

**STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION**

**Re: EnergyNorth Natural Gas, Inc.
d/b/a KeySpan Energy Delivery New England**

Indirect Gas Costs

DG 07-050

PREFILED TESTIMONY OF ANNE E. LEARY

August 31, 2007

TABLE OF CONTENTS

I.	Interest on Gas Cost Deferred Balance	Page 3
II.	Lead/Lag Study	Page 7
	a. Collection performance is not the cause of the difference between KeySpan and Northern's collection lag	Page 8
	b. Mr. McCluskey's three criticisms of the lead/lag study are misplaced	Page 9
	c. The lead/lag study should not be reconsidered in this docket	Page 24
III.	Rate Case Expense	Page 28

1 **Q. Ms. Leary, please state your full name and business address.**

2 A. My name is Ann E. Leary. My business address is 52 Second Avenue, Waltham,
3 Massachusetts 02451.

4

5 **Q. Please state your position with KeySpan Energy Delivery New England**
6 **(“KeySpan” or the “Company”).**

7 A. I am the Manager of Rates and Regulatory Affairs for KeySpan Energy Delivery
8 New England.

9

10 **Q. How long have you been employed by KeySpan or its affiliates and in what**
11 **capacities?**

12 A. In 1985, I joined the Essex County Gas Company as Staff Engineer. In 1987, I
13 became a planning analyst and later became the Manager of Rates. Following the
14 acquisition of Essex by Eastern Enterprises in 1998, I became Manager of Rates
15 for Boston Gas and then subsequently for KeySpan Energy Delivery New
16 England after Eastern was acquired by KeySpan Corporation. Since the
17 acquisition of EnergyNorth Natural Gas, Inc. by KeySpan Corporation, I have
18 been responsible for these matters for EnergyNorth as well.

19

20 **Q. What do your responsibilities as Manager of Rates include?**

21 A. As the Manager of Rates, I am responsible for preparing and submitting various
22 regulatory filings with both the New Hampshire Public Utilities Commission and
23 the Massachusetts Department of Telecommunications and Energy on behalf of

1 KeySpan's New England local distribution companies, including Boston Gas
2 Company, Essex Gas, Colonial Gas, and EnergyNorth. This includes Cost of Gas
3 ("COG") filings, Local Distribution Adjustment Charge ("LDAC") filings and
4 reconciliations, energy conservation, performance-based revenue calculations,
5 lost-base revenues, and exogenous cost filings. In particular, I had overall
6 responsibility for submission of the Winter 2007-08 cost of gas filing that the
7 Company made in DG 06-121, which led to the opening of this proceeding.

8
9 **Q. Please summarize your educational background.**

10 A. I received a Bachelor of Science in Mechanical Engineering from Cornell
11 University in 1983.

12
13 **Q. Have you previously testified in regulatory proceedings?**

14 A. I have testified in a number of regulatory proceedings before the Massachusetts
15 Department of Telecommunications and Energy in rate matters, including
16 providing testimony relating to cost allocation studies, rate design, cost of gas
17 adjustment clause proposals, and exogenous cost filings. I have testified before
18 the New Hampshire Public Utilities Commission in Docket DG 04-152 regarding
19 the Company's fixed price option, in Docket DG 05-049 regarding the Company's
20 2005 Off Peak COG ,in Docket DG 05-141 regarding the Company's 2005/06
21 Peak COG and in Docket DG 06-040 regarding the Company's 2006 Off Peak
22 COG.

1 **Q. What is the purpose of your testimony?**

2 A. My testimony addresses one aspect of the issue relating to calculation of the
3 Company's deferred gas cost balance that was raised by the Staff with regard to
4 KeySpan in Docket DG 07-034 and DG 06-121 and with regard to Northern
5 Utilities in Docket DG 07-033. I will also respond to the testimony of Utility
6 Analyst George McCluskey regarding the Company's bad debt ratio and the
7 lead/lag study used to determine the level of gas supply cash working capital
8 needed by the Company.

9

10 **I. Interest on Gas Cost Deferred Balance**

11 **Q. In Docket DG 07-033, relating to Northern Utilities, the Commission is**
12 **addressing the issue of whether accrued or billed revenues should be used as**
13 **the basis for calculating interest on the gas cost reconciliation account. In his**
14 **testimony in the current proceeding, Mr. McCluskey stated that the**
15 **Company has indicated that it does not plan to file additional testimony**
16 **regarding that issue. Could you clarify the Company's position in that**
17 **regard?**

18 A. First, and I recognize that this is a relatively small point, the Company indicated
19 during settlement discussions that it was hoping to avoid having to file additional
20 testimony on the issue regarding the use of accrued versus billed revenues. It
21 never provided any assurance that it would not do so, although it is my
22 understanding from discovery in this case, that that is not what Mr. McCluskey
23 intended by the comment in his testimony.

1 Second, the Company does in fact believe that the issue of whether billed or
2 accrued revenues should be used as the basis for calculating interest on gas costs
3 has generally been adequately argued in Northern's cost of gas proceeding, and
4 does not believe that testimony regarding the same issue in this case would add
5 anything significant.

6 That said, if the Commission were to order that a change should be made from
7 using billed revenues to calculate the deferred gas cost balance to using accrued
8 revenues, there would still be a need to ensure that any transition from one
9 method to the other is accomplished in a way that does not inadvertently create a
10 mismatch between revenues and costs in the first month of the transition.

