

FILE

Columbia Exhibit No. 2

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Regulation of the Purchased)
Gas Adjustment Clause Contained Within the) Case No. 05-221-GA-GCR
Rate Schedules of Columbia Gas of Ohio, Inc.,)
and Related Matters.)

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PREPARED REBUTTAL TESTIMONY
OF SCOTT D. PHELPS
ON BEHALF OF COLUMBIA GAS OF OHIO, INC.

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**PREPARED REBUTTAL TESTIMONY
OF SCOTT D. PHELPS**

1 Q. Please state your name and business address.

2 A. My name is Scott D. Phelps. My business address is Post Office Box 117, 200 Civic Center
3 Drive, Columbus, Ohio 43216-0117.
4

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

6 A. I am the Director, Gas Management Services, in the NiSource Corporate Services' Energy
7 Supply Services Group, providing gas procurement services for Columbia Gas of Ohio, Inc.
8 ("Columbia").
9

10 Q. Have you previously supplied testimony in this proceeding?

11 A. Yes.
12

13 Q. What is the purpose of your testimony?

14 A. I will respond to the testimony provided by The Office of the Ohio Consumers' Counsel
15 ("OCC") Witness Haugh regarding his recommendation that Columbia procure its gas
16 through a wholesale auction process similar to one that Dominion East Ohio Gas ("DEOG")
17 recently completed for supplying its GCR customers pursuant to PUCO Case No. 05-474-
18 GA-UNC ("Auction"). I will also respond to an issue that arose during cross examination
19 related to one industrial off system sales arrangement.
20

21 Q. What is the nature of the Auction that Mr. Haugh refers to?

1 A. The Auction referred to by Mr. Haugh is a process that results in between four and twelve
2 natural gas suppliers being assigned access to DEOG's on-system storage capacity and
3 DEOG's upstream firm pipeline transportation capacity rights in return for the firm delivery
4 of gas supply to DEOG's city gate as required by DEOG to maintain reliable deliveries to
5 its customers. In the gas industry, this type of contract is often referred to as an asset
6 management contract. In this case, the assets that are referred to include on-system storage
7 assets owned by DEOG and upstream pipeline capacity contracts held by an DEOG that are
8 assigned to the gas suppliers. In such an arrangement, the LDC no longer has direct control
9 of the upstream transportation capacity assets. As a result, rules must be developed within
10 the asset management contract that are intended to mimic the LDC's former ability to
11 control its gas supplies, capacity, and/or provision of customer services in
12 acknowledgement of the LDC's loss of direct control of the delivering capacity. As
13 described in Mr. Haugh's testimony, DEOG employed a "descending clock process"
14 designed to arrive at a New York Mercantile Exchange ("NYMEX") oriented price. In the
15 DEOG Auction, the auctioneer adjusted the price downward until only twelve equal
16 segments of demand ("tranch") were bid upon, with the provision that no one bidder ends
17 up with more than four tranches. The price being bid by gas marketers involved was a dollar
18 amount per Mcf to be added to the final settle price of the NYMEX natural gas contract for
19 the month of gas delivery.

20
21 Q. What is Mr. Haugh's recommendation in this case?

22 A. Mr. Haugh recommends that the Commission order Columbia to implement a DEOG-style
23 auction to be effective for gas flows in April 2007.

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Q. What is the basis of Mr. Haugh's recommendation that Columbia perform an immediate auction?

A. In his testimony, Mr. Haugh arrives at his recommendation through the following conclusions: (1) that the DEOG Auction results are a success; (2) that the DEOG and Columbia systems are not sufficiently unique to make an immediate and essentially identical Auction a significant problem for Columbia; (3) that moving to a wholesale auction would not be a significant change in Columbia's current procurement process; (4) that there are no regulatory impediments to such an Auction; and, (5) that there is no reason to believe that a wholesale auction would not result in prices lower than the historical average when compared to the NYMEX for Columbia's GCR customers.

Q. Do you agree with Mr. Haugh's recommendation for a Columbia auction?

A. No I do not. There are several aspects of Mr. Haugh's viewpoint, including his notion of how quickly such a process could materialize, that are premature, speculative, misinformed, or incorrect. I do not think that an implementation of an Auction by Columbia at this time is necessary or in the best interest of our customers, nor could it be accomplished in the time frame set forth by Mr. Haugh.

Q. Mr. Haugh has concluded that Columbia should be ordered to conduct an Auction because, in his opinion, the DEOG Auction was a success. Do you agree that the DEOG Auction was a success?

1 A. In the sense that a new process was implemented and the bidding was conducted within
2 rules and concluded with contracts being signed, I think it is fair to say that the initial
3 administrative process of the Auction appears to have been a success. I think that this
4 conclusion is and should be separate and distinct from the claim that DEOG's Phase I
5 process is a success and that it should be copied immediately by other Ohio LDC's. Mr.
6 Haugh's reasoning behind declaring the Auction a success appears to be solely that it
7 resulted in a contract price formula which, when compared to DEOG's GCR over two years
8 of historic data, would have resulted in a lower gas price during those two historic years.
9 More specifically, Mr. Haugh claims that the resulting price of the Auction, \$1.44 per Mcf
10 above the NYMEX for each month is a lower amount than the average DEOG GCR price
11 experienced over the last two years when compared to the NYMEX. In addition to this
12 historic review of prices, Mr. Haugh also gives weight to the price of the first few months of
13 the contract which has resulted in relatively low DEOG prices.

14
15 Q. What is wrong with this reasoning?

16 A. DEOG requested approval of its Auction, and the Commission approved DEOG's "Phase I"
17 project in preparation of DEOG's exit from the merchant function. I am not aware of any
18 other comparable LDC auctions that have taken place anywhere in the country. At least in
19 part, the parties involved expect to be monitoring the benefits and risks, successes and
20 failures experienced during Phase I. Within this backdrop, I would characterize this Auction
21 process as a pilot or an experiment. The Auction therefore, is a twenty-three month gas
22 supply experiment, which Mr. Haugh has proclaimed a success after only a few months of
23 operation.

1
2 Q. Why is not a few months enough time to conclude that other LDCs should adopt the process
3 immediately?

4 A. There is more to consider when monitoring and judging this supply experiment than just the
5 initial price of the contract. A long term, core change to an LDC's gas supply process is at
6 stake. When considering core changes related to the long term reliability and economics of
7 gas supply for 1.4 million customers, a more comprehensive approach to the decision
8 making is called for.

9
10 Q. Mr. Haugh has based his conclusion solely on the contract price results. That being the case,
11 do you agree that the bid price, and the first few months of actual pricing prove that
12 DEOG's Auction was a successful experiment that resulted in the best gas price for
13 customers?

14 A. No. First, it should be recognized that the price equation of the supply contracts is only one
15 factor in the overall performance of the contract and the related processes on DEOG's
16 system.

17 Next, even if price were the only measure of success, the first few months of prices
18 for the program is not the measure of that success. It must be recognized that the DEOG gas
19 price mechanism does not include a price hedge on the gas commodity for a two year
20 period. In other words, none of the gas is purchased at a fixed price nor is the gas coming
21 from storage fixed at the price that it was originally purchased at. Rather, the price of 100%
22 of the gas purchased acquired for each month is tied directly to the final settle price on the
23 NYMEX for each month's natural gas futures contracts. As I have mentioned before, there

1 is no longer any price volatility mitigation as the result of buying gas at summer prices and
2 injecting that gas into storage to be used the following winter. For example, during the
3 summer of 2007, if prices are low, the suppliers will fill storage with those lower summer
4 prices. Then, come January 2008, customers will be charged the January 2008 market price,
5 even though a significant portion of the supply used to serve them was gas from storage
6 bought in the summer at summer prices. This lack of price volatility mitigation, or gas price
7 hedging was a serious concern of the OCC's when DEOG first proposed its auction. In the
8 case of the DEOG Auction contract, the first few months of this unhedged program have
9 experienced volatile pricing, but until now those volatile NYMEX prices have been
10 relatively low as a result of record levels of gas in storage nationwide and a hurricane-free
11 summer. The supply rich summer of 2006 has been followed by extremely warm
12 temperatures during the November, December, and January period. The OCC's earlier
13 concern, over an unhedged supply has quickly turned to enthusiasm for the unhedged
14 arrangement. This turnabout seems to be attributable only to the circumstances of the
15 unusually warm temperature conditions and the lack of hurricanes in the Gulf of Mexico
16 last summer. If these chance circumstances had turned out differently I question whether the
17 OCC's view today of DEOG's experiment be the same.

