STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

NORTH SHORE GAS COMPANY	:	
	:	
Proposed General Increase	:	No. 09-____
In Rates For Gas Service	:	

Direct Testimony of

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I. INTRODUCTION AND WITNESS QUALIFICATIONS

A. Identification of Witness

Q. Please state your name and business address.

A. My name is Valerie H. Grace. My business address is 130 E. Randolph Drive, Chicago, Illinois 60601.

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

A. I am employed by Integrys Business Support, LLC ("IBS"), a wholly-owned subsidiary of Integrys Energy Group, Inc. ("Integrys") as Manager of the Gas Regulatory Services Department.

B. Purpose of Testimony

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to explain and analyze the changes proposed to North Shore Gas Company's ("North Shore") Schedule of Rates for Gas Service, provide support for the proposed changes, and to discuss the new rates and riders that have been filed as a part of this proceeding. I will also address adjustments made to test year billing units.

C. Summary of Conclusions

Q. Please summarize your conclusions.

A. I conclude that North Shore's proposed rate design is just and reasonable, and while better aligning revenues with costs and recovering the revenue requirement, also comports with the Illinois Commerce Commission's (the "Commission" or "ICC") objectives of continuity and gradualism in changing rate design. North Shore's proposed changes to its tariffs, charges, and riders are also appropriate and reasonable.

D. Itemized Attachments to Direct Testimony

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

A. Yes. I sponsor the following exhibits:

1. North Shore Exhibit ("Ex.") VG-1.1 sets forth the tariff sheets which include the proposed revisions to North Shore's Schedule of Rates for Gas Service, ILL. C.C. No. 17 (the "tariff" or "Schedule of Rates").
2. North Shore Ex.VG-1.2 is a Summary of Revenues under Present and Proposed Rates for each service classification.
3. North Shore Ex. VG-1.3 reflects North Shore's proposed method for allocating its revenue requirement among the various service classifications.
4. North Shore Ex. VG-1.4 reflects a comparison of present and proposed rates for affected North Shore service classifications, riders and miscellaneous charges.
5. North Shore Ex. VG-1.5 provides a summary of the unit costs for Service Classification ("S.C.") No. 1, Small Residential Service.
6. North Shore Ex. VG-1.6 provides the bill impacts for the average S.C. No. 1 sales customer and transportation customer under present and proposed rates, assuming normal weather.
7. North Shore Ex. VG-1.7 provides a summary of embedded fixed unit costs for S.C. No. 2, General Service.
8. North Shore Ex. VG-1.8 provides North Shore's Schedule E-9 of its standard filing requirements in this proceeding. It shows bill impacts for S.C. Nos. 1 and

2, as well as S.C. No. 3, Large Volume Demand Service; and S.C. No. 5, Standby Service, at various usage levels under present and proposed rates.

9. North Shore Ex. VG-1.9 provides a summary of the cost analysis supporting the proposed rates for miscellaneous charges in North Shore's Terms and Conditions of Service.

10. North Shore Ex. VG-1.10 reflects the cost analysis that supports rate proposals for Rider FST, Full Standby Transportation; Rider SST, Selected Standby Transportation; Rider P, Pooling Service; and Rider AGG, Aggregation Service.

11. North Shore Ex. VG-1.11 reflects the cost analysis which supports the storage credit for Rider AGG.

12. North Shore Ex. VG-1.12 reflects the cost analysis which supports the number of proposed Allowable Bank Base Rate Days for Riders FST, SST and AGG.

13. North Shore Ex. VG-1.13 reflects the derivation of the Uncollectible Factors for Rider UEA, Uncollectible Expense Adjustment.

14. North Shore Ex. VG-1.14 provides an example, based on the most recent year for which filed information is available, of the supporting data that would be filed with the Commission to implement charges under proposed Rider FCA, Franchise Gas Adjustment.

Q. Were North Shore Exs. VG-1.1 through VG-1.14 prepared by you, or under your supervision and direction?

A. Yes, they were.

E. <u>Background and Experience</u>

Q. How long have you been employed by IBS?

A. I have been employed by IBS since January 2008 and previously was employed by Peoples Energy Corporation ("Peoples Energy") and its subsidiaries, affiliates of IBS, for over 28 years.

Q. What are your responsibilities in your current position?

A. As the Manager of the Gas Regulatory Services Department, I am responsible for performing and managing activities related to rate research, rate design, rate and tariff administration, and for developing recommendations regarding rate policies for North Shore and The Peoples Gas Light and Coke Company ("Peoples Gas").

Q. Please summarize your educational background and experience.

A. In 1980, I graduated from Illinois State University with a Bachelor of Science degree in Business Administration. In 1988, I received a Master of Management Degree from Northwestern University. I have been employed by IBS and two affiliated companies from September 1980 to the present. I began my employment at Peoples Gas in the Gas Supply Planning Department. Since then, I have been employed in various positions and levels of responsibility at Peoples Gas including the Rates Department, the Office of the Chairman, the Executive Office of the Customer Relations Division and the Gas Transportation Services Department. I have also been employed by Peoples Energy, the parent company of Peoples Gas and North Shore and a wholly-owned subsidiary of Integrys, as Director of Strategic Development. I have been in my present position since the merger between Peoples Energy and Integrys (formerly, WPS Resources Corporation) in February, 2007.

Q. Have you testified before the Commission previously?

A. Yes, I have testified in several gas charge reconciliation proceedings, proceedings related to customer choice, the Section 7-204 merger proceeding (ICC Docket No. 06-0540) involving Peoples Energy and Integrys and the recent general rate increase proceedings for North Shore and Peoples Gas (ICC Docket Nos. 07-0241/07-0242 (cons.)).

II. SCHEDULE OF RATES FOR GAS SERVICE

Q. Will North Shore give public notice of the proposed changes it filed?

A. Yes. Notice will be published twice in the Waukegan News-Sun, a newspaper of general circulation in the area which North Shore serves, in accordance with the provisions of 83 Illinois Administrative Code Part 255. North Shore will submit for the record copies of the Publisher's certification that public notice of the changes was published in the Waukegan News-Sun. Copies of the proposed changes are on file and open for public inspection at North Shore's corporate office. North Shore has also posted public notice of the proposed changes in its corporate office.

