

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

THE PEOPLES GAS LIGHT AND	:	
COKE COMPANY	:	
	:	No. 07-____
Proposed General Increase	:	
In Rates For Gas Service	:	

Direct Testimony of

RUSSELL A. FEINGOLD

Managing Director
Navigant Consulting, Inc.

On Behalf of
The Peoples Gas Light and Coke Company

March 9, 2007

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1 **I. INTRODUCTION AND BACKGROUND**

2 **A. Identification of Witness**

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

4 A. My name is Russell A. Feingold and my business address is Four PPG Place, Pittsburgh,
5 Pennsylvania 15222.

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

7 A. I am a Managing Director of Navigant Consulting, Inc. (“NCI”) and co-leader of the
8 Litigation, Regulatory & Markets Group within the firm’s Energy Practice. NCI is a
9 specialized independent consulting firm providing professional services to assist clients in
10 identifying practical solutions to the challenges of uncertainty, risk and distress. We focus on
11 large industry segments that are typically highly regulated and are undergoing significant
12 change.

13 **B. Purpose of Testimony**

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

15 A. The purpose of my testimony is to present and explain the proposal of The Peoples Gas Light
16 and Coke Company (“Peoples Gas”) to implement: (1) a Volume Balancing Adjustment
17 Rider (“Rider VBA”) to adjust base rates on a monthly basis for fluctuations in Peoples Gas’
18 actual volumes caused primarily by variations from “normal” weather and by the energy
19 efficiency efforts of its customers; (2) an Enhanced Efficiency Program Rider (“Rider EEP”)
20 to provide ongoing funding necessary to implement the various energy conservation and
21 efficiency programs envisioned for its customers; (3) an Uncollectible Balancing Adjustment

22 Rider (“Rider UBA”) to enable the timely recovery of bad debt (uncollectible accounts)
23 expenses related to gas costs that Peoples Gas incurs over time; and (4) an Infrastructure Cost
24 Recovery Rider (“Rider ICR”) to enable the timely recovery of certain incremental capital-
25 related costs (i.e., return on investment, associated income taxes, and depreciation expenses)
26 incurred by Peoples Gas to support proposed acceleration of its ongoing gas system
27 enhancements to replace cast iron and ductile iron (“CI/DI”) mains. Specifically, I will
28 discuss the reasons why Peoples Gas has decided to propose these ratemaking mechanisms at
29 this time, the industry-wide conditions that support the implementation of such concepts, the
30 conceptual underpinnings of Peoples Gas’ proposals, and the significant benefits to gas
31 customers and to Peoples Gas created by these proposals. Peoples Gas witness James Schott
32 (Peoples Gas Exhibit (“Ex.”) JFS-1.0) discusses the justification for Rider ICR and Peoples
33 Gas witness Ilze Rukis (Peoples Gas Ex. IR-1.0) discusses the background for Rider EEP.
34 The details of the operations of each of these proposed riders are discussed in the testimony
35 of Peoples Gas witness Valerie Grace (Peoples Gas Ex. VG-1.0). Ms. Grace also sponsors
36 the tariff sheets that include these proposed riders.

37 **C. Summary of Conclusions**

38 **Q. PLEASE SUMMARIZE THE CONCLUSIONS YOU HAVE REACHED IN YOUR**
39 **TESTIMONY.**

40 **A.** I have concluded that Peoples Gas’ business conditions present considerable challenges to its
41 ability to achieve reasonable financial performance and stability. Among these conditions
42 are unpredictable and changeable weather conditions, volatile natural gas commodity prices,

43 declining customer gas usage, and growth in the level of uncollectible accounts expenses on
44 Peoples Gas' system. These conditions have added elements of volatility and uncertainty to
45 the utility's operations that necessitate a fundamental change to the traditional ratemaking
46 process through the application of new ratemaking mechanisms in the form of the
47 Rider VBA, the Rider UBA, and the Rider EEP to preserve Peoples Gas' financial health.
48 Additionally, I have concluded that Peoples Gas' proposal to implement a ratemaking
49 mechanism to recover the cost of the accelerated replacement of CI/DI piping in Rider ICR is
50 reasonable and appropriate.

51 **D. Attachments to Direct Testimony**

52 **Q. ARE YOU SPONSORING ANY EXHIBITS TO YOUR TESTIMONY?**

53 A. Yes, I am. Peoples Gas Exs. RAF-1.1 through RAF-1.5 were prepared by me or under my
54 supervision. They are discussed later in my testimony.

55 **E. Background and Experience**

56 **Q. PLEASE DESCRIBE IN MORE DETAIL THE BUSINESS ACTIVITIES OF NCI.**

57 A. NCI has served the electric and natural gas industries since 1983. We offer a wide range of
58 consulting services related to information technology, process/operations management,
59 business strategy development, and marketing and sales designed to assist our clients in a
60 business environment of changing regulation, increased competition and evolving
61 technology. From an industry-wide perspective, NCI has extensive experience in all aspects
62 of the North American natural gas industry, including utility costing and pricing, gas supply
63 and transportation planning, competitive market analysis and regulatory practices and

64 policies gained through management and operating responsibilities at gas distribution,
65 pipeline and other energy-related companies, and through a wide variety of client
66 assignments. NCI has assisted numerous gas distribution companies located in the U.S. and
67 Canada.

68 **Q. WHAT HAS BEEN THE NATURE OF YOUR WORK IN THE UTILITY**
69 **CONSULTING FIELD?**

70 A. I have over thirty-one (31) years of experience in the utility industry, the last twenty-eight
71 (28) years of which have been in the field of utility management and economic consulting.
72 Specializing in the gas industry, I have advised and assisted utility management, industry
73 trade and research organizations and large energy users in matters pertaining to costing and
74 pricing, competitive market analysis, regulatory planning and policy development, gas supply
75 planning issues, strategic business planning, merger and acquisition analysis, corporate
76 restructuring, new product and service development, load research studies and market
77 planning. I have prepared and presented expert testimony before the Federal Energy
78 Regulatory Commission (“FERC”) and several state and provincial regulatory commissions
79 and have spoken widely on issues and activities dealing with the pricing and marketing of
80 gas utility services. Further background information summarizing my education,
81 presentation of expert testimony and other industry-related activities is included in Peoples
82 Gas Ex. RAF-1.1.

83 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE ILLINOIS COMMERCE**
84 **COMMISSION (“COMMISSION”)?**

85 A. Yes. I previously testified before this Commission on the subjects of gas utility costing,
86 ratemaking, gas supply portfolio planning and procurement, and functional cost allocation
87 methods for electric utilities.

88 Q. **ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

89 A. I am testifying on behalf of Peoples Gas.

90 Q. **WHY HAVE YOU BEEN RETAINED BY PEOPLES GAS?**

91 A. I have been retained by Peoples Gas as a consultant in the area of utility costing and rate
92 design and related regulatory matters. Specifically, Peoples Gas has requested that I provide
93 assistance with the development of its proposals to implement ratemaking mechanisms
94 intended to address the impact weather and declining use per customer have on Peoples Gas'
95 financial performance and on its customers' bills, as well as ratemaking proposals to address
96 Peoples Gas' bad debt expense, its energy efficiency and conservation programs, and its
97 proposed infrastructure improvement initiative.

98 **II. PEOPLES GAS' BUSINESS CHALLENGES**

99 Q. **WHY IS PEOPLES GAS PROPOSING THE RATEMAKING MECHANISMS YOU
100 HAVE DESCRIBED AT THIS TIME?**

101 A. Peoples Gas is proposing Riders VBA, UBA, EEP and ICR at this time because the current
102 business conditions it is experiencing include certain volatile and unpredictable
103 circumstances which Peoples Gas is unable to control. These business conditions have
104 created considerable challenges for Peoples Gas, as evidenced by its ongoing difficulties in

105 recovering its Commission-approved level of costs through base rates. To enable Peoples
106 Gas to achieve the level of financial performance upon which its rates are premised, this
107 situation must be addressed through properly designed rates that reflect Peoples Gas’
108 ongoing costs for the level of service actually demanded by its customers.

109 Q. **HOW DOES THE UTILITIES INDUSTRY REFER TO RATEMAKING**
110 **MECHANISMS SUCH AS PEOPLES GAS’ PROPOSED RIDER VBA?**

111 A. The utilities industry commonly refers to such ratemaking mechanisms as “revenue
112 decoupling” mechanisms. They are referred to in this manner in recognition of their
113 underlying conceptual basis which is to “decouple” a utility’s sales from its revenues so that
114 the utility no longer must rely upon customer sales levels to enable the recovery of its
115 approved cost of service. I will further explain the conceptual basis for such ratemaking
116 mechanisms later in my testimony.

117 Q. **WHAT ARE THE BUSINESS CHALLENGES TO WHICH YOU PREVIOUSLY**
118 **REFERRED?**

119 A. The major business challenges faced by gas utilities in general and by Peoples Gas, in
120 particular, include:

- 121 • Weather variability;
- 122 • Declining use per customer;
- 123 • Rising and volatile wholesale natural gas prices;
- 124 • Increases and volatility in customers’ bills as a result of gas price fluctuation;

- 125 • Rising and uncontrollable bad debt expenses caused primarily by the level of
126 wholesale natural gas prices;
- 127 • Increased impact and promotion of energy efficiency and conservation
128 measures; and
- 129 • Increasing requirements applicable to infrastructure maintenance and
130 improvement and system reliability.