11
12 **Q. What is the Company's concern regarding how any transition should work?**

13 **A.** First, I should stress that this discussion relates only to a situation where the
14 Commission has already determined that accrued revenues, rather than billed
15 revenues, should be used. If the Commission determines in DG 07-033 that the
16 current method of calculating the gas cost reconciliation balance should not be
17 changed, the transition issue I am addressing here would be of no concern.

18 The gas cost reconciliation process involves complex accounting of gas costs and
19 gas cost revenues, but the basic concept is fairly straightforward. Each month, the
20 Company books a month of gas costs and a month of revenues from customers
21 that reflect the amount billed to them for the gas supply portion of the service
22 rendered to them. If the Commission determines that the revenue figure used in
23 this reconciliation process should be done using accrued revenues (i.e. revenues

1 calculated based on gas that as been delivered to customers but not necessarily
2 billed to them as yet), rather than the current method of using revenues reflecting
3 amounts billed to customers, there is the possibility that the first month of the
4 transition would include a month and a half of revenues, but only a month's worth
5 of gas costs. The result would be a significant and inappropriate reduction in the
6 net amount in the gas cost reconciliation account at the start of the period, which
7 in turn would significantly reduce the interest recovered by the Company. I have
8 calculated that annual amount for the period November 2005 through October
9 2006 to be approximately \$471,230 if such a change were made effective
10 November 2005, the date suggested by Staff. (Schedule AEL-1 sets forth the
11 basis for this calculation.)
12

13 **Q. How does the Company suggest such a transition should occur?**

14 **A.** Again, the subject is complex to explain in detail, and at this point the Staff has
15 not put forward its position on the subject in testimony in this docket. I have had
16 several informal discussions with Staff about this issue, and have some concern
17 that they may propose a transition method that would create the mismatch that I
18 am concerned about.

19 In essence, under the Company's proposed methodology, in the month of the
20 transition, the amount booked for billed gas revenues under the current
21 methodology that reflect the prior month's usage would need to be reversed, and
22 the amount of accrued gas revenues for that same month would need to be
23 booked. Schedule AEL-2 shows this change and demonstrates, as one would

1 expect, that the amount of gas costs for the month approximately equals the
2 amount of gas revenues after such a change is made. (The two amounts are never
3 exactly equal because revenues are calculated on COG rates that were derived
4 using projected gas costs. The projected gas costs obviously differ from the
5 actual monthly gas costs, given the volatility of the gas commodity market.)

6 Given that the Staff has not yet submitted testimony on this subject, the Company
7 must reserve the right to respond if Staff asserts that a different approach should
8 be taken.

9
10 **Q. Is there a specific method that the Company believes should be used to effect**
11 **the transition from billed to accrued revenues if the Commission orders the**
12 **Company to adopt the use of accrued revenues in its calculation of the gas**
13 **cost reconciliation?**

14 **A.** As long as the total revenues reflect only one month of revenues and the
15 beginning balances for November 2005 for both gas cost reconciliation accounts
16 (i.e., for both the peak and off peak periods) do not change from the amounts filed
17 in DG 06-121, the Company would generally be indifferent as to the exact
18 methodology used to transition from billed to accrued gas revenues if such a
19 change is required at all. The Company is prepared to work with the Staff to
20 come to agreement on the precise methodology. The Company's concern on this
21 issue is that, if it is not done properly and there is a failure to match a month of
22 revenues with a month of costs, the result would be confiscatory because it would
23 artificially reduce the gas cost reconciliation balance on which interest is

1 calculated. Therefore, it is important to ensure that more than a single month's
2 revenues are not included in the month in which the transition occurs.

3
4 **II. Lead/Lag Study**

5 **Q. In his testimony, Mr. McCluskey argues that the Commission should adjust**
6 **the Company's indirect gas costs downward because, he asserts, the**
7 **methodology used in the Company's lead/lag study was flawed and because**
8 **the Company's collection lag (essentially the time between when service is**
9 **rendered and when bills are paid) is longer than it should be for reasons put**
10 **forth by Ms. Noonan. What is the Company's response?**

11 **A. First, as previously indicated by the Company during the prehearing conference in**
12 **this matter, the Company feels strongly that this issue is not properly before the**
13 **Commission in this docket. I will explain the basis for that belief in more detail**
14 **later in my testimony. Second, Mr. McCluskey's position that the Company's**
15 **collection practices have improperly added to the length of the collection lag is**
16 **based on Ms. Noonan's testimony. As Kimberly Ahern explained in her**
17 **testimony, Ms. Noonan's testimony not only does not support such a conclusion**
18 **but actually would support a finding that the Company's collection practices have**
19 **not caused an increase in the collection lag. Third, Mr. McCluskey's analysis**
20 **includes several errors which result in a miscalculation of the collection lag.**
21 **Finally, Mr. McCluskey simply chooses an arbitrary number (2 days) by which to**
22 **further reduce the collection lag that he calculated for the Company, in order to**
23 **address the concerns he says are substantiated by Ms. Noonan's testimony.**

1 **II a. Collection performance is not a cause of the difference between**
2 **KeySpan and Northern's collection lag.**

