

1 **I. Introduction**

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

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

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

6 A. My responsibilities include retaining, expanding and attracting business within
7 Northern Utilities' service territories. I am the point of contact with Northern's
8 designated key business and industrial customers, and I am responsible for insuring
9 quality service and opening business communications to counter competitive pressures.

10 In addition, I manage other field sales representatives in our New Hampshire and Maine
11 Division service territories.

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

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

20

21 **II. Purpose of Testimony and Description of Schedules**

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

1 A. The purpose of my testimony is to present information and documentation to
2 support Northern's proposal for extending the terms and conditions of an existing Special
3 Firm Transportation Agreement ("Special Contract") for Delivery Service (a.k.a.
4 "transportation service") with Foss Manufacturing Company, Inc. ("Foss" or "the
5 Customer") for five (5) additional years beyond the Special Contract's stated expiration
6 date to February 28, 2017 with five (5) one-year optional evergreen renewals

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

9 A. Yes. My testimony includes information and documentation supplied by Paul
10 Normand of Management Applications Consulting ("MAC") who estimated the
11 annualized long-run marginal cost to serve Foss.

12 **Q. Please identify the documents that are submitted with this prefiled testimony.**

13 A. The following Schedules are submitted with this prefiled testimony:

14	Schedule NU-1:	Special Firm Transportation Agreement;
15	Schedule NU-2:	Amendment of Agreement;
16	Schedule NU-3:	Letter Agreement (March 8, 2005);
17	Schedule NU-4:	Second Amendment of Agreement;
18	Schedule NU-5:	Third Amendment of Agreement;
19	Schedule NU-6:	Fourth Amendment of Agreement;
20	Schedule NU-7:	Fifth Amendment of Agreement;
21	Schedule NU-8:	Letter from Paul Koroski to Michael Smith
22		(November 3, 2016);

- 1 Schedule NU-9: Sixth Amendment of Agreement
- 2 Schedule NU-10: Marginal Cost and Revenue Analysis
- 3 Schedule NU-11: MAC cost data used in Marginal Cost Analysis

4 **Q. Are you familiar with the provisions of the Special Contract and the six**
5 **amendments to the Special Contract that are submitted with this filing?**

6 A. Yes. I worked directly with the Customer to negotiate the initial Special Contract
7 in 1999 and all of the Amendments of Agreement.

8

9 **III. Special Contract and (First) Amendment of Agreement**

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

12 A. Foss is Northern's second largest customer. It has a manufacturing facility
13 located in Hampton, New Hampshire which currently employs close to 500 people and
14 produces specialty fibers and engineered fabrics. Foss has been a customer of Northern
15 Utilities since 1988. In May of 1999, Foss switched from Sales to Delivery Service and
16 began purchasing gas through a third party supplier. At that time, Foss had multiple
17 alternative fuel capabilities. Prior to the execution of the Special Contract, this fuel
18 switching capability had resulted in substantial reductions in Foss's natural gas usage.
19 Although Foss had significantly increased its gas consumption during the times when the
20 Company's summer season rates applied, it was not expected to do the same during the
21 times when the Company's winter season rates applied, given the Customer's fuel
22 switching capabilities. Northern negotiated the Special Contract in October, 1999 to

1 obtain more of the Customer's firm load year round at a competitive price while
2 minimizing the risks to other customers.

3 **Q. Please summarize the terms and conditions under which Northern is**
4 **currently providing service to Foss.**

5 A. The Special Contract dated October 28, 1999 together with the Third Amendment
6 of Agreement (Schedule NU-5) and Fifth Amendment of Agreement (Schedule NU-7)
7 establish the current contractual service and payment obligations. Northern is obligated
8 to transport and deliver to the Customer during any Gas Day up to a Maximum
9 Transportation quantity of 15,500 therms. However, such transportation and delivery is
10 limited to no more than 860 therms per hour. In each contract year, the Customer is
11 required to use and/or pay Northern for the transportation services for a minimum of
12 2,400,000 therms of natural gas. The Special Contract rates are subject to an inflation
13 factor.

14
15 Currently, the Customer is required to pay a monthly customer charge of [REDACTED], a
16 monthly minimum fixed charge of [REDACTED] for the first 200,000 therms or less of usage,
17 and a minimum annual payment of [REDACTED]. Further, monthly usage volumes above
18 200,000 therms are billed at the following rates:

- 19 • Quantities between 200,000 and 300,000 therms: \$ [REDACTED] per therm
20 • Quantities between 300,000 and 400,000 therms: \$ [REDACTED] per therm
21 • All quantities over 400,000 therms: [REDACTED] per therm

1 In addition to the above-described service and payment provisions, the Customer is
2 subject to all of the other charges and fees set out in Northern's General Terms and
3 Conditions and Transportation Terms and Conditions as are in effect from time to time
4 (unless otherwise specified in Article 3 of the Special Contract).

