STATE OF NEW HAMPSHIRE

PUBLIC UTILITIES COMMISSION

DG 07-050

<u>In the Matter of:</u>
<u>KeySpan Energy Delivery New England</u>
<u>Indirect Gas Costs</u>

Joint Surrebuttal Testimony

of

Amanda O. Noonan and
George R. McCluskey

October 19, 2007

STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Docket No. DE 07-050

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAMES AND BUSINESS ADDRESSES.

A. Our names are Amanda Noonan and George McCluskey, and our business address is 21 South Fruit Street, Suite 10, Concord, NH 03301.

Q. ARE YOU THE SAME AMANDA NOONAN AND GEORGE MCCLUSKEY THAT FILED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes, we individually filed direct testimony on June 22, 2007. A summary of our educational and professional experiences can be found in that testimony.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. Our testimony responds to the rebuttal testimony filed on behalf of KeySpan Energy Delivery New England ("KeySpan" or "Company") by Anne Leary and Kimberly Ahern on August 31, 2007. Specifically, we respond to the following statements by Ms. Leary:

(a) That the implementation of accrued accounting in KeySpan's Cost of Gas ("COG") reconciliation calculation may result in an unfair reduction in the amount of interest due to the Company on under/over collected gas costs;

(b) The methodology used by the Company to estimate collections lag is not flawed as argued by Mr. McCluskey. Rather, each of the three methodological flaws described by Mr. McCluskey is misplaced; and

(c) That Mr. McCluskey inappropriately mixed gas costs and gas revenues in the calculation of collections lag using the accounts receivable turnover method.

In addition, we respond to the following statements by Ms. Ahern:

(a) That KeySpan's management of its accounts receivables had no impact on the increase in the Company's uncollectible accounts and bad debt percentage. Rather, the increase in those items was caused by the increase in gas prices; and

(b) There are demographic differences between the KeySpan and Northern Utilities service areas which make a comparison of the two companies' bad debt percentages inappropriate.

Q. HOW IS YOUR SURREBUTTAL TESTIMONY ORGANIZED?

A. Our testimony is in four parts. Following this introduction, we respond to the portion of Ms. Leary's testimony that addresses the implementation of accrual accounting in the reconciliation of gas costs. Next, we respond to Ms. Leary's criticisms of the accounts receivable turnover method used by Mr. McCluskey to estimate collections lag. We follow this by responding to the arguments of Ms. Leary and Ms. Ahern regarding the Company's bad debt percentage.

II. IMPLEMENTATION OF ACCRUAL ACCOUNTING

Q. WHAT IS THE COMPANY'S POSITION ON THE ISSUE OF ACCRUED VERSUS BILLED REVENUE ACCOUNTING IN THE RECONCILIATION OF GAS COSTS?

A. KeySpan believes that this issue has been adequately argued in Docket DG 07-033, Northern Utilities' 2007 Summer COG proceeding, and therefore declines to address it further. In short, KeySpan appears to signal that it will accept whatever policy decision the Commission issues in Docket DG 07-033. KeySpan does, however, take issue with the manner in which Staff proposes to implement accrued revenue accounting.

Q. DID THE COMMISSION ADOPT ACCRUED REVENUE ACCOUNTING IN DOCKET DG 07-033?

A. Yes, although that decision is currently the subject of a motion for rehearing filed by Northern.

Q. WHAT IS KEYSPAN'S CONCERN WITH STAFF'S PROPOSED IMPLEMENTATION OF ACCRUED REVENUE ACCOUNTING?

A. Ms. Leary asserts in her rebuttal testimony that the change to accrued revenue accounting could result in a mismatch between accrued costs and accrued revenues that would unfairly lower the interest due to the Company. Specifically, Ms. Leary asserts that in the first month of the transition to accrued revenue accounting (November 2005) one and a half months of revenue may be matched with only one month's of gas costs. If true, this would lower the monthly under collection balances on which interest is earned.

Q. DOES STAFF AGREE WITH THIS ASSERTION?

A. No. The sole purpose of replacing billed revenues in the reconciliation calculation with accrued revenues is to eliminate the mismatch between gas costs and gas revenues caused by the billing cycle.[1] Since this change is to take effect beginning November 2005, there should be no mismatch of gas costs and gas revenues in that month.

Q. WHY THEN DOES MS. LEARY CLAIM OTHERWISE?

A. It is unclear why Ms. Leary makes this claim because none of the schedules attached to her testimony show this mismatch.

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[1] The Company is compensated for the costs of the billing cycle mismatch through a separate rate mechanism.

Q. HAS MS. LEARY CHANGED HER POSITION ON THE MISMATCH OF COSTS AND REVENUES?

A. Yes. As noted above, Ms. Leary alleges that in the first month of the transition to accrued revenues (i.e., November 2005) there is a mismatch between costs and revenues under accrued revenue accounting. In response to a request to explain the fundamental cause of the alleged mismatch, Ms. Leary states that the mismatch actually occurs in October 2005 in the Off-Peak account.[2] The cause of this mismatch is the transfer to the month of October 2005 of October unbilled revenue (i.e., revenue associated with gas consumed in October but billed in November) into the Off-Peak account. The transfer occurs because of the switch to accrued revenue accounting. According to Ms. Leary, adding these unbilled revenues to the billed revenues for October 2005 results in one and a half months of revenue in the month. She goes on to say that although this imputation of revenue occurs outside the period impacted by the Commission's Order in DG 07-033, the adjustment will nonetheless impact KeySpan's interest calculation going forward. Ms. Leary explains that the imputation of an extra half month of revenue in October will lower the November 2005 beginning balance in the Off-Peak account, which in turn reduces the interest due to the Company.