131 Q. **HOW HAVE THE BUSINESS CHALLENGES YOU JUST DESCRIBED**
132 **CONTRIBUTED TO GREATER PRICE UNCERTAINTY AND VOLATILITY FOR**
133 **CUSTOMERS OF PEOPLES GAS?**

134 A. These challenges have considerably impacted the charges Peoples Gas’ customers see on
135 their gas bill. The gas bill of Peoples Gas’ customers essentially consists of two parts – a
136 commodity charge and a delivery charge. The commodity charge is merely a flow-through
137 charge, *i.e.*, Peoples Gas only collects from its customers what it actually paid to its gas
138 suppliers. Hence, any rise in wholesale natural gas prices and any associated commodity
139 price volatility have a direct monthly impact upon the levels of the commodity component in
140 gas bills received by Peoples Gas’ customers. Thus, when gas commodity prices rise,
141 customers’ bills increase proportionately. This situation for Peoples Gas’ customers is no
142 different than that faced by the customers of all gas distribution utilities.

143 Q. **PLEASE CONTINUE.**

144 A. Similarly, the challenges I have described impact the second component of Peoples Gas’
145 rates, the delivery charge. There are rate components of Peoples Gas’ delivery charges that

146 are volumetrically designed. Therefore, as the weather changes and customers use more or
147 less gas, the delivery service portion of the customer's gas bill also will change. When the
148 weather gets colder, customers' gas bills increase and when the weather gets warmer,
149 customers' gas bills decrease. Finally, if colder weather happens to occur when gas
150 commodity prices are increasing, customers will experience a "double whammy" increase in
151 their bills i.e., both the commodity and the delivery portions of the bill will increase. Taken
152 together, these three factors, gas cost pass-through, weather variability, and the level of
153 wholesale natural gas prices, can have a material impact on the monthly level and month-to-
154 month volatility of customers' gas bills.

155 **Q. HOW DO THE BUSINESS CHALLENGES YOU HAVE DESCRIBED IMPACT**
156 **PEOPLES GAS' DELIVERY SERVICE COSTS AND ITS ABILITY TO RECOVER**
157 **THESE COSTS THROUGH BASE RATES?**

158 A. The business challenges I have described pertaining to weather, customer use, wholesale gas
159 prices, bad debt expenses, energy efficiency and conservation, and infrastructure initiatives
160 have a combined effect of introducing elements of considerable and recurring variability,
161 unpredictability and uncontrollability related to Peoples Gas' costs of delivery service and
162 the gas usage factors used to set its base rates to recover such costs.

163 **Q. PLEASE EXPLAIN THIS PHENOMENON.**

164 A. Very simply, these elements of variability cannot be accommodated within the context of the
165 traditional utility ratemaking process. First, the traditional volumetric structure of a utility's
166 base rates does not allow for the full recovery of a utility's non-gas cost of service approved

167 by its utility regulator whenever a decline is experienced in the level of the billing
168 determinants (*i.e.*, customers' gas consumption) used to establish base rates. Second, the
169 static nature of how a utility's revenue requirement is determined precludes the recognition
170 and timely recovery of additional costs incurred by the utility in providing delivery service
171 that is necessitated by unpredictable or uncontrollable business conditions that the utility has
172 to accommodate.

173 Q. **DO YOU BELIEVE THESE ARE DEFICIENCIES THAT WARRANT A**
174 **FUNDAMENTAL RETHINKING OF THE TRADITIONAL RATEMAKING**
175 **PROCESS?**

176 A. Yes, I do. Today's ratemaking process used to design a gas utility's base rates is a static
177 process that relies upon test year assumptions of customer gas usage and weather. In today's
178 highly uncertain and volatile energy environment, however, these assumptions seldom, if
179 ever reflect the actual gas usage levels and weather patterns experienced by the utility during
180 the period the rates remain in effect. This unpredictability in gas usage, exacerbated by the
181 uncertainty of weather, has created the need for a more dynamic process to ensure a utility's
182 base rates will actually recover the commission-approved cost of service. Rather than
183 directly tie a utility's rates to the normalized gas use per customer assumed in its most
184 recently-completed rate case, and keep those rates fixed until the utility's next rate case, the
185 utility should have the ability to periodically adjust its rates to reflect the fluctuations in
186 actual gas volumes, and the associated delivery service revenues, from those assumed in its
187 rate case.

188 Without this fundamental change, the utility will continue to be either adversely or favorably
189 affected financially by the sales level it achieves during any 12-month period relative to the
190 historical sales level used to set its base rates.

191 Q. **MORE SPECIFICALLY, DOES THE TEST YEAR CONCEPT TRADITIONALLY**
192 **USED IN A RATE CASE PRESENT CHALLENGES FOR A GAS UTILITY?**

193 A. Yes. There are certain key assumptions inherent in the use of a test year for purposes of
194 establishing a gas utility's base rates. These assumptions are as follows:

- 195 • A historical test year represents a snapshot in time that attempts to reflect a
196 level of plant and other rate base (the costs of capital investments) and
197 expenses, comprising the utility's total revenue requirement, which will be
198 representative of the period the new rates will be in effect.
- 199 • Use of a test year assumes that the utility's costs in a future period can be
200 reasonably represented by its historical costs (often with adjustments for
201 known and measurable changes), which means such costs are assumed to be
202 predictable, stable and controllable.

203 In a highly volatile and unpredictable cost environment, these assumptions by definition are
204 not realistic ones as to such costs. The static snapshot in time of utility costs presents a
205 flawed assumption in the current unstable and changing environment. As a result, it becomes
206 increasingly difficult in such an environment for a gas utility to reasonably predict several
207 important cost of service components normally established in its rates.

208 Q. **CAN YOU PROVIDE AN EXAMPLE OF A COST COMPONENT OF A GAS**
209 **UTILITY THAT EXHIBITS UNPREDICTABLE AND OFTEN VOLATILE**
210 **CHARACTERISTICS?**

211 A. Yes. The most notable example of a cost component that is unpredictable, unstable, and
212 uncontrollable is a gas utility's cost of purchased gas. Gas costs, particularly over the last
213 decade, have risen and fallen rather dramatically and in a manner that could not have been
214 reasonably anticipated. These unpredictable gas costs are universally recovered through an
215 automatic rate adjustment mechanism, such as the Gas Charge mechanism employed in
216 Illinois.

217 Q. **HAVE THE GAS COSTS ON PEOPLES GAS' SYSTEM DEMONSTRATED THIS**
218 **VOLATILITY AND UNPREDICTABILITY?**

219 A. Yes, they have. Peoples Gas witness Lawrence Borgard (Peoples Gas Ex. LTB-1.0)
220 discussed this in his testimony.

221 Q. **DO ANY OF A UTILITY'S BASE RATE COMPONENTS EXHIBIT VOLATILITY**
222 **AND UNPREDICTABILITY?**

223 A. Yes. Examples of base rate components that exhibit volatile or unpredictable characteristics
224 include bad debt (uncollectible accounts) expense, infrastructure improvement costs,
225 government-mandated gas system safety costs, costs related to public improvement projects,
226 property taxes, pension expenses, and environmental costs. In my opinion, there is a growing
227 recognition in the gas utility industry that such base rate components should be recovered
228 through automatic rate adjustment mechanisms, rather than through fixed charges. I will

229 discuss this issue later in my testimony in conjunction with the conceptual basis for proposed
230 Rider UBA.

231 **Q. DOES THE TRADITIONAL UTILITY RATEMAKING PROCESS ENCOURAGE A**
232 **UTILITY TO PROMOTE ENERGY EFFICIENCY FOR ITS CUSTOMERS?**

233 A. No. Traditional utility ratemaking requires that rates be designed to capture most of the
234 approved revenue requirements for fixed costs through volumetric sales of gas, so that a
235 utility can recover these costs fully only if its customers consume a certain level of gas. As
236 previously discussed, this level of gas usage is typically established in the utility's most
237 recently completed rate case, either based directly upon its historical gas volumes, or
238 indirectly when forecasted gas volumes are used in a future test period. Basing the utility's
239 rates upon a static level of gas volumes, however, creates a significant financial disincentive
240 for the utility to promote energy efficiency for its customers. When customers use less gas,
241 the utility's financial performance almost always suffers because recovery of fixed costs is
242 reduced in proportion to the reduction in gas sales. Hence, it is in the utility's best interests
243 financially to encourage gas usage so as to increase the likelihood of greater recovery of fixed
244 costs.

245 **Q. PLEASE DESCRIBE HOW THE RATEMAKING MECHANISMS PROPOSED BY**
246 **PEOPLES GAS WILL ADDRESS THE BUSINESS CHALLENGES AND**
247 **RATEMAKING DEFICIENCIES THAT YOU HAVE DESCRIBED.**

248 A. Peoples Gas' Rider VBA will: (1) recognize the variability in use per customer and its impact
249 upon the volumetric components of its base rates and (2) will adjust rates (up or down) on a

250 monthly basis to enable the utility to recover its approved level of margin revenues. Peoples
251 Gas' proposed Rider UBA will adjust rates (up or down) on a monthly basis to enable the
252 utility to reflect changes in its bad debt expenses associated with purchased gas costs.
253 Peoples Gas' proposed Riders EEP and ICR will adjust rates on an annual basis to enable the
254 utility to reflect changes in: (1) the costs of its energy efficiency and conservation programs;
255 and (2) the incremental costs of acceleration of its CI/DI infrastructure improvement program
256 that were not included in its proposed revenue requirement in this case.

