

PUC LATE-FILED EXHIBITS

Docket No. R-00017034 F 0002
Hearing Date 3-26-02
Judge Fordham
Hearing held in PHILA, PA
Exhibit No. (See attached)
Reporter Robert Stonaker

1. Above exhibit to be supplied to reporter by:

2. Above exhibit to be filed directly with PUC by:

Additional Comments: **DOCUMENT FOLDER**
Please add to exhibit file

EXHIBIT INDEX

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<u>PGW</u>		
ERP Statement No. 4 (Bisgaier)	74	74
Exhibits Nos. BCB-1, BCB-2 & BCB-3	74	74
ERP Statement No. 2 (Bogdonavage)	109	109
Exhibits Nos. JRB-1 & JRB-2	109	109
Bogdonavage Rebuttal Exhibit No. 1	78	109
Bogdonavage Rebuttal Exhibit No. 2	89	109
√ ERP Statements Nos. 1 & 3 with Volume II (Supporting Testimony & Documentation)	110	110
√ ERP Statement No. 3 (Krellenstein)	126	126
Knudsen Rebuttal Exhibit No. 1	128	4-2-02 191
ERP Statements Nos. 5 & 5.1 (Davis)	162	162
ERP Statement No. 1 (Knudsen)	191	191
Exhibit No. TEK-1	191	191
Cross-Examination Exhibit No. 1 (Bond Buyer Article)	226	242

EXHIBIT INDEX

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<u>OCA</u>		
Cross-Examination Exhibit No. 1 (IR-OSBA-II-5, 6 & 7)	62	68
Cross-Examination Exhibit No. 2 (IR-OCA-I-2, 4 & 6)	65	68
Statement No. 1-ERP (Lelash)	210	242
<u>OTS</u>		
Cross-Examination Exhibit No. 1 (IR-OTS-III-RE-20)	146	190
Statement No. 1 w/Exhibit No. 1 and errata sheets (Weakley)	196	196
Statement No. 2 w/Exhibit No. 2 (Deardorff)	210	210

-- 0 --

DOCUMENT
FOLDER

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY
COMMISSION

DOCKETED

APR 30 2002

RE: PHILADELPHIA GAS WORKS
BASE RATE PROCEEDING

SUPPORTING DOCUMENTATION

SUPPORTING FINANCIAL
INFORMATION

VOLUME II

3/26/02

Phila, PA

RDS

DOCKET NO. R-00017034

F0002

FEBRUARY 2002

PA.P.U.C.
SECRETARY'S BUREAU

02 APR -2 PM 1:53

RECEIVED

SUPPORTING DOCUMENTATION

TABLE OF CONTENTS

EXHIBITS

A-1	Statement of Income
A-1-1	Statement of Income (Conventional Format)
A-2	Cash Flow Statement
A-3	Debt Service Coverage
A-4	Balance Sheet
B	Operating Revenues
B-1	Reconciliation of Billed Revenues
B-1-1	Gas Revenues
B-2	Gas Sales
C-1-1	1999-2000 Actual Natural Gas Expense
C-1-2	2000-2001 Estimate Natural Gas Expense
C-1-3	2001-2002 Budget Natural Gas Expense
C-3	Labor & Fringe Benefits
C-3-1	Detail of Direct Labor Expenses
C-4	Detail of Other Expenses
D-1	Other Income
E-1	Revenue Bond Debt Service (Interest)

- E-2 Other Long-Term Debt Service (Interest)
- E-3 Other Interest
- F-1 Capital Funding & Expenditures
- G-1 Revenue Bond Debt Service (Principal)
- G-2 Other Long-Term Debt Service (Principal)
- H-1 Working Capital Detail
- H-2 Working Capital Changes

SCHEDULES

- SD-1 Detail of Non-Cash Expenses
- SD-2 Insurance Expenses
- SD-3 Personnel & Payroll Detail
- SD-4A 1999-2000 Actual Normalized Expenses
- SD-4B 2000-2001 Estimate Normalized Expenses
- SD-4C 2001-2002 Budget Normalized Expenses
- SD-5 CRP Regulatory Asset Amortization
- SD-6 Accounts Receivable & Bad Debt Expense
- SD-7 Collectibility Study – August 2001
- SD-7-1 Collectibility Study – December 2001

PHILADELPHIA GAS WORKS
STATEMENT OF INCOME
(Dollars in Thousands)

Line No.	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Current Rates Budget <u>2001-02</u>	Proposed \$60.0M Budget <u>2001-02</u>	
OPERATING REVENUES					
1.	Non-Heating	\$87,830	\$104,680	\$92,633	\$92,633
2.	Gas Transport Service	3,313	2,355	2,130	2,130
3.	Heating	434,544	620,857	539,502	539,502
4.	Proposed Base Rate Increase	-	-	-	60,000
5.	Unbilled Gas Adjustment	7,299	(8,967)	3,268	4,468
6.	Total Gas Revenues	<u>532,986</u>	<u>718,925</u>	<u>637,533</u>	<u>698,733</u>
7.	Appliance Repair & Other Service Revenues	11,978	12,075	10,610	10,610
8.	Other Operating Revenues	<u>10,911</u>	<u>19,046</u>	<u>16,376</u>	<u>17,918</u>
9.	Total Other Revenues	22,889	31,121	26,986	28,528
10.	Total Operating Revenues	\$555,875	\$750,046	\$664,519	\$727,261
OPERATING EXPENSES					
11.	Natural Gas	\$266,350	\$431,320	\$334,566	\$334,566
12.	Other Raw Material	<u>4</u>	<u>7</u>	<u>10</u>	<u>10</u>
13.	Sub-Total Fuel	266,354	431,327	334,576	334,576
14.	Contribution Margins	\$289,521	\$318,719	\$329,943	\$392,685
15.	Labor & Fringe Benefits	\$112,813	\$117,787	\$113,505	\$113,505
16.	Bad Debt Expense	54,642	67,633	51,796	52,944
17.	Other Expenses & Depreciation	<u>74,891</u>	<u>67,996</u>	<u>85,387</u>	<u>85,387</u>
18.	Sub-Total Other O&M & Depreciation	242,346	253,416	250,688	251,836
19.	Total Operating Expenses	\$508,700	\$684,743	\$585,264	\$586,412
20.	Operating Income	\$47,175	\$65,303	\$79,255	\$140,849
21.	Other Income	\$9,417	\$12,343	\$4,893	\$5,843
22.	Loss on Write Off of SNG Plant	-	(8,087)	-	-
23.	Income Before Interest	<u>\$56,592</u>	<u>\$69,559</u>	<u>\$84,148</u>	<u>\$146,692</u>
INTEREST					
24.	Long Term Debt	\$49,256	\$48,151	\$50,966	\$50,966
25.	Other Interest	5,810	6,680	6,498	6,498
26.	AFUDC	(374)	(588)	(775)	(775)
27.	Loss from Extinguishment of Debt	<u>4,311</u>	<u>4,162</u>	<u>3,976</u>	<u>3,976</u>
28.	Total Interest Expense	\$59,003	\$58,405	\$60,665	\$60,665
29.	Net Income Before City Payment	(2,411)	11,154	23,483	86,027
30.	City Payment	<u>18,000</u>	<u>18,000</u>	<u>18,000</u>	<u>18,000</u>
31.	Net Earnings/(Loss) from Operations	<u>(\$20,411)</u>	<u>(\$6,846)</u>	<u>\$5,483</u>	<u>\$68,027</u>

1
PHILADELPHIA GAS WORKS
STATEMENT OF INCOME
(Dollars in Thousands)

	Actual	Actual	Current Rates Budget	\$60M Budget
	<u>1999-2000</u>	<u>2000-01</u>	<u>2000-01</u>	<u>2001-02</u>
OPERATING REVENUES				
Non-Heating	\$87,830	\$104,680	\$92,633	\$92,633
Gas Transport Service	3,313	2,355	2,130	2,130
Heating	434,544	620,857	539,502	539,502
Proposed Base Rate Increase	-	-	-	60,000
Unbilled Gas Adjustment	7,299	(8,967)	3,268	4,468
Total Gas Revenues	<u>532,986</u>	<u>718,925</u>	<u>637,533</u>	<u>698,733</u>
Appliance Repair & Bill Paid Turn-Ons	11,978	12,075	10,610	10,610
Other Operating Revenues	22,911	19,046	16,376	17,918
Total Other Operating Revenues	<u>22,889</u>	<u>31,121</u>	<u>26,986</u>	<u>28,528</u>
Total Operating Revenues	\$555,875	\$750,046	\$664,519	\$727,261
OPERATING EXPENSES				
Natural Gas	\$266,350	\$431,320	\$334,566	\$334,566
Other Raw Material	4	7	10	10
Sub-Total Fuel	<u>266,354</u>	<u>431,327</u>	<u>334,576</u>	<u>334,576</u>
CONTRIBUTION MARGINS	\$289,521	\$318,719	\$329,943	\$392,685
Gas Processing	14,032	13,400	13,161	13,161
Field Services	33,704	33,202	31,730	31,730
Distribution	14,246	14,837	14,440	14,440
Collection	12,609	11,473	13,040	13,040
Customer Service	11,753	14,228	14,582	14,582
Customer Accounting	3,669	1,717	2,600	2,600
Bad Debt Expense	54,642	67,633	51,796	52,944
Marketing	3,041	3,486	5,596	5,596
Administrative & General	37,676	37,516	39,086	39,086
Health Insurance	24,241	27,404	30,490	30,490
Capitalized Fringe Benefits	(4,654)	(5,035)	(5,703)	(5,703)
Capitalized Administrative Charges	(4,857)	(7,224)	(7,727)	(7,727)
Regulatory Asset Amortization	1,984	(1,508)	3,000	3,000
Amortization of Restructuring Costs	965	965	965	965
Year 2000 & Deregulation Amortization	882	882	-	-
Pensions	1,096	2,301	3,091	3,091
Taxes	6,512	6,299	6,054	6,054
Labor/Cost Savings	-	-	(7,100)	(7,100)
Additional Costs for PUC Safety & Other	-	-	10,000	10,000
Sub-Total Other Oper. & Maintenance	<u>211,541</u>	<u>221,576</u>	<u>219,101</u>	<u>220,249</u>
Depreciation	32,614	32,559	32,581	32,581
Cost of Removal	2,519	2,625	2,500	2,500
To Clearing Accounts	(4,328)	(3,344)	(3,494)	(3,494)
	<u>30,805</u>	<u>31,840</u>	<u>31,587</u>	<u>31,587</u>
TOTAL OPERATING EXPENSES	\$508,700	\$684,743	\$585,264	\$586,412
OPERATING INCOME	47,175	65,303	79,255	140,849
Other Income	9,417	12,343	4,893	5,843
Loss on Write Off of SNG Plant	-	(8,087)	-	-
INCOME BEFORE INTEREST	\$56,592	\$69,559	\$84,148	\$146,692
INTEREST				
Long-Term Debt	\$49,256	\$48,151	\$50,966	\$50,966
Other	5,810	6,680	6,498	6,498
AFUDC	(374)	(588)	(775)	(775)
Loss From Extinguishment of Debt	4,311	4,162	3,976	3,976
Total Interest	<u>59,003</u>	<u>58,405</u>	<u>60,665</u>	<u>60,665</u>
NET INCOME	(2,411)	11,154	23,483	86,027
City Payment	18,000	18,000	18,000	18,000
Net Earnings/(Loss) From Operations	(\$20,411)	(\$6,846)	\$5,483	\$68,027

**PHILADELPHIA GAS WORKS
CASH FLOW STATEMENT
(Dollars in Thousands)**

Line No.	<u>SOURCES</u>	Actual 1999-2000	Actual 2000-01	Current Rates Budget 2001-02	\$60M Budget 2001-02
1.	Net Income	(\$2,411)	\$11,154	\$23,483	\$86,027
2.	Depreciation & Amortization	40,985	40,506	42,832	42,832
3.	Earnings on Restricted Funds	563	(361)	163	163
4.	Loss on Disposition of SNG Plant	-	8,087	-	-
5.	Increased/(Decreased) Long Term Debt	548	(468)	468	468
6.	Increased/(Decreased) Other Liabilities	14,800	2,861	1,809	1,809
7.	Available From Operations	54,485	61,779	68,755	131,299
8.	Funds Required for Capital	69,264	50,401	60,943	60,943
9.	Capital Leasing	2,228	4,955	2,000	2,000
10.	City Loan	-	45,000	-	-
11.	Temporary Financing	22,000	-	-	-
12.	TOTAL SOURCES	<u>\$147,977</u>	<u>\$162,135</u>	<u>\$131,698</u>	<u>\$194,242</u>
	USES				
13.	Net Construction Expenditures	\$48,139	\$57,424	\$62,943	\$62,943
	Funded Debt Reduction:				
14.	Revenue Bonds	33,595	34,192	33,977	33,977
15.	PMA Lease/Subordinate Debt	1,020	1,065	1,105	1,105
16.	Capital Lease	6,538	6,901	5,273	5,273
17.	Notes Payable - CNG Acquisition	219	59	-	-
18.	Tax Exempt Commercial Paper Repayment Fund	-	19,000	1,000	11,000
19.	\$45.0 M City Loan Repayment Fund	-	-	-	22,500
20.	Distribution of Earnings	18,000	18,000	18,000	18,000
	Additions to (Reductions of)				
21.	Non-Cash Working Capital	48,128	33,399	7,166	12,212
22.	Cash Needs	155,639	170,040	129,464	167,010
23.	Cash Surplus (Shortfall)	(7,662)	(7,905)	2,234	27,232
24.	TOTAL USES	<u>\$147,977</u>	<u>\$162,135</u>	<u>\$131,698</u>	<u>\$194,242</u>
25.	Cash - Beginning of Period	\$16,087	\$8,425	\$520	\$520
26.	Cash - Surplus (Shortfall)	(7,662)	(7,905)	2,234	27,232
27.	Ending Cash	<u>\$8,425</u>	<u>\$520</u>	<u>\$2,754</u>	<u>\$27,752</u>
28.	Other Capital Funding Sources	-	-	-	-
29.	Outstanding Commercial Paper	\$97,000	\$78,000	\$77,000	\$67,000
30.	City Loan Outstanding	-	\$45,000	\$45,000	\$22,500

**PHILADELPHIA GAS WORKS
DEBT SERVICE COVERAGE
(Dollars in Thousands)**

Line No.	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Current Rates Budget <u>2001-02</u>	\$60M Budget <u>2001-02</u>
<u>FUNDS PROVIDED</u>				
1.	\$532,986	\$718,925	\$637,533	\$698,733
2.	22,889	31,121	26,986	28,528
3.	555,875	750,046	664,519	727,261
4.	9,980	7,477	5,056	6,006
5.	374	588	775	775
6.	TOTAL FUNDS PROVIDED	\$758,111	\$670,350	\$734,042
<u>FUNDS APPLIED</u>				
7.	\$266,354	\$431,327	\$334,576	\$334,576
8.	242,346	253,416	250,688	251,836
9.	508,700	684,743	585,264	586,412
10.	7,988	7,977	5,954	5,954
11.	44,343	36,380	36,165	36,165
12.	TOTAL FUNDS APPLIED	\$656,340	\$555,053	\$556,201
13.	\$93,884	\$101,771	\$115,297	\$177,841
14.	7,988	7,977	5,954	5,954
15.	101,872	109,748	121,251	183,795
16.	\$59,345	\$51,611	\$55,528	\$55,528
17.	1.72	2.13	2.18	3.31
18.	\$42,527	\$58,137	\$65,723	\$128,267
19.	7,988	7,977	5,954	5,954
20.	34,539	50,160	59,769	122,313
21.	\$21,659	\$29,449	\$30,926	\$30,926
22.	1.59	1.70	1.93	3.96
23.	\$12,880	\$20,711	\$28,843	\$91,387
24.	1,987	1,990	1,986	1,986
25.	6.48	10.41	14.52	46.02
26.	\$ 101,872	\$ 109,748	\$ 121,251	\$ 183,795
27.	\$ 90,979	\$ 91,027	\$ 94,394	\$ 94,394
28.	1.12	1.21	1.28	1.95
29.	0.93	1.01	1.08	1.64
30.	Fixed Coverage Ratio including \$18.0 M City Fee			
31.	& \$30.0 M TXCP Reduction	-	0.85	1.29

PHILADELPHIA GAS WORKS
BALANCE SHEET
(Dollars in Thousands)

Line No.		Actual		Current Rates	\$60M
		8/31/2000	8/31/2001	Budget 8/31/2002	Budget 8/31/2002
ASSETS					
1.	Utility Plant Net	\$869,472	\$883,727	\$909,524	\$909,524
2.	Sinking Fund Reserve	91,246	96,598	96,130	96,130
3.	Capital Improvement Fund	33,842	92,850	31,907	31,907
4.	Capital Lease Fund	10,458	5,349	3,186	3,186
5.	Cash	8,425	520	2,754	27,752
Accounts Receivable:					
6.	Gas Receivable	168,234	270,300	258,134	263,128
7.	Other	2,887	4,774	1,503	1,503
8.	Accrued Gas Revenues	14,300	5,332	8,600	9,800
9.	Reserve for Uncollectible	<u>(129,154)</u>	<u>(184,324)</u>	<u>(194,198)</u>	<u>(195,346)</u>
Accounts Receivable Net		56,267	96,082	74,039	79,085
10.	Materials & Supplies	67,699	91,234	100,964	100,964
11.	Other Current Assets	1,911	1,099	2,010	2,010
12.	Deferred Debits	23,692	3,753	4,101	4,101
13.	Unamortized Bond Issuance Expense	12,340	17,596	16,282	16,282
14.	Unamortized Extraordinary Loss	43,758	39,596	35,620	35,620
15.	Regulatory Asset	15,000	11,250	7,500	7,500
16.	Other Assets	4,602	4,049	3,370	3,370
17.	TOTAL ASSETS	\$1,238,712	\$1,343,703	\$1,287,387	\$1,317,431
EQUITY & LIABILITIES					
18.	City Equity	\$211,300	\$204,454	\$209,937	\$272,481
Long Term Debt:					
19.	Revenue Bonds	814,250	899,218	864,136	864,136
20.	TECA Accretions	29,354	27,928	25,828	25,828
21.	Unamortized Discount	(12,816)	(12,135)	(11,256)	(11,256)
22.	Unamortized Premium	4,293	3,871	3,462	3,462
23.	Capital Equipment Leasing	21,421	14,520	9,247	9,247
24.	CNG Acquisition	59			
25.	Notes Payable	97,000	78,000	77,000	67,000
26.	City Loan		45,000	45,000	22,500
Accounts Payable:					
27.	Natural Gas	23,364	37,296	22,876	22,876
28.	General	12,726	14,553	14,750	14,750
29.	Customer Deposits	1,109	401	1,200	1,200
30.	Other Current Liabilities	7,888	4,035	1,649	1,649
31.	Deferred Credits	3,008	2,100	327	327
Accrued Credits:					
32.	Interest	8,187	8,369	7,924	7,924
33.	Taxes & Wages	3,930	2,657	2,465	2,465
34.	Distribution to City	3,000	3,000	3,000	3,000
35.	Other Liabilities	10,639	10,436	9,842	9,842
36.	TOTAL EQUITY & LIABILITIES	\$1,238,712	\$1,343,703	\$1,287,387	\$1,317,431

PHILADELPHIA GAS WORKS OPERATING REVENUES

(Dollars in Thousands)

Line No.	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Current Rates Budget <u>2001-02</u>	\$60M Budget <u>2001-02</u>
1. Non-Heating	\$87,830	\$104,680	\$ 92,633	\$92,633
2. Gas Transportation Service	3,313	2,355	2,130	2,130
3. Heating	434,544	620,857	539,502	539,502
4. Proposed Base Rate Increase	-	-	-	60,000
5. Unbilled Gas Adjustment	<u>7,299</u>	<u>(8,967)</u>	<u>3,268</u>	<u>4,468</u>
6. Sub-Total Gas Revenues	532,986	718,925	637,533	698,733
7. Appliance Repair & Other Service Revenues	11,978	12,075	10,610	10,610
8. Other Operating Revenues	<u>10,911</u>	<u>19,046</u>	<u>16,376</u>	<u>17,918</u>
9. Sub-Total Other Revenues	22,889	31,121	26,986	28,528
10. Total Operating Revenues	<u><u>\$555,875</u></u>	<u><u>\$750,046</u></u>	<u><u>\$664,519</u></u>	<u><u>\$727,261</u></u>

PGW
RECONCILIATION OF BILLED REVENUES
(Dollars in Thousands)

1999-2000 ACTUAL	<u>Billed Revenues</u>	<u>1998-99 Over recovery</u>	<u>1999-2000 Under recovery</u>	<u>Total Revenues</u>
Firm Non-Heating	\$43,690	1,434	700	\$45,824
Interruptible	42,006			42,006
Total Non Heating	85,696	1,434	700	87,830
Gas Transportation Service	3,313			3,313
Heating	406,536	14,660	13,348	434,544
Total Revenues	<u>\$495,545</u>	<u>\$16,094</u>	<u>\$14,048</u>	<u>\$525,687</u>
2000-01 ACTUAL	<u>Billed Revenues</u>	<u>1999-2000 Under recovery</u>		<u>Total Revenues</u>
Firm Non-Heating	\$65,306	(\$701)		\$64,605
Interruptible	40,075			40,075
Total Non Heating	105,381	(701)		104,680
Gas Transportation Service	2,355			2,355
Heating	634,228	(13,371)		620,857
Total Revenues	<u>\$741,964</u>	<u>(\$14,072)</u>	<u>\$0</u>	<u>\$727,892</u>
2001-02 BUDGET	<u>Billed Revenues</u>			<u>Total Revenues</u>
Firm Non-Heating	\$55,271			\$55,271
Interruptible	37,362			37,362
Total Non Heating	92,633			92,633
Gas Transportation Service	2,130			2,130
Heating	539,502			539,502
Total Revenues	<u>\$634,265</u>			<u>\$634,265</u>

PHILADELPHIA GAS WORKS
GAS REVENUES
(Dollars in Thousands)

GAS REVENUES	Actual	Actual	\$60.0 M
<u>NON HEATING</u>	<u>1999-2000</u>	<u>2000-01</u>	<u>Budget</u>
			<u>2001-02</u>
Residential	21,437	32,121	28,851
CRP Shortfall	(399)	(1,037)	(491)
Commercial	16,424	25,007	19,186
Industrial	4,111	6,144	5,165
Municipal	1,978	3,077	2,557
Housing Authority	139	(6)	3
Total Firm Non-Heating	43,690	65,306	55,271
BPS - Small	1,737	1,403	2,623
BPS - Large	19,662	18,521	21,147
BPS - A/C	0	0	2,153
LBS-L Direct	798	1,863	388
LBS-L Indirect	4,944	4,961	3,637
LBS-S Indirect	7,358	7,584	4,005
LBS-XL Direct	1,334	1,930	698
LBS-XL Indirect	4,578	2,795	1,913
Co-Generation - Indirect	848	741	750
GTS - Sales	694	339	0
NGV	53	(62)	48
Total Interruptibles	42,006	40,075	37,362
Total Non Heating	85,696	105,381	92,633
 <u>HEATING</u>			
Residential	333,608	531,850	438,837
CRP Shortfall	(18,381)	(36,731)	(24,049)
Commercial	69,435	108,559	91,876
Industrial	7,140	11,913	9,854
Municipal	7,459	11,954	9,372
Housing Authority	7,275	6,683	13,612
Total Heating	406,536	634,228	539,502
Net Billed Revenues	492,232	739,609	632,135
GTS Revenues	3,313	2,355	2,130
Total Billed Revenues	495,545	741,964	634,265
2/22/02 GCR Factor per MCF	1.0982	6.6959	2.6003

PHILADELPHIA GAS WORKS
GAS SALES
(MCF's)

GAS SALES	Actual 1999-2000	Actual 2000-01	\$60.0 M Budget 2001-02
<u>NON HEATING</u>			
Residential	1,940	2,168	2,079
Commercial	1,920	2,068	1,820
Industrial	456	536	504
Municipal	261	270	274
Housing Authority	17	(1)	0
Total Firm Non-Heating	4,594	5,041	4,677
BPS - Small	177	154	352
BPS - Large	3,768	2,650	3,478
BPS - A/C	0	0	465
LBS - L Direct	177	300	146
LBS - L Indirect	1,114	474	1,122
LBS - S Indirect	1,648	258	1,176
LBS - XL Direct	312	796	211
LBS - XL Indirect	1,063	1,195	599
Co-Generation - Indirect	208	123	150
GTS - Sales	134	56	0
NGV Indirect	3	(18)	10
Total Interruptibles	8,604	5,988	7,709
Total Non Heating	13,198	11,029	12,386
<u>HEATING</u>			
Residential	39,048	44,060	41,843
Commercial	8,191	8,929	8,965
Industrial	844	985	964
Municipal	978	1,109	1,021
Housing Authority	871	556	1,353
Total Heating	49,932	55,639	54,146
Net Billed Sales	63,130	66,668	66,532
GTS Volumes	14,092	7,631	8,790
Total Billed Sales	77,222	74,299	75,322
Firm Sales	54,526	60,680	58,823

PHILADELPHIA GAS WORKS
NATURAL GAS EXPENSE
1999-2000 ACTUAL
(Dollars in Thousands)

Line No.		Billed	(To) Inventory	From Inventory	Refunds	Seasonal Adjustment	Total
1.	September	\$19,035	(\$8,211)	\$222	\$ -	(\$3,598)	\$7,448
2.	October	19,097	(4,430)	338		(2,012)	12,993
3.	November	23,959	(2,821)	1,640	(21)	1,218	23,975
4.	December	24,885	(460)	9,637		4,895	38,957
5.	January	24,792	(959)	18,947		6,677	49,457
6.	February	25,932	(217)	10,213		5,243	41,171
7.	March	18,919	(1,126)	6,746		2,941	27,480
8.	April	25,195	(5,593)	2,035		(1,133)	20,504
9.	May	21,805	(9,357)	250	(2)	(3,046)	9,650
10.	June	26,945	(11,080)	183		(3,763)	12,285
11.	July	26,364	(11,218)	328		(3,704)	11,770
12.	August	23,364	(9,852)	866		(3,718)	10,660
13.	Total	<u>\$280,292</u>	<u>(\$65,324)</u>	<u>\$51,405</u>	<u>(\$23)</u>	<u>\$0</u>	<u>\$266,350</u>

PHILADELPHIA GAS WORKS
NATURAL GAS EXPENSE
2000-01 ACTUAL
(Dollars in Thousands)

Line No.		<u>Billed</u>	<u>(To) Inventory</u>	<u>From Inventory</u>	<u>Refunds</u>	<u>Seasonal Adjustment</u>	<u>Total</u>
1.	September	\$25,184	(\$9,113)	\$392	\$ -	(\$3,634)	\$12,829
2.	October	32,033	(6,656)	976	(17)	(2,124)	24,212
3.	November	37,175	(1,826)	4,480	(346)	1,043	40,526
4.	December	58,221	(2,631)	17,124	(341)	4,539	76,912
5.	January	69,786	(423)	15,483	(322)	6,391	90,915
6.	February	49,002	320	10,746	(322)	4,677	64,423
7.	March	37,011	(88)	14,029	(498)	2,988	53,440
8.	April	32,183	(902)	2,724	(498)	(692)	32,815
9.	May	31,034	(11,568)	340	(498)	(2,658)	16,650
10.	June	28,441	(20,163)	317	(498)	(3,553)	4,544
11.	July	30,609	(16,438)	705	(498)	(3,491)	10,887
12.	August	<u>26,603</u>	<u>(19,589)</u>	<u>140</u>	<u>(503)</u>	<u>(3,484)</u>	<u>3,167</u>
13.	Total	<u>\$457,282</u>	<u>(\$89,077)</u>	<u>\$67,456</u>	<u>(\$4,341)</u>	<u>\$0</u>	<u>\$431,320</u>

PHILADELPHIA GAS WORKS
NATURAL GAS EXPENSE
2001-02 BUDGET
(Dollars in Thousands)

Line No.		<u>Billed</u>	(To) <u>Inventory</u>	From <u>Inventory</u>	<u>Refunds</u>	<u>Seasonal Adjustment</u>	<u>Total</u>
1.	September	\$23,165	(\$11,106)	\$448	\$ -	(\$3,196)	\$9,311
2.	October	27,297	(9,312)	537	-	(1,618)	16,904
3.	November	29,516	(3,189)	5,301	-	1,230	32,858
4.	December	34,714	-	11,262	-	4,060	50,036
5.	January	39,319	-	19,606	-	5,955	64,880
6.	February	35,406	-	14,693	-	4,246	54,345
7.	March	31,139	-	7,948	-	2,357	41,444
8.	April	29,154	(7,438)	1,076	-	(568)	22,224
9.	May	28,086	(12,859)	489	-	(2,609)	13,107
10.	June	23,503	(11,386)	364	-	(3,340)	9,141
11.	July	23,537	(10,530)	364	-	(3,266)	10,105
12.	August	<u>22,876</u>	<u>(9,772)</u>	<u>358</u>	<u>-</u>	<u>(3,251)</u>	<u>10,211</u>
13.	Total	<u>\$347,712</u>	<u>(\$75,592)</u>	<u>\$62,446</u>	<u>\$0</u>	<u>\$0</u>	<u>\$334,566</u>

PHILADELPHIA GAS WORKS LABOR & FRINGE BENEFITS

(Dollars in Thousands)

Line No.	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
OPERATING LABOR			
1.	\$99,329	\$99,764	\$99,386
2.	To Capital & Non-Operating Accounts <u>(20,068)</u>	<u>(19,610)</u>	<u>(20,540)</u>
3.	Total Operating Labor 79,261	80,154	78,846
PENSIONS			
4.	Beneficiaries 27,463	28,405	30,100
5.	Payments to (Withdrawals from) Fund <u>(26,367)</u>	<u>(26,104)</u>	<u>(27,009)</u>
6.	Total Pensions 1,096	2,301	3,091
INSURANCE			
7.	Group Life 1,308	1,278	1,801
8.	Health <u>24,241</u>	<u>27,404</u>	<u>30,490</u>
9.	Total Insurance 25,549	28,682	32,291
TAXES			
10.	FICA - OASI 6,142	6,166	6,026
11.	FICA - Medical 1,405	1,451	1,435
12.	State Unemployment 223	57	200
13.	Federal Unemployment 105	107	(300)
14.	Allocated to Capital <u>(1,363)</u>	<u>(1,482)</u>	<u>(1,307)</u>
15.	Total Taxes 6,512	6,299	6,054
OTHER			
16.	Perfect Attendance Incentive 395	351	323
17.	Union/Management Reductions -	-	(7,100)
18.	Total Labor & Fringe Benefits <u>\$112,813</u>	<u>\$117,787</u>	<u>\$113,505</u>

PHILADELPHIA GAS WORKS
DETAIL OF DIRECT LABOR EXPENSES
(Dollars in Thousands)

Line No.	Actual 1999-2000		Actual 2000-01		Budget 2001-02	
	Average Personnel	Payroll	Average Personnel	Payroll	Average Personnel	Payroll
1. Administration	53	\$3,760	47	\$3,438	54	\$3,918
2. Finance	49	2,421	48	2,267	45	2,205
3. Customer Activities	299	16,130	323	18,320	357	18,999
4. Marketing & Planning	56	3,192	66	3,695	80	4,545
5. Operations	1,099	59,024	1,037	57,413	988	54,826
6. Systems & Services	281	14,339	275	14,173	279	14,432
7. Philadelphia Gas Commission		463		458		461
8. Total Personnel & Payroll	1,837	\$99,329	1,796	\$99,764	1,803	\$99,386
9. Allocated to Capital & Appliances		(20,068)		(19,610)		(20,540)
10. Net Operating Labor	1,837	\$79,261	1,796	\$80,154	1,803	\$78,846

PHILADELPHIA GAS WORKS
DETAIL OF OTHER EXPENSES
(Dollars in Thousands)

LINE NO.	<u>OTHER EXPENSES</u>	<u>Actual 1999-2000</u>	<u>Actual 2001-02</u>	<u>Budget 2001-02</u>
1.	Appropriation for Reserves and Other Losses	\$3,415	\$2,540	\$2,454
2.	Advertising	383	871	1,122
3.	General Material	4,833	4,484	4,008
4.	Insurance	2,143	1,317	1,896
5.	Contracted Maintenance	3,052	3,316	4,483
6.	Utilities	3,631	3,750	3,442
7.	Rentals	1,411	1,297	1,276
8.	Purchased Services	17,982	17,768	18,853
9.	Postage	2,142	2,050	2,468
10.	Promotion	94	336	1,100
11.	Non-Utility Revenues	(64)	(128)	(80)
12.	Labor Related Fringe Benefits and A&G Charged to Capital	(9,512)	(12,259)	(13,430)
13.	Depreciation	35,133	35,184	35,081
14.	Less: Cleared to Capital	(1,259)	(841)	(979)
15.	Miscellaneous	11,507	8,311	23,693
16.	Total Other Expenses	<u>\$74,891</u>	<u>\$67,996</u>	<u>\$85,387</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

**APPROPRIATION FOR RESERVE
AND OTHER LOSSES**

	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Distribution	(\$21)	(\$67)	\$26
Risk Management	2,939	2,123	1,877
Compensated Absences	84	233	151
Corporate Settlements	413	251	400
Grand Total	<u><u>\$3,415</u></u>	<u><u>\$2,540</u></u>	<u><u>\$2,454</u></u>

ADVERTISING

	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Field Services	\$130	\$258	\$264
Collection & Revenue Recovery	150	40	60
Marketing	2	5	200
VP Public Policy	9	230	200
Human Resources	9	49	60
VP Customer Affairs	-	85	150
PUC	-	66	80
Gas Commission	54	108	60
Telecommunications	24	18	12
Building Services	-	1	-
IT	-	1	-
Materials Management	5	10	36
Grand Total	<u><u>\$383</u></u>	<u><u>\$871</u></u>	<u><u>\$1,122</u></u>

DETAIL OF OTHER OPERATING EXPENSES C-4

GENERAL MATERIAL	Actual 1999-2000	Actual 2000-01	Budget 2001-02
Gas Processing	\$1,760	\$1,693	\$1,502
Distribution	1,840	2,323	1,852
Field Services	2,688	1,273	1,699
Collection & Revenue Recovery	380	363	400
Customer Service	32	61	70
Customer Accounting	5	-	5
Marketing	30	18	50
Marketing Point of Sale	7	-	-
VP Public Policy	44	29	45
Gas Control & Acquisition	6	5	18
Human Resources	21	8	37
Risk Management	4	2	4
Accounting & Reporting	9	12	7
Treasury	63	32	36
Other A & G	20	18	45
Sr VP Legal & Genl Counsel	29	27	24
VP Customer Affairs	8	4	25
VP Regulatory Affairs	5	23	36
Gas Commission	19	15	20
Emergency Operations	-	60	(10)
Utility Gas Use	(233)	(616)	(865)
Building Service	333	478	662
Engineering Service	22	51	24
Information Technology	231	335	373
Office Services	86	101	79
Telecommunications	8	6	9
Transportation Services	1,107	1,312	1,189
Chemical Laboratory Services	15	18	25
Materials Management	(3,706)	(3,167)	(3,353)
Grand Total	\$4,833	\$4,484	\$4,008

DETAIL OF OTHER OPERATING EXPENSES C-4

INSURANCE	Actual 1999-2000	Actual 2000-01	Budget 2001-02
Human Resources	\$24,261	\$27,392	\$30,500
Risk Management	2,432	2,545	3,632
Gas Planning & FRA	950	-	-
Gas Commission	49	62	55
Sub-Total	27,692	29,999	34,187
Less Group Life & Health	25,549	28,682	32,291
Grand Total	<u>\$2,143</u>	<u>\$1,317</u>	<u>\$1,896</u>

CONTRACTED MAINTENANCE	Actual 1999-2000	Actual 2000-01	Budget 2001-02
Maintenance Contractors	\$1,308	\$1,126	\$1,156
Maintenance Software	1,092	1,443	2,119
Maintenance - Capital		17	
Maintenance Office Equipment	652	730	1,208
Grand Total	<u>\$3,052</u>	<u>\$3,316</u>	<u>\$4,483</u>

UTILITIES	Actual 1999-2000	Actual 2000-01	Budget 2001-02
Electric	\$1,880	\$1,884	\$1,861
Purchased Telephone	1,566	1,691	1,387
Water	185	175	194
Grand Total	<u>\$3,631</u>	<u>\$3,750</u>	<u>\$3,442</u>

RENTALS	Actual 1999-2000	Actual 2000-01	Budget 2001-02
Other Rents	\$345	\$373	\$372
Equipment Rentals & Leasing	1,066	924	904
Operating Leases			
Grand Total	<u>\$1,411</u>	<u>\$1,297</u>	<u>\$1,276</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

	Actual	Actual	Budget
<u>Maintenance Contractors</u>	<u>1999-2000</u>	<u>2000-01</u>	<u>2001-02</u>
Gas Processing	\$552	\$383	\$482
Distribution	271	304	216
Field Services	-	-	8
Collection & Revenue Recovery	1	-	8
Human Resources	3	4	5
Environment		5	
Security	-	-	4
Building Services	444	315	433
Transportation Service	37	25	-
Engineering		10	
IT		56	
Office Services		7	
Telecommunications		3	
Material Management		14	
Grand Total	<u>\$1,308</u>	<u>\$1,126</u>	<u>\$1,156</u>

	Actual	Actual	Budget
<u>Maintenance Software</u>	<u>1999-2000</u>	<u>2000-01</u>	<u>2001-02</u>
Field Services	\$132	\$155	\$170
Customer Service	15	-	-
Gas Control & Acquisition	-	-	120
Security	-	-	8
Gas Planning	-	-	26
Engineering	8	10	15
Information Technology	925	1,177	1,780
Telecommunications	12	51	-
Building Services		5	
Transportation		7	
Chemical Laboratory		2	
Material Management		36	
Grand Total	<u>\$1,092</u>	<u>\$1,443</u>	<u>\$2,119</u>

	Actual	Actual	Budget
<u>Maintenance Office Equipment</u>	<u>1999-2000</u>	<u>2000-01</u>	<u>2001-02</u>
Gas Processing	-	-	\$1
Field Services	15	8	15
Collection & Revenue Recovery	63	1	5
Customer Service	9	-	20
VP Public Policy	-	2	4
Marketing		1	
Human Resources	-	-	2
Other A & G	3	9	8
Maintenance Office Equipment	106	117	50
Building Service	-	10	-
Information Technology	310	369	758
Office Services	15	16	42
Engineering		6	
Transportation		5	
Material Mgt		18	
Chemical Lab		2	
Telecommunications	131	166	303
Grand Total	<u>\$652</u>	<u>\$730</u>	<u>\$1,208</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

<u>Electric</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Processing	\$1,029	\$958	\$1,020
Distribution	59	23	24
Building Service	792	679	817
Engineering		22	
IT		122	
Office Services		15	
Telecommunications		6	
Transportation		33	
Material Management		26	
Grand Total	<u>\$1,880</u>	<u>\$1,884</u>	<u>\$1,861</u>

<u>Purchased Telephone</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Commission	\$5	\$5	\$6
Building Services		53	
Engineering		28	
IT		82	
Office Services		4	
Transportation		21	
Chemical Lab		10	
Material Management		38	
Telecommunications	1,561	1,450	1,381
Grand Total	<u>\$1,566</u>	<u>\$1,691</u>	<u>\$1,387</u>

<u>Water</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Processing	\$104	\$86	\$90
Distribution	2	1	1
Building Service	79	66	103
Engineering		2	
IT		12	
Office Services		1	
Telecommunications		1	
Transportation		3	
Material Management		3	
Grand Total	<u>\$185</u>	<u>\$175</u>	<u>\$194</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

<u>Other Rents</u>	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
Distribution	\$1	\$3	\$2
Customer Service	292	297	277
Gas Commission	51	72	92
Building Services	1	1	1
Grand Total	\$345	\$373	\$372

<u>Equipment Rentals & Leasing</u>	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
Gas Processing	\$146	\$25	\$15
Distribution	5	1	2
Field Services	81	61	67
Collection & Revenue Recovery	229	209	250
Customer Service	84	74	80
Customer Accounting	-	-	1
Marketing	17	2	2
VP Public Policy	21	7	-
Gas Control & Acquisition	2	1	2
Human Resources	4	3	6
Risk Management	-	1	2
Accounting & Reporting	4	4	5
Other A&G	18	21	21
Sr VP General Counsel & Legal	5	8	5
Gas Commission	13	11	14
Building Services	59	53	11
Engineering	30	53	14
Information Technology	197	270	266
Office Services	67	13	19
Telecommunicaytions	10	1	36
Transportation Service	63	78	58
Chemical Services	1	2	3
Materials Management	10	26	25
Grand Total	\$1,066	\$924	\$904

DETAIL OF OTHER OPERATING EXPENSES C-4

PURCHASED SERVICES & BANK FEES

	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Processing	\$817	\$396	\$582
Distribution	85	74	74
Field Services	317	366	282
Collection & Revenue Recovery	706	1,187	3,300
Customer Service	122	188	140
Customer Service Bank Fees	10	235	25
Customer Accounting	-	6	5
Marketing	35	21	750
Marketing Point of Sale	1	-	-
VP Public Policy	379	216	375
Gas Control & Acquisition	58	102	48
Human Resources	1,214	1,117	1,020
Risk Management	704	672	655
Accounting & Reporting	11	9	20
Treasury	79	85	214
Treasury Bank Fees	83	-	90
Other A & G	15	-	(120)
President & CEO	3	2	5
Executive Search		176	50
Sr VP Gen'l Counsel & Legal	132	112	100
Conservation Works Program	2,020	-	2,200
VP Customer Affairs	235	2,808	150
Security	1,354	1,408	1,545
VP Regulatory Affairs	10	1	3
Public Utility Commission	128	809	942
Director Strategic Planning		-	100
Gas Planning & Fed Reg Aff	100	94	103
PMO	-	853	325
VP Human Resources	44	17	15
Internal Auditing	-	44	10
Gas Commission	562	326	560
Administrative Consultants	3,792	1,883	867
FERC Matters	117	96	75
Special Legal	1,721	570	1,200
Emergency Operations	-	163	75
Environmental	-	7	200
Building Service	226	225	205
Engineering Service	13	43	33
Information Technology	2,409	2,950	2,203
Office Services	1	6	2
Telecommunications	145	138	111
Transportation Services	107	142	132
Chemical Laboratory Services	2	8	8
Materials Management	225	193	174
SR VP Operations		1	
Customer Review		3	
CFO		5	
SR VP Marketing		11	
Grand Total	<u>\$17,982</u>	<u>\$17,768</u>	<u>\$18,853</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

POSTAGE

	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Budget <u>2001-02</u>
Gas Processing	-	-	\$1
Distribution	-	-	1
Field Services	92	142	175
Collection & Revenue Recovery	1,981	1,828	2,045
Customer Service	7	1	4
Marketing	8	4	75
VP Public Policy	2	4	10
Human Resources	3	8	12
Risk Management	-	2	3
Accounting & Reporting	-	1	2
Treasury	8	10	12
Other A & G	3	9	12
VP Customer Affairs	2	26	75
Materials Management	36	15	41
Grand Total	<u>\$2,142</u>	<u>\$2,050</u>	<u>\$2,468</u>

PROMOTION

	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Budget <u>2001-02</u>
Marketing	\$94	\$336	\$1,100
Grand Total	<u>\$94</u>	<u>\$336</u>	<u>\$1,100</u>

NON-UTILITY REVENUE

	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Budget <u>2001-02</u>
Customer Accounting	(\$32)	(\$64)	(\$40)
Customer Service	(32)	(64)	(40)
Grand Total	<u>(\$64)</u>	<u>(\$128)</u>	<u>(\$80)</u>

**LABOR RELATED FRINGE BENEFITS &
A&G CHARGED to CAPITAL**

	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Budget <u>2001-02</u>
Construction Overheads	(\$4,654)	(\$7,225)	(\$5,703)
A & G Additive	(4,858)	(5,034)	(7,727)
Grand Total	<u>(\$9,512)</u>	<u>(\$12,259)</u>	<u>(\$13,430)</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

MISCELLANEOUS

	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Expense of Employees	\$419	\$252	\$1,047
Dues & Subscriptions	888	2,034	2,096
Taxes	33	33	35
PFMC - Management Fee	363	270	673
Deferred Compensation	382	388	388
LNG Inventory	(198)	211	(383)
Capital Lease Amortization	2,144	1,634	3,357
Amortization	7,476	3,489	6,480
MISCELLANEOUS			10,000
 Grand Total	 <u>\$11,507</u>	 <u>\$8,311</u>	 <u>\$23,693</u>

DETAIL OF OTHER OPERATING EXPENSES C-4

<u>Expense of Employees</u>	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
Gas Processing	\$30	\$21	\$25
Distribution	35	10	22
Field Services	46	7	187
Collection & Revenue Recovery	11	6	8
Customer Service	8	5	25
Customer Accounting	-	4	5
Marketing	45	15	175
VP Public Policy	13	1	10
Gas Control & Acquisition	15	5	30
Human Resources	10	4	40
Risk Management	1	-	4
Accounting & Reporting	8	12	25
Treasury	5	3	15
Other A & G	1	47	15
President & CEO	5	1	5
Sr VP General Counsel & Legal	5	4	22
VP Customer Affairs	10	5	80
COO	2	-	5
Security	5	1	10
VP Regulatory Affairs	9	2	15
Sr VP Finance	4	4	8
Gas Planning	6	16	45
VP Human Resources	2	-	5
CFO	-	-	5
Internal Auditing	12	1	29
SR VP Operations	3	1	3
SR VP Marketing	6	3	5
Gas Commission	4	-	5
Building Service	13	10	14
Engineering Service	7	7	7
Information Technology	55	39	123
Office Services	1	-	-
Telecommunications	-	3	13
Transportation Services	7	3	9
Chemical Laboratory Services	2	5	16
Materials Management	33	7	37
Grand Total	\$419	\$252	\$1,047

DETAIL OF OTHER OPERATING EXPENSES C-4

<u>Dues & Subscriptions</u>	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
Gas Processing	-	\$1	\$1
Distribution	2	2	5
Field Services	1	1	2
Collection & Revenue Recovery	1	-	1
Customer Service	1	-	2
Customer Accounting	-	-	1
Marketing	56	52	80
VP Public Policy	17	1	15
Gas Control & Acquisition	3	21	20
Human Resources	95	117	125
Risk Management	3	-	2
Accounting & Reporting	2	1	2
Treasury	1	1	2
Other A & G	12	8	29
Sr VP Genl Counsel & Legal	6	6	13
VP Customer Affairs	-	-	10
PUC	223	1,358	1,450
Gas Planning	26	15	23
Company Dues & Subscriptions	422	432	275
Building Service	1	2	2
Engineering Service	4	7	3
Information Technology	1	2	18
Telecommunications	-	1	-
Transportation Services	3	3	3
Chemical Laboratory	1	1	1
Materials Management	7	2	11
Grand Total	\$888	\$2,034	\$2,096

DETAIL OF OTHER OPERATING EXPENSES C-4

<u>Taxes</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Commission	\$33	\$33	\$35
Grand Total	<u>\$33</u>	<u>\$33</u>	<u>\$35</u>

<u>Amortization</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
Gas Processing	\$52	\$33	-
Field Services	82	255	-
Risk Management	15	-	-
Public Utility Commission	23	262	704
Director Strategic Planning	7	7	7
PMO	-	-	333
Gas Commission	2	2	-
Administrative Consulting	307	196	205
Grays Ferry Legal Expense	89	-	-
Emergency Operations	-	-	212
Relocation Expenses	78	78	78
Regulatory Asset	1,984	339	3,000
Restructuring	965	-	965
Year 2000 & Deregulation	882	-	-
Information Technology	2,990	2,217	976
Building Expense	-	5	-
Enginnering	-	12	-
Transportation	-	12	-
Chemical Laboratory	-	4	-
Material Management	-	67	-
Grand Total	<u>\$7,476</u>	<u>\$3,489</u>	<u>\$6,480</u>

PHILADELPHIA GAS WORKS
OTHER INCOME
(Dollars in Thousands)

	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Current</u> <u>Rates</u> <u>Budget</u> <u>2000-02</u>	<u>\$60.0M</u> <u>Budget</u> <u>2000-02</u>
<u>Interest Earnings On:</u>				
Capital Improvement Fund	\$3,215	\$600	\$1,858	\$1,858
Capital Lease Fund	616	452	192	192
Revenue Bond Sinking Fund	1,799	2,196	1,667	1,667
Temporary Investments	2,253	727	750	1,700
Gain (Loss) on Investments	(21)	532	-	-
Natural Gas Refunds	2	661	-	-
Notes Receivable - Intl House		24	24	24
Rev & Exp - Non-Utility Operations		502		
Total Interest Earnings	7,864	5,694	4,491	5,441
Rental Income	49	64	71	71
Miscellaneous	1,289	6,265	11	11
Swap Option Proceeds	215	320	320	320
AFUDC	-	-	-	-
Total Other Income	\$9,417	\$12,343	\$4,893	\$5,843

PHILADELPHIA GAS WORKS
REVENUE BOND DEBT SERVICE
(Dollars in Thousands)

Line No.	Year Issued	Series	Actual 1999-00	Actual 2000-01	Budget 2001-02
<u>Interest Payments</u>					
1.	1989	11th C TECA	\$3,811	\$4,043	\$4,274
2.	1989	12th A	111	-	-
3.	1990	12th A TECA	-	920	979
4.	1990	12th B	-	-	-
5.	1991	13th	196	102	-
6.	1993	14th	14,607	14,098	13,684
7.	1994	15th	5,972	5,306	4,834
8.	1998	1st A	8,358	8,332	7,927
9.	1998	1st B	5,190	5,190	5,190
10.	1999	16th	3,352	3,265	3,239
11.	1999	2nd	5,811	5,612	5,535
12.	2001	3rd	-	-	6,814
13.	Total Interest Payments		<u>\$47,408</u>	<u>\$46,868</u>	<u>\$52,476</u>
<u>Interest Accruals</u>					
14.	1989	11th C TECA	\$2,671	\$2,349	\$2,002
15.	1989	12th A	79	-	-
16.	1990	12th A TECA	1,142	1,188	1,151
17.	1990	12th B	-	-	-
18.	1991	13th	177	81	-
19.	1993	14th	14,522	14,029	13,491
20.	1994	15th	5,917	5,266	4,804
21.	1998	1st A	8,353	8,264	7,898
22.	1998	1st B	5,190	5,190	5,190
23.	1999	16th	3,277	3,261	3,235
24.	1999	2nd	5,672	5,599	5,522
25.	2001	3rd	-	1,092	6,241
26.	Total Interest Accruals		<u>\$47,000</u>	<u>\$46,319</u>	<u>\$49,534</u>

**PHILADELPHIA GAS WORKS
OTHER LONG TERM DEBT SERVICE**
(Dollars in Thousands)

Line No.	<u>Year Issued</u>	<u>Series</u>	<u>Actual 1999-00</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
<u>Interest Payments</u>					
1.	1996	Capital Lease	\$491	\$280	\$57
2.	1997	Capital Lease	959	796	624
3.	1998	1st C Subordinate	967	925	881
4.	Total Interest Payments		<u>\$2,417</u>	<u>\$2,001</u>	<u>\$1,562</u>
<u>Interest Accruals</u>					
5.	1996	Capital Lease	\$404	\$188	\$9
6.	1997	Capital Lease	892	726	550
7.	1998	1st C Subordinate	960	918	873
8.	Total Interest Accruals		<u>\$2,256</u>	<u>\$1,832</u>	<u>\$1,432</u>

PHILADELPHIA GAS WORKS
OTHER INTEREST
(Dollars in Thousands)

Line No.	<u>Other Interest</u>	<u>Actual 1999-00</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
1.	Tax-Exempt Commercial Paper	\$3,927	\$4,552	\$4,714
2.	Bond Discount, Issuance & Premium Expense	1,557	1,537	1,710
3.	Customer Deposits	-	589	74
4.	Miscellaneous Interest Expense	311	-	-
5.	Interest on Notes Payable	15	2	-
6.	Extraordinary Loss	4,311	4,162	3,976
	Total Other Interest	<u>\$10,121</u>	<u>\$10,842</u>	<u>\$10,474</u>
7.	AFUDC *	<u>\$374</u>	<u>\$588</u>	<u>\$775</u>
8.	* Total AFUDC	\$374	\$588	\$775
9.	Included In Other Income	-	-	-

**PHILADELPHIA GAS WORKS
CAPITAL FUNDING & EXPENDITURES
(Dollars In Thousands)**

Line No.		<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Budget 2001-02</u>
SOURCE:				
1.	Capital Improvement Fund & Leasing	\$71,492	\$55,356	\$62,943
2.	Temporary Financing	22,000	45,000	-
3.	Internally Generated Funds	-	-	-
4.	Total Sources	<u>\$93,492</u>	<u>\$100,356</u>	<u>\$62,943</u>
 USE:				
Capital Expenditures:				
5.	Gas Processing	\$926	\$14,255	\$12,528
6.	Distribution	31,194	34,043	35,125
7.	Field Services	8,097	5,080	7,356
8.	Information Technology	1,293	1,193	2,603
9.	Other Department	6,629	2,853	5,331
10.	Total Uses	<u>\$48,139</u>	<u>\$57,424</u>	<u>\$62,943</u>

**PHILADELPHIA GAS WORKS
REVENUE BOND DEBT SERVICE**
(Dollars in Thousands)

Line No.	Year <u>Issued</u>	<u>Series</u>	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Budget <u>2001-02</u>
Principal Payments					
1.	1989	11th C	\$3,421	\$3,197	\$2,966
2.	1990	12th A	1,635	825	767
3.	1991	13th	1,270	1,365	
4.	1993	14th	8,925	7,125	16,625
5.	1994	15th	15,690	10,725	7,490
6.	1998	1st A	580	8,525	3,595
7.	1999	16th	355	640	670
8.	1999	2nd	<u>1,720</u>	<u>1,790</u>	<u>1,865</u>
9.	Total Principal Payments		<u><u>\$33,596</u></u>	<u><u>\$34,192</u></u>	<u><u>\$33,978</u></u>

PHILADELPHIA GAS WORKS
OTHER LONG TERM DEBT SERVICE
(Dollars in Thousands)

Line No.	Year <u>Issued</u>	<u>Series</u>	<u>Actual</u> <u>1999-2000</u>	<u>Actual</u> <u>2000-01</u>	<u>Budget</u> <u>2001-02</u>
<u>Principal Payments</u>					
1.	1996	Capital Lease	\$3,500	\$3,700	\$1,900
2.	1997	Capital Lease	3,038	3,201	3,373
3.	1998	1st C Subordinate	1,020	1,065	1,105
4.	Total Principal Payments		<u>\$7,558</u>	<u>\$7,966</u>	<u>\$6,378</u>

PHILADELPHIA GAS WORKS WORKING CAPITAL DETAIL

(Dollars in Thousands)