Q. DOES STAFF AGREE WITH THIS EXPLANATION?

A. Staff agrees that in transitioning from billed revenue accounting to accrued revenue accounting the Company must record approximately one and a half months of revenue in the month of October in its Off-Peak account. The effect

[2] See KeySpan response to Staff 3-1 shown in Staff Exhibit-1.

will be to reduce the October end-of-month balance in that account and, in turn, lower the average balance for November and all subsequent months. The net effect of these lower monthly balances will be a reduction in interest due to the Company in its Off-Peak account.

Q. IS THIS REDUCTION IN INTEREST APPROPRIATE?

A. Yes, to do otherwise would defeat the purpose of the accounting change. In order to transition to an accounting method where accrued costs are matched with accrued revenues every month, unbilled revenue must be transferred from the month in which it is billed to the month in which it is accrued. Assuming accrued revenue accounting begins November 2005, in every month but one the transfer out of unbilled revenue related to the prior month will be largely offset by the transfer in of unbilled revenue related to the subsequent month. The exception is October 2005. In that month, the transfer in of October unbilled revenue from November is not offset by the transfer out of September unbilled revenue because accrued revenue accounting does not begin until the next month. Even though the resulting month and a half of revenue in October 2005 reduces the interest due to KeySpan going forward, it would be wrong to view this as a penalty. Rather, the inclusion of the extra revenue in October corrects an error made when the billed revenue accounting methodology was first implemented: namely, the inclusion of only half a month's revenue in the initial month. Thus, the correct interpretation of the extra revenue is that it eliminates a benefit (i.e., high interest receipts) that the Company was never entitled to.

Q. HAS STAFF PREPARED A REVISED RECONCILATION CALCULATION THAT REFLECTS THE COMMISSION'S DECISION IN DOCKET 07-033?

A. Yes. Using data in schedule AEL-2, we calculate the interest on gas costs for the peak account, which is a twelve month calculation beginning November 2005 and ending October 2006, to be negative $16,544 instead of the $290,455 proposed by Ms Leary. For the off-peak period, the number is $32,390 instead of $110,641 calculated by Ms. Leary. Staff's calculations are shown in Staff Exhibit-2, pages 1 and 2.

III. COLLECTIONS LAG

Q. MS. LEARY CONTENDS THAT THE FLAWS MR. MCCLUSKEY FOUND IN HER METHODOLOGY FOR CALCULATING COLLECTIONS LAG ARE MISPLACED. PLEASE SUMMARIZE THESE FLAWS.

A. Mr. McCluskey found three fundamental flaws in the methodology used by KeySpan to calculate the collections lag. They are: (i) the use of gas costs as a proxy for gas revenues; (ii) the use of rolling twelve month gas costs instead of monthly gas revenues; and (iii) the use of net write-offs instead of gross write-offs to adjust accounts receivable ("A/R") balances. Each of these flaws causes the collections lag to be longer than it would otherwise be, based on the standard A/R turnover method.

Flaw 1: Gas Costs Are Not A Reasonable Proxy For Gas Revenues

Q. PLEASE RESPOND TO THE ARGUMENT MADE BY MS. LEARY FOR USING GAS COSTS INSTEAD OF GAS REVENUES TO CALCULATE COLLECTIONS LAG.

A. Because the methodology used by KeySpan to calculate collections lag employs rolling twelve month data rather than individual monthly data, support for Ms. Leary's claim that gas costs are a reasonable proxy for gas revenues must rest on a comparison of rolling twelve month gas costs and rolling twelve month gas revenues. According to Ms. Leary, "over time these two amounts will be quite close to one another and therefore do serve as reasonable proxy for one another."

The problem with this statement is that the data prove otherwise, as Mr. McCluskey convincingly demonstrated in Exhibit GRM-2 to his direct testimony. Specifically, using the same data sources that produced the rolling twelve month gas costs found in the Company's lead/lag study, Mr. McCluskey calculated for each month in 2005 the corresponding rolling twelve month gas revenues. A comparison of these two data streams is provided in Staff Exhibit-3, which is a variant of Exhibit GRM-2 attached to my original testimony. The exhibit shows that rolling twelve month gas revenues exceeded rolling twelve month gas costs in every month and by more than $5 million in January 2005 alone. Over 2005 as a whole, gas revenues exceeded gas costs by more than $37 million. Based on these results, gas costs are not a reasonable proxy for gas revenues.

