STATE OF NEW HAMPSHIRE
BEFORE THE
PUBLIC UTILITIES COMMISSION

Docket DG 08-009

EnergyNorth Natural Gas, Inc.

d/b/a

National Grid NH

Rebuttal Testimony
of
Nickolas Stavropoulos

December 15, 2008

Q. Please state your name and business address.

A. My name is Nickolas Stavropoulos. My business address is 52 Second Avenue, Waltham, MA 02451.

Q. Did you prefile testimony in this case?

A. Yes. On February 25, 2008, I submitted direct testimony in support of Energy North Natural Gas, Inc. d/b/a National Grid NH's ("National Grid" or the "Company") request for a rate increase.

Overview

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is to respond to issues raised by the Staff of the New Hampshire Public Utilities Commission in their October 31, 2008 testimony, including the overall impact of their testimony on the Company's request for a rate increase and its ability to earn a reasonable return, concerns regarding the Staff's recommendation to decrease the level of depreciation included in rates, the pension and OPEB reconciling mechanism proposed by the Company, the need to allow the Company to recover a reasonable portion of its advertising and promotional expense, and the need to address the Company's proposed changes to its main extension policy in this docket. I have limited my testimony to the most significant areas of concern, although I must say that the Company made a real effort to limit its initial request for rate relief to one that it believed the Commission would find to be extremely reasonable and moderate.

Q. Are there any areas of particular concern that you feel warrant particular

attention from the Commission?

A. There are two issues that are likely to cause real concern in the investment community if the Commission does not provide the Company with adequate relief. One is the return on equity that the Commission decides to authorize, particularly in light of the highly volatile nature of the equity market and the significant tightening of the credit market that has taken hold in recent months and shows no sign of abating in any significant way. Second is the level of depreciation that is included in rates, in light of the level of capital spending that the Company has undertaken and is continuing to implement. These are areas that investors tend to pay close attention to and send a strong signal of regulatory support or lack thereof.

Q. What is the overall import of the Staff's position in this case?

A. The Staff's position, if adopted by the Commission, would effectively deny the Company any rate relief in this case. As explained in my direct testimony, the Company has not sought an increase in its base rates since 1993, despite experiencing inflation of nearly 50% during that period as well as declining average use per customer as a result of customer conservation and energy efficiency improvements to homes and natural gas heating equipment. During that same time, the Company's customers have benefited from the Company's efforts to manage costs, achieve efficiencies in its operations through two significant mergers, and invest new capital in the system to expand the Company's customer base wisely and enhance system reliability.

As shown on Attachment NS-2, since its last rate increase in 1993 the Company's operations and maintenance expense has increased on a nominal basis by approximately 24%, which represents a significant reduction taking into account inflation of nearly 50%. At the same time, that the Company's rate base has more than doubled, and the Company has implemented many new programs in New Hampshire at virtually no costs to its customers. For example, the Company was able to roll out its customer choice and energy efficiency programs by using complex systems that had already been developed and tested in other jurisdictions, thereby avoiding significant administrative costs to New Hampshire customers. In addition, the Company has streamlined much of its administrative and operating structure in order to achieve significant operating efficiencies. For example, with the implementation of a tracking system, the Company is now able to update its mapping system within 14 days, thereby improving safety and avoiding potential dig safe problems such as incorrect identification of gas mains and services. Prior to the merger, EnergyNorth was not able to update its maps on a regular basis. This record of cost-effectively operating the utility is one of which the Company is justifiably proud and which I believe should be recognized by the Commission.

In its initial filing, the Company sought an increase in its rates to address an annual revenue deficiency of $9,896,601, which represents an average increase of approximately 5.6 percent on the total bill for the average customer. In contrast, the Staff's testimony concludes that the Company has experienced a revenue deficiency of only $283,000[1]. Ironically, even though the Company's ability to achieve significant operating efficiencies has enabled it to avoid seeking a base rate increase

[1] Although Mr. Frink's testimony states that Staff calculated a revenue deficiency of $1,667,996, that figure does not reflect the impact of Staff's recommendation regarding the Company's bad debt ratio on the gas supply costs that are recovered through the Company's cost of gas mechanism. Once that impact is taken into account, the entirety of the Company's request for rate relief is essentially eliminated.

for over 15 years, thereby saving customers millions of dollars, Staff is seeking substantial disallowances for what it argues are inefficiencies in how the Company is operated. Viewing Staff's criticisms in the best light--as identifying an area where the Company could pursue further improvement--Staff's approach fails to give the Company any credit for the significant savings it has achieved and instead wrongly puts limited areas of the Company's operations under a microscope without looking at the bigger picture. In particular, the Staff has criticized the Company's collection process and has initiated an investigation into the appropriate level of bad debt expense based primarily on comparison with collections process prior to the EnergyNorth/KeySpan merger. However, the Staff fails to recognize the benefits that NH ratepayers have enjoyed as a result of various costs savings measures implemented since the time of the merger with KeySpan.

