BEFORE THE

STATE OF NEW YORK

PUBLIC SERVICE COMMISSION

IN THE MATTER OF

CASE 93-G-0756

NATIONAL FUEL GAS DISTRIUBTION CORPORATION

Prepared Testimony Of

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Three Empire State Plaza
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January 1994

months ended March 31, 1993. Column 3 is merely the extension of columns (1) and (2). Column (4) shows Staff adjustments to reflect the rate year projection. Column (5) is merely the extension of columns (3) and (4). The explanation of the adjustments in column (2) and column (4) are explained on Sheet 2 of Schedule 8.

Q. Why have you included certain items in the historic earnings base and historic rate base?

A. I have included in historic rate base the average non-interest bearing booked historic asset balances that are supported by capitalization. In addition to the items included in the historic rate base, I have included in earnings base the interest bearing historic booked asset balances supported by capitalization. I have made these inclusions in order that the EB/CAP adjustment would be properly calculated (See Adjustment (e), Schedule 8).

<u>TRA IMPACTS - UNCOLLECTIBLES</u>

Q. Please explain adjustment (a) of $1,038,000.

A. I have included the historic booked average balance that's supported by capitalization.

A. Adjustment (e) increases the EB/CAP adjustment by ($6,773,000) from ($3,156,000) to ($9,929,000) and reduces rate base by a like amount. The calculation of this adjustment is shown on Schedule 8, Sheet 3 . The calculation is similar to the Company's Exhibit 3 (SA-1) Schedule 13, Sheets 1-3, Revised 11/93.

Q. Please explain Schedule 8, Sheet 3.

A. The schedule calculates the excess earnings base over capitalization. The earnings base for the Total Distribution and New York Division of the Distribution are shown on Sheet 5 and Sheet 7 of Schedule 8, respectively.

Q. Please explain Sheet 5 of Schedule 8.

A. Column (1) shows the Total Distribution Average Earnings Base as shown on Exhibit 3 (SA-1), Schedule 13, Sheet 2, Revised 11/93 of the Company's presentation. Column (2) shows Staff adjustments and Column (3) is merely the extension of Columns (1) and (2). An explanation of the adjustments in Column (2) are shown on Sheet 6 of Schedule 8.

Q. Please explain the adjustments on Sheet 5.

A. Adjustment (a) of $ 7,871,000 includes the Pennsylvania portion of the comparable New York

Gas Corporation does not keep separate balance sheets for the New York and Pennsylvania Divisions of the Distribution Corporation. The methodology I propose was accepted by the Commission in Case 26929, National Fuel Gas Distribution Corporation-Gas Rates (Opinion 76-24) as a fair way of allocating capital and has been used since 1976.

Q. Please explain your understanding of this allocation.

A. It is impossible to charge capital directly to either Pennsylvania or New York. However, the jurisdictional identity of assets that are financed by capital can be determined. By taking the total of the New York jurisdiction's assets and dividing it by the total assets of the Distribution Corporation, a percentage can be calculated. Based on this percentage, capital would be allocated to each jurisdiction.

Q. Why is it necessary to include the Pennsylvania deferred expense items in Earnings Base - Total Distribution?

A. Earnings Base must include all historic assets that are supported by historic capitalization in order to calculate a fair allocation. Company witness Ayers

A. Adjustment (d) of $2,239,000 increases Total Distribution Earnings Base from $1,976,000 to $4,215,000. This includes the historical level of a tax payment made (September 1987) to the IRS relating to the examination of the federal income tax returns going back to 1977. This booked historic balance is supported by capitalization.

Q. Please continue.

A. Adjustment (e) of $1,899,000 includes the Total Distribution Corporation's average historic level of TRA Impacts-Unbilled Revenue and TRA Impacts of Unbilled Revenue Reserve Addback.

Q. What is adjustment (f) of $1,213,000?

A. This includes the average historic level of the Total Distribution Corporation's Deferred Paragon Costs that are supported by capitalization.

Q. Please continue.

A. Adjustment (g) eliminates the adjustment for reorganization costs. These costs are embedded in the historic year, supported by capital and must be left in the earnings base.

Q. What does Sheet 7, of Schedule 8 show?

A. Column (1) shows the New York Division Average that are supported by capitalization.

Q. Please explain adjustment (f) of $93,000.

A. To include Reorganization Costs in Earnings Base since they are supported by capitalization.

Q. Please explain this Schedule 8, Sheet 4.

A. Column (1) is Staff Adjusted Total Distribution Average Earnings Base and column (2) shows the NY Division Average Earnings Base. The calculation of the Total Distribution Average Earnings Base and NY Division Earnings Base is shown on Schedule 8, Sheet 5 and Schedule 8 Sheet 7, respectively. Since the Total Distribution Earnings Base includes all items that are supported by capitalization, dividing the New York Division Distribution Earnings Base by the Total Distribution Earnings Base gives a percentage to allocate New York capitalization. Therefore, 72.11% of the historic capitalization is allocated to the New York Division of the Distribution. Schedule 8, Sheet 3 shows the New York Division Earnings Base and Capitalization. The difference between the New York Division Earnings Base of $512,945,000 and New York Division capitalization of $503,016,000 produces an EB/CAP an adjustment to that balance of $1,078,000 that is testified to by Mr. Lurski.

NONINTEREST BEARING CWIP-RATE YEAR

Q. Please explain adjustment (i) of $1,000.

A. This adjustment increases this item to the company requested level shown on Exh 2 (SA-2), Sch 2, Sh 2.

RESERVE FOR DEPRECIATION DEPLETION AND AMORTIZATION-RATE YEAR

Q. Please explain adjustment (j) of ($17,497,000)?

A. This adjustment increases the item per the company request shown on Exh 2 (SA-2), Sch 2, Sh 2.

CASH WORKING CAPITAL ALLOWANCE-RATE YEAR

Q. Please explain adjustment (k) of $1,632,000.

A. This is calculated by taking 1/8 of the Staff Adjusted Operating and Maintenance Expense.

PREPAYMENTS-RATE YEAR

Q. Please explain adjustment (l) of $1,968,000

A. I have taken the Company requested level of $10,972,000 (Exh__(SA-2), Sch 4,) and reduced it by Staff's adjustment of ($298,000) for a rate year level of $10,674,000. This is due to a reduction in the projected level of property tax expense.

DEFERRED INVESTMENT TAX CREDIT-RATE YEAR

Q. Please explain adjustment (p) of $1,336,000.

A. I have taken the company requested level of ($8,775,000) (Exh 33 DFR-3) and reduced it by $306,000 to ($8,469,000). This adjustment is consistent with my treatment under adjustment 23.

DEFERRED HIECA-RATE YEAR

Q. Please explain adjustment (q) of ($1,068,000)?

A. I have taken the company requested level of $(535,000) and reduced it by Staff's adjustment of ($321,000) to a total of ($856,000). Mr. Luthringer testifies to this adjustment.