Q. WAS MS. LEARY ABLE TO REFUTE THE REVENUE ESTIMATES IN EXHIBIT GRM-2?

A. On the contrary, Ms. Leary accepted as reasonable the monthly and rolling twelve month gas revenue estimates shown in that exhibit.[3]

Q. GIVEN THE RESULTS OF THE ANALYSIS PRESENTED IN STAFF EXHIBIT-3, HOW COULD MS. LEARY CLAIM THAT OVER TIME ANNUAL GAS COSTS ARE A GOOD PROXY FOR ANNUAL GAS REVENUES?

A. When confronted with these results, Ms. Leary chose to skirt the question by claiming that because the results of the lead/lag study do not change if gas revenues are substituted for gas costs, the analysis presented in Exhibit GRM-2 has no bearing on the case.[4]

Q. DOES STAFF AGREE THAT THE VARIANCE BETWEEN REVENUES AND COSTS HAS NO EFFECT ON COLLECTIONS LAG?

A. No, replacing the monthly revenues in Exhibit GRM-3 with monthly gas costs from Exhibit GRM-2 does change the collections lag. As can be seen in Staff Exhibit-5, the collections lag increases from 37.68 days using gas revenues to 38.42 days using gas costs, a change of 0.74 days.

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[3] See KeySpan response to Staff 3-18(1) shown in Staff Exhibit-4.
[4] See KeySpan response to Staff 3-18(2) shown in Staff Exhibit-4.

Flaw 2: Rolling Twelve Month Gas Costs Create A Mismatch With Monthly Accounts Receivables

Q. MS. LEARY CRITICIZES THE A/R TURNOVER METHOD USED BY STAFF TO CALCULATE COLLECTIONS LAG. PLEASE RECAP THE TERMS A/R AND A/R TURNOVER METHOD.

A. A utility's A/R account tracks the amount owed by customers that the utility expects to receive.[5] As such, the balance in this account may reflect invoices that have been outstanding for as short as a few days and for as long as a year or more. If we know the average daily revenue billed to customers, we can estimate the average number of days that bills have been over due by dividing the A/R balance by the daily revenue. This statistic is the basis of the standard A/R turnover method employed by Staff to estimate collections lag. However, instead of using a single A/R balance, the A/R turnover method employs an average of monthly A/R balances for a representative period, usually twelve months. This average balance is then divided by the average daily revenue, calculated over the same time period. The result of this division is the average number of days per month that bills have been outstanding, also known as the collections lag.

Q. PLEASE EXPLAIN WHY STAFF REFERS TO THE ABOVE METHOD AS THE STANDARD A/R TURNOVER METHOD.

A. Staff believes the method is standard for two reasons. First, it is used in New Hampshire to estimate supply-related collections lag for both gas and electric utilities. This is so because the currently effective supply-related cash working

[5] A/R amounts written off as uncollectible reduce the balance in the A/R account.

capital allowances for Northern, Unitil and National Grid are based on this method. Because PSNH does not collect a supply-related cash working capital allowance, it does not use this method. Second, the method is commonly used in other states. In California, for example, the Commission's Standard Practice U-16 specifies two basic approaches for computing collections lag: namely, statistical sampling and the ratio of A/R to credit sales method (also known as accounts receivable turnover method). It is also used in Massachusetts by Fitchburg Gas and Electric to calculate collections lag for that company's electric and gas divisions.

Q. MS. LEARY DISPUTES MR. MCCLUSKEY'S CLAIM THAT THE REPLACEMENT OF MONTHLY REVENUES IN THE A/R TURNOVER METHOD WITH ROLLING TWELVE MONTH GAS COSTS CREATES A MISMATCH WITH THE MONTHLY A/R BALANCES. HOW DOES STAFF RESPOND?

A. In his direct testimony, Mr. McCluskey asserted that the great majority of the revenues that make up A/R balances relate to accounts that have been outstanding for less than 30 days.[6] This means that almost all of the 2005 monthly A/R balances used by both Ms. Leary and Mr. McCluskey to calculate collections lag reflect in large part 2005 gas prices. However, if each of these A/R balances is divided by the average daily revenue for the previous twelve months, as advocated by KeySpan, a mismatch will be created if gas prices in 2004 are

[6] That is, most customers pay their bills on time.

significantly different from gas prices in 2005. For this reason, Mr. McCluskey recommended that the use of rolling twelve month gas costs be rejected.

Ms. Leary responded to this recommendation by claiming that the mismatch is insignificant because only 55% of the A/R balances, not the great majority as Mr. McCluskey alleged, relate to accounts that have been outstanding for fewer than 30 days. Using this percentage, Ms. Leary then asserted that "in the first month" of Mr. McCluskey's calculation (i.e., January 2005) "45% of the accounts receivable balance relates to the prior months' revenues…... In other words, 45% of the A/R balance for the month of January 2005 reflects revenues that were billed sometime in 2004." Clearly, Ms. Leary's purpose in making this claim is to justify the use of revenues in the divisor that reflect some level of consumption in 2004. The problem with this claim, however, is that it is based on bogus data, as the table below clearly demonstrates.

