

LAW OFFICES

GULLETT, SANFORD, ROBINSON & MARTIN, PLLC

GARETH S. ADEN
G. RHEA BUCY
CHRISTOPHER W. CARDWELL
GEORGE V. CRAWFORD, JR.
GEORGE V. CRAWFORD III
A. SCOTT DERRICK
THOMAS H. FORRESTER
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MARY BETH HAGAN
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M. TAYLOR HARRIS, JR.
DAN HASKELL
ANDRA J. HEDRICK
LINDA W. KNIGHT
JOEL M. LEEMAN
ALLEN D. LENTZ
MOLLIE E. MAHAN

STREET ADDRESS:
315 DEADERICK STREET, SUITE 1100
NASHVILLE, TENNESSEE 37238

MAILING ADDRESS:
POST OFFICE BOX 198888
NASHVILLE, TENNESSEE 37219-8888

TELEPHONE (615) 244-4994

FACSIMILE (615) 256-6339

WWW.GSRM.NET

JOSEPH MARTIN, JR.
MARISSA A. MOSES
WM. ROBERT POPE, JR.
JACK W. ROBINSON, JR.
JACK W. ROBINSON, SR.
WESLEY D. TURNER
PHILLIP P. WELTY
MARK H. WESTLAKE

OF COUNSEL

TREVOR W. HOWELL
JOHN D. LENTZ
SULLIVAN F. MARSDEN

B. B. GULLETT
1905-1992
VALERIUS SANFORD
1923-2001

December 29, 2006

Hon. Sara Kyle, Chairman
c/o Sharla Dillon, Docket Manager
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243-0505

RE: Application of Community Initiative for a Certificate of Public Convenience and Necessity to Provide Natural Gas Services in Certain Areas of Macon County, Tennessee (including within the City of Red Boiling Springs); to Approve the Transfer of Certain Assets and Customers of RBS Gas Utility, Inc.; to Approve Franchise from The City of Red Boiling Springs; to Confirm Cancellation of Special Contract of RBS Utility, Inc.; and to Set Rates and Approve Tariff

Docket No.: 06-00281

Dear Chairman Kyle:

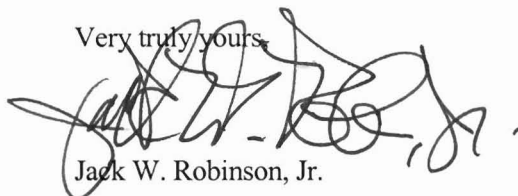
Enclosed for filing is the Pre-Filed Testimony of William H. (Hal) Novak.

Community Initiative published Notice of the upcoming TRA hearing just as soon as it learned that the hearing would take place on January 8. Thus, enclosed for filing is a copy of the Notice, as published in the *Tennessean*. The *Tennessean's* circulation covers Macon County (including Red Boiling Springs), and CI published in it in order to get the Notice out promptly, since the local Macon County newspapers only publish weekly. Further, enclosed for filing is a copy of the Notice, as published in the *Macon County Chronicle*.

As you will note, there is an original and fourteen copies of each of these enclosures. Please stamp one copy of all of the documents "filed" and return it to me for my files.

Should you have any questions with respect to this filing, please do not hesitate to contact me.

Very truly yours,



Jack W. Robinson, Jr.

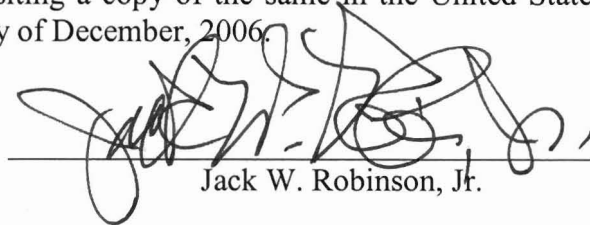
Enclosures

December 29, 2006

Page 2

CERTIFICATE OF SERVICE

I hereby certify that I have served a copy of the foregoing document, together with the enclosures, upon the City of Red Boiling Springs, Tennessee, c/o Jon A. Wells, Esq., city attorney, 206 Court Square, P. O. Box 116, Lafayette, Tennessee 37083-0116; Macon County, Tennessee, c/o County Mayor Shelvy Linville, Room 201 Macon County Courthouse, Lafayette, Tennessee 37083; the City of Lafayette, Tennessee, c/o Jon A. Wells, Esq., city attorney, 206 Court Square, P. O. Box 116, Lafayette, Tennessee 37083-0116; the Consumer Advocate Division, Tennessee Attorney General's Office, Attn.: Timothy Phillips, Esq., Senior Counsel, 425 Fifth Avenue North, Nashville, Tennessee 37243-0491; J. Graham Matherne, Esq., attorney for Receiver of RBS Gas Utility, Inc., Wyatt, Tarrant & Combs LLP, Suite 1500, 2525 West End Avenue, Nashville, Tennessee 37203-1423; John A. Gupton III, Esq., attorney for Nestle Waters North America, Baker, Donelson, Bearman, Caldwell & Berkowitz, P.C., 211 Commerce Suite, Suite 1000, Nashville, TN 37201, by depositing a copy of the same in the United States mail, first class mail, postage prepaid, this 29th day of December, 2006.



