

TENNESSEE PUBLIC UTILITY COMMISSION



502 Deaderick Street, 4th Floor
Nashville, TN 37243-0001

NOTICE OF DOCKET FILING OF RESPONSES TO REQUEST FOR INFORMATION

**IN RE: DOCKET TO EVALUATE CHATTANOOGA GAS
COMPANY'S PURCHASES AND RELATED SHARING
INCENTIVES**

DOCKET NO.: 20-00139

DATE: November 5, 2021

Attached for filing in the above-referenced docket are the responses and affidavit of Mr. Jerome Mierzwa of Exeter Associates, Inc. to Chattanooga Gas Company's Information Requests, which were issued on October 19, 2021.

FOR THE TENNESSEE PUBLIC UTILITY COMMISSION:

Monica Smith-Ashford

Monica Smith-Ashford, Hearing Officer

C: Via email
Floyd Self
J.W. Luna
Rachel Bowen
Karen Stachowski
Vance Broemel

Docket file

AFFIDAVIT

STATE OF MD)

COUNTY OF Howard)

I hereby certify that on this 4 day of November, 2021, before me, an officer duly authorized in the State and County aforesaid to take acknowledgments, personally appeared Jerome D Mierzwa, who is personally known to me or who produced as identification a valid driver's license or other government issued identification, and he/she acknowledged before me that he/she provided the answers to Tennessee Public Utility Commission data request number(s) 1-8 to be used in Docket No. 20-00139, and that the responses are true and correct based on his/her personal knowledge.

In Witness Whereof, I have hereunto set my hand and seal in the State and County aforesaid as of this 4 day of November, 2021.

Deborah M Adams

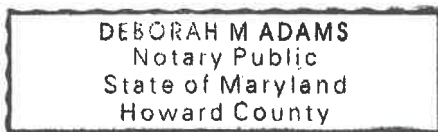
Notary Public

State of MD, at Large

My Commission Expires:

2/2023

[SEAL/STAMP]



STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

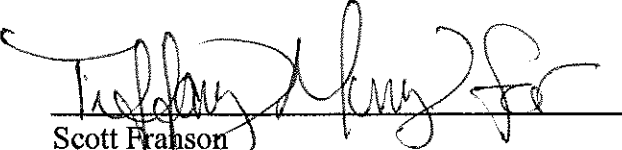
VERIFIED JOINT PETITION OF INDIANA GAS)
COMPANY, INC., SOUTHERN INDIANA GAS AND)
ELECTRIC COMPANY AND THE BOARD OF)
DIRECTORS FOR UTILITIES OF THE DEPARTMENT OF)
PUBLIC UTILITIES OF THE CITY OF INDIANAPOLIS,)
AS SUCCESSOR TRUSTEE OF A PUBLIC CHARITABLE)
TRUST, D/B/A CITIZENS GAS, PURSUANT TO IND.)
CODE 8-1-2.5 ET SEQ. FOR APPROVAL OF AN)
ALTERNATIVE REGULATORY PLAN ESTABLISHING)
FLEXIBLE TERMS, RATES AND CHARGES FOR)
CERTAIN RETAIL ENERGY SERVICES, INCLUDING)
CONTINUED USE OF A GAS COST INCENTIVE)
MECHANISM AND APPROVAL OF NEW SUPPLY)
AGREEMENTS WITH PROLIANCE ENERGY, LLC)

CAUSE NO. 43963

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR'S
SUBMISSION OF ANNUAL REPORT

Pursuant to paragraph five (page 8) of the Commission's Order in this Cause, dated March 17, 2011, the OUCC submits the attached report concerning the audit and consultant work conducted by the OUCC and its consultant, Exeter Associates.

Respectfully Submitted,



Scott Franson
Attorney No. 27839-49
Deputy Consumer Counselor

INDIANA UTILITY REGULATORY COMMISSION
Cause No. 43963

**Report on the Auditing and Consulting Review and Costs
of the 2011 Settlement for the Period April 2015 – March 2016**

1.0 Introduction

On March 17, 2011, the Indiana Utility Regulatory Commission (“IURC”) approved a settlement agreement between Indiana Gas Company, Inc. d/b/a Vectren Energy Delivery of Indiana, Inc. (“Vectren North”); Southern Indiana Gas & Electric Company d/b/a Vectren Energy Delivery Indiana, Inc. (“Vectren South”); Citizens Gas; the Indiana Office of Utility Consumer Counselor (“OUCC”); the I.G.C.G. Industrial Group (“Industrial Group”); the Citizens Action Coalition (“CAC”); and ProLiance Energy, LLC (“ProLiance”) (“2011 Settlement Agreement”). Under the 2011 Settlement Agreement, Vectren North, Vectren South, and Citizens Gas (collectively, “Utilities”) each entered into a Gas Sales and Portfolio Administration Agreement (“GSPA Agreement”) with ProLiance that established terms, rates, and conditions for delivered supply services that ProLiance would provide through March 31, 2016. The 2011 Settlement Agreement also provided for the continued use of a Gas Cost Incentive Mechanism (“GCIM”). The 2011 Settlement Agreement was built on prior settlement agreements, including a settlement agreement in 2006 in Cause No. 42973. The 2011 Settlement Agreement was executed by the parties to ensure that a proper allocation of benefits and a continual review of information are facilitated, as well as to ensure that certain concepts are addressed. These concepts included: (1) transparency of information; (2) sharing of synergies; (3) capacity release access; (4) supply planning protocol; and (5) affiliate guideline clarity, compliance, and non-discrimination.

On June 19, 2013, ETC ProLiance Energy, LLC was formed when ETC Marketing, Ltd. acquired the natural gas marketing assets of ProLiance. As part of the acquisition, ETC ProLiance Energy assumed ProLiance’s natural gas marketing contractual obligations, including the Utilities’ GSPA Agreements. On March 31, 2014, Exelon Generation Company, LLC (“Exelon”) acquired

ETC ProLiance Energy, LLC, and ETC ProLiance Energy's name was changed to Constellation ProLiance, LLC. Effective August 28, 2014, Constellation ProLiance, LLC assigned all its rights, title, and interest in, to, and under the GSPA Agreements to Exelon.

Article IX of the 2011 Settlement Agreement provides that three times per year, the books, records, and data reasonably related to the provisions of the 2011 Settlement Agreement may be formally reviewed by the OUCC. In the event the OUCC employs an outside auditor or consultant to assist in this review process, the Utilities will pay up to \$125,000 each year, which may be used to offset the OUCC's reasonable costs specifically incurred for the review. The Order approving the 2011 Settlement Agreement also provided that an annual update would be submitted to the IURC concerning the audit and consultant work conducted by the OUCC and its auditor and outside consultants (Order at 8). This Report summarizes the auditing work of the OUCC and its outside consultant, Exeter Associates, Inc. ("Exeter"), for the fifth and final year (April 2015 – March 2016) ("review period") of the Utilities' GSPA agreements with Exelon under the 2011 Settlement Agreement.

The 2011 Settlement Agreement provides that once each year during the term of the 2011 Settlement Agreement, the IURC, the OUCC, and all outside auditors or consultants employed by the OUCC will meet to provide the IURC with an update on the work conducted by the OUCC and its auditors and consultants (Order at 5-6). The OUCC will schedule this meeting at the IURC's direction. Identified in Table 1 is the value of the services each Utility purchased from Exelon during the fifth year of the 2011 Settlement Agreement. Table 2 identifies the quantity of gas purchased by each Utility from Exelon and the average cost of those purchases during the fifth year of the 2011 Settlement Agreement.

Table 1. Exelon Utility Charges (April 2015 – March 2016)	
Utility	Total Charges
Vectren North	\$167,443,214
Vectren South	24,533,477
Citizens Gas	82,710,291
Total	\$274,686,982

Table 2. Summary of Gas Supply Commodity Purchases and Unit Costs (April 2015 – March 2016) (MDth)			
Utility	Purchases	Unit Cost	Total Cost
Vectren North	45,618	\$2.41	\$110,013,759
Vectren South	7,501	\$2.58	\$19,361,698
Citizens Gas	22,063	\$2.46	\$54,206,784

2.0 Overview of Auditing Procedures

The 2011 Settlement Agreement provides that three times per year, the books, records, and data reasonably related to the provisions of the 2011 Settlement Agreement may be formally reviewed by the OUCC. This is accomplished by obtaining the following monthly information from the Utilities and Exelon:

- Monthly invoices from Exelon to each of the Utilities;
- Each Utility's monthly gas supply plan;
- Schedules detailing the results of the Value Sharing and Entitlement Auction provisions of the 2011 Settlement Agreement;
- Schedules detailing the results of the GCIM; and
- Monthly invoices from each of the interstate pipelines Exelon uses to serve the Utilities.

The review related to each of the above is subsequently discussed in the following section of this Report. Exeter's initial review of the information identified above occasionally leads to the

submission of additional data requests to the Utilities. Exeter also briefly reviews the quarterly GCA filings of each Utility to determine whether those filings contain information that may be relevant to Exeter's ongoing review process (e.g., changes in pipeline capacity arrangements). The OUCC has found that the above process has generally provided for an adequate review of Exelon's and the Utilities' operations under the 2011 Settlement Agreement.

The 2011 Settlement Agreement provides for the establishment of an Annual Demand Cost Cap following a review process conducted by the OUCC, the Utilities, and Exelon (Article 3.4.2 of the 2011 Settlement Agreement). This review process also provides for the exchange of data and is discussed later in this Report.

3.0 Detail of Auditing Procedures

3.1 Monthly Invoices from ProLiance

Each Utility purchases a number of gas supply delivery services from Exelon. The terms and conditions of service, maximum contract quantities, and applicable pipeline variable and gas supply charges for these delivered services are reflected in the Appendices to each Utility's GSPA Agreement with Exelon. Under the 2011 Settlement Agreement, the initial set of Appendices for each Utility was to be filed with the Commission after the 2011 Settlement Agreement was approved. The 2011 Settlement Agreement provided for the initial set of Appendices to be provided to the OUCC and the Industrial Group at least 15 days prior to filing with the Commission to determine if either party had any objections to the Appendices. Absent an objection by either party, the Appendices became effective upon filing. The same filing procedures are applicable for any proposed revisions to the Appendices.

Under the Utilities' GSPA Agreements with Exelon, specific interstate pipeline transportation and/or storage services are designated as supporting each gas supply delivery service. Each Utility nominates the amount of each delivery service to be used by Exelon to serve that Utility on a daily basis. Exelon may use the interstate pipeline services designated as

supporting a delivered service or any other interstate pipeline service that may be available to satisfy a Utility's nomination. Utility delivery service nominations are referred to as "virtual dispatch" and differ from "physical dispatch" which represents the actual use of interstate pipeline services by Exelon to serve the Utility. The Utilities are billed by Exelon based upon virtual dispatch.

The initial step in Exeter's auditing process is to enter the monthly purchase quantities, prices, and costs for each delivered service for each Utility into an Excel spreadsheet model ("Purchase Model"). This assists in several key auditing functions, the primary of which requires additional background information and is discussed later in this Report in Sections 3.3 and 4.0. It also ensures that pipeline variable and gas supply charges are correctly applied and determined. During the first review year under the 2011 Settlement Agreement, Panhandle storage variable charges were incorrectly applied under a delivery service purchased by Vectren South, resulting in a small Utility overcharge of approximately \$5,000. Upon notice by Exeter, this overcharge was subsequently corrected. Exeter's review for year three also discovered a double collection of overrun charges by Exelon from Vectren North in March 2014. The amount of the double collection was not material, and Vectren North adjusted its September 2014 payment to Exelon to refund the overcollection.

3.2 Monthly Gas Supply Plans

Each monthly gas supply plan prepared by the Utilities is reviewed and evaluated for reasonableness. Projected purchases under each delivered service are input into the Purchase Model and significant discrepancies between actual and projected purchases are investigated. Differences between the maximum monthly contract quantities available under a delivered service and the planned monthly level of purchases serve as the basis for determining the monthly quantities available under the Value Sharing and the Entitlement Auction provisions of the 2011 Settlement Agreement, which are discussed in the following section.

3.3 Value Sharing and Entitlement Auction

In order to obtain revenues to offset gas sales customers' costs, while also providing non-discriminatory access to available pipeline transportation capacity, the 2011 Settlement Agreement requires the Utilities to identify on a monthly basis the planned level of unutilized transportation entitlements under each delivered service (i.e., maximum available capacity entitlements less planned use of capacity entitlements). After the anticipated unused transportation entitlements are identified, they are split in half. One half is retained by Exelon in exchange for Exelon providing an annual credit to the Utilities of \$3.5 million (referred to as "Value Sharing"). The other half is posted as capacity available for release through certain procedures outlined in the 2011 Settlement Agreement ("Entitlement Auction"). The goals of the capacity release process are to: (1) promote competition; (2) provide nondiscriminatory open access; (3) generate the highest economic value consistent with reliable supply; and (4) provide process transparency.

The level of unused entitlements is reviewed by Exeter to ensure they are reasonable and that Exelon's share is properly determined. For example, under the 2011 Settlement Agreement, Exelon is entitled to use all capacity that is not released in addition to the Value Sharing capacity. If the level of unused capacity is improperly understated, the amount of capacity that is released through the Entitlement Auction will be lower, and the amount of capacity available to Exelon will be greater than is appropriate under the 2011 Settlement Agreement.

Exelon's administration of the Value Sharing/Entitlement Auction process is detailed in the monthly capacity auction information. This monthly data is reviewed to ensure compliance with the 2011 Settlement Agreement which requires that capacity that is recalled is recalled equally from the Value Sharing and Entitlement Auction components.

3.4 Gas Cost Incentive Mechanism

The 2011 Settlement Agreement provided for a Gas Cost Incentive Mechanism that provides risks and rewards for gas supply acquisition performance compared to a market standard.

As stated in the 2011 Settlement Agreement, the goals of the GCIM are to: (1) reduce customer gas costs; (2) fairly measure costs of supply against market; (3) employ a measurement that recognizes the Utilities' specific portfolio characteristics; and (4) reward performance that beats the market and penalize performance that does not beat the market. The GCIM does not apply to fixed-price purchases made pursuant to the Utilities' Price Volatility Mitigation Program.

Under the GCIM, the actual cost of each gas purchase made by each Utility from Exelon is compared to a Benchmark that reflects the cost of the purchase had it been made at a market price for the location, type of purchase, and time at which the purchase was made. Index prices reported in gas industry publications serve as market prices under the GCIM. On a monthly basis, each Utility's actual gas costs are compared to the Benchmark. If a Utility's actual gas costs are less than the Benchmark, a positive differential exists. If a Utility's actual gas costs exceed the Benchmark, a negative differential exists. Positive and negative differentials are shared between the Utility (or Exelon, as determined by the Utility) and its customers as follows:

Negative Differential (Actual Cost>Benchmark Price)		
% of Price Above Benchmark Price	% of Sharing Customer	% of Sharing Utility
>4%	30	70
>2% to 4%	50	50
0% to 2%	70	30
Positive Differential (Actual Cost<Benchmark Price)		
% of Price Above Benchmark Price	% of Sharing Customer	% of Sharing Utility
0% to 2%	70	30
>2% to 4%	50	50
>4%	30	70

Exeter's review of the Utilities' GCIMs found that the GCIMs were administered consistent with the requirements of the 2011 Settlement Agreement during the fifth year of the 2011 Settlement Agreement. Table 3 identifies the Utilities' and customers' share of savings

realized under the GCIM during the fifth year of the 2011 Settlement Agreement. As shown, Vectren North and Vectren South realized no savings under the GCIM during the period.

Table 3. Utility and Customer GCIM Savings (April 2015 – March 2016)			
Utility	Utility	Customer	Total
Vectren North	\$0	\$0	\$0
Vectren South	\$0	\$0	\$0
Citizens Gas	\$16,253	\$37,918	\$54,171
Total	\$16,253	\$37,918	\$54,171

Exeter's previous report for the period April 2012 – March 2014 indicated that certain ANR Pipeline delivered gas supply purchases made by Vectren North during the period January – March 2014 were improperly excluded from the GCIM. The exclusion of these purchases was raised as an issue by the OUCC in Cause No. 37394-GCA-123. In that proceeding, the OUCC and Vectren North agreed to defer litigation of the GCIM issue to Cause No. 37394-GCA-124, and a subdocket was subsequently established in Cause No. 37394-GCA-124 S1 to address the GCIM issue. In March 2015, an agreement in principal was reached by the OUCC, Vectren North, and Exelon to settle the subdocket, and a settlement was filed with the Commission on April 1, 2015. The settlement provided for a net credit of \$1,601,132 to Vectren North's GCA customers. The settlement was approved by the Commission in an order issued June 10, 2015.

3.5 Monthly Interstate Pipeline Invoices

Interstate pipeline services are used by Exelon to provide delivered gas supply services to the Utilities and Exelon's other customers. Exelon's other customers include gas utilities other than Vectren North, Vectren South, and Citizens, and the transportation customers of these Utilities. As previously explained in Section 3.1 (Monthly Invoices from Exelon) and subsequently discussed in greater detail in Section 4.0 (Annual Demand Cost Cap) of this Report, certain interstate pipeline services are designated as being used to serve the Utilities; however, in actuality the designated services may or may not be used to serve the Utilities, and pipeline services

that are not designated as serving the Utilities may be used to serve the Utilities. On a monthly basis, the invoices from the interstate pipelines Exelon utilizes to serve the Utilities are reviewed. The review is used to validate the variable commodity and fuel charges assessed to the Utilities by Exelon, and to validate the services that have been designated as serving the Utilities in the Annual Demand Cost Cap analysis. The interstate pipeline invoices are also reviewed to confirm that each Utility is purchasing gas in accordance with least-cost procurement principles. For example, gas supplies delivered to the Utilities from different pipelines have different delivered costs. Each Utility should be maximizing deliveries from the pipeline with the lowest delivered cost and minimizing deliveries from the highest delivered cost pipelines, within physical operating constraints. If the actual quantity of gas delivered to a Utility from the lowest-cost pipeline (per the pipeline invoice) exceeded the quantity purchased and billed by the Utility from Exelon, there would be concern that the Utility was not adhering to the least-cost gas procurement principles.

Another area of focused review with respect to the pipeline invoices is the actual storage inventory balances under the interstate pipeline storage services designated as serving the Utilities. For each of the Appendices storage services purchased by a Utility, there is an interstate pipeline storage service with identical maximum daily seasonal contract quantities that is designated as providing the storage service. This enables, but does not require, Exelon to match physical dispatch with a Utility's virtual dispatch nominations. Exelon is not required to match physical and virtual dispatch activity under the designated supporting pipeline storage service. Therefore, the actual storage inventory balance under the supporting pipeline service, which is based on physical dispatch, may potentially differ from the Utility's storage inventory balance, which is based on virtual dispatch. An area of focused review in Exeter's monitoring of activity under the Utilities' arrangements with Exelon is the difference between actual and Utility storage inventory balances. A significant difference in inventory balances would suggest that Exelon is pursuing an advantageous strategy that is not being pursued by the Utility. In such instances, Exeter would investigate the difference and attempt to determine whether a similar strategy should or could have

been pursued by the Utility. No significant differences in inventory balances were observed during the period addressed in this Report.

3.6 Capacity Release Process

As indicated in Section 3.3 of this Report, the 2011 Settlement Agreement provides for the release of 50 percent of each Utility's anticipated monthly unused transportation entitlements through an Entitlement Auction. Each month, each Utility identifies its anticipated unused entitlements, by pipeline, available for the Entitlement Auction and this information is emailed to a list of potential bidders, along with bidding timelines. Upon conclusion of the bidding process, an email is sent to the list of potential bidders, identifying the winning bidders and prices. Exeter is a recipient of the emails identifying the unused monthly entitlements and winning bidders. Our monitoring of the Entitlement Auction process revealed no concerns. It should be noted that Exelon itself is frequently a participant in the Entitlement Auction, and is generally the winning bidder no more frequently than other bidders. Capacity release revenues by Utility for the review period for this Report are summarized in Table 4.

Table 4. Capacity Release Revenues (April 2015 – March 2016)	
Utility	Revenues
Vectren North	\$698,331
Vectren South	\$20,225
Citizens Gas	\$171,993

3.7 Storage Arrangements

The Utilities have agreed to specified storage refill arrangements under the GSPA Agreements. Under these arrangements, the total quantity of gas to be injected into storage for each Utility's storage service is determined at the beginning of the storage injection season. The Utility then pays for the gas injected into storage as if an equal quantity (1/7th) had been injected during each of the summer months (April through October). This is standard practice under an

asset management agreement (“AMA”) such as the GSPA Agreements. However, storage is not *actually* filled equally each month. This mismatch between the payment for storage gas by the Utilities and actual injection of storage gas has the potential to adversely affect GCA customers if actual storage injection quantities are greater during the summer months with the lowest costs. For example, less than the 1/7th equal monthly quantity could be injected during a relatively high-cost month, and then the Utilities would be charged as if the 1/7th monthly quantity was injected. The shortfall between the 1/7th monthly quantity and the actual injection quantity would then be injected during a lower-cost month. Exeter’s review and analysis indicates that for the summer of 2015, storage refill arrangements had a negligible impact on the Utilities’ gas costs.

During the winter of 2015-2016, Vectren North failed to reduce its storage inventory balance on Panhandle Eastern Pipeline (Panhandle) to the required maximum quantity and was penalized. Panhandle was entitled to retain 3,394 Dth of Vectren North’s storage inventory. Vectren North claims that during the winter of 2015-2016 it was able to purchase lower-cost supplies and displace higher-cost storage supplies, and that this contributed to the assessment of the storage inventory penalty. Citizens was also assessed a storage penalty by Panhandle of 5,355 Dth. Citizens did not present any justification for the penalty, but indicated that significantly warmer-than-normal temperatures were experienced during the winter of 2015-2016, which caused it at times to sell gas it had nominated back to Exelon at *Gas Daily* index prices. The reasonableness of Vectren North’s and Citizens’ claims and the appropriateness of collecting the Panhandle penalties from GCR customers was not investigated further due to the *de minimis* amounts involved (≈\$10,000).

4.0 Annual Demand Cost Cap

ProLiance was created in 1996 to, among other things, reduce the amount and the associated costs of the interstate pipeline capacity required to serve Vectren North. This was to be

accomplished largely through ProLiance's use of Citizens Gas' LNG storage facilities to meet a portion of Vectren North's design day capacity requirements. The use of Citizens Gas' LNG storage facilities is reflected in the Appendices approved for Vectren North under the 2011 Settlement Agreement as "Appendix I – Diversion of Entitlements." The 2011 Settlement Agreement initially provided that up to 70,000 Dth per day would be available to Vectren North from ProLiance under Appendix I.

Under the 2011 Settlement Agreement, due to Appendix I and other factors, it was anticipated that ProLiance would sell delivered gas supply services to the Utilities at a savings compared to what the Utilities could achieve individually without the benefit of joint portfolio administration by ProLiance. The Utilities' customers and ProLiance were to share the benefit of such economies or synergies. Following a review process conducted by the OUCC, the Utilities', and ProLiance, the synergies and efficiencies associated with the joint portfolio of interstate pipeline transportation and storage services were to be shared on a 50/50 basis through the establishment of an Annual Demand Cost Cap, which is an amount negotiated by the OUCC and ProLiance.

The initial Annual Demand Cost Cap analysis performed by the Utilities and ProLiance for the first year of the 2011 Settlement Agreement (April 2011 – March 2012) indicated synergies of \$166,719 and an Annual Demand Cost Cap for the three Utilities of \$94,470,247. These amounts were determined by averaging the costs associated with the interstate pipeline services that ProLiance designated as being used to provide the Appendices services to the Utilities and ProLiance's actual cost of providing service. The initial analysis was thoroughly reviewed by Exeter. This review including assessing whether:

- The Appendices service quantities were consistent with the design day and winter season service obligation of the Utilities' customers;
- The designated pipeline services were reasonable; and
- Rates used in ProLiance's analysis were consistent with actual pipeline rates.

Exeter's first-year review suggested that ProLiance's costs were understated and that the synergies associated with joint portfolio administration were also understated. Relying on information maintained in Exeter's Purchase Model, the OUCC negotiated an Annual Demand Cost Cap of \$93,742,378 for the period April 2011 – March 2012, which reflected synergy savings of \$1,926,226. This reflected a reduction of \$727,869 from the Annual Demand Cost Cap initially proposed by the Utilities and ProLiance.

The initial Annual Demand Cost Cap analysis performed by the Utilities and ProLiance for the second year of the 2011 Settlement Agreement (April 2012 – March 2013) indicated synergies of \$256,111 and an Annual Demand Cost Cap for the three Utilities of \$92,414,276. Following a review process similar to that conducted for the first year of the 2011 Settlement Agreement, Exeter found that ProLiance's costs were understated and that the synergies associated with joint portfolio administration were also understated. Relying on information maintained in Exeter's Purchase Model, the OUCC negotiated an Annual Demand Cost Cap of \$92,055,676 for the period April 2012 – March 2013. This reflected a reduction of \$358,600 from the Annual Demand Cost Cap initially proposed by the Utilities and ProLiance.

The initial Annual Demand Cost Cap analysis performed by the Utilities and ProLiance/ETC ProLiance for the third year of the 2011 Settlement Agreement (April 2013 – March 2014) indicated synergies of \$591,305 and an Annual Demand Cost Cap for the three Utilities of \$91,483,103. In 2013, Citizens Gas elected to decommission one of its two LNG storage facilities. This made the Appendix I – Diversion of Entitlements service unavailable to Vectren North and, therefore, the associated synergies were not reflected in the initial third-year analysis. Exeter's review of the third-year analysis found that ProLiance's costs were overstated, and that the OUCC negotiated an Annual Demand Cost Cap of \$91,398,103 for the period April 2013 – March 2014. This reflected a reduction of \$85,000 from the Annual Demand Cost Cap initially proposed by the Utilities and ProLiance/ETC ProLiance, and a reduction of \$657,573 from the prior year's Annual Demand Cost Cap.

The initial Annual Demand Cost Cap analysis performed by the Utilities and ETC ProLiance/Exelon for the fourth year of the 2011 Settlement Agreement (April 2014 – March 2015) indicated synergies of \$290,761 and an Annual Demand Cost Cap of \$90,774,259 for the three Utilities. Exeter's review of the fourth-year analysis found that ProLiance's costs were overstated, and that the OUCC negotiated an Annual Demand Cost Cap of \$90,629,392 for the period April 2014 – March 2015. This reflected a reduction of \$144,867 from the Annual Demand Cost Cap initially proposed by the Utilities and ProLiance/ETC ProLiance, and a reduction of \$768,711 from the prior year's Annual Demand Cost Cap.

Negotiations for the fifth and final year of the 2011 Settlement Agreement were recently concluded. The initial Annual Demand Cost Cap analysis performed by the Utilities and Exelon indicated synergies of \$42,034; an Annual Demand Cost Cap of \$89,608,018; and a reduction of \$1,021,374 from the prior year's Annual Demand Cost Cap. This initial analysis was subsequently revised by the Utilities to reflect synergies of \$40,482; and Annual Demand Cost Cap of \$89,771,614, and a reduction of \$857,778 from the prior year's Annual Demand Cost Cap. The parties subsequently agreed to the revised analysis.

Exeter's review found that Vectren North's December 2015 and January 2016 invoices from Exelon included pipeline demand charge adjustments totaling \$215,000 for the period May 2013 through November 2015. These were prior period adjustments related to certain ANR Pipeline contracts. During the period May 2013 through November 2015, Annual Demand Cost Cap were in effect. Recovery of these adjustment amounts appears to be prohibited under the Annual Demand Cost Cap provision of the 2011 Settlement Agreement.

5.0 Auditing Fees

The 2011 Settlement Agreement provided outside auditor and consulting fees of up to \$125,000 per year. For services during the annual period April 2015 – March 2016, Exeter's billed fees totaled \$26,121.

CERTIFICATE OF SERVICE

This is to certify that a copy of the foregoing *Indiana Office of Utility Consumer Counselor's Submission of Annual Report* has been served upon the following counsel of record in the captioned proceeding by electronic service on July 7, 2016.

