New Hampshire Gas Company

Direct Testimony of Karen L. Zink
(DG 09-038)

I. Introduction

Q. Please state your name, employer and business address.

A. My name is Karen Zink. I am employed by The Berkshire Gas Company ("Berkshire") and my business address is 115 Cheshire Rd., Pittsfield, MA 01201.

Q. What is your position?

A. I am President, Treasurer and Chief Operating Officer for Berkshire and Treasurer for New Hampshire Gas Corporation ("NHGC" or "the Company").

Q. Could you please briefly describe your educational and professional background?

A. Yes. I graduated from Central Connecticut State University in 1979 with a Bachelor of Science degree in Finance and from Western New England College in 1997 with a Masters of Business Administration. I have held several positions with Berkshire including Supervisor of Financial Services, Supervisor of Planning, Manager of Rates and Planning, Director of Rates, Regulation and Resource Planning and Vice President. I have been the President of Berkshire since May 2004. I was elected Treasurer of NHGC in November 2003.

Q. Please summarize your responsibilities.

A. As President, Treasurer and Chief Operating Officer for Berkshire, I am responsible for the daily operations of Berkshire. I have direct responsibility for the design and implementation of Berkshire's retail rates, the preparation and presentation of rate filings before regulatory agencies, including testifying in rate case proceedings, directing the gas procurement function, and directing the transportation services of Berkshire during the transition from selling gas to transporting gas. Additionally, I have direct responsibility for long-range strategic planning and forecasting and the chief financial officer functions of Berkshire. As Treasurer of NHGC, I have chief financial officer responsibility as well as overall regulatory responsibility for the Company.

Q. Have you testified as a witness in any other proceedings involving either company?

A. I have extensive experience as a witness in Massachusetts testifying before the Massachusetts Department of Public Utilities ("MDPU"). I testified as a witness in Berkshire's last three base rate cases regarding rate design, revenue and weather normalization, and in the most recent case, I testified on behalf of a ten-year performance based rate plan (D.P.U. 90-121, D.P.U. 92-210, and D.T.E. 01-56). Further, I actively participated in the Massachusetts Gas Collaborative effort in developing model terms and conditions pursuant to D.T.E. 98-32 and D.T.E. 00-13, and sponsored Berkshire's unbundled rate initiative in D.T.E. 98-65. I have testified as a witness in Berkshire's request for approval of a LNG supply contract (D.T.E. 98-110); for approval of the Forecast and Supply Plan (D.T.E. 98-99 and D.T.E. 02-17); for approval of Berkshire's seasonal cost of gas adjustment revision (D.T.E. 01-10); for approval of a Canadian supply contract with EnCana (D.T.E. 02-56); for approval of a gas supply contract with BP Energy (D.T.E. 02-81); and for approval of an alliance arrangement between BP

Energy and the Energy East Corporation gas distribution companies, including Berkshire (D.T.E. 01-41, D.T.E. 02-19 and D.T.E. 04-47). I testified before the New Hampshire Public Utilities Commission on behalf of 1) various summer and winter Cost of Gas Adjustment Factor filings for NHGC (DG 04-050, DG 05-055, DG 05-158, DG 06-048); 2) a propane purchasing stabilization plan (DG 06-037); 3) amendments to a fixed price option program (DG 05-144); and, 4) on behalf of a joint petition for approval of the acquisition of NHGC (DG 07-083).

Q. Please describe the various industry groups of which you are a member.

A. I am a member of the Northeast Gas Association, formerly New England Gas Association. I was previously the Chairperson of the Board of Directors of the Marketing Division. I also served for several years as Chairman of the Planning and Rates Committee. Finally, I am a member of the Guild of Gas Managers.

II. <u>Overview of Testimony</u>

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to support the Company's request for a rate increase. My testimony will address the operational aspects of the Company, cost of service, capital budgets, and revenue requirements for rate relief, rate design and customer impacts. In my testimony I will present the proposed rates and the costs that support the revenue requirement and rate design proposals. My testimony will also address merger requirements. Finally, I will discuss the potential for a multi-year rate plan that will address the Company's rate requirements.