Line No.	Actual Balance <u>8/31/99</u>	Actual Balance <u>8/31/00</u>	Actual Balance <u>8/31/01</u>	Current Rates Budget Balance <u>8/31/02</u>	\$60.0M Budget Balance <u>8/31/02</u>
ASSETS					
1. Accounts Receivable	\$127,606	\$171,121	\$275,074	\$259,637	\$264,631
2. Accrued Gas Revenues	7,001	14,300	5,332	8,600	9,800
3. Uncollectible Reserve	<u>(94,224)</u>	<u>(129,154)</u>	<u>(184,324)</u>	<u>(194,198)</u>	<u>(195,346)</u>
4. Net Accounts Receivable	40,383	56,267	96,082	74,039	79,085
5. Materials & Supplies	53,850	67,699	91,234	100,964	100,964
6. Other Current Assets	<u>21,771</u>	<u>25,603</u>	<u>4,851</u>	<u>6,111</u>	<u>6,111</u>
7. Total Assets	<u>\$116,004</u>	<u>\$149,569</u>	<u>\$192,167</u>	<u>\$181,114</u>	<u>\$186,160</u>
LIABILITIES					
Accounts Payable:					
8. Natural Gas	\$18,972	\$23,364	\$37,296	\$22,876	\$22,876
9. General	<u>19,658</u>	<u>12,726</u>	<u>14,553</u>	<u>14,750</u>	<u>14,750</u>
10. Total Accounts Payable	38,630	36,090	51,849	37,626	37,626
11. Other Current Liabilities	<u>36,144</u>	<u>24,122</u>	<u>17,562</u>	<u>13,566</u>	<u>13,566</u>
12. Total Liabilities	<u>\$74,774</u>	<u>\$60,212</u>	<u>\$69,411</u>	<u>\$51,192</u>	<u>\$51,192</u>
13. Total Working Capital	<u>\$41,230</u>	<u>\$89,357</u>	<u>\$122,756</u>	<u>\$129,922</u>	<u>\$134,968</u>
14. Net Increase/(Decrease)		\$48,127	\$33,399	\$7,166	\$12,212

PHILADELPHIA GAS WORKS WORKING CAPITAL CHANGES

(Dollars in Thousands)

Line No.	Actual Change <u>8/31/00</u>	Actual Change <u>8/31/01</u>	Current Rates Budget Change <u>8/31/02</u>	\$60.0 M Budget Change <u>8/31/02</u>	
ASSETS					
1.	Accounts Receivable	\$43,515	\$103,953	(\$15,437)	(\$10,443)
2.	Accrued Gas Revenues	7,299	(8,968)	3,268	4,468
3.	Uncollectible Reserve	<u>(34,930)</u>	<u>(55,170)</u>	<u>(9,874)</u>	<u>(11,022)</u>
4.	Net Accounts Receivable	15,884	39,815	(22,043)	(16,997)
5.	Materials & Supplies	13,849	23,535	9,730	9,730
6.	Other Current Assets	<u>3,832</u>	<u>(20,752)</u>	<u>1,260</u>	<u>1,260</u>
7.	Total Assets	<u><u>\$33,565</u></u>	<u><u>\$42,598</u></u>	<u><u>(\$11,053)</u></u>	<u><u>(\$6,007)</u></u>
LIABILITIES					
Accounts Payable:					
8.	Natural Gas	\$4,392	\$13,932	(\$14,420)	(\$14,420)
9.	General	<u>(6,932)</u>	<u>1,827</u>	<u>197</u>	<u>197</u>
10.	Total Accounts Payable	(2,540)	15,759	(14,223)	(14,223)
11.	Other Current Liabilities	<u>(12,022)</u>	<u>(6,560)</u>	<u>(3,996)</u>	<u>(3,996)</u>
12.	Total Liabilities	<u><u>(\$14,562)</u></u>	<u><u>\$9,199</u></u>	<u><u>(\$18,219)</u></u>	<u><u>(\$18,219)</u></u>
13.	Total Working Capital	<u><u>\$48,127</u></u>	<u><u>\$33,399</u></u>	<u><u>\$7,166</u></u>	<u><u>\$12,212</u></u>

PHILADELPHIA GAS WORKS
DETAIL OF NON-CASH EXPENSES
(Dollars in Thousands)

Line No.	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Revised Budget <u>2001-02</u>
DEPRECIATION			
1.	\$35,133	\$35,184	\$35,081
2.	(1,259)	(841)	(979)
	<u>33,874</u>	<u>34,343</u>	<u>34,102</u>
SUBORDINATE PAYMENTS			
3.	1,271	1,165	1,383
4.	767	872	1,000
5.	8,431	0	(320)
	<u>10,469</u>	<u>2,037</u>	<u>2,063</u>
5.	<u><u>\$44,343</u></u>	<u><u>\$36,380</u></u>	<u><u>\$36,165</u></u>
DETAIL OF DEPRECIATION & AMORTIZATION			
	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Revised Budget <u>2001-02</u>
6.	\$32,614	\$32,559	\$32,581
7.	2,503	2,336	4,565
8.	1,557	1,449	1,710
9.	4,311	4,162	3,976
10.	-	-	-
11.	<u><u>\$40,985</u></u>	<u><u>\$40,506</u></u>	<u><u>\$42,832</u></u>
NET CHANGE OTHER LONG TERM			
	Actual <u>1999-2000</u>	Actual <u>2000-01</u>	Revised Budget <u>2001-02</u>
12.	\$6,018	\$4,491	\$4,503
13.	8,780	(202)	(594)
14.	2	(1,427)	(2,100)
15.	<u><u>\$14,800</u></u>	<u><u>\$2,862</u></u>	<u><u>\$1,809</u></u>

PHILADELPHIA GAS WORKS INSURANCE EXPENSE

(Dollars in Thousands)

Line No.	<u>Insurance Type</u>	<u>Actual 1999-2000</u>	<u>Actual 2000-01</u>	<u>Revised Budget 2001-02</u>
1.	Property	\$310	\$412	\$585
2.	Public Liability	754	792	1,159
3.	Workers' Compensation	60	63	87
4.	Revenue Protection	950	-	-
5.	Miscellaneous	69	50	65
6.	Sub-Total	<u>\$2,143</u>	<u>\$1,317</u>	<u>\$1,896</u>
7.	Employees' Health	24,241	27,404	30,490
8.	Employees' Group Life	1,308	1,278	1,801
9.	Sub-Total	<u>\$25,549</u>	<u>\$28,682</u>	<u>\$32,291</u>
10.	Total Insurance	<u><u>\$27,692</u></u>	<u><u>\$29,999</u></u>	<u><u>\$34,187</u></u>

**PHILADELPHIA GAS WORKS
PERSONNEL & PAYROLL DETAIL
(Dollars in Thousands)**

DEPARTMENTS	Actual 1999-2000		Actual 2000-2001		Budget 2001-02	
	Average Personnel	Payroll	Average Personnel	Payroll	Average Personnel	Payroll
ADMINISTRATION						
Officer's Salaries		\$1,186		\$1,066		\$1,172
President & Chief Executive Officer	2	64	1	57	2	57
Director Internal Auditing	7	385	4	243	6	348
Senior VP General Counsel & Legal	13	660	11	605	14	735
VP Human Resources	19	935	23	1,108	25	1,302
VP Corporate Communications	12	530	8	359	7	304
Total	53	\$3,760	47	\$3,438	54	\$3,918
FINANCE						
Chief Financial Officer	1	\$11	1	\$34	1	\$0
Accounting & Reporting	22	990	26	1,233	24	1,290
SR VP Finance/Budget & Finl Forecasting	5	303	2	91	2	46
Corporate Planning & Analysis	2	126	1	33	-	-
Risk Management	7	364	6	283	6	287
Treasury	12	627	12	593	12	582
Total	49	\$2,421	48	\$2,267	45	\$2,205
CUSTOMER ACTIVITIES						
VP Customer Affairs	7	\$313	5	\$267	8	\$353
Collections	105	5,855	104	6,332	105	5,469
Bonus Awards		40		39		45
Customer Accounting	22	1,271	22	1,204	38	2,002
Customer Service	164	8,583	177	9,720	183	9,872
Customer Review Unit	1	68	11	474	11	570
PMO	-	-	4	284	12	688
Total	299	\$16,130	323	\$18,320	357	\$18,999
MARKETING & PLANNING						
Senior VP Marketing & Econ. Bus. Dev.	2	\$47	2	\$47	2	\$46
Marketing	30	1,720	37	2,020	40	2,220
Director Strategic Planning			1	56	3	197
VP Regulatory Affairs	2	80	3	120	6	324
Director Tariffs, Reg. Affairs & Reporting	2	114	1	88	-	-
Gas Acquisition & Control	15	967	18	1,143	20	1,215
Gas Planning & Federal Reg Affairs	5	264	4	221	9	543
Total	56	\$3,192	66	\$3,695	80	\$4,545
OPERATIONS						
Chief Operating Officer	1	\$45	0	-	2	54
Senior VP Operations	3	128	4	187	4	213
Field Services	494	27,218	442	25,065	385	22,141
Distribution	446	22,879	439	22,839	443	23,664
Gas Processing	155	8,754	151	9,268	150	8,545
Operations Systems Support	-	-	1	54	4	209
Total	1,099	\$59,024	1,037	\$57,413	988	\$54,826
SYSTEMS & SERVICES						
VP Information Technology	43	\$2,422	44	\$2,358	53	\$2,777
VP Operation Support	2	56	0	-	-	-
Director Procurement	2	146	8	427	10	535
Engineering Services	30	1,731	26	1,484	25	1,451
Building Services	67	2,854	68	2,892	64	2,865
Telecommunications	2	57	1	87	2	150
Security	3	150	4	258	5	261
Materials Management	75	3,975	68	3,641	63	3,350
Chemical Services	4	228	4	255	6	311
Transportation	53	2,720	52	2,771	51	2,732
Total	281	\$14,339	275	\$14,173	279	\$14,432
SUB-TOTAL	1,837	\$98,866	1,796	\$99,306	1,803	\$98,925
Philadelphia Gas Commission		463		458		461
GRAND TOTAL PAYROLL	1,837	\$99,329	1,796	\$99,764	1,803	\$99,386

**PHILADELPHIA GAS WORKS
NORMALIZED EXPENSES
1999-2000 ACTUAL**

<u>Description</u>	<u>Department</u>	<u>Cash Expenditure</u>	<u>Years Amortized</u>	<u>1999-2000</u>	<u>2000-01</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>
Mainframe Technical & Network Serv	Information Technology	516,437	3	172,237	172,100	172,100				
Application Services - Legacy	Information Technology	1,214,865	3	404,965	404,950	404,950				
PUC Management Audit	PUC	418,932	6	23,274	69,822	69,822	69,822	69,822	69,822	46,548
PUC Rate Case	PUC	255,036	2	127,518	127,518					
Total		2,405,270		727,994	774,390	646,872	69,822	69,822	69,822	46,548

**PHILADELPHIA GAS WORKS
NORMALIZED EXPENSES
2000-01 ACTUAL**

<u>Description</u>	<u>Department</u>	<u>Cash Expenditure</u>	<u>Years Amortized</u>	<u>2000-01</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>	<u>2004-05</u>	<u>2005-06</u>
Rate Case Expense	PUC	819,471	2	409,735	409,736				
Management Audit	PUC	387,521	6	68,386	68,386	68,386	68,386	68,386	45,591
Emergency Operations	A&G	678,867	3	226,289	226,289	226,289			
Total		<u>1,885,859</u>		<u>704,410</u>	<u>704,411</u>	<u>294,675</u>	<u>68,386</u>	<u>68,386</u>	<u>45,591</u>

**PHILADELPHIA GAS WORKS
NORMALIZED EXPENSES
2001-02 BUDGET**

<u>Description</u>	<u>Department</u>	<u>Cash Expenditure</u>	<u>Years Amortized</u>	<u>2001-02</u>	<u>2002-03</u>	<u>2003-04</u>
Rate Case Expense	PUC	1,135,000	2	567,000	567,000	
Anderson Consulting	A & G	200,000	3	67,000	67,000	66,000
Emergency Operations	A & G	150,000	2	75,000	75,000	
PFMC Executive Search	A & G	50,000	3	16,667	16,667	16,666
Environmental Study	A & G	700,000	5	140,000	140,000	140,000
Administrative Consulting	A & G	200,000	2	100,000	100,000	
Total		2,435,000		965,667	965,667	222,666

**PHILADELPHIA GAS WORKS
CRP REGULATORY ASSET
(Dollars in Thousands)**

	Beginning Balance	Amortized	Crisis Grants	Ending Balance
Actual 1994-95	\$37,500	(\$3,750)	-	\$33,750
Actual 1995-96	33,750	(3,750)	(1,160)	28,840
Actual 1996-97	28,840	(3,750)	(2,397)	22,693
Actual 1997-98	22,693	2,076	(2,269)	22,500
Actual 1998-99	22,500	(3,156)	(594)	18,750
Actual 1999-2000	18,750	(1,984)	(1,766)	15,000
Actual 2000-01	15,000	1,508	(5,258)	11,250
Budget 2001-02	11,250	(3,000)	(750)	7,500
Forecast 2002-03	7,500	(3,750)		3,750
Forecast 2003-04	3,750	(3,750)		0

ACCOUNTS RECEIVABLE / BAD DEBT EXPENSE

SD-6

	Actual 1999-00	Actual 2000-01	Current Rates Budget 2001-02	\$60.0 M Budget 2001-02
Accounts Receivable				
Beginning Receivable Balance	97,038	168,234	270,300	270,300
Billed Gas Revenues	495,545	741,964	634,265	634,265
Proposed Rate increase	-	-	-	60,000
Adjustments	-	-	-	-
Other Operating Revenues	29,497	41,015	35,368	37,786
Total Revenues	525,042	782,979	669,633	732,051
	87.96%	85.16%	92.00%	92.00%
Collections Current Revenues	(461,824)	(666,817)	(616,063)	(673,486)
Prior Period Adjustments	27,443	5,782	-	-
Collections on Prior AR	0		(23,736)	(23,736)
Write-Offs Less Reactivations	(19,465)	(19,878)	(42,000)	(42,000)
Total Credit / Reductions	(453,846)	(680,913)	(681,799)	(739,223)
Ending Receivable Balance	168,234	270,300	258,134	263,128
Bad Debt Expense				
Current Year Gross Receivable	168,234	270,300	258,134	263,128
Prior Period Adjustments	(27,154)	(32,936)	(32,936)	(32,936)
Adjusted Net Recievable	141,080	237,364	225,198	230,192
Reserve Factor	38.73%	28.49%	23.00%	23.00%
Total Bad Debt Expense	54,642	67,633	51,796	52,944
Write Off Account Balance	19,465	19,878	42,000	42,000
Total Reserve Balance				
Beginning Reserve Balance	66,697	129,028	182,565	182,565
Write-Off Balance	(19,465)	(19,878)	(42,000)	(42,000)
Prior Period Adjustments	27,154	5,782	-	-
Appropriation to Reserve	54,642	67,633	51,796	52,944
Ending Reserve Balance	129,028	182,565	192,361	193,509
OAR Reserve	253	1,412	1,462	1,462
M & J Reserve	(127)	347	375	375
Total Reserve Balance	129,154	184,324	194,198	195,346

COLLECTIBILITY STUDY - August, 2001

Classification	Balance Per Study		Reserve % Uncollectible	\$ Uncollectible
	Receivable	Collectible		
Defaulted Non-Budget Agreement				
Commercial				
Residential				
Total		-	0.00%	-
Active Non-budget Agreement				
Commercial	3,254,485.39	2,538,840.32	21.99%	715,645.07
Residential	20,727,424.88	15,255,820.78	26.40%	5,471,604.10
Total	<u>23,981,910.27</u>	<u>17,794,661.10</u>	<u>25.80%</u>	<u>6,187,249.17</u>
Off - Curb & Dig				
Commercial	1,645,074.55		100.00%	1,645,074.55
Residential	10,511,269.11	1,060,634.87	89.91%	9,450,634.24
Total	<u>12,156,343.66</u>	<u>1,060,634.87</u>	<u>91.28%</u>	<u>11,095,708.79</u>
Finals				
Commercial	4,711,673.65	1,091,954.71	76.82%	3,619,718.94
Residential	47,000,004.12	6,342,626.17	86.51%	40,657,377.95
Total	<u>51,711,677.77</u>	<u>7,434,580.88</u>	<u>85.62%</u>	<u>44,277,096.89</u>
Non-Budget Non-Agreement				
Commercial	21,444,503.60	15,537,575.85	27.55%	5,906,927.75
Residential	85,843,485.00	45,270,639.43	47.26%	40,572,845.57
Total	<u>107,287,988.60</u>	<u>60,808,215.28</u>	<u>43.32%</u>	<u>46,479,773.32</u>
Defaulted Budget Agreement				
Total	6,446.82	2,875.64	55.39%	3,570.98
Active Budget Agreement				
Total	-	-		-
EMPP				
Total	1,730,419.04	1,619,908.24	6.39%	110,510.80
Sub-Total Before CRP	<u>\$ 196,874,785.96</u>	<u>\$ 88,720,876.01</u>	<u>54.94%</u>	<u>\$ 108,153,909.95</u>
CRP AGREEMENTS				
CRP Current Program	21,976,645.81	4,160,646.51	81.07%	17,815,999.30
CRP Program	8,862,238.17	3,426,564.77	61.34%	5,435,673.40
CRP Arrears	46,363,852.32	27,227,680.11	41.27%	19,136,172.21
CRP Regulatory Asset	24,056,000.45		100.00%	24,056,000.45
Total CRP	<u>\$ 101,258,736.75</u>	<u>\$ 34,814,891.39</u>	<u>65.62%</u>	<u>66,443,845.36</u>
Other - Inactive Accounts	\$ 9,619,125.20	\$ 2,662,825.42	72.03%	6,856,299.78
Credit Balances	\$ (15,394,681.99)			
Non-Gas/Disputed Bills	\$ 2,764,757.22		100.00%	2,764,757.22
Grand Total	<u>\$ 295,022,823.14</u>	<u>\$ 126,198,592.82</u>		<u>\$ 184,218,812.31</u>

COLLECTIBILITY STUDY - December 2001

Classification	Balance Per Study		Reserve	
	Receivable	Collectible	% Uncollectible	\$ Uncollectible
Defaulted Non-Budget Agreement				
Commercial				
Residential				
Total			0.00%	
Active Non-budget Agreement				
Commercial	2,388,381.91	1,927,116.90	19.31%	461,265.01
Residential	12,561,741.15	10,026,538.57	20.18%	2,535,202.58
Total	14,950,123.06	11,953,655.47	20.04%	2,996,467.59
Off - Curb & Dig				
Commercial	1,482,740.95		100.00%	1,482,740.95
Residential	8,762,741.08	666,137.14	92.40%	8,096,603.94
Total	10,245,482.03	666,137.14	93.50%	9,579,344.89
Finals				
Commercial	5,925,196.64	7,032,572.03	-18.69%	(1,107,375.39)
Residential	58,921,419.93	7,032,572.03	88.06%	51,888,847.90
Total	64,846,616.57	14,065,144.06	78.31%	50,781,472.51
Non-Budget Non-Agreement				
Commercial	32,907,903.11	26,325,481.67	20.00%	6,582,421.44
Residential	99,232,829.17	52,896,022.71	46.70%	46,336,806.46
Total	132,140,732.28	79,221,504.38	40.65%	52,919,227.90
Defaulted Budget Agreement				
Total	8,011.47	3,192.14	60.16%	4,819.33
Active Budget Agreement				
Total				
EMPP				
Total	72.56	49.11	32.32%	23.45
Sub-Total Before CRP	<u>\$ 222,191,037.97</u>	<u>\$ 105,909,682.30</u>	<u>52.33%</u>	<u>\$ 116,281,355.67</u>
CRP AGREEMENTS				
CRP Current Program	30,843,323.25	4,871,748.88	84.20%	25,971,574.37
CRP Program	9,704,007.15	3,752,032.88	61.34%	5,951,974.27
CRP Arrears	50,040,417.10	28,649,215.75	42.75%	21,391,201.35
CRP Regulatory Asset	24,056,000.45		100.00%	24,056,000.45
Total CRP	\$ 114,643,747.95	\$ 37,272,997.50	67.49%	77,370,750.45
Other - Inactive Accounts	\$ 2,190,166.17	\$ 762,921.91	65.17%	1,427,244.26
Credit Balances	\$ (19,237,370.93)			
Non-Gas/Disputed Bills	\$ 2,898,623.93		100.00%	2,898,623.93
Grand Total	<u>\$ 322,686,205.09</u>	<u>\$ 143,945,601.71</u>		<u>\$ 187,977,974.31</u>

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC
UTILITY COMMISSION

v.

Docket No. R-000170340002

PHILADELPHIA GAS WORKS

DOCUMENT
FOLDER

DOCKETED
APR 30 2002

TESTIMONY AND EXHIBITS . PGW ERP STMT 1
W/EX TEK-1

IN SUPPORT OF

PGW ERP STMT 2
W/EXS JRB-1 JJRB-2

PHILADELPHIA GAS WORKS'

PGW ERP STMT 4
W/EXS BCB-1, BCB-2 +
BCP-3

EXTRAORDINARY RATE PETITION

PGW ERP STMT 5

3/26/02

PHB PD

ORS

PA.P.U.C.
SECRETARY'S BUREAU

02 APR -2 PM 1:54

RECEIVED

DOCUMENT
FOLDER

PGW BRP St. 1
R-00017034F0002
3/26/02

Phila, PA *REQ*

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

DOCKETED

APR 30 2002

TESTIMONY OF

JOSEPH R. BOGDONAVAGE

ON BEHALF OF

PHILADELPHIA GAS WORKS

PHILADELPHIA GAS WORKS

BASE RATE REQUEST

R-00017034

FEBRUARY 2002

RECEIVED
02 APR -2 PM 1:53
PA P.U.C.
SECRETARY'S BUREAU

1 **Q. PLEASE STATE YOUR NAME AND POSITION WITH THE COMPANY.**

2 A. My name is Joseph R. Bogdonavage. My position is Senior Vice President, Finance.

3 **Q. HOW LONG HAVE YOU HELD THIS POSITION?**

4 A. I was promoted to this position in December 2000.

5 **Q. PLEASE SUMMARIZE YOUR WORK EXPERIENCE.**

6 A. I have been employed with PGW since 1973, during which time I have held various
7 positions in the Finance area. I most recently held the position of Director – Budget &
8 Financial Forecasting. My principal responsibilities included the preparation of the
9 financial areas for the operating and capital budgets, review of operating budgets
10 prepared by the individual departments, and the coordination, analysis, issuance and
11 overall control of the complete annual Operating Budget filing.

12 **Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND.**

13 A. I received a Bachelor's Degree in Accounting from Temple University in 1972.

14 **Q. HAVE YOU EVER TESTIFIED BEFORE ANY REGULATORY AGENCIES?**

15 A. Yes, I testified before the Pennsylvania Public Utility Commission ("PUC") in
16 conjunction with PGW's 2001 base rate case. I have also testified before the
17 Philadelphia Gas Commission ("PGC") on numerous occasions, most recently on matters
18 associated with PGW's FY 2002 Operating Budget.

19 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THESE PROCEEDINGS?**

20 A. The purpose of my testimony is to: 1) provide the documentation and supporting
21 methodology for the schedules and exhibits that are included in PGW's base rate filing
22 and provide detailed information regarding PGW's fully forecasted test year financial
23 data; 2) provide an explanation for certain adjustments to the fully forecasted test year to
24 reflect the impact of various programs and expenditures that PGW anticipates incurring

1 but which were not included in PGW's approved FY 2002 operating budget; 3) explain
2 PGW's calculation of the amount of year-end cash it needs to satisfy minimum operating
3 standards including the standard for maintaining an investment grade bond rating as
4 provided by Standard & Poor's ("S&P"); 4) explain PGW's proposed charge to permit
5 the company to pay down its outstanding long-term debt to more reasonable levels; and
6 5) explain the derivation of PGW's \$60.0 million incremental revenue requirement.

7 **Q. MR. BOGDONAVAGE, WHAT IS THE LEVEL OF RATE RELIEF THAT THE**
8 **COMPANY IS REQUESTING OVERALL?**

9
10 A. The company is requesting a rate increase of \$60.0 million.

11
12 **Q. PLEASE PROVIDE THE OVERALL JUSTIFICATION FOR THE RATE**
13 **REQUEST?**

14
15 A. The company is facing a continuing liquidity crisis. That condition was recently
16 acknowledged by Standard and Poor's, one of PGW's principal bond rating agencies, and
17 is the subject of a recent notice wherein management was informed that unless there was
18 an immediate increase in PGW's cash flow the company's securities would be
19 downgraded (this is explained in Mr. Knudsen's Extraordinary Rate Petition). The fact
20 that the S&P Notice reflects the unfortunate fact that PGW has not made sufficient
21 progress over the last two years in changing the financial fundamentals of this utility.
22 The recent level of rate relief, when combined with forecasts of future operations, did not
23 provide the evaluators with enough assurance that PGW could meet its fixed cost
24 obligation into the future. Most directly, S&P was unwilling to wait for this permanent
25 base rate application to be resolved by November to determine, only then, whether the
26 rate award would be sufficient.

27

1 It is the view of management that PGW must get back on track quickly, that it is in the
2 best interest of customers to have a financially healthy utility sooner rather than later, that
3 the costs of delay are mounting – particularly capital charges and that \$60 million of rate
4 relief will accomplish the task over the next several years. But, the task must commence
5 in earnest and PGW must stay the course. However if, by 2004 or 2005, it is determined
6 that PGW is well on the way toward meeting its financial objectives, the company will
7 consider filing for a rate reduction.

8
9 **Q. PGW SEEKS A WEATHER NORMALIZATION CLAUSE AT THE SAME**
10 **TIME. PLEASE EXPLAIN.**

11
12 A. PGW has no investor of last resort who is paid a risk premium for a return on capital to
13 absorb earnings losses based on the vagaries of weather. In four out of the last five years,
14 PGW has experienced a substantially warmer than normal heating season. PGW is in its
15 current financial straits mainly because of this fact. PGW and the City of Philadelphia
16 can no longer be subject to these risks. As a municipal utility this risk belongs on the
17 customer. Moreover, there is neither the means within, nor the legal basis to call upon,
18 the City's General Fund as a source of risk capital. Therefore, as explained by Mr.
19 White, the company is proposing a rate clause which shares the risks with the customers
20 when the weather is warmer than normal but also shares the rewards when weather is
21 colder than normal and customers are bearing the double burden of higher sales and most
22 likely higher gas costs at the same time.

23 **Q. MR. BOGDONAVAGE, WHAT CIRCUMSTANCES ARE DIFFERENT NOW**
24 **COMPARED TO THE PERIOD IN WHICH PGW REQUESTED ITS LAST**
25 **BASE RATE CASE?**

26
27 A. Most significantly, natural gas costs which were at all time high levels in the fall and

1 winter of 2000-01, have now returned virtually to levels prior to the price spike. To the
2 extent that other parties or the PUC were concerned about raising PGW's base rates to
3 provide otherwise justified revenue requirement, that concern clearly does not exist
4 presently. I should add that the same is true of other "concerns" raised by some parties
5 such as the adequacy of PGW's service, and particularly its call center access. These
6 issues, while clearly important, were never appropriately raised as a reason to deny an
7 otherwise justified rate hike. At any rate, PGW has made significant progress in most
8 aspects of its performance. Most notable, it has, since October 2001 achieved (and, in
9 fact, exceeded) the PUC's access standard for PGW – 80% of all calls answered within
10 30 seconds. PGW is also in the process of implementing all of the PUC Management
11 Audit recommendations and is on target to achieve the productivity/cost reduction goals
12 the Company described in the last base rate case. In PGW's opinion, there are "non-
13 financial" issues that stand in the way of responding to PGW's legitimate financial and
14 increased liquidity needs.

15 **Q. MR. BOGDONAVAGE, ARE YOU SPONSORING THE FINANCIAL DATA**
16 **SUPPORTING PGW'S CLAIM FOR A \$60.0 MILLION BASE RATE**
17 **INCREASE?**

18
19 A. Yes. Those schedules are displayed in Volume 2 of the Company's filing and reflect
20 PGW's "fully forecasted" fiscal year 2002 projection. This presentation utilizes as a
21 starting point PGW's 2002 fiscal year operating budget that was approved by the PGC on
22 January 23, 2002. My testimony provides details of the pertinent line items in PGW's
23 Income Statement, Cash Flow Statement and Debt Service Coverage Statement derived
24 from the approved budget.

1 **Q. MR. BOGDONAVAGE, WHAT ASSUMPTIONS AND EXPENSE**
2 **ADJUSTMENTS DID YOU MAKE TO PGW'S APPROVED BUDGET TO MAKE**
3 **THE TEST YEAR REPRESENTATIVE OF FUTURE PERIODS?**
4

5 A. The major changes made to the approved FY 2002 reflect the following:

- 6 • The utilization of actual FY 2001 data as the basis for working capital and balance
7 sheet accounts instead of an estimate of FY 2001 results.
- 8 • The utilization of more recent price projections for natural gas purchases and related
9 inventory activities and the resultant impact on gas revenue projections (explained in
10 Mr. Muntzer's testimony).
- 11 • The FY 2002 test year, at proposed rates, incorporates the \$60.0 million proposed
12 base rate increase and its impact on accrued gas revenues, assessed finance charges,
13 bad debt expense, year-end accounts receivable and reserve requirements.
- 14 • Other income was adjusted to reflect increased earnings associated with higher
15 investable cash balances.
- 16 • The Marketing Department's funding was restored to its original level. Within the
17 budget, as prepared, the company included funding for programs in which PGW
18 provides economic incentives to customers to convert to or increase the usage of
19 natural gas. Those incentives are included in the sales analysis of each account and no
20 sale is completed unless PGW receives its necessary rate of return. The excluded
21 costs from the approved budget were judged as more than could be actually spent in
22 FY 2002. However, the Marketing Plan assumes higher levels of expenditures for
23 next year. The amount of this adjustment is \$1,596,000.
- 24 • Pension expense was increased reflecting the utilization of an updated actuarial
25 analysis on the status of PGW's pension fund assets. At the time of the evaluation of

1 PGW's pension fund during the budget proceedings, no recognition had been given in
2 the prepared analysis for the events of September 11 and the impact on financial
3 markets. I believe a subsequent analysis, now being prepared will show that pension
4 expense would increase as a result of a substantial decline in the over-funded status of
5 PGW's Pension Fund. I have included an additional \$778,000 as an adjustment
6 recognizing the information that was provided during the Philadelphia Gas
7 Commission budget hearings..

- 8 • The amortization expense reflecting the previously approved regulatory asset
9 associated with CRP low income customer arrearages was increased. In the budget
10 proceeding, it was assumed that the \$3,750,000 expense could be reduced by
11 \$1,750,000 reflecting the receipt of crisis grants from eligible participants. PGW has
12 adjusted the reduction by \$1,000,000 resulting in an anticipated expense of \$3.0
13 million reflecting an anticipated reduction in the level of eligible participants and
14 available funding.

15 **Q. ON YOUR SCHEDULES YOU ALSO SHOW AN ENTRY OF \$10 MILLION FOR**
16 **ADDITIONAL NORMALIZING EXPENSES. PLEASE EXPLAIN.**

17
18 A. PGW anticipates that during the period in which rates will be in effect, there were
19
20 expenses that were not included in the approved FY 2002 budget that will be on-going. It
21
22 is critical that they be included in the rate determination at this time. There are five items:
23

24	• Environmental clean-up expenditures	\$3,500,000
25	• PUC-Leak Survey requirements	\$2,500,000
26	• PUC-Meter change requirements	\$2,000,000
27	• Department of Transportation Operator	\$1,000,000
28	Qualification Training Requirements.	
29	• Security (Physical Plant facility upgrades)	\$1,000,000
30		<u>\$10,000,000</u>
31		

1 The first item is environmental expense. The Company has taken an aggressive posture in
2 addressing possible environmental related problems. At the present time, an
3 environmental impact study is being conducted that will be completed in August 2002
4 and will attempt to quantify PGW's exposure at its former manufactured gas sites. PGW
5 has also made extensive internal efforts to identify possible environmental exposures.
6 The estimate for spending on this combined initiative in the rate period is \$3,500,000
7 annually. PGW anticipates that it will experience this level of spending starting in FY
8 2003.

9 The second item is the leak survey. The PUC Safety Bureau has mandated that PGW
10 conduct a leak survey at every customer's premise or establishment from the street to the
11 meter. The present practice is to monitor leaks from the street to the outside wall. The
12 reason for PGW's approach is that a large percentage of its customer's meters are inside
13 the home and access has proven difficult. This is the reason why PGW has installed
14 AMR's in its residential accounts because PGW doesn't enter the premises on a timely
15 basis. This program is expected to be completed during 2002.

16 PGW anticipates difficulty and additional costs to provide the data the Safety Bureau
17 requires. PGW anticipates spending an additional \$2,500,000 annually.

18 The third item is related to accelerated meter change-out requirements. PGW currently
19 has an age-in-service meter change program. However, the PUC requirement reduces the
20 years that a meter can reside in a residential account to eight (8) years before it is
21 replaced. PGW projects that this mandate will require spending an additional \$2,000,000
22 annually.

1 The fourth item is the federally mandated Operator Qualification Training requirement.

2 PGW currently provides training to its field personnel; however, the new requirement to
3 fully train, test and document personnel that work on live gas will result in the loss of
4 productivity that will have to be backfilled with overtime, as needed. The adherence to
5 this requirement is anticipated to result in \$1,000,000 in additional expenses annually.

6 The fifth item is security. The Company has had several separate analyses performed to
7 address PGW's security-related issues in a post-September 11 environment. The estimate
8 for increased spending during the rate period is \$1,000,000.

9 **Q. COULD YOU EXPLAIN PGW'S CLAIM FOR BAD DEBT EXPENSE?**

10 A. PGW has incorporated bad debt expense at present rates totaling \$51,796,000 and
11 \$52,944,000 at proposed rates, respectively. The latter represents approximately 7.6% of
12 Total Gas Revenues.

13 **Q. COULD YOU EXPLAIN THE MANNER IN WHICH PGW'S BAD DEBT AND**
14 **UNCOLLECTIBLE RESERVE REQUIREMENTS WERE CALCULATED**
15 **PRIOR TO PGW COMING UNDER PUC JURISDICTION?**
16

17 A. The PGC would approve an appropriation for bad debt that took into account the
18 projected level of year-end receivables and a reserve requirement for the ultimate level of
19 uncollectible accounts. That amount was then added to PGW's uncollectible reserve, less
20 write-offs, which the Company used to account for its annual bad debt expense. This
21 method was necessary because PGW operates as a cash flow company. The
22 determination of the annual level of uncollectibles obviously has a significant impact on
23 PGW's cash flow. As to the technical manner in which the requirement was calculated,
24 PGW utilizes an automated collectibility study that is performed several times during the
25 year and at fiscal year end. This evaluation is reviewed by PGW's independent auditors

1 as part of the annual audit of its financial statements. The study identifies each customer
2 account with an amount due, reviews payments made on the account during the period,
3 and compares the amount paid with the amount due. The lower amount is considered the
4 likely collectible amount. The collectible amounts are totaled and subtracted from the
5 total receivable balance. The difference is the expected uncollectible balance. This
6 uncollectible balance is then compared to the reserve balance in the general ledger and
7 adjustments are made as appropriate.

8 **Q. DO YOU BELIEVE PGW'S BAD DEBT EXPENSE SHOULD CONTINUE TO BE**
9 **CALCULATED IN THIS MANNER?**

10 A. Yes. I am advised by counsel that the Commission is required by the Public Utility Code
11 to adhere to the same rate-making method and requirements that were applicable to PGW
12 prior to its assumption of jurisdiction over the Company. The prior method for setting
13 PGW's rates and calculating its uncollectible reserve was as I have described, and really
14 is the only way to determine bad debt expense for a cash flow regulated company.

15 **Q: IN PGW'S 2001 PERMANENT BASE RATE CASE, DID THE COMMISSION**
16 **UTILIZE PGW'S PRIOR METHOD FOR DETERMINING ITS BAD DEBT**
17 **EXPENSE?**

18 A: No. The Commission adopted a methodology proposed by the Office of Trial Staff that
19 has traditionally been utilized by the Commission to calculate the bad debt expense for
20 typical investor-owned utilities. The Commission set PGW's bad debt expense
21 allowance by applying a write-off percentage to the Company's projected total future test
22 year sales revenues. The write-off percentage used by the Commission was based on a
23 five year average of actual net write-offs to gross revenues.

1 **Q. SHOULD THE COMMISSION USE ACTUAL WRITE-OFFS, AND ARE THEY**
2 **REFLECTIVE OF PGW'S ACTUAL EXPERIENCE WITH**
3 **UNCOLLECTIBLES?**

4 A. The answer is no on both points. As stated previously, PGW is a cash flow company.
5 Write-offs are geared toward income, not cash, and they do not accurately reflect PGW's
6 experience with uncollectibles. To the contrary, PGW's projection of the annual level of
7 uncollectible receivables is reflective of its actual experience and the impact that bad debt
8 has on its cash flow needs. Moreover, the level of uncollectible receivables is audited
9 annually by outside auditors. In addition, using actual write-offs distorts PGW's
10 experience because of certain deficiencies that had existed previously in its billing and
11 collection systems. Using actual write-offs dramatically understates PGW's bad debt in
12 the last two fiscal years. Because of past difficulties with PGW's BCCS system, PGW
13 was not able to write off all the accounts that it would have if its billing system had been
14 functioning properly. Thus, at a time when PGW experienced uncollectible receivables
15 as a percentage of revenues in the range of 25.6 percent in 2001 and 24.2 percent in
16 2000, actual write-offs of uncollectible accounts were reflected as 2.8 and 3.7 percent of
17 revenues. Clearly, if one looks at experience over time, it is implausible to believe that
18 PGW's bad debt levels in FY 2000 and 2001 would decline so dramatically. In actuality,
19 PGW's audited bad debt expense in 2001 and 2000 was \$67.6 and \$54.6 million,
20 respectively. Given these facts, the Commission cannot continue to utilize actual write-
21 offs as a basis for determining PGW's bad debt expense and provide for a reasonable
22 allowance for this item.

23 **Q: DO YOU BELIEVE THAT THE USE OF THE FIVE YEAR HISTORIC**
24 **AVERAGE WAS REFLECTIVE OF PGW'S BAD DEBT LEVELS?**

1 A: No, I do not. Since 2000, bad debt levels have seen dramatic increases due to a variety of
2 reasons. PGW, and the rest of the nation, experienced record high natural gas commodity
3 prices. In addition, PGW's overall collection efforts were hampered by a billing system
4 that was not fully functional. All of these factors have lead to significantly higher levels
5 of uncollectibles which are simply not reflected or accounted for by the use a five year
6 historical average that reaches back to the mid 1990s.

7 **Q: HOW DID PGW CALCULATE ITS BAD DEBT EXPENSE IN THE TEST YEAR?**

8 A. PGW utilized actual data from its audited FY 2001 financial statements, including the
9 results of the independently reviewed Collectibility Study as the basis for its FY 2002 bad
10 debt expense claim. PGW utilized the beginning customer receivable balance at
11 09/01/01. It then projected customer billings, including the proposed base rate increase,
12 a level of collections and write-offs, and the resultant change was reflected in the year-
13 end receivable balance, bad debt reserve requirement and bad debt expense. PGW
14 utilized an updated Collectibility Study in December 2001 to compare its projected
15 results for bad debt expense at year-end for reasonableness. Furthermore, as noted, the
16 bad debt expense projected in the test year at proposed rates approximates 7.6% of Total
17 Gas Revenues, the standard that was accepted in PGW's recent base rate case.

18 **Q. IF PGW WAS AWARDED A BASE RATE INCREASE LESS THAN \$60.0**
19 **MILLION, HOW WOULD BAD DEBT EXPENSE BE CALCULATED IN**
20 **ACCORDANCE WITH PGW'S METHODOLOGY?**

21 A. PGW would utilize 7.6% of the proposed base rate reduction as the applicable decrease
22 to bad debt expense.

23 **Q. MR. BOGDONAVAGE, PLEASE EXPLAIN PGW'S ON-GOING LIQUIDITY**
24 **REQUIREMENTS.**

1 A. As has been discussed in previous PUC hearings, PGW, as a cash flow method regulated
2 company, obtains all of its liquidity from rates or from borrowing. Mr. Knudsen has
3 testified previously that PGW's benchmark for adequate end-of-year liquidity is \$35-40
4 million. That is the level that is needed on a normal, on-going basis in order to have
5 sufficient funds to pay obligations in the September through January time frame. PGW
6 has a negative cash-flow during the first several months of its fiscal year but has several
7 large obligations culminating in January when it must pay a nearly \$25.0 million debt
8 service obligation and natural gas bills that come due later in the month. Accordingly,
9 rates must be set to get as close to this target as possible. The testimony of Mr. Dan Ives
10 of Lukens and Associates shows that a liquidity requirement of \$35-40 million is well
11 within the level required and received by gas utilities similar in size to PGW. In addition,
12 as I explained in the Extraordinary Rate Petition phase of the case, Standard and Poor's
13 range for an investment grade securities rating requires that PGW have 20-30% more
14 in earnings than its total fixed obligation requirement at fiscal year-end. For the test year,
15 this equates to an additional revenue requirement of between \$47.0 to \$61.0 million.

16 **Q. HAS PGW BEEN ABLE TO ACHIEVE THIS LEVEL OF END-OF-YEAR CASH**
17 **FROM OPERATIONS.**

18
19 A. No. For the last several years, PGW's end-of-year cash has fallen well below this level.
20 It has instead made up this difference by a more or less permanent utilization of its
21 commercial paper program. It has also borrowed from its restricted Capital Fund as a
22 source of liquidity. PGW has been forced to pre-draw funds from its restricted capital
23 accounts in advance of capital expenditures. The Capital Fund is established by proceeds
24 from the issuance of long-term debt. At the present time, PGW's capital programs are
25 funded 100% by external financing. In the last few years, PGW's liquidity has been so

1 thin that it has resorted to drawing down from the Capital Fund at the beginning of the
2 year as an intra-fund transfer prior to actually expending funds on capital improvements.
3 All funds drawn from the restricted account not utilized for capital expenditures must be
4 re-paid by August 31 of each fiscal year. In the past, PGW reimbursed capital
5 expenditures on a month-by-month basis, not pre-drawing to meet working capital
6 requirements at the beginning of the year.

7 **Q. WHY CAN'T PGW RELY ON ITS CAPITAL FUND TO SUPPLY LIQUIDITY**
8 **NOT OTHERWISE AVAILABLE FROM RATES?**

9
10 A. For several reasons. First, this source of liquidity relies on the ability to enter the
11 financial marketplace to issue long-term debt at the right time and amount. No company
12 can prudently rely on the ability to issue long-term debt to supply basic liquidity.
13 Second, debt issuances aren't regular annual occurrences; indeed, to supplement PGW's
14 cash from operations, it was the exhausting of proceeds from its restricted Capital
15 account that forced PGW to ask the City for a \$45.0 million working capital loan. It is
16 for these reasons that analysts and rating agencies such as Standard & Poor's are
17 demanding liquidity from revenues over and above all fixed charges in order to maintain
18 a financially healthy rating.

19
20 **Q. WHAT END-OF-YEAR CASH BALANCE HAVE YOU CALCULATED FOR**
21 **PGW AT PRESENT RATES USING THE FULLY FORECASTED,**
22 **NORMALIZED TEST YEAR.**

23
24 A. At present rates, the end-of-year cash balance is just \$2.7 million.

25 **Q. HOW WAS THE PROPOSED RATE INCREASE DERIVED?**

26 A. Focusing on the \$60.0 million increase, PGW calculated the increase required by
27 attempting to achieve a liquidity balance which first, satisfies the S&P fixed charge

1 coverage requirement and second comes as close to the \$30-40 million in year-end cash
2 balances as possible. PGW took into account the known and definite uses of funds that
3 will come due at the end of, or after, the test year:

- 4 • Paydown of commercial paper limit from \$100.0 million to \$80.0 million
- 5 • Repayment of the \$45.0 million City loan (currently due in January 2003)
- 6 • Working capital requirements (i.e. gas storage inventories, accounts
7 receivable and bad debt reserve requirements, etc.)
- 8 • Paydown of outstanding commercial paper by \$11.0 million

9 **Q. WHAT IS THE RESULTING END-OF-YEAR CASH BALANCE?**

10 A. The projected year-end cash balance at August 2003 in the test year is \$27.8 million.

11 **Q. PLEASE EXPLAIN THE BASIS FOR PGW'S PROPOSED DEBT REDUCTION**
12 **ADJUSTMENT.**

13
14 A. PGW is proposing that the PUC approve the inclusion in base rates an amount of \$10.0
15 million annually which would be earmarked to pay down or retire PGW's outstanding
16 commercial paper over the next several years. As has been testified to elsewhere, PGW's
17 only source of short-term external financing is its commercial paper program, supported
18 by a letter of credit from a consortium of banks. Currently, the total amount available to
19 be issued (the extent of the letter of credit) is a combination of \$100.0 million of principal
20 and interest. By the terms of the agreement with the banks, this maximum level will drop
21 to \$80.0 million on August 10, 2002.

22 The purpose of the commercial paper program is to provide the Company with the ability
23 to respond to short-term liquidity deficiencies and emergencies when the cash flow
24 provided by PGW's rates charged to ratepayers proves insufficient. Ideally, the short-

1 term commercial paper program should be available to the full extent of the letter of
2 credit so that PGW can call on it when needed.

3 **Q. HOW IS THE COMMERCIAL PAPER PROGRAM PRESENTLY BEING**
4 **UTILIZED?**

5
6 A. Unfortunately, for the last several years, PGW has had to fully utilize its available
7 commercial paper so that it has effectively become a semi-permanent part of PGW's
8 capital structure. Rather than using it to cover unanticipated timing differences between
9 the payment of expenses and the receipt of revenues, PGW has been forced to call on the
10 commercial paper to supply what has now become a permanent loss of liquidity caused
11 by weather related margin losses of the past. Special action needs to be taken to pay off
12 this "credit card" balance to return the commercial paper to the place it properly should
13 serve in PGW's finances.

14 **Q. MR. BOGDONAVAGE, IF THE PUC GRANTS PGW'S REQUEST FOR \$50.0**
15 **MILLION IN PERMANENT RATE RELIEF, WILL THE COMPANY BE IN A**
16 **POSITION TO PAY DOWN THE OUTSTANDING COMMERCIAL PAPER?**

17
18 A. The only portion of the commercial paper letter of credit that is considered in calculating
19 PGW's \$50 million base rate request is the required reduction in the outstanding
20 commercial paper available from \$100 million to \$80 million (the projected amounts
21 available are \$97 million and \$77 million respectively). This is required by the current
22 agreement and thus was incorporated into PGW's projected financial requirements. The
23 additional rate increase that PGW is proposing would be earmarked for further reductions
24 not in the available letter of credit but in the amount of commercial paper outstanding. In
25 other words, this \$10 million annual charge would not got to address PGW's current
26 financial obligations but would address past obligations that have been deferred by the
27 utilization of the commercial paper program.

1 **Q. HAVE THERE BEEN ANY INDEPENDENT EVALUATIONS OF THE**
2 **COMMERCIAL PAPER PROGRAM THAT SUPPORT YOUR PROPOSAL TO**
3 **FUND A RETIREMENT OF SOME OF THE OUTSTANDING PAPER**
4

5 A. The independent Engineer's Report, issued in conjunction with last year's sale of long-
6 term bonds, came to the conclusion that, with adequate rate relief, PGW could satisfy
7 these additional long-term obligations. One of the key assumptions however was that
8 PGW would retire all of its outstanding commercial paper by 2005. Similarly, the PUC's
9 Management Audit, as I understand it, indicated that, as a result of allowing the
10 commercial paper program to become a permanent part of its capitalization, PGW has
11 resorted to "financial transaction that have affected its cash flows, raised its debt to equity
12 ratio and ultimately reduced its overall financial flexibility." (Audit, pg. X-8)

13 **Q. WILL THE RETIREMENT OF THE OUTSTANDING COMMERCIAL PAPER**
14 **HAVE BENEFITS FOR RATEPAYERS?**
15

16 A. Yes. Principally, PGW will recapture some short-term flexibility, completely non-
17 existent today, to allow it to respond to emergencies or reductions in revenues caused by
18 such events as increased uncollectibles or escalating natural gas costs (if the Company's
19 proposed weather normalization clause is approved its earnings will be further protected
20 from fluctuations in weather for the most part). In addition, PGW will be able to reduce
21 the level of interest charges associated with its commercial paper program.

22 **Q. HOW WILL THE PROPOSED DEBT RECOVERY ADJUSTMENT WORK?**

23 A. PGW proposes to earmark \$10.0 million annually to the paydown of the outstanding
24 commercial paper. To avoid creating an additional bill line item, the amount will be
25 charged as a part of the approved volumetric rate.

26 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

27 A. Yes.

PGW BRP St. 3

R-00017034 Feb 02

3/26/02

Phil, PA,

PA

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

DIRECT TESTIMONY OF

WILLIAM C. MUNTZER

ON BEHALF OF
PHILADELPHIA GAS WORKS

DOCUMENT
FOLDER

Docket No. R-00017034

Philadelphia Gas Works
Proposed 2002 Rate Increase

February, 2002

DOCKETED

APR 30 2002

RECEIVED
PA, P.U.C.
SECRETARY'S BUREAU

02 APR - 2 PM 1:53

RECEIVED

1 **Q. PLEASE STATE YOUR NAME AND POSITION WITH THE COMPANY.**

2
3 A. My name is William Muntzer. My position is Director - Rates, Gas Planning &
4 Federal Regulatory Affairs (RGP&FRA).

5 **Q. HOW LONG HAVE YOU HELD THIS POSITION?**

6 A. I assumed the position of Director - RGP&FRA on December 1, 2000.

7 **Q. WHAT ARE YOUR VARIOUS JOB RESPONSIBILITIES?**

8 A. In my present position I am responsible for overseeing the development of
9 monthly pricing for PGW's 500 interruptible customers, proposing new rates and
10 rate design, overseeing the development of the various filings before the
11 Pennsylvania Public Utility Commission (PUC) and Philadelphia Gas
12 Commission (PGC), including the monthly and annual Gas Cost Rate (GCR)
13 filings, Integrated Resource Planning Report and providing supporting
14 documentation for gas costs related to PGW's Operating Budget before the PGC.
15 Additionally, I am responsible for all PGW regulatory activity related to various
16 pipeline filings before the Federal Energy Regulatory Commission (FERC).

17 **Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND.**

18 A. I received both my Master's and Bachelor's Degrees in Business from LaSalle
19 University in Philadelphia.

20 **Q. HAVE YOU EVER PROVIDED TESTIMONY BEFORE THIS**
21 **COMMISSION.**

22 A. No, I have not.

23 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

24 A. First, I will describe how PGW estimated natural gas cost levels for the fully
25 forecasted test year. Second I will identify the number, and usage per customer
26 methodology PGW utilized in determining the pro-forma revenues.

1 Q. **WHY ARE GAS COSTS RELEVANT IN A BASE RATE CASE**
2 **PROCEEDING?**

3 A. Under the cash flow method of ratemaking, certain financial elements such as
4 collections, bad debt expense and liquidity are impacted by the level of gas costs
5 experienced or projected for the company. Therefore, identifying an appropriate
6 level of gas costs is necessary to calculate PGW's cash flow and income results.
7 The impacts on these various elements are more fully discussed in the testimony
8 of Joseph Bogdonavage. (PGW BRP St. 1).

9 Q. **WHAT IS YOUR UNDERSTANDING OF THE TEST YEAR PERIOD**
10 **BEING UTILIZED BY PGW IN THIS RATE PROCEEDING?**

11 A. PGW is utilizing its Fiscal Year 2002 fully forecasted and revised budgeted data
12 as a starting point. These data were then adjusted to take account of projected
13 future changes in revenues and expenses in order to make the period
14 representative of future conditions.

15 Q. **PLEASE DESCRIBE HOW NATURAL GAS COST LEVELS WERE**
16 **PROJECTED FOR USE IN THE FULLY FORECASTED TEST YEAR.**

17 A. We used the same calculation methodology normally employed in PGW's GCR
18 filings before the PUC. However, since this case represents a fully forecasted test
19 period, the calculations stand alone and are not impacted by prior period
20 adjustments for over/under collections.

21 Q. **WHAT IS THE BASIS FOR THE PRICES USED IN DETERMINING THE**
22 **GAS COSTS USED IN THIS FILING.**

23 A. The projected natural gas prices for the test year were derived from forecasted
24 pricing data for the period September 1, 2002 through August 31, 2003. This
25 information was produced specifically for PGW by Standard and Poor's Fuel

1 Price Service on January 3rd. Additionally, PGW used the NYMEX futures
2 information, from January 25th.
3 Specifically, the company used the average of the NYMEX futures and the DRI
4 for the 4 month period, September 1 through December 31, 2002. The NYMEX
5 was slightly lower in each of these months, therefore, the impact of this decision
6 lowered the company's expected natural gas expense during that period, thus
7 lowering the revenue requirement. The per Dth difference between the DRI prices
8 and the NYMEX/DRI average price for the months of September through
9 December was \$0.2620, \$0.3235, \$0.2335 and \$0.1775 respectively.

10 **Q. HOW DOES THIS PROJECTED LEVEL OF GAS COSTS COMPARE**
11 **WITH THE LEVEL OF GAS COSTS IT IS PROJECTING IT WILL**
12 **EXPERIENCE IN ITS FISCAL YEAR 2002 GCR?**

13 A. The level I have projected is lower than the level we anticipate that we will be
14 actually experiencing in the fiscal year 2002 GCR. In our opinion , those levels
15 are still influenced by the extraordinary price spikes in the winter 2000-2001
16 which we do not expect to experience on a going forward basis. Since the fully
17 forecasted test period should be calculated to reflect normal, ongoing operations,
18 we elected to utilize a reasonable projection of going forward gas prices for PGW.

19 **Q. DESCRIBE THE LEVEL OF HEATING DEGREE DAYS THAT WERE**
20 **USED IN YOUR ANALYSIS.**

21
22 A. The company subtracts the mean temperature from 65 degrees to arrive a the
23 number of degree days for the day. The degree days for all of the days in the year
24 are then summed up to arrive at the total number of degree days for the year.

1 Next, the company calculates the 30 year average to arrive at the anticipated
2 heating degree days.
3 For simplicity, PGW has opted to continue to use 4,555 degree days in its analysis
4 in lieu of the actual 30 year average. The actual 30 year average data indicates
5 that this number should be revised down to 4,549 degree days, reflecting the
6 recent trend of warm winters in this area. Such a reduction in degree days would
7 ultimately result in higher per unit charges to PGW's customers since there would
8 be fewer resulting units over which to spread the costs.

9 **Q. HOW HAS THE COMPANY DETERMINED THE NUMBER OF**
10 **CUSTOMERS IN EACH RATE CLASS.**

11
12 A. PGW started with the actual number of customers on August 31, 2001 from the
13 PGW Gas Sales and Revenue Report. The Marketing Department load forecast
14 was then used to determine the addition and loss of customers. In addition, the
15 number of customers was adjusted due to loss of customers shut off for non-
16 payment.

