

BEFORE THE  
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 080318-GU

In the Matter of:

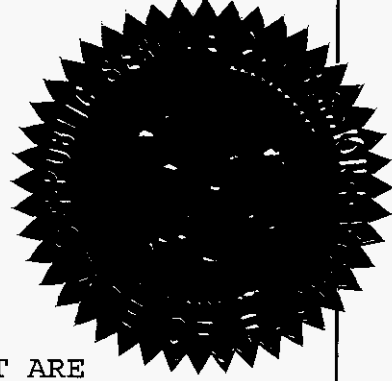
PETITION FOR RATE INCREASE BY  
PEOPLES GAS SYSTEM.

\_\_\_\_\_ /

VOLUME 4

Pages 431 through 527

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PROCEEDINGS: HEARING

BEFORE: CHAIRMAN MATTHEW M. CARTER, II  
COMMISSIONER LISA POLAK EDGAR  
COMMISSIONER KATRINA J. McMURRIAN  
COMMISSIONER NANCY ARGENZIANO  
COMMISSIONER NATHAN A. SKOP

DATE: Wednesday, March 4, 2009

TIME: Commenced at 9:30 a.m.  
Recessed at 5:01 p.m.

PLACE: Betty Easley Conference Center  
Room 148  
4075 Esplanade Way  
Tallahassee, Florida

REPORTED BY: MARY ALLEN NEEL, RPR, FPR

APPEARANCES: (As heretofore noted.)

DOCUMENT NUMBER-DATE

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FPSC-COMMISSION CLERK

## I N D E X

## WITNESSES

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## EXHIBITS

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## P R O C E E D I N G S

1  
2 (Transcript continues in sequence from  
3 Volume 3.)

4 CHAIRMAN CARTER: Staff and to the parties,  
5 we're now on witness -- don't tell me. Let me get it.  
6 Yardley. And this is one of the witnesses that was  
7 stipulated, so for witness Yardley, the prefiled  
8 testimony of the witness will be inserted into the  
9 record as though read.

10 CHAIRMAN CARTER: And we have for witness  
11 Yardley Exhibits 54 through 59; is that correct?

12 MR. WATSON: That's correct.

13 CHAIRMAN CARTER: Any objections? Without  
14 objection, show it done.

15 (Exhibits 54 through 59 were admitted into the  
16 record.)

1 I. INTRODUCTION

2 Q. PLEASE STATE YOUR NAME, AFFILIATION AND BUSINESS  
3 ADDRESS.

4 A. My name is Daniel P. Yardley. I am Principal, Yardley & Associates and  
5 my business address is 3 Apollo Circle, Lexington, MA 02421.

6 Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

7 A. I am testifying on behalf of Peoples Gas System ("Peoples" or the  
8 "Company").

9 Q. PLEASE PROVIDE A BRIEF OUTLINE OF YOUR  
10 PROFESSIONAL AND EDUCATIONAL BACKGROUND.

11 A. I have been employed as a consultant to the natural gas industry for the  
12 past 18 years. During this period, I have directed or participated in  
13 numerous consulting assignments on behalf of local distribution  
14 companies ("LDCs"). A number of these assignments involved the  
15 development of gas distribution company cost allocation, pricing, service  
16 unbundling, revenue decoupling and other tariff analyses. In addition to  
17 this work, I have performed interstate pipeline cost of service and rate  
18 design analyses, gas supply planning analyses, and financial evaluation  
19 analyses. I received a Bachelor of Science Degree in Electrical  
20 Engineering from the Massachusetts Institute of Technology in 1988.

21 Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE REGULATORY  
22 BODIES CONCERNING RATE AND REGULATORY MATTERS?

23 A. Yes. Although I have not previously testified before the Florida Public  
24 Service Commission (the "Commission"), I have testified in  
25 approximately 20 proceedings before public utility commissions in other

1 states and before the Federal Energy Regulatory Commission. The subject  
2 matters addressed in my testimony in these proceedings included cost of  
3 service, cost allocation, rate design, revenue decoupling and capacity  
4 planning.

5 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**  
6 **PROCEEDING?**

7 A. The primary purpose of my testimony is to develop and support Peoples'  
8 proposed rate design applicable to the Company's firm and interruptible  
9 distribution services. I will highlight important industry developments  
10 since Peoples' last base rate case in 2002 and explain the implications for  
11 the rate design that is appropriate to implement in this proceeding. The  
12 rates that I propose fairly apportion the Company's revenue requirement  
13 among customer classes, to be recovered through appropriate rate  
14 components applicable to each class. The non-uniform increases to  
15 various rates and charges reflect the results of the Company's allocated  
16 cost of service study ("COSS"), which I am supporting through my  
17 testimony.

18 I am also presenting a reclassification of some General Service  
19 ("GS") customers. GS customers include all commercial and industrial  
20 customers taking firm service from Peoples and vary in size from those  
21 with similar load characteristics as residential customers to very large  
22 processing loads. I am also proposing to reclassify a limited number of  
23 larger residential customers into corresponding GS rate schedules. The  
24 reclassification leads to greater uniformity within each group of GS  
25 customers and supports the effectiveness of the Company's rate design

1 proposals in meeting important rate design objectives.

2 **Q. HAVE YOU PREPARED OR CAUSED TO BE PREPARED ANY**  
3 **EXHIBITS TO BE INTRODUCED IN THIS PROCEEDING?**

4 A. Yes. The schedules of the MFRs listed in Exhibit \_\_ (DPY-1) were  
5 prepared by me or under my supervision. Each MFR contains a general  
6 explanation of what is called for and shown on the schedule. In addition, I  
7 am presenting the following additional exhibits with my testimony:

8 Exhibit \_\_ (DPY-2): Summary of Reclassification of Residential  
9 and GS Customers

10 Exhibit \_\_ (DPY-3): Rate of Return and Required Revenue  
11 Increase by Class to Yield Uniform Rate of  
12 Return

13 Exhibit \_\_ (DPY-4): Comparison of Existing and Proposed  
14 Revenues

15 Exhibit \_\_ (DPY-5): Comparison of Class-by-Class Rate of  
16 Return at Current and Proposed Rates

17 Exhibit \_\_ (DPY-6): Comparison of Monthly Customer Charges /  
18 Customer-Related Costs

19 **Q. HOW IS YOUR TESTIMONY ORGANIZED?**

20 A. My testimony is organized into four sections following this introduction.  
21 Section II provides important background on shifting industry  
22 fundamentals and the impact that they have on the specific rate design  
23 proposed by Peoples. Section III details the changes to the classification  
24 of the Company's GS and residential rate classes. Section IV explains the  
25 methodology, inputs and results of the COSS analysis. Lastly, Section V

1 presents the specific approach to developing Peoples' proposed base rates  
2 designed to recover its total revenue requirements.

## 3 II. RECENT GAS INDUSTRY TRENDS

### 4 Q. WHY IS RATE DESIGN AN IMPORTANT ELEMENT OF THE 5 COMPANY'S PROPOSALS IN THIS PROCEEDING?

6 A. Rate design provides a means of achieving important goals from a variety  
7 of perspectives. For customers, rate design conveys price signals that  
8 affect consumption decisions. Price signals inherent in any rate design  
9 include the cost of connecting to Peoples' distribution system, which  
10 affects which fuel the customer will choose for a particular end use. In  
11 addition, rate design influences customer consumption decisions based on  
12 the marginal cost or savings to the customer of increasing or decreasing  
13 monthly consumption. Lastly, rate design influences the fairness of prices  
14 from one customer class to another as well as within customer classes,  
15 each of which is comprised of many different but similarly situated  
16 customers paying the same rates.

17 From the perspective of an LDC such as Peoples, rate design  
18 governs the manner in which revenues are collected, and – more  
19 importantly – the manner in which costs of providing service are  
20 recovered from customers. The implications of a particular rate design for  
21 an LDC include the likelihood that the design enables the LDC to recover  
22 its approved level of revenue requirements. This directly affects the terms  
23 on which it is able to retain and attract capital to provide ongoing  
24 reliability and fund customer growth.

25 From a public policy perspective, rate design can be an important



1 tool for achieving specific energy policy goals that influence the quality of  
2 life for citizens and the competitive position of the State of Florida. Policy  
3 goals affected by rate design include end-use fuel mix, energy efficiency  
4 and environmental impacts of energy consumption. Therefore, the form of  
5 a utility's rate structure is an important building block that can contribute  
6 to achieving important goals that are presently at the forefront of Florida's  
7 energy policy.

8 **Q. PLEASE DESCRIBE THE SPECIFIC RATE DESIGN GOALS FOR**  
9 **PEOPLES THAT GUIDED THE DEVELOPMENT OF THE RATE**  
10 **DESIGN YOU ARE RECOMMENDING.**

11 A. The rate design approach I am recommending seeks to achieve the  
12 following five goals:

13 (1) **Fairness** – Fairness is accomplished through pricing services  
14 based on the underlying cost. Fairness is important in many  
15 respects including between the Company and its customers, across  
16 the classes served by Peoples, and within individual customer  
17 classes.

18 (2) **Energy Efficiency** – Reducing energy consumption through  
19 energy efficiency and conservation helps implement important  
20 policy objectives that will benefit customers and the environment.

21 (3) **Revenue Stability** – Revenue stability indicates that Peoples' base  
22 rate revenues are more predictable in view of future uncertainties.  
23 As customer use patterns have become less predictable, improved  
24 revenue stability through rate design takes on greater importance.

25 (4) **Rate Moderation** – Moderation ensures that customers are not

1 exposed to dramatic price changes that could result in undesirable  
2 impacts including cost increases or economic decisions by existing  
3 customers to cease taking gas service from Peoples.

4 **(5) Simplicity** – Simplicity means a rate structure that is easy for  
5 customers to understand and straightforward to administer.

6 At times, these individual goals compete with one another and  
7 must be balanced to achieve an appropriate set of rates and tariff  
8 provisions to recover the Company's cost of service.

9 **Q. PLEASE DESCRIBE PEOPLES' EXISTING RATE SCHEDULES.**

10 A. Peoples' existing rate schedules are segregated by sector, nature of service  
11 (firm or interruptible) and by customer size. Firm service is primarily  
12 provided under one Residential Service ("RS") and six GS rate schedules.  
13 A limited number of customers take firm service under Commercial Street  
14 Lighting Service ("CSLS"), Natural Gas Vehicle Service ("NGVS"),  
15 Residential Standby Generator Service ("RS-SG"), Commercial Standby  
16 Generator Service ("CS-SG"), and Wholesale Service ("WHS").

17 Peoples also provides interruptible service under three size-based  
18 rate schedules – Small Interruptible Service ("SIS"), Interruptible Service  
19 ("IS") and Interruptible Service – Large Volume ("ISLV"). Lastly, in  
20 some cases, customers taking interruptible service enter into a contract  
21 with Peoples under the Contract Interruptible Service ("CIS") rate  
22 schedule that governs the pricing and other terms of the service they  
23 receive.

24 **Q. WHAT RATES AND CHARGES ARE INCORPORATED INTO**  
25 **THE RS AND GS RATE SCHEDULES?**

1 A. The existing rate design for these two rate schedules is similar and  
2 includes two types of base rate charges that are intended to recover  
3 Peoples' non-gas revenue requirements, and a purchased gas adjustment  
4 ("PGA") charge to recover the costs of gas supply. The residential base  
5 rates consist of a \$10 customer charge and a \$0.37667 per therm delivery  
6 or distribution charge. Customer charges are applied per customer per  
7 month and distribution charges are applied to each customer's monthly  
8 therm usage. Under this rate structure, all residential customers pay a  
9 minimum amount to Peoples, regardless of their monthly usage. The per-  
10 therm distribution charge results in customers paying lower amounts as  
11 their consumption decreases. The distribution charge is considered a  
12 variable charge because all of the associated revenues are linked to  
13 customer usage or throughput.

14 The existing rate design for GS customers is very similar to that for  
15 residential customers. The existing monthly customer charges range from  
16 a low of \$14 for SGS customers up to \$150 for GS-5 customers. The per-  
17 therm distribution rate is \$0.26955 for SGS customers and decreases to  
18 \$0.10041 for GS-5 customers, with the greatest reduction occurring  
19 between the GS-4 and GS-5 rate classes. Although Peoples' rate structure  
20 employs both fixed and variable charges, the vast majority of firm base  
21 revenues are recovered through the variable per-therm charges. During  
22 2007, over 70% of total firm base rate revenue was attributable to variable  
23 charges.

24 **Q. DO THE REMAINING RATE SCHEDULES EMPLOY THE SAME**  
25 **TYPE OF RATE DESIGN?**

1 A. The majority of the other rate schedules also utilize a combination of  
2 monthly customer charges and per-therm distribution charges.  
3 Specifically, the CSLS, NGVS, WHS, SIS, IS and ISLV rate schedules  
4 employ this type of rate structure with varying levels of customer and  
5 distribution charges that are intended to reflect the costs incurred to  
6 provide service.

7 The standby generator-only services, RS-SG and CS-SG, represent  
8 an exception to the typical rate structure. The generator-only rate  
9 schedules were developed and approved after the Commission approved  
10 rates in the Company's last base rate case. The services were developed in  
11 response to customer needs to back up their electric service during  
12 hurricane-induced or other electric service outages. Standby generator-  
13 only customers do not utilize natural gas as their primary fuel for any end-  
14 use. As a result, it is typical for these customers to have zero monthly  
15 usage. The existing rate structure for standby generator-only customers  
16 reflects a higher customer charge and an initial block of use that includes  
17 no per-therm charge. The level of the customer charge and the size of the  
18 initial block were derived to yield revenue for an average residential or  
19 SGS customer based on the Company's last base rate case.

20 **Q. ARE THERE SEPARATE CHARGES FOR GAS SUPPLY?**

21 A. Yes. Sales customers that purchase their gas supply from Peoples pay a  
22 volumetric PGA rate for gas supply. Sales customers include all  
23 residential customers and many GS customers. The PGA rate recovers the  
24 costs of purchased gas and upstream pipeline capacity and storage  
25 resources necessary to ensure firm delivery to customers throughout the

1 year, and is adjusted periodically to track changes in Peoples' delivered  
2 cost of gas supply. The PGA rate includes an over- or under-recovery  
3 component (the true-up) that carries forward any difference between gas  
4 costs and PGA revenues for recovery or refund in a future period.

5 Many non-residential customers are transportation-only customers,  
6 and pay Peoples to deliver gas the customers have purchased from various  
7 third-party marketers other than Peoples. The gas price for a firm  
8 transportation customer is negotiated in a competitive marketplace  
9 between the customer and the marketers. All transportation customers are  
10 subject to the additional terms of either the Natural Choice Transportation  
11 Service Rider ("NCTS") or the Individual Transportation Service Rider,  
12 which govern the relationship among customers, Peoples and marketers  
13 including all pool administration functions. Transportation customers also  
14 have the option of returning to sales service at any point in the future,  
15 subject to certain notice requirements. Due to rising natural gas  
16 commodity prices, gas supply charges (whether through the PGA or from  
17 marketers) have been rising and now represent 50-75% of the total natural  
18 gas bill for the vast majority of Peoples' customers.

19 **Q. HOW DOES THE COMPANY'S CURRENT RATE DESIGN**  
20 **COMPARE WITH THE RATE DESIGNS OF OTHER LDCS?**

21 A. Peoples' base rate structure mirrors that of many LDCs. In particular, the  
22 use of a monthly customer charge and a variable distribution charge based  
23 on consumption to recover revenue requirements is fairly prevalent across  
24 the U.S. This particular form of rate design reflects historical industry  
25 drivers and economic conditions that are now changing in many respects.

1           While the basic structure of the Company's rate design is similar to  
2           that of many other LDCs, there are also differences. Many firm and  
3           industrial customers of other LDCs pay a higher portion of their bills  
4           through fixed customer and demand charges. In addition, many LDCs  
5           employ weather normalization or other revenue stability mechanisms that  
6           affect revenue recovery.

7   **Q.   WHAT FACTORS INFLUENCED THE DEVELOPMENT OF THE**  
8   **TRADITIONAL RATE DESIGN THAT RELIES UPON**  
9   **CONSUMPTION-BASED CHARGES TO RECOVER A**  
10   **SUBSTANTIAL PROPORTION OF REVENUE REQUIREMENTS?**

11   A.   This somewhat longstanding approach reflects many historical industry  
12       drivers. The country's natural gas delivery system underwent a period of  
13       broad expansion that lasted for decades following World War II. This  
14       expansion, enabled by advances in metallurgical technologies and welding  
15       techniques, brought the benefits of reliable, affordable and clean-burning  
16       natural gas to millions of households and businesses throughout the United  
17       States, including Florida. Public policy promoted the expansion of natural  
18       gas infrastructure and additional penetration of natural gas into more  
19       homes and for additional end-uses. This public policy was reflected in  
20       rate design as expanding systems and growing loads allowed the LDCs'  
21       fixed costs to be spread over higher levels of billing units, lowering  
22       average costs to consumers.

