

**STATE OF ILLINOIS**  
**ILLINOIS COMMERCE COMMISSION**

NORTH SHORE GAS COMPANY	:	
	:	
Proposed General Increase	:	No. 07-_____
In Rates for Gas Service	:	

Direct Testimony of

**THOMAS E. ZACK**

Vice President – Gas Supply  
Integrus Energy Group, Inc.

On Behalf of  
North Shore Gas Company

March 9, 2007

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1 **I. INTRODUCTION AND BACKGROUND**

2 **A. Witness Introduction**

3 Q. Please state your name and business address.

4 A. Thomas E. Zack, 130 East Randolph Drive, Chicago, Illinois 60601.

5 Q. By whom are you employed?

6 A. The Peoples Gas Light and Coke Company (“Peoples Gas”)

7 Q. What position do you hold with Peoples Gas?

8 A. I am Vice President, Gas Supply of the Integrys Gas Group.

9 Q. What are your responsibilities in that position?

10 A. I am responsible for the overall direction, management and leadership of the Gas  
11 Supply, Gas Storage and Gas Control areas for the Integrys Energy Group, Inc.  
12 gas utilities, which include Peoples Gas and North Shore Gas Company (“North  
13 Shore Gas” or the “Company”).

14 **B. Purpose of Testimony**

15 Q. What is the purpose of your testimony?

16 A. The purpose of my testimony is to describe the changes the Company is  
17 proposing to its transportation tariffs. First, my testimony will describe the  
18 Company’s current transportation program. Second, my testimony will describe  
19 the changes being proposed to the Company’s’ transportation programs, including  
20 the expansion of Rider SVT, elimination of Rider FST, changes to Rider SST, the  
21 merging of Rider LST into SST, revisions to Rider P and elimination of Rider TB.

22 I will discuss in some detail why the transportation services the Company

23 provides must reflect the assets in place to support them and the costs of those  
24 assets. Included in that discussion is a proposed revision to the Diversity Factor  
25 applied to the rates of transportation customers and transportation related charges  
26 which have been developed from cost studies.

27 Q. What are the Company's overall objectives in this case with respect to  
28 transportation service?

29 A. The Company's overall objectives include the following:

- 30 • Continuing to provide all customers the opportunity to select an alternative  
31 natural gas supplier.
- 32 • Enhancing the transportation services available to customers and  
33 suppliers.
- 34 • Ensuring that the decision by some customers to choose an alternative  
35 natural gas supplier does not harm the Company's remaining retail sales  
36 customers.
- 37 • Ensuring that transportation customers, who currently represent about  
38 33% of annual throughput, receive all of the services for which they are  
39 paying and pay for all of the services they receive.

40 Q. What do you mean when you use the term "Transportation Tariff"?

41 A. When I use the term "Transportation Tariff," I am referring to that portion of the  
42 Company's current Schedule of Rates for Gas Service (Ill.C.C.No. 16) that  
43 consists of Riders SVT, AGG, FST, SST, LST, P and TB. The Transportation  
44 Tariff and the matters pertaining to it comprise the Company's transportation  
45 program.

46 **C. Summary of Testimony**

47 Q. Please summarize the conclusions of your direct testimony.

48 A. In brief, the conclusions of my direct testimony are that North Shore Gas'  
49 transportation program needs to be changed in the following respects:

50 (1) The storage and standby rights of the transportation customers  
51 need to be shaped to be consistent with the capabilities of North Shore Gas' gas  
52 supply portfolio, and the Company needs to have an annual mechanism to adjust  
53 those rights as its gas supply portfolio changes.

54 (2) The Company's tariff must establish provisions that insure that  
55 transportation customers and their suppliers manage the supplies and services they  
56 have elected in a way that complies with North Shore Gas' intrinsic daily and  
57 seasonal operational limitations.

58 (3) The Company's tariff should eliminate any cross-subsidies that  
59 exist.

60 (4) The Company should eliminate any unnecessary provisions in its  
61 transportation tariff.

62 (5) The Company's tariff should be revised to reflect changes in the  
63 natural gas market that have occurred since the Company's current transportation  
64 program was established.

65 (6) The Company's transportation program needs to be modified to  
66 reflect customer and supplier suggestions that are acceptable to the Company.

67 (7) The Company needs to revise its transportation tariff to encourage  
68 growth in the number and throughput of transportation customers without  
69 adversely affecting retail gas sales customers or the reliability of the Company's  
70 services to all customers.

71 **D. Exhibits to Direct Testimony**

72 Q. Are you sponsoring any attachments to your direct testimony?

73 A. Yes. I am the sponsor of North Shore Gas Ex. Nos. TZ 1.1 through TZ 1.17.

74 Q. Were Ex. Nos. TZ 1.1 through TZ 1.17 prepared by you or under your supervision  
75 and direction?

76 A. Yes, they were.

77 **E. Background and Experience**

78 Q. Please summarize your educational background and experience.

79 A. In 1983, I received my Bachelor of Arts degree, with majors in Accounting and  
80 Business Administration, from St. Ambrose University in Davenport, Iowa. In  
81 1986, I received a Masters of Business Administration, with a concentration in  
82 Finance, from DePaul University.

83 I began my employment with North Shore Gas in 1984 in the Auditing  
84 Department. In 1986, I transferred to the Financial Reporting Department. In  
85 1988, I transferred to the Rate Research and Policy Department. Four years later I  
86 transferred to the Office of Corporate Planning. In November 1996, I transferred  
87 to the Rates Department as a Supervisor. In September 1997, I was promoted to  
88 Manager of the Rates Department. In October 2000, I was promoted to Director,  
89 Customer Relations. In March 2003, I transferred to the position of Director, Gas  
90 Supply. In February 2007, I became Vice President of Gas Supply for the  
91 Integrys Energy Group.

92 **II. CURRENT TRANSPORTATION PROGRAMS**

93 Q. Please provide a brief overview of the transportation program.

94 A. The Company first made transportation available to large volume customers in the  
95 mid-1980s. The current Riders that set forth the detail of transportation service  
96 were largely put in place in the Company's last rate case in Docket No. 95-0031.  
97 Currently, about 2,500 (19%) General Service customers and all Large Volume  
98 Demand customers use these transportation services.

99 Q. Please continue.

100 A. The Company currently offers a small volume program and a large volume  
101 program. The small volume program is set forth in Riders SVT and AGG. Rider  
102 SVT defines the customer's service and Rider AGG defines the aggregation  
103 service that the supplier purchases. The Company introduced Riders SVT and  
104 AGG in 2002, for all Small Residential Service customers and for small volume  
105 General Service customers. Improvements to the program have been put into  
106 place since its inception and, as a result, Rider SVT customers have grown to  
107 make up the majority of the Company's transportation accounts.

108 Q. Please explain the large volume transportation programs.

109 A. The Company's large volume programs are set forth in Riders FST, SST, LST,  
110 TB and P. Riders FST, SST and LST define the customer's service. Rider FST is  
111 a full standby service that is available to all customers, except those served under  
112 S.C. No. 1 (Small Residential). Rider SST is a partial standby service that is  
113 available to S.C. No. 2 (General Service) customers. Rider LST is a partial  
114 standby service that is very similar to Rider SST, but it is available to S.C. No. 3

115 (Large Volume Demand Service) customers. The S.C. No. 3 customers have fully  
 116 unbundled base rates and Rider LST reflects this rate design. Rider TB is the  
 117 required balancing service used by Rider LST customers who elect 0% standby  
 118 service. Finally, Rider P is similar to Rider AGG in that it is the aggregation or  
 119 pooling service that the supplier purchases. Below is a table illustrating which  
 120 transportation riders are currently available to each service classification.

Service Classification	Applicable Transportation Riders
1 – Small Residential	SVT, AGG
2 – General Service	SVT, AGG, FST, SST, P
3 – Large Volume Demand Service	FST, LST, TB, P

121 Q. You stated that the Company has modified its transportation program to  
 122 accommodate customer and supplier suggestions. Please explain.

123 A. As an ongoing matter, the Company receives feedback from customers and  
 124 suppliers in its day-to-day administration of the transportation program.  
 125 Additionally, prior to filing this rate case, Company personnel met with various  
 126 suppliers to obtain valuable feedback concerning the operation of the  
 127 transportation program. Furthermore, in the merger proceeding, Docket No. 06-  
 128 0540, the Company agreed to a number of Conditions of Approval. North Shore  
 129 Gas witness Mr. Borgard (North Shore Ex. LTB-1.0) testifies more fully as to  
 130 North Shore Gas' compliance with all of the Conditions of Approval. However, I  
 131 will briefly describe the Conditions of Approval that pertain to the transportation  
 132 programs. Under Condition 34, the Company agreed to revise certain tariff  
 133 provisions and to make the filings within 90 days of the order. Since these filings

134 affect the proposals made in this filing, they are discussed in my testimony.  
135 Under Condition 35, the Company agreed to make certain proposals in its  
136 upcoming rate filing, and those proposals are also discussed below. Under  
137 Condition 36 the Company agreed to meet with stakeholders to discuss certain  
138 issues. Those meetings were held.