257 **Q. PLEASE TURN TO EACH OF PEOPLES GAS' PROPOSED RATE MECHANISMS**
258 **AND EXPLAIN IN DETAIL HOW THEY ADDRESS THE BUSINESS**
259 **CHALLENGES FOUND BY PEOPLES GAS AND HOW THEY ACHIEVE**
260 **DESIRABLE RATE MAKING GOALS.**

261 A. I am happy to do so. I will first discuss proposed Rider VBA. Then I will turn to proposed
262 Rider UBA and the proposed Rider EEP. I will lastly discuss proposed Rider ICR.

263 **III. PROPOSED RIDER VBA**

264 **Q. PLEASE INDICATE THE BUSINESS CHALLENGES THAT WERE MOST**
265 **INFLUENTIAL IN PEOPLES GAS' DECISION TO PROPOSE RIDER VBA.**

266 A. The business challenges that primarily gave rise to Peoples Gas' Rider VBA proposal
267 included weather variability, declining use per customer, and the ongoing energy efficiency
268 and conservation efforts of its customers, all of which have impacted Peoples Gas' financial
269 performance and its customers' bills.

270 Q. **PLEASE EXPLAIN HOW WEATHER INFLUENCES THE RATEMAKING**
271 **PROCESS FOR A GAS UTILITY.**

272 A. As part of the ratemaking process, both test year costs and revenues of a gas utility are
273 established based on normal weather. The test year used by the utility is designed to be a
274 reasonable picture of the operating conditions expected to occur during the period in which
275 the utility's approved rates will be in effect. The process of computing revenue under normal
276 weather conditions consists of either increasing or decreasing actual gas volumes, in relative
277 terms, based on the difference between normal temperatures established for the utility's
278 service area and actual temperatures experienced during the actual year.

279 Q. **HOW ARE WEATHER-NORMALIZED GAS VOLUMES USED TO DERIVE A GAS**
280 **UTILITY'S BASE RATES?**

281 A. While the following explanation is somewhat over-simplified, essentially the utility's unit
282 rates and charges for gas service are derived by dividing the appropriate costs, to be
283 recovered through rates, by the weather-normalized gas volumes. These rates and charges
284 are designed to provide the utility with an opportunity to recover the significant level of fixed
285 costs it incurs to provide utility service, at the levels determined in the utility's last
286 completed rate case. Fixed costs are costs incurred by a utility that do not vary with the
287 amount of gas delivered to customers. For Peoples Gas, these costs are composed of fixed
288 operation and maintenance ("O&M") expenses, administrative and general expenses,
289 depreciation, certain taxes, a portion of working capital requirements, and return on
290 investment. These costs also do not vary in the short-term with changes in temperature. If

291 actual temperatures are normal, the utility has a reasonable opportunity to fully recover its
292 fixed costs of service at established levels. Unfortunately, normal temperatures seldom, if
293 ever, occur. Therefore, as a result of abnormal weather, the margin revenues and resulting
294 earnings of a utility such as Peoples Gas can vary widely from the levels authorized by its
295 regulator.

296 **Q. PLEASE EXPLAIN MORE SPECIFICALLY WHAT YOU MEAN BY “MARGIN**
297 **REVENUES”.**

298 A. “Margin revenues” consist of a utility’s total cost of service, exclusive of purchased gas
299 expenses and any other expenses that are treated as “flow-through” items in rates (*e.g.*,
300 revenue taxes). A utility generates margin revenues through base rates for delivering gas to
301 its customers. A utility’s margin revenues reflect its overall costs of operations (exclusive of
302 flow-through items), with most of it fixed, including a fair and reasonable return on its utility
303 assets. A portion of margin revenues are typically recovered through fixed charges such as a
304 monthly customer charge, leaving the remaining portion of margin revenues to be recovered
305 through volumetric distribution charges.

306 **Q. WHAT IS THE SIGNIFICANCE OF ANY PORTION OF MARGIN REVENUES**
307 **BEING RECOVERED THROUGH A VOLUMETRIC CHARGE?**

308 A. To the extent any margin revenue is subject to recovery in a volumetric charge, the
309 realization of full recovery of such margin revenue amount is entirely dependent upon the
310 volumes of gas usage experienced by the utility. Therefore, the recovery of margin revenue
311 in a volumetric component of rates puts full recovery at risk.

312 Q. **IS IT IMPORTANT THAT A UTILITY SUCH AS PEOPLES GAS REALIZES THE**
313 **MARGIN REVENUE THAT WAS ALLOWED BY THE REGULATOR IN THE**
314 **UTILITY'S MOST RECENT RATE CASE?**

315 A. Yes. The utility's financial health is directly tied to its ability to recover the total cost of
316 service (excluding purchased costs) approved by its regulator through the margin revenues
317 upon which its base rates were previously established.

318 Q. **PLEASE EXPLAIN HOW FLUCTUATIONS IN WEATHER OVER TIME IMPACT**
319 **A GAS UTILITY'S TEMPERATURE-SENSITIVE CUSTOMERS AND THE**
320 **UTILITY'S FINANCIAL PERFORMANCE.**

321 A. Since the bills of gas customers are largely based on the level of gas usage, temperature-
322 sensitive customers' monthly bills can vary widely due to changing weather conditions.
323 Under traditional ratemaking methods, if actual temperatures were colder than normal, the
324 typical gas customer would use more gas, pay more for service, and potentially overpay its
325 share of fixed costs. This occurs because the unit rates used to recover fixed costs are not
326 reduced to recognize the higher gas volumes used by customers during colder weather.
327 Since the gas utility's level of fixed costs does not change, the higher gas volumes applied
328 against the same unit rate would generate comparatively higher non-gas revenues than the
329 level of fixed costs established for ratemaking purposes. Conversely, in warmer than normal
330 weather, the reverse situation will occur. Customers' gas usage decreases with warmer
331 temperatures, thus generating comparatively lower non-gas revenues than required to recover
332 the gas utility's total fixed costs that do not decrease due to warm weather.

333 Q. **WHAT IS YOUR UNDERSTANDING OF PEOPLES GAS' HISTORICAL**
334 **WEATHER PATTERNS?**

335 A. Based on my discussion with Peoples Gas' staff, it is my understanding that there has been a
336 wide variation in actual weather compared to normal weather, and that over the most recent
337 ten (10) year period of Fiscal Years 1997 - 2006 ("10 Year Period"), there were four (4) years
338 of colder than normal weather and six (6) years of warmer than normal weather. It is also
339 my understanding that in some monthly and annual periods, the magnitude of the variation in
340 actual weather from normal levels was significant.

341 Q. **HOW WOULD YOU DESCRIBE PEOPLES GAS' HISTORICAL GAS USAGE**
342 **EXPERIENCE?**

343 A. Over the 10 Year Period, Peoples Gas has experienced substantial declines in use per
344 customer. Mr. Borgard's Exhibits Peoples Gas Exs. LTB-1.2 and LTB-1.3 demonstrate that
345 during the 10 Year Period, the annual average use per customer has declined in Peoples Gas'
346 small residential service (S. C. No. 1) and general service (S. C. No. 2) classes. The most
347 dramatic declines have occurred in its heating classes. In addition, my Exhibit Peoples Gas
348 Ex. RAF-1.2 presents the results of a recent American Gas Association study that analyzed
349 the decline in use per customer in the U.S. residential market since 1980¹. Peoples Gas'

¹ On average, natural gas use per customer in the U.S. has been declining by about one percent per year since 1980. See American Gas Association Energy Analysis entitled, "Forecasted Patterns in Residential Natural Gas Consumption, 2001-2020", EA 2004-04 (dated September 24, 2004) and "Patterns in Residential Natural Gas Consumption, 1997-2001", EA 2003-01 (dated June 16, 2003).

350 customers during that period have shown a material reduction in their gas consumption,
351 similar to other gas customers throughout the U.S.

352 **Q. AGAINST WHAT REFERENCE POINT SHOULD PEOPLES GAS' DECLINE IN**
353 **USE PER CUSTOMER BE REVIEWED?**

354 A. The reference point should be the use per customer levels established in Peoples Gas' last
355 base rate case – Docket No. 95-0032 (“1995 Rate Case”). Peoples Gas' base rates in that
356 proceeding were implemented in November 1995. The annual “baseline” use per customer
357 for the small residential heating service class (S. C. No. 1) established in the 1995 Rate Case
358 to design Peoples Gas' base rates was approximately 160 Dt per customer. You can readily
359 see in Mr. Borgard's Exhibit Peoples Gas Ex. LTB-1.2 that over the succeeding years since
360 the 1995 Rate Case was completed, Peoples Gas never experienced a gas sales level of 160
361 Dt per customer. A similar assessment can be made for Peoples Gas' general service class
362 (S. C. No. 2), as shown on Mr. Borgard's Exhibit Peoples Gas Ex. LTB-1.3. In the 1995
363 Rate Case, Peoples Gas' base rates for S. C. No. 2 were premised upon a use per customer of
364 approximately 1,064 Dt – a level rarely reached in the 10 Year Period.

365 **Q. WHAT CONCLUSION DO YOU REACH FROM THIS ASSESSMENT?**

366 A. The “baseline” use per customer levels established in the 1995 Rate Case is not
367 representative of the actual use per customer Peoples Gas experienced in subsequent years.
368 In fact, the data presented in Mr. Borgard's Exhibit Peoples Gas Ex. LTB-1.2 demonstrates
369 that the “baseline” use per customer level for S. C. No. 1 was always high relative to the
370 actual amounts. Therefore, it is not surprising at all that the application of Peoples Gas'

371 base rates to customers' bills resulted in the collection of margin revenues that almost always
372 were low relative to the level this Commission approved as reflected on my Exhibit Peoples
373 Gas Ex. RAF-1.4. To the extent the "baseline" use per customer level established in this
374 case is not representative of Peoples Gas' expected future trends, its base rates will not
375 properly recover the fixed costs incurred to provide its customers with gas delivery service.