23           The historical period up to and including the 1990s was also  
24       characterized by relatively low and stable gas commodity prices, which in  
25       turn contributed to stable customer consumption. Although many existing

1 appliances were replaced with more efficient ones, customers continued to  
2 add appliances over this timeframe as natural gas gained market share for  
3 many end-uses including water heating and heating.

4 Frequent base rate cases could be considered the norm as LDCs  
5 filed to recover the capital costs of expansion through base rates. More  
6 frequent base rate cases also provided opportunities for LDCs to reflect  
7 the current consumption characteristics of customers in rates on a regular  
8 basis.

9 **Q. ARE THERE ANY CHANGES UNDERWAY IN THE GAS**  
10 **INDUSTRY THAT AFFECT HOW RATE DESIGN SHOULD BE**  
11 **APPROACHED IN THIS PROCEEDING?**

12 A. A confluence of factors is leading to the need to reconsider the most  
13 appropriate approach to rate design and whether the existing approach that  
14 recovers a substantial portion of fixed costs through variable charges  
15 should be supplanted. The first of these factors is a significant tightening  
16 of the supply-demand balance in wholesale natural gas markets caused  
17 primarily by the increased use of natural gas to generate electricity. In  
18 recent years, gas commodity prices have been subject to material  
19 increases. The impact on customers has been negative as gas supply costs  
20 have increased by over 200% compared with levels prevalent during the  
21 1990s. In response, many customers have cut their consumption, which  
22 leads – under the traditional rate design currently used by Peoples – to an  
23 underrecovery of the revenue requirements embedded in their base rates.

24 Second, environmental concerns associated with human activity  
25 are perhaps greater today than at any other time in history. Responsible

1 energy consumption falls squarely under the rubric of important  
2 environmental challenges receiving significant focus by politicians,  
3 scientists and engineers alike. There is an increasing emphasis on  
4 reducing carbon emissions in order to achieve environmental and quality  
5 of life benefits that result. In addition, potential climate-change risks,  
6 including global warming and energy security concerns, are receiving  
7 greater attention from environmental advocates and local and national  
8 policy makers. In 2007, Governor Crist convened the Serve to Preserve  
9 Florida Summit on Global Climate Change and signed executive orders  
10 that promote additional energy efficiency and reduced greenhouse gas  
11 emissions.

12 Third, a number of financial challenges are facing many LDCs,  
13 including Peoples. Improvements in appliance efficiency contribute to  
14 declining use for existing end-uses, resulting in a downward trend in  
15 consumption associated with existing capital investments. This downward  
16 trend leads to revenue erosion under the existing rate design. In the past,  
17 the impact of declining use trends was generally offset by customer  
18 growth and increased natural gas appliance saturation. These mitigating  
19 effects on revenue losses have diminished as the natural gas industry  
20 continues to mature and the housing expansion has experienced a dramatic  
21 slowdown. In addition, substantial LDC investments in cast iron and  
22 unprotected steel distribution mains installed post-World War II are  
23 nearing the ends of their useful lives and require replacement or  
24 protection.

25 The gas distribution industry has also seen a substantial shift with



1 respect to capital expenditures. In the past, the majority of capital  
2 expenditures were associated with adding profitable new loads, while  
3 today substantial capital spending is associated with non-revenue  
4 producing projects. These elements are affecting the economics of utility  
5 service as LDCs are no longer able to fund as high a proportion of their  
6 non-revenue producing capital investments through revenues derived from  
7 customer growth. The impact of these changing economics can be acute  
8 in an environment where base rate cases are less frequent.

### 9 III. RATE RECLASSIFICATION

#### 10 Q. HOW ARE GS CUSTOMERS PRESENTLY CLASSIFIED INTO 11 GROUPS?

12 A. The six size- or consumption-based GS rate schedules are segregated as  
13 follows:

- 14 ▪ Small General Service (“SGS”) includes all customers smaller  
15 than 1,000 annual therms,
- 16 ▪ GS-1 includes customers between 1,000 and 17,499 annual  
17 therms,
- 18 ▪ GS-2 includes customers between 17,500 and 49,999 annual  
19 therms,
- 20 ▪ GS-3 includes customers between 50,000 and 249,999 annual  
21 therms,
- 22 ▪ GS-4 includes customers between 250,000 and 499,999 annual  
23 therms, and
- 24 ▪ GS-5 includes all customers above 500,000 annual therms.

25 Peoples performs an annual review of customer consumption and

1 reassigns customers to a different rate schedule on a prospective basis if  
2 necessary.

3 **Q. WHY IS IT APPROPRIATE TO REEXAMINE THE**  
4 **CONSUMPTION THRESHOLDS AMONG PEOPLES' GS RATE**  
5 **CLASSES?**

6 A. The primary purpose of modifying some of the existing breakpoints  
7 between rate classes is to introduce greater homogeneity among customers  
8 served under the same rate schedule. This improves the ability to develop  
9 a fair rate design that achieves the overall pricing goals I described earlier  
10 and reduces the potential for intraclass subsidies among customers. In  
11 addition, it is important to smooth some of the revenue transitions  
12 underlying the existing groupings. The greatest emphasis of the  
13 regrouping is on the existing GS-1 class, which encompasses both the  
14 most diverse range of GS customers as well as largest number of  
15 customers.

16 **Q. PLEASE DESCRIBE THE SPECIFIC CHANGES YOU**  
17 **RECOMMEND.**

18 A. The size of the GS-1 class would be reduced under my proposal by  
19 reclassifying the smallest GS-1 customers into the SGS class and  
20 reclassifying the largest GS-1 customers into the GS-2 class. Specifically,  
21 the SGS class would include all customers with annual usage up to 1,999  
22 therms. The GS-1 class would now include customers from 2,000 up to  
23 9,999 annual therms and the GS-2 class would include customers from  
24 10,000 up to 49,999 annual therms. The annual thresholds and  
25 designations for customers with 50,000 annual therms and above would

1 remain the same as today. Under these new groupings, the largest  
2 customers within any of the rate schedules are no more than five times the  
3 size of the smallest ones measured by annual consumption. This  
4 represents an improvement over the existing groupings.

5 **Q. ARE YOU PROPOSING ANY CHANGE TO THE RESIDENTIAL**  
6 **RATE CLASSES?**

7 A. Yes, but this change is driven by a separate classification issue associated  
8 with common areas of condominiums. The common areas of  
9 condominiums are considered to be for residential use even though many  
10 of Peoples' condominium association customers have load characteristics  
11 that are more similar to GS customers than to residential. As a result,  
12 many condominium association customers have sought to be reclassified  
13 as GS on the basis of various interpretations of the distinctions between  
14 residential and commercial end-uses by the Commission and other Florida  
15 agencies.

16 I am proposing to maintain separate residential and general service  
17 rate schedules for customers below 2,000 annual therms. Residential  
18 customers under this threshold would continue to receive service under the  
19 RS rate schedule. General service customers under this threshold would  
20 be served on the SGS rate schedule, which is now expanded to cover  
21 customers up to 2,000 annual therms. All residential and general service  
22 customers with annual loads of 2,000 therms or greater would be served  
23 under a GS rate schedule based on the new thresholds I described  
24 previously.

25 As a result, all larger condominium associations would be included

1 in a general service rate schedule reflecting the same service pricing as for  
2 GS customers of the same size. In addition, these customers would also  
3 be eligible to purchase supply from a marketer and receive transportation  
4 service under the NCTS rider. All existing condominium transportation  
5 customers whose consumption falls below 2,000 annual therms would be  
6 allowed to continue transporting until such time as the customer elected to  
7 return to bundled sales service.

8 Under my recommendation, condominium association customers  
9 would achieve all of the benefits of service under a GS rate schedule,  
10 while continuing to maintain a residential designation for deposit terms  
11 and conditions. I believe this approach reasonably groups customers with  
12 similar load characteristics under a common rate schedule. Furthermore,  
13 this approach alleviates the need for a case-by-case evaluation of  
14 condominium association customers that believe they should be  
15 designated as GS instead of residential, saving considerable administrative  
16 resources.

17 **Q. HAVE YOU PREPARED A SUMMARY THAT COMPARES THE**  
18 **EXISTING AND NEW GROUPING OF GS AND RS CUSTOMERS?**

19 A. Yes. Exhibit \_\_\_(DPY-2) shows the number of customers and annual  
20 loads for existing GS and RS classes mapped into the new classifications.  
21 Approximately 43% of Peoples' GS customers fall in the new GS-1 group,  
22 compared with 68% under the existing classification. In addition, the new  
23 SGS and GS-2 groups include approximately 34% and 20% of total GS  
24 customers, respectively.

25 **IV. ALLOCATED COST OF SERVICE STUDY**

1 **Q. WHAT IS THE PURPOSE OF AN ALLOCATED COSS AND HOW**  
2 **DOES IT AFFECT THE DEVELOPMENT OF PROPOSED RATES**  
3 **FOR PEOPLES?**

4 A. An allocated COSS provides an excellent means of assessing the  
5 reasonableness of existing prices, and guides the development of price  
6 changes. In particular, the COSS examines all of a utility's common  
7 costs, and through appropriate cost assignments and allocations,  
8 establishes measures of investments, expenses and income by customer  
9 class. An allocated COSS is necessary to determine the cost responsibility  
10 of each customer class because many of the Company's costs are common  
11 and are incurred collectively to serve multiple classes of customers.

12 The COSS calculates the total investment and operating costs  
13 incurred to serve each customer class by establishing class-specific total  
14 revenue requirements. The class-specific revenue requirements are  
15 compared to class revenues in order to establish class income. Class-  
16 specific income is then compared to allocated rate base in order to  
17 determine class rate of return on investment. The class-specific rates of  
18 return are used to guide the apportionment of the revenue increase among  
19 all of Peoples' customer classes in conjunction with the development of  
20 proposed rates. The COSS also determines the classification of costs  
21 among demand, customer and commodity components. The classification  
22 of costs within a customer class is used to guide the development of the  
23 form of billing rates for that class. Although the COSS is not the only  
24 factor relied upon to design rates, it is an invaluable guide to ensuring that  
25 the process is fair and reasonable.

1 **Q. WHAT PRINCIPLES GUIDE THE DEVELOPMENT OF THE**  
2 **COSS YOU ARE PRESENTING?**

3 A. The primary principle guiding the COSS process is that of cost causation.  
4 That is, each step in the development of a COSS should be consistent with  
5 the factors that drive or contribute to the incurrence of costs on the  
6 Peoples system. For example, the principle of cost causation requires that  
7 the costs incurred by the Company for meter reading be apportioned to  
8 classes on the basis of the number of meter readings in each class.

9 In addition, it is also necessary to take into consideration the  
10 availability of required data and the degree of complexity involved in  
11 performing various aspects of the COSS. For instance, some of the  
12 Company's individual facility investments are decades old, which may not  
13 easily or cost-effectively be associated with an individual customer class  
14 based on available data. In such cases, reasonable approximations that are  
15 consistent with cost causation principles must be made. Similarly, it is not  
16 worthwhile to develop a complex algorithm for allocating a small  
17 investment or operating cost item that would ultimately have little or no  
18 impact on the overall results of the COSS.

19 **Q. PLEASE DESCRIBE THE DATA YOU RELIED ON TO PREPARE**  
20 **THE COSS.**

21 A. The primary data sources fall in two general categories: data related to the  
22 establishment of the total cost of service or revenue requirements, and data  
23 used as the basis for allocating the total cost of service among customer  
24 classes. The total cost of service or revenue requirement data utilized in  
25 the COSS are taken from MFRs filed by Peoples in this proceeding. The

1 Company's forecasts of sales, customers and revenues by class as adjusted  
2 for pro forma changes, and contained in the MFRs, are used as allocation  
3 bases for several categories of costs. The remaining allocation data are  
4 derived from studies of facility investments, which will be described later  
5 in my testimony. All of the data utilized in the COSS correspond to a  
6 common time period of January through December 2009. This is the  
7 projected test year, which is the period for which rates are to be  
8 determined.

9 **Q. WHAT STEPS ARE FOLLOWED IN PREPARING THE COSS?**

10 A. The COSS follows a simple two-step process to arrive at appropriate  
11 allocations for each rate schedule. The first step in the process, cost  
12 classification, separates costs according to the primary cost causative  
13 forces exhibited on Peoples' system. The cost classifications used in the  
14 COSS relate to fixed costs required to serve peak requirements (demand-  
15 related), fixed costs associated with providing customers with access to  
16 and active status on the system (customer-related), and variable costs  
17 associated with system throughput (commodity-related). Second, cost  
18 allocation takes each classification of cost and apportions that cost to each  
19 of the Company's customer classes. Cost allocation utilizes a variety of  
20 factors to apportion the various types of costs among classes in a manner  
21 that is consistent with principles of cost responsibility.

22 **Q. PLEASE DESCRIBE THE FACILITY INVESTMENT STUDIES**  
23 **YOU MENTIONED EARLIER.**

24 A. Three facility investment studies were performed to allocate significant  
25 components of the Company's rate base as follows:

1                   **(1) Meter and Service Investment Study:** The typical replacement  
2                   cost of connecting each class of customer including service,  
3                   meter and meter installation costs formed the basis for allocating  
4                   the associated rate base included in Peoples' cost of service. The  
5                   allocation of these investments was performed using a weighted-  
6                   customer allocator derived from the forecasted number of  
7                   customers and relative investment in meters and services  
8                   compared to the residential class.

9                   **(2) Mains Investment Study:** The Company's investment in mains  
10                  was segregated into three categories based on a replacement cost  
11                  analysis. The three categories were distinguished by pipe  
12                  diameter size with 0-4" representing small, 4-8" representing  
13                  medium and 8" and above representing large diameter mains.  
14                  Based on typical facility configurations, large diameter mains  
15                  were allocated to all customers with the exception of those  
16                  directly served off of a dedicated interconnection with an  
17                  interstate pipeline. Medium diameter mains were allocated to all  
18                  customers up to GS-5 and SIS. Lastly, small diameter mains  
19                  were allocated to all customers up to GS-4.

20                 **(3) Direct Assignment Study:** Customer-specific investments in  
21                 mains, services and meters for the SIS, IS, ISLV and Special  
22                 Contract classes were utilized to allocate rate base investment  
23                 costs to Peoples' largest customers.

24                 Approximately 90% of the Company's total rate base is allocated  
25                 based on the results of these facility studies.



1 **Q. PLEASE DESCRIBE THE RESULTS OF THE COSS.**

2 A. The results of the COSS indicating the rate of return by class are provided  
3 on Exhibit \_\_ (DPY-3). As shown on this exhibit, the rate of return for the  
4 residential class is only 2.45%, well below the current system-average rate  
5 of return of 6.02%. The residential class is by far Peoples' largest class in  
6 terms of number of customers. Other classes that are earning below the  
7 system-average rate of return include the CSLS, CS-SG, SGS and NGVS  
8 classes. Classes that are earning near the system-average rate of return  
9 include the GS-1 through GS-5 and WHS classes, while the largest  
10 customers on the system in the SIS, IS, ISLV and Special Contract classes  
11 are earning above the system average rate of return.

12 Exhibit \_\_ (DPY-3) also provides the required revenue increase  
13 and associated percentage increase for each of the classes that is necessary  
14 to yield the proposed overall rate of return on rate base of 8.88%. While  
15 most classes would require a base rate increase in order to yield an 8.88%  
16 rate of return, the residential class indicates the largest required increase of  
17 approximately \$15.7 million. The RS-SG, IS and ISLV classes indicate a  
18 small decrease in rates is appropriate based on the underlying cost of  
19 providing service.

20 **Q. PLEASE DESCRIBE THE RESULTS OF YOUR COSS WITH**  
21 **RESPECT TO CUSTOMER-RELATED COSTS.**

22 A. Monthly customer costs are derived from the costs that are classified as  
23 customer-related and the apportionment of these costs to Peoples' various  
24 customer classes. The system-wide average monthly customer cost is  
25 \$21.09, and the cost generally varies with the size of the customer. The

1 lowest average customer cost of \$15.45 per month is indicated for the  
2 residential customer class.