3
4 **Q. Mr. McCluskey compares the lead/lag studies of KeySpan with other New**
5 **Hampshire gas and electric companies and concludes that, absent a showing**
6 **that the differences are attributable to KeySpan's service area, the**
7 **Company's longer net lag must arise from problems with the Company's**
8 **revenue collection process and/or expense payment procedures. Do you**
9 **agree with his conclusion?**

10 **A. No, I do not. First, as Ms. Ahern notes in her testimony, in discovery the Staff**
11 **conceded that comparing gas utilities with electric utilities is not appropriate.**
12 **Second, as Ms. Ahern's testimony explains as well, there are demographic**
13 **differences between the service territories of KeySpan and Northern Utilities that**
14 **need to be considered. In particular, KeySpan has twice as many low income**
15 **customers as a percent of residential heating customers as Northern. Hence, Mr.**
16 **McCluskey's critical assumption—that the demographics for the two utilities are**
17 **the same—turns out to be incorrect. In addition, Mr. McCluskey ignores the fact**
18 **that historically KeySpan has typically experienced a greater lag than Northern.**
19 **He does not consider the fact that the two companies have had very different lags**
20 **since the time that data was first used in determining indirect gas costs for**
21 **collection through the two companies' cost of gas rates, which preceded**
22 **KeySpan's acquisition of EnergyNorth. Thus, the difference that exists today has**
23 **nothing to do with KeySpan's collection practices. Rather, it reflects inherent**

1 differences in the two companies' services territories and customer bases. The
2 fact is that KeySpan's net lag has historically been higher than Northern's, as
3 demonstrated in Mr. McCluskey's testimony. According to Mr. McCluskey, the
4 net lag for ENGI was 11.3 days, based on DR 91-212, while Northern's was 6.33
5 days. Therefore the net lag for ENGI was approximately 1.8 times that of
6 Northern's. By comparison, KeySpan's net lag for 2005 was 19.90 (corrected in
7 Staff 1-10), which is approximately 1.9 times the 2006 net lag of 10.26 days for
8 Northern, as shown in Mr. McCluskey's response to KeySpan 1-50 (See Schedule
9 AEL-3). (The Company does not have access to 2005 data for Northern and
10 therefore used 2006 data.) Thus, Northern and KeySpan's net lags have grown at
11 a similar pace, and it is not fair to conclude that KeySpan had ineffective
12 collection processes.

13
14 **II. b Mr. McCluskey's three criticisms of the lead/lag study are misplaced.**

15 **Q. In his testimony, Mr. McCluskey cited three specific problems with the**
16 **lead/lag study used by the Company in its indirect gas cost filing. Please**
17 **summarize the problems he claims to have identified.**

18 **A. First, Mr. McCluskey claims that the Company's study was flawed because it used**
19 **gas costs as a proxy for gas revenues for purposes of calculating the revenue lag**
20 **from billing to collection. Second, Mr. McCluskey argues that the Company**
21 **erred when it used a rolling twelve months of gas costs to calculate monthly**
22 **collection lags. Third, Mr. McCluskey asserted that the monthly accounts**

1 receivable balances should have been adjusted for gross write-offs, rather than net
2 write-offs as the Company did.

3
4 **Q. Please explain why Mr. McCluskey is incorrect when he rejects the use of gas**
5 **costs as a proxy for gas revenues in calculating the lag from billing to**
6 **collection.**

7 A. Mr. McCluskey argues that the Company's lead/lag study is flawed because it
8 relied on gas costs rather than gas revenues to calculate the lag from billing to
9 collection. As evidence of this he points to his Exhibit GRM-2 and attempts to
10 show that supply related revenues exceed gas costs in some months by as much as
11 \$5 million. However, there is no correlation between the monthly gas cost and
12 revenue figures he refers to and the way in which gas costs were used as a proxy
13 for revenues in the lead/lag study. Mr. McCluskey makes the statement, which is
14 true but unremarkable, and then fails to explain how the variance impacts the
15 lead/lag study. The fact is that it does not because the Company relied on *annual*
16 gas costs, not individual *monthly* data, as a proxy for gas supply revenues, and as I
17 briefly explained earlier in my testimony, over time these two amounts will be
18 quite close to one another and therefore do serve as reasonable proxies for one
19 another.

20 More important, however, is understanding in the first place why gas costs were
21 used as a proxy for revenues and what impact that has on the lead/lag study. The
22 study used gas costs instead of revenues solely for the purpose of approximating
23 the portion of total accounts receivable associated with the gas supply portion of

1 customers' bills. In order to conduct a lead/lag study on a separate basis for the
2 gas supply function, one must know the portion of total receivables that arise from
3 the sale of gas to customers, as opposed to the portion that arises from the
4 provision of delivery service.

5 As can be seen in Schedule AEL-4 if the calculation from the lead/lag study is
6 redone and gas revenues are substituted for gas costs, there is no impact on the
7 results of the Company's study. This is because the gas cost information has only
8 been used to estimate the gas cost portion of the total accounts receivable balance,
9 not for any other purpose. This is done by multiplying the total accounts
10 receivable balance by the ratio of gas costs to total firm revenues. The result (i.e.,
11 the portion of the total accounts receivable that relates to gas costs) is then divided
12 by total gas costs to determine the revenue lag. This methodology is based on the
13 reasonable assumption that the both the base distribution revenues and gas supply
14 revenues have the same lag, i.e. that there is the same delay between the time that
15 distribution service is rendered and the distribution portion of the bill is paid as
16 there is between when the gas is consumed by the customer and the gas supply
17 portion of the bill is paid. As I have demonstrated in Schedule AEL-4, this use of
18 COG revenues in lieu of actual gas costs does not change the outcome of the
19 analysis.