VECTREN ENERGY GROUP

Robert E. Heidorn
Jason Stephenson
One Vectren Square
Evansville, IN 47708
rheidorn@vectren.com
jstephenson@vectren.com

CITIZENS ENERGY GROUP

Michael E. Allen
2010 N. Meridian Street
Indianapolis, IN 46204-2030
mallen@citizensenergygroup.com

ICE MILLER

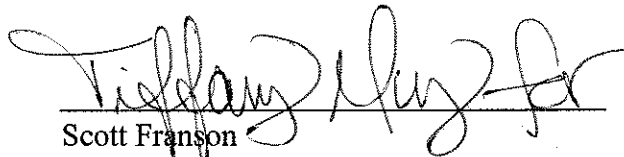
Michael B. Cracraft
One American Square
Suite 2900
Indianapolis, IN 46282-0200
Michael.cracraft@icemiller.com

LEWIS & KAPPES

Todd A. Richardson
Jennifer Wheeler Terry
One American Square, Suite 2500
Indianapolis, IN 46282
trichardson@lewis-kappes.com
jterry@lewis-kappes.com

POLK & ASSOCIATES, LLC

Jerome E. Polk
Russell L. Ellis
101 West Washington Street, Suite 2000
Indianapolis, IN 46204
jpolk@polk-law.com
russel.ellis@polk-law.com



Scott Franson
Attorney No. 27839-49
Deputy Consumer Counselor

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

115 West Washington Street
Suite 1500 South
Indianapolis, IN 46204
infomgt@oucc.in.gov
317/232-2494 – Phone
317/232-5923 – Facsimile

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission)	
on its own motion)	
)	Docket No. 01-0705
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Reconciliation of Revenues collected under)	
Gas Adjustment Charges with Actual Costs)	
prudently incurred)	
)	
Illinois Commerce Commission)	
on its own motion)	
)	
)	Docket No. 02-0067
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Proceeding to review Rider 4, Gas Cost, pursuant)	
to Section 9-244(c) of the Public Utilities Act)	
)	
Illinois Commerce Commission)	
on its own motion)	
)	
)	Docket No. 02-0725
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Reconciliation of Revenues collected under)	
Gas Adjustment Charges with Actual Costs)	
prudently incurred)	

REDACTED

DIRECT TESTIMONY ON REOPENING

OF

JEROME D. MIERZWA

ON BEHALF OF

THE CITIZENS UTILITY BOARD

AND COOK COUNTY STATE'S ATTORNEY'S OFFICE

I. Introduction

Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?

A. My name is Jerome D. Mierzwa. I am a principal and a vice president of Exeter Associates, Inc. My business address is 5565 Sterrett Place, Suite 310, Columbia, Maryland 21044. Exeter specializes in providing public utility-related consulting services.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A. I graduated from Canisius College in Buffalo, New York, in 1981 with a Bachelor of Science Degree in Marketing. In 1985, I received a Master's Degree in Business Administration with a concentration in Finance, also from Canisius College. In July 1986, I joined National Fuel Gas Distribution Corporation ("NFG Distribution") as a Management Trainee in the Research and Statistical Services Department ("RSS"). I was promoted to Supervisor RSS in January 1987. While employed with NFG Distribution, I conducted various financial and statistical analyses related to the company's market research activity and state regulatory affairs. In April 1987, as part of a corporate reorganization, I was transferred to National Fuel Gas Supply Corporation's ("NFG Supply's") rate department where my responsibilities included utility cost of service and rate design analysis, expense and revenue requirement forecasting and activities related to federal regulation. I was also responsible for preparing NFG Supply's Purchase Gas Adjustment ("PGA") filings and developing interstate pipeline and spot market supply

23 gas price projections. These forecasts were utilized for internal planning purposes as well
24 as in NFG Distribution's purchased gas cost review proceedings.

25 In April 1990, I accepted a position as a Utility Analyst with Exeter Associates, Inc.
26 In December 1992, I was promoted to Senior Regulatory Analyst. Effective April 1,
27 1996, I became a principal of Exeter Associates. Since joining Exeter Associates, I have
28 specialized in evaluating the gas purchasing practices and policies of natural gas utilities,
29 utility class cost of service and rate design analysis, sales and rate forecasting,
30 performance-based incentive regulation, revenue requirement analysis, the unbundling of
31 utility services and the evaluation of small customer choice transportation programs.

32
33 Q. HAVE YOU PREVIOUSLY TESTIFIED IN REGULATORY PROCEEDINGS ON
34 UTILITY RATES?

35 A. Yes. I have provided testimony on more than 100 occasions in proceedings before the
36 Federal Energy Regulatory Commission ("FERC"), utility regulatory commissions in
37 Delaware, Georgia, Indiana, Louisiana, Montana, Nevada, New Jersey, Ohio,
38 Pennsylvania, Rhode Island, Texas, and Virginia, as well as before the Illinois Commerce
39 Commission ("ICC" or "Commission"). Before the ICC, this includes presenting
40 testimony in Docket No. 99-0127, the proceeding in which Nicor Gas Company's
41 ("Nicor" or "the Company") Gas Cost Performance Program ("GCPP") at issue in this
42 proceeding was approved, and in Docket No. 02-0067, the proceeding in which the
43 approved GCPP was initially subject to review, prior to the reopening of the record.

44
45 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

46 A. Exeter Associates, Inc. has been retained by the Citizens Utility Board (“CUB”) and the
47 Cook County State’s Attorney’s Office (“CCSAO”), collectively Consumer and
48 Governmental Intervenors (“CGI”), to review the results of Nicor’s GCPP for the period
49 2000-2002.

50
51 Q. HAVE YOU PREPARED EXHIBITS TO ACCOMPANY YOUR TESTIMONY?

52 A. Yes, I have. CGI Exhibits 2.0 through 14.0 on Reopening are attached to my testimony.
53 GCI Exhibit 2.0 summarizes my adjustments to Nicor’s performance under the GCPP.
54 These adjustments are developed in GCI Exhibits 3.0 through 14.0. Attached to my
55 testimony is Appendix A, which contains various documents provided by the Company
56 in discovery and other relevant documents.

57
58 Q. PLEASE SUMMARIZE YOUR CONCLUSIONS AND RECOMMENDATIONS
59 CONCERNING NICOR’S GAS COST PERFORMANCE PROGRAM.

60 A. Nicor has mislead and deceived the ICC with respect to its GCPP in both Docket No. 99-
61 0127 in which the GCPP was approved, and in Docket No. 02-0067 in which the
62 approved GCPP was subject to review. Although more so prior to restatement, Nicor has
63 improperly manipulated its GCPP results, denying ratepayers to what they are entitled.
64 Strong action by the ICC is required in this proceeding. The ICC should send the
65 message that the type of behavior and practices engaged in by Nicor will not be tolerated.
66 Nicor’s claimed performance under the GCPP requires numerous adjustments to correct
67 for the Company’s inappropriate activities and to accurately reflect GCPP results. As a

68 result of these adjustments, which are summarized on Exhibit GCI 2.0, Nicor should
69 refund \$143.3 million to ratepayers.
70

71 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

72 A. In the section following this introduction, I provide a brief history of certain events
73 relevant to matters at issue in this docket, and discuss other relevant matters. In the next
74 section, I describe the GCPP in effect during the period 2000 - 2002. In Section IV, I
75 summarize the Company's performance under the GCPP prior to and after restatement.
76 In Section V, I summarize Nicor's inappropriate behavior and activities under the GCPP.
77 Section VI identifies adjustments to Nicor's claimed performance under the GCPP which
78 are necessary to accurately reflect GCPP results. These adjustments attempt to undo the
79 harm to ratepayers resulting from Nicor's misleading, deceptive and manipulative
80 practices. The next section identifies potential implications of the GCPP on Nicor's 2003
81 purchased gas costs. The last section of my testimony responds to certain claims made
82 by the Company in its direct testimony on reopening.
83

II. Background

Q. PLEASE PROVIDE A BRIEF HISTORY OF THE RELEVANT EVENTS IN THIS DOCKET.

A. Nicor initially filed with the ICC for a performance-based rate (“PBR”) program for gas costs referred to as the Gas Cost Performance Program in August 1996 (Docket No. 96-0386). In January 1997, Nicor filed a motion with the ICC requesting that its GCPP be withdrawn, and the ICC subsequently approved Nicor’s motion.

Nicor filed a second petition for the approval of a GCPP in March 1999 (Docket No. 99-0127). The GCPP included in Nicor’s second petition was very similar to that filed in 1996. Nicor’s second GCPP petition was filed pursuant to Section 9-244 of the Illinois Public Utilities Act (“Act”). The ICC approved and Nicor accepted the GCPP effective January 1, 2000. Under Section 9-244(c) of the Act, the ICC was required to conduct a review of the GCPP after two years of operation to determine whether the GCPP was meeting its objectives. On January 24, 2002, the ICC initiated Docket No. 02-0067 to review the GCPP as required by the Act. An evidentiary hearing was held in Docket No. 02-0067 on June 10, 2002. At the close of the hearing, the record was marked “Heard and Taken.”

On June 20, 2002, CUB received a “whistleblower” fax which alleged that Nicor was operating improperly under the PBR. In response, CUB filed a *Motion to Reopen the Record* on June 27, 2002. As a result, the parties to the proceeding agreed through Stipulation that additional discovery was necessary, and that the existing procedural schedule should be suspended. On December 9, 2002 the parties to Docket No. 02-0067 filed a *Joint Motion to Reopen the Record and Expand Scope of the Proceeding*. On

106 December 17, 2002, the ICC issued an order reopening the review of Nicor's GCPP. On
107 November 7, 2002, Nicor filed documents with the ICC canceling its GCPP effective
108 January 1, 2003.

109 In response to the allegations contained in the whistleblower fax, the Company
110 formed a Special Committee of the Board of Directors ("Special Committee") to
111 investigate Nicor's GCPP activities. The Special Committee in turn engaged Scott R.
112 Lassar of Sidley, Austin, Brown and Wood ("Sidley") to investigate Nicor's GCPP
113 activities. To assist in the investigation, Sidley hired the accounting firm KPMG LLP
114 ("KPMG"). On October 28, 2002, Sidley filed a Report ("Lassar Report") with the
115 Special Committee which presented its findings and conclusions. The Lassar Report
116 found that Nicor's GCPP activities had adverse consequences on ratepayers and
117 recommended certain adjustments to eliminate the adverse consequences. The Lassar
118 Report further recommended that the Board of Directors direct the Company to promptly
119 undertake a re-audit of its financial statements for the years 1999-2001 and the first two
120 quarters of 2002, and to make any filings with the ICC, the U.S. Securities and Exchange
121 Commission and any other regulatory agencies as necessary as a result of the re-audit or
122 any of the recommendations in the Lassar Report.

123 On April 1, 2003 Nicor filed with the ICC restatements of the results of its
124 performance under the GCPP for 2000 and 2001, and its GCPP results for 2002. The
125 accounting firm Deloitte & Touché LLP audited Nicor's financial results for the period
126 1999-2002. This audit resulted in Nicor's parent company, Nicor, Inc., restating its
127 earnings for 2000 and 2001 to reflect a number of adjustments, including those associated

with the GCPP and the Lassar Report. On August 5, 2003, the Company filed testimony with the ICC supporting the restated results of its performance under the GCPP.

Q. WHAT DOCUMENTS DID YOU REVIEW IN CONJUNCTION WITH YOUR INVESTIGATION OF NICOR'S GCPP ACTIVITIES AND THE PREPARATION OF YOUR TESTIMONY?

A. In conjunction with my investigation of Nicor's GCPP activities and the preparation of my testimony, I reviewed the following:

- The testimony submitted by the Nicor witnesses, the transcript of the oral argument presented before the ICC and the Order in Docket No. 99-0127, the proceeding in which the GCPP was approved. I also reviewed the Company's responses to discovery submitted by GCI in Docket No. 99-0127;
- The testimony submitted by Nicor witness and ICC Staff, and the responses to discovery submitted by the intervening parties in Docket No. 02-0067, the proceeding in which the GCPP was subject to review;
- The whistleblower fax received by CUB on June 20, 2002;
- The transcripts of the following current and former Nicor employees:
 - Theodore Lenart, Assistant Vice President;
 - Philip Cali, Former Executive Vice President of Operations;
 - Beth Hohisel, Manager of Supply Services;
 - Lonnie Upshaw, Former Vice President Supply and Technical Services;
 - George Behrens, Vice President Administration and Treasurer;
 - Albert Harms, Manager of Rate Research;
 - Leonard Gilmore, Manager Pipeline Regulation and Supply Planning;
 - David Brown, Compliance Coordinator, Pipeline Rates and Regulatory Group;

- Kathy Halloran, Executive Vice President of Finance and Administration;
 - Richard Rayapan, Manager, Treasury Investments;
 - Rose Gorman, Former Supervisor Gas Accounting; and
 - Thomas Fisher, Chairman, Chief Executive Officer.
- Approximately 140,000 documents provided by the Company in response to discovery since the receipt of the whistleblower fax; and
 - The Company's testimony on rehearing and the responses to discovery submitted by the intervening parties relating to that testimony.

Q. WHY DID YOU REVIEW ALL OF THESE DOCUMENTS?

A. As an expert witness, it is important to review and analyze all available relevant documents prior to rendering your opinion. The documents I reviewed related to Nicor's activities under the GCPP and, therefore, in order to reach findings and conclusions concerning the Company's activities under the GCPP, review of these documents was required. It is normal procedure to review all available relevant documents in any investigation.

Q. PRIOR TO THE RECEIPT OF THE WHISTLEBLOWER FAX, YOU SUBMITTED TESTIMONY IN DOCKET NO. 99-0127 IN WHICH THE GCPP WAS APPROVED, AND IN DOCKET NO. 02-0067 IN WHICH THE APPROVED GCPP WAS SUBJECT TO REVIEW. HAVE YOU DISCOVERED EVIDENCE SINCE THE RECEIPT OF THE WHISTLEBLOWER FAX AND SUBSEQUENT INVESTIGATION WHICH WOULD HAVE AFFECTED THE OPINIONS EXPRESSED IN YOUR PRIOR TESTIMONIES?

191 A. Yes. Since the receipt of the whistleblower fax, critical information has surfaced
192 concerning the design of the GCPP and Nicor's activities under the GCPP, which would
193 have significantly affected the opinions expressed in my prior testimonies, had that
194 information been known at the time. Nicor purposely concealed some of this
195 information. Based on my experience in other proceedings, this is exactly the type of
196 information that utilities reveal voluntarily. Because this information was not available,
197 the parties to these proceedings could not properly evaluate the design of the GCPP, nor
198 Nicor's performance under the GCPP.

199 For example, as discussed later in my testimony, *Nicor failed to produce an*
200 *Inventory Value Team Report*, which would have revealed the Company's intentions with
201 respect to the liquidation of low-cost in storage inventory. Had Nicor's intentions been
202 known concerning the liquidation of low-cost storage inventory during the review of the
203 GCPP, my position concerning the sharing of savings would have changed. In addition,
204 as also discussed later in my testimony, because Nicor failed to inform the parties
205 concerning its intention to liquidate low-cost storage inventory, the parties to Docket No.
206 99-0127 were unable to evaluate whether it was in the best interest of ratepayers to do so.
207 Moreover, before it could be approved by the ICC, the Company was required to show
208 that the GCPP was likely to result in rates lower than those which would have been in
209 effect under traditional regulation. As discussed in greater detail in my testimony, under
210 traditional regulation, 100 percent of the benefits associated with the liquidation of low-
211 cost storage inventory would have accrued to ratepayers. Under the GCPP, only 50
212 percent of the benefit accrued to ratepayers, resulting in rates which were higher than
213 those which would have existed under traditional regulation. Thus, Nicor's withholding

of crucial information did not allow the parties to Docket No. 99-0127 to properly evaluate whether rates would have been lower under the GCPP, a necessary finding required before the GCPP could be approved by the ICC.

Q. DID THE COMPANY ADOPT THE FINDINGS AND RECOMMENDATIONS PRESENTED IN THE LASSAR REPORT?

A. Yes. Nicor claims to have accepted the findings and recommendations contained in the Lassar Report.

Q. DOES GCI ACCEPT THE FINDINGS AND RECOMMENDATIONS PRESENTED IN THE LASSAR REPORT?

A. Based upon our limited review of the Report and the underlying documents, GCI accepts the Lassar Report as accurately describing Nicor's behavior and activities under the GCPP from a historical perspective. However, GCI cannot independently verify that it is without errors. In addition, as discussed in my testimony, GCI does not agree with many of the conclusions and recommendations reached by the Lassar Report.

Q. DO YOU THINK THE CORPORATE CULTURE WHICH EXISTED AT NICOR DURING THE GCPP PERMITTED MISLEADING, DECEPTIVE AND MANIPULATIVE PRACTICES TO OCCUR?

Yes, I believe the fact that CUB received a "whistleblower" fax with which alleged that Nicor was operating improperly under the PBR is sufficient evidence.

[REDACTED]

[REDACTED]

237 [REDACTED]
238 [REDACTED]
239 [REDACTED]
240 [REDACTED]
241 [REDACTED]
242 [REDACTED]
243 [REDACTED]
244 [REDACTED]
245 [REDACTED]
246 [REDACTED]
247 [REDACTED] Based on these
248 depositions, it appears that there was a strong emphasis on generating profits at Nicor
249 during this period, even if the means to doing so was questionable. Those legitimately
250 questioning Nicor's profitable practices were unlikely to remain Nicor employees.
251 Organizational charts for the Nicor employees involved in the operation of the GCPP are
252 provided in GCI Exhibit 3.0.

253

254 **III. Gas Cost Performance Program**

255 Q. IN GENERAL TERMS, PLEASE DESCRIBE THE GCPP.

256 A. Under the GCPP, the Company's total actual annual purchased gas costs ("Actual Gas
257 Costs") each year were compared with an annual gas cost benchmark ("Benchmark").

The Benchmark reflected published market prices for gas (“Market Index Cost”) at the time the gas was sold to customers. The Market Index Cost was adjusted under the GCPP to reflect other factors impacting upon the costs Nicor incurred to provide sales service as follows:

- (1) less a “Storage Credit Adjustment” for the gas price benefit realized from the seasonal price differential associated with gas that is purchased and stored by the Company during non-peak summer periods and used later to serve demand during peak winter periods;
- (2) plus a “Firm Deliverability Adjustment” for the annual cost of reserving firm transportation and purchased storage capacity on the interstate pipelines delivering gas to Nicor; and
- (3) plus a “Commodity Adjustment” reflecting the Company’s historical performance relative to Benchmark Gas Costs after taking into account the Storage Credit Adjustment and the Firm Deliverability Adjustment.

That is, the Benchmark was equal to the Market Index Cost, less the Storage Credit Adjustment, plus the Firm Deliverability Adjustment and the Commodity Adjustment. The difference between Actual Gas Costs and the Benchmark was to be shared equally between Nicor and its customers.

A. Market Index Cost

Q. PLEASE DESCRIBE THE MARKET INDEX COST AND HOW IT WAS DETERMINED.

A. The Market Index Cost represented the annual gas costs that the Company would have incurred if all of its gas supplies were purchased at prevailing Chicago citygate market index prices at the time the gas was sold. The Market Index Cost component was

determined by multiplying sales deliveries on a monthly basis by the applicable Market Index Prices, and summing the resulting monthly costs for an annual period.

The Market Index Price was based on the average of two separate groups of published Chicago citygate price indices. The first group was based on indices reporting first-of-the-month prices (monthly index price). The second group was based on indices reporting daily prices (daily index price). The monthly index price reflected the average of four first-of-the-month published index prices, while the daily market index price reflected the average of three daily published index prices. The monthly index price was given a 65 percent weighting and the daily index price was given a 35 percent weighting in calculating the market index price.

B. Storage Credit

Q. PLEASE DESCRIBE THE STORAGE CREDIT ADJUSTMENT.

A. The Storage Credit Adjustment adjusted the Benchmark to reflect the benefit that ratepayers received as a result of purchasing gas supplies during off-peak summer periods, when prices are typically lower, injecting that gas into storage, and then withdrawing those gas supplies to meet demand during peak winter periods, when prices are typically higher.

Q. HOW WAS THE STORAGE CREDIT ADJUSTMENT DETERMINED?

A. The Storage Credit Adjustment was determined by multiplying the actual quantity of gas withdrawn from storage by Nicor during a calendar year by a calculated Storage Credit Rate. The Storage Credit Rate was intended to reflect the seasonal price difference

between the cost of gas purchased during the summer and the cost of gas purchased during the winter. The Storage Credit Rate was calculated by subtracting the weighted average price of storage injections from the weighted average price of storage withdrawals. The weighted average price of storage injections was calculated by multiplying the monthly Market Index Price by a fixed percentage reflective of Nicor's historical storage injection activity. The weighted average price of storage withdrawals was calculated by multiplying the monthly Market Index Price by a fixed percentage reflective of Nicor's historical storage withdrawal activity.

C. Firm Deliverability Adjustment

Q. PLEASE DESCRIBE THE FIRM DELIVERABILITY ADJUSTMENT.

A. The Firm Deliverability Adjustment adjusted the Benchmark to account for the costs incurred by Nicor on an annual basis to reserve firm transportation and storage capacity from interstate pipelines. Deducted from Nicor's interstate pipeline capacity costs were capacity management credits related to the Company's capacity release activity, buy/sell transactions, sales for resale and linked-purchase sell agreements. The Firm Deliverability Adjustment approved by the Commission in Docket No. 99-0127 was \$116,582,612 for each year under the GCPP. This figure consisted of firm transportation and storage capacity charges of \$124,768,288, reduced by a capacity management credit of \$8,185,676.

D. Commodity Adjustment

Q. PLEASE DESCRIBE THE COMMODITY ADJUSTMENT.

A. The Commodity Adjustment adjusted the Benchmark to reflect historical variations between the Market Index Cost and the Company's Actual Gas Costs after removing the variation accounted for by the Storage Credit Adjustment and the Firm Deliverability Adjustment. That is, the Commodity Adjustment was intended to adjust the Benchmark so that when viewed on a historical basis, Nicor's actual gas costs and the Benchmark were equal. The variation accounted for by the Commodity Adjustment was attributable to a number of factors including:

- (1) the premium associated with reserving firm gas supplies;
- (2) distribution system lost and unaccounted-for gas;
- (3) any differences in the timing of purchases, or pricing terms and locations; and
- (4) revenue from off-system storage arrangements.

The Commodity Adjustment Rate adopted by the Commission in Docket No. 99-0127 was \$0.168 per MMBtu.

Q. HOW WAS THE COMMODITY ADJUSTMENT DETERMINED?

A. The Commodity Adjustment was calculated by multiplying actual total delivered sales volumes for the GCPP year by \$0.168 per MMBtu.

IV. Nicor's GCPP Performance

357 Q. HOW DID NICOR CLAIM IT PERFORMED UNDER THE GCPP DURING 2000
358 AND 2001 PRIOR TO RESTATEMENT AND THE WHISTLEBLOWER FAX?

359 A. In its direct testimony in Docket No. 02-0067, for 2000 and 2001, Nicor claimed Actual
360 Gas Costs of \$2,591.1 million and a Benchmark of \$2,645.2 million. Thus, Nicor
361 claimed to have outperformed the Benchmark by \$54.1 million. Based on these results,
362 ratepayers would have been required to pay Nicor's Actual Gas Costs of \$2,591.1
363 million, plus 50 percent of the \$54.1 million in alleged savings, or a total of \$2,618.1
364 million ($\$2,591.1 + (50 \text{ percent} \times \$54.1)$).

365
366 Q. HOW DID NICOR'S PERFORMANCE UNDER THE GCPP DURING 2000
367 AND 2001 CHANGE UPON RESTATEMENT?

368 A. On restatement, Nicor's Actual Gas Costs increased by \$55.6 million to \$2,646.7 million,
369 while the Benchmark decreased by \$34.5 million to \$2,610.7 million. As a result of these
370 changes, instead of out performing the Benchmark by \$54.1 million, Nicor's Actual Gas
371 Costs exceeded the Benchmark by \$36.0 million, and ratepayers are owed a credit of
372 \$18.0 million ($\$36 \times 50 \text{ percent}$). In summary, instead of being required to pay \$2,618.1
373 million, ratepayers would be required to pay \$2,628.7 million ($\$2,646.7 - \18.0), or an
374 additional \$10.6 million. The derivation of this amount is shown in Table 1, which is
375 presented later in this section of my testimony.

376
377 Q. HOW DOES NICOR CLAIM IT PERFORMED UNDER THE GCPP DURING 2002?

378 A. Nicor is claiming Actual Gas Cost of \$947.7 million and a Benchmark of \$1,001.5
379 million for 2002. As such, Nicor is claiming savings of \$53.8 million, and that it is

entitled to 50 percent of the savings, or \$26.9 million. In total, as also shown later in Table 1, for the period 2000-2002, Nicor claims it is owed \$37.4 million by ratepayers.

Q. AT LINE 129 OF HIS DIRECT TESTIMONY ON REOPENING, NICOR WITNESS ROCCO J. D’ALESSANDRO CLAIMS THAT THE COMPANY IS ONLY SEEKING AN ADDITIONAL \$7.0 MILLION FROM RATEPAYERS. WHY DOES YOUR AMOUNT DIFFER FROM THE AMOUNT REFERENCED BY WITNESS D’ALESSANDRO?

A. The difference between the \$37.4 million and \$7.0 million figures is attributable to various adjustments and can be reconciled as follows. Nicor’s actual gas costs for 1999 have been reduced by \$13.7 million in conjunction with the sale of certain gas to IMD Storage Transportation and Asset Management Company, LLC (“IMD”). This adjustment, discussed later in my testimony, reflects a \$13.7 million reduction to the amount owed by ratepayers. Nicor claims to have underbooked the savings it was entitled to under the GCPP in 2001 by \$1.3 million. This represents an additional amount to be collected from ratepayers. In addition, Nicor claims that it is owed \$0.8 million in interest from ratepayers for the period 2000-2003. Finally, the Company claims that a \$18.8 million reduction to actual gas costs for 2002 is appropriate to reflect final gas costs for 2002. Table 1 summarizes the reconciliation of the \$37.4 million and \$7.0 million figures.

TABLE 1			
NICOR GAS COMPANY			
Development of Company Collection Claim			
2000 GCPP	Original	Restatement	Change
Benchmark	\$1,318,322,153	\$1,323,453,373	\$5,131,220
Actual Gas Cost	1,293,886,874	1,329,904,654	36,017,780
Savings (Loss)	\$24,435,279	(\$6,451,281)	(\$30,886,560)
Ratepayer Share	\$12,217,640	(\$3,225,641)	(\$15,443,280)
2001 GCPP	Original	Restatement	Change
Benchmark	\$1,326,858,624	\$1,287,206,360	(\$39,652,264)
Actual Gas Costs	1,297,155,766	1,316,760,421	19,604,655
Savings (Loss)	\$29,702,858	(\$29,554,061)	(\$59,256,919)
Ratepayer Share	\$14,851,429	(\$14,777,031)	(\$29,628,460)
Total 2000-01 GCPP	Original	Restatement	Change
Benchmark	\$2,645,180,777	\$2,610,659,733	(\$34,521,044)
Actual Gas Costs	2,591,042,640	2,646,665,075	55,622,435
Savings (Loss)	\$54,138,137	(\$36,005,342)	(\$90,143,479)
Ratepayer Share	\$27,069,069	(\$18,002,671)	(\$45,071,740)
Total 2000 - 01 Charges	Original	Restatement	Change
Actual	\$2,591,042,640	\$2,646,665,075	\$55,622,435
Savings (Loss)	\$27,069,069	(\$18,002,671)	(\$45,071,740)
Total	\$2,618,111,709	\$2,628,662,404	\$10,550,696
2002 GCPP			Amount
Benchmark			\$1,001,490,233
Actual Gas Costs			947,738,492
Savings (Loss)			\$53,751,741
Ratepayer Share			\$26,875,871
Total 2000 - 02 Charges			Amount
2000 -2001 Over/(Under) Collection			\$10,550,696
2002 Over/(Under) Collection			26,875,871
Total			\$37,426,566
Adjustments			Amount
1999 Sale to IMD			(\$13,751,764)
Interest			780,374
2001 Savings Booking			1,329,699
2002 Gas Cost Adjustment			(18,793,860)
Amount to be Collected per Company			\$6,991,015

435 **V. Overview of Nicor's GCPP Activities**

436 Q. SHOULD THE COMMISSION APPROVE NICOR'S CLAIMS IN THIS
437 PROCEEDING NOW THAT THE COMPANY HAS RESTATED THE RESULTS
438 OF THE GCPP?

439 A. No. As subsequently explained, Nicor has mislead and deceived the ICC with respect to
440 its GCPP in both Docket No. 99-0127 in which the GCPP was approved, and in Docket
441 No. 02-0067 in which the approved GCPP was subject to review. Although more so
442 prior to restatement, Nicor has improperly manipulated its GCPP results, denying
443 ratepayers to what they are entitled.

444
445 Q. WHAT DID THE COMPANY SAY IN ITS ORAL ARGUMENT BEFORE THE
446 ICC IN DOCKET NO. 99-0127 WITH RESPECT TO HOW IT WOULD
447 OPERATE UNDER THE GCPP?