3 **Q. ARE THERE DETAILED SCHEDULES SUPPORTING THESE**  
4 **RESULTS?**

5 A. Yes. Schedule H-1 of the Company's MFRs provides detailed reporting  
6 of all COSS results. Specifically, Schedule H-1, pages 3 and 4 provide the  
7 allocated cost of service associated with each class, which is compared to  
8 the existing revenues to yield the class-specific revenue deficiency. Also,  
9 Schedule H-1, pages 5 and 6 provide a class-specific income statement  
10 showing the earned rate of return by class.

11 **Q. PLEASE DESCRIBE THE IMPLICATIONS OF THE COSS**  
12 **RESULTS FOR PEOPLES' RATE DESIGN.**

13 A. The results of the COSS clearly indicate that class-differentiated base rate  
14 revenue increases are appropriate given the disparity in rates of return by  
15 customer class. In addition, the monthly customer-related costs should be  
16 taken into consideration in the development of proposed modifications to  
17 existing customer charges.

18 **V. DEVELOPMENT OF PROPOSED RATE DESIGN**

19 **Q. PLEASE EXPLAIN THE STEPS YOU PERFORMED TO**  
20 **DEVELOP SPECIFIC CHARGES APPLICABLE TO EACH**  
21 **CUSTOMER CLASS.**

22 A. First, I determined the class-by-class revenue requirements, which reflect  
23 the results of the COSS and other rate design principles. Next, I evaluated  
24 the existing level of customer charges and proposed increases, where  
25 appropriate, to recover a greater proportion of customer-related costs

1 through the customer charges. Lastly, I established the appropriate peak  
2 demand rate.

3 **Q. HOW DID YOU DEVELOP THE REVENUE REQUIREMENT TO**  
4 **BE RECOVERED THROUGH THE RATES APPLICABLE TO**  
5 **EACH CUSTOMER CLASS?**

6 A. The revenue requirement by customer class is based upon the rates of  
7 return under the present rates as well as the required increase by class to  
8 achieve the overall rate of return of 8.88%. In most cases, the increase to  
9 each class is equal to that required to achieve a uniform rate of return at  
10 proposed rates.

11 Within the residential classes, I established a new rate for the  
12 residential generator class that yielded a rate of return that is above system  
13 average. This is a reasonable approach given the uncertainty with respect  
14 to when these customers will take service from Peoples and the potential  
15 cost consequences that may differ from those captured through a COSS  
16 analysis. Further, the fact these customers have elected to install gas fired  
17 back-up generators, which will only be used in emergencies, reflects that  
18 they value the service offered. The increased revenues received from the  
19 residential generator class offset the increase applied to the RS class.

20 A second exception to a pure cost-based revenue allocation was  
21 associated with the NGVS class. In this case, the COSS indicates a  
22 substantial revenue increase is required; however, I limited the increase to  
23 one-half of the required amount. Applying a reduced allocation is  
24 appropriate to moderate the rate impact to NGVS customers as well as to  
25 support the potential advanced market penetration in vehicle markets,

1 which would support Florida's energy policy goals.

2 The last exception relates to commercial customers within the GS-  
3 2 through GS-4 designations. Specifically, I reduced the revenue  
4 allocation to the GS-4 class as a means of lowering the current per-therm  
5 rate differential between the GS-4 and GS-5 classes. The difference as  
6 well as the revenue reduction to NGVS customers is made up through an  
7 increased revenue allocation to GS-2 and GS-3 classes. The increased  
8 revenues to these two classes result in base rate increases that remain  
9 below the system-average increase.

10 The proposed base revenue increase by class is summarized in  
11 Exhibit \_\_\_ (DPY-4). In addition, I have reflected the proposed revenues  
12 in the COSS in order to derive class-specific rates of return on rate base.  
13 These are shown in Exhibit \_\_\_ (DPY-5) in absolute terms and in relation  
14 to the proposed system-average return.

15 **Q. WHY IS IT APPROPRIATE TO REDUCE THE PER-THERM**  
16 **RATE DIFFERENTIAL BETWEEN THE GS-4 AND GS-5**  
17 **CLASSES?**

18 A. GS-4 customers are not markedly different in size than GS-5 customers.  
19 Under the existing pricing structure, the per-therm charge applicable to  
20 GS-5 use is 44% below the corresponding charge for GS-4 customers.  
21 Given the fact that the majority of revenues for these classes are recovered  
22 through the per-therm charges, uneven revenue consequences result when  
23 customers cross-over the threshold of 500,000 annual therms between  
24 these classes. I am particularly concerned that GS-5 customers that may  
25 reduce their usage and fall into the GS-4 class would end up paying more

1 in base revenues than if they had not reduced their consumption. The  
2 revenue allocation I propose reduces the impact of this phenomenon on  
3 customers. It may be appropriate in a future base rate proceeding to  
4 consolidate the GS-4 and GS-5 classes into a single rate schedule.

5 **Q. HAVE YOU PERFORMED A COMPARISON OF EXISTING**  
6 **MONTHLY CUSTOMER CHARGES AND MONTHLY**  
7 **CUSTOMER COSTS?**

8 A. Yes. Exhibit \_\_\_ (DPY-6) shows the difference between existing monthly  
9 customer charges and monthly customer costs as determined by the COSS.

10 **Q. WHY IS THE LEVEL OF THE CUSTOMER CHARGE**  
11 **IMPORTANT?**

12 A. The level of the customer charge is important for a variety of reasons.  
13 First, the customer charge provides customers with an important price  
14 signal concerning the impact of connecting to Peoples' distribution system  
15 because it is a charge payable every month whether or not any gas is  
16 consumed. Second, recovering customer-related costs through customer  
17 charges contributes to intra-class fairness. Third, the customer charge  
18 provides revenue stability for the Company by allowing it to recover fixed  
19 costs that are incurred to serve customers through a fixed charge.

20 **Q. ARE YOU PROPOSING ANY MODIFICATION TO THE RATE**  
21 **STRUCTURE APPLICABLE TO RESIDENTIAL CUSTOMERS?**

22 A. Yes. I am proposing to substantially increase the proportion of fixed costs  
23 recovered through the customer charge for residential customers.  
24 However, this could lead to undesirable bill impacts for smaller residential  
25 customers. As a means of mitigating these bill impacts, I am proposing

1 distinct monthly customer charges for different sizes of residential  
2 customers.

3 **Q. PLEASE DESCRIBE THE SPECIFIC CHARGES YOU ARE**  
4 **RECOMMENDING FOR RESIDENTIAL CUSTOMERS.**

5 A. First, I established the proposed customer charges for the three sizes of  
6 residential customers. Residential customers with annual use between 0  
7 and 99 therms would pay a monthly customer charge of \$12. Residential  
8 customers with annual use between 100 and 249 therms would pay a  
9 monthly customer charge of \$15 and residential customers above 250  
10 annual therms would pay a monthly customer charge of \$20. The average  
11 monthly customer charge of \$15.40 is very close to the monthly customer  
12 cost associated with serving Peoples' residential customers. The  
13 remaining revenue requirements allocated to the residential class are  
14 recovered through an equal per-therm charge of \$0.32120.

15 Larger residential customers will experience a more substantial  
16 increase to the existing monthly customer charge of \$10. However, the  
17 specific charges and therm thresholds I am proposing result in reasonable  
18 bill impacts across the entire residential class. This results from the fact  
19 that the higher customer charges for larger residential customers are offset  
20 by a lower proposed per-therm charge, which also has the greatest impact  
21 on reducing bills for those customers that will pay the higher customer  
22 charges.

23 **Q. HOW DID YOU DERIVE PROPOSED RATES FOR THE GS**  
24 **CUSTOMER CLASSES?**

25 A. The proposed rates for the GS classes were developed using the same

1 approach as for the residential class. I first established an appropriate  
2 customer charge for each class. The proposed customer charge for the  
3 SGS class is \$25.00 per month, a 25% increase over the existing level of  
4 \$20.00. Similarly, I recommend increases to the customer charges for  
5 other GS classes to yield new charges that range from \$35.00 for GS-1  
6 customers to \$300.00 per month for GS-5 customers. For each GS class,  
7 the remaining revenue requirements indicated in Exhibit \_\_ (DPY-5) are  
8 recovered through revised per-therm charges.

9 **Q. PLEASE DESCRIBE THE PROPOSED CHANGES TO THE**  
10 **RATES FOR THE STANDBY GENERATOR CLASSES.**

11 A. These rate schedules were developed since the last rate case in response to  
12 customer needs. I propose to continue the same form of rate design,  
13 which reflects a higher fixed customer charge given these customers may  
14 go for extended periods without using their natural gas service. However,  
15 I am proposing to derive the average fixed charge based on 20 therms for  
16 residential standby generators and 40 therms for commercial standby  
17 generators. Any use above these levels would be priced at the existing  
18 delivery charge reflected in the corresponding RS-SG or CS-SG rate  
19 schedule. The customer charge for the residential standby generator class  
20 is set equal to the largest customer charge for residential customers, or  
21 \$20. Similarly, the customer charge for commercial standby generators is  
22 \$35, which is equal to the proposed customer charge for GS-1 customers.

23 **Q. PLEASE SUMMARIZE YOUR FINDINGS WITH RESPECT TO**  
24 **THE RATES YOU ARE PROPOSING FOR PEOPLES.**

25 A. My testimony concerning Peoples' rates leads to two important

1 conclusions. The first is that a greater proportion of fixed costs should be  
2 recovered through fixed charges. The second is that non-uniform  
3 increases in class-specific revenue requirements are appropriate to reflect  
4 the underlying cost of providing service. These conclusions are supported  
5 by the COSS I am supporting in this proceeding.

6 Increasing fixed charges will better align Peoples' prices with  
7 underlying costs of providing service, thereby improving price signals to  
8 customers and achieving a greater degree of fairness. Existing customer  
9 charges for most customers are substantially below cost-based levels and  
10 should be increased by a greater percentage than the overall level of  
11 increase in base rates proposed by Peoples. Lastly, increased use of fixed  
12 charges to recover fixed costs is consistent with recent initiatives to  
13 promote greater energy efficiency and conservation by customers.

14 The proposed class-specific revenue requirements reasonably  
15 apportion the Company's requested revenue increase among rate classes.  
16 The results of the COSS indicate that the class-specific rate of return for  
17 residential customers is lower than for most other customer groups and is  
18 contributing more significantly to the need for rate relief. By assigning  
19 the largest proportion of the revenue increase to the residential class, the  
20 proposed class-specific revenue requirements promote fairness. In most  
21 cases, the rates that I propose are designed to recover the target revenues  
22 indicated by the COSS. Limited exceptions are associated with the  
23 NGVS, RS-SG and GS-2 through GS-4 classes.

24 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

25 **A.** Yes, it does.



1           CHAIRMAN CARTER: Okay. Commissioners, I'm  
2 going to keep my commitment to you about us for today.  
3 I suppose we can probably get started, but we are going  
4 to break at the time that I gave, because I know you  
5 made plans based on that representation, and I'm going  
6 to keep my word to you. So let's do this. We can at  
7 least get the witness on the stand and go from there.

8           Call your next witness.

9           MR. WATSON: Lewis Binswanger.

10          Thereupon,

11                           LEWIS M. BINSWANGER

12 was called as a witness on behalf of Peoples Gas System  
13 and, having been first duly sworn, was examined and  
14 testified as follows:

15                           DIRECT EXAMINATION

16          BY MR. WATSON:

17           Q. Please state your name and business address.

18           A. Lewis Binswanger, 704 Franklin Street, Tampa,  
19 Florida.

20           Q. By whom are you employed, and in what  
21 position?

22           A. Peoples Gas, Director of Strategic Planning  
23 and Regulatory.

24           Q. Did you prepare and cause to be prefiled in  
25 this proceeding direct testimony consisting of 25 pages?

1           A.    Yes.

2           Q.    Do you have any corrections or changes to that  
3 testimony?

4           A.    I do.  I have three corrections.  They were  
5 typographical errors.

6                    On page 20 of my direct testimony, line 10,  
7 there's a reference to Sheets Number 7.807 through  
8 7.807-2.  It should be "dash 3."  On page 24, line 6,  
9 the year should be 2010 rather than 2011.

10                   And on Exhibit LMB-2, the notes on the bottom,  
11 Note B should say, "Applicable depreciation rate is  
12 2.9," rather than 2.4.

13           Q.    Well, you jumped ahead of me on the exhibit,  
14 but did you file two exhibits marked as Exhibits LMB-1  
15 and LMB-2 and identified as Hearing Exhibits 60 and 61?

16           A.    I did.

17           Q.    And the correction you gave to that exhibit  
18 has already been given?

19           A.    Yes.

20                   MR. WATSON:  Mr. Chairman, we would ask that  
21 Mr. Binswanger's prefiled direct testimony be inserted  
22 into the record as though read.

23                   CHAIRMAN CARTER:  The prefiled direct  
24 testimony of the witness will be inserted into the  
25 record as though read.

1                   MR. WATSON: And that his Exhibits LMB-1 and  
2 LMB-2 be formally identified for the record as Hearing  
3 Exhibits 60 and 61.

4                   CHAIRMAN CARTER: For the record, identified  
5 as Exhibits 60 and 61.

6                   (Exhibits 61 and 62 were identified for the  
7 record.)

8 BY MR. WATSON:

9                   Q. Mr. Binswanger, if I were to ask you the  
10 questions in your direct testimony today, would your  
11 answers be the same?

12                   A. Yes.

13                   MR. WATSON: We would ask that  
14 Mr. Binswanger's direct testimony be inserted into the  
15 record as though read.

16                   CHAIRMAN CARTER: The prefiled direct  
17 testimony of the witness will be inserted into the  
18 record as though read.

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1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Lewis M. Binswanger and my business address is 702 N.  
3 Franklin Street, Tampa, Florida 33602.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am employed by Peoples Gas System ("Peoples" or the "Company") as  
6 Director, Strategic Planning and Regulatory.

7 **Q. PLEASE PROVIDE A BRIEF OUTLINE OF YOUR**  
8 **EDUCATIONAL BACKGROUND AND BUSINESS EXPERIENCE.**

9 A. I received a Bachelor of Science degree in Electrical Engineering in 1982  
10 from the University of Texas at El Paso. I am a registered professional  
11 engineer in the State of Texas. In 1998, I completed a Finance and  
12 Accounting Executive Program at the Wharton School of the University of  
13 Pennsylvania.

14 I have diverse business experience with over 25 years in the energy  
15 industry. I have managed several different energy business segments  
16 including areas responsible for engineering, operations, marketing,  
17 regulatory and customer service. In recent years, I have held senior  
18 management positions including Vice President Operations, Chief  
19 Engineer, Vice President Technical Services, General Manager and  
20 Director.

21 I have been employed by Peoples since 2001, when I was hired as  
22 General Manager for the South Region. My responsibility at that time was  
23 the overall management of distribution, transmission, engineering,  
24 marketing and retail sales of natural gas to over 100,000 customers in nine  
25 counties and 60 municipalities. Over 230 team members located in six

1 different division offices were under my supervision. I relocated to  
2 Tampa in 2005 to assume the position of Director of Operations for one  
3 year, after which I became Director, Strategic Planning and Regulatory.

4 **Q. WHAT ARE YOUR CURRENT RESPONSIBILITIES?**

5 A. I am responsible for Peoples' overall strategic plans and for directing rate  
6 and regulatory matters under the jurisdiction of the Florida Public Service  
7 Commission (the "Commission"). I have also coordinated the preparation  
8 and filing of Peoples' case in this proceeding. I am a member of the  
9 American Gas Association's Rates Committee and the Southern Gas  
10 Association's Rates and Regulatory Affairs Committee.

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

12 A. The primary purpose of my testimony is to explain and support Peoples'  
13 proposed Gas System Reliability Rider and Carbon Reduction Rider.

14 The Gas System Reliability Rider ("Rider GSR") is designed to  
15 address and help manage the substantial investments the Company must  
16 make each year due to government-mandated relocations of Peoples'  
17 facilities. The Carbon Reduction Rider ("Rider CR") is designed to  
18 address, manage, and encourage the expansion of natural gas to new  
19 developments that are not located near interstate pipelines or existing  
20 Company supply mains.

21 To place the purposes of these riders in proper perspective, I will  
22 first explain Peoples' standard policy of routing supply and distribution  
23 mains in public rights-of-way. I will also explain the challenges the  
24 Company faces when deciding whether to extend its facilities to make  
25 natural gas available to new residential and commercial developments.

1           Because the policy and the challenges encountered are interrelated, both  
2           will be discussed in the context of potential system expansions.