5 **Q. Please describe the initial term of the Special Contract and any extension**
6 **thereof.**

7 A. Commission Order No. 23,381 dated January 6, 2000 in Docket DG 99-171
8 approved the Special Contract for a five (5) year term and required that the provisions of
9 the Special Contract describing the term thereof be revised to require Commission
10 approval for any extension period beyond five (5) years. The Amendment of Agreement
11 dated January 11, 2000 (Schedule NU-2) was executed in compliance with Commission
12 Order No. 23, 381. It provides that the initial term of the contract is five (5) years from
13 the Service Commencement Date which is described in Article 5 of the Special Contract.

14

15 **IV. Second and Third Amendments**

16 **Q. Please explain the circumstances that led to the execution and submission to**
17 **the Commission of the Second Amendment of Agreement.**

18 A. The amended Special Contract expired on February 28, 2005. Foss and Northern
19 executed the Second Amendment of Agreement (Schedule NU-4) effective March 1,
20 2005 to extend the Special Contract term for another five (5) years until February 29,
21 2010. By letter agreement dated March 8, 2005 (Schedule NU-3), Foss and Northern
22 agreed that if the Commission did not approve the Second Amendment of Agreement in

1 form and substance acceptable to Northern and Foss, the rate for transportation service
2 rendered from March 1, 2005 would be Northern's applicable rate schedule and that
3 Northern would recalculate the charges for services rendered since March 1, 2005 and
4 Foss would be responsible for those charges. The Second Amendment to Agreement
5 stated that Commission approval was required to effectuate an extension of the Special
6 Contract beyond the stated expiration date of February 29, 2010. On April 1, 2005,
7 Northern filed a Petition and supporting documents with the Commission seeking
8 approval of the Second Amendment of Agreement.

9 **Q. Please provide some additional background on the Second and Third**
10 **Amendments, the Staff recommendation to the Commission and the Commission's**
11 **approval of those amendments.**

12 A. In the April 1, 2005 Petition requesting approval of the Second Amendment
13 Northern explained that the Customer's desire for cost certainty and Northern's
14 commitment to continue to provide firm transportation service were the primary reasons
15 for Northern's willingness to negotiate a contract extension for five (5) more years at the
16 2000 rates expressed in the amended Special Contract. The filing also indicated that
17 there were no system improvements needed to continue serving the Customer under the
18 amended Special Contract and that revenue generated under the amended Special
19 Contract would clearly exceed the annual marginal cost revenue requirement. The filing
20 further stated that the amended Special Contract would provide Northern with a
21 continued guaranteed revenue stream that might escalate with inflation through the

1 application of an annual inflation escalator provision, and that this guaranteed revenue
2 stream would benefit Northern's other ratepayers.

3 Staff's investigation of the April 1, 2005 filing led it to conclude that an increase
4 in the Special Contract rate would be appropriate because the value of service to Foss had
5 increased slightly from when the initial Special Contract rates were established and
6 because the actual usage over the five years of the Special Contract greatly exceeded the
7 must-take provisions of the Special Contract. At Staff's request, Northern approached
8 Foss regarding an increase in the minimum payment requirements. Foss agreed to the
9 proposed increase and, along with Northern, executed the Third Amendment of
10 Agreement (Schedule NU-5) reflecting the increase. On July 1, 2005, the Commission
11 issued Order No. 24,478 approving the Second Amendment of Agreement (extending the
12 contract term to February 29, 2010 and subjecting the contract rates to an annual inflation
13 adjustment) and the Third Amendment of Agreement (which increased Foss's minimum
14 payment obligations).

15

16 **V. Fourth Amendment**

17 **Q. Please explain the circumstances that led to the execution and approval of the**
18 **Fourth Amendment of Agreement (Schedule NU-6).**

19 A. Northern informed Foss that the Special Contract as amended was scheduled to
20 expire at the end of February 2010 and that, at that time, Foss would take service from
21 Northern under tariff rates. Foss responded with a letter dated February 2, 2010
22 requesting that a filing be made with the Commission to extend the Special Contract as