448 A. Stephen J. Mattson, arguing on behalf of Nicor, stated the following:

449
450 "And we're absolutely confident that not only the company but
451 very, very importantly, maybe more importantly, the customers
452 will benefit. We don't want them upset with us. It would be pretty
453 stupid business on our part if we did something that tarnished the
454 Company's reputation." (Tr. 56).
455

456 Q. DID THE COMPANY OPERATE UNDER THE GCPP AS MR. MATTSON
457 REPRESENTED TO THE ICC?

458 A. No. As subsequently explained, Nicor mislead and deceived the ICC and the parties to
459 Docket Nos. 99-0127 and 02-0067 by mischaracterizing how it would operate under its
460 GCPP, manipulated its GCPP results, and engaged in a "catch us if you can" theory of
461 regulation.

462 Q. DO YOU HAVE AN OPINION AS TO WHETHER STRONG ACTION IS
463 REQUIRED BY THE ICC IN THIS PROCEEDING?

464 A. Yes. My opinion is that strong action by the ICC is required in this proceeding in order
465 to signal to other utilities in Illinois that the type of behavior and practices engaged in by
466 Nicor will not be tolerated by the ICC. If this Commission were merely to require
467 adjustments which placed Nicor in the same position as if it had not engaged in its
468 misleading, deceptive and manipulative behavior and practices, then the ICC would send
469 Illinois utilities the wrong message. That is, it would send the message that it is
470 acceptable to be misleading, deceptive and manipulative in proceedings before the ICC
471 because the worse thing that can happen to the utility is that if you are caught, you will
472 end up with a result as though you had been forthright to begin with. After all, if not for
473 the whistleblower fax, none of Nicor's inappropriate behavior and practices would have
474 been revealed. If strong action is not taken, it would give utilities the incentive to pursue
475 Nicor's "catch us if you can" theory of regulation.

476

477 Q. WHAT IS THE BASIS FOR THAT OPINION?

478 A. In all of my years of providing services to clients and testifying before regulatory
479 agencies, I have never before found a utility which has engaged in behavior and
480 practices that in my opinion can be described in no other way than being misleading,
481 deceptive and manipulative. This opinion is based upon the thousands of documents I
482 have reviewed as part of my investigation of Nicor's GCPP activities, the depositions of
483 Nicor employees and the review of the other materials previously identified.

484

485 Q. WHY DO YOU CHARACTERIZE NICOR'S ACTIONS UNDER THE GCPP
486 AS ENGAGING IN MISLEADING, DECEPTIVE AND MANIPULATIVE
487 BEHAVIOR AND PRACTICES?

488 A. These behaviors and practices will be detailed in my testimony but they include
489 concealing information from the ICC, misrepresenting the Company's intentions under
490 the GCPP and including in the GCPP costs that were clearly ineligible for recovery.
491 There is no other way to describe these actions as other than being misleading, deceptive
492 and manipulative.

493
494 Q. DO YOU HAVE ANY OTHER COMMENTS BEFORE CONTINUING WITH
495 YOUR TESTIMONY?

496 A. Yes. Although CUB, CCSAO and other parties have spent a considerable amount of
497 effort investigating Nicor's GCPP activities, there is no assurance that the parties to the
498 proceeding have been able to discover all of the ways in which Nicor has mislead and
499 deceived the parties, manipulated its GCPP results and harmed ratepayers.

500

501 **VI. Specific GCPP Activities**

502 Q. PLEASE SUMMARIZE NICOR'S MISLEADING, DECEPTIVE AND
503 MANIPULATIVE GCPP ACTIVITIES.

504 A. Nicor's misleading, deceptive and manipulative GCPP practices included the following:

505

506 ○ Concealing its intentions to liquidate LIFO gas in inventory;

507

508 ○ Including interest charges as a cost of gas;

509

510 ○ Selling gas at a loss prior to the adoption of the GCPP in 1999 which was charged
511 entirely to ratepayers in order to improve its performance under the GCPP;

512

- Treating gas withdrawn from contract storage as flowing supplies, thus denying ratepayers the seasonal price savings generated by storage operations;
- Engaging in virtual storage transactions in an attempt to further manipulate GCPP results;
- Improperly passing through a portion of the costs associated with a weather insurance product as a gas cost;
- Manipulating storage withdrawal quantities to improve its GCPP performance;
- Misrepresenting the status of its contract negotiations with Tennessee Gas Pipeline and Midwestern Gas Transmission before the Commission;
- Inappropriately including gas deliveries made in 1999 in its 2000 GCPP results; and
- Selling gas to an affiliate at below market prices.

A. LIFO Storage Inventory

Q. PLEASE EXPLAIN LIFO ACCOUNTING FOR GAS IN STORAGE INVENTORY?

A. As discussed at pages 15 and 16 of the Lassar Report:

“The value of gas owned by Nicor and kept in its storage fields is determined using a Last-In-First-Out (“LIFO”) method of accounting. Under the LIFO method, the inventory is considered to exist in layers, with each layer priced at its cost in the year it was added to the storage reservoir. When gas is withdrawn from storage, the most recent layer is considered withdrawn for accounting purposes, hence the term “last-in, first-out.” Additional layers are added to the inventory when layers added to inventory exceeds layers withdrawn. At the end of each calendar year, a determination is made whether a layer has been added to Nicor’s inventory or whether there has been a LIFO decrement (liquidation), that is, a net withdrawal from Nicor’s inventory.”

Q. WHAT IS THE SIGNIFICANCE OF NICOR’S LIFO STORAGE INVENTORY LAYERS AND THE GCPP?

552 A. Prior to the adoption of GCPP, Nicor had a significant quantity (approximately
553 75,000,000 Dth) of gas in LIFO storage inventory layers on its books valued at about
554 \$0.30 per Dth. The market value of this gas was significantly in excess of \$0.30 per Dth.
555 For example, if the market price of gas were \$3.00, the market value of the 75,000,000
556 Dth of stored gas acquired at a cost of \$0.30 would be in excess of \$200 million. Under
557 the traditional regulatory system which Nicor operated under prior to the GCPP, if Nicor
558 accessed or liquidated a portion of this low-cost gas in inventory, the entire benefit of the
559 low-cost gas would have accrued to ratepayers.

560 In 1998, Nicor was concerned that due to the unbundling of natural gas sales
561 service under its customer choice program, the benefits associated with this low-cost gas
562 would accrue entirely to ratepayers. As a result, Nicor created an internal “team,”
563 referred to as the Inventory Value Team, whose purpose was to investigate various
564 opportunities to capture the value of the low-cost LIFO inventory layers for Nicor. In
565 1998, the Inventory Team issued an *Inventory Value Team Report*, included in the Lassar
566 Report as Appendix 7, which recommended that Nicor pursue a PBR mechanism, which
567 would permit the Company to realize a portion of the LIFO inventory value if sold to
568 ratepayers. Nicor filed its PBR, the GCPP, with the ICC in March 1999. The potential
569 profit to Nicor from the value of the low-cost LIFO gas was a key driver in Nicor’s going
570 forward with the GCPP. [REDACTED]

571 [REDACTED]
572 [REDACTED]
573 [REDACTED]
574 [REDACTED] The Lassar Report reached this
575 same conclusion (at 19). As such, the low-cost LIFO inventory was a risk mitigation tool

576 for Nicor under the GCPP. Thus, as Nicor pursued its proposed GCPP before the
577 Commission, it planned to utilize its low-cost LIFO layers of gas to generate “savings” in
578 which it would share, not through the purchase of gas at prices below that of other market
579 participants, but through the draw-down of its older, lower cost layers of gas in storage.

580
581 Q. DID NICOR REVEAL TO THE ICC IN DOCKET NO. 99-0127 THAT IT
582 INTENDED TO LIQUIDATE ITS LOW COST LIFO INVENTORY UNDER
583 THE PBR?

584 A. No. Nicor’s witnesses failed to reveal this key profit source the Company was seeking to
585 include in its proposed PBR.

586
587 Q. DO YOU BELIEVE THE COMPANY HAD AN OBLIGATION TO REVEAL
588 ITS INTENTIONS TO LIQUIDATE ITS LOW COST LIFO INVENTORY TO
589 THE COMMISSION?

590 A. Absolutely. It is incumbent upon a utility to fully reveal its proposals to the Commission
591 rather than adopting a “catch us if you can” approach. Unlike a court proceeding in
592 which the judge decides in favor of one party or the other on the basis of information
593 presented, utility regulatory commissions have an affirmative responsibility to set just
594 and reasonable rates. Just and reasonable rates should be based on conclusions, which
595 should be based on findings of facts, which should be based on record evidence, and that
596 evidence should be substantial. Just and reasonable rates cannot result when the record is
597 incomplete due to the Company’s failure to affirmatively disclose to the Commission
598 how its GCPP would operate, and the Company’s further failure to disclose its plans
599 when asked for such plans. This present case stands for the principle that just and

reasonable rates cannot be the result when important information is hidden by a utility from its regulatory oversight authority.

Q. WAS SPECIFIC DISCOVERY SERVED ON NICOR IN DOCKET NO. 99-0127 WHICH WOULD HAVE REVEALED THE COMPANY'S INTENTIONS TO LIQUIDATE ITS LOW-COST LIFO INVENTORY?

A. Yes. In CUB 27, the Company was asked:

Q. Please provide a copy of all projections, analyses and studies prepared which examine the extent to which the Company may profit under its proposal. Include copies of all communications which discuss the profit potential of the Company's proposal.

Nicor responded:

A. The Company has not performed any projections, analyses or studies related to its potential performance under its proposal nor does the Company have any communications which address this issue. (Appendix A, Tab 2).

The *Inventory Value Team Report* specifically addressed the profit potential associated with liquidating low-cost LIFO storage inventory and, therefore, was a responsive document sought by this interrogatory. Thus, in addition to being misled and deceived by Nicor because it did not voluntarily reveal its intentions under the GCPP in its direct testimony, Nicor concealed its intentions even when explicitly and directly requested to do so in discovery.

628 Q. IN YOUR OPINION, DID NICOR PURSUE A STRATEGY TO
629 CONSCIOUSLY CONCEAL ITS INTENTIONS TO LIQUIDATE ITS LOW-
630 COST LIFO INVENTORY IN DOCKET NO. 99-0127?

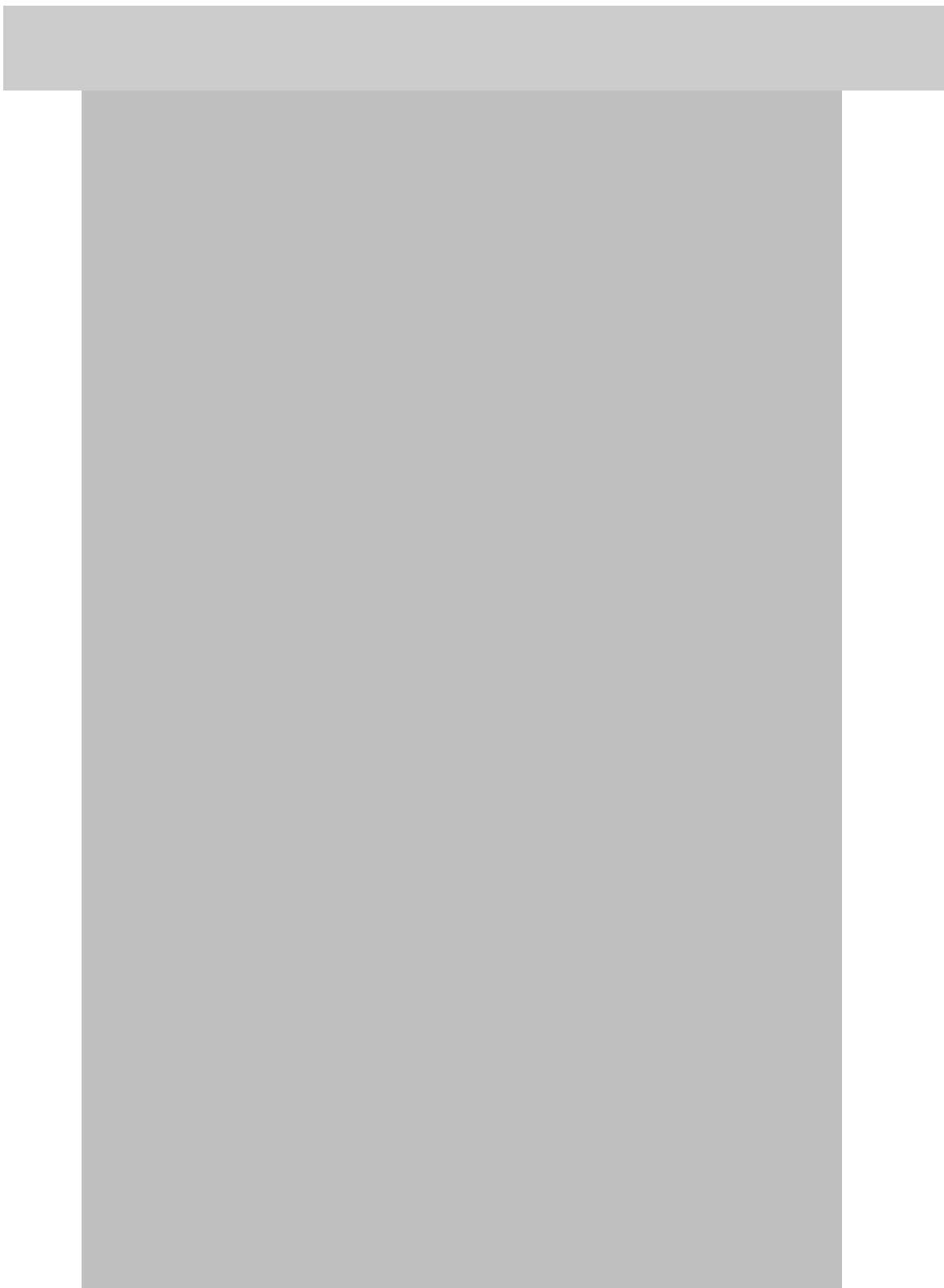
631 A. Yes.

632 Q. WHAT IS THE BASIS FOR YOUR OPINION?

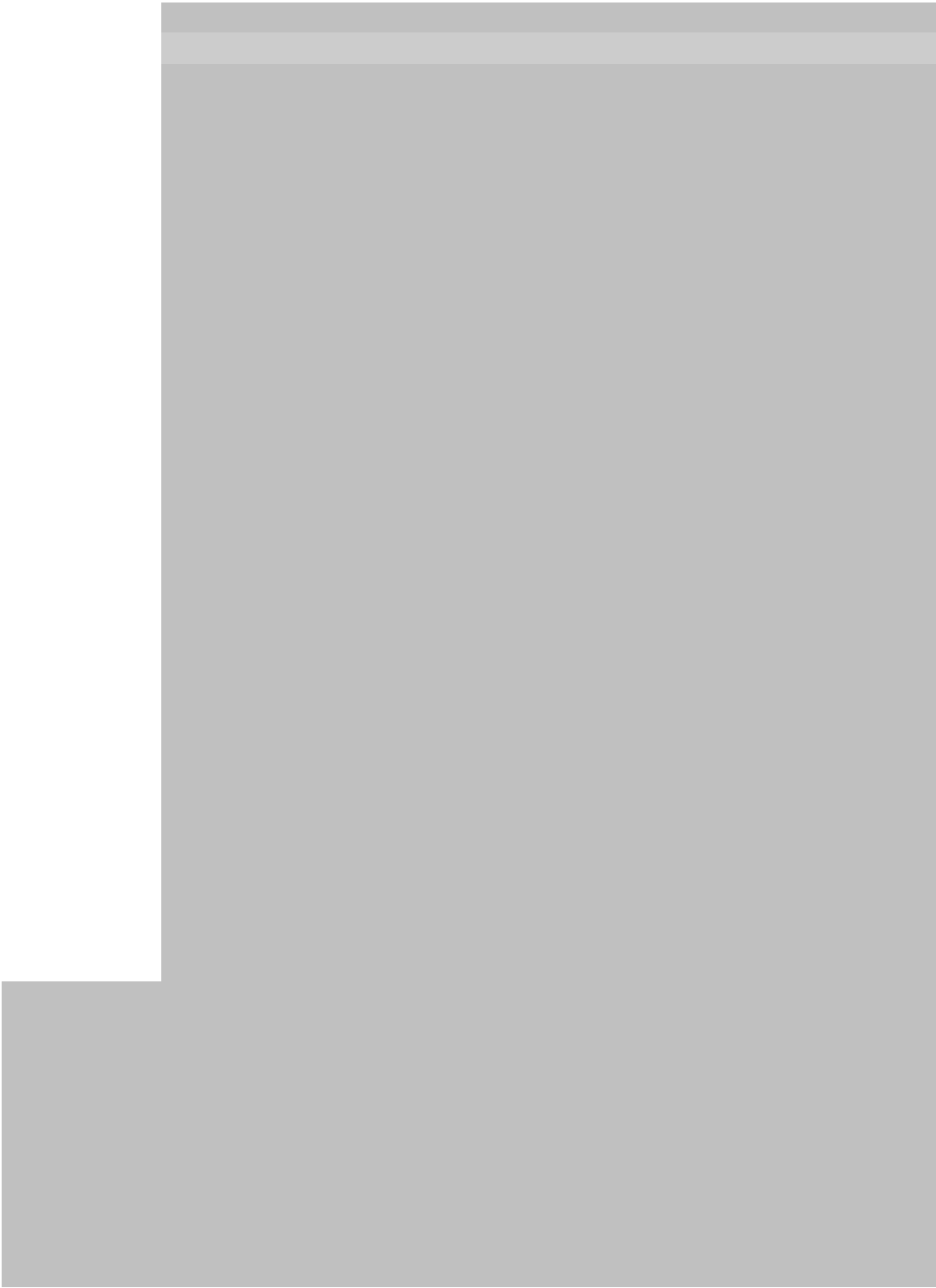
634 A. The *Inventory Value Team Report* recommended that Nicor “capture” the LIFO inventory
635 value by filing and implementing a gas rate performance plan related to gas costs.
636 Capturing the LIFO inventory value was not addressed by the Company in testimony in
637 Docket No. 99-0127. Utilities have an affirmative obligation to fully reveal their
638 proposals to the Commission, and it is my experience in other jurisdictions that utilities
639 do fully reveal their proposals to their commissions. This indicates that Nicor
640 consciously concealed its intentions to liquidate its low-cost LIFO inventory and that the
641 failure to reveal its intentions was not a simple oversight.

642
643
644
645
646
647
648
649

650
651
652
653
654
655
656
657
658
659
660
661
662
663
664
665
666
667
668
669
670
671
672
673
674
675
676
677
678
679
680
681
682
683
684
685
686
687
688
689
690
691



692
693
694
695
696
697
698
699
700
701
702
703
704
705
706
707
708
709
710
711
712
713
714
715
716
717
718
719
720
721
722
723
724
725
726
727
728
729
730
731
732
733



734
735
736
737
738
739
740
741
742
743
744
745
746
747
748
749
750
751
752
753
754
755
756
757
758
759
760
761
762
763
764
765
766
767
768
769
770
771
772
773



774
775
776
777

[REDACTED]

778

779 Q. DID THE COMPANY DELIBERATELY HIDE ITS ACTIVITIES WITH
780 RESPECT TO THE LIQUIDATION OF LOW-COST LIFO INVENTORY AT
781 OTHER TIMES?

782 A. Yes. As a result of the Order in Docket No. 99-0127, Nicor was required to file regular
783 quarterly reports on its GCPP with ICC Staff. [REDACTED]

784 [REDACTED]

785 [REDACTED]

786 [REDACTED]

787 [REDACTED]

788

789 Q. IN YOUR OPINION, WAS THE TESTIMONY BY NICOR'S WITNESSES IN
790 DOCKET NO. 99-0127 MISLEADING OR DECEPTIVE IN LIGHT OF THE
791 COMPANY'S INTENTIONS TO LIQUIDATE ITS LOW-COST STORAGE
792 INVENTORY?

793 A. Yes.

794

795 Q. WHAT IS THE BASIS FOR YOUR OPINION?

796

797

798

799

[REDACTED]

800
801
802
803
804
805
806
807
808
809
810
811
812
813
814
815
816
817
818
819
820
821
822
823
824
825
826
827
828
829
830
831



832
833
834
835
836
837
838
839
840
841
842
843
844
845
846
847
848
849
850
851
852
853
854
855
856
857
858
859
860
861
862
863
864
865
866
867
868
869
870
871
872
873



874
875
876
877
878
879
880
881
882
883
884
885
886
887
888
889
890
891
892
893
894
895
896
897
898
899
900
901
902
903
904
905
906
907
908
909
910
911
912
913
914
915



916
917
918
919
920
921
922
923
924
925
926
927
928
929
930
931
932
933
934



935 Q. IN YOUR OPINION, WERE THERE OTHER WAYS IN WHICH THE
936 COMPANY'S TESTIMONY IN DOCKET NO. 99-0127 WAS MISLEADING?

937 A. Yes. The Benchmark was portrayed and designed to reflect what Nicor's actual gas costs
938 would have been under traditional regulation (Order at 5). Under traditional regulation,
939 the full benefit of Nicor's low-cost LIFO inventory would have accrued to ratepayers. ■

940 ■

941 ■

942 ■. Nicor deceived the parties and the ICC because it not only planned to
943 manipulate its LIFO storage inventory to generate profits and failed to reveal this to the
944 Commission, but it failed to include provisions in the Benchmark in the event it
945 liquidated low-cost LIFO inventory.
946

947 IN YOUR OPINION, DID NICOR PURSUE A STRATEGY TO CONSCIOUSLY
948 CONCEAL THE FACT THAT IT HAD LIQUIDATED LOW-COST LIFO
949 INVENTORY?

950 Yes. In Docket No. 02-0067, the Company presented testimony describing how it was able to
951 achieve savings under the GCPP. Prior to restatement of the claimed savings of \$54.1 million,
952 [REDACTED] was attributed to the liquidation of low-cost LIFO inventory. Even though the vast
953 majority of the savings achieved by Nicor in 2000 and 2001 was attributable to the liquidation of
954 low-cost LIFO inventory, this was never mentioned in testimony as an activity which generated
955 GCPP savings. The document included as Appendix A, Tab 4, clearly indicated that Company's
956 witness were directed not to reveal the LIFO savings in their direct testimony.

957 Also in Docket 02-0067, the CUB served discovery on Nicor which would have revealed
958 how Nicor was able to generate savings under the GCPP (Appendix A, Tab 5). In its response,
959 the Company objected to the request because it called for speculation, requested information not
960 maintained by the Company, and sought information which was irrelevant, beyond the scope of
961 the proceeding, and not reasonably calculated to lead to the discovery of admissible evidence.
962 Without waiving these objections, the Company stated that the GCPP was a comprehensive
963 benchmark, and it was not possible to determine how much of the savings were attributable to
964 specific actions. After the receipt of the whistleblower fax, the Company produced numerous
965 documents that previously existed at the time of the data request but were not provided until after
966 the fax, which identified the activities that generated savings under the GCPP, including the
967 savings generated by the liquidation of low-cost LIFO inventory (Appendix A, Tab 6). Clearly,
968 Nicor mislead and deceived the parties to Docket No. 02-0067 by not providing these
969 documents.

970
971
972
973
974
975
976
977
978
979
980
981
982
983
984
985
986
987
988
989
990
991
992
993

[REDACTED]

[REDACTED] I would note that George Behrens was a Company witness in Docket No. 02-0067 prior to reopening, and was identified as the witness sponsoring the response to CUB 1.17.

Q. NICOR HAS CLAIMED THAT THE LIQUIDATION OF LOW-COST LIFO INVENTORY UNDER THE GCPP WAS A BENEFIT TO RATEPAYERS. DO YOU AGREE?

A. No. Under the GCPP, ratepayers receive 50 percent of the benefit associated with liquidating low-cost LIFO inventory. During the period 2000 – 2002, Nicor liquidated approximately [REDACTED] Dth of its LIFO inventory. As shown on GCI Exhibit 4.0, the savings generated by the liquidation of low-cost LIFO inventory was [REDACTED]. Thus, the benefit to ratepayers was [REDACTED], or 50 percent. This is a one-time benefit for ratepayers. In the future, it is likely that Nicor will need to replace the liquidated low-cost inventory with much higher cost gas. Unless the ICC directs otherwise, ratepayers will be required to pay the carrying charges on this higher cost inventory when Nicor files a base rate proceeding. Based on the pre-tax return of 16.7 percent approved in Nicor’s last base rate case (Docket No. 95-0219), and a current cost of gas of \$5.00 per Dth, the additional carrying cost to ratepayers will be approximately [REDACTED]. Thus, the benefit from liquidating the low-cost inventory will be gone in [REDACTED], and ratepayers will be burdened into the future by the higher carrying costs associated with the higher cost inventories, while Nicor benefits from the collection of additional base rate revenues.

994 Q. NICOR CLAIMS THAT IT IS ENTITLED TO THE BENEFITS OF THE LOW-
995 COST LIFO INVENTORY. DO YOU AGREE?

996 A. No. As previously discussed, the GCPP Benchmark was intended to reflect Nicor's
997 actual gas costs under traditional regulation. Under traditional regulation, ratepayers
998 would have received 100 percent of the benefit from liquidating low-cost LIFO
999 inventory. Nicor witnesses Barrett and Russell Feingold both agree with this treatment
1000 (Appendix A, Tab 7, CB-1.12, and Tab 8, CF-1.16), as does the Lassar Report (at 18).
1001 Nevertheless, in discovery, witness Barrett identified two FERC cases he believes
1002 support Nicor's position that a share of the benefits from liquidating low-cost LIFO
1003 inventory should accrue to the Company (Appendix A, Tab 7, CB-1.1). They do not.
1004 Both cases involve the sale of gas in storage by interstate pipelines. Nicor is not an
1005 interstate pipeline. Nicor provides a regulated sales service to ratepayers. Interstate
1006 pipelines have not provided regulated sales service since at least 1993. Therefore, the
1007 activities of interstate pipelines have no relevance in this proceeding.

1008
1009 Q. DO YOU HAVE ANY COMMENTS ON THE MICHIGAN PROCEEDING
1010 CITED BY WITNESS BARRETT, CASE NO. U-12679?

1011 A. Yes. However, before addressing Case No. U-12679 cited by witness Barrett, a brief
1012 history of certain events is required. In Case No. U-11599, the Michigan Public Service
1013 Commission ("MPSC"), as part of a three-year experimental customer choice program,
1014 approved a fixed gas charge of \$2.8364 per Dth for Consumer Energy Company
1015 ("Consumers") which was to be applicable for sales service during the period April 1,
1016 1998 through March 31, 2001. This in essence established a PBR for Consumers, with

Consumers benefiting if it could acquire gas at less than \$2.8364 per Dth, and absorbing costs if it could not.

In Case No. U-12679, the proceeding referenced by witness Barrett, Consumers filed an application to reclassify approximately 75,500,000 Dth of recoverable base gas in storage. In essence, the reclassification allowed Consumers to include low-cost LIFO inventory in its cost of gas in storage. In its application, Consumers stated that during the first two years under the fixed gas charge approved in Case No. U-11599, revenues exceeded costs by \$45.1 million. Consumers was entitled to retain these revenues. In the third-year, Consumers claimed that gas costs were going to exceed revenues. Included in Consumers' application was a request to established a regulatory liability in the amount of \$45.1 million to reflect its estimated losses during the third year. Consumers' application in Case No. U-12679 requested approval of the deferred accounting treatment, and stated that if its losses were less than \$45.1 million, it would refund the difference to ratepayers. As such, ratepayers would benefit from Consumers' proposal to include low-cost LIFO in its cost of gas in storage. A copy of the MPSC's order in Case No. U-12679 is included in Appendix A, Tab 9.

The circumstances present in Case No. U-12679 are significantly different than those in this proceeding. First, unlike Nicor, Consumers informed the MPSC of its intentions. Second, Consumers' proposal provided for the return of profits realized during the first two years. Neither Docket Nos. 99-0127 or 02-0067 provided for the return of profits realized by Nicor. Third, the reclassification of base gas in storage reduced gas costs to Consumers' ratepayers on a dollar-for-dollar basis up to the \$45.1 million deferred liability amount. Consumers was not entitled to share in any portion of

1041 this benefit. Therefore, Case No. U-12679 does not support the notion that Nicor is
1042 entitled to the benefits associated with liquidating low-cost LIFO inventory.

1043
1044 Q. ARE THERE OTHER PROCEEDINGS IN MICHIGAN WHICH ADDRESS
1045 THE LIQUIDATION OF LOW-COST LIFO INVENTORY WHICH WITNESS
1046 BARRETT DID NOT REFERENCE?

1047 A. Yes. In Case No. U-11682, the MPSC approved an application by Michigan
1048 Consolidated Gas Company (“Mich Con”) to suspend its GCR (PGA) clause from
1049 January 1, 1999 through December 31, 2001, and to charge a fixed gas cost rate of \$2.95
1050 per Mcf during that period. In doing so, Mich Con stated that it would “assume
1051 significant risks” and that portions of its gas supply costs “could be unrecoverable.”
1052 During 1999 and 2000, Mich Con realized a gain of \$70 million. In 2001, gas prices rose
1053 significantly, and Mich Con faced significant losses. In response, Mich Con decided to
1054 liquidate a portion of its LIFO storage inventory, much of which was priced at \$0.40 per
1055 Mcf.

