

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

THE PEOPLES GAS LIGHT & COKE	:	
COMPANY	:	No. 09-_____
	:	
Proposed General Increase	:	
In Rates For Gas Service	:	

Direct Testimony of
CHRISTINE M. GREGOR
Director
Operations Accounting
The Peoples Gas Light and Coke Company

February 13, 2009

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1 **I. INTRODUCTION AND BACKGROUND**

2 **A. Identification of Witness**

3 Q. Please state your name and business address.

4 A. My name is Christine M. Gregor. My business address is 130 E. Randolph, Chicago,
5 Illinois 60601.

6 Q. By whom are you employed and in what capacity?

7 A. I am employed by The Peoples Gas Light and Coke Company (“Peoples Gas”) as
8 Director – Operations Accounting. (I also serve in the same capacity for its affiliate
9 North Shore Gas Company (“North Shore”).) The parent company of Peoples Gas is
10 Peoples Energy Corporation (“Peoples Energy”). The parent company of Peoples Energy
11 is Integrys Energy Group, Inc. (“Integrys”).

12 **B. Purposes of Testimony**

13 Q. What is the purpose of your direct testimony?

14 A. Peoples Gas is proposing the use of its forecasted calendar year 2010 as the test year in
15 this proceeding. I will support the prudence and reasonableness of the forecasted costs
16 and expenses for calendar year 2010. More specifically:

17 (1) I will discuss the preparation of Schedules under Part 285 of the Illinois
18 Commerce Commission’s (the “Commission” or “ICC”) rules, 83 Illinois
19 Administrative (“Ill. Admin.”) Code Part 285 (“Part 285”), based on Peoples Gas’
20 forecasted and historical financials. I will describe the procedures used by
21 Peoples Gas to prepare its Annual Budget for the calendar year ending
22 December 31, 2009, and its financial forecast for the calendar year ending
23 December 31, 2010. In my testimony, I will discuss the requirements of

24 Section 285.7010 of Part 285 regarding the financial forecast and assumptions
25 being reviewed by an independent Certified Public Accountant. I will present
26 Peoples Gas' projected operating income statement for the calendar 2010 test year
27 that was developed using its budgeting and financial forecasting processes.

28 (2) I will discuss operating expense categories for which significant changes are
29 forecasted in calendar year 2010 over the actual amounts incurred in calendar year
30 2007. For Peoples Gas, I define significant as a change (either an increase or
31 decrease) of 10%, but not less than \$500,000.

32 (3) In particular, I will address Peoples Gas' expenses for depreciation, taxes other
33 than income taxes, and intercompany services.

34 (4) I will also support the ratemaking adjustments proposed by Peoples Gas witness
35 Sharon Moy (Peoples Gas Exhibit ("Ex.") SM-1.0), related to pension and welfare
36 benefits and a proposal to begin accruing for net dismantling (cost of removal, net
37 of salvage).

38 (5) I will discuss Peoples Gas' compliance with requirements of the Order and
39 Conditions of Approval in ICC Docket No. 06-0540 on merger savings and costs
40 to achieve.

41 (6) I will discuss the inventory adjustment at Manlove Field

42 (7) Finally, I will discuss Peoples Gas' compliance with billing adjustment
43 documentation as required by the Order in ICC Docket No. 03-0124 related to
44 Mt. Pisgah Missionary Baptist Church.

45 C. **Summary of Conclusions**

46 Q. Please summarize the conclusions you make in your direct testimony.

47 A. In brief, the conclusions of my direct testimony are as follows. Peoples Gas' financial
48 statements for the test year, calendar year 2010, fairly state the forecasted results of
49 operations of Peoples Gas and are appropriate as the primary basis for the determination
50 of Peoples Gas' revenue requirement in this proceeding. The ratemaking adjustments
51 referenced herein are appropriate and prudent and reasonable, including properly and
52 correctly reflecting the accounting for pension and welfare benefits and the proposal to
53 accrue for net dismantling.

54 **D. Itemized Attachments to Direct Testimony**

55 Q. Are you sponsoring any attachments to your direct testimony?

56 A. Yes. I sponsor Peoples Gas Ex. CMG-1.1, which consists of the following Schedules
57 from Peoples Gas' filing under Part 285: Schedule C-4 (Comparative Operating Income
58 Statements for Prior Years and the Test Year), Schedule C-18 (Taxes Other Than Income
59 Taxes, Page 1 of 4), Schedule C-12 (Depreciation Expense), Schedule C-13 (Summary of
60 Affiliated Interest Transactions, Page 1 of 3), and Schedule G-5 (Assumptions Used in
61 the Forecast). I will discuss these exhibits later in my testimony.