Table 1

KeySpan Accounts Receivable
Aging Analysis (%)

	Days Outstanding				Percent
	0-30	31-60	61-120	Over 121	Prior Year
2006					
January	74%	13%	5%	9%	26.14%
February	64%	19%	8%	9%	17.11%
March	63%	15%	14%	9%	15.60%
April	52%	20%	17%	11%	11.12%
May	40%	18%	26%	17%	
June	36%	13%	27%	23%	
July	37%	11%	21%	31%	
August	34%	10%	16%	41%	
September	43%	8%	12%	37%	
October	52%	8%	9%	31%	
November	62%	8%	6%	24%	
December	68%	10%	6%	16%	
Annual Avg	**56%**	**14%**	**13%**	**18%**	

Although the table does show that on average 45% (actually 44%) of over due accounts in 2006 were outstanding for more than 30 days, that percentage cannot be applied to January 2005 for two reasons. First, the table says nothing about 2005 because the data relates to 2006. Because the Company chose to discard all of its pre-2006 data on the aging of A/R, neither Staff nor the Company has any way of knowing whether the percentages in the table are reasonably representative of 2005 conditions. Second, even if we make the assumption that 2006 is reasonably representative of 2005, it is simply inappropriate to apply the annual average percentage (i.e., 44%) to the month of January when the table shows the appropriate percentage for that month to be 26%. Furthermore, as we move further and further away from 2005 the percentage of the monthly A/R balance that reflects revenues billed sometime in 2005 gets progressively smaller. For example, the percentage falls to just 17% by the end of February 2005 and to 11% by the end of April 2005. In succeeding months, the actual percentage could be zero. Indeed, if we assumed that the percentage of the A/R balance for each month from May through December 2005 that reflects revenues billed in 2005 is zero, then the average for the whole of 2005 would be just 6%. For these reasons, Staff rejects Ms. Leary's argument that a significant percentage of the 2005 monthly A/R balances in Exhibit GRM-3 are reflective of 2004 gas prices.

Q. IF THE COMPANY CANNOT SUPPORT ITS CLAIM THAT A SIGNIFICANT PERCENTAGE OF THE MONTHLY A/R BALANCES IN EXHIBIT GRM-3 REFLECT 2004 GAS PRICES, WHAT DOES THAT SAY FOR THE USE OF ROLLING TWELVE MONTH GAS COSTS TO CALCULATE COLLECTIONS LAG?

A. If the Company cannot support its claim, the use of rolling twelve month gas costs in the A/R turnover method will cause the collections lag to be overstated during a period of rising gas prices.

Q. MS. LEARY ALSO ALLEGES THAT THE STANDARD A/R TURNOVER METHOD IS CONFISCATORY DURING A PERIOD OF GENERALLY RISING GAS PRICES. WHAT IS STAFF'S RESPONSE?

A. Ms. Leary's allegation is based on the claim that the 2005 A/R balances are substantially reflective of low 2004 gas prices. Because the Company can not support that claim, it cannot demonstrate that the standard A/R turnover method is confiscatory.

Flaw 3: Adjusting A/R Balances For Net Write-Offs Instead Of Gross Write-Offs Overstates Collections Lag

Q. MS. LEARY CLAIMS THAT MR. MCCLUSKEY INCORRECTLY REDUCED A/R BALANCES BY AN AMOUNT EQUAL TO THE SUM OF THE PAYMENTS RECEIVED FROM CUSTOMERS AFTER ACCOUNTS HAD BEEN WRITTEN OFF. WHAT IS THE BASIS FOR THIS CLAIM?

A. Ms. Leary's claims that KeySpan calculates its end-of-month A/R balances by taking the prior month's ending balance, adding the revenues billed for that month (i.e., new accounts receivable), and subtracting: (i) existing receivables written off during the month; and (ii) cash receipts received in that month (i.e., bills paid plus recoveries from previously written off accounts). Because the monthly cash receipts include recoveries of previously written off accounts, Ms. Leary contends that the existing receivables written off must be net of recoveries from previously written off accounts (i.e., net write-offs) in order to avoid double counting.

Q. DOES STAFF AGREE?

A. Yes.

Q. WAS STAFF AWARE THAT THE A/R BALANCES USED BY THE COMPANY IN ITS LEAD/LAG STUDY WERE NET OF RECOVERIES FROM PREVIOUSLY WRITTEN OFF ACCOUNTS?

A. No. In response to a discovery request enquiring whether the A/R balances had been adjusted for any reason other than the write-off of overdue accounts, the Company responded that they had not.[7]

Q. HOW DOES THIS CHANGE YOUR COLLECTIONS LAG RECOMMENDATION?

A. Adjusting the A/R balances for net write-offs instead of gross write-offs increases the collections lag from 37.68 days to 37.79 days, an increase of 0.11 days. The calculation is provided in Staff Exhibit-7.

Q. MS. LEARY CONTENDS THAT MR. MCCLUSKEY, WHEN CALCULATING GAS COST RELATED A/R BALANCES, MULTIPLIED THE TOTAL ACCOUNTS RECEIVABLE BALANCE BY THE RATIO OF GAS COSTS TO TOTAL FIRM REVENUES INSTEAD OF THE RATIO GAS REVENUES TO TOTAL FIRM REVENUES. DOES STAFF AGREE WITH THIS CRITICISM?