3           I will also describe how expanding the Peoples system supports the  
4           State of Florida's carbon dioxide ("CO<sub>2</sub>") emissions reduction initiatives  
5           and energy conservation efforts. Lastly, I will describe Peoples' safety  
6           and reliability efforts with respect to underground main and service lines.

7   **Q. DO YOU HAVE ANY EXHIBITS TO BE INTRODUCED IN THIS**  
8   **PROCEEDING?**

9   A. Yes. I am sponsoring, and prepared or caused to be prepared, Exhibits  
10       \_\_\_(LMB-1) through \_\_\_(LMB-2). I will also refer to portions of the  
11       new tariff sheets contained in Schedule E-9 of the MFRs (Composite  
12       Exhibit \_\_ (PGS-1)) when discussing Rider GSR and Rider CR.

13 **Q. HOW DOES PEOPLES DECIDE WHETHER IT WILL EXTEND**  
14 **ITS FACILITIES TO SERVE CUSTOMERS IN AN AREA NOT**  
15 **PREVIOUSLY HAVING NATURAL GAS SERVICE?**

16 A. Unless the area – generally a new development that will eventually consist  
17       of new homes and accompanying commercial development – is located  
18       adjacent to, or relatively near, an interstate pipeline or a Peoples supply  
19       main with adequate existing capacity to serve the development, the  
20       decision can be difficult. While interstate pipelines traverse Florida, the  
21       proximity of potential new customers to the pipelines, or to existing  
22       Peoples supply mains, can range from less than a mile to tens of miles.  
23       This proximity directly impacts Peoples' multi-step decision of whether or  
24       not to serve a new development.

25 **Q. PLEASE EXPLAIN THAT PROCESS.**

1 A. When a new development is identified, steps are taken to ensure that  
2 natural gas can be delivered either from a transmission pipeline, or an  
3 existing Peoples supply main, to the potential new customers in a safe,  
4 reliable and economical manner. At a high level, the steps are to  
5 determine the development's gas load potential, design the distribution  
6 main, and design the supply main. The distribution main is the main that  
7 will traverse the development, and off of which service lines will be run to  
8 serve individual customers. The supply main, if any, is the main that will  
9 be installed between a Peoples connection with an interstate pipeline, or  
10 existing Peoples supply main, and the distribution main.

11 **Q. PLEASE DESCRIBE THE FIRST STEP.**

12 A. In the first, or gas load determination step, Peoples obtains information  
13 with respect to potential natural gas load and customer locations in the  
14 proposed development. The Company meets with the potential developers  
15 and thoroughly reviews their master plans. Land use zone maps are  
16 reviewed to estimate the commercial and residential development mix that  
17 may occur in the proposed development.

18 Timing for build-out of the development is a critical part of the gas  
19 load determination phase because residential and commercial  
20 developments typically build out over several years. Smaller  
21 developments (less than 300 homes) generally fully build out in as little as  
22 three to five years, while larger developments of over 1,000 homes can  
23 fully build out in eight to 12 years. Overall economic conditions often  
24 affect these time frames. Completion of this phase results in a load  
25 forecast showing gas load locations and a preliminary build-out timeline

1 for the potential project.

2 **Q. WHAT ARE THE NEXT STEPS IN THE PROCESS?**

3 A. In the second step, the distribution main and service lines that will serve  
4 customers in the development are designed. Designing a distribution main  
5 requires each customer's estimated hourly demand for gas to be identified  
6 in the various locations within the proposed development. Company  
7 engineers use the estimated customer hourly demand to properly size the  
8 distribution main and service lines so Peoples can deliver natural gas at  
9 any time, on any day, during any year. The diameters of typical  
10 distribution mains range from two inches to four inches, and of service  
11 lines from three-quarters of an inch to two inches. Completion of this  
12 phase results in the design criteria for a natural gas distribution system,  
13 together with construction cost estimates.

14 The third step is the design of the natural gas supply main and  
15 associated appurtenances that will connect the development distribution  
16 system to the interstate transmission pipeline system or an existing  
17 Peoples supply main. Supply main design requirements include the length  
18 of the main, hourly customer demand and available gas supply pressure.  
19 To properly design the city gate station, regulator station, and supply  
20 main, Company engineers use available delivery pressure data from the  
21 interstate pipeline. Typical interstate pipeline operating pressures range  
22 from 750 to 1,480 pounds per square inch gauge ("psig"), so pressure-  
23 reducing equipment or regulator stations must be designed and installed to  
24 meet gas delivery requirements.

25 As I mentioned earlier, the proximity of a potential residential



1 and/or commercial development to an interstate pipeline system can range  
2 from less than a mile to tens of miles. Company engineers use the actual  
3 distance to design the proper size and operating pressure of the supply  
4 main. Typical supply main diameters are greater than four inches or  
5 certified to operate at pressures above 60 psig. Completion of this phase  
6 results in the designs for a city gate station, regulator station(s) and supply  
7 main, along with estimated construction costs.

8 **Q. HOW ARE SUPPLY AND DISTRIBUTION MAINS ROUTED?**

9 A. Peoples installs many miles of natural gas main annually and strives to do  
10 so in the most economical manner practicable, meaning we make every  
11 effort to select supply and distribution main routes that minimize  
12 installation cost. This typically means selecting the shortest possible route  
13 from supply source to the end-use customer. Peoples' standard practice is  
14 to install supply and distribution main within and at the edge of public  
15 rights-of-way at a depth of about 36 inches.

16 **Q. WHY IS INSTALLATION IN PUBLIC RIGHT-OF-WAY**  
17 **PEOPLES' STANDARD PRACTICE?**

18 A. Selecting a route for a natural gas main installation provides at least a  
19 theoretical choice between installing in private right-of-way or in public  
20 right-of-way. Installing in public right-of-way is substantially less  
21 expensive since the private right-of-way may require costly land  
22 acquisition or easements from one or more private entities. Installation of  
23 main in private right-of-way may also be almost impossible in instances  
24 where the main would occupy the land of several different land owners,  
25 which in most instances means it is not practical, and would be more

1           costly, to install supply or distribution mains within cities and residential  
2           developments.

3   **Q.   DOES PEOPLES HAVE CERTAIN RIGHTS TO USE PUBLIC**  
4           **RIGHT-OF-WAY FOR THE INSTALLATION OF NATURAL GAS**  
5           **INFRASTRUCTURE?**

6   A.   Yes. Peoples installs natural gas facilities in several different government-  
7           owned public rights-of-way including those owned or controlled by the  
8           Florida Department of Transportation, counties, municipalities and water  
9           management districts. Provisions for public utilities' use of these rights-  
10          of-way are made by statute, regulation, ordinance or franchise agreement.  
11          There may be costs, such as permit fees, associated with the Company's  
12          use of these rights-of-way, but they are generally far less than the costs  
13          associated with the Company's acquiring property or easements needed to  
14          install under privately owned lands. Even greater economies can be  
15          obtained if an installation in public right-of-way can be accomplished at  
16          the same time other utility facilities, such as water and wastewater  
17          facilities, are installed.

18   **Q.   DOES INSTALLING FACILITIES IN PUBLIC RIGHT-OF-WAY**  
19          **SUBJECT PEOPLES TO ANY REQUIREMENTS OF THE PUBLIC**  
20          **ENTITY CONTROLLING THE RIGHT-OF-WAY?**

21   A.   Yes. Peoples must generally abide by various rules, regulations and other  
22          requirements. These may include, but are not limited to, requirements that  
23          natural gas mains or service lines be installed at depths which will not  
24          conflict with other structures, requirements that the natural gas facilities be  
25          relocated in the future when mandated by the governmental entity

1 controlling the right-of-way, not installing natural gas facilities under  
2 pavement, and providing proper traffic control during construction and  
3 maintenance of the natural gas facilities.

4 **Q. CAN GOVERNMENTAL ENTITIES ORDER PEOPLES TO MOVE**  
5 **ITS FACILITIES INSTALLED IN THE PUBLIC RIGHT-OF WAY?**

6 A. Yes. When Peoples installs mains or service lines in, under or along  
7 public rights-of-way such as streets, roads and highways, the Company is  
8 generally required – by statute, rule or local franchise or ordinance – to  
9 relocate the facilities when the governmental body controlling the right-of-  
10 way orders the Company to do so. The entity may be re-routing or  
11 widening a road, installing or relocating water or wastewater lines, or re-  
12 configuring an intersection. In most instances, Peoples must replace or  
13 relocate its facilities at its own expense, without reimbursement, just to  
14 continue to meet its service obligations.

15 **Q. DOES PEOPLES ATTEMPT TO MINIMIZE OR LIMIT**  
16 **GOVERNMENT-MANDATED RELOCATIONS?**

17 A. Yes, the Company makes those efforts during the design phase of a  
18 project, as well as after the facilities have been placed in service.

19 The design phase is Peoples' first opportunity to minimize the  
20 possibility of a relocation mandate. Natural gas facilities are typically  
21 installed at the edge of rights-of-way, away from facilities of other  
22 utilities. In addition, the main in a development is generally installed  
23 behind the curb at a depth to avoid any conflict with road work or  
24 underground improvements.

25 Once Peoples' facilities have been installed and are in service, the

1           Company provides the government entity maps showing the location of  
2           natural gas facilities. To the extent possible, Peoples enlists the assistance  
3           of the governmental entity design engineer in making accommodations for  
4           the natural gas facilities to minimize any requirement that the Company  
5           relocate them.

6       **Q.   IF ALL OPTIONS HAVE BEEN EXHAUSTED, WHAT IS THE**  
7       **COMPANY'S PROCESS FOR PHYSICALLY RELOCATING ITS**  
8       **NATURAL GAS FACILITIES?**

9       A.   At this point, the Company has no choice but to prepare for the facilities  
10       relocation, including designing and engineering how natural gas service  
11       will be maintained to affected customers while new facilities are installed.  
12       The steps required to relocate facilities are similar to those I previously  
13       described when the Company plans for a new installation; that is,  
14       determining existing customers' loads, designing and routing supply  
15       and/or distribution mains, and coordinating actual construction with the  
16       requirements of the government entity that has mandated the relocation.

17      **Q.   WHY DOES THE COMPANY HAVE NO CHOICE IN WHETHER**  
18      **OR NOT IT RELOCATES ITS FACILITIES?**

19      A.   As I stated earlier, Peoples' rights to install supply and distribution main  
20      in public rights-of-way are in most cases subject to the requirement that  
21      the Company relocate its facilities if conflicts develop with work  
22      performed by or on behalf of a governmental entity within the right-of-  
23      way. As a practical matter, receipt of a relocation order also puts the  
24      Company on notice that at some point in the near future, actual road  
25      construction work will begin, increasing the possibility of damage to the

1           Company's underground facilities if they are not relocated outside the  
2           construction zone.

3                     Construction contracts between government entities and road work  
4           contractors also typically include completion deadlines. If Peoples' failure  
5           to timely relocate its facilities causes a contractor's failure to meet the  
6           completion deadline, the contractor and/or the governmental entity could  
7           impose fees on the Company for downtime reimbursement. Finally, as a  
8           practical matter, project delays caused by the Company also create ill will  
9           between Peoples and government entities.

10   **Q.   WHAT IS PEOPLES' ANNUAL CAPITAL COST FOR THESE**  
11   **GOVERNMENT-MANDATED RELOCATIONS?**

12   A.   The capital costs the Company has incurred for such relocations for each  
13   of the last five years are:

14	<u>Year</u>	<u>Cost in Millions</u>
15	2003	\$3.8
16	2004	\$4.3
17	2005	\$5.2
18	2006	\$2.9
19	2007	\$5.2

20                     For 2008 and the projected test year, the capital budget for these  
21   expenditures is \$6.3 million and \$3.8 million, respectively.

22                     Of the capital expenditures for this five-year period, Peoples has  
23   been able to recover its depreciation expense and earn a return only on  
24   those for 2003 – which was the projected test year in Peoples' last rate  
25   case. For the four years from 2004 through 2007, there were total capital

1 expenditures of \$17.6 million for government-mandated relocations for  
2 which Peoples received no revenues through which to recover the  
3 associated depreciation and ad valorem tax expenses or a return on its  
4 investment in the replacement facilities.

5 **Q. DOES PEOPLES INCUR OTHER GOVERNMENT-MANDATED**  
6 **EXPENDITURES?**

7 A. Yes. As Paul Higgins has testified, Peoples has included over \$750,000 in  
8 operations and maintenance (“O&M”) expense for the projected test year  
9 as a result of the federal Pipeline Safety Act of 2002 (the “2002 Act”), the  
10 Pipeline Inspection, Protection, Enforcement, and Safety Act of 2006  
11 passed by Congress and signed into law by President Bush (Public Law  
12 109-468, the “PIPES Act”) in December 2007, and the U.S. Department of  
13 Transportation’s Pipeline and Hazardous Materials Safety  
14 Administration’s (“PHMSA’s”) current and proposed regulations  
15 implementing those acts. The 2002 Act required the implementation of  
16 integrity management activities with respect to “transmission” pipelines,  
17 and the PIPES Act required similar measures with respect to “distribution”  
18 pipelines. The effect on Peoples of the 2002 Act and PHMSA’s  
19 implementing regulations was limited because of the relatively small  
20 proportion of pipelines within Peoples’ system that are classified as  
21 *transmission pipelines*. However, as Mr. Higgins has testified, the impact  
22 of the PIPES Act and PHMSA’s implementing regulations will much  
23 more directly affect Peoples and other natural gas local distribution  
24 companies (“LDCs”).

25 **Q. IS PEOPLES REQUIRED TO COMPLY WITH THE ACTS AND**

1           **THE IMPLEMENTING REGULATIONS?**

2       A.     Yes. The Company has no control over incurring the associated O&M  
3           expenses which will be required to comply with the acts. As shown by  
4           Mr. Higgins' Exhibit \_\_\_(JPH-4), the Company will incur government-  
5           mandated O&M expenses through 2013. As he also testified, the full  
6           impact of the costs of complying with the acts and the implementing  
7           regulations is not known, and not every item of the compliance costs will  
8           be incurred in every year.

9                     In essence, these government-mandated compliance costs are no  
10           different than the government-mandated relocation costs Peoples incurs as  
11           a result of installing its facilities in public rights-of-way – the Company  
12           simply has no control over the incurrence of the costs.

13       **Q.     RETURNING TO YOUR DISCUSSION OF THE STEPS**  
14           **INVOLVED IN EXPANSION OF FACILITIES, ONCE THE STEPS**  
15           **YOU DESCRIBED HAVE BEEN COMPLETED, HOW DOES**  
16           **PEOPLES DECIDE WHETHER TO EXPAND ITS**  
17           **INFRASTRUCTURE TO DELIVER GAS TO A PROPOSED NEW**  
18           **DEVELOPMENT?**

19       A.     Whether or not the Company will actually construct the facilities needed  
20           to deliver natural gas to a new development is largely a financial decision,  
21           one driven by a number of factors. The primary factor is the cost of  
22           installing the supply main. The supply main produces no revenues, but  
23           without it, potential revenue-producing customers in the development  
24           cannot become customers. The often lengthy lag between the time the  
25           Company must make the capital expenditures to install the necessary

1 facilities, and the time the development will be fully built-out also affects  
2 the decision.

3 **Q. ASSUME PEOPLES HAS DESIGNED AND ROUTED THE**  
4 **FACILITIES NEEDED TO SERVE A NEW DEVELOPMENT AND**  
5 **DECIDED TO MAKE THE REQUIRED CAPITAL**  
6 **EXPENDITURES. WHAT IS THE NEXT STEP?**

7 A. An overall timeline for the project is created with different tasks, such as  
8 gate station and regulator station construction (if there is to be a new  
9 connection to an interstate pipeline), and supply and development main  
10 construction to meet the developer's and other potential customers' needs.  
11 Peoples' internal guidelines are to install these facilities no sooner than  
12 absolutely required by the end-use customers to best manage capital.

13 When the first customer in a new development is ready for natural  
14 gas service, the Company will have already placed in service natural gas  
15 facilities that could include a gate station, regulator station(s), supply main  
16 and some or all of the required development main. Facilities that provide  
17 natural gas service must be in place before a single customer can begin to  
18 receive service, even though full build-out of the development, and the  
19 associated revenues, may not occur for several years. This is the major  
20 challenge in bringing the environmental and other benefits of the direct  
21 use of natural gas to more Florida residents.