139 **III. CHANGES SINCE THE LAST RATE CASE**

140 Q. What changes have occurred since the Company's last rate case that impact gas  
141 supply and transportation?

142 A. It has been over 11 years since the Company's last rate case and much has  
143 changed since then, including:

- 144 • The Company created Riders SVT and AGG, the Riders associated with  
145 the Choices For You<sup>sm</sup> small volume transportation program.
- 146 • In 1992, the Federal Energy Regulatory Commission ("FERC") issued  
147 Order No. 636, which required pipelines to fully exit the citygate merchant  
148 function. Although this occurred before the Company's last rate case  
149 filing, at that time, the pipelines were still developing new services to  
150 respond to these changes. The services available to the Company today  
151 from these pipelines are not the same as they were in 1995. When  
152 pipelines eliminated their bundled citygate sales service, they greatly  
153 changed the array of services available to shippers and, in particular, the  
154 way in which pipelines offered no notice service changed. Today, none of  
155 the pipelines serving the Company offer storage services that allow  
156 injection quantities to equal the Company's maximum daily contract  
157 quantity.
- 158 • Order No. 636 also required pipelines to apply the Straight Fixed Variable  
159 ("SFV") rate design. All pipelines connected to the Company's system  
160 have adopted this rate design. As North Shore Gas witness Ms. Grace  
161 (North shore Ex. VG-1.0) explains, the SFV rate design places all fixed  
162 costs in a demand or reservation charge and only commodity costs,  
163 typically a fairly small portion of total pipeline costs, are in a variable,  
164 commodity charge.
- 165 • Subsequent to Order No. 636, the purchasing/selling of natural gas has  
166 evolved to include four nomination cycles available each day (two prior to

167 the flowing gas day and two within the gas day). During each of these  
168 nomination cycles shippers can change the amount of gas they schedule to  
169 be received or delivered. This contrasts significantly with the pre-Order  
170 No. 636 system. The old system only allowed for a single daily  
171 nomination deadline, which occurred the day before gas would flow. The  
172 old system also required the nomination for the first day of each new  
173 month three business days prior to the start of the month.

174 • Since 1996, four new or expanded interstate pipelines, have entered the  
175 Chicago market area.

176 • The gas marketing landscape has changed. There has been a consolidation  
177 of natural gas suppliers that operate in the Company's service territory,  
178 from over 100 active suppliers in the early 1990's to fewer than 30 active  
179 suppliers currently operating.

180 • The commodity cost of gas has risen dramatically. The gas bubble that  
181 was present during the last rate case no longer exists.

182 • The trading of NYMEX natural gas futures contracts has increased  
183 dramatically over the past decade, fueling the growth of large over-the-  
184 counter market for natural gas products and services. For example, a  
185 "basis" market, relating to price differentials at different locations on the  
186 interstate transportation grid has emerged. This basis market provides a  
187 degree of price transparency that can be used to value pipeline  
188 transportation. Gas is now actively traded in physical and financial  
189 markets and many financial products have been created that relate to the  
190 commodity and to its underlying transportation.

191 Q. Why are these changes important?

192 A. These changes affect all aspects of the services that the Company purchases to  
193 serve both its retail sales and its transportation customers. The changes also  
194 influence what is available to alternative retail gas suppliers seeking to sell gas to  
195 end use customers. In light of these industry changes, it is appropriate to review  
196 the Company's transportation programs.

197 **IV. ISSUES IN PROVIDING TRANSPORTATION SERVICE**

198 Q. Describe how transportation service operates on the Company's system.

199 A. If a customer elects transportation service under the existing transportation  
200 programs, gas is delivered to the city gate by a supplier. The Company receives  
201 this gas and is responsible for delivering gas to the customer's premises. Since a  
202 supplier cannot accurately predict exactly how much gas a customer will consume  
203 on any given day, the Company balances the overage or underage and accounts  
204 for these differences in the customer's Allowable Bank ("AB").

205 Q. Is balancing the only function of AB?

206 A. No. The AB has two distinct functions: a daily balancing function and a gas  
207 banking function. The daily balancing function allows the customer the flexibility  
208 required when deliveries to the Company do not exactly match the customer's  
209 demand. The gas banking function allows transportation customers to take  
210 advantage of seasonal price differences by delivering to the Company and  
211 placing into the AB, normally lower cost summer gas for later use in the winter  
212 months. On any day that a customer's gas deliveries exceed its consumption, that  
213 excess gas is, subject to the size of the bank, accounted for as an increase in the  
214 AB. When consumption exceeds deliveries, this banked quantity of gas is  
215 available for the customer's use.

216 Q. What costs are incurred by the Company in order to provide the balancing and gas  
217 banking functions of the AB?

218 A. The two functions of the AB service that I have described are provided through  
219 the utilization of the Company's entire gas supply portfolio. Included in the  
220 portfolio are purchased gas supplies, transportation capacity, and leased storage.  
221 All costs that are incurred in order to maintain the portfolio are relevant to the

222 AB. These costs include the fixed gas costs associated with (1) reserving gas  
223 supplies; (2) reserving pipeline capacity; (3) reserving rights from non-pipeline  
224 storage service providers; (4) reserving the rights to store, withdraw gas from and  
225 inject gas into leased storage services; and (5) the variable costs of withdrawing,  
226 injecting and transporting that gas into and out of storage.

227 Q. How is the size of a customer's AB determined?

228 A. Under the current formula, previously approved by the Commission in Docket  
229 No. 95-0031, the Company's total storage top gas capacity is divided by the  
230 Company's total Design Peak Day Supply less expected peak day customer-  
231 owned gas deliveries to the Company. The resulting number is the total number  
232 of bank days. These bank days are then used to determine the customer's bank  
233 rights. The bank days are divided into Base Rate Days and Gas Charge Days.  
234 The number of Base Rate Days is based on the relationship of costs associated  
235 with storage costs accounted for in base rates to total storage costs and the Gas  
236 Charge Days are based on the relationship of costs associated with the Company's  
237 leased storage services to total storage costs. The total number of bank days each  
238 customer receives is related to the customer's service classification and the  
239 services the customer elects to buy from the Company.

240           **A.     Storage**

241       Q.     You stated that storage is one of the assets that supports the availability of AB for  
242           transportation customers. Describe generally the physical storage capability of  
243           the Company.

244       A.     The Company's gas storage generally consists of storage services that are leased  
245           from interstate pipelines and leased from Peoples Gas. The leased storage costs  
246           are recovered through Rider 2, the Gas Charge. Each of these storage assets  
247           operates differently for both physical and contractual reasons. Each storage asset  
248           or service has its own daily, monthly, and seasonal, injection and withdrawal  
249           limitations.

250       Q.     How does storage impact North Shore Gas' operations?

251       A.     North Shore Gas could not operate its system without storage. With multiple  
252           points of receipt of gas into North Shore Gas' system, and over 150,000 points of  
253           delivery of gas to North Shore Gas' sales and transportation customers (whose  
254           demand for gas changes constantly), it is practically impossible for the aggregate  
255           quantity of gas received by North Shore Gas on any day to equal the aggregate  
256           quantity of gas delivered by North Shore Gas to its sales and transportation  
257           customers on that day. With storage, North Shore Gas can take gas stored in  
258           services purchased by North Shore Gas into its system for delivery to its  
259           customers when the aggregate quantity of gas otherwise received by North Shore  
260           Gas on any day is less than the aggregate quantity of gas delivered by North  
261           Shore Gas to its sales and transportation customers on that day. Conversely, with  
262           storage, North Shore Gas can put gas into services purchased by North Shore Gas

263 when the aggregate quantity of gas otherwise received by North Shore Gas on any  
264 day is more than the aggregate quantity of gas delivered by North Shore Gas to its  
265 sales and transportation customers on that day, subject to physical and contractual  
266 limitations.

267 Q. Please describe how the Company's leased storage assets operate.

268 A. The Company purchases storage services from interstate pipelines under terms  
269 and conditions included in the pipelines' tariffs, which are approved by the FERC  
270 and from Peoples Gas under a contract approved by the Commission. The tariffs  
271 define how the Company can use the services and specify any daily, monthly, and  
272 seasonal limitations. The Company must adhere to these limitations. Currently,  
273 the Company purchases several types of leased storage services.