376 **Q. WHAT FACTORS IMPACT CUSTOMERS' GAS USAGE WHICH MIGHT HAVE**
377 **CONTRIBUTED TO THE USAGE DECLINES YOU HAVE DISCUSSED?**

378 A. Several factors influence the level of customer gas usage, including weather variation, the
379 level of wholesale gas prices, and the effects of conservation measures, including the impact
380 of energy efficiency gains on customer use.

381 **Q. HOW DOES THE LEVEL OF WHOLESALE GAS PRICES AFFECT CUSTOMER**
382 **GAS USAGE?**

383 A. As wholesale gas prices increase, customers' gas bills increase as well. As a result, some
384 customers undertake short-term actions to conserve natural gas (*e.g.*, "dialing-down" of home
385 thermostats) causing a decline in use per customer.

386 **Q. HOW DO CONSERVATION AND ENERGY EFFICIENCY GAINS AFFECT**
387 **CUSTOMER USAGE?**

388 A. The longer term actions of customers to conserve and efficiently use natural gas also result in
389 a decline in use per customer. These actions primarily relate to the increased efficiency of

390 gas appliances (especially space heaters), reduced appliance saturation of homes with natural
391 gas, and tighter, more energy efficient homes.

392 **Q. HAVE YOU EXAMINED THE HISTORICAL IMPACT OF WEATHER ON**
393 **CUSTOMERS' MONTHLY BILLS?**

394 A. Yes. My Exhibit Peoples Gas Ex. RAF-1.3 presents the actual average monthly gas bills for
395 Peoples Gas' residential heating customers over the 10 Year Period. This Exhibit illustrates
396 the extreme year-to-year variation in customers' monthly gas bills caused by the normal
397 seasonal variations in weather. Page 2 of this Exhibit highlights the very close relationship
398 between customers' gas bills and weather. In addition to the primary impact of weather,
399 monthly bills also were affected by the variation and level of gas commodity costs, which
400 spiked to high levels nationally during the 2000-2001 and 2005-2006 winter heating seasons.

401 **Q. HAVE YOU ALSO EXAMINED HOW THE MARGIN REVENUES COLLECTED**
402 **BY PEOPLES GAS HAVE VARIED HISTORICALLY?**

403 A. Yes. I have prepared Peoples Gas Ex. RAF-1.4 to demonstrate margin revenue losses that
404 Peoples Gas has experienced. As defined here, the margin revenue losses that Peoples Gas
405 experienced were due to its inability to fully collect delivery service costs through its
406 volumetrically designed charges because of the effects of fluctuations in gas volumes. This
407 Exhibit presents the margin revenue impact experienced by Peoples Gas in its small
408 residential and general service rate classes due to fluctuations in gas volumes caused
409 primarily by variations in weather from normal levels and declining use per customer. This
410 Exhibit also illustrates that Peoples Gas incurred margin revenue losses in nine years of the

411 10 Year Period. The total margin revenue losses during that period amounted to
412 approximately \$312 million. Moreover, in three years of the 10 Year Period, Peoples Gas
413 experienced margin revenue losses that were in excess of ten percent (10%) of its total
414 approved margin level (including customer charge and distribution charge revenue) of
415 approximately \$409 million in the 1995 Rate Case for these same rate classes.

416 **Q. IS PEOPLES GAS' EXPERIENCE UNUSUAL IN THE GAS DISTRIBUTION**
417 **INDUSTRY?**

418 A. No. This type of under-recovery of fixed costs is not unique to Peoples Gas. Under-recovery
419 has been quite commonplace in the gas distribution segment of the energy industry.

420 **Q. WHAT HAS BEEN THE INDUSTRY RESPONSE TO THIS UNDER-RECOVERY**
421 **OF COSTS SITUATION?**

422 A. To address the uncertainty of fixed-cost recovery, many gas utilities proposed and
423 implemented approved ratemaking solutions, such as weather normalization adjustment
424 clauses, revenue decoupling mechanisms, and increases to their monthly service or customer
425 charges to more closely reflect in rates their fixed costs of service.

426 **Q. HOW WILL THE PROPOSED RIDER VBA ADDRESS WEATHER, THE DECLINE**
427 **IN USE PER CUSTOMER AND THEIR ASSOCIATED VARIABILITY, WHICH**
428 **HAS BEEN EXPERIENCED BY PEOPLES GAS?**

429 A. The proposed Rider VBA will minimize the impact of weather on Peoples Gas' financial
430 condition and on the volatility of its customers' bills. The proposed Rider represents the

431 required fundamental change to the utility ratemaking process to recognize that a utility such
432 as Peoples Gas has difficulty in establishing a reasonable level of volumes in a rate case that
433 can represent its volumes in future periods. As a consequence of this process, the volumetric
434 base rates or distribution charges that Peoples Gas would derive in its rate case, and that the
435 Commission would approve, are unlikely to reflect the level of base rates required in future
436 periods to fully recover its approved level of fixed operating costs.

437 **Q. IN WHAT OTHER MANNER WILL THE PROPOSED RIDER VBA IMPACT**
438 **PEOPLES GAS?**

439 **A.** The proposed Rider VBA will remove the disincentive Peoples Gas has to promote energy
440 conservation and efficiency programs for its customers. It will place Peoples Gas in a much
441 stronger position to achieve the objectives and implement the plan it has developed to offer
442 to its customers various energy conservation and efficiency programs, through third party
443 administrators, to help offset the volatility and unpredictability of high gas prices. Peoples
444 Gas and its customers will benefit from this further alignment of interests and promoting
445 energy utility efficiency. The appropriateness of this type of ratemaking solution has been
446 recognized by the Oregon Public Utility Commission (“OPUC”) in its approval in 2002 of a
447 revenue decoupling mechanism for Northwest Natural Gas Company (“NW Natural”).
448 There, the OPUC affirmed the severance of the connection between profits and sales and
449 acknowledged the conflict between the motivation to sell energy and the motivation to
450 promote reduction in energy consumption.

451 Q. **PLEASE EXPLAIN THE IMPORTANCE OF “BREAKING THE LINK” BETWEEN**
452 **PEOPLES GAS’ EARNINGS AND SALES TO ACHIEVE ENHANCED ENERGY**
453 **EFFICIENCY AND CONSERVATION GOALS.**

454 A. Breaking this link is important because it eliminates Peoples Gas’ “Throughput Incentive”
455 that is inherent in the way its gas rates have been historically designed. The “Throughput
456 Incentive” encourages a utility such as Peoples Gas to be financially motivated to increase
457 sales of natural gas (relative to historical levels which underlie base rates) and to maximize
458 the “throughput” of natural gas across its utility system. Under the traditional utility rate
459 making structure, a utility is financially motivated to increase its sales levels in a future
460 period above that established in its previous rate case because its rates are designed to
461 recover most fixed costs on a volumetric basis – causing the utility’s revenues to increase as
462 its sales increase. Under traditional utility ratemaking, an increase in the recovery of fixed
463 costs will occur (compared to the level approved in the utility’s most recently completed rate
464 case) when sales are higher than assumed in the design of the utility’s rates. Conversely, a
465 decrease in the recovery of fixed costs will occur when sales are low relative to assumed
466 levels. This situation creates an automatic disincentive for utilities to promote conservation
467 or energy efficiency initiatives because such actions will reduce the utility’s revenues and
468 resulting earnings. Proposed Rider VBA will adjust Peoples Gas’ rates on a periodic basis to
469 offset the revenue impact of increases or decreases in sales. By doing so, proposed Rider
470 VBA would effectively eliminate the link between sales and earnings. Hence, Rider VBA
471 would encourage Peoples Gas to be supportive of measures which would promote decreased
472 energy usage, conservation, or other energy efficiency initiatives.

473 Q. **PLEASE EXPLAIN THE MECHANICS OF REVENUE DECOUPLING IN UTILITY**
474 **RATEMAKING.**

475 A. While such a ratemaking mechanism can take several forms, the basic approach consists of
476 defining a target for the utility's margin revenues and placing over- and under-collections of
477 revenue with reference to that target in a deferred account for refund or recovery in a
478 subsequent period. Under these mechanisms, the gas utility cannot increase its earnings by
479 increasing its sales volumes because any over-collected margin revenues are refunded to
480 customers.

481 Q. **IS IT NECESSARY TO CONTINUE TO USE SOME MEASURE OF SALES**
482 **VOLUMES TO COMPUTE A GAS UTILITY'S UNIT RATES?**

483 A. Yes, it is. Under a revenue decoupling mechanism, however, the sales level assumed in the
484 utility's last rate case upon which its base rates were designed is not blindly adhered to for
485 purposes of representing the level of sales the utility actually achieves in a future 12-month
486 period. By utilizing customers' actual sales levels and relating that amount to the utility's
487 approved level of distribution margin revenues, rates can be adjusted to recover the
488 appropriate level of revenues to produce the margin authorized by the regulator. In other
489 words, the utility's distribution margins are inextricably linked to its rate case sales level.

