

Appendix D

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Pennsylvania Public Utility Commission	:	Docket Nos. R-2010-2215623
Office of Consumer Advocate	:	C-2011-2224941
Office of Small Business Advocate	:	C-2011-2224985
Columbia Industrial Intervenors	:	C-2011-2227004
The Pennsylvania State University	:	C-2011-2230067
Pennsylvania Communities Organizing for	:	C-2011-2232186
Change d/b/a ACTION United, Nettie	:	
Pelton and Carol Collington	:	
James Landis	:	C-2011-2224944
Marie Weaver	:	C-2011-2225050
Margaret Sentz	:	C-2011-2225828
Albert Jochen	:	C-2011-2225878
Patsy Orlando	:	C-2011-2227222
Maureen A. Doerr-Roman	:	C-2011-2231015

and

Shipley Energy Company
 Dominion Retail, Inc.
 Interstate Gas Supply, Inc.

Intervenors

v.

Columbia Gas of Pennsylvania, Inc.

Pennsylvania Public Utility Commission	:	Docket Nos. R-2010-2201974
Office of Small Business Advocate	:	C-2010-2208133
Office of Consumer Advocate	:	C-2010-2208503

and

Columbia Industrial Intervenors

Intervenors

v.

Columbia Gas of Pennsylvania, Inc.

**STATEMENT OF COLUMBIA GAS OF PENNSYLVANIA, INC.
 IN SUPPORT OF THE JOINT PETITION FOR PARTIAL SETTLEMENT**

TO ADMINISTRATIVE LAW JUDGE KATRINA L. DUNDERDALE:

I. INTRODUCTION

Columbia Gas of Pennsylvania, Inc. (“Columbia” or the “Company”) hereby submits this Statement in Support of the Joint Petition for Partial Settlement (“Settlement”) entered into by Columbia, the Office of Trial Staff (“OTS”) of the Pennsylvania Public Utility Commission (“Commission”), the Office of Consumer Advocate (“OCA”), the Office of Small Business Advocate (“OSBA”), Columbia Industrial Intervenors (“CII”), Dominion Retail, Inc. (“Dominion”), Shipley Energy Company (“Shipley”), Interstate Gas Supply, Inc. (“IGS”),¹ The Pennsylvania State University (“PSU”), and Pennsylvania Communities Organizing for Change d/b/a ACTION United, Nettie Pelton and Carol Collington (“PCOC”) (hereinafter collectively referred to as the “Joint Petitioners”), parties to the above-captioned proceedings. Columbia respectfully requests that Administrative Law Judge Katrina L. Dunderdale (“ALJ Dunderdale” or the “ALJ”) recommend approval of, and the Commission approve, the Settlement, including the terms and conditions thereof, without modification.

The Settlement, if approved, will resolve all but two issues raised by the Joint Petitioners in this proceeding. The settled issues include revenue requirement, revenue allocation, non-residential rate design, Dth billing, certain universal service program and conservation program issues, and natural gas supplier issues. The two issues reserved for litigation are residential rate design and the challenge by PCOC to Columbia’s continued use of its Commission-approved CAP-Plus methodology. The Settlement is in the best interest of Columbia, its customers, and the Joint Petitioners and is otherwise in the public interest. It should accordingly be approved.

The Settlement was achieved only after a comprehensive investigation of Columbia’s claims and operations. In addition to informal discovery, Columbia responded to over 640 formal discovery requests (many of which had multiple subparts). The active parties filed

¹ Dominion, Shipley and IGS will be referred to collectively as the “NGS Parties”.

multiple rounds of testimony and accompanying exhibits, including Columbia's direct testimony, other parties' direct, rebuttal, surrebuttal and rejoinder testimony. Moreover, the active parties participated in numerous settlement discussions and formal negotiations, which ultimately led to the Settlement.

Finally, the active parties in this proceeding, and their counsel and experts, have considerable experience in rate proceedings. Their knowledge, experience, and ability to evaluate the strengths and weaknesses of their litigation positions provided a strong base upon which to build a consensus on the settled issues.

The Settlement reflects a carefully balanced compromise of the interests of the Joint Petitioners to this proceeding. For these reasons and the reasons set forth below, the Settlement is just and reasonable and, therefore, Columbia's above-captioned base rate filing as modified by the Settlement should be approved, subject to continued litigation of the reserved issues.

II. SPECIFIC SETTLEMENT TERMS

A. REVENUE REQUIREMENT

The Settlement provides for rates to be designed to produce an increase in operating revenues of \$17.0 million based upon the pro forma level of operations at September 30, 2011, with \$16.0 million of the increase to be recovered from increased distribution rates and \$1.0 million for increased funding of the Company's Low Income Usage Reduction Program ("LIURP"). This is approximately 45% of Columbia's original request of \$37.8 million. (Columbia Exhibit 102, Schedule 3, Page 5.) The \$17.0 million increase, although less than that requested by the Company, will provide Columbia the opportunity to earn a reasonable return in order to continue to provide safe and reliable service to its customers.

As explained by M. Carol Fox, President of Columbia Gas of Pennsylvania, Inc., the Company requires additional revenues so that the Company will have an opportunity to earn a

return on the significant capital investments made to its distribution system. (Columbia St. No. 1, pp. 4-5.) As detailed in Danny G. Cote's testimony, Columbia has replaced more than twice as much bare steel main as the next highest local distribution company among its peers in Pennsylvania. (Columbia St. No. 9, p. 19.) Indeed, Columbia's capital budget for age and condition replacement of cast iron and bare steel is approximately \$86,000,000 in 2011. (Columbia St. No. 9-Supp, Exh. DGC-1.)