274 Q. Please describe these services.

275 A. First, the Company leases storage from ANR Pipeline Company ("ANR") under  
276 its Firm Storage Service ("FSS") tariff. ANR's FSS is a 50 day service designed  
277 primarily to have gas injected during the April-October period and withdrawn  
278 during the November-March period. In addition the FSS tariff permits the  
279 Company to perform limited winter injections and limited summer withdrawals.  
280 The Company enhances ANR's FSS service through the purchase of No-Notice  
281 Service ("NNS") from ANR. ANR's NNS allows the Company to exercise a  
282 portion of its firm injection and withdrawal rights without the Company providing  
283 notice through one of four nomination cycles. ANR's daily no-notice balancing  
284 service is critical to enabling the Company to meet hourly demand fluctuations  
285 throughout the day and to manage gas consumption changes caused by changes in

286 weather. No-notice balancing also protects the Company against unexpected  
287 supply interruptions throughout the day. The ANR tariffs require that the  
288 Company also purchase firm transportation services from ANR to bring supplies  
289 to and from storage. In sum, the storage and firm transportation services that  
290 North Shore Gas buys from ANR give the Company the ability to deliver gas to  
291 its sales and transportation customers when their aggregate demand for gas  
292 exceeds the amount of gas being delivered to North Shore Gas by suppliers. The  
293 no-notice feature of the service also allows North Shore Gas to inject gas when  
294 deliveries to its system on a day exceed customers' requirements and the  
295 Company's planned storage injections.

296 The Company also leases storage from Natural Gas Pipeline Company of  
297 America ("NGPL") under its 50 day Delivered Storage Service ("DSS") tariff.  
298 The Company must also purchase firm transportation services from NGPL to use  
299 this storage service. In sum, the storage and firm transportation services that  
300 North Shore Gas buys from NGPL also give the Company the ability to deliver  
301 gas to its sales and transportation customers when their aggregate demand for gas  
302 exceeds the amount of gas otherwise being delivered to North Shore Gas by  
303 suppliers. The no-notice feature of the DSS service also allows North Shore Gas  
304 to inject gas when deliveries to its system on a day exceed customers'  
305 requirements and the Company's planned storage injections.

306 Finally, North Shore Gas purchases a service from Peoples Gas. Under  
307 that service contract, North Shore Gas can inject and withdraw gas up to the  
308 contract quantity set forth in the contract.

309 **B. Storage Rights**

310 Q. Please generally describe the storage rights granted to the Company by the  
311 pipeline storage suppliers.

312 A. Generally, the leased storage contracts grant the Company three specific rights:  
313 1) a right to a certain maximum inventory level or capacity; 2) a right to withdraw  
314 a certain amount from that inventory on a given day, for a maximum number of  
315 days, during a particular season; and 3) a right to inject a certain amount into that  
316 inventory on a given day, for a maximum number of days, during a particular  
317 season.

318 Q. Are the daily withdrawal and injection rights constant?

319 A. No. The daily injection and withdrawal rights change frequently.

320 Depending on the tariff, firm injection and withdrawal rights can be a  
321 function of the month of the year, the current inventory balance, or even the  
322 running average of activity over a period of days or some combination of these  
323 and other factors. In general, the daily withdrawal rights are higher than the daily  
324 injection rights in the winter and the daily injection rights are higher than the daily  
325 withdrawal rights in the summer.

326 Q. Are there other limitations?

327 A. Yes. In addition to these daily limits, each storage service has unique monthly  
328 and seasonal withdrawal and injection parameters imposed by the relevant  
329 pipeline tariffs.

330 For example, the NGPL DSS service has a required minimum storage  
331 inventory quantity that must be met during the injection months, and a minimum

332 injection requirement that must be met sometime between October 15 and  
333 November 15 in order for a shipper to retain full withdrawal rights under the  
334 services. Also, during the withdrawal period this service has monthly minimum  
335 and maximum withdrawal quantities, a rolling 15 day maximum withdrawal  
336 limitation, and a target end of season inventory level that must be met to retain  
337 full injection rights for the upcoming injection season.

338 Q. How does the Company manage its storage inventory levels seasonally?

339 A. To help put the Company's use of storage in context, North Shore Ex. TZ 1.1  
340 displays storage inventory levels, as a percent of capacity, for each month over  
341 the last six fiscal years (2001-2006). On average, the Company's inventories  
342 were at 90% on November 30 and at 15% at the end of March.

343 Q. What factors drive these percentages other than the Company's operating history?

344 A. These percentages are driven by three factors: 1) the tariff restrictions on NGPL's  
345 DSS storage (must be 95% full sometime between October 15 and November 15  
346 or the Company loses as much as 50% of its withdrawal rights, and no more than  
347 50% full as of April 30 or the Company is subject to tariff cycling charges), 2) the  
348 cycling charge levied by ANR if the Company's FSS storage is more than 20%  
349 full on April 1 and 3) the contingency needed in the event of a warm start to the  
350 winter season. The Company's use of its storage portfolio reflects these  
351 requirements.

352 Q. How does the Company combine its storage services in providing transportation  
353 to its customers?

354 A. Combining the storage services creates a “hybrid” storage portfolio that is used to  
355 service transportation customers in addition to being used to service North Shore  
356 Gas’ sales customers.

357 Q. Do the current tariffs create any operational concerns for the Company?

358 A. Yes. The current tariffs allow transportation customers to use a disproportionate  
359 share of the storage services used to support services to them.

360 Q. Under the Company’s current tariff, what are the consequences to the Company’s  
361 system when transportation customers use a disproportionate share of the  
362 Company’s storage services?

363 A. There are basically two types of consequences. First, when transportation  
364 customers or suppliers utilize a disproportionate share of storage balancing  
365 services, the Company must adjust its other operations, such as planned storage  
366 injections and withdrawals. These are system resources which could otherwise be  
367 used for retail sales customers. This can potentially create an inappropriate cross  
368 subsidization, and could cause the Company to incur increased costs.

369 Second, if the activity outside of service parameters is substantial, it could  
370 cause the Company to impose system wide restrictions on transportation  
371 customers, such as imposing delivery restrictions or constraints on the use of  
372 delivery points. These restrictions can cause considerable disruption of the  
373 marketplace.

374 Q. Are the negative consequences of actions of one transportation customer often  
375 offset or mitigated by the actions of another?

376 A. Sometimes they are. But there are times that the Company must impose delivery  
377 restrictions on the entire class of transportation customers when perhaps only a  
378 small portion of the transportation customers are operating outside their relative  
379 share of the storage services available to the Company.

380 Q. Please describe the extent to which transportation customers have operated  
381 outside the storage limitations necessary for the Company's system to operate  
382 effectively.

383 A. Ex. TZ 1.2 illustrates the degree to which daily metered transportation customers  
384 have operated outside the bounds of the Company's storage assets' capabilities.  
385 The four years cover a wide range of market and weather conditions. The exhibit  
386 shows, for each of the last four years (pages 1-4), the Company's storage injection  
387 and withdrawal capabilities as a percentage of the Company's design day. The  
388 injection percentages are represented as negatives in the lower line while the  
389 withdrawal percentages are represented as positives in the upper line. The dots  
390 represent the actual net daily storage injections and withdrawals of daily metered  
391 transportation customers, as a percent of their aggregate Selected Standby  
392 Quantity ("SSQ") which is a component of the level of storage rights for which  
393 they are paying. Even when netting the storage activity of these customers  
394 against each other, many of the dots are outside the Company's storage parameter  
395 lines, meaning that the storage activities of the transportation customers, in the  
396 aggregate, exceed the Company's storage injection or withdrawal capabilities as a  
397 percentage of the Company's design day. The Company cannot predict when

398 transportation storage activity will deviate so significantly, as it can be driven by  
399 many factors. But the Company must adjust when it does happen.

400 This daily adjustment issue is portrayed differently in Ex. TZ 1.3. This  
401 exhibit shows the daily change in all transportation customer deliveries (including  
402 customers not daily metered) over the same four year period. Page one displays  
403 the daily changes in volumes while page two displays them as percentage  
404 changes. Again, the Company can only accommodate these volatile swings using  
405 the assets at its disposal.

406 Q. What does the Company currently do to avoid such consequences?

407 A. The Company, under its current tariffs, imposes operational restrictions and  
408 penalties to discourage actions by customers that adversely impact system  
409 operations.

410 Q. Please explain the Company's proposal.

411 A. Under the Company's proposed system shaping, the Company would more  
412 closely define the operational parameters in which suppliers and customers may  
413 act in order to better guard against the imposition of system-wide restrictions.  
414 Hence, the Company is proposing that the transportation customers have  
415 injection, withdrawal and storage balance limitations based on their pro rata share  
416 of all of the storage capabilities available to the Company. The Company  
417 believes that this is a more equitable and potentially less market-disruptive  
418 method of avoiding operational restrictions. The precise amount of this storage  
419 available to a given transportation customer will be determined by the proportion  
420 of the base rates and gas charge demand charges a particular customer pays.

421 Q. What impact does this proposal have on storage available to transportation  
422 customers?

423 A. The hybrid storage I previously described will require customers to comply with a  
424 more defined seasonal shaping of injection, withdrawal and inventory balance  
425 parameters commensurate with the daily, monthly and seasonal limitations  
426 imposed upon the Company by its regulated suppliers and the operating  
427 constraints of its own storage. This should minimize the likelihood that the  
428 Company might have to impose additional restrictions on all transportation  
429 customers.