The Company is managed with the overall objective to deliver safe, reliable service in the most cost effective manner. It is unfair to judge and penalize the Company for individual practices that the Staff views as sub-par while ignoring those practices/processes that have improved and achieved significant cost savings that benefit customers. The Company believes it should be judged on its total overall performance and not solely on those specific areas identified by Staff as potential problem areas. The Staff's position is highly punitive and sends utility investors the wrong message regarding utilities in New Hampshire.

<u>Return on Equity</u>

Q. Please explain your concerns regarding the return on equity that Staff recommends the Commission authorize for the Company.

A. Compounding Staff's failure to recognize the significant operating efficiencies that the Company has achieved, the Staff recommends an inappropriately low return on equity of 9.01%. Staff's recommendation gives no meaningful consideration to the state of the equity markets, the spread between utility bond rates and those of government bonds or the need to offer equity investors a return substantially in excess of what they can expect to earn through debt issuances.

As detailed in Mr. Moul's rebuttal testimony, the turmoil in global capital markets justifies a return on equity that is even higher than what the Company initially proposed. In fact, the Staff's cost of equity witness actually points to the current economic turmoil as a basis for *lowering* the Company's allowed return, apparently ignoring the fact that investors require *higher* returns in order to invest in a volatile market.

The return proposed by Staff is a mere 1.45% above the interest rate an investor can receive on A rated utility bonds. As Mr. Moul explains in more detail, it simply is not credible that an investor would be willing to accept the added risk of an equity investment in a company such as EnergyNorth Natural Gas, Inc., when it can obtain a return of 7.56 % as a debt holder in an A rated company. Investors are skittish during these difficult times, and they need assurance from regulators in the form of reasonable allowed returns that they will be able to earn a fair return on their investment. This is particularly true in an environment in which we are experiencing declining use per customer amid significantly increased focus on the need for energy efficiency by customers.

Depreciation

Q. What is the effect of the Staff's recommendation regarding depreciation?

A. While Mr. Normand's rebuttal testimony addresses the Staff's position on depreciation in detail, I did want to comment on the overall impact of the Staff's recommendation. The Staff has recommended a reduction in the Company's depreciation expense by approximately $2.2 million. As the Commission is aware, the Company is currently in the process of making significant capital investments in New Hampshire. The Company's two year capital budget, which was submitted with the Company's filing in this case, shows a total planned investment of $51.5 million for the period 2008-09. The Company expects a similar rate of spending for the foreseeable future. Given the significant need to generate cash to help fund the Company's capital investment program, particularly given its heavy emphasis on renewal and replacement of aging infrastructure, it is simply the wrong time to significantly reduce the level of depreciation allowed to be recovered through rates. It is particularly troubling that Staff has recommended that the depreciation reserve variance be amortized over an accelerated period, thereby significantly reducing the Company's revenue requirement. The result of this treatment is likely to be considerable rate instability over time because depreciation rates frequently change from one rate case to another. I am certain that if the Company needed to recover a significant under depreciation, the Staff would not recommend that the entire amount be recovered over seven years as it has done in this case with regard to the excess depreciation that has accumulated since the Company's last rate case.

Pension/OPEB Reconciling Mechanism

Q. The Staff's testimony opposes the reconciling mechanism proposed by the Company for pension and OPEB expense; please explain your concerns.