Q. Could you please briefly summarize your testimony?

A. NHGC is requesting an increase in delivery rates. The current rates are insufficient to support current operations and maintenance expenses and ongoing capital expenditures. The computation of the revenue deficiency demonstrates that the Company requires a rate increase of $423,806 which would provide the Company a fair rate of return as discussed below. These additional revenues would enable NHGC to continue to invest in the capital improvements necessary to provide a safe and reliable distribution system. In order to mitigate the bill impacts to customers immediately, the Company would like to discuss the potential for a multi-year rate plan which would distribute the rate increase over a longer period of time. Regardless of whether the increase is applied immediately or over several years, this level of rate increase will not allow the Company to achieve its requested rate of return by the end of the plan due to inflation during the term of the plan, capital expenditures, and limited growth opportunity. Nonetheless, the Company is willing to balance its needs with those of its customers. In order to simplify the rate design, the Company proposes increasing both the Customer Charge and Delivery charges in each block for both the Residential and Commercial and Industrial service classes by the overall rate increase each year.

Q. How have you organized your testimony?

A. First, I will describe the current factors causing the Company to seek rate relief. Next, I will discuss the operations and associated costs of NHGC. Third, I will discuss the test year costs and associated rate of return and revenue requirement associated with the test year. Fourth, I will discuss the Company's merger requirements pursuant to DG 07-083. Finally, I will discuss the potential for a multi-year rate plan.

Q. Are you sponsoring any exhibits as part of your filing?

A. Yes. I am sponsoring the submitted exhibits that have been included in the rate case filing pursuant to PUC 1604.01, 1604.04, 1604.07 and 1604.08, which were prepared under my supervision and direction.

Q. Can you summarize the primary factors that have caused the Company to seek rate relief?

Yes. The Company is seeking an increase in rates because it is earning significantly less than its allowed rate of return. As described in more detail below, NHGC operated at a utility net loss for the test year and will continue to operate at a loss in future years without rate relief. NHGC last received a general rate increase in January, 2003 (DG 02-003, Order No. 24,102, December 23, 2002). Since that time, the Company has experienced increases in the cost of labor, benefits, insurance, and most other operating expenses due to normal inflationary pressures. In addition, necessary capital expenditures have grown. The Company does not generate sufficient cash flow to fund these capital expenditures and NHGC's parent company must provide equity infusions in order for NHGC to meet its capital commitments. Another factor affecting revenues is continued decline in average use per customer that is being experienced by all heat related energy providers as a result of customer conservation and energy efficiency improvements.

III. Overview of Company

Q. Please describe how NHGC operates.

A. NHGC distributes propane air to approximately 1,100 customers along its 28 miles of buried main. The Company purchases propane air at cost plus an operating fee of $5,000 annually, from Keene Gas Corporation ("Keene Gas") at its plant located on Emerald Street in Keene. NHGC is a wholly owned subsidiary of Energy East Corporation. Due to its size, NHGC receives administrative, regulatory, operations and management support from The Berkshire Gas Company.

Q. How are Keene Gas and Berkshire Gas reimbursed by NHGC for their services?

A. Each month, Keene Gas submits an invoice detailing the cost of liquid propane purchased during the prior month as well as the cost of any labor and utilities expended during that period. Keene Gas is also reimbursed for property taxes, the cost of insurance and plant replacement parts throughout the year on an as-occurred basis.

Each month, Berkshire Gas submits an invoice detailing the services it provides to NHGC pursuant to a Service Agreement in effect from year to year. The most recent Service Agreement is attached as Exhibit NHG-A.

Q. Please discuss the construction budget for the calendar year 2009 as shown on Filing Requirement Data Sheet PUC 1604.01(a)(8).

A. Data Sheet PUC 1604.01(a)(8) lists various projects and initiatives which the Company intends to complete during calendar year 2009. The largest expenditure, cast and wrought iron replacement program, is in conjunction with a project for the city of Keene. The city of Keene has been mandated by the EPA to replace various sewer lines within the city limits of Keene. This project, which began in 2006 and is tentatively projected to be completed in 2014, has resulted in the replacement of existing infrastructure on the streets affected. The replacement of the sewer lines consists of full depth reconstruction which can impact the existing infrastructure and result in full replacement. Through this project, the Company expects to replace approximately 5,000 feet of cast and wrought iron main annually.

Q. Has the Company considered the use of a liquefied natural gas facility in order to serve current and potential load on its system?

A. The use of a liquefied natural gas facility is discussed below under merger requirements.

IV. <u>Development of Operating Expenses Included in the Revenue Requirement</u>

Q. Please summarize how the cost of service for New Hampshire Gas Company was determined in this proceeding.

A. The proposed revenue requirement is based upon an historical test year, which is the twelve months ended December 31, 2008. Each revenue and cost item was reviewed to determine if adjustments were necessary to reflect a normal test year. Any adjustments are described in further detail below.