1 amended. In support of its request, Foss stated that if it reverted to tariff rates, the
2 company's operations and job security at Foss's Hampton facility would be adversely
3 affected. Foss noted that it employed 319 employees whose wages have a positive
4 economic impact to the State of New Hampshire. Foss also advised Northern that the
5 State of New Hampshire, through the Business Finance Authority and Coastal Economic
6 Development Corporation, had assisted Foss with [REDACTED] in loans to acquire a state
7 of the art production line to improve operational efficiencies to maintain jobs and to keep
8 Foss competitive with its competition located in other areas of the U.S. where utility costs
9 are lower. Foss further stated that it was trying to preserve jobs that benefit New
10 Hampshire but that if the Company's tariff rates go into effect, Foss would have to
11 seriously consider eliminating skilled associate positions in its New Hampshire facility.
12 In reaction to Foss's circumstances, Northern and Foss executed the Fourth Amendment
13 to Agreement to extend the existing terms under which firm transportation service was
14 being provided to Foss for two (2) additional years, i.e. until February 29, 2012.

15 Northern and Foss sought approval for the Fourth Amendment of Agreement
16 from the Commission because the Second Amendment of Agreement expressly stated
17 that any further extension of the amended Special Contract beyond February 29, 2010
18 required Commission approval in a form and substance acceptable to Northern and Foss
19 and because the marginal cost to serve Foss was less than the marginal revenue. The
20 Commission approved the Fourth Amendment of Agreement in Order No. 25,085 issued
21 on March 25, 2010.

22

1 VI. Fifth Amendment

2 Q. Please explain the circumstances that led to the execution and approval of the
3 Fifth Amendment of Agreement (Schedule NU-7)

4 A. Northern informed Foss that the Special Contract as amended was scheduled to
5 expire at the end of February 2012 and that, at that time, Foss would take service from
6 Northern under tariff rates. Foss responded with a letter dated January 17, 2012
7 requesting that a filing be made with the Commission to extend the Special Contract as
8 amended. In support of its request, Foss stated that if it were required to pay the
9 Company's tariff rates for gas transportation service, the savings it had achieved from a
10 variety of improvement efforts made to remain competitive with companies from Mexico
11 and China, as well as from southern U.S. states, which it detailed in the letter (including
12 investments in technological improvements, replacement of the unit fork truck force,
13 negotiated reduced property tax assessment) would be lost and it would have to seriously
14 consider other options. In reaction to Foss's circumstances, Northern and Foss executed
15 the Fifth Amendment to Agreement to extend the existing terms under which firm
16 transportation service was being provided to Foss for five (5) additional years, i.e. until
17 February 28, 2017.

18 Northern and Foss sought approval for the Fifth Amendment of Agreement from
19 the Commission because the Fourth Amendment of Agreement expressly stated that any
20 further extension of the amended Special Contract beyond February 29, 2012 required
21 Commission approval in a form and substance acceptable to Northern and Foss and
22 because the marginal cost to serve Foss was less than the marginal revenue. The

1 Commission approved the Fifth Amendment of Agreement in Order No. 25,330 issued on
2 February 6, 2012.

3

4 **VI. Sixth Amendment**

5 **Q. Please explain the circumstances that led to the execution of the Sixth**
6 **Amendment of Agreement (Schedule NU-9) and this submission to the Commission**
7 **for approval.**

8 A. Northern informed Foss that the Special Contract as amended was scheduled to
9 expire at the end of February 2017 and that, at that time, Foss would take service from
10 Northern under tariff rates. Foss responded with a letter dated November 3, 2016
11 requesting an extension to the amended Special Contract. Schedule NU-8. In support of
12 its request, Foss stated that it does not compete with local companies (in New Hampshire
13 or New England) and their major U.S. competition is from companies located in Georgia
14 and the Carolinas. These southern companies benefit from lower energy costs, tax
15 burdens, and labor costs. In addition Foss continues to experience competition from
16 companies in China and Mexico. Savings experienced from the existing amended
17 Special Contract have enabled Foss to invest in multiple energy savings initiatives
18 throughout their Hampton facilities. See Schedule NU-8. Foss undertook these
19 initiatives not only to remain competitive, but also to preserve and increase the number of
20 employees at its Hampton facility. Foss has indicated that, if it were required to pay the
21 Company's tariff rates, it would consider options to mitigate the increased operating costs

1 which could lead to moving parts of their New Hampshire operation to more cost
2 effective areas of the U.S.

3 In reaction to Foss's circumstances, Northern and Foss executed the Sixth
4 Amendment of Agreement to extend the amended Special Contract for five (5) additional
5 years, i.e. until February 28, 2022. The amended Special Contract shall further continue
6 thereafter for successive one year periods unless terminated by the Company or
7 Customer. There shall be no more than five (5) renewals and the amended Special
8 Contract shall terminate on February 28, 2027.

9 This filing is being made because the Fifth Amendment of Agreement expressly
10 stated that any further extension of the amended Special Contract beyond February 28,
11 2017 required Commission approval in a form and substance acceptable to Northern and
12 Foss.