22 **Q. PLEASE EXPAND ON THOSE ENVIRONMENTAL AND OTHER**  
23 **BENEFITS.**

24 A. Natural gas is an extremely important source of energy for Florida  
25 consumers. It provides economical benefits, is environmentally friendly



1 and domestically produced, with 99% of the natural gas consumed in the  
2 United States originating in North America. Natural gas service is also  
3 very reliable. During the major storms Florida experienced during the  
4 2004 and 2005 hurricane seasons, less than one percent of Peoples'  
5 customers were without gas service. Natural gas appliances also have  
6 lower annual operating costs than appliances that use other fuels.

7 In addition to being a domestically abundant and secure source of  
8 energy, the direct use of natural gas offers a number of environmental  
9 benefits over other sources of energy, particularly other fossil fuels.  
10 Composed primarily of methane, it is the cleanest of all fossil fuels with  
11 the main products of its combustion being CO<sub>2</sub> and water vapor, the same  
12 compounds we exhale when we breathe.

13 Direct use of natural gas is also about 90% efficient compared to  
14 electricity at about 30% when the full fuel cycle is considered. This  
15 efficiency equates to fewer electric power plants required to serve the  
16 same number of customers. In fact, had Peoples' 305,000 residential  
17 customers used all electric appliances, the State of Florida would have  
18 needed an equivalent 250 megawatt power plant that would produced in  
19 excess of 650,000 tons net of carbon dioxide emissions per year.

20 Reducing net carbon emissions attributable to residential customer  
21 energy usage is also a major benefit to Florida. An overall net reduction  
22 of about 4,000 pounds of CO<sub>2</sub> and an annual operating savings of \$75 per  
23 year can be achieved by a residential natural gas customer with a natural  
24 gas dryer, range, water heater and furnace, when compared to a like  
25 residential customer with all electric appliances installed. My Exhibit

1           \_\_\_(LMB-1) shows these annual operating savings along with the reduced  
2           CO<sub>2</sub> emissions of a typical natural gas home versus a typical all-electric  
3           home.

4   **Q.   DESPITE THESE BENEFITS, DOES PEOPLES FACE ANY**  
5           **DIFFICULTIES IN MAKING NATURAL GAS SERVICE**  
6           **AVAILABLE TO MORE CUSTOMERS?**

7   A.   Yes.  Currently, there is only one natural gas customer for every 10  
8           electric customers in Florida.  That is, despite the benefits described,  
9           natural gas end-use represents only about a 10% saturation of the state's  
10          energy customers.

11                 One reason for this low saturation I have already mentioned is the  
12           lack of proximity of potential natural gas customers to natural gas  
13           pipelines, or to existing supply mains of LDCs such as Peoples.  The  
14           Company's engineering requirements to install natural gas supply main to  
15           connect potential end-use customers to transmission pipelines are  
16           challenging both financially and operationally.  Operationally, the supply  
17           main must be in service when the first customer needs natural gas, even  
18           though full build-out of the residential and commercial development may  
19           take 10 or more years.  The simple fact is that supply main investment  
20           must be made so that natural gas is available for the first customer  
21           although the majority of the development's customers may not produce  
22           revenue for several years thereafter.  If Peoples is unable to timely recover  
23           the costs associated with its investment in the supply main, the planning,  
24           engineering and financing of the natural gas infrastructure may occur so  
25           late in the process that the developer may move on with the project and

1 build less environmentally friendly homes.

2 Another reason the Company faces difficulties in making natural  
3 gas available to more customers is that, unlike northern states where  
4 winter temperatures are cold enough to make natural gas heat practically a  
5 requirement for homeowners, many Florida builders and developers don't  
6 believe natural gas is required, even though potential home purchasers  
7 want natural gas.

8 **Q. PLEASE DESCRIBE THE RIDERS FOR WHICH PEOPLES IS**  
9 **SEEKING APPROVAL THAT WILL ADDRESS THE**  
10 **CHALLENGES IN PROVIDING A SAFE, RELIABLE AND**  
11 **ENVIRONMENTALLY FRIENDLY FUEL.**

12 A. As mentioned earlier, there are two -- the Gas System Reliability Rider  
13 ("Rider GSR"), and the Carbon Reduction Rider ("Rider CR").

14 Rider GSR would allow the Company to recover, in a timely  
15 manner, certain costs incurred as a result of government-mandated  
16 relocations of Company facilities or safety requirements.

17 Rider CR would act as an incentive to Peoples in making natural  
18 gas available to customers in areas where it is not currently available by  
19 permitting the Company to recover, on a more timely basis, the costs  
20 associated with installing a supply main that is needed to provide such  
21 service.

22 The two riders are similar in terms of the manner in which eligible  
23 costs would be recovered, and would be similar to the means by which  
24 energy conservation and environmental costs Florida utilities recover. I  
25 will discuss the eligible costs to be recovered under each rider separately,

1           because the costs are different in terms of their qualifying criteria. The  
2           actual recovery mechanism for each rider, however, is virtually identical  
3           to the other.

4   **Q.   WHY IS PEOPLES SEEKING APPROVAL OF THE GAS SYSTEM**  
5   **RELIABILITY RIDER?**

6   A.   Peoples invests millions of dollars annually for the installation and  
7        replacement of natural gas supply and distribution mains, service lines and  
8        other facilities used to provide safe and reliable natural gas service to over  
9        334,000 customers in Florida. As discussed in Bruce Narzissenfeld's  
10       testimony and as I have previously testified, the Company expects to make  
11       capital expenditures of approximately \$60 million in the 2009 projected  
12       test year, approximately \$3.8 million of which is designated for  
13       government-mandated relocations of Company facilities. However, there  
14       can be a significant lag in recovery of the revenue requirements associated  
15       with these capital expenditures from the time the investments are made  
16       until they are included in the Company's rate base in a base rate  
17       proceeding. When these relocations are ordered by the governmental  
18       entity, the expenses of the Company's complying with the order are in  
19       most cases not reimbursed by the governmental entity. In addition,  
20       Peoples anticipates being faced with additional O&M expenses not  
21       covered in the projected test year in this case for pipeline safety mandates  
22       pursuant to the PIPES Act.

23                 Rider GSR would help address this lag and would provide Peoples  
24        more timely recovery of the costs associated with, and recovery of the  
25        weighted average cost of capital on its capital investment. Through timely

1 recovery, the Commission's approval of Rider GSR will also result in the  
2 Company's having more capital dollars available for expansion projects  
3 that would bring the benefits of natural gas to more Florida residents.

4 **Q. IS PEOPLES SEEKING PROJECT "PRE-APPROVAL" BEFORE**  
5 **CAPITAL EXPENDITURES ASSOCIATED WITH RELOCATION**  
6 **PROJECTS ARE MADE?**

7 A. No. The Company must continue to relocate facilities as mandated by  
8 governmental agencies although the recovery mechanism involves  
9 projections of the investments. Resulting costs with a true-up to actual  
10 expenses are proposed to be recovered only on plant investments that have  
11 been placed in service and that are used and useful for Peoples' existing  
12 customer base.

13 **Q. WHAT COSTS WOULD BE RECOVERED UNDER RIDER GSR?**

14 A. The Rider GSR would recover the revenue requirements (i.e., the  
15 Company's weighted average cost of capital, depreciation expense and ad  
16 valorem taxes, grossed up for federal and state income taxes) associated  
17 with eligible infrastructure system replacements. It would also recover  
18 incremental O&M expenses incurred to comply with the federal  
19 transmission and distribution pipeline integrity requirements I have  
20 described. By "incremental," I mean expenses of this type in excess of the  
21 levels included for ratemaking purposes in this proceeding or a subsequent  
22 base rate proceeding.

23 As set forth in Rider GSR, "Eligible Replacements" would consist  
24 of:

25 1. Mains, service lines, regulator stations and other pipeline

1 components installed to comply with state or federal safety requirements  
 2 as replacements for existing facilities;

3 2. Main and service line projects extending the useful life or  
 4 enhancing the integrity of the pipeline components, undertaken to comply  
 5 with state or federal safety requirements; and

6 3. Facility relocations due to construction or improvement of  
 7 a highway, road, street, public way or other public work by or on behalf of  
 8 a government or other entity having the power of eminent domain, to the  
 9 extent costs of the project are not reimbursed to Peoples.

10 No infrastructure system replacement described above would be  
 11 eligible if its cost was included in the Company's most recent base rate  
 12 proceeding, or if it increased the Company's revenues by being directly  
 13 connected to new customers. Since all items of the type described are  
 14 included through the end of the 2009 projected test year in this  
 15 proceeding, no item described above would constitute an Eligible  
 16 Replacement unless installed on or after January 1, 2010.

17 **Q. WHY IS IT APPROPRIATE TO REQUEST O&M EXPENSE FOR**  
 18 **PIPELINE INTEGRITY COSTS IF, ACCORDING TO MR.**  
 19 **HIGGINS' TESTIMONY, PEOPLES HAS ALREADY INCLUDED**  
 20 **\$750,000 FOR THESE COSTS IN THE PROJECTED TEST YEAR?**

21 **A.** *It is appropriate because Peoples cannot predict associated future expenses*  
 22 *and has no ability to prevent the expenses from being incurred. Incurrence*  
 23 *of these expenses is mandated by the federal government.*

24 **Q. IF RIDER GSR IS APPROVED AND, IN 2010, PEOPLES**  
 25 **INCURRED THESE TYPES OF EXPENSES AT A LEVEL LESS**

1           **THAN THE APPROXIMATELY \$750,000 INCLUDED IN THE**  
2           **PROJECTED TEST YEAR, WOULD THE REDUCTION BE**  
3           **CAPTURED IN CALCULATING THE REVENUE**  
4           **REQUIREMENTS TO BE RECOVERED THROUGH THE RIDER?**

5    A.    Yes. Any reduction in O&M expense for transmission and distribution  
6           pipeline integrity below what is allowed in the projected test year in this  
7           case would reduce the revenue requirement to be recovered through the  
8           rider. All of the qualifying criteria, as well as how charges would be  
9           developed, are set forth in proposed Rider GSR, which is found on Sheets  
10           Nos. 7.807 through 7.807-<sup>3</sup>~~2~~ of the new tariff sheets contained in MFR  
11           Schedule E-9.

12   **Q.    WHY IS THE COMPANY REQUESTING APPROVAL OF THE**  
13           **CARBON REDUCTION RIDER?**

14    A.    As I have previously testified, despite the environmental benefits of the  
15           direct use of natural gas, the Company faces financial obstacles in  
16           extending its facilities – particularly necessary, but non-revenue  
17           producing, supply mains – to many areas of Florida that are not in close  
18           proximity to an interstate natural gas pipeline to which the Company could  
19           connect, or to existing Company supply mains.

20                   Approval of Rider CR is consistent with, and responsive to,  
21           Governor Crist’s efforts as outlined in Executive Order No. 07-127, titled  
22           “Establishing Immediate Actions to Reduce Greenhouse Gas Emissions  
23           within Florida.” In addition, Rider CR aligns well with several sections of  
24           the omnibus energy legislation contained in House Bill 7135 that was  
25           passed during the 2008 Session of the Florida Legislature including

1 Section 187.201 that in part encourages the development of low-carbon-  
2 emitting electric power plants and Section 377.601 that establishes policy  
3 to develop and promote the effective use of energy in the state, discourage  
4 all forms of energy waste, and recognize and address the potential of  
5 global climate change wherever possible. In essence, a home with natural  
6 gas appliances versus all electric appliances produces net lower carbon  
7 emissions within the state of Florida.

8 **Q. HAS PEOPLES IDENTIFIED AREAS OF THE STATE WHERE**  
9 **DEVELOPMENTS ARE PLANNED THAT ARE NOT**  
10 **CURRENTLY IN A POSITION TO BE SERVED WITH NATURAL**  
11 **GAS?**

12 A. Yes. Peoples has identified over 25 such areas representing approximately  
13 100,000 new residential customers and the commercial customers such as  
14 restaurants and other gas-consuming businesses that generally follow large  
15 residential developments.

16 **Q. HOW WERE THESE AREAS IDENTIFIED BY PEOPLES?**

17 A. Areas for potential gas service are identified by sales personnel that track  
18 general development growth trends in addition to using data from the  
19 census bureau and other studies.

20 **Q. WHAT COSTS WOULD BE ELIGIBLE FOR RECOVERY**  
21 **THROUGH THE CARBON REDUCTION RIDER?**

22 A. Rider CR would recover the revenue requirements (i.e., the Company's  
23 weighted average cost of capital, depreciation expense and ad valorem  
24 taxes, grossed up for federal and state income taxes) associated with  
25 supply mains installed to reach a new development. As indicated earlier,



1           these supply mains produce no revenue for the Company, but the revenues  
2           from a potential new development cannot be obtained without their  
3           installation.

4   **Q.    WOULD THE COSTS OF EVERY COMPANY EXPANSION**  
5           **QUALIFY FOR RECOVERY THROUGH THE RIDER?**

6   A.    No. The expenses to be recovered by Rider CR would be limited to  
7           Eligible Installations that are defined as extensions of main greater than  
8           four inches in diameter, or that are certified to operate at a pressure of 60  
9           psig or greater that serve Company distribution systems serving primarily  
10          residential customers. All of the qualifying criteria, as well as how  
11          charges would be developed, are set forth in proposed Rider CR, found on  
12          Sheets Nos. 7.809 through 7.809-2 of the new tariff sheets contained in  
13          MFR Schedule E-9.

14   **Q.    ON WHAT ANNUAL AMOUNT OF CAPITAL INVESTMENT IN**  
15          **“ELIGIBLE INSTALLATIONS” DO YOU ANTICIPATE PEOPLES**  
16          **WILL SEEK TO RECOVER REVENUE REQUIREMENTS IF**  
17          **RIDER CR IS APPROVED?**

18   A.    The amount would obviously vary from year to year, depending on  
19          economic conditions in the housing market. Even during “good”  
20          economic periods in the housing market, and despite the potential  
21          developments the Company has identified, not every development will  
22          become a reality, and not all that become a reality will elect to make  
23          natural gas available.

24                    However, assume Rider CR was in place and Peoples had not  
25                    initiated this base rate proceeding. Mr. Narzissenfeld has testified that

1 Peoples will make total capital expenditures of \$62 million in 2008, and  
2 \$60 million in the 2009 projected test year. Of these total capital  
3 expenditures, \$5.8 million during 2008 and \$3.6 million during the  
4 projected test year would have been Eligible Installations on which  
5 Peoples could have petitioned the Commission to recover the revenue  
6 requirements associated with such plant investments had Rider CR been in  
7 place and this rate case not been initiated.

8 **Q. HOW WOULD THE CHARGES UNDER RIDERS GSR AND CR**  
9 **BE ESTABLISHED?**

10 A. Each rider contemplates the Company's filing of a petition for approval of  
11 the projected revenue requirement to be recovered. In the case of the  
12 Rider GSR petition, the projected revenue requirement would be  
13 associated with the projected Eligible Replacements and government-  
14 mandated safety measures. In the Rider CR petition, the projected  
15 revenue requirement would be associated with projected Eligible  
16 Installations of mains greater than four inches in diameter, or certified to  
17 operate at 60 psig or greater, that serve Company distribution systems  
18 serving primarily residential customers. The revenue requirement under  
19 each rider would be calculated and trued up much as expenses are  
20 projected and trued up under the Energy Conservation Cost Recovery  
21 clauses used by both electric and natural gas utilities. As is the case with  
22 proceedings under those clauses, the Commission would have the  
23 opportunity to thoroughly review and audit the Company's filings and  
24 make any necessary adjustments.

25 **Q. WHEN WOULD THE PETITIONS BE FILED?**

1 A. If the Commission approves Riders GSR and CR, Peoples' first petitions  
2 would be filed in late 2009, and would be based on eligible investments  
3 projected to be placed in service, and incremental expenses to be incurred  
4 by the Company, during 2010. The charges resulting from each filing  
5 would be included on customers' bills commencing in January 2010.  
6 Peoples would again file petitions in ~~2011~~<sup>2010</sup> which would recalculate the  
7 charges to recover the revenue requirements under each rider based on  
8 eligible costs for both 2010 and 2011, as adjusted by projected true-ups of  
9 the initially projected 2010 revenue requirements and the amount  
10 recovered through the surcharges imposed. Charges approved by the  
11 Commission as a result of a petition would continue in effect until new  
12 Commission-approved charges were authorized.

13 **Q. HOW WOULD THE REVENUE REQUIREMENTS TO BE**  
14 **RECOVERED THROUGH CHARGES IMPOSED PURSUANT TO**  
15 **THE RIDERS BE ALLOCATED AMONG AND BILLED TO THE**  
16 **COMPANY'S CUSTOMERS?**

17 A. The CRR Revenue Requirements would be allocated to customer classes  
18 based on the same allocation methodology pursuant to the Energy  
19 Conservation Cost Recovery Rule 25-17.015, Florida Administrative  
20 Code. The GSRR Revenue Requirements would be allocated to customer  
21 classes using the same methodology used in the cost of service study in  
22 the Company's most recent base rate proceeding, and would be recovered  
23 through a per therm surcharge.

