to the frequency and volatility of utility tariff adjustments here, it is becoming more difficult to convince others that it is effective and beneficial to contribute capital in Tennessee as opposed to supporting other competing facilities within the company.

Q. **Please describe your company's use of natural gas in its manufacturing and production processes in Chattanooga.**

A. Natural gas is used to produce steam and hot water for manufacturing feed and our slaughtering processes.

Q. Does your company have a secondary fuel to use in the production processes currently fueled by natural gas?

A We have fuel oil at the feed mill. We have no backup for our processing plant on Kerr Street.

Q. **Please explain.**

A. We have space limitations and permit issues with installing a backup system at our processing plant on Kerr Street.

Q. **Is natural gas the cleanest, most efficient burning fuel your company can use?**

A Yes.

Q. Would there be any adverse effects to Koch Foods caused by switching over from natural gas to your backup fuel?

A: Yes, and possibly to the City of Chattanooga as well It could cause us negative publicity and diminished stature in the eyes of city officials or local regulators In November, 2004, the Environmental Protection Agency will make final designations of counties that are in nonattainment of national air quality standards for fine particulate matter. Hamilton County, Tennessee has already been designated as a nonattainment area in preliminary reports by both the State of Tennessee and the Environmental Protection Agency. I have no information that Hamilton County will be removed from the EPA's final listing of non-attainment areas in November. As nonattainment areas will be subject to requirements to reduce pollutants and resultant particles, the State of Tennessee and local air pollution control officials will be required to submit a plan to attain the newly imposed cleaner air standards no later than 2010. EPA has noted that these plans should include stricter controls on industrial facilities. Moreover, nonattainment areas such as

Hamilton County will be subjected to more stringent permitting and enforcement programs. We want to assist local and state efforts to avoid any possible sanctions, including the avoidance of any possible economic growth restrictions, due to the new standards. Of course, the use of fuel oil (our backup) creates much more severe particulate matter problems than natural gas and even if we are permitted to use it we would like to avoid doing so as much as we can.

Q. **Does your company have the ability to bypass Chattanooga Gas Company's gas pipeline?**

A No.

Q. **Describe the impacts on Koch Foods facility or production processes that Chattanooga Gas Company's proposed tariff, penalty and balancing provisions will have if approved by the Tennessee Regulatory Authority.**

A The poultry industry has been operating on slim to non-existent margins for several years. An increase in the natural gas rates will only add to the hardships of operating successfully in the food production industry. Koch Foods is involved in a pure commodity- based industry and does not have the luxury of simply raising its prices in a manner equal to the production cost increases it will experience if utility rates, penalties and balancing provisions are allowed to be changed as requested by Chattanooga Gas.

Q **From your point of view would Chattanooga Gas Company's petition constitute an appropriate natural gas policy for the State of Tennessee?**

A. No, not in all respects I can understand the rising costs of doing business - we fight it daily. However, I cannot understand some of the proposed changes, especially the way they are requested. Chattanooga Gas is a monopoly, but if a nonmonoply provider attempted such an overall rate increase then I would immediately search out a new supplier. Koch Foods is also very concerned with the complexity of billing and associated administrative costs that the proposed tariff will present.

Q. **Has Koch Foods experienced recent billing problems?**

A. Yes, a relief valve malfunctioned back in late 2003, and we brought it to Chattanooga Gas Company's attention. The gas that was lost through Chattanooga Gas Company's equipment was metered and billed to us over several months. We made a proposal to resolve this billing issue, and this issue has yet to be resolved even though we contacted them almost six months ago.

Q. **What other concerns does Koch Foods have?**

A The proposed balancing tariff by Chattanooga Gas Company will require us to monitor our gas usage and nominations much closer to avoid balancing costs. Therefore, we will incur additional administrative costs with managing our gas accounts.

Q. **What is your position regarding the Chattanooga Gas Company's proposal to charge for data collection equipment and communication costs?**

A Koch Foods was required to pay a $2500 contribution last year to add electronic monitoring equipment to our gas meter. We feel this cost should be treated similar to other capital investment and recovered through the Chattanooga's proposed rate tariffs. We also make significant revenue contributions to Chattanooga Gas Company, which should be sufficient to reimburse them the full costs of communication required to monitor our gas consumption.

Q. **Would your Chattanooga facility operate at a competitive disadvantage if the Company's proposed changes are allowed to be implemented?**

A. Yes. Increased rates would immediately put my facility at a disadvantage considering the very tight margins in the poultry industry, and the increases we just suffered at the hands of the foreign-owned Tennessee American Water Company.

Q **Please explain.**

A. Certainly. Koch Foods has invested a significant amount of money in the Chattanooga, Tennessee operation. Of course, we would like to continue to attract additional investment in this production facility, however, to the extent that the margins are lowered or extinguished due to increased costs, then capital investment and jobs will not be assigned or implemented in the Chattanooga facility but could go elsewhere, including any of the five other states in which Koch Foods already operates or to another state.

Q **Is there anything you would propose with respect to the tariffs, pricing, penalty or balancing policy that you would suggest the Authority consider?**

A. Koch Foods is concerned that the proposed changes in balancing will result in a revenue windfall for Chattanooga Gas Company. We are also concerned with the Company's non-regulated affiliate and whether or not the Company's assets are being managed for the benefit of the ratepayers or managed for profit. We would request that the Authority scrutinize this relationship and question the merits of this arrangement.

Q **Does this complete your testimony in this rate increase proceeding?**

A. Yes.