13 **Q. Has Northern performed an analysis of its marginal costs to serve the**
14 **customer? If so, please describe that analysis.**

15 A. Yes. Northern is providing an estimated annualized long-run marginal cost to
16 serve Foss (Schedule NU-10). The marginal cost is based on the 2012 marginal cost
17 study developed by Paul Normand of MAC and used to support Northern's current
18 distribution rates approved by the Commission in the Company's most recent rate case
19 proceeding, Docket DG 13-086, updated by inflation to February 2017 dollars when the
20 Sixth Amendment of Agreement becomes effective. I believe this marginal cost study
21 should be used to derive the marginal cost to serve Foss, especially on a going-forward
22 basis.

1 The MAC marginal cost analysis indicates the estimated annual cost to serve the
2 Customer is [REDACTED] in February 2017 dollars (see Schedule NU-10, Page 1 of 2.). I've
3 included as back-up MAC's 2012 marginal costs (Schedule NU-11) used to derive the
4 marginal cost estimate to serve Foss.

5 **Q. Please explain whether the price and revenue to be paid by Foss during the**
6 **extension of the amended Special Contract proposed in this filing exceeds**
7 **Northern's estimated marginal cost to serve this Customer.**

8 A. Given the pricing provisions of the Sixth Amendment, the estimated annual
9 revenue to be paid by Foss is [REDACTED] as adjusted to February 2017 dollars (see
10 Schedule NU-10, Page 2 of 2.) This is well above the aforementioned estimated
11 annualized marginal cost of [REDACTED]

12 During each year of the contract extension, marginal costs are expected to
13 escalate. Accordingly, the Sixth Amendment prices are subject to an inflation factor.
14 Therefore marginal revenue is expected to exceed the long-run marginal costs to serve
15 Foss.

16 **Q. Based on your analysis, do you believe that extending the amended Special**
17 **Contract for five (5) years will allow Foss to gain an unfair advantage over its**
18 **competitors?**

19 A. No. In my opinion special circumstances exist which support the extension of the
20 amended Special Contract for five (5) more years. As explained in Schedule NU-8, Foss
21 has made significant investments to improve its facilities and upgrade its equipment. The
22 Customer faces competitive pressures from companies located in southern states, like

1 North Carolina, South Carolina and Georgia, as well as companies located in Mexico and
2 China, where labor and utility costs are lower and where there are government subsidies
3 and a lower tax burden. Thus, Foss is under significant pressure to maintain its energy
4 costs such that it remains competitive. Foss has indicated that if it were required to take
5 transportation service under Northern's tariff rates, the savings it has achieved from a
6 variety of improvement efforts made to remain competitive with these southern
7 companies, as well as those located in Mexico and China, would be lost and it would
8 have to seriously consider other options.

9 **Q. Does Northern know whether Foss has taken steps to reduce its energy**
10 **consumption?**

11 A. The Foss letter of November 3, 2016 states that savings from the Special Contract
12 has allowed it to invest in many energy savings initiatives. Most recently, it installed
13 new lighting, an air compressor, cooling tower controls and a state-of-the-art resin drying
14 system which reduced energy cost to operate by 50%.

15

16 **Q. Based on your analysis, do you have an opinion as to whether extending the**
17 **amended Special Contract for five years with an annual evergreen provision is just,**
18 **reasonable and in the public interest?**

19 A. Yes. I believe that Foss's competitive situation continues to present special
20 circumstances which permit departure from Northern's tariff rates. Foss states that it is
21 doing its part to be a successful manufacturer and to preserve jobs that benefit New
22 Hampshire in a challenging business climate as other companies look to move their

1 operations elsewhere. Foss states that if they are to pay Northern's tariff rates, its cost
2 savings from recent facility investments would be reduced and Foss would have to
3 consider options to mitigate the cost increase which could lead to moving parts of their
4 operation from New Hampshire to more cost effective locations. Retaining Foss's load
5 under the amended Special Contract for five more years with the option to renew
6 annually for another five years, provides benefits to Northern's other customers because
7 the annual revenue under the amended Special Contract are expected to exceed
8 Northern's marginal cost to serve this Customer. Thus, retaining Foss as Northern's
9 customer should continue to keep the average system cost of transporting gas applicable
10 to all of Northern's firm customers lower than if Northern were to lose this Customer. In
11 addition, the amended Special Contract helps Foss to remain competitive with other
12 manufactures outside the area and to continue its operations in New Hampshire without
13 potential layoffs, which contributes positively to the state's economy.

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

15 **A. Yes.**