Jack W. Robinson, Jr.

BEFORE THE TENNESSEE REGULATORY AUTHORITY

Nashville, Tennessee

2006 DEC 29 AM 10:03
T.R.A. DOCKET NO. 06-00281

IN RE: APPLICATION OF COMMUNITY INITIATIVE FOR A CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY TO PROVIDE NATURAL GAS SERVICES IN CERTAIN AREAS OF MACON COUNTY, TENNESSEE (INCLUDING WITHIN THE CITY OF RED BOILING SPRINGS); TO APPROVE THE TRANSFER OF CERTAIN ASSETS AND CUSTOMERS OF RBS GAS UTILITY, INC.; TO APPROVE FRANCHISE FROM THE CITY OF RED BOILING SPRINGS; TO CONFIRM CANCELLATION OF SPECIAL CONTRACT OF RBS UTILITY, INC.; AND TO SET RATES AND APPROVE TARIFF

Docket No.: 06-00281

PRE-FILED TESTIMONY OF WILLIAM H. NOVAK

1 **Q. Would you state your name, business address and occupation for the record,**
2 **please?**

3 A. My name is William H. Novak. My business address is 19 Morning Arbor Place,
4 The Woodlands, TX, 77381. I am the owner of WHN Consulting, a utility
5 consulting and expert witness services company. I was engaged by AUI to assist
6 it and Community Initiative (“CI” or “the Company”) with this filing.

7 **Q. Please provide a summary of your background and professional experience.**

8 A. I have both a Bachelors degree in Business Administration with a major in
9 Accounting, and a Masters degree in Business Administration from Middle
10 Tennessee State University. I am also licensed to practice as a Certified Public
11 Accountant in Tennessee.

12 My work experience has centered around regulated utilities for over 24 years.
13 Before establishing WHN Consulting, I was Chief of the Energy & Water
14 Division of the Tennessee Regulatory Authority where I had either presented
15 testimony or advised the Authority on a host of regulatory issues for over 19
16 years. In addition, I was previously the Director of Rates & Regulatory Analysis
17 for two years with Atlanta Gas Light Company, a natural gas distribution utility
18 with operations in Georgia and Tennessee. I also served for two years as the Vice
19 President of Regulatory Compliance for Sequent Energy Management, a natural
20 gas trading and optimization company in Texas.

21 **Q. What is the purpose of your testimony in this proceeding?**

22 A. The purpose of my testimony is to present to the TRA the underlying support for
23 the rates and charges proposed by CI in its application to the TRA for a Certificate
24 of Public Convenience and Necessity.

25 **Q. What is the basis for the proposed rates that were included in the Company’s**
26 **filing?**

1 A. Because the historical books and records from the previous owner of RBS Gas
2 Utility could not be relied upon, the Company was forced to prepare a long-term
3 financial forecast for each of the next five (5) years as shown on Company Exhibit
4 WHN-1, Schedule 1.

5 **Q. Please explain how the Company's revenue forecast was prepared.**

6 A. We began with a forecast of base rate revenues for 2007 as shown on Company
7 Exhibit WHN-1, Schedule 2. To calculate the pro forma 2007 revenues, we used
8 the expected sales volumes and customer counts and then applied them to both the
9 current and proposed rate structures. The Company's proposed rate structure will
10 produce an increase in revenues of approximately \$144,000 from the base rates
11 currently being charged by the Receiver. Most of this revenue increase
12 (approximately \$110,000) will come from the Industrial customer class which
13 includes only one (1) customer that was previously being served under a special
14 contract that has recently expired.

15 To calculate revenues for the remainder of the five-year budget as shown on
16 Company Exhibit WHN-1, Schedule 1, we increased the pro forma 2007
17 Residential and Commercial revenues under the proposed rates by ten percent
18 each year for the remainder of the five-year budget in order to match the
19 Company's expected new investment in utility plant. Industrial revenues were left
20 unchanged at the 2007 pro forma amounts for the remainder of the five-year
21 budget.