490 Q. **PLEASE CONTINUE.**

491 A. The de-emphasis of sales volumes in the operation of a revenue decoupling mechanism better
492 recognizes the way consumers actually perceive, value, and purchase services offered by gas
493 and electric utilities. A consumer does not look at utility services and consciously make a

494 decision to purchase a certain number of therms of gas or kilowatt-hours of electricity.
495 Instead, the consumer purchases utility services to acquire light, heat, air conditioning and a
496 wide range of other consumer needs and conveniences. Therefore, we should not continue to
497 hold the financial health of utilities hostage to the fluctuating sales levels resulting from such
498 consumer choices. If over time consumers are able to utilize energy commodities more
499 efficiently, through adoption of energy conservation and energy efficiency techniques
500 promoted by utilities and others, the utilities should not be penalized for these beneficial
501 societal actions.

502 **Q. WOULD IMPLEMENTATION OF A REVENUE DECOUPLING MECHANISM**
503 **LESSEN THE COMPUTATIONAL PRECISION BY WHICH A GAS UTILITY'S**
504 **BASE RATES ARE SET?**

505 A. No. Under a revenue decoupling mechanism, the utility's base rates will continue to be
506 computed by rate class and they will continue to be designed to recover Peoples Gas'
507 approved level of margin revenue. Even more precisely, however, they will reflect the
508 customers' actual gas consumption.

509 **Q. DOES THE IMPLEMENTATION OF A REVENUE DECOUPLING MECHANISM**
510 **SUCH AS RIDER VBA PROVIDE THE UTILITY WITH A GUARANTEE THAT IT**
511 **WILL ACHIEVE THE FINANCIAL PERFORMANCE PREVIOUSLY APPROVED**
512 **BY THE REGULATOR?**

513 A. No. In order to achieve its financial expectations, the utility must still actively manage its
514 costs and growth in customers relative to the levels approved in its last rate case to achieve

515 its financial expectations. The re-establishment of the utility's sales levels that I just
516 described only takes gas volumes out of the ratemaking equation. It does not eliminate any
517 of the utility's responsibilities to prudently manage the business factors that are under its
518 control.

519 **Q. HAVE OTHER PARTICIPANTS IN THE GAS INDUSTRY ENDORSED THE**
520 **CONCEPT OF A REVENUE DECOUPLING MECHANISM TO ADDRESS THE**
521 **INHERENT DISINCENTIVE THAT A UTILITY HAS TO PROMOTE ENERGY**
522 **EFFICIENCY?**

523 **A.** Yes. With the increased volatility in energy prices and the resultant unprecedented upward
524 pressure being placed on customers' utility bills, many energy industry groups are now
525 publicly advocating a renewed focus on promoting cost-effective energy efficiency measures
526 to help relieve these consumer burdens. These groups include the American Gas Association
527 ("AGA"), the Edison Electric Institute ("EEI"), the Natural Resources Defense Council
528 ("NRDC"), the Alliance to Save Energy, and the American Council for an Energy Efficient
529 Economy ("ACEEE"). These groups realize that a fundamental change must be made to the
530 utility ratemaking process in order to achieve these consumer benefits. They have endorsed
531 the concept of a revenue decoupling mechanism as their solution to the problem.²

532 **Q. PLEASE CONTINUE.**

533 **A.** The NRDC and EEI issued a particularly pointed statement. It noted that:

² Joint Statement of the American Gas Association and the Natural Resources Defense Council submitted to the National Association of Regulatory Utility Commissioners ("NARUC") (July 2004).

534 *To eliminate a powerful disincentive for energy efficiency and distributed-resource*
535 *investment, we both support the use of modest, regular true-ups in rates to ensure*
536 *that any fixed costs recovered in kilowatt-hour charges are not held hostage to sales*
537 *volumes.*³

538 **Q. HAS ANY OTHER INDUSTRY ORGANIZATION RECOGNIZED REVENUE**
539 **DECOUPLING AS A VIABLE RATEMAKING CONCEPT TO ADDRESS THIS**
540 **ISSUE?**

541 **A.** Yes. NARUC has recognized that revenue decoupling as a ratemaking concept provides
542 earnings stability for utilities and removes the disincentives for promoting energy
543 conservation. In particular, NARUC made reference to the above-mentioned groups and
544 stated that:

545 *Among the mechanisms supported by these groups are the use of automatic rate true-*
546 *ups to ensure the utility's opportunity to recover authorized fixed costs is not held*
547 *hostage to fluctuations on (sic) retail sales.*⁴

548 In its 2005 Fall Meeting, NARUC's Board of Directors adopted the "Resolution on Energy
549 Efficiency and Innovative Rate Design," dated November 16, 2005. As set forth in this
550 second resolution:

³ Joint recommendation submitted in November 2003 to the NARUC by the NRDC and the EEI.

⁴ NARUC Resolution on Gas and Electric Efficiency, Sponsored by NARUC Natural Gas Task Force, Committee on Gas, Committee on Consumer Affairs, Committee on Electricity, Committee on Energy Resources and the Environment, adopted by the NARUC Board of Directors on July 14, 2004.

551 *[NARUC]...encourages State commissions and other policy makers to review the*
552 *rate designs they have previously approved to determine whether they should be*
553 *reconsidered in order to implement innovative rate designs that will encourage*
554 *energy conservation and energy efficiency that will assist in moderating natural gas*
555 *demand and reducing upward pressure on natural gas prices...⁵*

556 The NARUC resolution recognized that the traditional volume driven state approach to
557 regulating the rates that utilities charge to deliver natural gas might tend to misalign the
558 interests of natural gas utilities and the goals of energy efficiency and energy conservation.⁶
559 As part of this review, NARUC further encouraged state utility regulators and other policy
560 makers to consider in their review innovative rate designs including “energy efficiency
561 tariffs” and “decoupling tariffs.”⁷ The resolution recognized several utilities that have
562 received approval of revenue decoupling mechanisms, fixed-variable rates and other
563 innovative rate design approaches.

564 **Q. HAVE ANY NATIONAL POLICY INITIATIVES BEEN UNDERTAKEN TO**
565 **ADDRESS THE DEFICIENCIES IN TRADITIONAL UTILITY RATEMAKING?**

⁵ NARUC Resolution on Energy Efficiency and Innovative Rate Design, Sponsored by the Committee on Gas, recommended by the NARUC Board of Directors on November 15, 2005, adopted by the NARUC on November 16, 2005.

⁶ Ibid.

⁷ Ibid.

566 A. Yes. The recently issued National Action Plan for Energy Efficiency⁸ (“Action Plan”)
567 emphasizes the need to eliminate ratemaking and regulatory disincentives or barriers through
568 its recommendation that utility regulators “modify policies to align utility incentives with the
569 delivery of cost-effective energy efficiency and modify ratemaking practices to promote
570 energy efficiency investments.” Specifically, the Action Plan states that, “removing the
571 throughput incentive is one way to remove a disincentive to invest in efficiency.” It is widely
572 recognized that a revenue decoupling mechanism is a ratemaking approach that can address
573 the Throughput Incentive utilities have when their rates are designed so that fixed costs are
574 recovered through volumetrically-based energy charges.

575 Q. **WOULD YOU LIKE TO MAKE ANOTHER OBSERVATION?**

576 A. Yes. I also would note that in NARUC’s “Resolution Supporting the National Action Plan
577 on Energy Efficiency” (“NARUC Resolution”), it endorsed “the principal objectives and
578 recommendations of the Action Plan, and commends to its member commissions a state-
579 specific, or where appropriate, regional review of the elements and potential applicability of
580 energy efficiency policy recommendations outlined in the Action Plan, in an effort to identify
581 potential improvements in energy efficiency policy nationwide.”⁹ The NARUC Resolution
582 cites five key elements of the Action Plan, including the modification of ratemaking practices

⁸ Issued in July 2005, the “Action Plan” was facilitated by the U.S. Department of Energy and U.S. Environmental Protection Agency with the participation of over 50 utilities, public utility commissions, energy consumers, and non-governmental groups to set a broad course for encouraging greater energy efficiency investment in the United States.

⁹ NARUC Resolution Supporting the National Action Plan for Energy Efficiency, Sponsored by the Executive Committee and the Committees on Consumer Affairs, Electricity, Energy Resources and the Environment, and Gas, adopted by the NARUC Board of Directors August 2, 2006.

583 to align utility incentives with the delivery of cost effective energy efficiency and to promote
584 energy efficiency investments.

585 **Q. WHICH STATE UTILITY REGULATORS HAVE APPROVED THE CONCEPT OF**
586 **REVENUE DECOUPLING IN CONJUNCTION WITH THE SETTING OF UTILITY**
587 **RATES?**

588 A. Currently there are nine (9) states where utility regulators have approved the concept of
589 revenue decoupling in setting a utility's gas rates. These states are California, Indiana,
590 Maryland, New Jersey, North Carolina, Ohio, Oregon, Utah, and Washington. Specifically,
591 revenue decoupling mechanisms have been approved for sixteen (16) utilities, including
592 Pacific Gas and Electric Company, San Diego Gas and Electric Company, Southern
593 California Gas Company, Southwest Gas Corporation, Vectren Energy Delivery (Indiana),
594 Baltimore Gas & Electric Company, Washington Gas, New Jersey Natural Gas, South Jersey
595 Gas, Piedmont Natural Gas Company, Inc., Vectren Energy Delivery (Ohio), Cascade
596 Natural Gas Corporation (Oregon), Northwest Natural Gas Company, Questar Gas, Avista
597 Utilities and Cascade Natural Gas Corporation (Washington). In addition, eleven (11) other
598 gas utilities have proposed revenue decoupling mechanisms in regulatory proceedings
599 currently pending before utility regulators in eleven (11) states.

