

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

THE SOUTHERN COMPANY,)	
AGL RESOURCES INC., and)	
NORTHERN ILLINOIS GAS COMPANY)	
d/b/a NICOR GAS COMPANY)	
)	Docket No. 15-0558
Application for Approval of a)	
Reorganization Pursuant to)	
Section 7-204 of the Public Utilities Act)	

Rebuttal Testimony of

MICHAEL J. MORLEY

Managing Director, Rates and Regulatory Accounting
AGL Resources Inc.

On behalf of Joint Applicants

March 3, 2016

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1 **I. INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. Michael J. Morley, 10 Peachtree Place, Atlanta, Georgia 30309.

4 **Q. By whom and in what position are you employed?**

5 A. I am Managing Director, Rates and Regulatory Accounting of AGL Resources Inc.
6 (“AGL Resources”) and I am employed by AGL Resources’ wholly-owned subsidiary
7 AGL Services Company (“AGSC”).

8 **Q. What are your duties in your position as Managing Director, Rates and**
9 **Regulatory Accounting of AGL Resources?**

10 A. I have responsibility for the preparation and coordination of financial information for rate
11 cases and for the monthly and annual reporting requirements of AGL Resources’
12 regulated subsidiaries to their respective state public service commissions. I am also
13 responsible for directing and coordinating responses to various requests of state and
14 federal regulatory agencies, for directing the development and implementation of
15 customer rates and tariffs, and for providing various analyses and regulatory
16 interpretations and consulting to senior management.

17 **Q. Please summarize your educational background and experience.**

18 A. I obtained a Bachelor of Business Administration from the University of Georgia in June
19 1991 with a major in Accounting. Prior to my current position, I served as the Director
20 of Financial Accounting where my responsibilities included general ledger management,
21 coordinating with external auditors and technical accounting research, and serving as the

22 primary accounting contact for operational groups including rates and regulatory, gas
23 operations field operations, and corporate.

24 **II. ITEMIZED ATTACHMENTS**

25 **Q. Are there any exhibits to your rebuttal testimony?**

26 A. Yes. I am sponsoring one exhibit, Joint Applicants Exhibit (“Ex.”) 6.1, which is a copy
27 of the data request response provided by the Office of the Illinois Attorney General
28 (“AG”) and the Citizens Utility Board (“CUB”) (collectively “AG/CUB”) witness David
29 Effron to JA-AG-CUB 2.02.

30 **III. PURPOSE OF TESTIMONY**

31 **Q. What is the purpose of your rebuttal testimony?**

32 A. The purpose of my rebuttal testimony is to address the direct testimony of AG/CUB
33 witness David Effron.

34 **IV. RESPONSE TO AG/CUB WITNESS EFFRON**

35 **Q. Does Mr. Effron address the requirements of Section 7-204(b) of the Public**
36 **Utilities Act (“Act”) relating to the Commission’s approval of the proposed**
37 **transaction between Southern Company and AGL Resources (the**
38 **“Reorganization”)?**

39 A. No. Mr. Effron offers no testimony regarding the requirements for Commission approval
40 of the Reorganization under Section 7-204(b). Instead, Mr. Effron points to Section 7-
41 204(f) of the Act, which provides that the Commission may impose conditions in
42 approving any proposed reorganization that are, in its judgment, necessary to protect the
43 interests of the public utility and its customers. (Effron Dir., AG/CUB Ex. 1.0, 9:15-18).

44 **Q. What is Mr. Effron's recommendation under Section 7-204(f)?**

45 A. Mr. Effron recommends that the Commission order a temporary reduction to Nicor Gas'
46 rates to reduce its base rate revenues by \$52 million as a condition of merger approval.
47 (Effron Dir., AG/CUB Ex. 1.0, 10:1-2).

48 **Q. What basis does Mr. Effron provide for his recommendation?**

49 A. Mr. Effron claims that, as a result of the Commission-approved reduction to Nicor Gas'
50 2014 depreciation expense, Nicor Gas is earning a return on equity in excess of its
51 authorized return. (Effron Dir., AG/CUB Ex. 1.0, 6:9-7:4). This claim is supported by a
52 flawed analysis, as I discuss below.

53 **Q. What is wrong with Mr. Effron's claim?**

54 A. Mr. Effron's analysis is flawed in that it is contrary to long-standing and fundamental
55 ratemaking principles. As an initial matter, I first turn to the propriety of raising an
56 alleged overearning claim in this docket. From a procedural perspective, I am advised by
57 counsel that a merger approval proceeding is an improper forum to assess whether a
58 utility is earning in excess of its Commission-authorized return on equity. In this regard,
59 I am aware of no instance where the Commission has ever reduced a utility's rates in a
60 merger proceeding based on an alleged overearning claim.

61 **Q. Can Mr. Effron's claim be more appropriately addressed in another context?**

62 A. Yes. The assessment of rates is a complex undertaking that can take many months, and
63 there are appropriate tools available to AG/CUB to address their claim. For example, if
64 AG/CUB have an issue with whether Nicor Gas is overearning, I understand from

65 counsel that they can file a complaint, or can seek to have the Commission initiate an
66 investigation. However, as I describe herein, the basis for this claim is flawed.

67 **Q. You state that Mr. Effron’s conclusion is contrary to fundamental ratemaking**
68 **principles. Can you explain your statement?**

69 A. Yes. Mr. Effron fails to employ the principle of normalization, a fundamental ratemaking
70 concept that the Commission has used for years in ratemaking proceedings.