1056 In a separate docket designed to set a GCR for 2002 (Docket No. U-13060),
1057 MPSC Staff argued that Mich Con’s decision to liquidate 19,000,000 Dth of storage in
1058 2001 violated the spirit of the order in Case No. U-11682. The MPSC Staff calculated a
1059 \$26,529,000 cost reduction to 2002 gas costs at issue in the proceeding based on the
1060 premise that Mich Con should have been in a position to withdraw 19,000,000 Dth of gas
1061 at the beginning of 2002. The ALJ recommended and the MPSC approved an adjustment
1062 to Mich Con’s 2002 GCR rate by adding 19,000,000 Dth of natural gas to Mich Con’s
1063 January 1, 2002 storage level to nullify the financial effect of Mich Con’s earlier decision

to liquidate 19,000,000 Dth of storage in 2001. This adjustment was approved by the MPSC. A copy of the order in Case No. U-13060 is included in Appendix A, Tab 10.

Q. DO ANY OF NICOR'S OTHER WITNESSES CITE PROCEEDINGS IN WHICH A UTILITY WAS ENTITLED TO RETAIN THE BENEFITS FROM THE LIQUIDATION OF LOW-COST LIFO INVENTORY?

A. Yes. In a data request, Witness Russell Feingold claims that Dominion Peoples, a gas utility in Pennsylvania, has proposed to liquidate a portion of its low-cost LIFO gas as part of its sale of a small underground storage facility (Appendix A, Tab 8, CF-1.9). He claims that one of the conditions of the sale is that all the proceeds from the sale of the gas in the storage facility accrue to Dominion Peoples' shareholders. I presented testimony in that proceeding, claiming that Dominion Peoples' proposal should be dismissed because the term and conditions of the sale were not established. Contrary to Mr. Feingold's claims, the Pennsylvania Commission agreed with my recommendation, thus nullifying the treatment that Dominion proposed regarding gains on the sale of gas in storage. Relevant portions of the Pennsylvania Commission's order in that proceeding are included in Appendix A, Tab 11.

Q. NICOR WITNESS FEINGOLD ALSO CLAIMS THAT THE ICC STAFF AND OTHER PARTIES TO NICOR'S GCPP SHOULD HAVE KNOWN ABOUT NICOR'S LOW-COST LIFO INVENTORY. DO YOU HAVE ANY COMMENTS?

A. Yes. This is another example of the "catch me if you can" theory of regulation embodied in Nicor's GCPP operations. This claim is also inconsistent with Nicor's conscious efforts to conceal its intentions to manipulate storage inventory to produce profits for

1089 itself. After all, if Staff and intervenors should reasonably have known of the Company's
1090 intentions, why would Nicor pursue a strategy of concealing such intentions? Moreover,
1091 storage fields are operated to maximize reliability at reasonable cost. Nicor's decision to
1092 manage its storage operations to produce profit levels was a new consideration for Nicor,
1093 and could not possibly have been known by Staff and intervenors unless revealed by
1094 Nicor. While Staff and the other intervenors may have known that Nicor used the LIFO
1095 method to value gas in storage, as do most gas utilities, this is not the issue. The issue is
1096 that it would not have reasonably been known that Nicor was going to liquidate low-cost
1097 gas that had been in storage as long ago as [REDACTED]. Stated alternatively, Nicor's low-cost
1098 LIFO inventory layers existed for over [REDACTED]. There was no reason to believe that the
1099 layers would be affected by the GCPP. The liquidation of LIFO layers by a gas utility
1100 dating back [REDACTED] is a very unusual event.

1101
1102 Q. WHAT IS YOUR RECOMMENDATION WITH RESPECT TO THE BENEFITS
1103 ASSOCIATED WITH THE LIQUIDATION OF LOW-COST LIFO
1104 INVENTORY?

1105 A. I recommend that 100 percent of the benefits associated with the liquidation of low-cost
1106 LIFO inventory be credited to ratepayers. As shown on GCI Exhibit 4.0, [REDACTED]
1107 [REDACTED]. In addition, in future base rate proceedings, I
1108 recommend that the ICC impute carrying costs for storage inventory as if Nicor had not
1109 liquidated its low-cost LIFO inventory. Implementation of both these recommendations
1110 is necessary to undo the adverse consequences to ratepayers of Nicor's liquidation of
1111 low-cost LIFO inventory, and to eliminate any benefit to Nicor from its decision to

1112 liquidate low-cost LIFO inventory which would result from the collection of higher
1113 carrying charges.
1114

1115 **B. Storage Prefills**

1116 Q. HOW WAS NICOR ABLE TO LIQUIDATE ITS LOW-COST LIFO
1117 INVENTORY?

1118 A. As discussed next in this section of my testimony, Nicor was able to liquidate low-cost
1119 LIFO inventory, some of which dated back to [REDACTED], through the sale of storage inventory.
1120 Nicor also liquidated its low-cost LIFO inventory by entering into storage prefill
1121 arrangements with third parties such as IMD.
1122

1123 Q. WHAT ARE STORAGE PREFILLS?

1124 A. Storage prefills are arrangements wherein a third-party injects gas into Nicor's on-system
1125 storage facilities, which Nicor then commits to purchase at a later time. Because the gas
1126 is owned by a third-party, the inventory is not considered Nicor's gas and, therefore, is
1127 not reflected on Nicor's books. This allowed Nicor to fill its storage facilities prior to the
1128 beginning of the winter season, and provided Nicor with the ability to access the low-cost
1129 LIFO inventory layers whose costs were recorded on Nicor's books. It was necessary for
1130 Nicor to fill its storage prior to the beginning of the winter season in order to reliably
1131 serve its customers.
1132

1133 Q. COULD YOU GIVE A SIMPLIFIED EXAMPLE AS TO HOW STORAGE
1134 PREFILLS ENABLED NICOR TO ACCESS LOW-COST LIFO INVENTORY?

1135 A. Yes. Say, for example, when filled, there are 100 units in Nicor's storage, and that every
1136 year Nicor cycles 40 units (i.e., 40 units are injected and withdrawn annually). This

would mean that there are 60 units in Nicor's continuing LIFO inventory layers. Further assume that all 60 units are priced significantly below current market prices.

If Nicor arranged for a storage prefill of 10 units during a particular injection season, when filled, Nicor's books would show storage inventory of only 90 units, since 10 units were owned by a third-party. When Nicor withdrew its typical 40 units, 10 units would be considered to come from low-cost LIFO inventory.

Q. HOW WERE STORAGE PREFILLS TREATED AFTER RESTATEMENT?

A. As explained beginning at page 61 of the Lassar Report, upon restatement, storage prefill volumes, in many instances, should have been considered part of Nicor's storage inventory. As such, the extent to which liquidation of low-cost LIFO inventory occurred was significantly reduced. [REDACTED]

[REDACTED]

[REDACTED].

1152 Q. ARE YOU PROPOSING ANY ADJUSTMENTS TO THE TREATMENT
1153 AFFORDED PREFILL ARRANGEMENTS AFTER RESTATEMENT?

1154 A. No. However, I would like to point out that when Nicor repurchased the storage prefill
1155 volumes from third-parties, it generally paid a price equal to the market price at the time
1156 the gas was injected, plus carrying, or interest charges. The interest charges were passed
1157 through the GCPP as a gas cost. Interest charges are not recoverable gas costs. While
1158 the inappropriate treatment of interest charges appears to have been addressed upon
1159 restatement, it reflects another example of Nicor attempting to manipulate its GCPP
1160 results.

1161

1162 C. **1999 Sale of DSS Storage to IMD**

1163 Q. PLEASE DESCRIBE THE 1999 SALE OF DSS STORAGE TO IMD.

1164 A. In 1999, Nicor purchased storage service from Natural Gas Pipeline Company of
1165 America (“NGPL”) under Rate Schedule DSS - Delivered Storage Service. In December
1166 1999, Nicor released its DSS storage capacity to IMD. Nicor also sold its gas in DSS
1167 inventory to IMD in December 1999. This sale was made at a loss of \$13.7 million,
1168 which was charged entirely to ratepayers. This sale was made to enable the Company to
1169 liquidate certain higher cost LIFO inventory so that once the GCPP began in 2000, the
1170 Company could access the low-cost LIFO inventory. This sale is discussed further in the
1171 Lassar Report beginning at page 20. The Lassar Report found this sale to be
1172 inappropriate, and I agree with this finding.

1173

1174 Q. IS AN ADJUSTMENT TO THE COMPANY’S RESTATED GCPP RESULTS
1175 APPROPRIATE DUE TO THIS TRANSACTION?

1176 A. No. On restatement, the transaction with IMD is not considered a sale, and Nicor's actual
1177 gas costs for 1999 have been reduced by the amount of the loss, resulting in a refund of
1178 \$13.7 million for ratepayers. As such, it appears that ratepayers have been compensated
1179 for this inappropriate transaction.

1180

1181 **D. Additional DSS and NSS Storage Withdrawals**

1182 Q. PLEASE DESCRIBE NICOR'S DSS AND NSS STORAGE ARRANGEMENTS
1183 DURING THE GCPP.

1184 A. Like DSS, NSS ("Nominated Storage Service") is a storage service which Nicor
1185 purchased from NGPL. Under the GCPP, a Storage Credit Rate was applied to volumes
1186 withdrawn by Nicor from DSS and NSS storage to calculate a Storage Credit Adjustment
1187 ("SCA"), which was subtracted from the Benchmark. Thus, under typical conditions
1188 wherein winter gas prices are higher than summer gas prices, the withdrawal of gas from
1189 storage would reduce the Benchmark, thereby making it more difficult for Nicor to
1190 generate savings under the GCPP. To eliminate the Benchmark decreasing impact of the
1191 SCA, Nicor entered into "managed" storage arrangements with third-parties. Generally,
1192 under these arrangements, Nicor released its DSS and NSS storage capacity to a third-
1193 party which filled the released storage. Prior to restatement, when the gas was
1194 withdrawn, it was considered to be withdrawn by the third-party, not Nicor. As such,
1195 these withdrawals were not included in calculating the SCA, because the purchases were
1196 considered flowing supplies (defined as gas not originating from storage). This is further
1197 explained by the Company in the document found in Appendix A, Tab 12, NIC 3205.
1198 Nicor would then purchase this gas after it was withdrawn, using it to serve ratepayers.

1199 Nicor received payments under these arrangements from the third-party representing the
1200 benefits obtained from winter/summer price spreads which existed at the time the
1201 arrangements were entered into. As a result, prior to restatement, Nicor's actual gas costs
1202 were reduced by the winter/summer price spread, but the winter/summer price spread was
1203 not reflected in the Benchmark as explained by the Company:

1204
1205
1206
1207
1208
1209
1210
1211
1212
1213
1214
1215



1216 Q. DID THE RESTATEMENT CHANGE THE TREATMENT AFFORDED THE
1217 DSS AND NSS WITHDRAWALS INITIALLY EXCLUDED FROM THE
1218 CALCULATION OF THE SCA?

1219 A. Yes. Upon restatement, certain DSS and NSS volumes have been included in the
1220 calculation of the SCA, while others have not. Nicor's direct testimony on restatement
1221 does not address the continued exclusion of DSS and NSS volumes from the calculation
1222 of the SCA.

1223

1224 Q. IN YOUR OPINION, WAS IT REASONABLE FOR NICOR TO EXCLUDE
1225 GAS PURCHASED UNDER ITS MANAGED STORAGE ARRANGEMENTS
1226 FROM THE CALCULATION OF THE STORAGE CREDIT ADJUSTMENT?

1227 No. The SCA was intended to reflect the benefit that ratepayers traditionally received
1228 by Nicor's injection of lower cost gas into storage during the summer and the withdrawal
1229 of that gas during the winter when market prices were higher. Under Nicor's managed
1230 storage arrangements, gas was still injected into storage during the summer and
1231 withdrawn during the winter, and a seasonal price benefit was realized. However, this
1232 seasonal price benefit was credited against Nicor's actual gas costs. It was not reflected
1233 in the SCA component of the Benchmark. The SCA was designed to give ratepayers
1234 100 percent of the seasonal price benefit they enjoyed under traditional regulation. By
1235 excluding gas under its managed storage arrangements from the calculation of the SCA,
1236 Nicor manipulated the Benchmark and its GCPP results.

1237
1238 Q. ARE YOU PROPOSING AN ADJUSTMENT TO NICOR'S RESTATED GCPP
1239 RESULTS?

1240 A. Yes. Although some of the DSS and NSS volumes initially treated as flowing gas prior
1241 to restatement are now considered storage withdrawals, certain volumes continue to be
1242 treated as flowing volumes. I am adjusting Nicor's GCPP results to include all DSS and
1243 NSS withdrawals in the calculation of the SCA. As shown on GCI Exhibit 5.0, this
1244 results in a \$9.3 million credit to ratepayers.

1245 **E. Virtual Storage**

1246 Q. PLEASE EXPLAIN THE VIRTUAL STORAGE ISSUE.

1247 A. As just explained, it was expected that the SCA would decrease the Benchmark against
1248 which Nicor's performance would be compared under the GCPP to reflect the seasonal
1249 price benefit of storage. As also just discussed, Nicor attempted to circumvent this effect
1250 by entering into managed storage arrangements with third-parties which treated DSS and
1251 NSS withdrawals as flowing supplies. In early 2000, Nicor had entered into such an
1252 arrangement with IMD for its DSS withdrawals. At that time it was expected that the
1253 SCA would be positive, meaning winter prices would exceed summer prices and it would
1254 be to Nicor's benefit to reduce withdrawal quantities. However, as 2000 progressed, it
1255 became evident that the SCA would be inverted. That is, summer prices were going to
1256 exceed winter prices and storage withdrawals would increase the Benchmark. Thus,
1257 Nicor's scheme to circumvent the SCA was having the opposite impact. In response, in
1258 September 2000, the Company modified its treatment of DSS withdrawals so that these
1259 volumes were once again considered to be storage withdrawals. These storage
1260 withdrawals were deemed to be "virtual storage." The virtual storage issue is discussed
1261 further in the Lassar Report beginning at page 27.

1262

1263 Q. ARE YOU PROPOSING AN ADJUSTMENT TO NICOR'S GCPP RESULTS
1264 FOR VIRTUAL STORAGE?

1265 A. No. On restatement, the DSS volumes under Nicor's arrangement with IMD in 2000 are
1266 now all considered storage withdrawals. I have addressed this issue to highlight another
1267 example of Nicor's deceptive, manipulative, and self-serving behavior.

1268 **F. Weather Insurance Purchase**

1269 Q. BRIEFLY DISCUSS THE COMPANY'S PURCHASE OF A WEATHER
1270 ISSUANCE PRODUCT.

1271 A. Weather insurance is a financial derivative product designed to help a utility recover lost
1272 revenue resulting from in Nicor's case, warmer-than-normal weather. Nicor purchased a
1273 weather insurance product from Aquila for fiscal 2001. The total cost of the insurance
1274 was \$3.5 million. A portion of the purchase price, \$2.0 million, was to be paid by
1275 Nicor's selling of gas to Aquila at a discount to market prices. This arrangement was
1276 executed in the Fall of 2000, and provided for the delivery of the discounted gas to
1277 Aquila in March and April 2001. Additional detail describing this arrangement can be
1278 found in the Lassar Report beginning at page 40.

1279

1280 Q. WHAT DID THE LASSAR REPORT CONCLUDE CONCERNING THE
1281 AQUILA TRANSACTION?

1282 A. The Lassar Report concluded that the Aquila transaction as structured was clearly
1283 improper. It noted that when the deal was executed, the amount of the discount to Aquila
1284 was \$2 million; however, when the gas was eventually delivered, the actual amount of the
1285 discount was approximately \$6.2 million, of which ratepayers were required to absorb
1286 one-half.

1287

1288 Q. DO YOU AGREE WITH THE LASSAR REPORT THAT THE AQUILA
1289 TRANSACTION WAS IMPROPER?

1290 A. Yes. The effect of the Aquila transaction was to include a portion of the cost of the
1291 weather insurance product as a recoverable gas cost under the GCPP. Since this is not a

1292 recoverable gas cost, this transaction was improper. [REDACTED]

1293 [REDACTED]

1294 [REDACTED]

1295

1296 Q. HOW WAS THE AQUILA TRANSACTION REFLECTED IN THE
1297 COMPANY'S RESTATEMENT?

1298 A. The restated results adjusted ratepayer costs for the initial \$2 million discount.

1299

1300 Q. IN YOUR OPINION, IS THE RESTATEMENT ADJUSTMENT
1301 REASONABLE?

1302 A. No, the adjustment is not sufficient. It is undisputed that the Aquila transmission was
1303 improperly structured. The amount of the discount associated with the below market sale
1304 was \$6.2 million. Because the Aquila transaction was clearly improper, ratepayers
1305 should bear no responsibility for the discount. GCI Exhibit 6.0 adjusts GCPP results and
1306 costs to eliminate all ratepayer responsibility for the \$6.2 million discount.

1307

1308 **G. In-Field Storage Transfers**

1309 Q. PLEASE EXPLAIN THE IN-FIELD STORAGE TRANSFER ISSUE.

1310 A. Gas withdrawn from Nicor's storage facilities is typically delivered to serve ratepayers.
1311 However, gas can also be withdrawn from one storage field and injected into another.
1312 These later transactions are referred to as in-field storage transfers. Under the GCPP, gas
1313 withdrawn from storage which is delivered to ratepayers is used to compute the Storage
1314 Credit Adjustment.

1315 Prior to 2000, and in 2000, the first year of the GCPP, Nicor did not keep track of
1316 in-field storage transfers. It was not in Nicor's interest to do so in 2000 because, as
1317 previously explained, the Storage Credit Rate was inverted. That is, Nicor's performance
1318 under the GCPP was enhanced by including in-field transfer storage withdrawals in the
1319 calculation of the SCA.

1320 In 2001, the SCA was positive, and significant (\$2.7503 per Dth). Thus, each Dth
1321 of gas withdrawn from storage to serve ratepayers had the effect of significantly lowering
1322 the Benchmark by \$2.7503. In 2001, the average cost of gas purchased by Nicor was
1323 \$5.36 per Dth. Therefore, it was in Nicor's interest to track in-field transfers to reduce
1324 storage withdrawals. To keep track of in-field transfers, Nicor adopted a "netting"
1325 approach. Under this approach, by way of example, if Nicor withdrew 5 units from its
1326 storage facilities on a particular day, but also injected 2 units, the assumption was that 3
1327 units were delivered to ratepayers. The in-field storage transfer issue is discussed in
1328 greater detail beginning at page 49 of the Lassar Report.

1329
1330 Q. WHAT DID THE LASSAR REPORT CONCLUDE WITH RESPECT TO IN-
1331 FIELD STORAGE TRANSFERS?

1332 A. The Lassar Report noted that the Company did not use a consistent method for tracking
1333 and reporting in-field storage transfers. The Lassar Report identifies two approaches in
1334 which this issue could be addressed. Under the first, netting would be applied for all of
1335 2000 and 2001. This approach would result in a refund of \$3.45 million. Under the
1336 second approach, because Nicor did not uniformly keep track of in-field transfers and
1337 they are not mentioned under the GCPP, no in-field storage transfers should be
1338 recognized. The Lassar Report recommended application of the first approach.

1339

1340 Q. WHAT IS THE COMPANY'S POSITION WITH RESPECT TO IN-FIELD
1341 TRANSFERS?

1342 A. In its restatement, the Company has adopted the approach recommended in the Lassar
1343 Report.

1344

1345 Q. SHOULD IN-FIELD STORAGE TRANSFER VOLUMES BE REFLECTED IN
1346 THE CALCULATION OF THE SCA?

1347 A Yes, for a number of reasons. As noted in the Lassar Report, the GCPP does not mention
1348 in-field storage transfers and Nicor did not consistently track these transfers. In addition,
1349 as also explained in the Lassar Report, the storage weightings developed for the SCA
1350 component of the GCPP included in-field transfers. Therefore, although not explicitly
1351 discussed in the GCPP, in-field storage transfers were included in the SCA component of
1352 the GCPP approved in Docket No. 99-0127.

1353 Moreover, as previously explained, the Commodity Adjustment adjusted the
1354 Benchmark to reflect historical variations between the Market Index cost and the
1355 Company's actual gas costs after removing the variation accounted for by the Storage
1356 Credit Adjustment and the Firm Deliverability Adjustment. That is, it corrected for
1357 differences between Nicor's actual gas costs and the Benchmark on a historical basis to
1358 remove any bias which may be present. The Company's netting approach was not used
1359 to calculate the Commodity Adjustment. If it had, the Commodity Adjustment would
1360 have been less than the \$0.0168 cents established in Docket No. 99-0127. Thus, the
1361 Benchmark would have been lower, meaning it would have been more difficult for Nicor
1362 to achieve savings. It is unreasonable and inconsistent to now adopt a netting approach

for storage withdrawals without also considering the impact this approach would have had on the Commodity Adjustment. In rebutting my testimony in Docket No. 96-0386, Nicor witness Edwin Werneke claimed that one of my proposed changes to the calculation of the Benchmark was inappropriate because it failed to consider the impact of the change on other components of the Benchmark, such as the Commodity Adjustment (Rebuttal at 3-4).

Q. PLEASE EXPLAIN WHY THE COMMODITY ADJUSTMENT WOULD HAVE BEEN LESS IF NETTING WAS UTILIZED.

A. On a historical basis, Nicor's actual gas costs exceeded calculated Benchmark gas costs, hence the positive Commodity Adjustment. If netting had been applied on a historical basis, storage withdrawal quantities would have been lower and, therefore, the impact of the Storage Credit Adjustment would have been less, meaning the calculated Benchmark gas costs would have been greater. Because calculated Benchmark gas costs would have been greater, the Commodity Adjustment would have had to of been lower so that actual gas costs and calculated Benchmark gas costs would have been equal on a historical basis.

Q. HAVE YOU PREPARED AN ADJUSTMENT TO NICOR'S PERFORMANCE UNDER THE GCPP TO REMOVE THE IMPACT OF THE COMPANY'S NETTING APPROACH?

A. Yes. As shown on GCI Exhibit 7.0, adjusting the SCA to remove the impact of the netting approach results in an \$11.1 million refund for ratepayers.

1387 Q. ARE THERE OTHER REASONS WHY THE NETTING APPROACH
1388 SHOULD NOT BE ADOPTED FOR PURPOSES OF COMPUTING THE SCA?

1389 A. Yes. As discussed in greater detail in the next issue, in Docket Nos. 96-0386 and 99-
1390 0127, Nicor claimed that it could not manipulate storage withdrawals. In my opinion,
1391 transferring gas from one storage field to another to avoid having to withdraw gas is an
1392 extreme case of storage withdrawal manipulation.

1393

1394 **H. Manipulation of Storage Withdrawals**

1395 Q. PLEASE EXPLAIN YOUR CONCERN WITH RESPECT TO THE
1396 MANIPULATION OF STORAGE WITHDRAWALS.

1397 A. In Docket Nos. 96-0386 and 99-0127, the Company claimed that storage withdrawals
1398 were a function of weather and operational requirements. The Company claimed that it
1399 could not manipulate storage to its benefit under the GCPP. Here again the Company
1400 misinformed the Commission because it was able to significantly affect storage
1401 withdrawals during the GCPP as shown below (inclusive of in-field transfers):

1402

1402

Year	Withdrawals (Dth)

1403

1404 Q. WHAT DID THE COMPANY SPECIFICALLY SAY IN DOCKET NOS. 96-
1405 0386 and 99-0127 CONCERNING ITS ABILITY TO MANIPULATE
1406 STORAGE ACTIVITY?

1407 A. In Docket Nos. 96-0386 and 99-0127, the Company and its witnesses made the following
1408 statements:
1409

1410 Witness Edwin Werneke: "On the other hand, the Company has
1411 very limited ability to adjust the timing of storage withdrawal
1412 volumes, which are determined largely by weather and operational
1413 requirements," (Docket No. 99-0127, Direct at 10).
1414

1415 Witness Edwin Werneke: "Second, Mr. Mierzwa apparently
1416 believes that the Company has wide discretion with respect to its
1417 storage injection and withdrawal cycle, and can therefore accelerate
1418 or defer gas purchases at will. In fact, the Company's discretion
1419 with respect to inter-month storage injections and withdrawals is
1420 limited, reflecting the physical characteristics of the Company's
1421 aquifer storage fields and contractual limitations on purchased
1422 storage," (Docket No. 96-0386, Rebuttal at 3).
1423

1424 Witness Leonard Gilmore: "the Company cannot shift inventory
1425 withdrawals without impacting its design peak day capabilities and
1426 overall storage field performance. Consequently, even if the
1427 Company could predict prices such that it could gain from shifting
1428 withdrawals, it would be a bad business decision for the Company
1429 to do so," (Docket No. 99-0127, Surrebuttal at 4).

1430 “Nicor states...it has very limited ability to adjust the timing of
1431 storage withdrawals, which are largely determined by weather and
1432 operational requirements and therefore cannot be manipulated,”
1433 (Docket No. 99-0127, Order at 8).

1434
1435 In addition, in Docket No. 99-0127, Staff claimed that under certain circumstances, the
1436 SCA could give the Company an incentive to create false savings by shifting withdrawals
1437 to months when Market Index Prices were low, and meet demand with current purchases
1438 when Market Index Prices are high. By doing so, Staff claimed that the Company could
1439 reduce the Storage Credit Rate and raise the Benchmark, thereby enabling the Company
1440 to share in greater “savings” or fewer “losses.” The net result could be an increase in the
1441 cost of gas to ratepayers.

1442
1443 In response, the Company argued:

1444 In addition, Nicor Gas disputes Staff’s assertion that the Storage
1445 Credit Adjustment creates an incentive for the Company to shift
1446 withdrawals. The Company states that in order for it to manipulate
1447 the system as Staff suggests, the Company would have to be able to
1448 predict Market Index Prices, actual variable commodity costs, and
1449 the relative difference between the two and do so for multiple
1450 monthly periods. The Company denies having any ability to make
1451 such accurate predictions. According to the Company, to the
1452 degree that it currently makes estimates regarding future gas prices,
1453 those estimates are made for financial planning purposes and not for
1454 the timing of gas purchases. The Company states that the examples
1455 Staff used purportedly to show that shifting could occur were
1456 developed only with the benefit of 20/20 hindsight.

1457 Moreover, the Company states that the steps it would need to
1458 take to manipulate the system as Staff suggests would, in fact, be
1459 bad business decisions. For instance, the Company states that the
1460 timing of withdrawals is largely determined by weather and,
1461 operational requirements. As such, the Company states that peak
1462 day delivery could be impaired if the Company were to alter the
1463 timing of withdrawals arbitrarily. Likewise, the Company states

1464 that required inventory cycling could be adversely by delaying
1465 withdrawals, which could affect deliverability negatively in the
1466 succeeding heating season. The Company states that because it is
1467 required to provide reliable service, tinkering with the operational
1468 characteristics, which could have a negative impact on the
1469 performance of storage fields, would not be a sound business
1470 practice. For this reason, the Company concludes that it would
1471 have compelling incentives not to abuse the system in the manner
1472 Staff suggests (even if it were able to do so).

1473 The Company added that any action that would increase the
1474 customer's cost would be contrary to its long-term business
1475 objectives. For example, the first stated objective in Nicor's
1476 Petition in this proceeding is to "align the interests of ratepayers and
1477 the Company by providing customers with the best prices
1478 available." (Petition at 3.) The Company claims that it specifically
1479 structured its calculation of the Storage Credit Adjustment in order
1480 to pass along to customers the full seasonal benefit from storage."
1481 (Gilmore Rebuttal at 4). Nicor Gas indicates that Staff offered no
1482 evidence to contradict this testimony. (Order at 15).
1483

1484 Q. DID THE COMPANY MAKE DECISIONS TO ADJUST STORAGE
1485 WITHDRAWALS DURING THE GCPP WHICH INCREASED COSTS TO
1486 CUSTOMERS?

1487 [REDACTED]
1488 [REDACTED]
1489 [REDACTED]
1490 [REDACTED]
1491 [REDACTED]

1492 [REDACTED]

1493 [REDACTED]

1494 [REDACTED]

1495 [REDACTED]

1496 [REDACTED]

1497 [REDACTED]

1498 [REDACTED]

1499 [REDACTED]

1500 [REDACTED]

1501 [REDACTED]

1502 [REDACTED]. Based on the criteria set forth by Nicor in Docket

1503 No. 99-0127, this was a bad business decision.

1504

1505 Q. DO YOU HAVE OTHER EXAMPLES WHERE NICOR ADJUSTED
1506 STORAGE WITHDRAWALS FOR ITS BENEFIT TO THE DETRIMENT OF
1507 RATEPAYERS?