Q. Is North Shore proposing changes to its Schedule of Rates for Gas Service, ILL. C.C. No. 17?

A. Yes, North Shore Ex. VG-1.1 contains copies of the tariff sheets filed by North Shore in this proceeding. In my testimony and exhibits, the term "proposed changes" will refer to the rate levels and other changes reflected in these tariff sheets.

III. RATE DESIGN OBJECTIVES

Q. What are the objectives that North Shore seeks to achieve through the rate design modifications it is proposing?

A. Through the proposed rate design, North Shore would accomplish seven major objectives. They are to (1) recover North Shore's revenue requirement, (2) better align revenues with underlying costs, (3) send the proper price signals, (4) provide more equity between and within rate classes, (5) maintain rate design continuity, (6) reflect gradualism and (7) retain customers on North Shore's system.

IV. INCREASE AMOUNT AND ALLOCATION OF THE REVENUE REQUIREMENT

Q. Please describe North Shore Ex. VG-1.2, Summary of Revenues under Present and Proposed Rates.

A. North Shore Ex. VG-1.2 shows revenues arising from present and proposed rates from various revenue sources. Column K of the exhibit shows the increase in base rate revenues arising from proposed charges for North Shore's various service classifications ($21.9 million, line 26), and from other base rate charges and items ($98,000, line 30), for a total base rate increase of $22.0 million (line 31). The exhibit also shows pass-through revenues arising from North Shore's (1) Rider 2, Gas Charge as well as gas charge related charges in North Shore's transportation riders; (2) Rider 11, Adjustment for Incremental Costs of Environmental Activities; and (3) Rider EEP, Enhanced Efficiency Program. It does not reflect any revenues that would arise from North Shore's proposed Rider UEA, Uncollectible Expense Adjustment, and Rider FCA, Franchise Cost Adjustment. It also excludes municipal and state taxes and other state charges.

Q. Would the revenues shown in North Shore Ex. VG-1.2 change if the Commission approved Rider UEA?

A. Yes, if the Commission were to approve Rider UEA, the revenue requirement and any resulting revenues would be reduced by the gas cost related Account No. 904 Uncollectible Accounts expenses as such costs would be recoverable through the rider. The affected amount is discussed later in my testimony.

Q. What is the basis of North Shore's determination of rates to be proposed in this proceeding?

A. North Shore uses an Embedded Cost of Service Study ("ECOSS") as the basis for the determination of the revenue requirement and resulting proposed rates in this proceeding. The ECOSS has been submitted as North Shore Exs. JCHM-1.1 through JCHM-1.9 and is sponsored by Ms. Joylyn Hoffman Malueg (North Shore Ex. JCHM-1.0).

Q. Please discuss any tariff proposals that are incorporated in the ECOSS under proposed rates.

A. The ECOSS under proposed rates reflects a proposal to eliminate S.C. No. 5, Standby Service as well as a proposal to place eligibility requirements, based on usage, for customers taking service under S.C. No. 2, General Service. These proposals resulted in the transfer of all customers and their related costs from S.C. No. 5 to S.C. No. 2 and the transfer of certain customers from S.C. No. 2 to S.C. No. 3, Large Volume Demand Service. These proposals are discussed later in my testimony.

Q. How does North Shore use the ECOSS to determine the proposed rates?

A. North Shore uses the ECOSS to move toward cost based rates and to better align charges and resulting revenues with like costs. The results of the ECOSS are used to increase rates for S.C. Nos. 1, 2 and 3, setting all at cost. North Shore Ex. VG-1.3 shows the allocation of the revenue requirement and rate increase for all service classes. North Shore has set all its service classifications at cost since its rate case in ICC Docket No. 91-0010.

Q. Does the proposed rate design equalize rates of return and ratios of revenue to cost among the service classifications?

A. Yes.

Q. Have any of North Shore’s service classifications been omitted from the cost of service analyses filed in this case, and from consideration for an increase in rates?

A. Yes, S.C. No. 4, Contract Service to Prevent Bypass, was excluded from consideration, because the revenues from customers served under this service classification are based on a negotiated rate rather than the cost of service analysis filed in this case. These contracts have been filed with the Commission. Revenues arising from S.C. No. 4 are credited back to other service classifications in the ECOSS, thereby lowering their costs. S.C. No. 6, Contract Service For Electric Generation, was also excluded as there are currently no customers being served under this service classification, and in any event, this is also a negotiated rate service.

V. CHANGES TO BASE RATES AND OTHER CHARGES

Q. How is North Shore proposing to meet its objective to better align revenues with underlying costs?

A. To meet this objective, North Shore is proposing to recover a greater portion of its fixed costs through fixed charges. Almost all of North Shore's costs, about 99.2%, are fixed, *i.e.*, they do not vary with the volume of gas delivered to customers. However, in the interest of rate design continuity, North Shore has historically recovered a large portion of such fixed costs through non-fixed volumetric charges. For instance, in North Shore's rate case filed fourteen years ago in ICC Docket No. 95-0031, about 97% of North Shore's costs were also fixed. However, only 28% of costs were recovered through fixed charges. North Shore reduced this mismatch in ICC Docket No. 07-0241, whereby its fixed cost recovery under present rates would increase to 50% in test year 2010. However, a continued mismatch of fixed costs and non-fixed charges would practically assure that North Shore will either recover more or less than its Commission approved revenue requirement from customers. To remedy this, at least partially, and to meet its objective to earn its revenue requirement, North Shore is proposing rates that would recover about 56% of its fixed costs through fixed charges. This modest, but necessary, increase in fixed cost recovery is well below the fixed cost recovery of 80% approved by the Commission in recent proceedings for the Ameren Illinois gas utilities (ICC Docket Nos. 07-0585 - 07-0590, (cons.)). While not yet completely matching fixed costs and fixed charges, North Shore's proposed rates will provide more balance than its present rates and will send more appropriate price signals to customers about the largely fixed costs underlying its delivery service.

Q. Consistent with the objectives you described above and the move towards placing more fixed cost recovery in fixed charges, what major changes to rates and charges is North Shore proposing?

A. North Shore is proposing six major changes to its base rates and other charges. I will discuss these changes in detail later in my testimony.

