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Patrick C. Lynch, Attorney General

August 28, 2008

Via Electronic Delivery and Regular Mail

Luly E. Massaro, Commission Clerk
Public Utilities Commission
89 Jefferson Boulevard
Warwick RI 02889-1046

In Re: National Grid – Request for Change in Gas Distribution Rates
Docket No. 3943

Dear Luly:

On behalf of the Division of Public Utilities and Carriers, I enclose an original and (9) copies of the surrebuttal testimony of David Effron. Division witnesses James Rothschild and Bruce Oliver are still in the process of preparing their respective surrebuttal testimonies, which will be filed tomorrow.

Thank you for your attention to this matter.

Very truly yours,

Paul J. Roberti /kz

Paul J. Roberti
Assistant Attorney General
Chief, Regulatory Unit

PJR/kz
Enclosures

cc: Thomas F. Ahern, Administrator
Service List

NATIONAL GRID
RHODE ISLAND GAS

REQUEST FOR CHANGE OF
GAS DISTRIBUTION RATES

RIPUC DOCKET NO. 3943

BEFORE THE
RHODE ISLAND PUBLIC UTILITIES COMMISSION

SURREBUTTAL TESTIMONY AND EXHIBITS
OF DAVID J. EFFRON

ON BEHALF OF THE

DIVISION OF
PUBLIC UTILITIES AND CARRIERS

AUGUST 28, 2008

Q. Please state your name and business address.

A. My name is David J. Effron. My business address is 12 Pond Path, North Hampton, New Hampshire, 03862.

Q. Have you previously submitted testimony in this docket?

A. Yes. I submitted direct testimony on July 25, 2008 on behalf of the Division. My qualifications and experience are included with my direct testimony.

Q. What is the purpose of this surrebuttal testimony?

A. The purpose of this surrebuttal testimony is to respond to the rebuttal testimony of National Grid witnesses Laflamme and Czekanski. My silence on any particular issues addressed in the Company's rebuttal testimony should not be interpreted as agreement with the Company's position on those issues. At the time of the preparation of this surrebuttal testimony, I have not received responses to data requests on the Company's rebuttal testimony. I reserve the right to amend or modify this surrebuttal based on the Company's responses to those data requests.

Medical and Dental Expense

Q. In his rebuttal testimony, Mr. Laflamme states that he disagree with your proposal to eliminate the Company's pro forma adjustment to medical and dental expenses because "the Company does not believe that seven months of actual claims data is a representative sample for estimating the level of health care actual claims that can be expected over the long term." Do you have a response?

A. Yes. I agree that ideally it would be better to have additional current data available. However, the Company has provided no reason to believe that the actual experience for the period October 2007 to April 2008 is abnormal or unrepresentative of the ongoing level of medical and dental costs. Therefore, I continue to believe that my adjustment is reasonable.

Q. The actual proposal in the Company's rebuttal testimony is to treat the FAS 112 accrual for post-employment benefits, which was inadvertently omitted from its original test year cost of service, as an offset to your proposed elimination of the pro forma adjustment for medical and dental costs, and that no adjustment to the Company's originally filed cost of service be made for either. In your opinion, is this a reasonable proposal?

A. Based on the information presented, no. The actuarial study supporting the FAS 112 accrual shows an accrued liability balance of zero as of April 1, 2007. To the extent that the FAS 112 accrual currently being booked by the Company is necessary to "catch up" for failing to have accrued the liability in prior years, the current expense being booked reflects amounts that should have been booked previously and is a non-recurring expense. Therefore, it appears that this is not the type of expense that should be considered in the determination of the Company's prospective revenue requirement. Accordingly, this expense should not be treated as an offset to my proposed elimination of the Company's pro forma adjustment for medical and dental costs. I have not modified the position in my direct testimony, and I am still adjusting the pro forma test year operation and maintenance expense to eliminate the Company's pro forma adjustment for medical and dental costs.