DEFERRED NEW YORK SALES AND USE TAX LIABILITY

Q. Please explain adjustment (r) of $560,000.

A. This adjustment is necessary to reflect the Company's request of $716,000.

DEFERRED MANAGEMENT AUDIT-RATE YEAR

Q. Please explain adjustment (s) of ($85,000).

A. This adjustment eliminates this item from the rate year and is consistent with the Company's request.

DEFERRED PSC ASSESSMENT

Q. Please explain adjustment (t) of $289,000.

A. This adjustment increases this item to the company

A. I have calculated the rate year level for this item.

<u>90/10 BOILER FUEL SYM SHARING-RATE YEAR</u>

Q. Please explain adjustment (aa) of $959,000.

A. This ajustment eliminates this item from the rate year.

<u>DEFERRED PARAGON COSTS</u>

Q. Please explain your adjustment (bb) of ($827,000).

A. This adjustment eliminates this item from the rate year and is testified to by Mr. Lurski.

<u>ELIMINATION OF REORGANIZATION COSTS PER CASE 27934</u>

Q. Please explain your adjustment (cc) of ($93,000).

A. This adjustment eliminates this item from the rate year.

Q. What is staff's recommendation in this proceeding?

A. Based on staff's calculation of revenues, expenses, rate base and rate of return the company should increase its rates by no more than $2,851,000.

Q. Does this conclude your testimony at this time?

A. Yes, it does.

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Exhibit (GW-1)
Schedule 6
Sheet 1 of 1

National Fuel Gas Distribution Corporation
New York Division
Statement of Rate Base at Mid-Point (January 31, 1995)
For the Twelve Months Ending July 31, 1995
($000)

	Exh 2 (SA-2) Schedule 1 Sheet 1		Differences	Exh.(GRW-1) Sch 8 Sh 1 Column 5
Net Plant	$576,362	(a)	($1,078)	575,284
Working Capital				
Operating and Maintenance Expense Allow.	18,555	(b)	(1,135)	17,419
Prepayments	10,972	(c)	(298)	10,674
Materials & Supplies	4,718		0	4,718
Gas Storage Inventory	10,702	(d)	(16,999)	(6,297)
Accrued Liability for Annuity Program	0		0	0
Total Working Capital	44,947		(18,432)	26,514
Deferred Income Taxes-Liberalized Depr.	(52,087)	(e)	(453)	(52,540)
Deferred Income Taxes-Investment Tax Cr.	(8,775)	(f)	306	(8,469)
NYGAS-Weaver	0		0	0
Deferred HIECA	(535)	(g)	(321)	(856)
Deferred Management Audit	0		0	0
Deferred NYPSC Assessment	290		0	290
Deferred R,D&D	(178)		0	(178)
Deferred Property Tax True Up (89-G-179)	0		0	0
Deferred Sales Tax	716		0	716
Deferred Site Remediation Costs	1,323		0	1,323
Deferred Income Taxes - FIT Audit	310	(h)	(310)	0
Deferred Meter Transfer	190		0	190
Deferred Gas Planning	1,525	(i)	(928)	597
Deferred Transition Costs	7,052	(j)	(7,052)	0
Deferred Memberships	100	(k)	(100)	0
Deferred Paragon/TGX	1,304	(l)	(1,304)	0
Deferred Tax Rate Change	284	(m)	(284)	0
Elimination of Reorganization Cost-C.27934	(93)		0	(93)
TRA Impacts - Uncollectibles	0	(n)	1,990	1,990
Deferred Income Taxes - FIT	0	(o)	3,161	3,161
TRA Impacts - Unbilled Revenues	0	(p)	4,850	4,850
Earnings Base in Excess of Capitalization	1,586	(q)	(11,515)	(9,929)
Rate Base @ Midpoint - Jan 31, 1995	574,321		(31,470)	542,850

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Exhibit (GW-1)
Schedule 7
Sheet 1 of 2

National Fuel Gas Distribution Corporation
New York Division
Explanation of Staff Adjustments

a) Net Plant
Include Staff's estimate.

b) Operating and Maintenance Expense Allowance
1/8 of Staff adjustments to Operating and Maintenance expense excluding purchased gas.

c) Prepayments
Include Staff's estimate for this item.

d) Gas Storage Inventory
Includes Staff's estimate for this item.

e) Deferred Income Taxes - Liberalized Depreciation
ACRS - ADR (Depreciation) on calendar 1981 additions.

f) Deferred Income Taxes -Investment Tax Credit
Reflect the use of Option II for the former Pennsylvania Gas Corp.

g) Deferred HIECA
Reflect the impact of this item consistent with staff's treatment.

h) Deferred Income Tax - FIT
Eliminate this item since no additional expenditures will be made in the link or rate year period.

i) Deferred Gas Planning
Includes staff's estimate.

j) Transition Costs
Eliminate this item from rate base.

k) Deferred Membership
Eliminate these charges from rate base.

l) Deferred Paragon TGX
Eliminate these charges from rate base.

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Exhibit (GW-1)
Schedule 7
Sheet 2 of 2

m) Deferred Tax Rate Change
Eliminate this item from rate base.

n) TRA-Impacts Uncollectibles
Include rate year estimate for this item.

o) Deferred Income taxes - FIT
Include rate year level.

p) TRA Impacts - Unbilled Revenues
Include rate year level.

q) Rate Base in Excess of Capitalization
Include staff's calculation of this item.

National Fuel Gas Distribution Corporation
New York Division
Statement of Rate Base At Midpoint (January 31, 1995)
From the Twelve Months Ended March 31, 1993
$(000)

Gas Plant in Service	Exh 3 (SA-1) Sch 13, Sh 1 Rev 11/93		Staff Adj.	Historic Rate Base Staff Adj.		Rate Year Adj.	Staff Rate Base Rate Year
Gas Plant	$653,676			$653,676	(h)	$87,212	$740,888
NIBCWIP	2,782			2,782	(i)	1	2,783
Total	656,458		0	656,458		87,213	743,671
Reserve for Depr. Depl. & Amort	(150,890)			(150,890)	(j)	(17,497)	(168,387)
	505,568		0	505,568		69,716	575,284
Working Capital							
Cash Allowance	15,787			15,787	(k)	1,632	17,419
Prepayments	8,706			8,706	(l)	1,968	10,674
Material and Supplies	4,719			4,719	(m)	(1)	4,718
Gas Storage Inventory	0			0	(n)	(6,297)	(6,297)
Total Working Capital	29,212		0	29,212		(2,698)	26,514
Deferred Income Taxes ADR	(39,516)			(39,516)	(o)	(13,024)	(52,540)
Deferred Investment Tax Credit	(9,805)			(9,805)	(p)	1,336	(8,469)
Deferred HIECA	212			212	(q)	(1,068)	(856)
Deferred NY Sales & Use Tax Liab.	156			156	(r)	560	716
eferred Management Audit	85			85	(s)	(85)	0
Deferred PSC Assessment	1			1	(t)	289	290
Deferred Research, Development & Expense	(27)			(27)	(u)	(151)	(178)
Deferred Site Remediation Costs	258			258	(v)	1,065	1,323
Deferred Income Taxes - FIT	0			0		0	0
Deferred Meter Transfer	0			0	(w)	190	190
Deferred Gas PLanning	0			0	(x)	597	597
Deferred Transition Costs	0			0		0	0
Deferred Memberships	0			0		0	0
Deferred Tax Rate Change	0			0		0	0
Property Tax TrueUp(C89-G-179)	669			669	(y)	(669)	0
TRA Impacts - Uncollectible	0	(a)	1,038	1,038	(z)	952	1,990
90/10 Boiler Fuel Sym Sharing	0	(b)	(959)	(959)	(aa)	959	0
Deferred Income Taxes - FIT Audit	1,976	(c)	1,185	3,161		0	3,161
TRA Impacts-Unbilled Revenues	4,505	(d)	345	4,850		0	4,850
Capital. in Excess of Earnings Base	(3,156)	(e)	(6,773)	(9,929)		0	(9,929)
Deferred Paragon Costs	0	(f)	827	827	(bb)	(827)	0
Elim. of Reor. Costs Per Case 27934	(93)	(g)	93	0	(cc)	(93)	(93)
Total Annual Rate Base	$490,045		($4,244)	$485,801		$57,049	$542,850

