

REDACTED VERSION

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

Docket No. DG 19-_____

NORTHERN UTILITIES, INC.

**PETITION FOR APPROVAL OF
FOURTH AMENDMENT TO SPECIAL CONTRACT
WITH NATIONAL GYPSUM COMPANY**

TESTIMONY OF MICHAEL SMITH

September 13, 2019

1 **Q. Please state your name, position and business address.**

2 A. Michael Smith, Manager, Business Services, Northern Utilities, 376 Riverside Industrial
3 Parkway, Portland, Maine 04103.

4 **Q. Please describe your employment responsibilities.**

5 A. My responsibilities include retaining, expanding and attracting business within the
6 service territories of Northern Utilities (“Northern” or “the Company”). I am the point of
7 contact with Northern’s designated key business and industrial customers, and I am
8 responsible for insuring quality service and opening business communications to counter
9 competitive pressures. In addition, I manage other field sales representatives in our New
10 Hampshire and Maine service territories.

11 **Q. Please describe your education and employment background.**

12 A. I received a Bachelor of Science in Mechanical Engineering Technology in 1989 from
13 Wentworth Institute of Technology in Boston, Massachusetts. From 1989 to 1996, I was
14 employed at Northrop, Devine and Tarbell in Portland, Maine. While there, I worked as
15 a consulting engineer focusing on energy projects. In 1996, I began my career with
16 Northern Utilities and have held several positions in which I have been responsible for
17 managing Northern’s industrial and key account customers in New Hampshire and
18 Maine.

19 **Q. What is the purpose of your testimony in this docket?**

20 A. The purpose of my testimony is to present information to support Northern’s proposal for
21 extending the terms and conditions of an existing Special Contract for firm transportation

1 service with National Gypsum Company (“National Gypsum” or “the Customer”) for
2 five (5) additional years beyond the expiration date of November 30, 2019, and provide
3 for up to three (3) one-year automatic contract extension periods. As discussed below, in
4 Commission Order No. 23, 314 and the Amendment to Agreement filed in compliance
5 with that Order, Commission approval is required to effectuate an extension of the
6 Special Contract beyond the initial ten-year term.

7 **Q. Does your testimony include input from other individuals employed or previously**
8 **retained by Northern Utilities?**

9 A. Yes. My testimony relies upon the Marginal Cost Study (MCS) performed by Paul
10 Normand of Management Applications Consulting, which was filed in the Company’s
11 last rate case proceeding, DG17-070, and the results of which were filed in Exhibit 2 in
12 support of the Settlement Agreement approved by the Commission in that docket. The
13 Company updated the Customer Charge, the Main Reinforcement and Main Extension of
14 the MCS results for inflation expected through the beginning of the contract, December
15 1, 2019.

16 **Q. Are you familiar with the provisions of the Special Contract and four (4)**
17 **Amendments of Agreement that are submitted with this filing as Schedules NU 1-1**
18 **(Special Contract), NU 1-2 (Amendment of Agreement), NU 1-3 (Second**
19 **Amendment of Agreement), NU 1-4 (Third Amendment of Agreement) and NU 1-6**
20 **(Fourth Amendment of Agreement)?**

1 A. Yes. I worked directly with the Customer to negotiate the Special Contract in 1999, the
2 First Amendment of Agreement and Second Amendment of Agreement in 2009, the
3 Third Amendment of Agreement in 2011 and the Fourth Amendment of Agreement that
4 is submitted for the Commission's approval in the instant docket.

5 **Q. Please describe the circumstances that led to the negotiation and execution of the**
6 **initial Special Contract (Schedule NU 1-1).**

7 A. National Gypsum is a manufacturer of gypsum wallboard. Its corporate offices are
8 located in Charlotte, North Carolina and one of its manufacturing facilities is located at 1
9 Succi Drive, Portsmouth, New Hampshire. Natural gas is consumed in the facility's
10 drying and mill operations. National Gypsum began as an interruptible transportation
11 customer of Northern's in 1990. However, because of the extremely large volume of
12 natural gas it consumed and because Northern was going to experience at least a thirty-
13 day curtailment period for the winter of 1999-2000, the Customer wanted the security
14 associated with firm transportation service. In addition to that circumstance, newly-
15 installed interstate pipeline facilities provided the Customer with a viable option to
16 bypass Northern's system by interconnecting directly to the pipeline to obtain 365 days
17 per year firm gas service. These circumstances led the Customer to approach Northern
18 for a special pricing arrangement for firm transportation in 1999.