1508 A. Yes. [REDACTED]

1509 [REDACTED]

1510 [REDACTED]

1511 [REDACTED]

1512 [REDACTED]

1513 [REDACTED]




1514 [REDACTED].

1515 Q. IN YOUR OPINION, IS AN ADJUSTMENT TO NICOR'S STORAGE
1516 WITHDRAWALS UNDER THE GCPP APPROPRIATE?

1517 A Yes. In Docket No. 99-0127, Nicor represented to the ICC that it had little ability to
1518 adjust storage withdrawals, and that storage withdrawals were driven by weather and
1519 operational concerns. [REDACTED].

1520 [REDACTED] Clearly,

1521 Nicor had the ability to shift withdrawals, contrary to its representations to the ICC.

1522 Therefore, annual storage withdrawals, the Storage Credit Adjustment, and subsequently
1523 Nicor's performance under the GCPP should be based on the Company's initial
1524 representations concerning its inability to manipulate withdrawal storage quantities. 
1525 
1526 .

1527

1528 Q. WHAT DID THE DEPOSITIONS OF COMPANY PERSONNEL REVEAL
1529 WITH RESPECT TO THE MANIPULATION OF STORAGE
1530 WITHDRAWALS?

1531
1532
1533
1534
1535
1536
1537
1538
1539
1540
1541



1542
1543
1544
1545
1546
1547
1548
1549
1550
1551
1552
1553
1554
1555
1556
1557
1558
1559
1560
1561



1562

1563 Q. HAVE YOU DEVELOPED AN ADJUSTMENT?

1564 A Yes. GCI Exhibit 8.0 adjusts Nicor's performance to reflect what the Company testified
1565 to before the ICC in Docket No. 99-0127 with respect the ability the manipulate storage
1566 withdrawals. To be conservative, my adjustment imputes storage withdrawals for 2001
1567 based on the lowest quantity of withdrawals from storage during the period 1994-1999.
1568 This occurred in 1996. [REDACTED]

1569

[REDACTED].

1570

1571 **I. Management Fees**

1572 Q. PLEASE DESCRIBE THE STORAGE MANAGEMENT FEES PAID BY
1573 NICOR.

1574 A. Nicor engaged IMD to develop strategies utilizing its on-system storage and the contract
1575 storage purchased from NGPL (DSS and NSS) to generate revenues under the GCPP.
1576 Nicor paid management fees to IMD for its services. These fees were included as a cost
1577 of gas under the GCPP. [REDACTED]
1578 [REDACTED].

1579

1580 Q. IN YOUR OPINION, SHOULD THESE FEES BE RECOVERED FROM
1581 RATEPAYERS?

1582 A. No. As previously explained, these fees were paid to develop strategies to assist Nicor in
1583 manipulating its GCPP results. Therefore, these fees should not be recovered from
1584 ratepayers. GCI Exhibit 9.0 adjusts GCPP results accordingly.

1585

1586 **J. Interest Charges**

1587 Q. WHAT IS NICOR'S PROPOSAL WITH RESPECT TO THE COLLECTION OF
1588 INTEREST?

1589 A. Nicor is proposing to charge ratepayers interest on the amounts it claims it is owed by
1590 ratepayers. As shown on Attachment TMM-3 to the Direct Testimony on Reopening of
1591 Thomas M. Moretti, Nicor is proposing to charge ratepayers \$2,161,067 interest as a
1592 result of its restatements for 2001, and \$126,449 in interest related to restated results in
1593 2002.

1594 Q. IN YOUR OPINION, IS THIS REASONABLE?

1595 A. No. Ratepayers should not be required to pay interest to Nicor. As explained in my
1596 testimony, Nicor owes ratepayers a refund. Ratepayers do not owe Nicor money.
1597 Therefore, there is no basis to calculate interest. In addition, the prior undercollections
1598 upon which Nicor claims interest is due are attributable to Nicor's misleading, deceptive
1599 and manipulative practices and behavior. Ratepayers should not be required to pay
1600 interest because Nicor elected to pursue such practices and behavior.

1601

1602 **K. Tennessee and Midwestern Capacity Costs**

1603 Q. WHAT IS THE ISSUE ASSOCIATED WITH TENNESSEE AND
1604 MIDWESTERN CAPACITY COSTS?

1605 A. Nicor relies on interstate pipelines Tennessee Gas Pipeline and Midwestern Gas
1606 Transmission to deliver gas to meet a portion of its sales customers' requirements. At the
1607 time Nicor filed its application in Docket No. 99-0127, the Company's existing firm
1608 transportation arrangements with Tennessee and Midwestern were scheduled to expire in
1609 October 2000. During 1999, the Company entered into negotiations with Tennessee and
1610 Midwestern to extend its capacity arrangements beyond October 2000. Among those
1611 items subject to negotiation were the rates to be effective beyond October 2000. Nicor's
1612 capacity arrangements with NGPL, its primary interstate pipeline supplier, were also
1613 subject to negotiation in 1999. When Nicor filed its application in Docket No. 99-0127,
1614 the Firm Deliverability Adjustment was based on what Nicor's actual costs for 1998, and
1615 the Company indicated that it would update its cost projections to reflect the results of its
1616 negotiations. In July 1999, Nicor filed its updated transportation and storage cost
1617 projections to reflect the final results of its negotiations with NGPL. However, the

1618 projections for Tennessee and Midwestern continued to reflect estimates since these
1619 negotiations had not been completed.

1620 In its oral argument before the ICC on November 2, 1999, the Company claimed
1621 that its Tennessee and Midwestern contracts were still being negotiated (Tr. 20). This
1622 was misleading because the Company had finalized its agreements with Tennessee and
1623 Midwestern on [REDACTED]. The Company should have informed the ICC that an
1624 agreement on rates had been achieved rather than implying the rates remained subject to
1625 negotiation.

1626
1627 Q. IN YOUR OPINION, IS AN ADJUSTMENT TO NICOR'S PERFORMANCE
1628 UNDER THE GCPP WARRANTED DUE TO NICOR'S FAILURE TO
1629 INFORM THE ICC THAT IT HAD REACHED AN AGREEMENT WITH
1630 TENNESSEE AND MIDWESTERN?

1631 A. Yes. Nicor should not earn rewards under the GCPP because it misrepresented the facts
1632 and concealed critical information from its regulators concerning its future transportation
1633 and storage costs which served as the basis for the Firm Deliverability Adjustment
1634 component of the GCPP. GCI Exhibit 10.0 adjusts the Firm Deliverability Adjustment
1635 and Nicor's performance to reflect the rates agreed to by Nicor, Tennessee and
1636 Midwestern. As shown there, this results in a refund of \$3,554,559 to ratepayers.

1637

1638 **L. Accounts Payable Reversal**

1639 Q. PLEASE EXPLAIN THE ISSUE WITH RESPECT TO THE ACCOUNTS
1640 PAYABLE REVERSAL.

1641 A. On occasion, Nicor purchases gas from a supplier, but the supplier fails to invoice Nicor
1642 for the gas. In such instances, Nicor will initially enter an account payable on its books.

1643
1644
1645
1646
1647
1648
1649
1650

1651
1652 Q. IN YOUR OPINION, IS THIS APPROPRIATE?

1653
1654
1655
1656

1657

1658 **M. Below Market Sale to Affiliate**

1659 Q. DID NICOR SELL GAS TO AN AFFILIATE AT BELOW MARKET PRICES?

1660 A. Yes. During January 2000, Nicor sold gas to its affiliate, Enerchange, at less than the
1661 market price (Appendix A, Tab 19).

1662

1663 Q. WAS THIS APPROPRIATE?

1664 A. No. This resulted in higher costs to ratepayers because Nicor did not maximize its profit
1665 on the sale, which is subsequently shared with ratepayers under the GCPP. GCI Exhibit
1666 13.0 adjusts Nicor's performance under the GCPP to eliminate the adverse impact of this
1667 transaction on ratepayers. As shown there, this results in a refund of \$372,000 to
1668 ratepayers.

1669

1670 N. **2002 GCPP Reward**

1671 Q. AFTER CONSIDERING ALL OF YOUR ADJUSTMENTS TO NICOR'S
1672 PERFORMANCE, DOES NICOR EARN A REWARD UNDER THE GCPP IN
1673 2002?

1674 A. Yes. Nicor earns a reward of \$16,970,310.

1675

1676 Q. IN YOUR OPINION, IS IT APPROPRIATE FOR NICOR TO EARN A
1677 REWARD OF \$17.0 MILLION FOR 2002?

1678 A. No. The ICC was reviewing the results of the GCPP for 2000 and 2001 when the
1679 whistleblower fax surfaced. The purpose of the review was to determine if the GCPP
1680 was operating as intended. As subsequently explained, the GCPP was clearly not
1681 operating as intended. Moreover, I cannot imagine the ICC allowing Nicor to continue to
1682 operate under the GCPP if it had known during the review proceeding of Nicor's
1683 deceptions, manipulations and concealment of relevant facts that has been revealed since
1684 the whistleblower fax surfaced. Therefore, it is reasonable to expect that the GCPP
1685 would have been terminated after the first two years. After much work and cost to

participants to uncover Nicor's inappropriate and self-serving activities under the GCPP, the Company should not now realize a reward under the GCPP because the procedural schedule had been extended in order to investigate Nicor's misleading, deceptive and manipulative practices. GCI Exhibit 14.0 adjusts GCPP results accordingly, returning \$17.0 million to ratepayers.

Q. PLEASE EXPLAIN YOUR COMMENT THAT THE GCPP WAS NOT OPERATING AS INTENDED.

The GCPP was required to satisfy certain standards prior to its approval by the ICC. The standards which the GCPP was required to satisfy are identified in Section 9-244 of the Illinois Public Utilities Act. Section 9-244 requires that in reviewing or assessing alternatives to rate of return regulation that reward or penalize utilities based on performance, the Commission shall approve such programs if it finds that:

- (1) the program is likely to result in rates lower than otherwise would have been in effect under traditional rate of return regulation for the services covered by the program and that are consistent with the provisions of Section 9-241 of the Act;
- (2) the program is likely to result in other substantial and identifiable benefits that would be realized by customers served under the program and that would not be realized in the absence of the program;
- (3) the utility is in compliance with applicable Commission standards for reliability and implementation of the program is not likely to adversely affect service reliability;
- (4) implementation of the program is not likely to result in deterioration of the utility's financial condition;
- (5) implementation of the program is not likely to adversely affect the development of competitive markets;
- (6) the electric utility is in compliance with its obligation to offer delivery services pursuant to Article XVI;

- 1721
- 1722 (7) the program includes annual reporting requirements and other provisions that
- 1723 will enable the Commission to adequately monitor its implementation of the
- 1724 program; and
- 1725
- 1726 (8) the program includes provisions for an equitable sharing of any net economic
- 1727 benefits between the utility and its customers to the extent the program is
- 1728 likely to result in such benefits.
- 1729

1730 Cleary, as already addressed, the GCPP violated standards 1, 4, and 8 because it did not

1731 result in rates that were lower than would have otherwise been achieved, resulted in the

1732 deterioration of the Company's financial condition, and the sharing provisions were not

1733 equitable.

1734 In addition, as explained in detail in the testimony I have already submitted in

1735 Docket No. 02-0067, the Storage Credit Adjustment was not operating as intended and

1736 therefore, the GCPP was flawed. The whistleblower fax and subsequent investigation has

1737 not changed this.

1738 Finally, the review in Docket No. 02-0067 was conducted to determine whether

1739 the GCPP was achieving its objectives. The first of those stated objectives were to:

1740

1741 Align the interests of ratepayers and the Company by

1742 providing the appropriate incentives for Nicor Gas to improve

1743 its performance in providing customers with the best gas

1744 prices available, while recognizing the need for continued

1745 reliability and security of supply.

1746

1747 As previously discussed, the interests of Nicor and ratepayers were not aligned

1748 under the GCPP because of the conflicting incentives existing in the design of the Storage

1749 Credit Adjustment.

1750

1751 **VII. Implication of GCPP Activities on Nicor's 2003 Purchased Gas Costs**

1752 Q. WILL NICOR'S ACTIVITIES UNDER THE GCPP HAVE AN IMPACT ON
1753 GAS COSTS IN 2003?

1754 A. Potentially, yes.

1755 In doing so, Nicor may have acted imprudently, failing to
1756 husband storage for use during the later part of the 2002-2003 heating season.

1757

1758 These could have potentially adversely affected the Company's gas costs and ratepayers.

1759

1760 Q. DID YOUR INVESTIGATION REVEAL OTHER ASPECTS OF NICOR'S
1761 GAS PROCUREMENT PRACTICES WHICH SHOULD BE INVESTIGATED?

1762 A. Yes.

1763

1764

1765

1766

1767

1768

1769

1770

1771

VIII. Response to Company Direct on Reopening on Additional Issues

1772

Q.

ARE THERE ANY ADDITIONAL ISSUES DISCUSSED IN THE

1773

COMPANY'S DIRECT TESTIMONY ON REOPENING TO WHICH YOU

1774

WOULD LIKE TO RESPOND?

1775

A.

Yes. Nicor witness Feingold claims that ratepayers achieved significant benefits under

1776

the GCPP due to the design of the Benchmark. More specifically, he claims that for the

1777

period 2000 – 2002, Nicor was required to lower its gas costs by \$29 million each year

1778

below those levels which would have been achieved under traditional regulation just to

1779

meet the Benchmark. He refers to this as “stretch factor.” This is misleading at best and

1780

meaningless.

1781

The Benchmark was designed to reflect what Nicor's gas cost would have been

1782

under traditional regulation during 2000 and 2001. Witness Feingold's claim is based on

1783

how Nicor would have performed under the GCPP had it been in place during the period

1784

1994 – 1999. During this period Nicor's annual supply, transportation, and storage

1785

reservation charges declined from [REDACTED], due to, among other

1786

things, increased competition in the gas procurement markets. Witness Feingold's claim

1787

implies that the GCPP approved for 2000 and 2001 would have been approved for the

1788

period 1994 – 1999. The Benchmark approved for 2000 and 2001 included

1789

transportation and storage reservation charges of \$124.8 million. It is beyond reason to

1790

think that the Company would accept a PBR for 1994 which had a Benchmark of \$124.8

1791 million for transportation and storage reservation charges at a time those charges were

1792 [REDACTED]. Therefore, witness Feingold's claim should be dismissed.

1793

1794 Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY ON REOPENING?

1795 A. Yes, it does at this time. However, it may be necessary to supplement my testimony

1796 upon the receipt and analysis of any discovery not received within sufficient time to be

1797 analyzed prior to the filing of my testimony.

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

Illinois Commerce Commission)	
on its own motion)	
)	Docket No. 01-0705
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Reconciliation of Revenues collected under)	
Gas Adjustment Charges with Actual Costs)	
prudently incurred)	
)	
Illinois Commerce Commission)	
on its own motion)	
)	
)	Docket No. 02-0067
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Proceeding to review Rider 4, Gas Cost, pursuant)	
to Section 9-244(c) of the Public Utilities Act)	
)	
Illinois Commerce Commission)	
on its own motion)	
)	Docket No. 02-0725
Northern Illinois Gas Company d/b/a NICOR)	
Gas Company)	
Reconciliation of Revenues collected under)	
Gas Adjustment Charges with Actual Costs)	
prudently incurred)	

REDACTED

**REBUTTAL TESTIMONY ON REOPENING OF JEROME D. MIERZWA
ON BEHALF OF THE CITIZENS UTILITY BOARD AND THE COOK COUNTY
STATE'S ATTORNEY'S OFFICE (GCI)**

FEBRUARY 27, 2004

TABLE OF CONTENTS

	<u>Page</u>
I. Introduction	1
II. Witness Russell A. Feingold	2
III. Witness Michael E. Barrett	27
IV. Witness Theodore J. Lenart	32
V. Witness Albert E. Harms	38
VI. Other	43

I. Introduction

Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?

A. My name is Jerome D. Mierzwa. I am a principal and a vice president of Exeter Associates, Inc. My business address is 5565 Sterrett Place, Suite 310, Columbia, Maryland 21044. Exeter specializes in providing public utility-related consulting services.

Q. HAVE YOU PREVIOUSLY PRESENTED TESTIMONY IN THIS PROCEEDING?

A. Yes. My direct testimony on reopening was filed with the ICC on November 21, 2003.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to respond to the rebuttal testimony on reopening presented by Company witnesses Russell A. Feingold, Michael E. Barrett, Theodore J. Lenart and Albert E. Harms.

Q. HOW IS YOUR REBUTTAL ORGANIZED?

A. My rebuttal testimony addresses each witness individually except in instances where multiple witnesses address common issues.

II. Witness: Russell A. Feingold

**Q. A CONSISTENT CLAIM MADE BY WITNESS FEINGOLD
THROUGHOUT HIS REBUTTAL TESTIMONY IS THAT THE
ADJUSTMENTS YOU HAVE PROPOSED TO NICOR'S
PERFORMANCE UNDER THE GCPP CONSTITUTE RETROACTIVE
RATEMAKING AND THAT RETROACTIVE RATEMAKING IS NOT
APPROPRIATE. WHAT IS YOUR RESPONSE TO THIS CLAIM?**

A. First, it is Nicor that has had to make retroactive adjustments to its performance under the GCPP due to its inappropriate activities. In addition, the Second Interim Order in this proceeding issued on December 17, 2002, provided that all issues related to the operation of Nicor's GCCP would be litigated in this proceeding. Therefore, retroactive ratemaking is permitted in this proceeding. Furthermore, it is my opinion that in instances where a utility has withheld information from the Commission in the ratemaking process, retroactive ratemaking is appropriate.

**Q. WHAT IS THE BASIS FOR YOUR POSITION THAT RETROACTIVE
RATEMAKING IS APPROPRIATE IN THIS PROCEEDING?**

A. From a policy standpoint, witness Feingold's position is untenable. Under witness Feingold's position, the Commission would have no recourse if a utility provides inaccurate, incomplete or misleading information. In my opinion, if a utility fails to disclose pertinent information in a ratemaking proceeding, a utility should not be able to avoid being required to refund revenues improperly collected by claiming such refunding constitutes retroactive ratemaking. The prohibition against retroactive ratemaking should not permit a utility to undermine the integrity of the ratemaking process. If the information that is provided by a utility misleads the Commission, or if the utility

withholds information, the rates established by the Commission cannot be considered reasonable and, therefore, the prohibition against retroactive ratemaking should not apply.

**Q. ARE YOU AWARE OF ANY PROCEEDINGS THAT SUPPORT YOUR
RETROACTIVE RATEMAKING POSITION?**

A. Yes. In a Mountain States Telephone and Telegraph Company proceeding at Docket No. 88-049-18, the Public Service Commission of Utah upheld this position. Relevant portions of the Utah Commission's order in that proceeding are as follows, and justify retroactive ratemaking as appropriate under the circumstance present in this proceeding:

This case stems from the 1985 general rate case establishing utility rates. After those rates were established, various matters transpired resulting in a stipulated series of reductions of rates and ultimately, pursuant to a 1988 rate case, the establishment of new general rates effective November 15, 1989. Various utility customers filed a proceeding challenging the rates and requesting refunds of U S West's charges. The Commission ruled that such would constitute retroactive ratemaking, that there were no exceptions to that rule, and therefore dismissed the claim. On appeal, the Utah Supreme Court in *MCI Telecommunications Corp. v. Public Service Commission*, 840 P.2d 765 (Utah 1992) (*MCI*), reversed the decision of the Commission, ruling that certain exceptions to the rule against retroactive rulemaking might be available, and remanded the case to the Commission with directions. The two exceptions recognized by the Court as possibly applying were the exception for extraordinary and unforeseeable expenses or revenues and "utility misconduct".

As noted by the Court in *MCI*, in a general rate proceeding utility rates are fixed on the basis of an analysis of costs and revenues for a "test" year, and that those rates are to be just and reasonable. As stated by the Court, at page 770:

[T]he prohibition against retroactive ratemaking is designed to provide utilities with an incentive to operate efficiently. ...This process places both the utility and the consumers at risk that the ratemaking procedures have not accurately predicted costs and revenues. If the utility underestimates its costs or overestimates revenues, the utility makes less money. By the same token, if the utility's revenues exceed expectations or if costs are below predictions, the utility

74 keeps the excess. Overestimates and underestimates are then taken into account at
75 the next general rate proceeding in an attempt to arrive at a just and reasonable
76 future rate. (internal quotation omitted)

77 In general, rates are set prospectively only. This encourages the parties to the
78 ratemaking proceedings to ensure the best possible estimates, an appropriate rate
79 of return for the utility, but provide incentives for the utility to operate efficiently.
80 Retroactive ratemaking - revisiting the utilities costs and revenues on the basis of
81 information obtained subsequent to the setting of the rates - is generally
82 prohibited.

83 As found by the Supreme Court in MCI, there are exceptions to the prohibition of
84 retroactive ratemaking allowing the Commission to look backward, based upon
85 actual experience and figures, to set a just and reasonable rate. Retroactive
86 ratemaking is not an assessment of "damages", assessment of a "penalty", or
87 "punishment" to a utility. Further, its purpose is not to make the ratepayers whole,
88 to compensate them for harm suffered as a result of either the actions of the utility
89 or the existence of unjust or unreasonable rates. Rather, the purpose is the
90 fulfillment of the statutory duty of the Commission to establish a just and
91 reasonable utility rate. However, accomplishing its statutory purpose by
92 retroactive ratemaking is justified only under certain circumstances - i.e. the
93 exceptions to the rule against retroactive ratemaking. The imposition of a
94 proximate cause analysis and damage assessment, as in an ordinary tort case, is
95 inappropriate in the ratemaking context. It is the law and processes of utility
96 ratemaking that should apply.

97 As stated by the Court:

98 A utility that misleads or fails to disclose information pertinent to whether
99 ratemaking proceeding should be initiated or to the proper resolution of such a
100 proceeding cannot invoke the rule against retroactive ratemaking to avoid
101 refunding rates improperly collected. The rule against retroactive ratemaking was
102 not intended to permit a utility to subvert the integrity of ratemaking proceedings.

103 A complete copy of the Utah Commission's Order is attached to my testimony as

104 GCI Exhibit 15.0.

105 **Q. WITNESS FEINGOLD CLAIMS THAT THE STAFF AND**
106 **INTERVENORS LIKE GCI HAVE PROVIDED NO MEANINGFUL**
107 **GUIDANCE AS TO WHAT SHOULD BE THE COMMISSION'S FOCUS**

**IN THIS PROCEEDING. WHAT SHOULD BE THE COMMISSION'S
FOCUS IN THIS PROCEEDING?**

A. The Commission's focus in this proceeding should be on Nicor's performance under the GCPP measured based on the representations it made and should have made to the Commission in Docket No. 99-0127. The focus should not be on whether the Company complied with the Commission's Order approving the GCPP in Docket No. 99-0127. This Commission is required to set rates that are just and reasonable. Just and reasonable rates were not established in Docket No. 99-0127 because Nicor mislead the Commission and failed to disclose critical information. Therefore, Nicor's compliance with the Commission's Order in Docket No. 99-0127 should not be the focus of this proceeding.

**Q. WITNESS FEINGOLD CLAIMS YOU HAVE IGNORED THE FACT
THAT THE COMPANY WAS THE LOWEST COST PROVIDER OF
NATURAL GAS IN ILLINOIS DURING THE GCPP (LINES 65-68, 160-
163, AND 623-632). WHAT IS YOUR RESPONSE?**

A. The relationship between Nicor's gas costs and those of other Illinois utilities is not a proper consideration in this proceeding. This Commission does not set rates for one Illinois gas utility based on the costs of another. Many factors can affect the gas cost rates of a utility, and a direct comparison of rates is not a valid basis for evaluating utility performance. For example, one utility may own on-system storage, while another does not and must purchase storage from an interstate pipeline. In this instance, all else being equal, the utility with on-system storage would have lower gas cost rates because the costs of on-system storage are recovered through base rates, while the costs of storage purchased from an interstate pipeline are recovered through gas cost rates. Finally, Nicor

could have proposed a gas cost incentive program based on its performance versus other Illinois utilities. Nicor made no such proposal and, therefore, a comparison of Nicor's rates with those of other Illinois utilities is not a proper basis for the determination of Nicor rates.

Q. WITNESS FEINGOLD CLAIMS THAT YOU HAVE ERRONEOUSLY CRITICIZED THE COMPANY FOR FAILING TO SPECIFY GAS RESOURCE STRATEGIES TO THE COMMISSION DURING THE GCPP APPROVAL PROCESS BECAUSE THE COMMISSION ORDER IN DOCKET NO. 99-0127 SPECIFICALLY STATED THAT THE COMPANY NEED NOT SPECIFICALLY ARTICULATE SUCH STRATEGIES (LINES 314-330 AND 428-430). WHAT IS YOUR RESPONSE?

A. In CUB Data Request No. 27 in Docket No. 99-0127, the Company was specifically asked to provide a copy of all projections, analyses, and studies prepared which examined the extent to which the Company may profit under the GCPP. In that request, the Company was also asked to provide copies of all communications that discussed the profit potential of the GCPP. The Company responded that it had not performed any projections, analyses, or studies related to its potential performance under its GCPP proposal, nor did the Company have any communications that addressed the issue. In order for this response to have been accurate, Nicor could not have developed any strategies that it intended to pursue under the GCPP. Clearly, as explained in my direct testimony, this was not the case because Nicor examined the extent it could profit under a GCPP by liquidating low-cost LIFO inventory. It was the Company's position in Docket No. 99-0127 that it had general ideas as to how it would operate under the GCPP, but it

154 had no specific strategies. The Commission relied upon this false representation in
155 rendering its decision to approve the GCPP. The Commission did not say that if Nicor
156 had strategies it did not have to reveal them as witness Feingold suggests, nor did the
157 Commission permit the Company to provide inaccurate responses to data requests. I
158 believe that if Nicor had strategies it intended to pursue, the Commission would have
159 been interested in hearing them. Since witness Feingold did not participate in Docket No.
160 99-0127, it is not surprising that he has misinterpreted the Commission's order. Had the
161 Company provided the pertinent information when requested, it is likely that a GCPP
162 would have approved by the Commission, albeit different than the one that was actually
163 approved. As indicated in my direct testimony, x x x x x x x x x x x x x x x x x x x x x x

164 x x x x x x x x

165 **Q. WITNESS FEINGOLD CLAIMS THAT GIVEN THE UNPRECEDENTED**
166 **AND UNPREDICTED MARKET CONDITIONS AND CIRCUMSTANCES**
167 **THE COMPANY FACED DURING THE TERM OF THE GCPP, ANY**
168 **PREDICTION OF STRATEGIES AND TACTICS THAT THE COMPANY**
169 **MAY HAVE MADE IN DOCKET NO. 99-0127 WOULD HAVE**
170 **ULTIMATELY PROVEN TO BE INACCURATE, AS THE COMPANY**
171 **WOULD HAVE REASONABLY BEEN EXPECTED TO ABANDON**
172 **CONTEMPLATED STRATEGIES AND DEVELOP NEW APPROACHES**
173 **TO RESPOND TO UNPRECEDENTED MARKET CONDITIONS (LINES**
174 **430-436). DO YOU HAVE ANY COMMENTS?**

175 **A.** Yes. The 1998 *Inventory Value Team Report* clearly set forth a strategy the Company
176 would employ under the GCPP - the liquidation of low cost LIFO inventory layers. In

addition, as explained in the document included at Tab A-12 of Appendix A to my direct testimony, [REDACTED]

[REDACTED]

[REDACTED]. These strategies were not abandoned, but in fact, pursued by the Company despite the unprecedented market conditions. Witness Feingold's suggestion that had Nicor proposed strategies in the Docket No. 99-0127, it was somehow obligated to pursue each of those strategies, is wrong. There was no such requirement.

Q. WITNESS FEINGOLD CHARACTERIZES THE ADJUSTMENTS PRESENTED BY THE PARTIES IN THIS PROCEEDING AS AN INAPPROPRIATE ATTEMPT TO CONDUCT A COMPLETE PRUDENCE REVIEW OF THE COMPANY'S GAS PURCHASING PRACTICES DURING THE GCPP (LINES 471-485). HOW DO YOU RESPOND?

A. Regardless of how witness Feingold categorizes the various adjustments proposed by the parties, the Commission has an obligation to review Nicor's activities under the GCPP, and should not abandon this authority. A review of Nicor's GCPP activities is necessary due to the Company's manipulative, misleading and deceptive practices under the GCPP.