18 For example, if a hot summer, with damaging hurricanes, had been followed by a
19 cold first half of the winter that resulted in reduced supply levels and fear of continued cold
20 weather, NYMEX closing prices might have spiked near the end of summer in a manner
21 similar to that which we experienced in the autumn months of 2005, and continued upward
22 due to a colder winter. The scenario is not far fetched. On Attachment A, data is provided
23 which compares the NYMEX prompt month closing prices during the summer of 2005 and

2006. Note the extreme volatility in prices that occurred in the final trading of the September and October contracts in 2005, driving the final settle prices for those two months to new higher levels. The summer of 2005 can be contrasted with the summer of 2006 which experienced declining prices as the market realized that there would be no damaging hurricanes and that storage would remain very full entering the winter months. The lower prices in the early months of the DEOG Phase I are the result of these 2006 gas market actions, and not because auctions are the cure for high prices. When buying an unhedged price, one should expect highs and lows. With the bearish market conditions that have been in place in the gas market last fall and this winter during DEOG's Phase I process, it is not surprising that an unhedged program is reaping short-term benefits from these particular circumstances. However, the price benefit today does not necessarily mean that the benefit will continue throughout the term of the agreement or beyond.

Q. Should all of an LDC's GCR volatility be left to the vagaries of the final settle price of the NYMEX natural gas futures contract?

A. The natural gas futures contract has, for many years, been the most volatile contract traded on the NYMEX. For this reason, many state regulators and local distribution companies have focused, and continue to focus, on the diversity of the LDCs' pricing efforts, in an effort to mitigate some of the impacts of that volatile market. Many gas buyers, including Columbia, make significant use of published market indices which are representative of the market for gas at specific locations. For monthly indices, these are developed using trades that occur over a two or three day period near the end of the month. Some buyers also incorporate the settle price of NYMEX or some average of a few days of NYMEX prices

1 for a portion of their supply. In addition, buyers sometimes further diversify their pricing by
2 purchasing monthly supplies and locking in prices earlier in the month prior to the gas flow
3 month. Many LDC's also lock in prices through a hedging program months or years prior to
4 receiving the gas for at least part of their portfolio. These efforts, combined with the
5 summer purchase of gas for injection into storage, combine to diversify the price
6 methodology so that the impact of price volatility in one or more of these mechanisms is
7 mitigated to a degree within the portfolio. With the DEOG Auction price, one hundred
8 percent of the purchased volume each month will be priced solely on the settle price of
9 NYMEX. The settle price is determined by NYMEX using the last thirty minutes of the last
10 day of trading for a month's contract. As a basic supply plan principle, it is Columbia's
11 current view that an unhedged price for 100% of supply is not the best approach for a core
12 market supply portfolio.

13
14 Q. Have you reviewed Mr. Haugh's prices related to the two-year history of the program?

15 A. Yes I have. Mr. Haugh limited his review to the recent period of time that DEOG and
16 Columbia were filing monthly GCRs, which began in 2004. Mr. Haugh indicates that the
17 Auction bid price of \$1.44 per Mcf is lower than the DEOG historic GCR price when
18 compared to the NYMEX price.

19
20 Q. Has Mr. Haugh shown how much customers will save under the auction price?

21 A. No, this would be an impossible task, since no one knows if the next two years results will
22 be like the last two years.

1 Q. In the last paragraph on page 10 of his testimony Mr. Haugh states, "When comparing
2 these GCR rates to the NYMEX for the period of November 2004 through September
3 2006 the COH GCR rate was on average \$2.60 per Mcf above the NYMEX and the
4 DEOG GCR was \$2.37 per Mcf above the NYMEX." Do you agree with these price com-
5 parisons?

6 A. No. I do not. Both Columbia and DEOG GCR prices are reported volumetrically (\$ per
7 Mcf) while the NYMEX is reported in energy units (dollars per Dth). In order to compare
8 a GCR volumetric value to the NYMEX energy value a conversion should be made so
9 that both the GCR and NYMEX values are in common units. Furthermore, to make this
10 comparison valid between different LDCs the conversion must utilize the LDC-specific
11 Mcf / Dth conversion value. Attachment B to my testimony performs this conversion by
12 converting the GCRs from dollars per Mcf to dollars per Dth. Attachment B utilizes a
13 1.031 Dth per Mcf conversion factor for DEOG and individual month Mcf per Dth
14 conversion factors for Columbia from Columbia's accounting records. As noted on
15 Attachment B the per Dth difference between Columbia's GCR and NYMEX is \$2.2309
16 while DEOG's difference between GCR and NYMEX is \$2.0536. These figures are
17 substantially different than the numbers calculated by Mr. Haugh.

18
19 Q. Are you able to calculate numbers that match Mr. Haugh's?

20 A. Yes, I am able to match the numbers for both Columbia and DEOG. If you simply
21 subtract the NYMEX average (in dollars per Dth) from the average Columbia GCR (in
22 dollars per Mcf) for this period (which is an inappropriate measurement) I am able to ar-
23 rive at the \$2.60 difference for Columbia and \$2.37 for DEOG as stated by Mr. Haugh.

1
2 Q. When Mr. Haugh compares the two-year historic DEOG gas prices with the historic
3 Columbia gas prices in his testimony, are there any inconsistencies that he has failed to
4 address?

5 A. Yes. DEOG holds a large position of on-system storage. As a result, most of DEOG's
6 storage management costs were not included within its GCR. With Columbia's GCR on
7 the other hand, all storage costs are included. For example, as of November 2004, Co-
8 lumbia's storage-related costs amounted to \$0.798 per Mcf of its GCR price. Because
9 similar costs are not recovered by DEOG through its GCR, the direct comparison is
10 flawed.

11
12 Q. Are there any other differences between Columbia and DEOG's GCRs that cause Mr.
13 Haugh's comparison to be incomplete or inaccurate?

14 A. Yes, during the study of the two-year historic period that Mr. Haugh included in his
15 spread sheet, he ignored the impact of the Actual Cost Adjustments ("ACA") of the two
16 companies. Columbia's ACA averaged \$0.9533 per Mcf during the period and DEOG's
17 ACA averaged \$0.4369, a difference of \$0.5164 which, when viewing only the two years
18 in question, appears to make Columbia's costs look higher by comparison. By not taking
19 these types of things into account, Mr. Haugh's comparison between GCRs and NYMEX
20 prices are inaccurate.

1 Q. Other than these high level comparisons of GCR's and NYMEX settlement contracts over
2 two years of history, did Mr. Haugh present any analysis of the market place in which this
3 Auction occurred in order to better understand the bids that were received?

4 A. No other analysis was presented.
5

6 Q. Are there any other factors that either as a result of market conditions or as part of the
7 DEOG program that appear to have impacted the Auction bid price?