600 **Q. HAS THE FINANCIAL COMMUNITY RECOGNIZED THE VALUE OF**
601 **RATEMAKING SOLUTIONS TO ADDRESS THE CONDITIONS FACED BY GAS**
602 **UTILITIES?**

603 A. Yes. The financial community has discussed the impact of energy conservation and usage on
604 gas utilities. The financial community has acknowledged that rate design solutions such as
605 revenue decoupling, favorably address the financial consequences of reduced usage on gas
606 utility systems.

607 Q. **PLEASE CONTINUE.**

608 A. The financial community has specifically addressed the favorable impact on margin that can
609 result from the application of appropriate ratemaking methods. For example, Moody's
610 Investor Service issued a *Special Comment* report that specifically addressed this topic. The
611 Moody's report stated:

612 *Moody's believes that having utility rate designs that compensate the gas LDCs for*
613 *margin losses caused by variations in gas consumption due to conservation as with*
614 *variations due to weather, would serve to stabilize the utility's credit metrics and*
615 *credit ratings. Utilities having these ratemaking mechanisms also tend to carry 'A'*
616 *credit ratings.*¹⁰

617 Q. **DOES PEOPLES GAS' PROPOSED RIDER VBA REPRESENT AN EFFECTIVE**
618 **SOLUTION TO THE AFOREMENTIONED RATEMAKING PROBLEMS IT HAS**
619 **EXPERIENCED?**

620 A. Yes. Peoples Gas' proposed Rider VBA is fair, symmetrical, and beneficial to the utility
621 and its customers for the following reasons:

622 (1) Rider VBA would effectuate the Commission’s assumption of normal weather in
623 rates. Rider VBA simply allows for the weather-normalized recovery of margin as is
624 intended through the weather-normalization of base rates. When it is colder than
625 normal, customers would not overpay for the utility’s fixed costs and the utility
626 would not over-recover margin. Conversely, when it is warmer than normal,
627 customers would not underpay for the utility’s fixed costs and the utility would not
628 under-recover margin.

629 (2) Rider VBA would rely upon realistic gas volume levels for computing Peoples Gas’
630 unit rates.

631 (3) Rider VBA would be a more effective ratemaking method to address the issue of
632 margin volatility on a seasonal basis, and year to year compared to budget billing and
633 monthly service charge increases.

634 (4) Rider VBA would enable Peoples Gas to promote energy conservation and efficiency
635 programs for its customers without the continual threat of margin losses due to
636 declining gas sales per customer.

637 Q. **PLEASE EXPLAIN THE KEY ELEMENTS OF PEOPLES GAS’ PROPOSED**
638 **RIDER VBA.**

639 A. Peoples Gas’ proposed Rider VBA, as described in greater detail by Ms. Grace, will
640 periodically adjust its rates to reflect changes in distribution margin due to variances in gas
641 volumes, but it will not address margin changes due to changes in numbers of customers.

¹⁰ “Impact of Conservation on Gas Margins and Financial Stability in the Gas LDC Sector,” Special Comment Report, Moody’s Investor Service, June 2005.

642 This is because a revenue decoupling mechanism should only address the effect of changing
643 gas volumes on Peoples Gas' collection of distribution margin. Therefore, the calculations
644 under Rider VBA assume that the number of customers served in each of the three applicable
645 rate classes will be the "baseline" number established in Peoples Gas' current rate case.

646 **Q. HAVE YOU EVALUATED THE EXPECTED PERFORMANCE OF PEOPLES GAS'**
647 **PROPOSED RIDER VBA BASED ON ITS RECENT EXPERIENCE WITH**
648 **DECLINING USE PER CUSTOMER AND WEATHER VARIABILITY?**

649 A. Yes. My Exhibit Peoples Gas Ex. RAF-1.5 illustrates the results of a simulation of the
650 operation of Rider VBA and the determination of the Rider VBA factors for the small
651 residential heating, small residential non-heating, and general service classes under proposed
652 rates during a six-year period. Customer billing adjustments under Rider VBA were
653 computed for the average customer in each of these rate classes as if Rider VBA was in effect
654 during this six-year period. The simulation used as a base the sales and customer levels for
655 these classes that are included in Peoples Gas' test year, the weather it experienced during its
656 last six fiscal years (2001-2006), and the annual percentage decline in average use per
657 customer experienced by Peoples Gas in its recent history.

658 **Q. PLEASE DESCRIBE THE RESULTS OF YOUR ANALYSIS FOR PEOPLES GAS'**
659 **RESIDENTIAL SERVICE CLASS.**

660 A. The analysis shown on Pages 1 and 2 of Peoples Gas Ex. RAF-1.5 presents the monthly bill
661 impacts of Rider VBA for Peoples Gas' residential non-heating and heating customers. As a
662 point of reference, the average monthly gas bill of the average-sized residential heating

663 customer is approximately \$136.00 (excluding taxes). Specifically, the maximum positive
664 Rider VBA amount during any month (bill increase) was \$6.94 in March of Year 6. The
665 heating degree-days associated with that amount were 26 percent warmer-than-normal.
666 The maximum negative Rider VBA amount (bill decrease) during any month was (\$9.10) in
667 February of Year 1. The heating degree-days associated with that amount were 36 percent
668 colder-than-normal.

669 **Q. WHAT IS THE AGGREGATE IMPACT ON CUSTOMERS' BILLS SHOWN BY**
670 **THE ANALYSIS?**

671 A. Approximately 95 percent of the average customers' monthly bill adjustments due to
672 Rider VBA during the three-year period fell within the range of (\$3.00) to \$3.00.
673 Approximately 84 percent of the average customers' monthly bill adjustments due to
674 Rider VBA during that time period fell within the range of (\$2.00) to \$2.00. During the
675 period, (i.e. 140 billing months), there are only seven months where a typical customer would
676 have received a Rider VBA bill adjustment greater than \pm \$3.00.

677 **Q. PLEASE DESCRIBE THE RESULTS OF YOUR ANALYSIS FOR THE UTILITY'S**
678 **GENERAL SERVICE CLASS.**

679 A. The analysis shown on Page 3 of Peoples Gas Ex. RAF-1.5 presents the monthly bill impacts
680 of Rider VBA for general service customers. The average monthly gas bill of the average-
681 sized general service heating customer is approximately \$929.00 (excluding taxes).
682 Specifically, the maximum positive Rider VBA amount during any month (bill increase) was
683 \$45.33 in March of Year 6. The heating degree-days associated with that amount were 26

684 percent warmer than normal. The maximum negative Rider VBA amount (bill decrease)
685 during any month was (\$58.98) in February of Year 6. The heating degree-days associated
686 with that amount were 36 percent colder than normal.

687 **Q. WHAT IS THE AGGREGATE IMPACT ON GENERAL SERVICE CUSTOMERS**
688 **SHOWN BY THE ANALYSIS?**

689 A. Approximately 90 percent of the average customers' monthly bill adjustments due to
690 Rider VBA during the three-year period fell within the range of (\$20.00) to \$20.00.
691 Approximately 70 percent of the average customers' monthly bill adjustments due to Rider
692 VBA during that time period fell within the range of (\$10.00) to \$10.00. During the period,
693 there are only seven months where a typical customer would have received a Rider VBA bill
694 adjustment greater than \pm \$20.00.

695 **Q. WHAT OVERALL CONCLUSION WOULD YOU DRAW FROM THE**
696 **FOREGOING DISCUSSED ANALYSES OF THE IMPACT OF PROPOSED RIDER**
697 **VBA?**

698 A. These results indicate that the impact of proposed Rider VBA on customers' bills will be
699 minimal. Yet in the aggregate, Rider VBA will have a significant positive impact on Peoples
700 Gas' ability to recover its authorized level of margin revenues.

701 **Q. PLEASE SUMMARIZE THE EXPECTED BILLING EFFECTS OF RIDER VBA.**

702 A. When temperatures are colder than normal, Rider VBA would result in customers' bills that
703 are lower than without Rider VBA, which provides some relief from the higher bills caused
704 primarily by the increased level of gas costs reflected on customers' bills as a result of their

705 increased gas usage. When temperatures are warmer than normal and when customers have
706 improved their energy efficiency, Rider VBA would result in customers' bills that are higher
707 than without the Rider VBA, but overall, still lower than the expected bill under normal
708 temperature conditions. This is because the customer still uses less gas – gas costs currently
709 are 65% or more of the typical annual bill. Thus, customers still realize savings associated
710 with warmer temperatures and energy efficiency and because the adjustment assumes normal
711 weather, they do not experience as large a bill increase as when weather is colder than
712 normal.

713 **Q. EVEN WITH A POSITIVE RIDER VBA FACTOR APPLIED TO CUSTOMERS'**
714 **BILLS, WHY WILL CUSTOMERS STILL REALIZE SAVINGS DURING**
715 **WARMER THAN NORMAL WEATHER?**

716 **A.** Customers generally realize significantly reduced bills during warm weather for two reasons.
717 First, a temperature-sensitive customer will have significantly reduced gas usage during
718 warmer than normal periods. Therefore, although the amount of fixed costs to be recovered
719 by Peoples Gas using Rider VBA does not change, the customer will purchase and pay for
720 less gas. Second, during warmer than normal weather conditions, commodity gas costs are
721 typically lower, and these gas costs savings are flowed through to customers.