17 **Q. WHAT IS THE WEATHER NORMALIZED AVERAGE USE PER**
18 **CUSTOMER USED IN YOUR ANALYSIS?**

19
20 A. PGW used a two step process to arrive at the appropriate level of usage per
21 customer. First, the company identified the actual average usage per customer,
22 per rate class for the period July, August and September, 2001. This represents
23 the level of base load usage. Base load usage represents the level of usage that
24 occurs absent the effects of weather.
25 The total base load usage (using the base load per customer times the number of
26 customers) is then subtracted from the actual sales during the other heating

1 months of calendar year 2001 to determine the temperature sensitive or heating
2 load for these months. The heating load for each heating month is then divided by
3 the number of cycle degree days (the average degree days billed in a month) in
4 that month to determine the heating (or temperature sensitive) usage per degree
5 day.

6 The heating usage per degree day is then multiplied by the normal cycle degree
7 days (which total 4555 for the year) in that month to determine the normalized
8 heating (or temperature sensitive) load. Added to that is the total base load usage
9 for that month and the result is the normalized load for that month. This was done
10 for each rate class. The total for all the rate classes for each month of the year
11 results in PGW's normalized load for the year.

12 PGW then divided the total normalized yearly load by the average number of
13 customers to arrive at the weather normalized average use per customer.

14 **Q. IS THIS THE CALCULATION METHODOLOGY PGW UTILIZED IN**
15 **ITS LAST BASE RATE PROCEEDING?**

16
17 A. No. In our last rate case, the Office of Trial Staff (OTS) recommended that we
18 *utilize the method I just described to arrive at average usage per customer. In its*
19 *final Order, the Commission adopted the OTS's recommendation. Accordingly,*
20 *we determined to apply the OTS method to calculate the average usage per*
21 *customer for the fully forecasted test year.*

22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**
23

24 A. Yes.

**DOCUMENT
FOLDER**

PGW E.R.P. St 1

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

TESTIMONY OF

THOMAS E. KNUDSEN

DOCKETED
APR 30 2002

**ON BEHALF OF
PHILADELPHIA GAS WORKS**

**PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE PETITION**

Docket No. R-000170340002

FEBRUARY 2002

1 Q. MR. KNUDSEN, PLEASE STATE YOUR NAME, YOUR TITLE AND
2 YOUR BUSINESS ADDRESS.

3
4 A. My name is Thomas E. Knudsen. I am Interim President and Chief Executive
5 Officer of the Philadelphia Gas Works, and my business address is 800 West
6 Montgomery Avenue, Philadelphia, PA 19122.

7 Q. HAVE YOU TESTIFIED PREVIOUSLY IN PGW MATTERS OR
8 BEFORE THIS COMMISSION?

9
10 A. Yes. I appeared before the Pennsylvania Public Utility Commission (PaPUC) as
11 Interim Chief Financial Officer of PGW in the recently completed base rate
12 proceeding. I have also appeared numerous times before the PaPUC in a variety
13 of matters brought before it by all of the major electric and gas utilities in the state
14 when I was a witness on behalf of the Office of Consumer Advocate.

15 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

16 A. The purpose of this testimony, along with additional PGW witnesses, Joseph
17 Bogdonavage (Senior Vice President, Finance, PGW), Gary Krellenstein (J.P.
18 Morgan), Barbara Bisgaier (Public Financial Management) and Janice Davis
19 (Finance Director, City of Philadelphia), is to present the evidentiary basis and
20 support for PGW's Petition for Extraordinary Rate Relief that accompanies our
21 filing for base rate relief and to emphasize, in the strongest terms possible, what
22 the consequences will be for PGW if the company is not able to secure the
23 necessary permanent rate relief on an emergency basis. In short, PGW needs the
24 PUC to implement an immediate base rate increase of sufficient size to avoid a
25 downgrading of the company's long term bonds by Standard and Poor's (S&P).
26 We calculate that an increase of \$ 44 million is necessary in order to do that. If

1 we are unsuccessful in securing the necessary emergency relief and the company's
2 bonds are downgraded, PGW would immediately find itself in a financial crisis
3 that would imperil the company as a going concern and impose enormous
4 additional costs on its customers if PGW survives such setbacks. I cannot
5 emphasize enough the seriousness of the situation in which the company finds
6 itself.

7 **Q. WHAT CIRCUMSTANCES GAVE RISE TO THIS REQUEST?**

8 The company gave notice to the PaPUC in December 2001 that it would file for
9 permanent base rate relief of approximately \$50 million in January 2002. (We
10 have since determined to request an increase of \$60 million.) The expectation
11 was that this case would follow the normal processes, culminating in rate relief in
12 November 2002. Circumstances at the company precluded our filing last month.
13 However, on February 12, 2001, S&P, one of three rating agencies that evaluates
14 our debt instruments, took a step which has materially changed the course of
15 future events for the company. Specifically, S&P released, in the form of a press
16 notice (attached as Exh. BCB-1 to Ms. Bisgaier's testimony), that they refer to as
17 an update to their prior evaluation, a Credit Watch (With Negative Implications),
18 that had initially been issued in July 2000. It is my understanding that a Credit
19 Watch is normally issued for only a few months in anticipation of an enterprise
20 taking immediate corrective action. S&P has been willing to maintain our rating
21 status for more than a year and a half as we worked through the changes at PGW
22 to make it a functionally and financially stable enterprise – and, for now,
23 continues to do so. The primary reason that S&P waited nineteen months to take

1 action is that it wanted to evaluate the Company after all permanent rate action
2 had been taken.

3 There is specific language in the press release/update that gives rise to the
4 need for this extraordinary rate action. That language is the following: "Without
5 immediate cash flow improvement, ratings will be lowered." In its press release,
6 S&P lists the factors that went into the determination that PGW's credit rating
7 should be challenged at this time. These factors include poor liquidity and
8 reliance on restricted funds, weak fixed charge coverage, potential inability to
9 meet legal debt requirements, limited ability of the City of Philadelphia to assist
10 the company, PGW's continuing problems with reducing levels of accounts
11 receivable and a warmer than normal winter which will strain whatever
12 mechanisms we have left to make coverage ratios this year and next. While the
13 \$33.6 million of rate relief proved salutary and addressed, in the main, PGW's
14 needs regarding ongoing operating requirements, S&P recognized that the level
15 was insufficient to address PGW's total lack of liquidity.

16 It is my understanding that S&P looked at the levels of funds and the fund
17 flows available to PGW over the next 18 months and determined that there is an
18 insufficient basis for assuming that the company can meet all of its operating and
19 financially/legally mandated obligations and maintain the level of liquidity (cash)
20 on hand, which is required for an investment grade company. S&P includes
21 within its evaluation both the regular debt service requirements associated with
22 over \$1 billion of debt, payments on its capital leases, and interest on commercial
23 paper, as well as PGW's legal obligations to the City, including repayment of the

1 S45 million working capital loan. Ms. Bisgaier's testimony describes the
2 coverage formula and criteria that we understand S&P utilized to evaluate PGW.
3 Mr. Bogdonavage's testimony calculates where PGW stands using that formula
4 and what level of permanent rate relief is needed to satisfy S&P's investment
5 grade requirements. In short, having waited 19 months for the financial
6 fundamentals of the company to improve, S&P will not wait any longer. If it will
7 not wait, neither can we. It is my understanding that S&P will evaluate our
8 circumstances in the next 6 weeks and will determine whether the company has
9 received sufficient permanent revenues to improve its calculated coverages per
10 S&P's formula. If not, PGW bonds will be downgraded. Because at least one
11 series of PGW's long term bonds are already at the lowest "investment" grade, a
12 downgrade will necessarily put PGW below investment grade -- with disastrous
13 results. To avoid these results, we had no choice but to file this request for an
14 extraordinary rate increase.

15 One can argue that the evaluations, considerations, formulas and
16 judgments that go into S&P's determination should be more flexible or this fact or
17 that development should have been given more weight. I want to assure the
18 Commission and the parties that management has done everything it could over
19 the last 19 months to sustain the rating at the current level. The fact is that a
20 major review of our credit quality was undertaken, and PGW is found wanting.
21 Now it is time to take the corrective action necessary to avoid a disaster.

22 **Q. ARE THERE ANY IMMEDIATE CONSEQUENCES TO THE ACTION**
23 **THAT S&P TOOK THIS WEEK?**
24

1 A. Just the mere act of issuing the press release has jeopardized PGW in the short
2 term. Even before the S&P announcement, PGW had been planning to use a
3 certain financial instrument to secure a one-time source of cash. This winter will
4 likely be the warmest winter to date on record. Even if the remainder of the
5 winter is normal, PGW has lost upward of \$24 million of margin, (i.e., revenues
6 in excess of gas costs). PGW needed to find a way to replace that lost income in
7 order to satisfy its bond covenants and obtain sufficient cash working capital.

8 As a result of S&P's announcement, the one action that we could take
9 without complication to fill this gaping earnings hole will now have to be held in
10 abeyance until the extraordinary rate setting process is finished. Specifically,
11 management has been pursuing the opportunity to complete a forward purchase
12 agreement with an underwriting firm. It was anticipated that PGW could realize
13 \$20 million in project revenues from the sale of 7 years of future earnings,
14 discounted to present value, on a portion of the sinking funds on the outstanding
15 \$933 million of long term debt. However, due to the S&P announcement, and
16 because we cannot give assurance to the underwriter: that we (a) will not need
17 the funds for payment of debt service and (b) we will not be downgraded below
18 investment grade, we will not be able to act. Without action by the Commission
19 that would remove the impediments to this transaction, we cannot make our bond
20 debt service requirements for this fiscal period (FY 2002). Even assuming we
21 could have the full \$18 million of the City payment granted back to us, that
22 amount would still be inadequate, as Mr. Bogdonavage shows in his testimony
23 and schedules.

1 Q. WHAT ARE THE FINANCIAL CONSEQUENCES TO THE COMPANY
2 IF S&P WERE TO ACTUALLY DOWNGRADE PGW'S LONG TERM
3 SECURITIES?
4

5 A. There are three major financial consequences, and these are immediate and
6 severe. First, as I have explained above, the forward purchase agreement
7 transaction will not be able to go forward, which immediately puts our ability to
8 make debt service payments in July and August at risk. Such an outcome also
9 places at risk PGW's ability to satisfy the overall year-end debt service coverage
10 requirements imposed by our bond ordinance covenants.

11 Q. WHAT IS THE SECOND FINANCIAL CONSEQUENCE?

12 A. The second major consequence of a downgrade to non-investment grade is the
13 elimination of our commercial paper program. As Ms. Bisgaier and I have
14 testified previously, the commercial paper program is the only source of short
15 term debt available to the company, even if, in the last 2-3 years, it has been fully
16 extended by year end. The paper is backed by a Letter of Credit, which is
17 supplied by a consortium of banks, with Morgan being in the lead.

18 Ms. Bisgaier and Mr. Krellenstein testify that if PGW is downgraded, the
19 banking consortium will come undone and the whole effort since July 2000 to re-
20 build the financial stability of the company will have been for naught. We must
21 renew our Letter of Credit by August 29, 2002. For over 8 years, the company
22 has had \$100 million of short-term funds available to use as a revolving credit
23 instrument; that is, to finance seasonal needs for fuel purchases or to finance
24 seasonal increases in accounts receivable. Mr. Krellenstein, testifying from the
25 perspective of one of the major banks, as a representative of the financial

1 markets and security purchasers, and as one who is intimately familiar with
2 PGW's financial situation, has concluded that a downgrade would result in most if
3 not all of the existing banks declining to renew their portion of the letter of credit
4 (Morgan may stay with us because PGW is a longstanding customer). It must be
5 noted that last year it was extremely difficult to enlist the banks in support of a
6 Letter of Credit for \$100 million. The commitment contained an instruction to
7 pay the balance down to \$80 million by August 2002. The mere fact of the S&P
8 challenge will drive potential players away. It must also be noted that there are
9 fewer and fewer banks actively participating in these types of instruments.

10 A downgrade would allow the banks that provide the underlying Letter of
11 Credit to cancel the program in six month's time. However, since six months and
12 August 29 are essentially coterminus, all or virtually all of the supporting banks
13 would simply exercise their option not to renew the program in August 2001 for
14 any amount. I understand that amounts outstanding at that point would be
15 restructured with the advances being turned into taxable instruments when the
16 commercial paper matures. While it may be that one bank might stay with us to
17 some degree, it appears clear that the level of available credit would be drastically
18 reduced by \$70-75 million, at the very least. This means that PGW will be
19 robbed of the intra-year liquidity that the commercial paper program provides,
20 and at the same time would be responsible for paying back the outstanding
21 borrowings. This will create enormous additional annual payment requirements,
22 which alone would force PGW to spend the next few years doing nothing but
23 paying back the banks.

1 Q. **WHAT IS THE THIRD FINANCIAL CONSEQUENCE?**

2 A. Third, and perhaps most important, the downgrade would eliminate PGW's ability
3 to access the long term debt market. Most immediately, there could be no sale of
4 a long-term bond this December. A bond sale is essential in order to fund the
5 construction program and keep the system safe and reliable. As is shown on
6 Exhibit TEK-1, for the last several years, PGW's construction program is 100%
7 externally financed. Moreover, PGW has used the proceeds of each bond to
8 supply crucial working capital by drawing from the Construction Fund in advance
9 of actually expending the funds for construction (by fiscal year end, all capital
10 fund draws must either be expended on construction projects or returned to the
11 fund). Without a bond, this supportive source of intra-year cash working capital
12 will be eliminated.

13 Q. **WHY WILL A BOND SALE BE IMPOSSIBLE?**

14 A. Both Mr. Krellenstein and Ms. Bisgaier testify that, especially in the present
15 environment, the ability of a non-investment grade municipal utility to access the
16 capital markets to meet its construction needs would be simply nonexistent. In
17 addition, by the time we would move to sell the bond in the late fall, the lack of
18 confidence in the company, expressed first by the rating agencies and forward
19 purchase agreement underwriters and then by the banks, will have destroyed any
20 remaining interest by investors.

21 Q. **MR. KNUDSEN, ARE YOU AWARE OF THE STANDARD FOR
22 OBTAINING EXTRAORDINARY RATE RELIEF AS SET OUT IN THE
23 PUBLIC UTILITY CODE?**

24 A. Yes, I have reviewed it.
25

1
2 **Q. WILL A DOWNGRADE BY S&P CAUSE THE TYPES OF**
3 **OPERATIONAL EVENTS SET FORTH IN THE STATUTE TO OCCUR?**
4

5 A. It should be obvious that the answer is clearly yes. The cancellation of the
6 forward purchase and all or substantially all of the Letter of Credit and the
7 creation of payback requirements for the cancelled portion of the short-term debt
8 amounts that remain outstanding in August 2002, by themselves would put the
9 company in the position of not having the cash it needs to pay its debt service, gas
10 bills and other obligations when they come due. In addition, the lack of the
11 ability to issue a long-term bond at the end of 2002 means that, once the existing
12 construction funds are depleted, all construction would have to terminate. In
13 addressing the first criterion for extraordinary rate relief, a downgrading will
14 result in the financial stability of PGW being totally compromised.

15 Mr. Bogdonavage's testimony presents an analysis which shows PGW's
16 month-by-month cash flows assuming the loss of the forward purchase
17 agreement, the commercial paper line of credit and the inability to issue another
18 bond. Assuming that the company did not proactively respond to the crisis
19 (which it would) PGW would stop being able to pay its bills, fund payroll or do
20 any construction whatsoever by August of 2002.

21 **Q. DOES THAT ANALYSIS ACCURATELY DEPICT HOW PGW WOULD**
22 **RESPOND TO THE DOWNGRADE AND ITS ANTICIPATED**
23 **CONSEQUENCES?**
24

25 A. No. As CEO, it is my responsibility to prepare contingency plans for PGW.
26 Actions must start immediately and continue after a possible downgrading in
27 order to maintain the company's ability to operate at minimally acceptable levels

of safety and adequacy for as long as possible. Indeed, because the potential downgrade would put PGW in such difficult financial circumstances, we have already taken the following steps. First, under a plan that anticipated rate relief in the fall, the company is planning to petition the City Council to defer payment of the \$45 million short-term loan. The Administration has prepared the ordinance change and will be submitting that request shortly (this is a step we had set in motion even before the S&P notice). Second, we have been actively discussing when and/or under what circumstances we might deplete gas inventories which are presently unit priced above current market rates.

Third, I have instructed Mr. White, our Acting Chief Operating Officer, and Ms. Walsh, our Acting Vice President for Operations, to undertake an immediate review of our construction program in order to be in a position immediately to conserve the remaining balances in the Construction Fund for only the most essential needs going forward. To that end, we have contracted with Navigant Consultants, the group who developed our main replacement models, to study our options so that we can obtain the most safety improvements on the system for the lowest expenditure of dollars. This also means that we must coordinate with the Water and Highway Departments to minimize our enforced replacement investment. If a downgrade were to occur, we would immediately stop all construction that hasn't already been funded and which does not respond to an immediate safety concern. This means that PGW's present efforts to replace 18 miles of cast iron distribution mains each year -- which is part of its normal maintenance program, would have to be suspended immediately. It is

1 very clear that the maintenance of PGW's distribution system will suffer
2 materially from a downgrade of its securities.

3 Fourth, I have instructed all of the Vice Presidents to immediately place a
4 hold on any unnecessary spending. I have also instructed all of the Vice
5 Presidents to determine how the operating budget can be reduced by shrinking the
6 operations of the utility. They are to determine what functions are not absolutely
7 essential and can be eliminated and what services can be reduced or done without.
8 If a downgrade occurs, we would move to minimize the impact on the levels and
9 types of services to which our customers have only recently grown accustomed.
10 Essentially we would have to cut back substantially or eliminate servicing
11 appliances and redeploying field service personnel to essential maintenance
12 services only. Our efforts to improve call center access and operations through
13 further system modifications would have to be terminated. Our ability to respond
14 to and address consumer complaints would be drastically reduced. Changes in
15 operations and procedures to implement the suggestions of the management audit
16 would be suspended. All work on the deregulation initiative and the July 1, 2002
17 filing would have to be stopped. Marginal services such as those supplied by the
18 district offices would also have to be suspended and so forth. In short, we would
19 focus only on assuring that gas flows through the mains and services and that we
20 bill and collect – that is all! Customer service that is not directly related to gas
21 delivery, billing and collection will suffer.

22 Fifth, in the context of the abrupt and profound downsizing that is implicit
23 in the actions above, we would be forced to cut staff and all non-essential

1 expenditures on personnel (overtime, temporary employees, etc.) – union and
2 non-union. Senior management will be asked to prioritize the positions that are
3 essential to a revised mission of survival and target all other people for separation.
4 Although the union contract contains a no-layoff clause, there is also a provision
5 in the Collective Bargaining Agreement that the PUC can modify any of the terms
6 of the Agreement as they determine appropriate. If the downgrade occurs, we
7 will present the PUC with a proposed downsizing plan and request that it take the
8 appropriate measures to effect the lay-offs, across the board, to meet the financial
9 requirements. Similarly, we will cut all nonpayroll discretionary spending, as
10 well. Obviously, the effect of these lay offs will be to further reduce the quality
11 of customer service. Tragically, the progress we have made on a variety of fronts,
12 including improving call center access, field service delivery, plant safety and
13 upgrades would be severely compromised.

14 Last, if a downgrade occurs, I will seek the advice of the PUC, the Bureau
15 of Consumer Services and the parties to suspend pertinent sections of Chapter 56,
16 which will allow us to approach our delinquent customers for payment more
17 aggressively. Management is very sensitive to the social contract which PGW has
18 as a provider of a municipal service. But in this financial emergency, PGW
19 would be required to preserve the assets to serve the greatest good. At a very
20 minimum, if we have reason to believe that a party has not paid for gas in the
21 past, we should not be required to reinstate that customer or someone in that
22 household going forward. PGW is providing tens of millions of dollars of gas to

1 people who will not or cannot pay for a host of reasons. For the system to survive,
2 even in skeletal form, customers must be required to pay for the gas they receive.

3 **Q. WHAT DO YOU SEE AS THE RESULT OF A DOWNGRADING AND**
4 **ALL OF THE ACTIONS THAT YOU DESCRIBE ABOVE?**

5
6 A. There will be immediate reduction in customer service, normal maintenance
7 levels and layoffs, resulting in irreparable harm to PGW, the City, investors,
8 employees and, most directly and importantly, PGW's customers.

9 **Q. ARE THERE OTHER COLLATERAL EFFECTS ON THE CITY IF PGW**
10 **LOSES ACCESS TO THE FINANCIAL MARKETS?**

11
12 A. Yes. There will be pressure on the City – Administration and City Council - to
13 support PGW operations following a downgrade. First, it is my understanding
14 that a one-time, or non-permanent cash allowance will not be sufficient to stop
15 S&P from downgrading. The rating agency is looking for evidence that, on an
16 ongoing basis, PGW has revenues and liquidity consistent with an investment
17 grade enterprise. Any one time assistance from the City to temporarily improve
18 PGW's S&P calculated coverages would not result in avoiding the downgrade.
19 Moreover, under the present fiscal circumstances, any redirection of funding to
20 PGW from the City will have an immediate adverse impact. We know from Ms.
21 Davis' testimony that the City is facing a substantial deficit over the next five
22 years. Were some portion of the General Fund to be needed for PGW, the City
23 department heads would have to make up an imposed level of austerity by cutting
24 services, cutting people, cutting discretionary spending or all of the above. The
25 citizens of Philadelphia will lose twice: first as customers of PGW and then as
26 taxpayers.

1 Q. MR. KNUDSEN, HOW DOES PGW PROPOSE THAT THE PUC
2 INTERPRET THE "RETURN ON EQUITY" STANDARD SET FORTH IN
3 SECTION 1308(E)?
4

5 A. It should be obvious that the financial standard that must be focused on here is the
6 maintenance of an investment grade rating for PGW's bonds and commercial
7 paper. The PUC's prior order clearly assumed that its decision would allow PGW
8 to maintain its existing external financing and continue to raise new capital. That
9 is only possible, for PGW, in today's environment, by the maintenance of an
10 investment grade rating. Now, on a going forward basis, and considering the
11 effect on the company of a much warmer than normal winter, and other factors, it
12 is necessary for the PUC to act by providing more rate relief if this goal is to be
13 achieved and disaster is to be avoided.

14 Q. WHY IS THERE AN IMMEDIATE NEED FOR THE PUC TO ACT?

15 A. Essentially, this is the deadline that S&P has imposed. It is looking to see
16 immediate, permanent improvement in PGW's liquidity or it will downgrade now.
17 Thus, the PUC must act now.

18 Q. IF S&P DOWNGRADED AND THEN THE PUC PROVIDED
19 SUFFICIENT ADDITIONAL REVENUES IN NOVEMBER, IN THE
20 CONTEXT OF PGW'S BASE RATE REQUEST, WOULDN'T THAT BE
21 SUFFICIENT.
22

23 A. Very definitely not. A downgrade now would cause irreversible harm to the
24 company and customers as detailed above. Moreover, as Mr. Krellenstein
25 testifies, even if the PUC were to act to increase PGW's rates sufficiently to put its
26 S&P calculated coverages at investment grade, there is no assurance that S&P
27 would act quickly to reverse its decision. It could take years. Moreover, in the
28 meantime, PGW would have lost all or most of its commercial paper program and

1 would be forced to pay premium for any long term debt it was able to issue after it
2 returned to investment grade. Waiting and hoping for the best is very definitely
3 not a viable option.

4

5 **Q. DOES THAT COMPLETE YOUR TESTIMONY?**

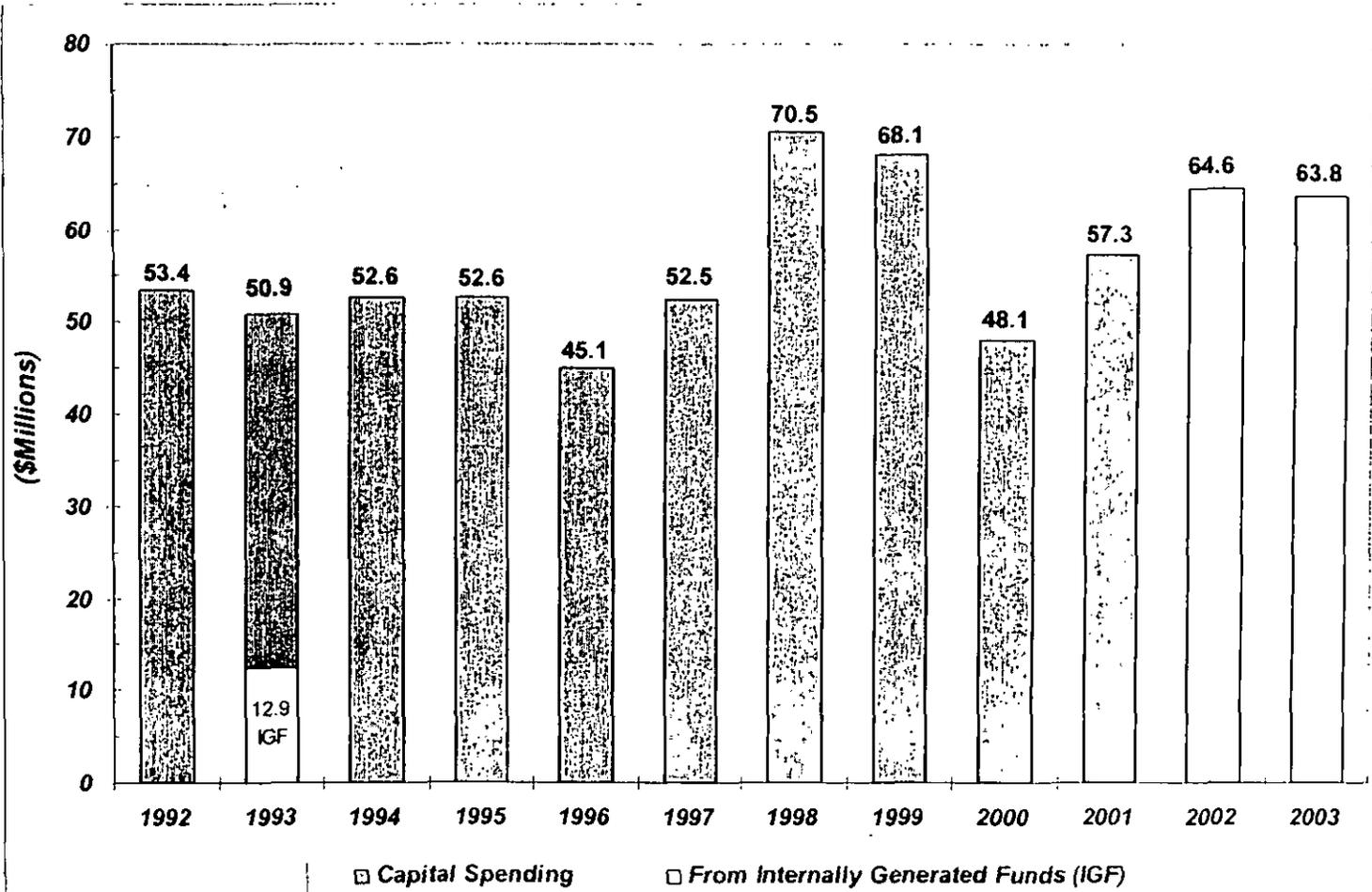
6 **A.** Yes it does.

Exhibit TEK-1

Docket No. R-000170340002

Philadelphia Gas Works

FY1992 - 2003 Capital Spending, & Internally Generated Funds



DOCUMENT
FOLDER

PGW E.R.P. St. 2

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

TESTIMONY OF

JOSEPH R. BOGDONAVAGE APR 30 2002

BOCKETED

**ON BEHALF OF
PHILADELPHIA GAS WORKS**

**PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE PETITION**

R-000170340002

FEBRUARY 2002

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. My name is Joseph R. Bogdonavage. My business address is 800 West Montgomery
3 Avenue, Philadelphia, PA 19122.

4 Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

5 A. I am employed by the Philadelphia Gas Works in the capacity of Senior Vice President
6 Finance.

7 Q. WHAT ARE YOUR PRINCIPAL RESPONSIBILITIES AS SENIOR VICE
8 PRESIDENT?

9 A. My principal responsibilities include the oversight of PGW's Accounting & Budget,
10 Treasury, Risk management and Procurement & Contract Services Departments. I am
11 currently responsible for the overall preparation of the financial areas of the operating and
12 capital budgets, review of operating budgets prepared by the individual departments, and
13 the coordination, analysis, issuance and overall control of the complete annual Operating
14 Budget filing. These activities include the preparation of varied analyses for the purpose
15 of generating alternative financial initiatives; i.e., proposed revenue bond and capital
16 lease offerings and base rate case presentations. Finally, in coordination with my staff,
17 the Budget area acts as a liaison between all department budget representatives regarding
18 budgeting and financial forecasting procedures and variance analysis reporting.

19 Q. HAVE YOU PREVIOUSLY PRESENTED TESTIMONY BEFORE THE
20 PENNSYLVANIA PUBLIC UTILITY COMMISSION ("PUC")?

21 A. Yes, I testified in PGW's last base rate proceeding (R-00006042).

22 Q. PLEASE EXPLAIN THE REASON FOR YOUR TESTIMONY.

23 A. The purpose of my testimony is twofold: (1) I will demonstrate the financial
24 consequences to PGW if it were in fact to be downgraded by S&P and it were to lose all
25 or most of its commercial paper program and be unable to sell long term debt to finance

1 its construction program. (2) I will show PGW's calculation of the level of rate relief
2 needed to produce the required fixed cost coverage ratios so that PGW will be able to
3 maintain an investment grade bond rating.

4 **Q. PLEASE EXPLAIN YOUR ANALYSES OF THE EFFECT ON THE COMPANY**
5 **IF IT WERE TO BE DOWNGRADED TO BELOW INVESTMENT GRADE.**

6
7 A. This analysis is shown on JRB-Exh. 1, page 1. It shows that if PGW took no proactive
8 steps the company would effectively stop functioning in August 2002 when it could not
9 make a debt service payment. Assuming the Company availed itself of the Debt Service
10 Reserve Fund to make that payment, it would still be \$7 million short of cash for other
11 operations. Being short of cash means that PGW doesn't have the funds to pay bills
12 when due. Looking at JRB-Exh. 1, page 2, the projections for FY 2003, PGW projects
13 negative cash positions from November to March. Even assuming the commercial paper
14 payment of \$77 million were pushed back to August of 2003, there is no way to repay the
15 commercial paper note or repay the \$45.0 million City loan.

16 **Q. PLEASE DESCRIBE YOUR ANALYSIS OF THE RATE INCREASE NEEDED**
17 **TO SATISFY STANDARD & POOR'S COVERAGE CRITERIA.**

18
19 A. I present the results of my analysis of the level of rate increase PGW needs on a
20 permanent and immediate basis if the Company is going to avoid a downgrade to "junk"
21 status by the rating agencies on JRB-Exh.2. This calculation utilizes the "coverage"
22 calculation and requirements that Ms. Bisgaier testifies S&P utilizes in evaluating the
23 financial position of a municipal utility. The analysis shows that a rate increase of \$44
24 million is needed if PGW's permanent revenues are to satisfy investment grade status,
25 thus maintaining our bond rating at its present levels.

26 **Q. WHAT PERIODS DID YOU ANALYZE TO CALCULATE THESE RESULTS?**

1 A. I applied the Standard & Poor's formula to actual projected 2002 and to our fully
2 forecasted, normalized FY 2002 Test Year because that is my best estimate of PGW's
3 earnings and cash flow on a normal, going forward basis; i.e. FY 2003. Utilizing this
4 data, I have calculated that a rate increase of \$44 million will be needed to produce the
5 necessary fixed charge coverage. It should be noted that the fully forecasted 2002 results
6 produce coverages of 1.27 times without considering the repayment of the \$45.0 million
7 City loan. Coverages drop to just under one when repayment of the \$45.0 million City
8 loan is factored in. This is consistent with our understanding of the S&P's criteria which
9 recognizes that the ratios may fall below the required levels when the repayment of a
10 large obligation comes due.

11 **Q. HOW DID YOU TREAT THE \$18.0 MILLION CITY PAYMENT FOR THE**
12 **PURPOSES OF THE STANDARD & POOR'S CALCULATION?**

13 A. As an annual obligation. As I understand S&P's approach, it must be shown that the
14 Company's financials satisfy an investment grade level on a permanent, ongoing basis.
15 S&P includes all ongoing legal obligations such as the City Payment in its "uses" of
16 funds whether the payment is granted back on a temporary or one time basis or not.
17 Accordingly, whether the City Payment is granted back from one year to the next to
18 respond to some special emergency in that year, PGW must have the capacity to make
19 this payment in its rates plus 30% liquidity over and above that amount if it is to maintain
20 its investment grade.

21 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

22 A. Yes.

Exhibit JRB-1

Docket No. R-000170340002

Estimated weather 3800 degree days
 City Loan \$45.0 MM Fully Outstanding @ 8/31/02
 \$33.6M Rate Increase - Current
 TXCP \$100.0 M with \$77.0 M Outstanding @ 8/31/02
 Reduced expenses per union contract settlement
 Pre-Draw Capital Funding during the Fiscal Period

ACTUAL WEATHER THRU 2/15/02 NO FINANCIAL TRANSACTIONS

ESTIMATE OF CASH RECEIPTS AND DISBURSEMENTS
 FISCAL YEAR ENDING AUGUST 31, 2002
 (Millions of Dollars)

	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	TOTAL
2/19/02	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	
OPENING BALANCE - CASH INCLUDES 97.0 TXCP RECEIPTS	\$1.7	\$0.7	\$3.7	\$4.2	\$3.8	\$1.0	\$35.2	\$46.4	\$58.8	\$65.7	\$44.1	(\$2.5)	\$1.7
Gas	32.2	40.9	42.9	41.5	63.1	65.0	63.0	63.0	59.0	45.8	39.0	37.0	592.4
Other	0.7	0.6	0.3	1.6	0.6	1.6	1.5	1.5	1.5	1.5	1.5	2.9	15.8
Drawn from Capital Funds - Principal (\$80.9MM)	12.9	20.0	0.0	20.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	52.9
Drawn from Capital Funds - Interest	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.7	1.9
Drawn from Lease Funds - Principal (\$3.8MM)	0.0	0.0	0.0	0.0	0.0	2.0	0.0	0.0	0.0	0.0	1.8	0.0	3.8
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.2
Advance (Repayment) of Capital Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension Draw	0.0	0.0	0.0	9.2	6.5	0.0	0.0	2.3	2.3	2.3	2.4	2.4	27.4
City Loan	11.9	32.2	22.5	47.4	22.5	15.5	0.0	0.0	0.0	0.0	0.0	0.0	152.0
Rate Relief	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL RECEIPTS	57.7	93.7	65.9	119.7	92.7	84.1	64.5	66.8	62.8	49.6	44.7	44.2	846.4
TOTAL	59.4	94.4	66.6	123.9	96.5	85.2	99.7	113.3	121.6	115.3	88.8	41.7	848.1
DISBURSEMENTS													
Labor	10.3	11.1	11.9	10.9	10.6	10.5	11.1	11.3	11.5	10.4	11.4	10.9	131.9
Natural Gas	26.3	27.8	28.9	33.3	36.0	36.1	32.5	31.5	28.0	29.0	23.2	24.0	355.6
Debt Service	0.0	4.0	0.0	0.0	25.5	6.1	0.0	2.0	1.7	0.0	42.1	13.0	94.4
TXCP: Interest	3.5	0.1	0.2	0.1	0.0	0.2	0.3	0.3	0.3	0.3	0.3	0.2	2.5
Repayment of City Loan	14.5	36.7	17.2	68.1	15.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	152.0
Cost Savings/Reductions	0.0	0.0	0.0	0.0	0.0	(0.8)	(0.9)	(0.9)	(0.9)	(1.0)	(1.0)	(1.0)	(6.5)
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	18.2	0.0	0.0	18.2
Other Disbursements	7.5	7.9	10.6	10.2	10.9	10.8	10.3	10.3	10.3	10.3	10.3	10.3	119.7
TOTAL DISBURSEMENTS	58.7	87.7	68.8	122.6	98.5	83.0	53.3	54.5	50.9	66.2	86.2	57.5	867.8
MONTHLY CASH FLOW	(1.0)	6.0	(2.9)	(2.9)	(5.8)	21.1	11.2	12.4	11.9	(16.6)	(41.6)	(13.3)	(21.5)
CUMULATIVE CASH FLOW	(1.0)	5.0	2.0	(0.9)	(6.7)	14.5	25.7	38.1	50.0	33.4	(8.2)	(21.5)	
OPENING TXCP	78.0	78.0	75.0	78.5	81.0	84.0	97.0	97.0	97.0	92.0	87.0	82.0	78.0
TXCP ISSUED DURING MONTH	0.0	0.0	3.5	2.5	3.0	13.0	0.0	0.0	0.0	0.0	0.0	0.0	22.0
TXCP ISSUED PAID DOWN DURING MONTH	0.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0	5.0	5.0	5.0	5.0	23.0
ENDING TXCP	78.0	75.0	78.5	81.0	84.0	97.0	97.0	97.0	92.0	87.0	82.0	77.0	77.0
OPENING BALANCE - CASH	1.7	0.7	3.7	4.2	3.8	1.0	35.2	46.4	58.8	65.7	44.1	(2.5)	1.7
MONTHLY CASH FLOW	(1.0)	6.0	(2.9)	(2.9)	(5.8)	21.1	11.2	12.4	11.9	(16.6)	(41.6)	(13.3)	(21.5)
NET TXCP ACTIVITY MONTHLY	0.0	(3.0)	3.5	2.5	3.0	13.0	0.0	0.0	(5.0)	(5.0)	(5.0)	(5.0)	(1.0)
ENDING BALANCE - CASH	0.7	3.7	4.2	3.8	1.0	35.2	46.4	58.8	65.7	44.1	(2.5)	(20.8)	(20.8)
CITY LOAN AVAILABLE - END OF MONTH	0.0	2.6	7.1	1.8	22.5	15.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CITY LOAN UTILIZED - END OF MONTH	45.0	42.4	37.9	43.2	22.5	29.5	45.0	45.0	45.0	45.0	45.0	45.0	45.0
CASH POSITION NET OF TXCP AND CITY LOAN	(119.7)	(109.2)	(117.5)	(99.7)	(112.5)	(106.8)	(95.6)	(83.2)	(71.3)	(87.9)	(129.5)	(142.8)	

Normal weather 4555 degree days
 \$33.6M Rate Incr. - Current
 City Loan Repayment Due 8/31/03
 TXCP @ \$77.0 Million
 No Bond Sale
 PreDraw Capital Funding during Fiscal Period

BUDGET OF CASH RECEIPTS AND DISBURSEMENTS
 FISCAL YEAR ENDING AUGUST 31, 2003
 (Millions of Dollars)

	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	TOTAL
2/19/2002	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	
OPENING BALANCE - CASH INCLUDES 77.0 TXCP RECEIPTS	(\$20.8)	\$3.3	(\$0.3)	(\$12.1)	(\$9.0)	(\$32.1)	(\$23.8)	\$9.9	\$38.5	\$51.9	\$38.2	(\$4.3)	(\$20.8)
Gas	33.7	36.0	37.4	48.9	60.2	71.0	79.7	73.4	60.2	44.4	35.4	35.3	615.6
Other	1.5	1.4	1.6	1.7	1.8	1.6	1.8	2.0	2.1	2.0	1.9	9.2	28.6
Drawn from Capital Funds - Principal (\$27.1MM)	27.1	6.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	33.3
Drawn from Capital Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.7	1.7
Drawn from Lease Funds - Principal (\$1.9MM)	0.0	0.0	0.0	0.0	0.0	1.9	0.0	0.0	0.0	0.0	0.0	0.0	1.9
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.2
Advance (Repayment) of Capital Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension Draw	2.4	2.4	2.4	7.2	0.0	0.0	2.4	2.4	2.3	2.3	2.3	2.3	28.4
City Loan													0.0
Rate Relief	1.6	1.7	1.9	2.6	3.2	3.7	4.2	3.8	3.1	2.3	1.8	1.6	31.6
TOTAL RECEIPTS	66.4	47.7	43.4	60.4	65.2	78.2	88.1	81.6	67.7	51.0	41.4	50.4	741.2
TOTAL	45.6	51.0	43.1	48.3	56.2	46.1	64.2	91.5	106.2	102.9	79.6	46.0	720.4
DISBURSEMENTS													
Labor	10.7	12.3	12.1	11.9	12.6	11.0	11.1	11.3	11.5	10.4	11.4	10.9	137.2
Natural Gas	24.3	29.6	34.8	36.3	41.4	43.7	33.4	30.2	28.8	27.1	22.1	22.7	374.4
Debt Service	0.0	1.9	0.0	0.0	24.7	5.3	0.0	2.0	4.7	0.0	41.5	9.6	89.7
TXCP - Interest	3.5	0.2	0.2	0.3	0.3	0.2	0.3	0.3	0.3	0.3	0.2	0.2	3.3
Repayment of City Loan												45.0	45.0
Union/Management Reductions	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.1)	(1.1)	(1.1)	(1.1)	(12.4)
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	18.2	0.0	0.0	18.2
Other Disbursements	6.0	6.2	9.1	9.8	10.2	10.7	10.5	10.2	10.0	9.8	9.8	9.7	116.1
TOTAL DISBURSEMENTS	42.3	51.3	55.2	57.3	88.2	70.0	54.3	53.0	54.3	64.7	83.9	97.0	771.5
MONTHLY CASH FLOW	24.1	(3.6)	(11.9)	3.1	(23.0)	8.3	33.7	28.6	13.4	(13.7)	(42.5)	(46.7)	(30.2)
CUMULATIVE CASH FLOW	24.1	20.5	8.7	11.8	(11.3)	(3.0)	30.7	59.3	72.7	59.0	16.5	(30.2)	
OPENING TXCP	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0
TXCP ISSUED DURING MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TXCP ISSUED PAID DOWN DURING MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ENDING TXCP	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0
OPENING BALANCE - CASH	(20.8)	3.3	(0.3)	(12.1)	(9.0)	(32.1)	(23.8)	9.9	38.5	51.9	38.2	(4.3)	(20.8)
MONTHLY CASH FLOW	24.1	(3.6)	(11.9)	3.1	(23.0)	8.3	33.7	28.6	13.4	(13.7)	(42.5)	(46.7)	(30.2)
NET TXCP ACTIVITY MONTHLY	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ENDING BALANCE - CASH	3.3	(0.3)	(12.1)	(9.0)	(32.1)	(23.8)	9.9	38.5	51.9	38.2	(4.3)	(51.0)	(51.0)
CITY LOAN AVAILABLE - END OF MONTH	0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	45.0	45.0
CITY LOAN UTILIZED - END OF MONTH	45	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	0.0	0.0
CASH POSITION NET OF TXCP AND CITY LOAN	(118.7)	(122.3)	(134.1)	(131.0)	(154.1)	(145.8)	(112.1)	(83.5)	(70.1)	(83.8)	(126.3)	(128.0)	

Exhibit JRB-2

Docket No. R-000170340002

Corrected 3/15/02

PHILADELPHIA GAS WORKS
FISCAL YEAR 2001-02
PROJECTED INCOME STATEMENT

Revised 3-06-02

	<u>Current</u> <u>Estimate</u> <u>2001-02</u>	<u>Test Year</u> <u>Budget</u> <u>2001-02</u>
Operating Revenues		
Gas Revenues	\$672,188	\$638,733
Margin Loss Gas Sales	(25,000)	-
Proposed Base Rate Incr.	-	44,000
Other Revenues	27,450	28,117
Total Operating Revenues	<u>\$674,638</u>	<u>\$710,850</u>
Operating Expenses		
Natural Gas Costs	\$373,016	\$334,566
Raw Material Exp.	10	10
Total Nat. Gas & Raw Mat	<u>\$373,026</u>	<u>\$334,576</u>
Contribution Margins		
	\$301,612	\$376,274
Supply & Field Expenses	\$58,331	\$59,331
Customer Services	29,722	30,222
Bad Debt Expense	54,553	52,544
Marketing	4,000	5,596
Administrative & General	39,086	39,086
Health Insurance	31,490	30,490
Capitalized Benefits & A&G	(12,430)	(13,430)
Amortization	3,965	3,965
Pensions	3,091	3,091
Taxes	6,054	6,054
Added Costs PUC & Other	0	10,000
Labor/Cost Savings	(7,100)	(7,100)
Total Oper. & Maint.	<u>\$210,762</u>	<u>\$219,849</u>
Depreciation	\$31,585	\$31,587
Total Oper. & Maint. Exp.	<u>\$242,347</u>	<u>\$251,436</u>
Total Operating Expenses	<u>\$615,373</u>	<u>\$586,012</u>
Operating Income	\$59,265	\$124,838
Other Income	4,963	5,743
Income Before Interest	<u>\$64,228</u>	<u>\$130,581</u>
Interest		
Long-Term Debt	\$50,965	\$50,965
Other	6,148	6,498
AFUDC	(775)	(775)
Loss on Extinguished Debt	3,976	3,976
Total Interest	<u>\$60,315</u>	<u>\$60,665</u>
Net Income	\$3,913	\$69,916
City Payment	18,000	18,000
Net Loss From Operations	<u>(\$14,087)</u>	<u>\$51,916</u>

PHILADELPHIA GAS WORKS
FISCAL YEAR 2001-02
PROJECTED DEBT SERVICE COVERAGE

	<u>Current</u> <u>Estimate</u> <u>2001-02</u>	<u>Test Year</u> <u>Budget</u> <u>2001-02</u>
Debt Service Calculation		
Funds Provided		
Operating Revenues	\$674,638	\$710,850
Other Income +/-		
Restricted Funds	4,963	5,743
AFUDC	775	775
Total Funds Provided	<u>\$680,376</u>	<u>\$717,368</u>
Funds Applied		
Fuel Costs	\$373,026	\$334,576
Other Operating Exp.	242,347	251,436
Less: Non-Cash Exp.	(36,165)	(36,165)
Total Funds Applied	<u>\$579,208</u>	<u>\$549,847</u>
Funds Available To Cover Debt Service		
	\$101,168	\$167,521
1975 Debt Service Coverage Ratio		
	<u>1.82</u>	<u>3.02</u>
Funds Available To Cover Capital Leases		
	\$45,640	\$111,993
	<u>5,954</u>	<u>5,954</u>
Funds Available To Cover 1998 Sr. Debt Service Coverage Ratio		
	<u>30,926</u>	<u>30,926</u>
	1.28	3.43
Funds Available To Cover 1998 Subordinate Debt Ser. Coverage Ratio		
	\$8,760	\$75,113
	<u>1,986</u>	<u>1,986</u>
	4.41	37.82
Revised Standard & Poor's Fixed Charge Coverage Ratio		
Net Available To Service Aggregate Debt Service		
	\$102,542	\$168,897
Aggregate Debt Service		
	\$94,394	\$94,394
Fixed Rate Coverage Ratio on Aggregate Debt Service		
	1.09	1.79
Fixed Rate Coverage Ratio Including \$18.0 M City Fee		
	0.91	1.50
Fixed Rate Coverage Ratio Including \$18.0 M City Fee & \$20.0 M TXCP Payment		
	0.77	1.28

DOCUMENT
FOLDER

PGW E.R.P. St. 3

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

TESTIMONY OF

DOCKETED

APR 30 2002

GARY KRELLENSTEIN

ON BEHALF OF
PHILADELPHIA GAS WORKS

PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE PETITION

R- 000170340002

FEBRUARY 2002

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. My name is Gary Krellenstein. My business address is JP Morgan Guaranty, 60 Wall
3 Street, 33rd Floor, New York, NY 10260.

4 Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

5 A. I am a senior analyst and vice president in JPMorgan's Municipal Finance Department.
6 My areas of specialty are municipal utilities, cogeneration facilities, resource recovery
7 projects, and pollution control and industrial development bonds. I am the former
8 chairman of *The Bond Marketing Association's (TBMA)* Credit Committee and sat on the
9 Advisory Committee for *Public Utilities Fortnightly Magazine*. Since the early 1990s I
10 have been ranked as one of the top fixed-income (bond) analysts on Wall Street by
11 various financial publications such as *Institutional Investor Magazine* and the *Bond*
12 *Buyer*.

13 Q. WHAT ARE YOUR PRINCIPAL RESPONSIBILITIES AS SENIOR ANALYST
14 AND VICE PRESIDENT?

15 A. My responsibilities at JPMorgan include providing credit research and recommendations
16 to the firm's sales and trading desk, institutional investor clients and issuers. I also
17 advise JPMorgan Chase Bank regarding its municipal utility lending policies and
18 practices.
19

20 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

21 A. The purpose of this testimony is to advise the Commission about the risks that PGW
22 faces in renewing its commercial paper instrument and the consequences for both its
23 commercial paper program as well as its ability to issue long term debt should its bonds
24 be downgraded by Standard and Poors. It should also be noted that I am speaking as a

1 research analyst and not as a representative of JPMorgan Chase Bank. In that capacity, I
2 am very familiar with PGW's current financial and credit position.

3 **Q. PLEASE PROVIDE YOUR UNDERSTANDING OF S&P'S RECENT ACTION.**

4 A. On February 12, 2002, Standard & Poors issued a press release warning that "*without*
5 *immediate cash flow improvement, ratings [on PGW] will be lowered.*" The S&P release
6 also states that ratings will be affirmed only if the PUC grants emergency rate relief
7 sufficient to address concerns over the utility's weak liquidity position and overall
8 financial operations.

9 Morgan Bank has been the Agent Bank for the letter of credit (LOC) facility that
10 supports PGW's Tax Exempt Commercial Paper for several years. One of the key
11 criteria used by Morgan and other banks in determining PGW's credit quality are the
12 ratings assigned by independent credit agencies such as *Standard & Poors*, *Fitch's* and
13 *Moody's Investor's Services*. The Gas Works' bank facilities are on parity with its
14 subordinate debt and are currently rated BBB- by S&P. This is the lowest investment
15 grade rating assigned by S&P. If that rating were lowered further, they would be
16 characterized as sub-investment grade debt (i.e., "junk bonds").

17 It should be noted that it was difficult to receive internal approval to renew the
18 facility last year (June 2001) and that the other banks involved in this transaction were
19 reluctant to renew their respective portions. Consequently, the renewal came at a
20 substantial cost increase (double the cost of a similar transaction two years prior) and was
21 approved in anticipation of PGW receiving adequate rate relief sufficient to support these
22 instruments. Also, a condition for renewal of the letter of credit was a requirement for
23 PGW to reduce the outstanding balance from \$100 to \$80 million by August 2002.

1
2 **Q. WHAT WILL BE THE CONSEQUENCES OF A DOWNGRADE ON THE**
3 **ABILITY OF PGW TO SUSTAIN ITS COMMERCIAL PAPER PROGRAM?**
4

5 A. Since the renewal, there have been several developments (e.g., the economic downturn,
6 high level of losses incurred by banks on loans and credit facilities, Enron's bankruptcy,
7 etc.) that have adversely impacted the ability and willingness of banks and investors to
8 loan funds to entities such as PGW. Should the PUC fail to grant emergency rate relief
9 sufficient to prevent a downgrade by S&P, it is my professional opinion that one or more,
10 and possibly all, of the participating banks in the LOC facility will refuse to renew the
11 commitment when it comes due in August 2002. Furthermore, it will be difficult or
12 impossible to find other bank(s) to step forward as a substitute. Certainly, if PGW were
13 now, for the first time, seeking an LOC facility, I do not believe it would be available to
14 them.

15 The loss (or significant reduction in size) of the LOC facility and attendant
16 reduction in outstanding commercial paper will exacerbate the utility's cash flow and
17 credit problems and seriously impact its day-to-day operations and ability to purchase gas
18 for its customers by drawing funds from operations without maintaining the flexibility
19 provided by the commercial paper. It will also be viewed as a material adverse event by
20 investors and the rating agencies and would likely lead to additional downgrades by
21 Standard & Poors and/or the other credit agencies, effectively cutting off PGW's access
22 to the capital markets. Even if the utility were then granted an adequate rate increase, the
23 evidence shows that downgrades occur much more quickly than upgrades, and an
24 upgrade would not be guaranteed. Any upgrade, should one occur, could easily take as
25 long as 18 months to effect. During that time, PGW's access to capital markets would

1 continue to be severely constrained or non-existent. Furthermore, even after a return to
2 investment grade, the experience of other municipal utilities (MMWEC, WPPSS) is that
3 the damage done by the prior downgrades to sub-investment grade ratings would cause
4 PGW to incur dramatically higher financing costs for years to come, and those higher
5 costs would eventually have to be passed on to its customers (the utility has no equity
6 investors).

7 While no customer wants to see rates increase, it seems clear that an emergency
8 rate hike granted now would be the lowest cost option for maintaining a functional gas
9 utility that can adequately meet the needs of its customers. It is my view that without
10 further immediate attention to PGW's situation by the Commission, the utility's
11 customers will ultimately incur significantly higher costs as well as the potential for
12 inadequate gas service.

13 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

14 **A. Yes.**

DOCUMENT
FOLDER

PGW E.R.P. St. 4

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

TESTIMONY OF

BARBARA C. BISGAIER

DOCKETED
APR 30 2002

**ON BEHALF OF
PHILADELPHIA GAS WORKS**

**PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE PETITION**

R- 000170340002

FEBRUARY 2002

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. Barbara C. Bisgaier, Managing Director, Public Financial Management, Inc., 2 Logan
3 Square, Suite 1600, Philadelphia, Pennsylvania 19103-2770, (215) 567-6100. I am a
4 Financial Advisor to state and local governments and authorities.

5 Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

6 A. I am employed by Public Financial Management, Inc. I am a shareholder in the firm.

7 Q. SUMMARIZE YOUR PROFESSIONAL QUALIFICATIONS.

8 I have been employed by PFM for more than 18 years. For approximately 16 of those
9 years, I have had the title of managing director and have managed the firm's municipal
10 utility practice. During my career at Public Financial Management, Inc., I have served as
11 a Financial Advisor to a broad range of state and local governments and authorities. In
12 particular, my experience has been concentrated in the area of publicly-owned utility
13 systems. In addition to the Philadelphia Gas Works, my utility clients have included the
14 Water Department of the City of Philadelphia, the Pittsburgh Water and Sewer Authority,
15 the Harrisburg Water and Sewer Authority, the New Jersey Water Supply Authority, the
16 North Jersey District Water Commissioners, the Passaic Valley Sewerage
17 Commissioners, the Middlesex County (NJ) Utilities Authority, the Ocean County (NJ)
18 Utilities Authority, the Atlantic County (NJ) Utilities Authority, the Southeast Morris
19 County Water Authority and the Atlantic City Sewerage Authority.

20 In addition, I have served, since 1992, as the Financial Advisor to the City of
21 Philadelphia. In that capacity, I have served as the City's advisor for all debt issued by
22 the City and by its authorities and enterprises (the Water Department, the Division of
23 Aviation, the Philadelphia Municipal Authority and PGW). This has included serving as
24 the advisor for two bond issues that were each in excess of one billion dollars. I served

1 as the Financial Advisor for the largest issue of municipal bonds to come to market in
2 2000: \$1.8 billion of Turnpike Revenue Bonds for the New Jersey Turnpike Authority.
3 Over the course of my career, I have served as the advisor for the issuance of long-term
4 debt having a par value in excess of \$25 billion.