24 **Q. HOW LONG WOULD PEOPLES COLLECT CHARGES IMPOSED**  
25 **PURSUANT TO RIDERS GSR AND CR FROM ITS CUSTOMERS?**

1 A. Collection of the GSRR Surcharges from customers would continue until  
2 such time as Peoples began billing new base rates resulting from a full  
3 base rate proceeding. Collection of the CRR Surcharges from customers  
4 for each Eligible Installation would continue for five years or until such  
5 time as Peoples began billing new base rates resulting from a full base rate  
6 proceeding, whichever occurs first.

7 **Q. CAN YOU PROVIDE AN EXAMPLE OF HOW THE REVENUE**  
8 **REQUIREMENT TO BE RECOVERED THROUGH RIDER GSR**  
9 **WOULD BE CALCULATED AND ALLOCATED AMONG THE**  
10 **CUSTOMER CLASSES?**

11 A. A summary of that calculation is found in my Exhibit \_\_\_(LMB-2). As  
12 shown by the exhibit, using the Company's 5-year average \$4.3 million  
13 investment in Rider GSR Eligible Replacements would result in a  
14 surcharge of \$0.00213 per therm to a typical residential customer in the  
15 first year of implementation. This would be approximately \$0.04 per  
16 month for the average residential customer using 222 therms per year. A  
17 \$1 million investment in Rider CR Eligible Installations would result in a  
18 surcharge of \$0.00069 per therm to a typical residential customer.

19 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

20 A. Yes, it does.

21

22

23

24

25

1 BY MR. WATSON:

2 Q. Did you also prepare and cause to be prefiled  
3 in this docket rebuttal testimony consisting of 20  
4 pages?

5 A. Yes.

6 Q. And did you also file with your rebuttal  
7 testimony an exhibit premarked Exhibit LMB-3 and  
8 identified as Hearing Exhibit 87?

9 A. Yes.

10 MR. WATSON: Mr. Chairman, could we ask that  
11 Exhibit LMB-3 be formally identified for the record as  
12 Hearing Exhibit Number 87.

13 CHAIRMAN CARTER: For the record, Exhibit 87.

14 (Exhibit 87 was identified for the record.)

15 BY MR. WATSON:

16 Q. Do you have any changes or corrections to  
17 Hearing Exhibit 87?

18 A. No.

19 Q. If I were to ask you the questions in your  
20 rebuttal testimony today, would your answers be the  
21 same?

22 A. Yes.

23 MR. WATSON: We would ask that  
24 Mr. Binswanger's rebuttal testimony be inserted into the  
25 record as though read.

- 1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.
- 2 A. My name is Lewis M. Binswanger and my business address is 702 North  
3 Franklin Street, Tampa, Florida 33602.
- 4 Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?
- 5 A. I am employed by Peoples Gas System ("Peoples" or the "Company") as  
6 Director, Strategic Planning and Regulatory.
- 7 Q. ARE YOU THE SAME LEWIS M. BINSWANGER WHO FILED  
8 DIRECT TESTIMONY IN THIS PROCEEDING?
- 9 A. Yes, I am.
- 10 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?
- 11 A. The purpose of my rebuttal testimony is to address certain positions taken  
12 in the prepared direct testimony of witness Helmuth W. Schultz, III, hired  
13 by the Office of Public Counsel ("OPC"), and testifying on behalf of the  
14 Citizens of the State of Florida ("Citizens"), with which I have concern.
- 15 Q. ARE THERE ANY EXHIBITS SUPPORTING YOUR REBUTTAL  
16 TESTIMONY?
- 17 A. Yes. Exhibit No. \_\_\_ (LMB-3) is attached to my rebuttal testimony.
- 18 Q. PLEASE SUMMARIZE YOUR CONCERNS AND  
19 DISAGREEMENTS REGARDING THE SUBSTANCE OF  
20 WITNESS SCHULTZ'S TESTIMONY.
- 21 A. My concerns and disagreements are with the following matters:
- 22 • Mr. Schultz rejects the Company's proposed Gas System Reliability  
23 Rider ("Rider GSR"). In addition to what appears to be a general  
24 objection to the use of new riders, or cost recovery mechanisms, Mr.  
25 Schultz claims that the rider could potentially allow the Company to

1           overearn. These assertions are unfounded. He also contends there is  
2           no need to include pipeline integrity operating expenses for recovery  
3           through the rider, a position that fails to recognize the uncertainty in  
4           predicting the level of such costs to be included in base rates. Finally,  
5           Mr. Shultz says the amounts involved are too small to justify Rider  
6           GSR. I disagree with this assertion. Rider GSR addresses  
7           government-mandated facility relocations and pipeline integrity  
8           management requirements that cause the Company to incur costs in  
9           order to comply with these requirements. The costs are significant,  
10          potentially volatile and difficult to predict. In addition, and unlike  
11          what Mr. Schultz suggests, Peoples has no opportunity to recover these  
12          costs absent the filing of base rate cases. These are appropriate criteria  
13          for use of a rider.

- 14          ● Mr. Schultz rejects the Company's proposed Carbon Reduction Rider  
15          ("Rider CR"). Again, Mr. Schultz seems to be generally opposed to  
16          the implementation of new riders. In addition, he claims that the risk  
17          of expansion should be placed on new customers rather than existing  
18          customers and that expansion revenue should be sufficient to cover the  
19          expansion costs. Finally, he states that the amounts involved are too  
20          small to justify Rider CR. I disagree with his assertions.
- 21          ● Mr. Schultz is proposing to increase the Company's projection of off-  
22          system sales revenue, claiming Peoples needs a greater incentive  
23          before it should share in these revenues. This is not appropriate.

24   **Q.   WHY DO YOU SAY THAT MR. SCHULTZ APPEARS TO HAVE A**  
25   **GENERAL OPPOSITION TO NEW RIDERS?**

1 A. I think it is fair to say that the overall theme of Mr. Schultz's testimony  
2 related to the Company's proposed riders is that all riders are bad and  
3 there is no need to change anything with respect to the way certain costs  
4 are recovered. Many of his statements could apply to any rider or cost  
5 recovery clause. For example, Mr. Schultz states that using a mechanism  
6 for "automatic" recovery of costs is contrary to principles underlying the  
7 regulatory process, and that riders eliminate regulatory review, lessen the  
8 Company's need to control costs, and lower the financial risks already  
9 reflected in the allowed return on equity ("ROE"). He concludes by  
10 stating that there is no reason to change prior ratemaking treatment  
11 because the types of costs involved are not new. I do not agree with these  
12 general assertions.

13 **Q. DO THE RIDERS ALLOW FOR "AUTOMATIC" OR**  
14 **"GUARANTEED" RECOVERY OF COSTS?**

15 A. Absolutely not. Recovery of costs would be based on prudent investments  
16 and certainly not "automatic." There are no "automatic" cost recovery  
17 clauses in Florida. This Commission regularly reviews several cost  
18 recovery clauses similar to the Company's proposed riders, one of which  
19 Mr. Schultz notes in his testimony. Thus, the mechanisms are consistent  
20 with principles underlying the existing regulatory process.

21 **Q. DO THE COMPANY'S RIDERS CONTEMPLATE REVIEW BY**  
22 **THE COMMISSION?**

23 A. Yes. The Company would expect no less than a thorough review by the  
24 Commission (as is its practice for all existing cost recovery clauses)  
25 during an annual audit, review and reconciliation process contemplated by



1 Riders GSR and CR. Mr. Schultz's statements that the Company is  
2 "trying to eliminate regulatory review," and that riders result in less  
3 regulatory scrutiny than would otherwise be the case, are totally  
4 unsupported, and certainly not the case in Florida.

5 **Q. HOW DO YOU RESPOND TO MR. SCHULTZ'S COMPLAINT**  
6 **THAT PEOPLES' PROPOSED RIDERS WILL INCREASE**  
7 **ADMINISTRATIVE COSTS FOR THE COMMISSION?**

8 A. There is no question these riders will require some administrative time  
9 from both the Commission and the Company. The Company believes this  
10 will be minimal, and much less than the otherwise likely alternative of  
11 more frequent rate cases or "limited proceedings" authorized by Section  
12 366.076, Florida Statutes.

13 **Q. DO YOU AGREE WITH MR. SCHULTZ THAT PEOPLES'**  
14 **PROPOSED RIDERS WILL SUBSTANTIALLY LIMIT THE**  
15 **COMMISSION'S DISCRETION REGARDING APPROVAL OF**  
16 **THE ANNUAL RIDER FILINGS?**

17 No. Peoples drafted the proposed tariff language very similar to Rule 25-  
18 17.015 – Energy Conservation Cost Recovery – to maintain the same level  
19 of regulatory scrutiny, including the annual required filings, review and  
20 audit.

21 **Q. ARE YOU AWARE OF ANY APPROVED RIDERS THAT ARE**  
22 **SIMILAR TO RIDER GSR OR RIDER CR IN FLORIDA OR IN**  
23 **ANY OTHER STATE?**

24 A. Yes. In Florida, Rider GSR is similar to the approved mechanism for  
25 environmental cost recovery under which electric utilities are authorized

1 to recover revenue requirements associated with capital costs and O&M  
2 expenses incurred to comply with government-mandated programs. In  
3 addition, there are several states (for example, Missouri, Kansas and  
4 Oklahoma) that have similar mechanisms to address the recovery of costs  
5 associated with government-mandated programs. Exhibit \_\_\_(LMB-3)  
6 attached to my rebuttal testimony is an American Gas Association report  
7 listing and summarizing infrastructure cost recovery mechanisms that  
8 were in place, or pending approval, in a number of states as of December  
9 2007.

10 I am not aware of any utility that has a rider similar to Rider CR,  
11 which seeks to recover the revenue requirements associated with  
12 investments in supply main.

13 **Q. DO RIDERS LESSEN THE NEED FOR THE COMPANY TO**  
14 **CONTROL COSTS?**

15 **A.** No. Neither the proposed riders nor the cost recovery clauses currently  
16 used by Peoples has any impact on the Company's need to control costs.  
17 From a regulatory perspective, the Company must be able to demonstrate  
18 that costs are necessary and prudently incurred. From a business  
19 perspective, the natural gas business in Florida is highly competitive,  
20 evidenced by the fact that only one in 10 electric customers is a natural gas  
21 customer, and that all-electric homes are available for purchase. In short,  
22 every existing and potential natural gas customer in Florida has an energy  
23 choice to use natural gas or not. The Company therefore has, and will  
24 always have, every incentive to deliver natural gas at the lowest possible  
25 price in order to remain competitive with alternative energy options to

1 maintain existing customers and attract new or conversion customers. To  
2 achieve these objectives, the Company must control costs. The need to  
3 control costs recovered through the proposed riders is no different than the  
4 Company's need to control costs in all areas, including costs recovered  
5 through the current purchased gas adjustment and conservation cost  
6 recovery clauses.

7 **Q. HOW DO YOU RESPOND TO MR. SHULTZ'S ASSERTION THAT**  
8 **RIDERS LOWER THE FINANCIAL RISKS ALREADY**  
9 **REFLECTED IN THE ALLOWED RETURN ON EQUITY?**

10 A. Riders are commonplace in the natural gas industry. I believe that most if  
11 not all of the peer companies used by Dr. Murry in supporting the  
12 Company's proposed return on equity have cost recovery riders. Thus to  
13 the extent risks are lowered with the riders, this is already accounted for.  
14 Further, neither Mr. Schultz nor OPC witness Dr. Woolridge has  
15 quantified the impact, if any, riders might have on the returns required by  
16 investors.

17 **Q. HOW DO YOU RESPOND TO MR. SCHULTZ'S ASSERTION**  
18 **THAT THERE IS NO REASON TO CHANGE PRIOR**  
19 **RATEMAKING TREATMENT BECAUSE THESE TYPES OF**  
20 **COSTS ARE NOT NEW?**

21 A. Mr. Schultz's "no change" philosophy fails to recognize the need for  
22 ratemaking to evolve to address changing circumstances. Pipeline  
23 integrity costs imposed on Peoples as a result of federal legislation  
24 described in my direct testimony are indeed new. The same is true of  
25 various Florida initiatives associated with lowering carbon emissions,

1 including Governor Crist's Executive Order Number 07-126 which states,  
2 in part, that Florida has committed to becoming a leader in reducing  
3 emissions of greenhouse gases. Just because a cost such as government-  
4 mandated relocations is not new does not mean that a changed regulatory  
5 approach such as a rider is in any way inappropriate.

6 **Q. ARE THE PROPOSED RECOVERY MECHANISMS AN**  
7 **EXAMPLE OF IMPLEMENTING "SINGLE ISSUE**  
8 **RATEMAKING" WITHOUT APPROPRIATE OVERSIGHT AS**  
9 **MR. SCHULTZ CONTENDS?**

10 **A.** No. As noted previously, these riders are subject to ongoing regulatory  
11 review and they are proposed to be effective after the conclusion of a full  
12 rate proceeding during which the Company's investment level, operating  
13 revenue and expense, depreciation, and taxes were fully vetted. As is the  
14 case with existing cost recovery clauses, the costs included for recovery  
15 under the proposed riders will be reviewed and audited on an annual basis,  
16 and quarterly earnings surveillance reports will continue to be filed  
17 providing the Company's rate of return along with appropriate entries  
18 relating to the riders. The term "single issue ratemaking" is a red herring,  
19 because it is specifically authorized by the "limited proceeding" section of  
20 the Florida Statutes – Section 366.076. The central issue with respect to  
21 Peoples' proposed riders is whether the Company should be permitted to  
22 recover its costs – particularly government-mandated costs – at the time  
23 they are incurred, rather than having to wait for a base rate proceeding.

24 **Q. UNDER BOTH RIDER GSR AND RIDER CR, PEOPLES HAS**  
25 **PROPOSED PROJECTIONS OF THE REVENUE**

1           **REQUIREMENTS TO BE RECOVERED THROUGH THE**  
2           **SURCHARGES CONTEMPLATED BY THE RIDERS. IS THERE**  
3           **ANOTHER WAY PEOPLES MIGHT RECOVER THE COSTS?**

4    A.    Yes. Instead of recovering only the revenue requirements associated with  
5           the capital and/or O&M expenditures, Peoples could recover the actual  
6           costs incurred in several other ways.

7    **Q.    PLEASE DESCRIBE ONE WAY IN WHICH THESE COSTS**  
8           **MIGHT BE RECOVERED BY PEOPLES.**

9    A.    Peoples could recover the costs in the year incurred, in the same manner  
10           that it recovers the costs of purchased gas and the costs for its energy  
11           conservation programs in the year the costs are incurred. There would still  
12           be a projection going into each year, and a true-up of the projection to the  
13           actual costs, so that the Company's customers would not pay more or less,  
14           and the Company would not receive more or less, than the actual costs  
15           incurred by the Company.

16   **Q.    IN WHAT OTHER WAYS MIGHT THE COSTS BE**  
17           **RECOVERED?**

18   A.    Recovery of the capital costs could be amortized over a period of time.  
19           However, under this option, and the single-year recovery option I just  
20           mentioned, the immediate cost to Peoples' customers would be greater  
21           than what the Company is proposing in this proceeding, which  
22           contemplates only the recovery of the revenue requirements associated  
23           with the expenditures, not the expenditures themselves (except the gas  
24           safety O&M expenditures).

25           Finally, the Company could file a petition to increase its rates

1 through a limited proceeding under Section 366.076, Florida Statutes,  
2 either at the time plant items installed to comply with governmental  
3 mandates are placed in service, or incremental increases or reductions in  
4 O&M expenses incurred to comply with mandatory pipeline safety  
5 regulations are experienced. This could be done on a monthly or quarterly  
6 basis.

7 Peoples elected to construct the cost recovery procedure and  
8 methodology under Riders GSR and CR in the manner included in its  
9 filing because it most closely matched the way costs are recovered through  
10 base rates for plant additions and O&M expenses. Peoples is certainly  
11 amenable, however, to recovering the costs in a different manner if the  
12 Commission deems another methodology more appropriate.

13 **Q. DO YOU HAVE ANY OTHER COMMENTS REGARDING**  
14 **RIDERS IN GENERAL?**

15 A. Yes. The Company has proposed Rider GSR and Rider CR to address  
16 specific situations in which traditional ratemaking is, and has been, less  
17 than adequate.