62 Q. Were these exhibits prepared under your supervision and direction?

63 A. Yes.

64 **E. Background and Experience**

65 Q. What is your educational background?

66 A. I graduated from the Eastern Illinois University 1987 and received a Bachelor of Science
67 degree in accounting. I also became a Certified Public Accountant registered in Illinois

68 in 1989. In 1993, I received a Masters of Business Administration degree from DePaul
69 University.

70 Q. Please describe your business experience.

71 A. My business experience with the Peoples Energy companies began in 1987. I was
72 directly employed by Peoples Gas from 1987 until 2002, at which time I became an
73 employee of Peoples Energy. My experience generally has involved duties and
74 supervisory positions relating to accounting and decision support/budgeting. In May
75 2006, I became an employee of Peoples Gas and assumed the position of Assistant
76 Controller – Utility Accounting and Control. I assumed my current position at Peoples
77 Gas as Director – Operations Accounting as of February 21, 2007, the date of the
78 transaction involving Peoples Energy and WPS Resources Corporation that led to the
79 latter changing its name to Integrys Energy Group, Inc., and becoming the parent
80 company of Peoples Energy.

81 Q. What are your responsibilities as Director – Operations Accounting - Peoples Gas and
82 North Shore?

83 A. My responsibilities include providing financial management analysis and direction for
84 Peoples Gas. I perform many controller-like functions for this utility. I am responsible
85 for reviewing and signing off on the monthly financial statements, including the analysis
86 of margin and unbilled revenues. I coordinate and/or participate in the preparation of the
87 Peoples Gas' operating budget (the "Annual Operating Budget") and the capital
88 expenditure budget (the Annual Capital Budget), which together comprise the Annual
89 Budget, and provide analysis of variances between actual results and forecasted amounts
90 for the entity.

91 **II. FINANCIAL STATEMENTS AND PART 285 SCHEDULES**

92 **A. Preparation of Part 285 Schedules**

93 Q. Peoples Gas Ex. CMG-1.1 sets forth certain of the Schedules required to be filed pursuant
94 to Part 285. Are those the only Part 285 Schedules in Peoples Gas' filing that were
95 prepared under your supervision and direction?

96 A. No, I am responsible for a large number of the Part 285 Schedules. I am responsible for
97 the Schedules attached hereto as part of Peoples Gas Ex. CMG-1.1 plus the other
98 Schedules attached to other Peoples Gas witnesses' testimony or included in the Part 285
99 filing to the extent that those Schedules were derived from Peoples Gas' forecasted
100 financials.

101 Q. Is the information contained in the Part 285 Schedules that is drawn from Peoples Gas'
102 forecasted financials just and reasonable?

103 A. Yes. Peoples Gas' forecasted financials for the test year, calendar year 2010, were
104 prepared in accordance with Generally Accepted Accounting Principles and they record
105 its forecasted revenues, costs, and expenses incurred in calendar year 2010. The data in
106 the Part 285 Schedules was drawn from Peoples Gas' forecasting processes and systems
107 for calendar year 2010 that I will describe later in my testimony. The data in the Part 285
108 Schedules that is drawn from Peoples Gas' books and records for prior periods is also
109 prudent and reasonable.

110 **B. Forecasting Methodology**

111 Q. What is the basis for the projected calendar 2010 financial data presented by Peoples Gas
112 in this filing?

113 A. Peoples Gas' forecast for calendar 2008, updated for actual results through June 2008
114 ("6&6" Forecast) and its calendar 2009 Annual Budget were the basic building blocks for
115 the financial projections for test year calendar 2010 presented in this filing. The Annual
116 Budget, as I noted earlier, is composed of the Annual Operating Budget and the Annual
117 Capital Budget.

118 The Annual Operating Budget reflects anticipated operation and maintenance
119 expenses for each home center as well as estimates for revenue, gas costs, depreciation,
120 taxes, interest income and interest expense. A home center is usually a company
121 department but may be related to a specific cost or activity, such as benefits expenses.

122 The Annual Capital Budget details all capital projects, mainly construction and
123 retirement expenditures, for each home center, by major capital category and general
124 charges. General charges include such items as overhead expenses (e.g., pensions and
125 employee welfare benefits) and redistribution expenses (e.g., loadings for absent time
126 allowed, stores expense, capitalized depreciation, tools and work equipment expenses,
127 and self-constructed assets).