In this proceeding, Columbia, OTS, OCA, and OSBA presented testimony on Columbia's overall revenue requirement and related issues. As indicated above, Columbia initially requested an increase of \$37.8 million, as adjusted in rebuttal testimony to approximately \$34.5 million. (Exhibit JTG-2R, Schedule 10.)

The Settlement revenue increase of \$17.0 million reflects a reasonable compromise of Joint Petitioners' positions in this proceeding. The amount of the increase falls within the range of outcomes bounded by Columbia's proposed increase and the revenue requirements contained in the direct testimonies of OTS and OCA. Columbia notes that in its rebuttal testimony, it took issue with virtually all of the proposed adjustments advanced by OTS and OCA. The Joint Petitioners, while supporting their required revenue requirement for litigation purposes, recognized that the Commission likely would have accepted certain adjustments proposed by Joint Petitioners, but would not have accepted all of the adjustments.

Under the Settlement, with only a few select exceptions further explained below, the settlement revenue requirement is a "black box" amount. Under a "black box" settlement, parties do not specifically identify revenues and expenses that are allowed or disallowed. Columbia believes that "black box" settlements facilitate agreements as parties are not required

to identify a specific return on equity or identify specific revenues and/or expenses that are allowed or disallowed.

Under the Settlement, the revenue requirement is within the range of revenue requirements proposed by the Joint Petitioners. Given the entire Settlement, Columbia believes that the revenue requirement is reasonable and will provide Columbia with additional revenues that are necessary to provide reliable service to customers. In addition, Columbia believes that the Settlement appropriately balances the need of the Company to have an opportunity to earn a reasonable rate of return with its customers' need for reasonable rates. Finally, Columbia notes that the Joint Petitioners have agreed in the Settlement that the Commission's resolution of the issues reserved for litigation does not and shall not affect or otherwise alter the agreed upon revenue requirement amount identified in the Settlement. (Settlement, ¶ 43.)

1. Tax Repair Allowance Treatment

In 2008, Columbia sought and obtained permission from the Internal Revenue Service ("IRS") to change its definition of "unit of property" for tax purposes. This enabled Columbia to deduct certain expenditures on its tax return rather than capitalize them and it resulted in a tax refund of \$37,487,634 for Columbia's customers. (Columbia St. No. 2-Supp, p. 4.)² In Columbia's 2010 base rate case at Docket No. R-2009-2149262, the Commission approved a ten-year amortization of this refund, without interest or deduction from rate base of the unamortized amount. (Columbia St. No. 11, pp. 5-6.) In its 2010 base rate case, Columbia proposed and the Commission approved the use of a flow through methodology to account for the on-going impact of the change. (Columbia St. No. 2-Supp, p. 4.) That is, under the current structure, the Company flows through to its customers the tax benefit of the additional repairs

² The amount of the refund remains subject to IRS audit. (Columbia St. No. 11, p. 5.)

deduction by incorporating the current tax year impact in the future test year. (Columbia St. No. 2-Supp, p. 2.)

As detailed in the Company's supplemental direct testimony, after Columbia prepared the instant rate case it received \$24,000,000 in incremental capital dollars for investment during 2011. Columbia St. No. 9-Supp, p. 1. As explained by Columbia Witness Marianne L. Schuster, \$21,620,000 of this additional capital falls within the future test year. (Columbia St. No. 8-Supp, p. 2.) As shown by Columbia Witness John M. O'Brien, the additional capital investment results in an additional \$5,844,720 of repairs allowance which would reduce the Company's tax allowance claim in the tax year. (Columbia St. No. 11-Supp, Supplemental Revised Exhibit No. 107 Page 16, Line 18C.) Therefore, under the current structure, the more the Company invests in replacing cast iron and bare steel pipe, the more it lowers its revenue requirement because the current tax year impact of the additional repairs deduction is not representative of the ongoing level of repairs allowance after the future test year. (Columbia St. No. 2-Supp, p. 2.) As explained by Columbia witness Kempic:

The unfortunate effect of the flow-through approach is that it encourages the Company to limit the amount of its incremental capital investments during a test period or invest during a test period only in projects that do not qualify for the repairs deduction. This runs against the goal of replacing the Company's aging cast iron and bare steel pipe. Moreover, the flow through approach results in intergenerational mismatches. Although the assets qualifying for the repairs deduction are depreciated for book purposes, their deduction is taken in a single year for ratemaking purposes. If the investment in assets qualifying for the repairs deduction occurs outside a test period, customers will never receive the benefit of a tax deduction related to that asset.

(Columbia St. No. 2-Supp, p. 3.) To remove these disincentives, Columbia proposed to switch from the existing flow through methodology for the tax repairs allowance to an approach where the repairs allowance benefit is normalized for rate making purposes. Under the normalization

approach, the tax effect of the additional repair allowance deduction is not flowed through but deducted from rate base in future cases. The Company explained that the normalization approach is appropriate because the level of the repairs allowance will widely fluctuate with investment levels and with the amount of the capital investment that qualifies for the repairs allowance. (Columbia St. No. 2-Supp, p. 3.) Moreover, since the time the Commission approved Columbia's 2010 base rate case settlement, other Pennsylvania utilities have received approval from the Commission to normalize the on-going impact of the change in definition of "unit of property". See, e.g., *Pa. P.U.C. v. PPL Electric Utilities Corporation*, Docket No. R-2010-2161694, Order entered December 21, 2010; *Pa. P.U.C. v. Duquesne Light Company*, Docket No. R-2010-2179522 2010 Order entered February 24, 2011. No party to the instant proceeding opposed the change to normalization accounting.