First, S.C. No. 1 will reflect different monthly customer charges for sales and transportation customers. The customer charges will increase for both types of customers. The distribution charge will be the same for sales and transportation customers and will reflect increases in both blocks of the two-block rate structure.

Second, a third meter class will be added for S.C. No. 2, and different customer charges will be set for sales and transportation customers. The customer charge will be increased for all three meter classes and both types of customers. The distribution charge, which will be the same for sales and transportation customers, will reflect changes in all three blocks. Sales customers will see a decrease in the first two blocks and an increase in the third block of the three-block rate structure. Transportation customers will see a decrease in the first block and increases in the second and third block of the three-block rate structure. S.C. No. 2 will only be available to customers who consume an average of 41,000 monthly therms or less, determined annually based on the most recent two calendar year period. Higher usage customers would take service under S.C. No. 3.

Third, the monthly customer charge, demand charge, standby service charge and the distribution charge for S.C. No. 3 will be changed. The demand charge will be changed from a declining block to a flat rate. The distribution charge and standby service charge will be increased. This service classification is set at cost. Setting this service classification at cost will help North Shore to meet its objective of maintaining customers on the system.

Fourth, S.C. No. 5, Standby Service, will be eliminated with all customers being transferred to S.C. No. 2. S.C. No. 2 will be revised to remove a prohibition on standby service under that service classification.

Fifth, certain service reconnection charges and service activation charges will be increased toward cost.

Sixth, certain administrative charges related to North Shore's transportation programs will be reduced and a credit related to storage will be increased.

Q. Are the present and proposed charges under each service classification summarized in an exhibit?

A. Yes. North Shore Ex. VG-1.4, Comparison of Present and Proposed Rates shows the proposed charges for each service classification. The exhibit also shows this information for the transportation riders and the miscellaneous charges included in the Terms and Conditions of Service. Lastly, the exhibit shows the increase or decrease in proposed rates as compared to present rates.

A. S.C. No. 1, Small Residential Service

Q. Please describe North Shore's proposal to differentiate customer charges for S.C. No. 1.

A. North Shore is proposing to set different customer charges for sales and transportation customers rather than different distribution charges for such customers as the rates are presently set. In ICC Docket No. 07-0241, North Shore and Staff agreed to, and the Commission approved, different distribution rates for sales and transportation customers. This differentiation was made so that rates for transportation customers, who buy their gas from gas suppliers other than North Shore, would not include gas cost related Account No. 904 Uncollectible Accounts expenses. While it still agrees with this differentiation, North Shore believes that such differentiation should be reflected in the customer charge.

Q. Why should it be reflected in the customer charges?

A. There are two reasons for this. First, North Shore's ECOSS classifies Account No. 904 costs as customer costs, so they are included in the customer charge. Therefore, it is appropriate that the customer charge rather than the distribution charge reflect the differentiation. Second, S.C. No. 1 customers have migrated in large numbers from sales to transportation service. The present distribution charge differentiation, which is based on sales and transportation volumes in a fiscal 2006 test year, is skewed based on the large migration since the test year in the last rate case. Reflecting the differentiation in the customer charge would assure that gas cost related Account No. 904 Uncollectible Accounts expenses would properly migrate with the customer.

Q. Please describe North Shore's proposals for S.C. No. 1 customer and distribution charges.

A. North Shore is proposing to increase the monthly customer charge for S.C. No. 1 from $13.50 to $19.90 for sales customers and from $13.50 to $19.00 for transportation customers. This difference of $.90 ($19.90 - $19.00, each rounded to the nearest 10 cents) arises from gas cost related Account No. 904 Uncollectible Accounts expenses (about $.90 for sales customers and $.05 for transportation customers). North Shore is also proposing Rider UEA, Uncollectible Expense Adjustment, which would recover gas cost related Account No. 904 Uncollectible Accounts expenses through the rider rather than base rates. If the Commission were to approve this proposal, the customer charge for sales and transportation customers would be the same at $19.00 per month. This charge reflects the removal of all gas cost related Account No. 904 Uncollectible

Accounts expenses. North Shore Ex. VG-1.5 compares proposed monthly customer charges under S.C. No. 1 with the embedded monthly customer and demand costs per customer. As shown in the exhibit, the customer cost for S.C. No. 1 is $24.88 and the demand cost per customer is $11.14 for a total fixed cost per customer of $36.02 (lines 1-3). In the interest of gradualism, North Shore is proposing to set the customer charges for S.C. No. 1 below its embedded customer costs. In the interest of rate design continuity, North Shore is proposing to recover all demand costs through volumetric distribution rates rather than a fixed charge such as the customer charge. This results in only 55% of fixed costs for S.C. No. 1 being recovered through fixed charges.

Q. Why should the demand costs be included in a fixed monthly charge such as the customer charge?

A. Both demand and customer costs are fixed, meaning they do not vary with the amount of gas that North Shore delivers to its customers. Demand costs are typically recovered from large volume customers through demand charges. This is feasible because such customers normally have demand meters that allow for accurate measurement of daily demand volumes. However, demand meters and demand charges are uncommon for smaller volume customers, and the cost for demand meters would add additional costs to the customer charge. As a result, it would be more practical to recover demand costs through a fixed monthly charge such as the customer charge.

Q. Has North Shore proposed any changes to its S.C. No. 1 distribution charge blocking?

A. No. North Shore is proposing to maintain its two declining rate block structure for S.C. No. 1. The front block (0-50 therms) proposed distribution charge is 29.260 cents per therm and was computed by allocating two-thirds of remaining customer, demand and commodity costs to this block. The remainder of the S.C. No. 1 revenue will be collected through an end block (over 50 therms) distribution charge of 8.224 cents per therm.

Q. Will North Shore's proposals for S.C. No. 1 have any effect on the calculation of adjustments under Rider VBA, Volume Balancing Adjustment?

A. Yes. North Shore's proposed revenue increase and rate designs will result in new distribution rates and Rate Case Margins ("RCM") for Rider VBA. Under present rates, RCM differs for sales and transportation customers since their distribution rates differ. As North Shore is proposing the same distribution rates for sales and transportation customers, the RCM and adjustments determined under Rider VBA will be the same for S.C. No. 1 sales and transportation customers.

Q. Please describe how North Shore S.C. No. 1 customers have been impacted by Rider VBA to date.

A. North Shore's Rider VBA became effective May 1, 2008. From May, 2008 through February, 2009, about $475,000 will have been refunded to North Shore S.C. No. 1 customers.