20
21 **Q. If the use of gas costs instead of COG revenues yields the same result, why**
22 **did the Company use gas costs for this purpose at all?**

1 A. The Company used gas costs for this purpose because there is no way to
2 determine independently what portion of accounts receivable relate to the COG.
3 All the Company knows is its total level of receivables at any point in time, but it
4 has no independent way to determine what portion of those bills is attributable to
5 the COG. In order to do that, it must use some other known data to allocate the
6 costs.

7

8 **Q. If the use of COG revenues as a proxy for gas costs in this way has no effect**
9 **on the results of the analysis, what is Mr. McCluskey's purpose in addressing**
10 **this issue?**

11 A. That is unclear. It appears to be intended to create an implication that the entire
12 study is somehow flawed and should be disregarded, but as noted above the fact is
13 that there is nothing wrong with the method utilized by the Company. Mr.
14 McCluskey's testimony does appear designed to create the impression that the
15 Company's approach is invalid and therefore should not be relied on by the
16 Commission, which is certainly not the case.

17

18 **Q. Please explain why you disagree with Mr. McCluskey's second criticism—**
19 **that the Company used rolling twelve month periods of gas costs to calculate**
20 **monthly collection lags.**

21 A. Mr. McCluskey claims that the Company's use of gas costs from the previous
22 twelve months creates a mismatch with end-of-month accounts receivable
23 balances that are used because a "great majority" of the revenues that make up

1 accounts receivable balances relate to accounts that have been outstanding for less
2 than 30 days. It turns out that 55% of the balances in 2006 relate to accounts that
3 have been outstanding for fewer than 30 days, which cannot fairly be called a
4 “great majority”. More important, however, under Mr. McCluskey's method there
5 is a mismatch as well because 45% of the accounts receivable balance that are
6 included relate to revenues booked in the prior months. This is because 45% of
7 customers do not pay their gas bill within 30 days, but rather carry over balances
8 from month to month. In other words, 55% of customers pay their bills within 30
9 days, while 45% of customers take longer than 30 days to pay their bills.

10 In Mr. McCluskey's methodology, in the first month, 45% of the accounts
11 receivable balance relates to the prior months' revenues, thereby creating a
12 mismatch between accounts receivable balances and current month revenues. In
13 other words, 45% of the A/R balance for the month of January 2005 reflects
14 revenues that were billed sometime in 2004. Mr. McCluskey's method divides an
15 average accounts receivable balance by an average revenue figure. However, the
16 A/R balances and revenues used by Mr. McCluskey cover different time periods,
17 making his calculation inconsistent. This inconsistency might historically have
18 been insignificant when gas costs were relatively stable, but it creates a significant
19 flaw when the analysis is based upon a period of increasing gas costs, as was the
20 case in 2005, the test year in this case. During that year, annual COG revenues
21 increased approximately 20% over 2004. As Mr. McCluskey has already pointed
22 out, on average 45% of the accounts receivable balance reflects prior periods,
23 which would include the lower COG revenues experienced in 2004. Therefore

1 the collection lag calculated by Mr. McCloskey is significantly understated since
2 the numerator (the accounts receivable balance) reflects a portion of the lower
3 2004 COG revenues while the denominator incorporates the higher 2005 COG
4 revenues. For that reason, even though the simplified approach used by Mr.
5 McCluskey in his testimony has been used by some in the industry at times, it is
6 not a good measure of true lag under the conditions that have prevailed in recent
7 years and should be rejected in this case. The method used by the Company
8 better reflects the Company's collection lag since it addresses the issue of rising
9 gas costs in its calculation by using a rolling 12 month average gas costs.

10
11 **Q. Please explain why the Company disagrees with Mr. McCluskey's third**
12 **point, that the monthly accounts receivable balances used in the lead/lag**
13 **study should be adjusted for gross write-offs, rather than net write-offs.**

14 **A.** Gross write-offs are all amounts written off during a given period. Net write-offs,
15 on the other hand, consist of gross write-offs less amounts that were previously
16 written off but that were subsequently paid (i.e., they were paid after they were
17 written off). By reducing accounts receivable by gross write-offs, Mr.

18 McCluskey's method double counts amounts paid by customers whose accounts
19 were previously written off.

20 Mr. McCluskey's method incorrectly reduces gas cost related accounts receivable
21 by payments that are received after an account has been written off when in fact
22 the Company's receivables are already net of this amount. Specifically, the
23 accounts receivable balance, which is a balance sheet account, is calculated