18 Rider GSR addresses government-mandated facility relocations  
19 and pipeline integrity management requirements that cause the Company  
20 to incur costs in order to comply with these requirements. The costs are  
21 significant, potentially volatile and difficult to predict. In addition, and  
22 unlike what Mr. Schultz suggests, Peoples has no opportunity to recover  
23 these costs absent the filing of base rate cases. These are appropriate  
24 criteria for use of a rider.

25 Rider CR, which deals with supply main expansions, partially

1 addresses the potentially significant revenue lag involved with bringing  
2 natural gas to areas not currently served. While a supply main must be in  
3 place to serve the first customer in a development, it produces no revenue  
4 in and of itself. The revenues will come - over time - from the main(s)  
5 serving the development the supply main was installed to connect to an  
6 interstate pipeline or other Company supply main. The costs associated  
7 with the supply main (depreciation expense, return on investment, etc.)  
8 cannot be recovered by the Company without the filing of a base rate case.  
9 The approval of Rider CR would remove this financial barrier and position  
10 the Company to proactively capture expansion opportunities that support  
11 Florida's initiatives to improve fuel diversity and reduce the state's carbon  
12 footprint – both worthy objectives.

13 **Q. WHAT ARE MR. SCHULTZ'S SPECIFIC CONCERNS WITH THE**  
14 **GAS SYSTEM RELIABILITY RIDER?**

15 A. In addition to the general objections to the riders discussed above, Mr.  
16 Schultz claims that Rider GSR could potentially allow the Company to  
17 earn more than it should, that there is an opportunity to include costs for  
18 expansion of capacity, that there is no need to include pipeline integrity  
19 costs in the rider, and that the amounts involved are too small to justify a  
20 rider.

21 **Q. WILL RIDER GSR ALLOW THE COMPANY TO EARN MORE**  
22 **THAN IT SHOULD?**

23 A. Mr. Schultz does not appear to understand the provisions of the  
24 Company's proposed Rider GSR. He states, "If the Company is earning  
25 within its range and then is allowed to have certain normal base rate type

1 costs shifted to clause recovery, then the Company could, in effect, be  
2 placed in an overearnings posture.” This misses the point that there is no  
3 shifting of costs recovered through base rates to a clause recovery. As  
4 discussed in my direct testimony, the Company has proposed that the rider  
5 include only those incremental costs incurred starting in 2010, *after* the  
6 base rates have been established in this proceeding.

7 **Q. IS THERE AN OPPORTUNITY TO INCREASE PIPELINE**  
8 **CAPACITY BY INCLUDING COSTS FOR EXPANSION**  
9 **CAPACITY IN RIDER GSR AS MR. SCHULTZ ASSERTS?**

10 A. No. This assertion is contrary to the language set forth in the rider.  
11 Further, from an engineering perspective, such an expansion would be  
12 impractical. For example, if Peoples had installed a two-inch diameter gas  
13 main to serve customers along 10 city blocks and was required to relocate  
14 a one-block section in the middle of the 10-block run, installing gas main  
15 greater in size than two inches in diameter would not increase the capacity  
16 of the 10-block run because of the size constraints of the existing two-inch  
17 main. Finally, the assertion assumes the Commission will not  
18 appropriately review costs to be recovered through the rider.

19 **Q. HOW DO YOU RESPOND TO MR. SCHULTZ’S POSITION THAT**  
20 **IT IS INAPPROPRIATE TO RECOVER PIPELINE INTEGRITY**  
21 **COSTS THROUGH RIDER GSR?**

22 A. Mr. Schultz suggests that recovering pipeline integrity costs through the  
23 rider is inappropriate because an estimate of these costs is included in base  
24 rates. He appears to believe -- incorrectly -- that only costs in excess of  
25 those included in base rates would be included for recovery under the rider



1 so that the Company would be insulated from costs in excess of those  
2 already included in base rates. The Company's proposal is to include both  
3 positive and negative variances from the base rate expense to ensure that  
4 customers pay only the actual costs incurred by the Company.

5 As I noted earlier, pipeline integrity costs are very difficult to  
6 estimate. Associated regulations are either new or still in their proposal  
7 stage. It is for this very reason that the Company has proposed that any  
8 variance from the base rate amount be "trued-up" through Rider GSR.  
9 This aspect of Rider GSR will address the uncertainty involved in  
10 estimating these costs and ensures that neither the Company nor its  
11 customers will either gain or lose financially.

12 **Q. WHAT ARE MR. SCHULTZ'S CONCERNS WITH RESPECT TO**  
13 **THE PIPELINE INTEGRITY EXPENSES?**

14 A. Mr. Schultz asserts that the steps enumerated on page 35 of Mr. Higgins'  
15 direct testimony are steps that a prudently operated distribution company  
16 should already have had in existence. He also claims that history does not  
17 support the Company's estimate and that due to the unknown nature of  
18 these costs, they should not be allowed at the level requested.

19 **Q. PLEASE ADDRESS THESE CONCERNS.**

20 A. The U.S. Department of Transportation's Inspector General testified  
21 before Congress on July 20, 2004 regarding the need for a distribution  
22 integrity management program ("DIMP"). I do not believe that the federal  
23 government would have spent the last four-plus years crafting these  
24 requirements, in addition to the time industry has spent in addressing the  
25 requirements of DIMP, if prudently operated distribution companies

1 already had them in existence as Mr. Schultz suggests. In this particular  
2 case, the fact that history does not support the Company's estimate for  
3 future DIMP costs is quite understandable. The programs are either new  
4 or relatively new to the industry and would not have historical expenses to  
5 justify future expenses. I disagree with Mr. Schultz's proposed  
6 adjustments as they ignore the integrity management mandates.

7 **Q. PLEASE EXPLAIN AND ADDRESS MR. SCHULTZ'S PROPOSED**  
8 **ADJUSTMENT FOR PIPELINE INTEGRITY EXPENSES.**

9 A. Mr. Schultz is proposing to arbitrarily reduce the Company's base rate  
10 provision for pipeline integrity expense by \$250,000. While the  
11 Company's estimates were developed based on data included in a study  
12 completed by the American Gas Association, in an effort to reduce the  
13 areas of disagreement in this case, the Company would agree to this  
14 reduction provided the pipeline integrity management true-up provision  
15 remains in Rider GSR and is approved. Absent approval of Rider GSR, I  
16 see no logical rationale for the \$250,000 adjustment proposed.

17 **Q. DO YOU AGREE WITH MR. SCHULTZ'S CLAIM THAT THE**  
18 **AMOUNTS INVOLVED ARE TOO SMALL TO JUSTIFY THE**  
19 **NEED FOR RIDER GSR?**

20 A. No. Mr. Schultz acknowledges that Peoples' capital costs over the last  
21 five years for government-mandated projects have averaged over \$4.28  
22 million annually and seems to think this amount is small. The \$4.28  
23 million per year is definitely not small by Company standards and these  
24 mandatory relocations occur every year and do not provide any  
25 incremental revenue. Over a five year period, total expenditures for

1 government-mandated relocations could exceed \$21 million with no  
2 possibility of recovering the costs associated with these investments  
3 absent new base rate relief.

4 Another factor that may impact the annual expenditures for  
5 government-mandated programs is that Congress will be considering the  
6 American Recovery and Reinvestment Bill of 2009. In part, this  
7 economic stimulus package proposes \$90 billion in government spending  
8 to modernize roads, bridges, transit and waterways.

9 **Q. WHAT ARE MR. SCHULTZ'S SPECIFIC CONCERNS ABOUT**  
10 **THE CARBON REDUCTION MECHANISM?**

11 A. In addition to the general objections to riders discussed earlier, Mr.  
12 Schultz claims that the risk of expansion should be placed on new  
13 customers rather than existing customers, expansion revenue should be  
14 sufficient to cover the expansion costs, and developer agreements  
15 eliminate all risk to the general body of ratepayers and the Company.  
16 Finally, he notes that the amounts involved are not significant enough to  
17 justify a rider.

18 **Q. PLEASE ADDRESS THESE CONCERNS.**

19 A. In his proposition that the cost of expansion should be paid for by new  
20 customers and not existing customers, Mr. Schultz seems to be suggesting  
21 some sort of incremental cost of service pricing. However, he offers no  
22 specifics on how this should be implemented, or what implications it  
23 might have for other aspects of the Company's historic embedded cost of  
24 service pricing. In addition, while Mr. Schultz can theorize about how  
25 revenue from new customers "should" be sufficient to cover the cost of

1 new plant and operating expenses, he totally ignores the reality that  
2 customer additions resulting from expansion capital expenditures occur  
3 over a number of years. As I stated in my direct testimony, “operationally,  
4 the supply main must be in service when the first customer needs natural  
5 gas, even though full build-out of the residential and commercial  
6 development may take 10 or more years.” Rider CR addresses this  
7 regulatory lag for only the supply main and only for the first five years of  
8 the project. In addition, Rider CR provides the Company with the  
9 financial incentives necessary to bring gas to areas currently not served.

10 With respect to the developer agreements, these agreements are for  
11 construction within an identified development. They address the costs  
12 associated with the development main for which the general body of  
13 ratepayers is not at risk in the event that the development fails. Developer  
14 agreements are not used for supply mains installed to serve multiple  
15 developments that build-out over an extended period of time. Providing  
16 more real-time recovery of the revenue requirements associated with the  
17 Company’s investment in supply mains, without which new developments  
18 with developer agreements cannot be supplied with natural gas, would  
19 help further Florida’s policy of reducing carbon emissions in the state.

20 **Q IS MR. SCHULTZ CORRECT THAT THE AMOUNTS INVOLVED**  
21 **ARE NOT SIGNIFICANT ENOUGH TO JUSTIFY THE USE OF**  
22 **THE RIDER?**

23 **A.** No. While Mr. Schultz states that the annual capital costs under the  
24 proposed rider for the years 2005 through 2007 would have been only  
25 \$436,943 per year for a total capital investment of \$1.3 million, he failed

1 to acknowledge an additional \$4.7 million for projects that could have  
2 been undertaken had the rider been in effect for the same period of time,  
3 as described in Peoples' answer to Interrogatory No. 44 of Staff's Third  
4 Set. This represents a total of \$6 million or an average of \$2 million per  
5 year.

6 **Q. DO YOU AGREE WITH MR. SCHULTZ'S POSITION THAT**  
7 **RIDER CR IS INAPPROPRIATE BECAUSE OF CURRENT**  
8 **ECONOMIC CONDITIONS?**

9 A. No. Providing supply main is market driven thus if economic conditions  
10 are such that no developments are occurring then no supply main would be  
11 installed and there would be no revenue requirements to recover through  
12 the rider.

13 **Q. WHAT ADJUSTMENT IS MR. SCHULTZ PROPOSING**  
14 **REGARDING OFF-SYSTEM SALES ("OSS")?**

15 A. Mr. Schultz is proposing to increase the amount of OSS revenue included  
16 in the 2009 projected test year from \$500,000 to \$2 million. He is not  
17 proposing any change in the sharing mechanism.

18 **Q. DO YOU AGREE WITH MR. SCHULTZ'S PROPOSED**  
19 **ADJUSTMENT?**

20 A. No. Mr. Schultz's adjustment does not reflect the clear trend of declining  
21 OSS discussed in the direct testimony of Peoples witness J. Paul Higgins.  
22 Because of this trend, Mr. Schultz's proposal does not represent a realistic  
23 sales level that Peoples expects to generate in 2009. The Company's  
24 \$500,000 projection is a reasonably attainable amount and it represents the  
25 Company's 25 percent share of total net margin of \$2 million with the

1 remaining 75 percent being returned directly to customers through the  
2 PGA. Peoples proposal for OSS treatment is consistent with the  
3 Commission's previous decision.

4 **Q. PLEASE EXPLAIN WHY MR. SCHULTZ'S PROPOSED**  
5 **ADJUSTMENT IS INAPPROPRIATE.**

6 A. Mr. Schultz's adjustment, which is based on a five-year average of OSS,  
7 fails to consider that these sales are sporadic and opportunistic transactions  
8 that are highly dependent on natural gas supply- and demand-related  
9 market conditions both within and outside Florida. His analysis is made  
10 without addressing any of the market considerations that must be  
11 addressed in order to determine and quantify Peoples' future ability to  
12 make OSS in any amount, and the net margins, or prices, at which such  
13 sales – if any – might be made.

14 While Peoples clearly wants to make OSS in the future, that desire  
15 must not be confused with whether or not market conditions will provide  
16 Peoples with the ability to actually make these sales, and to obtain the net  
17 margins implied in Mr. Schultz's proposed adjustment so as to actually  
18 result in the additional revenue he proposes be included in determining the  
19 Company's revenue requirements in this proceeding.

20 Peoples' initial OSS rate schedule was approved by the  
21 Commission in September 1994 (Order No. PSC-94-1187-FOF-GU,  
22 issued September 28, 1994, in Docket No. 940856-GU). The Commission  
23 approved the rate schedule outside of a full revenue requirement  
24 proceeding based on the following findings:

25 1) If any person not directly connected to Peoples Gas'

1 distribution system purchases capacity that is not needed at  
2 the time by Peoples Gas, the savings in FGT, Southern  
3 Natural and South Georgia reservation charges<sup>1</sup> will flow  
4 directly to Peoples Gas customers through the Purchased  
5 Gas Adjustment Clause; 2) Fifty percent of any gas  
6 revenues Peoples Gas derives from off-system or  
7 opportunity sales under the OSS rate schedule will be  
8 credited to the firm sales customers as a credit to the cost of  
9 purchased gas. Fifty percent would be retained by Peoples  
10 Gas above the line; and 3) The Off-System Sales will  
11 improve system load factor and provide additional revenue  
12 from which to meet the company's revenue requirements.

13 The "fifty percent" sharing of any net margin on OSS sales was changed  
14 in Peoples' last base rate proceeding so that the Company now receives 25  
15 percent of any net margin above the line, with the remainder being a credit  
16 to the cost of gas recovered through the PGA.

17 While the current economic crisis may result in some reduced  
18 consumption by some Peoples customers served directly through its  
19 distribution system, it may well have an even greater impact in reducing  
20 "opportunistic" OSS to entities (primarily electric generators) not  
21 connected to Peoples' system, who hold their own capacity on the  
22 interstate pipelines, and have relied on Peoples' OSS to meet natural gas

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<sup>1</sup> At the time of the Commission's approval of Rate Schedule OSS, only Florida Gas Transmission Company ("FGT"), Southern Natural Gas Company ("Southern Natural"), and its affiliate, South Georgia Natural Gas Company ("South Georgia"), delivered natural gas in Florida. Peoples now receives deliveries from FGT, Southern Natural, South Georgia and Gulfstream Natural Gas System, LLC.

1 requirements in excess of their contracted demand. That is, there may  
2 well be fewer “opportunities” for Peoples to make such sales, and there is  
3 no assurance that the net margins, if any, associated with any such sales  
4 will be at the levels experienced during the years used by Mr. Schultz to  
5 calculate his proposed adjustment.

6 The \$500,000 of OSS revenues the Company has included in its  
7 projected test year is appropriate, and an historical average such as that  
8 used by Mr. Schultz may well create a hurdle that cannot be achieved. If  
9 Peoples is incorrect, and is placed in an overearnings posture because its  
10 share of OSS exceeds the \$500,000 included in this proceeding for  
11 purposes of determining the Company’s revenue requirements, the  
12 Commission has ample authority to require refunds to customers.

13 **Summary of Rebuttal Testimony**

14 **Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY.**

15 **A.** I disagree with Mr. Schultz’s assertions that proposed Riders GSR and CR  
16 are not justified or necessary. The Company proposed these riders to  
17 address specific facts and circumstances where it considers traditional  
18 ratemaking to be less than adequate.

19 More specifically, Rider GSR addresses facility relocations and  
20 pipeline integrity costs that are government-mandated. These costs must  
21 be incurred by the Company in order to comply with these mandatory  
22 requirements. The costs are significant, potentially volatile and difficult to  
23 predict. In addition, Peoples has no opportunity to recover these costs  
24 absent the filing of base rate cases. These are appropriate criteria for use  
25 of a rider.



1 Pipeline integrity management regulations are either new or still in  
2 the proposal stage with future expenses developed based on data included  
3 in a study completed by the American Gas Association. The amount  
4 included for these mandates in the projected test year is accurate and  
5 Peoples has proposed that any variance from the proposed amount be  
6 “trued-up” through Rider GSR to ensure that neither it nor its customers  
7 will either gain or lose financially.