Under the Settlement, the Joint Petitioners have agreed that with the effective date of rates in this proceeding, Columbia shall convert from flow through to normalization accounting procedures with respect to the benefits of the tax repairs allowance. (Settlement, ¶ 37.) Conversion to normalization accounting will remove the current disincentives discussed above and encourage the Company to continue significant capital investment to replace aging cast iron and bare steel without depriving customers of the benefits of tax deductions based upon the timing of investments in plant qualifying for the repairs deduction in relation to rate cases. Therefore, Columbia requests, consistent with recent Commission orders, that the ALJ recommend Commission approval of the Company's conversion to a normalization accounting with respect to the benefits of the tax repairs.

2. Amortizations

The Settlement specifies the continued amortizations of costs related to Long Wall Mining and Blackhawk Storage. These amortizations were established in Columbia's 2008 rate

case settlement at Docket No. R-2008-2011621 and will continue. (Settlement ¶ 38.) No party objected to the Company's inclusion of these amortization amounts in its rate filing.

As noted in the preceding section of this Statement in Support, Columbia is currently amortizing over a ten-year period, beginning October 2010, the \$37.5 million tax refund received as a result of the tax repair allowance change. As explained in Mr. O'Brien's supplemental direct testimony, the change from flow through to normalization accounting treatment for the tax repair deduction would decrease the Company's tax deduction, and thereby increase its revenue requirement in this filing. To offset the elimination of the flow through deduction of the repair allowance, the Joint Petitioners have agreed, commencing with the effective date of rates in this proceeding, to accelerate the amortization of the remaining refund amount of \$33,557,479 million with the tax relative to the change in method for the repairs deduction over 2.25 period, rather than the existing 10 year amortization period. This accelerated amortization results in an annual reduction of \$14,914,435 to the Company's claimed income tax expense. The amortization shall continue to be without interest and without a deduction of the unamortized balance from rate base. (Settlement ¶ 38.)

3. Other Post Employment Benefits ("OBEP") Expense

The Settlement includes key provisions concerning accounting for Columbia's ongoing contributions to trusts for OPEBs. In particular, under the Settlement Columbia will be permitted to continue its established procedure to defer the difference between the annual OPEB expense calculated pursuant to Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 715, "Compensation – Retirement Benefits ("SFAS No. 106") and the annual OPEB allowance included in rates of \$1,898,955. (Settlement ¶ 39.) Only those amounts attributable to operation and maintenance would be deferred and recognized as a regulatory asset. The deferred difference between the annual allowance and actual expense is

amortized in later rate cases. Columbia will continue to place OPEB amounts into dedicated trusts. If annual amounts deposited into trusts, pursuant to this Settlement, exceed allowable income tax deduction limits, any income taxes paid will be recorded as negative deferred income taxes, to be added to rate base in future proceedings. (Settlement ¶ 40.)

In addition, the Settlement resolves an issue raised by the OTS regarding the Company's original proposal to continue to annually recover its OPEB transition obligations, associated with a 1994 accounting change pursuant to Financial Accounting Standard 106 ("SFAS 106"). Specifically, in adopting SFAS 106, the Financial Accounting Standard Board ("FASB") adopted an accounting standard directing companies to convert from pay as you go accounting, to accrual accounting for post-employment benefits. (Columbia St. No. 106-R, p. 17.) At that time, a transition obligation was established to recognize the accrued liability for OPEB costs related to employee service prior to the adoption of FAS 106. Consistent with the newly adopted accounting policy, the Commission granted, at Docket No. R-00943001, Columbia's recovery of its OPEB transition obligations through an amortization set to expire in December 2012. As part of its original claim in this proceeding, Columbia proposed to continue the previously approved accounting treatment. (Columbia St. No. 6, p. 15.) However, the OTS proposed to extend the recovery period for the remaining unamortized balance of OPEB transition obligation. (OTS St. No. 2, p. 11.) In rebuttal testimony, Columbia proposed a compromise whereby the amortization of the transition obligation remains unchanged, but the Company accelerates the amortization of an existing balance of deferred OPEB over-recoveries. The effect is to avoid over-recovery of OPEB costs upon expiration of the amortization of the transition obligation. (Columbia St. 106-R, pp. 17-18.) Settlement ¶ 39 adopts this proposal.

B. REVENUE ALLOCATION AND NON RESIDENTIAL RATE DESIGN

As in many base rate cases, the revenue allocation issues were among the most contentious issues in this proceeding. The Joint Petitioners proposed a variety of class cost of service studies and cost allocation methodologies. Moreover, even to the extent certain of the Joint Petitioners agreed on the basic overall methodology, i.e. the Design Day demand allocation versus the Peak & Average methodology, these Joint Petitioners still disagreed on how to allocate certain other costs to the different rate classes, as well as how much movement toward cost of service was appropriate. Despite the fact that the Joint Petitioners were not able to agree on a class “cost of service,” they were able to agree to a revenue allocation that is within the range of revenue allocations proposed by the Joint Petitioners in this proceeding, and Columbia believes that this revenue allocation meets the “cost of service” standards adopted by the Courts and the Commission.

All parties supported their respective cost of service studies for litigation purposes. However, the parties were willing to compromise in order to achieve a settlement of the revenue allocation issues. Therefore, the revenue allocation set forth in the Settlement is not based upon a specific agreed to formulaic approach.³ Moreover, the Settlement rates are not based upon any specific cost of service study results. Instead, the Settlement reflects a compromise of various parties’ revenue allocation and rate design proposals. The resulting class increases, as compared to the Company’s as-filed increases, are as follows:

³ The Settlement designs rates based upon the Company’s volumes reflecting a 20-year weather normalization, with restated volumes to reflect 1.073 Dth per Mcf, based on the actual heat content in the historical year. (Settlement ¶ 47(i).)