8 A. Yes, the price of storage gas sold by DEOG was set at the average of a then current
9 summer month index, whereas, the accounting LIFO (last in first out) value of the storage
10 gas was somewhat lower than those current prices.
11

12 Q. When that storage gas was sold to the winning marketers in the Auction at current market
13 prices, how was the left over LIFO value of the storage treated?

14 A. The value from the difference between the LIFO value of gas and this year's summer
15 index prices was passed back, to the winning bidders by deferring the charge of a balanc-
16 ing fee that would have otherwise been charged, and which presumably will be charged
17 again after the conclusion of the Phase I. Using the LIFO price to credit the cost of gas is
18 a one-time benefit of pulling out layers of old gas from storage (on an accounting basis).
19

20 Q. What would the DEOG balancing fee likely have been if the LIFO price credit had not
21 been used to eliminate the balancing fee for the twenty-three months of the program?

22 A. DEOG's balancing fee, absent this one-time offset, would be approximately \$0.13 per
23 Mcf. For comparison purposes, this would have been added to the \$1.44 per Mcf to get

1 \$1.57 per Mcf. This is an example of making sure we understand the factors and variables
2 involved in the bid process before arriving at premature conclusions.

3
4 Q. Were there any other pricing events occurring in the market that likely had an impact on
5 the bid process of the DEOG Auction?

6 A. As I have discussed already, storage sold by DEOG to the Auction winners at average
7 summer prices brought a value forward from the LIFO method of accounting for storage
8 gas. Another storage-related event in the market that was occurring at the time of the
9 Auction was an extremely large divergence in futures prices between the summer of 2006
10 and the winter of 2007-2008, as well as between the summer of 2007 and the winter of
11 2007-2008. In fact, the differences between summer and winter prices at that time in 2006
12 during which the Auction was occurring were at all time highs. On August 29, 2006 (the
13 day of the Auction), the price difference between the September 2006 and February 2007
14 NYMEX natural gas futures contracts had grown to \$4.305 per Dth. In Attachment C, it can
15 be seen how high this difference was compared to the historic differential between those
16 two NYMEX contracts.

17
18 Q. Why did the price differentials between summer and winter become so large at that
19 particular time?

20 A. Much of the run up in price for the winter of 2006-2007, and then ultimate collapse of that
21 same price, has been attributed to an anomaly in the market. Specifically, a hedge fund
22 named Amaranth Advisors accumulated a huge trading position where it bought billions
23 of dollars worth of March 2007 futures contracts and sold April 2007 futures contracts. In

1 accumulating this position during the summer of 2006, Amaranth's activities pushed the
2 winter prices up for both the 2006-2007 winter and the 2007-2008 winter while driving
3 down the summer prices in 2006 and in 2007. The extreme differentials in place on
4 August 29, 2006 would not have occurred without Amaranth's impact. In fact only a
5 couple of weeks after the August 29th auction, Aramanth lost its huge bet. As the
6 differential value between March and April 2007 started to drop, Amaranth had to
7 liquidate its trading position which caused a further and dramatic reduction in winter
8 prices with a corresponding reduction in the summer to winter price differentials. As a
9 result, Aramanth lost \$5 billion in one week of September, and another \$1 billion a few
10 days later. The repercussions of this are displayed on Attachment D, which is a line graph
11 of the history of the differential between the October 2006 contract and the February 2007
12 contract. The drop in winter prices that begins in the middle of September is evident in
13 this graph.

14
15 Q. How did this summer winter price spread impacted the Auction bids?

16 A. The Auction bidders knew they would be acquiring certain significant volumes of gas in
17 storage from DEOG at a known price based on the summer 2006 indices, and that they
18 would have a contract to sell those same supplies during the winter of 2006-2007 at winter
19 prices. The February 2007 NYMEX price on August 29, 2006 closed at \$11.115 per Dth. At
20 that time, the bidders would have known that they could lock in, through use of natural gas
21 futures contracts, a large margin (roughly \$4 per Dth) on that supply selling winter futures.
22 These price differentials, which can be considered a market anomaly due to the Aramanth
23 actions, would have been used by bidders to follow the Auction bid price to lower levels

1 than they otherwise would have found practical. Likewise, since the supply contract spans
2 two winter periods, the bidders would have also been able to lock in the margin generated
3 between the summer of 2007 and the winter of 2007-2008. Attachment E shows the historic
4 actual spread between the summer months of 2007 and the winter months of 2007-2008.
5 That price spread on August 29, 2006, was \$2.24 – not as large as the 2006 spread but still
6 unusually large for that time. Note the huge drop in the differential value in mid September
7 as the Aramant fund collapsed, causing the summer-to-winter price spread to drop back to
8 between \$1.20 and \$1.30 per Dth. It is very likely that this large price spread provided an
9 additional opportunity for bidders to bid prices lower than would otherwise been expected.
10 This unusual action in the futures market at the time of the bidding process is, at a
11 minimum, worth further study to determine what the probable effect was on the bidding
12 process, and if, without this spread, it should be expected that the Auction results would or
13 could be repeated when more normal price spreads exist.

14
15 Q. Is there anything wrong with hedging the summer winter values in this way?

16 A. No, I am not indicating that there would be something wrong with the approach that
17 Auction bidders took to lock in those summer-to-winter values, so long as parties involved
18 understand and agree to the process as appears to have been the case. However, variables
19 with this much impact on the process should at a minimum be identified, understood and
20 considered when reviewing the values, successes, and risks of an Auction such as DEOG's.
21 The problem is not with the practice, but with the potential for lack of review that results in
22 a better understanding of how variables such as this impacted this Auction and how they
23 might be expected to influence future Auctions.

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Q. Are there any other pricing variables that should be reviewed in order to better understand the bidding results?

A. These are only those variables that I have been able to determine with a quick review of the circumstances. With a more thorough investigation of the DEOG Phase I process, it is possible that other items might be identified that influenced bid prices.

Q. Mr. Haugh's conclusions about the DEOG Auction are based primarily upon the bid price and the prices delivered over the first few months of the program. Should price be the only measure of success for a process like DEOG's Phase I program?

A. Price is one aspect of the value one should expect from a purchase arrangement intended to supply the LDC's core market. However, it is certainly not the only variable by which to measure a change as critical as a DEOG styled Auction.

Q. Other than price, what else needs to be studied prior to designing an Auction like DEOG's?

A. One important consideration needs to be the makeup of the LDC itself. For example, the LDC's need to be thoroughly analyzed. Columbia has about 1.4 million customers that are served under various sales, CHOICE, and transportation rules, some of which are relatively complex, and all of which are currently provided as an outcome of carefully balanced regulatory agreements and orders. Will any of those tariff services, and in turn, the customers served on those tariffs, be impacted by the implementation of an Auction? Must any of those tariffs be modified to make the Auction contracts operate most effectively?

1 DEOG also relies heavily upon its on system storage fields to assign out and balance
2 supplies with demand on its system. Columbia on the other hand has no on-system storage,
3 but instead, contracts for one hundred percent of its storage from upstream interstate
4 pipelines. This, in and of itself, is a significant difference in the way the two LDCs operate
5 and manage their systems on a day-to-day basis.

6 Furthermore, Columbia must contract for certain locally produced gas supplies that
7 are the sole supply source in certain areas of Columbia's system. Columbia's additional
8 local gas production receipts amount to about 4 Bcf per year, while DEOG's local
9 production supplies, provide about 55 Bcf of DEOG's annual throughput. These DEOG
10 local gas supplies can apparently be utilized throughout DEOG's system, and in fact, can be
11 used by Auction winners as supply comparable to a firm transportation contract with
12 upstream pipelines. These are further examples of the kind of topics and questions that
13 should be studied before drawing conclusions about what action Columbia should or should
14 not be taking.