430 **C. Demand Diversity**

431 Q. What is demand diversity?

432 A. Demand diversity is the concept that the Company's system peak day is not  
433 necessarily the peak day for each individual transportation customer. Commercial  
434 and industrial transportation customers may have requirements that are relatively  
435 less sensitive to weather in relation to customers whose primary use of gas is for  
436 space heating. Consequently, the resources needed to provide peak day service to  
437 transportation customers as a class are reduced to the extent that some  
438 transportation customers experience their peak on a day other than the system  
439 peak.

440 Q. What is the purpose of the Company's Diversity Factor?

441 A. The Company's Diversity Factor recognizes the demand diversity that exists  
442 among the Company's transportation customers and adjusts those customers'  
443 rates to account for the differences in demand.

444 Q. How is the Diversity Factor determined?

445 A. The Diversity Factor is the result of dividing the transportation customers' total  
446 demand on the Company's peak day (i.e., coincident peak demand) by the sum of  
447 each individual customer's peak demand on any day (i.e., non-coincident peak  
448 demand).

449 Q. How does the Company use the Diversity Factor?

450 A. It is used in calculating the Standby Demand Charge and the Standby Commodity  
451 Charge (by applying one minus the Diversity Factor), which is billed to the  
452 Company's transportation customers, and to adjust the number of AB days a  
453 transportation customer receives. In addition, it will adjust the maximum daily  
454 injection and withdrawal rights available under the proposed Rider SST.

455 Q. What is the current value for the Diversity Factor?

456 A. The Commission, in its order in the Company's last rate case, Docket 95-0031,  
457 approved a value of .50 for the Standby Demand Charge Diversity Factor.

458 Q. Is .50 the appropriate value for the Diversity Factor?

459 A. No, it is not the appropriate value for the Company's system. The Company has  
460 performed studies that analyze the previous four years. Each of these studies  
461 indicates that the actual value is at least .68 and has averaged .75. Thus, the  
462 Company proposes to set the Diversity Factor at .75.

463 Q. Why is it appropriate to establish the correct Diversity Factor value?

464 A. This factor should be set correctly so that there is no cross subsidization between  
465 retail and transportation customers. If the factor is too low, the price of reserving  
466 standby service is below cost, and retail customers bear those costs.

467 Q. Please describe Ex. TZ 1.4.

468 A. Ex. TZ 1.4 describes the methodology underlying the Diversity Factor analysis  
469 performed on three groups of customers (Riders FST, SST and LST customers  
470 with daily meters). The analysis includes four contract years (May 1, 2002  
471 through April 30, 2006) evaluated by individual years and as an average of the  
472 four years.

473 Q. Please summarize the findings of your study.

474 A. As shown in Ex. TZ 1.5, the annual Diversity Factor determined for daily metered  
475 customers ranged from .6764 to .8386 and averaged .7549 for the four years. The  
476 range by rider for the four year average was .7427 to .9366.

477 Q. What conclusions can be drawn from this analysis?

478 A. The Diversity Factor for the largest group of individually metered customers does  
479 not vary much year to year. The Company proposes to use .75, which is the  
480 average.

481 Q. What would be the impact of this change in the Diversity Factor?

482 A. The effects on revenues for the test year reflecting proposed rates resulting from  
483 the proposed Diversity Factor are shown on page 1 of North Shore Gas witness  
484 Ms. Grace's Ex. VG 1.2. As indicated in line 16 column M thereof, the amount  
485 of additional Gas Charge revenue received from transportation customers would

486 increase by about \$400,000 due to the change in Demand Charge Revenue caused  
487 by the change in the Diversity Factor. The net increase to transportation  
488 customers' gas charge revenue of about \$400,000 would result in a corresponding  
489 net decrease to retail sales customers. While the impact of an increase in the  
490 Diversity Factor is to shift costs from the retail customers to the transportation  
491 customers, the increased Diversity Factor also provides more storage AB to the  
492 transportation customers.

493 **V. CHANGES TO TRANSPORTATION TARIFFS**

494 Q. What major changes does the Company propose to its transportation riders?

495 A. The Company is proposing 15 major changes to its transportation riders. These  
496 changes will move the Company to having one monthly based service and one  
497 daily based service. Each transportation customer can make its own election on  
498 which service to use based on its particular risk preference and load  
499 characteristics. The proposals are to:

- 500 1. Eliminate enrollment limitations associated with Rider SVT and to rename  
501 the service Rider CFY (Choices For You<sup>sm</sup>).
- 502 2. Make the Rider CFY enrollment process simpler.
- 503 3. Increase Rider CFY's monthly delivery tolerance and change the way  
504 storage is handled to have storage better match the CFY supplier's  
505 customer requirements and rights.
- 506 4. Eliminate Rider FST and enable Rider FST customers to (1) take service  
507 under a more inclusive Rider CFY, (2) take service under a modified  
508 Rider SST, or (3) elect to return to retail sales service.
- 509 5. Merge Rider LST into a revamped Rider SST.
- 510 6. Modify the Rider SST injection and withdrawal formulae as well as the  
511 charges and the methodologies applicable to Rider SST. The Company

512 also proposes to incorporate an annual mechanism to adjust the storage  
513 rights of the programs as the portfolio changes.

514 7. Include seasonal inventory requirements for Rider SST.

515 8. Eliminate Rider TB.

516 9. Eliminate the Customer Change and Activation Charges for Riders P and  
517 AGG, respectively.

518 10. Eliminate charges to suppliers for the use of PEGASys<sup>®</sup> (the Company's  
519 electronic bulletin board).

520 11. Revise the Diversity Factor.

521 12. Modify the cash-out index that is currently in Rider TB and move it to  
522 Rider SST.

523 13. Allow imbalance trades in more circumstances with no change to the fee.

524 14. Introduce an intra-day allocation service.

525 15. Update various transportation administrative fees to reflect the associated  
526 cost of service.

527 Q. Are the present and proposed charges under each transportation rider summarized  
528 in an exhibit?

529 A. Yes. Ex. TZ 1.6 illustrates the charges for each present and proposed  
530 transportation rider. The exhibit also shows the decrease in the Standby  
531 Commodity Charge and the increase in the Standby Demand Charge due to the  
532 change in the Diversity Factor from .50 to .75.

533 **A. Changes to Rider SVT, Small Volume Transportation Service and**  
534 **Rider AGG, Aggregation Service**

535 Q. Please discuss the specific changes the Company proposes for Riders SVT and  
536 AGG.

537 A. Certain restrictions will be removed for Riders SVT and AGG services. First, the  
538 Company will eliminate the Application Period, which is outdated. Second, the

539 Company proposes to eliminate the minimum pool size of 50 accounts. Instead,  
540 the Company will allow the monthly Aggregation Charge to act as the economic  
541 incentive to encourage larger pools. Pursuant to the Commission's Order in  
542 Docket No. 06-0540, the Company will file to change this provision not later than  
543 May 8, 2007. Accordingly, the proposal in this rate case to eliminate the  
544 minimum pool size will become moot if the filing is accepted. Finally, the  
545 Company proposes to eliminate the 50,000 annual therm cap to participate in  
546 CFY. Note that the Company addressed this topic as part of the workshops called  
547 for in the Commission's Order in Docket No. 06-0540. By removing this cap,  
548 mid-sized to larger accounts could become part of the pools. This would allow  
549 suppliers to solicit all customers for CFY Service, except S.C. No. 3, and move  
550 any of their existing FST customers to CFY.

551 Q. Why is the Company proposing that S.C. No. 3 customers be ineligible for CFY  
552 Service?

553 A. The S.C. No. 3 base rates are fully unbundled, which means that no storage costs  
554 are embedded in these customers' base rates. The storage rights available to  
555 Rider CFY customers are determined in a uniform manner and assume that  
556 customers pay the same amount for Company provided balancing and storage.  
557 By definition, S.C. No. 3 does not fit in this structure. Rider SST is designed to  
558 accommodate variable levels of storage and balancing, and S.C. No. 3 customers  
559 are more appropriately served under that transportation service.

560 Q. What technical improvements is the Company proposing to better manage data?

561 A. The Company will provide enhanced self-serve functionality through its  
562 PEGASys<sup>®</sup> system and will implement secure FTP automated file exchanges.

563 Specifically, the Company will:

564 • Modify PEGASys<sup>®</sup> to accept intra-day end-user re-allocation of confirmed  
565 gas deliveries. This will allow a customer to be able to re-allocate, on an  
566 intra-day basis, the customer gas deliveries within its own pools and  
567 transportation contracts – subject to the applicable storage and contract  
568 balancing rules.

569 • Provide enhanced on-line access to customer billing information, such as  
570 data concerning the most recent meter read.

571 • Eliminate the requirement that a customer's meter number must be entered  
572 to retrieve historical usage data on-line through PEGASys<sup>®</sup>.

573 Q. Beyond these technological improvements, what changes have been made to  
574 Rider CFY to make enrollment easier?