1 monthly by taking the prior month's ending balance, adding the revenues billed
2 for that month (i.e., new accounts receivable) and subtracting all cash receipts
3 received in that month (including any recoveries from previously written off
4 accounts) as well as any existing receivables that were written off during the
5 month. It is important to note that the recovery of previously written off balances
6 is treated by the Company as cash receipts, and therefore treated as a reduction to
7 the accounts receivable balance. Because the monthly cash receipts contain any
8 recoveries of previously written off accounts, the Company must also add back
9 these recoveries, which is accomplished by using net write-offs instead of gross
10 write-offs. This can be shown in the following formula: $A/R \text{ Balance} = \text{Prior}$
11 $\text{Month's Balance} + \text{Current Month Revenue} - \text{Cash Receipts (including}$
12 $\text{recoveries from previously written off accounts)} - \text{Net Write-Offs (i.e., gross}$
13 $\text{write-offs minus recoveries from previously written off accounts)}$. As can be seen
14 from this formula, because recoveries from previously written off accounts are
15 included in "cash receipts" they cancel out the recoveries from previously written
16 off accounts that are included in the net write-offs. The remaining calculation is
17 simply $A/R \text{ Balance} = \text{Prior Month's Balance} + \text{Current Month Revenues} - \text{Cash}$
18 $\text{Receipts} - \text{Gross Write-offs}$. The Company must use net and not gross write-offs
19 in this calculation or the recovery portion would be double counted and the
20 accounts receivable balance would be understated. If the Company used gross
21 write-offs instead of net write-offs, the A/R balance would first be reduced when
22 the account was written off and would then be reduced a second time when the

1 recovery portion of previously written off accounts was recorded as “Cash
2 receipts”.

3

4 **Q. Can you provide an example of this problem?**

5 A. Yes. Assume Customer A does not pay his bill, and therefore the Company
6 writes off the bill and reduces its accounts receivable balance to reflect the write-
7 off. (Recall that net write-offs equal gross write-offs minus amounts subsequently
8 recovered.) Under the Company’s method, if that customer pays his bill the
9 month after the write-off is taken, the Company would credit the cash received
10 and debit the recoveries, and therefore these two transactions will cancel each
11 other out and have no impact on the A/R balance. . Said another way, the
12 recovery included as part of “Cash receipts” cancels out the recovery included in
13 “net write-offs” and hence has no impact on the A/R balance. On the other hand,
14 under Mr. McCluskey's approach, the Company would reduce the A/R balance
15 twice because when the Company writes off the particular A/R item, the
16 Company would reduce the A/R balance by the gross write offs and then when the
17 customer pays his bill (after it has been written off), the Company would record
18 the transaction as a “Cash receipt” and reduce the A/R balance again. The result
19 would be an understatement of the A/R balance.

20 Mr. McCluskey justifies his approach, in part, based on the practices of other
21 utilities. However, what he fails to consider is the fact that utilities that follow the
22 method he proposes do not include the recovery of write-offs as “cash receipts,”

1 and thus they do not have the double counting issue that would be created for
2 KeySpan given how accounts receivable are calculated on its balance sheet.

3

4 **Q. What is the impact on the results of the lead/lag study of adopting Mr.
5 McCluskey's methodology on this point, rather than the Company's?**

6 A. The accounting change proposed by Mr. McCluskey reduces the net lag by .11
7 days, from 37.79 to 37.68 (See Response to KeySpan 1-52, attached as Schedule
8 AEL-5.).

9

10 **Q. Aside from responding to Mr. McCluskey's three criticisms of the
11 Company's lead/lag study methodology, what other concerns do you have
12 regarding his calculation of the net lag for the Company?**

13 A. I have three significant concerns. First, Mr. McCluskey mixes and matches gas
14 costs and gas revenues in his calculation of the collections lag (See Exhibit GRM-
15 2), which creates a significant error and results in an incorrect collection lag.
16 Second, Mr. McCluskey ignores the fact that his proposed use of the Accounts
17 Receivable Turnover Method is confiscatory during a period of generally rising
18 gas prices, which was the case in the test year used for the Company's study.
19 Third, Mr. McCluskey completes his testimony by making an arbitrary downward
20 adjustment in the collection lag that he calculates in order to penalize the
21 Company for the matters discussed by Ms. Noonan.

22

1 **Q. Please explain how Mr. McCluskey mixed and matched the use of gas costs**
2 **and gas revenues in his calculation of the collection lag and why that is**
3 **incorrect.**

4 A. In Exhibit GRM-2 Mr. McCluskey used the gas accounts receivable balance from
5 the Company's lead/lag study. However, the gas accounts receivable balance was
6 a calculation derived by multiplying the firm accounts receivable balance by the
7 ratio of gas costs to firm revenues. He then calculated the collections lag by
8 dividing the gas cost A/R balance (which was derived using gas *costs*) by annual
9 COG *revenues*. In other words, he mixed and matched COG revenues and gas
10 costs in his calculation of collection lag. Unlike the earlier discussion regarding
11 the use of gas costs as a proxy for gas revenues in calculating the portion of
12 accounts receivable that relates to gas supply costs, gas costs and gas revenues
13 *cannot* be used interchangeably for purposes of determining the collection lag in a
14 given twelve month period, and the Company, in fact, did not use it for this
15 purpose. The Company used gas costs as a proxy for COG revenues only for
16 purposes of determining the percentage of total receivables that related to the gas
17 supply portion of customers' bills.