5 In the course of these various engagements, my responsibilities include general financial
6 planning and the management of the debt issuance process. With regard to the financial
7 planning aspect of my work, I assist clients with their development of capital financing
8 strategies, debt policies, budgets and rate setting issues. With regard to the debt issuance
9 process, I frequently serve as the liaison between my clients and the bond rating agencies,
10 the municipal bond insurers and other credit-providing agencies. I also advise my clients
11 throughout the debt issuance process as to the costs and benefits of various alternative
12 approaches to business and financial issues under consideration. I am also frequently
13 responsible for working with my clients to prepare disclosure documents, offering
14 circulars and presentations to the bond rating agencies and credit enhancers.

15 **Q. DESCRIBE YOUR EDUCATIONAL BACKGROUND.**

16 A. I have an A.B. degree from Mount Holyoke College and a Masters of City and Regional
17 Planning degree from Rutgers University.

18 **Q. HAVE YOU EVER TESTIFIED BEFORE ANY REGULATORY AGENCIES?**

19 A. Yes, I have testified before the Philadelphia Gas Commission and I submitted testimony
20 to the Public Utility Commission in PGW's interim rate proceeding and the Company's
21 last general rate case.

22 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

23 A. The purpose of my testimony is to provide my expert opinion regarding the effect on the
24 Company of the downgrading to non-investment grade of PGW's bonds. I am also

1 incorporating into this submission my previous testimony in PGW's interim rate
2 proceeding and general rate case in which I explained the bond coverage requirements.

3 **Q. PLEASE EXPLAIN THE PRESENT STATUS OF PGW'S BOND RATINGS**
4 **PROVIDED BY THE RELEVANT BOND RATING AGENCIES?**

5
6 A. As may be recalled, in my previous testimony I discussed the implications to PGW of the
7 downgrade of its credit rating to below investment-grade status. In this previous
8 testimony, the concerns expressed were occasioned by the fact that two of the three credit
9 rating agencies, Moody's Investors Service and Standard & Poors Rating Services had
10 placed PGW on their respective watch lists with negative implications. Unfortunately,
11 the threat of a downgrade has now become imminent with the announcement by Standard
12 & Poors on February 12, 2002 that without immediate cash flow improvement, the
13 ratings of PGW's bonds¹ would be lowered. A copy of that report is attached hereto as
14 Exhibit BCB-1. Standard & Poors has not indicated the extent to which they will lower
15 the outstanding ratings; however, it is correct to say that, at a minimum, the subordinated
16 1998 Bonds (which are currently rated BBB-, the lowest investment-grade rating) would
17 be reduced to a below investment grade rating. There is also a significant likelihood that
18 the rating of the senior 1998 Bonds would also be lowered to below investment grade.

19 **Q. PROVIDE THE BACKGROUND OF S&P'S PRESENT ACTION.**

20 A. S&P originally placed PGW on credit watch with negative implications in July 2000. A
21 copy of that report (which was originally made part of my August 2000 testimony) is
22 attached hereto as Exhibit BCB-2. Normally, S&P uses its credit watch status to notify
23 the broader credit markets that they intend to take action on a particular credit rating

¹ The bonds covered by the announcement include bonds issued pursuant to the 1975 Ordinance and both the senior and subordinated debt issued pursuant to the 1998 Ordinance.

1 within, at most, two or three months once a particular milestone or action has or has not
2 occurred. The fact that PGW has remained on credit watch with negative implications
3 for almost 20 months is highly unusual and runs counter to normal practice at S&P. S&P
4 has sustained PGW's credit watch status because they have been willing to defer a final
5 determination while the various rate proceedings undertaken by PGW were in process.
6 The decision by the PUC in December to decline to revise upward PGW's authorized
7 rate increase from \$33.6 million, taken together with the increased pressure on PGW's
8 liquidity as a result of the historically warm winter of 2001-2002, has caused S&P to
9 notify the market that, absent sufficient emergency rate relief, it intends to lower PGW's
10 credit rating.

11 **Q. ARE YOU FAMILIAR WITH THE STANDARDS UTILIZED BY STANDARD**
12 **AND POORS TO EVALUATE THE FINANCIAL STATUS OF AN ENTITY FOR**
13 **RATING PURPOSES?**

14 A. Yes, in addition to scores of discussions which I have had with S&P analysts over a
15 number of years, Standard & Poors has provided to PGW the actual coverage formula,
16 standards and calculations that it is using to evaluate PGW.

17 **Q. CAN YOU EXPLAIN THE QUANTITATIVE STANDARDS THAT S&P IS**
18 **USING TO EVALUATE PGW AND THE RESULTS OF THAT ANALYSIS AS**
19 **YOU UNDERSTAND IT?**

20 A. Yes, S&P has been consistent in enunciating the standard by which it measures PGW.
21 While they have recognized that PGW's debt service coverage requirement of 1.5 times
22 annual debt service as a positive credit factor, they (along with Moody's) have expressed
23 concern that PGW's coverage, after the payment of operating expenses, of its fixed
24

1 obligations has been and will continue to be less than 1, absent reliance on non-recurring
2 revenues. They make a fairly simple calculation of this "fixed cost coverage ratio".
3 They subtract operating expenses and depreciation from revenues to obtain the amount
4 available to pay fixed costs. They define these fixed costs as debt service on the 1975
5 ordinance bonds and the 1998 ordinance bonds, the capital lease payments, interest on the
6 commercial paper and the \$18,000,000 payment to the City of Philadelphia. To this they
7 have added an additional \$20 million annual reduction in the commercial paper program.
8 Based upon this calculation, they project that PGW's fixed cost coverage ratio for the
9 year ended August 31, 2002 will be .88 and for the year ended August 31, 2003 will be
10 .97. The S&P worksheet is attached as Exhibit BCB-3. The S&P analyst responsible for
11 evaluating PGW was quoted on February 22 as stating that "given [PGW's] current
12 financial profile, they don't look investment grade."²
13 Obviously, anything below 1 times coverage gives extreme cause for concern.
14 **However, Standard & Poors has indicated that their standard for an investment**
15 **grade bond for a utility like PGW is not merely 1 times coverage, but rather fixed**
16 **cost coverage of at least 1.2 to 1.3 times.** This formula is specifically designed to insure
17 that the entity that they are rating has sufficient liquidity to withstand a variety of
18 exigencies. In fact, the loss of cash and margin that PGW has experienced during this
19 historically warm winter precisely illustrates why S&P is so insistent on this level of
20 fixed cost coverage. Absent the grant of emergency rate relief so that this fixed cost
21 coverage ratio can be achieved on a permanent ongoing basis, Standard & Poors will take
22 negative credit action within the next two months.

² *The Bond Buyer*, February 22, 2002.

1 Q. PLEASE DETAIL THE CONSEQUENCES TO PGW OF A DOWNGRADE BY
2 STANDARD AND POORS.

3
4 A. As I have previously testified, the impact of a downgrade of PGW's credit will be swift
5 and painful. The following is a discussion of what will occur.

6
7 Further Downgrades

8 Because the other two rating agencies, Moody's and Fitch, will quickly understand the
9 impacts of the S&P down-grade that are described below and the financial crisis that will
10 result, they too will reduce the rating of some or all of PGW's bonds to non-investment
11 grade status.

12
13 The Commercial Paper Program

14 In June 2001, PGW was able to renew the letter of credit that supports its \$100,000,000
15 commercial paper program. That letter of credit expires in August 2002. As a condition
16 of granting the 2001 extension of the letter of credit, the syndicate of banks that provide it
17 extracted two concessions from PGW. The annual fee more than doubled with an
18 increased cost to PGW of approximately \$800,000. More critically, the amount of the
19 letter of credit begins to decrease in April 2002 by \$5,000,000/month so that by the time
20 it expires in August, PGW must pay down the amount of commercial paper outstanding
21 to \$80,000,000. This \$20,000,000 pay down is mandatory.

22
23 PGW was barely able to renew the letter of credit in 2001. The decision by the syndicate
24 members to participate was not finalized until the week prior to the expiration of the
25 previous letter of credit and was obtained only after significant jaw boning by City

1 officials and with PGW's agreement to the concessions noted above. The renewal was
2 obtained while PGW's permanent rate case was being adjudicated so the syndicate
3 members were able to anticipate a favorable outcome to that case in making their lending
4 decision.

5
6 In my opinion, if any portion of PGW's bonds are downgraded to below investment
7 grade, the majority of the participants in the letter of credit will use this fact to justify
8 their withdrawal from the letter of credit syndicate., *At best*, only the syndicate leader,
9 Morgan Guaranty Trust will continue to participate in the letter of credit and the
10 commercial paper program (this is due to PGW's status as a "core" customer of
11 Morgan's). The result will be a reduction in the letter of credit from \$80,000,000 to
12 \$30,000,000, at the very least. I should note that even if PGW avoids a downgrade by
13 virtue of being awarded extraordinary rate relief, the Company may have some difficulty
14 getting the letter of credit renewal at the full \$80 million. This is due to such factors as
15 the California energy crisis, concerns created by the Enron bankruptcy and the general
16 business climate as well as specific concerns about PGW.

17
18 When the reduction of the letter of credit and the commercial paper program prompted by
19 the downgrade occurs in August 2002, PGW will be required to pay down at least
20 \$70,000,000 of commercial paper as it matures. When it is unable to do that, there will
21 be a \$70,000,000 (or whatever portion of the letter of credit is not renewed) draw on the
22 letter of credit and the banks will hold an immediately payable demand note. Because
23 PGW will be unable to make this demand payment, it will be necessary to try to enter

1 into some sort of loan workout agreement with the banks. While the loan is unpaid,
2 interest at a taxable rate will be due and owing the banks.

3
4 The impact of such an outcome on PGW will be devastating. The legitimate demands of
5 the bank creditors will pose a permanent barrier to PGW's ability to re-establish itself on
6 a firm financial basis. All remaining liquidity will be wrung out of the company.
7 Vendors, including gas providers, will be unwilling to advance credit to PGW. The
8 company will be in a financial meltdown.

9
10 Future Borrowings

11
12 It has been a number of years since PGW has been able to fund any portion of its capital
13 requirements on a pay-as-you-go basis from internally generated funds. Instead, it has
14 borrowed through the issuance of bonds to fund virtually 100% of its capital needs. In
15 order to continue to make improvements to its LNG plant and, more critically, to
16 continue to implement its main replacement safety program, it is imperative that PGW be
17 able to sell bonds. Prior to the current crisis, PGW had intended to sell its next series of
18 bonds in December 2002. Bond proceeds were to be used for capital purposes while also
19 providing a source of interim liquidity for the company.

20
21 **If PGW's rating is reduced to a below investment grade status, it will be unable to**
22 **sell its bonds.** Like the City of Philadelphia (which was unable to sell its general
23 obligation bonds from 1988-1993 while its credit rating was below investment grade),

PGW will be unable to sell bonds and will have no means of funding even the most critical of its capital requirements. PGW would immediately need to suspend normal operations in order to husband its resources so as to be able to respond to real emergencies and to continue to provide gas service to customers as long as possible. Mr. Knudsen describes some of those responses in detail.

The Forward Purchase Agreement

PGW's financial forecast for 2002 included the implementation of a new Forward Purchase Agreement for its sinking fund reserve. This transaction, which was in progress when the S&P credit statement was released, was anticipated to yield cash in the amount of approximately \$20,000,000 during the spring of 2002. The transaction is now on hold. If the investment grade rating is not sustained, PGW will be unable to complete this transaction and will be short an additional \$20,000,000 in cash.

Q. PLEASE SUMMARIZE YOUR ANALYSES OF THE EFFECT ON PGW AND ITS CUSTOMERS IF THE COMPANY'S BONDS ARE DOWNGRADED.

A. I cannot stress too strongly that the effect on PGW of a downgrade will be swift and disastrous. It will almost immediately result in suspension of normal operations and service will force the Company to lay off employees. As I indicated, it would begin a complete financial meltdown which would impose enormous additional costs on ratepayers from which PGW will not be able to extricate itself for years to come.

Q. DOES THIS COMPLETE YOUR TESTIMONY?

A. Yes.

Exhibit BCB-1

Docket No. R-000170340002

STANDARD & POORS	RATINGS DIRECT
-----------------------------	-----------------------

Return to Regular Format

Research:

Summary: Philadelphia, PA; Utility, Gas

Publication date: 12-Feb-2002

Analyst: Anesh Prabhu, New York (1) 212-438-1285; Jodi E Hecht, New York (1) 212-433-2617

Credit Profile

CREDITWATCH UPDATE

	To	From
\$160.660 mil. Philadelphia gas wks rev bnds (1998 Gen Ordinance) ser A dtd 06/01/1998 due 07/01/1999-2014 2018 2026	AAA/BBB(SPUR)	BBB
\$103.550 mil. Philadelphia gas wks rev bnds (1998 Gen Ordinance) ser B dtd 06/01/1998 due 07/01/2014 2018 2028	AAA/BBB(SPUR)	BBB
\$20.010 mil. Philadelphia gas wks rev bnds (Sub1998 Gen Ordinance) ser C dtd 06/01/1998 due 07/01/1999-2014	AAA/BBB-(SPUR)	BBB-
\$61.960 mil. Philadelphia gas wks rev bnds 16th ser dtd 05/07/1999 due 07/01/2000-2009 2013-2015	AAA/BBB(SPUR)	BBB
\$112.245 mil. Philadelphia gas wks rev bnds 2nd ser dtd 05/07/1999 due 07/01/2000-2029	AAA/BBB(SPUR)	BBB
\$120.225 mil. Philadelphia gas works rev bnds (1998 Gen Ordinance) third ser dtd 06/01/2001 due 08/01/2003-2019 2021 2031	AAA/BBB(SPUR)	
\$355.825 mil. Philadelphia gas wks	BBB	BBB

Rationale

Standard & Poor's 'BBB' underlying rating (SPUR) and 'BBB' uninsured rating on Ordinance 1975 and 1998 senior bonds, and its 'BBB- SPUR' on the 1998 Ordinance subordinated bonds remain on CreditWatch with negative implications where they were placed July 20, 2000.

Philadelphia Gas Works' (PGW) PGW's poor liquidity position has worsened with December 2001 cash balances at \$3.8 million (2.5 days' cash) compared to ending cash of about \$8.4 million at fiscal year-end August 2000. PGW is filing an emergency rate relief in February 2002 with the Pennsylvania Public Utility Commission (PUC) to address liquidity issues. Without immediate cash flow improvement, ratings will be lowered. PGW's poor liquidity is due, in part, to the PUC final rate order of a \$33.6 million rate increase in December 2001, about \$31.0 million less than requested. This rate shortfall, combined with the warmer-than-budgeted weather this winter and higher receivables, contributes to poor liquidity, which is not appropriate for the current rating level. "If the PUC approves an emergency rate request, Standard & Poor's will review the adequacy of the increase and determine if ratings will be affirmed or lowered," said Standard & Poor's credit analyst Anesh Prabhu.

PGW, the largest municipality owned gas utility in the U.S., purchases, sells, and distributes gas to more than a half-million customers within the city of Philadelphia. At fiscal year-end August 2001, PGW had about \$900 million of debt outstanding.

The ratings reflect the following risks:

- The poor liquidity position required PGW to temporarily borrow from its capital fund account in January 2002 for servicing debt obligations, and requires PGW to rely on financial transactions that create nonrecurring revenues in this fiscal year. Without additional project revenues or rate relief, PGW may be unable to reimburse its capital fund. PGW will also seek a deferral on the \$45 million working capital city loan, due in January 2003.

- Weak fixed-charge coverage that, including lease payments and the annual payment to the city of Philadelphia, has ranged between 1.0 times (x)-1.1x during the past four years.
- Limited ability of the city of Philadelphia to provide assistance due to the city's tight financial situation.
- PGW's problems with high account receivables, which were exacerbated in 2001 due to escalating fuel prices recoverable through the gas cost recovery (GCR) mechanism. Receivables have been historically high due to a high proportion of low-income residents in the demographics of PGW's service territory.
- A warm winter, which likely will cause PGW to miss budgeted forecasts in fiscal 2002.
- Inability to convert from interim management to permanent management by December 2001, as directed by PUC's interim rate order in November 2000. The search for permanent management is at an advanced stage and is expected to conclude by April 2002.

Nonetheless, the following strengths offset the risks:

- A favorable closing to the labor contract negotiations in June 2001; the contract freezes labor costs for the next two years, reduces benefits, and reasserts management prerogatives regarding work rules.
- Operational improvements that included correcting the faulty billing system, improving call center performance, and auditing procedure improvements.
- Sound legal provisions that require 1.5x coverage on an accrual basis on the senior bonds.
- The PUC's timely approvals of required gas cost rate increases since regulatory oversight changed in July 2000.
- PGW has successfully solicited federal and state funds in the form of LIHEAP and Crisis grants, which have aided the company's cash flow and earnings position.

Copyright © 1994-2002 Standard & Poor's, a division of The McGraw-Hill Companies. All Rights Reserved. Privacy Policy

A Division of The McGraw-Hill Companies 

Philadelphia Gas Works' Ratings Remain on CreditWatch Due To Worsened Liquidity Position

Aneesh Prabhu, New York (1) 212-438-1285;

Jodi E Hecht, New York (1) 212-438-2019

NEW YORK (Standard & Poor's) Feb. 12, 2002--Standard & Poor's triple-'B' underlying rating (SPUR) and triple-'B' uninsured rating on Philadelphia Gas Works' (PGW) Ordinance 1975 and 1998 senior bonds, and its triple-'B'-minus SPUR on the 1998 Ordinance subordinated bonds remain on CreditWatch with negative implications where they were placed July 20, 2000.

PGW's poor liquidity position has worsened with December 2001 cash balances at \$3.8 million (2.5 days' cash) compared to ending cash of about \$8.4 million at fiscal year-end August 2000. PGW is filing an emergency rate relief in February 2002 with the Pennsylvania Public Utility Commission (PUC) to address liquidity issues. Without immediate cash flow improvement, ratings will be lowered. PGW's poor liquidity is due, in part, to the PUC final rate order of a \$33.6 million rate increase in December 2001, about \$31.0 million less than requested. This rate shortfall, combined with the warmer-than-budgeted weather this winter and higher receivables, contributes to poor liquidity, which is not appropriate for the current rating level. "If the PUC approves an emergency rate request, Standard & Poor's will review the adequacy of the increase and determine if ratings will be affirmed or lowered," said Standard & Poor's credit analyst Aneesh Prabhu.

PGW, the largest municipally owned gas utility in the U.S., purchases, sells, and distributes gas to more than a half-million customers within the city of Philadelphia. At fiscal year-end August 2001, PGW had about \$900 million of debt outstanding.

The ratings reflect the following risks:

-- The poor liquidity position required PGW to temporarily borrow from its capital fund account in January 2002 for servicing debt obligations, and requires PGW to rely on financial transactions that create nonrecurring revenues in this fiscal year. Without additional project revenues or rate relief, PGW may be unable to reimburse its capital fund. PGW will also seek a deferral on the \$45 million working capital city loan, due in January 2003.

-- Weak fixed-charge coverage that, including lease payments and the annual payment to the city of Philadelphia,

has ranged between 1.0 times (x)-1.1x during the past four years.

-- Limited ability of the city of Philadelphia to provide assistance due to the city's tight financial situation.

-- PGW's problems with high account receivables, which were exacerbated in 2001 due to escalating fuel prices recoverable through the gas cost recovery (GCR) mechanism. Receivables have been historically high due to a high proportion of low-income residents in the demographics of PGW's service territory.

-- A warm winter, which likely will cause PGW to miss budgeted forecasts in fiscal 2002.

-- Inability to convert from interim management to permanent management by December 2001, as directed by PUC's interim rate order in November 2000. The search for permanent management is at an advanced stage and is expected to conclude by April 2002.

Nonetheless, the following strengths offset the risks:

-- A favorable closing to the labor contract negotiations in June 2001; the contract freezes labor costs for the next two years, reduces benefits, and reasserts management prerogatives regarding work rules.

-- Operational improvements that included correcting the faulty billing system, improving call center performance, and auditing procedure improvements.

-- Sound legal provisions that require 1.5x coverage on an accrual basis on the senior bonds.

-- The PUC's timely approvals of required gas cost rate increases since regulatory oversight changed in July 2000.

-- PGW has successfully solicited federal and state funds in the form of LIHEAP and Crisis grants, which have aided the company's cash flow and earnings position.

Exhibit BCB-2

Docket No. R-000170340002

Ratings Services
33 Water Street, 18th Floor
New York, NY 10041-0003
Tel: (212) 438-2064
Reference No:

Curtis Moulton
Managing Director
Infrastructure Finance Ratings

Standard & Poor's

A Division of The McGraw-Hill Companies



July 20, 2000

Mr. Kumar Kishinchand, P.E.
President & Chief Executive Officer
Philadelphia Gas Works
800 W. Montgomery Avenue
Philadelphia, PA 19122

Re: *\$355,825,000 Philadelphia Gas Works, Revenue Bonds*
\$103,550,000 Philadelphia Gas Works, Revenue Bonds, 1998 General Ordinance, Series B (SPUR)
\$160,660,000 Philadelphia Gas Works, Revenue Bonds, 1998 General Ordinance, Series A (SPUR)
\$112,245,000 Philadelphia Gas Works, Revenue Bonds, Second Series (SPUR)
\$67,960,000 Philadelphia Gas Works, Revenue Bonds, Sixteenth Series (SPUR)

Dear Mr. Kishinchand:

As part of Standard & Poor's ongoing secondary market surveillance, we have reviewed the latest financial report and other relevant data on the above debt. After such review, we have placed the rating of 'BBB' on CreditWatch with negative implications due to PGW's very weak cash flows arising from a convergence of budgeting that did not reflect the trend toward warmer winters; historic ongoing problems with high revenue receivables; and the faulty implementation of a new billing system.

Please continue to send updated information including annual audit reports and budgets, and if applicable, updated operating and construction progress data, addressed to:

*Standard & Poor's Ratings Services
Public Finance Secondary Market Surveillance
33 Water Street, Muni Drop Box No. 1, 38-2-2
New York, NY 10041-0003*

If you have any questions please feel free to contact Jodi Hecht at (212) 438-2019.

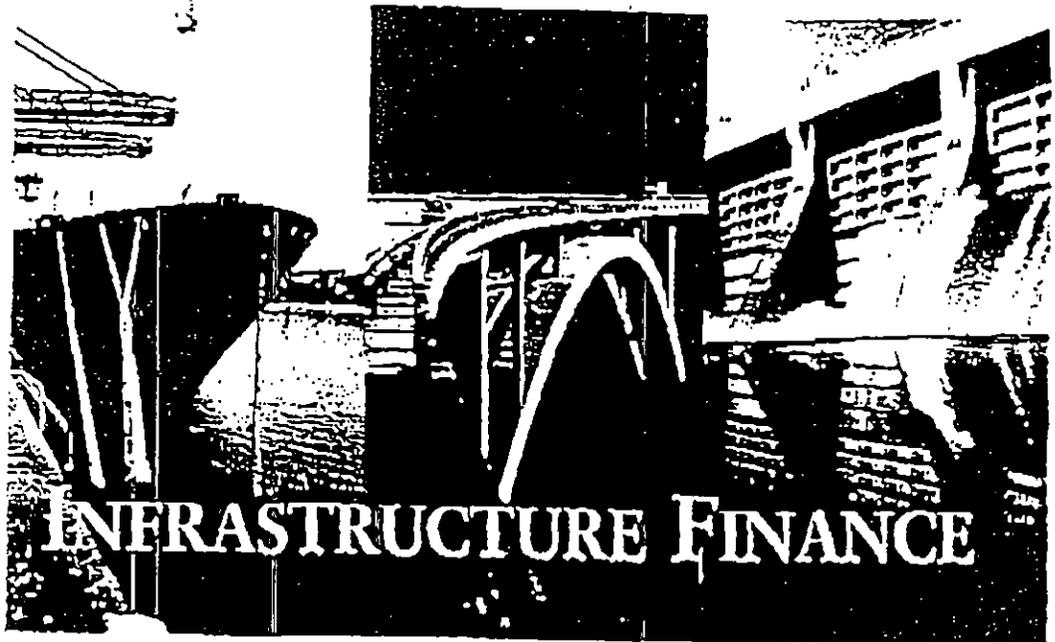
Thank you for continuing your relationship with Standard & Poor's Ratings Services.

Very truly yours,

Curtis Moulton

cc: Barbara C. Bisgajer, Public Financial Management

STANDARD
& POOR'S



PHILADELPHIA GAS WORKS, PENNSYLVANIA

Credit Profile

Outstanding Ratings
\$794.2 mil rev bnds,
varies series **BBB**
\$20.0 mil rev bnds,
subordinate, 1998 gen ordinance, **BBB-**

Revised: CreditWatch
Negative

Analysts:
Iodi Hecht, New York
212) 438-2019
Elizabeth Fitzgerald Smith, Chicago
312) 669-2172

Rationale

The rating action reflects PGW's very weak cash flows arising from a convergence of budgeting that did not reflect the trend toward warmer winters; historic ongoing problems with high revenue receivables; and the faulty implementation of a new billing system. Rate relief is needed by this fall. The tariffs that PGW has filed before the state Public Utilities Commission are projected to generate an additional \$52 million and increase base rates and monthly charges by 10%. The proposed tariff will increase rates to above-average in a service area with below-average income levels.

Rate applications to the PUC are typically resolved over a nine-month period, but it is not clear that PGW's application, which was filed in July 2000, will be approved before the 2000 winter heating season that is a critical component of the utility's cash flow.

Other credit weaknesses include the following:

- Potentially above average gas rates if PGW's five year plan is not fully implemented, especially in a market that will be open to retail choice beginning in fiscal 2004;

- Aggressive future projections which assume normal weather conditions that have not been realized in recent years and productivity cost savings, ranging from 5% to 10% of expenditures;

- Deferred capital spending limited by declining excess cash flow; and

- Uncertainty regarding the long term management structure and operating strategy.

These are offset by sound legal provisions, which require, on an accrual basis, 1.50 times (x) coverage on the senior bonds, in spite of the lowered revenue requirement from the creation of a subordinate lien.

The bonds are secured by the net revenues of the gas system. Under provisions of the Natural Gas Choice and Competition Act, which was signed into law in June 1999 by Gov. Tom Ridge, after July 1, 2000 the rate relief and customer service functions for PGW were to be regulated by the PUC. Previously, these powers belonged to the Philadelphia Gas Commission (PGC). The PGC maintains the authority to approve operating and capital budgets, while the city of Philadelphia remains the owner of the system.

PGW filed a rate increase in July 2000, which they would like to take effect before the 2000 winter heating season. However, the PUC's approval process takes nine months to complete. PGW requested that the PUC allow this rate filing to be reviewed by PGW, which has a shorter process, and would enable the new rates to be effective by October 2000. Without the rate increase in place, the ending cash position for fiscal 2001 is projected to be negative \$16.9 million (approximately 4% of operating expenditures).

The 1998 indenture created senior and subordinate liens. The senior lien rate

PHILADELPHIA GAS WORKS, PENNSYLVANIA

covenant remains at 1.50 times (x) annual debt service, while the subordinate lien and refunded 1975 bond rate covenant require only 1x coverage of annual debt service. While 1.5x coverage is sound for a triple-B-rated gas system, debt service coverage of all obligations after the \$18 million annual transfer to the city was less than 1 times (x) in fiscals 1998 and 1999. The payment is made throughout the year. However, the city had been willing to defer the payment until year end, providing some latitude to address unanticipated year-end financial needs.

Minimal coverage has been a historic problem. PGW implemented non-recurring actions in fiscals 1995, 1998, and 1999 to meet its rate covenant. Steps were not needed in fiscal 2000, because the calculation of the rate covenant was liberalized under the provisions of the 1998 indenture. Another warmer-than-budgeted winter in 2000 led to reduced gas sales, and revenues were 15% lower than budget. Debt service coverage in fiscal 1999 of all revenue bonds was 1.11 times (x), with estimated fiscal 2000 results generating 1.31x DSC. However, when coverage of all fixed payments—including lease payments—is calculated, fiscal 1999 DSC was a minimal 1.01x, and fiscal 2000 DSC is 1.20x. Financial projections, while somewhat aggressive, assume a normal number of degree days, which has not occurred in the past three years; approval of the rate increase; discontinuation of the senior citizen discount program; and productivity and cost savings that are expected to be implemented under a new labor contract beginning in late fiscal 2001.

Over the past three years, including estimates for fiscal 2000, operating expenses have exceeded operating revenues, reducing reserves and cash balances. In fiscal 2000, no excess revenues were generated to contribute to ongoing and long-term capital needs. The revised five-year fiscal 2002-2006 capital program totals \$266.4 million—a \$91 million decline from the previous program. While current management believes this program is better targeted to address immediate needs, it is unclear that the ongoing investment has been adequately made in the system. Funding

for this program includes a \$75 million bond issue next fiscal year (23% of the program) with the balance (72%) funded from internally generated funds. Funding for the capital program is largely dependent on PGW's ability to implement the five-year operating plan, as projected.

Outlook

To preserve its ratings, PGW will need to obtain rate relief and implement the projected productivity savings ranging between 5% to 10% annually. Cost reductions are critical to PGW's ability to fund future capital needs and maintain competitive commodity charges to retain customers following the introduction of customer choice in fiscal 2004.

Exhibit BCB-3

Docket No. R-000170340002

PGWORKS

Fiscal Year Ending: 08/31
Operating Revenue ('000)

Revenue & Debt Service Analysis

	1998-99	1999-00	2000-01	2001-02	2001-02	2001-02	2002-03
Base Rate Scenarios				\$ 33.6 Million	\$ 65 Million **	\$ 65 Million **	\$ 65 Million
Non-heating/Gas transportation/Unpiled gas adj.	\$72,751	\$91,143	\$107,035	\$103,103	\$103,103	\$103,103	\$100,966
Heating	\$390,242	\$434,544	\$620,867	\$536,079	\$536,079	\$536,079	\$525,008
Proposed Base Rate			\$0	\$32,224	\$34,724	\$62,224	\$62,417
Marginal Revenue Loss Customer Utilization			\$0				(\$2,000)
Unbilled Adjustment	(\$349)	\$7,299	(\$8,967)	(\$1,400)	(\$700)	(\$700)	\$950
Appliance and other revenues	\$13,683	\$11,978	\$12,075	\$12,260	\$12,250	\$12,250	\$20,571
Other operating revenues	\$10,558	\$10,911	\$19,048	\$16,785	\$17,540	\$17,540	\$17,210
Total Operating Revenues	\$486,885	\$555,875	\$750,058	\$699,051	\$703,006	\$730,506	\$725,122

Interest & other income	\$8,263	\$9,417	\$12,343	\$4,934	\$5,894	\$5,894	\$8,380
Swap and option agreement	\$0	\$8,645	\$0		\$0	\$0	
AFUDC (Interest)	\$0	\$0	\$0	\$765	\$765	\$765	\$623
Total Non-Operating Revenues	\$8,263	\$18,062	\$12,343	\$5,699	\$6,659	\$6,659	\$9,003

Total Revenues	\$495,148	\$573,937	\$762,401	\$704,750	\$709,665	\$737,165	\$734,125
-----------------------	------------------	------------------	------------------	------------------	------------------	------------------	------------------

Operating Expenses

Natural Gas	\$219,090	\$266,354	\$431,327	\$373,026	\$373,026	\$373,026	\$355,234
Gas Processing	\$13,881	\$14,033	\$13,400	\$13,161	\$13,161	\$13,161	\$13,643
Field Services	\$35,090	\$33,704	\$33,202	\$32,730	\$32,730	\$32,730	\$33,113
Distribution	\$15,527	\$14,246	\$14,837	\$14,440	\$14,440	\$14,440	\$14,434
Customer affairs	\$27,044	\$28,031	\$27,418	\$28,722	\$28,722	\$28,722	\$27,936
Bad Debt expense	\$39,000	\$54,642	\$67,633	\$60,823	\$61,601	\$61,601	\$58,802
Marketing	\$5,253	\$3,041	\$3,486	\$6,596	\$6,596	\$6,596	\$5,616
Administrative & General	\$27,545	\$56,236	\$25,257	\$32,043	\$32,043	\$32,043	\$28,972
Health Insurance	\$23,432		\$27,404	\$30,490	\$29,190	\$29,190	\$33,559
Pensions	\$787	\$1,096	\$2,301	\$2,313	\$2,313	\$2,313	\$2,266
Taxes	\$6,091	\$6,512	\$6,299	\$6,430	\$6,430	\$6,430	\$6,374
Personal reductions/retirements				(\$7,100)	(\$10,500)	(\$10,500)	(\$10,000)
Total Operating Expenses	\$412,740	\$477,895	\$652,564	\$593,674	\$589,752	\$589,752	\$569,949

Net Depreciation	\$29,075	\$30,805	\$31,840	\$33,285	\$33,285	\$33,285	\$34,911
Payment in Lieu of Taxes	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Other - Amortization of Demand Side Management	\$0	\$0	\$0	\$0	\$0	\$0	\$0

Net Available To Service Debt (Exc. Depr.)	\$82,408	\$96,042	\$109,837	\$111,076	\$119,913	\$147,413	\$164,176
Add Capital leases	\$7,882	\$7,988	\$7,977	\$5,954	\$5,954	\$5,954	\$3,997
Net Available To Service aggregate debt	\$90,290	\$104,030	\$117,814	\$117,030	\$125,867	\$153,367	\$168,173
PGW Provided Numbers	\$88,167	\$101,872		\$115,654	\$152,184	\$152,185	\$167,921

Debt Service Coverage Analysis	1998-99	1999-00	2000-01	2001-02	2001-02	2001-02	2002-03
Net Available To Service 1975 Bonds	\$90,290	\$104,030	\$117,814	\$117,030	\$125,867	\$153,367	\$168,173
1975 Ordinance bonds debt service	\$57,741	\$59,345	\$51,611	\$55,528	\$55,528	\$55,528	\$47,292
Debt Service 1975 Bonds	1.56	1.75	2.28	2.11	2.27	2.76	3.56
1998 Ordinance bonds debt service	\$14,230	\$21,659	\$29,449	\$30,926	\$30,926	\$30,926	\$36,539
DS 1975 Senior Bonds/and 1998 Ordinance Senior Bonds	1.25	1.28	1.45	1.35	1.46	1.77	2.01
Capital Lease Costs	\$7,882	\$7,988	\$7,977	\$5,954	\$5,954	\$5,954	\$3,997
Debt Service 1975 bonds/Capital Leases/1998 senior	1.13	1.17	1.32	1.27	1.36	1.66	1.91
1998 Ordinance Subordinated Debt	\$1,988	\$1,987	\$1,990	\$1,986	\$1,986	\$1,986	\$1,988
Debt Service (revenue bonds plus capital leases)	1.10	1.14	1.29	1.24	1.33	1.62	1.87
Total Debt Service (Interest & Capital repayments)	\$81,841	\$90,979	\$91,027	\$94,394	\$94,394	\$94,394	\$89,816
Others-Commercial Paper Notes	\$2,822	\$3,927	\$4,537	\$20,000	\$20,000	\$20,000	\$20,000
Fixed Charge Cov. - Aggregate Debt Service	1.07	1.10	1.23	1.02	1.10	1.34	1.53
City Annual Payment			\$18,000	\$18,000	\$18,000	\$18,000	\$18,000
Fixed charge Cov., including city payment of \$18 million			1.04	0.88	0.95	1.16	1.32

Fixed Charge Cov. Weather adjusted in 2001-2002 (@ \$10 million impact)				0.81	0.88	1.08	
Fixed Charge Coverage, including financial transaction @ \$20 million				0.96	1.03	1.23	
Fixed charge coverage, including financial transaction and city annual payment grant back (all \$18 m)				1.11	1.19	1.43	
Fixed Charge Coverage with City \$45 mill repayment (2002-2003)							0.97

Column F volumetric relief ; Column G compressed relief

Aggregate Fixed Charge Coverage for 2003 includes \$18 million city payment & the \$45 million loan repayment. However, \$20 million CP paydown, shown under debt service, is not mandatory
 **2001-2002 emergency rate increase assumes an additional \$30 million permanent rate over the amount already granted. However, the cash impact is only \$2.5 million in fiscal 2002 on a volumetric basis. If the additional \$30 million is available on a cash basis in 2002, fixed charge coverage assuming the financial transaction is 1.23 and with the city loan grantback is 1.43. The entire \$30 million emergency additional relief is available on a permanent basis in 2003 (first full year with \$65 million rate increase) 2002-2003 assumes normal degree days (4,555 degree-days). Past 3 winters have averaged lower.

DOCUMENT
FOLDER

PGW E.R.P. St. 5

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

TESTIMONY OF

JANICE DAVIS

DOCKETED
APR 30 2002

**ON BEHALF OF
PHILADELPHIA GAS WORKS**

**PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE PETITION**

R- 000170340002

FEBRUARY 2002

1 Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS ADDRESS.

2 A. My name is Janice Davis. My business address is 1401 J.F. Kennedy Boulevard, Suite
3 1330, Philadelphia, PA 19102.

4 Q. ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

5 A. My testimony is presented on behalf of the City of Philadelphia as the owner of
6 Philadelphia Gas Works ("PGW").

7 Q. PLEASE SUMMARIZE YOUR EDUCATION AND PROFESSIONAL
8 EXPERIENCE FOR THE RECORD.

9 A. I was appointed as Director of Finance of the City of Philadelphia by Mayor John F.
10 Street. As a member of the Mayor's Cabinet and Chief Financial Officer of the City, I
11 am involved with financial and fiscal policy development and directly oversee all City
12 financial activities, including budget, accounting, revenue collection, treasury functions
13 and procurement, as well as activities related to risk management, the Minority Business
14 Enterprise Council and Bureau of Administrative Adjudication. I also serve as the
15 Chairman of the Philadelphia Board of Pensions and Retirement and as a member of
16 various boards and commissions, including City Planning Commission, Mayor's Office
17 of Community Services, Pennsylvania Intergovernmental Cooperation Authority,
18 Philadelphia Industrial Development Corporation, Philadelphia Housing Development
19 Corporation, and the Sinking Fund Commission. I also serve on the Board of Directors
20 of the Philadelphia Facilities Management Corporation. My curriculum vitae detailing
21 my professional experience is attached as Exhibit JD-1 to this testimony.

22 Q. WHAT ARE YOUR RESPONSIBILITIES AS FINANCE DIRECTOR?

23 A. As Director of Finance, I have responsibilities under the Management Agreement to
24 oversee the operations of PGW. Specifically, I assist in the preparation of the operating

1 budget and forecast and offer recommendations as to the form and extent of the capital
2 budget and forecast prior to its submission for City Council approval. My office further
3 receives plans for capital loans and participates in the approval process for short and
4 long-term borrowing, among other duties.

5 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUC ABOUT THE**
6 **LEVEL AND TYPES OF SUPPORT PROVIDED BY THE CITY OF**
7 **PHILADELPHIA TO PGW?**

8 A. Yes. I submitted testimony in PGW's previous base rate proceeding detailing the various
9 types of financial and other support that Philadelphia had provided to PGW at that time to
10 respond to PGW's existing and continuing financial crisis.

11 **Q. CAN YOU UPDATE THAT SUMMARY?**

12 A. Yes. Most importantly, PGW continues to have use of a \$45 million interest free
13 revolving loan provided by the City to assist its cash working capital needs. As I
14 testified, the cost of such a loan would be \$2-3 million annually if it had been obtained
15 conventionally (which PGW would not have been able to do in any event). While, by its
16 terms, the loan is due to be paid back in January 2003, the administration shortly will
17 propose to permit PGW to delay repayment until August 2003. In addition, although the
18 earnings on PGW's bond sinking funds belong to the City, (since the bonds, technically
19 are City bonds), we have agreed to allow those earnings to be booked as Other Income.
20 Those earnings also form the basis of any forward purchase agreement when the
21 Company requires such a financing. (Mr. Knudsen explains the forward purchase
22 agreement in greater detail in his testimony.)

1 Q. **IN LIGHT OF STANDARD AND POORS THREATENED DOWNGRADE,**
2 **WHAT IS THE CITY'S PRESENT ABILITY TO PROVIDE ADDITIONAL**
3 **FINANCIAL SUPPORT TO PGW?**

4 A. Since the last time I testified, Philadelphia's financial circumstances, which mirror the
5 economy, have materially changed for the worse. In May 2001, (the date of my last PUC
6 submission) for a five year period I was projecting a surplus for the City in excess of \$
7 180 million. This year, in preparing our five year plan for fiscal years 2003 -2007, the
8 City was forced to take drastic steps to avoid a \$ 296 million deficit over the life of the
9 Plan. These steps included reducing our contribution to the pension fund and curtailing
10 planned tax reductions. Philadelphia's budget is subject to review and approval by the
11 Pennsylvania Intergovernmental Cooperation Authority ("PICA"). In its current five
12 year plan, (Fiscal years 2002 -2006) there is neither capacity nor provision for additional -
13 subsidies to PGW. The City's five year plan is predicated on receiving \$135 million of
14 revenue from PGW, consisting of the \$18 million annual payment to the City for five
15 years, as well as a payback of the \$45 million emergency loan. Without these revenues
16 from PGW, there will be a hole in the City's plan that must be filled through other cuts.

17 Q. **IN LIGHT OF PGW'S PRESENT FINANCIAL EMERGENCY, WHAT**
18 **ADDITIONAL STEPS WILL THE CITY BE ABLE TO TAKE TO ASSIST THE**
19 **COMPANY?**

20 A. Under the circumstances, the City presently has very limited ability to provide even
21 temporary additional assistance to PGW. However, PGW has explained that, in light of
22 the effects of the extremely warm winter and the possibility of not being able to move
23 forward with a planned forward purchase financing, the Company is in danger of failing
24 to satisfy the debt service coverage requirements of its bond covenants for this fiscal
25 year. At present, the Company is projecting that even if the PUC awarded the Company
26 additional extraordinary rate relief this Spring, PGW will not be able to collect sufficient

1 additional revenue to offset the magnitude of losses it will experience by fiscal year end.
2 Missing the coverage requirement would be a disastrous consequence that must be
3 avoided at all costs.

4 To prevent this outcome the Administration may have no option but to grant back
5 to PGW all or the necessary portion of its \$18 million payment on a one time basis, to the
6 extent it is necessary, to assure that PGW will not fall below its covenant requirements
7 and be in technical default on its bonds. This cannot be done without having some
8 negative impact on the City's finances.

9 **Q. DO YOU EXPECT THAT THE CITY WILL BE ABLE TO PROVIDE ANY**
10 **FURTHER ASSISTANCE OF ANY SORT UNDER ANY CONDITION?**

11 **A.** No. To repeat, the City is facing a tight budget, principally due to the down turn in the
12 economy as well as additional funding requirements for the School District, another
13 financially troubled entity. PGW's City payment and payback of its loan are key
14 elements of our plan to balance our budget. We are truly in a situation where any
15 reduction in those sources of revenue for the City would result in a reduction in City
16 services, layoffs or a hiring freeze.

17 Additionally, it is my understanding that one-time stop gap measures will not
18 satisfy the liquidity deficiency that the rating agency has identified for PGW. The City is
19 in no position to provide ongoing support to the Company.

20 Any assistance will be for the current fiscal year only; to do more would be to
21 jeopardize the fiscal stability of the City.

1 Q. ASSUME, IF YOU WOULD, THAT PGW IS DOWNGRADED AND THAT THE
2 COURSE OF EVENTS AS OUTLINED BY MR. KNUDSEN OCCURS. WHAT
3 WOULD PGW'S CRISIS MEAN TO THE CITY?

4 A. Frankly, a scenario such as Mr. Knudsen describes would be a catastrophe. First, the
5 City would lose the string of \$18 million dollar payments and the \$45 million loan, as a
6 subordinate instrument to all other debt, would be placed in some indefinite position.
7 Given the nature of the work-out that would ensue – bank loan restructuring, payment
8 deferrals, etc., I assume that the City could not count on repayment during the planning
9 period. I would then have a \$135 million larger gap in the budget. Some combination of
10 drastic reductions in programs and tax/fee changes would be needed. Without seeing the
11 specifics of a workout plan, I can't speculate further. Where the money would come from
12 other than customers at that point, I don't know.

13 Q. DOES THAT CONCLUDE YOUR TESTIMONY?

14 A. Yes.

Exhibit JD-1

Docket No. R-000170340002

JANICE D. DAVIS

EXPERIENCE

**May, 2000-
Present**

City Of Philadelphia

**Secretary of Financial
Oversight/Director of
Finance**

Directs the financial operations of the City. Supervises the following departments: Purchasing, Accounting, Budget, Revenue, Minority Business Enterprise Commission, Treasury, Pension Trust, Risk Management, Board Of Administrative Review and the Sinking Fund Commission. Exercises financial oversight of related City entities such as the Philadelphia School District, Philadelphia Gas Works and the Philadelphia Parking Authority. Serves on the Board of Directors of several boards and commissions, including the Pennsylvania Convention Center, Penn's Landing, the Philadelphia Intergovernmental Cooperation Authority, the Philadelphia Facilities Management Corporation and the Philadelphia Industrial Development Authority. Participates in labor contract negotiations. Supervises the issuance of all debt of the City and its related entities. Serves on the City planning commission. Serves as a member of the Mayor's cabinet.

**October 1998-
May, 2000**

Dallas Independent School District

Chief Financial Officer

Directed the financial operations of the school district. Supervised the following departments: Purchasing, Finance and Accounting, Budget Development and Control, Risk Management, and Minority and Women Business Enterprise. Served as a member of the Superintendent's cabinet. Recommended policies and establishes procedures relating to the financial, cash management, risk management, debt management, procurement, minority business, budget and accounting operations of the District.

**September 1995-
September 1998**

Dallas/Fort Worth International Airport

**Director of Finance
and Budget**

Supervised Accounts Payable, Accounts Receivable, Payroll, Financial Planning, Grants Management, Cash Management, Cost Systems Budget and Risk Management. Established policies and procedures relating to the financial, cash management, risk management, debt management, budget and accounting operations of the Airport. Had responsibility for setting rates charged for use of Airport facilities. Evaluated borrowing alternatives and initiated all debt issuance. Served on the following committees: Investment, Capital, Information Technology Strategic Planning. Prepared monthly projections of revenues and expenses. Supervised the preparation of monthly report to the Board of Directors, quarterly report to the

airlines, the annual operating and capital budgets and the Comprehensive Annual Financial Report.

May 1993-
September 1995

**Finance and Administration
City of Houston, Texas**

**Deputy Director
Financial Services**

Supervised the Office of Budget and Management, Cash and Debt Management, Capital Improvement Management and Grants Management. Established policies and procedures relating to the financial, budget and debt operations of the City of Houston. Had responsibility for the development, preparation and management of all city budgets, which combined totaled in excess of one billion dollars. Supervised the preparation of the five year economic forecast and Capital Improvement Plan. Supervised capital spending to ensure compliance with IRS and other regulatory requirements. Evaluated borrowing alternatives and initiated all debt issuance. Appeared before rating agencies in conjunction with the issuance of debt. Supervised the preparation of monthly projections of revenues and expenditures for all City funds. Served as an advisor to the Mayor on matters relating to finance. Served on the following permanent committees: Investment, Arbitrage, Accounting Improvement. Appeared before the City Council and Council committees as needed. Served as City appointee and Treasurer on the Board of Directors of a tax increment/public improvement district.

August 1992-
May 1993

**City Controller's Office
City of Houston, Texas**

**Deputy Director/Director
General Accounting**

Directed, managed, planned and evaluated the accounting and financial reporting activities. Reviewed the analysis of revenue and expenditure projections for all fund types. Supervised the preparation of the Controller's Monthly Financial Report. Acted as the lead in the preparation, review and submission of the Comprehensive Annual Financial Report.

June 1989-
August 1992

**Sewerage and Water Board
New Orleans, Louisiana**

Utility Financial Administrator

Supervised the Finance, Payroll, Customer Accounting and General Accounting Departments. Established policies and procedures to provide for efficient operation of the financial and accounting functions. Served on various committees charged with designing and implementing new software systems. Served on the capital and operating budget committees. Supervised the preparation of the Comprehensive Annual Financial Report. Worked with the external auditors and the Computer Center to design an interface between the Customer Account Management

System and the general ledger. Appeared, as needed, before legislative, educational and community groups to address issues of fiscal importance to the Board. Participated in the Quality Management Project as a member of the implementation task force. Participated in the preparation of RFP's for a fixed asset inventory, computer management services and privatization of sewer treatment operations.

March 1979-
June 1989

New Orleans Public Schools

**Accounting Manager;
General Ledger Accountant;
Accountant II; Accountant I**

As Accounting Manager, directed the accounting functions of the Finance Department which included Accounts Payable, Payroll, Fixed Assets and General Ledger. Prepared cashflow/cash need projections. Served as the department's liaison to the various departments as it related to the MSA general Ledger and subsystems. Assisted in the preparation, review and submission of the Comprehensive Annual Financial Report. Assisted in bond sales.

As the General Ledger Accountant, developed the system for balancing the subsystem input into the general ledger posting. Supervised staff responsible for the data input and verification. Prepared departmental budget and monitored expenditures. Participated in the District's first audit.

As Accountant I and II, assisted in the installation and implementation of the computerized general ledger. Prepared and balanced all initializing input into the new general ledger. Supervised staff responsible for data input.

EDUCATION

University of New Orleans
Bachelor of Science in Accounting, 1978

PROFESSIONAL DESIGNATION

Licensed Certified Public Accountant, Louisiana, Texas; Certified Government Financial Manager

ORGANIZATIONS

American Institute of Certified Public Accountants; Texas Society of Certified Public Accountants; Government Finance Officers Association; Association of Government Accountants; 2001- 2003 Fellow, Urban Health Initiative

DOCKETED

APR 30 2002

PGW E.R.P. St. 5.1

R-00017034F0002

3/26/02 Phila PA
025

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

REBUTTAL TESTIMONY

OF

**DOCUMENT
FOLDER**

JANICE DAVIS

ON BEHALF OF

PHILADELPHIA GAS WORKS

PHILADELPHIA GAS WORKS

EXTRAORDINARY RATE PETITION

R-000170340002

RECEIVED
02 APR -2 PM 1:54
P.A.P.U.C.
SECRETARY'S BUREAU

MARCH 2002

1 **Q. OFFICE OF CONSUMER ADVOCATE WITNESS RICHARD W. LELASH HAS**
2 **TESTIFIED THAT THE CITY HAS OFFERED TO GRANT BACK THE \$18**
3 **MILLION CITY PAYMENT AS "PROJECT REVENUES." PLEASE CLARIFY**
4 **THE CITY'S POSITION IN REGARD TO THE CITY PAYMENT.**

5 A. The City recognizes that due to PGW's financial condition it may be forced to grant back
6 to the Company a portion of the \$18 million payment for FY 2002 in order to ensure that
7 the Company can meet its bond coverage requirements. The City is only prepared to
8 grant back the entire \$18 million if the entire payment is necessary to satisfy the bond
9 coverages.

10 **Q. MR. LELASH RECOMMENDS THAT AS A PRECONDITION TO PGW**
11 **RECEIVING ANY EXTRAORDINARY RATE OR OTHER RELIEF THE CITY**
12 **SHOULD BE REQUIRED TO FOREGO OR GRANT BACK THE \$18 MILLION**
13 **CITY PAYMENT FOR THREE YEARS. HE ALSO SUGGESTS THAT THE**
14 **CITY SHOULD RESTRUCTURE THE \$45 LOAN OVER THREE YEARS. IS**
15 **THE CITY ABLE TO DO EITHER OF THESE?**

16 A. No, it would not. As I stated in my testimony, the City is capable of granting back the
17 \$18 million on a one time basis only. In addition, if the full \$18 million is needed this
18 year in order to meet PGW's bond coverage requirements, the City will have difficulty
19 making the grant back and may have to go to City Council for an appropriation.

20 Given the City's financial constraints there is simply no way for it to forego \$54
21 million in City payments from PGW (\$18 million for three years) and, at the same time
22 push off repayment of the \$45 loan for three years. The one-time grant back of the \$18
23 million would result in a \$14 million deficit at the end of the City's current five year plan
24 for 2003-2007. That level of deficit can be accommodated if absolutely necessary by
25 making adjustments to the plan. However, the City simply cannot make up a \$54 million
26 hole and forgo receipt of another \$45 million, by tinkering with expenditures and
27 programs here and there.

1 Additionally, the OCA's proposal would creates a significant variation in the
2 City's Five Year Financial Plan FY 2003—FY 2007 which is submitted to and approved
3 by the state pursuant to the Pennsylvania Intergovernmental Cooperation Act ("PICA").
4 The City's PICA Plan expressly states that it is relying on the continued transfer by PGW
5 of the \$18 million payment as well as the repayment of the \$45 million loan in FY 2003.
6 Relevant portions of the PICA Plan are attached hereto as Exhibit JD-R-1. The OCA's
7 suggestion would result in a \$54 million hole in the PICA Plan. Without these revenues,
8 the City will be forced to consider major cuts in City services, lay-offs or a hiring freeze,
9 increases in taxes and fees or a combination of those steps. All of these steps would have
10 to be presented and approved by PICA; the City can't simply decide to forgo or defer
11 these revenues, even if such a plan was approved by City Council.

12 **Q. ARE THERE OTHER FACTORS AFFECTING THE CITY'S FINANCES THAT**
13 **WOULD PROHIBIT IT FROM BEING ABLE TO GRANT BACK \$54 MILLION**
14 **TO PGW AND DELAY THE REPAYMENT OF THE CITY LOAN?**

15 **A.** Yes. I summarized some of those factors, such as the impact of the recession, in my
16 direct testimony. Additional challenges facing the City's fiscal health are discussed in
17 Exhibit JD-R-2, attached hereto, which is from Philadelphia's Five Year Financial Plan
18 FY 2003—FY 2007. However, one of the major additional burdens facing the City at
19 this time, which would make it simply incapable of foregoing three year's worth of City
20 payments from PGW, is the fact that the City will be providing the school district with an
21 additional \$45 million per year as part of our effort, in conjunction with the
22 Commonwealth, to save our schools. As we move forward, the City may well have to
23 consider additional support to PGW, but we simply can't promise to forgo 100% of the
24 City's only return on its investment in PGW; we very simply can't afford it.