Customer Group	As Filed (000s)	Percentage of Proposed Increase	As Settled	Percentage of Settled Increase
Residential	\$30,990	81.88%	\$12,700	74.71%
Small General Service (SGS/SGDS/SCD)	\$5,680	15.48%	\$3,200	18.82%
Large Sales Service/Med. Transportation (LGS/SDS)	\$1,000	2.64%	\$900	5.29%
Large Transportation Service (LDS)	\$0	0%	\$200	1.18%
Mainline Service	\$0	0%	\$0	0%
Total	\$37,850	100%	\$17,000⁴	100%

As noted above, the revenue allocation under the Settlement represents a compromise and falls within the litigation positions of the Joint Petitioners. Columbia notes that because of the disagreement over cost allocation studies and the “black box” nature of the settlement, it is not possible to precisely calculate the extent to which the Settlement moves rates closer to cost of service for all Joint Petitioners. However, Columbia believes that the Settlement achieves progress in the movement toward cost-based rates. The class revenue requirements agreed to by the Joint Petitioners under the terms of the Settlement are set forth in Appendix “A” to the Settlement.

As noted in the Settlement, issues related to residential rate design have been reserved for litigation in this proceeding. (Settlement ¶ 46.) However, another important aspect of the Settlement is the agreement among the Parties with regard to non-residential rate design. In its filing, the Company proposed changes in certain of Columbia’s current monthly customer

⁴ As in Section II.A above, \$1.0 million of the settled revenue requirement will increase funding to the Company’s LIURP and will be collected via Rider USP.

charges for its non-residential rate classes, with the remaining amount of the revenue change proposed in each class to be recovered through their commodity charges. In proposing these changes Columbia was guided by the customer-related costs for these rate classes indicated in the Company's cost of service studies. (Columbia St. No. 12, p. 56; Columbia Exhibit 111, Schedule 6.)

The proposed changes to the non-residential rate design as set forth in Appendix "B" to the Settlement, reflect an accord reached between the Joint Petitioners as to the rate design to be used to recover the rate increases allocated under the Settlement to the Company's non-residential customers.

Columbia submits that the Settlement reflects an acceptable compromise of the competing litigation positions parties relative to revenue allocation and non-residential rate design.

C. DTH BILLING

Prior to making its base rate case filing, the Company filed Supplement No. 156 to Tariff Gas – Pa. P.U.C. No. 9 ("Supplement No. 156" or "BTU factor proceeding") with the Commission at Docket No. R-2010-2201974 and later consolidated into this proceeding.⁵ As part of its filing in the BTU factor proceeding, Columbia proposed to adjust customers' Mcf billings by a BTU factor adjustment, to reflect the heat content of gas. In addition, as part of its filing in this case, Columbia adjusted projected volumes to assume a future test year heat content of 1.097 Dth per Mcf. (Columbia St. No. 4, pp. 13-14.)

The OTS, OSBA and OCA each raised concerns relative to the Company's proposed Supplement No. 156, including the data used to establish the BTU adjustment factor, the

⁵ Supplement No. 156 and the Company's related direct testimony in that proceeding were included in the record through the direct testimony of Columbia witness Kempic as Exhibit MRK-3.

Company's method of billing and the future test year heat factor. To address these concerns regarding the data used to establish the BTU adjustment factor, the Joint Petitioners have agreed that Columbia will work with the Joint Petitioners to reconcile the data Columbia uses to measure gas received and the throughput data Columbia uses for rate design and billing – system-wide and by Pipeline Scheduling Point (“PSP”) area. (Settlement ¶ 47.) In addition, consistent with its rebuttal testimony, Columbia has agreed to accept OCA's proposal to bill base rates and commodity costs on a Dth basis, with conversion from Mcf to Dth to be determined for each PSP area on a monthly basis. (Columbia St. No. 116-R, pp. 12-13.) Further, to provide time for education of customers and conversion to Dth billing, the Joint Petitioners have agreed that Columbia will begin Dth billing no later than with bills rendered June 2012. (Settlement ¶ 47(ii).) Prior to implementing Dth billing, rates from the effective date of the Commission's final order until the commencement of Dth billing will be on an Mcf basis, without a BTU adjustment applied to customers' bills. The Company will submit compliance tariffs both on an Mcf and a Dth basis. Finally, to resolve issues related to the future test year heat content, Columbia has agreed to present its pro forma future test year volumes on an Mcf basis revised to reflect the historic test year level of 1.073 Dth per Mcf and the base rates on a Dth basis will be designed on billing units with the Mcf quantities converted to Dth at 1.073 Dth per Mcf. (Settlement ¶ 47(i).) These Settlement provisions reflect a carefully balanced compromise of diverse interests in these proceedings.

D. UNIVERSAL SERVICE AND CONSERVATION

The Settlement includes several provisions related to Columbia's Universal Service Programs, Columbia's Rider USP – Universal Service Plan, and proposed energy efficiency and customer programs.

In its filing, Columbia proposed to add three new programs designed for consumers who are 65 years of age or older. (Columbia St. No. 16, p. 2.) The OTS, OCA and PCOC raised many issues regarding the need and structure of these programs. Under the terms of the Settlement, the Company has agreed to withdraw its proposal to implement its Safe at Home Senior Program, its Senior Universal Service Program (“USP”) Rider Waiver and its Senior Flexible Due Date Program. (Settlement ¶ 48.)

In addition, as noted above, the challenge to Columbia’s continued use of CAP Plus has been reserved for litigation. However, under the Settlement, the Joint Petitioners have agreed that the cost of any changes in the CAP Plus approach, including programming changes, will be reflected under Columbia’s Universal Service Rider. (Settlement ¶ 49.)