128 Q. Please describe Peoples Gas' methodology for developing the financial projections
129 presented in this case.

130 A. For the calendar 2009 Annual Budget and the 2010 test year forecast, a set of
131 assumptions and guidelines were developed by subject matter experts and were reviewed
132 and approved prior to being entered into the system. All home centers and other
133 participants providing input for the financial projections were then required to utilize
134 these assumptions and guidelines.

158 Peoples Gas Ex. CMG-1.1 (Schedule G-5) is a summary of the principal
159 significant assumptions used to prepare the financial forecast for the test year.

160 Q. Please describe the approval process for the Annual Budget.

161 A. The Cognos system generates a variety of reports including comparisons to the prior year.
162 These reports are analyzed to ensure that the system algorithms and allocation factors
163 were inputted correctly and the results are in line with expectations and prior results, and
164 that any deviations can be explained. A detailed review of the output is performed by the
165 Director of Accounting and other personnel within the financial services division of
166 Integrys Business Support, LLC (“IBS”). Once the Annual Budget is thoroughly
167 reviewed, it is presented to the senior management of Integrys for review and approval.
168 Based on that review, the Annual Budget is deemed final or revisions are made as
169 required. Once the Annual Budget is approved by senior management, it is presented in
170 summary form to the Integrys Board of Directors. The Board reviews and approves both
171 the Annual Operating and Annual Capital Budgets. The 2009 Annual Budget was
172 presented (and approved by) the Integrys Board of Directors in December 2008. At that
173 meeting, senior management also presented several initiatives to increase net income
174 (revenues less all costs, including depreciation, interest and taxes) and reduce capital
175 expenditures for Integrys (including Peoples Gas) due to the current and potential further
176 decline in economic conditions in the United States and Illinois. These initiatives are still
177 being analyzed and are not reflected in the 2009 forecasted numbers.

178 Q. Please describe the process for the preparation of the financial forecast for the test year,
179 calendar 2010.

180 A. The test year financial forecast being presented in this case was developed following
181 essentially the same process that is used for the Annual Budget, including review and
182 approval by senior staff of Peoples Gas. However, the test year forecast was not
183 presented to the Board of Directors prior to the filing in this case because that is not a
184 regular or required business process. Similar to the above described initiatives requested
185 by the Board for 2009, senior staff of Integrys requested initiatives to increase net income
186 and reduce capital expenditures for Integrys (including Peoples Gas) for 2010. These
187 initiatives are still being analyzed and are not reflected in the 2010 forecasted numbers.

188 Q. Was the financial forecast – the Statement of Income, Balance Sheet, Statement of Cash
189 Flows and Statement of Retained Earnings – and the related notes, including Peoples
190 Gas’ summary of the underlying assumptions, examined by an independent Certified
191 Public Accountant?

192 A. Yes. The financial forecast - the Statement of Income, Balance Sheet, Statement of Cash
193 Flows and Statement of Retained Earnings – and the related notes, including Peoples
194 Gas’ summary of the assumptions underlying its forecast were examined by an
195 independent Certified Public Accountant, Deloitte and Touche LLP. The examination
196 was performed in accordance with standards established by the American Institute of
197 Certified Public Accountants (“AICPA”), including AICPA Audit and Accounting
198 Guide: Guide for Prospective Financial Information. Deloitte & Touche LLP has
199 supplied to Peoples Gas the report of an independent accountant required by Section
200 285.7010 of the ICC’s rules, and Peoples Gas has submitted that report as part of its
201 submissions under Part 285 to the ICC.

202 **C. Financial Statements**

203 Q. Please describe Schedule C-4, page 1, which is part of Peoples Gas Ex. CMG-1.1.

204 A. Schedule C-4 shows Peoples Gas' Operating Income Statements for the calendar 2010
205 test year and the three preceding years by Federal Energy Regulatory Commission
206 ("FERC") Accounts (the "Uniform System of Accounts" or "USOA"). Page 1 provides
207 aggregate figures for the categories of items within Operating Revenues, Operating
208 Expenses, and Operating Income. Column A identifies Account numbers. Column B
209 identifies Account names or categories. Columns C, D and E set forth figures based on
210 Peoples Gas' forecasted financials for calendar years 2010, 2009, and 2008 respectively.
211 Column F sets forth figures based on Peoples Gas' books and records for calendar year
212 2007.