A. Staff agrees that using gas costs instead of gas revenues introduces an element of inconsistency into the calculation of collections lag. Staff points out, however, that the gas cost related A/R balances used by Mr. McCluskey to calculate collections lag were not calculated by him but taken directly from Page 7 of the KeySpan lead/lag study. Thus, Ms. Leary rather than Mr. McCluskey erred in mixing gas costs and total firm revenues. Nonetheless, correcting for this error

[7] See KeySpan response to Staff 1-9 shown as Staff Exhibit-6.

increases the collections from 37.68 days to 38.75 days inclusive of 0.11 days for the change from gross to net write-offs discussed above. The two changes combined increase Staff's recommended collections lag by 1.07 days. The calculation is provided in Staff Exhibit-8.

Q. HOW DOES THIS CHANGE YOUR RECOMMENDED NET LAG?

A. My revised collections lag is 36.75 days. When this lag is added to a 15.21 days service lag and a 1.51 days billing lag, it produces a revised revenue lag of 53.47 days. Subtracting an expense lead of 39.99 days from the revised revenue lag produces a net lag of 13.48 days.

IV. BAD DEBT PERCENTAGE

Q. MR. MCCLUSKEY RECOMMENDED IN HIS DIRECT TESTIMONY THAT KEYSPAN'S BAD DEBT PERCENTAGE BE BASED ON ACTUAL WRITE-OFFS INSTEAD OF THE UNCOLLECTIBLE ACCOUNTS EXPENSE. THIS RECOMMENDATION, IF ADOPTED, WOULD BRING KEYSPAN IN LINE WITH NORTHERN, UNITIL, PSNH AND ITS PARENT NATIONAL GRID. DID THE COMPANY ADDRESS THAT RECOMMENDATION?

A. Neither Ms. Leary nor Ms. Ahern address this issue in rebuttal testimony. Ms. Ahern, however, continues to recommend a bad debt percentage (i.e., 2.98%) based on KeySpan's uncollectible accounts expense for 2005. Thus, because KeySpan did not rebut the arguments put forth by Mr. McCluskey in support of a bad debt percentage based on net write-offs, the Commission should find that the Company failed to meet its burden of showing that use of uncollectible accounts expense is just and reasonable.

Q. IN ADDITION TO RECOMMENDING THAT THE BAD DEBT PERCENTAGE BE BASED ON ACTUAL NET WRITE-OFFS, MR. MCCLUSKEY RECOMMENDED THAT KEYSPAN BE ALLOWED TO COLLECT ONLY A PORTION OF THE ACTUAL NET WRITE-OFF IN 2005. WHAT WAS THE BASIS OF THAT RECOMMENDATION?

A. Mr. McCluskey's recommendation was made in recognition of two basic facts. First, KeySpan's collections performance, as measured by the ratio of net write-offs to revenues (i.e., the bad debt percentage), was substantially below that of any other New Hampshire utility in 2005 and 2006.[8] Second, allowing 100% recovery of the net write-off would simply flow the costs of KeySpan's sub-standard collection practices through to paying customers without providing an incentive to improve.

Q. DID THE COMPANY ADDRESS THIS RECOMMENDATION?

A. Yes, Ms. Leary responded with three arguments. First, she contends that comparing gas utilities with electric utilities is not appropriate. Second, she claims that differences in the bad debt percentage for KeySpan and Northern are explained by demographic differences between the two service territories rather than differences in collection performance. Third, she notes that KeySpan has historically experienced a greater collection lag than Northern.

As regards the first argument, Staff notes that the Company provided no evidence to support its contention that electric utility data is not relevant when drawing

[8] See direct testimony of George McCluskey, page 12, Table 2.

conclusions regarding the collection performance of gas utilities. Rather, the Company makes the assumption that consumers are likely to give a significantly higher priority to payment of their electric bills than their gas bills. Absent reliable information in support of that assumption, Staff recommends that the Commission weigh equally electric and gas utility data on collections performance.

Q. WHAT DOES THAT DATA SHOW?

A. The data in Table 2 to Mr. McCluskey's direct testimony shows that KeySpan's bad debt percentage, a reliable measure of collections performance, is approximately seven times the average for electric utilities and approximately three times the percentage for Northern.

Q. HOW DOES STAFF RESPOND TO MS. LEARY'S SECOND ARGUMENT?

A. Based on a single fact[9] (i.e, that KeySpan has twice as many customers receiving the low income discount as a percent of residential heating customers as Northern), Ms. Leary claimed that demographic differences exist between the KeySpan and Northern service territories While Staff does not dispute this fact, it does dispute the conclusion drawn by Ms. Leary. Rather than explain KeySpan's poor collections performance compared to Northern, Staff believes that Keyspan's collections performance should be marginally better than Northern's if the only difference between the two companies is that KeySpan has twice as many customers receiving the low income discount as Northern. This is so because

[9] See KeySpan response to Staff 3-47 shown in Staff Exhibit-9.

there is a greater likelihood that low income customers would pay their bills if they receive low income discounts.

Q. IS THERE ANY DIRECT OR INDIRECT SUPPORT FOR STAFF'S POSITION?

A. Yes, we believe there is. The fact that the Company was unable to explain why its collections performance would be adversely impacted simply because a larger percentage of its customers receive a discount on their bills raises serious concerns as to the validity of the argument.[10] It is also important to note that the Company declined to quantify the effect of the alleged impact on KeySpan's collections lag.