22 **Q. How were the Company's pro forma operating expenses shown on Company**
23 **Exhibit, Schedule 1 were forecasted?**

24 A. We began with a forecast of salary and wages. We expect the 2007 salary and
25 wage expense to be approximately \$192,000. Because the expected time and
26 attention necessary to initially set the policy and procedures of running the day-to-
27 day operations should decrease after the first year, we have reduced the annual

1 forecast for salary and wages by \$70,000 for each of the remaining years of the
2 five-year forecast.

3 To calculate depreciation expense, we applied a 10% depreciation rate to the
4 average balance of plant in service for each year of the five-year forecast. A 10%
5 depreciation rate was used because the Company determined that the expected
6 remaining life of the existing plant in service was approximately 10 years.

7 The Company forecasted \$21,120, \$3,116, \$25,000 and \$2,715 respectively for
8 the annual Office Expense, Repair & Maintenance Expense, Insurance Expense
9 and Licenses & Permits Expense. These forecasts were based on the anticipated
10 costs of these services, and the same amounts were used for each year of the five-
11 year forecast.

12 For Professional Services, the Company included \$50,000 as the first year cost of
13 preparing, filing and defending this case before the TRA. This cost was reduced
14 to \$15,000 for the remaining periods of the five-year budget.

15 After considering each of the adjustments mentioned above, the total operating
16 expenses were forecast and ranged from a low of approximately \$231,000 in 2008
17 to a high of approximately \$361,000 in 2011. In addition, the net revenue and
18 expense forecasts produce an annual net operating income ranging from a loss of
19 approximately \$-21,000 in 2007 to a high of approximately \$83,000 in 2008.

20 **Q. Please explain the Company's rate base forecast as shown on Company**
21 **Exhibit WHN-1, Schedule 1.**

22 A. We began with the purchase price of \$250,000 that the Company will pay the
23 Receiver for the assets of RBS Gas Utility in 2007. We then added \$1.7 million
24 to this amount over the remaining four years of the five-year budget that the
25 Company expects to invest for inspection, mapping and system expansion.

26 We next calculated accumulated depreciation by totaling up the depreciation
27 expense for all years and taking the average of the beginning and ending balances.

1 Finally, we calculated an amount for working capital by taking one eighth (1/8) to
2 the total operating expenses.

3 After considering each of the adjustments mentioned above, the total rate base
4 forecast was calculated and ranged from a low of approximately \$278,000 in 2007
5 to a high of approximately \$1,558,000 in 2011.

6 **Q. What rate of return has the Company forecast on this projected rate base?**

7 A. As shown at the bottom of Company Exhibit WHN-1, Schedule 1 the Company's
8 projected overall rate of return forecast under proposed rates would be as follows:

2007	-7.67%
2008	14.38%
2009	6.52%
2010	2.96%
2011	1.02%
Average	3.82%

9 As can be seen, for 2007 the Company expects to incur a loss primarily due to the
10 one-time incremental costs of transitioning the utility from the Receiver.
11 Thereafter, the Company expects to operate at a positive rate of return. The
12 average expected rate of return for the entire five-year budget is 3.82%.

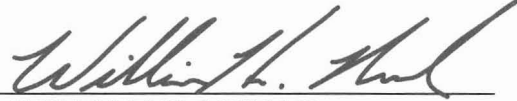
13 **Q. Does this conclude your testimony?**

14 A. Yes, it does.

STATE OF TEXAS)

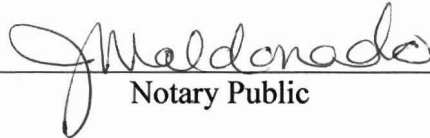
COUNTY OF MONTGOMERY)

I swear that the foregoing testimony is true and correct to the best of my knowledge.



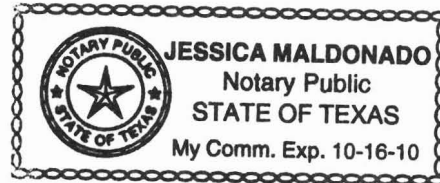
WILLIAM H. NOVAK

Sworn to and subscribed before me this 28th day of December, 2006.



Notary Public

My Commission Expires: 10-16-10



Community Initiative
Income, Investment and Rate of Return Analysis of Red Boiling Springs Gas Company Acquisition