575 A. The Company will eliminate the requirement that the supplier include the  
576 customer's meter number as part of the electronic enrollment process. Pursuant to  
577 the Commission's Order in Docket No. 06-0540, the Company will file to change  
578 this provision not later than May 8, 2007. Accordingly, the proposal in this rate  
579 case eliminating the customer meter number requirement will become moot if the  
580 filing is accepted. The customer account number will be sufficient for enrollment  
581 purposes.

582 Q. Pursuant to Condition 35 of the merger Conditions of Approval, North Shore Gas  
583 agreed that it would consider providing customer lists (customer name and  
584 address) to Rider SVT suppliers on substantially the same terms and conditions  
585 that these lists are provided for commercial customers. Has North Shore Gas  
586 developed such a proposal?

587 A. Yes. North Shore Gas proposes providing, by contract, two tiers of information to  
588 suppliers. The information would not be limited to residential customers.

589 The first tier would be account level information that does not identify the  
590 customer. The supplier would not need customer authorization to view this  
591 information because it would not receive any information that was identified with  
592 particular customers. For example, the first tier information would include terms  
593 billed, billing dates and whether the information is based on an actual or estimated  
594 meter reading. The information would be at the account level, but the account  
595 would not be identified by name, address or other customer-specific information.

596 The second tier would be customer-specific information. A supplier could  
597 only view this information if it had the customer's consent, and consent would be  
598 evidenced by the supplier having one or two customer-specific pieces of  
599 information to input as keys to access the information. Keys could include, for  
600 example, the account number or meter number in combination with a telephone  
601 number or amount billed on one of the two most recently issued bills. The type of  
602 information available would include name, account number, billing address,  
603 premises address, usage, type of meter reading, and meter reading dates.

604 Q. You stated that the supplier would need to contract with North Shore Gas. What  
605 would the contract address?

606 A. The contract would define each party's rights and obligations more specifically.  
607 For example, it would define each item of information available in the first and  
608 second tiers. It would specify limits on the use, such as disclosure and retention,  
609 of the information and address the confidential nature of the information. It

610 would include typical contract terms and conditions such as definitions, charges  
611 and payment, term and termination rights, and clauses governing the  
612 interpretation of the contract.

613 Q. Are suppliers required to purchase this service?

614 A. No. North Shore Gas is offering the service because some suppliers have  
615 requested it, and we think it can assist suppliers in serving customers without  
616 detriment to the customers who do not wish to participate in the transportation  
617 programs. Suppliers can participate in the transportation programs without  
618 obtaining any of this information from North Shore Gas, as they have done under  
619 the current program. Notably, the second tier information is all information that  
620 the customer could provide to the supplier. The service that North Shore Gas is  
621 proposing allows a supplier to review information in an electronic format, but  
622 only after the supplier has obtained the customer's consent in the form of  
623 customer-specific keys. This is easier for the supplier, and it is less burdensome  
624 to a customer who wants to participate in the program.

625 Q. What other enhancements is the Company proposing?

626 A. As I mentioned previously, the minimum requirement of 50 accounts in a pool has  
627 been eliminated.

628 Q. Please describe the changes proposed for delivery requirements.

629 A. The Company currently establishes Required Daily Delivery Quantities  
630 ("RDDQs") and a Required Monthly Delivery Quantity ("RMDQ"). The RMDQ  
631 is simply the sum of the RDDQs for the month. These are the amounts of gas,

632 subject to daily and monthly tolerances, that the supplier must deliver each day or  
633 month. The Company is making no changes to the RDDQ tolerance, but it is  
634 adding more flexibility to the RMDQ tolerance. Specifically, the Company  
635 proposes to increase the monthly tolerance applicable to the RMDQ from 2% to  
636 5%.

637 Q. Please describe the impact of this change on the Company and its customers.

638 A. This change can be made manageable for the Company within its gas supply  
639 portfolios and provides benefits to the suppliers by granting them greater monthly  
640 tolerances. The 150% increase in the monthly tolerance benefits customers  
641 because it reduces the cashout concerns of the supplier and allows suppliers to  
642 further utilize the current daily 10% tolerance level applicable to the RDDQ.

643 Q. What changes are proposed with respect to Rider CFY and Rider AGG storage?

644 A. The Company proposes to introduce a storage “true up” mechanism that would  
645 provide suppliers with a customer’s full storage rights at the time the suppliers  
646 enroll customers. Currently, unless the supplier has all of its customers in place at  
647 April 1, the supplier will not get the full benefit of its customers’ storage rights  
648 because customers enrolled after April 1 will have missed part of the injection  
649 season. Conversely, for customers no longer with the supplier, the amount of  
650 storage available to the supplier exceeds what is properly associated with its  
651 customer group. Thus, the Company proposes to adjust (reduce or increase) the  
652 supplier’s Maximum Storage Quantity monthly during most of the injection  
653 period (May through September) as its customer base changes by allocating to the  
654 suppliers their customers’ pro rata share of storage. The storage true-up would be

655 accomplished by charging or crediting the supplier's Rider CFY pool each month  
656 with storage gas priced at the Chicago City Gate First-of-Month ("FOM) index  
657 price. In this way, a pool's storage inventory will mirror the inventory rights of  
658 the pool's current customer base. These true-up dollars will be credited or  
659 charged to Rider 2, as appropriate.

660 Q. What does the Company expect to be the effect of the proposed changes to the  
661 RMDQ tolerance and the storage true up mechanism?

662 A. The combined effect of these proposed delivery and storage changes should be to  
663 offer additional value components which will encourage large volume  
664 transportation customers to switch to Rider CFY service. They reduce the impact  
665 to current Rider FST customers who elect to switch to CFY.

666 Q. Previously you discussed how the Company used its system storage and stated  
667 that changes would be proposed to bring the operations of the transportation  
668 customers more in line with Company operations. How do the proposals for  
669 Rider CFY contribute to this goal?

670 A. With the exception of the change in the monthly tolerance applicable to the  
671 RMDQ, no significant changes are necessary for Rider CFY. Basing CFY storage  
672 use on how the Company uses its storage was approved in the Commission's  
673 Order in Docket No. 01-0469. The Company annually provides CFY suppliers  
674 the monthly storage injection and withdrawal parameters for CFY pools. In  
675 addition to the daily tolerance (+/- 10% of the RDDQ) the Company provides  
676 suppliers under CFY, the Company must provide additional balancing for weather  
677 changes and forecast error. Unlike the large volume transportation program with

678 daily metering to determine actual consumption, the Company takes the  
679 responsibility for forecasting daily CFY volumes correctly. The supplier does not  
680 bear the forecasting risk. In addition, the newly proposed storage true-up  
681 provision transfers appropriate storage gas to and from the Company and the  
682 supplier. This allows both parties to have the appropriate amount of storage gas  
683 operationally for their respective customers.

684 Q. What changes, and what remains the same, for the Rider CFY/AGG rates?

685 A. First, the Company proposes to eliminate the Customer Pool Activation Charge of  
686 \$10 per account. This will encourage additional participation by suppliers by  
687 removing a disincentive to pooling. Second, the Company proposes to maintain  
688 the per pool Aggregation Charge at \$200 per month and to change the per account  
689 Aggregation Charge from \$0.73 per month to \$1.40 per month. Support for the  
690 per account charge is in Ex. TZ 1.7, column F. Third, the Company proposes to  
691 move the billing of the Aggregation Balancing Gas Charge (“ABGC”) from the  
692 supplier to the customer at the account level. Suppliers have raised this as an  
693 important issue. Given the nature of the ABGC monthly calculation, the rate  
694 fluctuates considerably and renders it more problematic for suppliers to include  
695 this varying charge in their fixed rate quotes. The change will make it easier for  
696 suppliers to price their services and explain those services to the customer. The  
697 customers should not be adversely impacted by this change since they were likely  
698 paying this charge as part of their supplier charges.

699 Q. Have you calculated bill impacts that show the proposed increase in delivery  
700 charges as proposed by North Shore Gas witness Ms. Grace and the changes that  
701 you propose?

702 A. Yes. Illustrative examples of annual bill impacts are presented in Exhibit TZ 1.8.  
703 Page 1 displays the bill impacts for a typical size S.C. No. 1 space-heating  
704 customer under present and proposed rates. The top section breaks the bill out by  
705 component for a sales customer while the bottom section does the same for a CFY  
706 transportation customer. The comparison illustrates that the most significant  
707 portion of the increase is due to the base rate component. Page 2 is a similar  
708 comparison, but it shows an actual overall decrease for a typical S.C. No. 2  
709 customer.

710 **B. Elimination of Rider FST – Full Standby Transportation Service**

711 Q. Why does the Company propose to eliminate Rider FST?

712 A. The Company proposes to eliminate Rider FST, Full Standby Transportation  
713 Service, because the program is unnecessary. Changes since the Company's last  
714 rate case and proposed changes in this case justify its elimination. The Company  
715 is also proposing to allow Rider SST customers to choose up to 100% standby,  
716 thus providing another option for customers currently taking service under Rider  
717 FST.