213 Test year Other Operation and Maintenance Expenses of \$356,965,000, shown on
214 page 1, Column C, line 8, reflects all expenses recorded in Accounts 401 and 402 (detail
215 O&M accounts 700-932) other than the Cost of Gas, which is shown on page 1, Column
216 C, line 7. The test year amount shown for Other Operation and Maintenance Expenses,
217 \$356,965,000, is the same as that shown on Peoples Gas Ex. SM-1.1 at Schedule C-1,
218 page 1 of 1, line 13, Column C, sponsored by Peoples Gas witness Ms. Moy.

219 Other than Depreciation and Amortization Expense totaling \$76,004,000, (shown
220 on Schedule C-4, page 1, lines 9 and 10, Column C), the remaining operating expenses
221 (shown on Schedule C-4, page 1, lines 11 through 15, Column C) essentially represent
222 taxes imposed by federal, state, and local governments. The test year amounts shown for
223 Depreciation Expense, Amortization Expense and taxes are the same as those shown on

224 Peoples Gas Ex. SM-1.1 at Schedule C-1, page 1 of 1, lines 14-16, Column C, lines 18
225 through 21, Column C, sponsored by Ms. Moy.

226 The test year amount shown for Operating Income, \$40,505,000, on
227 Schedule C-4, page 1, line 17, Column C, is the same as that shown on Peoples Gas
228 Ex. SM-1.1 at Schedule C-1, page 1 of 1, line 23, Column C, sponsored by Ms. Moy.

229 The total operating revenues figure, \$1,658,859,000, on Schedule C-4, page 1,
230 line 5, Column C, is the same as that shown on Peoples Gas Ex. SM-1.1 at Schedule C-1,
231 page 1 of 1, line 1, Column C, sponsored by Ms. Moy.

232 The Cost of Gas figure, \$1,167,228,000, on Schedule C-4, page 1, line 7, Column
233 C, is the same as that shown on Peoples Gas Ex. SM-1.1 at Schedule C-1, page 1 of 1,
234 line 3, Column C, sponsored by Ms. Moy.

235 Q. Please describe pages 2 through 4 of Schedule C-4.

236 A. Pages 2 through 4 show in more detail Peoples Gas' Operation and Maintenance Expense
237 for the test year and the three preceding years by Account, including Cost of Gas. Total
238 Operation and Maintenance Expense for the test year, shown on page 4, Column C, line
239 44, is \$1,524,193,000. This amount is equal to the sum of the Cost of Gas on page 2,
240 Column C, line 6, and Total Operation and Maintenance, Excluding Cost of Gas on
241 page 4, Column C, line 43. Total Operation and Maintenance, Excluding Cost of Gas, for
242 the test year is \$356,965,000, as also noted above. (Also page 1, lines 7 and 8,
243 Column C.)

244 Q. Is it your position that all of the expenses reflected on Schedule C-4 that are incorporated
245 in Peoples Gas' proposed revenue requirement are prudent and reasonable in amount?

246 A. Yes, based on the information in my testimony and its attachments and that provided by
247 Peoples Gas' other witnesses.

248 **III. ACCOUNT VARIANCES**

249 Q. Have you undertaken an analysis to determine if there were significant variances in the
250 operating expense Accounts from calendar year 2007 to the test year, calendar year 2010?

251 A. Yes.

252 Q. Please explain the major events that overall lead to reasons for these variances.

253 A. Two major events have occurred that impact year to year variations shown on
254 Schedule C-4. The first is the formation of IBS and its commencement of operation at
255 the beginning of calendar year 2008. The second is the conversion of accounting data
256 from SAP to Peoplesoft. I should note that, as I explain further below, the variances to a
257 large degree consist of nominal variances, in the sense that they only reflect changes in
258 the Accounts in which amounts are recorded rather than actual changes in the total net
259 amounts.

260 Q. How did the formation of IBS impact the year to year variations?

261 A. As part of the formation of IBS, certain functions which were previously imbedded
262 within Peoples Gas were moved. These included customer relations, gas engineering, gas
263 supply, rate administration and environmental activities. In addition, prior to calendar
264 2008, service company costs were recorded in Account 923.00 (Outside Services
265 Employed) on Peoples Gas' books. During the 2007 rate case, Staff stated that Peoples
266 Gas was not in compliance with General Instruction 14 of the USOA, which states that
267 transactions with associated companies shall be recorded in the appropriate accounts for

268 affiliated transactions of the same nature. In Peoples Gas and North Shore Gas witness
269 Linda Kallas' rebuttal testimony, she responded billings from the shared services
270 organization would be recorded to the appropriate account under the USOA, as if the
271 activity had been performed directly by the utility. (ICC Docket 07-0241/07-0242 Cons.,
272 NS-PGL Ex. LK-2.0 Rev., lines 160-171). As a result, Account 923.00 has a large
273 decrease and other Administrative and General ("A&G") accounts have large increases,
274 reflecting the changes in the locations of where these amounts are recorded but no net
275 increase or decrease in costs resulted from this new accounting practice.