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Exhibit (GW-1)
Schedule 8
Sheet 2 of 8

National Fuel Gas Distribution Corporation
New York Division
Explanation of Staff Adjustments

a-d) Include the historic level for each of these items since they are supported by capitalization.

e) Staff calculation of EB/CAP (Schedule 8, Sheet 3).

f&g) Include historic level for each of these items since they are supported by capitalization.

h-j) Include Staff's rate year projection for each of these items.

k) 1/8 of Staff adjusted operating and maintenance expenses.

l) Staff adjusts property tax prepayments.

m-q) Include Staff's rate year projection.

r-w Reflect Company's request.

x) Include Staff's rate year projection.

y) Company eliminates this item from rate base.

z) Include Staff's rate year projection.

aa) Include the Company's projection.

bb) Staff eliminates the recovery of this item.

cc) Eliminate the recovery of Reorganization Costs.

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National Fuel Gas Distribution Corporation
New York Division
Comparison of Historic Earnings Base Vs. Capitalization
For the Twelve Months Ended March 31, 1993
$(000)

	Total Distribution	Total New York Division
Earnings Base (Sch.8, Sh.4)	$711,301	$512,945
Average Capitalization (See Below)	697,568	503,016
Excess Earnings Base Over Capitalization	$13,733	$9,929

	Total Distribution
Average Capitalization Per Company (Exhibit 3 (SA–1), Schedule 13, Sheet 3 Of 3)	$697,568
Staff Adjustments:	
PA closed cycles	0
	697,568
New York Capitalization (72.11%)	0.7211
	$503,016

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National Fuel Gas Distribution Corporation
Total Distribution/New York Division
Average Earnings Base
For the Twelve Months Ended March 31, 1993
$(000)

Exhibit (GRW-1)
Schedule 8
Sheet 4 of 8

	Total Dist. Sch8, Sh5	NY Division Sch8, Sh7
Gas Plant	$890,085	$634,264
Work in Progress		
Completed Construction Not Classified Account 106	22,975	19,412
Construction Account 107	10,888	8,766
NFTA Acct. 186 (Rapid Transit)	0	0
	923,948	662,442
Reserve for Depreciation Depletion, and Amortization	(209,795)	(150,890)
	714,153	511,552
Working Capital		
Operating and Maintenance Exp. Allowance	21,301	15,787
Prepayments	11,318	8,706
Material and Supplies	6,597	4,719
Accrued Liability for Annuity Program	0	0
Total Working Capital	39,216	29,212
Deferred Income Taxes – ADR,ACRS	(60,104)	(39,516)
Deferred Investment Tax Credit	(14,946)	(9,805)
Deferred Net HIECA	216	212
Deferred Sales Tax	156	156
Deferred Management Audit	124	85
Deferred Commission Assessment	1	1
Deferred Conservation Programs	322	0
Deferred R D & D	(27)	(27)
Deferred Ashland Settlement	0	0
Deferred Take-or-Pay – NY	11,231	11,231
Deferred Take-or-Pay – PA	7,155	0
Deferred Acumen	32	0
Deferred Quality of Service	42	0
90\10 Boiler Fuel Sym Sharing – NY	(959)	(959)
Deferred Mfg. Gas Plant Cleanup – MSW & BSC	258	258
Property Tax TrueUp (89-G-179)	669	669
TRA Impacts-Uncollectibles	1,930	1,038
Deferred Income Taxes – FIT Audit	4,215	3,161
Deferred Paragon Costs	1,213	827
TRA Impacts-Unbilled Revenues	6,404	4,850
TRA Impacts-Unbilled (Reserve	0	0
Total Earnings Base	$711,301	$512,945
NY Earnings Base as Percentage of Distribution Corporation		72.11%

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National Fuel Gas Distribution Corporatic
Total Distribution
Average Earnings Base
For the Twelve Months Ended March 31, 1993
$(000)

Exhibit (GRW-1)
Schedule 8
Sheet 5 of 8

	Total Dist.		Staff Adj.	As Adj.
Gas Plant	$890,085			$890,085
Work in Progress				
Completed Construction Not Classified Account-106	22,975			22,975
Construction Account-107	10,888			10,888
NFTA Acct. 186 (Rapid Transit)	0			0
	923,948		0	923,948
Reserve for Depreciation Depletion, and Amortization	(209,795)			(209,795)
	714,153		0	714,153
Working Capital				
Operating and Maintenance Exp. Allowance	21,301			21,301
Prepayments	11,037	(a)	281	11,318
Material and Supplies	6,597			6,597
Accrued Liability for Annuity Program	0			0
Total Working Capital	38,935		281	39,216
Deferred Income Taxes - ADR,ACRS	(60,104)			(60,104)
Deferred Investment Tax Credit	(14,946)			(14,946)
Deferred Net HIECA	216			216
Deferred Sales Tax	156			156
Deferred Management Audit	85	(a)	39	124
Deferred Commission Assessment	1			1
Deferred Conservation Programs	0	(a)	322	322
Deferred R D & D	(27)			(27)
Deferred Ashland Settlement	0			0
Deferred Take-or-Pay - NY	17,016	(b)	(5,785)	11,231
Deferred Take-or-Pay - PA	0	(a)	7,155	7,155
Deferred Acumen	0	(a)	32	32
Deferred Quality of Service	0	(a)	42	42
90\10 Boiler Fuel Sym Sharing - NY	(959)			(959)
Deferred Mfg. Gas Plant Cleanup - MSW & BSC	258			258
Property Tax TrueUp (89-G-179)	669			669
TRA Impacts-Uncollectibles	0	(c)	1,930	1,930
Deferred Income Taxes - FIT Audit	1,976	(d)	2,239	4,215
TRA Impacts-Unbilled Revenues	4,505	(e)	1,899	6,404
TRA Impacts-Unbilled (Reserve)			0	0
Deferred Paragon Costs	0	(f)	1,213	1,213
Elimination of Reorganization Costs	(93)	(g)	93	0
Total Earnings Base	$701,841		$9,460	$711,301

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Exhibit (GW-1)
Schedule 8
Sheet 6 of 8

National Fuel Gas Distribution Corporation
New York Division
Explanation of Staff Adjustments
Average Earnings Base
Total Distribution

a) Include Pennsylvania's Earnings Base Components.

b) Take-or-Pay costs should be net of tax.

c-g) Include Distribution's historic level balance for each of these items.