15
16 Q. On page twelve and thirteen of his testimony, Mr. Haugh describes the two companies,
17 DEOG and Columbia, at a high level, and proclaims that there is no reason why Columbia
18 could not mimic the DEOG auction successfully. Does this provide enough information
19 upon which to base a recommendation?

20 A. No. The two paragraphs that Mr. Haugh devotes to mentioning the differences between the
21 two companies falls far short of the type of knowledge or review that would be needed to
22 determine if an asset management supply structure would be beneficial and if so, what
23 would need to be done to facilitate such a change without disrupting or putting at undue risk

1 existing, long-standing services to GCR, CHOICE, and transportation customer services.
2 Furthermore, Mr. Haugh has failed to propose how such things would be accomplished. He
3 inappropriately concludes only that such a change should “not be significant” and that
4 “COH should be indifferent” and other simplifications of this type.

5
6 Q. On page 13 of his testimony, Mr. Haugh states that “Additionally, COH is already using an
7 RFP process to acquire its winter supply such that moving to a wholesale auction process
8 would not be a significant change in COH’s current procurement process.” Do you agree
9 with this statement?

10 A. Not at all. An Auction is similar to Columbia’s process only in that they both serve to
11 determine the price of a gas purchase. Beyond that, Mr. Haugh’s gross over-simplification is
12 incorrect. The DEOG Auction is materially different from the current Columbia
13 procurement process. First, Columbia’s process results in Columbia having control of the
14 capacity assets to best meet its customer’s demands. In Columbia’s RFP and negotiating
15 process for firm supplies, only a portion of Columbia’s supply needs are contracted for.
16 Much of Columbia’s needs are satisfied through short-term monthly and daily spot
17 purchases, which add flexibility to Columbia’s process. The current process that Columbia
18 employs to procure gas has been reviewed on multiple occasions by the Commission. It is a
19 process that acquires gas at the market prices combined with hedged and storage supply
20 prices. It is a process that is both market sensitive and flexible in its implementation.
21 Furthermore, in DEOG’s case, the two or three years of discussion by interested parties that
22 preceded the August 29, 2006 Auction was used to address longer term portfolio decisions
23 to make way for the Auction, and ultimately for DEOG’s departure from the merchant

1 function. Action to assure that Columbia's contracts expire or renew at the right time to
2 make such an Auction possible have not begun because an Auction has not been part of our
3 plan. At a minimum, an Auction conducted in the near term for Columbia would need to
4 address the Company's existing capacity release, hedging, longer term purchases, and off
5 system sales contracts that extend beyond April 1, 2007 (i.e. OCC's proposed
6 implementation date for an Auction) and in some cases out to March 31, 2009. Mr. Haugh
7 apparently made no review of Columbia's customer services, tariff rules, supply portfolio or
8 customer requirements before jumping to the conclusion that the process would not be
9 significantly different for Columbia.

10
11 Q. You have discussed price issues, customer service variables, and supply portfolio
12 differences that exist between Columbia and DEOG. What else should be considered when
13 reviewing the success of such a program?

14 A. Supply reliability must also be discussed. Price is always important, but without confidence
15 in reliability when serving the core firm market, that price is much less meaningful.
16 Columbia's current process involves scheduling and supply relationships with several
17 pipelines and dozens of potential suppliers, many of them the largest gas producers or
18 marketing arms of the largest gas producers in the country. Columbia is confident with the
19 reliability that such an operation provides. The Auction process results in only one contract
20 design with only a few counterparties on which to rely. Columbia's current process places
21 responsibility for seeing to it that required supplies, whether in storage or from flowing gas
22 purchases, are in place when needed to meet extreme demand conditions during the coldest
23 days or season of the year on Columbia alone. It is a process that has weathered major

1 hurricanes disruptions and extreme cold weather conditions. The DEOG process requires
2 that transportation and storage capacity is released to the Auction winners. In Columbia's
3 process, managing storage levels, injections and withdraws is the key stone of reliable
4 supply planning process. If Columbia were to adopt the DEOG Auction, Columbia would
5 be delegating that important responsibility to others, but would remain accountable for a
6 failure of that supply should a marketer decided to take storage risks that Columbia would
7 not take, particularly in light of the fact that Columbia does not have 1 Bcf of peak day
8 deliverability provided by on-system storage as does DEOG.

9
10 Q. On page 13 of his testimony, Mr. Haugh states that he knows of no regulatory barriers to
11 such an Auction. Are you aware of any such barriers?

12 A. I am not aware of any barriers presented by the state of Ohio, other than a need to have such
13 a large change in the procurement process pre-approved by the Commission , and accepted
14 to a degree by Columbia's customers and other interested parties if it was determined that
15 they would likely be impacted by the change.

16 There is however, a significant issue currently before the Federal Energy and
17 Regulatory Commission ("FERC") that involves asset management contracts. Asset
18 management agreements are in question as a result of their potential conflict with FERC
19 rules and policies regarding capacity release. As an example, in FERC docket 114 FERC
20 61,246 (2006) supplier Louis Dreyfus attempted to gain approval of a release of capacity
21 that was tied to a second arrangement, namely a supply arrangement. The FERC denied the
22 Louis Dreyfus request. FERC's action rekindled doubt and resulted in many in the gas
23 industry questioning the rules and their own procedures. As a result, during 2006, many

1 major suppliers decided not to bid on asset management contracts due to their concern that
2 it would be found in conflict with the FERC's ruling. Likewise, some LDC's also stopped
3 soliciting bids for such arrangements. This discussion throughout the industry led to a filing
4 at the FERC and ongoing rulemaking in Docket No. RM91-11-009 sponsored by a number
5 of the country's largest suppliers, including Coral Energy Resources, L.P., ConocoPhillips
6 Company, Chevron U.S.A. Inc., Constellation Energy Commodities Group, Inc., Tenaska
7 Marketing Ventures, Merrill Lynch Commodities, Inc., Nexen Marketing U.S.A. Inc., and
8 UBS Energy LLC. In the filing, the petitioners made specific recommendations regarding
9 how the FERC might best clarify existing rules so that asset management arrangements
10 could be seen to be in accordance with the FERC's rules.

11
12 Q. What are the principle issues related to the FERC rules that might call into question the
13 ability to enter into asset management contracts going forward?

14 A. First, counsel has advised me that the FERC has indicated that a release of capacity cannot
15 be tied to another arrangement. For example, if capacity is released to a counter party
16 because that counter party has agreed under another contract to delivery and sell a firm
17 supply of gas to the releaser, that contract might be considered a tying arrangement and
18 counter to the FERC rules. Second, and no less relevant to the Auction process than the
19 first, is that the relationship between a release agreement and a second agreement (e.g. a
20 firm gas supply contract) could constitute either a release above maximum pipeline rates,
21 which is counter to FERC rules, or a release below the maximum pipeline rate, in which
22 case the release would need to be posted for bidding by other parties (including those not
23 involved in the auction).

1

2 Q. If the capacity released as part of an Auction arrangement is posted at maximum pipeline
3 rates, how could it be considered to be above or below maximum rates?

4 A. Counsel advises me that the value equation of a contract tied to the release might be
5 considered part of the capacity release value. For example, the gas price of a gas sales
6 contract could be influenced by the fact that related capacity was released at a specified rate,
7 such as the maximum pipeline rate. The FERC's rules favor and protect price transparency
8 in the capacity release marketplace.

9

10 Q. What is currently being done about this issue?

11 A. At this point in time, the FERC has initiated an industry-wide Request for Comments
12 proceeding related to a broad array of the existing capacity release rules and policies.
13 Industry comments are due back to the FERC on March 12, 2007. FERC will then take time
14 to consider those comments and issue its reaction, probably some number of months later.