Q. WITNESS FEINGOLD ALSO CLAIMS THAT THE MOST APPROPRIATE DETERMINATION IN EVALUATING THE SUCCESS OF THE PBR PROGRAM IS THE OUTCOME OF THE UTILITY EFFORTS AS MEASURED BY ITS PERFORMANCE AGAINST THE BENCHMARK (LINES 483-485). DO YOU AGREE WITH WITNESS FEINGOLD?

200 A. Yes, to a certain extent. Nicor performance should be measured by its performance
201 against the Benchmark. However, Nicor's performance should be measured based on the
202 representations it made and should have made to the Commission. Nicor's manipulative,
203 deceptive and misleading practices should not be considered in measuring its GCPP
204 performance.

205 **Q. WITNESS FEINGOLD CATEGORIZES YOUR AQUILA WEATHER**
206 **INSURANCE ADJUSTMENT AS THE USE OF HINDSIGHT (LINES 532-**
207 **539). HOW DO YOU RESPOND?**

208 A. Witness Feingold's position implies that the Aquila weather insurance transaction was
209 prudent and reasonable. It was not. The Aquila transaction was improper and Nicor
210 should have never engaged in the transaction. As such, it is appropriate for Nicor to bear
211 fully responsibility for the adverse impact of the Aquila transaction as I have proposed.
212 Failing to hold Nicor responsible for the entire adverse impact would place Nicor in the
213 same position as if it had properly structured the original Aquila transaction. That is, it
214 did not improperly flow any of the costs associated with the insurance product through as
215 a gas cost. As I explained in my direct testimony, placing Nicor in the same situation as
216 though it had engaged in legitimate activities all along would set a bad regulatory
217 precedent. It would indicate that it was acceptable for utilities to be manipulative,
218 deceptive and misleading because the worse that could happen is to be treated as though
219 you were forthright all along.

220 In addition, Nicor could have hedged the price of the gas sold to Aquila to protect
221 against the adverse consequences of an increase in gas prices. It did not and ratepayers
222 bore this risk. This risk should not have been borne by ratepayers. Finally, it appears

223 that despite witness Feingold's claim, it appears that the Company has accepted my
224 adjustment (witness Moretti rebuttal, lines 35-37). If this is the case, witness Feingold's
225 testimony is inconsistent with that of Company witness Moretti. Witness Feingold has
226 criticized such inconsistencies in the positions of the various intervenors.

227 **Q. WITNESS FEINGOLD CLAIMS THAT A NUMBER OF THE**
228 **ADJUSTMENTS YOU HAVE PROPOSED ARE SERIOUSLY FLAWED**
229 **BECAUSE THEY ATTEMPT TO REPLACE THE COMPANY'S ACTUAL**
230 **PERFORMANCE UNDER THE GCPP WITH CALCULATED RESULTS**
231 **WHICH ARE OVERLY SIMPLISTIC AND DO NOT REALISTICALLY**
232 **REFLECT THE DAY-TO-DAY DECISION MAKING AND RESULTING**
233 **TRANSACTIONS ASSOCIATED WITH MANAGING THE COMPANY'S**
234 **GAS SUPPLY PORTFOLIO AT THE TIME THE DECISIONS WERE**
235 **REQUIRED TO HAVE BEEN MADE (LINES 567-576). WHAT IS YOUR**
236 **RESPONSE?**

237 A. I will address witness Feingold's criticisms of each adjustment as they are raised
238 individually, and demonstrate that the adjustments are appropriate despite his claims.

239 **Q. WITNESS FEINGOLD CLAIMS THAT THE COMPANY WOULD NOT**
240 **HAVE IMPLEMENTED THE STRATEGY OF UTILIZING LOW-COST**
241 **LIFO GAS LAYERS IN THE ABSENCE OF THE GCPP, AND THAT**
242 **HISTORY BEARS THIS OUT (LINES 671-674; 714-717). WHAT IS YOUR**
243 **RESPONSE?**

244 A. As explained in my direct testimony, the liquidation of low-cost LIFO inventory is not a
245 benefit to ratepayers in the long-run due to the fact that the liquidated inventory will be

246 replaced by much higher cost inventory in the future and, unless the ICC decides
247 otherwise, ratepayers will be required to pay the additional carrying costs associated with
248 the higher cost inventory. As indicated in my direct testimony, these additional carrying
249 charges will total approximately \$12.5 million per year.

250 **Q. WITNESS FEINGOLD CLAIMS THAT IF THE LOW-COST LIFO**
251 **LAYERS HAD NOT BEEN LIQUIDATED, THE COST OF GAS TO**
252 **CUSTOMERS WOULD HAVE BEEN \$32 MILLION HIGHER, WITH 50**
253 **PERCENT OF THE HIGHER COSTS BORNE BY RATEPAYERS (LINES**
254 **170-175, 674-678). HOW DO YOU RESPOND TO WITNESS**
255 **FEINGOLD'S ASSERTION?**

256 A. There is no dispute in this proceeding that the liquidation of low-cost LIFO inventory
257 reduced Nicor's actual gas costs during the term of the GCPP. The issue is who should
258 receive the benefits of the low-cost LIFO inventory liquidation. Witness Feingold claims
259 that his calculation shows the impact of replacing low-cost LIFO inventory withdrawals
260 with flowing supplies. However, his adjustment is incomplete. Witness Feingold fails to
261 consider the impact of the decrease in withdrawals on the Storage Credit Adjustment
262 component of the Benchmark, and the resulting impact on rates. During two of the three
263 years the GCPP was in operation, the Storage Credit Rate used to compute the Storage
264 Credit Adjustment was inverted. Thus, a decrease in storage withdrawals would have
265 decreased the Benchmark and costs to ratepayers. As shown on GCI Exhibit 16.0,
266 consideration of withdrawals on the Benchmark would reduce the claimed \$16 million in
267 savings to ratepayers by \$10.4 million.

268 In addition, Nicor did not purchase flowing gas supplies in lieu of liquidating low-
269 cost LIFO inventory. Therefore, his comparison is not valid. Finally, witness Feingold's
270 analysis fails to consider other alternatives to purchasing flowing supplies such as
271 purchasing gas under the Company's prefill arrangements with IMD. Therefore, his
272 analysis should not be considered.

273 **Q. WITNESS FEINGOLD TESTIFIES THAT, BASED UPON THE RECORD**
274 **IN DOCKET NO. 99-0127, THE COMMISSION FOUND THAT THE**
275 **COMPANY, IN OPERATING THE GCPP, WAS LIKELY TO PERFORM**
276 **IN A MANNER THAT WOULD BE BENEFICIAL TO CUSTOMERS**
277 **(LINES 695-698). DO YOU HAVE ANY COMMENTS?**

278 A. Yes. The Company misled and deceived the Commission and the parties in Docket No.
279 99-0127, and withheld pertinent information. Therefore, the Commissions findings in
280 Docket No. 99-0127 were not based on an accurate record.

281 **Q. WITNESS FEINGOLD EXPRESSES SURPRISE AT YOUR STATEMENT**
282 **THAT "NICOR'S DECISION TO MANAGE ITS STORAGE**
283 **OPERATIONS TO PROVIDE PROFIT LEVELS WAS A NEW**
284 **CONSIDERATION FOR NICOR, (LINES 748-754)." WHAT IS YOUR**
285 **RESPONSE?**

286 A. Witness Feingold expresses surprise because the Company had been managing its storage
287 operations for some time "to produce profit levels," with the creation of its Chicago Hub
288 operations. Witness Feingold has quoted my testimony out of context. The testimony
289 cited by witness Feingold was related to the liquidation of low-cost LIFO layers. Clearly,

the liquidation of LIFO inventory to generate a profit for the Company was a new consideration for the Company.

Q. WITNESS FEINGOLD CLAIMS YOUR COMPUTATION OF THE BENEFIT DERIVED FROM THE LIQUIDATION OF LOW-COST LIFO INVENTORY IS OVERLY SIMPLISTIC AND IGNORES THE LIFO LAYER ESTABLISHED IN 2001 (LINES 794-813). DOES YOUR COMPUTATION IGNORE THE LIFO LAYER ESTABLISHED IN 2001?

A. No. In 2000, Nicor liquidated 17,501,960 Dth of LIFO inventory. In 2001, Nicor added 2,025,097 Dth to its LIFO inventory. In 2002, Nicor liquidated 9,991,370 Dth of LIFO inventory. Thus, over the 3-year period, the net liquidation of LIFO inventory was 25,468,232 Dth (17,501,960 minus 2,025,097 plus 9,991,370). As shown on GCI Exhibit 4.0 on Rehearing, my adjustment to GCCP savings for the low-cost LIFO benefit is based on the liquidation of 25,468,232 Dth. Thus, I have not ignored the LIFO layer established in 2001. I have simply netted the layer established in 2001 with the layer liquidated in 2002. This is consistent with the fact that the LIFO layer established in 2001 was liquidated in 2002. I would also note that the method I used to determine the LIFO benefit is consistent to that which had been used by the Company in its bucket reports.

x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x

x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x This is shown on the document included in Appendix A-6, NIC 4518 of my direct testimony.

Q. WITNESS FEINGOLD CLAIMS YOU ENGAGED IN SOME UNDISCLOSED MANIPULATION OF THE 2002 LIFO ADJUSTMENT IN

**ORDER TO MAXIMIZE YOUR PROPOSED LIFO ADJUSTMENT
(LINES 835-848). DO YOU AGREE?**

A. No. I have just explained how my 2002 LIFO liquidation quantity was calculated, and the procedure I used to calculate my LIFO benefit adjustment was fully explained in my response to NG-CUB/CCSAO 4.03 (See GCI Exhibit 17.0). Without this response, witness Feingold would not have been able to determine how my adjustment was calculated. With this response, witness Feingold can easily determine how my adjustment was calculated. In my opinion, this does not qualify as undisclosed manipulation.

Q. WERE YOU AWARE OF THE INHERENT VALUE OF THE COMPANY'S LOW-COST LIFO LAYERS AT THE BEGINNING OF THE GCPP PROCESS AS WITNESS FEINGOLD CLAIMS (LINES 821-823)?

A. No. At the beginning of the GCPP process, I was aware that most gas utilities utilized the LIFO approach to valuing storage inventory. However, I was not aware of the inherent value of Nicor's low-cost layers, but more importantly, was not aware that Nicor intended to, in contrast to traditional storage use considerations, liquidate LIFO layers under the GCPP. At the beginning of the GCPP process, CUB submitted discovery expressly intended to reveal such intentions (CUB Data Request 27). Nicor failed to reveal its intentions. Therefore, the conversion of storage operations to a profit center through the liquidation of LIFO inventory could not be properly anticipated or evaluated in the GCPP process. As explained in my direct testimony, Nicor's low-cost storage inventory had existed for over 30 years. There was no reason to believe that it would not continue to exist.

Clearly, this suggests that the parties

were not aware of the inherent value of the Company's low-cost LIFO layers.

Q. WITNESS FEINGOLD CLAIMS YOUR ADJUSTMENT TO RECOGNIZE THE IMPACT OF ADDITIONAL STORAGE WITHDRAWALS IN 2001 IS INCOMPLETE (LINES 1005-1025). HOW DO YOU RESPOND?

A. Witness Feingold claims my adjustment is incomplete because I failed to consider the commensurate decrease in the Company's cost of gas. As subsequently demonstrated, consideration of the gas cost impact would double the amount of the appropriate adjustment.

In GCI Exhibit 18.0 on Rehearing, I have prepared an analysis of the impact of additional storage withdrawals on Nicor's gas costs based on three different adjustments to Nicor's 2001 storage withdrawal quantities. The three adjustments are as follows. First, in its restatement, Nicor reflects storage withdrawals of 54,289,000 Dth for 2001. In my direct testimony, I recommend that withdrawals of 115,132,000 be utilized to measure Nicor's performance under the GCPP in 2001. Page 1 of GCI Exhibit 18.0 reflects the gas cost impact of increasing Nicor's 2001 storage withdrawals from 54,289,000 Dth to 115,132 000 Dth. Thus, page 1 of GCI Exhibit 18.0 reflects the gas cost impact of an additional 60,843,000 Dth in 2001 storage withdrawals. As shown there, increasing the 2001 storage withdrawal quantity from 54,289,000 Dth to 115,132,000 Dth reduces 2001 gas costs by \$167.3 million.

Second, I am also proposing adjustments to Nicor's 2001 storage withdrawal quantity to include in-field storage transfers (12,059,000 Dth), and additional DSS

358 volumes of 7,265,000.¹ If these two adjustments are adopted by the Commission, Nicor's
359 2001 storage withdrawal quantity under the GCPP will increase by the proposed
360 amounts. Thus, the adjustment to the 2001 storage withdrawal quantity would be
361 reduced. Page 2 of GCI Exhibit 18.0 reflects an adjustment to gas costs assuming my
362 adjustment for in-field transfers is adopted by the Commission. That is, it reflects
363 withdrawals of 66,348,000 Dth (54,289,000 plus 12,059,000) from storage in 2001. This
364 is the 2001 storage withdrawal quantity reflected in my direct testimony. As shown on
365 page 2, the impact on Nicor's gas costs is \$134.2 million. Since ratepayers pay Nicor's
366 actual gas costs under the GCPP, the full \$134.2 million would be refunded to ratepayers.

367 Page 3 of GCI Exhibit 18.0 reflects an adjustment to gas costs assuming that both
368 my adjustments for in-field transfers and additional DSS withdrawals are adopted by the
369 Commission. That is, it reflects withdrawals of 75,613,000 Dth (54,289,000 plus
370 12,059,000 plus 7,265,000) from storage in 2001. As shown there, this results in a refund
371 of \$114.2 million to ratepayers. Since both these adjustments are appropriate, from this
372 point forward, my recommended adjustment for additional 2001 storage withdrawals will
373 assume both adjustments are adopted. If one or both of these adjustments are not
374 adopted, my recommendation should be revised as appropriate.

375 **Q. BY WAY OF EXAMPLE, PLEASE EXPLAIN IN GREATER DETAIL**
376 **THE CALCULATIONS REFLECTED ON GCI EXHIBIT 18.0.**

377 A. Certainly. Each page of GCI Exhibit 18.0 is similar, with the difference being the
378 previously described adjustment to the 2001 storage withdrawal quantity. In general, the
379 top half of each page reflects Nicor's gas costs under the GCPP at the various previously

¹ In my direct testimony, adjustments to both DSS and NSS volumes were proposed. As subsequently discussed, only adjustments to DSS volumes are now proposed.

described 2001 storage withdrawal quantity, while the lower half reflects Nicor's gas costs under my recommended storage withdrawal quantity of 115,132,000 Dth.

Columns (C) and (D) of each page of GCI Exhibit 18.0 reflect the actual quantity of gas purchased by Nicor during 2001 priced at the market index price. Columns (E) and (F) reflect the quantity of gas Nicor would have been required to purchase each month to meet its customer requirements (adjusted purchases quantity) and the cost of those purchases priced at the market index price. That is, the adjusted purchase quantity reflects the quantity of gas delivered to Nicor's sales customers each month that did not come from storage. Ideally, the actual purchase and adjusted purchase quantities should match. However, for various reasons including cycle billing, lost and unaccounted-for gas and possibly pipeline fuel retention quantities, they do not. I have presented actual and adjusted purchase quantities to show that actual and adjusted purchase quantities and prices are nearly identical and do not skew the results of my analysis.

The SCR withdrawal volumes (column I) reflect an allocation of annual storage withdrawals to month based on the percentage weightings approved for developing the Storage Credit Adjustment component of the Benchmark. This eliminated the minor impact of differences in Nicor's cost of gas due to variations from the approved percentage weightings and allows for the impact of changes in storage withdrawal quantities to be isolated. This change did not skew the results of the analysis. Annual SCR injection volumes in Column (J) were set equal to annual withdrawal quantities and also allocated based on the approved SCR weightings. Again, this was done to isolate the impact of changes in storage withdrawal quantities and does not skew the results of the analysis. As shown on page 1 of GCI Exhibit 18.0, Nicor's commodity cost of gas was

403 \$1,315.3 million for 2001 based on the restatement withdrawal quantity of 54,289,000
404 Dth.

405 The lower half of page 1 shows Nicor's cost of gas under the recommended
406 higher level of storage withdrawals of 115,132,000 Dth. Columns (O) through (V) are
407 computed in the same fashion as columns (E) through (L) as described above. As shown
408 there, under the recommended higher level of storage withdrawals for 2001, Nicor's gas
409 costs would have been \$167.3 million less. As previously explained, because of other
410 adjustments I am proposing to Nicor's 2001 storage withdrawal quantity, my
411 recommended adjustment to gas costs is shown on page 3 of GCI Exhibit 18.0.

412 **Q. WITNESS FEINGOLD'S ATTACHMENT RAF-R2, PAGE 1, IS VERY**
413 **SIMILAR TO GCI EXHIBIT 18.0. DO YOU HAVE ANY**
414 **OBSERVATIONS?**

415 A. Attachment RAF-R2, page 1, computes the effect on the cost of gas of additional storage
416 withdrawals in 2001. I would note that this attachment reflects withdrawals of
417 115,000,000 Dth and injections of 120,000,000 Dth. I would also note that the monthly
418 purchase quantities are nearly identical, while the annual purchase quantity is identical.
419 Witness Feingold's attachment indicates a 2001 cost of gas of \$985,289,000 based on a
420 withdrawal quantity of 115,000,000 Dth, while GCI Exhibit 18.0 reflects a 2001 cost of
421 gas of \$998,678,000, or a difference of 1.4 percent. As such witness Feingold's
422 attachment confirms my analysis.

423 **Q. WITNESS FEINGOLD CLAIMS, BEGINNING AT LINE 1030, THAT**
424 **THE INCLUSION OF THE GAS RELEASED TO IMD IN THE SCA**

425 **COMPONENT OF THE GCPP BENCHMARK IS INAPPROPRIATE.**

426 **WHAT IS YOUR RESPONSE?**

427 A. The Storage Credit Adjustment was intended to adjust the Benchmark to reflect the
428 benefits that ratepayers traditionally received as a result of purchasing gas supplies during
429 off-peak summer months, when prices are typically higher, injecting that gas into storage;
430 and then withdrawing those gas supplies to meet demand during peak winter periods,
431 when prices are typically higher. The gas released to IMD was withdrawn from the
432 storage Nicor purchased from NGPL, and Nicor received payments from IMD
433 representing the benefits obtained from the summer/winter price spreads which existed at
434 the time arrangements with IMD were entered into. Therefore, to provide ratepayers with
435 the benefit traditionally obtained from storage operations, it is appropriate to include
436 withdrawals of the gas released to IMD in the SCA component of the Benchmark.

437 **Q. HOW DO YOU RESPOND TO WITNESS FEINGOLD'S CLAIMS THAT**
438 **PRIOR TO THE GCPP, THE COMPANY ENGAGED IN SIMILAR**
439 **RELEASES OF ITS NSS CAPACITY AND THOSE RELEASES WERE**
440 **NOT INCLUDED IN THE COMPUTATION OF THE SCR COMPONENT**
441 **OF THE GCPP BENCHMARK (LINES 1090-1109)?**

442 A. I now agree that prior to the adoption of the GCPP, Nicor did release its NSS capacity to
443 a third-party. Thus, I have eliminated NSS volumes from my adjustment.

444 **Q. WITH RESPECT TO THE RELEASE OF STORAGE TO THIRD-**
445 **PARTIES, WITNESS FEINGOLD STATES HIS OPINION THAT "ANY**
446 **ATTEMPT TO CAPTURE THE 'EXPECTED BENEFITS' FROM SUCH**
447 **STORAGE OUTSOURCING ACTIVITIES THROUGH THE**

**IMPUTATION OF THE SCA OF STORAGE WITHDRAWALS THAT
THE COMPANY NO LONGER CONTROLS WOULD BE
COUNTERPRODUCTIVE TO IMPLEMENTING THE GCPP AND THE
FOSTERING OF INNOVATIVE GAS RESOURCE STRATEGIES BY
THE COMPANY” (LINES 1109 – 1113). WHAT IS YOUR RESPONSE TO
WITNESS FEINGOLD?**

A. Nicor’s DSS outsourcing activities with IMD were an attempt to manipulate the results of the GCPP at expense of ratepayers by denying ratepayers the seasonal price benefit they enjoyed from storage operations under traditional regulation. Nicor should not realize rewards under the GCPP for engaging in manipulative activities.

**Q. BUT WITNESS FEINGOLD CLAIMS HE CAN FIND NO SUPPORT FOR
YOUR CONTENTIONS THAT THE COMPANY ATTEMPTED TO
MANIPULATE THE CGPP BENCHMARK BY EXCLUDING GAS
UNDER THE COMPANY’S MANAGED DSS STORAGE
ARRANGEMENT WITH IMD. HOW DO YOU RESPOND?**

A. The benefit to Nicor from excluding gas under the DSS arrangement with IMD is explained in detail in my direct testimony. The document included at Appendix A-12, NIC 3205, clearly reveals Nicor’s intentions to manipulate the GCPP Benchmark by excluding withdrawals under a managed DSS arrangement:

x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x
x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x
x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x
x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x
x x

474 Of course, the storage credit is a component of the Benchmark. I present
475 additional comments on this issue in responding to witness Barrett.

476 **Q. WITNESS FEINGOLD POINTS OUT THAT IN 2000 THE SCR WAS**
477 **INVERTED AND, THEREFORE, NICOR GAINED NO BENEFIT FROM**
478 **DECREASING STORAGE WITHDRAWALS FOR THE IMD**
479 **TRANSACTIONS, AND REACHES THE CONCLUSION THAT THE**
480 **COMPANY WAS NOT AT ALL MOTIVATED AT THE TIME TO**
481 **DECREASE STORAGE WITHDRAWALS SO IT COULD RAISE THE**
482 **GCPP BENCHMARK (LINES 1135-1145). WHAT IS YOUR RESPONSE?**

483 **A.** In 2000, when the Company realized the SCR would be inverted, it created the notion of
484 virtual storage to create additional storage withdrawals and subsequently additional
485 profits for itself. In addition, in 2001, as explained in detail in my direct testimony, the
486 Storage Credit Adjustment had a significant impact on withdrawal quantities in 2001.
487 Clearly, contrary to witness Feingold's claim, the SCR had a significant motivating
488 influence on Nicor during the GCPP.

489 **Q. WITNESS FEINGOLD DISAGREES WITH YOUR ADJUSTMENT TO**
490 **INCLUDE IN-FIELD STORAGE TRANSFERS IN THE SCA BECAUSE**
491 **OF THE COMMODITY ADJUSTMENT IMPACT (LINES 1179-1185).**
492 **WHAT IS YOUR RESPONSE?**

493 **A.** Witness Feingold agrees that the Commodity Adjustment was designed to account for
494 differences between Market Index costs and actual gas costs. However, he claims that
495 this factor was the subject of much debate during the GCPP approval process, and that
496 Commodity Adjustment approved by the Commission incorporated many factors and

cannot be characterized by an exact representation of the difference between Market Index costs and actual costs. Contrary to witness Feingold's claims, the Order in Docket No. 99-0127 is very specific as to how the Commodity Adjustment under the GCPP was to be determined. Specifically, it was determined by taking the average actual historical Commodity Adjustment for the years 1994 through 1998, with 1996 given a 50 percent weight.

Q. WITNESS FEINGOLD FINDS YOUR PROPOSAL THAT IN FUTURE BASE RATE PROCEEDINGS THE COMMISSION SHOULD IMPUTE CARRYING CHARGES AS IF NICOR HAD NOT LIQUIDATED ITS LOW-COST LIFO INVENTORY TO BE FLAWED AND UNPRINCIPLED (LINES 1513-1522). HOW DO YOU RESPOND?

A. Nicor improperly benefited under the GCPP by retaining for itself a portion of the savings generated by the liquidation of low-cost LIFO inventory. Nicor will also benefit if it is allowed to earn a return, or carrying charges, on the higher cost gas put into storage to replace the liquidated low-cost layers. Witness Feingold appears to take issue with my proposal to deny Nicor the benefits of both liquidating low-cost LIFO inventory while at the same time denying the recovery of additional carrying charges. Presumably, he believes that if Nicor is denied any benefit from the liquidation of low-cost inventory, it would be unfair to also then deny Nicor the recovery of additional carrying charges which I have estimated at \$12.5 million per year. Under witness Feingold's approach, Nicor would be held to the same ratemaking standard as if the Company had been forthright all along. However, since Nicor has not been forthright all along, they are not entitled to be treated under this standard.

520 **Q. WITNESS FEINGOLD DISAGREES WITH YOUR ADJUSTMENT TO**
521 **ELIMINATE NICOR'S 2002 GCPP REWARD BECAUSE BY STATUTE,**
522 **THE GCPP WOULD HAVE BEEN IN EFFECT UNTIL SEPTEMBER**
523 **2002. WHAT IS YOUR RESPONSE?**

524 A. The legal interpretation of the statute offered by witness Feingold will be addressed in
525 brief by GCI's attorneys. However, assuming witness Feingold's interpretation is correct
526 and the GCPP was eliminated in September 2002, Nicor's reward under the GCPP for
527 2002 would have been greatly reduced. On restatement, Nicor's total 2002 GCPP reward
528 is \$26.9 million. After considering all other GCI adjustments, Nicor would actually be
529 entitled to a slightly larger reward of \$27.8 million. Of this amount \$12.0 million was
530 realized from the liquidation of low-cost LIFO inventory (GCI Exhibit 4.0). Had the
531 GCPP been terminated on September 30, 2002, none of Nicor's low-cost LIFO inventory
532 would have been liquidated in 2002. In addition, the Storage Credit Rate component of
533 the Storage Credit Adjustment was inverted in 2002 at a negative 32.61 cents, thus it
534 increased the Benchmark and Nicor's reward under the GCPP. Had the GCPP been
535 terminated September 30, 2002, withdrawals occurring during the months of October –
536 December 2002 would not have been included in the Storage Credit Adjustment and
537 subsequently the Benchmark. Storage withdrawals during these three months totaled
538 34,291,744 Dth (NIC 109406), thus Nicor's reward under the GCPP would have been
539 reduced by \$5.6 million (34,291,744 Dth x \$.3261 x 50 percent). These two adjustments
540 would have reduced Nicor's 2002 reward by \$17.6 million, and Nicor's 2002 GCPP
541 reward would total at most \$10.2 million.

**Q. DO YOU HAVE ANY OTHER COMMENTS ABOUT NICOR'S 2002
GCPP REWARD?**

A. Yes. The 2002 10-K of Nicor, Inc. indicates that, because the Company is unable to predict the outcome of the Commission's review of the GCPP, Nicor has not recognized its \$26.9 million 2002 GCPP reward (GCI Exhibit 19.0).

**Q. WITNESS FEINGOLD FINDS YOUR ASSERTION THAT THE
COMPANY'S GAS COSTS IN 2003 COULD BE NEGATIVELY
AFFECTED BY THE COMPANY'S ACTIONS UNDER THE GCPP TO BE
SPECULATIVE, AND CLAIMS YOU HAVE MADE THIS ASSERTION
BECAUSE YOUR PROPOSED ADJUSTMENTS ARE RESULTS-
ORIENTED (LINES 1575-1590). HOW DO YOU RESPOND?**

A. Interestingly, witness Feingold does not address whether the Company's GCPP activities in 2002 had an adverse impact on gas costs in 2003. Nevertheless, I have simply raised this issue to preserve it for the Company's 2003 gas cost reconciliation proceeding. I have proposed no adjustment to Nicor's 2003 gas costs in this proceeding. It would be unfortunate for this Commission to foreclose investigation of the impact of Nicor's 2002 GCPP activities on gas costs in 2003, particularly if manipulative, misleading and deceptive 2002 GCPP activities raised gas costs for 2003.

**Q. WITNESS FEINGOLD FINDS YOUR CONTENTION THAT THE
COMPANY MAY BE RESERVING EXCESS PIPELINE CAPACITY TO
BE ANOTHER EXAMPLE OF THE UNPRINCIPLED AND RESULTS-
ORIENTED NATURE OF YOUR PRESENTATION IN THIS**

**PROCEEDING (LINES 1591-1601). HOW DO YOU ADDRESS THIS
CLAIM?**

A. Again, witness Feingold does not address the merits of my claim, and this issue should be reserved for review in Nicor's 2003 gas cost reconciliation proceeding. I am proposing no adjustment to Nicor's 2003 gas costs in this proceeding.

**Q. WITNESS FEINGOLD CLAIMS THAT YOUR TESTIMONY IN THE
PEOPLES NATURAL GAS COMPANY ("PNG") CASE WAS
MISLEADING (LINES 1602-1625). WHAT IS YOUR RESPONSE?**

A. Witness Feingold claims that the primary purpose of citing the PNG case was to point out to the Commission that there were other gas utilities that shared Nicor's position that the benefits of liquidating low-cost LIFO storage gas belonged to the Company. This was not the intent expressed by witness Feingold in his response to CUB Data Request CF-1.9 (See Appendix A-8 to my direct testimony). CUB Data Request CF-1.9 inquired of witness Feingold as to whether he was aware of any other distribution companies that had liquidated low-cost LIFO gas. In his response dated September 26, 2003, he identified Peoples' proposal to liquidate a portion of its low-cost LIFO gas. He did not claim to cite this case because Peoples shared the same view as Nicor with respect to who should benefit from the liquidation of low-cost LIFO inventory. Rather, in my opinion, it was portrayed as a pending matter. Contrary to this, Peoples' proposal was dismissed in a Pennsylvania Commission order dated September 18, 2003, and in an Administrative Law Judges' Recommended Decision on July 30, 2003.