In this proceeding, OTS recommended changes to the operation of Columbia’s CAP, including the use of control features such as the use of a maximum CAP credit and historical usage percentage. (OTS St. No. 4, p. 18.) In order to settle OTS’ request for a maximum CAP credit, the Joint Petitioners have agreed that in 2012 the Company will implement a two-year pilot program to evaluate all CAP customers with a CAP credit of \$1,000 or more (“Maximum CAP Credit”). The initial Maximum CAP Credit of \$1,000 will be adjusted annually to reflect changes in Purchased Gas Cost rates and for any increase in base rates subsequent to the instant proceeding proceedings. (Settlement ¶ 50.) Upon commencement of the Pilot, Columbia will evaluate each CAP customer that exceeds the Maximum CAP Credit, in order to identify those customers that have not received weatherization services through Columbia’s Low Income Usage Reduction Program (“LIURP”) and to prioritize those customers for weatherization. In addition, the Company has also agreed to survey the remaining customers to determine the existence of any control limit exceptions as defined in the CAP policy statement, 52 Pa. Code §

265(3), and refer these customers to the Company's Commission-approved Remedial Energy Efficiency Program ("REEP" – previously known as "HURP").

Further, the Settlement provides consequences, via increased CAP payments, for those customers who fail to reduce their consumption after twelve months of participation in REEP. Columbia has also agreed to review the remaining accounts that do not qualify with a valid exception individually, and raise payments such that the CAP discount for the next twelve month period is projected to be less than the Maximum CAP Credit. (Settlement ¶ 51.) Finally, Columbia will provide a status report once the survey is completed and will provide reports on all pilot customers' current account status, any program consumption savings results and an annual cost of the program. These reports will be served upon the parties of record in this proceeding. (Settlement ¶ 52.) All administrative costs for this pilot will be recovered through the Rider USP. (Settlement ¶ 53.)

In this proceeding, PCOC advocated for an increase to the Company's LIURP budget. (PCOC St. No. 1, p. 23.) As noted above in Section II (A), under the Settlement the Company annual LIURP budget will increase by \$1.0 million, from \$3.0 million to \$4.0 million, commencing with the effective date of rates in this proceeding. (Settlement ¶ 54.) LIURP funding will continue to be recovered under Rider USP. (Settlement ¶ 54.) Further, due to the additional LIURP funding provided by this Settlement, Columbia has agreed to withdraw its proposed Pilot Home Energy Efficiency Program at this time, because it believes expenditures on LIURP will be more effective in reducing consumption. (Settlement ¶ 55.)

Finally, under the Settlement Columbia has agreed to continue its current practice of waiving late payment charges as to CAP customers and customers with incomes equal to or less than 150% of the Federal Poverty Level that enter into payment arrangements with Columbia, as

long as such customers comply with such payment arrangements. (Settlement ¶ 56.) Collectively, these Settlement provisions reflect a carefully balanced compromise of diverse interests in this proceeding.

E. RIDER DSIC – DISTRIBUTION SYSTEM IMPROVEMENT CHARGE (“DSIC”)

Columbia proposed a Rider DSIC in this proceeding for recovery of capital costs associated with replacement of mains, meters and services. Columbia’s proposed adoption of the DSIC was contingent upon legislative authority for a gas DSIC. (Columbia St. No. 3, p. 3.) As the Pennsylvania General Assembly has not yet adopted legislation granting the Commission authority to implement a DSIC for a natural gas utility, Columbia has agreed under the Settlement to withdraw its Rider DSIC proposal from this proceeding. (Settlement ¶ 57.) However, Columbia has reserved the right to propose a DSIC if so authorized, to reflect amounts not included in rate base in this proceeding. Further, Columbia has agreed that it will exclude, in calculating any future DSIC charge related to eligible facilities placed in service in the six months immediately following the future test year of this case, \$11.6 million in order to reflect the inclusion in rate base of CWIP as of September 30, 2011, in the calculation of revenue requirement under this Settlement. (Settlement ¶ 57.)

F. NATURAL GAS SUPPLIER (“NGS”) ISSUES

Three NGSs that are active on Columbia’s system, Dominion Retail, Inc., Shipley Energy Company and Interstate Gas Supply, Inc., collectively intervened in the base rate proceeding. The Settlement resolves all of the issues presented by the NGS Parties in the base rate proceeding.

In this proceeding, the NGS Parties suggested that Columbia increase the current Choice participation limit of 4,000 Mcf/yr. (NGS St. No. 1, p. 19.) This issue was previously addressed

as part of the comprehensive settlement of the Company's 2010 base rate case settlement, wherein the Company agreed to expand eligibility under its Choice program for commercial customers from the 600 Mcf/year maximum to the current participation limit of 4,000 Mcf/year. However, in order to settle this issue, the Company has agreed to raise the volumetric limit under Rate SCD – Small Commercial Distribution to 6,000 Mcf/year. Further, Columbia has agreed that eligible customers will be permitted to switch between Small General Distribution Service (“SGDS”) and Choice in accordance with the expiration and renewal terms of their existing General Distribution Agreement. (Settlement ¶ 58.) These provisions reflect a significant compromise on the part of Columbia. However, by agreeing to increase the participation limit, all of Columbia's customers on Rate Schedule SGDS will have the opportunity to elect Choice service.