15

16 Q. Are there any other potential regulatory hurdles?

17 A. Yes, as I pointed out earlier, Columbia relies heavily on upstream interstate storage capacity
18 to balance the supply and demand on its system. It is more than likely that in a DEOG style
19 Auction, the same would still hold true. As a result of such a process, Columbia will still
20 manage storage, but will no longer hold title to the gas that is being injected and withdrawn
21 from the storage that Columbia is holding to help balance its system. As a result, Columbia
22 could be in conflict with the FERC's rule that interstate shippers (transportation and storage
23 capacity holders) must have title to the gas that is being transported or stored in their

1 capacity. In a DEOG style auction for Columbia, only CHOICE marketers, GTS customers
2 (and their marketers), and the Auction suppliers would be buying gas. By the very nature of
3 Columbia's storage contracts, only gas from those shippers would be in Columbia's
4 retained upstream storage. Otherwise, violation of those rules could result in fines up to \$1
5 million dollars per day of the infraction.

6
7 Q. How are the implications of the shipper must have title rule different for Columbia than for
8 DEOG?

9 A. DEOG has a significant storage system of its own that resides on its own system. As it is not
10 an interstate pipeline, DEOG's storage does not fall under the FERC's shipper must have
11 title rule.

12
13 Q. Would these two FERC issues, the one questioning the legitimacy of asset management
14 contracts and the one requiring the shipper to have title to gas, impact Columbia's ability to
15 enter into a DEOG style auction in the near term?

16 A. Yes, currently they would represent a potential barrier. If an LDC wished to pursue such a
17 course, it could make a filing with the FERC, presenting a case to convince the FERC to
18 waive the rules that require the shipper to hold title. With regard to the capacity release
19 issues at the FERC, LDCs, including Columbia are monitoring and participating in hopes of
20 clarifying the FERC rules such that asset management contracting would be seen as being
21 within the FERC rules.

22
23 Q. Did Mr. Haugh address these FERC issues in his testimony?

1 A. No, in his written testimony he only indicated that he could not identify any regulatory
2 barriers. During his cross examination he stated that he was not aware of any potential
3 issues at the FERC.

4
5 Q. Mr. Haugh has recommended implementation of a Columbia auction by April 2007. What
6 is your reaction to this proposed timeline?

7 A. Because of the many issues that I have raised in this testimony, such a timeline is
8 impractical. It should be remembered that DEOG's process included discussions with
9 customers, suppliers, and others that took place over a period of years, not days.

10
11 Q. Would an Auction be best for Columbia's customers?

12 A. It is too early to determine. Phase I of DEOG's plan to leave the merchant business to gas
13 marketers was apparently deemed to be needed to pave the way for Phase II of DEOG's
14 plans to leave the merchant business. It seems likely that at least part of the purpose for
15 having a Phase I was to learn from the process and consider various problems that might
16 occur when allocating all transportation and storage assets to marketers except for some
17 kept for balancing. For example, does the process present problems when volatility,
18 particularly extreme high prices occur in a cold month. What will occur on DEOG's system
19 during times of operational stress, that is, when temperatures reach design conditions? Will
20 deliveries from suppliers equal what is expected on a day-to-day basis? Did DEOG retain
21 the optimum amount of balancing assets? Will any suppliers have supply problems under
22 extreme conditions as a result of less than conservative storage management? What issues
23 or problems will arise in the remaining term of the agreements that DEOG can learn from,

1 either when redesigning the Auction or when pursuing Phase II of its plan? How do large
2 quantities of local gas production in the hands of the Auction winners impact the bid
3 results? What are the impacts of the process on the DEOG choice program? Are the
4 suppliers as reliable under extreme conditions as DEOG's traditional suppliers were? Do
5 unforeseen credit issues arise? Does the new process result in any problems related to
6 balancing the system on a daily, monthly, or seasonal basis? What will the suppliers learn
7 from their experience? Will the marketers find that too much risk (or too little) was taken in
8 their assumptions when making their bids in the first term of the contract? Will the
9 marketers have other recommendations to make in the process or in the pricing or the
10 operational characteristics of the contract, once they have lived with it for a year or two?

11
12 Q. What are the answers to these questions?

13 A. It is too early to say, but they are important questions that should be considered when
14 modifying a process that is important to so many people. It is my assumption that these are
15 the types of questions that could be expected to be monitored or addressed during Phase I of
16 the experiment.

17
18 Q. Is a DEOG style Auction process unacceptable to Columbia?

19 A. Columbia remains open to ideas and discussion regarding ways to best serve its customers.
20 However, we disagree with OCC's premature conclusions, oversimplifications, and
21 unrealistic timing expectations.

22 First, the DEOG auction contract is still in its infancy with a long way to go before it
23 can be declared a success. Second, placing all of the volume in customers' gas costs at risk

1 to the last thirty minutes of trading in the natural gas futures market will create lower lows
2 and higher highs when it comes to gas prices, for a customer base that values consistency.
3 Third, there is a lot yet for interested parties to learn and understand about why the DEOG
4 bid price is what it is, and to what extent non-recurring factors or unique events played a roll
5 in that bid price. Fourth, there exist significant issues with capacity release and shipper must
6 have title rules at the FERC which must be resolved. Fifth, Columbia's processes are
7 interrelated with a regulatory construct that is complex and balanced among the interests of
8 many participants and customers, was approved by the PUCO, and continues through
9 October 31, 2008. Finally, such a process would require an in depth review of the
10 operational and supply portfolio positions and requirements of Columbia, not DEOG.

11 We have not indicated that the problems with an auction approach might not be
12 overcome. Columbia's point of view is that the OCC's demand to pursue such an activity at
13 this time is fraught with many problems and complexities that would require a good deal of
14 time in order to consider the merits of an auction, understand the issues and obstacles and
15 develop workable solutions.

16
17 Q. What would you propose in response to Mr. Haugh's recommendation that the PUCO order
18 Columbia to implement an Auction by February 2007?

19 A. As pointed out in my testimony, an Auction, though not out of the question in the longer
20 run, presents several issues that must be dealt with. It is Columbia's intent to begin
21 stakeholders discussions by April 15, 2007, about what will replace Columbia's current
22 regulatory stipulation. These discussions will, at a minimum, begin to deal with the broader
23 issues of Columbia's CHOICE program and Columbia's merchant role in the post-October

1 2008 time frame. The issue of utilizing traditional purchase contracting processes verses an
2 asset management or portfolio management contract that could result from an Auction
3 process could be included within the context of those merchant discussions.
4

5 Q. Do you have any further issues to discuss related to the Auction process?

6 A. Yes, on page 14 of his testimony, Mr. Haugh recommends a "weighted average RFP
7 wholesale auction". On page 15 of his testimony, he calculates what customers of DEOG
8 would have saved compared to the Auction process that was approved by the PUCO. I do
9 not favor one process over the other, but I do not believe one should take the actual results
10 of an Auction that have been taken place under one set of rules, and assume those same bids
11 would have been placed under a different set of auction rules. I disagree with an assumption
12 like this that means the bidding strategy does not change under different rules.
13

14 Q. Are there any other issues that you would like to address at this time?

15 A. Yes. During my cross examination on January 31, 2007, I was asked about some off system
16 sales made to one particular industrial customer. It was suggested that the currently effective
17 regulatory construct does not provide for Columbia to make off system sales to its own
18 customers.
19

20 Q. Please describe the history of the transactions in question.

21 A. The transactions with this customer were all of the same type under an arrangement that was
22 first effective in November 2000, several years before the 2003 Stipulation became
23 effective. The final winter of the arrangement was the November 2005 through March 2006

1 period. Prior to extending that arrangement for the 2006-2007 winter, Columbia determined
2 that continuation of the arrangement might not be consistent with the 2003 Stipulation that
3 became effective in November 2004, and decided to discontinue the arrangement.
4