1 Q. DOES THAT COMPLETE YOUR REBUTTAL TESTIMONY?

2 A. Yes.

3

EXHIBIT JD-R-1

Docket No. R-000170340002

Janice Davis
Secretary for Financial Oversight &
Director of Finance
Room 1330 - MSB

City of Philadelphia

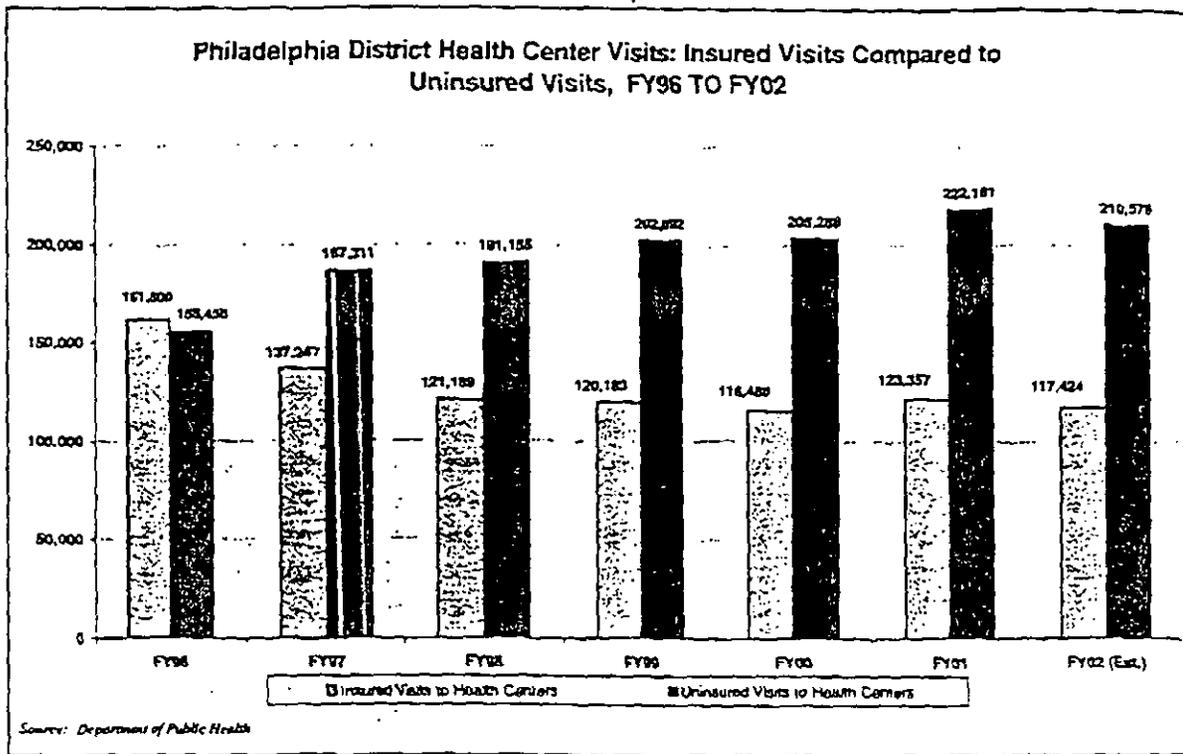


Five-Year Financial Plan

**Fiscal Year 2003 - Fiscal Year 2007
(including Fiscal Year 2002)**

**Eleventh Five-Year Plan for the City of Philadelphia pursuant
to the Pennsylvania Intergovernmental Cooperation Act**

Presented by the Mayor, January 29, 2002



The Financial Crisis of the Philadelphia Gas Works

The Philadelphia Gas Works (PGW), the largest municipally owned gas utility in the nation, has encountered cash flow problems and long-term financial uncertainty in recent years as a result of numerous internal and environmental challenges. These challenges have included:

- Management instability, featuring five different management teams in nine years;
- Costly and inflexible labor agreements;
- Fluctuating natural gas prices, particularly during the winter of 2000-2001 when prices skyrocketed;
- A high proportion of low-income and senior citizen customers that receive discounted rates;
- A high proportion of non-paying customers;
- Severely flawed financial and customer service operations; and
- Failure to receive timely and adequate rate relief from the Pennsylvania Public Utility Commission (PUC).

As a result of these issues, the City was forced to loan PGW \$45 million in FY01 in order to provide sufficient cash to operate until PUC rate relief took effect. Following the loan, PGW made significant progress in meeting these challenges. Most prominently, a new three-year labor agreement is projected to save \$76.5 million over five years. Reductions in natural gas prices and rate relief from the PUC in January, March and October 2001 – albeit less relief than requested by PGW – eased cash flow pressures. Finally, enhancements to the billing and

collections system and to customer service operations have improved revenues and PGW's long-term ability to retain customers. Despite this progress, the financial situation of PGW remains tenuous. This Financial Plan incorporates the continued transfer of PGW's annual \$18 million payment to the City's General Fund, as required by statute, in addition to repayment of the \$45 million loan in FY03. The inability of PGW to meet these obligations to the City would have serious impacts to the City's General Fund and to the fund balances estimated in this Financial Plan.

Each of these contingencies could create substantial strains on the City's budget. A series of factors make it particularly difficult for the City to meet these challenges.

Factors Inhibiting the City's Ability to Meet Fiscal Challenges

Ongoing Loss of Middle Income Population

The 2000 U.S. Census confirmed that Philadelphia continued to lose population in the 1990s. This loss of 68,027 residents, or 4.3 percent of the population, was not as severe as the annual Census estimates had predicted, and it was not as severe on a numeric or percentage basis as the losses of the 1970s and 1980s. While other cities in the region such as Baltimore and Washington, D.C. experienced greater population losses over the same period, major cities in the Northeast and Midwest such as New York City, Boston, and Chicago actually gained population. Census demographic data indicates that the nature of the population loss continues to negatively impact both the City of Philadelphia's tax base and its service demands.

Contrary to regional and national trends, key indicators of economic health continued to deteriorate in Philadelphia between the 1990 Census and the 2000 Census, as shown in the following table. Median household income declined by over seven percent in Philadelphia over this period after adjusting for inflation, while the inflation-adjusted median household income increased in the four Pennsylvania suburban counties, as well as the state and nation as a whole. In addition, the poverty rate in Philadelphia increased over this period, even as it fell in the rest of the state and nation. This data indicates that the net population loss in Philadelphia is disproportionately made up of middle-income residents, leaving behind a population that is proportionately poorer, less able to contribute to the tax base, and more in need of public services.

EXHIBIT JD-R-2

Docket No. R-000170340002

Fiscal Health

Overview

The Street Administration is maintaining the City of Philadelphia's fiscal health during challenging times, even as it continues to reduce taxes, improve the climate for residents and businesses, and make strategic investments in the future of our city, its schools and its neighborhoods. While there are a number of sizable contingencies, including the economic recession, increasing labor costs, and the potential impact of welfare reform, the City's \$230.0 million fund balance at the end of FY01 provided a buffer against those uncertainties. A number of risks that the City had faced for years became realities during FY01, as tax collections slowed in the fourth quarter and the City had to provide an unanticipated \$45 million loan to the Philadelphia Gas Works. The slower than anticipated growth in tax collections coincided with the onset of a national recession in March 2001, the first in ten years. This recession continues to impact the City's budget in FY02, while new large scale costs have also been incurred, such as the costs of responding to terrorism and the City's share of resolving the School District of Philadelphia's financial crisis. While this Plan illustrates how the City will adapt to the major fiscal burdens imposed by the national recession and the financial crisis of the School District of Philadelphia, the City continues to face a number of potential challenges to its fiscal stability.

These challenges include:

- Increasing labor costs and new collective bargaining agreements
- Increasing pension costs
- Increasing criminal justice costs and the response to terrorism
- Effects of welfare reform
- The financial crisis of the Philadelphia Gas Works.

In addition, if the national recession is of greater length or severity than currently forecasted, the revenue estimates described in this chapter will be negatively impacted.

It is particularly difficult for the City to meet these fiscal challenges due to on-going, inter-related pressures on the City's fiscal position, including:

- Ongoing loss of middle income population
- High poverty rates
- Low state government fiscal support
- A weak tax base
- A relatively low level of expenditures and staffing for core city government services, which limits the ability of the City to impose further cuts in those services, and relatively high and increasing expenditures and staffing on mandated, non-core, county government services.

DOCUMENT
FOLDER

PGW E.R.P. St. 6

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

TESTIMONY OF

CRAIG WHITE

DOCKETED
APR 30 2002

ON BEHALF OF

PHILADELPHIA GAS WORKS

PHILADELPHIA GAS WORKS

EXTRAORDINARY RATE PETITION

R-0001734F0002

MARCH 2002

SECRETARY'S BUREAU
APR 12 PM 3:25

Q. PLEASE STATE YOUR NAME AND POSITION WITH THE COMPANY.

A. My name is Craig White. My position is Acting Chief Operating Officer.

Q. HAVE YOU SUBMITTED TESTIMONY IN CONJUNCTION WITH THE BASE RATE CASE?

A. Yes.

Q. DID YOU DISCUSS YOUR JOB RESPONSIBILITIES, WORK EXPERIENCE, AND EDUCATIONAL BACKGROUND IN THAT TESTIMONY?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN SUPPORT OF PGW'S REQUEST FOR EXTRAORDINARY RATE RELIEF?

A. The purpose of my testimony is to discuss how PGW proposes to allocate the \$44 million of extraordinary rate relief that it has requested.

Q. HOW DOES PGW PROPOSE TO ALLOCATE THE EXTRAORDINARY RATE RELIEF IT HAS REQUESTED?

A. The Company proposes to allocate the \$44 million in extraordinary rates, or any lesser amount that the Commission might award, in the same manner as it has proposed to allocate the overall requested base rate increase of \$60 million. I discussed that allocation proposal in my base rate testimony at PGW BRP St. 2.

The proposed allocation for the extraordinary increase (shown on Attachment 1) is generally consistent with the approach PGW supported in its 2001 base rate case. In that case, PGW proposed to increase the charge for residential customers by slightly more than the overall average percentage increase. The Company's proposal was in recognition of the results of our Cost of Service analysis which showed that, at present rates, residential customer total revenues were not covering their allocated costs.

For this increase, in regard to both the extraordinary and base rate increase, we propose to follow the same general methodology for determining the volumetric increase

for each class. As to the extraordinary rate request, we would increase the residential volumetric charge by 11.96% over the total average volumetric increase of 11.46% for an overall extraordinary rate related increase to residential customers of \$34.8 million, or 79% of the requested increase. The difference between \$44 million and the amount recovered from residential customers increase would be spread across the remaining classes on a pro rata basis. This amounts to a 9.91% increase to the remaining firm classes.

Q. HOW DOES THAT PROPOSED ALLOCATION COMPARE TO THE MANNER APPROVED BY THE COMMISSION IN THE COMPANY'S LAST BASE RATE CASE?

A. Under the allocation proposed by PGW, the residential class (Res GS and PHA GS) would receive less of the increase than it otherwise would under the allocation approved by the Commission in PGW's last base rate case. Pursuant to the Commission's December 6, 2001 Order in PGW's last base rate case, the residential class was assigned 91% of the approved \$33.558 million increase between the customer charge and volumetric rate increases (as shown on Attachment 2).

If the extraordinary rate increase was allocated consistent with the Commission-approved method, then the volumetric rates for the residential class would increase by 13.7% and the rate increases for the remaining firm classes would fall within a range of 2.58% to 5.30% (as shown on Attachment 3). The extraordinary rate related increase for the residential class would be \$39.9 million, or 91% of the total amount requested.

Q. DOES PGW SEE ANY FLEXIBILITY ON THE ALLOCATION OF THE EXTRAORDINARY RATE INCREASE?

A. Yes. Obviously, PGW's main concern is for the Commission to grant the needed \$44 million in extraordinary rates. PGW would be willing to revisit and adjust the allocation

of the extraordinary rate relief – on a going forward basis – as part of the final resolution of the base rate case.

Q. DOES THIS COMPLETE YOUR TESTIMONY IN THE EXTRAORDINARY RATE PROCEEDING?

A. Yes.

VOLUMETRIC RATE INCREASE

<u>Rate</u>	<u>Forecasted Applicable Sales</u> 9/1/01 thru 8/31/02 (mcf)	<u>Current Volumetric Charge</u>	<u>Proposed Volumetric Charge</u>	<u>Current Volumetric Revenue</u>	<u>Proposed Volumetric Revenue</u>	<u>Volumetric Revenue Increase</u>	<u>Percentage Increase</u>
ResGS/PHAGS	42,984,183	\$ 6.7770	\$ 7.5875	\$ 291,303,805	\$ 326,142,485	\$ 34,838,680	11.96%
Commercial/GS	10,785,098	\$ 7.1200	\$ 7.8256	\$ 76,789,898	\$ 84,399,863	\$ 7,609,965	9.91%
Industrial/GS	1,468,077	\$ 7.1200	\$ 7.8256	\$ 10,452,708	\$ 11,488,583	\$ 1,035,875	9.91%
PHA/PHA	735,256	\$ 7.1260	\$ 7.8322	\$ 5,239,434	\$ 5,758,672	\$ 519,238	9.91%
MUN/MS	1,294,519	\$ 6.4130	\$ 6.4130	\$ 8,301,750	\$ 8,301,750	\$ -	
Total Applicable Sales	57,267,133			\$ 392,087,596	\$ 436,091,354	\$ 44,003,758	
Applicable to Rate Increase (Res/Com/Ind/PHA)	55,972,614			\$ 383,785,846	\$ 427,789,604		
Rate Increase	\$ 44,000,000						
Overall % Increase	0.1146						
Residential % Increase	0.1196						
Ind, Com & PHA Increase	\$ 9,161,320						
Current Revenue	\$ 92,482,040						
% Increase	0.0991						

ATTACHMENT 1

RATE INCREASE
\$33,558,000

CUSTOMER CHARGE

<u>Rate</u>	<u>Forecasted</u> <u>Applicable Sales</u> 9/1/00 thru 8/31/01 (mcf)	<u>Current</u> <u>Customer</u> <u>Charge</u>	<u>Proposed</u> <u>Customer</u> <u>Charge</u>	<u>Current</u> <u>Customer Charge</u> <u>Revenue</u>	<u>Proposed</u> <u>Customer Charge</u> <u>Revenue</u>	<u>Customer Charge</u> <u>Revenue</u> <u>Increase</u>
ResGS/PHAGS	45,770,982	\$ 8	\$ 12	\$ 45,881,722	\$ 68,822,582	\$ 22,940,860
ComGS/MUNGS	11,078,058	\$ 10	\$ 18	\$ 2,993,006	\$ 5,387,411	\$ 2,394,405
Industrial/GS	1,479,249	\$ 20	\$ 50	\$ 281,600	\$ 704,000	\$ 422,400
PHA/PHA	171,505	\$ -	\$ 18	\$ -	\$ 103,248	\$ 103,248
MUN/MS	1,285,030	\$ -	\$ 18	\$ -	\$ 192,672	\$ 192,672
Total Applicable Sales	59,784,824			\$ 49,156,328	\$ 75,209,913	\$ 26,053,585
Increase in Customer Charge		\$ 26,053,585				
Increase in Rate		\$ 7,506,441				
Total Increase		\$ 33,560,026				

VOLUMETRIC RATE INCREASE

<u>Rate</u>	<u>Forecasted</u> <u>Applicable Sales</u> 9/1/00 thru 8/31/01 (mcf)	<u>Current</u> <u>Volumetric</u> <u>Charge</u>	<u>Proposed</u> <u>Volumetric</u> <u>Charge</u>	<u>Current</u> <u>Volumetric</u> <u>Revenue</u>	<u>Proposed</u> <u>Volumetric</u> <u>Revenue</u>	<u>Volumetric</u> <u>Revenue</u> <u>Increase</u>	<u>Current</u> <u>Total</u> <u>Revenue</u>	<u>Proposed</u> <u>Total</u> <u>Revenue</u>	<u>Percentage</u> <u>Increase</u>	<u>%</u> <u>of Total</u> <u>Increase</u>
ResGS/PHAGS	45,770,982	\$ 6.6130	\$ 6.7770	\$ 302,683,504	\$ 310,189,945	\$ 7,506,441	\$ 348,565,226	\$ 379,012,527	8.74%	90.72%
ComGS/MUNGS	11,078,058	\$ 7.1200	\$ 7.1200	\$ 78,875,773	\$ 78,875,773	\$ -	\$ 81,868,779	\$ 84,263,184	2.92%	7.13%
Industrial/GS	1,479,249	\$ 7.1200	\$ 7.1200	\$ 10,532,253	\$ 10,532,253	\$ -	\$ 10,813,853	\$ 11,236,253	3.91%	1.26%
PHA/PHA	171,505	\$ 7.1260	\$ 7.1260	\$ 1,222,145	\$ 1,222,145	\$ -	\$ 1,222,145	\$ 1,325,393	8.45%	0.31%
MUN/MS	1,285,030	\$ 6.4130	\$ 6.4130	\$ 8,240,897	\$ 8,240,897	\$ -	\$ 8,240,897	\$ 8,433,569	2.34%	0.57%
Total Applicable Sales	59,784,824			\$ 401,554,572	\$ 409,061,013	\$ 7,506,441	\$ 450,710,900	\$ 484,270,926		100.00%

VOLUMETRIC RATE INCREASE

\$44 Million Rate Increase Allocated by Percentage From 2001 Rate Increase

<u>Rate</u>	<u>Forecasted Applicable Sales</u> 9/1/01 thru 8/31/02 (mcf)	<u>Current Volumetric Charge</u>	<u>Proposed Volumetric Charge</u>	<u>Current Volumetric Revenue</u>	<u>Proposed Volumetric Revenue</u>	<u>Volumetric Revenue Increase</u>	<u>% Increase</u>	<u>% of Total Increase</u>
ResGS/PHAGS	42,984,183	\$ 6.7770	\$ 7.7057	\$ 291,303,805	\$ 331,223,216	\$ 39,919,410	13.70%	90.72%
CommercialGS	10,785,098	\$ 7.1200	\$ 7.4111	\$ 76,789,898	\$ 79,929,440	\$ 3,139,542	4.09%	7.14%
Industrial/GS	1,468,077	\$ 7.1200	\$ 7.4972	\$ 10,452,708	\$ 11,006,467	\$ 553,759	5.30%	1.26%
PHA/PHA	735,256	\$ 7.1260	\$ 7.3101	\$ 5,239,434	\$ 5,374,795	\$ 135,361	2.58%	0.31%
SubTotal Applicable Sales	55,972,614			\$ 383,785,846	\$ 427,533,917	\$ 43,748,072		
MUN/MS*	<u>1,294,519</u>	\$ 6.4130	\$ 6.6081	<u>\$ 8,301,750</u>	<u>\$ 8,554,311</u>	<u>\$ 252,561</u>	3.04%	<u>0.57%</u>
Total Applicable Sales	57,267,133			\$ 392,087,596	\$ 436,088,228	\$ 44,000,632		100.00%

* Pending City Council approval

Rate Increase \$ 44,000,000

DOCUMENT
FOLDER

POCKETED
APR 30 2002

PGW CROSS EXAM. EXH. 1

R-00017034F0002

3/26/02

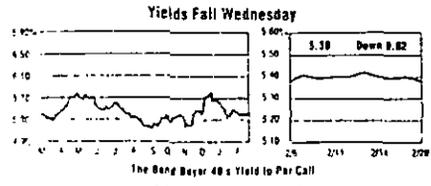
Plth, PA

AKS

RECEIVED
02 APR -2 PM 1:55
12:11:00
SECRETARY'S BUREAU

BB 00120844 0503 BE191107
 JOHN WHITE
 PUBLIC FINANCIAL MGMT
 18TH & ARCH STREETS
 2 LOGAN SQUARE SUITE 1500
 PHILADELPHIA PA 19103-2707

The Digest



Underwriters won \$1 billion of California general obligation bonds in tight competitive bidding yesterday and reoffered the loan with a top yield of 5.27% in 2032, overshadowing the secondary market, where prices were firm in light trading. *Complete market coverage by Sean Munsarrat and Nicholas Chesko appears on page 2*

California Power Bond Deal Shrinks

The California Department of Water Resources is now expected to issue \$10.85 billion in power purchase revenue bonds, state Public Utilities Commission president Loretta Lynch said yesterday. Previously, the state expected to sell between \$12 billion and \$13 billion in bonds. The PUC is expected to vote on three items today that would allow the DWR to market its power revenue bond issue, which has been anticipated since last year. Under a new financing plan, the bonds would mature in 19 to 21 years, rather than 15 years, to provide more cash up front to pay back the state general fund, according to Lynch. The general fund loaned about \$6 billion to the department early last year for power purchases and needs the money to help balance its budget. State Treasurer Philip Angelides said last year the bonds would mature over 15 years under a different structure. The PUC is expected to vote today on a rate agreement that would establish separate charges on utility customer's bills to cover bond-related costs and operations of the power program. "I believe it's a go," Lynch said. She was one of four commissioners on the five-member board who rejected the previous financing plan in October. The PUC is also expected to approve DWR's revenue requirements for the past and current year and may amend a ruling that cuts off large customer's ability to buy power from a provider other than the local utility.

— Deborah Finestone

Underwriters & Dealers

CLAYTON B. ERICKSON, vice president and manager for municipals at St. Louis-based A.G. Edwards & Sons Inc., is retiring at the end of the month along with four other fixed-income officers as part of a voluntary retirement program intended to cut costs at the firm. *Page 7*

Listings

- New-Issue Calendar *Pages 8-12*
- Requests for Proposals *Page 12*
- Notices of Sale *Pages 15-17*
- Employment Opportunities *Pages 21-23*
- Bond Redemptions *Pages 25-26*
- Market Statistics *Pages 34-37*

<http://www.bondbuyer.com>

MSRB Plans G-37 Changes Automatic Exemption Possible in Some Cases

By Lynn Hume

WASHINGTON — The Municipal Securities Rulemaking Board plans to propose several revisions to its Rule G-37 on political contributions late next month, and market sources say they expect those revisions will include a provision automatically exempting broker-dealers from the rule's two-year ban on business under certain limited circumstances.

The board, which met late last week in Puerto Rico, also plans to increase price transparency in the market in late May or early June by lowering the threshold of frequently traded securities to mean those securities traded three rather than four or more times a day, according to Ward Marsh, the MSRB's chairman, and Christopher Taylor, the board's executive director. The two briefed reporters on the results of the meeting in a telephone conference call yesterday.

Currently the board issues daily reports containing the trade data from municipal securities that traded frequently the previous day. At the same time, the board — as a result of the Sept. 11 terrorist attacks — plans to delay by a year to mid-2004 plans to move to real-time reporting of trade data.

In other actions, the board will to propose a new Rule G-40 to spur electronic communications in the municipal market and will file with the Securities and



MSRB chairman Ward Marsh says Rule G-37 is complex and its provisions are "inextricably interwoven."

Exchange Commission a new professional qualification category for firms whose municipal securities business is limited to selling municipal fund securities, Marsh and Taylor said.

Marsh, a managing director of Salomon Smith Barney Inc.'s municipal securities division, said board members agreed to propose revisions to G-37 to ensure that the seven-year-old rule will

Please turn to MSRB page 44

Warm Winters, Debt Burden Push Philadelphia Gas Works to Brink

By Martin Z. Braun

Yesterday, the forecast was for 62 degrees in Philadelphia, but officials at the Philadelphia Gas Works were not enjoying the balmy weather.

Instead, top management of the chronically cash-strapped and highly leveraged city-owned utility were busy preparing to file an approximately \$50 million emergency base-rate relief request with the state's Public Utilities Commission tomorrow.

"The weather is killing us," said Harvey Clark, a spokesman for PGW. "Nobody's turning those thermostats on."

Without significant rate relief, PGW's barely investment grade rating could be in jeopardy, said analysts with Moody's Investors Service and Standard & Poor's. PGW has nearly \$1 billion in out-

standing debt, a debt burden that has grown 30% since 1994.

As if a crushing debt burden and a string of unusually warm winters were not enough, PGW labors under uncertainty about its top management and a troubled collection history. Approximately 20% of the utility's customer base is poor, and uncollected accounts rose to \$184 million last year from \$129 million in 2000. When the utility installed a new billing system two years ago, more than 30,000 customers were not billed for four months.

"Given their current financial profile, they don't look investment grade," said Anesh Prabhu, a Standard & Poor's analyst. "If they don't get further relief than the \$33 million they got [from the PUC last year], their ratings aren't tenable."

Last month, in a stark sign of

Please turn to Philadelphia page 44

California Needs to Cut Another \$5B

State Analysts See Ever-Larger Shortfall

By Rochelle Williams

SAN FRANCISCO — Citing continued revenue weaknesses in the California economy, the state Legislative Analyst's Office yesterday said an additional \$5 billion in cuts are needed to address budget shortfalls for the current year and fiscal 2003.

Elizabeth G. Hill, the LAO analyst, projects a budget shortfall of \$14.5 billion, up from the \$12.5 billion originally identified by her office in November, and she offered suggestions for reductions including limiting the deductions on mortgage interest to stepping up the elimination of exemptions on capital gains upon death. The state's overall fiscal 2003 budget is \$100 billion and the fiscal 2003 general fund is about \$79 billion.

In a radio talk show yesterday, Gov. Gray Davis said he thought Hill's figures were "high."

The governor said he instituted a hiring freeze, made \$3 billion worth of cuts mainly from this fiscal year, and requested lawmakers to cut the budget by \$2 billion, which was done. He also supports state Treasurer Philip Angelides' debt-refinancing plan, which is expected to produce a cost savings of \$2 billion

Please turn to California page 44

Southeast Public Finance Conference



Tennessee bond finance director Mary-Margaret Collier discusses the unique problems facing her state. *Page 4*

To subscribe to The Bond Buyer, call 800-982-0633.

apped California Considers Options to Cope With Shortfall

Continued from page 1

due to low-interest rates on loans.

"But the bottom line is everyone in Sacramento knows we have an obligation to balance the budget and we'll get the work done. It's very hard to make predictions because this economy is bumping along here," Davis said. He expects May will reveal final revenue numbers to adjust the budget.

The LAO, an independent audit office, yesterday identified 100 "options" as solutions for expenditure reductions and raising revenues to aid the governor and state lawmakers in formulating the budget, they include cutting a state holiday, and early release of nonviolent inmates.

None of the options comes without a negative impact, according to the report, but "in better fiscal times, we would not necessarily put such options on the table. However, we offer them in the context of a need to solve a growing budget shortfall," she wrote in the analysis.

One option is a one-time \$300 million deferral on the Traffic Congestion Relief Fund loan to the general fund. Last fiscal year, the traffic congestion relief fund received \$2 billion from the general fund, sales taxes, and motor vehicle fuel taxes.

"Of this amount, \$400 million was allocated to cities and counties for local streets

and roads, leaving \$1.6 billion available for 141 projects in the Traffic Congestion Relief Program," according to the report. "Because the majority of the TCRF money is for project construction that will not occur in the near term, TCRF does not need such a large cash balance at this time."

Another alternative is increasing nonresident student fees at public universities. That action could raise an estimated \$6 million and could decrease general fund support for the same amount.

Another suggestion is to transfer revenue from the state highway account to the general fund on a one-time basis. Shifting the funds would not impact transportation projects immediately but will reduce the amount of money available for future transportation projects.

Sandy Harrison, assistant director of the state Department of Finance, said his office will closely examine every option listed in the report, "but at this point it is too soon for us to endorse or throw it out. We have to look at them in context of the big picture and figure it out."

The LAO announcement came as the state sold \$1 billion in general obligation bonds. The loan captured a fair amount of the focus of market participants, but had minor impact on the broad market.

Moody's Investors Service rates Califor-

nia general obligation bonds A1. Standard & Poor's assigns an A-plus rating to the state's GOs. Fitch Ratings rates the GOs AA.

Steve Zimmermann, a managing director at Standard & Poor's, said his agency has had discussions with state officials about revenues and expenditures.

"We are looking for the elected officials to take appropriate action for 2002-03," Zimmermann said.

Claire Cohen, vice chairman at Fitch, said she was gratified by the steps California

made to reduce expenditures this current year. January was "terrible" for California, which found personal income tax about \$800 million below budget forecasts, she said.

"Clearly, to reduce your expenditures is one way to absorb the loss, unless they have discovered something new," Cohen said. "All of the capital gains and bonuses, the conventional wisdom is that it is not going to come back. It is gone. If it is gone, you have to lower expenditures to balance it or raise revenues." □

Highly Leveraged Philadelphia Gas Works Threatens to Tumble Into Junk Territory

Continued from page 1

PGW's poor liquidity position, the utility was forced to borrow \$20 million from its capital fund account to pay debt service, according to a recent Standard & Poor's report. Without rate relief or additional project revenues, PGW may be unable to reimburse its capital fund, the report said.

So far, the utility has lost \$23 million in revenue this winter and is faced with repaying a \$45 million city loan in January. The utility is asking the City Council to defer the loan until August 2003.

Meanwhile, the city failed to meet a Dec. 31 deadline to install a permanent management team at PGW, a condition set forth by the PUC when it took over the regulation of the utility in July 2000.

"If the utility does not get that base-rate increase and is required to pay back the city loan, the stress on the utility's liquidity will be significant," said Dan Aschenbach, a Moody's analyst. "It's very possible that at that point the rating could be in trouble."

Despite some recent financial and operational improvements — including favorable labor contract settlements and limited base-rate increases — Aschenbach said the city's failure to appoint permanent management was a real concern.

"This type of management instability has been part of the problem for a number of years," he said. Aschenbach was unsure whether the city's inability to meet the deadline for appointing a permanent management team would affect the PUC's rate-making decision.

In July 2000, the PUC took over regulation of PGW following years of disappointing performance and a corruption scandal that led to the indictment of four top managers for charges ranging from credit-card abuse to fraud. In the last seven years, the gas works has had seven leaders.

Moody's rates the PGW's senior debt Baa2 and its subordinated debt Baa3 with a negative outlook on both. Standard & Poor's assigns a triple-B rating on the senior bonds and a triple-B-minus on the subordinated debt and has the debt on CreditWatch with negative implications. Fitch Ratings assigns a triple-B-plus rating to PGW's senior debt and a triple-B to its junior debt.

Fitch analyst Richard Larkin said that regardless of the PUC's decision, the agency would not adjust its rating.

"It's bouncing along at the triple-B level, and we'll continue to watch it," he

said. "We expect things are not going to run smoothly for them but we still continue to feel that they're going to be able to pay their debts."

Thomas Knudsen, interim PGW president, said he was optimistic that the PUC would grant significant relief.

"The consequences to their not doing this level of rate relief that we need is so horrific, that I don't think they'll want to pay that cost. The lowest cost solution for the customer is to give us the money now, because not to do so is going to raise capital costs," Knudsen said.

Last year, the PUC granted \$33.6 million in rate relief after PGW requested a \$65 million base rate increase. Base rates pay for debt-service payments, operating expenses, and annual payments to the city. In 2000, PGW requested a \$52 million rate increase from the PUC and received \$11 million.

Between 1992 and 2000, when PGW was regulated by the Philadelphia Gas Commission, customers did not see base-rate increases at all. City officials, said Clark, were unable or unwilling to increase rates for political reasons.

Although Mayor John Street has hired Lehman Brothers to study the possibility of selling off the utility, the long-awaited privatization study has not been released.

"The longer we wait, the less value the asset has and the more problems it's going to have," said City Councilman James Kenney. In the past, he said, PGW has used capital dollars for operating expenses, a dangerous practice both financially and in terms of citizen safety.

"There is a desire in this government, politically, to hold onto those entities that can continue to get bond work from, pinstripe patronage from, and use it as a political tool," he said. "That's one of the reasons why the company is in the condition it's in."

Joyce Wilkerson, chief of staff for the mayor and a PGW board member, did not return calls seeking comment.

According to the recent Standard & Poor's report, PGW had \$3.8 million cash on hand in December, compared to an ending cash balance of \$8.1 million in August 2000. Moody's calculates PGW's total debt-service coverage, including its city loan obligation and subordinate liens, at .90 times coverage. The utility's debt ratio, net funded debt to net fixed assets, was 83.1% in 2001, according to Moody's annual credit review. □

MSRB Plans Changes to Rule G-37; 1-Time Reporting Pushed Back

Continued from page 1

not have unintended consequences in today's environment. But Marsh said that neither he nor Taylor will discuss details of the proposals until next month after the staff drafts the proposed changes and board members review them again.

"While we have made decisions about what we think ought to be changed in G-37, the rule is complex and its provisions are 'invariably intertwined,'" Marsh said. "We want to make sure that we don't create unintended consequences in the way the drafting is structured or the message is delivered."

"We just want one more really thorough look at this once the notice is prepared," said Taylor.

However, sources said they expect the board to propose providing firms with an automatic exemption from the two-year ban if a firm has a good system in place for complying with the rule but discovers an inadvertent contribution to an issuer official soon after it was made and obtains an immediate refund. Both The Bond Market Association and the National Association of Securities Dealers have urged the MSRB to allow an automatic exemption under such circumstances.

G-37, which took effect in April 1994, was designed to prevent municipal broker-dealers from engaging in pay-to-play practices. Under the rule, dealers generally are banned from engaging in any negotiated municipal securities business with an issuer for two years if "for one of their municipal finance products makes a significant political contribution to an issuer official who could influence the award of bond business.

Taylor said the board hopes to propose the revisions in late March, seek public comments over a 60-day period, and then review those comments at its meeting in July. If the board can agree on final revisions at that meeting, it

will then file the proposals with the Securities and Exchange Commission, which must also seek comments on them and then approve them before they go into effect.

On price transparency, Taylor said that by lowering the threshold of what is meant by frequently traded municipal securities, the board will increase the amount of municipal securities trade data it is releasing on a daily basis. The change will mean the board will report trade data for about 55% or \$5.23 billion of the \$9.5 billion of par value traded per day, instead of the current \$3.90 billion or 41% of that amount, he said. The expanded data will cover 54% or 14,040 of the average 26,000 transactions that occur each day (up from the current 42% or 10,920 transactions) and 26% or 2,600 of the average 10,000 individual securities traded each day (up from the current 11% or 1,100 securities), he said.

The new Rule G-40 to be proposed by the board will require broker-dealers in the municipal market to provide the MSRB with e-mail addresses, Taylor said. "Communications with the industry from now on will be done electronically" whenever possible, he told reporters.

In other action, the MSRB will soon file with the SEC a proposal to create a new professional qualification category for firms whose sole municipal securities activity is selling municipal fund securities for college savings programs or state and local government investment pools. These firms' employees will be permitted to qualify as municipal fund securities limited principals under the new category, or as municipal securities principals under the MSRB's Series 53 test. In addition, the board will extend to December from August transition rules allowing general securities principals or investment company limited principals to sell municipal fund securities. □

DOCUMENT
FOLDER

DOCKETED

APR 30 2002

PGW – KNUDSEN REBUTTAL EXH. 1

R-00017034F002

PGW Answers to:

OTS-RS-1

OTS-RS-6

OCA-II-3

3/26/02

Phila OA

mg

PA.P.U.C.
SECRETARY'S BUREAU

02 APR - 2 PM 1:55

RECEIVED

3

**RESPONSE TO OFFICE OF TRIAL STAFF DATA REQUEST REGARDING
PGW'S RATE PROCEEDING**

- Question OTS-Set I-RS-1:** Refer to page 7 of the Petition, paragraph C:
- a.) Provide a list of the marginal services, relating to customers, that would be reduced based on the downgrade
 - b.) What impact would this have on PGW's service to its customers?
 - c.) Describe how "marginal services" relate to "safe and reliable" service to PGW's customers.

Response Provided By: Thomas E. Knudsen, Interim Chief Executive Officer

- Response:**
- a.-b.) The premise on which the discussion in the petition and in Mr. Knudsen's testimony is based is that PGW's bonds will have been downgraded, there will be no forward purchase agreement to offset weather related losses in FY 2002, there will be no Letter of Credit but an immediate requirement to pay \$50 to \$80 million to the participating banks and there will be no bond sale in December to fund capital projects. PGW will be in the position of having to conserve all cash sources for essential services and emergent situations.

In this context, management will attempt to sustain gas service to the maximum number of customers for the longest time possible. At this writing the operational details of such a retrenchment are being developed. See the response to OCA Set II - 3 for a more detailed discussion and rationale for company-wide steps.

Examples of customer-related services that would have to be reduced and their impact would include:

Parts and Labor Plan

- suspend the program activities immediately
- Appliance repair to low income and the elderly, suspend this essential service completely

Call Center

- reduce to bare minimum to handle emergency calls

District Offices

- close all facilities and find alternative methods for payments and various customer program enrollments

Collection efforts for non-paying customers

- seek exemption from restrictive tariff conditions and suspend all efforts on the assumption that only those who pay or seek payment arrangement retain service

Dispute Resolution and Customer Response Units

- suspend all operations and investigative activities

Low income outreach programs

- eliminate all activities

New customer service line installations

- suspend all non-safety related construction

Restructuring

- suspend all activities involving conversion to Chapter 56 and implementation of the Choice Act including the web site

Project Management Officer

- suspend all activities for further refinement of BCCS

AMR battery replacement

- suspend all activity and rely on estimated billing

Gas theft investigation

- suspend program

- c.) All of the above activities affect the level of service provided to customers and the steps outlined will result in PGW not being able to continue to provide its present, normal level of service. Actual loss of service could result from these changes, as well, raising serious questions of safety and reliability. For example, if appliance repairs are not made (because PGW repairs systems which no contractors will fix due to age or parts which PGW personnel still continue to fabricate) people will seek other means to keep warm. Or, if we must close the District Office and people lose service for want of payment arrangements or the company's ability to service accounts through the Call Center or Collections Department is impaired and customers are dropped from the system, safety, again, is an

issue as people seek alternatives. This service territory has, and this utility serves, the heating and cooking needs of 50% of the low income population of the state. They have limited means, live in old structures, have special needs and PGW has the structure, developed over many years, to sustain these customers in their homes. The dismemberment of the part of the social safety net which PGW's services represent will lead to people doing what they must: electric stove doors open, kerosene heaters, illegal gas connections, etc. PGW deals with these issues now. After a downgrading, and without PGW's ability to address these concerns, the circumstances will be disastrous. Obviously, reductions in Call Center coverage and response time will directly affect PGW's present (very high) level of performance in that area. The same is true for every issue listed in a) and b) above.

**RESPONSE TO OFFICE OF TRIAL STAFF DATA REQUEST REGARDING
PGW'S RATE PROCEEDING**

Question OTS-Set I-RS-6: Refer to the last line on page 8, paragraph 14. of the Petition. Provide a schedule listing the procedures the Company will implement, in terms of priority, if the Commission does not grant the Company's petition.

Response Provided By: Thomas E. Knudsen, Interim Chief Executive Officer

Response: While all of these actions would be taken more or less in a short time frame, the approximate order of major action steps to be taken by management is the following:

- a.) Seek the \$45 million deferral of the City loan until August, 2003
- b.) Immediately stop all non-essential spending
- c.) Deplete the gas storage inventories rather than expending cash on purchases of flowing gas
- d.) Request the Commission to invoke the regulatory exemption clause in the Collective Bargaining Agreement to permit lay offs, furloughs and the working on live gas by other than PGW personnel.
- e.) Request the Commission to alter tariff rules allowing more aggressive collection practices.
- f.) Implement changed collection practices
- g.) Eliminate all systems development programs and special initiatives such as deregulation, BCCS modifications, cost reduction initiatives, etc.
- h.) Suspend efforts to file restructuring proceeding
- i.) Lay-off or furlough personnel and re-dispatch remaining personnel according to plan which supports the new mission. These would include
 - Customer Affairs (See OTS-Set I-RS-1)
 - Field Services (See OTS-Set I-RS-4)
 - Distribution
 - Management
 - Support Services: IT, HR, Finance, Legal, Building Services, etc.
- j.) Eliminate all non-payroll spending/services not related to the revised mission of providing gas, billing and collecting, only, while recognizing some need for additional contracting especially in Distribution.

- k.) Cancel all contracts not related to PGW's mission invoking force majeure clauses or equivalent, if available.
- l.) Eliminate all capital projects that do not involve safety or reliability in an effort to conserve remaining cash balances, and funds for construction necessary to maintain the distribution system in a safe and minimally reliable manner.

RESPONSE TO OFFICE OF CONSUMER ADVOCATE DATA REQUEST
REGARDING PGW'S RATE PROCEEDING

- Question OCA-Set II-3:** Regarding the testimony of Thomas E. Knudsen, please quantify the possible savings to ratepayers and/or the company of the following actions:
- a.) deferral of payment of the \$45 million short term loan
 - b.) depletion of gas inventories which are presently unit priced above current market rates
 - c.) reduced construction program
 - d.) hold on unnecessary spending
 - e.) shrinking the operations of the utility
 - f.) cut back substantially or eliminate servicing appliances
 - g.) redeployment of field service personnel to essential maintenance services only
 - h.) stop work on the deregulation initiative
 - i.) suspend district offices
 - j.) cut staff and all non-essential expenditures on personnel
 - k.) cut all nonpayroll discretionary spending

Response Provided By: Thomas E. Knudsen, Interim Chief Executive Officer

Response: The premise of the question is that by PGW implementing a "doomsday" scenario there will be "savings" for the ratepayer. In this scenario there is no assumption of a change in rates. Ratepayers will not save. Only additional costs will be added. Any "savings" realized are those in cash and conserved expenses necessary to keep PGW operating as long as possible at the expense of normal, continued operations. The overall plan, at present, would be to attempt to assemble an incremental cash flow approaching \$100 million dollars. It must be appreciated that the true costs of a degradation or elimination of the services that PGW provides the citizens of Philadelphia cannot be truly estimated.

The response below delineates actions which management will take to reduce operational and capital investment expenditures to the lowest level possible so as to (1) conserve cash and (2) operate PGW as long as possible until some solution, of undetermined origin, presents itself. Lest there be any misunderstanding, PGW would be facing the equivalent of bankruptcy if management must act to implement the program below. Also see responses to OTS Set I-RS-1, 3 and 6.

- a.) the \$45 million loan is interest free; thus deferral would provide PGW implicit value but no new cash or expense savings.
- b.) the depletion of gas inventories, if effected within the next few weeks, would preserve PGW \$4-6 million in working capital.
- c.) PGW's analysis indicates that it has approximately \$35-40 million in annual construction that must be incurred to maintain the system in safe and minimally reliable levels. PGW would stop all construction that does not fit into these strict requirements. Because PGW will have no way of knowing when it would be able to access the capital markets for the level of borrowing needed to maintain safe and reliable service, PGW would have to engage this emergency plan for an indeterminate period. The reduction in the construction conserves cash for potential emergencies and to fund this critical investment. A benefit is investment earnings on unspent funds at fiscal year end.
- d.) by placing a hold on unnecessary spending defined as no new hires, no promotions, no new contracts, elimination of nonessential purchases, training, etc. management hopes to realize a reduction in costs of \$1 million/month from budgeted non-commodity expense levels. This amount would be subsumed within the savings identifies in e.) below once the downsizing action was taken
- e.) shrinking the operations of the utility is the most complex of the proposed steps requiring careful study and addressing a myriad of legal, safety and contractual questions. As a general matter, there would be targeted layoffs in the range of 400-500 persons with concomitant "savings" of \$24-\$30 million less approximately \$5-6 million in unemployment costs (PGW self-insures) and required outsourcing. The areas most directly affected would be management ranks (100), Customer Affairs (80), Field Services (150), Distribution (50), general support services (120): transportation, buildings and maintenance, IT, PMO, marketing, legal, corporate communications, etc. Management would look to eliminate an additional \$5-10 million in non-labor expenditures beyond the public commitments already made to reduce all cost levels by \$25 million between FY 2000 and 2003.
- f.) a cut back in appliance repair (non-Parts and Labor Plan) would "save" \$1.5 million of direct costs. Again, these costs are subsumed within the estimates in e.) above.
- g.) the concept of redeployment of Field Service personnel assumes the elimination of all customer support-type

services, attenuation of turn on and shut off work, no survey work, no meter calibration work, etc. Attention would shift to basic system maintenance.

- h.) it is currently estimated that the restructuring initiative will ultimately cost PGW approximately \$5 million. All work would be discontinued.
- i.) elimination of the district offices would save \$4-5 million of direct costs but are included in e.) above.
- j.) cutting staff and non-essential expenditures on personnel is addressed in e.) above.
- k.) cutting non-payroll costs is also addressed in e.) above. An additional charge that is also targeted is Bad Debt Expense on the theory that rigid enforcement of the tariff and relief from putting people back on the system who do not pay their bills (CRP customers or customers who now receive "payment plans" under Chapter 56) would provide a substantial benefit. A rough estimate is that PGW could save several million by this last step.

R-00017034F0002
3/26/02 Philo, PA RJS

Operating Margin Lost Due to Weather

	Base Case Rate Increase	Act/Est 2001-02 6 & 6	6 & 6 Over/Under Base Case	Non Fuel Margin	Gain/(loss)
NON HEAT					
RESIDENTIAL/CRP/PHA	2,049,647	1,917,528	(132,119)	\$3.5970	(\$475,232)
COMMERCIAL	1,819,996	1,762,683	(57,313)	\$3.9400	(\$225,813)
INDUSTRIAL	504,213	441,585	(62,628)	\$3.9400	(\$246,754)
MUNICIPAL	273,714	224,226	(49,488)	\$3.2330	(\$159,995)
TOTAL NON HEAT	4,647,570	4,346,022	(301,548)		(\$1,107,794)
HEATING					
RESIDENTIAL/CRP/PHA GS	40,934,787	34,341,386	(6,593,401)	\$3.5970	(\$23,716,463)
COMMERCIAL	8,965,102	7,517,462	(1,447,640)	\$3.9400	(\$5,703,702)
INDUSTRIAL	963,864	799,088	(164,776)	\$3.9400	(\$649,217)
MUNICIPAL	1,020,805	813,219	(207,586)	\$3.2330	(\$671,126)
PHA PHA	735,004	594,769	(140,235)	\$3.9460	(\$553,367)
TOTAL HEAT	52,619,562	44,065,924	(8,553,638)		(\$31,293,875)
TOTAL TOTAL	57,267,132	48,411,946	(8,855,186)		(\$32,401,670)

DOCUMENT
FOLDER

BOGNETE
APR 30 2002

R-00017034 F0002
3/26/02

PHILADELPHIA GAS WORKS
FISCAL YEAR 2001-02
PROJECTED INCOME STATEMENT

PHILADELPHIA GAS WORKS
FISCAL YEAR 2001-02
PROJECTED DEBT SERVICE COVERAGE

Revised 3-25-02	Revised 3-25-02	Current	\$44.0 M	\$18.0 M
	Estimate	Estimate	Test Year	Test Year
	2001-02	2001-02	2001-02	2001-02
Operating Revenues				
Gas Revenues	\$672,188	\$672,188	\$638,733	\$638,733
Margin Loss Gas Sales	(48,800)	(25,000)		
Proposed Base Rate Incr.	8,000	-	44,000	18,000
Other Revenues	27,550	27,450	28,117	27,817
Total Operating Revenues	\$658,938	\$674,638	\$710,850	\$684,550
Operating Expenses				
Natural Gas Costs	\$373,016	\$373,016	\$334,566	\$334,566
Raw Material Exp.	10	10	10	10
Total Nat. Gas & Raw Mat	\$373,026	\$373,026	\$334,576	\$334,576
Contribution Margins	\$285,912	\$301,612	\$376,274	\$349,974
Supply & Field Expenses	\$58,331	\$58,331	\$59,331	\$59,331
Customer Services	29,722	29,722	30,222	30,222
Bad Debt Expense	56,553	54,553	52,544	51,794
Marketing	4,000	4,000	5,596	5,596
Administrative & General	39,086	39,086	39,086	39,086
Health Insurance	31,490	31,490	30,490	30,490
Capitalized Benefits & A&G	(12,430)	(12,430)	(13,430)	(13,430)
Amortization	3,965	3,965	3,965	3,965
Pensions	6,000	3,091	3,091	3,091
Taxes	6,054	6,054	6,054	6,054
Added Costs PUC & Other	0	0	10,000	10,000
Labor/Cost Savings	(7,100)	(7,100)	(7,100)	(7,100)
Total Oper. & Maint.	\$215,671	\$210,762	\$219,849	\$219,099
Depreciation	\$31,585	\$31,585	\$31,587	\$31,587
Total Oper. & Maint. Exp.	\$247,256	\$242,347	\$251,436	\$250,686
Total Operating Expenses	\$620,282	\$615,373	\$586,012	\$585,262
Operating Income	\$38,656	\$59,265	\$124,838	\$99,288
Other Income	32,463	4,963	5,743	5,543
Income Before Interest	\$71,119	\$64,228	\$130,581	\$104,831
Interest				
Long-Term Debt	\$50,966	\$50,966	\$50,966	\$50,966
Other	6,148	6,148	6,498	6,498
AFUDC	(775)	(775)	(775)	(775)
Loss on Extinguished Debt	3,976	3,976	3,976	3,976
Total Interest	\$60,315	\$60,315	\$60,665	\$60,665
Net Income	\$10,804	\$3,913	\$69,916	\$44,166
City Payment	18,000	18,000	18,000	18,000
Net Loss From Operations	(\$7,196)	(\$14,087)	\$51,916	\$26,166

Debt Service Calculation	Revised 3-25-02	Current	\$44.0 M	\$18.0 M
	Estimate	Estimate	Test Year	Test Year
	2001-02	2001-02	2001-02	2001-02
Funds Provided				
Operating Revenues	\$658,938	\$674,638	\$710,850	\$684,550
Other Income +/-				
Restricted Funds	32,463	4,963	5,743	5,543
AFUDC	775	775	775	775
Total Funds Provided	\$692,176	\$680,376	\$717,368	\$690,668
Funds Applied				
Fuel Costs	\$373,026	\$373,026	\$334,576	\$334,576
Other Operating Exp.	247,256	242,347	251,436	250,686
Less: Non-Cash Exp.	(36,165)	(36,165)	(36,165)	(36,165)
Total Funds Applied	\$584,117	\$579,208	\$549,847	\$549,097
Funds Available To Cover Debt Service	\$108,059	\$101,168	\$167,521	\$141,771
1975 Debt Service	\$55,528	\$55,528	\$55,528	\$55,528
Coverage Ratio	1.95	1.82	3.02	2.55
Funds Available To Cover Capital Leases	\$52,531	\$45,640	\$111,993	\$86,243
Funds Available To Cover	\$46,577	\$39,686	\$106,039	\$80,289
1998 Sr. Debt Service	30,926	30,926	30,926	30,926
Coverage Ratio	1.51	1.28	3.43	2.60
Funds Available To Cover 1998 Subordinate Debt Ser.	\$15,651	\$8,760	\$75,113	\$49,363
Coverage Ratio	7.88	4.41	37.82	24.86
Revised Standard & Poor's Fixed Charge Coverage Ratio				
Net Available To Service				
Aggregate Debt Service	\$109,433	\$102,542	\$168,897	\$143,147
Aggregate Debt Service	\$94,394	\$94,394	\$94,394	\$94,394
Fixed Rate Coverage Ratio on Aggregate Debt Service	1.16	1.09	1.79	1.52
Fixed Rate Coverage Ratio Including \$18.0 M City Fee	0.97	0.91	1.50	1.27
Fixed Rate Coverage Ratio Including \$18.0 M City Fee & \$20.0 M TXCP Payment	0.83	0.77	1.28	1.08

Phila, PA
RLS

DOCUMENT
FOOTPRINT

DOCKETED
APR 30 2002

Pennsylvania Public Utility Commission
v.
Philadelphia Gas Works
Docket No. R-00017034F0002

OCA Cross-Examination Exhibit No. 1

Dated:

3/26/02

Phils Pls RJ

DOCKETED

APR 30 2002

DOCUMENT
FOLDER

RECEIVED
02 APR - 2 PM 1:55
P.U.C.
SECRETARY'S BUREAU

RESPONSE TO OFFICE OF SMALL BUSINESS ADVOCATE
DATTA REQUEST REGARDING PGW'S RATE PROCEEDING

Question OSBA-Set II-5: Please provide copies of all ratings reports and related analyses of PGW by Standard and Poors over the past two calendar years.

Question OSBA-Set II-6: Please provide copies of all ratings reports and related analyses of PGW by Moody's Investor Services over the past two calendar years.

Question OSBA-Set II-7: Please provide copies of all ratings reports and related analyses of Fitch Services over the past two calendar years.

Response Provided By: Barbara Bisgaier

Response: Please see the attachments to Barbara Bisgaier's response to OCA Set 1- 10 and the attachments to this response.

Date Provided: March 13, 2002

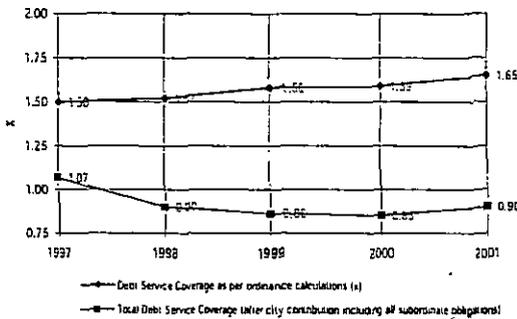


Philadelphia Gas Works

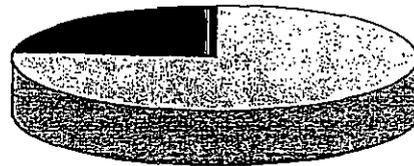
Ratings & Contacts

Category	Moody's Rating	Analyst	Phone
Gas Works Revenue Bonds	Baa2	Dan Aschenbach/New York	212.553.0880
Subordinate Revenue Bonds	Baa3	Renée Boicourt/New York	212.553.7162

Debt Service Coverage Trend



Account Receivable As % Of Billed Gas Revenues



□ BILLED GAS REVENUES, 2000 ESTIMATE
■ ACCOUNTS RECEIVABLE, 2000 ESTIMATE

Key Indicators

Philadelphia Gas Works

	1997	1998	1999	2000	2001
Debt-service coverage (x)	1.50	1.52	1.53/1.58	1.72/1.59	2.00/1.65
Total debt-service coverage (x)	1.07	0.90	0.85	0.78	0.9
Operating ratio (%)	81.9	84.0	84.8	86.0	87.0
Current ratio (%)	1.00	0.81	0.68	0.78	0.82
Distribution to city (\$000)	\$18,000	\$18,000	\$18,000	\$18,000	\$18,000
Accounts receivable as % of billed gas charges	24.2	22.2	24.0	30.90	32.1
Customers	511,337	512,000	512,000	512,000	512,000
Debt ratio (%)	82.0	86.6	89.7	84.3	83.1

Opinion

Rating Rationale

Moody's has affirmed Philadelphia Gas Works' Baa2-rated senior lien revenue bonds and its Baa3-rated subordinate lien bonds.

The credit ratings reflect the utility's highly leveraged assets, weak liquidity exacerbated by the weather's effect on gas use and revenues, continued high bill-payment delinquency rate, and recurring administrative instability, which has negatively affected its operations in the past. In addition, the city missed a December 31, 2001, state regulatory board deadline to appoint permanent management.

PGW has had several accomplishments that improve the utility's financial and operational position. Interim management has continued, with some success, in an effort to achieve base-rate increases to improve liquidity.

PGW has also managed the new state regulatory process well, and it concluded successful labor negotiations with positive work rule changes and without major adverse effect on the utility's budget. The utility also implemented several key customer service improvements.

PGW had, in the past, a multiyear record of poorly managed finances and operational problems, including a new billing system that resulted in more than 30,000 customers not being billed in 2000 for four months.

PGW has tried several times over the past decade to turn the utility around, but after good starts, setbacks occurred. Prior to the current interim management, the last effort to improve the utility's operations in 1998

ended with the entire management team being fired or having to resign because of ethical charges.