The NGS Parties also requested that Columbia make administrative changes relative to transportation service. (NGS St. No. 1, pp. 25-28.) Although the Company responded to all of the concerns raised by the NGS Parties in its rebuttal testimony, to achieve a settlement on these issues the Company has agreed to several provisions to address the NGS Parties' concerns. (Columbia St. No. 115-R, p. 30-32.) Specifically, under the Settlement Columbia has agreed to provide NGSs with a rescind file, which will notify suppliers if a newly enrolled distribution service customer has elected not to complete an enrollment within 10 days of signing up with a natural gas supplier. (Settlement ¶ 59.) In addition, Columbia has agreed to provide on a monthly basis to each NGS actively serving customers on Columbia's system, without charge, a synchronization list (ACT file). (Settlement ¶ 60.) As to the NGS Parties' concerns relating to data retention, elimination of fees, discontinuance of “black-out dates”, and drop the practice of check digits, Columbia has agreed to discuss these issues in a separate collaborative process with

the NGS Parties to begin as soon as practical. (Settlement ¶ 61.) Any agreements resulting from the collaborative discussion may require future tariff changes, which would be reflected in a subsequent tariff filing.

Columbia has cash out/in tolerance parameters on a NGS' monthly delivered volumes for those situations when a transportation customer's bank or, as is the predominate case, the bank managed by a NGS for its pooled transportation customers, is either depleted, in which case Columbia is selling gas to the customer, or it exceeds the bank tolerance level, which is the maximum amount of banked gas the customer/NGS can maintain in any month. (Columbia St. No. 115-R, p. 5.) The Company's bank tolerance levels provide room for the transportation customer or its NGS to manage their supply on a monthly basis. (Columbia St. No. 115-R, p. 6.) In this proceeding, the NGS Parties' raised concerns regarding the Company's monthly cash in/out based upon a NGS' monthly delivered amounts in order to bring a NGS within tolerance parameters set forth in the Company's existing tariff. (NGS St. No. 1, p. 14.) To address these concerns, under the Settlement, Columbia has agreed to revise the cash in/ cash out adjustment factors related to seasonal flow orders, consumption in excess of deliveries and for deliveries in excess of consumption. (Settlement ¶ 62.)

To address concerns related to the Company's Rate Negotiated Sale Service ("Rate NSS"), under the Settlement, Columbia has agreed to limit Rate NSS to competitive situations, where a customer would not initiate service from Columbia or would no longer take service from Columbia, but for the availability of service under Rate NSS. Columbia will begin to transition existing non-competitive NSS customers to other services (Sales or Transportation) upon contract expiration but no later than July 1, 2012. (Settlement ¶ 63.)

In response to the number of concessions agreed to by the Company in Settlement, the NGS Parties have agreed to withdraw all of their other proposals in this proceeding. Further, the NGS Parties have agreed, individually and collectively, that for a period of thirty (30) months from the effective date of the final order in this case, not to present any of the withdrawn proposals either through the filing of a separate complaint, petition or application, or through intervention in a base rate or other proceeding of Columbia. (Settlement ¶ 64.)

Finally, the Settlement provides that commencing with the effective date of rates in this proceeding, the unbundled gas cost portion of uncollectible accounts, also referred to as the uncollectible expense ratio for purposes of Columbia's Purchase of Receivables Program, shall be 1.52%. As a result, the discount rate for purchased Choice NGS receivables shall be 2.11% (1.52% + 0.59% administrative adder). (Settlement ¶ 65.) Collectively, these Settlement provisions reflect a carefully balanced compromise of diverse interests in this proceeding.

G. FLEX RATES

Under Rule 20 of Columbia's Commission-approved tariff, Columbia currently has the right to provide customers a flexed rate when a "lower rate is required to meet competition from an alternate fuel." (Columbia St. No. 102-R, p. 27.) Columbia, like other NGDCs, flexes its rates when a customer demonstrates an ability to leave the distribution system by switching to an alternative fuel like fuel oil or by taking service from an interstate pipeline or another NGDC. (Id.) Columbia is not atypical in this regard as most other regulated Pennsylvania energy utilities have the ability to negotiate rates with customers who have other energy options. Negotiated rates allow Columbia the necessary flexibility to compete with other energy providers in or near its service territory. Competition for customer load comes from many sources, including other natural gas distribution companies, interstate pipeline companies, private well gas, landfill gas, and alternate fuels (*i.e.*, electricity, fuel oil, propane, etc.). Columbia's service territory overlaps

the service territories of other natural gas distribution companies. As noted by Mark R. Kempic, a total of 166,713 of Columbia's customers, roughly 40% of Columbia's entire customer base has access to another NGDC. (Columbia St. No. 102-R, p. 24; Exhibit MRK-6R.) However, through careful management, Columbia currently provides flexed distribution rates to only 23 customers whose only identified alternative is another NGDC. In addition, Columbia's service territory is traversed by interstate pipeline facilities, contains gas reserves that can be used to serve customers and, with the expected growth of Marcellus Shale, more competition is expected from service to customers directly from independent Pennsylvania producers without use of Columbia's facilities. Customers' ability to access any of these other energy suppliers requires Columbia to have the ability to offer flexed transportation rates in order to retain these customers when it is beneficial to its customer base to do so. (Columbia St. No. 102-R, p. 26.)

Columbia's success in competing for the patronage of these competitive customers has enabled it to spread its costs of service among more customers and resulted in more consumption, thereby reducing the bills to all of its customers. If Columbia would lose any load to competition, the amount of fixed costs to be recovered from the remaining customers would increase. In summary, all of Columbia's customers benefit from the use of flexed rates to retain load and prevent switching to an alternative energy source.