5 Q. What was the nature of the off system sale?

6 A. The arrangement was for a peaking service, or in other words, a call option, which meant
7 that Columbia would deliver to the city gate, a supply at a specified volume at the
8 customer's request. The contract contained daily and winter season maximum volumes.
9 Payment from the customer was in the form of a demand charge each month as well as a
10 commodity price for the gas when and if the customer called on the gas supply.
11

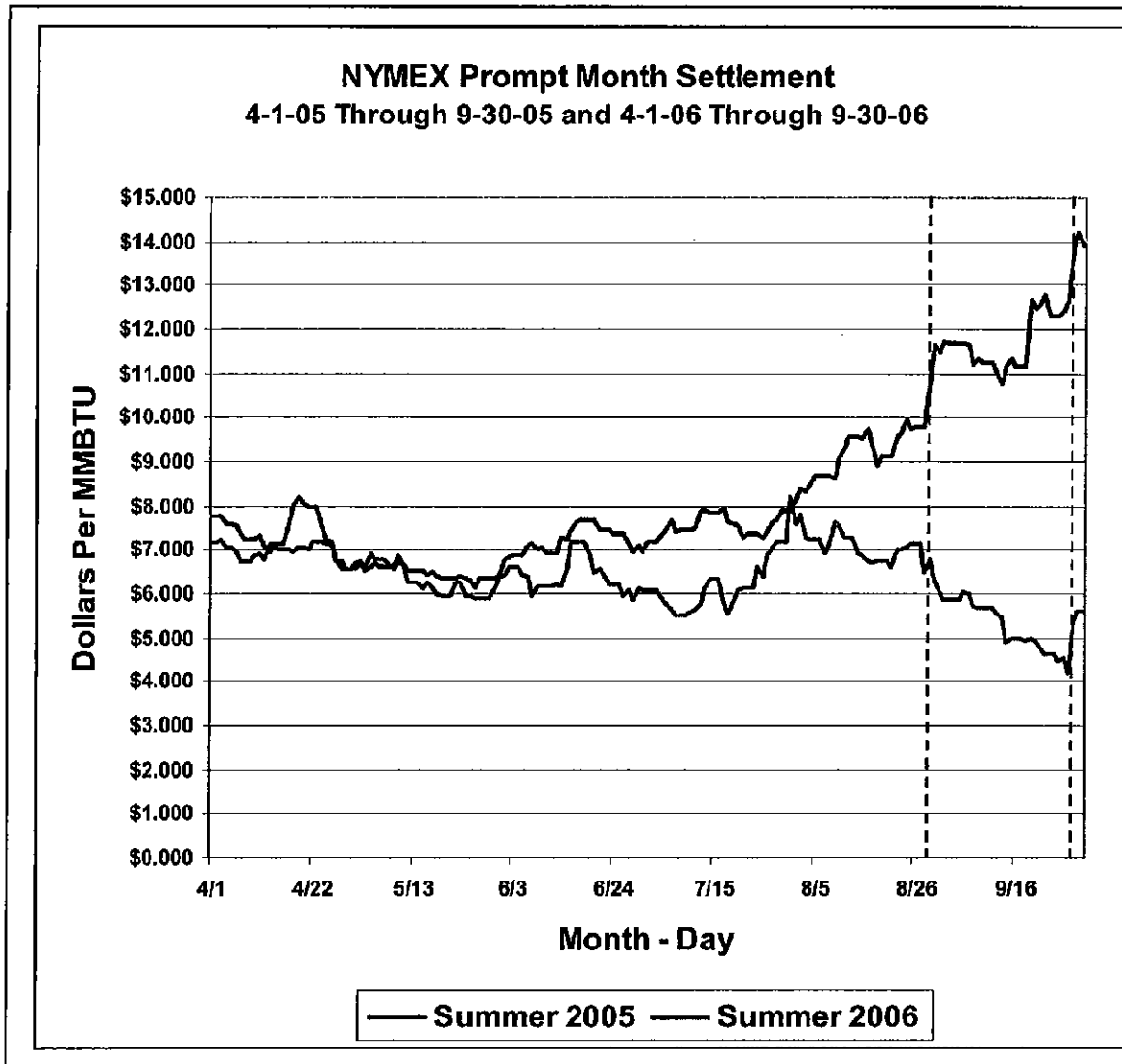
12 Q. If the customer called on one hundred percent of the volume available, approximately how
13 much of the customer's total gas supply needs would that entail each year?