722 **IV. PROPOSED RIDER UBA**

723 **Q. WHAT IMPACT HAS THE MAGNITUDE AND VOLATILITY OF WHOLESALE**
724 **GAS PRICES HAD ON UTILITIES' BAD DEBT EXPERIENCE?**

725 A. Numerous gas utilities have experienced higher than forecast bad debt (uncollectible
726 accounts) expense from the significant rise in customers' gas bills caused by the
727 unprecedented level of wholesale gas prices. The higher customer bills result in more
728 customers being slow or unable to pay, with resultant higher delinquent balances. More and
729 higher delinquent balances have led to greater net write-offs for the utility. Those utilities
730 that recover bad debt expense as a fixed cost component established in their base rate cases
731 have experienced in recent years an under-recovery of actual bad debt expenses, especially
732 those utilities that have not had a recent rate case.

733 Q. **HOW WOULD YOU CHARACTERIZE THIS RECENT BAD DEBT EXPERIENCE?**

734 A. The circumstances that have given rise to the greater magnitude and more volatile nature of
735 bad debt experienced by utilities are certainly challenging and are caused by events that are
736 almost entirely out of the control of the utilities. Moreover, the static and historically based
737 method upon which rates are designed renders it largely impossible for utilities to protect
738 themselves financially, except for the employment of post-bad debt measures.

739 Q. **WHAT DO YOU MEAN BY POST-BAD DEBT MEASURES?**

740 A. When bad debt spikes on a utility system such as Peoples Gas, the utility's rates only permit
741 it to collect an amount that is not representative of current experience. The only response left
742 to the utility is to employ mitigation measures that only address bad debt that has already
743 accumulated, hence my use of the term "post-bad debt measures."

744 Q. **PLEASE CONTINUE.**

745 A. These measures include credit and collection enhancements, as well as strategic management
746 of termination of service opportunities. While many utilities - including Peoples Gas - have
747 undertaken management initiatives to enhance their credit and collections activities in an
748 attempt to reduce bad debt levels, there is just so much that can be done in the face of
749 escalating gas prices and higher customer gas bills. Moreover, statutory and regulatory
750 limitations prevent service disconnection in some cases and require Peoples Gas to follow
751 specific procedures in all cases. This can increase the amount of time required to disconnect
752 service for non-payment, thus increasing bad debt.

753 Q. **HAS THE FINANCIAL COMMUNITY RECOGNIZED THE SIGNIFICANCE OF**
754 **GAS UTILITIES' BAD DEBT?**

755 A. Yes. In October 2005, Citigroup Research, a division of Citigroup Global Markets,
756 conducted a survey ¹¹ of 42 publicly traded gas utilities in order to determine the impact of
757 high natural gas prices on bad debt expense for 2005 and 2006. Citigroup found that about
758 43 percent of the utilities it surveyed have ratemaking mechanisms that alleviate some bad
759 debt concerns. The impact to earnings from higher gas prices generally is the “result of
760 utilities obtaining rate relief in the form of bad debt trackers in recent years.” Citigroup
761 listed thirteen (13) utilities that have some sort of regulatory mechanism in place to recover
762 most or all bad debt. The report notes “the lack of trackers in the rest of the U.S. is
763 discouraging given the trend in natural gas prices over the last several years.” Citigroup

¹¹ Citigroup Global Markets, “Integrated Natural Gas & Gas Utilities – How Bad Will Bad Debt Expense Be?”
– October 20, 2005.

764 estimated that the highest impact on earnings due to bad debt expense would be to those
765 utilities that have a combination of high heating load, a high percentage of uncollectibles and
766 a lack of regulatory relief. The report specifically noted that utilities in Illinois face the
767 highest potential impact to earnings, with a 17 percent level identified for Peoples Energy
768 Corporation.

769 **Q. HAS PEOPLES GAS EXPERIENCED A SIMILAR INCREASE IN THE**
770 **MAGNITUDE AND VOLATILITY OF ITS BAD DEBT EXPENSES COMPARED**
771 **TO THE EXPERIENCES OF OTHER GAS UTILITIES THAT YOU JUST**
772 **DISCUSSED?**

773 A. Yes. Mr. Bogard's Exhibit Peoples Gas Ex. LTB-1.5 illustrates the magnitude and volatility
774 of Peoples Gas' bad debt over the last ten (10) years. You can readily observe that when
775 natural gas prices increased significantly in 2001, there was an equivalent increase in the bad
776 debt expense level for Peoples Gas. In addition, over the last five years, it is evident that a
777 larger portion of Peoples Gas' bad debt expense was driven by its purchased gas costs rather
778 than by its base rates (*i.e.*, service and distribution charges).

779 **Q. HOW WILL THE PROPOSED RIDER VBA ADDRESS THE BUSINESS**
780 **CHALLENGES YOU HAVE DESCRIBED FOR PEOPLES GAS?**

781 A. Uncollectible accounts are a rising and recurring business expense for Peoples Gas. The
782 level of bad debt is a reflection of economic conditions that exist from time to time, the level
783 of gas commodity and delivery prices, and the demographics of Peoples Gas' service
784 territory. As a result, bad debt is a utility operating expense that is uncontrollable, highly

785 variable and unpredictable. Peoples Gas' inability to sufficiently recover bad debt expense
786 on a timely basis contributes to its financial condition. Peoples Gas' proposed Rider UBA
787 will provide it with the ability to recover the ongoing level of bad debt expenses related to
788 purchased gas costs that are largely uncontrollable, variable and of an unpredictable nature,
789 particularly in an environment of widely fluctuating gas costs. In addition, to the extent that
790 gas commodity prices could moderate in the future, the mechanism will immediately
791 recognize in customers' bills any decrease in Peoples Gas' bad debt expense level caused by
792 such price changes.

793 **Q. PLEASE DESCRIBE THE CONCEPTUAL UNDERPINNINGS OF PEOPLES GAS'**
794 **PROPOSED RIDER UBA.**

795 A. Peoples Gas has proposed through Rider UBA a monthly volumetric adjustment, to be
796 applied to company supplied gas, to recover gas cost related bad debt expense. The
797 adjustment will be computed by applying Peoples Gas' allowable uncollectible expense
798 percentage (as approved by the Commission in this proceeding) to its monthly gas cost
799 related revenues (*i.e.*, gas charge revenues). Peoples Gas' non-gas cost portion of
800 uncollectible expense will continue to be recovered through base rates. This type of
801 ratemaking solution was discussed by Citigroup (in its previously cited report) and is an
802 approach that has been approved by utility regulators in other states. For those utilities
803 included in the Citigroup survey, the report stated that, "the relatively mild impact to
804 earnings from higher gas prices and higher bad debt levels is generally a result of utilities
805 obtaining rate relief in the form of bad debt trackers in recent years."

806 Q. **WHY HAS PEOPLES GAS CHOSEN TO STRUCTURE ITS RECOVERY OF BAD**
807 **DEBT COSTS IN THIS MANNER?**

808 A. Peoples Gas structured its Rider UBA to recognize that its bad debt expenses are volatile,
809 unpredictable and largely uncontrollable. Peoples Gas concluded that the portion of bad debt
810 expense that is the largest and that is the most volatile, unpredictable, and uncontrollable is
811 the portion related to its purchased gas costs. Therefore, Peoples Gas has chosen to propose
812 to recover that portion of its bad debt expense through a ratemaking adjustment mechanism.

813 At the same time, because Peoples Gas' bad debt expense level is at an all time high level,
814 its customers will benefit from lower bad debt levels as gas prices decline through the use of
815 a ratemaking adjustment mechanism. Finally, Peoples Gas concluded it should remain at risk
816 for a portion of its bad debt expense to ensure it continues to focus on its credit and
817 collections activities in an effort to effectively manage its bad debt and write-off levels.

818 Q. **PLEASE INDICATE WHICH STATE UTILITY REGULATORS HAVE APPROVED**
819 **THE CONCEPT OF A BAD DEBT RATEMAKING MECHANISM TO ENABLE A**
820 **UTILITY TO RECOVER ITS ACTUAL BAD DEBT EXPENSES.**

821 A. Utility regulators have approved bad debt ratemaking mechanisms for seventeen (17) gas
822 utilities in the following ten (10) states: Maine, Massachusetts, New Hampshire, New York,
823 North Carolina, Ohio, Rhode Island, Tennessee, Utah, and Wyoming.

824 Q. **PLEASE EXPLAIN THE KEY ELEMENTS OF PEOPLES GAS' PROPOSED**
825 **RIDER UBA.**

826 A. Peoples Gas' proposed Rider UBA, which is discussed in greater detail by Ms. Grace, would
827 compute a monthly adjustment to reflect changes in the purchased gas cost portion of
828 uncollectible expenses. The amount recoverable under this Rider will be a function of the
829 level of purchased gas costs incurred by Peoples Gas in recognition of the fact that this
830 expense component is volatile, unpredictable, and largely uncontrollable, very similar to the
831 characteristics exhibited by the utility's purchased gas costs.

832 V. **PROPOSED RIDER EEP**

833 Q. **HOW WILL THE PROPOSED RIDER EEP ADDRESS THE BUSINESS**
834 **CHALLENGES YOU HAVE DESCRIBED FOR PEOPLES GAS?**

835 A. Peoples Gas' proposed Rider EEP will provide for funding for the costs of energy
836 conservation and efficiency programs for its customers commensurate with the
837 implementation of each program through qualified, independent third-party administrator(s).
838 This ratemaking proposal is a necessary complement to Peoples Gas' proposed energy
839 conservation and efficiency programs. Rider EEP ensures that the defined level of funding is
840 made available on an ongoing basis to the chosen service providers and that the utility's
841 applicable customers will be charged only for the program costs actually incurred as the types
842 and mix of implemented programs changes over time.