In this proceeding, OTS proposed to disallow recovery of base rate discounts provided to Columbia's 23 customers who can obtain gas service from another natural gas distribution company because the revenue shortfall, and the resulting impact upon customers, from NGDC versus NGDC competition could be avoided if such competition could be eliminated. (OTS St. No. pp. 54-55.) The OCA and OSBA witnesses argued in favor of the Commission initiating a generic investigation concerning NGDC on NGDC competition in Western Pennsylvania. CII

suggested that flex rates are desirable but raised concerns related to the process Columbia uses to determine the flexed rate.

In order to achieve an overall resolution of this base rate proceeding, under the Settlement, Columbia has agreed to join with OTS, OCA and/or OSBA in requesting that the Commission initiate a generic investigation or rulemaking to address whether flex rate discounts solely as a result of competition from other NGDCs should be permitted to continue and, if permitted to continue, under what circumstances it will be considered appropriate. (Settlement ¶ 66). In addition, to resolve the issues raised by CII, under the Settlement Columbia has agreed to clarify the process to be used for affidavits related to flex rates, and to maintain requested customer information confidential. (Settlement ¶ 67.)

These Settlement provisions reflect a carefully balanced compromise of the diverse interests in this proceeding and also recognize that the issue of NGDC on NGDC competition is not an issue that is unique to Columbia. The requested generic investigation or rulemaking, if subsequently initiated by the Commission, will provide all interested persons with an opportunity to address the issue of NGDC on NGDC competition on an “across the board” basis. Further, the Settlement details a workable process for both Columbia and its customers to follow when negotiating flexed rate agreements.

H. THE SETTLEMENT SATISFIES THE ISSUES AND AREAS OF CONCERNS RAISED BY THE COMMISSION

In its March 17, 2011 Order to suspend and investigate Supplement No. 163, the Commission also identified several areas of concern to be investigated and addressed by the parties in this proceeding. Specifically, the Commission identified eight (8) areas of concern for parties to address. As explained below, the Columbia’s 2011 base rate filing, as modified by the

terms and conditions of the Settlement, satisfies the issues and areas of concern identified by the Commission.

- 1. Columbia's cast iron and bare steel replacement program must be closely examined to ensure that such claim is accurate, that the investment was prudently made, and that all utility plant acquired is necessary, used and useful for the provision of gas distribution service.**

As explained by Columbia Witness Danny G. Cote, in 2007 Columbia began to accelerate the replacement rate of unprotected bare steel and cast iron pipe which represent approximately 26% of Columbia's distribution system. (Columbia St. No. 9, pp. 16-17.) Indeed, Columbia has replaced more than twice as much bare steel main as the next highest local distribution company among its peers in Pennsylvania. (Columbia St. No. 9, p. 19.) In fact, between 2007 and 2010, Columbia replaced 1,554,812 feet of cast iron and bare steel mains. (Columbia St. No. 9, p. 17.) This represents a 97% increase in Columbia's cast iron and bare steel replacements, as compared to 2002 through 2005. (*Id.*) Further, as addressed in Mr. Cote's supplemental direct testimony, the Company has received an incremental allotment of \$24 million for capital expenditures from its parent in 2011, \$19 million of which is allocated to the replacement of bare steel and cast iron pipe. (Columbia St. No. 9-Supp, p. 2.)

The Joint Petitioners have thoroughly investigated Columbia's cast iron and bare steel replacement program through informal and formal discovery. After this extensive investigation, no party challenged the Company's claim related to this program. The Joint Petitioners reached a settlement of all but two issues, and the Joint Petitioners have deemed the revenue increase and revenue requirement to be a reasonable outcome.

2. **Columbia's rate base claim relating to the installation of automatic meter reading devices must be closely examined to ensure that its claim is accurate, that the investment was prudently made, and that all utility plant acquired is necessary, used and useful for the provision of the Company's gas distribution service.**

As detailed by Columbia Witness Danny G. Cote, Columbia presently installs automated meter reading ("AMR") technology at the request of customer and as part of the Company's pipeline replacement program. (Columbia St. No. 9, pp. 5-6.) At the time of filing, this strategy resulted in Columbia installing approximately 70,000 AMR devices across Columbia's entire service territory. (Columbia St. No. 9, p. 6.) However, to fully realize the benefits of AMR, it is necessary that there is an adequate number of AMR devices installed within in a particular geographic territory. (Id.) In February of 2011, Columbia began to expand its installation of AMR devices under a plan that will result in AMR installation on the remaining 354,000 meters over a two year period. (Id.) Once AMR devices are fully deployed, Columbia will be able to provide customers with enhanced services such as actual meter readings each month, reduced non-access issues, and fewer estimated bills, to name a few. Further, as noted above, Columbia received an incremental \$24 million in capital dollars for 2011; \$5 million of this incremental capital has been earmarked for AMR deployment. (Columbia St. No. 9-Supp, p. 2.)

The Joint Petitioners have thoroughly investigated Columbia's AMR proposal through informal and formal discovery. After this extensive investigation, no party challenged the Company's claim related to this program and the Joint Petitioners reached a settlement of all but two issues, and the Joint Petitioners have deemed the revenue increase and revenue requirement to be a reasonable outcome.

3. **Columbia's proposed DSIC would represent a major change in the way the Company recovers its capital costs and depreciation associated with its CIBS program, and any other costs to which the DSIC is meant to apply. As such, the DSIC should be thoroughly examined to determine its effect on all customers, and whether it is necessary, lawful, just, and reasonable. We note, however, that absent legislation granting us the authority to approve such a charge, we cannot lawfully permit the DSIC to be implemented.**

As addressed in Section II(E) above, Columbia's proposed adoption of the DSIC was contingent upon legislative authority for a gas DSIC. (Columbia St. No. 3, p. 3.) As the Pennsylvania General Assembly has not yet adopted legislation granting the Commission authority to implement a DSIC for a natural gas utility, Columbia has agreed, subject to the terms of the Settlement, to withdraw its Rider DSIC proposal from this proceeding. (Settlement ¶ 57.)