**Q. WITNESS FEINGOLD CLAIMS THAT THE INCONSISTENCIES AND
CONTRADICTIONS AMONG THE STAFF AND INTERVENERS**

**WITNESSES EMPHASIZE JUST HOW SUBJECTIVE AND
UNRELIABLE THE PARTIES ADJUSTMENT ARE IN THIS
PROCEEDING (LINES 1628-1698). DO YOU HAVE ANY COMMENTS?**

A. Yes. I have never been in a proceeding where all of the parties have presented identical issues and adjustments. Neither has witness Feingold. The purpose of this proceeding is to ferret out the claims of the various parties. It is not unreasonable or uncommon for experts to have differences of opinion.

III. Witness: Michael E. Barrett

**Q. IS THERE A RECURRING THEME TO WITNESS BARRETT'S
TESTIMONY THAT MERITS COMMENT?**

A. Yes. Witness Barrett claims that many of the proposed adjustments are inconsistent with or contradict Generally Accepted Accounting Principles ("GAAP") and are, therefore, faulty. Taken to its logical conclusion, adoption of witness Barrett's novel GAAP theory of regulation would mean that no commission could ever disallow the recovery of any costs incurred by a utility, for whatever reason including imprudence, if the costs in question were based on actual numbers. Regulation simply does not, and should not, work in this fashion.

The issue in this proceeding is not whether a particular adjustment is consistent with GAAP. Witness Barrett's claim is an attempt to divert attention from the real issue in this proceeding. The real issue in this proceeding is that Nicor made representations and commitments to this Commission with respect to the purpose of the GCPP and how Nicor would operate under the GCPP. The GCPP imposed additional requirements on Nicor beyond that required by GAAP. Nicor did not abide by the compact it made with this Commission and ratepayers. The restatement adjustments to Nicor's performance under the GCPP proposed by the Company restore some of the adverse impact on ratepayers of Nicor's inappropriate GCPP activities. They do not restate Nicor's performance as if the Company has abided by all of its representations and commitments. The additional adjustments proposed by the intervening parties are an attempt to measure Nicor's performance based on the representations and commitments made to the Commission and ratepayers in Docket No. 99-0127. GAAP does not consider Nicor's representations and commitments. The adjustments to Nicor's performance adopted by

the Commission in this proceeding will be reflected in Nicor's financial statements consistent with GAAP.

Q. DO YOU HAVE ANY ADDITIONAL COMMENTS ON WITNESS BARRETT'S CLAIM THAT THE ADJUSTMENTS PROPOSED TO NICOR'S RESTATED FINANCIAL RESULTS ARE INCONSISTENT WITH GAAP?

A. Yes. Statement of Financial Accounting Standards No. 71 ("FASB 71"), *Accounting for the Effects of Certain Types of Regulation*, recognizes that accounting requirements may be imposed on regulated entities by orders of regulatory authorities that do not conform with GAAP. FASB 71 also recognizes that rate actions of a regulator can reduce or eliminate the value of a utility's asset, or impose a liability on a regulated enterprise. FASB 71 discusses how these regulatory actions are to be recognized for accounting purposes. It does not limit the ability of a commission to disallow the recovery of costs. FASB statements are one component of what constitute GAAP.

In addition, the financial statements reflected in the 2002 10-K Report of Nicor, Inc. are based on Nicor's restated results. The 2002 10-K notes that the GCPP is still under Commission review and that the review may have an impact on the reported financial results (GCI Exhibit 19.0). This clearly invalidates witness Barrett novel GAAP theory of regulation.

Q. ON THE ISSUE OF THE LIQUIDATION OF LOW-COST LIFO INVENTORY, WITNESS BARRETT CLAIMS YOU HAVE MISINTERPRETED THE CONSUMERS DECISION (LINES 209-235). WHAT IS YOUR RESPONSE?

641 A. Witness Barrett claims that the point of the Consumers decision is that it demonstrates
642 that a utility can enter into alternative forms of regulation that give it the potential to
643 receive some of the benefits from the withdrawing of low-cost inventory, which is what
644 the Nicor's GCPP does. Consumers adopted an upfront approach with its Commission,
645 requesting authority to liquidate a portion of its low-cost LIFO inventory. Nicor's catch-
646 us-if-you-can approach to regulation is a far cry from the appropriate approach adopted
647 by Consumers. Had Nicor adopted Consumers' approach, perhaps they would have been
648 able to share in a fraction of the low-cost LIFO proceeds, if the liquidation of LIFO
649 layers were found to be in the best interest of ratepayers. Clearly, the Consumers
650 decision does not condone Nicor's approach to alternative regulation.

651 **Q. WITNESS BARRETT CLAIMS YOU HAVE MISINTERPRETED THE**
652 **MICHCON DECISION (LINES 236-265). IS HE CORRECT?**

653 A. No. As explained in my direct testimony, the Michigan Commission ordered a \$26.5
654 million gas cost disallowance because MichCon liquidated 19,000,000 of low cost
655 storage inventory in 2001.

656 **Q. WITNESS BARRETT CLAIMS THAT YOU HAVE NOT**
657 **APPROPRIATELY REFLECTED YOUR PROPOSED LIFO**
658 **ADJUSTMENT IN THE GCPP CALCULATION (LINE 306-325). DO**
659 **YOU AGREE?**

660 A. No. Witness Barrett makes this claim based on the assumption that the LIFO layers were
661 not liquidated. These layers were in fact liquidated, and the gas is gone. Thus, there is
662 no basis to evaluate what would have happened if the layers were not liquidated. The

issue in this proceeding is who should realize the benefits of the liquidation, not what would have happened absent the liquidation.

Q. WITNESS BARRETT CLAIMS THERE IS NO BASIS OR JUSTIFICATION FOR YOUR ADJUSTMENT TO 2001 STORAGE WITHDRAWALS UNDER GAAP, BECAUSE THEY DID NOT OCCUR (LINES 331-337, 380-385). WHAT IS YOUR RESPONSE?

A. Witness Barrett claims that I have failed to explain why an adjustment to storage withdrawals for 2001 is appropriate. Witness Barrett is wrong. In my direct testimony I explained that an adjustment was appropriate because Nicor represented to the Commission in Docket No. 99-0127 that it had little control over storage withdrawal quantities, and then once the GCPP was approved, it proceeded to significantly manipulate its storage withdrawal quantities to enhance its performance under the GCPP. As previously explained, witness Barrett's claim that such adjustments are not appropriate because they are inconsistent with GAAP is misplaced.

Q. WITNESS BARRETT IMPLIES THAT BECAUSE THE TRANSACTION WITH ENERCHANGE WAS EQUIVALENT IN TERMS TO THOSE DONE WITH UNRELATED PARTIES, THE TRANSACTION WAS LEGITIMATE (LINES 572-584). DO YOU HAVE ANY COMMENTS?

A. Yes. The transaction with Enerchange was conducted at below market prices. Therefore, it is not surprising that other parties would agree to similar transactions and this in no way legitimatizes the transaction.

684 **Q. WITNESS BARRETT CLAIMS THAT AT MOST THE ADJUSTMENTS**
685 **FOR ENERCHANGE TRANSACTIONS SHOULD BE \$262,500 (LINES**
686 **589-590). DO YOU ACCEPT THIS AMOUNT?**

687 A. No. Witness Barrett's adjustment does not credit ratepayers for the full amount of the
688 below market discount provided to Enerchange.

689 **Q. WITNESS BARRETT CLAIMS THERE IS NO ACCOUNTING BASIS**
690 **FOR YOUR ADJUSTMENT RELATED TO THE AQUILA WEATHER**
691 **INSURANCE PURCHASE (LINES 609 - 633). DO YOU HAVE ANY**
692 **COMMENTS?**

693 A. Yes. Again, witness Barrett's claim is based on the faulty assumption that regulatory
694 authorities are bound by GAAP. Additional comments related to this issue were
695 previously presented in my rebuttal to witness Feingold.

696 **Q. WITNESS BARRETT TESTIFIED THAT YOUR PROPOSED**
697 **ADJUSTMENT FOR INFELD STORAGE TRANSFERS IS INCORRECT**
698 **(LINES 658-684). IS HE RIGHT?**

699 A. No. Witness Barrett claims that my adjustment ignores the GAAP requirement that
700 financial statements be based on actual historical events and verifiable data, and
701 consistently applied calculation methods. Once more, witness Barrett's claim is based on
702 the faulty assumption that regulatory authorities are bound by GAAP.

703 **Q. WITNESS BARRETT DISAGREES WITH YOUR ADJUSTMENT TO**
704 **EXCLUDE MANAGEMENT FEES FROM THE GCPP (LINES 722 – 736).**
705 **DO YOU HAVE ANY COMMENTS?**

706 A. Yes. Witness Barrett claims my adjustment is inconsistent with certain accounting
707 concepts. Again, witness Barrett relies on the faulty assumption that regulation is
708 dictated by accounting concepts.

709 **Q. WITNESS BARRETT CLAIMS YOUR CALCULATION OF THE**
710 **MANAGEMENT FEE ADJUSTMENT IS WRONG (LINES 737 – 741).**
711 **HOW DO YOU RESPOND?**

712 A. My initial management fee adjustment calculation was based on documents provided by
713 Nicor (NIC 114092). More specifically, the amounts included in my adjustments were
714 taken directly from the audit of these fees recommended in the Lassar Report (see Exhibit
715 GCI 20.0). A portion of the differences cited by witness Barrett is attributable to his
716 exclusion of NSS fees (\$5.88 million), which I am no longer proposing to disallow. The
717 remainder is an adjustment of \$3.64 million reflected on Appendix IV to his testimony
718 that was not identified in the audit. Therefore, this adjustment should not be considered.

719 **Q. WITNESS BARRETT ALSO DISAGREES WITH YOUR ADJUSTMENT**
720 **FOR THE ACCOUNTS PAYABLE REVERSAL (LINES 744 – 799). HOW**
721 **DO YOU RESPOND?**

722 A. Witness Barrett claims that if an adjustment associated with the reversal of payables is
723 appropriate, the impact of the reversal in 2003 should be considered. I find this to be a
724 reasonable consideration, and have modified my adjustment accordingly.
725

726 **IV. Witness Theodore J. Lenart**

727 **Q. WITNESS LENART CLAIMS THAT AT NO TIME DURING THE**
728 **DEVELOPMENT OF THE GCPP DID NICOR INTEND TO LIQUIDATE**

THE LOW-COST LIFO STORAGE INVENTORY (LINES 58 – 65).

WHAT IS YOUR RESPONSE?

A. Witness Lenart's claims are simply inconsistent with the *Inventory Value Team Report* and the other evidence presented. As indicated in the *Inventory Value Team Report*, the GCPP was conceived in order for Nicor to capture a portion of the benefit of the low-cost LIFO storage inventory. In his deposition, witness Lenart testified as follows, clearly revealing that Nicor did intend to liquidate the low-cost LIFO storage inventory:

X X X X X X X X X X X X X X X

[illegible]

X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X X
X

[illegible]

X X X X X X X X X X X X X

[illegible][illegible]

X X X X X X X X X X X X X X X X X X X X X X X

766 X
767
768 X X X
769
770 X X X X X X X X X X X X X X X X X
771
772 X X X
773
774 X X X X X X X X X X X X X X X X X X X X X X X
775 X X X X X X X X X X X X X X X X X X X X X X X
776 X X X X X X X X X X X X X X X X X X X X X X X
777 X X X X X X X X X X X X X X X X X X X X X X X
778 X X
779
780
781
782 X X X X X X X X X X X X X X X X X X X X X X X
783 X X X X
784
785 X X X X X X X X X X X X X X X X X X X X X X X
786 X
787
788 X X X X X X X X X X X X X X X X X X X X X X X
789
790

791 **Q. WITNESS LENART CLAIMS THAT AT THE TIME THE GCPP WAS**
792 **APPROVED, NICOR WASN'T CERTAIN IT COULD ACCESS THE LIFO**
793 **LAYERS (LINES 66 – 69). WITNESS LENART ALSO CLAIMS THAT AT**
794 **THE COMPANY'S NOVEMBER 29, 1999 MEETING, THE**
795 **LIQUIDATION OF LIFO INVENTORY WAS NOT INCLUDED AS A**
796 **STRATEGY UNDER WHICH NICOR WOULD BENEFIT UNDER THE**
797 **GCPP (LINES 114 – 140). DO YOU HAVE COMMENTS?**

798 **A.** Yes. Within less than two weeks of that meeting Nicor executed an arrangement with
799 IMD structured to allow Nicor to access its low-cost LIFO inventory layers. At line 222
800 of his testimony, Witness Lenart acknowledges that the Company began considering this

801 arrangement in late November. This was Nicor's first transaction designed to generate
802 rewards under GCPP, and clearly demonstrates that the low-cost LIFO inventory was a
803 major factor considered in adopting the GCPP. It does not surprise me that liquidating
804 low-cost LIFO inventory was not included in the document outlining potential GCPP
805 strategies given Nicor's revealed practice of concealing the liquidation of low-cost LIFO
806 inventory. Moreover, the document included in Appendix A-18 of my direct testimony
807 (NIC 2409), clearly identifies the liquidation of low-cost LIFO inventory as a GCPP
808 strategy. This document listed potential GCPP strategies and was distributed at a meeting
809 held on August 25, 1999.

810 **Q. WITNESS LENART CLAIMS THAT WHEN THE AGREEMENT WITH**
811 **IMD IN DECEMBER 1999 TO SELL STORAGE INVENTORY WAS**
812 **EXECUTED, NICOR DID NOT AND COULD NOT KNOW THAT THE**
813 **PRICE OF GAS WOULD BE BELOW NICOR'S COST OF GAS**
814 **BECAUSE NICOR COULD NOT DETERMINE ITS WACOG UNTIL**
815 **WELL AFTER THE END OF THE YEAR (LINES 290 – 301). DO YOU**
816 **HAVE ANY OBSERVATIONS?**

817 **A.** Yes. Witness Lenart claims that at the time of the December 1999 storage inventory sale
818 to IMD, Nicor could not have known that the sale would have been at a loss. This claim
819 is simply not valid. The gas was sold at a price of approximately \$2.20 per Dth, and this
820 was known at the time of the sale. The cost of the storage gas being sold was
821 approximately \$3.00 per Dth, and was also known at the time of the sale. Thus, Nicor
822 knew, or should have known, a loss would be experienced. Regardless of witness

823 Lenart's claim, ratepayers have already been compensated for the sale Nicor made to
824 IMD at a loss.

825 In his testimony on this issue, witness Lenart refers to Nicor's weighted average
826 cost of gas ("WACOG") for the year. I have two comments with respect to this
827 testimony. First, the cost associated with the gas sold to IMD was not equal to Nicor's
828 WACOG for 1999 as witness Lenart implies. The cost was based on the price of the
829 liquidated LIFO inventory. Second, the sale to IMD occurred in the middle of December
830 1999. If the price was based on Nicor's WACOG, by that time, Nicor should have had a
831 very good estimate of its WACOG for the year, and certainly it would have been
832 unreasonable for that estimate to be in error by more than 80 cents per Dth.

833 **Q. WITNESS LENART CLAIMS THAT YOU FAILED TO RECOGNIZE**
834 **THAT NICOR'S PRIMARY RESPONSIBILITY UNDER THE GCPP WAS**
835 **TO ENSURE SYSTEM RELIABILITY (LINES 316 - 326). WOULD YOU**
836 **LIKE TO COMMENT?**

837 **A.** Yes. One of the prerequisites for approval of the GCPP was that it could not adversely
838 affect system reliability. Therefore, there is no basis for witness Lenart's allegations.

839 **Q. WITNESS LENART CHARACTERIZES YOUR CLAIM THAT NICOR**
840 **ADJUSTED ITS STORAGE WITHDRAWALS TO FOLLOW THE**
841 **STORAGE CREDIT RATE AS BEING FLAT WRONG (LINES 316 – 365).**
842 **WITNESS LENART ALSO CLAIMS THAT NICOR'S DECISION TO**
843 **REDUCE WITHDRAWALS IN 2001 WAS UNRELATED TO THE**
844 **STORAGE CREDIT RATE (LINES 464 – 472). WHAT IS YOUR**
845 **RESPONSE?**

846 A. The Storage Credit Rate is utilized to compute the Storage Credit Adjustment component
847 of the GCPP Benchmark. The evidence presented in my direct testimony clearly
848 indicates that storage withdrawals were influenced by the GCPP (For example, See
849 Appendix A Tab A-15). At lines 398-407, witness Lenart himself acknowledges that the
850 GCPP had a significant impact on storage withdrawals as previously explained. Nicor's
851 decision to adjust storage withdrawals in 2001 significantly increased the cost of gas for
852 ratepayers.

853 **Q. WITH RESPECT TO THE ENERCHANGE TRANSACTION, WITNESS**
854 **LENART CLAIMS THE TRANSACTION WAS BENEFICIAL FROM A**
855 **STORAGE OPERATIONS ASPECT (LINES 413-415). DO YOU HAVE**
856 **ANY COMMENTS?**

857 A. Yes. In his response to CUB/CCSAO 18.06 (GCI Exhibit 21.0), witness Lenart explains
858 that the Enerchange transaction was done to mitigate the price risk imposed on Nicor by
859 the GCPP Benchmark. It was not done to eliminate any immediate physical operational
860 concerns.

861 **Q. WITNESS LENART EXPRESSES HIS OPINION THAT ABSENT THE**
862 **GCPP, THE SAVINGS RECEIVED BY RATEPAYERS FROM THE SALE**
863 **OF LOW-COST LIFO INVENTORY WOULD NOT HAVE BEEN**
864 **REALIZED. DO YOU HAVE ANY COMMENTS?**

865 A. Yes. As explained previously, the liquidation of low-cost LIFO inventory was not in the
866 long-run best interest of ratepayers due to the additional carrying charges on higher-cost
867 replacement gas supplies.

V. Witness: Albert E. Harms

Q. WITNESS HARMS CLAIMS THAT AT THE TIME THE GCPP WAS ENTERED INTO, HE WAS UNAWARE OF ANY DISCUSSIONS REGARDING HOW THE LOW-COST LIFO INVENTORY COULD BE LIQUIDATED (LINES 99 – 102). DO YOU HAVE ANY COMMENTS?

A. Yes. Simply because witness Harms was not aware of any discussions regarding how the low-cost LIFO inventory could be liquidated does not mean the discussions did not take place. Witness Harms was not responsible for developing strategies to liquidate LIFO storage inventory.

Moreover, as revealed by the deposition of witness Harms, x x x x x x x x x x

[illegible][illegible][illegible]

X X X X X X X X X X X X X X X X X X X

[illegible]

[illegible]

924 Q. WITNESS HARMS DISMISSES YOUR CLAIM THAT THE GCPP
925 WOULD NOT HAVE BEEN PURSUED IF NOT FOR THE LOW-COST
926 LIFO INVENTORY BECAUSE HE CLAIMS THAT THE “POST BOARD
927 OF DIRECTORS PRESENTATION” YOU RELIED UPON DOES NOT
928 ACCURATELY PORTRAY HIS UNDERSTANDING OF THE
929 COMPANY’S INTENTIONS (LINES 103 – 115). DO YOU HAVE ANY
930 COMMENTS?

931 A. Yes. "Post Board of Directors" presentations are made by upper management or
932 someone directly involved with the topic being presented (GCI Exhibit 22.0). Witness
933 Harms was not responsible for deciding whether to pursue the GCPP, nor was he or his
934 department responsible for operations under the GCPP.

935 Q. WITNESS HARMS BELIEVES THAT THE *INVENTORY VALUE TEAM*
936 *REPORT* WAS NOT RESPONSIVE TO CUB DATA REQUEST NO. 1-27
937 (LINES 166 – 187). WHAT IS YOUR RESPONSE?

938 A. In his deposition, witness Harm's testified as follows,

X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X X X X X

X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X

X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X

[illegible][illegible]

X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X

X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X

X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X

X X X X X X X X X

[illegible]

1025 A. Yes. Witness Harms acknowledges that if he had been aware of the bucket reports, he
1026 would have consulted with counsel as to their responsiveness. Witness Harms was not a
1027 witness in Docket No. 02-0067. George Behrens was the witness in Docket No. 02-0067
1028 who sponsored the response to CUB Request 1.17. In his deposition, x x x x x x x x x x
1029 x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x. Witness Behrens is
1030 witness Harms' supervisor. In addition, witness Lenart testified as follows with respect
1031 to the bucket reports. Witness Lenart is responsible for Nicor's gas supply operations
1032 and was involved in developing GCPP strategies. His deposition clearly reveals that the
1033 x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x x
1034 x x x x x x x x x x x x x x x x x x x x x x x x

42

1049 X X X X X X X X X X X X X X X X X X
1050
1051 X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X
1052 X X X X X X X X X X
1053
1054 X X X X X X X X X X X X X X X X X X X X X X X X X X X X X X
1055 X
1056
1057 X X X X X X X
1058
1059
1060

VI. Other

1061 **Q. HAVE YOU REVISED YOUR DIRECT TESTIMONY EXHIBITS TO**
1062 **REFLECT THE CHANGES DISCUSSED IN YOUR REBUTTAL**
1063 **TESTIMONY AS APPROPRIATE?**

1064 A. Yes. Revised exhibits are attached to my testimony. I would note that GCI Exhibit No.
1065 5.0 reflects a minor correction for a typographical error for 2002 storage withdrawals. As
1066 shown on Revised GCI Exhibit 2.0, the amount which should be refunded to ratepayers
1067 under the GCPP is \$190.1 million. I recommend that this amount be returned to
1068 ratepayers, with interest, over a three-year period, consistent with the three-year period
1069 during which ratepayers were adversely affected.

1070 **Q. PLEASE EXPLAIN WHY YOUR RECOMMENDED ADJUSTMENT HAS**
1071 **INCREASED FROM THE INITIAL \$143.3 MILLION ADJUSTMENT**
1072 **REFLECTED IN YOUR DIRECT TESTIMONY ON REOPENING.**

1073 A. The following table compares on a line item basis the changes in my recommended
1074 adjustments from those reflected in my direct testimony:

1075

1075

Line Item	Direct	Rebuttal
Restated Ratepayer GCPP Share	\$ 8,873,200	\$ 8,873,200
Adjustments		
1. LIFO Benefit	\$ 25,637,667	\$ 25,637,667
2. DSS/NSS Withdrawals	XXXXXXXXXX	XXXXXXXXXX
3. Aquila Transaction	2,100,000	2,100,000
4. In-Field Storage Transfers	XXXXXXXXXX	XXXXXXXXXX
5. 2001 Storage Withdrawals	67,084,352	114,189,822
6. Management Fees	6,090,000	3,134,585
7. Interest Charges	2,287,516	2,287,516
8. TGP& MGT Capacity Costs	XXXXXXXXXX	XXXXXXXXXX
9. Accounts Payable Reversal	667,259	153,869
10. Affiliate Below Market Sale	372,000	372,000
11. 2002 Reward	16,970,310	15,783,707
Total Adjustments	\$145,199,445	\$186,513,145
Interest Charges	5,080,294	6,481,640
Total Adjustment to Restatement	\$150,279,739	\$192,994,785
Company Refund (Charge)	(6,991,014)	(2,900,000)
GCI Refund (Charge)	\$143,288,725	\$190,094,785

1076

1077

1078

1079

1080

1081

1082

1083

1084

1085

1086

As shown above, I have made no changes to adjustments to Nos. 1,3, 4, 7, 8 and 10. Adjustment No. 2 has decreased slightly due to the exclusion of NSS withdrawals. Adjustment No. 5 has increased significantly due to the consideration of the impact of additional withdrawals on Nicor's actual gas costs as witness Feingold claims is appropriate. Previously, my adjustment only considered the Benchmark impact of additional withdrawals. Adjustment No. 6 related to management fees is reduced due to the exclusion of NSS fees. A reduction to Adjustment No. 9 which relates to the accounts payable reversal has been made to consider the impact on 2003 gas costs as suggested by witness Barrett. Adjustment No. 11, which eliminates Nicor's 2002 GCPP reward, is reduced as a result of the impact of other changes to my adjustments on

1087 Nicor's 2002 GCPP reward. Interest charges have been increased to reflect the increase
1088 in the total amount of my recommended refund to ratepayers. The Company Refund
1089 (Charge) amount has been decreased to reflect the additional amounts Nicor has credited
1090 to ratepayers as discussed in the rebuttal testimony of witness Moretti.

1091 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY ON**
1092 **REOPENING?**

1093 A. Yes, it does.

1094

**NORTHERN INDIANA PUBLIC SERVICE COMPANY LLC
CAUSE NO. 43629 GCA 59
PREPARED TESTIMONY OF JEROME D. MIERZWA**

I. INTRODUCTION

Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?

A. My name is Jerome D. Mierzwa. I am a Principal and a Vice President of Exeter Associates, Inc. ("Exeter"). My business address is 10480 Little Patuxent Parkway, Suite 300, Columbia, Maryland 21044. Exeter specializes in providing public utility-related consulting services.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A. I graduated from Canisius College in Buffalo, New York, in 1981 with a Bachelor of Science Degree in Marketing. In 1985, I received a Master's Degree in Business Administration with a concentration in finance, also from Canisius College. In July 1986, I joined National Fuel Gas Distribution Corporation ("NFG Distribution") as a Management Trainee in the Research and Statistical Services Department ("RSS"). I was promoted to Supervisor RSS in January 1987. While employed with NFG Distribution, I conducted various financial and statistical analyses related to the company's market research activity and state regulatory affairs. In April 1987, as part of a corporate reorganization, I was transferred to National Fuel Gas Supply Corporation's ("NFG Supply") rate department where my responsibilities included utility cost of service and rate design analysis, expense and revenue requirement forecasting and activities related to federal regulation. I was also responsible for preparing NFG Supply's Federal Energy Regulatory Commission ("FERC") Purchase

1 Gas Adjustment ("PGA") filings and developing interstate pipeline and spot market
2 supply gas price projections. These forecasts were utilized for internal planning
3 purposes as well as in NFG Distribution's state purchased gas cost review proceedings.

4 In April 1990, I accepted a position as a Utility Analyst with Exeter. In
5 December 1992, I was promoted to Senior Regulatory Analyst. Effective April 1, 1996,
6 I became a principal of Exeter. Since joining Exeter, my assignments have included
7 evaluating the gas purchasing practices and policies of natural gas utilities, utility class
8 cost of service and rate design analysis, sales and rate forecasting, performance-based
9 incentive regulation, revenue requirement analysis, the unbundling of utility services
10 and the evaluation of customer choice natural gas transportation programs.

11 **Q. HAVE YOU PREVIOUSLY TESTIFIED IN REGULATORY PROCEEDINGS**
12 **ON UTILITY RATES?**

13 A. Yes. I have provided testimony on nearly 400 occasions in proceedings before the
14 FERC, utility regulatory commissions in Arkansas, Delaware, Georgia, Illinois,
15 Louisiana, Maine, Maryland, Massachusetts, Montana, Nevada, New Hampshire, New
16 Jersey, Ohio, Pennsylvania, Rhode Island, South Carolina, Texas, Utah, and Virginia,
17 as well as before this Commission.

18 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

19 A. Exeter has been retained by the Indiana Office of Utility Consumer Counselor
20 ("OUCC") to assist in the review of the reasonableness of the actual gas costs of the
21 Northern Indiana Public Service Company LLC ("NIPSCO" or "the Company")
22 reported for the period March through May 2021 in its filing at Cause No. 43629 GCA
23 59 ("GCA-59 review period" or "review period"). My review focused on evaluating
24 the results of the Company's Gas Cost Incentive Mechanism ("GCIM") under which

1 NIPSCO operated during the GCA-59 review period. I also examined whether
2 NIPSCO's gas procurement practices and policies were reasonable and consistent with
3 least cost procurement standards during the review period. My testimony presents the
4 results of my review and my recommendations.

5 Also presenting testimony on behalf of the OUCC in this proceeding is Mark
6 H. Grosskopf. Mr. Grosskopf addresses whether NIPSCO has adequately documented
7 its actual gas costs and the accuracy of the calculations supporting the Company's
8 proposed GCA factors to be applied during the September through November 2021
9 billing cycles.

