

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

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

**REDACTED**

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

**FEBRUARY 27, 2004**

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**I. Introduction**

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

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

**Q. HAVE YOU PREVIOUSLY PRESENTED TESTIMONY IN THIS PROCEEDING?**

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

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

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

**Q. HOW IS YOUR REBUTTAL ORGANIZED?**

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

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**II. Witness: Russell A. Feingold**

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

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

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

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

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

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

46 A. Yes. In a Mountain States Telephone and Telegraph Company proceeding at Docket No.  
47 88-049-18, the Public Service Commission of Utah upheld this position. Relevant  
48 portions of the Utah Commission's order in that proceeding are as follows, and justify  
49 retroactive ratemaking as appropriate under the circumstance present in this proceeding:  
50

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

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

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

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

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

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

97 As stated by the Court:

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

103 A complete copy of the Utah Commission's Order is attached to my testimony as  
104 GCI Exhibit 15.0.

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

108                   **IN THIS PROCEEDING. WHAT SHOULD BE THE COMMISSION’S**  
109                   **FOCUS IN THIS PROCEEDING?**

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

118    **Q.                    WITNESS FEINGOLD CLAIMS YOU HAVE IGNORED THE FACT**  
119                    **THAT THE COMPANY WAS THE LOWEST COST PROVIDER OF**  
120                    **NATURAL GAS IN ILLINOIS DURING THE GCPP (LINES 65-68, 160-**  
121                    **163, AND 623-632). WHAT IS YOUR RESPONSE?**

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

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

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

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

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

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

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

177 addition, as explained in the document included at Tab A-12 of Appendix A to my direct  
178 testimony, x  
179 x  
180 x x x x. These strategies were not abandoned, but in fact, pursued by the Company  
181 despite the unprecedented market conditions. Witness Feingold’s suggestion that had  
182 Nicor proposed strategies in the Docket No. 99-0127, it was somehow obligated to  
183 pursue each of those strategies, is wrong. There was no such requirement.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

297 A. No. In 2000, Nicor liquidated 17,501,960 Dth of LIFO inventory. In 2001, Nicor added  
298 2,025,097 Dth to its LIFO inventory. In 2002, Nicor liquidated 9,991,370 Dth of LIFO  
299 inventory. Thus, over the 3-year period, the net liquidation of LIFO inventory was  
300 25,468,232 Dth (17,501,960 minus 2,025,097 plus 9,991,370). As shown on GCI Exhibit  
301 4.0 on Rehearing, my adjustment to GCPP savings for the low-cost LIFO benefit is based  
302 on the liquidation of 25,468,232 Dth. Thus, I have not ignored the LIFO layer  
303 established in 2001. I have simply netted the layer established in 2001 with the layer  
304 liquidated in 2002. This is consistent with the fact that the LIFO layer established in  
305 2001 was liquidated in 2002. I would also note that the method I used to determine the  
306 LIFO benefit is consistent to that which had been used by the Company in its bucket  
307 reports. x  
308 x This is shown on  
309 the document included in Appendix A-6, NIC 4518 of my direct testimony.

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





358 volumes of 7,265,000.<sup>1</sup> If these two adjustments are adopted by the Commission, Nicor's  
359 2001 storage withdrawal quantity under the GCPP will increase by the proposed  
360 amounts. Thus, the adjustment to the 2001 storage withdrawal quantity would be  
361 reduced. Page 2 of GCI Exhibit 18.0 reflects an adjustment to gas costs assuming my  
362 adjustment for in-field transfers is adopted by the Commission. That is, it reflects  
363 withdrawals of 66,348,000 Dth (54,289,000 plus 12,059,000) from storage in 2001. This  
364 is the 2001 storage withdrawal quantity reflected in my direct testimony. As shown on  
365 page 2, the impact on Nicor's gas costs is \$134.2 million. Since ratepayers pay Nicor's  
366 actual gas costs under the GCPP, the full \$134.2 million would be refunded to ratepayers.

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

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

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

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

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

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

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

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

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

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

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

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

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

426 **WHAT IS YOUR RESPONSE?**

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

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

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

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



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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

590    A.    Yes. I have never been in a proceeding where all of the parties have presented identical  
591            issues and adjustments. Neither has witness Feingold. The purpose of this proceeding is  
592            to ferret out the claims of the various parties. It is not unreasonable or uncommon for  
593            experts to have differences of opinion.  
594

594

**III. Witness: Michael E. Barrett**

595

**Q. IS THERE A RECURRING THEME TO WITNESS BARRETT'S**

596

**TESTIMONY THAT MERITS COMMENT?**

597

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

604

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

617

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

730 **WHAT IS YOUR RESPONSE?**

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

736 [REDACTED]

737 [REDACTED]

738 [REDACTED]

739 [REDACTED]

740 [REDACTED]

741 [REDACTED]

742 [REDACTED]

743 [REDACTED]

744 [REDACTED]



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

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

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

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

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

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

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

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

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

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

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

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

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

868  
869  
870



902 [REDACTED]  
903 [REDACTED]  
904 [REDACTED]  
905 [REDACTED]  
906 x [REDACTED]  
907 x  
908 [REDACTED]  
909 x [REDACTED]  
910 [REDACTED]  
911 [REDACTED]  
912 [REDACTED]  
913 x [REDACTED]  
914 x  
915 [REDACTED]  
916 x [REDACTED]  
917 [REDACTED]  
918 x [REDACTED]  
919 [REDACTED]  
920 [REDACTED]  
921 [REDACTED]  
922 x [REDACTED]  
923 [REDACTED]

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

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

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

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

939 [REDACTED]

940 [REDACTED]

941 [REDACTED]

942 [REDACTED]

943 [REDACTED]

944 [REDACTED]

945 [REDACTED]

946 [REDACTED]

947 [REDACTED]

948 [REDACTED]

949 [REDACTED]

950 [REDACTED]

951 [REDACTED]

952 [REDACTED]

953 [REDACTED]

954 [REDACTED]

955 [REDACTED]

956 [REDACTED]

957 [REDACTED]

958 [REDACTED]

959 [REDACTED]

960 [REDACTED]

961 [REDACTED]





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

**VI. Other**

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

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

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

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

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

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

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

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

1093 A. Yes, it does.

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