Q. Please describe the data in Exhibit NHG 1-1: Computation of Revenue Deficiency.

A. This schedule presents the computation of revenue deficiency and the resulting increase in the base revenue requirement of $423,806, based on an allowed rate of return of 9.625% on a rate base of $2,755,117.

Q. Please describe the data in Exhibit NHG 1-2: Operating Income Statement.

A. This schedule presents the unadjusted operating income statement including the detail accounts for the test year.

Q. Please describe the data in Exhibit NHG 1-3: Summary of Pro Forma Adjustments Income or Expense.

This schedule presents a summary of the pro-forma adjustments to both revenues and expenses by cost of service category. Revenues are only adjusted for weather normalization and non-utility revenues and expenses, which are removed in Exhibit NHG 1-3, lines 80-90, and expenses are only adjusted for contributions, non-utility expenses, and the tax effect of these adjustments.

Q. Why did the Company only make a few adjustments?

A. In this instant filing, the Company is limiting the adjustments due to concern for bill impacts to customers. At the same time, the demonstration of the revenue deficiency supports the Company's need for an increase of $423,806. Adjustments that are not considered in this filing, among other things, are for inflation, payroll and benefit cost increases, rate base, cost of capital on incremental capital expenditures, and increased depreciation. By excluding these adjustments, there is an immediate regulatory lag in the Company's request. Thus, we would ask that the PUC consider the revenue deficiency in its entirety.

Q. Please describe the data in Exhibit NHG 1-4: Property Taxes.

A. Exhibit NHG 1-4 details property taxes expensed during the test year. There have been no pro forma adjustments.

Q. Please describe the data in Exhibit NHG 1-5: Payroll.

A. Exhibit NHG 1-5 details payroll by operating function expensed during the test year. There have been no pro forma adjustments

Q. Please describe the data in Exhibit NHG 1-7: Assets and Deferred charges.

A. Exhibit NHG 1-7 shows the Assets and Deferred Charges for the Company at December 31, 2008 and the prior years five quarter average.

Q. Please describe the data in Exhibit NHG 1-8: Stockholders Equity and Liabilities.

A. Exhibit NHG 1-8 shows the Stockholders Equity and Liabilities for the Company at December 31, 2008 and the prior years five quarter average.

Q. Please describe the data in Exhibit NHG 1-9: Materials and Supplies.

A. Exhibit NHG 1-9 shows the Materials and Supplies for the Company by account number at December 31, 2008 and the prior years five quarter average.

Q. Please describe the data in Exhibit NHG 1-10: Calculation of Rate Base.

A. Exhibit NHG 1-10 shows the calculation of the Company's Rate Base at December 31, 2008. The Company is using the 13-month average for plant, accumulated depreciation, materials and supplies, prepayments, customer deposits and deferred taxes. The average net utility plant, prepayments, customer deposits and working capital requirements are summed before subtracting the average customer deposits and deferred taxes to develop the average annual rate base for the test year. As stated previously, any capital expenditures the Company makes going forward will not be included in rates, thus, there is an immediate regulatory lag for this cost recovery. While this helps mitigate the bill impact to customers, we would request that the PUC consider the revenue deficiency in its entirety.

Q. Please describe the data in Exhibit NHG 1-11: Working Capital.

A. The Company did not perform a detailed lead lag study because the costs of such a study would be burdensome for such a small company. NHGC is making every attempt to contain costs in this rate proceeding. The Company used a 45-day lag for the operating and maintenance costs and a 30-day lag for purchased gas. These lag times are consistent with the working capital calculation approved in the Company's previous rate filing, DG 02-003, Order No. 24,102, December 23, 2002.

V. Revenue Requirements and Rate of Return

Q. How did the Company determine its revenue requirement?

A. The Company calculated the revenue requirement using a 9.625% rate of return on the average test year rate base. The required return was grossed up for taxes and compared to the current adjusted test year income. The results show that an increase in base rates of $423,806 is necessary to meet this rate of return.

Q. How was the rate of return of 9.625% developed?

A. The 9.625% rate is based on a debt/equity capital structure of 50% debt at a rate of 8% and 50% equity at a rate of 11.25%. The Company does not carry long-term debt and is currently financed with 100% equity.