Q. Why is North Shore proposing to increase its monthly customer charges, given that its decoupling mechanism, Rider VBA, was approved in its last rate case?

A. Increasing the customer charge would better align the charge with its underlying costs and would also reduce the magnitude of adjustments that would need to be generated under Rider VBA. In addition, Rider VBA was approved on a pilot basis, with the pilot set to expire in March, 2012, unless the Commission grants permission for it to be permanent in a general rate proceeding. If the Commission does not permanently approve Rider VBA before its sunset date, the S.C. No. 1 customer charge would be well below its embedded fixed cost in 2012.

North Shore's proposal to increase its customer charge is also consistent with policies endorsed by the Commission in several rate proceedings. In ICC Docket No. 95-0032 the Commission urged Peoples Gas to increase the customer charge in future rate proceedings to move it closer to cost. In ICC Docket Nos. 07-0241/07-0242 (Cons.), the Commission found it appropriate that rates reflect a greater recovery of fixed costs in customer charges. In a case involving Union Electric (ICC Docket No. 03-0009), the Commission endorsed the utility's efforts to recover all of a utility's fixed customer related costs of serving residential customers through the customer charge component of rates as well as a gradualism approach to doing so. Lastly, as mentioned previously, the Commission allowed the Ameren gas utilities (ICC Docket Nos. 07-0585 - 07-0590, (Cons).) to recover, for its residential (GDS-1) and small commercial (GDS-2) rate classes, 80% of their fixed costs through the customer charge on a permanent, rather than a pilot, basis.

Q. Why doesn't North Shore simply propose Straight Fixed Variable ("SFV") rates that would recover all, or nearly all fixed costs through fixed charges?

A. North Shore does consider SFV rates the most appropriate rate design to best align revenue recovery with its mostly fixed costs. However, while SFV rates would offer stability to North Shore and its customers as well as eliminate the need for a decoupling rider such as Rider VBA, some may view SFV rates as too significant a departure from North Shore's current rate structure. North Shore Ex. VG-1.5, line 5, reflect the monthly SFV rate of $36.02 that would arise from North Shore's ECOSS. I note that the SFV rate structure is widely used in other industries. For example, many customers are accustomed to paying flat cable, telephone (local, long distance and wireless), internet services, and sewer and waste disposal bills, among others. Many of these service providers, who had traditionally charged on a volumetric basis, are now charging a flat fee.

Q. What benefits would a flat fee such as a SFV rate offer?

A. A SFV rate would be equivalent to putting customers on a budget plan for the delivery service portion of their bill but without any need for a true-up when conditions change. Customers would pay a fixed monthly fee and a small distribution charge and the delivery portion of their bill would be largely unaffected by variations in weather or other conditions. As a result, they would not over or under pay for the services that they receive. A SFV rate would also lower the delivery charge portion of a customer's bills during the winter period when gas usage and market commodity prices are typically at their highest. A SFV rate would be especially beneficial to high usage customers who live in energy inefficient housing, particularly those who are low income, as with SFV, the delivery charge portion of the bill would be almost entirely fixed, with usage being affected by a very small volumetric charge.

Q. Would North Shore consider a SFV rate design if it is accepted or proposed by other parties in this proceeding?

A. Yes.

Q. Please describe North Shore Ex. VG-1.6.

A. North Shore Ex. VG-1.6 illustrates the effect of the proposed charges on an average S.C. No. 1 sales customer and an average S.C. No. 1 transportation customer, assuming normal weather. The average monthly bill for a S.C. No. 1 sales customer and a transportation customer will increase by about $9.91 and $9.09, respectively (lines 14 and 28, col. M). The annual bill will increase by about 6.4% for sales customers and about 5.9% for transportation customers (lines 13 and 27, col. N).

B. <u>S.C. No. 2, General Service</u>

Q. Please describe North Shore's proposal to add a new meter class for S.C. No. 2, General Service.

A. To reduce intra-class subsidies, North Shore is proposing to expand the meter classes for S.C. No. 2, General Service, from two to three. Currently North Shore has two meter classes, Meter Class 1, for customers with meters up to 700 cubic feet per hour and Meter Class 2, for customers with meters over 700 cubic feet per hour. Under North Shore's current two meter class rate structure, the smaller meter customers subsidize those customers with large meters over 2,300 cubic feet per hour. To reduce this subsidy, North Shore is proposing a third meter class rate, which will be set closer to cost, for those customers with large meters over 2,300 cubic feet per hour.

Q. Please describe North Shore's proposal for changes in S.C. No. 2 charges.

A. North Shore proposes to increase the monthly customer charges for S.C. No. 2, while moving the charges for all three meter classes closer to cost. North Shore also proposes to differentiate customer charges for sales and transportation customers for the same reasons explained for S.C. No. 1. North Shore Ex. VG-1.7 reflects a summary of embedded fixed costs per customer for the three meter classes. Fixed costs include customer and demand costs. Customer related costs are allocated to each meter class based on the investment in meters. Demand related costs are allocated to each meter class based on peak day demand. Based on these allocations, total embedded fixed costs per customer for Meter Classes 1, 2 and 3 are $35.77, $123.45 and $398.84, respectively (line 3). For Meter Classes 1 and 2, North Shore proposes to recover all customer costs and a portion of demand costs through the customer charge to minimize intra-class subsidies. This results in proposed customer charges of $22.30, $68.00 and $189.60, for Meter Classes 1, 2 and 3 sales customers, respectively (line 5) and proposed customer charges of $20.20, $65.80 and $187.50 for Meter Classes 1, 2 and 3 transportation customers, respectively (line 6). While the proposed customer charges for Meter Classes 1 and 2 recover 30% of their respective demand costs, in the interest of gradualism, only 18% of costs are recovered through the proposed Meter Class 3 customer charge. The difference of about $2.10 between sales and transportation customer charges arise from gas cost related Account No. 904 Uncollectible Accounts expenses (about $2.50 for sales customers and $.40 for transportation customers). If the Commission were to approve North Shore's proposed Rider UEA, the customer charge would be the same for sales and transportation customers and would be $19.80, $65.40 and $187.10 for Meter Classes 1, 2 and 3 customers, respectively. These charges reflect the removal of all gas cost related Account No. 904 Uncollectible Accounts expenses. North Shore is proposing to maintain the three declining block distribution charge for S.C. No. 2 and allocate the remaining customer, demand costs and commodity costs to the front, middle, and end blocks. The front block (0-100 therms) has been decreased to 15.445 cents per therm, the middle block (over 100-3,000 therms) has been decreased to

7.963 cents per therm (an increase for transportation customers), and the end block (over 3,000 therms) has been increased to 6.398 cents per therm. As fewer demand costs have been allocated to the Meter Class 3 customer charge than Meter Classes 1 and 2, the end block reflects a larger increase so that such costs are recovered from Meter Class 3 customers whose usage would typically exceed the first two blocks. Under North Shore's proposals, only 54% of the revenue requirement for S.C. No. 2 will be recovered through fixed charges.