A. As Mr. O'Shaughnessy explained in the Company's direct case, the annual expense for pension and OPEBs (post-retirement benefits other than pensions) is unlike other operating and maintenance expenses that the Company incurs. It is highly volatile, and the Company has almost no control over the level of expense because the expense is computed based on critical data that are largely dictated by law and are subject to the vagaries of the returns achieved in the market by the pension and OPEB funds as well as numerous actuarial assumptions. The Staff's testimony actually points out just how volatile pension and OPEB expense can be. The Company filed its case using the level of pension and OPEB expense that it had booked for the test year (the 12 months ending June 30, 2007). Staff argued that a better period to consider would be the 12 months ending at the end of the Company's recently adopted fiscal year (March 31, 2008), which showed a pension and OPEB expense that was $336,646 lower than during the test year. In his rebuttal testimony, Mr. O'Shaughnessy shows that a more current figure would be still more appropriate because it reflects the latest data based on changes in the market value of the pension and OPEB assets. That figure, as of October 31, 2008 is $318,535 more than the amount booked for the test year. In other words, during the sixteen months since the end of the test year, pension and OPEB expense first dropped by at least $336,000 and then increased from that point by approximately $655,000. A rate setting process that randomly selects a particular date for determining pension and OPEB expense is unlikely to protect either customers or shareholders. The increasing volatility of this single expense arguably adds significant risk to an investors' perceived ability to earn a reasonable return. By way of example, the $655,000 swing noted above represents approximately 4.49% of the Company's required net income after taxes and approximately 13.4% of the Company's actual net income for the test year.

Promotional and Advertising Expense

Q. What are your concerns regarding the Staff's position on promotional and advertising expenses incurred by the Company?

A. The Staff takes the position that the Company should not be allowed to recover any of the expense associated with its promotion and advertising efforts. These amounts were spent as part of the Company's efforts to achieve customer growth and decrease the cost of service to all of its customers. Specifically, the Staff has removed $778,317 in advertising and promotional expense from the test year, arguing that because the Company's last approved integrated resource plan did not explicitly discuss the Company's advertising program the costs should be disallowed under N.H. Code of Admin. Rule Puc 510.03(a)(7). The Staff also claims that the discrepancy in the price between oil and gas effectively eliminates the need for financial incentives for customers to convert to gas. (The Staff also argues that the Company's most recent IRP filing has not been approved and, therefore, these amounts should be disallowed. I will not address that argument since I believe it is inappropriate and unfair to disallow an amount based on a delay that is not the fault of the Company.)

Q. Do you agree with Staff's assessment of these expenses?

A. No. The primary purpose of the Company's advertising and promotional expense is to provide educational information about the Company's products, which in turn encourages customers who find it cost-effective to do so to use or convert to natural gas. All of the Company's customers benefit from the conversion of customers to natural gas because it gives the Company a broader base across which to spread its costs. Customer growth is an important means of keeping increases in rates in check, something which the Company has done very effectively during the last 15 years to the benefit of all of its customers.

Staff's claim that price differentials between oil and gas serve as a sufficient basis to motivate consumers to undertake gas conversions is similarly misplaced. Regardless of the price differential, which will necessarily fluctuate over time, the focus of the Company's advertising and promotion program is to address the factors that create obstacles to customer conversions which exist at all times, not simply when natural gas prices are higher than oil. As the Commission is well aware, the recent differential between gas and oil costs is not something that can be relied on to remain in place indefinitely, and in fact it has diminished substantially in recent months, which has substantially reduced the number of conversion requests the Company has received. Staff has provided no evidence to support its claim that the Company's advertising and promotional expenditures are unnecessary to bring about the growth relied upon to help the Company expand its customer base, other than one statement by the Company that it has recently experienced an above average number of conversions from oil to gas (and, as noted above, even that spate of conversions has now died off). Currently, the price differential between the cost for natural gas and oil for a typical residential heating customer is approximately $260 on an annual basis. However, the upfront costs associated with a gas conversion are significant – in the case of residential customers, they can range from $2,000 to $6,000,equating to a 3-10 year payback period. This incremental investment necessary to convert to natural gas is a significant obstacle for many customers, especially residential customers. Therefore, in order to promote oil to gas conversions the Company must implement various marketing programs which incent customers to convert. These conversions will result in customer growth which will benefit all customers by allowing the Company to spread its costs over a larger base and hence reduce costs to current customers. Therefore the Company believes it should be able to recover these marketing expenses in its rates.

With regard to the Staff's argument that the Company's IRP did not include consideration of the Company's marketing expenditures, a review of the information submitted in the 2004 IRP proceeding shows that the Company's promotional efforts were specifically discussed. Not only was the growth associated with the Company's marketing programs a significant component of the load forecasts that were used in preparing the IRP, but my understanding is that those programs were the subject of discovery and discussion among the parties. For the Commission's reference, I am attaching the Company's response to Data Request Staff 1-9 in that proceeding, Docket DG 04-133/DG 04-175. (Because the attachments to the response were confidential and voluminous, I am not burdening the record in this proceeding by providing them.)