18 Having criticized the Company for that legitimate simplifying assumption, he
19 then made the error of shifting between the use of gas costs and COG revenues
20 when he calculated the Company's collection lag. Specifically, to determine the
21 gas cost related accounts receivable balance, Mr. McCluskey multiplied the total
22 accounts receivable balance by the ratio of gas *costs* to total firm revenues, but he
23 then determined the collection lag by dividing the average gas cost related

1 accounts receivable balance by average COG *revenues*. In other words, in his
2 calculation of the collections lag he used the gas cost related portion of the
3 accounts receivable balance (numerator) based upon a gas costs allocation (not
4 COG revenue allocation) and then divided this gas cost related A/R balance by
5 the annual COG revenues, thereby using gas costs in the numerator and COG
6 revenues in the denominator. As Mr. McCluskey showed in his Exhibit GRM-1,
7 there can be a variance between gas costs and COG revenues in a given 12 month
8 period. It would be incorrect to mix and match by using gas costs in the
9 numerator and COG revenues (a larger number) in the denominator. In Schedule
10 AEL-6 Scenario 2, I have corrected Mr. McCluskey's Exhibit GRM-3 by properly
11 recalculating the gas cost related accounts receivable balance (i.e., by multiplying
12 the total accounts receivable balance by the ratio of COG revenues to total firm
13 revenues). This correction results in a lag of 38.60, not 37.68 days as shown in
14 Exhibit GRM-3.

15
16 **Q. Your second concern with Mr. McCluskey's methodology related to his use**
17 **of the Accounts Receivable Turnover Method to calculate collection lag.**

18 **What is your concern in this regard?**

19 A. The Accounts Receivable Turnover Method proposed by Mr. McCluskey offers
20 the advantage of simplicity, but that comes at the expense of accuracy. While Mr.
21 McCluskey's method can provide reliable results on average, it does not reflect
22 the true collection lag during periods of rising and falling gas cost revenues.

23 Schedule AEL-7 shows a side by side comparison of the method used by the

1 Company in its lead/lag study and the method used by Mr. McCluskey. (For this
2 comparison I employed the corrected version of Mr. McCluskey's method shown
3 in Schedule AEL-6, Scenario 2). The major difference between the two
4 methodologies lies in the amount reflected in the Annual COG Revenue, the
5 denominator that is used in the calculation of the collections lag. Because the
6 Annual COG Revenue figure used by Mr. McCluskey is larger than the twelve
7 month Annual Rolling COG Revenues used in the Company's analysis, the
8 collection lag determined by Mr. McCluskey is smaller. In Mr. McCluskey's
9 methodology the Annual COG Revenue represents the period January through
10 December 2005 (See Schedule AEL-7, column a.) In the KeySpan methodology,
11 the COG revenues for each month during the period January 2005 through
12 December 2005 represent a rolling twelve months (see Schedule AEL-7, column
13 o). If there were no increases in gas costs between 2004 and 2005, the Annual
14 COG Revenue found in column o would equal the 2005 Annual COG Revenue
15 found in column l, in which case the two methodologies would result in similar
16 lags. As shown in Schedule AEL-7, however, COG revenues increased
17 throughout 2005, and as a result the collections lag is understated by Mr.
18 McCluskey's analysis because the numerator is based on an accounts receivable
19 balance that incorporates lower 2004 COG revenues, while the denominator
20 reflects higher 2005 annual COG revenues. Because the Annual COG Revenue
21 figure (i.e., the denominator) used by Mr. McCluskey is not in synch with the A/R
22 balances (i.e., the numerator), the resulting collection lag (the quotient) is

1 artificially low, and the resulting collection lag calculated by Mr. McCluskey is
2 understated.

3
4 **Q. Your third criticism of Mr. McCluskey's calculation of the net lag is that he**
5 **proposes to reduce the Company's collection lag by two days to reflect what**
6 **he characterizes as the expected improvement in collections performance**
7 **associated with Staff's recommendation on KeySpan's bad debt percentage.**
8 **Do you agree with this proposal?**

9 A. No. Mr. McCluskey claims that the Company needs to be incentivized to
10 improve its collections performance. But as Ms. Ahern's testimony explains, the
11 Company's collections practices have been prudent, and the increase it has
12 experienced in its uncollectible accounts expense in recent years is not the result
13 of poor collections management. Mr. McCluskey provides no basis for the
14 adjustment he proposes. Mr. McCluskey's comparison of KeySpan's net write-
15 offs to other utilities is flawed.

16
17 **Q. Mr. McCluskey claims that KeySpan's net write-offs compare unfavorably**
18 **with those of other New Hampshire utilities. Do you agree with his**
19 **conclusions?**

20 A. No, I do not agree that the Company has experienced a decline in collections
21 performance since KeySpan acquired ENGI. Ms. Ahern has already addressed
22 this point to the extent that Mr. McCluskey relies on Ms. Noonan's testimony. In
23 addition, I believe there are some underlying errors in Mr. McCluskey's analysis.

1 **Q. What are those errors?**

2 A. First, Mr. McCluskey examines the historical write-off percentage for KeySpan
3 for 2001-2006 and claims that this creates a reliable measure of collections
4 performance because, by expressing billings written off as a percentage of
5 revenues, the effects of temporal changes in sales growth and gas prices can be
6 eliminated. In doing so, however, he does not take account of the fact that during
7 periods of increasing gas costs the number of customers who can not pay their
8 bills also increases. As shown in Table 1 of Mr. McCluskey's testimony,
9 KeySpan's total revenues increased by 23% from 2001 to 2006 and 68% from
10 2002 to 2006. This increase in revenues is due primarily to the increase in gas
11 costs. Mr. McCluskey's observation that the write-off percentage is a good
12 indicator of collections performance is incorrect during a period of such drastic
13 price increases.