Although PGW has complied with its strong 1.5 times rate covenant, actual cash-flow assessment has reflected that minimal liquidity is available after PGW's payment of a transfer to the City of Philadelphia and its subordinate lien obligations.

PGW's interim management team appointed by Mayor John F. Street in 2000 began to implement a new strategic direction. Some clear successes have been achieved, but the duration of that interim management group remains uncertain since the city missed a deadline to appoint permanent management, as noted above.

PGW continues to face some difficult challenges, such as obtaining approval of adequate base-rate increases to improve financial liquidity, complying with state regulatory board capital and operational orders, and implementing a transition plan for customer choice.

PGW's Baa3 subordinate lien bond rating reflects the subordinate position of debt-service payment.

Outlook

Moody's believes the credit outlook remains negative. Despite some recent financial and operational improvements, failure to appoint permanent management leaves open the potential for another change in direction and slows the utility's efforts to implement changes to improve operational performance and financial liquidity as it operates in a competitive and changing industry.

Philadelphia Gas Works

Debt Statement as of January 1, 2002 (\$000) [1]

Issue	Ratings	Amount Issued	Amount Outstanding (\$000)
Commercial Paper	Prime-1	\$100,000	\$0 [2]
Philadelphia Municipal Authority, 1997 capital equipment		26,000[3]	12,780
First Series C Bonds	Baa3	25,000	25,000
Subordinated Revenue Bonds	Baa2	[4]	869,479

(1) Excluding \$45 million loan to City of Philadelphia.

(2) PGW has authorization to issue \$100 million commercial paper notes.

(3) Not rated

(4) Several series of bonds are insured by either AMBAC or MBIA and rated Aaa with a Baa1 underlying rating.

Author

Dan Aschtenbach

Editor

Michael Oneal

Production Associate

Marisela Guzmán

© Copyright 2002 by Moody's Investors Service, Inc., 99 Church Street, New York, New York 10007. All rights reserved. ALL INFORMATION CONTAINED HEREIN IS COPYRIGHTED IN THE NAME OF MOODY'S INVESTORS SERVICE, INC. ("MOODY'S"), AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind and MOODY'S, in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such information. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The credit ratings, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER. Each rating or other opinion must be weighed solely as one factor in any investment decision made by or on behalf of any user of the information contained herein, and each such user must accordingly make its own study and evaluation of each security and of each issuer and guarantor of, and each provider of credit support for, each security that it may consider purchasing, holding or selling. Pursuant to Section 17(b) of the Securities Act of 1933, MOODY'S hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MOODY'S have, prior to assignment of any rating, agreed to pay to MOODY'S for appraisal and rating services rendered by it fees ranging from \$1,000 to \$1,500,000. PRINTED IN U.S.A.

Opportunities/Strengths

- PGW's interim management has achieved various accomplishments to improve PGW's financial position, including base rate increases, labor contract settlements and operational changes such as obtaining adequate gas cost recovery adjustments.
- State legislation approved in 1999 provides for a longer transition (in 2003) to customer choice of natural gas supplier in PGW's service area. PGW is in process of proposing how it will meet the requirement. While PGW earns a relatively small margin from its large customers, thus lessening the impact of any customer loss, customer aggregation efforts could be a more serious competitive threat.
- PGW management has succeeded managing the transition to state regulation, including making rate-filing settlements and implementing operating improvements pursuant to state Public Utilities Commission audits.
- With a 1.5 times rate covenant and a debt service reserve fund that is fully funded at maximum annual debt-service level, PGW provides bondholders with favorable legal protections. Recent bond covenant changes that permit subordinate lien bonds with weaker covenants is a credit weakness.
- PGW has had a relatively stable customer base and has succeeded in attracting new, large customers partly because its commodity is competitively priced.
- PGW is owned by the city and thus is linked to its economic development and retention strategies. The utility's relationship with the city, while sometimes mired in red-tape, ensures that these objectives remain in the forefront.

Risks/Weaknesses

- A record of management instability has long affected the utility's progress in sustaining a record of financial soundness and improvement in its competitive position. Failure to meet deadline to appoint new management remains a concern.
- While there are opportunities in the transition to state regulation, PGW, as a city-owned utility, will still be pressured by potential political influences that could complicate management of the gas business.
- PGW has a consistently poor cash position and high debt ratios. Its weak actual debt-service coverage provides limited financial flexibility. Mild winter weather in the past several years has affected gas use, which further weakens already-weak financials.
- Poor management of the utility's accounts receivable problem in the past has burdened PGW's financial soundness. PGW has established a new collections strategy that management believes will improve the utility's financials.
- PGW's options to grow its revenue stream are limited because of its fully developed service area, low-income population, and need to price its services competitively.

New Managers Still Meet Transition to State Regulation, Establish Sounder Finances, but Risks Remain

Moody's believes PGW has successfully met challenges of its transition to state regulation while managing the utility well during a difficult financial period. As of July 1, 2000, PGW, as a municipally owned utility, became subject to regulation by Pennsylvania's Public Utilities Commission (PUC). This unique status as a municipally owned utility regulated by a state regulatory board was necessitated by a disappointing financial and customer performance record that prompted the state legislature to act.

Moody's has remained cautious about the success of PGW in this process since PGW's past record prior to state regulation was filled with management turnover and financial and operational problems. The current management team has an interim appointment. An agreement between PGW and the state PUC required that permanent, independent, professional, and experienced management be selected by December 31, 2001. The city missed the deadline.

A nationwide search had been conducted and several members of the current management group have applied for permanent status. While the potential change of management again looms, in the interim, the

utility has been managing the transition to state regulation well and has been taking steps to improve the utility's financial flexibility.

The transition to state regulation has been challenging since PGW has had to participate in a newly established rate-setting process amid the equally challenging heating season of past several years. It is important to bondholders that the state public utility code requires rate setting of the state PUC to follow the prior rate-setting methodology until all bonds are retired, including adherence to rate covenants and debt-service-reserve requirements.

Moody's believes that state regulation could become a credit strength since the state PUC may focus more on PGW's financial performance than the city Gas Commission had in the discharge of its responsibilities. A key challenge for the PGW interim management is to convince the state PUC to provide it with additional base rate increases to improve its fundamental financial flexibility. (See Figure 1 for the base-rate-request history over the past two years.)

In addition, several major risks are on the horizon that require sound management decisions-for example, establishing a restructuring plan by July 1, 2002, which will set forth how PGW will unbundle its gas rates and services for customer choice of gas supplier.

Figure 1-Permanent Base Rate Increase History

Year	Requested of State PUC	Received by PGW
2000	\$52 million	\$11 million
2001	\$65 million	\$33.6 million
2002 (1)	\$50 million	

(1) Expected to be filed.

Rate-Setting Process Caused Gas Cost Recovery and Some Base Rate Changes; Pending Rate Increase to Improve Finances

PGW's major expense item is the cost of the natural gas delivered into its distribution system. Changes in these costs are to be recovered on a dollar-for-dollar basis through the gas cost recovery charge (GCR) approved by the state PUC. Moody's believes that PGW has been able to manage this process adequately to ensure customers are charged accordingly in the upcoming period for under or overpayments.

In 2000/2001, charging customers appropriately was especially important as gas prices rose significantly. For example, between June 2000 and November 2001, PGW received more than \$230 million in gas cost recovery. As natural gas prices dropped in the later part of 2001, PGW also reduced gas recovery charges twice, amounting to a combined reduction of nearly \$200 million.

The more difficult part of rate setting has been achieving satisfactory base rates. As Figure 1 shows, PGW has attempted to request base rates it deemed necessary to manage its business. Base rates pay for PGW debt-service payments, operating expenses, and annual payments to the city. PGW was able to get, after a six month process, an \$18 million interim increase in base rates in a joint petition approved February 8, 2001, which included \$11 million that was permanent.

In addition, the agreement allowed PGW to hold in reserve any GCR over collection incurred by August 31, 2001, not to exceed \$18 million, to insure that it has funds to meet bond covenants and to satisfy other obligations through January 2002. As part of the agreement, PGW was required to implement various management audit recommendations and several other recommendations of the state PUC. PGW complied with that requirement.

On January 5, 2001, PGW filed with the PUC a proposal to increase permanently its base rates by \$65 million annually. This increase would replace the \$18 million interim rate hike approved in February 2001. The higher permanent base rate increase is what PGW's management believed it required to improve fundamentally PGW's ongoing weak liquidity position and to repay the revolving loan from the city by 2003. The state PUC approved \$33.6 million. PGW expects to file a new request for base rate increase above the \$33.6 million amounting to \$50 million in 2002.

Moody's notes that the utility's weak liquidity position is a major credit weakness and has been a key factor in past rating downgrades. While adequate base rates are important to financial margins, the expenditure side of the budget represents another area of focus, which could improve financial balances.

The state PUC may continue to step up its focus on making PGW more efficient than granting further base rate charges. PGW's current management has established expenditure targets and is addressing numerous recommendations made by the state PUC, including implementing a best practices group process.

City Ownership/Bond Covenant Key to PGW Keeping Minimum Debt Service Coverage Record

PGW is owned by the City of Philadelphia (general obligation bonds rated Baa1) and, as an operating enterprise of the city, is considered an important municipal asset, having just celebrated its 165th year in business. Past privatization proposals have gone nowhere. The importance of PGW to the city is evident by the decisive action city officials took to shore up the enterprise's liquidity during 2000 with the advance of a \$45 million loan. The loan bears no interest and must be repaid by January 25, 2003.

The mayor of the city has expressed his continued commitment to implement a plan to improve PGW's performance so it can be a city asset. PGW serves more than 500,000 customers within city boundaries and plays an important role in economic development programs. While controversial, another important role PGW continues to play is service to the city's large disadvantaged service population. The city receives an annual \$18 million payment from PGW as a payment to the owner.

Another key credit strength is the utility's bond covenants that require debt service to be covered 1.5 times by net revenues and that a fully funded debt-service reserve be at maximum annual debt service. Despite the difficult financial period the utility weathered in the past year, both city ownership and bond covenants were positive factors in assuring that minimum financial coverages were maintained.

As part of the restructuring review of PGW, which is required by July 1, 2002, a study to sell PGW is also being undertaken. Moody's believes that any sale of the PGW assets if the outstanding bonds are not defeased would need consent of the bondholders since the physical assets of the gas works as well as its revenues secure the bonds.

While the Pennsylvania Gas Choice Act protects compliance with bond covenants and the state's PUC agrees with that obligation, the Gas Choice Act could potentially affect PGW's financial results adversely. Customer aggregation could be a major threat to PGW. PGW continues to prepare its restructuring plan due on July 1, 2002 in order to provide customers with choice of supplier. PUC will have to approve the filed plan.

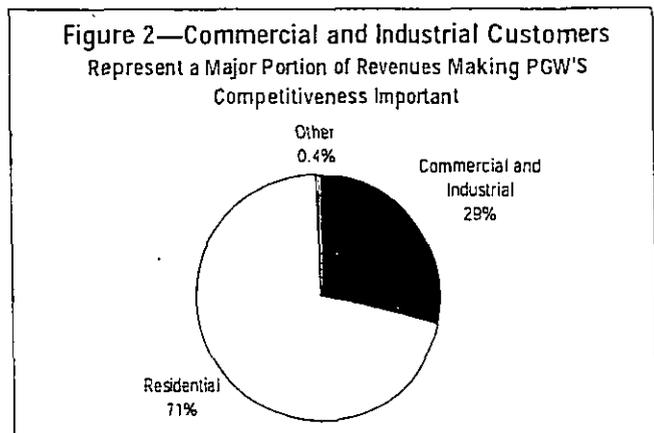
Legislation Gives PGW Until End of 2003 to Prepare for Industry Deregulation

PGW has been operating in a partly deregulated natural gas industry in Pennsylvania, with large customers already having the option of getting their natural gas from an alternative gas supplier. The state legislation broadens choice to all customers in PGW's service area after 2003 and after a PGW plan for competition is approved by the state PUC.

Policy considerations still make PGW somewhat unique in a deregulated market. The utility's large low-income population presents PGW with a heavier burden than that of other gas utilities. How the state PUC will treat this factor in its assessment of PGW's competition plan is not yet known.

PGW still needs to focus now on being competitive since it must compete with other sources that effect sales, such as space and water heating. Also, more than 25% of its revenue comes from industrial and commercial customers (see Figure 2), most of whom have retail choice of supplier.

Moody's believes that most publicly owned utilities face uncertainty about the intensity of competition and that implementing a plan early to face such a challenge is critical. PGW's lack of stable management over the past several years has been a factor in its lack of strategic direction.

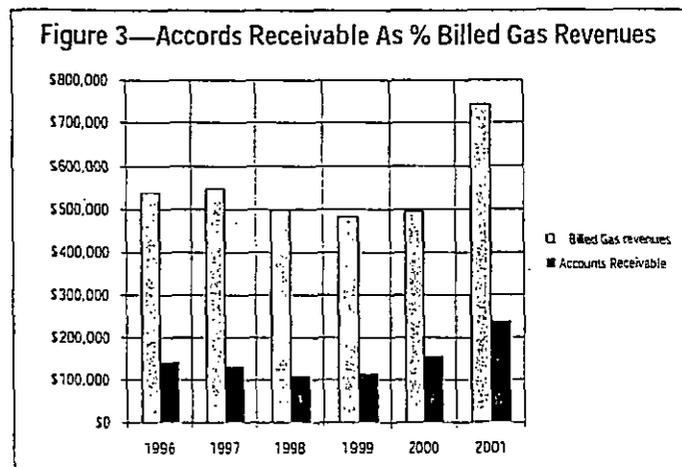


Utility's Customer Base Stable, but Its High Receivables Still a Credit Pressure

The utility's options for revenue growth are limited because its service area is fully developed, total rates (including distribution, commodity, and other PGW charges) are high relative to those of the competition, and the service area population is declining. About 95% of PGW's customers are residential—a favorable attribute since residential customers are typically less aware of the price in the marketplace for gas and are therefore less likely to switch providers.

Although the customer base has been relatively stable, the mix of residential customers presents a vulnerability. The utility carries the burden of Philadelphia's relatively poorer population (about one-fifth of residents have incomes below the poverty threshold). This profile accounts for a long-term trend of high receivables. At fiscal year-end 2001, receivables represented about 32% of gross billed gas revenues; this percentage is high for any utility.

To address its high receivables rate, PGW management, in the past, has implemented several programs to encourage payment of delinquent accounts and instituted a more aggressive schedule for writing off the same. In the past year, interim management has improved the collection rate and established several new strategies to mitigate this problem. As Figure 3 shows, collection remains a problem for PGW. Moody's believes that the high level of delinquencies and uncollectible accounts is an inherent weakness in PGW's revenue base.

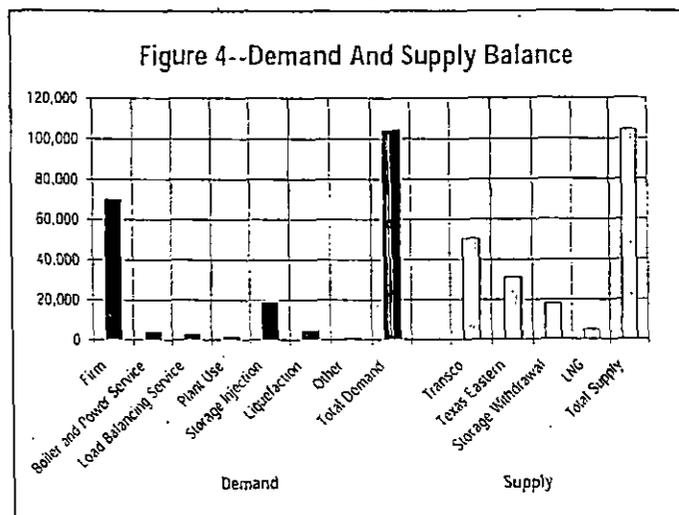


PGW's Competitively Priced Commodity Still a Key Fundamental Strength

PGW has been able to offer its customers a competitively priced commodity because of its effort to optimize and enhance its natural-gas-supply purchasing procedures and its use of storage to match supplies to winter-period peak demands. Since it is the commodity that is open to competition, this effort represents a fundamentally important credit strength.

The competitive commodity has allowed the utility to succeed in retaining and attracting large users of gas as these customers began to shop for the most competitive rate for natural gas. PGW has had continued success in locking in its gas-supply needs at a price that is below the spot rate.

PGW has established a favorable record in successfully managing its supply requirements meeting maximum demands with a mix of spot, contracted, and storage capacities as well as the use of its liquefied natural gas facilities. (See Figure 4.) An independent evaluation found in a 1999 report that PGW's transportation, storage, and supplies of natural gas under contract, along with LNG normally available to PGW, are adequate to meet PGW's forecast of peak hour, peak day, and peak year demand through 2005.



Financial Analysis

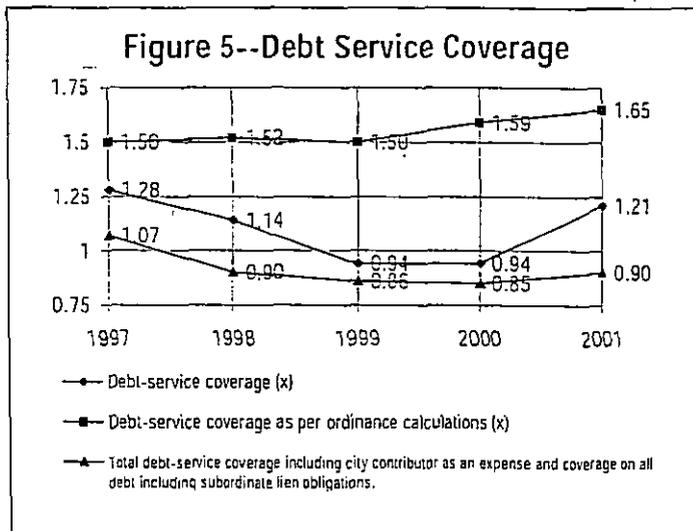
LIMITED FINANCIAL FLEXIBILITY WEAKENS CREDIT POSITION

Moody's believes that PGW's limited financial flexibility has been a material credit weakness, particularly for a utility in the natural gas business. Compared with other city-owned enterprises in the US, PGW's financial ratios reflect a utility with bonds rated in the Baa range. PGW's current ratio has consistently reflected a marginal financial cushion.

PGW has had to maintain its operating liquidity by use of an external source of funds either through a short-term commercial paper line or, in 2001, a \$45 million loan from the city's general fund, as noted above. The absence of these external sources would seriously compromise PGW's ability to meet its debt obligations.

While PGW has maintained the strong 1.5 times rate covenant required by the revenue bond ordinance, it is also obligated to make lease payments to the Philadelphia Municipal Authority for its lease revenue bonds. PGW also makes an annual transfer payment to the City of Philadelphia as a dividend contribution. Both the lease and the annual transfer payments are subordinate to debt-service payments on the senior revenue bonds, but in practice they are paid when required.

An assessment of PGW's financial results for the past two years shows that the utility continues to manage with limited flexibility. Bond ordinance debt-service-coverage calculation reflects coverage above 1.5 times in both years, but Moody's calculation from the utility's financial statements indicates a coverage margin closer to at or below 1 times coverage. (See Figure 5.)



The current ratio, which measures current assets to current liabilities, was less than 1 times in both 2000 and 2001. The accumulated provision for uncollectible accounts rose to \$184 million in 2001 versus the 2000 level of \$129 million.

Financial forecasts rest on various assumptions that are key to financial stability. PGW management believes that a base rate increase to \$50 million will restore financial liquidity, including paying off the city loan. Various debt management strategies are also being evaluated. If the base rate increase is not approved and an extension of the terms of the city loan to 2003 is not possible, further credit deterioration would result without other options.

Highly Leveraged Utility Seeks Restructured Bond Resolution for Flexibility

PGW is a highly leveraged utility, with outstanding debt increasing by about 30% since 1994. PGW's debt ratio (net funded debt to net fixed assets) has ranged between 82% in 1995 to 83.1% in 2001. PGW's fiscal-year 2002 capital budget includes almost \$60 million of capital spending for various purposes, including a cast iron main replacement program. Funding of the CIP is expected to come from internally generated funds.

PGW restructured its debt in 1998 by introducing a new resolution that permits a senior/junior debt structure with the subordinate lien bonds issued under the new 1998 resolution, requiring only a sum sufficient rate covenant instead of the 1.5 times coverage test required in the prior resolution. The lower coverage test for all its debt-service requirements makes it easier for the utility to meet the coverage test.

The bond resolution also provides PGW with the ability to issue variable-rate debt, surety bonds, and interest-rate swaps. The new and old resolutions require a sinking fund reserve in the amount of maximum annual debt service.

Moody's believes the strength of the 150% rate covenant is weakened by the subordinate lien test, since PGW is obligated, as noted above, to make both lease payments to the Philadelphia Municipal Authority for its lease revenue bonds and an annual transfer payment to the city, both of which are subordinate to the debt-service payments on the bonds.

Philadelphia Gas Works

Balance Sheet Data (fiscal years ended 8/31 \$000)

	1994	1995	1996	1997	1998	1999	2000	2001
Gross fixed assets	\$1,077,975	\$1,124,757	\$1,156,201	\$1,203,720	\$1,271,131	\$1,334,942	\$1,382,645	\$1,353,864
Net fixed assets	743,048	766,908	772,942	788,779	821,365	856,450	869,472	883,727
Net working capital	81,936	16,568	11,940	2,515	25,257	40,957	38,200	122,791
Long-term debt	778,118	750,571	739,408	728,130	818,323	897,134	856,502	933,402
Debt-service reserve and debt-service funds	78,589	77,767	78,678	79,679	85,111	92,381	91,246	96,598
Net funded debt	699,529	672,804	660,730	648,451	733,212	804,753	765,256	836,904

(1) Excludes \$97,059,000 notes payable in 2000 and \$78,000,000 in 2001. Also, excludes \$45,000,000 loan from city in 2001.

Philadelphia Gas Works

FINANCIAL PERFORMANCE (fiscal years ended 8/31 0000)

	1994	1995	1996	1997	1998	1999	2000	2001
Heating revenues	\$472,626	\$385,995	\$476,806	\$450,241	\$406,826	\$390,242	\$434,544	\$620,857
Non-heating	88,895	85,678	91,146	91,892	83,771	72,751	87,830	104,680
Other	12,398	7,277	8,296	8,837	23,035	23,241	33,601	24,514
Operating revenues	573,919	478,950	576,048	550,970	511,803	486,885	555,875	750,046
Non-operating revenues	6,989	29,293	7,904	7,514	5,131	8,263	9,417	12,343
Gross revenue and income	580,908	508,243	583,952	558,484	516,934	495,148	563,225	762,389
Natural gas purchases	274,103	213,645	276,856	271,627	246,699	219,081	266,354	431,327
Provision for bad debt	43,401	43,276	38,340	33,474	34,130	38,999	54,642	67,633
Administrative and general	36,793	44,593	41,247	45,200	42,268	50,978	56,236	53,000
Distribution	25,003	19,561	22,817	20,454	16,500	15,527	14,246	14,837
Field services			18,492	18,883	28,006	30,942	33,704	33,202
Customer services	23,036	17,448	11,669	13,205	12,826	11,104	11,753	14,228
Gas processing	21,822	18,645	14,846	14,238	13,582	13,881	14,033	13,400
Pensions	12,712	4,462	7,337	4,590	3,334	787	1,096	2,301
Marketing			3,454	3,841	5,268	4,453	3,041	3,486
Amortization of regulatory asset			3,750					
Taxes	11,615	5,999	6,532	6,517	6,235	6,091	6,512	6,299
All other	33,420	35,317	19,567	19,206	19,369	21,685	16,278	13,190
Total O&M expenses	481,905	402,946	464,907	451,235	430,112	412,741	477,895	652,903
Net revenues	99,003	105,297	119,045	107,249	86,822	82,407	85,330	109,486
Interest expense/revenue bonds	48,268	47,494	41,253	44,887	43,027	46,990	49,256	48,151
Principal and interest	71,858	79,304	74,878	83,592	76,365	87,664	90,401	90,309
Total principal and interest-all debt obligations 2			80,762	90,235	83,793	96,458	100,522	100,563
Distribution to city	18,000	18,000	18,000	18,000	18,000	18,000	18,000	18,000
Retained equity	1,711	7,274	13,541	5,971	-17,025	-20,251	-20,411	-6,846
Depreciation (1)	27,913	28,755	39,052	36,652	41,019	29,075	30,805	31,840

(1) In 1996, depreciation rate was increased to 3.5% from 2%.

(2) Beginning in 1996, revenue and other subordinated debt is detailed separately.

(3) Includes \$21.135 million grant from the debt service reserve fund forward purchase agreement.

(4) Including appliance & other revenues in 1998 and 1999.

(5) Expenditure items left blank are included in all other category for estimated 2000.

Philadelphia Gas Works

Balance Sheet Data (fiscal years ended 8/31 \$000)

KEY RATIOS (fiscal years ended 8/31)	1994	1995	1996	1997	1998	1999	2000	2001
Income Statement								
Operating ratio (%)	84.0%	84.1%	80.7%	81.90%	84.0%	84.8	86.0	87.0
Net take down (%)	17.0	20.7	20.4	19.2	16.8	16.6	15.1	14.4
Debt-service coverage (x)	1.38	1.33	1.60	1.28	1.14	0.94	0.94	1.21
Debt-service coverage as								
per ordinance calculations (x)[1]	1.50	1.50	1.67	1.50	1.52	1.53/1.58	1.72/1.59	2.00/1.65
Total debt-service coverage (x)[2]	1.10	1.25	1.07	0.90	0.86	0.85	0.90	
Debt service safety margin (%)	4.7	5.1	6.6	4.2	2.1	0	0	17.5
Operating margin (%)	16.0	15.9	19.3	18.1	16.0	15.2	14.3	12.9
Annual debt service as % of expenses	16.4	14.8	16.7	16.3	18.9	17.4	13.3	
Balance Sheet								
Current ratio (%)	1.58	1.15	1.16	1.00	0.81	0.68	0.78	0.82
Debt ratio (%)	84.8	85.9	84.2	82.0	86.6	89.7	84.3	83.1
Net working capital as % of gross revenue	14.1	3.3	2.00	0.4	5.0	8.3	6.8	16.1

(1) For years 1999-2001, debt service coverage by ordinance calculation includes for 1975 ordinance bonds and 1988 ordinance bonds, respectively.

(2) As calculated by Moody's Investors Service including distribution to the city as expense and total debt service includes subordinate obligations.

Pennsylvania Public Utility Commission

v.

Philadelphia Gas Works

Docket No. R-00017034F0002

OCA Cross-Examination Exhibit No. 2

Dated:

3/26/02

Phila, PB P/S

DOCUMENT
FOLDER

DOCKETED

APR 30 2002

RECEIVED
02 APR -2 PM 1:56
SECRETARY'S BUREAU

RESPONSE TO OFFICE OF CONSUMER ADVOCATE DATA REQUEST
REGARDING PGW'S RATE PROCEEDING

Question OCA-Set I-2,4,6: Please provide copies of all data, presentations, etc. provided to S&P personnel by PGW and/or its representatives over the past twelve months.

Response Provided by: Joseph R. Bogdonavage, Senior VP – Finance

Response: See the attached presentation. The formal presentations that were made to the rating agencies utilized the same documentation in each case. In addition, PGW's unaudited financial statements for FY 2001 were provided. Also numerous emails were received from the rating agencies requesting clarification of previous data and some additional questions were proffered. The available emails are attached.

Joseph Golden

From: Prabhu, Aneesh (Aneesh_Prabhu@standardandpoors.com)
Sent: Monday, February 11, 2002 8:45 AM
To: 'Thomas Knudsen'
Cc: Joseph Bogdonavage; Joseph Golden; 'bigaierb@publicfm.com'
Subject: RE: Most Recent PGW Cash flows FY 2002 & FY2003

Hi Tom,

The press release on PGW is with an editor. I will send that over later today, as and when I receive it. It will be released only after we get your comments. I will also include a workbook from the financial analysis that will list the bond coverage and fixed charge coverage calculations. Formulas and footnotes will assist Joe in following the calculations involved.

A brief on the rating process itself. S&P first rates the business position. The business position includes aspects such as markets, operations, regulation, competitive position and management, among others. Subsequently, the financial position is risk weighted to reflect the business position in the analysis, i.e. a stronger business position can support relatively weaker financial numbers to maintain a specific rating. Also, while bond coverages and fixed charge coverages are some major indicators used in the financial analysis, S&P also looks at other indicators like month-end cash in hand, liquidity position (unencumbered cash to operating expenses), among others.

I expect to have the press release over to you by the afternoon. If it's delayed coming back from the editors, we will push the release so that you have adequate time to look through it. In any event, since we don't make press releases later in the evening, I'm expecting the release to go out tomorrow.
thanks
aneesh

The information contained in this message is intended only for the recipient, may be privileged and confidential and protected from disclosure. If the reader of this message is not the intended recipient, or an employee or agent responsible for delivering this message to the intended recipient, please be aware that any dissemination or copying of this communication is strictly prohibited. If you have received this communication in error, please immediately notify us by replying to the message and deleting it from your computer.

Thank you,
Standard & Poor's

OCA Statement No. 1-ERP

DOCUMENT
FOLDER

3/26/02

R-00017034F002

Phb PB

RIS

BEFORE THE PENNSYLVANIA
PUBLIC UTILITY COMMISSION
DOCKET NO. R-00017034F002

DOCKETED
APR 30 2002

IN THE MATTER OF THE FILING OF
PHILADELPHIA GAS WORKS
FOR EXTRAORDINARY RATE RELIEF

DIRECT TESTIMONY OF
RICHARD W. LELASH
ON BEHALF OF THE
OFFICE OF CONSUMER ADVOCATE

RECEIVED
02 APR -2 PM 1:57
P.U.C.
SECRETARY'S BUREAU

MARCH, 2002

PHILADELPHIA GAS WORKS
DOCKET NO. R-00017034F002
TESTIMONY OF RICHARD W. LELASH

TABLE OF CONTENTS

	<u>PAGE</u>
I. STATEMENT OF QUALIFICATIONS	1
II. SCOPE AND PURPOSE OF TESTIMONY	3
III. SUMMARY OF FINDINGS AND RECOMMENDATIONS	5
IV. EXTRAORDINARY RATE RELIEF	15
- Immediate Necessity	15
- Bond Downgradings	17
V. BASIS FOR PGW'S CLAIM	21
- The Standard and Poor's Formula	21
- Traditional Coverage Measurements	24
- Capital Vs. Revenue Need	27
VI. CAPITAL SOURCES AND RESPONSIBILITIES	31
- City Ownership Obligations	32
- Required PGW Actions	36
- Ratepayer Responsibilities	38
VII. SUPPORTING SCHEDULES	43
VIII. APPENDIX: PRIOR R.W. LELASH TESTIMONIES	

1 I. STATEMENT OF QUALIFICATIONS

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS FOR THE RECORD.

3 A. My name is Richard W. LeLash and my business address is 18 Seventy Acre Road,
4 Redding, Connecticut.

5 Q. WHAT IS YOUR CURRENT BUSINESS AFFILIATION?

6 A. I am an independent financial and regulatory consultant working on behalf of several
7 state public utility commissions, attorneys general, and consumer advocates.

8 Q. PRIOR TO YOUR WORK AS AN INDEPENDENT CONSULTANT, WHAT WAS
9 YOUR BUSINESS AFFILIATION, AND WHAT WAS YOUR REGULATORY
10 EXPERIENCE?

11 A. I was a principal with the Georgetown Consulting Group for twenty years. During my
12 affiliation with Georgetown, and continuing to date, I have testified on cost of service,
13 rate of return, and regulatory policy issues in about 240 regulatory proceedings.
14 These testimonies were presented before the Philadelphia Gas Commission, the
15 Federal Energy Regulatory Commission and in the following jurisdictions: Alabama,
16 Arizona, Colorado, Delaware, District of Columbia, Georgia, Illinois, Kansas, Maine,

1 Maryland, Minnesota, Missouri, New Jersey, New Mexico, New York, Ohio,
2 Oklahoma, Pennsylvania, Rhode Island, U.S. Virgin Islands, and Vermont.

3 Q. MR. LELASH, WHAT IS YOUR EDUCATIONAL BACKGROUND?

4 A. I graduated in 1967 from the Wharton School with a BS in Economics and in 1969
5 from the Wharton Graduate School with an MBA.

6 Q. DURING THE COURSE OF YOUR REGULATORY WORK, WHAT HAS BEEN
7 YOUR EXPERIENCE WITH GAS DISTRIBUTION COMPANIES?

8 A. Since 1980, I have worked extensively on gas policy and procurement issues. In my
9 Appendix there is a listing of the recent cases in which I have sponsored testimony.
10 In addition to these cases, I have reviewed and analyzed many other gas policy filings
11 which were resolved through stipulation. Among other issues, my testimonies have
12 involved gas revenue requirements, unbundling and restructuring, performance based
13 regulation, gas plant remediation costs, gas price hedging, general gas procurement
14 reviews, and least cost gas standards. In addressing these issues, I have analyzed gas
15 regulatory filings involving about 30 different local distribution companies. With
16 respect to PGW, I have testified on behalf of the OCA in all of the Company's
17 previous rate matters before this Commission.

1 II. SCOPE AND PURPOSE OF TESTIMONY

2 Q. WOULD YOU PLEASE STATE THE SCOPE AND PURPOSE OF YOUR
3 TESTIMONY IN THIS PROCEEDING?

4 A. I was hired by the Office of Consumer Advocate ("OCA") to review the Petition for
5 Extraordinary Rate Relief made by the Philadelphia Gas Works ("PGW" or
6 "Company") and evaluate it against applicable regulatory standards.

7 *The purpose of my testimony is to present findings and recommendations to*
8 *the Public Utility Commission ("PUC" or "Commission") concerning issues raised*
9 *by the filing, the financial condition of the Company, the measurement of fixed*
10 *charge coverages, and the appropriate capital sources for the Company.*

11 Q. IN PERFORMING YOUR REVIEW AND ANALYSIS, WHAT DATA SOURCES
12 DID YOU UTILIZE?

13 A. *My review and analysis encompassed the Company's filing, responses to discovery*
14 *requests, and information provided during a discovery meeting. I also utilized*
15 *information provided in previous PGW proceedings before the Commission and*
16 *general data concerning the financial profiles and capital needs of other gas*
17 *distribution utilities.*

1 Q. WERE THERE ANY LIMITATIONS PLACED ON THE CONDUCT OF YOUR
2 REVIEW?

3 A. With the passage of the Natural Gas Choice and Competition Act ("Act"), there are
4 several rate setting issues which are subject to legal interpretation. This testimony
5 addresses such issues based on regulatory practice rather than from a legal
6 perspective, and where necessary, legal conclusions were developed through
7 consultation with Counsel.

8 I would also like to note that I will not restate certain regulatory principles and
9 policy issues which I have previously presented to this Commission. However, like
10 Ms. Bisgaier, I would like to incorporate by reference my testimony from the
11 Company's last base rate case, Docket No. R-00006042, into this proceeding.

12 Q. WAS THIS TESTIMONY PREPARED BY YOU OR UNDER YOUR
13 SUPERVISION?

14 A. I prepared this testimony with the assistance of Michael Bleiweis, another OCA
15 consultant. Mr. Bleiweis prepared the supporting schedules under my supervision.

1 III. SUMMARY OF FINDINGS AND RECOMMENDATIONS

2 Q. BASED ON YOUR INVESTIGATION, WHAT ARE YOUR FINDINGS AND
3 RECOMMENDATIONS CONCERNING THE COMPANY'S EXTRAORDINARY
4 RATE RELIEF FILING?

5 A. As a result of my review and analysis, I make the following findings and
6 recommendations:

7 Extraordinary Rate Relief

8 1. The Company has not presented sufficient evidence to satisfy the criteria
9 necessary to warrant extraordinary revenue relief. It appears to be relying
10 solely upon a Standard and Poor's ("S&P") announcement concerning the
11 potential for a future downgrading of PGW's outstanding bond issues. While
12 there have been and are valid concerns about PGW's financial condition, there
13 remain several alternative courses of action which do not necessarily involve
14 the need for extraordinary revenue relief.

15 2. The S&P announcement, which is being relied upon by PGW, provides little
16 guidance concerning necessary remedial actions since its relevant content is

1 contained in an analyst's quote that "If the PUC approves an emergency rate
2 request, Standard and Poor's will review the adequacy of the increase and
3 determine if ratings will be affirmed or lowered." Regulated utilities should
4 not obtain revenue relief, particularly extraordinary revenue relief, based on
5 speculation concerning what actions a rating agency may or may not take.

6 3. Additionally, the referenced announcement reflects an inadequate assessment
7 of several relevant facts. S&P cites the PUC's very recent \$33.6 million rate
8 increase as having created a rate shortfall which contributed to PGW's poor
9 liquidity. It fails to mention the additional \$10.8 million which was provided
10 to PGW by the Commission in January of this year. Likewise, while
11 acknowledging that the liquidity problem can be addressed by either additional
12 revenue relief or project revenues, it fails to meaningfully evaluate the nature
13 or extent of improved liquidity which could be obtained from project revenues
14 received from the City. This deficiency in the S&P announcement stems from
15 an unquantified statement alleging a "limited ability of the city of Philadelphia
16 to provide assistance due to the city's tight financial situation."

17 4. In the end analysis, the Company has made no claim, other than the potential
18 bond downgrading, that would make it unable to continue to provide safe and

1 adequate service. Indeed, even with a bond downgrading, the Company
2 appears to acknowledge that it could take proactive measures in order to
3 respond to the ensuing crisis and continue to operate. Accordingly, the
4 Company is sending mixed signals since it has yet to obtain a loan payment
5 deferral from the City Council, seek a long-term grant back of the annual \$18
6 million City payment, or prioritize its operating expenses and Construction
7 Fund expenditures.

8 5. Practically, any S&P decision on a potential lowering of PGW's bond ratings
9 is dependent upon the availability of capital from the City as well as upon any
10 potential working capital relief. It is perplexing as to why S&P is not placing
11 equal pressure on PGW's owner, the City, to augment its investment either by
12 direct capital contributions or, at a minimum, by leaving its \$18 million
13 dividend in the Company in order to alleviate the current liquidity problem.
14 While the Natural Gas Choice and Competition Act ("Act") provides that the
15 Commission will permit PGW to collect rates and charges for a transfer or
16 payment to the City, it does not require that such funds be paid as a dividend
17 as opposed to being transferred to the City as retained equity in its wholly
18 owned enterprise.

1 6. It should be understood that the Company's petition for extraordinary rate
2 relief is not predicated on any claimed inability to pay its operating expenses.
3 Rather, its filing seeks a capital infusion in order to alleviate its long standing
4 lack of liquidity. There is no evidence per se which would indicate that,
5 during the pendency of its base rate case, it would suffer an impairment to its
6 ability to provide on-going safe and reliable gas service to its customers. It is
7 only the threat of S&P, that the Company's bonds will be downgraded, which
8 the Company relies on to support the need for extraordinary action. Indeed,
9 it is only the potential downgrading by S&P which apparently will trigger the
10 Company's actions to constrain operations and thereby conserve cash.

11 - Basis For Capital Claim

12 7. The Company's claim for extraordinary revenue relief is predicated on a
13 coverage formula represented by PGW as the one being used by S&P. The use
14 of this formula and its relative weighting as part of S&P's overall bond rating
15 process is unknown. As such, the Commission is being asked to approve a rate
16 increase based on a determination which can only be described as a "black
17 box."

1 8. In the S&P coverage methodology, the \$18 million annual obligation to the
2 City as well as the \$20 million reduction to the outstanding commercial paper
3 amount have been added to the debt service amounts in order to define fixed
4 obligations. With this revised definition, which is not in conformity with, and
5 is even more stringent than, the provisions of PGW's bond indentures, the
6 Company is estimated to have a 0.88 times coverage for its fiscal year ended
7 August 31, 2002. Since PGW has represented that S&P requires a 1.20 to 1.30
8 times coverage minimum, a \$44 million rate increase is claimed by PGW to be
9 necessary to meet the S&P requirements concerning PGW's liquidity.

10 9. In a separate presentation, PGW derives the \$44 million rate increase based on
11 financial forecasts which are presented in support of the Company's base rate
12 filing. Of necessity, these forecasts have not yet been analyzed or evaluated
13 in the context of a general rate investigation. As such, it is impossible to make
14 any comprehensive evaluation of the reasonableness of the Company's derived
15 \$44 million amount.

16 10. By conventional measurements, the \$44 million extraordinary rate relief
17 appears overstated. Under the existing bond indenture provisions the fiscal
18 year 2002 forecasts show coverage of 1.28x under current rates. Were the City

1 to grant back the annual \$18 million, the indenture coverage would be 1.87x
2 or well above the required 1.50x level called for under PGW's bond indenture.
3 Under the S&P coverage formula, which differs from that of the bond
4 indenture, \$35.4 million of capital or City project revenues would satisfy the
5 lower end of S&P's defined 1.2x to 1.3x coverage range.

6 - Capital Sources and Responsibilities

7 11. There is no doubt that PGW's lack of liquidity stems from its actions and those
8 of its owner, the City of Philadelphia. Inadequate rate filings during the 1990's
9 forced the Company to utilize both short and long-term borrowings to the
10 degree that it is currently precluded from obtaining further debt capital from
11 the financial markets. Adding to the current capital deficiency was the fact
12 that the City continued to withdraw its annual \$18 million dividend from its
13 Company despite the readily apparent deterioration in the Company's capital
14 position.

15 12. Now S&P is demanding increased liquidity to remedy the capital deficiencies
16 and the Company, in turn, is seeking extraordinary revenue relief to compel
17 ratepayers to do what its owner has been unwilling to do for years - provide

1 needed capital to the utility. Were the City to have been willing to leave a
2 portion of its earnings from PGW in the Company for several years, as all
3 other utility owners routinely do, there would be no current liquidity problem.
4 Accordingly, a request for extraordinary revenue increases now, while the City
5 continues to have PGW pay a dividend without a grant back, is unreasonable
6 and unwarranted. No other utility in this country would continue to pay
7 dividends to its owners were it facing the liquidity problems which PGW
8 faces.

9 13. The Natural Gas Choice and Competition Act specifically provides that, “The
10 Commission shall permit the City Natural Gas Distribution operation to
11 impose, charge or collect rates and charges as necessary to permit the City
12 Natural Gas Distribution operation to transfer or pay to the City . . . such
13 amount as may be specified from time to time . . .” This provision does not
14 specifically require the payment of dividends to the City, and the Company
15 could instead transfer income to the City Equity account to satisfy the intent
16 of the Act. By transferring income to the City as retained earnings, the City
17 would be credited with the required \$18 million in equity, and the Company
18 would be able to build up the equity capital necessary to prudently run its
19 operation rather than making a cash payment to the City.

1 14. As part of any process to determine what will constitute adequate capital
2 contributions to address PGW's liquidity and financial position, the
3 Commission should specify a reasonable regulatory framework to address both
4 the short and long-term PGW problems. Such a framework would require
5 capital commitments from the City, mandatory actions by PGW, and the
6 Commission's specification of what amount of working capital would be
7 reasonable to obtain from ratepayers. It is hoped that in doing this, the
8 Commission will be able to establish sufficient support for PGW so that the
9 rating agencies have justification for maintaining PGW's current bond ratings.

10 15. The City should be required to acknowledge its ownership responsibilities and
11 financial interest in resolving PGW's financial problems. To this end, it
12 should be required to designate permanent management for PGW in the very
13 near future and disclose the findings and conclusions of its investigation into
14 the potential sale of PGW. It should also restructure the term of the current
15 City loan by deferring repayment with interest over three years. And finally,
16 the City should grant back its annual PGW dividend for at least three years in
17 order to reduce PGW's excessive short-term debt and debt leverage. Such a

1 grant back would effectively have the City convert its short-term loan into
2 equity over the initial three year period.

3 16. PGW should be required to conserve its cash by prioritizing its operating and
4 capital expenditures. This prioritization should yield revised budgets and
5 capital spending programs for the next three years. Operationally, the
6 Company must develop and implement a comprehensive collection program
7 to improve accounts receivable collection. In response to the current liquidity
8 problem, the Company should also be required to state specific, aggressive
9 objectives concerning cash flow related options involving gas inventory
10 management, asset management agreements, low income (LIHEAP and Crisis)
11 grant programs, and other special projects.

12 17. If both the City and PGW make the necessary commitments, the Commission
13 should then authorize the imposition of a capital surcharge on ratepayers which
14 will match the City's annual commitment, up to \$18 million. The capital
15 surcharge would recover sufficient funds to pay interest (at a prevailing rate)
16 on the deferred City loan and eliminate the Company's short-term debt over
17 the next three years. The Commission should also allow PGW to submit a

1 restructuring plan which would allow a phase-in of certain restructuring
2 initiatives over time given its current financial position.

1 IV. EXTRAORDINARY RATE RELIEF

2 - Immediate Necessity

3 Q. WHAT IS YOUR UNDERSTANDING OF THE CRITERIA WHICH NEED TO BE
4 FULFILLED IN ORDER TO ALLOW ANY UTILITY TO SEEK
5 EXTRAORDINARY RATE RELIEF?

6 A. I have been advised by Counsel that the applicable Section 1308(e) states that such
7 revenue relief is appropriate if it is, among other things:

8 "Immediately necessary for the maintenance of financial stability in
9 order to enable the utility to continue providing normal services to its
10 customers, avoid reductions in its normal maintenance programs, [and]
11 avoid substantially reducing its employment . . ."

12 Q. HAS PGW ASSERTED THAT IT DOES NOT HAVE SUFFICIENT FINANCIAL
13 SECURITY TO FULFILL SUCH CRITERIA?

14 A. Not directly. Mr. Knudsen, at page 9 of his direct testimony, states that if S&P
15 downgrades the Company's bonds, PGW would then be unable to do its contemplated
16 forward purchase, have its Letter of Credit renewed for its current commercial paper
17 borrowing, or issue long-term bonds. He goes on to state, "Assuming that the
18 Company did not proactively respond to the crisis (which it would) PGW would stop
19 being able to pay its bills, fund payroll or do any construction whatever by August of

1 2002.” Thus, it would appear that there are two preconditions for the Company
2 before it would fulfill the section 1308(e) criteria. It would have to have its debt
3 downgraded by S&P and it would have to not respond to the envisioned, ensuing
4 crisis. At the current time, absent the actual bond downgrading, the Company has yet
5 to obtain from the City Council the deferred payment of its \$45 million loan or
6 prioritize its operating expenses and Construction Fund expenditures.

7 Q. WHAT IS THE SPECIFIC NATURE OF THE COMPANY’S EXTRAORDINARY
8 REVENUE RELIEF REQUEST?

9 A. Based on my review, the request addresses a working capital deficiency rather than
10 a traditional revenue requirement. This is not surprising, given that the Commission
11 recently authorized PGW a \$33.6 million base rate increase and granted an additional
12 \$10.8 million capital supplement from its ratepayers from the Company’s deferred
13 fuel account over recovery.

14 While S&P states that PGW needs approval of an adequate revenue increase
15 to forestall a downgrading, in reality PGW’s problem is inadequate capital. If PGW
16 had additional equity capital and no City loan and no outstanding commercial paper,
17 we would not have S&P threatening a downgrading. As stated, the extraordinary
18 revenue request is not intended to cover operating expenses, but rather it is an artifice
19 to justify funds above and beyond those necessary to meet bond coverages so that the

1 Company's deficient retained earnings can be augmented, not by its owner, but by its
2 captive firm ratepayers.

3 - Bond Downgradings

4 Q. WOULD YOU PLEASE DISCUSS THE S&P ANNOUNCEMENT WHICH
5 PROVIDES THE BASIS FOR THE COMPANY'S CLAIM FOR \$44 MILLION IN
6 EXTRAORDINARY RATE RELIEF?

7 A. On February 12, S&P issued a press release stating that without immediate cash flow
8 improvement, PGW's bond rating would be lowered. It went on to state that PGW's
9 poor liquidity was due, in part, to the Commission's action in authorizing the
10 Company \$31.0 million less than its previously requested rate increase. In order to
11 ensure that S&P's apparent requirements are met, the Company calculates that it now
12 needs an additional \$44 million revenue increase for its customers. This is based on
13 Ms. Bisgaier's interpretation of the S&P coverage formula and Mr. Bogdonavage's
14 analysis.

15 Q. DOES THE S&P ANNOUNCEMENT STATE ANY SPECIFIC AMOUNT OF
16 RATE RELIEF IT BELIEVES IS NECESSARY OR ANY TIME PERIOD IN
17 WHICH THE REVENUES MUST BE ADJUSTED?

1 A. No, it does not. As stated, the quantification of the necessary revenue relief is based
2 upon Ms. Bisgaier's formula. However, it is my experience that S&P looks at a large
3 number of factors when determining bond ratings. In order to satisfy the overall
4 requirements for a certain rating, a company may have deficiencies in some areas
5 which can be offset by strengths in others. Indeed, in S&P's announcement, various
6 PGW risk indicators associated with its liquidity problem are enumerated, but it is
7 also noted that PGW has several strengths which "offset the risks." Therefore, it is
8 unclear that any subsequent S&P rating reevaluation will be based solely on the
9 formula which is presented by Ms. Bisgaier. As for the time period of any
10 reevaluation, Mr. Knudsen states, on page 4 of his testimony, that "It is my
11 understanding that S&P will evaluate our circumstances in the next 6 weeks and will
12 determine whether the company has received sufficient permanent revenues to
13 improve its calculated coverages per S&P's formula." However, this time interval is
14 not contained within the referenced S&P announcement.

15 Q. HAVE THE OTHER RATING AGENCIES INDICATED ANY NEED FOR AN
16 IMMEDIATE REVENUE INCREASE IN ORDER FOR PGW TO AVOID A
17 DOWNGRADING?

18 A. Based on the rating reports provided by PGW in response to Request OCA-I-10 and
19 a recent article in The Bond Buyer (response to OCA-I-25), it does not appear so.

1 The Fitch analyst is quoted in The Bond Buyer as stated, “It’s bouncing along at the
2 triple-B level, and we’ll continue to watch it . . . We expect things are not going to run
3 smoothly for them but we still continue to feel that they’re going to be able to pay
4 their debts.” In the same article, the Moody’s analyst stated “If the utility does not get
5 that base rate increase and is required to pay back the city loan, the stress on the
6 utility’s liquidity will be significant . . . It’s very possible that at that point the rating
7 could be in trouble.”

8 Thus, it is only the Company’s interpretation of the views of the S&P analyst
9 which implies that without immediate revenue relief or project revenues the PGW
10 debt will be downgraded. This is not to say that PGW does not have a liquidity
11 problem, but rather it is unclear that the sole remedy is an immediate \$44 million
12 revenue increase. To place the liquidity problem in context, it is useful to note some
13 of the elements cited as PGW’s risks and weaknesses by Moody’s Investors Service
14 in a February 2002 analysis contained in the response to Request OCA-I-10. Some
15 of the noted risks were:

- 16 – A record of management instability has long affected the utility’s
17 progress in sustaining a record of financial soundness and improvement
18 in its competitive position. Failure to meet deadline to appoint new
19 management remains a concern.
- 20 – While there are opportunities in the transition to state regulation, PGW,
21 as a city owned utility, will still be pressured by potential political
22 influences that could complicate management of the gas business.

1 – Poor management of the utility’s accounts receivable problem in the
2 past has burdened PGW’s financial soundness.

3 Accordingly, PGW’s impaired financial condition is not solely a function of
4 cash flow, nor does its financial improvement rely solely on the immediate attainment
5 of additional revenues. S&P, along with the other rating agencies, would be more
6 favorably inclined toward PGW if permanent management had been approved, the
7 \$45 million City debt had been restructured with a realistic deferred payback period,
8 the accounts receivable balance had been managed effectively, and capital
9 expenditures and cash flow had been managed better in the past. It is not the
10 Commission which has control over these determinants of financial improvement, and
11 it is unreasonable that it be given an immediate ultimatum to require PGW’s
12 ratepayers to be the only ones to shoulder the burden.

1 V. BASIS FOR PGW'S CLAIM

2 - The Standard and Poor's Formula

3 Q. WOULD YOU PLEASE DISCUSS THE S&P FORMULA WHICH PROVIDES
4 THE BASIS FOR THE COMPANY'S \$44 MILLION EXTRAORDINARY RATE
5 REQUEST?

6 A. According to Ms. Bisgaier's testimony, S&P has provided the Company with the
7 standards and calculations it uses to evaluate PGW's debt. In addition, she states that
8 S&P provided PGW with the coverage formula which it uses in assessing PGW.
9 While S&P recognizes that PGW's 1.5 times debt service indenture requirement is a
10 positive credit factor, it dramatically raises the debt rating threshold by measuring
11 fixed obligations rather than just debt service. Under this revised coverage test, the
12 \$18 million obligation to the City, as well as the \$20 million reduction to the
13 commercial paper amount, in effect, become part of the coverage equation which they
14 are not under PGW's bond indenture. Based on Ms. Bisgaier's testimony, under this
15 revised calculation, PGW's coverage is estimated to be 0.88x for the year ended
16 August 31, 2002 and 0.97x for the year ended August 31, 2003. Ms. Bisgaier's
17 description of the S&P coverage derivation is contained on pages 4 and 5 of her
18 testimony and the associated S&P worksheet is reproduced as Exhibit BCB-3.

1 Once having established this coverage calculation, S&P requires that in order
2 for PGW to maintain an investment grade bond rating, it would have to show at least
3 a 1.20x to 1.30x coverage level apparently without taking into account any funds
4 which S&P deems to be “non-recurring.” Were this not enough of a challenge, Ms.
5 Bisgaier goes on to state, “Absent the grant of emergency rate relief so that this fixed
6 cost coverage can be achieved on a permanent ongoing basis, Standard and Poor’s
7 will take negative credit action within the next two months” (Bisgaier Testimony,
8 page 5).

9 Q. GIVEN THIS DESCRIPTION OF S&P’S COVERAGE CALCULATION AND ITS
10 “REQUIRED” MINIMUM ACCEPTABLE COVERAGE THRESHOLD RANGE,
11 HOW DOES THIS GET TRANSLATED INTO A \$44 MILLION REVENUE
12 INCREASE REQUIREMENT?

13 A. In Mr. Bogdonavage’s testimony at page 2, he states that he makes a calculation on
14 his Exhibit JRB-2 which “utilizes the ‘coverage’ calculation and requirements that
15 Ms. Bisgaier testifies S&P utilizes in evaluating the financial position of a municipal
16 utility.”

17 Q. PLEASE COMMENT ON MR. BOGDONAVAGE’S EXHIBIT JRB-2.

1 A. Exhibit JRB-2 purports to show a projected income statement and a projected debt
2 service coverage statement utilizing a “current estimate” of fiscal year 2002 data and
3 a “test year budget”.

4 Q. HAS MR. BOGDONAVAGE EXPLAINED AND SUPPORTED THE BASIS FOR
5 HIS CURRENT 2002 ESTIMATE AND THE TEST YEAR BUDGET?

6 A. Not within the extraordinary rate relief filing. He has provided supporting
7 information within the Company’s base rate filing, but that material has yet to be
8 subjected to the review and analysis which will be done within the base rate
9 investigation.