Main Extension Policy

Q. Staff has also recommended that the Commission open a docket to consider the Company's proposed main extension policy. What is your position on this recommendation?

A. The Company does not believe that it is necessary to open another docket to consider the Company's proposed main extension policy. The Company has provided analysis and documentation demonstrating that the current Commission approved policy results in a return of approximately 4.4 % on a residential service extension job. The Company has proposed changes to the current main extension policy to address these unacceptably low returns, which are sufficiently described in its prefiled testimony and have been subject to extensive discovery in this proceeding. The effect of the Staff's recommendation is simply to put off for another day changes to the main extension policy, which the Company believes is not only inefficient but unnecessary. The Company has incurred significant regulatory expense because of multiple dockets in recent years on matters that were really more appropriate for a rate case. In the event that the Commission were to grant the Staff's request, the Company should be permitted to recover all of the costs associated with that effort as part of its rate case expense.

Conclusion

Q. Does this conclude your testimony?

A Yes.

ENERGYNORTH NATURAL GAS, INC.
d/b/a KeySpan Energy Delivery New England

DG 04-133/DG 04-175

EnergyNorth Natural Gas, Inc.'s Responses to Staff's Data Requests – Set 1

Data Request Received: October 29, 2004
Request No.: Staff 1-9

Date of Response: November 12, 2004
Witness: Elizabeth Arangio

REQUEST: Please provide a copy of any ENGI marketing plans in effect or developed during the Analysis Period.

RESPONSE: Although the Company did not initially object to this data request, on further review the Company has determined that it does not understand what specific documents the question is seeking. The Company intends to contact the Staff to discuss the request and determine what information the question is intended to obtain.

ENERGYNORTH NATURAL GAS, INC.
d/b/a KeySpan Energy Delivery New England

DG 04-133/DG 04-175

EnergyNorth Natural Gas, Inc.'s Responses to Staff's Data Requests – Set 1

Data Request Received: November 23, 2004

Request No.: Staff 1-9

Date of Response: December 3, 2004
Supplemental
Witness: Leo Silvestrini

REQUEST: Please provide a copy of any ENGI marketing plans in effect or developed during the Analysis Period.

The following clarification was provided by Staff on November 23, 2004. "With reference to data request 1-9, Liberty explained that the ENGI marketing plans requested were plans in effect or developed during the Analysis period that describe ENGI's overall marketing program and marketing objectives and targets, including quantitative data and data relating to new business."

RESPONSE: Attachments PUC 1-9 (a) and (b) to this response are the ENGI-specific goals excerpted from KeySpan-wide documents used to establish sales goals for the relevant years. Please note that the sales goals in the attachments are "stretch goals" used for business development purposes and therefore they are not relied on by the Company for load forecasting and supply planning purposes. Attachments PUC 1-9 (c), (d), (e) and (f) to this response are KeySpan's Gas Business Unit Marketing Plans for 2003 and 2004. These plans describe the Company's efforts to design and develop marketing strategies and tactics, advertising and promotional programs and materials, trade ally relationships, and market research to support the achievement of its sales goals. Because Attachments PUC 1-9(c) through (f) are highly sensitive confidential commercial information, they should be treated as confidential and are being provided subject to a Motion for Protective Order, which is being submitted under separate cover.

- Attachment PUC 1-9 (a), *Growth and Capital Budget Forecast EnergyNorth Fiscal Year 2003,*
- Attachment PUC 1-9 (b) *Growth and Capital Budget Forecast EnergyNorth Fiscal Year 2004*
- Attachment PUC 1-9 (c) *KeySpan Energy Delivery Gas Business Unit 2003 Residential Market Plan* (redacted),
- Attachment PUC 1-9 (d) *KeySpan Energy Delivery Gas Business Unit 2003 Business Market Plan* (redacted),
- Attachment PUC 1-9 (e) *KeySpan Energy Delivery Gas Business Unit 2004 Residential Market Plan* (redacted), and
- Attachment PUC 1-9 (f) *KeySpan Energy Delivery Gas Business Unit 2004 Business Market Plan* (redacted).