C. 93-G-0756 National Fuel Gas Distribution Corporation Exhibit (GRW-1)
New York Division Schedule 8
Average Earnings Base Sheet 7 of 8
For the Twelve Months Ended March 31, 1993
$(000)

	Total Dist.		Staff Adj.	As Adj.
Gas Plant	$634,264		$0	$634,264
Work in Progress				
Completed Construction Not Classified Account-106	19,412			19,412
Construction Account-107	8,766			8,766
NFTA Acct. 186 (Rapid Transit)	0			0
	662,442		0	662,442
Reserve for Depreciation Depletion, and Amortization	(150,890)		0	(150,890)
	511,552		0	511,552
Working Capital				
Operating and Maintenance Exp. Allowance	15,787			15,787
Prepayments	8,706			8,706
Material and Supplies	4,719			4,719
Accrued Liability for Annuity Program	0			0
Total Working Capital	29,212		0	29,212
Deferred Income Taxes - ADR,ACRS	(39,516)			(39,516)
Deferred Investment Tax Credit	(9,805)			(9,805)
Deferred Net HIECA	212			212
Deferred Sales Tax	156			156
Deferred Management Audit	85			85
Deferred Commission Assessment	1			1
Deferred Conservation Programs	0			0
Deferred R D & D	(27)			(27)
Deferred Ashland Settlement	0			0
Deferred Take-or-Pay - NY	17,016	(a)	(5,785)	11,231
90\10 Boiler Fuel Sym Sharing - NY	(959)			(959)
Deferred Mfg. Gas Plant Cleanup - MSW & BSC	258			258
Property Tax TrueUp (C.89-G-179)	669			669
TRA Impacts-Uncollectibles	0	(b)	1,038	1,038
Deferred Income Taxes - FIT Audit	1,976	(c)	1,185	3,161
TRA Impacts-Unbilled Revenues	4,505	(d)	345	4,850
TRA-Impacts Unbilled (Reserve)	0		0	0
Deferred Paragon Costs	0	(e)	827	827
Elimination of Reorganization Costs	(93)	(f)	93	0
Total Earnings Base	$515,242		($2,297)	$512,945

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Exhibit (GW-1)
Schedule 8
Sheet 8 of 8

National Fuel Gas Distribution Corporation
New York Division
Explanation of Staff Adjustments
Average Earnings Base
New York Division

a) Include the balance of Take-or-Pay net of tax.

b-e) Include historic level of New York Division Distribution items since they are supported by capitalization.

f) Eliminate reorganization Costs.

STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

OPINION NO. 94-16

CASE 93-G-0756 - Proceeding on Motion of the Commission as to the Rates, Charges, Rules and Regulations of National Fuel Gas Distribution Corporation for Gas Service.

OPINION AND ORDER DETERMINING REVENUE REQUIREMENT AND RATE DESIGN

Issued and Effective: July 19, 1994

RATE BASE

Gas Storage Inventory

On August 1, 1993, responsibility for gas storage was transferred from NFG Supply to the distribution company. The transfer raised, for the first time in a National Fuel rate case, the issue of whether the company should receive a cash working capital allowance for its gas storage inventory. The Judge agreed with staff that no cash working capital allowance was necessary, since ratepayers prepay the cost of the gas held in storage. In addition to eliminating a $10.7 million working capital allowance the company had claimed, the Judge also reduced rate base by another $6.3 million to compensate ratepayers fully for the cost-free capital their prepayments provide the company. National Fuel excepts.

The company acknowledges that ratepayers provide cost-free working capital by prepaying for gas held in storage. But, since the customer prepayments are fully dissipated by the time the gas is withdrawn, it claims, ratepayers should receive only a short-term financial benefit. Accordingly, National Fuel has proposed, instead of a rate base reduction, that interest be permitted on GAC open cycle over- and under-collections. The company claims this would be a better way to measure accurately the benefit resulting from customer prepayments. In support, National Fuel notes that it is the only gas distribution company in New York to use the last-in, first-out (LIFO) method of valuing its gas storage inventory. If it were to use another accounting method, it says, it could support a $45 million rate base addition and a $7.5 million revenue requirement for this item. Under such circumstances, National Fuel believes it only fair to change its GAC to permit interest on the open cycle.

In reply, staff says the company's proposal for interest on the GAC open cycle has nothing to do with the proposed rate base reduction. It also sees no basis for the company's claim that a rate base deduction over-compensates ratepayers. According to staff, National Fuel's cash working capital is financed by all forms of capital, and it is not necessary to ascribe a short-term financing rate to the customer prepayments.

Staff's position is correct and there is no need here to modify the current operation of the GAC. The company's exception is denied and a rate base reduction will be made consistent with staff's proposal.

Earnings Base/Capitalization Adjustment

In this case the Judge accepted staff's recalculation of the earning base/capitalization adjustment National Fuel presented. Staff corrected the company's calculation of its total capitalization and applied a net-of-tax return to the take-or-pay costs that the company has been deferring.

The company has not excepted to the Judge's recommendation; however, staff has requested that this matter be put to rest for all time. Staff requests that Judge's finding be expressly endorsed so National Fuel will not relitigate the issue in a future case.

Staff has properly calculated the earnings base/capitalization adjustment to be applied here.

RATE OF RETURN

Common Equity

The only contested issue in this category concerns the cost of common equity. In National Fuel's last rate case, decided in July 1992, its equity return was set at 12%. In this case, the Judge has recommended a cost of 10.4%, using data from January 1994.

In January 1994, the company was seeking a return on equity of about 11.5%. It arrived at this figure by using a consensus method developed in Case 91-M-0509,[1] the Generic Financing Case, and by adding 50 basis points to the result for new business risks brought about by the restructuring of the gas industry pursuant to FERC Order 636. Using a discounted cash flow (DCF) approach, staff and CPB were supporting equity returns just under 10%.

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1 Case 91-M-0509, Proceeding to Consider Financial Regulatory Policies for New York.

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Witness: Koch

NATIONAL FUEL GAS DISTRIBUTION CORPORATION
NEW YORK DIVISION
RESPONSE TO DEPARTMENT OF PUBLIC SERVICE
REQUEST FOR INFORMATION
CASE 16-G-0257

Question

Re: EB/CAP
1) Provide an explanation why the Company applied the allocation of NY earnings base, to total earnings base (74.28%), to the total capitalization, rather than using the NY Only capitalization in their EB/CAP calculation. Provide all supporting documentation, explanations, and rationales.

2) Referring to Exhibit___ (DNK-1) Schedule 9, Sheet 3, provide an explanation of account "Cap Rel/OSS/SC11 85%. In addition, explain how it is allocated to NY, and PA. Provide all supporting calculations in excel format with formulas intact.

Response

1. The allocation of NY earnings base to total earnings base has been well established in previous cases. The Company presented an EB/Cap adjustment based on NY capitalization in Case 04-G-1047. Staff rejected that approach. Please refer to attachment 1, pages 2 - 7 of Mr. Wojcinski Testimony provided in Case 04-G-1047 which argues against the merits of utilizing the NY-only capitalization method. In Case 07-G-0141, the Company did not employ a NY-only capitalization. See Direct Testimony of Regina L. Truitt at 38-39. Staff witness Wojcinski stated that he agreed with Ms. Truitt's EB/Cap method. Wojcinski at 15.