8 Rider CR, which deals with supply main expansions, partially  
9 addresses the potentially significant revenue lag involved with bringing  
10 natural gas to areas not currently served. The approval of this rider would  
11 remove this financial barrier and position the Company to proactively  
12 capture expansion opportunities that support Florida’s initiatives to  
13 improve fuel diversity and reduce the carbon footprint – both worthy  
14 objectives.

15 The OSS revenue included in the Company’s filed MFRs is  
16 appropriate and reasonably attainable. Off-system sales are sporadic,  
17 opportunistic transactions that are highly dependent on natural gas supply-  
18 and demand-related market conditions both within and outside Florida.

19 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

20 **A. Yes.**

21

22

23

24

25

1 BY MR. WATSON:

2 Q. Please summarize your direct and rebuttal  
3 testimonies.

4 A. Good afternoon, Commissioners. The purpose of  
5 my testimony is to present two recovery mechanisms that  
6 address the installation and maintenance of natural gas  
7 pipelines. The first mechanism would allow for natural  
8 gas to be more readily available to customers that have  
9 made the choice to use natural gas as a clean and  
10 environmentally friendly fuel.

11 The number of natural gas customers in the  
12 State of Florida is only about 10 percent that of the  
13 number of electric customers. Every utility customer in  
14 Florida has a choice when selecting an energy solution  
15 for their home, and natural gas in many cases is not  
16 considered a necessity. However, the direct use of  
17 natural gas not only support's Governor Crist's  
18 executive orders on climate change, but it also supports  
19 legislation focused on reducing carbon dioxide  
20 emissions. I also describe some of the challenges in  
21 providing natural gas service to areas in Florida that  
22 do not have natural gas.

23 The second mechanism I propose addresses  
24 government-mandated programs with which Peoples must  
25 comply. I discuss the significant historical

1 expenditures that were required to meet those  
2 non-discretionary requirements. The recovery mechanism  
3 supports Peoples' commitment to providing safe and  
4 reliable natural gas service, while allowing for more  
5 timely recovery of revenue requirements associated with  
6 government-mandated costs the company must incur.

7 My rebuttal testimony addresses certain  
8 positions taken by OPC's witness, including the  
9 unsupported assumption that the proposed mechanisms will  
10 eliminate regulatory review.

11 Finally, I address the appropriate level of  
12 off-system sales included in the company's projected  
13 test year.

14 This concludes my summary.

15 MR. WATSON: The witness is tendered for  
16 cross.

17 CHAIRMAN CARTER: Mr. McWhirter.

18 CROSS-EXAMINATION

19 BY MR. McWHIRTER:

20 Q. Mr. B, that last statement you made that said  
21 it would eliminate the need for regulatory review, did I  
22 understand you to say something like that?

23 A. No. I said that my rebuttal testimony  
24 addresses certain positions taken by OPC's witness,  
25 including an unsupported assumption that the proposed

1 mechanism will eliminate regulatory review.

2 Q. So there will still be a determination of  
3 prudence; is that right?

4 A. Correct.

5 Q. And these will come up in proceedings in  
6 November along with the conservation clause, the  
7 capacity clause, the fuel clause, the environmental  
8 clause, and the securities clause, and the nuclear plant  
9 cost recovery clause, and the renewable energy portfolio  
10 standard cost recovery clause?

11 A. Well, for Peoples Gas, it would be during the  
12 same time as we file our PGA clause and our energy  
13 conservation clause, and then throughout the year, we  
14 would go through an audit process of the actual  
15 expenditures.

16 Q. But you would file the capital assets that you  
17 wanted recovery for in September of the year for  
18 consideration and November along with those other cost  
19 recovery clauses?

20 A. Yes.

21 Q. I see. Which component of this cost recovery  
22 would you classify as volatile? Is there any that's  
23 volatile, that's an unusual and unanticipated type cost?

24 A. Right. Are you referring to -- well, which  
25 clause are you referring to?

1           Q.   Well, let's talk about the gas system  
2 reliability rider.

3           A.   Sure.  It would be the actual expenditures  
4 that are brought upon us on an annual basis.  I would  
5 consider those volatile.

6           Q.   And the expenses you're talking about are  
7 going out and digging ditches and putting pipes in the  
8 ground?

9           A.   Those costs would be associated with  
10 government-mandated relocation projects.

11          Q.   Well, look at -- I presume you have before you  
12 a copy of this rider.  It would be 7.807 in your tariff.

13          A.   Yes.

14          Q.   A three-page rider?

15          A.   Yes.

16          Q.   And do you see the definitions section?

17          A.   I do.

18          Q.   Under the first definition for eligible  
19 replacement are mains, service lines, regulated  
20 stations, and other pipeline system components installed  
21 to comply with state or federal safety regulation --  
22 requirements as replacements for existing facilities.  
23 Is that --

24          A.   Yes.

25          Q.   That's what qualifies?

1           A.    Yes.

2           Q.    Now, I would presume that you have safety  
3 standards that govern your company at this time.

4           A.    Correct.

5           Q.    Are you talking about the existing standards,  
6 or are you talking about new standards that would  
7 suddenly come upon you?

8           A.    New standards.

9           Q.    I see.  So any standard that's in place as of,  
10 say, January 1, 2009, any cost to comply with that  
11 standard would not count under this clause; is that  
12 correct?

13          A.    Actually, through January 1st, 2010.

14          Q.    2010.

15          A.    Yes.

16          Q.    So this would be only new standards and  
17 nothing that's in place at the current time?

18          A.    Correct.

19          Q.    Okay.  Section B is main relining projects,  
20 service line insertion projects, joint encapsulation  
21 projects, and other similar projects extending the  
22 useful life or enhancing the integrity of existing  
23 pipeline system components undertaken to comply with  
24 state or federal safety requirements.  So when a line  
25 wears out and you replace it, that wouldn't count under

1 this rider. It would just be something new that had to  
2 be done under a new standard; is that correct?

3 A. That is correct.

4 Q. What are the federal/state safety requirements  
5 that are presently in place? Where I do find those, and  
6 give us a quick narrative of what they are.

7 A. The current safety requirements, is that the  
8 question?

9 Q. Yes, sir.

10 A. Currently we operate under Part 192 of the DOT  
11 Handbook that essentially established certain minimum  
12 safety guidelines for us to undertake. This primary  
13 rider is focused for any new government mandates that  
14 may come down associated with pipeline integrity,  
15 whether it be transmission pipeline integrity or  
16 distribution pipeline integrity programs.

17 Q. I see. Now, are those published in the  
18 Federal Register?

19 A. The new mandates?

20 Q. Yes.

21 A. Yes.

22 Q. And you obviously developed this in response  
23 to something that's coming down the pike that gives you  
24 concern. Has anything yet been published in the Federal  
25 Register that tells you that you're going to have to do

1 something significant in connection with improving your  
2 system?

3 A. Right. As of today, what we are undertaking  
4 is a review of our system based on the guidelines of  
5 transmission and distribution system programs. To date,  
6 nothing has come up to where it would require us to  
7 either implement Part A or Part B of this particular  
8 rider. Part of the requirements of the transmission and  
9 distribution system -- or transmission pipeline  
10 integrity system is to conduct an assessment of your  
11 system, and if anything comes up during that assessment,  
12 that would be included in this particular rider.

13 Q. But when you do the assessment, if you find  
14 that your current system is deficient, that wouldn't  
15 count under this rider; is that correct?

16 A. Did you say deficient?

17 Q. If it's deficient under current rules and  
18 regulations, that would not count; is that correct?

19 A. It would count only if we are undertaking the  
20 new rules of either the transmission pipeline integrity  
21 system or distribution integrity system that resulted in  
22 a deficiency at that point in time.

23 Q. I didn't understand that answer.

24 A. Well, maybe I didn't understand the question.

25 Q. You're going out to inspect your lines.



1           A.    Yes.

2           Q.    And an engineer comes back and says, "Oh, my  
3 goodness, this is does not comply with existing safety  
4 regulations, and we have to upgrade it." My  
5 understanding of what you told us was that that would  
6 not be applicable for treatment under this clause.

7           A.    That's correct. It would have to be under the  
8 new guidelines of the new mandate just brought in by the  
9 government, yes.

10          Q.    And these are new mandates that may be enacted  
11 after January 1, 2010?

12          A.    Well, no. They have already been enacted, but  
13 we are in the process of evaluating our systems under  
14 those guidelines.

15          Q.    I see. So when were the guidelines enacted?

16          A.    One of the guidelines -- and let me refer back  
17 to my testimony to get you the dates. The Pipeline  
18 Safety Act of 2002 addressed the transmission portion of  
19 that, and the Pipeline Inspection, Protection,  
20 Enforcement, and Safety Act of 2006 is more for  
21 distribution systems. So those are the two acts.

22          Q.    So these are statutes and rules that are  
23 currently in place, and you're currently doing an  
24 inspection to see if your system complies with those  
25 Safety Act requirements?

1           A.    We are currently doing an assessment for the  
2 transmission facilities we have in place.  The Pipes Act  
3 of 2006 deals with distribution systems.  Those are not  
4 fully implemented at this point in time, so they haven't  
5 come out with the full guidelines on distribution  
6 systems yet.

7           Q.    Is the Safety Act a law, or is it a rule?

8           A.    I believe it's law, because it was signed into  
9 law by President Bush.

10          Q.    Now, Peoples Gas has been around a pretty long  
11 time, has it not?  When was Peoples Gas founded?  Back  
12 in the '20s?

13          A.    I don't know, but years.

14          Q.    Okay.  Well, I guess you have some older pipes  
15 that actually are really beyond the useful life that  
16 they were originally forecasted to live; is that  
17 correct?

18          A.    We have pipes of varying ages in our system,  
19 yes.

20          Q.    I didn't understand what you said.

21          A.    We have pipes of various ages in our system.

22          Q.    Do you have any pipes as old as 20 years old?

23          A.    Yes.

24          Q.    And I heard by the last witness that the  
25 depreciation rate is -- what?  2.9 percent?

1           A.    That would be this witness.

2           Q.    You're the guy that said that?

3           A.    Yes.

4           Q.    It seemed so long ago to Mr. Carter, because  
5 he doesn't really like me to ask all these questions.

6           A.    That particular reference to depreciation was  
7 for a certain schedule that I had attached as an  
8 exhibit.

9           Q.    I see.  But 2.9, you divide that into 100, and  
10 so it would indicate that something with that  
11 depreciation life would normally last 30 years.  Does  
12 your system have pipes that are over 30 years old?

13          A.    We do.

14          Q.    You do.  Now, when with you analyze these  
15 pipes under this new program, if you've got a  
16 30-year-old pipe that's being replaced, you're not going  
17 to use the depreciation charges you've accumulated over  
18 the years and collected from customers to replace it?  
19 You're going to use a new cost recovery clause to do  
20 that with?

21          A.    If a certain mandate is brought forth to us  
22 that requires us to make an additional investment that  
23 we normally would not have made because of a mandate,  
24 then the answer is yes.

25          Q.    Can you give me a specific example, three of

1 those particular -- three examples of mandates that  
2 didn't exist before the new law?

3 A. I'm not sure I understand the question.

4 Q. Well, you've got a 30-year-old transmission  
5 line.

6 A. Right.

7 Q. You've got a 2006 law that has either been  
8 implemented by rules or is in the process of being  
9 implemented by rules, and you said in your last answer  
10 that you would look at the pipe and determine whether it  
11 met one of these new criteria. Give me three examples  
12 of situations that might arise when you would employ  
13 this mechanism as opposed to just standard replacement  
14 of old, worn-out pipes.

15 A. Well, for the Pipes Act, which handles  
16 distribution systems, I don't think I can give three  
17 examples on that, because that was newly implemented,  
18 and we don't have the rules for that yet.

19 For transmission, I don't know that I can  
20 specifically give you three, but part of the process  
21 right now for the transmission and distribution pipeline  
22 system is for us to first identify transmission systems,  
23 transmission pipelines within our system. And based on  
24 the location of where those transmission systems are  
25 located, they are qualified as either high consequence

1 areas or non-high consequence areas, and that's really  
2 because of population density, or buildings such as  
3 school buildings or downtown, and things of that nature.

4 The transmission pipeline integrity program  
5 calls for us to do an assessment of those transmission  
6 facilities within those high consequence areas. And if  
7 for whatever reason, part of the requirement is that it  
8 doesn't meet certain guidelines under the new rule, then  
9 we have to implement some type of corrective action for  
10 that. Prior to that, we didn't have that particular  
11 designation of either high consequence area or non-high  
12 consequence area.

13 CHAIRMAN CARTER: Mr. McWhirter, would you  
14 yield for a moment, please?

15 MR. McWHIRTER: Yes, sir.

16 CHAIRMAN CARTER: Thank you. Commissioner  
17 Skop, you're recognized.

18 COMMISSIONER SKOP: Thank you, Mr. Chairman.  
19 I guess we're getting close to the adjournment hour, but  
20 I just had two quick questions that I kind of wanted to  
21 get in before we adjourn for the day if Mr. McWhirter  
22 would be kind enough to have yielded.

23 I just have two questions with respect to the  
24 proposed GRS, which is the gas system reliability rider,  
25 and also the CR, carbon reduction rider. Would it be

1 correct, based on what I've heard so far, to understand  
2 that the GSR rider provides for relocation requiring no  
3 pre-approval, and also for other government-mandated  
4 expenses under the Pipes Act that you mentioned?

5 THE WITNESS: Yes.

6 COMMISSIONER SKOP: Okay. And with respect to  
7 relocation, I know that the federal stimulus package has  
8 provided substantial funding to various states within  
9 our nation for transportation projects. Does the  
10 language within the federal stimulus package as enacted  
11 provide for the use of federal funds for reimbursement  
12 where relocation is necessitated or necessary to  
13 accommodate a project authorized by the federal stimulus  
14 package?

15 THE WITNESS: That is discussion that's going  
16 on in Washington. I know that several utilities, and in  
17 particular, the American Gas Association was concerned  
18 about the language in the stimulus program, that it did  
19 not cover some of the reimbursement for relocations  
20 associated with road programs under the stimulus  
21 program. So I don't know that it's covered or not at  
22 this point.

23 COMMISSIONER SKOP: Okay. But there may be  
24 some hope of getting some federal funding or being able  
25 to tap into federal funding to the extent that it's not

1 a stranded cost on ratepayers?

2 THE WITNESS: Yes.

3 COMMISSIONER SKOP: Okay. And then secondly  
4 -- and I know we haven't really gotten into this, but on  
5 the carbon reduction rider, again, both of these are  
6 fairly new concepts to our Commission, but readily  
7 utilized, from my understanding, throughout other states  
8 in our nation. With respect to the carbon reduction  
9 rider, I understand the environmental benefits of using  
10 natural gas. It's a clean source of water heating,  
11 et cetera.

12 But with respect to that proposed rider, you  
13 know, essentially, if it is recovered in a clause, as  
14 I've heard some discussion on, theoretically, you know,  
15 you could put in various mains to serve, you know, new  
16 developments or proposed developments, and that could  
17 get kind of costly relatively quickly. Is there any  
18 pre-approval process that would need to come to the  
19 Commission to get approval, or would it be more  
20 appropriate to put a dollar limitation on what could be  
21 recovered on an annual basis to the extent that, you  
22 know, a company, not Peoples, but a given company could  
23 go, you know, put gas in all places of the state if they  
24 wanted to and have no check and balance on what  
25 expenditures might be passed through to the customers in

1 a given year?

2 THE WITNESS: Sure. The way it's currently  
3 written, the only limitation that is in there right now  
4 is by type of main and size of main, and that it has to  
5 serve primarily residential developments. As far as  
6 putting in a cap or pre-approval, it wasn't drafted that  
7 way, but we are open to that. I mean, if -- so if, you  
8 know, during discussions with staff, it's appropriate to  
9 say, "We would like to review certain projects," then we  
10 would be willing to do something like that.

11 COMMISSIONER SKOP: And I'm not suggesting one  
12 is required or not. I'm just trying to get a better  
13 understanding of the concept and the various mechanisms  
14 under which something that this Commission may be asked  
15 to approve would operate. So I appreciate that.

16 And I think, Mr. Chair, I kept us right on  
17 time.

18 CHAIRMAN CARTER: Thank you. Guess what.  
19 Tomorrow morning, Mr. McWhirter, you can kick us off,  
20 and it's going to be a great day. I really look forward  
21 to seeing you tomorrow and hearing from you. And the  
22 witness will be in the same place, and we'll continue.

23 With that, we are adjourned.

24 (Proceedings recessed at 5:31 p.m.)

25