Gas Marketing Expenses

Q. On page 23 oh his rebuttal testimony, Mr. Czekanski states that "it is not consistent with legal or ratemaking principles to include 'future' [sales] growth in a post-test year period" if the Company's proposed Gas Marketing Expense is not included in the Company's revenue requirement. Do you have a response?

A. Yes. Mr. Oliver has provided ample explanation of why it is likely that the forecasted sales growth will be achieved even in the absence of the Gas Marketing Program. I would further note that the investment to serve the "future" sales growth is included in the Company's rate base, so the inclusion of future sales growth through the rate year in this case is completely consistent with all legal and ratemaking principles that I know of.

Q. Mr. Czekanski goes on to state that if the expense associated with the Gas Marketing Program is eliminated from the Company's revenue requirement, "the load growth that was projected to result from that program should be removed from the proposed rates consistent with generally accepted ratemaking practice." Is his description of the necessary adjustments complete?

A. No. I do not agree that if the expense associated with the Gas Marketing Program is eliminated from the revenue requirement, the load growth should be removed from the projected rate year sales. However, if the Commission were to eliminate the load growth related to the Gas Marketing Program, then the plant supporting that customer growth would also have to be removed from the rate year rate base and the depreciation on that plant would have to be removed from test year expenses. Rate year operation and maintenance expenses would also have to be adjusted to remove any expenses related to the load growth from the program. The increase to the Company's calculated revenue deficiency would be significantly less than the increase from simply removing the margin on the forecasted load growth.

Merger Synergies/Costs to Achieve

National Grid/Southern Union Transaction

Q. At pages 11-12 of his rebuttal testimony, Mr. Laflamme cites several reasons why the Company does not concur with your savings test for the National Grid/Southern Union transaction. Do any of the cited reasons invalidate your test of savings from that transaction?

A. No. The first reason cited is that "due to the large number of adjustments required to be made to the test year expenses directly related to the effects of the merger, most notably to employee levels, the Company feels that any comparison must compare to the requested rate year cost of service levels rather than to test year levels." My test of achieved savings related to the National Grid/Southern Union transaction shows that the normalized test year cost of service exceeds the benchmark cost of service by \$12.4 million. Attachment NG-MDL-Rebuttal-4 shows a merger related decrease to payroll costs of \$5.0 million and merger related facilities savings of \$1.3 million.

Even adjusting my test of savings for these items, the normalized post-transaction cost of service would still substantially exceed the benchmark cost of service.

The second reason cited by Mr. Laflamme is that the proof of savings calculation previously agreed to by National Grid for the Narragansett electric operations "did not contemplate that proven savings should suffer due to an unlikely decrease in electricity load as is the case for gas sales over the period presented in the Division calculation." The decrease in sales to which Mr. Laflamme refers reduced the benchmark by $320,000. The effect on the comparison of the benchmark to the post-transaction cost of service is immaterial.

If my test of achieved savings had showed that post-transaction cost of service narrowly exceeded the benchmark, then these factors may have influenced the conclusions of my analysis. However, with the post-transaction cost of service exceeding the benchmark by $12.4 million, these factors have no effect on my conclusions.

Q. What is the next point cited by Mr. Laflamme in his critique of your savings test?

A. Mr. Laflamme states that "the Rhode Island gas business is facing a period of unprecedented infrastructure investment requirements, as evidenced by the capital forecasts contained in the instant proceeding, along with a desire to accelerate the rate of leak-prone pipe replacements." The capital forecasts contained in the instant proceeding were not included my calculation of the post-transaction cost of service. While the future capital additions will affect the Company's cost of service prospectively, they do not influence my calculation of the difference between the cost of service before and after the National Grid/Southern Union transaction.

Q. What is the last reason given by Mr. Laflamme for the Company's disagreement with your calculation?

A. His final point is that "The calculation employed by the Division includes the fiscal years ended June 2003 through the twelve months ended September 30, 2007 even though National Grid's ownership of the Rhode Island gas business began in August 2006." Arguably, a comparison of the post-transaction cost of service to an adjusted cost of service for the twelve months ended June 30, 2006 (which immediately preceded National Grid ownership of the Rhode Island gas operations) as the benchmark for measuring achieved savings could, in theory, also be useful. However, the Company failed to provide any such comparison. I would also note that use of the cost of service for the twelve months ended June 30, 2006 to establish a benchmark would itself, in practice, be problematic, as the expenses for that period were unusually high and might not be indicative of the reasonable, normal level of ongoing expenses necessary to operate the business (see Division ESM testimony in Docket No.3760, pages 5-8).