2. Cap Rel/OSS/SC11 85% is the balance of Capacity Release Credits, Offsystem Sales and the SC 11 revenues that are shared 85%/15% with the NY ratepayers. The 85% amount shared with the ratepayers is deferred for passback to the ratepayers until the November through March period as directed in the Settlement Agreements. This is allocated 100% to NY.

DIRECT TESTIMONY OF REGINA L. TRUITT

A. The cash working capital allowance should be calculated using the more precise and more specific to Distribution lead lag study.

Q. But hasn't the Commission prohibited the use of a lead lag study?

A. While the Commission has greatly discouraged the use of a lead lag study, the basis for its decision has greatly diminished with the use of computers and new accounting systems.

Q. What method of calculation for cash working capital allowance is used by the Pennsylvania Division for ratemaking?

A. The Pennsylvania Division of Distribution uses a lead lag study, which is the preferred method of determination of cash working capital by the PUC.

Q. Have you calculated cash working capital allowance using a lead lag study for this filing?

A. Yes, I have. However, I did not use the lead lag for the cash working capital allowance. I did use the 1/8 O&M and the EB/Cap method prevalent in NY. I prefer the lead lag and agree with staff that it is the most precise method for determining cash working capital allowance. However, since the amount in the Rate Year would be similar to the combination of the FPC method and EB/Cap, I will use the Commission's preferred method as a way of decreasing controversy in the rate case filing.

Q. Is the EB/CAP adjustment calculated the same way as in Case 04-G-1047, Distribution's last base rate filing?

A. In the last rate case filing, I recommended that the items specifically created by NY decisions and can be attributed solely to the New York Division, should be allocated 100% to Distribution with the remaining capitalization allocated based on the NY Division's portion of the Total earnings base. Again in order to reduce

DIRECT TESTIMONY OF REGINA L. TRUITT

controversy in this proceeding I have not recommended a specific New York Division calculation, even though it would provide a more accurate allocation of capitalization to the NY Division.

Q. Please describe Exhibit___(RLT-6).

A. Exhibit___(RLT-6) consists of seven schedules. It is a statement of rate base calculated for the Rate Year ending December 31, 2008.

Q. Please describe Schedule 1 of Exhibit___(RLT-6).

A. This schedule is a summary of rate base for the Rate Year ending December 31, 2008. Detailed computations appear in Schedules 2 – 7.

Q. Please describe the $1,648,000 Deferred PSC Assessment amount shown on Schedule 1.

A. I have reflected the historic amount because the expense has been reflected as the latest known invoice.

Q. Please describe Exhibit___(RLT-6), Schedule 2.

A. Schedule 2 consists of five sheets and shows the estimated average net plant at December 31, 2008. Sheet 1 shows the derivation of estimated average plant in service at December 31, 2008. I began with the actual plant in service and actual reserve for depreciation at September 30, 2006. Based upon the Company's construction budget I estimated the monthly changes from October 2006 through December 2008 to arrive at the projected average net plant of $1,126,623,000 at December 31, 2008. I have also included the non interest bearing construction work in progress at September 30, 2006. The Company will be updating numerous items when it files its Brief on Exceptions. The Plant in Service should also be updated at that time.

BEFORE THE
STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

In the Matter of

National Fuel Gas Distribution Corporation

Case 04-G-1047

December 2004

Prepared Testimony of:

Gerald R. Wojcinski
Public Utilities Auditor II
Office of Accounting & Finance
State of New York
Department of Public Service
Three Empire State Plaza
Albany, New York 12223-1350

Q. Please state your name and business address.

A. Gerald R. Wojcinski, 6333 Main Street, Suite 4 Williamsville, NY 14221-5887

Q. By whom are you employed and in what capacity?

A. I am employed by the New York State Department of Public Service as a Public Utilities Auditor II in the Office of Accounting and Finance.

Q. Please state your educational background and professional experience?

A. I graduated from Canisius College in 1972 with a Bachelor's degree in Business Administration. My major was Accounting. From January 1973 to April 1974, I was employed as an Assistant to the Comptroller at the Wurlitzer Company. Thereafter, I joined the Staff of the Department of Public Service. Since that time I have participated in numerous utility accounting examinations including rate proceedings, finance cases, Public Involvement Process and a merger. I have previously testified before this Commission.

Q. What is your responsibility in this case?

A. I have overall supervision for the accounting examination in this proceeding.

Q. What is the scope of Staff's accounting examination?

A. In examining the company's presentation, the exhibits were checked to the books and records, where appropriate and the underlying assumptions and allocations were checked and reviewed. The test year was compared with prior periods. Transactions were also examined in order to ascertain a consistency between the test period and subsequent events. As a result of this examination and the company responses to staff interrogatories, Staff proposes certain adjustments to the company's presentation.

Q. Please describe the Exhibits that you are sponsoring in this proceeding

A. I am sponsoring three Exhibits under a cover page titled "Exhibits Referred to in the Prepared Testimony of Gerald R. Wojcinski". They are labeled:

1. Exhibit__ (GRW-1) – Rate Year Revenue Requirement
2. Exhibit__ (GRW-2) – Earnings Base Capitalization Adjustment
3. Exhibit__ (GRW-3) – Rate Year Uncollectible Calculation

Q. Please explain your adjustments to rate base.

A. Adjustments are shown in the revenue requirement calculation on Exhibit__ (GRW-1), Page 7.

RATE BASE

EARNINGS BASE/CAPITALIZATION ADJUSTMENT (EB/CAP)

Q. Please explain Exhibit__ (GRW-2), that contains six pages and reduces the company's EB/CAP adjustment of $50,648,000 by $35,549,000 to $15,099,000.

A. In Pages 2-4 of my Exhibit__ (GRW-2), the first column on each page shows the company calculation of the EB/CAP, Exhibit__ (RLT-5), Sch 10, Sheets, 1-3. My adjustments are shown in the next five columns on those sheets to arrive at an adjusted New York Capital level of $669,555,000 (page 4). The Earnings Base comparison to New York Capital is made on Page 1.

Q. Please summarize briefly your adjustments to arrive at your EB/CAP adjustment of $35,549,000.

A. My adjustment consists of four parts:

1. $10,986,000 Capital Allocation Correction
2. 5,797,000 Include Certain Debt Net of Tax
3. 5,104,000 Other Miscellaneous
4. 13,662,000 Correct Earnings Base per Exhibit__ (RLT- 5), Sch 1.

The first three adjustments decrease the NY allocated capital by 21,887,000 and adjustment 4 increases earnings base by $13,662,000.

CAPITAL ALLOCATION CORRECTION

Q. Please explain your adjustment of $10,986,000.

A. The company has proposed a novel approach to the allocation of capital. Under the company's proposal the company would allocate to the New York Division certain items of capitalization that "can be directly tied to the New York Division, created by direct involvement of the New York Public Service Commission"(Witness Truitt, page 44, lines 15-17). These items are Refund Pool, Gas Supplier Case Refunds, Over (Under Collection of Gas Costs, Internal Pension Reserve, Internal OPEB Reserve, Provision for Refund and Cap/Rel/OSS/SC11 85%. The calculation of this refinement is shown on Exhibit__ (RLT-5), Schedule 10, Sheet 3.