14
15 **Q. Mr. McCluskey compares the 2005 and 2006 net write-offs for KeySpan and**
16 **other New Hampshire utilities and concludes that KeySpan has a higher**
17 **percentage of write-offs to revenues than any other New Hampshire utility,**
18 **and implies that there is some correlation between KeySpan's supposed**
19 **decline in revenue collections performance and its higher percentage of**
20 **write-offs. Do you agree with his conclusion?**

21 A. No. Underlying this comparison is the assumption that KeySpan and Northern
22 have similar service territories. As I have already discussed, and as described in
23 Ms. Ahern's testimony, it is incorrect to assume that demographics for Northern

1 and KeySpan's service territories are similar. As demonstrated previously, the
2 service territories for KeySpan and Northern are different. KeySpan has double
3 the percent of residential low income customers than Northern. Plainly, this could
4 well have a significant impact on collections performance. There is no indication
5 that the Company's collection practices are the cause of the increase in write offs.

6
7 **Q. Mr. McCluskey compares the aging of A/R for 2006 and points to KeySpan's**
8 **120 day A/R balance as being excessive compared to other New Hampshire**
9 **utilities. He appears to imply that because the Company does not maintain**
10 **historical data regarding accounts receivable aging, one would conclude that**
11 **the difference in collections lag for KeySpan is due to a difference in**
12 **collections performance. Is that a fair conclusion?**

13 **A.** No, if that is what Mr. McCluskey intended, it is not a fair conclusion. Mr.
14 McCluskey acknowledges in his testimony that different service territory
15 demographics would impact A/R aging for a utility and therefore it would be
16 reflected in data from before KeySpan's acquisition of EnergyNorth. He then
17 apparently rejects this theory in this case because the Company doesn't retain
18 certain information on an historical basis. There are other ways to confirm such a
19 thesis, however, and Mr. McCluskey failed to pursue them. As I described
20 earlier, enrollment in KeySpan's low income discount program shows that it has
21 approximately twice as many low income customers as Northern, yet Mr.
22 McCluskey did not look at this data that is filed with the Commission on a
23 quarterly basis. It is unfair to simply assume that the Company has ineffective

1 collections processes because the Company doesn't maintain a specific form of
2 data that Mr. McCluskey was interested in examining.

3
4 **II. c The lead/lag study should not be reconsidered in this docket.**

5 **Q. You mentioned earlier in your testimony that the Company does not agree**
6 **that the issue of the lead/lag study is properly before the Commission in this**
7 **proceeding. Please explain.**

8 A. The lead/lag issue is a new one that was first raised by Staff after the conclusion
9 of last winter's cost of gas proceeding, DG 06-121. The Company believes that
10 addressing that issue as a separate item subsequent to DG 06-121 is inconsistent
11 with the understanding that the Company had with the Staff regarding
12 implementation of updated indirect gas costs and is improper single-issue
13 ratemaking. The issue is certainly one that could be raised in the Company's rate
14 case that will be filed five months from now, in accordance with the settlement
15 and Commission order in the KeySpan/National Grid merger proceeding, but the
16 Company feels strongly that a rate adjustment relating to this item would be
17 inappropriate at this time or in this proceeding.

18
19 **Q. The Company hasn't raised the issue of single-issue ratemaking with regard**
20 **to the other two issues in this docket. Why not?**

21 A. The Company has not raised the issue of single-issue ratemaking regarding these
22 two issues because the Company understood that the Staff was reserving its right
23 to continue to investigate those two issues when the indirect gas costs were

1 considered in DG 06-121. The Company accepted the risk as to how those two
2 issues would ultimately be resolved when it decided to proceed with
3 implementation of the remaining updated indirect gas costs. If it had told Staff
4 that it did not agree to leave the two identified issues open, it understood that the
5 remaining indirect gas costs would not go into effect either. The Company did
6 not agree that other matters, such as the lead/lag study, which were not even
7 mentioned in discussions between the Staff and the Company at the time would
8 remain open. The issue of the lead/lag study was first raised by Staff only after
9 DG 06-121 concluded, something which the Staff does not dispute and to which it
10 has agreed to stipulate. (See Staff response to KeySpan 2-22, attached as
11 Schedule AEL-8.) It was the Company's understanding that, other than the two
12 identified issues that were left open by agreement, the Commission's order
13 approved the rates proposed by the Company and, therefore, the underlying costs
14 were accepted as a basis for those rates.

15
16 **Q. Do you have some support for believing that the Commission staff shared the**
17 **understanding you just articulated?**

18 **A.** Yes. In addition to the history that I just noted, I would point to the transcript of
19 the hearing on the merits in DG 06-121 at pages 145-147, which I have attached
20 to my testimony as Schedule AEL-9. It is clear from that discussion that the
21 Staff's position and their understanding at the time was that the bad debt ratio
22 remained a cost that was subject to adjustment; there was no mention of any other
23 related cost item. It would not be a fair reading of that testimony, or any other

1 portion of the testimony, to infer that Staff believed it was reserving the right to
2 seek a later adjustment of other indirect gas costs. I do not doubt that, at some
3 point after the proceeding closed, the Staff determined that there might be other
4 costs, besides the bad debt ratio itself, that they would like to review in more
5 detail, but that was not what was communicated to the Company or to the
6 Commission, and looking at individual additional cost elements now would be
7 improper. Had the Company known that the Staff could subsequently reopen
8 other issues and make downward adjustments to individual items, it might not
9 have agreed to go forward with updating other indirect gas costs without seeking
10 upward adjustments for some of them because of issues related to normalization
11 or on other grounds.