276 Q. How did the conversion of data to Peoplesoft impact the year to year variations?

277 A. Peoples Gas and North Shore Gas Company ("North Shore") implemented Peoplesoft in
278 the beginning of calendar year 2008. The data conversion included conformity of
279 accounting and regulatory reporting among the regulated utilities of the Integrys
280 companies, which include Peoples Gas and North Shore. Specific Accounts that changed
281 include the following: unbilled revenues moved from Account 142.00 (Customer
282 Accounts Receivable) to Account 173.00 (Accrued Utility Revenues); amounts
283 refundable to customers moved from Account 232.00 (Accounts Payable) to Account
284 242.00 (Miscellaneous Current and Accrued Liabilities). In addition, some customer
285 accounts that were not previously utilized by Peoples Gas are now having charges
286 recorded to them. These include Accounts 901.00 (Customer Service Supervision –
287 Customer Accounts Expense), 907.00 (Customer Service Supervision – Customer
288 Service and Informational Services) and 908.00 (Customer Assistance Expenses). Again,
289 the use of these new accounting practices do not result in any new net costs.

290 Q. Please explain the remaining variations.

291 A. For purposes of this analysis, I looked at major groupings of Accounts and I defined
292 “significant” to be a change, whether an increase or decrease, of at least 10% but not less
293 than \$500,000. For example, the first grouping of Accounts on Schedule C-4 is labeled
294 “Cost of Gas”. The total for these accounts for calendar year 2007 was \$899,228,000 as
295 shown on Schedule C-4, page 2, Column F, line 6. The total for these same accounts for
296 calendar year 2010 was \$1,167,228,000 (as shown on Schedule C-4, page 2, Column C,
297 line 6), a difference of over 29% and almost \$268,000,000. Therefore, I will present an
298 explanation of the variance, although it should be noted that Cost of Gas is not part of the
299 revenue requirement. However, the next grouping of Accounts on Schedule C-4 is
300 labeled “Production-Operation”. The total for these accounts for calendar year 2007 was
301 \$710,000, as shown on Schedule C-4, page 2, column F, line 10. The total for these same
302 accounts for calendar year 2010 was \$1,012,000 (Schedule C-4, page 2, column C,
303 line 10). Because the difference was only \$302,000, less than \$500,000, I am not
304 offering an explanation of this variance.

305 Q. Please explain the main driver(s) causing the increase of \$268,000,000 in Cost of Gas
306 from calendar year 2007 to the test year as shown on Schedule C-4, page 2, Columns F
307 vs. C, line 6.

308 A. Gas Costs increased mainly due to the increases in gas prices. The average cost of gas in
309 calendar year 2007 was \$7.64 per dekatherm (“dth”), compared to \$10.33 per dth for the
310 forecasted test year. These prices primarily reflect the commodity costs, hedge
311 settlements, and non-commodity costs, primarily pipeline transportation and storage
312 demand charges.

313 Note that gas costs are recovered in customers' bills under Peoples Gas' Rider 2.
314 Therefore, this increase has no effect on the portion of Peoples Gas' revenue requirement
315 to be recovered through the base rates and riders to be established in this case. The costs
316 incurred and charged to customers under Rider 2 are reviewed annually by the
317 Commission in a separate reconciliation proceeding and are not to be set in this rate case.

318 Q. Please explain the \$1,521,000 increase in expenses for the category Total Underground
319 Storage Expenses-Operation shown on Schedule C-4, page 2, Columns F and C, line 21.

320 A. There are two main reasons for this increase. One reason is a \$629,000 increase in
321 Compressor Fuel and Power (Schedule C-4, page 2, Columns F and C, line 16).
322 Compressor fuel expense is a function of the volumes used and the price of gas. This
323 increase is mainly due to the increase in gas costs described above. The other reason is a
324 \$657,000 increase in Purification Expenses (Schedule C-4, page 2, Columns F and C,
325 line 18). This increase is due to an increase in fuel used in the dehydration and CO₂
326 removal processes. The reason for the increase in these gas costs have been described
327 above.