71 Normalization is a tool to address the fact that, from year to year, a utility may experience
72 fluctuations in a variety of factors that may impact such rate case items as costs,
73 revenues, capital structure, and billing determinants. Normalization is a recognized
74 regulatory tool used to levelize costs, revenues and/or billing determinants in a test year
75 in order to arrive at a just and reasonable revenue requirement and rate design.

76 In this proceeding, a major flaw in the way Mr. Effron calculates Nicor Gas’
77 return on equity for calendar year 2014 is by using raw data, where he fails to normalize
78 the Company’s revenues to recognize the impacts of weather. In doing so, he
79 unreasonably inflates the Company’s 2014 return on equity. (AG/CUB Ex. 1.1). As
80 Joint Applicants witness Henry Linginfelter described in his direct testimony, during the
81 2013-14 heating season, Nicor Gas’ service territory experienced record customer
82 demand resulting from record cold weather that blanketed the area. (Linginfelter Dir.,
83 Joint Applicants Ex. 2.0, 6:128-135). This extreme weather included the “Polar Vortex”
84 in January 2014, which brought extreme weather and record customer demand. On the
85 peak demand day of January 6, 2014, which was the record peak demand day in Nicor
86 Gas’ history, Nicor Gas provided 4.6 Bcf of gas to meet customer demand. Mr. Effron’s

87 assessment fails to consider the impact that these extreme weather conditions had on
88 revenue in 2014.

89 Instead, Mr. Effron relies solely on Nicor Gas' Form 21 data, which was filed
90 with the Commission in April 2015. (AG/CUB Ex. 1.1). It is widely understood that this
91 data is not normalized and should not be relied on solely for ratemaking purposes.
92 Nonetheless, Mr. Effron takes the raw data from the Company's Form 21 and makes no
93 adjustment to account for the extreme weather experienced in 2014. It is my
94 understanding that such an approach is contrary to the manner in which the Commission
95 historically has assessed rates.

96 Finally, even if the Company's Form 21 data could be relied on solely for
97 ratemaking purposes, and it cannot, I also observe that this information became publicly
98 available in April 2015, almost one year ago. However, at no time prior to the filing of
99 Mr. Effron's direct testimony in this proceeding did the AG or CUB raise a claim that
100 Nicor Gas was overearning.

101 **Q. Has Mr. Effron acknowledged that he did not employ the principle of**
102 **normalization in his analysis?**

103 A. Yes. In response to Joint Applicants' data request JA-AG-CUB 2.02, attached as Joint
104 Applicants Exhibit 6.1, Mr. Effron admits that he did not weather-normalize the data in
105 preparing his calculation provided in his direct testimony.

106 **Q. Do you have any other concerns with Mr. Effron's assessment?**

107 A. Yes. The basis for Mr. Effron's claim focuses solely on Nicor Gas' Commission-
108 approved change to its depreciation rates. (Effron Dir., AG/CUB Ex. 1.0, 6:19-7:4). In
109 doing so, he improperly employs a single-issue ratemaking approach as the basis for his

110 proposal to reduce Nicor Gas' rates. In my experience, and contrary to Mr. Effron's
111 approach, the application of sound regulatory policy for ratemaking purposes does not
112 focus on one revenue requirement component, but instead analyzes costs, revenues,
113 working capital, and capital structure in a holistic fashion for an appropriate test year.

114 In addition, I note that Mr. Effron's rate reduction claim essentially rests on the
115 application of improper retroactive ratemaking theory. He concludes that Nicor Gas
116 made too much money in 2014 and proposes a prospective rate decrease to recover
117 revenues from two years ago. Such an approach is inconsistent with long-standing
118 ratemaking principles. The purpose in establishing prospective rates should not be to
119 reach back in time to claim revenues recovered pursuant to Commission-approved rates.
120 Instead, the establishment of prospective rates should be based on test-year or current
121 costs, and Mr. Effron does not engage in such an assessment.

122 **Q. Given your review of Mr. Effron's testimony and taking into consideration**
123 **ratemaking principles, have you come to any conclusions?**

124 A. Yes. First, Mr. Effron's conclusion illustrates precisely why it is essential that
125 ratemaking matters properly should be considered in the context of a rate review, where
126 all of the myriad factors that affect cost of service can be fully and fairly assessed.

127 Second, Mr. Effron's position to reduce Nicor Gas' current rates based on a single
128 revenue requirement component and using financial information from 2014 – financial
129 information that is not adjusted to reflect normal ratemaking principles – is contrary to
130 the well-established rules against single-issue and retroactive ratemaking.

131 In summary, Mr. Effron's proposed rate decrease is not supported by normal
132 ratemaking principles and is inconsistent with well-established Commission policies
133 governing the establishment of just and reasonable utility rates.

134 **Q. As part of his claims concerning Nicor Gas' earnings, Mr. Effron asserts that the**
135 **Commission could take certain action pursuant to Section 9-202(a) of the Act in**
136 **an effort to reduce existing rates. (Effron Dir., AG/CUB Ex. 1.0, 9:18-23). Does**
137 **this assertion have any merit?**

138 A. No. As I understand the process from discussions with counsel, should the Commission
139 exercise its authority under Section 9-202(a), it does so based on actual information
140 reported by the utility, adjusted to apply long-standing ratemaking principles. The
141 Commission should not act based on speculative, unsupported or incorrect claims. As
142 demonstrated in my testimony above, Mr. Effron's claims concerning Nicor Gas' return
143 on equity in years 2014 and thereafter are not supported by long-standing ratemaking
144 principles. Thus, Mr. Effron's suggestion that the Commission undertake action pursuant
145 to Section 9-202(a) is without merit.

146 **V. CONCLUSION**

147 **Q. Does this conclude your rebuttal testimony?**

148 A. Yes.