Q. WHAT IS STAFF'S RESPONSE TO MS. LEARY'S THIRD ARGUMENT?

A. Ms. Leary argued that because KeySpan has historically experienced a greater collections lag than Northern the differences must be attributable to differences in service territory demographics, specifically the percentage of residential customers enrolled on the low income discount rate. For the reasons provided above, Staff believes that this difference should improve rather than worsen KeySpan's collections performance. Our testimony will also later explain why the difference in enrollment in the low income discount rate is not sufficient evidence to support the view that there are different income demographics in the two companies' service areas.

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[10] See KeySpan response to Staff 3-13 shown in Staff Exhibit-10.

Q. DID THE COMPANY ALSO ARGUE THAT THE INCREASE IN THE BAD DEBT PERCENTAGE EXPERIENCED BY KEYSPAN OVER THE PERIOD 2001-2006 IS NOT NECESSARILY AN INDICATOR OF DECLINING COLLECTIONS PERFORMANCE?

A. Yes, Ms. Leary argued that the bad debt percentage is not a good indicator of collections performance during periods of increasing gas prices and that the increase in the percentage could be explained by "the fact that during periods of increasing gas costs the number of customers who can not pay their bills increases." Staff disagrees with this argument for two reasons. First, Ms. Leary provides no evidence to support her contention that increasing gas prices result in higher levels of bad debt and, by implication, increase in the bad debt percentage. We point this out because Northern experienced the same increase in gas prices over the period 2001-2006 but reported relatively little increase in its bad debt percentage. In addition, if disposable income increased at the same rate as gas prices, it would not be unreasonable to expect little if any increase in bad debt levels. Second, even if bad debt levels did increase during the period 2001-2006, it does not follow that the bad debt percentage would increase also. As Ms. Leary indicated, the increase in bad debt levels is attributable to increasing gas prices, which translates into increasing revenues. Since the bad debt percentage is the ratio of net write-offs to revenues, it is possible that both the numerator and denominator could increase without a change in the percentage.

Q. IN ADDITION TO ARGUING THAT THE INCREASE IN BAD DEBT IS NOT NECESSARILY AN INDICATION OF DECLINING COLLECTIONS PERFORMANCE, KEYSPAN ALSO ARGUED THAT HIGHER GAS PRICES HAVE BEEN THE MOST SIGNIFICANT FACTOR IN ITS INCREASING BAD DEBT PERCENTAGE. WHAT IS STAFF'S POSITION?

A. It is not reasonable to claim that higher gas prices are the most significant factor in the increase in KeySpan's bad debt percentage when there is strong evidence that other factors have also contributed significantly to the increase.

Staff has already provided testimony that KeySpan's collection efforts are less robust than those of Northern Utilities. Specifically, Ms. Noonan compared the monthly disconnection data of KeySpan and Northern in Exhibit AON-3 to her June 22, 2007 testimony and noted that Northern sent out more disconnection notices as a percentage of active residential customers between November 2005 and March 2007 than did KeySpan.

In her response to Ms. Noonan's testimony, Ms. Ahern explains KeySpan's lower number of disconnection notices by noting that it is KeySpan's practice to focus more attention in its collections process on larger overdue accounts. During discovery, when questioned about Northern's collection practice, Ms. Ahern noted that, while she was not directly aware of Northern's collection practice, it was common collection practice to focus more attention on the oldest, highest balance receivables.[11] From this, Staff concludes it is a reasonable to expect that Northern also focuses more attention on its largest overdue accounts and, therefore, the difference in disconnection notices issued is attributable to something else.

Staff looked at the parameters that KeySpan uses when issuing disconnection notices.[12] Between April 1 and November 15, KeySpan issues disconnection notices to heating customers with balances greater than $500 and non-heating customers with balances greater than $125. Between November 15 and March 31, disconnection notices are not issued to heating customers; however, disconnection notices are issued to non-heating customers with balances greater than $125. Given that a typical gas heat bill is between $200 and $300[13] a month during the heating season, it is reasonable to expect that customers carrying arrears would be very likely to have balances in excess of $500 and thus be eligible to receive a disconnection notice when KeySpan begins to issue notices in April.

Q. GIVEN THE ABOVE, WHAT EXPLANATION IS THERE FOR THE LOWER PERCENTAGE OF DISCONNECTION NOTICES ISSUED BY KEYSPAN

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[11] See KeySpan response to Staff 3-52 shown in Staff Exhibit-11.

[12] See KeySpan response to Staff 3-52 and Tech 1-2 shown in Staff Exhibit-12

[13] Staff Exhibit-13 is a copy of Schedule 8 to KeySpan's 2007-2008 winter cost of gas filing. The schedules provides the estimated typical residential heating bill for the period November 1, 2007 – April 30, 2008 as well as the actual typical residential heating bill for the period November 1, 2006 – April 31, 2007. For the former period, the bills range between $172 and $281; and for the latter period, the bills ranged from $161 to $276.

AND WHY IS HAVING A LOWER NUMBER OF DISCONNECTIONION NOTICES AS A PERCENTAGE OF CUSTOMERS SIGNIFICANT?