718 Q. Why is the Rider FST program unnecessary?

719 A. The FST program results in inefficient meter reading procedures and the actual  
720 operation of the program expends assets beyond those reasonably appropriate for  
721 the provision of the service.

722 Q. Please explain.

723 A. The FST program is a full standby program that is billed on a calendar month  
724 basis. This requires that manual meter readings be taken outside of normal meter  
725 reading routes (cycles). This is much less efficient than reading meters on their  
726 scheduled “cycle” dates by geographic routes as the CFY program does.  
727 Presently, this additional cost of out of cycle meter reads is recovered in the  
728 monthly Administrative Charge and provides little benefit. Beyond the  
729 inefficiency of obtaining the readings, monthly meter readings do not provide the  
730 daily consumption information that is required to assure that assets are being  
731 utilized equitably by the transportation customers.

732 Q. Why is FST inappropriate for the assets associated with the service?

733 A. The FST program is incompatible with the current operational capabilities of the  
734 Company. Ex. TZ 1.9 illustrates the current withdrawal (page 1 of 2) and  
735 injection (page 2 of 2) rights of FST customers expressed as a percentage of  
736 Maximum Daily Quantity (“MDQ”), compared with the Company’s rights  
737 expressed as a percentage of the Company’s design peak day. As shown by the  
738 data in Ex. TZ-1.9, the rights of the FST service are much too broad in relation to  
739 the assets available to support this service. As an example, while the Company’s  
740 summertime storage injection rights may only be the equivalent to 10% of its  
741 peak day sendout, an FST customer could inject 20% of its peak day (MDQ)  
742 under the Company’s current program. Likewise, the Company’s withdrawal  
743 rights in the summer would be an even lower percentage of its peak day  
744 withdrawal rights, but FST customers can withdraw up to 100% of their peak day.

745 Similar inequities exist for the winter season. The Company strongly believes  
746 that the services that transportation customers receive must correspond to the  
747 assets available to support those services.

748 As proposed in this proceeding, Riders CFY and SST will have daily  
749 tolerance responsibilities linked to actual or estimated daily consumption.  
750 Proposed Rider SST will require the supplier to keep the difference between its  
751 deliveries and consumption within its daily storage rights. As with the current  
752 program, the CFY supplier will be responsible for delivering to the Company a  
753 quantity of gas (adjusted for storage activity) that is within a defined tolerance  
754 range of the best estimate of that pool's daily consumption provided by the  
755 Company (that is, the RDDQ). Eliminating FST and transferring these customers  
756 to CFY or SST will align the FST customers' use of the services to the assets used  
757 to support them.

758 Q. How does North Shore Gas expect the existing Rider FST customers to be  
759 affected by the proposal to eliminate Rider FST?

760 A. There are currently about 1,100 Rider FST customers. Rider FST customers will  
761 have the choice to participate in the enhanced and expanded Rider CFY or Rider  
762 SST. The FST customers can also choose retail sales service. The Company  
763 expects that most Rider FST customers would switch to Rider CFY partly because  
764 these customers would have their monthly administrative fees reduced  
765 substantially.

766 A smaller number of the Rider FST accounts, those using above 30,000  
767 therms annually, are likely to switch to service under Rider SST. As stated above,

768 the Company is proposing to allow customers to choose 100% standby under  
769 Rider SST, as they did under Rider FST. By choosing Rider SST, the customers,  
770 or their supplier, would be responsible for managing their daily deliveries and  
771 storage balances. To ensure that this is being done, the requirement that all SST  
772 customers have daily metering devices will remain in place. Rider FST does not  
773 have such a requirement.

774 Q. Is the cost of the daily metering device a significant burden for customers  
775 currently on FST that want to switch to SST?

776 A. No. Under the Company's proposed daily metering device rates, Rider SST  
777 customers will pay about \$408 per year. For a 50,000 annual therm customer,  
778 that works out to be about 0.8¢ per therm. Also, as a portion of the total gas bill,  
779 that amount would be small (less than 1% of the annual gas bill) and should not  
780 be an obstacle. However, a less expensive alternative is offered under Rider CFY.  
781 The 50,000 therm annual usage limit on CFY is being removed, so larger  
782 customers can go to CFY, if it is a better fit for them.

783 Q. What is the bill impact of these changes on the S.C. No. 2 Rider FST  
784 transportation customers switching to Rider CFY?

785 A. Ex. TZ 1.10, pages 1 (5,000 annual therms) and 2 (30,000 annual therms)  
786 illustrate the bill impacts by component for Rider FST customers switching to the  
787 Rider CFY program. The Exhibit shows decreases in administrative charges and  
788 base rate charges and increases in other charges.

789 Q. What is the bill impact of these changes on the S.C. No. 2 Rider FST  
790 transportation customers switching to Rider SST?

791 A. Ex. TZ 1.11, pages 1 (30,000 therms) and 2 (50,000 therms) illustrate the bill  
792 impacts by component for Rider FST customers switching to the Rider SST  
793 program. The largest decreases are in the base rate components. While the  
794 Standby Demand Gas Charge is increasing due to the change in the Diversity  
795 Factor, there will be an associated increase in the amount of AB. As can be seen  
796 by comparing column C of Ex. TZ 1.10, page 2 of 2, and Column C of Ex. TZ  
797 1.11, page 1 of 2, the 30,000 annual therm customer would pay less under the  
798 proposed Rider SST than under the proposed Rider CFY tariffs.

799 Q. Operationally what effect do these changes have on the Rider FST customers  
800 switching to Rider SST?

801 A. The most important change is that customers' and their suppliers' rights and  
802 obligations will be defined in daily, and not monthly, terms. Rider FST customers  
803 switching to Rider SST will know their daily consumption *via* the daily metering  
804 device. The customers or their suppliers will be responsible for providing daily  
805 gas supply to satisfy those daily requirements within their *pro rata* share of the  
806 Company's storage and balancing capabilities. These customers have chosen an  
807 alternative supplier. The alternative supplier has agreed to supply them. The  
808 Company simply wants to make sure that individual transportation customers  
809 have a right to call on their fair share of the Company's storage and balancing  
810 resources without usurping the shares rightfully available to other transportation  
811 customers and to the Company to serve sales customers.

812           **C.     Changes to and the Merging of Rider SST,**  
813                     **Selected Standby Transportation Service,**  
814                     **and Rider LST, Large Volume Selected**  
815                     **Standby Transportation Service**

816    Q.     What changes do you propose for existing Riders SST and LST?

817    A.     First, the Company proposes to merge Riders SST and LST into a new Rider SST  
818            Tariff.    Currently, Riders SST and LST are largely identical, except for  
819            distinctions that are needed to accommodate the fact that the S.C. No. 3 customers  
820            who take service under Rider LST have fully unbundled rates.  The tariff requires  
821            daily metering.  Rider LST is currently available to S.C. No. 3 customers.

822                     Second, due to the merger of the two tariffs, the Company will make a  
823            distinction in the AB formulas to account for the differences between bundled and  
824            unbundled rates.  In essence, the distinction recognizes that S.C. No. 3 rates are  
825            fully unbundled.

826                     Third, rates have been adjusted to reflect current cost of service study  
827            results.

828                     Fourth, gas delivery and storage requirements have been revised to reflect  
829            the services the customers are paying for and the gas supply, storage, and  
830            transportation portfolio supporting them.  This includes a more defined seasonal  
831            shaping of storage injection and withdrawal rights, as well as seasonal storage  
832            balance requirements.

833                     Fifth, the Standby Demand Charge is being revised to reflect the revised  
834            Diversity Factor of 75%.  The remaining 25% is recovered in the Standby  
835            Commodity Charge.

836    Q.     What language changes were made to Rider SST?

837 A. To accommodate the changes to storage use and the merger of Riders SST and  
838 LST, additional terms and acronyms have been added. The terms are defined in  
839 the Company's proposed Rider SST tariff, which is included in North Shore Gas  
840 witness Ms. Grace's Ex. VG-1.1.

841 Q. Please explain the new Maximum Daily Withdrawal Quantity ("MDWQ") and  
842 the Maximum Daily Injection Quantity ("MDIQ") terms.

843 A. The MDWQ is the maximum amount of gas, accounted for in the AB, that a  
844 customer can withdraw from its AB on a daily basis. The MDWQ is the  
845 customer's pro rata share of the Company's total storage portfolio maximum daily  
846 withdrawal that is allocated to a transportation customer. It is based on the  
847 relationship of the customer's contract Maximum Daily Quantity ("MDQ") to the  
848 Company's Design Peak Day Demand ("DPD"). It takes into account the  
849 proportion of base rate storage assets the customer is paying for and the gas  
850 charge storage assets the customer is paying for through the Standby Demand  
851 Charge, which is determined by that customer's Selected Standby Quantity  
852 ("SSQ"). The Company proposes to annually provide to transportation customers  
853 the information needed to determine the monthly MDWQ. The MDIQ is the  
854 injection counterpart to the MDWQ and works in a similar fashion.