328 Q. Please explain the \$676,000 increase in expenses for the category Total Underground
329 Storage Expense-Maintenance shown on Schedule C-4, page 3, Columns F and C,
330 line 10.

331 A. The major reason for the increase relates to higher contractor costs for maintenance
332 related to specific maintenance projects for 2010. Some of these include the replacement
333 of block studs on compressors, painting and repairing insulation at the CO₂ plant, black
334 top repair and additional painting on piping, wells and oxidizers

335 Q. Please explain the \$10,940,000 increase in expenses for the category Total Distribution
336 Expenses-Operation shown on Schedule C-4, page 3, Columns F and C, line 43.

337 A. There are several reasons that make up most of this increase. There are increased building
338 costs related to maintenance work that needs to be done at the shops, increased
339 engineering costs, and increased costs of transportation fuel and other costs related to
340 transportation vehicles.

341 Q. Please explain the \$11,807,000 increase in expenses for the category Total Distribution
342 Expenses-Maintenance shown on Schedule C-4, page 4, Columns F and C, line 9.

343 A. The major reason for this increase was the \$13,992,000 increase in Maintenance of Mains
344 Expenses (Schedule C-4, page 4, Columns F and C, line 4). In turn, the largest factor
345 causing the increase in Maintenance of Mains Expenses is increased street restoration
346 costs of \$6,328,000. In order to comply with the City of Chicago's more stringent street
347 resurfacing practices, Peoples Gas has had to expand the number of restoration
348 contractors, which has substantially increased the overall cost. Other factors causing this
349 increase were increased headcount costs related to the implementation of certain audit
350 recommendations and higher material costs. The audit was a pipeline safety audit
351 conducted by The Liberty Consulting Group under contract with the Commission.

352 Q. Please explain the \$3,463,000 increase in expenses for the category Total Customer
353 Service and Informational Services - Operation shown on Schedule C-4, page 4,
354 Columns F and C, line 22.

355 A. The reason for this increase is due to Peoples Gas conforming to the accounting and
356 regulatory reporting policies and procedures of the various regulated entities of Integrys.

357 In 2007, some of the costs that are now being recorded in this category were being
358 recorded in Sales Expenses – Operations and Customer Accounts Expense – Operation.

359 Q. Please explain the \$1,358,000 decrease in expenses for the category Total Sales
360 Expense - Operation shown on Schedule C-4, page 4, Columns F and C, line 25.

361 A. As noted in the previous questions, the major reason for this decrease is due to Peoples
362 Gas conforming to the accounting and regulatory reporting policies and procedures
363 among the regulatory entities of Integrys. Expenses previously booked into this category
364 are now being recorded in the category Total Customer Service and Informational
365 Services - Operation

366 Q. Please explain the \$29,326,000 decrease in the category Total Administrative and
367 General Expenses-Operation shown on Schedule C-4, page 4, Columns F and C, line 39.

368 A. There were two major reasons for this decrease. First and foremost, there was a
369 \$45,252,000 decrease in Miscellaneous General Expenses (Schedule C-4, page 4,
370 columns F vs. C, line 37). The largest factor causing the decrease in Miscellaneous
371 General Expenses is the \$29,448,000 decrease in amortization of environmental costs.
372 Also decreasing costs in Miscellaneous General Expenses were the one time \$23,000,000
373 conservation accrual and the \$10,900,000 charge related to the fiscal 2005 Gas Charge
374 reconciliation case that were booked in calendar 2007. Partially offsetting these
375 reductions in Miscellaneous General Expenses were increases in the amortization of the
376 costs to achieve of \$6,190,000 and Enhanced Efficiency Program (“EEP”) costs (the EEP
377 costs are recovered through Rider EEP) of \$6,362,000. Also offsetting the \$45,252,000
378 decrease in Miscellaneous General Expenses was an \$11,279,000 increase in Employee
379 Pension and Benefits. This increase is due to the movement of intercompany costs out of

380 account 923.00 and into the various accounts that would have been recorded to had that
381 transaction happened on the utility and changes in plan assumptions (primarily a change
382 in the pension and benefits discount rate and a change in the medical trend rate).

383 **IV. DEPRECIATION**

384 Q. Please explain the main driver(s) causing the increase of \$13,166,000 in Depreciation
385 expense from calendar year 2007 to the test year as shown on Schedule C-12, page 1,
386 Column L, line 9 vs. Schedule C-12, page 4, Column L, line 9.

387 A. The main driver of this increase is the increased capital costs related to the accelerated
388 cast iron replacement program.