A. Without information about the number of accounts in arrears during the same time period, it is difficult to provide a definitive explanation. While this information was requested during discovery, KeySpan stated that it did not have historical data regarding the number of accounts in arrears.[14] One possible explanation for the lower percentage of disconnection notices, however, is that KeySpan is not sending notices to every customer with a balance in excess of $500 and, therefore, not following its own collection policies.

Disconnection notices are generally the first step in the utility collection process. A disconnection notice informs the customer that the bill needs their attention or service could be shut off. For customers that are experiencing difficulty paying their bills, it notifies them to contact the utility to discuss payment and payment arrangements. Additionally, it is the trigger for many sources of financial assistance. Municipal welfare officials typically will not provide assistance to customers unless the customer is facing a potential disconnection of utility service. Emergency assistance is available from the Department of Health and Human Services, Division of Family Services, for customers facing a potential disconnection of utility service. Appointments for fuel assistance are prioritized based on whether the customer has an active disconnection notice. The disconnection notice serves as documentation for all of these agencies that the

[14] See KeySpan response to Staff 3-42 shown in Staff Exhibit-14.

customer is facing a potential disconnection of service. Assistance from all of these agencies is a guaranteed payment to KeySpan.

If KeySpan is not sending disconnection notices as outlined in its collections policy, it is likely that its lower income customers are either not seeking financial assistance with their bills or are unable to receive assistance as they cannot demonstrate that service is in jeopardy of being disconnected. As a result, KeySpan loses a source of payments that it could otherwise be receiving.

Q. IF KEYSPAN COULD HAVE DOCUMENTED THAT IT IS SENDING OUT THE APPROPRIATE NUMBER OF DISCONNECTION NOTICES, WOULD YOU AGREE WITH KEYSPAN'S POSITION THAT INCREASES IN GAS PRICES ARE THE REASON BAD DEBT LEVELS HAVE RISEN?

A. No. As is discussed in Ms. Noonan's June 22, 2007 testimony, calls from KeySpan customers clearly indicate problems with the collections process. While the disconnection notice is the first step, it is not the only step in the collections process. In her testimony, Ms. Ahern states that KeySpan's collection system is a risk-based program and that accounts receivables are managed through field activity and high risk collections. Ms. Ahern further indicates that accounts for disconnection are assigned to the field collectors by highest balance and oldest aged account and that collections staff are assigned to work all accounts greater than $2500. It is not until collections efforts for higher balance accounts have been exhausted that the company focuses attention on lower balance accounts.

From this description, it appears that little collection activity occurs on accounts with balances lower than $2,500 other than the possible issuance of a disconnection notice.

Q. WHAT IS THE POTENTIAL EFFECT OF THIS PRACTICE ON KEYSPAN'S BAD DEBT PERCENTAGE?

A. Insufficient collection activity on an account once a disconnection notice is issued can and often does result in higher arrearages. If a customer receives a disconnection notice, and does not contact KeySpan regarding a payment arrangement or make a payment, and nothing happens to his or her utility service, the notices received the following month and every month thereafter become less and less effective in collecting payment.

Customers on fixed or limited incomes will direct their scarce resources to their most pressing needs. The customer e-mail contained in Ms. Noonan's June 22, 2007 testimony provides an example of the declining effectiveness of disconnection notices when there is not sufficient collection activity beyond the notice itself.[15]

In addition, a common complaint that the Commission's Consumer Affairs Division receives from social service agencies dealing with KeySpan customers is that by the time the KeySpan bill becomes a pressing need and a customer comes

[15] Page 4 of Ms. Noonan's June 22, 2007 testimony contains an e-mail to the Consumer Affairs Division from a KeySpan customer documenting the decline in the effectiveness of disconnection notices when no further collection activity occurs.

to them for assistance, the balance is so large that they cannot provide any meaningful assistance to the customers.

Q. IS THERE OTHER EVIDENCE THAT KEYSPAN'S COLLECTION PROCESS IS LESS ROBUST THAN NORTHERN'S?

A. Yes. Staff reviewed the billing and collection related contacts it received from customers of KeySpan and Northern in 2005, 2006 and 2007. As part of its review, Staff looked at the average dollar amount owed in 2005, 2006 and 2007 as well as the average of those three years. On average over the three year period, KeySpan customers who contacted the Commission had balances that were 90% higher than those of Northern customers who contacted the Commission, as shown in the table below.

Table 2

	KeySpan	Northern Utilities
Average Balance 2005	$3412.41	$2116.64
Average Balance 2006	$2253.48	$945.25
Average Balance 2007	$2687.86	$1243.48
3 Year Average	$2755.73	$1451.82

Q. WHY IS THIS EVIDENCE THAT KEYSPAN'S COLLECTION EFFORTS ARE LESS ROBUST THAN NORTHERN'S?

A. Customers who contact the Commission's Consumer Affairs Division about billing and collection issues generally do so in response to a disconnection notice from their utility or the physical disconnection of their utility service. From the data above, it is clear that Northern is either issuing its disconnection notices earlier than KeySpan, performing disconnection of service earlier than KeySpan or both. As a result, Northern's potential bad debt exposure would be lower than that of KeySpan.