Q. Will the Company be requesting recovery of the $423,806 revenue deficiency immediately?

A. No. As described below under "Rate Plan", the Company is concerned about bill impacts to its customers. An immediate $423,806 rate increase would result in an immediate distribution revenue increase of over 40%. However, due to lower gas prices, there will be a slight rate decrease even if the entire rate increase was implemented in Year One. In order to mitigate the annual impact, a multi-year rate plan with smaller rate increases each year will be more manageable for customers, especially if gas prices were to rise again.

VI. Merger Requirements

Q. In DG 07-083, Joint Petition for Approval of the Acquisition of New Hampshire Gas Corporation, there were various requirements that NHGC agreed to. Has the Company complied with those requirements?

A. Yes. Specifically, in DG 07-083, the Company agreed to (1) maintain the current level of eight full-time employees, (2) maintain its operations and service center in Keene, and (3) maintain average annual capital expenditures at no less than $275,000, adjusted for inflation, for a period of not less than five years, *i.e.* through December 31, 2012. However, these commitments would be subject to reevaluation in NHGC's next base rate case. The Company is mindful of its obligations for safe and reliable service. However, due to the state of the economy, NHGC may need to adjust some of these requirements as financial conditions warrant. Thus, the Company proposes these requirements be reevaluated in the context of its multi-year rate plan.

Q. NHGC also agreed to provide a feasibility study for siting a liquefied natural gas facility in NHGC's service territory.

A. The Company has provided that feasibility study as NHG Exhibit NHG-B.

Q. What were the results of the study?

A. The Company will provide an updated executive summary to the 2000 feasibility study by no later than April 30, 2009.

Q. Were there any other merger requirements?

A. The Company agreed not to seek to recover through rates any transaction costs or an acquisition premium associated with the transaction as well as identifying in its annual reports any accounting changes or impacts resulting from the transaction. Both of these conditions have been met.

VII. <u>Rate Plan</u>

Q. Please describe the rate plan being proposed by the Company.

A. As described previously, an immediate delivery rate increase of over 40% would be difficult for customers to manage during these economic times, even with lower gas prices. The Company recognizes the impact of costs and competitiveness of its rates and would propose working with staff to develop a multi-year rate plan that works for all parties. In the interim, the Company will be requesting temporary rates which will have no bill impact to customers. This is discussed in my pre-filed direct testimony in support of the Company's temporary rate filing.

Q. How will the rates be designed?

A. In order to simplify the rate design, the Company is proposing that each line item on the bill be increased by the overall rate increase regardless of customer class. Thus, if the Company were to implement the entire rate increase in Year One, the customer charge and three steps in the distribution rate would all be increased 42.15% for each rate class. This rate design example is demonstrated on Exhibit NHG-C. However, as discussed previously, the Company would propose working with staff to develop a multi-year rate plan that works for all parties. Nonetheless, the principles of the rate design would stay the same.

Q. Are there any other cost considerations?

A. Yes. In the Company's last rate order DG 02-003, rate case expenses were recovered as a surcharge on customer's bills. The Company would propose the same recovery mechanism this time, however, the recovery period would mirror the time period of the multi-year rate plan. Thus, for instance, if the plan is five years, the estimate of rate case expense of approximately $95,000, which includes an update for the LNG feasibility study, means an annual recovery of approximately $19,000, or $0.0143 per therm. NHGC would propose these expenses be reconciled at the end of the rate proceeding so the most up-to-date costs can be recovered.

Q. How will this rate plan impact customer's bills?

A. There will be a slightly greater than 40% distribution rate increase over the term of the plan for customers. However, by spreading the increase out evenly over the term of the plan, the year-to-year bill impact to customers will be mitigated. Nonetheless, due to lower commodity costs and the fact that the level of temporary rates is already borne by customers, the bill impact shows a slight reduction. Sample bill impacts are provided as Exhibit NHG-D. Thus, if the rate increase is spread over multiple years, there will be even more beneficial savings to customers in the first year of the plan.

VIII. Conclusion

Q. Please summarize your testimony.

A. NHGC is requesting an increase in delivery rates. The current rates are insufficient to support current operations and maintenance expenses and ongoing capital expenditures. The Company is earning significantly less than its allowed rate of return and, without rate relief, will be in a negative earnings position. A rate increase would enable NHGC to continue to invest in the capital improvements necessary to provide a safe and reliable distribution system. In order to mitigate the bill impacts to customers immediately, the Company would like to discuss the potential for a multi-year rate plan which would distribute the rate increase over a longer period of time.

Q. Does this conclude your testimony?

A. Yes it does.