Q. Do you agree with this refinement?

A. For purposes of this proceeding I agree with the direct allocation of these items. A case could be made that NY capital items can be handled in a similar manner as Deferred Income Taxes-ADR, ACRS and Investment Tax Credits. That is, even though it is impossible to track the flow of money to a specific Distribution Division, the level of deferred taxes for each division of the Distribution can be measured.

Q. Do you agree with NFG's methodology for incorporating these NY items in the allocation of capital?

A. No. The company's method produces an unreasonable allocation of capital to the New York Division of the

Distribution.

Q. Please explain.

A. The calculation of the EB/CAP requires two steps;(1) the allocation of capital between the New York & Pennsylvania divisions of the Distribution Corporation and (2) a comparison of that allocated New York capital to the New York Division earning's base. Step 1 is necessary because financings of capital are made by the Parent, who transfers the proceeds to the total Distribution Company. Allocations of these Financings (capital) are not made to specific divisions. Since it is possible, however, to determine the level of assets in each division, we use that relationship to allocate capital.

Q. Please explain how the company allocated capital between the two divisions.

A. The company's methodology is shown on Exhibit__ (RLT-5), Schedule 10. The company's first step is to reduce total capitalization of $952,652,000 by $17,513,000 to eliminate New York & Pennsylvania direct capital. This results in an adjusted capitalization of $935,139,000.

Q. Once the level of capitalization is determined. What is the next step?

A The next step is to calculate the New York Earnings Base as a percentage of total distribution earnings base - 71.50%.

This is necessary so the capital can be allocated to the two divisions. The company multiplies the 71.50%, by the company adjusted capitalization of $935,139,000 to arrive at a New York capital level of $668,624,000. Finally, an additional $22,818,000 (New York items) is added to the New York capitalization for a total of $691,442,000.

Q. What is wrong with the company methodology?

A. Exhibit__ (GRW-2), Page 4, shows the company's calculation. The company assumes all earnings base assets are financed by the adjusted capitalization (capital net of direct capital. As shown on page 6, for each dollar of earnings base asset in both Pennsylvania and New York a $1.04 of capital is required. Then the company adds $22,818,000 to New York capitalization and reduces the Pennsylvania capitalization by $5,305,000. The company claims this $22,818,000 is financing NY assets but does not demonstrate how. What results is a disproportionate allocation of capital to New York of $1.08 compared to $1.02 to Pennsylvania, Exhibit__ (GRW-2), Page 5. It is unclear how the company can make a claim that it requires more financing per earnings base dollar in New York than Pennsylvania.

Q. Please explain your proposal for the New York only items.

A. I propose that the New York Only Items be treated in the same manner as Deferred ADR-ACRS and Investment Tax Credits. Therefore, I first reduce the earnings bases of the total Distribution by $17,513,000 (Exhibit__ (GRW-2), Page 2 and New York by $22,818,000, Exhibit__ (GRW-2), Page 3) for the identifiable items. By reducing the two bases, the identifiable capital of each Division is assumed to finance a corresponding level of earnings base in each division. Secondly, I calculate a percentage of New York to total Distribution of 70.33% using the reduced earnings bases, Exhibit__ (GRW-2), page 4. Thirdly, I multiply the capital reduced for the directly identifiable capital (remaining capital) by the 70.33% (remaining earnings base assets requiring capital). This results in a fair allocation of capital to the two divisions (See Exhibit__ (GRW-2), Page 5, of $1.06 for both Pennsylvania and New York.

INCLUDE CERTAIN DEBT NET OF TAX

Q. Please explain part 2 of your adjustment to earnings base of $5,797,000.

A. This adjustment includes adjustments to Refund Pool, Internal Pension Reserve, Internal OPEBs Reserve and Provision for Refund to show the averages net of tax. The company has agreed that the four items should be reflected in the EB/CAP adjustment net of tax (DPS-16). I show the adjustments on Exhibit__(GRW-2), pages 2-4.

OTHER MISCELLANEOUS

The other miscellaneous adjustment consists of two parts; (1) $3,593,000 (rate base impact) for non-capital Account 229.003 and (2) $1,512,000 (rate base impact) for Deferred Taxes – Restricted Stock & SARs.

The calculation is shown on Exhibit__ (GRW-2), page 6.

Q. Please explain part one of your adjustments.

A. The company included the average balance for Account 229.003 – Estimated Provision for refunds, for the period March 2003 through March 2004 as capitalization, even though the company did not accrue interest nor was required to accrue interest on this account balance until October 2003 per the settlement agreement. Therefore, I have included the balances for the period October 2003 through March 2004,only. This treatment is similar to the treatment of over/under collection of gas costs. During the open cycle - no interest is accrued and not included in the capitalization, until the cycle is closed. When the cycle is closed it is included in capitalization.

Q Please explain part two.

A. Part two eliminates the balances for account 283.100

deferred taxes for Product 3040 Restricted Stock and 3041 NQSO/SARs since the cost will be offset by productivity.

CORRECT EARNINGS BASE

Q. Please explain your adjustment 4 of $13,662,000.

A. My adjustment is to increase by $13,662,000 the company's claimed earnings base of $640,794,000 to $654,456,000 in order to properly calculate the EB/CAP adjustment.

Q. How did the company calculate its earnings base.

A. The company claims the earnings base in this proceeding is the $640,794,000 shown on Exhibit__ (RLT-5), Schedule 10, Sheet 2 of 3 – New York Division Earnings Base. Although the page claims to calculate the average earnings base, the term earnings base in their presentation is a misnomer. It is a base for allocating capital between the two divisions and not the proper base for calculating the EB/CAP adjustment.

Q. Please continue.

A. The proper calculation of historic earnings base for the EB/CAP adjustment is historic rate base plus interest bearing CWIP. The following statement from Opinion 75-4, page 4, confirms this calculation:

"The rate base, plus construction work in progress, should not exceed the capitalization. If, as in this case, the amount exceeds capitalization and the company actually earns the allowed rate of return on rate base, it will be earning considerably more on its capitalization - more than required to service its debt obligations and to provide a fair return to its investors."

Q. Please explain your calculation of earnings base.

A. My calculation of earnings base can be found on Exhibit__(GRW-2), page 1. I begin with the rate base found on Exhibit__ (RLT-5) of $699,754,000 for the historic year. Subtracting out the company's EB/CAP adjustment of $50,648,000 leaves a rate base of $649,106,000. I then add to the rate base interest bearing CWIP of $5,350,000 to derive an earnings base of $654,456,000. Comparing this base against the New York allocated capital of $669,555,000 results in EB/CAP adjustment of $15,099,000.

Eliminate Prepaid Pension or Debit Balance from Rate Base

Q. Please explain your adjustment (c) to rate base on Exhibit__ (GRW-1), Page 7.

A. Adjustment (c) eliminates $19,290,000 from the rate year rate base. Instead I recommend that the company accrue interest on the actual net of tax prepaid balance at the short term capital rate.