Q. Has the Company established that your test of the savings from the National Grid/Southern Union transaction should be rejected?

A. No. Based on the method of measuring achieved savings that has been approved for both Narragansett Electric Company and the former New England Gas Company, there are no savings to be shared from the National Grid/Southern Union transaction. Accordingly, both the shared savings of $897,000 and the amortization of costs to achieve of $158,000 (as shown on Attachment NG-MDL-Rebuttal-4) associated with this transaction should be eliminated from the Company's revenue requirement.

<u>National Grid/KeySpan Transaction</u>

Q. The Company believes that the customer credit of $2,450,000 for the National Grid/KeySpan transaction should be tied to the absence of a savings proof in future cases. Do you agree?

A. Not entirely. I do agree that the Company has been reasonable in basing the customer credit on the "steady state" annual savings. Mr. Laflamme states that those saving are not expected to be achieved until four years following the transaction, which closed in August 2007. Thus, if the Company comes in for a rate case with a test year of 2010, for example, it would be punitive to disallow the shared savings of $2,450,000 when there was not even an expectation that they would be fully achieved by that time.

The Company does not appear to disagree with my proposed limit of ten years on the inclusion of this item in its revenue requirement. I would propose that in any rate case within five years from the present case, no proof of savings from the National Grid/KeySpan transaction should be required for the Company to include the shared savings of $2,450,000 in its revenue requirement. In any rate case more than five years from the present case, proof of continuing savings should be required in order for the Company to continue including the shared savings in its revenue requirement.

Q. The Company suggests that any such proof of savings related to the National Grid/KeySpan transaction should be based on total operation and maintenance expenses, rather than the total cost of service. Is the Company's position unreasonable?

A. No. Given the rebuttal testimony by Mr. Laflamme, with regard to the National Grid/KeySpan transaction, I believe that a proof of savings based on total operation and maintenance expenses would be acceptable.

Rate Year Plant in Service

Q. What is the Company's position on your proposed adjustment to rate year plant in service?

A. At his rebuttal testimony on page 25, Mr. Laflamme indicates that the Company "does not agree" with my proposed adjustments "to the Company's forecasted capital plan." However, I could find no substantive rebuttal testimony directed to this matter. Therefore, I have no reason to modify my direct testimony on this issue.

ARP Rate Adjustment Mechanism

Q. The Company proposes to modify certain elements of the proposed ARP rate adjustment mechanism in response to the points raised in your direct testimony. Do the modifications adequately address your expressed concerns?

A. Yes. It should be noted that I have proposed certain adjustments to the Company's forecast of ARP plant additions through the rate year in this case. To the extent that the Commission adopts those adjustments, I agree with Mr. Laflamme that the base of ARP expenditures to which actual expenditures are compared in Fiscal Years 2009 and 2010 must be modified accordingly.

Summary

Q. Have you prepared a revised revenue requirement calculation based on this surrebuttal testimony?

A. Yes. My Schedules DJE-1S through DJE-8S show the Division's revised revenue deficiency, which reflects the positions in our surrebuttal testimony. In response to Commission Data Request 1-1 to Intervenors & the Division, I have also prepared Schedule DJE-9S, which shows the revenue requirement effect of each of the discrete adjustments proposed by the Division.