Q. Why is a portion of the demand charge recovered through the customer charge for Meter Classes 1 and 2?

A. As explained for S.C. No. 1, both demand and customer costs are fixed, meaning they do not vary with the amount of gas that North Shore delivers to its customers. Demand costs are typically recovered from large volume customers through demand charges. This is feasible because such customers normally have demand meters that allow for accurate measurement of daily demand volumes. However, the costs for demand meters would add additional costs to the customer charge. S.C. No. 2 does not require demand metering. As a result, it would be more practical to recover demand costs through a fixed monthly charge such as the customer charge. North Shore is proposing that certain larger S.C. No. 2 customers be transferred to S.C. No. 3, where their demand will be measured by a demand meter and they will be assessed a demand charge. This will be discussed later in my testimony.

Q. Will North Shore's proposals for S.C. No. 2 have any effect on the calculation of adjustments under Rider VBA, Volume Balancing Adjustment?

A. Yes. North Shore's proposed revenue increase and rate designs will result in new distribution rates and Rate Case Margins ("RCM") for Rider VBA. Under present rates, RCM differs for sales and transportation customers since their distribution rates differ. As North Shore is proposing the same distribution rates for sales and transportation customers, the RCM and adjustments determined under Rider VBA will be the same for S.C. No. 2 sales and transportation customers.

Q. Please describe how North Shore S.C. No. 2 customers have been impacted by Rider VBA to date.

A. North Shore's Rider VBA became effective May 1, 2008. From May, 2008 through February, 2009, about $397,000 will have been refunded to North Shore S.C. No. 2 customers.

Q. Why is North Shore proposing to increase its monthly customer charges for S.C. No. 2, given that a decoupling mechanism, Rider VBA, was approved in its last rate case?

A. North Shore is proposing to increase its customer charges for S.C. No. 2 for the same reasons described for S.C. No. 1.

Q. Are there any other proposals for S.C. No. 2?

A. Yes. North Shore proposes to limit S.C. No. 2 to those customers who consume an average of 41,000 monthly therms or less as measured by data for the most recent twenty-four month period or two calendar years. North Shore will make this determination every two years, although it will also review eligibility if there is evidence of changed usage.

Q. Why is North Shore proposing this eligibility requirement for S.C. No. 2?

A. North Shore's tariff includes S.C. No. 3, Large Volume Demand Service, which is designed for customers with high demands whose average monthly usage exceeds 41,000 therms. As a result of the rates resulting from the final order in ICC Docket No. 07-0241, many S.C. No. 3 customers switched to S.C. No. 2, at rates which were below their cost of service and a service classification that does not require demand meters or impose a demand charge. A limitation for S.C. No. 2 eligibility would assure that customers take service under their appropriate cost based service classification and that other customers are not unfairly impacted by customers switching to service classifications below their cost of service.

C. S.C. No. 3, Large Volume Demand Service

Q. Please describe the changes proposed for S.C. No. 3, Large Volume Demand Service.

A. All charges for S.C. No. 3 will be changed. The monthly customer charge will be set at cost and will be increased to $760.00. The demand charge will be set at 67% of cost. The demand charge, which under present rates, is a declining block rate structure of 10,000 therms and over 10,000 therms, will be set at a flat charge of 61.719 cents per therm. The monthly standby service charge, which recovers storage and production costs will be increased to 11 cents per therm of standby demand. The distribution charge, which will recover remaining demand costs and commodity costs, will be increased to 1.578 cents per therm.

Q. Why is North Shore proposing to change its demand charge from a declining block rate to a flat rate?

A. A flat demand charge mitigates the bill impacts for the S.C. No. 2 customers who will be transferred to S.C. No. 3, and it results in reasonable bill impacts for all S.C. No. 3 customers under proposed rates.

Q. Is North Shore proposing any different charges for sales and transportation customers?

A. No. North Shore is proposing the same charges for sales and transportation customers as there are no S.C. No. 3 sales customers forecasted for test year 2010.

Q. Please discuss other proposals that North Shore is making for S.C. No. 3.

A. North Shore is proposing to eliminate the requirement that S.C. No. 3 customers sign a contract. This would no longer be necessary if the Commission accepts North Shore's proposal to include usage eligibility requirements for S.C. No. 2. North Shore is proposing other editorial revisions that are related to the proposed elimination of the contract requirement. However, if the Commission does not accept North Shore's proposal to impose usage eligibility requirements for S.C. No. 2, North Shore will need to revise S.C. No. 3 to address switches to S.C. No. 2. The contract requirement included a twelve-month term, and, if a customer terminated the contract early, it remained responsible for payment of fixed charges for the unexpired portion of the term. This was intended to, but did not successfully, limit movement to rates below the cost of serving these large volume customers. The proposed changes to S.C. Nos. 2 and 3 for eligibility is a more effective and simpler mechanism. North Shore is proposing to retain a term requirement, but is excluding switches to S.C. No. 2 associated with the usage criterion.

D. <u>S.C. No. 5, Standby Service</u>

Q. Please describe the proposed changes to S.C. No. 5, Standby Service.

A. North Shore proposes to eliminate S.C. No. 5 and transfer all customers served under this service classification to S.C. No. 2. Other than using gas for standby purposes, customers served under this service classification share no similar usage or cost characteristics. Accordingly, such customers would be more appropriately served under a general service rate.