Q. Please explain why there is a prepaid pension.

A. According to Mr. Bauer (DPS-15), "Because of the nature of income tax regulations, the New York Division historically has been unable to fund the full amount of its non-union OPEB rate recovery. Consequently, the New York Division's OPEB reserve has grown subsequently. Because it can borrow funds at a rate much lower than the internal reserve's interest rate, Distribution has sought to maximize its non-union OPEB funding contributions (and thus minimize the size of the OPEB internal reserve). One method Distribution has employed is the use of a 401(h) account, which is another vehicle for funding post-retirement benefits. Under the tax law, 401(h) contributions, which are made simultaneously with normal pension contributions, are generally calculated as 25% of the normal pension contributions. In order to maximize the benefit of the 401(h) contributions, the New York Division has accelerated the funding of its normal pension contributions. By funding the pension earlier in the year, the New York Division in turn also accelerates the funding of the 401(h) accounts. The effect of funding the 401(h) accounts is a reduction of the OPEB internal reserve balance, which in turn, results in lower annual interest expense."

Q. Please explain why rate base treatment for the prepaid balance is not appropriate.

A. There are three reasons. First, the ratepayer is providing a return to the company at the overall rate of return. Mr. Bauer claims that the company can borrow at a much lower rate. Secondly, the company would have to earn a higher return on the prepaid balance in the external fund than the cost to the ratepayer (rate of return) for ratepayers to benefit. For the last ten years the external reserve earned an average of a little over 5% (DPS-100). Finally, rate base estimates of the prepaid pension balance can lead to gaming and unfair gains which is clearly in opposition of the intent of the Policy Statement - Case 91-M-0890 where full deferral of rate allowance variations is required.

Q. Please explain your recommendation concerning the accrual rate based on the short term debt rate, for the prepaid pension balance.

A. Since only the New York Division of Distribution is making prepayments, New York ratepayers should receive a benefit by paying the short term cost rate on the balance.

OPERATING REVENUES

AMORTIZATION OF CUSTOMER REFUNDS

Q. Please explain your adjustment (2), Exhibit__ (GRW-1), Page

1 to increase revenues by $6,010,000.

A. I recommend that the balance in Account 229.003–Estimated Refund Provision Case 00-G-1858 ($12,020,000) be amortized over two years. The $12,020,000 is ratepayers' share (50%) of equity earnings in excess of 11.5% for the three years ended September 30, 2004 (Case 00-G-1495). In light of the anticipated substantial increases in the cost of natural gas, it would be beneficial to mitigate these costs as soon as possible with monies owed to customers.

Q. Do you have any further recommendations?

A. When the final level of earnings sharing is determined for the three years ending September 30, 2003, any differences from the amortization and the actual should be charged or credited to the Cost Mitigation Reserve (CMR).

OPERATION AND MAINTENANCE EXPENSE

Uncollectible Expense

Q. Please explain your adjustment (7), Exhibit__ (GRW-1), Page 1), of $9,760,989 to uncollectible expense.

A. My adjustment reduces the company's request of $22,572,507 by $9,760,989 to $12,811,518 and consists of two parts:

1. Reduce the company's projected net write-offs applicable to the rate year of $13,828,546 by $1,017,028 to

$12,811,518.

2. Eliminate the additional expected accrual to be made in the rate year of $8,743,507.

Q. Please explain your first adjustment of $1,017,028.

A. My adjustment corrects for two computational errors in the formula and eliminates the Company's modification to the long established formula. NFG's proposes to include as the rate year uncollectible expense the level of estimated rate year write-offs. My calculation of rate year uncollectible Expense is shown on Exhibit__ (GRW-3).

Q. Please explain the company's errors in the formula.

A. The company claims that only sales tax (3.63%), Exhibit__ (KAF-1), Schedule 1, line 35, should be eliminated from the past due final. I disagree, and have eliminated on line 17, Exhibit__ (GRW-3), all recoverable taxes, including gross receipt taxes billed to these non-paying customers to arrive at 6.82%.

Q. Please explain why this adjustment is necessary.

A. Line 16, Exhibit__ (GRW-3), - Past due final bills includes sales tax and gross receipt tax surcharge billed to customers. The company is an agent for the various taxing authorities but is not liable to pay these taxes if not collected. Therefore, it is necessary to eliminate these dollars from the past due finals or the uncollectible expense allowance will be overstated.

Q. Have the revenues collected from customers from the current gross receipt tax surcharge been higher than the actual expense (gross receipt tax & State Income Tax) charged the company?

A. Yes, for years 2001 through 2003. Until base rates are changed, the company will continue to charge the customer at the pre 2000 revenue tax receipt rate. However, any over or under collections are being passed back or billed to customers.

Q. Is an annual reconciliation of collected revenue tax receipts to the actual expense done?

A. An annual reconciliation is made (Commission Order Case 00-M-1556) by comparing total gross receipts taxes collected to the actual expense, the difference is passed back or billed to customers. Since, this true-up compares collected revenues, not billed, to actual expense, any non collected gross receipt revenues are reduced from billed revenues so only collected revenues are included. Therefore, none of the revenue taxes billed but not collected impacts the uncollectible calculation.

Q. Please summarize.

A. It is important to exclude all revenue taxes included in the formula's past due finals since those taxes are neither a liability if owed to a taxing jurisdiction or a loss to the company in the annual true-up calculation.

Q. Please explain part 2 of your adjustment to the uncollectible expense formula, Exhibit__ (GRW-3).

A. Part 2 of my adjustment is to calculate recovery of amounts previously written off (Line 19). The company calculates a 25.02% factor that is based on the relationship of recoveries to gross write-offs (which includes all taxes). Consistent with this historic relationship I have applied that 25.02% to line 16. This is consistent with the Commission Decision in Case 94-G-0885.

Q. Please explain your opposition to the company's modification to the formula.

A. The formula had been developed over a number of years with former NFG employees Tom Ring and Gerald Wehrlin. The company's proposed modification to that methodology is not appropriate. The purpose of the formula is to estimate the level of rate year revenues that will not be collected from customers. This is achieved primarily by taking a known level of non-paying customers (at September 30, 2004) adjusting for gas costs and other historic information (revenue taxes, write-offs of non paying, recoveries) to arrive at an uncollectible expense level in the rate year.

Q. Continue.

A. Under the company's proposal the rate year uncollectible expense will be the same as the rate year net write-offs. However, there is no connection between rate year revenues and rate year net write offs. Net write-offs occur approximately a year after the related revenues have been booked. Therefore the write-offs taken in the rate year are for revenues booked in the previous year.

Q. Please explain your adjustment of $8,743,507.

A. This adjustment reduces the company's request for an additional rate year uncollectible expense accrual of $8,743,507. The company proposed to recover a short fall that results from prior years bookings of uncollectible expense being lower than actual experience. This results in a true-up of prior period uncollectible expense.

Q. Please explain the company's uncollectible reserve accounting.

A. Under Generally Accepted Accounting Principles (GAAP), the company books revenues and correspondingly, is required to book an estimated expense for non collection (uncollectible expense) of a portion of those revenues. The company chose to book an uncollectible expense amount using an old rate case allowance, even though that allowance was not mandated by the Commission nor does it represent a realistic level of actual uncollectible experience. Ideally, the actual amount of uncollectible booked expense will equal the actual level of non collection. However at NFG it takes approximately a year from the book recognition of revenues until the company knows how much of those revenues are not collected (written off). In order to accommodate the lag the company uses a reserve accounting technique where the expense levels are set aside, into a reserve. When the amounts are known and written off, the reserve is reduced. At any point of time there should be enough in the reserve to offset the estimated write-offs to be made in the next twelve months. When the expensed amount is less then the actual experience level, a problem arises. This is the case here.