14 A. The contract volume was equal to about 5% of the customer's requirements.
15

16 Q. Does this complete your Prepared Rebuttal Testimony?

17 A. Yes, it does.

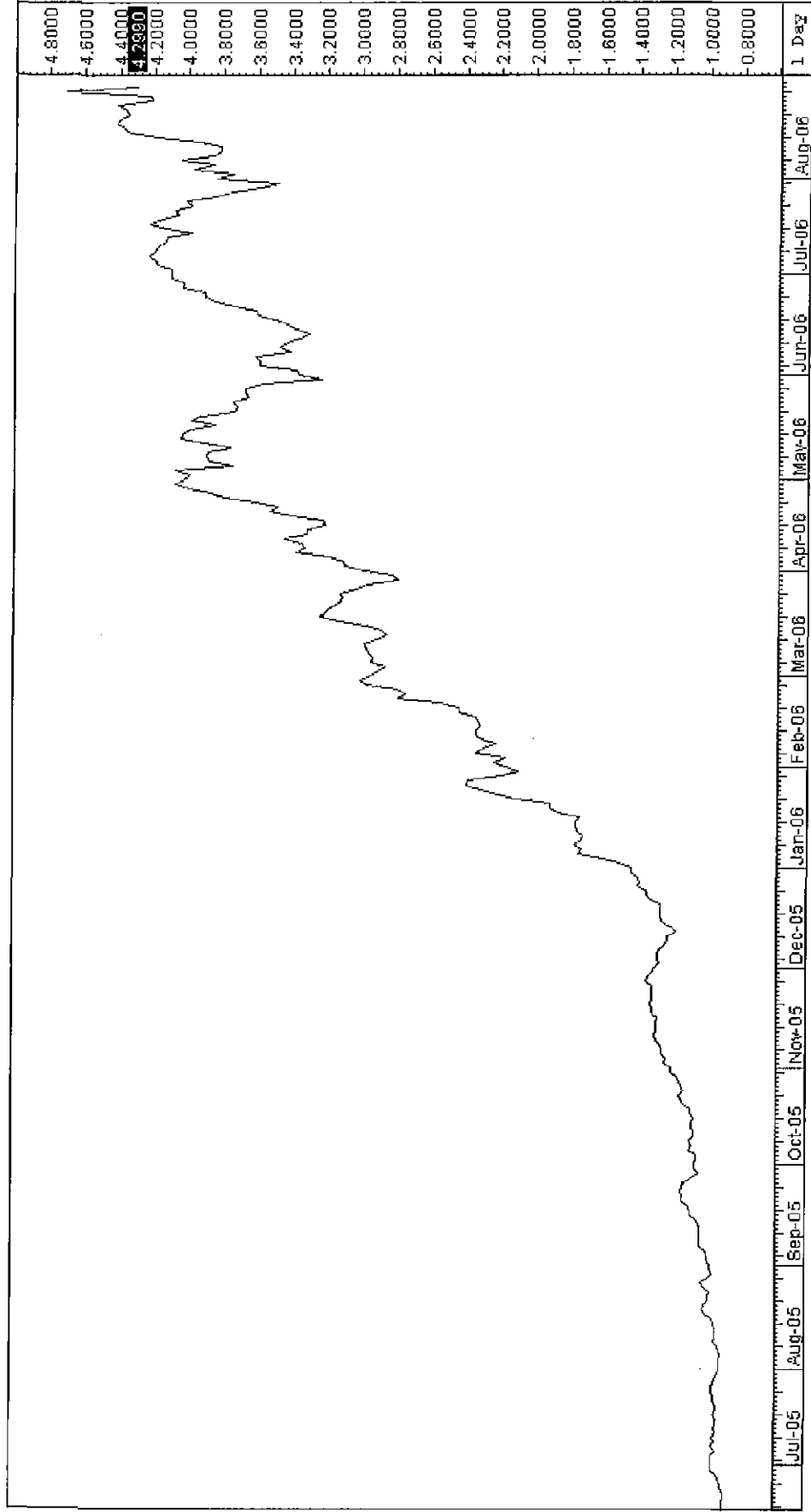
ATTACHMENTS



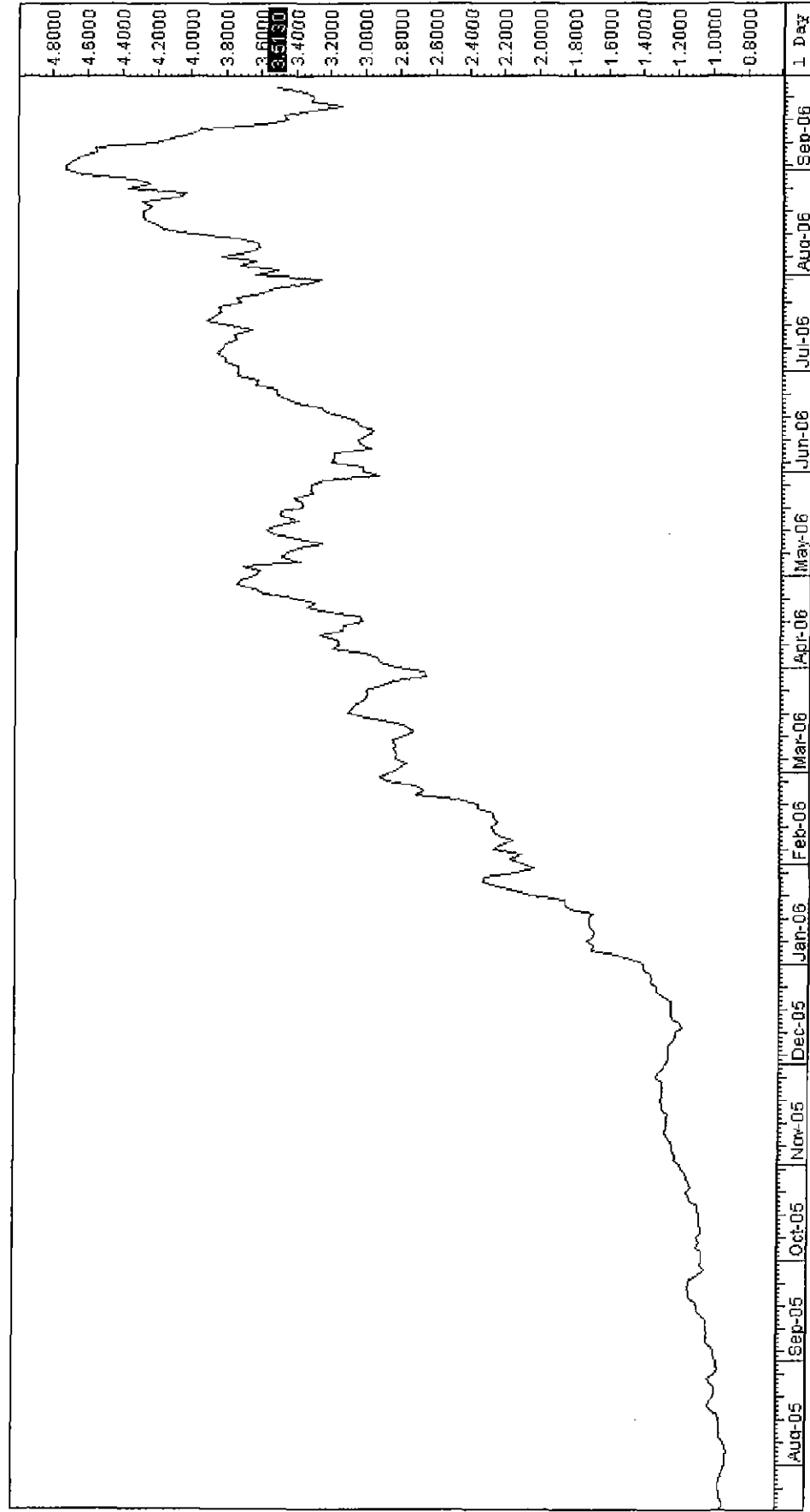
Month	As Filed GCRs				BTU Adjusted GCRs (1)				NYMEX Closing Price	Adjusted GCR vs NYMEX	
	Columbia		Dominion		Columbia		Dominion			Gas of Ohio	Gas of East Ohio
	Gas of Ohio	Gas	Gas of Ohio	Gas	Gas of Ohio	Gas	Gas of Ohio	Gas			
Nov-04	\$ 8.7947	\$ 8.7930	\$ 8.7930	\$ 0.0017	\$ 8.4589	\$ 8.5286	\$ 8.5286	\$(0.0697)	\$ 7.626	0.83	0.90
Dec-04	\$ 9.2371	\$ 9.3250	\$ 9.3250	\$(0.0879)	\$ 8.9101	\$ 9.0446	\$ 9.0446	\$(0.1345)	\$ 7.976	0.93	1.07
Jan-05	\$ 9.8909	\$ 9.0820	\$ 9.0820	\$ 0.8089	\$ 9.5527	\$ 8.8089	\$ 8.8089	\$ 0.7438	\$ 6.213	3.34	2.60
Feb-05	\$ 8.8763	\$ 9.0850	\$ 9.0850	\$(0.2087)	\$ 8.5745	\$ 8.8118	\$ 8.8118	\$(0.2374)	\$ 6.288	2.29	2.52
Mar-05	\$ 8.7557	\$ 9.0690	\$ 9.0690	\$(0.3133)	\$ 8.4572	\$ 8.7963	\$ 8.7963	\$(0.3392)	\$ 6.304	2.15	2.49
Apr-05	\$ 9.8114	\$ 9.9170	\$ 9.9170	\$(0.1056)	\$ 9.4705	\$ 9.6188	\$ 9.6188	\$(0.1484)	\$ 7.323	2.15	2.30
May-05	\$ 9.8114	\$ 9.5690	\$ 9.5690	\$ 0.2424	\$ 9.4980	\$ 9.2813	\$ 9.2813	\$ 0.2167	\$ 6.748	2.75	2.53
Jun-05	\$ 9.7724	\$ 8.8970	\$ 8.8970	\$ 0.8754	\$ 9.4274	\$ 8.6295	\$ 8.6295	\$ 0.7979	\$ 6.123	3.30	2.51
Jul-05	\$ 10.1199	\$ 9.7660	\$ 9.7660	\$ 0.3539	\$ 9.7260	\$ 9.4724	\$ 9.4724	\$ 0.2536	\$ 6.976	2.75	2.50
Aug-05	\$ 10.6184	\$ 10.1480	\$ 10.1480	\$ 0.4704	\$ 10.2732	\$ 9.8429	\$ 9.8429	\$ 0.4303	\$ 7.647	2.63	2.20
Sep-05	\$ 11.3891	\$ 11.3020	\$ 11.3020	\$ 0.0871	\$ 10.9965	\$ 10.9622	\$ 10.9622	\$ 0.0344	\$ 10.847	0.15	0.12
Oct-05	\$ 13.1797	\$ 13.2200	\$ 13.2200	\$(0.0403)	\$ 12.7352	\$ 12.8225	\$ 12.8225	\$(0.0873)	\$ 13.907	(1.17)	(1.08)
Nov-05	\$ 12.9102	\$ 13.7790	\$ 13.7790	\$(0.8688)	\$ 12.4160	\$ 13.3647	\$ 13.3647	\$(0.9487)	\$ 13.832	(1.42)	(0.47)
Dec-05	\$ 12.8659	\$ 13.0240	\$ 13.0240	\$(0.1581)	\$ 12.3794	\$ 12.6324	\$ 12.6324	\$(0.2530)	\$ 11.180	1.20	1.45
Jan-06	\$ 13.6149	\$ 14.8760	\$ 14.8760	\$(1.2611)	\$ 13.1621	\$ 14.4287	\$ 14.4287	\$(1.2666)	\$ 11.431	1.73	3.00
Feb-06	\$ 12.8061	\$ 12.5040	\$ 12.5040	\$ 0.3021	\$ 12.3886	\$ 12.1280	\$ 12.1280	\$ 0.2606	\$ 8.400	3.99	3.73
Mar-06	\$ 11.3926	\$ 11.0740	\$ 11.0740	\$ 0.3186	\$ 11.0393	\$ 10.7410	\$ 10.7410	\$ 0.2983	\$ 7.112	3.93	3.63
Apr-06	\$ 10.8496	\$ 9.7160	\$ 9.7160	\$ 1.1336	\$ 10.5142	\$ 9.4239	\$ 9.4239	\$ 1.0903	\$ 7.233	3.28	2.19
May-06	\$ 10.6830	\$ 10.9340	\$ 10.9340	\$(0.2510)	\$ 10.3578	\$ 10.6052	\$ 10.6052	\$(0.2475)	\$ 7.198	3.16	3.41
Jun-06	\$ 10.3652	\$ 9.1520	\$ 9.1520	\$ 1.2132	\$ 9.9992	\$ 8.8768	\$ 8.8768	\$ 1.1224	\$ 5.925	4.07	2.95
Jul-06	\$ 10.1640	\$ 9.8590	\$ 9.8590	\$ 0.3050	\$ 9.8004	\$ 9.5626	\$ 9.5626	\$ 0.2378	\$ 5.887	3.91	3.68
Aug-06	\$ 9.3756	\$ 9.1020	\$ 9.1020	\$ 0.2736	\$ 9.0411	\$ 8.8283	\$ 8.8283	\$ 0.2128	\$ 7.042	2.00	1.79
Sep-06	\$ 10.5185	\$ 9.9010	\$ 9.9010	\$ 0.6175	\$ 10.1657	\$ 9.6033	\$ 9.6033	\$ 0.5625	\$ 6.816	3.35	2.79
Average	\$ 10.6871	\$ 10.5258	\$ 10.5258	\$ 0.1612	\$ 10.3193	\$ 10.2093	\$ 10.2093	\$ 0.1100	\$ 8.0884	\$ 2.2309	\$ 2.1209