E. Other Service Classifications

Q. Are there any proposed changes to S.C. No. 6, Contract Service for Electric Generation and S.C. No. 4, Contract Service to Prevent Bypass?

A. No, North Shore is not proposing any changes to these service classifications.

F. Bill Impacts

Q. Please describe North Shore Ex. VG-1.8.

A. North Shore Ex. VG-1.8 shows North Shore's Schedule E-9 of its standard filing requirements which provides bill impacts under present and proposed rates for S.C. Nos. 1, 2, 3, 4, and 5. The exhibit reflects the bill impacts of North Shore's rate proposals as well as the bill impacts arising from North Shore's proposals which would transfer certain customers from S.C. No. 2 to 3 and all customers from S.C. No. 5 to 2.

G. Miscellaneous Charges

Q. Please describe the items included in Miscellaneous Charges.

A. Miscellaneous Charges include the Service Activation Charges and Service Reconnection Charges as well as other charges. North Shore is proposing changes only to the Service Activation Charges and Service Reconnection Charges.

1. Service Activation Charges

Q. Please describe North Shore's proposal with respect to the Service Activation Charges.

A. North Shore is proposing to change its Service Activation Charges, which recover a portion of the costs related to initiating gas service at a premises. The Service Activation Charges apply to those customers moving into or within North Shore's service territory. There are two types of service activations. A succession turn-on occurs when the customer moving out calls and discontinues gas service at approximately the same time as the applicant moving in calls and requests gas service. In this instance, only a meter reading is taken. A straight turn-on occurs when there has never been gas service at a location, or when the prior customer canceled service some time before the new applicant calls to request gas service and the gas has actually been turned off. In this instance, the gas has to be turned on and appliances have to be relit. A study was performed to measure the costs of these activities and is summarized in North Shore Ex. VG-1.9. The study shows that the cost for a succession turn-on is $16.59 (column J, line 1), the cost of a straight turn-on is $43.91 (column J, line 2) and the cost to light an additional appliance over four is $8.91 (column J, line 3). North Shore's proposed charges, which would recover a significant, but not all costs, are $15.00 for a succession turn-on and $35.00 for a straight turn-on. There will be no change in the current $5.00 charge for relighting each appliance over four.

2. Service Reconnection Charges

Q. What is the proposal for changes in the Service Reconnection Charges?

A. A Service Reconnection Charge is a charge assessed to a customer whose gas has been turned off for any number of reasons. These include disconnections for non-payment of bills and at the customer's request. Each customer is granted a waiver of one reconnection charge each year, except in the situation where the customer voluntarily disconnects and then requests reconnection within twelve months or in the situation in which service is disconnected at the main. An analysis was performed to determine the cost basis of the three types of service reconnections following an involuntary disconnection for which North Shore currently charges customers: basic reconnections which only require a meter turn-on, reconnections which require setting a new meter, and reconnections that involve excavating at the main. The results of this analysis are summarized in North Shore Ex. VG-1.9. The study shows that the cost for a reconnection at the meter is $65.88 (column J, line 8); the cost for a reconnection when the meter has to be reset is $256.04 (column J, line 21); and the cost for a reconnection at the main is $1,988.89 (column J, line 26). The cost to light each additional appliance over four is the same as under the Service Activation Charge. North Shore proposes to recover only a portion of these costs. North Shore proposes that the basic reconnection charge be increased from $50.00 to $60.00, that the reconnection charge when the meter has to be reset be increased from $90.00 to $125.00, and that the reconnection charge when service has to be reconnected at the main be increased from $275 to $350. While these charges are still less than cost based, they have been increased to collect a higher percentage of the costs from the customers creating the costs. There will be no change in the current $5.00 charge for relighting each appliance over four.

H. <u>Transportation Rider Charges</u>

Q. Please discuss North Shore's proposals for charges in its transportation riders.

A. North Shore proposes to reduce certain charges in its transportation Riders FST, Full Standby Transportation, Rider SST, Selected Standby Transportation, Rider P, Pooling Service and Rider AGG, Aggregation Service. Specifically, North Shore proposes to reduce the Administrative Charge for Riders FST and SST from $8.94 to $7.32 per account and the Pooling Charge for Rider P from $4.95 to $3.44 per account. North Shore also proposes to decrease the Aggregation Charge for Rider AGG from a charge of $.03 per account to a credit of $.36 per account. The Aggregation Charge credit arises from an Aggregation Charge of $1.41 and a storage credit offset of $1.77. The cost studies supporting the charges for the Administrative and Aggregation charges are shown in North Shore Ex. VG-1.10. The analysis supporting the storage credit is shown in North Shore Ex. VG-1.11.

VI. SUMMARY OF INCREASE

Q. Please summarize the increase in the base rate revenues arising from North Shore's proposals for S.C. Nos. 1, 2, 3 and 5.

A. North Shore's proposals for S.C. Nos. 1, 2, 3 and 5 will result in an increase of $21.9 million (North Shore Ex. VG-1.2, line 26, column K).

Q. Please describe the revenues that will arise from North Shore's increase in miscellaneous charges.

A. North Shore will experience an increase in miscellaneous charges of about $33,000 (North Shore Ex. VG-1.2, line 28, column K). This includes $15,000 in miscellaneous revenue, including that arising from service activation and service reconnection charges, and $18,000 from accounting charge revenues, which North Shore receives from state and local governments for billing and remitting state and local taxes. These increase amounts are reflected in North Shore's Schedule A-2, Overall Financial Summary, of its standard filing requirements.

Q. Please describe any other revenues that will arise from North Shore's increase in base rate delivery charges.

A. North Shore will experience an increase in forfeited discount revenues that are estimated to be $65,000 (North Shore Ex. VG-1.2, line 29, column K). Combined with a base rate increase of $21.9 million and the miscellaneous charges increase of $33,000, the total proposed revenue increase is $22.0 million (North Shore Ex. VG-1.2, line 31, column K).

Q. Would base rates and the revenue increase amount change if the Commission were to approve Rider UEA?

A. Yes. If the Commission were to approve Rider UEA, the revenue requirement would be reduced by gas cost related Account No. 904, Uncollectible Accounts expenses. Base rates would be reduced and there would be a lesser revenue increase. As stated above, this would reduce the proposed customer charges for S.C. Nos. 1 and 2.