Q. MS. LEARY AND MS. AHERN CONTEND THAT A COMPARISON OF KEYSPAN'S PERFORMANCE TO THAT OF NORTHERN UTILITIES IS NOT APPROPRIATE. DOES STAFF AGREE WITH THIS ASSERTION?

A. No. Ms. Leary and Ms. Ahern both maintain that the demographics of KeySpan's service area are different from the demographics of Northern service area. Despite U.S. Census data provided by Staff showing that the income demographics for the communities served are essentially identical, the Company's witnesses point to the enrollment levels in the gas residential low income assistance program as evidence that the demographics are different. Ms. Ahern testified that 7.5% of KeySpan's residential heating customers enrolled in the discount program in 2006 as compared to an enrollment level of 3.5% of residential heating customers for Northern and therefore concludes that KeySpan's service territory has a substantially higher level of families whose limited incomes make it difficult to pay their gas bills.

In and of itself, a difference in the percentage of customers participating in the residential low income assistance program cannot be attributed to a difference in the income demographics of the service areas. As is demonstrated by applications made to the Fuel Assistance Program, there is a significant population of customers who do not apply for assistance. Experience with the Fuel Assistance Program reveals that approximately one half of the eligible households apply for assistance from the program. There are a number of reasons why a customer may not apply for assistance. Elderly customers are generally less likely to seek assistance than other customers. Some percentage of customers is too proud to ask for help. Other customers perceive the fuel assistance program as a welfare program and are resistant because of the stigma they attach to welfare. Without surveying the customers within each service area, it would be unwise to attribute meaning to the differences in the enrollment levels in the two companies programs.

Ms. Ahern further argues that it is not appropriate to compare KeySpan to Northern alone without any consideration of other gas utilities in the country. While it is interesting to see how gas utilities across the country have performed, we do not believe that is the most appropriate comparison. Unlike utilities across the country, Northern and KeySpan operate in the same regulatory and economic climate making a comparison of their performance very appropriate.

Q. ARE THERE OTHER PROBLEMS WITH THE COMPANY'S POSITION THAT THE INCREASE IN THE BAD DEBT RATIO IS CAUSED BY INCREASED GAS PRICES?

A. Yes. In response to the three customer examples provided in Ms. Noonan's testimony, Ms. Ahern stated that to shut off one of the customers "the Company went so far as to install a curb valve, which is a significant expense that is hard to justify in all but the most extreme cases." In subsequent discovery, Staff asked KeySpan to provide the costs of performing a service disconnection when there was no access to the meter.[16] Ms. Ahern indicated that the average cost of installing the curb valve necessary to perform a street shut off was $960 and that the service disconnection itself would cost $100.

Earlier in our testimony, we indicated that the average dollar amount owed by KeySpan customers contacting the Commission during the period 2005- 2007 was $2755.73. Given that the cost of performing a street shut off is less than $1100, this further supports our position that KeySpan's collections activities are not adequate.

KeySpan maintains that the examples in Ms. Noonan's testimony are atypical in large part due to the size of the balances. While the balances are high, the lack of adequate collection efforts on these three accounts are no different from the majority of the billing and collection calls the Consumer Affairs Division receives from KeySpan customers. Staff does not disagree, however, that at least two of the three balances are atypical. Under the KeySpan collections policy, all three of these accounts would have been identified as high risk and therefore should have

[16] See KeySpan response to Staff 3-51 shown in Staff Exhibit-15.

received more collection activity than other accounts. This raises even more questions about the adequacy of KeySpan's collection activities on its lower balance receivables.

As noted previously in our testimony, allowing 100% recovery of the net write-off simply flow the costs of KeySpan's sub-standard collection practices through to paying customers without providing an incentive to improve. It is possible that this lack of incentive is in fact a contributor to KeySpan's inadequate collection activity. In support of that position, Staff offers the following information. A utility analyst in the Consumer Affairs Division was recently working with KeySpan and a customer to negotiate a payment arrangement for restoration of service. The customer had an outstanding balance of $1400 at her current service location and outstanding balances of $4000 and $250 for service to prior addresses. All three accounts had been held in the same name, and the customer had provided the same social security number each time service was requested.. The Commission's administrative rules, Puc 1200, allow the transfer of balances at prior service locations to a current service location in certain circumstances. In this instance, both of the prior balances could have, and should have, been transferred to the customer's current account when she applied for service. Although KeySpan had failed to identify these two prior balances when establishing subsequent service accounts for this customer, those balances could certainly have still been transferred to her current location and been included in any calculation of an up-front payment from the customer for service restoration and the accompanying payment arrangement. In discussing the account with the KeySpan representative, the analyst was advised that Keyspan would only be pursuing collection of the outstanding balance of $1400 due on current account as the balances on the two old accounts would be put into bad debt and recovered through rates.

Q. WHAT BAD DEBT PERCENTAGE DOES STAFF RECOMMEND?

A. Staff continues to recommend that KeySpan's bad debt percentage be based on actual net write-offs and be set at the level 1.54%.

Q. DOES THIS CONCLUDE STAFF'S SURREBUTTAL TESTIMONY?

A. Yes.