(1) Since GCRs are filed in volumetric units (Mcf) and the NYMEX is traded in energy units (Dth) to make a valid comparison between the two, particularly involving two or more GCR values, one must convert the individual LDC GCR volumetric price to an energy equivalent price using the LDC's own Btu per Mcf conversion factors.

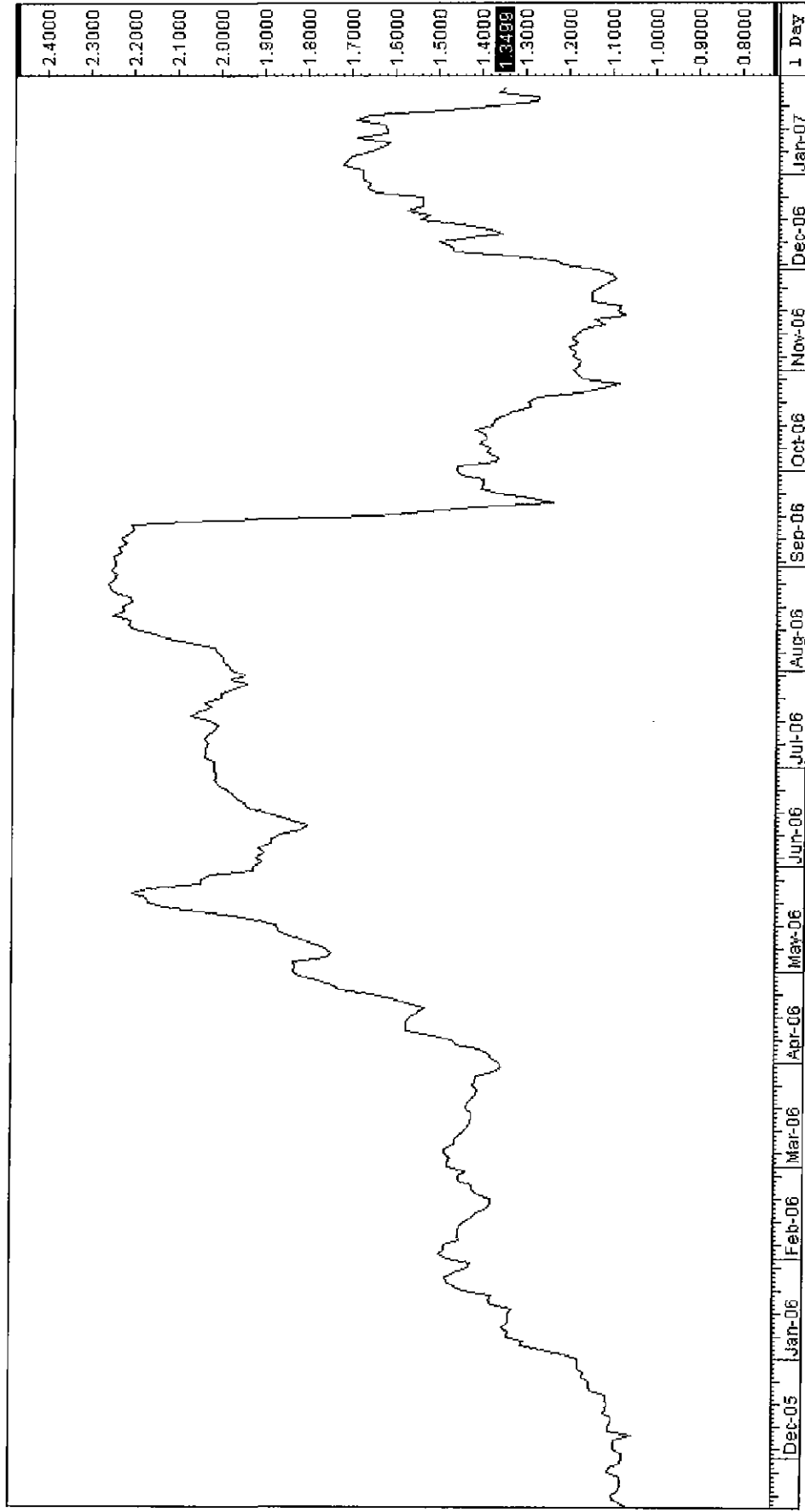
Daily Chart: February 2007 minus September 2006



Daily Chart: February 2007 minus October 2006

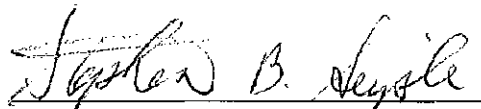


Daily Chart: Winter 2007-2008 minus Summer 2007



CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Prepared Rebuttal Testimony of Scott D. Phelps was served upon all parties of record by email and by regular U.S. Mail this 8th day of February 2007.



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