VII. OTHER TARIFF REVISIONS

A. General Revisions

Q. Please describe any general revisions that were made to the North Shore tariff.

A. As discussed previously in my testimony, North Shore is proposing to eliminate S.C No. 5, Standby Service. Accordingly, any references to S.C. No. 5 have been removed from the tariff. North Shore is also proposing to eliminate Rider FST-T, Full Standby Transportation Transition Service, Rider SST-T, Selected Standby Transportation Transition Service, Rider LST-T, Large Volume Selected Standby Transportation

Transition Service, and Rider P-T, Pooling Transition Service. Accordingly, any references to these riders have also been removed from the tariff. The reasons for the proposed elimination of these riders will be discussed later in my testimony.

B. <u>Terms and Conditions of Service</u>

Q. What changes were made to North Shore's Terms and Conditions of Service?

A. North Shore is proposing to revise its Service Activation Charges and Service Reconnection Charges as previously discussed in my testimony. The new charges are reflected in their respective sections. Additional minor editorial changes are being made to language describing these charges. For the Second Pulse Capability, North Shore is proposing to insert a February 14, 2008 grandfathering date so that the language remains accurate after the effective date for the tariff sheet changes. North Shore is proposing to revise language for Correction for Pressure, Temperature and/or Supercompressibility so that it is consistent with North Shore's practices concerning the pressure at which customers are served. North Shore is proposing to add a definition of "person" related to changes it is proposing to Riders 4 and 5, which I discuss below.

C. <u>Rider 2, Gas Charge</u>

Q. Please discuss North Shore's proposed changes to Rider 2, Gas Charge.

A. Rider 2 has been revised to remove references to S.C. No. 5 and the transportation transition tariffs.

D. <u>Rider 4, Extension of Mains, and Rider 5, Service Pipe</u>

Q. Please discuss North Shore's proposed changes to Rider 4, Extension of Mains and Rider 5, Service Pipe.

A. The current language in Rider 4 assumes that the requestor for a main would be a customer. However, there are often situations where the requestor is a person or a group of persons who are developing the property for eventual gas service. The language proposed by North Shore is needed to address those types of situations. North Shore proposes to expand the definition of customer under Rider 5 for the same reasons.

E. <u>Transportation Riders</u>

Q. Please discuss North Shore's proposed changes for its transitional transportation riders.

A. In ICC Docket No.07-0241, North Shore had proposed extensive revisions to its transportation programs. Such revisions required a transitional period that would allow North Shore to continue to provide transportation service to its customers until the new programs were implemented. Riders FST-T, SST-T, LST-T, and P-T were in place to continue transportation service during the transition period. The new programs were implemented on August 1, 2008. Accordingly, North Shore proposes to eliminate the transition riders, which are no longer necessary.

Q. Please describe any other revisions that were made to the transportation riders.

A. Riders FST, SST and P reflect an August 1, 2008 effective date. As these tariffs are now in effect, this date has been removed as it is no longer necessary. All of the riders have also been revised to eliminate any references to S.C. No. 5 as it is being eliminated. Riders FST, SST and AGG are also revised to show that certain therm calculations are rounded to the nearest 10 (*i.e.*, to the nearest dekatherm).

Q. What is the number of Allowable Bank Base Rate Days for Riders FST, SST and AGG that would arise from North Shore's proposed revenue requirement?

A. Four (4) Allowable Bank Base Rate Days (days of bank for Rider AGG) would arise from North Shore's proposed revenue requirement. North Shore Ex. VG-1.12 shows how the number of Allowable Bank Base Rate Days was derived. The number of Allowable Bank Base Rate Days that transportation customers receive as part of the storage part of the service is to be based on North Shore's most recent rate case.

Q. Does North Shore propose to make any operational changes to its transportation riders?

A. No. North Shore's transportation riders were implemented on August 1, 2008 with new operational provisions that were approved by the Commission in ICC Docket No. 07-0241. North Shore believes that it would be more beneficial to gain experience under the new riders rather than to propose any new modifications at this time.

VIII. <u>NEW RIDERS</u>

Q. Does North Shore propose to add any new riders?

A. Yes, North Shore proposes three new riders. They are Rider UEA, Uncollectible Expense Adjustment; Rider FCA, Franchise Cost Adjustment; and Rider GCA, Governmental Agency Compensation Adjustment. Rider UEA proposes factors that are to be applied to a portion of the customer's bill. Rider FCA proposes municipality specific charges to recover the cost of franchise agreements. Rider GCA proposes charges to recover governmental costs other than franchise fees.

A. <u>Rider UEA, Uncollectible Expense Adjustment</u>

Q. What is the purpose of Rider UEA?

A. The purpose of Rider UEA is to recover Account No. 904 gas cost related Uncollectible Accounts expenses through a factor that will be applied to customer bills rather than through base rates. Rider UEA will apply a service class specific factor to the gas charge portion of sales customers' bills. Those factors will be set in this rate case. Rider UEA will be applicable to S.C. Nos. 1 and 2.

Q. Please explain how North Shore's proposed Rider UEA will operate.

A. Rider UEA shows the factors that will be applied to the gas charge portion of sales customers' bills. Each factor is rate class specific and is based on the bad debt allocations for each rate class in North Shore's ECOSS. The derivation of the Uncollectible Factor for each service classification is shown on North Shore Ex. VG-1.13 (column C).

Q. Are the revenues that would be recovered through Rider UEA reflected in North Shore's revenue requirement?

A. Yes. If the Commission were to approve Rider UEA, expenses that would be recovered under the rider would need to be removed from North Shore's revenue requirement. This would amount to about $1.9 million based on gas costs forecasted for the test year (North Shore Ex. VG-1.13, column E).

Q. Has the Commission approved any riders similar to Rider UEA?

A. Yes. The Commission approved Rider UF, Uncollectible Factors, for Commonwealth Edison on September 10, 2008 (ICC Docket No. 07-0566).

B. <u>Rider FCA, Franchise Cost Adjustment</u>

Q. What is the purpose of Rider FCA?

A. Proposed Rider FCA will recover the costs of reduced rate service or monetary contribution provided by North Shore solely from those customers residing in each local governmental unit receiving such rate or contribution. These costs are reflected in Account No. 927.