10 Q. REGARDING THE “CURRENT ESTIMATE” DATA, IS INFORMATION
11 PROVIDED EXPLAINING WHAT PERIOD THE ACTUAL DATA
12 REPRESENTS?

13 A. No, that information is not provided, nor is information provided explaining how the
14 projected data was determined. However, during informal discovery, Mr.
15 Bogdonavage stated that the Current Estimate is composed of five months of actual
16 data (September - January) and seven months of projected data. It is assumed that the
17 projected data for the months February - August represents the Fiscal Year 2002
18 Compliance Budget presented to the Philadelphia Gas Commission.

1 Q. REGARDING THE FULLY FORECASTED "TEST YEAR BUDGET" DATA, IS
2 IT CLEAR HOW THIS DATA WAS DETERMINED?

3 A. The basis for the forecast appears to be the above-mentioned Compliance Budget.
4 The reply to OCA-21c states that the major assumptions included in the fully
5 forecasted data are included in Mr. Bogdonavage's base rate testimony. However, the
6 test year budget data includes a number of claimed pro forma adjustments which may
7 or may not be accepted by the Commission for ratemaking purposes. Therefore, the
8 Company's claimed revenue requirement may be overstated.

9 - Traditional Coverage Measurements

10 Q. THE MAJOR PURPOSE OF HIS EXHIBIT APPEARS TO BE TO DERIVE THE
11 REVENUE REQUIREMENT NECESSARY FOR THE COMPANY TO ACHIEVE
12 THE S&P COVERAGE RATIO OF BETWEEN 1.20X AND 1.30X AS STATED
13 BY MS. BISGAIER. PLEASE COMMENT ON THE USE OF THE S&P
14 FORMULA AS COMPARED TO THE NORMAL DEBT SERVICE COVERAGE
15 FORMULA.

16 A. The debt service coverage formula, as contained in the 1998 bond ordinance, is
17 calculated as follows: Funds Provided, which are mainly operating revenue and other
18 income are reduced by Funds Applied which are comprised of operating expense

1 including fuel but not depreciation. The resultant amount equals Funds Available.
2 In turn, Funds Available, when divided by the 1975 Debt Service, equals Coverage
3 on the 1975 Debt. Similar calculations are then made for coverage on the 1998 Debt
4 Service and for Debt Service on the small amount of subordinated debt.

5 Q. HOW, THEN, DOES THE S&P FIXED RATE COVERAGE RATIO DIFFER
6 FROM THE BOND ORDINANCE COVERAGE CALCULATION?

7 A. As discussed previously, the main differences are that the S&P formula requires
8 coverage on the \$18 million City dividend and the \$20 million Tax Exempt
9 Commercial Paper payback (due by the end of the fiscal year) while the bond
10 ordinance debt coverage ratio does not. Needless to say, these additional payments
11 of \$38 million lower the coverage ratio calculated by the S&P formula by a
12 considerable amount. To be clear, this additional coverage is not legally required by
13 the 1998 bond ordinance; rather it is used by S&P for its own purposes. The
14 Company then utilizes this formula to show that a \$44 million base revenue increase
15 is necessary to achieve the fixed coverage ratio, required by S&P, for the “test year
16 budget” numbers.

17 Q. THE CURRENT ESTIMATE FOR FISCAL YEAR 2002 SHOWS A 1.28X
18 COVERAGE ON 1998 SENIOR DEBT SERVICE UNDER THE PGW BOND

1 INDENTURE FORMULA. WHAT WOULD BE THE COVERAGE IF THE \$18
2 MILLION CITY PAYMENT WAS GRANTED BACK TO THE PGW AS
3 "PROJECT REVENUE", AS THE CITY HAS OFFERED?

4 A. As shown on Schedule 1, the grant back would result in coverage on 1998 senior debt
5 of 1.87x, well above the required 1.50x. Thus, if the City actually were to grant back
6 the City payment, there would be no actual coverage problem for FY2002 under
7 PGW's bond indenture. If one assumes that the Company's Margin Loss due to
8 warmer than normal weather will actually equal \$30 million, then the indenture
9 coverage falls to 1.12x and with an \$18 million grant back it would be 1.70x or still
10 above the required 1.50x under PGW's bond indenture.

11 Q. BASED ON THE S&P RANGE OF TARGETED OR ACCEPTABLE
12 COVERAGES, OF BETWEEN 1.2X AND 1.3X, WHAT WOULD BE THE
13 MINIMUM PROJECT REVENUES NEEDED FOR PGW TO ACHIEVE THE 1.2X
14 COVERAGE IT STATES THAT S&P IS LOOKING FOR?

15 A. On Schedule 2, calculations are shown which measure the level of project revenues
16 necessary to achieve 1.2x coverage using the Company's calculations under the S&P
17 formula. As shown, project revenues of \$35.4 million would meet this minimum S&P
18 coverage level all other things being equal. It is again important to note that this

1 \$35.4 million is far more than under PGW's bond indenture and is being driven by
2 S&P's inclusion of capital requirements and the City payment in its formula.

3 - Capital Vs. Revenue Need

4 Q. WHY HAVE YOU DIFFERENTIATED BETWEEN A CAPITAL AS OPPOSED
5 TO A REVENUE REQUIREMENT IN YOUR TESTIMONY?

6 A. As I understand it, Section 1308(e) addresses extraordinary needs for revenues to
7 meet operating expenses. It does not contemplate a utility seeking a capital
8 contribution from its ratepayers. Accordingly, it is my belief that the Section 1308(e)
9 provisions are not applicable to PGW's rate relief request.

10 Utility regulation has consistently recognized that ratepayers are responsible
11 for a utility's operating expense, including a return on the utility's capital. However,
12 there is no precedent, to my knowledge, where ratepayers have been held responsible
13 to serve as the initial source of funds to meet a utility's capital needs. Therefore, by
14 definition, the Section 1308(e) provisions do not contemplate, nor provide, a standard
15 for PGW's pending request.

1 Q. DOES THE COMPANY'S SO-CALLED CASH FLOW METHOD OF RATE
2 SETTING SPECIFY WHAT WOULD BE A REASONABLE LEVEL OF
3 WORKING CAPITAL TO BE OBTAINED FROM RATEPAYERS?

4 A. No, it does not. Nor is there any specification as to what treatment should be afforded
5 any capital contribution which is obtained from ratepayers under the cash flow
6 methodology. In my opinion, if the basis for recovery from ratepayers is a capital
7 insufficiency, then such a recovery must be viewed as a capital contribution which
8 will be recorded on the Company's books.

9 Q. MR. LELASH, YOU TESTIFY THAT PGW DOES NOT REQUIRE
10 EXTRAORDINARY RELIEF TO MEET ITS OPERATING EXPENSES. DOES
11 PGW NEED ASSISTANCE TO STABILIZE ITS FINANCIAL CONDITION?

12 A. Based on the severity of the Company's liquidity problems, it would appear that a
13 capital surcharge may have to be considered if the Commission believes that the
14 Company's current financial condition warrants it. However, any associated capital
15 which is authorized cannot be considered to be traditional revenues for operating
16 expenses. Accordingly, it is recommended that the Commission address the Company
17 request for what it is, a capital requirement under the cash flow method and not an
18 extraordinary rate request.

1 If the Commission takes action to address PGW's capital situation, it should
2 define both the showing required for the granting of capital relief for PGW and the
3 procedures which must be followed by PGW in accounting for the capital.

4 Q. GIVEN THE NATURE OF PGW'S FINANCIAL POSITION, DO YOU BELIEVE
5 THAT IT IS APPROPRIATE TO EVALUATE PGW'S CAPITAL NEED AT THIS
6 TIME?

7 A. As the Commission is aware, PGW has been a troubled utility for an extended period
8 of time. When the Company's rate setting authority was transferred to this
9 Commission, service was at unacceptable levels, wholesale gas prices were rising to
10 unprecedented highs, and the Company's financial condition was severely impaired.
11 However, despite the financial constraints, the situation has improved due to lower
12 natural gas prices and progress toward improved service. This is not to say that there
13 are not many continuing problems which have to be addressed and solved. However,
14 were the Company to be downgraded at this time, thereby requiring contingency
15 actions in order to maintain service, the progress to date could be lost and the prospect
16 for PGW achieving acceptable performance levels would be delayed for an extended
17 period of time.

18 Therefore, if the Commission determines that incremental capital is required,
19 if the City makes the necessary commitments and the Commission further determines

1 that it would now be reasonable for ratepayers to provide a portion of such capital to
2 address this problem, then I believe a time-limited capital surcharge would be
3 appropriate.

4 However, such a surcharge should not be based on the potential requirements
5 of one rating agency, but rather it must represent a balance considering just and
6 reasonable rates and PGW's long-term capital needs. It also should put into place a
7 multi-year rehabilitation plan for the Company which will restore its liquidity and
8 stabilize its financial condition.

1 VI. CAPITAL SOURCES AND RESPONSIBILITIES

2 Q. HOW SHOULD THE COMMISSION ADDRESS PGW'S CAPITAL AND
3 LIQUIDITY PROBLEMS?

4 A. It is important that the Commission take actions which will stabilize PGW's financial
5 condition in concert with actions by the other PGW stakeholders. The Commission
6 recognized this concept in its December 6, 2001 Opinion and Order (Docket No. R-
7 00006042) when it stated that PGW's "Management Agreement does not assure that
8 customer rates will cover all PGW's capital and cash needs as if no other sources of
9 capital or revenues are available to PGW."

10 This Commission position had previously been expressed in its October 4,
11 2001 Opinion and Order where the Commission "urged the City of Philadelphia, as
12 owner of PGW, to continue to take measures to insure the financial health of PGW.
13 It is the expectation of this Commission that the City of Philadelphia, as owner of
14 PGW, will continue to assist PGW in its cash flow requirements so that a financial
15 crisis does not take place."

16 The appropriate catalyst for such concerted efforts would be for the
17 Commission to seek commitments from PGW and the City to take the necessary steps
18 to ameliorate the current financial crisis with the assurance that it will address and

1 require ratepayer capital which is sufficient to enable PGW to improve its overall
2 financial condition.

3 - City Ownership Obligations

4 Q. WHAT TYPE OF COMMITMENTS DO YOU BELIEVE NEED TO BE MADE BY
5 THE CITY?

6 A. The first and most significant commitment would be direct recognition that the City,
7 as PGW's owner, must acknowledge its ownership obligations. Were PGW to fail,
8 it would be the City itself, and indirectly the gas consumers of the City, who would
9 be harmed. A reasonable analogy would be a homeowner who fails to do necessary
10 maintenance on his house. Ultimately, in addition to having to live in a state of
11 disrepair, the owner will realize a substantial decline in the value of his asset and
12 ultimately a lower sales price if and when he decides to sell.

13 Q. HASN'T THE CITY CLAIMED THAT ITS CURRENT AND PROJECTED
14 FINANCIAL CONDITION PRECLUDE IT FROM PROVIDING ASSISTANCE TO
15 PGW?

16 A. Yes, Ms. Davis, in her direct testimony at page 3, states that, "the City presently has
17 very limited ability to provide even temporary additional assistance to PGW." She

1 enforces this point by stating that, “the City was forced to take drastic steps to avoid
2 a \$296 million deficit . . .” Ms. Davis also makes a comparison to May of 2001 when
3 the City was then projecting a surplus in excess of \$180 million. Her testimony at that
4 time is instructive. When asked whether or not the City would be able to grant
5 additional assistance to PGW, her answer was “Unfortunately no. The City is not in
6 a position to offer any additional monetary assistance to PGW.” Thus, in good or bad
7 times the City has taken the position that “PGW, as a municipal utility, is intended to
8 be self sufficient” (Davis Testimony, Docket No. R-00006042, page 3).

9 As the Director of Finance for the City, and the only City representative to
10 testify in prior rate proceedings, her statements reflect the City’s views and its
11 willingness to acknowledge the City’s obligations to PGW. The City’s position as
12 expressed by Ms. Davis has been:

13 “. . . a decision to set PGW’s revenue requirement at inadequate levels,
14 with the assumption that the City will produce the necessary additional
15 dollars to make up for the inadequate award, would inappropriately
16 transfer City policy decisions to a state administrative agency - the
17 PUC.”

18 “PGW’s cash requirements are driven entirely by its operating
19 expenses, and customers are not asked to provide a return on the cash
20 working capital or on equity.” (Davis Testimony, Docket No.
21 R-00006042, pages 3-4).

22 “. . . PGW assets have been accumulated with the City’s involvement
23 as the entity bearing the ultimate risk and responsibility for the
24 enterprise and as the equity participant.”

1 “In that retained earnings are treated as equity for accounting purposes,
2 the City Payment is appropriately viewed as a distribution of retained
3 earnings to the owners of the enterprise.” (Davis PGC Testimony,
4 FY2001, page 4).

5 Q. WHAT DO THESE FOUR QUOTATIONS INDICATE CONCERNING THE
6 CITY’S FINANCIAL OBLIGATIONS TO PGW AND THE THREATENED
7 DOWNGRADING OF PGW’S DEBT?

8 A. The first quotation reflects the City’s overall view of the current ratemaking calculus.
9 It has taken the position that it should be able to obtain revenue increases regardless
10 of whether or not the associated rates are just and reasonable. In my view, the City
11 must acknowledge the Commission’s rate setting authority and it must understand
12 that, if just and reasonable rates are not enough, then it needs to augment PGW’s
13 finances.

14 The second quotation reflects a misunderstanding of utility regulation and
15 PGW’s current financial situation. PGW’s cash requirements are not entirely driven
16 by its operating expenses. Capital repayments and the need for the retirement of
17 short-term debt balances are the major determinant of the liquidity problem.
18 Additionally, ratepayers, in fact, pay a return on both working capital and equity. The
19 interest on the outstanding commercial paper and the dividend received by the City,
20 as discussed in the fourth quotation, are clear evidence of both types of payments.

1 However, it is the third quotation which best illustrates the dichotomy of the
2 City's position concerning PGW. If the City actually bears the risk and responsibility
3 for the enterprise, and solely receives any earnings and profits from its operation, then
4 it must be at least partially responsible for its capital sufficiency.

5 Q. OVER THE PAST SEVERAL YEARS, WHAT HAS BEEN THE CITY'S RETURN
6 ON ITS PGW INVESTMENT?

7 A. Since 1996, the City has received \$108 million dollars from PGW. During this same
8 time period its City Equity has declined from \$263 million to \$204 million and
9 PGW's equity percentage has fallen from 25.9% to 16.2%. Had the City been willing
10 to receive a 50% payment of earnings rather than 100%, this dramatic decline in
11 equity would not have occurred. The data which shows the capital accounts for PGW
12 during the last six years is shown on Schedule 3. It is instructive that the \$108 million
13 which was withdrawn from PGW is equal to the amount of PGW's increase in
14 short-term debt since 1996. Thus, had PGW's earnings during the period been
15 retained rather than paid out as dividends, the Company's short-term debt would be
16 \$15 million and there would not be either a financial or liquidity crisis.

1 Q. BASED ON YOUR EVALUATION OF THE SITUATION, WHAT ACTIONS
2 SHOULD THE CITY COMMIT TO AS PART OF ANY PROSPECTIVE
3 FINANCIAL RECOVERY?

4 A. The following appear to be the necessary commitments:

- 5 • Restructuring of the City's loan with payback over the next three fiscal years.
6 Additionally, interest should be paid to the City during the payback period.
- 7 • Grant back of the City's payment (\$18 million) for at least three years.
- 8 • The designation of permanent management for PGW and disclosure of the
9 major findings and conclusions concerning the feasibility and desirability of
10 the City's sale of PGW.

11 - Required PGW Actions

12 Q. AS PART OF ANY FRAMEWORK FOR PGW'S FINANCIAL RECOVERY,
13 WHAT ACTIONS WILL BE REQUIRED BY THE COMPANY ITSELF?

14 A. In order to conserve cash, the Company needs to take a thorough look at all aspects
15 of its on-going operations and determine which activities, if any, can realistically be
16 deferred without harming reliability or customer service. Once identified, the
17 Company should establish written objectives and action plans concerning identified

1 activities and it should quantify their impact on operational and financial results. A
2 second requirement should be for the Company to finish developing and then
3 implement a comprehensive collection program. This program should enable the
4 Company to substantially increase its collection percentage and increase its on-going
5 cash flow.

6 In addition to these activities, the Company should be required to establish
7 specific and aggressive initiatives concerning several cash flow related areas
8 including the following:

- 9 • Gas storage management which will minimize the Company's overall
10 investment in gas inventory.
- 11 • utilization of asset management agreements if they can be structured
12 economically and allow the deferral of gas acquisition.
- 13 • increased customer sign up for external low income assistance (LIHEAP and
14 Crisis Grants) in order to maximize revenues while reducing customer bills.
- 15 • deferral, if feasible, of special projects and a phase in of the restructuring
16 contemplated by the Act.

1 While I believe that such actions by PGW will delay current management's
2 initiatives in certain areas, their deferral is required if the contemplated regulatory
3 framework is to be sufficient to restore the Company's long-term financial health.

4 - Ratepayer Responsibilities

5 Q. WHAT ACTIONS WILL NEED TO BE TAKEN BY THE COMMISSION IN
6 ORDER TO ENSURE THAT RATEPAYERS ARE RESPONSIBLE FOR ONLY A
7 FAIR SHARE OF THE COST TO RESTORE PGW'S LIQUIDITY?

8 A. The Commission must determine if ratepayers should be required to supply some
9 reasonable amount of the Company's working capital requirements. And, as stated
10 in the prior Commission Opinion and Order in Docket No. R-00006042, the rates for
11 customers do not need to cover all of the Company's capital and cash needs.
12 Therefore, given the current financial condition of PGW, it appears that ratepayers,
13 separate and apart from paying for the Company's operating expenses, may need to
14 make some capital contribution as part of a comprehensive plan to restore PGW's
15 financial health.

16 In previous testimony concerning PGW's prior base rate request, I
17 recommended that the Commission award the minimum reasonable rate increase
18 because of the very high prevailing wholesale natural gas prices and, to a lesser

1 degree, the Company's then inadequate service levels. At that time I also
2 acknowledged that some augmentation of the Company's retained earnings would be
3 necessary in the future. As is evident, the future is now, and PGW can no longer
4 work around its liquidity problems or its highly leveraged capital structure.

5 Since the prior base rate proceeding, wholesale natural gas prices have fallen
6 considerably such that the Company's March 1, 2002 Quarterly Gas Cost Rate
7 ("GCR") filing reflects a decrease to a \$2.0203 per Mcf level. This is in sharp
8 contrast to the GCR in effect during 2001 of \$6.6959 per Mcf. With respect to
9 service levels, the Company has pursued activities which have lessened the problems
10 which were identified in the last proceeding. Accordingly, with far lower GCR levels
11 and improved customer service, it now may be an appropriate time for the
12 Commission to address PGW's capital deficiency.

13 Q. BASED ON THE CONSIDERATIONS YOU HAVE DISCUSSED, DO YOU HAVE
14 A SPECIFIC CAPITAL SURCHARGE RECOMMENDATION FOR THE
15 COMMISSION?

16 A. Any ratepayer capital contribution which is authorized will have to be determined
17 within the context of what the City is prepared to contribute to address the liquidity
18 problem. In my opinion, it would be reasonable for ratepayers to match any amount
19 of annual project revenues, up to \$18 million, which the City would make available

1 to PGW during the next three years. Additionally, any such capital contributions
2 should be separately recorded on the Company's books.

3 At this point I recommend that the Commission establish this framework
4 contingent on the commitments from the City and PGW as discussed previously. It
5 appears that the PGW liquidity issue must be addressed first before the traditional
6 revenue requirement determination. To this end, I recommend that any capital
7 contribution which may ultimately be granted should be recovered through a
8 time-limited capital surcharge which would be used exclusively for interest on the
9 deferred City loan and for short-term debt reduction. By utilizing a surcharge
10 mechanism, any associated capital contribution from ratepayers would have a defined
11 duration and specified purpose.

12 Q. WOULD THE TYPE OF COMMITMENTS AND CAPITAL CONTRIBUTION
13 WHICH YOU ENVISION BE SUFFICIENT TO RESTORE PGW'S LIQUIDITY
14 AND FINANCIAL STABILITY?

15 A. In my opinion, they would. It must be understood that PGW needs to have a working
16 capital reserve in order to meet the cash requirements associated with escalations in
17 wholesale gas prices and the seasonal nature of its revenues and expenses. As
18 specified, the three year capital contribution would provide an opportunity for a
19 permanent solution. Short-term debt would be reduced by almost \$110 million and

1 retained earnings should be increased by at least that amount. Such capital
2 contributions would increase PGW's equity ratio to about 25% and reduce its
3 commercial paper balance to about \$15 million which is about what they were in
4 1996. The capital contributions would also represent an on-going commitment for the
5 three year period. As such, they should provide sufficient justification for PGW's
6 bond ratings to remain at current levels.

7 Q. WILL THIS LEVEL OF CAPITAL INFUSION BE SUFFICIENT DURING THE
8 PERIOD WHILE THE FILED BASE RATE CASE IS PENDING?

9 A. Yes, it should be. There never was an expectation that capital contributions, whether
10 at the \$44 or \$36 million level, would be able to provide a significant increase in
11 working capital over the next several months. Rather, if PGW's bond rating are
12 affirmed, the Company will be able to obtain its planned forward purchase agreement
13 which will yield about \$20 million of incremental project revenues. This agreement,
14 along with the impact of the capital contributions and proactive efforts by the
15 Company on accounts receivable collection and operating expense and capital
16 expenditure control, should provide sufficient working capital for the remainder of
17 this year.

1 Q. DOES THAT COMPLETE YOUR TESTIMONY IN THIS MATTER?

2 A. Yes, it does.

VII. SUPPORTING SCHEDULES

**Philadelphia Gas Works
Debt Service Coverage
Fiscal Year 2001-02
\$(000)**

	Current Estimate 2001-02 (1)	Current Estimate 2001-02 (2)
<u>Funds Provided</u>		
Total Operating Revenues	\$672,188	\$672,188
Margin Loss	(25,000)	(25,000)
City Fee Grant Back		18,000
Other Revenues	27,450	27,450
Other Income	4,963	4,963
AFUDC	775	775
Total Funds Provided	<u>680,376</u>	<u>698,376</u>
<u>Funds Applied</u>		
Fuel Costs	373,026	373,026
Other Operating Expenses	242,347	242,347
Less: Non-Cash Expenses	36,165	36,165
Total Funds Applied	<u>579,208</u>	<u>579,208</u>
Funds Available to Cover Debt Svc.	<u>\$101,168</u>	<u>\$119,168</u>
1975 Ordinance Bonds Debt Service	\$55,528	\$55,528
Debt Service Coverage 1975 Bonds	<u>1.82</u>	<u>2.15</u>
Net Available After Prior Debt Service	\$45,640	\$63,640
PMA & Other Capital Leases	5,954	5,954
Net Available After Prior Capital Leases	<u>\$39,686</u>	<u>\$57,686</u>
1998 Ordinance Bonds Debt Service	\$30,926	\$30,926
Debt Service Coverage 1998 Bonds	<u>1.28</u>	<u>1.87</u>
Net Available After 1998 Debt Service	\$8,760	\$26,760
1998 Ordinance Subordinate Bond Debt Serv	\$1,986	\$1,986
Debt Service Coverage Subordinate Bond	<u>4.41</u>	<u>13.47</u>

Note: Column (2) includes an \$18 million grant-back from the City.

Source: Exhibit JRB-2

Philadelphia Gas Works
Fixed Rate Coverage Ratio
Fiscal Year 2001-02
\$(000)

	Current Estimate 2001-02 (1)	Test Year Budget 2001-02 (2)
<u>Funds Provided</u>		
Total Operating Revenues	\$672,188	\$638,733
(Margin Loss)/Rate Increase	(25,000)	35,352
Other Revenues	27,450	28,117
Other Income	4,963	5,743
AFUDC	775	775
Total Funds Provided	<u>680,376</u>	<u>708,720</u>
<u>Funds Applied</u>		
Fuel Costs	373,026	334,576
Other Operating Expenses	242,347	251,436
Less: Non-Cash Expenses	36,165	36,165
Total Funds Applied	<u>579,208</u>	<u>549,847</u>
Funds Available to Cover Debt Svc.	<u>\$101,168</u>	<u>\$158,873</u>
1975 Ordinance Bonds Debt Service	\$55,528	\$55,528
Debt Service Coverage 1975 Bonds	<u>1.82</u>	<u>2.86</u>
Net Available After Prior Debt Service	\$45,640	\$103,345
PMA & Other Capital Leases	5,954	5,954
Net Available After Prior Capital Leases	<u>\$39,686</u>	<u>\$97,391</u>
1998 Ordinance Bonds Debt Service	\$30,926	\$30,926
Debt Service Coverage 1998 Bonds	<u>1.28</u>	<u>3.15</u>
Net Available After 1998 Debt Service	\$8,760	\$66,465
1998 Ordinance Subordinate Bond Debt Serv	\$1,986	\$1,986
Debt Service Coverage Subordinate Bond	<u>4.41</u>	<u>33.47</u>
Net Avail to Service Aggregate Debt	<u>\$101,168</u>	<u>\$158,873</u>
Aggregate Debt Service	\$94,394	\$94,394
Fixed Rate Coverage Ratio on Aggregate Debt Service	1.07	1.68
Aggregate Debt Service & \$18M	\$112,394	\$112,394
Fixed Rate Coverage Ratio Incl. \$18M City Fee	0.90	1.41
Aggregate Debt Service & \$18M & \$20M	\$132,394	\$132,394
Fixed Rate Coverage Ratio Incl. \$18M City Fee & \$20M TXCP Payment	0.76	1.20

Source: Exhibit JRB-2

Schedule 3

**Philadelphia Gas Works
Debt and Equity Data
\$(000)**

Fiscal Year Ended	Long Term Debt (1)	Short Term Debt (2)	City Equity (3)	Total Capital (4)	Equity % (5)
1996	739,408	15,000	263,252	1,017,660	25.9%
1997	728,130	30,000	268,987	1,027,117	26.2%
1998	818,323	56,190	251,962	1,126,475	22.4%
1999	897,134	75,278	231,711	1,204,123	19.2%
2000	856,502	97,059	211,300	1,164,861	18.1%
2001	933,402	123,000	204,454	1,260,856	16.2%

Source: 1996-2000, Deloitte & Touche Independent Auditors' Reports
2001, Volume II, Exhibit A-4

VIII. APPENDIX: PRIOR R.W. LELASH TESTIMONIES

R. W. LELASH'S REGULATORY TESTIMONIES
(1997 to Present)

198. Georgia, Atlanta Gas Light (Docket No. 6717-U) Gas Service Unbundling Testimony for the Georgia Public Service Commission (January, 1997).
199. FERC, Cleveland Electric and Toledo Edison (Docket No. ER97-529-000, Consolidated) Rate of Return Rebuttal Testimony for Centerior Energy (April, 1997).
200. Rhode Island, Providence Gas Company (Docket No. 2581) Price Stabilization Plan Testimony for the Rhode Island Division of Public Utilities (August, 1997).
201. New Jersey, New Jersey Natural Gas Company (Docket No. GT96070524) Gas Policy Testimony for the New Jersey Division of the Ratepayer Advocate (August, 1997).
202. Vermont, Green Mountain Power Corporation (Docket No. 5983) Gas Remediation Recovery Testimony for the Vermont Department of Public Service (October, 1997).
203. Philadelphia Gas Commission, Philadelphia Gas Works (1998 GCR Proceeding) Gas Procurement and Policy Testimony for the Public Advocate (December, 1997).
204. Vermont, Green Mountain Power Corporation (Docket No. 5983) Gas Remediation Surrebuttal Testimony for the Vermont Department of Public Service (December, 1997).
205. Delaware, Delmarva Power & Light Company (Docket No. 97-293F) Gas Price Hedging Testimony for the Delaware Public Service Commission (January, 1998).
206. Delaware, Artesian Water Company (Docket No. 97-340) Rate of Return Testimony for the Delaware Public Service Commission (February, 1998).
207. Georgia, Atlanta Gas Light Company (Docket No. 8390-U) Regulatory Policy Testimony for the Energy Service Providers Association (March, 1998).
208. New Jersey, Public Service Electric & Gas Company (Docket No. GR97110839) Gas Procurement and Policy Direct Testimony for the New Jersey Division of the Ratepayer Advocate (April, 1998).
209. New Jersey, Public Service Electric & Gas Company (Docket No. GR97110839) Gas Procurement and Policy Surrebuttal Testimony for the New Jersey Division of the Ratepayer Advocate (April, 1998).
210. Philadelphia Gas Commission, Philadelphia Gas Works (1998 GCR Proceeding) Gas Price Hedging Position Statement for the Public Advocate (May, 1998).
211. Philadelphia Gas Commission, Philadelphia Gas Works (1999 GCR Proceeding) Gas Procurement and Policy Testimony for the Public Advocate (October, 1998).
212. Georgia, Cumberland Pipeline Investigation (Docket No. 10064-U) Regulatory Policy Testimony for East Tennessee Natural Gas Company (March, 1999).

213. New Jersey, Generic Unbundling Proceeding (Docket No. GX99030121) Gas Policy Testimony for the New Jersey Division of the Ratepayer Advocate (July, 1999).
214. New Jersey, Public Service Electric & Gas Company (Docket No. GO99030124) Gas Unbundling Testimony for the New Jersey Division of the Ratepayer Advocate (July, 1999).
215. Philadelphia Gas Commission, Philadelphia Gas Works (2000 GCR Proceeding) Gas Procurement and Policy Testimony for the Public Advocate (September, 1999).
216. New Jersey, Generic Unbundling Proceeding (Docket No. GX99030121) Gas Policy Surrebuttal Testimony for the New Jersey Division of the Ratepayer Advocate (September, 1999).
217. New Jersey, Public Service Electric & Gas Company (Docket No. GO99030124) Gas Unbundling Surrebuttal Testimony for the New Jersey Division of the Ratepayer Advocate (September, 1999).
218. Pennsylvania, Columbia Gas of Pennsylvania, Inc. (Docket No. R-00994781) Restructuring Testimony for the Pennsylvania Office of Consumer Advocate (October, 1999).
219. Pennsylvania, Columbia Gas of Pennsylvania, Inc. (Docket No. R-00994781) Restructuring Surrebuttal Testimony for the Pennsylvania Office of Consumer Advocate (October, 1999).
220. Rhode Island, Narragansett Electric Company et al. (Docket No. 2930) Merger Policy Testimony for the Rhode Island Department of Attorney General (November, 1999).
221. Delaware, Delmarva Power & Light Company (Docket No. 99-425F) Evaluation of Price Hedging Testimony for the Delaware Public Service Commission (December, 1999).
222. Rhode Island, Narragansett Electric Company et al. (Docket No. D-99-12) Merger Policy Testimony for the Rhode Island Department of Attorney General (December, 1999).
223. Pennsylvania, PECO Energy Company (Docket No. R-00994787) Restructuring Testimony for the Pennsylvania Office of Consumer Advocate (January, 2000).
224. Pennsylvania, PECO Energy Company (Docket No. R-00994787) Restructuring Surrebuttal Testimony for the Pennsylvania Office of Consumer Advocate (February, 2000).
225. Rhode Island, Providence Gas Company and Southern Union (Docket No. D-00-3) Merger Policy Testimony for the Rhode Island Division of Public Utilities and Department of Attorney General (May, 2000).
226. Philadelphia Gas Commission, Philadelphia Gas Works (2001 GCR Proceeding) Gas Procurement and Policy Testimony for the Public Advocate (August, 2000).
227. Rhode Island, Providence Gas Company (Docket No. 1673) Price Stability Plan Testimony for the Rhode Island Division of Public Utilities (September, 2000).
228. Pennsylvania, Philadelphia Gas Works (Docket No. R-00005654) Interim Base Rate Testimony for the Pennsylvania Office of Consumer Advocate (September, 2000).
229. Pennsylvania, Philadelphia Gas Works (Docket No. R-00005619) Gas Procurement and Policy Testimony for the Pennsylvania Office of Consumer Advocate (September, 2000).

230. New Jersey, Public Service Electric & Gas Company (Docket No. GR00070491) Levelized Gas Adjustment Clause Testimony for the New Jersey Division of the Ratepayer Advocate (November, 2000).
231. New Jersey, Generic Provisional Rate Proceeding (Docket Nos. GR00070491, et al.) Provisional Rate, Flexible Pricing, and Price Hedging Testimony for the New Jersey Division of the Ratepayer Advocate (December, 2000).
232. Rhode Island, Providence and Valley Gas Companies (Docket Nos. 1673 and 1736) Gas Price Mitigation Testimony for the Rhode Island Division of Public Utilities (January, 2001).
233. Delaware, Delmarva Power & Light Company (Docket No. 00-463F) Gas Price Hedging Testimony for the Delaware Public Service Commission (February, 2001).
234. Pennsylvania, Philadelphia Gas Works (Docket No. R-00006042) Base Rate and Policy Testimony for the Pennsylvania Office of Consumer Advocate (April, 2001).
235. Pennsylvania, Philadelphia Gas Works (Docket No. R-00006042) Base Rate and Policy Surrebuttal Testimony for the Pennsylvania Office of Consumer Advocate (May, 2001).
236. New Jersey, Public Service Electric & Gas Company (Docket No. GM00080564) Capacity Contract Transfer Testimony for the New Jersey Division of the Ratepayer Advocate (June, 2001).
237. Vermont, Vermont Gas Systems (Docket No. 6495) Rate Stabilization Plan Testimony for the Vermont Department of Public Service (June, 2001).
238. Pennsylvania, Philadelphia Gas Works (Docket No. R-00016378) Gas Cost Rate Testimony for the Pennsylvania Office of Consumer Advocate (July, 2001).
239. Pennsylvania, PECO Energy Company (Docket No. R-00016366) Gas Cost Rate Testimony for the Pennsylvania Office of Consumer Advocate (July, 2001).
240. Pennsylvania, Philadelphia Gas Works (Docket No. R-00016378) Gas Cost Rate Surrebuttal Testimony for the Pennsylvania Office of Consumer Advocate (August, 2001).
241. Vermont, Vermont Gas Systems (Docket No. 6495) Rate Stabilization Plan Rebuttal Testimony for the Vermont Department of Public Service (August, 2001)
242. Georgia, Atlanta Gas Light Company (Docket No. 14060-U) Procurement and Capacity Plan Testimony for the Georgia Public Service Commission (August, 2001).
243. Rhode Island, New England Gas Company (Docket No. 3401) Earnings Sharing and Gas Policy Testimony for the Rhode Island Division of Public Utilities (March, 2002).

OTS CROSS-EXAMINATION EXHIBIT

NUMBER 1

3/26/02

Phila DD PJS

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PHILADELPHIA GAS COMMISSION

DOCKET NO. R-00017034F0002

DOCUMENT
FOLDER

DOCKETED
APR 30 2002

RECEIVED
02 APR - 2 PM 1:55
P.U.C.
SECRETARY'S BUREAU

RESPONSE TO OFFICE OF TRIAL STAFF
DATA REQUEST REGARDING PGW'S RATE PROCEEDING

Question OTS-Set III-RE-20: Reference PGW ERP St. 1, page 12; lines 14-17: Provide a detailed discussion on the steps the Company will take to aggressively approach delinquent customers.

Response Provided By: Thomas E. Knudsen, Interim Chief Executive Officer

Response: See the attached collection program.

**The Philadelphia Gas Works
Comprehensive Collection Plan**

1. Executive Summary
2. Industry Best Practices
3. Receivable Report
4. Collection Program Calendar

The Comprehensive Collection Plan Executive Summary

As of January 15, 2002, PGW's gas accounts receivable was over \$159 million dollars, of that \$90 million was 90+ days past due. Over 189,000 of our customers are delinquent and 64,500 of them are participating in CRP. In order to address this delinquency PGW segregated the receivable into protected and unprotected customers. A protected customer is one who is actively participating in an authorized PGW payment plan, is disputing their bill or has filed for bankruptcy. The unprotected population is over 84,000 customers owing \$70 million.

The factors which have caused PGW receivables to grow are numerous, the most significant reason is the lack of consistent credit and collection practices. Collection efforts can not stop in December and begin again in March they must be ongoing. Not reminding customers to pay their bills during the time of highest usage is inappropriate. This is the time we should be diligent in our efforts to collect. Another factor affecting the collection of past due debts is staffing. PGW will utilize the flexibility clause in the GWEU contract to augment the collection staff on an as needed basis.

One of PGW's poor collection practices have been to wait until a customer is significantly delinquent before contacting them, this practice will stop. An early intervention process is being instituted, this program will consist of sending letters and calling slow paying customers. As we improve our collection performance Customers who allow their bills to become 60 days delinquent will be placed on the credit and collection path.

PGW's repayment agreement procedure has been to enroll delinquent customers in repayment plans and do very little follow up activity. This created the negative behavior of making and breaking payment arrangements. To tackle this "make 'em" and "break 'em" cycle PGW will institute a program similar to early intervention. Another change to our policy will be to break the arrangement if the payment is not received by the next billing. This will move the debtor into the shut off path 30 days earlier than is the current practice.

Currently 64,892 customers are participating in the Customer Responsibility Program., 32,058, or 49%, have missed 2 or more payments. The programming and testing is completed for the CRP suspension process and anticipate beginning sometime in March, 2002.

PGW is also examining a pilot project combining the PGW tariff requirements and the Public Utilities Commission's Bureau of Consumer Services (BCS) payment agreement guidelines. PGW is looking to partner, on a pilot basis, with a 3rd party to assist those customers who are unable to reach satisfactory payment arrangements with PGW. This vendor will determine disposable income, utilizing the BCS guidelines, and offer the bottom line payment arrangement. This is being explored to avoid an onslaught of BCS informal complaints regarding our payment agreement requirements. We anticipate our early intervention program will result in an elevated level of customers entering into payment arrangements. Prior to conversion, PGW entered into 54,161 payment arrangements in 1997 and 52,278 in 1998. In 2001, there were only 9,396 payment arrangements and 1,972 in 2000.

Termination of service is the final action PGW will undertake. After exhausting all other efforts to collect there is no alternative except shut off. The criteria for placing accounts on the C&C Event Path will be driven by our ability to terminate their service within the time frame allotted by the regulations. PGW, unless otherwise directed by the BCS, will require a security deposit along with payment of the outstanding bill to have service restored.

Collecting from non-residential accounts requires a balance between our need to be paid and our need to sell our product. To address this issue a Commercial Resource Center (CRC) is being established. This unit will consist of employees throughout the organization that have expertise in marketing, meter reading and billing. Their charge will be to provide quality account management to ensure our commercial industrial customers "One-Stop Service". If the CRC turns an account over for collections PGW's policy will be to collect 100% of the delinquency or terminate service.

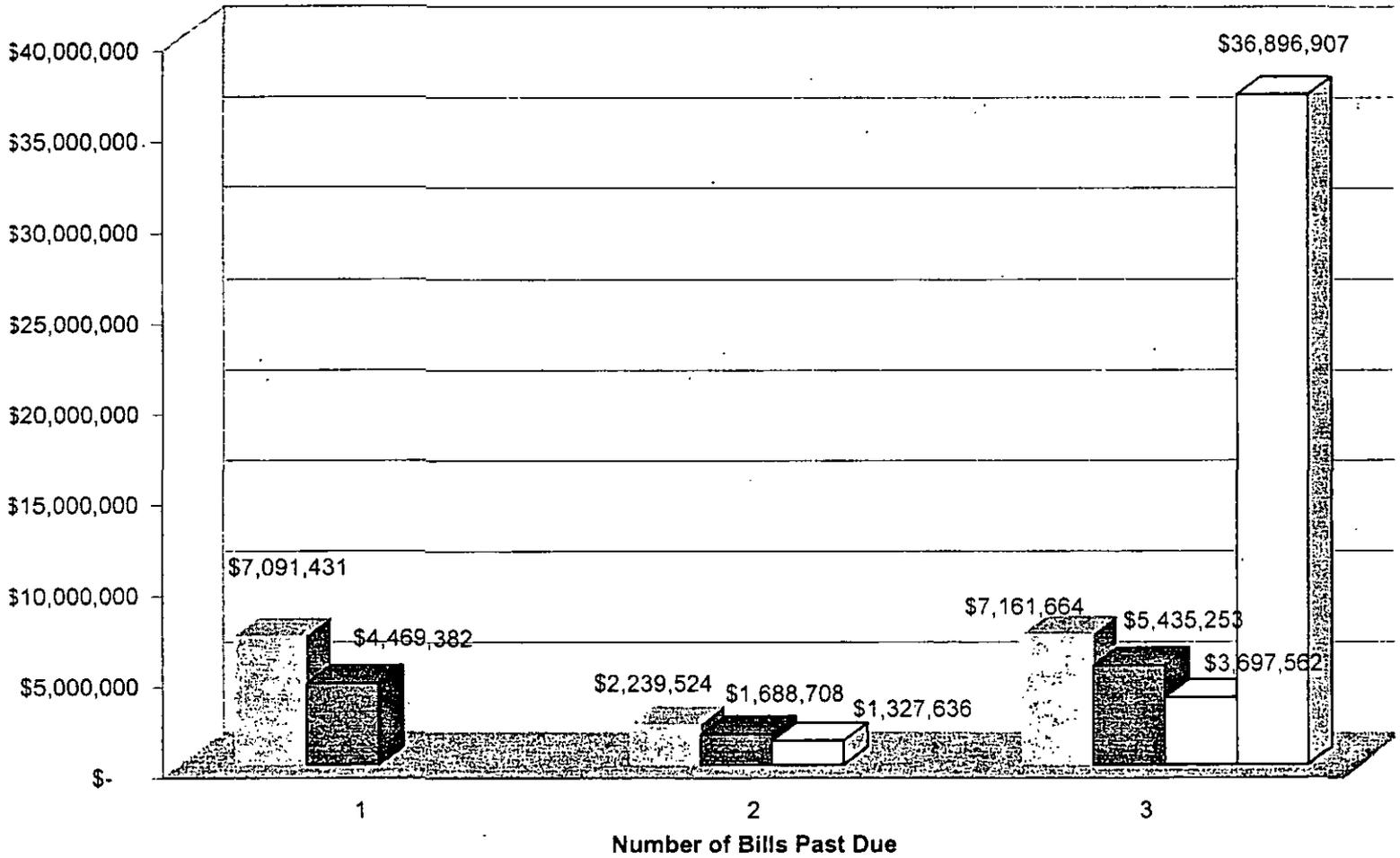
This submission contains information on how we will manage each segment of the delinquency. It is a working document so strategies will change as we learn what works. The course of action outlined in this package will be incorporated into our daily operation throughout the year. This will provide for a consistent collection strategy which will enable PGW to improve collections and change the behavior of our slow paying customers.

Utility Industry Best Collection Practices

- **Follow disconnection policy more than 80% of the time**
- **Billing to disconnection should be less than 45 days**
- **Customer payments must be processed within one day of receipt**
- **Imposition of late payment fees on all missed bill payments**
- **Utilize a behavioral scoring model**
- **Use predictive dialer for telephone dunning efforts over 80% of the time**

The objective of PGW's Comprehensive Collection Plan is to improve credit and collection practices to meet industry standards. Current practices have been mapped and analyzed to identify areas for improvement and will be redesigned to optimize performance.

January 15, 2002
Non Agreement
Total Receivable \$70 Million
Arrears \$53.5 Million



Total All Accounts Receivable - UTILITY Only

January 15, 2002

	Accounts	Current	30	60	90	Total
Zero Balance	84,361					\$ -
Credit Balance	64,479	\$ (14,576,485)				\$ (14,576,485)
Current Only	171,594	\$ 25,397,841				\$ 25,397,841
30 Days	47,647	\$ 9,037,987	\$ 5,811,937			\$ 14,849,924
60Days	20,843	\$ 3,157,059	\$ 2,436,759	\$ 2,365,252		\$ 7,959,070
90 Days	121,273	\$15,296,497	\$11,904,849	\$8,718,284	\$89,934,176	\$125,853,807
Total.	510,197	\$ 38,312,899	\$20,153,545	\$11,083,536	\$89,934,176	\$159,484,157

Excluding Active Agreements, CRP, Easyway, Bankrupt, Disputed Accounts, Written Off and Final Billed Accounts, Accounts Shut Off for Non Payment

	Accounts	Current	30	60	90	Total
Zero Balance	74,032					\$ -
Credit Balance	18,371	\$ (6,221,300)				\$ (6,221,300)
Current Only	139,708	\$ 21,950,173				\$ 21,950,173
30 Days	34,859	\$ 7,091,431	\$ 4,469,382			\$ 11,560,813
60Days	13,209	\$2,239,524	\$1,688,708	\$1,327,636		\$ 5,255,868
90 Days	57,625	\$7,161,664	\$5,435,253	\$3,697,562	\$36,896,907	\$ 53,191,386
Total	337,804	\$ 32,221,492	\$11,593,343	\$ 5,025,198	\$36,896,907	\$ 85,736,940

30 Days	Accounts	Current	30	60	90	Total
Commercial	3,435	\$ 2,910,622	\$ 1,901,687	\$ -	\$ -	\$ 4,812,309
Industrial	181	\$717,871	\$437,842	\$0	\$ -	\$ 1,155,713
Residential	31,243	\$3,462,938	\$2,129,853	\$0	\$0	\$ 5,592,791
Total	34,859	\$ 7,091,431	\$ 4,469,382	\$ -	\$ -	\$ 11,560,814

60 Days	Accounts	Current	30	60	90	Total
Commercial	1,136	\$ 868,826	\$ 697,989	\$ 443,589	\$ -	\$ 2,010,404
Industrial	50	\$51,493	\$45,238	\$21,040	\$ -	\$ 117,770
Residential	12,023	\$1,319,205	\$945,481	\$863,008	\$0	\$ 3,127,694
Total:	13,209	\$ 2,239,524	\$ 1,688,708	\$ 1,327,636	\$ -	\$ 5,255,868

90 Days	Accounts	Current	30	60	90	Total
Commercial	1,921	\$ 801,660	\$ 699,206	\$ 423,026	\$ 3,371,348	\$ 5,295,240
Industrial	54	\$84,675	\$89,296	\$82,888	\$ 307,482	\$ 564,342
Residential	55,650	\$6,275,329	\$4,646,751	\$3,191,648	\$33,218,076	\$ 47,331,804
Total.	57,625	\$ 7,161,664	\$ 5,435,253	\$ 3,697,562	\$36,896,907	\$ 53,191,386

**Customer Responsibility Program
As of February 2002**

Pmts Missed	Accounts	Outstanding Ask to Pay	CRPLD	CRPLF	CRPLL	CRPLN	CRPRL
< 2	32,834	\$ 2,170,951	\$ 297,607	\$ 26,404,195	\$ 1,115,955	\$ 5,821	\$ 153,816
2	2,979	\$ 848,341	\$ 33,149	\$ 3,843,565	\$ 106,147	\$ 848	\$ 59,145
3	2,966	\$ 1,068,253	\$ 33,275	\$ 3,590,030	\$ 129,155	\$ 2,047	\$ 95,717
4	2,163	\$ 980,097	\$ 24,689	\$ 2,775,460	\$ 102,423	\$ 1,870	\$ 95,666
5	2,623	\$ 1,408,994	\$ 35,502	\$ 3,484,625	\$ 151,610	\$ 1,306	\$ 153,730
6	2,650	\$ 1,613,884	\$ 41,463	\$ 3,812,335	\$ 173,478	\$ 2,925	\$ 222,457
7	1,969	\$ 1,413,257	\$ 34,691	\$ 2,803,887	\$ 162,661	\$ 831	\$ 237,084
8	1,842	\$ 1,600,088	\$ 36,550	\$ 2,830,260	\$ 189,472	\$ 1,823	\$ 273,087
9	1,510	\$ 1,423,632	\$ 30,209	\$ 2,299,091	\$ 197,978	\$ 1,221	\$ 307,742
10	1,459	\$ 1,542,414	\$ 35,430	\$ 2,229,919	\$ 203,221	\$ 2,340	\$ 364,687
11	1,356	\$ 1,694,725	\$ 32,951	\$ 2,362,142	\$ 199,705	\$ 967	\$ 409,687
12	1,566	\$ 2,045,201	\$ 33,491	\$ 2,668,336	\$ 220,539	\$ 1,233	\$ 475,580
12+	8,975	\$ 15,994,482	\$ 240,328	\$ 16,278,849	\$ 1,678,172	\$ 5,780	\$ 2,210,438

64,892	\$ 33,804,319	\$ 909,334	\$ 75,382,694	\$ 4,630,515	\$ 29,011	\$ 5,058,836
---------------	----------------------	-------------------	----------------------	---------------------	------------------	---------------------

LD- Non CRP Chg Not Billed
LF- Frozen Arrears

LL- LIHEAP Makeup
LN- Non CRP Chg Billed

RL- Relief Loan

Collection Events Schedule

	28-Jan	01-Feb	04-Feb	Feb 11 - 14	18-Feb	Feb 19 - 21	25-Feb	01-Mar
Commercial / Industrial Delinquency Reduction Program	Monthly Delinquency Report	Prepare 7 Day Shut Off Notices	Field Visit 7 Day Shut Off Noticed Delivered	Field Visit Collect Outstanding Balance or Terminate Service	Status Report of 1/28/02 Delinquencies	Field Visit Collect Outstanding Balance or Terminate Service	Status Report of 1/28/02 Delinquencies	Monthly Delinquency Report
		Section 4.22	Section 4.22					
	22-Feb	04-Mar	14-Mar	14-Mar	18-Mar			
Residential Telephone Dunning	Delinquency Report Accounts Over 90 Days Delinquent	Weekly Phone Dunning File	10 Day Payment Report	Weekly Phone Dunning File	Begin Shut off Proceedings			
	11-Mar	18-Mar	25-Mar		01-Apr	03-Apr	11-Apr	15-Apr
Residential Shut Off Program Over 90 Days Delinquent	Reminder Collection Notice Mailed	14 Day Shut off Notice Mailed	Telephone Calls to prompt payment and avoid termination	If no Phone Number Field Visit	First Field visit attempt to collect, enter into payment arrangements and/or Post final shut off notice	Second field attempt to collect or terminate service.	2nd Posting if not shut off within 10 days of 4.25	Shut Off
	Section 4.21	Section 4.22	Section 4.24	Section 4.24	4.25P	4.25S	4.27P	4.27S
	March 4 - 31							
Advertising Campaign	Radio Neighborhood Newspapers PSA's							
	15-Feb	19-Feb	20-Feb	01-Mar	08-Mar	28-Mar	11-Apr	
USTRA Delinquent Tenant Occupied Buildings	Monthly Delinquency Report	Select Accounts	Send Notifications to Internal & External Stakeholders	Mail/Hand Deliver Landlord Notification	30 Day Tenant Notification	Send Notifications to Internal & External Stakeholders	Begin Termination	
				USTRA - 1	USTRA - 2			
	Daily	Every Friday						
Vacant Residential Accounts	Review Work Orders Marked as Vacant	Send Vacant Accounts on Street for Termination						
	Daily	Every Friday						
Vacant Commercial / Industrial Accounts	Review Work Orders Marked as Vacant	Send Vacant Accounts on Street for Termination						
Stop-N-Chop	??/??/??	??/??/??	??/??/??	??/??/??	??/??/??	??/??/??	??/??/??	??/??/??
No Shut Off Valve Access Residential Accounts over 90 days in arrears	Reminder Collection Notice Mailed	14 Day Shut off Notice Mailed	Telephone Calls to prompt payment and avoid termination	If no Phone Number Field Visit	First Field visit attempt to collect, enter into payment arrangements and/or Post final shut off notice	Second field attempt to collect or terminate service.	2nd Posting if not shut off within 10 days of 4.25	Utilize Distribution Department to Disconnect Service
	Section 4.21	Section 4.22	Section 4.24	Section 4.24	4.25P	4.25S	4.27P	4.27S



COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE
REFER TO OUR FILE

March 22, 2002

Honorable Cynthia W. Fordham
Administrative Law Judge
PA Public Utility Commission
1302 Philadelphia State Office Building
Broad and Spring Garden Streets
Philadelphia, PA 19130

DOCUMENT
FOLDER

Re: Pennsylvania Public Utility Commission
v.
Philadelphia Gas Works
Docket No. R-00017034F0002

Dear Judge Fordham:

Enclosed please find the following documents that were inadvertently omitted from the prepared Direct Testimony for Office of Trial Staff (OTS) witnesses.

OTS Statement No. 1--Errata Sheet--Pages 6, 7, 8 (Charles T. Weakley)

OTS Exhibit No. 2, Schedule 3 (Kevan Deardorff)

Copies of the above-mentioned documents are being served upon all active parties of record.

Sincerely,

Johnnie E. Simms
Senior Prosecutor
Office of Trial Staff

JES:ecm

c: Parties of Record

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission :
 :
 v. : Docket No. R-00017034F0002
 :
 Philadelphia Gas Works :

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing **OTS Statement No. 1
Errata Sheets and OTS Exhibit No. 2, Schedule 3**, dated March 22, 2002 either
personally, by first class mail, electronic mail, or by fax upon the persons listed below:

Daniel Clearfield, Esquire
Wolf, Block, Schorr and Solis-Cohen, LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101

Greg Stunder, Esquire
Philadelphia Gas Works
800 West Montgomery Avenue
Philadelphia, PA 19122

Steven J. Keene, Esquire
Tanya McCloskey, Esquire
Christy M. Appleby, Esquire
Office of Consumer Advocate
5th Floor, Forum Place
555 Walnut Street
Harrisburg, PA 17101-1923

Steven C. Gray, Esquire
Office of Small Business Advocate
Commerce Building, Suite 1102
300 North Second Street
Harrisburg, PA 17101

Phillip A. Bertocci, Esquire
Edward A. McCool, Esquire
1424 Chestnut Street 4th Floor
Philadelphia, PA 19102-2505

Charis M. Burak, Esquire
McNees, Wallace & Nurick, LLC
P. O. Box 1166
100 Pine Street
Harrisburg, PA 17108-1166

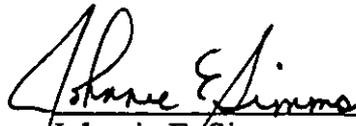
Mr. Lance Haver
6048 Ogontz Avenue
Philadelphia, PA 19141

Mr. Larry Speilvogel
203 Hughes Road
King of Prussia, PA 19406

Hon. Cynthia W. Fordham
Administrative Law Judge
PA Public Utility Commission
1302 Philadelphia State Office Bldg.
Broad & Spring Garden Streets
Philadelphia, PA 19130

Mr. Michael A. Bleiweis
243 Banks Road
Easton, CT 06612-1627

Mr. Richard Lelash
Financial & Regulatory Consultant
18 Seventy Acre Road
Redding, CT 06896



Johnnie E. Simms
Senior Prosecutor
Office of Trial Staff

Dated: March 22, 2002
Docket No. R-00017034F0002

1 **Q. IN CALCULATING YOUR ZERO DEFICIENCY, DID YOU MAKE**
2 **ANY ADJUSTMENTS OTHER THAN REFLECTING THE CASH**
3 **EFFECT OF \$2.5 MILLION BASED ON YOUR RECOMMENDED**
4 **INCREASE?**

5 **A. Yes. I removed the \$18.2 million city fee.**
6

7 **Q. WHAT IS THE BASIS OF YOUR ADJUSTMENT?**

8 **A. For the fiscal year 2002, the city fee should be granted back to PGW even if**
9 **they meet their bond covenant requirements in order to alleviate the cash**
10 **crisis that PGW finds itself. The Administration must realize the need to**
11 **assist PGW because, if its bond rating is downgraded, the city runs the risk**
12 **of loosing its \$45 million city loan and its \$18 million annual city fee.**

13
14 **Q. PLEASE EXPLAIN THE CHANGES IN THE CASH FLOW**
15 **STATEMENT TO THE OPENING CASH BALANCE FOR THE**
16 **FISCAL YEAR ENDED AUGUST 31, 2003.**

17 **A. PGW's cash flow analysis for August 31, 2003, reports an opening cash**
18 **balance of (\$20.8 million) and a projected ending cash balance of (\$51.0**
19 **million). The beginning cash balance is the carried forward of the fiscal**
20 **year August 31, 2002 ending cash balance. As I have previously discussed,**
21 **I have calculated a zero cash deficiency as of August 31, 2002, which I**

1 have incorporated as the beginning cash balance in the cash flow analysis
2 for August 31, 2003.