19 **Q. Please summarize the terms and conditions of the original Special Contract relating**
20 **to the services provided by Northern and the payment for those services by the**
21 **Customer.**

1 A. A copy of the Special Firm Transportation Agreement dated August 2, 1999 is submitted
2 with this filing as Schedule NUI-MS-1. Article 1 obligates Northern to transport and
3 deliver to the Customer during any Gas Day up to a Maximum Transportation quantity of
4 [REDACTED]. In each contract year, the Customer is required to use and/or pay
5 Northern for the transportation services for a minimum of [REDACTED] of natural
6 gas. After the initial ten-year term of the contract, the Company will determine the
7 cumulative average usage of gas over the initial term. The Customer is obligated to have
8 used and/or to pay Northern for transportation services for an annual average of
9 [REDACTED] per year during the initial term. This requirement is explained in
10 Article 3 of the Special Contract. Initially, the Customer was required to pay a customer
11 charge of [REDACTED] for the first year.
12 After the second year, Northern was allowed [REDACTED] to
13 that charge and rate as described in Article 3 of the Special Contract. Based on these
14 [REDACTED], the current rates are now [REDACTED] for the customer charge
15 and a volumetric rate of [REDACTED]. In addition to the above-described service
16 and payment provisions, the Special Contract incorporates by reference and makes a part
17 of the contract all of Northern's General Terms and Conditions and Transportation Terms
18 and Conditions as are in effect from time to time and filed with the New Hampshire
19 Public Utilities Commission. In the event of a conflict, the provisions of the Special
20 Contract govern.

21 Q. Please describe the initial term of the Special Contract.

1 A. Commission Order No. 23, 314 in docket DG 99-123 approved the Special Contract for a
2 ten-year term and required that the provisions of the Special Contract describing the term
3 thereof be amended to require Commission approval for any extension period beyond ten
4 years. The Amendment of Agreement dated October 30, 1999 (submitted herewith as
5 Schedule NUI-MS-2) was filed in compliance with Commission Order No. 23, 314. It
6 provides that the initial term of the contract is ten years from the Service Commencement
7 Date which is described in Article 5 of the Special Contract. The Service
8 Commencement date was December 1, 1999; accordingly the initial term of the contract
9 expired on November 30, 2009.

10 **Q. Please describe the provisions of the Second Amendment of Agreement, submitted**
11 **with this filing as Schedule NUI-MS-3.**

12 A. The Second Amendment of Agreement (Schedule NU-MS-3) was approved by the
13 Commission on November 25, 2009 in Order *Nisi* No. 25,047, in Docket DG 09-201. It
14 extends the provisions of the Special Contract (Schedule NUI-MS-1) as amended by the
15 Amendment of Agreement (Schedule NUI-MS-2) for an additional two years beyond the
16 contract's initial term, i.e. until November 30, 2011. The Second Amendment contains
17 language that modifies Article 4 of the Special Contract as amended by the first
18 amendment to extend the term of the contract as indicated above. The Second
19 Amendment also provides that all of the other provisions of the Special Contract remain
20 in full force and effect.

1 **Q. Please describe the provisions of the Third Amendment of Agreement, submitted**
2 **with this filing as Schedule NU-MS-4.**

3 A. The Third Amendment of Agreement (Schedule NUI-MS-4) accomplished three (3)
4 things: 1) it extended the provisions of the Special Contract as amended by the
5 Amendment of Agreement and Second Amendment of Agreement for five years beyond
6 the expiration date of November 30, 2011; 2) it provided for up to three (3) one-year
7 automatic contract extension periods; and 3) it eliminated National Gypsum's obligation
8 to make certain minimum annual payments if its facility in Portsmouth, New Hampshire
9 is permanently closed and ceases to operate. The Commission approved the Third
10 Amendment of Agreement in Order No. 25,306 issued December 22, 2011 in Docket DG
11 11-231.

12 **Q. Please describe the provisions of the Fourth Amendment of Agreement, submitted**
13 **with this filing as Schedule NUI-MS-5.**

14 A. The Fourth Amendment of Agreement (Schedule NUI-MS-5) extends the Special
15 Contract terms and conditions until November 30, 2024 and for up to three (3) successive
16 one-year periods unless terminated by the Customer or the Company with at least six (6)
17 months written notice to the other party prior to the expiration of any applicable
18 continuation period. All other provisions of the Special Contract as amended shall
19 remain in full force and effect.

20 **Q. Please explain the circumstances that led to the execution of the Fourth Amendment**
21 **of Agreement.**

1 A. Schedule NUI-MS-6 is a letter from the Customer setting forth the special circumstances
2 that support an extension of the Special Contract. In summary, many of the special
3 circumstances that led to the negotiation, execution and approval of the Special Contract
4 as described above continue to exist today. In addition, National Gypsum is facing
5 increasing competitive pressures.

6 As the second largest building material supplier in the country, National Gypsum is very
7 sensitive to changes in the general housing industry. Thus, it is imperative National
8 Gypsum take affirmative steps to manage its costs. Natural gas is the Customer's single
9 most expensive cost to operate its Portsmouth, New Hampshire plant. The Customer has
10 other plants that compete with the Portsmouth facility by producing the same products at
11 lower costs. In addition, the Customer's direct competitor, Georgia Pacific, which is
12 located in Newington, New Hampshire, bypassed Northern several years ago and is
13 taking natural gas service directly from the interstate pipeline which is located in close
14 proximity. This enables the competitor to avoid costs that National Gypsum is paying to
15 Northern and therefore puts the competitor in a stronger economic position than National
16 Gypsum. Accordingly, the National Gypsum plant in Portsmouth is under pressure to
17 control its natural gas energy costs to enable it to remain competitive. Ultimately, if
18 National Gypsum is not able to stabilize its energy costs, it could be driven out of
19 business in this region.