Q. Why does North Shore incur franchise costs?

A. North Shore has franchise agreements with local governmental units so that it can use the public rights-of-way to deliver gas to customers residing in the boundaries of such governmental units. North Shore, in turn, compensates the local government for allowing access.

Q. Why would Rider FCA be an effective cost recovery mechanism?

A. Rider FCA would be an effective recovery mechanism for two reasons. First, it would target franchise cost recovery from those customers residing in the governmental units that cause the costs. Second, it would recover actual franchise costs, with customers paying only the costs that North Shore incurs. In short, fairness in cost apportionment is the underlying reasoning and rationale for this rider.

Q. Has the Commission approved any riders similar to Rider FCA?

A. Yes. The Commission approved Rider FCA for Commonwealth Edison in ICC Docket No. 05-0597, where the proposed rider was uncontested. A similar proposal is pending for Nicor Gas (ICC Docket No. 08-0363).

Q. Please describe how North Shore's proposed Rider FCA would operate.

A. Rider FCA would apply to S.C. Nos. 1, 2, and 3. North Shore will make a filing with the Commission by April 20 of each year, with charges under the rider to be effective each May. The initial charges under the rider would be effective May 1, 2010. The per customer charge would be determined for each applicable governmental unit by dividing actual Account No. 927 costs for the previous calendar year, by the number of customers as of December 31 of the same year, and dividing again by 12. The charge would be billed over a 12-month cycle ending April 30. Using Form 21 data for 2007, North Shore Ex. VG-1.14 shows the determination of charges that would have been effective May 1, 2008, if Rider FCA had been in effect.

Q. If the Commission were to approve Rider FCA, how would it impact North Shore's base rates?

A. If the Commission were to approve Rider FCA, base rates through April 30, 2010 would reflect test year Account No. 927 costs of $1,939,217. Going forward, base rates effective May 1, 2010 would be reduced by the test year Account No. 927 costs, with such costs being recovered through the rider.

C. <u>Rider GCA, Governmental Agency Compensation Adjustment</u>

Q. What is the purpose of Rider GCA?

A. Rider GCA would recover fees and costs that North Shore incurs as a result of requirements that a local governmental unit imposes on North Shore solely from those customers taking service from North Shore within the boundaries of each local governmental unit imposing such costs. Rider GCA describes seven conditions that would allow North Shore to recover costs under the rider.

Q. Why would Rider GCA be an effective cost recovery mechanism?

A. Rider GCA would be an effective recovery mechanism as it would target recovery of any incremental costs above those set in base rates from those customers residing in the governmental units that cause the costs.

Q. Has the Commission approved any riders similar to Rider GCA?

A. Yes. The Commission has approved Rider 7, Governmental Agency Compensation Adjustment for Nicor Gas and Rider LGC, Local Government Compliance Adjustment for Commonwealth Edison. North Shore's proposal mirrors that approved for Nicor Gas.

Q. If the Commission were to approve Rider GCA, how would it impact North Shore's test year expenses?

A. If the Commission were to approve Rider GCA, North Shore's test year expenses would be unaffected, as Rider GCA would recover only those expenses not already recovered through base rates.

Q. Please describe how North Shore's proposed Rider GCA would operate.

A. Rider GCA would apply to S.C. Nos. 1, 2, and 3. North Shore will make a filing with the Commission by December 20 of each year, with charges under the rider to be effective each January and billed over a calendar year (Annual Recovery Period). Any initial charges under the rider would be effective January 1, 2011. The per customer charge would be determined for each applicable governmental unit by dividing applicable costs by the number of applicable customers, and dividing again by 12. If there is a mismatch between actual costs and revenues during the Annual Recovery Period, North Shore may make a filing with the Commission to adjust the charge. No later than April 1 of each year, North Shore would file a reconciliation of actual costs and revenues with the Commission and bill any reconciliation adjustments over the remaining months of the calendar year.

IX. TEST YEAR BILLING UNITS

Q. What billing units did North Shore use to derive its proposed rates?

A. North Shore used weather normalized sales volumes and forecasted customers (billing periods), billing demand volumes and transportation program units to derive rates for all service classifications. Collectively, these items can be referred to as billing units. The derivation of test year billing units is discussed in the direct testimony of Mr. David Clabots (North Shore Ex. DWC-1.0).

Q. Please discuss any changes to test year billing units that were made for rate design purposes.

A. As discussed previously in my direct testimony, North Shore is proposing eligibility limits for S.C. No. 2 and it is proposing to eliminate S.C. No. 5. Both of these proposals have resulted in a transfer of costs and billing units from S.C. No. 2 to 3 and S.C. No. 5 to 2. As a result of North Shore's proposals, 23 customers are being transferred from S.C. No. 2 to S.C. No. 3 and 79 customers are being transferred from S.C. No. 5 to S.C. No. 2. The cost transfers are reflected in the ECOSS completed by Ms. Hoffman Malueg (North Shore Exs. JCHM-1.6 to JCHM-1.9). The present and proposed revenues arising from these transfers are shown in North Shore Ex. VG-1.2, lines 6, 12, 15, 21and 24.

Q. Are there any other billing unit matters that need to be addressed?

A. Yes. The number of S.C. No. 2 Meter Class 1 and Meter Class 2 transportation customers (billing periods), at present rates, is under- and over- stated, respectively due to a formulaic error. As a result, S.C. No. 2 at present rates, reflects 21 (252 annual) Meter Class 1 customers and 2,452 (29,424 annual) Meter Class 2 customers, for a total of 2,473 (29,676 annual) transportation customers. North Shore has corrected this error at proposed rates. As corrected, S.C. No. 2 at proposed rates, reflects 911 (10,932 annual billing periods) Meter Class 1 customers; 731 (8,767 annual) Meter Class 2 customers; and 831 (9,977 annual) Meter Class 3 customers, for a total of 2,473 (29,676 annual) transportation customers. I note that the total number of S.C. No. 2 transportation customers under present and proposed rates remain unchanged.

Q. Please describe how this error impacts North Shore's present rate revenues and its increase amount.

A. This error has resulted in North Shore's present rate revenue being overstated by about $459,240 and its proposed increase being understated by the same amount. Accordingly, North Shore would need to make an adjustment during this proceeding to correct for this error.

Q. Does this conclude your direct testimony?

A. Yes, it does.