12
13 **Q. Were there other indirect gas costs that were updated in DG 06-121 that**
14 **were not addressed in the Commission's order?**

15 A. Yes, the Company also updated its Production and Storage costs and
16 Miscellaneous Overheads in DG 06-121. Both these costs *decreased* from the
17 amounts previously approved in DG 00-63. The Company included these updated
18 costs as well as the updated working capital costs in its Compliance filing to the
19 Commission on November 9, 2006, which was subsequently approved by Staff.
20 Again, if the Company had been aware that the Staff could reopen individual
21 costs that were not put into rates on a temporary basis in DG 06-121, it might not
22 have agreed to submit the other updated costs.

1 **Q. The Consumer Advocate has argued that the adjustment of the Company's**
2 **indirect gas costs in DG 06-121 constituted single issue ratemaking, and the**
3 **Company argued that it was not. How is a rate adjustment relating to the**
4 **lead/lag study issue different from what the Company proposed in DG 06-**
5 **121.**

6 **A.** First, I need to stress that the filing in DG 06-121 was not a proposal by the
7 Company. As I will explain below, the filing was made in response to a request
8 from Staff. Plainly, the Company supported the adjusting of rates to reflect the
9 information filed in response to Staff's request, subject to the understanding I've
10 already described. Second, in DG 06-121, the Company's filing supported an
11 adjustment of all of its gas supply related costs, not just a single item. Far from
12 being a single issue rate case, the case addressed all of the costs (both direct and
13 indirect) that make up the cost of gas rate, a rate that the Commission adjusts
14 twice annually and that is otherwise subject to monthly adjustments to reflect
15 changes in direct gas supply costs.

16
17 **Q. Mr. McCluskey points out in his testimony in this case that the Company**
18 **didn't provide any supporting testimony in DG 06-121 for its lead/lag study.**
19 **Is he correct?**

20 **A.** The Company provided an eleven page study which detailed its lead lag
21 calculation, although it did not provide any additional narrative testimony
22 regarding the study. In addition, in DG 06-121 the Company also provided
23 testimony apprising the Commission that the Company had updated its indirect

1 gas costs including its lead/lag factor. The Company didn't see any need for
2 additional testimony because it was simply complying with a request from Staff (a
3 request which the Company viewed itself as having little choice but to accede to)
4 to update its indirect gas costs. As it turned out, the updated costs reflected higher
5 costs than the costs from 1999 that were the subject of the earlier docket when the
6 Company's rates were redesigned, DG 00-063. The Company calculated its cost
7 of gas rates in DG 06-121 using the updated cost information, and except for the
8 two issues held open at the request of Staff understood that the remainder of the
9 costs would go into effect through rates and were approved by the Commission in
10 its order. There did not appear to be a need to submit any testimony, prefiled or
11 live, regarding the lead/lag study, since it was not a topic of discussion.

12
13 **III. Rate Case Expense**

14 **Q. Is the Company concerned about the expense it is incurring related to the**
15 **issued being raised by Staff in this proceeding?**

16 A. Yes. There has been a trend in the last year or so for the Staff to raise individual
17 rate related issues outside the context of a broader rate proceeding. This began
18 with the Staff's request that the Company file updated indirect gas costs,
19 continued with the Staff's request that two cost of gas issues (use of accrued vs.
20 billed revenues and bad debt ratio)_be addressed separately by the Commission,
21 continued with the Staff's request that the Commission undertake an investigation
22 of the return on gas supply cash working capital and extended to Staff's
23 recommendation that the Commission examine the Company's lead/lag study in

1 this proceeding. These issues all have a direct impact on the Company's rates. As
2 the Commission is aware, because failure to do so would be confiscatory, utilities
3 are allowed to recover reasonable costs related to the regulatory process. Because
4 rate cases tend to occur infrequently, those costs are not included in regular rate
5 adjustments but are normally recovered separately through special surcharges
6 after the conclusion of a rate case. Some of the issues being raised by Staff in
7 recent proceedings, including the lead/lag issue, are ones that should properly be
8 included in a rate case, in which case the Company would have a ready
9 mechanism to recover the associated costs.

10
11 **Q. Why did you identify the lead/lag issue in this case and not the other two**
12 **issues?**

13 **A.** The Company has identified the lead/lag issue and not the other two issues
14 because the Company accepts that the other two issues were properly raised
15 during a cost of gas proceeding. The first issue (billed vs. accrued revenues) is
16 not one that the Company objected to the Staff's having raised, even if the
17 Company has not agreed with the Staff's position on the underlying issue. The
18 second issue (bad debt ratio) is one the Company agreed to leave open as part of
19 what it believed was an agreement to allow the remainder of the Company's
20 indirect gas costs to go into effect in DG 06-121.

21
22 **Q. What is the Company requesting of the Commission at this time regarding**
23 **rate case expense.**

1 A. The Company is requesting that the Commission determine that the Company is
2 entitled to recover through its cost of gas rates the reasonable costs of litigating
3 the lead/lag issue since the conclusion of DG 06-121. At the conclusion of this
4 case, the Company would be prepared to make a submission that shows what it
5 believes to be a reasonable allocation of its total expense to this issue.

6

7 **Q. Does that conclude your testimony?**

8 A. Yes.