Q. How could the company have avoided this problem?

A. The company should have booked higher additional uncollectible expense in previous years. The company reviews the levels of past due finals (non - paying customers) and the level of the uncollectible reserve. Based on past collection of past due finals and historic levels of the uncollectible reserve the company should have concluded that the expense level was insufficient and higher levels of uncollectible expense were needed. This would be consistent with matching the expense with the related revenue.

Q. Why is it not appropriate to allow a recovery of $8,743,507 in the rate year?

A. The 8,743,507 occurs as a result of the company's shortfall in expense accruals in periods prior to the rate year. The company should be allowed an uncollectible expense of only $12,811,518 for the twelve months ended July 31, 2006 or an amount to compensate them for non-collection of rate year revenues. This is consistent with the Commission's "Statement of Policy on Test Periods in Major Rate Proceedings", Issued November 23, 1977, where the Commission makes clear that "To avoid…waste of valuable rate case time…we conclude that we must set a clear, specific policy on test years, designed to enhance our ability to set rates properly for the future. And we find that our deliberations will be served best by a rate case filing consisting of: (1) operating results, with normalizing adjustments, for a 12-month period expiring at the end of a calendar quarter no earlier in time than 150 days before the date of filing and (2) the projected results from the new 12-month rate period…The presentation must include a verifiable link between the two periods."

Q. The company would "prefer not to lock in the uncollectible expense dollar amount"(Witness Frank, page 12, lines 3 and 4) but proposes an uncollectible tracker. Do you agree with this proposal?

A No. The company's proposal is premised on the level of the uncollectible reserve. Since I have rejected the company's proposal for an additional $8,743,507 accrual, the reserve would already be deficient by $6,778,806 ($8,743,507 times 80%). As I have testified, the deficiency is a result of insufficient accruals in uncollectible expense in periods prior to the rate year. This proposal must be rejected.

Other Expense

Q. Please explain your adjustment (3), Exhibit__ (GRW-1), Page 4 of $806,000 to Other Expense.

A. My adjustment contains two parts: Part (1) is to reduce expense by $362,000 for National Fuel Gas Partnership for DG program costs since the additional cost will be offset by an incremental increase in consumption & revenues (DPS-101). Part (2) is to reduce other expense and increase uncollectible expense by $444,000 to include this amount in the proper cost element.

PROPERTY TAXES

Q. Please explain your adjustment (15), Exhibit__ (GRW-1), Page 2, to Property Taxes.

A. Adjustment (15) reduces expense by $1,299,000. This adjustment is to increase the latest known property taxes of $27,585,000 for the twelve months ended September 30, 2004 by a .76% annual increase. The .76% is an average of five year annual changes in property tax increases/decreases.

Q. Why is this proper?

A. This method is consistent with the one adopted by the Commission in Case 94-G-0885, Opinion 95-16. In that case the Company asserts that "The Commission has often used five-year averages to estimate categories, like property taxes suffering from year-to-year distortions." (Opinion 95-16 page 32). Clearly that's the case here where over the last five year period increases/(decreases) ranged from (3.79%) to 3.34%.

FEDERAL INCOME TAX IMPACT OF THE MEDICARE PRESCRIPTION DRUG, IMPROVEMENT ACT of 2003

Q. Please explain your understanding of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (Act).

A. Starting in 2006, the Act provides a subsidy from federal government to the employer for qualified prescription drug plan costs between $250 and $5,000 for each participant. This subsidy is considered an actuarial gain and will reduce future OPEB expense. In addition, for Federal Income Tax purposes the subsidy received from the Federal Government is non taxable and not netted against the employers prescription drug costs in calculating expense deduction.

Q. What is the company's position concerning the impacts of this Act.

A. DPS-193, states that "The company has deferred the full impact on FAS 106 (OPEB) expense of implementing FSP 106-2. The entries to defer the initial impact were previously provided to Staff (they are referred to in DPS-191). The ongoing impact of the Medicare subsidy will be reflected in Mercer's annual FAS 106 expense calculations, which in turn will be reflected in the normal FAS 106 deferral calculations recorded by the Company in accordance with the Commission's Policy Statement on such costs. Though the Company has not yet fully evaluated the impact of FSP 106-2 on deferred income tax expense, it intents to follow the Commission's Statement of Policy and Order Concerning the Accounting and Ratemaking Treatment for Pensions and Postretirement Benefits Other Than Pensions."

Q. Do you agree with the company recommendations?

A. Yes. However, I have two concerns and recommendations : 1. Concerning the deferred taxes, It is not clear how the deferred Federal Income Tax that results from the non taxable subsidy is included in the calculation of FAS 106 expense. I recommend that the company use these taxes, if they are not already doing so, to reduce future OPEB expense. The company should also demonstrate the impact of these taxes on FAS 106 calculation.

2. The company claims they will follow the Commission Policy Statement for the deferred taxes. I assume the company intends to deposit these balances and the subsidy into the internal or external reserve. If not, they should be required to do so.

RETENTION FACTOR

Q. Do you agree with the company's calculation of the uncollectible retention factor?

A. No. The company's calculates, Exhibit__ (RLT-1,), Workpapers, Sheet 7, the uncollectible retention factor by dividing their uncollectible expense $22,573,000 by residential revenues $662,662,496 only, Exhibit__ (RLT-2), Sheet 1. The company is claiming that only residential and not transportation customers are a source of uncollectible expense. Yet in their claim for additional uncollectible expense in their revenue requirement, they apply the retention factor against the entire rate increase, which includes an increase to transportation customers.

Q. What do you recommend?

A. Since the uncollectible retention factor is applied to the entire rate increase (including transportation), the calculation of the retention factor should also include transportation revenues (Exhibit__ (GRW-1), Page 8). This is consistent with past Commission orders.

STATE INCOME EXPENSE

Q. Please explain your recommendation concerning State Income Taxes.

A. Since State income tax expense will be included in base rates, I recommend that the company be ordered to provide a reconciliation of actual SIT expense to the booked expense from Calendar 2000 until rates go into effect in this proceeding.

Q. Does this conclude your testimony?

A. Yes, it does.

Barcelona CIS Project Cost Correction

	Staff Model	Corrected Amount	Difference
Total Barcelona Project	$59,311,000	$60,000,000	$689,000
NYD Allocated %	71%	71%	-
Total Allocated NY Distribution	$42,110,810	$42,600,000	$489,190

Average Net Plant with Barcelona Correction (In 000s)

	Staff Model	Corrected Amount	Difference
Average Net Plant at March 31, 2018	$ 1,486,336	$ 1,486,825	$ 489
Average Reserve at March 31, 2018	$ 584,078	$ 584,102	$ 24
Average Net Plant (Plant minus Reserve)	$ 902,258	$ 902,723	$ 465
Noninterest Bearing Construction Work in Progress	211	211	$ -
Total Average Net Plant at March 31, 2018	$ 902,469	$ 902,934	$ 465