Q. Does this conclude your surrebuttal testimony?

A. Yes.

Schedule DJE-1S

NATIONAL GRID - RI GAS
RATE YEAR REVENUE REQUIREMENT
($000)

	(A) Company Position	(B) Adjustments	Division Position
Base Rate Cost of Service	$ 144,920	$ (9,710)	$ 135,210
Costs Subject to Rider Recovery	3,385	-	3,385
Total Cost of Service	148,305	(9,710)	138,595
Rider Revenues	3,385		3,385
Interruptible Firm Revenues	1,600		1,600
Other Miscellaneous Revenues	2,167	-	2,167
Base Rate Revenue Requirement	$ 141,153	$ (9,710)	$ 131,443
Base Rate Revenues, Present Rates	122,698	-	122,698
Revenue Deficiency	$ 18,455	$ (9,710)	$ 8,745
Percentage Rate Increase	15.04%		7.13%

Sources:

(A) Attachment NG-MDL-Rebuttal-1, Page 1
(B) Schedule DJE-2S

NATIONAL GRID - RI GAS
COST OF SERVICE
($000)

	(A) Company Position	Adjustments		Division Position
Uncollectible Accounts Expense	$ 3,556	$ (644)	(B)	$ 2,912
Other Op & Maint Expense	76,561	(3,191)	(C)	73,370
Depreciation and Amortization	20,444	(347)	(D)	20,097
Taxes Other Than Income Taxes	10,021	-		10,021
Income Taxes	8,052	(2,869)	(E)	5,183
Return on Rate Base	26,286	(2,660)	(F)	23,627
Total Base Rate Cost of Service	$ 144,920	$ (9,710)		$ 135,210
Costs Subject to Rider Recovery	3,385	-		3,385
Total Cost of Service	$ 148,305	$ (9,710)		$ 138,595

Sources:
(A) Attachment NG-MDL-Rebuttal-1, Page 1
Expenses reclassified to be consistent with Schedule DJE-2
(B) Schedule DJE-3S
(C) Schedule DJE-4S
(D) Schedule DJE-5S
(E) Schedule DJE-6S
(F) Schedule DJE-7S

Schedule DJE-3S

NATIONAL GRID - RI GAS
ADJUSTMENTS TO UNCOLLECTIBLE ACCOUNTS EXPENSE
($000)

Other Adjustments to Revenue Requirement:

Other Op & Maint Expense		(A)	$ (3,191)
Depreciation and Amortization		(A)	(347)
Taxes Other Than Income Taxes			-
Income Taxes		(A)	(2,869)
Return on Rate Base		(A)	(2,660)
Total			(9,066)
Adjustment to Uncollectible Accounts Expense	2.46%	(B)	(229)
Adjustment for Low Income Rate Discounts		(C)	(415)
Total Adjustment to Uncollectible Accounts Expense			$ (644)

Sources:
- (A) Schedule DJE-2S
- (B) NG-MDL-1, Page 32
- (C) Testimony of Mr. Oliver

Schedule DJE-4S

NATIONAL GRID - RI GAS
OPERATION AND MAINTENANCE EXPENSE
($000)

Medical and Dental Expenses	(A)	$ (907)
Gas Marketing Expense	(B)	(1,229)
Increased Encroachment Activity Expense	(C)	-
Distribution Maintenance Expense	(D)	-
National Grid/Southern Union Synergies and CTA	(E)	(1,055)
Total Adjustment to Operation and Maintenance Expense		$ (3,191)

Sources

(A)	NG-MDL-1, Page 5	
(B)	Testimony of Division Witness Oliver	148-1377
(C)	Accepted by Company in Rebuttal	
(D)	Accepted by Company in Rebuttal	
(E)	Attachment NG-MDL-Rebuttal-4, Page 1	-897-158

NATIONAL GRID - RI GAS
ADJUSTMENTS TO DEPRECIATION EXPENSE
($000)

Adjustment to Plant in Service	(A)	$	(10,259)
Composite Book Depreciation Rate	(B)		3.38%
Adjustment to Pro Forma Depreciation Expense		$	(347)

Sources:
- (A) Schedule DJE-7.1S
- (B) NG-MDL-1, Page 31

NATIONAL GRID - RI GAS
INCOME TAX EXPENSE
($000)