855 Q. Are the definitions of MDIQ's and MDWQ's that you propose stringent relative  
856 to how the Company plans to use its storage?

857 A. No. These quantities will be determined based on monthly percentages (the  
858 Maximum Daily Injection Percentage or MDIP, and the Maximum Daily  
859 Withdrawal Percentage or MDWP) that will mirror the rights that are available to

860 the Company from its storage suppliers. Ex. TZ 1.12 illustrates the Company's  
861 planned average withdrawals (page 1 of 2) and injections (page 2 of 2) by month  
862 as a percentage of its design peak day. These are represented by the lines closest  
863 to "0%" on each graph. The outside lines on each graph (indicating greater  
864 withdrawal and injection capability than the Company's plan) represent the rights,  
865 as a percentage of MDQ, that a 100% standby Rider SST customer would have  
866 under the Company's proposals. As may be noted, there is a relatively large  
867 amount of flexibility for the customer, albeit less than the 100% of MDQ  
868 flexibility that exists today.

869 Q. How did the Company determine the total storage that is available to allocate to  
870 the AB?

871 A. Total available storage was calculated as the non-coincident maximum top-gas  
872 inventory for each storage service under the Company's contractual agreements  
873 with storage providers.

874 Q. How are the AB days calculated?

875 A. As illustrated in Ex. TZ 1.13, AB is calculated by dividing the maximum top-gas  
876 inventory by the system Design Peak Day Supply ("DPDS"), yielding a value of  
877 26 times DPDS. This figure is allocated between a base rates component of 4  
878 times MDQ (15%), and a Rider 2 (gas charge) component of 22 times MDQ  
879 (85%). The Rider 2 component is then adjusted to 17 times MDQ to reflect the  
880 proposed .75 Diversity Factor (22 times .75, rounded). All Rider SST S.C. No. 2  
881 transportation customers' base rates include the costs of the 4 times MDQ of AB,

882 while Rider SST S.C. No. 3 transportation customers elect how much they want in  
883 base rates and gas charge days.

884 Q. How is the proposed AB calculation different than it is under the current tariffs?

885 A. The proposed calculation is very similar to the calculation in the current tariffs.  
886 The only change is that the base rate days will be locked at 4, and will not change  
887 between rate cases. This is consistent with the rates being charged for base rate  
888 days. The gas charge days may change each year as gas charge assets supporting  
889 them change.

890 Q. What AB size can the transportation customer obtain under the Company's  
891 proposal in this proceeding?

892 A. Examples of the effect selected standby percentages have on AB size are  
893 presented in Ex. TZ 1.14. Ex. TZ 1.14 illustrates the results of the Company's  
894 proposed calculation for transportation customers for six sample rate/standby  
895 level combinations.

896 Q. Please continue.

897 A. The number of days of a transportation customer's AB, using these components,  
898 were calculated as shown in the following formulas:

899 For Rider SST S.C. Nos. 2 and 5 Transportation Customers

900 Days of AB = [Base Rate Days + (Gas Charge Days x DF x SSP)]  
901 rounded to the nearest day

902 For Rider SST S.C. No. 3 Transportation Customers

903 Days of AB = [(Base Rate Days x SSP) + (Gas Charge Days x DF x SSP)]

904 rounded to the nearest day

905 In the formulas, factor “DF” is the .75 Diversity Factor. “SSP” is the  
906 percentage of standby service selected by the Rider SST customers.

907 Q. How frequently will the Company calculate the storage day components of the  
908 formulas for determining the AB for transportation customers?

909 A. Since the base rate component is determined using the base rate costs determined  
910 in this proceeding, the Company would retain the base rate component exactly as  
911 determined and approved in this proceeding until a future rate case changes it. As  
912 the Company does today, every year, the Company will calculate the total  
913 Company Maximum Days of AB (“CMD”) and the Gas Charge components. By  
914 April 1 of each year, the Company will file the determinations with the  
915 Commission to be in effect for a one-year period commencing May 1 (except for  
916 the first year which is discussed in the “Timing of Tariff Changes” later in my  
917 testimony). This annual re-computation will enable the Company to reflect  
918 changes in the services supporting the AB and ensure that transportation  
919 customers receive the amount of bank for which they are paying through their  
920 base and gas charge rates.

921 Q. What specific storage inventory requirements is the Company proposing?

922 A. The Company proposes that each transportation customer or each supplier have  
923 its AB at least 85% full by November 30, and no more than 24% full by March 31

924 each year. This is supported by Ex. TZ 1.1, which shows that the Company  
925 generally has its storage filled to 90% of capacity by November 30 because of the  
926 demands of the winter season and its storage depleted to approximately 15% of  
927 capacity by March 31. To the extent the customer's inventory is less than 85% at  
928 November 30, the customer would purchase the deficient quantity from the  
929 Company at 110% of the average monthly index price ("AMIP") determined for  
930 November. To the extent the customer's inventory exceeds 24% at March 31, the  
931 Company would purchase the excess quantity from the customer at 90% of the  
932 AMIP determined for March. The AMIP will be the arithmetic average of daily  
933 Chicago citygate gas prices, published by Gas Daily, for the applicable month.

934 Q. Why is the Company proposing these limits?

935 A. As with other proposed operational changes, the Company is seeking to better  
936 match the suppliers' and customers' rights with the assets supporting those rights.

937 Q. What would be the effect of the new AB requirement?

938 A. The Company's proposal is reasonable with respect to how suppliers can manage  
939 their storage inventories relative to the Company's planned use of those assets.  
940 As illustrated in Ex. TZ 1.1, on average for the past six (fiscal years 2001-2006),  
941 the Company's inventories were at 90% on November 30 and at 15% at the end of  
942 March.

943 Between these dates, the Rider SST customers have the storage inventory  
944 flexibility allowed them within the MDIQ and MDWQ parameters. It is the  
945 Company's belief that most suppliers would plan to operate within these  
946 parameters anyway in order to take advantage of seasonal price differences. But

947 when economic incentives make other usage of storage patterns beneficial to  
948 suppliers, it would not be equitable for transportation suppliers to use storage far  
949 beyond normal operating parameters, thereby necessitating that the Company  
950 compensate in the opposite direction, perhaps to the detriment of sales customers.  
951 For example, a warm period in late February may reduce prices dramatically,  
952 creating an incentive for Rider SST customers to buy daily priced gas rather than  
953 reduce their inventory. If that were to happen, since the inventories in the storage  
954 services must be physically reduced, the Company and the retail sales customers  
955 are forced to make up for the necessary storage withdrawals

956 Q. Do these daily and seasonal storage parameters you propose to impose on  
957 transportation customers mirror exactly how the Company's plan performs?

958 A. No, the parameters reflect the hybrid storage concept I described above and are  
959 reasonable for the transporters for the following reasons:

- 960 • The Company is proposing only maximum daily limits on Rider SST  
961 customers, but no minimums.
- 962 • Inventory requirements going into and out of the winter are at the least  
963 restrictive extremes experienced by the Company, which is to the  
964 customers' benefit.
- 965 • NGPL's DSS tariff prescribes not only daily and monthly minimum and  
966 maximum limitations, but it also looks at running fifteen-day periods to  
967 limit withdrawals to ten days of rights, restrictions which were not  
968 incorporated into the Rider SST calculations.

969 Q. What changes does the Company propose with respect to the administrative  
970 charges for Rider SST?

971 A. The Company proposes to revise the administrative charges for Rider SST  
972 customers from \$60 for individual contracts and the greater of \$73 or \$23 times

973 the number of accounts for group contracts to a straight \$21 per account charge.  
974 The Company believes that these charges more accurately recover the costs of  
975 administering a transportation account. These costs are not incurred to serve  
976 retail sales customers. A cost study was done to determine the cost of serving  
977 transportation customers which is presented as Ex. TZ 1.7, with the results for  
978 Rider SST shown in Column D.

979 Q. Has the Company developed illustrative bill impacts for Rider SST customers  
980 under present and proposed rates?

981 A. Yes. Ex. TZ 1.15 reflects illustrative bill impacts by component for a 50,000  
982 annual therm Rider SST customer under present and proposed rates. The largest  
983 decreases are in the base rate and administrative charge components while the  
984 Standby Demand Gas Charge (“SDGC”) is increasing.

985 **D. Rider P, Pooling Service**

986 Q. What changes is the Company proposing for Rider P?

987 A. First, in response to supplier requests, the Company proposes to increase the  
988 maximum pool size from 150 to 200 accounts. This 33% increase will simplify  
989 management of pools for the suppliers and potentially reduces their costs.  
990 Second, the Customer Change Charge of \$10 is being eliminated. Third, while  
991 the monthly pooling charge remains at \$200 per month, the monthly per account  
992 charge will be changed from \$10 to \$13. This charge is supported in Ex. TZ 1.7,  
993 column E. This increase is mitigated and perhaps entirely eliminated by  
994 elimination of or reductions in other charges or other modifications. For example,  
995 customers will benefit from the elimination of customer change charges as well as

996 the increased pool sizes which effectively reduce the \$200 monthly charge. In  
997 addition, the more liberal trade rules and intra-day balancing have significant  
998 value.