4. **As directed in Columbia's 2010 1307(f) proceeding at Docket No. R-2010-2161920, the Commission directed that parties research and explain the public policy rationale for putting gas storage interest in the PGC C-factor versus the E-factor, and the effect of same on the Company and its customers. In addition, the Commission directed that the parties examine the effect of this issue on Columbia's change in storage accounting methodology from LIFO to WACOG as proposed by the Company in its Commission-approved petition at Docket No. P-2010-2209925.**

On November 12, 2010, Columbia filed its *Petition of Columbia Gas of Pennsylvania, Inc. for an Order Authorizing the Company to Revise its Accounting Methodology for Gas in Inventory* ("Petition"), at Docket No. P-2010-2209925. In its Petition, Columbia requested that the Commission approve Columbia's conversion from Last In First Out ("LIFO") accounting to a Weighted Average Cost of Gas ("WACOG") accounting methodology. Subsequent to the filing of the instant proceeding, the matter of the transition of Columbia's accounting methodology for gas in storage from LIFO to WACOG was resolved by the Commission's order approving Columbia's Petition by order entered on March 31, 2011. As a result of the settlement

converting Columbia's storage accounting to WACOG, the storage interest adjustment ceased to be computed effective January 1, 2011.

The matter of whether gas storage interest in the Purchased Gas Cost C-factor versus the E-factor, has become moot as reflected in the currently pending resolution of Columbia's purchased gas cost proceeding at Docket No. R-2011-2228696.

- 5. Columbia's preferred Design Day class cost of service study, as well as its Peak & Average study, and any other class cost of service studies submitted by the parties in this proceeding must be thoroughly examined in order to determine the most appropriate study to be used as a basis for the allocation of the final amount of total revenue allowed in this proceeding.**

As addressed in Section II (B) above, the Joint Petitioners proposed a variety of class cost of service studies and cost allocation. Despite the fact that the Joint Petitioners were not able to agree on a class "cost of service," they were able to agree to a revenue allocation that is within the range of revenue allocations proposed by the Joint Petitioners in this proceeding, and Columbia believes that this revenue allocation meets the "cost of service" standards adopted by the Courts and the Commission.

Columbia notes that because of the disagreement over cost allocation studies and the "black box" nature of the settlement, it is not possible to precisely calculate the extent to which the Settlement moves rates closer to cost of service for all classes. However, Columbia believes that the Settlement achieves progress in the movement toward cost-based rates.

- 6. Columbia's proposed levelized distribution charge for its residential customers must be thoroughly scrutinized to establish the possible effects on these customers, and to determine the overall appropriateness of such a rate design. Columbia's proposed rate design changes for its other customer classes must be closely examined as well.**

As noted above, issues related to residential rate design have been reserved for litigation in this proceeding. (Settlement ¶ 46.)

7. **Columbia's proposed BTU content adjustment must be examined to determine, whether or not it is supported by solid evidence, and how it will affect the customers to which it applies.**

The Joint Petitioners have thoroughly investigated Columbia's proposal to adjust customers' Mcf billing by a BTU fact adjustment, to reflect the heat content of gas through informal and formal discovery, multiple rounds of testimony and numerous settlement discussions. After this extensive investigation, the Joint Petitioners reached a settlement of the Company's BTU factor proceeding as more thoroughly addressed in Section II (C) above.

8. **Columbia's proposed Pilot HEEP and senior citizen programs must be closely reviewed to determine their necessity and cost effectiveness, and the accuracy of the costs of these programs claimed by the Company in this proceeding. The effect of these programs on the rates of non-participating customers must also be examined to determine the overall justness and reasonableness of these proposals.**

As addressed in Section 2 (D) above, due to the additional LIURP funding provided by this Settlement, Columbia has agreed to withdraw its proposed Pilot Home Energy Efficiency Program. (Settlement ¶ 55.) In addition, under the terms of the Settlement, the Company has agreed to withdraw its proposal to implement its Safe at Home Senior Program, its Senior Universal Service Program ("USP") Rider Waiver and its Senior Flexible Due Date Program. (Settlement ¶ 48.)

I. RESERVED ISSUES FOR LITIGATION

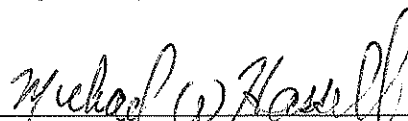
The primary issue reserved for litigation in this proceeding concerns the design of residential base rates. Columbia has proposed to recover all of its residential distribution costs through a Levelized Distribution Charge. The second issue reserved for litigation involves the challenge by PCOC to Columbia's continued use of CAP-Plus. Specifically, PCOC challenges the legality of Columbia's CAP Plus plan that was approved by the Commission in response to a Pennsylvania Department of Public Welfare directive that distribution companies apply the Low

Income Home Energy Assistance Program cash grants to a customer's monthly asked to pay amount, rather than the CAP credit.

III. CONCLUSION

The Settlement is the result of detailed examination of Columbia's proposals, multiple rounds of discovery, direct, rebuttal, surrebuttal and rejoinder testimony, and compromise by all parties. Columbia believes that fair and reasonable compromises have been achieved on the settled issues in this case, as is evident by the fact that all parties, including Columbia, OTS, OCA, OSBA, PSU, PCOC, CII and the NGS Parties have reached an agreement on all but two issues in this proceeding. Columbia fully supports this Settlement and respectfully requests that the ALJ and the Commission review and approve the Settlement in its entirety without modification.

Respectfully submitted,



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