Rate Base	DJE-7S	$ 276,052
Weighted Return on Equity	DJE-8S	3.76%
Preliminary Taxable Income Base		10,374
Tax Reconciling Items	NG-MDL-1, Page 31	(749)
Taxable Income Base		9,625
Taxable Income	Taxable Income Base/.65	14,808
Income Tax Rate		35%
Income Tax Expense		5,183

Schedule DJE-7S

NATIONAL GRID - RI GAS
RETURN ON RATE BASE
($000)

		(A) Company Position	Adjustments		Division Position
Gas Plant in Service		$ 589,769	(10,259)	(B)	$ 579,510
CWIP		8,981			8,981
Contributions in Aid of Construction		(99)			(99)
Accumulated Depreciation		(284,402)	279	(B)	(284,123)
Net Plant		314,249	(9,980)		304,269
Materials and Supplies		2,227			2,227
Prepaid Expenses		46			46
Deferred Debits		1,440			1,440
Cash Working Capital		11,935	-		11,935
Sub-total		15,648	-		15,648
					-
Accumulated Deferred FIT		8,952			8,952
Merger Hold Harmless Deferred FIT		30,337			30,337
Customer Deposits		3,736			3,736
Injuries and Damages Reserve		840			840
Sub-total		43,865	-		43,865
Net Rate Base		286,032	(9,980)		276,052
Rate of Return	(C)	9.19%	-0.63%		8.56%
Return on Rate Base		$ 26,286	$ (2,660)		$ 23,627

Sources
- (A) Attachment NG-MDL-Rebuttal-1, Page 2
- (B) Schedule DJE-7.1S, Page 2
- (C) Schedule DJE-8S

NATIONAL GRID - RI GAS
ADJUSTMENT TO RATE YEAR PLANT IN SERVICE
($000)

Adjustment to Plant Additions 10/01/07 - 9/30/08		(A)	$ (5,282)
Adjustment to Plant Additions 10/01/08 - 9/30/09		(A)	(9,954)
Effect on Average Rate Year Rate Base	50%		$ (4,977)
Total Adjustment to Rate Year Rate Base			$ (10,259)
Adjustment to Rate Year Depreciation Expense		(B)	$ (347)
Adjustment to Accumulated Depreciation 9/30/2008		(C)	(105)
Adjustment to Accumulated Depreciation 9/30/2009		(C)	(173)
Adjustment to Rate Year Accumulated Depreciation			$ (279)

Sources:
- (A) Schedule DJE-7.1, Page 2
- (B) Schedule DJE-4S
- (C) Adjustment to Plant Additions * Depreciation Rate * 1/2

Schedule DJE-8S

NATIONAL GRID - RI GAS
RATE OF RETURN
($000)

Company Position

	Percent of Total	Cost Rate	Weighted Cost
Long Term Debt	40.63%	7.99%	3.25%
Short Term Debt	11.66%	3.91%	0.46%
Common Equity	47.71%	11.50%	5.49%
Total Capital	100.00%		9.19%

Division Position

	Percent of Total	Cost Rate	Weighted Cost
Long Term Debt	59.06%	7.99%	4.72%
Short Term Debt	3.17%	2.58%	0.08%
Common Equity	37.77%	9.95%	3.76%
Total Capital	100.00%		8.56%

Sources:
Attachment NG-MDL-Rebuttal-4, Page 2
Testimony of Mr. Rothschild

Schedule DJE-9S

NATIONAL GRID - RI GAS
REVENUE REQUIREMENT EFFECT OF ISSUES
($Million)

Company Revenue Deficiency		**$ 18,455**
Division Adjustments		
Rate Year Plant in Service		(1,598)
Medical and Dental Expenses		(930)
Gas Marketing Expense		(1,260)
Increased Encroachment Activity Expense	*	-
Distribution Maintenance Expense	*	-
National Grid/SU Synergies and CTA		(1,082)
Low Income Rate Discounts		(415)
Capital Structure		(1,879)
Return on Equity		(2,547)
Total Division Adjustments		(9,710)
Division Revenue Deficiency		**$ 8,745**

* Accepted by Company in Rebuttal