389 Q. What is the impact on depreciation expense by using the proposed new average services
390 lives?

391 A. The impact on depreciation expense by using the proposed new average service lives is
392 an increase to depreciation expense of \$7,192,000.

393 **V. TAXES**

394 Q. Please describe Schedule C-18, included as part of Peoples Gas Ex. CMG-1.1.

395 A. Schedule C-18, page 1 of 4, details Peoples Gas' Taxes Other Than Income Taxes
396 (federal, state, and local) for the test year. The total of these taxes for the test year,
397 shown on line 20, column F is \$22,584,000. The amount charged to expense as reflected
398 in line 20, column B, \$21,496,000, ties to (agrees with) Schedule C-4, page 1, line 11,
399 column C and Schedule C-1, line 16, column C sponsored by Ms. Moy. Beginning in
400 2008, Peoples Gas adopted the accounting for regulatory reporting of netting pass-

401 through taxes with revenues and excluding these taxes from the other than income taxes
402 category with no impact on net income or the revenue requirement.

403 **VI. INTERCOMPANY SERVICES**

404 Q. Please describe Schedule C-13, included as part of Peoples Gas Ex. CMG-1.1.

405 A. Schedule C-13, pages 1 and 2, summarize Peoples Gas' transactions with affiliated
406 interests for calendar years 2010 and 2009. The exhibit shows amounts billed to Peoples
407 Gas by IBS pursuant to the Master Regulated Affiliated Interest Agreement ("Regulated
408 AIA") approved by the Commission in ICC Docket No. 07-0361 (the Regulated AIA is
409 discussed further in the direct testimony of Peoples Gas witness Michael Small, Peoples
410 Gas Ex. MAS-1.0) and the Intercompany Loan Arrangements approved by the
411 Commission in ICC Docket Nos. 04-0602 and 04-0603. The forecasted total amounts
412 billed to Peoples Gas for the test year are \$191,698,000. The exhibit also shows the
413 amounts billed by Peoples Gas to North Shore pursuant to the Services and Transfers
414 Agreement ("STA") and the Intercompany Loan Agreements, totaling \$2,245,000 for the
415 forecasted test year.

416 **VII. SUPPORT FOR RATEMAKING ADJUSTMENTS**

417 **A. Pension and Welfare Benefits Accounting**

418 Q. Please describe Peoples Gas' accounting treatment on pension and welfare.

419 A. Under accounting pronouncements (Statement of Financial Accounting Standards
420 ("SFAS") Nos. 87 and 106) of the Financial Accounting Standards Board ("FASB"),
421 actuarial gains and losses, prior service costs, and transition costs are gradually amortized
422 into net periodic benefit costs. Prior to SFAS No. 158, any unamortized amounts were
423 merely disclosed in the footnotes of Peoples Gas' year-end financial reports and were not

424 recorded on the balance sheet. SFAS No. 158 requires that these unamortized amounts
425 be recorded on Peoples Gas' balance sheet. Peoples Gas adopted this requirement
426 effective December 31, 2006.

427 The existing regulatory assets and liabilities related to benefits represent all
428 unamortized gains and losses related to Peoples Gas' pension and other postretirement
429 benefit plans, even amounts that existed as of the date of the merger with WPS Resources
430 Corporation. Such unamortized amounts at the merger date would normally be
431 eliminated if the effects of purchase accounting were pushed down to Peoples Gas. In
432 ICC Docket No. 06-0540, the Commission allowed Peoples Gas to retain these pre-
433 merger unamortized amounts on the balance sheet and continue to amortize them into
434 expense under SFAS Nos. 87 and 106. As a result, Peoples Gas' actuary is required to
435 prepare two distinct accounting valuations – one which reflects only unamortized
436 amounts since the merger date and one which reflects the unamortized amounts ignoring
437 any impact for purchase accounting.

438 At this time, Peoples Gas proposes to refine the method to account for the
439 amortization of the remaining pre-merger unamortized costs. Instead of including them
440 in the amortization in accordance with SFAS Nos. 87 and 106, PGL proposes to
441 separately identify the remaining pre-merger net regulatory assets for pension and other
442 welfare benefit plans and amortize those costs using a straight-line amortization based on
443 the average remaining service lives of the underlying benefit plans. This will eliminate
444 the need for the actuary to prepare a separate accounting valuation. This change will
445 reflect an additional decrease to pension costs and an additional increase to welfare costs
446 in the test year. While the timing of the amortization from year to year may vary, the

447 total amount recognized in expense is the same. Peoples Gas witness Ms. Moy reflects
448 these items as ratemaking adjustments in Schedule C- 2.9 and Schedule C-2.10 of
449 Peoples Gas Ex SM-1.1.