20 **Q. Has National Gypsum taken any steps to reduce its energy usage/costs at its**
21 **Portsmouth plant?**

1 A. Yes. Since 2003, National Gypsum has made significant investments in several projects
2 to reduce energy usage/costs at its Portsmouth facility. Those projects and costs are listed
3 in Schedule NUI-MS-6. In addition, National Gypsum [REDACTED]
4 [REDACTED]
5 [REDACTED]
6 [REDACTED]

7 **Q. Please describe the steps Northern has taken to evaluate whether the Customer**
8 **continues to have a viable bypass option.**

9 A. Northern's construction personnel have estimated and analyzed the costs associated with
10 the Customer's bypass option and have determined that the Customer continues to have
11 an economically viable option to physically bypass Northern's facilities by
12 interconnecting with the interstate pipeline. National Gypsum estimated the cost of the
13 bypass at [REDACTED] (Schedule NUI-MS-6). Northern has reviewed the cost estimate
14 and found it reasonable. At that cost, the Company believes that National Gypsum's
15 bypass option remains economically viable.

16 **Q. Has Northern performed an analysis of its long-run marginal costs to serve the**
17 **customer? If so, please describe that analysis.**

18 A. Yes. Northern used the MCS results which supported the Settlement submitted and
19 approved by the Commission in its most recent rate case, Docket DG-17-070, updated for
20 inflation through December 1, 2019. The MCS is used as a basis for computing the floor
21 price in connection with special contracts. The results of MCS were based on specific

1 customer-related and capacity-related unit marginal costs and National Gypsum's current
2 annual and design-day usage levels.

3 **Q. Please explain whether the price to be paid by National Gypsum within the Special**
4 **Contract is above Northern's long-run marginal cost to serve this Customer.**

5 A. Based on the Customer's existing gas usage and estimated December 2019 rates, annual
6 revenues of [REDACTED] would be generated under the Special Contract. These revenues
7 exceed the marginal cost estimate of [REDACTED] presented on Schedule NUI-MS-9, page 1
8 of 2. Further, the usage rate of [REDACTED] exceeds the marginal cost per therm,

9 [REDACTED] During each year of the contract, since rates and marginal costs are subject to
10 inflation factors, revenues are expected to continue to exceed the marginal costs
11 throughout the term of the Special Contract.

12 **Q. Based on your analysis, do you believe that extending the Special Contract for five**
13 **years will allow National Gypsum to gain an unfair advantage over its competitor?**

14 A. No. National Gypsum's competitor, Georgia Pacific, has already bypassed Northern and.
15 each company is subject to transportation costs on the interstate pipeline system. Also,
16 since the Company is seeking only an extension of the existing delivery service only
17 contract, then there should be no additional advantage for the Customer.

18 **Q. Do you have an opinion as to whether extending the Special Contract for five years**
19 **and modifying it to allow for up to three (3) automatic one-year extension periods is**
20 **just and reasonable and consistent with the public interest?**

1 A. Yes. I believe that National Gypsum's situation continues to present special
2 circumstances which render departure from Northern's tariffed rates just and reasonable
3 and consistent with the public interest. Extending the term of the Special Contract for
4 another five (5) years provides benefits and certainty to Northern and its other customers
5 because the annual revenues under the Special Contract exceed Northern's long-run
6 marginal costs of serving National Gypsum. Thus, retaining National Gypsum as
7 Northern's customer will continue to keep the average system costs of transporting gas
8 applicable to all of Northern's firm customers lower than it would be if Northern were to
9 lose this Customer to bypass. In addition, the Special Contract helps the Customer to
10 remain competitive and to continue its operations in New Hampshire, which contributes
11 to the state's economy.

12 Northern is mindful of the fact that the Commission expressed concerns in Order No. 23,
13 314 relative to the self-executing extension clause contained in the original Special
14 Contract executed in 1999. Those concerns were that because of the length of the term
15 of the contract, the circumstances that justified the Special Contract in 1999 might not
16 exist in the future, and therefore an extension without Commission review would be
17 inappropriate. However, many of the circumstances that justified the initial Special
18 Contract in 1999 have continued in the ensuing years and will likely continue for the
19 foreseeable future. Thus, for administrative efficiency and to provide certainty to
20 Northern, our other customers, and National Gypsum, Northern believes it is appropriate
21 for the Special Contract to continue for up to three (3) years beyond the five (5) year

1 extension period requested in this filing. This is accomplished by the self-executing
2 extension clause which provides for up to three (3) one-year extensions unless either
3 party notifies the other to the contrary at least six (6) months prior to the
4 upcoming/applicable expiration date.

5 **Q. Please explain the need for the instant filing.**

6 A. As indicated in Commission Order No. 23, 314 and the Amendment to Agreement
7 (Schedule NU 1-3) filed in compliance with that Order, Commission approval is required
8 to effectuate an extension of the Special Contract beyond the initial ten-year term.

9 **Q. Does this conclude your testimony?**

10 A. Yes.