999 Finally, the Rider SST changes related to the AB and use of the bank (for  
1000 example, the MDIQ and MDWQ) are all incorporated in Rider P. The supplier,  
1001 as is the case today, acquires the management of its customers' rights, and Rider P  
1002 has been revised to mirror the Rider SST changes.

1003 Q. Has the Company developed illustrative bill impacts for Rider P customers under  
1004 present and proposed rates?

1005 A. Yes. Ex. TZ 1.16 reflects illustrative bill impacts by component for a 50,000  
1006 annual therm, 20% standby Rider P (SST) customer under present and proposed  
1007 rates. The base rate component is decreasing, but it is partially offset by an  
1008 increase in the standby demand gas charge.

1009 **E. Rider TB, Transportation Balancing Service**

1010 Q. What changes is the Company proposing for Rider TB?

1011 A. The Company proposes to eliminate Rider TB. There are no customers at North  
1012 Shore taking this service.

1013 Q. The Company's other transportation tariffs reference Rider TB in connection with  
1014 the cash-out mechanism. How will this be handled with the elimination of Rider  
1015 TB?

1016 A. The cash-out mechanism will be moved to Rider SST.

1017 Q. Is the cash-out mechanism being modified?

1018 A. Yes, the Company is proposing a change in the calculation of the Average  
1019 Monthly Index Price (“AMIP”). The AMIP calculation is changing to better  
1020 reflect average daily prices throughout the month. Instead of the current practice  
1021 of averaging weekly indices for the Midwest region, the AMIP will now be the  
1022 arithmetic average of the daily Chicago City Gate price as published in Platts Gas  
1023 Daily.

1024 **F. PEGASys<sup>®</sup> System and Charges**

1025 Q. Please describe the PEGASys<sup>®</sup> system.

1026 A. PEGASys<sup>®</sup> is an electronic system accessible to transportation suppliers. The  
1027 system is designed to handle various business processes through on-line  
1028 interactive data entry panels and reports. PEGASys<sup>®</sup> exists to manage such  
1029 diverse business processes as scheduling gas deliveries to both North Shore Gas  
1030 and Peoples Gas; viewing, exporting and importing a variety of data such as  
1031 contract / pool balancing information; imbalance trades of gas volumes; and  
1032 monitoring daily meter usage. For CFY suppliers, the system is the required  
1033 mechanism through which enrollment and exchange of billing and usage data  
1034 occurs. Reporting functionality is extensive and can be viewed in aggregate or  
1035 drilled down to a single meter and day, if needed.

1036 Q. How are the costs of PEGASys<sup>®</sup> recovered today?

1037 A. PEGASys<sup>®</sup> costs are recovered through monthly charges and per minute of usage  
1038 fees. While most participating suppliers use the PEGASys<sup>®</sup> system, it is only  
1039 required for SVT/AGG suppliers today.

1040 Q. Does the Company propose to change these rates?

1041 A. Yes, the Company proposes to eliminate PEGASys<sup>®</sup> fees. In conjunction with  
1042 that elimination, the Company will require PEGASys<sup>®</sup> to be used by all  
1043 transportation suppliers.

1044 **G. Daily Demand Measurement Device Charge**

1045 Q. What changes are being proposed for the Daily Demand Measurement Device  
1046 Charge?

1047 A. The Company proposes to make it one single charge of \$34 per month for each  
1048 Daily Demand Measurement Device. Currently, there are three charges, that  
1049 range from \$34-\$45 per month, depending on the type of meter. The proposed  
1050 change is supported by a cost of service study. The calculation of the cost basis  
1051 for the charge is included in Ex. TZ 1.17.

1052 **H. Imbalance Trading**

1053 Q. Will the Company continue to allow imbalance trading?

1054 A. Yes. The Company will continue to allow imbalance trading for customers or  
1055 suppliers receiving service under Riders SST and P. The Company will also  
1056 expand the circumstances under which trades can be executed.

1057 Q. Under what expanded circumstances will trades be allowed?

1058 A. Trades will no longer be limited to gas volumes related to penalty situations.  
1059 Trades will now be allowed for any movement of gas to or from AB for any  
1060 reason.

1061 Q. What limitations is the Company placing on trades?

- 1062 A. The Company proposes to allow trades as long as:
- 1063 • they net to zero within the Company's system;
  - 1064 • they cannot reduce bank balances below minimum bank requirements or  
1065 increase them above maximum bank requirements;
  - 1066 • they are completed by 5:00 p.m. on the third working day following  
1067 notification of the trade window being open;
  - 1068 • they are confirmed by both parties;
  - 1069 • they are done via PEGASys<sup>®</sup>; and
  - 1070 • they may not eliminate daily imbalance penalties.

1071 **I. Intra Day Allocations**

1072 Q. Does the Company propose to allow intra-day allocations?

1073 A. Yes, in addition to imbalance trading, each day a customer or supplier with more  
1074 than one contract or pool may, on an intra-day basis, re-allocate deliveries  
1075 between or among its contracts.

1076 Q. How will the intra-day allocations work?

1077 A. Currently, allocation of deliveries to end users occurs only on the timely  
1078 nomination cycle. The nomination deadline is, and will remain, 11:30 a.m. on the  
1079 day prior to gas flow (i.e., timely cycle). The Company will offer intra-day  
1080 nominations only for purposes of re-allocation of deliveries. At any time prior to  
1081 4:00 p.m. on the day of gas flow, a customer or supplier may make an intra-day  
1082 nomination to re-allocate deliveries among its contracts. This will allow suppliers  
1083 to reallocate gas among their contracts as they wish to offset any potential gas  
1084 deficiencies and avoid penalties.

1085 **J. Cash-outs**

1086 Q. When do Cash Out Charges occur?

1087 A. A Cash Out Charge will occur when there is still some remaining imbalance after  
1088 imbalance trading has taken place or when contracts or pools are terminated.

1089 Q. Are you changing the way cash outs are determined?

1090 A. As explained above, we are changing the way the AMIP is calculated from using  
1091 weekly to using daily price indices to compute an average for the month. There  
1092 are no other changes being proposed.

1093 **K. Timing of Tariff Changes**

1094 Q. When does the Company propose that its new transportation riders take effect?

1095 A. The Company assumes that this filing will be suspended for eleven months and an  
1096 order will be received in mid winter of 2008. The Company proposes that the  
1097 new large volume (Riders SST and P) transportation tariffs take effect August 1,  
1098 2008. Until that time, the existing large volume transportation riders (FST, SST,  
1099 LST, and P), with revisions to have them serve as transitional riders, will remain  
1100 in effect. The reasons to delay effectiveness of the new transportation riders past  
1101 the base rate changes are: (1) the Company must know the ultimate, approved  
1102 changes to the transportation tariffs to finalize programming, which requires some  
1103 lead time before the changed tariffs can be implemented, (2) the August 1 date is  
1104 still well in advance of the winter high consumption period, and (3) it gives the  
1105 suppliers and customers time to evaluate their alternatives and adjust their  
1106 programs accordingly. Current Rider FST customers will be required to elect  
1107 another transportation program by June 15, 2008, or they will be returned to retail

1108 sales service on August 1. Current Rider LST customers will be transferred to  
1109 Rider SST with the option to change their level of standby service.

1110 During the transition period, Rider SST customers will utilize the same  
1111 MDQ as they had when contracting in the spring of 2008. The new Diversity  
1112 Factor and AB parameters will be effective August 1. The monthly MDIQ and  
1113 MDWQ parameters will also be effective August 1, 2008. These monthly factors  
1114 as well as the other pertinent storage parameters, will be made available to all  
1115 suppliers within ten days of the Commission's order. This will allow time for  
1116 suppliers to adjust standby levels and/or move customers to a new rider.

1117 If approved substantially as proposed, the Company's changes for the  
1118 Choices For You<sup>sm</sup> tariffs (Riders CFY and AGG) will become effective  
1119 simultaneously with the base rate changes. Changes to the CFY programs are  
1120 relatively modest and can be implemented shortly. However, significant  
1121 alterations to the Company's proposed changes may require adjusting the  
1122 implementation date.

1123 During the interim period between the effective date of the CFY tariff  
1124 changes and August 1, customers being served under the other transportation  
1125 riders may switch to Rider CFY. The Company will not impose any transfer  
1126 charges and will waive otherwise applicable standby demand charges for the  
1127 remainder of the contract period for such applicable transfers. The new storage  
1128 catch-up provision will allow the customers to acquire an appropriate level of  
1129 storage for the winter.

1130 Q. Does this conclude your direct testimony?

1131 A. Yes, it does.