843 Q. **IS IT IMPORTANT FOR A UTILITY SUCH AS PEOPLES GAS TO BE PROVIDED**
844 **WITH THE ASSURED RECOVERY OF ITS ACTUAL PROGRAM COSTS?**

845 A. Yes. According to the ACEEE, program cost recovery is considered to be “an essential
846 factor in order to achieve utility-sector energy efficiency programs.”¹² There should be a
847 clear, reliable, and timely regulatory process in place to ensure the recovery of these ongoing
848 expenditures. A ratemaking mechanism that ensures predictable and timely recovery of
849 energy efficiency and conservation program costs is particularly important for Peoples Gas
850 because there are added uncertainties surrounding the precise timing of the rollout of its
851 energy efficiency and conservation programs. This programmatic uncertainty makes it
852 difficult to develop a point specific amount to represent each year’s cost of program
853 implementation. As a result, I believe it is appropriate and necessary for Peoples Gas to have
854 the ability to recover such costs through a ratemaking mechanism that can accommodate the
855 anticipated variations in budgeted versus actual costs from year to year.

856 **Q. HAVE OTHER UTILITIES RECEIVED REGULATORY APPROVAL TO**
857 **RECOVER THE DIRECT COSTS OF THEIR ENERGY EFFICIENCY AND**
858 **CONSERVATION PROGRAMS THROUGH TARIFF PROVISIONS OTHER THAN**
859 **BASE RATES?**

860 A. Yes. There are many examples of utilities, in states such as Idaho, Massachusetts,
861 Minnesota, Vermont, and Washington, that have received regulatory approval to recover the
862 direct costs of their energy efficiency and conservation programs through tariff provisions

¹²“Aligning Utility Interests with Energy Efficiency Objectives: A Review of Recent Efforts at Decoupling and Performance Incentives,” American Council for an Energy Efficient Economy, Report Number U061, October 2006, page 7.

863 such as automatic adjustment riders or separate public benefits charges. In either case, there
864 is an explicit recognition by the regulator that assured recovery of such costs is a necessary
865 step in addressing the barriers many utilities face to investing in more energy efficiency.

866 Q. **PLEASE EXPLAIN THE KEY ELEMENTS OF PEOPLES GAS' PROPOSED**
867 **RIDER EEP.**

868 A. Peoples Gas' proposed Rider EEP, which is described in greater detail by Ms. Grace,
869 provides for funding of a portfolio of conservation programs that will be available to small
870 residential heating and general service customers. The rider also prescribes the
871 determination of the monthly charge per customer that is derived from the annual budget for
872 program funding purpose.

873 **VI. PROPOSED RIDER ICR**

874 Q. **HOW WILL THE PROPOSED RIDER ICR ADDRESS THE BUSINESS**
875 **CHALLENGES FACED BY PEOPLES GAS?**

876 A. Peoples Gas' proposed Rider ICR will provide it with a current basis to recover the recurring
877 capital-related costs of its proposed accelerated CI/DI main replacement program. Mr.
878 Doerk will describe Peoples Gas' ongoing replacement program and the replacement criteria
879 in more detail in his testimony. From a strict ratemaking perspective, Rider ICR will enable
880 Peoples Gas to take advantage of more opportunities as they arise to replace portions of its
881 gas system without the negative financial consequences such business actions would create
882 under traditional ratemaking methods.

883 Q. **PLEASE EXPLAIN WHY IT IS NOT APPROPRIATE TO RECOVER THESE**
884 **PROGRAM COSTS THROUGH PEOPLES GAS' BASE RATES?**

885 A. If the costs of Peoples Gas' proposed accelerated replacement program were recovered
886 through base rates, only the historical costs of the program would be includable at the time of
887 the rate case. To the extent Peoples Gas was provided with opportunities to accelerate its
888 pipe replacement process, by the types of unpredictable business events discussed by Mr.
889 Schott in his testimony, the additional costs of replacement would not be recoverable in base
890 rates until the completion of Peoples Gas' next rate case. Under this approach, the benefits
891 of longer-term cost savings from accelerated replacement described by Mr. Schott might not
892 be achievable with the increased financial burden placed on Peoples Gas.

893 Q. **HAVE OTHER UTILITIES RECEIVED REGULATORY APPROVAL TO**
894 **RECOVER THE RECURRING CAPITAL COSTS ASSOCIATED WITH THEIR**
895 **VARIOUS INFRASTRUCTURE IMPROVEMENT INITIATIVES THROUGH**
896 **RATEMAKING MECHANISMS SIMILAR TO PEOPLES GAS' RIDER ICR?**

897 A. Yes. Utility regulators have approved similar infrastructure cost recovery mechanisms for
898 ten (10) gas utilities in the following eight (8) states: Alabama, Arkansas, Georgia, Kentucky,
899 Missouri, Ohio, Oregon, and Texas.

900 Q. **PLEASE EXPLAIN THE KEY ELEMENTS OF PEOPLES GAS' PROPOSED**
901 **RIDER ICR.**

902 A. Peoples Gas' proposed Rider ICR, which is discussed in greater detail by Ms. Grace, would
903 compute an annual adjustment (that will be billed on a monthly basis) to reflect the

904 incremental capital-related costs associated with Peoples Gas’ proposed accelerated CI/DI
905 main replacement program. The amount recoverable under this Rider will be a function of
906 any differences between the “baseline” levels of capital expenditures of the program included
907 in this rate case and the actual expenditures made by Peoples Gas in each succeeding year.

908 **VII. CONCLUDING REMARKS**

909 **Q. PLEASE SUMMARIZE THE BENEFITS TO PEOPLES GAS AND ITS**
910 **CUSTOMERS OF IMPLEMENTING ITS PROPOSED RATEMAKING**
911 **MECHANISMS.**

912 **A.** There are several significant benefits from implementing Peoples Gas’ proposed ratemaking
913 mechanisms, including:

914 1. Rider VBA will break the link between the gas consumption of Peoples Gas’
915 customers and its earnings and result in a better alignment of the interests of
916 the utility and its customers. Under Rider VBA, Peoples Gas will be able to
917 promote energy conservation and efficiency programs for its customers
918 without the continual real threat of margin losses due to declining gas sales
919 per customer.

920 2. Rider VBA will mitigate the impact of significantly colder than normal
921 weather on customers’ bills and reduce the utility’s risk of lower earnings, if
922 the weather is warmer than normal. During those periods when a customer’s
923 gas usage and resulting bill are relatively high, Rider VBA will create a slight
924 downward adjustment in the customer’s bill. In warmer than normal

925 weather, when a customer's gas usage and resulting bill are relatively low,
926 there will be a slight upward adjustment in the customer's bill.

927 3. By decreasing the delivery charges when it is colder than normal, Rider VBA
928 mitigates against the adverse financial impact on customers of higher gas
929 consumption with cold weather when gas prices are at their highest level.

930 4. With the implementation of Rider VBA, customers will pay each year
931 approximately the same amount for gas delivery service as if Peoples Gas had
932 experienced normal weather and no incremental energy conservation by its
933 customers, which is the same basis upon which the Commission establishes
934 the utility's base rates. Ultimately, this Rider will result in a heating
935 customer's bill more accurately reflecting the margin recovery amounts
936 approved by the Commission in this rate case, while customers will recognize
937 the results of their energy conservation efforts and the impacts of warmer
938 than normal weather in the amount they pay for gas supply service.

939 5. Rider VBA will benefit Peoples Gas and its customers by reducing the
940 volatility of the base rates, delivery charge portion of customer bills and
941 utility revenues due to variations primarily from normal weather and gas
942 commodity costs.

943 6. Rider VBA may lessen the need for Peoples Gas to file future rate cases
944 because of the enhanced opportunity to recover its Commission-approved
945 revenue requirement which can lead to reduced rate case expense that
946 benefits all customers.

- 947 7. Rider EEP will benefit customers by providing funding for the costs of
948 conservation and energy efficiency programs, including programs tailored to
949 low income customers.
- 950 8. Rider UBA will provide a balanced ratemaking mechanism that will enable
951 Peoples Gas' customers to benefit from a lower uncollectible level as
952 purchased gas costs decline and will enable the utility to recover related bad
953 debt expense should purchased gas costs increase.
- 954 9. Rider ICR is consistent with the infrastructure improvement objectives
955 associated with Peoples Gas' proposed accelerated CI/DI pipe replacement
956 program and suitably provides for incremental cost recovery that would not
957 be provided for in base rates.

958 **Q. MR. FEINGOLD, DO YOU HAVE ANY FINAL RECOMMENDATIONS**
959 **REGARDING PEOPLES GAS' PROPOSED RATEMAKING MECHANISMS?**

960 **A.** Yes, I do. In my professional opinion, the ratemaking mechanisms proposed by Peoples Gas
961 are necessary and appropriate to solve the chronic business challenges faced by the utility
962 that I discussed earlier. These proposed ratemaking mechanisms are conceptually sound,
963 would provide significant benefits to Peoples Gas and its gas customers, would promote
964 energy conservation and efficiency, and address a fundamental deficiency in utility
965 ratemaking. Moreover, the proposed Rider VBA is a ratemaking approach which is broadly
966 endorsed by national and local policy makers, energy trade associations, NARUC,
967 environmental organizations, and members of the financial community to facilitate further

968 promoting and expanding the energy efficiency programs offered by gas utilities that are so
969 critical to their customers' ability to moderate the impact of rising energy prices. For these
970 reasons, I urge this Commission to approve Peoples Gas' proposed ratemaking mechanisms.

971 Q. **MR. FEINGOLD, DOES THIS COMPLETE YOUR DIRECT TESTIMONY?**

972 A. Yes, it does.