450 **B. Net Dismantling – Depreciation Expense**

451 Q. Please describe Peoples Gas’ proposed accounting treatment on net dismantling in
452 depreciation expense.

453 A. As I explained earlier in my testimony, net dismantling refers to the cost of removal of an
454 asset, net of salvage. In previous filings with the Commission over the years, Peoples
455 Gas has recognized the net dismantling portion of depreciation expense on a cash basis
456 (reflected in depreciation expense as incurred). On Schedule C-12 in Peoples Gas
457 Ex. CMG-1.1, the book depreciation expense for test year 2010 is \$76,004,000 of which
458 \$14,242,000 is related to net dismantling costs on a cash basis. Peoples Gas is proposing
459 to change its treatment of net dismantling to an accrual basis. Using the proposed net
460 salvage accrual component in the depreciation calculation results in the recognition of an
461 additional increase of \$8,094,000 of net dismantling costs and depreciation expense.
462 Peoples Gas witness Ms. Moy reflects this additional increase as a ratemaking adjustment
463 in Schedule C-2.11 of Peoples Gas Ex. SM-1.1.

464 Q. Why is the change from the cash method to the accrual method valid?

465 A. Peoples Gas is one of the few utilities that accounts for net dismantling costs on a cash
466 basis. The prevalent method is to book these costs on an accrual basis (i.e., over the life
467 of the asset) because the costs related to the life of an asset include not only the original
468 cost of the asset but also the costs to retire that asset. Therefore, customers receiving
469 service from the asset should pay rates including both of these costs over the useful life of

470 the asset which is the same period during which they received the benefit of the asset.
471 This methodology results in a better matching of costs and revenues versus the cash
472 basis.

473 **VIII. MERGER SAVINGS**

474 Q. Is Peoples Gas seeking to approve additional merger costs to be recovered beyond those
475 approved in ICC Docket No. 06-0540?

476 A. No, Peoples Gas is not seeking such an approval beyond ICC Docket No. 06-0540.
477 Peoples Gas witness Ms. Moy reflects a ratemaking adjustment to adjust amortization of
478 “cost to achieve” costs allowed in ICC Docket No. 06-0540 to avoid over-recovery, in
479 Schedule C-2.12 of Peoples Gas Ex. SM-1.1.

480 **IX. MANLOVE INVENTORY ADJUSTMENT**

481 Q. Are you aware of the adjustment to the inventory of gas in storage at Manlove Field?

482 A. Yes, I am aware of the adjustment related to the reclassification of 3.0 MMDth (million
483 dekatherms) from working gas to cushion gas as discussed by Peoples Gas witness
484 Thomas Puracchio. I am also aware of a separate reclassification of approximately
485 1.7 MMDth between recoverable and non-recoverable cushion gas.

486 Q. What is the accounting impact of these changes?

487 A. The entry to record this change will result in a reduction to Account 164 (Gas Stored –
488 Current) with a corresponding increase to Accounts 117 (Gas Stores Underground –
489 Noncurrent) and 101 (Gas Plant in Service) for the recoverable and nonrecoverable
490 pieces of cushion gas. The total reduction to Account 164 will be approximately
491 \$3.4 million and was recorded on Peoples Gas’ books in January 2009. The

492 reclassification between recoverable and non-recoverable cushion gas will result in an
493 increase to Account 117 with a corresponding decrease to Account 101 for approximately
494 \$2.0 million.

495 **X. MT. PISGAH MISSIONARY BAPTIST**
496 **CHURCH – BILLING ADJUSTMENT**

497 Q. Are you familiar with the requirements of the Commission’s final Order in ICC Docket
498 No. 03-0124 related to the billing of Mt. Pisgah Missionary Baptist Church?

499 A. Yes, as part of the final order, the Commission required documentation of the accounting
500 treatment for situations where Peoples Gas reduces a customer’s outstanding receivable
501 balance either through Commission determinations or voluntary action by the utility and
502 the effect of this action on uncollectibles.

503 Q. What is the accounting treatment for these situations?

504 A. The accounting treatment is an adjusting entry reversing the original entry. Thus the
505 accounting accorded these situations will have no effect on the calculation of the
506 percentage of Peoples Gas’ uncollectibles.

507 Q. Does this conclude your direct testimony?

508 A. Yes.