10 **Q. PLEASE SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS.**

11 A. My findings and recommendations concerning NIPSCO's GCIM, gas procurement
12 activities and related costs are as follows:

- 13 • NIPSCO reasonably administered the assignment of capacity to Choice
14 Suppliers and its Capacity Release Revenue Sharing Mechanism during the
15 GCA-59 review period;
- 16 • NIPSCO reasonably administered its GCIM and has been able to adequately
17 document the results of its GCIM during the review period; and
- 18 • The tagging procedures approved for exchange transactions under NIPSCO's
19 GCIM in Cause No. 41338-GCA-9 should be continued.

20 **II. CAPACITY ASSIGNMENT AND RELEASE ACTIVITIES**

21 **Q. PLEASE DESCRIBE NIPSCO'S CAPACITY ASSIGNMENT AND RELEASE**
22 **ACTIVITIES DURING THE REVIEW PERIOD.**

23 A. Under the settlement approved in Cause No. 43837, which became effective May 1,
24 2010 ("2010 Gas ARP Settlement"), NIPSCO adopted mandatory capacity assignment
25 for suppliers participating in its Choice Program ("Choice Supplier"). Mandatory
26 capacity assignment is a process through which NIPSCO allocates and releases a

1 pro-rata share of its interstate pipeline transportation and storage capacity to Choice
2 Suppliers. Choice Suppliers must either accept the assignment of their allocated
3 capacity and pay the costs associated with that capacity directly to the interstate
4 pipelines, or may elect to decline the assignment. If a Choice Supplier declines the
5 assignment, the Choice Supplier must reimburse NIPSCO for the costs associated with
6 their allocated share of interstate pipeline transportation and storage capacity
7 (“mitigated release revenues”).

8 In addition to assigning capacity to Choice Suppliers, NIPSCO may release
9 capacity to third parties. Under the 2010 Gas ARP Settlement, NIPSCO was permitted
10 to retain 15 percent of the revenues it was able to generate from releases to third parties
11 (“capacity release sharing mechanism”). This capacity release sharing mechanism was
12 continued under the settlement approved by the Commission in Cause No. 44081
13 (“2012 Gas ARP Settlement”). The 2012 Gas ARP Settlement also provided that for
14 each year ended March 31, capacity release revenues subject to sharing would be the
15 lower of \$1 million or the actual total revenues from the previous year, with NIPSCO
16 being required to credit the GCA for any revenue sharing deficiency.

17 The Stipulation and Settlement Agreement approved in Cause No. 43629 GCA
18 48 (“GCA-48 Settlement”) modified the capacity release sharing provisions in effect
19 beginning with the GCA-50 review period (September through November 2018). The
20 2012 Gas ARP Settlement provided that for each year ended March 31, capacity release
21 revenues subject to sharing would be the lower of \$1 million or the actual total revenues
22 from the previous year, with NIPSCO being required to credit the GCA for any revenue
23 sharing deficiency. The GCA-48 Settlement provided for the elimination of this
24 provision from the 2012 Gas ARP Settlement. In addition, the GCA-48 Settlement

1 provides that NIPSCO will be entitled to retain 25 percent of the revenues generated
2 by releasing interstate pipeline capacity not assigned to Choice Suppliers, and 75
3 percent would be credited to GCA customers. Under the 2012 Gas ARP Settlement,
4 NIPSCO was entitled to retain 15 percent of the revenues and 85 percent was credited
5 to GCA customers. NIPSCO did not realize any capacity release revenues which were
6 subject to sharing during the GCA-59 review period.

7 **Q. HAS NIPSCO REASONABLY ADMINISTERED THE ASSIGNMENT OF**
8 **CAPACITY TO CHOICE SUPPLIERS AND ITS CAPACITY RELEASE**
9 **REVENUE SHARING MECHANISM DURING THE GCA-59 REVIEW**
10 **PERIOD?**

11 A. Our audit revealed that NIPSCO reasonably administered the assignment of capacity
12 to Choice Suppliers. There were no revenues generated from the release of capacity
13 to third parties which were subject to the capacity release sharing mechanism during
14 the GCA-59 review period.

15 **III. GAS COST INCENTIVE MECHANISM**

16 **Q. PLEASE DESCRIBE NIPSCO'S GCIM.**

17 A. NIPSCO's GCIM is an incentive mechanism designed to reward the Company if it
18 acquires gas at less than market prices and penalize NIPSCO if it acquires gas at more
19 than market prices. Under the GCIM, the actual cost of each gas purchase made by
20 NIPSCO is compared to a benchmark which reflects the cost of the purchase had it
21 been made at a market price for the location, type of purchase, and time at which the
22 purchase was made. Index prices reported in gas industry publications serve as market
23 prices under the GCIM. On a monthly basis, NIPSCO's actual gas costs are compared
24 to the benchmark. If NIPSCO's actual gas costs are less than the benchmark, NIPSCO

1 is rewarded with 50 percent of the difference between actual costs and the benchmark.
2 If NIPSCO's actual gas costs exceed the benchmark, NIPSCO is penalized 50 percent
3 of the difference between actual costs and the benchmark.

4 The proceeds from structured deals and exchange transactions are reflected as
5 a reduction to NIPSCO's actual gas costs under the current GCIM procedures. These
6 arrangements are discussed later in my testimony.

7 **Q. PLEASE DESCRIBE THE GCIM BENCHMARKING PROCEDURES IN**
8 **GREATER DETAIL.**

9 A. NIPSCO purchases gas at a number of interstate pipeline receipt point trading locations.
10 These trading locations include the following:

11 **Alliance Pipeline**

- 12 • Alliance Chicago Exchange

13 **ANR Pipeline ("ANR")**

- 14 • Louisiana
15 • Oklahoma
16 • Rockies Express Pipeline

17 **Natural Gas Pipeline Company of America ("NGPL")**

- 18 • Mid-Continent
19 • South Texas
20 • Texas/Oklahoma
21 • Rockies Express

22 **Panhandle Eastern Pipeline ("PEPL")**

- 23 • Texas/Oklahoma
24 • Rockies Express

25 **Texas Eastern Transmission ("Texas Eastern")**

- 26 • East Louisiana
27 • West Louisiana
28 • South Texas
29 • Rockies Express

30 **Trunkline Pipeline**

- 31 • East Louisiana
32 • West Louisiana
33 • Zone 1A

Chicago Citygate

NIPSCO's purchases can generally be categorized as either monthly base load or daily swing purchases. Monthly base load purchases are generally arranged on a monthly basis, and the same quantity of gas is delivered on each day during the month. Monthly base load purchases are generally arranged several days prior to the month of flow (during what is referred to as "bidweek") and commence flowing on the first-of-the-month ("FOM"). All other purchases made by NIPSCO are generally considered daily purchases and, as the term implies, are typically made on a day-to-day basis. NIPSCO will frequently make daily purchases which flow for several consecutive days.

Gas industry publications report index prices on a monthly basis for FOM monthly base load purchases and on a daily basis for swing purchases for nearly all of the locations NIPSCO purchases gas. Under the GCIM in effect during the GCA-59 review period, each NIPSCO gas purchase is benchmarked based on the type of purchase (monthly base load or daily) and location. More specifically, monthly base load purchases are benchmarked based on the average of FOM index prices reported in *Inside FERC's Gas Market Report* ("*Inside FERC*") and the Natural Gas Intelligence ("*NGI*") Bidweek Survey for the applicable month and location. Daily purchases are benchmarked based on the average of prices reported in *Gas Daily* and the NGI Daily Price Survey for the applicable day and location. These benchmarking procedures, as well as the benchmarking procedures subsequently discussed for structured deals, were generally approved in 2004 in Cause No. 41338 GCA-5.¹

¹ In Cause No. 44988, a tariff using the NGI Bidweek Survey was approved for benchmarking monthly base load purchases in lieu of Natural Gas Week Bidweek prices. NIPSCO, Original Volume No. 8, Original Sheet No. 43.

1 **STRUCTURED DEALS**

2 **Q. PLEASE DESCRIBE THE STRUCTURED DEALS WHICH NIPSCO HAS**
3 **HISTORICALLY ARRANGED UNDER THE GCIM.**

4 A. Structured deals under NIPSCO's GCIM have included recallable baseload purchases,
5 straddles, continuous extendables, and summer and winter period virtual storage
6 AMAs. Under a recallable baseload purchase, a counter-party agrees to deliver a
7 specified quantity of gas to NIPSCO (usually 10,000 Dth per day) at a specified receipt
8 point on each day during a specific month, and NIPSCO sells the counter-party a call
9 option entitling the counter-party to discontinue, or recall, delivery of that gas on any
10 day during the month (call option deliveries).

11 A straddle is a recallable purchase that also gives the counter-party the option
12 to deliver an additional specified quantity of gas to NIPSCO (usually 10,000 Dth per
13 day) on any day during a specific month (put option deliveries). Deliveries to NIPSCO
14 by the counter-party under a recallable baseload purchase or straddle are priced at the
15 applicable FOM index price. Thus, if during the month the daily market price of gas
16 declines from the FOM index price, a counter-party would have the incentive to
17 continue call option deliveries under a recallable baseload purchase or straddle and,
18 under a straddle, to exercise the put option and deliver additional gas to NIPSCO. The
19 counter-party would maximize deliveries to NIPSCO under a recallable purchase or
20 straddle arrangement when prices decline because it could presumably buy gas at the
21 lower daily price and sell it to NIPSCO at the higher FOM index price. If the daily
22 price of gas increases above the FOM index price under a recallable purchase or
23 straddle, a counter-party would have the incentive to discontinue all deliveries. The

1 counter-party would do so because it could sell the gas being delivered to NIPSCO to
2 other markets at a higher price than it would receive from NIPSCO.

3 **Q. PLEASE DESCRIBE A CONTINUOUS EXTENDABLE.**

4 A. Under a continuous extendable, a counter-party is required to deliver gas at a specific
5 receipt point for a specified number of days commencing on the first day of the month.
6 Typically, the specified delivery period is seven days and the delivered quantity is
7 10,000 Dth per day. The price paid by NIPSCO for the gas is initially set at an
8 applicable FOM index minus a discount. After the specified delivery period, the
9 purchase price is equal to the FOM index price flat, that is, with no discount, and the
10 counter-party has the option to discontinue delivering the gas. Under a continuous
11 extendable, as with a recallable purchase or straddle, a counter-party has the incentive
12 to discontinue delivering gas after seven days if the daily market price of gas increases
13 above the FOM index price, and continue delivering gas if the daily price declines
14 below the FOM price.

15 **Q. PLEASE EXPLAIN HOW RECALLABLE BASELOAD PURCHASES,**
16 **STRADDLES, AND CONTINUOUS EXTENDABLES ARE ACCOUNTED FOR**
17 **UNDER THE GCIM.**

18 A. NIPSCO is typically paid a fee for entering into a recallable baseload purchase or
19 straddle which is reflected as a credit to NIPSCO's actual gas costs under the GCIM.
20 Call option deliveries under a recallable baseload purchase or straddle are benchmarked
21 at the applicable FOM index price because the supplies are intended to be monthly
22 baseload purchases. Put option deliveries under a straddle are benchmarked at the
23 applicable daily index price. If a counter-party discontinues call option deliveries under

1 a recallable baseload purchase or straddle and a replacement supply is purchased by
2 NIPSCO, the same FOM index price is used to benchmark the replacement purchase.

3 The applicable FOM index price is also utilized for benchmarking supplies
4 delivered under a continuous extendable. If a counter-party discontinues deliveries and
5 the discontinued supplies are replaced, similar to a recallable baseload purchase or
6 straddle, the replacement purchase is benchmarked against the applicable FOM index
7 price.

8 **Q. HOW IS IT DETERMINED WHETHER A PURCHASE BY NIPSCO IS A**
9 **REPLACEMENT PURCHASE FOR DELIVERIES THAT HAVE BEEN**
10 **DISCONTINUED UNDER A RECALLABLE BASELOAD PURCHASE,**
11 **STRADDLE, OR CONTINUOUS EXTENDABLE?**

12 A. The GCA-48 Settlement established the GCIM benchmarking procedures that were in
13 place during the GCA-59 review period, and a purchase is considered a replacement
14 purchase if NIPSCO makes an incremental purchase on the same interstate pipeline
15 segment delivering to the same delivery point that the recallable baseload purchase,
16 straddle, or continuous extendable was being made prior to being discontinued.

17 **Q. PLEASE DESCRIBE NIPSCO'S SUMMER PERIOD VIRTUAL STORAGE**
18 **AMA STRUCTURED DEALS.**

19 A. A summer period virtual storage AMA is an arrangement wherein a counter-party
20 agrees to inject into one of NIPSCO's interstate pipeline storage arrangements on
21 NIPSCO's behalf a specified quantity of gas generally during the 7-month summer
22 injection period (April – October). During the 7-month summer injection period, the
23 counter-party is entitled to inject or withdraw varying quantities of gas on a daily basis
24 subject to agreed upon quantity limitations, subject to the requirement that the net

1 amount injected into storage by the end of summer injection period is equivalent to the
2 amount specified in the AMA. Under a summer period virtual storage AMA, NIPSCO
3 generally releases a portion of its interstate pipeline transportation and storage capacity
4 to a counter-party, who then utilizes the released transportation capacity to fill the
5 released storage capacity.

6 **Q. HOW ARE NIPSCO'S SUMMER PERIOD VIRTUAL STORAGE AMA**
7 **STRUCTURED DEALS ACCOUNTED FOR UNDER THE GCIM?**

8 A. NIPSCO typically purchases 1/7th of the specified amount of gas to be injected into
9 storage on its behalf by the counter-party during each month of the summer injection
10 period. The purchase price for this gas is at a discount to the applicable GCIM
11 benchmark price. This discount is shared with GCA customers pursuant to the GCIM
12 sharing procedures.

13 **Q. PLEASE DESCRIBE NIPSCO'S WINTER PERIOD VIRTUAL STORAGE**
14 **AMA STRUCTURED DEALS.**

15 A. Under a winter period virtual storage AMA, NIPSCO generally releases a portion of
16 its interstate pipeline storage capacity and inventory to a counter-party which is entitled
17 to use that storage when not needed by NIPSCO. NIPSCO maintains full use of its
18 daily storage injection and withdrawal rights released to the counter-party. In return
19 for providing the counter-party access to this storage, NIPSCO is entitled to purchase
20 a specified monthly baseload quantity of gas from the counter-party at a discount to the
21 applicable first-of-the-month index price. This discount is shared with GCA customers
22 under the GCIM.

23 **Q. HAS NIPSCO REASONABLY ADMINISTERED THE GCIM DURING THE**
24 **REVIEW PERIOD?**

1 A. Yes. The GCIM benchmarking procedures in place during the GCA-59 review period
2 were those approved as part of the Stipulation and Agreement in Cause No.
3 41338-GCA-5, as modified by the GCA-48 Settlement. In total, during the GCA-59
4 review period, NIPSCO experienced a gain of \$969,777 under the GCIM which was
5 shared 50 percent with GCA customers.

6 **EXCHANGE TRANSACTIONS**

7 **Q. PLEASE DESCRIBE NIPSCO'S EXCHANGE TRANSACTIONS.**

8 A. NIPSCO's exchange transactions include parks and loans. A park is a transaction
9 wherein a counter-party delivers gas to NIPSCO during one month and NIPSCO
10 returns that gas during a subsequent month. A loan is a transaction wherein NIPSCO
11 delivers gas to a counter-party during one month and the counter-party returns that gas
12 during a subsequent month. Park and loan deliveries are generally made ratably during
13 a month. That is, the same quantity of gas is delivered or received on each day (usually
14 10,000 Dth per day). NIPSCO receives a fee for its park and loan activities which are
15 credited against actual gas costs under the GCIM.

16 **Q. PLEASE DESCRIBE THE PROCEDURES APPROVED BY THE**
17 **COMMISSION FOR EXCHANGE TRANSACTIONS IN CAUSE NO. 41338**
18 **GCA-9.**

19 A. The settlement approved in Cause No. 41388-GCA-9 provided for the assignment, or
20 tagging, of a price to each end of a park or loan transaction. More specifically, when
21 gas is received from a counter-party under an exchange transaction, NIPSCO tags the
22 transaction with the highest of the following three monthly prices:

- 23 • FOM index price at the actual point of the exchange;
- 24 • Average of the daily *Gas Daily* index prices for the month at the actual point of
- 25 the exchange; or

- NIPSCO's average monthly cost of gas exclusive of price volatility mitigation strategies.

When gas is delivered to a counter-party by NIPSCO, the transaction is tagged with the lowest of the above three monthly prices. Tagging procedures for exchange transactions were adopted to evaluate whether GCA customers were being adversely affected by NIPSCO's exchange transactions. GCA customers could be adversely affected by exchange transactions if NIPSCO was receiving gas from counter-parties when gas prices were low and returning the gas when prices were higher.

Q. SHOULD THE TAGGING PROCEDURES APPROVED IN CAUSE NO. 41338 GCA-9 BE CONTINUED?

A. Yes. Since tagging procedures have been implemented, they have revealed that to date, NIPSCO's exchange activities have not had an adverse impact on GCA costs. Therefore, the tagging procedures should be continued at this time. I would note, however, that since Cause No. 41338 GCA-9, NIPSCO has significantly reduced its exchange transaction activity, and engaged in no such activity during the GCA-59 review period.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes, it does.

VERIFICATION

STATE OF INDIANA)
)
COUNTY OF MARION) ss:

The undersigned, Jerome D. Mierzwa, under penalties of perjury and being first duly sworn on his oath, says that he is a Consultant for the Indiana Office of Utility Consumer Counselor; that he caused to be prepared and read the foregoing; that the representations set forth therein are true and correct to the best of his knowledge, information and belief.

By: Jerome D. Mierzwa
Indiana Office of
Utility Consumer Counselor

Subscribed and sworn to before me, a Notary Public, this _____ day of _____ 2021.

Signature

Printed Name

My Commission Expires: _____

My County of Residence: _____

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

1. [Page] 24 of the Report identifies now terminated gas incentive mechanisms for Nicor Gas in Illinois and Vectren North, Vectren South, and Citizens Gas in Indiana. For each of these companies, please provide the following information:
 - a. When did the sharing incentive start and stop for each utility?
 - b. Describe the type of sharing mechanism (percentage split or other basis) for each utility.
 - c. Please explain why the sharing incentive was terminated.

Response

With respect to the incentive mechanism of Nicor Gas, please see the attached Direct and Rebuttal Testimony of Mr. Mierzwa in Illinois commerce Commission Docket Nos. 01-0705, 02-0067, and 02-0725. Mr. Mierzwa does not presently recall the precise start and stop dates for the incentive mechanism which was terminated at the conclusion of this proceeding.

With respect to the incentive programs of Vectren North, Vectren South, and Citizens Gas, please see the attached Report on the Auditing and Consulting Review of the 2011 Settlement for the period April 2015 – March 2016. To the best of Mr. Mierzwa's recollection, an alternative incentive program was not pursued due to the sale of ProLiance Energy, LLC. Mr. Mierzwa does not presently recall the precise start and stop dates for the incentive mechanism.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

2. For the Gas Cost Incentive Mechanism for Northern Indiana Public Service Company identified on Page 24 of the Report, please provide the following information:
 - a. Identify when the sharing incentive started.
 - b. Describe the type of sharing mechanism (percentage split or other basis) for the utility.
 - c. Please explain the basis for the current sharing incentive.

Response

Mr. Mierzwa is uncertain of the exact starting date for the Gas Cost Incentive Mechanism for Northern Indiana Public Service Company, which has been in operation since at least 2003. Please see the attached testimony of Mr. Mierzwa in Indiana Case No. 43629 GCA59 for a summary of the Gas Cost Incentive Mechanism.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

3. For each of the utilities in Delaware, Louisiana, Massachusetts, Ohio, and Pennsylvania that Exeter identified on Page 24 for which Exeter regularly performs various reviews, please provide the following information:
- Identify each utility and the regulatory authority with oversight of that utility.
 - Identify for each utility when the sharing incentive started.
 - Describe the type of sharing mechanism (percentage split or other basis) for the utility.
 - Discuss the basis for the current sharing incentive.

Response

- a. Mr. Mierzwa regularly performs gas cost reviews of the following utilities:

<u>Utility</u>	<u>Regulatory Authority</u>
National Fuel Distribution Corporation	Pennsylvania Public Utility Commission
Peoples Gas Company	Pennsylvania Public Utility Commission
Peoples Natural Gas Company	Pennsylvania Public Utility Commission
Columbia Gas of Pennsylvania	Pennsylvania Public Utility Commission
UGI Utilities, Inc. – Gas Division	Pennsylvania Public Utility Commission
Philadelphia Gas Works	Pennsylvania Public Utility Commission
PECO Energy Company	Pennsylvania Public Utility Commission
Delmarva Power and Light Company	Delaware Public Service Commission
Chesapeake Utilities Corporation	Delaware Public Service Commission
Entergy Louisiana, LLC	Louisiana Public Service Commission
Duke Energy Ohio, Inc.	Public Utility Commission of Ohio
Fitchburg Gas and Electric Company	Massachusetts Department of Public Utilities
Eversource Gas of Massachusetts	Massachusetts Department of Public Utilities
The Berkshire Gas Company	Massachusetts Department of Public Utilities
Boston Gas Company	Massachusetts Department of Public Utilities
Liberty Utilities Corp.	Massachusetts Department of Public Utilities

- b. To the best of Mr. Mierzwa's recollection and based on his research, the Pennsylvania incentives were approved on an ad hoc basis beginning in 2002 in Columbia Gas of Pennsylvania Docket No. R-0027204. Mr. Mierzwa is not presently aware of when the Delaware, Ohio, or Massachusetts incentives were approved. The Louisiana incentives were approved March 24, 1999 in Docket No. U-22407.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

- c. Pennsylvania gas utilities are entitled to retain 25% of Asset Management Arrangement (AMA) fees, off-system sales margins, and capacity release revenues (excluding mandatory releases to suppliers serving on-system transportation customers). For Delmarva Power and Light margins from capacity release and off-system sales are credited to ratepayers at 100% until a total credit of \$3.0 million is reached for the 12-month period ending every June. Once the \$3.0 million threshold is met, the margins are then shared at 80% to sales customers and 20% to the Company level until the following July. Chesapeake Utilities Corporation is permitted to retain 7.5% of AMA fees. Because it has historically operated under AMAs, Chesapeake Utilities Corporation has not engaged in off-system sales or capacity release activities and Mr. Mierzwa is not presently aware of the incentive mechanism that would apply to such activities. Duke Energy Ohio is entitled to retain 20% of AMA fees. Because it has historically operated under a AMAs, the Company has not engaged in off-system sales or capacity release activities and Mr. Mierzwa is not presently aware of the incentive mechanism that would apply to such activities. Massachusetts utilities are entitled to retain 10% of AMA fees, off-system sales margins, and to the best of his recollection, capacity release revenues (excluding mandatory releases to suppliers serving on-system transportation customers). Louisiana gas utilities are entitled to retain 30% of off-system sales margins and entitled to retain 0% of capacity release revenues. Mr. Mierzwa is uncertain as to the treatment of AMA fees.
- d. Mr. Mierzwa did not participate in the decisions of the commissions approving the current sharing incentives of the utilities. Mr. Mierzwa assumes the basis for the current sharing incentives is to provide an incentive to the utilities to engage in and maximize AMA fees, off-system sales margins, and capacity release revenues.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

4. In Sections 6.1.2 and 6.1.3, the Report discusses the incentive programs of Atmos and Piedmont, respectfully. Answer the following questions based upon the information relied upon and assumptions made at the time the Report was written:
- a. Has Exeter ever audited the incentive mechanisms of Atmos and Piedmont? If so, please identify the dates for each final audit report, identify the dockets for which such audits were conducted, and, if such final report is not available on the TPUC website, provide an electronic copy (a non-confidential copy if the report includes confidential information) of each such reports prepared by Exeter.
 - b. If the incentive mechanism programs of Atmos and/or Piedmont have ever been audited or reported upon by Exeter, has Exeter ever proposed any changes to such programs? If so, please discuss each such change, including an identification of the change, the problem or issue proposed to be addressed by such changes, how the proposed changes would address such problems or issues, whether such changes were adopted in full or part, and a summary of any subsequent assessment or report as to whether such changes produced the results anticipated from such changes.
 - c. Why were Atmos and Piedmont chosen for comparison?
 - d. Why were none of the other utilities referenced by the Report on Page 24 with which Exeter has knowledge and experience utilized for discussion or comparison purposes?
 - e. Discuss how Atmos and Piedmont are similar to and different from CGC.
 - f. Discuss how the Atmos and Piedmont incentive mechanisms are similar to and different from the CGC incentive mechanisms.
 - g. Based upon the information known and considered at the time the Report was prepared, discuss why Exeter believes the Atmos and Piedmont incentive mechanism are relevant to an assessment of CGC's incentive mechanism and instructive to recommending changes to the CGC incentives.

Response

- a. Exeter has previously audited the incentive mechanisms of Piedmont for the periods July 1, 2008 – June 30, 2011; July 1, 2011 – June 30, 2014; and July 1, 2014 – June 30, 2017. A report for each audit can be found on the Commission's website under Docket No. 05-00165. Exeter also performed an audit of Piedmont's incentive mechanism for the period July 1, 2006 – June 30, 2008. However, Exeter is uncertain as to the applicable docket number and is unable to locate a hard copy of the audit report. Exeter has previously audited the incentive mechanism of Atmos for the period April 1, 2011 through March 31, 2014. A copy of that audit can be found on the Commission's website under Docket No. 07-00225.
- b. Please see the audit reports identified in subparts (a) and (b). To the best of Mr. Mierzwa's recollection, the RFP Scope of Work for the Piedmont audits specified that the

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

selected auditor shall not propose changes to the structure of the incentive mechanism in the audit report or otherwise. On March 15, 2016 in Docket No. 16-00028, Atmos filed a petition to revise its incentive mechanism to implement the changes recommended in Exeter's audit report.

- c. Atmos and Piedmont were chosen because they were both regulated by the Tennessee Public Utility Commission.
- d. It appears that the reference to page 24 is incorrect. However, the incentive mechanisms of utilities other than Atmos and Piedmont were not discussed in detail in the audit report because they are not regulated by the Tennessee Public Utility Commission.
- e. Please see the audit reports identified in subpart (a).
- f. Please see the audit reports identified in subpart (a).
- g. Exeter believes that the Atmos and Piedmont incentive mechanisms are relevant to an assessment of CGC's mechanism because the Atmos and Piedmont incentive mechanisms are also regulated by the Tennessee Public Utility Commission.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

5. Given the statements in the second paragraph of Section 6.2 of the Report regarding the sharing percentages used in other jurisdictions, for each jurisdiction Exeter looked at or knows about, provide the following information:
- a. Identify each jurisdiction reviewed.
 - b. Identify each utility by jurisdiction that was reviewed.
 - c. Provide the sharing percentage for each utility that was reviewed.

Response

- a. Please see the response to requests 3(a) and 3(c).
- b. Please see the response to subpart (a).
- c. Please see the response to subpart (a).

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

6. In preparing the Report, did Exeter identify any other natural gas utility in the United States with a 50/50 sharing incentive sharing split for AMA fees, capacity release revenues, and off-system sales margins? If so, please identify such utilities by jurisdiction and explain why information regarding those utilities was not discussed or otherwise included in the Report.

Response

No.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

7. The Report states at page 45, "Exeter has observed no material differences in the resource efforts of natural gas utilities to generate AMA fees, capacity release revenues, or off system sales margins under a 25% sharing incentive compared to a 10% sharing incentive nor has Exeter observed a natural gas utility failing to devote sufficient resources to maximize these revenues/margins when provided a sharing incentive." In connection with this statement, answer the following:
- a. At the time of preparing the Report, did Exeter assess whether there any material difference in the resource efforts of natural gas utilities to generate AMA fees, capacity release revenues, or off system sales margins under a 50% sharing incentive compared to either a 25% or a 10% sharing incentive?
 - b. If Exeter conducted such an analysis, what was the results of such an analysis?
 - c. If Exeter conducted such an analysis, why was that information not provided in the Report?

Response

- a. No.
- b. N/A.
- c. N/A.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Chattanooga Gas Company
TPUC Docket 07-00224
Performance Incentive Plan and Gas Procurement Audit (Third Triennial Review)
Exeter Associates, Inc. Responses to Discovery Requests

8. Please identify and provide electronic copies of all documents relied upon in the preparation of Section 6.0 of the Report. Where documents are publicly available electronically on a website, you may provide links to such documents in lieu of producing document copies.

Response

At the time Mr. Mierzwa prepared Section 6.0 of the Report, he relied on the existing tariffs of Atmos and Piedmont. Those tariffs are attached to the audit reports identified in response to Request 4(a). Mr. Mierzwa also relied upon the discovery request responses of CGC which were previously served on all parties.

Respondent :

Jerome D. Mierzwa
Vice President
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044