3

4 **Q. DID YOU INCLUDE OTS'S RECOMMENDED \$25 MILLION RATE**
5 **RELIEF IN YOUR CASH FLOW ANALYSIS?**

6 A. Yes. I included the recommended \$25 million extraordinary rate relief by
7 distributing the increase over the twelve months on the same basis as the
8 Company's last base rate increase.

9

10 **Q. DID YOU MAKE ANY OTHER ADJUSTMENTS?**

11 A. Yes. I reduced the \$45 million city loan payment to \$22.5.

12

13 **Q. WHAT IS THE BASIS FOR THIS ADJUSTMENT?**

14 A. In the current base rate filing, PGW has requested \$22.5 million to repay
15 the city loan (see PGW's base rate case at Docket R-00017034, Volume II,
16 Exhibit A-2 which is attached as OTS Exhibit No. 2, Schedule 3). I am
17 adjusting the cash flow analysis to be consistent with PGW's base rate case.

18

19 **Q. WHAT IS YOUR PROJECTED ENDING CASH BALANCE?**

20 A. The result of my recommended changes is a projected cash balance of
21 \$15.8 million at August 31, 2003.

1 **Q. WHAT STEPS CAN THE CITY OF PHILADELPHIA TAKE TO**
2 **HELP PGW MAINTAIN ITS CURRENT BOND RATINGS.**

3 **A. In my opinion, the City can reverse most of the negative risks mentioned in**
4 **the S&P draft press release by doing the following:**

5 a) Grant back the \$18 million city fee for fiscal year 2002 and
6 defer repayment of the city loan to improve PGW's liquidity.

7 b) Permit PGW to pursue collections of its accounts receivable
8 with the same vigor as other utilities.

9 c) Name permanent management.

10

11 **Q. WHAT IS THE BUDGETED ACCOUNTS RECEIVABLE BALANCE**
12 **AT CURRENT RATES FOR THE FISCAL YEAR 2002?**

13 **A. PGW's ending accounts receivable balance is projected to be \$258,134,000**
14 **(see PGW base rate filing at Docket No. R-00017034, Volume II, Schedule**
15 **SD-6).**

16

17 **Q. HAS PGW BEEN ABLE TO PURSUE COLLECTIONS OF ITS**
18 **ACCOUNTS RECEIVABLE WITH THE SAME VIGOR AS OTHER**
19 **UTILITIES?**

20 **A. No. It appears that PGW is either reluctant to fully pursue collection of its**
21 **accounts receivable or other parties are inhibiting these collection efforts.**

Exhibit A-2

**PHILADELPHIA GAS WORKS
CASH FLOW STATEMENT
(Dollars in Thousands)**

Line No.	SOURCES	Actual 1999-2000	Actual 2000-01	Current Rates Budget 2001-02	\$60M Budget 2001-02
1.	Net Income	(\$2,411)	\$11,154	\$23,483	\$86,027
2.	Depreciation & Amortization	40,985	40,506	42,832	42,632
3.	Earnings on Restricted Funds	863	(361)	163	163
4.	Loss on Disposition of SNG Plant	-	8,087	-	-
5.	Increased/(Decreased) Long Term Debt	548	(468)	468	468
6.	Increased/(Decreased) Other Liabilities	14,800	2,861	1,809	1,809
7.	Available From Operations	54,485	61,779	68,755	131,299
8.	Funds Required for Capital	69,264	50,401	60,943	60,943
9.	Capital Leasing	2,228	4,955	2,000	2,000
10.	City Loan	-	45,000	-	-
11.	Temporary Financing	22,000	-	-	-
12.	TOTAL SOURCES	\$147,877	\$162,135	\$131,698	\$194,242
USES					
13.	Net Construction Expenditures	\$48,139	\$57,424	\$62,943	\$62,943
<i>Funded Debt Reduction:</i>					
14.	Revenue Bonds	33,595	34,192	33,977	33,977
15.	PMA Lease/Subordinate Debt	1,020	1,065	1,105	1,105
16.	Capital Lease	6,538	6,901	5,273	5,273
17.	Notes Payable - CNG Acquisition	219	59	-	-
18.	Tax Exempt Commercial Paper Repayment Fund	-	19,000	1,000	11,000
19.	\$45.0 M City Loan Repayment Fund	-	-	-	22,500
20.	Distribution of Earnings	18,000	18,000	18,000	18,000
<i>Additions to (Reductions of)</i>					
21.	Non-Cash Working Capital	48,128	33,399	7,166	12,212
22.	Cash Needs	155,639	170,040	129,484	167,010
23.	Cash Surplus (Shortfall)	(7,662)	(7,905)	2,234	27,232
24.	TOTAL USES	\$147,877	\$162,135	\$131,698	\$194,242
25.	Cash - Beginning of Period	\$16,087	\$8,425	\$520	\$520
26.	Cash - Surplus (Shortfall)	(7,662)	(7,905)	2,234	27,232
27.	Ending Cash	\$8,425	\$520	\$2,754	\$27,752
28.	Other Capital Funding Sources	-	-	-	-
29.	Outstanding Commercial Paper	\$97,000	\$78,000	\$77,000	\$67,000
30.	City Loan Outstanding	-	\$45,000	\$45,000	\$22,500

DOCUMENT
FILED

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

FILED

APR 30 2002

**PENNSYLVANIA PUBLIC
UTILITY COMMISSION** :

v. :

Docket No. R-00017034F0002

PHILADELPHIA GAS WORKS :

THE OFFICE OF TRIAL STAFF'S

TESTIMONY AND EXHIBITS

IN OPPOSITION TO

**PHILADELPHIA GAS WORKS'
EXTRAORDINARY RATE PETITION**

SECRETARY'S BUREAU

02 APR -2 PM 1:55

070714750

**OTS Statement No. 1; OTS Exhibit No. 1
OTS Statement No. 2; OTS Exhibit No. 2**

R-00017034F0002

3/26/02

Phila, PA

PCS

OTS Statement No. 1

Witness: Charles T. Weakley, III

Date: March 21, 2002

**DOCUMENT
FOLDER**

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PHILADELPHIA GAS WORKS

Docket No. R-00017034F0002

BOOKETED
APR 30 2002

Direct Testimony

of

Charles T. Weakley, III

Office of Trial Staff

Concerning:

Extraordinary Rate Relief

1 **Q. STATE YOUR FULL NAME, EMPLOYER AND BUSINESS**
2 **ADDRESS.**

3 A. My name is Charles T. Weakley, III. I am employed by the Pennsylvania
4 Public Utility Commission, P.O. Box 3265, Harrisburg, PA 17105-3265.

5
6 **Q. WHAT IS YOUR POSITION WITH THE PENNSYLVANIA PUBLIC**
7 **UTILITY COMMISSION?**

8 A. I am a Fixed Utility Financial Analyst in the Office of Trial Staff (OTS).

9
10 **Q. WHAT ARE YOUR DUTIES AS AN ANALYST IN OTS?**

11 A. My duties as an OTS analyst include participation in formal base rate
12 proceedings as an expert witness, with responsibility for the preparation
13 and presentation of OTS exhibits, schedules and testimony. My education
14 and professional background are set forth in Appendix A, which is
15 attached.

16
17 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

18 A. The purpose of this testimony is to provide OTS's recommended level of
19 extraordinary rate relief for Philadelphia Gas Works (PGW or Company)
20 and to explain the impact of OTS's recommended rate relief has on the
21 Company's cash flow analysis.

1 **Q. WHAT IS THE COMPANY'S CLAIM FOR EXTRAORDINARY**
2 **RATE RELIEF?**

3 A. PGW has filed a base rate case at Docket No. R-00017034, requesting a
4 base rate increase of \$60 million. In this proceeding, PGW has requested
5 \$44 million in extraordinary rate relief.

6
7 **Q. WHY IS PGW REQUESTING EXTRAORDINARY RATE RELIEF?**

8 A. PGW is requesting extraordinary rate relief primarily to improve its
9 liquidity position and to maintain its current long-term bond rating by S&P.

10
11 **Q. WHAT MUST BE SHOWN IN ORDER FOR THE COMMISSION TO**
12 **GRANT EXTRAORDINARY RATE RELIEF?**

13 A. It must be shown that the rate relief requested is immediately necessary for
14 the maintenance of financial stability in order to enable the utility to:
15 a. Continue to provide normal services to its customers.
16 b. Avoid reductions in its normal maintenance programs.
17 c. Avoid substantially reducing its employment.
18 d. The relief will not increase the return on equity established by the
19 Commission in the Company's last base rate case.

20 Note: The rate of return requirement does not apply to PGW.

1 **Q. HAS PGW MET THE REQUIREMENTS TO RECIEVE**
2 **EXTRAORDINARY RATE RELIEF BASED ON ITS FILING?**

3 A. Yes. In Accordance with 66 Pa. C.S.A. §1308(e), PGW has demonstrated
4 the immediate need for extraordinary rate relief in order to maintain
5 financial stability. Absent immediate rate relief, PGW will have to cut
6 maintenance programs, services to customers and employee levels to avoid
7 a downgrade of its bond ratings.

8
9 **Q. DO YOU AGREE WITH THE \$44 MILLION EXTRAORDINARY**
10 **RATE RELIEF REQUEST?**

11 A. No. The \$44 million extraordinary rate relief request is excessive.

12
13 **Q. WHAT LEVEL OF EXTRAORDINARY RATE RELIEF IS OTS**
14 **RECOMMENDING?**

15 A. OTS is recommending \$25 million in extraordinary rate relief (see OTS
16 Exhibit No. 2, Schedule 1).

1 **Q. HOW DID OTS CALCULATE THE RECOMMENDED**
2 **EXTRAORDINARY RATE RELIEF INCREASE?**

3 A. OTS Witness Deardorff determined that the funds available to service
4 aggregate debt coverage of 1.25 needs to be \$148,521,000. To that, I added
5 the total funds applied and subtracted restricted funds and AFUDC to
6 calculate the total operating revenues of \$691,850,000 necessary to service
7 aggregate debt coverage. Then, I compared test year budget revenues of
8 \$666,850,000 (\$638,733,000 + \$28,117,000) to the calculated revenues and
9 determined that PGW needs \$25 million (\$691,850,000 - \$666,850,000) in
10 extraordinary rate relief.

11
12 **Q. HAS THE COMPANY SUBMITTED A CASH FLOW ANALYSIS?**

13 A. Yes. PGW's cash flow analysis is presented in Exhibit JRB-1.

14
15 **Q. WHAT DOES THE COMPANY'S CASH FLOW ANALYSIS**
16 **INDICATE?**

17 A. Absent any extraordinary rate relief, PGW would end its fiscal year 2002
18 with a cash deficit of \$20.8 million.

1 **Q. HAVE YOU PREPARED A CASH FLOW ANALYSIS TO INCLUDE**
2 **THE RECOMMENDED \$25 MILLION INCREASE?**

3 A. Yes, I have prepared a cash flow statement for the fiscal year ended August
4 31, 2002, and for the fiscal year ended August 31, 2003.

5
6 **Q. WHAT DOES YOUR CASH FLOW ANALYSIS INDICATE?**

7 A. My cash flow analysis shows no cash deficiency for the fiscal year ended
8 August 31, 2002.

9
10 **Q. WHAT IS THE CASH FLOW IMPACT OF A \$25 MILLION**
11 **INCREASE?**

12 A. For the fiscal year 2002, the cash flow impact is \$2.5 million.

13
14 **Q. HOW DID YOU CALCULATE THE CASH FLOW IMPACT OF \$2.5**
15 **MILLION?**

16 A. In response to the data request OCA-Set I-28, PGW provided the Mcf sales
17 volumes for the fiscal year 2002 and the increase rate per Mcf based on \$30
18 million. I scaled back the increase rate per Mcf to a \$25 million rate
19 increase and multiplied that rate by applicable Mcf sales for the months
20 May through August resulting in projected billings. Then, I used PGW's
21 collection factor of 94 percent to calculated the projected receipts of \$2.5
22 million (see OTS Exhibit No. 1, Schedule 3).

1 **Q. IN CALCULATING YOUR ZERO DEFICIENCY, DID YOU MAKE**
2 **ANY ADJUSTMENTS OTHER THAN REFLECTING THE CASH**
3 **EFFECT OF \$2.5 MILLION BASED ON YOUR RECOMMENDED**
4 **INCREASE?**

5 A. Yes. I removed the \$18.2 million city fee.

6
7 **Q. WHAT IS THE BASIS OF YOUR ADJUSTMENT?**

8 A. For the fiscal year 2002, the city fee should be granted back to PGW even if
9 they meet their bond covenant requirements in order to elevate the cash
10 crisis that PGW finds itself. The Administration must realize the need to
11 assist PGW because, if its bond rating is downgraded, the city runs the risk
12 of loosing its \$45 million city loan and its \$18 million annual city fee.

13
14 **Q. PLEASE EXPLAIN THE CHANGES IN THE CASH FLOW**
15 **STATEMENT TO THE OPENING CASH BALANCE FOR THE**
16 **FISCAL YEAR ENDED AUGUST 31, 2003.**

17 A. PGW's cash flow analysis for August 31, 2003, reports an opening cash
18 balance of (\$20.8 million) and a projected ending cash balance of (\$51.0
19 million). The beginning cash balance is the carried forward of the fiscal
20 year August 31, 2002 ending cash balance. As I have previously discussed,
21 I have calculated a zero cash deficiency as of August 31, 2002, which I

1 have incorporated as the beginning cash balance in the cash flow analysis
2 for August 31, 2003.

3
4 **Q. DID YOU INCLUDE OTS'S RECOMMENDED \$25 MILLION RATE
5 RELIEF IN YOUR CASH FLOW ANALYSIS?**

6 A. Yes. I included the recommended \$25 million extraordinary rate relief by
7 distributing the increase over the twelve months on the same basis as the
8 Company's last base rate increase.

9
10 **Q. DID YOU MAKE ANY OTHER ADJUSTMENTS?**

11 A. Yes. I reduced the \$45 million city loan payment to \$22.5.

12
13 **Q. WHAT IS THE BASIS FOR THIS ADJUSTMENT?**

14 A. In the current base rate filing, PGW has requested \$22.5 million to repay
15 the city loan (see Volume II, page). I am adjusting the cash flow analysis
16 to be consistent with PGW's base rate case.

17
18 **Q. WHAT IS YOUR PROJECTED ENDING CASH BALANCE?**

19 A. The result of my recommended changes is a projected cash balance of
20 \$15.8 million at August 31, 2003.

1 **Q. WHAT STEPS CAN THE CITY OF PHILADELPHIA TAKE TO**
2 **HELP PGW MAINTAIN ITS CURRENT BOND RATINGS.**

3 A. In my opinion, the City can reverse most of the negative risks mentioned in
4 the S&P draft press release by doing the following:

5 a) Grant back the \$18 million city fee for fiscal year 2002 and
6 defer repayment of the city loan to improve PGW's liquidity.

7 b) Permit PGW to pursue collections of its accounts receivable
8 with the same vigor as other utilities.

9 c) Name permanent management.

10

11 **Q. WHAT IS THE BUDGETED ACCOUNTS RECEIVABLES BALANCE**
12 **AT CURRENT RATES FOR THE FISCAL YEAR 2002?**

13 A. PGW's ending accounts receivable balance is projected to be \$258,134,000
14 (see PGW base rate filing at Docket No. R-00017034, Volume II, Schedule
15 SD-6).

16

17 **Q. HAS PGW BEEN ABLE TO PURSUE COLLECTIONS OF ITS**
18 **ACCOUNTS RECEIVABLE WITH THE SAME VIGOR AS OTHER**
19 **UTILITIES?**

20 A. No. It appears that PGW is either reluctant to fully pursue collection of its
21 accounts receivable or other parties are inhibiting these collection efforts.

1 This restricts not only PGW's ability to repay the \$45 million city loan but
2 has also contributed to the Company's current situation.

3

4 **Q. DOES THE CONCLUDE YOU DIRECT TESTIMONY?**

5 **A. Yes.**

APPENDIX A

Professional and Educational Background

Charles T. Weakley, III

Education:

A.A. in Accounting, Harrisburg Area Community College, 1973.

B.B.A. in Administration, Pennsylvania State University, 1975.

Graduate Studies in Operations Management, Pennsylvania State University, 1977.

Employment:

Prior to accepting my position with the PUC, in the Bureau of Rates in February 1984, I was a Corporation Tax Officer with the Pennsylvania Department of Revenue.

I am a Certified Public Accountant, however, my license is currently inactive, since I am no longer in public practice. In addition, I am a Member of the Pennsylvania Institute of Certified Public Accountants and have three years of public accounting experience.

Testimony:

I have testified and/or submitted testimony in the following proceedings:

PECO Rate Case, R-842590, R-850152 and R-891364

Penn Power Rate Case, R-842740, R-850267 and R-870732

Met-Ed Rate Case, R-842770 and R-00922314

Penelec Rate Case, R-842771

Duquesne Light Rate Case, R-850021, R-860378 and R-870651

PECO - Gas Operations Rate Case, R-870629

Philadelphia Suburban Water Company Rate Case, R-870860 and R-891270

Peoples Natural Gas Rate Case, R-880961

Equitable Gas Rate Case, R-880971, R-901595 and R-912164

PECO-PGC No. 6, 1307(f) Proceeding, R-891290

T.W. Phillips Gas and Oil Co. PGC-90, R-891572

T.W. Phillips Gas and Oil Co. Rate Case, R-891566

Arrowhead Public Service Corporation Rate Case, R-891557

Peoples Natural Gas - PGC-90, 1307(f) Proceeding, R-901640

Peoples Natural Gas - PGC-91, 1307(f) Proceeding, R-911919

PECO-PGC No. 8, 1307(f) Proceeding, R-911976

West Penn Power - Petitions (CAAA, 1990) P-910511 and R-910512

Borough of Phoenixville - Rate Case, R-912038

Shenango Valley Water Company - R-912060 and R-00932798

Dallas Water Company, Inc. - R-00922326

Harvey's Lake Water Company, Inc. - R-00922327

Noxen Water Company, Inc. - R-00922328

Shavertown Water Company, Inc. - R-00922329

Pennsylvania Gas and Water Company (Spring Brook/Crystal Lake) R-00922404

Pennsylvania-American Water Company - R-00922428

Pennsylvania Gas and Water Company (Scranton) R-000922482

National Fuel Gas Distribution Corporation - R-00932548

Lemont Water Company, Rate Case, R-00932673

The Peoples Natural Gas Company, Rate Case, R-00932866

The Peoples Natural Gas Company, 1994-1307(f), R-00943028, C-945601

Equitable Gas Company - R-00943246

Pennsylvania Power & Light Company - R-00943271

The Peoples Natural Gas Company, 1996-1307(f), R-00963563

The Peoples Natural Gas Company, 1997-1307(f), R-00973896, R-00973928, A-122250F0007

Peco Energy Company - R-00973877, R-00973953

Pennsylvania Electric Company - R-00974009

Metropolitan Edison Company - R-00974008

Bell/ GTE Merger - A-310200F0002, A-310222F0002, A-310291F0003,
A-311350F0002

The Peoples Natural Gas Company - Rate Restructuring - R-00994782

Equitable Gas Company - Rate Restructuring - R-00994784

UGI Utilities, Inc. - Rate Restructuring - R-00994786

PECO Energy Company - Rate Restructuring – R-00994787

National Fuel Gas Distribution Corporation – 1307(f) – R-00994898

PECO Energy Company – 1307(f) – R-00005285

UGI Utilities, Inc. – 1307(f) – R-00005281

Philadelphia Gas Works – Rate Case – R-00005654, R-0006042

OTS Exhibit No. 1

Witness: Charles T. Weakley, III

Date: March 21, 2002

**DOCUMENT
FOLDER**

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PHILADELPHIA GAS WORKS

Docket No. R-00017034F0002

**INDEXED
DOCKETED
APR 30 2002**

Exhibit to Accompany

the

Direct Testimony

of

Charles T. Weakley, III

Office of Trial Staff

Concerning:

Extraordinary Rate Relief

Estimated weather 3800 degree days
 City Loan \$45.0 MM Fully Outstanding @ 8/31/02
 \$33.8M Rate Incr. - Current
 TXCP \$100.0 M with \$77.0 M Outstanding @ 8/31/02
 Reduced expenses per union contract settlement
 PreDraw Capital Funding during Fiscal Period

ACTUAL WEATHER THRU 2/15/02 NO FINANCIAL TRANSACTIONS

BUDGET OF CASH RECEIPTS AND DISBURSEMENTS
 FISCAL YEAR ENDING AUGUST 31, 2002
 (Millions of Dollars)

	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	ESTIMATE	TOTAL
2/18/2002	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	
OPENING BALANCE - CASH INCLUDES 97.0 TXCP RECEIPTS	\$1.7	\$0.7	\$3.7	\$4.2	\$3.8	\$1.0	\$35.2	\$46.4	\$58.7	\$68.1	\$83.5	\$17.7	\$1.7
Gas	32.2	40.9	42.9	41.5	63.1	65.0	63.0	63.0	59.0	45.8	39.0	37.0	592.4
Other	0.7	0.8	0.3	1.8	0.8	1.8	1.5	1.5	1.5	1.5	1.5	2.9	15.8
Drawn from Capital Funds - Principal (\$80.9MM)	12.9	20.0	0.0	20.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	52.9
Drawn from Capital Funds - Interest	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.7	1.9
Drawn from Lease Funds - Principal (\$3.8MM)	0.0	0.0	0.0	0.0	0.0	2.0	0.0	0.0	0.0	0.0	1.8	0.0	3.8
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.2
Advance (Repayment) of Capital Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension Draw	0.0	0.0	0.0	9.2	6.5	0.0	0.0	2.3	2.3	2.3	2.4	2.4	27.4
City Loan	11.9	32.2	22.5	47.4	22.5	15.5							152.0
Extraordinary Rate Relief	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.5
TOTAL RECEIPTS	57.7	93.7	65.9	119.7	92.7	84.1	64.5	68.8	63.3	50.4	45.3	44.8	848.9
TOTAL	59.4	94.4	69.6	123.9	96.5	85.1	99.7	113.2	122.0	116.5	108.9	62.4	850.6
DISBURSEMENTS													
Labor	10.3	11.1	11.9	10.9	10.6	10.5	11.1	11.3	11.5	10.4	11.4	10.9	131.9
Natural Gas	26.3	27.8	28.9	33.3	38.0	36.1	32.5	31.5	28.0	28.0	23.2	24.0	355.8
Debt Service	0.0	4.0	0.0	0.0	25.5	6.1	0.0	2.0	1.7	0.0	42.1	13.0	94.4
TXCP: Interest	0.1	0.2	0.2	0.1	0.0	0.2	0.3	0.3	0.3	0.3	0.2	0.2	2.5
Repayment of City Loan	14.5	38.7	17.2	68.1	15.5								152.0
Cost Savings/Reductions	0.0	0.0	0.0	0.0	0.0	(0.8)	(0.9)	(0.9)	(0.9)	(1.0)	(1.0)	(1.0)	(6.5)
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Disbursements	7.5	7.9	10.6	10.2	10.9	10.8	10.3	10.3	10.3	10.3	10.3	10.3	119.7
TOTAL DISBURSEMENTS	58.7	87.7	68.8	122.6	98.5	62.9	53.3	54.5	50.9	48.0	86.2	57.4	849.6
MONTHLY CASH FLOW	(1.0)	6.0	(2.9)	(2.9)	(5.8)	21.2	11.2	12.3	12.4	2.4	(40.9)	(12.6)	(0.7)
CUMULATIVE CASH FLOW	(1.0)	5.0	2.0	(0.9)	(8.7)	14.5	25.7	38.0	50.4	52.8	12.0	(0.7)	
OPENING TXCP	78.0	78.0	75.0	78.5	81.0	84.0	97.0	97.0	97.0	92.0	87.0	82.0	78.0
TXCP ISSUED DURING MONTH	0.0	0.0	3.5	2.5	3.0	13.0	0.0	0.0	0.0	0.0	0.0	0.0	22.0
TXCP ISSUED PAID DOWN DURING MONTH	0.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0	5.0	5.0	5.0	5.0	23.0
ENDING TXCP	78.0	75.0	78.5	81.0	84.0	97.0	97.0	97.0	92.0	87.0	82.0	77.0	77.0
OPENING BALANCE - CASH	1.7	0.7	3.7	4.2	3.8	1.0	35.2	46.4	58.7	68.1	83.5	17.7	1.7
MONTHLY CASH FLOW	(1.0)	6.0	(2.9)	(2.9)	(5.8)	21.2	11.2	12.3	12.4	2.4	(40.9)	(12.6)	(0.7)
NET TXCP ACTIVITY MONTHLY	0.0	(3.0)	3.5	2.5	3.0	13.0	0.0	0.0	(5.0)	(5.0)	(5.0)	(5.0)	(1.0)
ENDING BALANCE - CASH	0.7	3.7	4.2	3.8	1.0	35.2	46.4	58.7	68.1	63.5	17.7	0.0	0.0
CITY LOAN AVAILABLE - END OF MONTH	0	2.6	7.1	1.8	22.6	15.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CITY LOAN UTILIZED - END OF MONTH	45	42.4	37.9	43.2	29.5	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0
CASH POSITION NET OF TXCP AND CITY LOAN	(119.7)	(109.2)	(117.5)	(98.7)	(112.5)	(108.8)	(95.6)	(83.3)	(70.8)	(68.6)	(109.3)	(122.0)	

Normal weather 4555 degree days
 \$33.6M Rate Incr. - Current
 City Loan Repayment Due 8/31/03
 TXCP @ \$77.0 Million
 No Bond Sale

BUDGET OF CASH RECEIPTS AND DISBURSEMENTS
 FISCAL YEAR ENDING AUGUST 31, 2003
 (Millions of Dollars)

PreDraw Capital Funding during Fiscal Period	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	BUDGET	TOTAL
2/19/2002	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	
OPENING BALANCE - CASH INCLUDES 77.0 TXCP RECEIPTS	77.0 0.0	\$25.3	\$23.1	\$12.6	\$17.6	(\$3.0)	\$8.0	\$44.9	\$76.2	\$92.0	\$79.9	\$38.8	\$0.0
Gas	33.7	36.0	37.4	48.9	60.2	71.0	79.7	73.4	60.2	44.4	35.4	35.3	615.6
Other	1.5	1.4	1.6	1.7	1.8	1.6	1.8	2.0	2.1	2.0	1.9	9.2	28.6
Drawn from Capital Funds - Principal (\$27.1MM)	27.1	6.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	33.3
Drawn from Capital Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.7	1.7
Drawn from Lease Funds - Principal (\$1.9MM)	0.0	0.0	0.0	0.0	0.0	1.9	0.0	0.0	0.0	0.0	0.0	0.0	1.9
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.2
Advance (Repayment) of Capital Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension Draw	2.4	2.4	2.4	7.2	0.0	0.0	2.4	2.4	2.3	2.3	2.3	2.3	28.4
City Loan													0.0
Extraordinary Rate Relief	1.6 1.2	1.7 1.1	1.8 1.4	2.6 1.9	3.2 2.4	3.7 2.8	4.2 3.1	3.8 2.8	3.1 2.5	2.3 1.7	1.8 1.5	1.6 1.2	31.6 23.6
Rate Relief	1.6	1.7	1.8	2.6	3.2	3.7	4.2	3.8	3.1	2.3	1.8	1.6	31.6
TOTAL RECEIPTS	67.6	49.0	44.8	62.3	67.6	81.0	91.2	84.4	70.0	52.7	42.7	51.6	764.7
TOTAL	67.6	74.3	67.8	74.9	85.2	78.0	99.2	129.2	146.2	144.6	122.7	90.3	764.7
DISBURSEMENTS													
Labor	10.7	12.3	12.1	11.9	12.6	11.0	11.1	11.3	11.5	10.4	11.4	10.9	137.2
Natural Gas	24.3	29.6	34.8	38.3	41.4	43.7	33.4	30.2	28.6	27.1	22.1	22.7	374.4
Debt Service	0.0	1.9	0.0	0.0	24.7	5.3	0.0	2.0	4.7	0.0	41.5	9.6	89.7
TXCP: Interest	3.5	0.2	0.2	0.3	0.3	0.2	0.3	0.3	0.3	0.3	0.2	0.2	3.3
Repayment of City Loan													22.6 22.6
Union/Management Reductions	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.0)	(1.1)	(1.1)	(1.1)	(1.1)	(12.4)
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	18.2	0.0	0.0	18.2
Other Disbursements	8.0	8.2	9.1	9.8	10.2	10.7	10.5	10.2	10.0	9.8	9.8	9.7	116.1
TOTAL DISBURSEMENTS	42.3	51.3	55.2	57.3	86.2	70.0	54.3	53.0	54.3	64.7	83.9	74.5	749.0
MONTHLY CASH FLOW	25.3	(2.3)	(10.4)	5.0	(20.7)	11.0	38.8	31.4	15.7	(12.0)	(41.2)	(23.0)	15.8
CUMULATIVE CASH FLOW	25.3	23.1	12.6	17.6	(3.0)	8.0	44.9	76.2	92.0	79.9	38.8	15.8	
OPENING TXCP	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0
TXCP ISSUED DURING MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TXCP ISSUED PAID DOWN DURING MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ENDING TXCP	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0	77.0
OPENING BALANCE - CASH	0.0	25.3	23.1	12.6	17.6	(3.0)	8.0	44.9	76.2	92.0	79.9	38.8	0.0
MONTHLY CASH FLOW	25.3	(2.3)	(10.4)	5.0	(20.7)	11.0	38.8	31.4	15.7	(12.0)	(41.2)	(23.0)	15.8
NET TXCP ACTIVITY MONTHLY	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ENDING BALANCE - CASH	25.3	23.1	12.6	17.6	(3.0)	8.0	44.9	76.2	92.0	79.9	38.8	15.8	15.8
CITY LOAN AVAILABLE - END OF MONTH	0	0.0	22.5	22.5									
CITY LOAN UTILIZED - END OF MONTH	45	45.0	22.5	22.5									
CASH POSITION NET OF TXCP AND CITY LOAN	(66.7)	(68.9)	(109.4)	(104.4)	(125.0)	(114.0)	(77.1)	(45.8)	(30.0)	(42.1)	(63.2)	(63.7)	

PHILADELPHIA GAS WORKS
EXTRAORDINARY RATE RELIEF
DOCKET NO. R-00017034F0002

OTS CALCULATION OF THE CASH FLOW
IMPACT OF A \$25 MILLION INCREASE
FOR THE FISCAL YEAR 2002

<u>MONTH</u>	<u>FY 2002 Mcf SALES</u>	<u>INCREASE RATE PER Mcf (a)</u>	<u>PROJECTED RATE INCREASE BILLED</u>	<u>PGW COLLECTION FACTOR</u>	<u>PROJECTED RATE INCREASE RECEIPTS</u>
May-02	2,828,307 (b)	\$0.427330756	\$604,311	0.9400	\$568,053
June-02	1,991,843	\$0.427330756	\$851,176	0.9400	\$800,105
July-02	1,496,513	\$0.427330756	\$639,506	0.9400	\$601,136
August-02	1,490,966	\$0.427330756	\$637,136	0.9400	\$598,907
					<u>\$2,568,201</u>

Notes: (a) The rate was scaled back from \$30 million. $(25/30) * 0.512796907$

(b) Assumes rate increase effective mid April (1/2 of the billing cycle).

OTS Statement No. 2
Witness: Kevan Deardorff
Date: March 21, 2002

**DOCUMENT
FOLDER**

DOCUMENT
APR 30 2002

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PHILADELPHIA GAS WORKS

Docket No. R-00017034F0002

Direct Testimony

of

Kevan Deardorff

Office of Trial Staff

Concerning:

Debt Service Coverage

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Kevan L. Deardorff. My business address is P.O. Box 3265,
3 Harrisburg, Pa. 17105-3265.

4
5 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6 A. I am currently employed by the Pennsylvania Public Utility Commission as
7 a Fixed Utility Financial Analyst. I am assigned to the Office of Trial Staff
8 as an expert witness.

9
10 **Q. WHAT IS YOUR EDUCATIONAL AND PROFESSIONAL
11 BACKGROUND?**

12 A. I have prepared this information in Appendix A supplementing my direct
13 testimony.

14
15 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

16 A. The purpose of my testimony is to address Philadelphia Gas Works' (PGW
17 or Company) claim that it requires extraordinary rate relief in order to
18 maintain Standard & Poor's (S&P) investment grade credit rating for their
19 outstanding debt.

20
21 **Q. WHAT CAUSED PGW TO BELIEVE THAT ITS CREDIT RATING
22 IS AT RISK OF BEING DOWNGRADED?**

1 A. Ms. Barbara Bisgaier testified that S&P issued a press release on February
2 12, 2002, that stated without immediate cash flow improvement, the ratings
3 of PGW's bonds would be lowered¹. Indeed, Schedule No. 1 of OTS
4 Exhibit No. 2 presents the Credit Watch report (with negative implications)
5 that was issued on February 12, 2002. In the report S&P states that the
6 current liquidity shortfall is not appropriate for the current rating level.

7

8 **Q. WHAT ARE S&P'S SPECIFIC REASONS FOR KEEPING PGW ON**
9 **CREDIT WATCH WITH NEGATIVE IMPLICATIONS?**

10 A. S&P's primary reasons for the threat are PGW's weak fixed charge
11 coverage and worsening liquidity position. Contributing to these problems
12 are the warmer than normal weather patterns, high accounts receivables, the
13 City of Philadelphia's limited ability to provide assistance, and the inability
14 to convert from interim management to permanent management.

15

16 **Q. WHAT IS PGW'S CLAIM?**

17 A. PGW claims that they need \$44 million in extraordinary rate relief in order
18 to reaffirm their investment grade S&P credit rating.

19

20 **Q. WHAT IS BASIS FOR PGW'S CLAIM?**

¹ Exhibit BCB-1, PGW E.R.P. St. 4. This press release was an announcement of the actual Credit Watch.

1 A. At pages 2 and 3 of his testimony, Mr. Joseph Bogdonavage states that a
2 \$44 million revenue increase is necessary to produce debt service coverage
3 at a level consistent with S&P's criteria for investment grade.
4

5 **Q. PLEASE DEFINE DEBT SERVICE?**

6 A. Debt service is the annual amount of principal and interest due on an
7 outstanding loan.
8

9 **Q. WHAT IS MEANT BY DEBT SERVICE COVERAGE?**

10 A. Debt service coverage is a ratio of annual funds available to cover annual
11 debt service divided by the annual debt service requirement (principal and
12 interest). The Company's filing calculates debt service coverage using two
13 different methods: 1) aggregate debt service coverage ratio and 2) debt
14 service coverage ratio for each debt issue ranked according to
15 subordination².
16

17 **Q. PLEASE DESCRIBE THE AGGREGATE DEBT SERVICE
18 COVERAGE RATIO?**

19 A. The aggregate debt service coverage ratio is calculated by dividing the total

² This method is required in PGW's bond ordinances.

1 cash available to service debt by the aggregate fixed charges. The
2 testimony of Ms. Bisgaier states that S&P defines these fixed charges to
3 include the following: debt service on the 1975 ordinance bonds and the
4 1998 ordinance bonds, the capital lease payments, interest on the
5 commercial paper, the \$18,000,000 payment to the City of Philadelphia,
6 and a \$20 million annual reduction in the commercial paper program.
7 Based on this definition, S&P calculated the aggregate debt service
8 coverage ratio for 2001-02 fiscal year to be .88.

9
10 **Q. WHAT LEVEL OF DEBT SERVICE COVERAGE IS REQUIRED**
11 **BY STANDARD AND POOR'S TO MAINTAIN PGW AT**
12 **INVESTMENT GRADE?**

13 A. Ms. Bisgaier testified at page 5 of PGW Statement E.R.P. No. 4 that S&P
14 requires this ratio to be in the range of 1.20 times to 1.30 times.

15
16 **Q. PLEASE DESCRIBE THE DEBT SERVICE COVERAGE RATIO**
17 **FOR EACH DEBT ISSUE?**

18 A. The debt service coverage ratio for each debt issue is calculated by dividing
19 the cash available to service debt (after all senior debt service is deducted)
20 by the bond's fixed charge.

1 **Q. WHAT IS PGW'S SPECIFIC DEBT SERVICE COVERAGE**
2 **REQUIREMENT?**

3 A. The Rate Covenant set forth in Article IV, Section 403 of its 1975 and 1998
4 Bond Ordinances requires PGW to maintain minimum debt service
5 coverage of 1.5 times for the 1975 Ordinance Revenue Bonds and 1998
6 Ordinance Senior Revenue Bonds and 1.0 times for 1998 Ordinance
7 Subordinate Revenue Bonds

8
9 **Q. WHAT IS THE REQUIRED AMOUNT OF FUNDS AVAILABLE TO**
10 **PROVIDE FOR ADEQUATE AGGREGATE DEBT SERVICE**
11 **COVERAGE?**

12 A. The required amount of funds available to provide for adequate aggregate
13 debt service coverage is \$148,521,000.

14
15 **Q. PLEASE EXPLAIN HOW YOU DETERMINED THE REQUIRED**
16 **FUNDS AVAILABLE NECESSARY TO MAINTAIN PGW'S**
17 **CREDIT RATING AT INVESTMENT GRADE.**

18 A. S&P's requires aggregate debt service coverage in the range of 1.20 times
19 to 1.30 times. To be conservative, I chose the middle of that range as a
20 reasonable target for this proceeding. Schedule No. 2 of OTS Exhibit No. 2
21 provides the calculation of the revenue level necessary to produce a debt

1 service coverage ratio of 1.25 times³. Working backwards in that schedule
2 shows that a 1.25 times coverage ratio would require \$148,521,000 for
3 funds available to cover debt service.

4
5 **Q. DOES YOUR RECOMMENDED FUNDS AVAILABLE OF**
6 **\$148,521,000 PROVIDE ADEQUATE DEBT SERVICE COVERAGE**
7 **FOR EACH BOND ORDINANCE CLASS?**

8 A. Yes. My recommended funds available of \$148,521,000 will provide for
9 coverage of the 1975 Ordinance Bonds and 1998 Senior Ordinance Bonds
10 of 2.78 times and 3.01 times, respectively. These are well in excess of the
11 requirement of 1.5 times. My recommended funds available of
12 \$148,521,000 also provides a coverage ratio of 31.25 times for the 1998
13 Subordinate Bonds, which require only 1.0 times.

14
15 **Q. HOW IS IT THAT MR. BOGDONAVAGE'S RECOMMENDATION**
16 **REQUIRES AN ADDITIONAL \$19 MILLION TO ACHIEVE A**
17 **DEBT COVERAGE THAT IS IN S&P'S RANGE OF 1.2 TO 1.3?**

18 A. Mr. Bogdonavage has made two errors in his debt service coverage
19 calculation in Exhibit JRB-2.

20

³ Schedule No. 2 is similar to Mr. Bogdonavage's Exhibit JRB-2, except that the two errors are corrected and the coverage ratio is lowered to 1.25 times from 1.27 times

1 **Q. PLEASE DESCRIBE MR. BOGDONAVAGE'S FIRST ERROR?**

2 A. Mr. Bogdonavage forgot to add-back capital leases (\$5,954,000) in his debt
3 service coverage calculation. The absence of the capital lease add-back
4 from the calculation has the effect of reducing the debt service coverage
5 ratio.

6

7 **Q. PLEASE DESCRIBE MR. BOGDONAVAGE'S SECOND ERROR?**

8 A. Mr. Bogdonavage has erroneously included \$20 million for budget year
9 2001-02 as the necessary debt service for the commercial paper in Exhibit
10 JRB-2. At line 18 of Exhibit A-2 in the base rate case, PGW is claiming
11 \$11 million for the budget year 2001-02⁴. In order to be consistent, Mr.
12 Bogdonavage should be using the \$11 million debt service for commercial
13 paper in his Exhibit JRB-2.

14

15 **Q. WHAT IMPACT DO THESE ERRORS HAVE ON THE**
16 **COMPANY'S \$44 MILLION EXTRAORDINARY RATE**
17 **REQUEST?**

18 A. If both errors were corrected on Exhibit JRB-2, the aggregate debt service
19 coverage ratio would be 1.41 times, which is excessive in comparison to
20 S&P's required range of 1.20 times to 1.30 times.

⁴ Supporting Financial Information, Volume II, Exhibit A-2.

1 Q. PLEASE SUMMARIZE YOUR RECOMMENDATION IN THIS
2 PROCEEDING?

3 A. I reviewed S&P's criteria and determined that an appropriate aggregate debt
4 service coverage ratio is 1.25 times. Based upon that debt service coverage
5 ratio, I determined that \$148,521,000 of funds available for debt service is
6 required.

7 Q. DOES THIS COMPLETE YOUR TESTIMONY?

8 A. Yes.

Kevan L. Deardorff
Educational and Professional Background

I am a graduate of the Pennsylvania State University, where I received a Bachelor of Science Degree in Business Economics and Finance and a Master of Arts Degree in Economics. Before coming to the Pennsylvania PUC in 1983, I worked as a consultant for the United States Environmental Protection Agency between 1980 and 1981, and as a Research Economist for the Pennsylvania Department of Commerce during 1982.

I am currently employed as a Fixed Utility Financial Analyst III. I have completed rate of return analyses in a large number of rate cases and assisted in the analyses of many electric, gas, water and telephone rate cases. I have prepared rate of return and price cap testimony in the following rate cases:

Keystone Water Company	R-822211-12
	R-822215-19
	R-822221
Western Pennsylvania Water Company	R-832381
Philadelphia Suburban Water Company	R-842592
Duquesne Light Company	R-842583
Western Pennsylvania Water Company	R-842621-25
Riverton Consolidated Water Company	R-842675
Keystone Water Company	R-842755-56
	R-842759
Equitable Gas Company	R-842769
Western Pennsylvania Water Company	R-850096-97
West Penn Power Company	R-850220
Dauphin Consolidated Water Supply Co.	R-860350
Western Pennsylvania Water Company	R-860397
Philadelphia Electric Company (Gas Division)	R-870629
National Fuel Gas Distribution Corp.	R-870719
Western Pennsylvania Water Company	R-870825
Philadelphia Suburban Water Company	R-870840
Equitable Gas Company	R-880971
Chartiers Natural Gas Company	R-891283
Columbia Gas of Pennsylvania, Inc.	R-891468
Arrowhead Public Service Corp.	R-891557
Pennsylvania-American Water Co.	R-901652
Citizens Utilities Water Company of Pennsylvania	R-901663
Citizens Utilities Home Water Company	R-901664

National Fuel Gas Distribution	R-901670
York Water Company	R-901813
Columbia Gas of Pennsylvania, Inc.	R-901873
National Fuel Gas Distribution Corp.	R-911912
The Peoples Natural Gas Company	R-00922180
York Water Company	R-00922168
Pennsylvania & Southern Gas Company	R-00922312
North Penn Gas Company	R-00922276
North East Heat and Light Company	R-00922309
Shenango Valley Water Company	R-00922420
Mechanicsburg Water Company	R-00922502
National Fuel Gas Distribution Corp.	R-00932548
Roaring Creek Water Company	R-00932665
Shenango Valley Water Company	R-00932798
The Peoples Natural Gas Company	R-00932866
Blue Mountain Consolidated Water Co.	R-00932873
Allied Gas Company, et. al.	R-00932952
National Fuel Gas Distribution Corp.	R-00942991
Borough of Media Water Works	R-00943098
Newtown Artesian Water Company	R-00943157
Roaring Creek Water Company	R-00943177
Borough of Schuylkill Haven	R-00943156
Pennsylvania Power & Light Company	R-00943271
National Fuel Gas Distribution Corp.	R-00953299
Frontier Companies	P-00951005
PFG Gas, Inc. and North Penn Gas Company	R-00953524
Commonwealth Telephone Company	P-00961024
PECO Energy Company	R-00973877
PECO Energy Company	R-00973953
Pennsylvania Power & Light Company	R-00973954
Ironton Telephone Company	P-00971182
Metropolitan Edison Company	R-00974008
Pennsylvania Electric Company	R-00974009
Pennsylvania Power Company	R-00974149
PG Energy, Inc.	R-00984280
ALLTEL Pennsylvania, Inc.	P-00981423
Pennsylvania Telephone Association Small Group	P-00981425, <u>et al</u>
United Telephone Company of Pennsylvania	P-00981410
City of Lancaster Water Fund	R-00984567
York Water Company	R-00994605
Pittsburgh Thermal, L.P.	R-00994641
PECO Energy Company	A-110550F0147

City of Lancaster Sewer Fund	R-00005109
PG Energy	R-00005119
City of Lancaster Sewer Fund	R-00005109
PFG Gas, Inc. and North Penn Gas Company	R-00005277
Emporium Water Company	R-00005050
T.W. Phillips Gas and Oil Company	R-00005459
Verizon North, Inc.	P-00001854
Metropolitan Edison Company	P-00001860
Pennsylvania Electric Company	P-00001861
Philadelphia Gas Works	R-00006042
Pennsylvania American Water Company	R-00016339
Wellsboro Electric Company	R-00016356
Verizon Pennsylvania Inc.	R-00016683

DOCUMENT
FOLDER

OTS Exhibit No. 2
Witness: Kevan Deardorff
Date: March 21, 2002

DOCUMENT
APR 30 2002

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

PHILADELPHIA GAS WORKS

Docket No. R-00017034F0002

Exhibits to Accompany

the

Direct Testimony

of

Kevan Deardorff

Office of Trial Staff

Concerning:

Debt Service Coverage

[12-Feb-2002] Summary: Philadelphia, PA; Utility, Gas

STANDARD & POORS	RATINGS DIRECT
---------------------------------	-----------------------

Return to Regular Format

Research:

Summary: Philadelphia, PA; Utility, Gas

Publication date: 12-Feb-2002

Analyst: Anesh Prabhu, New York (1) 212-438-1285; Jodi E Mecht, New York (1) 212-438-2018

Credit Profile

CREDITWATCH UPDATE	To	From
\$150.650 mil. Philadelphia gas wks rev bnds (1998 Gen Ordinance) ser A dtd 06/01/1998 due 07/01/1999-2014 2018 2026	AAA/BBB(SPUR)	BBB
\$103.550 mil. Philadelphia gas wks rev bnds (1998 Gen Ordinance) ser B dtd 06/01/1998 due 07/01/2014 2018 2028	AAA/BBB(SPUR)	BBB
\$20.010 mil. Philadelphia gas wks rev bnds (Sub1998 Gen Ordinance) ser C dtd 06/01/1998 due 07/01/1999-2014	AAA/BBB-(SPUR)	BBB-
\$51.860 mil. Philadelphia gas wks rev bnds 16th ser dtd 05/07/1999 due 07/01/2000-2009 2013-2015	AAA/BBB(SPUR)	BBB
\$112.245 mil. Philadelphia gas wks rev bnds 2nd ser dtd 05/07/1999 due 07/01/2000-2029	AAA/BBB(SPUR)	BBB
\$120.225 mil. Philadelphia gas works rev bnds (1998 Gen Ordinance) third ser dtd 06/01/2001 due 08/01/2003-2018 2021 2031	AAA/BBB(SPUR)	BBB
\$355.825 mil. Philadelphia gas wks	BBB	BBB

Rationale

Standard & Poor's 'BBB' underlying rating (SPUR) and 'BBB' uninsured rating on Ordinance 1975 and 1998 senior bonds, and its 'BBB- SPUR' on the 1998 Ordinance subordinated bonds remain on CreditWatch with negative implications where they were placed July 20, 2000.

Philadelphia Gas Works' (PGW) PGW's poor liquidity position has worsened with December 2001 cash balances at \$3.8 million (2.5 days' cash) compared to ending cash of about \$8.4 million at fiscal year-end August 2000. PGW is filing an emergency rate relief in February 2002 with the Pennsylvania Public Utility Commission (PUC) to address liquidity issues. Without immediate cash flow improvement, ratings will be lowered. PGW's poor liquidity is due, in part, to the PUC final rate order of a \$33.6 million rate increase in December 2001, about \$31.0 million less than requested. This rate shortfall, combined with the warmer-than-budgeted weather this winter and higher receivables, contributes to poor liquidity, which is not appropriate for the current rating level. "If the PUC approves an emergency rate request, Standard & Poor's will review the adequacy of the increase and determine if ratings will be affirmed or lowered," said Standard & Poor's credit analyst Anesh Prabhu.

PGW, the largest municipally owned gas utility in the U.S., purchases, sells, and distributes gas to more than a half-million customers within the city of Philadelphia. At fiscal year-end August 2001, PGW had about \$900 million of debt outstanding.

The ratings reflect the following risks:

- The poor liquidity position required PGW to temporarily borrow from its capital fund account in January 2002 for servicing debt obligations, and requires PGW to rely on financial transactions that create nonrecurring revenues in this fiscal year. Without additional project revenues or rate relief, PGW may be unable to reimburse its capital fund. PGW will also seek a deferral on the \$45 million working capital city loan, due in January 2003.

[12-Feb-2002] Summary: Philadelphia, PA; Utility, Gas

- Weak fixed-charge coverage that, including lease payments and the annual payment to the city of Philadelphia, has ranged between 1.0 times (x)-1.1x during the past four years.
- Limited ability of the city of Philadelphia to provide assistance due to the city's tight financial situation.
- PGW's problems with high account receivables, which were exacerbated in 2001 due to escalating fuel prices recoverable through the gas cost recovery (GCR) mechanism. Receivables have been historically high due to a high proportion of low-income residents in the demographics of PGW's service territory.
- A warm winter, which likely will cause PGW to miss budgeted forecasts in fiscal 2002.
- Inability to convert from interim management to permanent management by December 2001, as directed by PUC's interim rate order in November 2000. The search for permanent management is at an advanced stage and is expected to conclude by April 2002.

Nonetheless, the following strengths offset the risks:

- A favorable closing to the labor contract negotiations in June 2001; the contract freezes labor costs for the next two years, reduces benefits, and reasserts management prerogatives regarding work rules.
- Operational improvements that included correcting the faulty billing system, improving call center performance, and auditing procedure improvements.
- Sound legal provisions that require 1.5x coverage on an accrual basis on the senior bonds.
- The PUC's timely approvals of required gas cost rate increases since regulatory oversight changed in July 2000.
- PGW has successfully solicited federal and state funds in the form of LIHEAP and Crisis grants, which have aided the company's cash flow and earnings position.

OTS Exhibit No. 2
Schedule No. 2

PGW
Fiscal Year 2001-2002
Projected Income Statement

PGW
Fiscal Year 2001-2002
Projected Debt Service Coverage

	Test Year Budget 2001-2002
Operating Revenues	
(1) Gas Revenues	\$ 638,733
(2) Margin Loss Gas Sales	\$ -
(3) Proposed Base Rate Incr.	\$ 25,000
(4) Other Revenues	\$ 28,117
(5) Total Operating Revenues	<u>\$ 691,850</u>
Operating Expenses	
(6) Natural Gas Costs	\$ 334,566
(7) Raw Material Exp.	\$ 10
(8) Total Nat. Gas & Raw Mat.	<u>\$ 334,576</u>
Contribution Margins	\$ 357,274
(9) Supply & Field Expenses	\$ 59,331
(10) Customer Services	\$ 30,222
(11) Bad Debt Expense	\$ 52,544
(12) Marketing	\$ 5,596
(13) A&G	\$ 39,086
(14) Health Insurance	\$ 30,490
(15) Capitalized Benefits & A&G	\$ (13,430)
(16) Amortization	\$ 3,965
(17) Pensions	\$ 3,091
(18) Taxes	\$ 6,054
(19) Added Costs PUC&Other	\$ 10,000
(20) Labor/Cost Savings	\$ (7,100)
(21) Total Oper. & Maint.	\$ 219,849
(22) Depreciation	\$ 31,587
(23) Total Oper. & Maint. Exp.	\$ 251,436
(24) Total Operating Expenses	\$ 586,012
(25) Operating Income	\$ 105,838
(26) Other Income	\$ 5,743
(27) Income Before Interest	\$ 111,581
Interest	
(28) Long Term debt	\$ 50,966
(29) Other	\$ 6,498
(30) AFUDC	\$ (775)
(31) Loss on Extng. Debt	\$ 3,976
(32) Total Interest	\$ 60,665
(33) Net Income	\$ 50,916
(34) City Payment	\$ 18,000
(35) Net Income From Operations	\$ 32,916

	Test Year Budget 2001-02
Funds Provided	
(1) Operating Revenues	\$ 691,850
(2) Restricted Funds	\$ 5,743
(3) AFUDC	<u>\$ 775</u>
(4) Total Funds Provided	\$ 698,368
Funds Applied	
(5) Fuel Costs	\$ 334,576
(6) Other Op. Exp.	\$ 251,436
(7) Less Non-Cash Items	<u>\$ (36,165)</u>
(8) Total Funds Applied	\$ 549,847
Funds Available to	
(9) Cover Debt Service	\$ 148,521
(10) Add-back Capital Lease	<u>\$ 5,954</u>
(11) Funds Available	\$ 154,475
(12) 1975 Debt Service	<u>\$ 55,528</u>
(13) Coverage Ratio	2.78
(14) Funds Available to Cover	\$ 98,947
(15) Capital Lease	<u>\$ 5,954</u>
(16) Funds Available to Cover	\$ 92,993
(17) 1998 Sr. Debt Service	<u>\$ 30,926</u>
(18) Coverage Ratio	3.01
(19) Funds Available to Cover	\$ 62,067
(20) 1998 Subordinate Debt Ser.	<u>\$ 1,986</u>
(21) Coverage Ratio	31.25

Standard & Poor's Fixed Charge Coverage Ratio

Net Available To Service	
(22) Aggregate Debt Service	\$ 154,475
(23) Aggregate Debt Service	\$ 94,394
Fixed Rate Coverage Ratio on	
(24) Aggregate Debt Service	1.64
Fixed Rate Coverage Ratio	
(25) Include \$11 M TXCP Pay.	1.47
Fixed Rate Coverage Ratio	
(26) Include \$18 M City Fee	1.25