Exhibit WHN-1
Schedule 1

	2007	2008	2009	2010	2011	Average
Base Revenues:						
Residential	\$142,200 A/	\$156,420 H/	\$172,062 H/	\$189,268 H/	\$208,195 H/	\$173,629
Commercial	31,680 A/	34,848 H/	38,333 H/	42,166 H/	46,383 H/	38,682
Industrial/Special Contract	122,400 A/	122,400 A/	122,400 A/	122,400 A/	122,400 A/	122,400
Total Base Revenue	\$296,280	\$313,668	\$332,795	\$353,834	\$376,978	\$334,711
Operating Expenses:						
Salaries & Wages	\$191,615 B/	\$121,615 I/	\$121,615 I/	\$121,615 I/	\$121,615 I/	\$135,615
Depreciation Expense	24,000 C/	42,500 J/	82,500 J/	127,500 J/	172,500 J/	89,800
Office Expense	21,120 D/	21,120 D/	21,120 D/	21,120 D/	21,120 D/	21,120
Repair & Maintenance	3,116 D/	3,116 D/	3,116 D/	3,116 D/	3,116 D/	3,116
Professional Services	50,000 D/	15,000 D/	15,000 D/	15,000 D/	15,000 D/	22,000
Insurance Expense	25,000 D/	25,000 D/	25,000 D/	25,000 D/	25,000 D/	25,000
Licenses & Permits Expense	2,715 D/	2,715 D/	2,715 D/	2,715 D/	2,715 D/	2,715
Total Operating Expenses	\$317,566	\$231,066	\$271,066	\$316,066	\$361,066	\$299,366
Net Operating Income	-\$21,286	\$82,602	\$61,729	\$37,768	\$15,912	\$35,345
Rate Base (Average):						
Plant in Service	\$250,000 E/	\$600,000 K/	\$1,050,000 M/	\$1,500,000 M/	\$1,950,000 M/	\$1,070,000
Accumulated Depreciation	-12,000 F/	-54,500 L/	-137,000 L/	-264,500 L/	-437,000 L/	-181,000
Working Capital	39,696 G/	28,883 G/	33,883 G/	39,508 G/	45,133 G/	37,421
Rate Base	\$277,696	\$574,383	\$946,883	\$1,275,008	\$1,558,133	\$926,421
Rate of Return	-7.67%	14.38%	6.52%	2.96%	1.02%	3.82%

A/ See Sheet 2.

B/ First year expense of \$43,535 for Field Labor; \$28,080 for Clerical Labor; and \$120,000 for Management Labor.

C/ Average Plant in Service * 10%.

D/ Management assumptions based on anticipated costs.

E/ Initial Investment for purchase.

F/ One half (1/2) of Depreciation Expense.

G/ One eighth (1/8) of Total Operating Expenses.

H/ Ten percent (10%) increase over previous year due to plant expansion.

I/ Post first year expense of \$43,535 for Field Labor; \$28,080 for Clerical Labor; and \$50,000 for Management Labor.

J/ Average of current and previous year plant in service @ 10%.

K/ Previous Year Plant in Service + \$100,000 for inspection/mapping and \$250,000 for system expansion.

L/ Previous Year Balance of Accumulated Depreciation + Current Year Depreciation Expense.

M/ Previous Year Plant in Service + \$450,000 for system expansion and reserve.

Community Initiative
Revenue Analysis of Red Boiling Springs Gas Company Acquisition

Exhibit WHN-1
Schedule 2

	<u>Mcf/Dkt Determinant</u> A/	<u>Existing RBS Rate</u> D/	<u>Proposed AUI Rate</u> E/	<u>Existing RBS Revenues</u>	<u>Proposed AUI Revenues</u>	<u>Difference</u>
Residential:						
Mcf Volumes	24,000 B/	\$4.29	\$5.00	\$102,960	\$120,000	\$17,040
Customers (Bills):						
Winter	1,110 C/	5.00	12.00	5,550	13,320	7,770
Summer	1,110	5.00	8.00	5,550	8,880	3,330
Total Residential				\$114,060	\$142,200	\$28,140
Commercial:						
Mcf Volumes	6,000 B/	\$4.29	\$5.00	\$25,740	\$30,000	\$4,260
Customers (Bills):						
Winter	24 C/	5.00	35.00	120	840	720
Summer	24	5.00	35.00	120	840	720
Total Commercial				\$25,980	\$31,680	\$5,700
Industrial & Special Contract:						
Mcf Volumes	24,000 B/	\$0.50	\$5.00	\$12,000	\$120,000	\$108,000
Customers (Bills):						
Winter	6 C/	0.00	200.00	0	1,200	1,200
Summer	6	0.00	200.00	0	1,200	1,200
Total Industrial & Special Contract				\$12,000	\$122,400	\$110,400
Total Base Rate Margin				\$152,040	\$296,280	\$144,240

A/ For simplicity, we assume in this analysis that 1 Mcf = 1 Dkt.

B/ Customer charges assumes 185 residential, 4 commercial and 1 industrial customer.

C/ Mcf Volumes of 24,000 each customer class closely approximates current usage.

D/ RBS Tariff Sheets less \$3.21/Mcf of gas cost in base rates.

E/ Proposed tariff sheets included in Company's Petition.