

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Northeast Ohio	)	
Natural Gas Corp. for an Increase in Gas	)	Case No. 18-1720-GA-AIR
Distribution Rates	)	
	)	
In the Matter of the Application of Northeast Ohio	)	Case No. 18-1721-GA-ATA
Natural Gas Corp. for Tariff Approval	)	
	)	
In the Matter of the Application of Northeast Ohio	)	Case No. 18-1722-GA-ALT
Natural Gas Corp. for Approval of Alternative	)	
Regulation	)	

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**DIRECT TESTIMONY**

**OF**

**JED D. HENTHORNE  
ON BEHALF OF**

**NORTHEAST OHIO NATURAL GAS CORP.**

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_____	Management Policies, Practices, and Organization
<u>  X  </u>	Operating Income
<u>  X  </u>	Rate Base
<u>  X  </u>	Allocations
<u>  X  </u>	Rate of Return
<u>  X  </u>	Rates and Tariffs
_____	Other

January 11, 2019

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1   **I.    BACKGROUND AND QUALIFICATIONS**

2   **Q.    PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3   A.    My name is Jed D. Henthorne. My business address is #1 First Avenue South, Great Falls,  
4       Montana 59401.

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

6   A.    I am Vice President Finance and Administration for Hearthstone Utilities, Inc. (“HUI”),  
7       the ultimate parent company of Northeast Ohio Natural Gas Corp. (“NEO” or “Company”).  
8       In this role, my duties generally include budgeting, financial reporting and rates and other  
9       regulatory matters. I am also President and General Manager for Energy West Montana,  
10      Inc. (“EWM”) and Cut Bank Gas Company (“CBGC”), utilities in the Hearthstone  
11      organization affiliated with NEO. In this position, I am responsible for the overall  
12      operation and future direction of EWM and CBGC including employee relations,  
13      regulatory relations, and gas supply.

14   **Q.    PLEASE   DESCRIBE   YOUR   EDUCATIONAL   AND   PROFESSIONAL**  
15   **BACKGROUND.**

16   A.    I have a Bachelor of Science degree in Management Information Systems – Accounting  
17      Option from the University of Wyoming. I also hold a Wyoming Certified Public  
18      Accountant certificate, currently in inactive status. I have been employed by EWM,  
19      CBGC, HUI or their predecessors or affiliates since September 1, 1982. During that time,  
20      my duties and experience have been focused on accounting, rates, and information  
21      technology. Specific roles include Manager – Information Technology from September  
22      1998 – July 2005, Vice President Administration from August 2005 to November 2014

1 and Corporate Controller from December 2014 to June 2016 before taking on my current  
2 roles.

3 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC UTILITIES**  
4 **COMMISSION OF OHIO (“COMMISSION”)?**

5 A. No.

6 **Q. ON WHOSE BEHALF ARE YOU TESTIFYING?**

7 A. I am testifying on behalf of NEO.

8 **II. PURPOSE OF TESTIMONY**

9 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

10 A. My testimony describes the basis for the test period, the methods used in its calculation,  
11 and the adjustments needed to present a normalized test year. This includes sponsoring  
12 the relevant Standard Filing Requirement (“SFR”) schedules and describing the allocation  
13 process by which the costs of the common services provided by NEO’s parent, HUI, are  
14 allocated to NEO. I also describe the components of the Company’s cost of capital and  
15 present Schedules E-4 and E-4.1 comparing the revenues at current and proposed rates and  
16 Schedule E-5 showing the typical bill comparisons.

17 **Q. WHAT SECTIONS OF THE COMPANY’S APPLICATION ARE YOU**  
18 **SPONSORING IN THIS PROCEEDING?**

19 A. I am sponsoring portions of the SFR’s for Small Utilities, including Section A – Revenue  
20 Requirement, Section B - Rate Base, Section C - Operating Income, portions of Section D  
21 – Rate of Return, and portions of Section E - Rates and Tariffs.

1    **III.    TEST YEAR AND BASIS OF PRESENTATION**

2    **Q.    YOUR TESTIMONY ABOVE REFERENCES THE HEARTHSTONE**  
3    **ORGANIZATION. PLEASE DESCRIBE THE CORPORATE ORGANIZATION**  
4    **OF WHICH NEO IS A PART.**

5    A.    As described more fully in the testimony of NEO witness Kevin Degenstein, NEO is a  
6    direct subsidiary of PHC Utilities, Inc. (“PHC”) and an indirect subsidiary of HUI. NEO  
7    is one of six natural gas utilities owned by HUI.

8    **Q.    MR. DEGENSTEIN REFERENCES IN HIS TESTIMONY CASE NO. 18-1484-GA-**  
9    **UNC RECENTLY APPROVED BY THE COMMISSION, WHICH MERGES**  
10    **BRAINARD GAS CORP. (“BRAINARD”), ORWELL NATURAL GAS COMPANY**  
11    **(“ORWELL”), SPELMAN PIPELINE HOLDINGS, LLC (“SPELMAN”), AND**  
12    **NEO INTO THE SURVIVING ENTITY, NEO. HOW IS THIS MERGER**  
13    **REFLECTED IN THE SFR SCHEDULES AND IN THIS PROCEEDING IN**  
14    **GENERAL?**

15    A.    Each of the four entities (i.e., Brainard, Orwell, Spelman, and NEO) has its own  
16    Commission-approved tariffs and each has maintained separate books and records. NEO  
17    is continuing to maintain the separate books and records through the end of this case as  
18    required by the Commission’s order in Case No. 18-1484-GA-UNC, which approved the  
19    merger of all four Ohio entities into a single entity NEO. For this proceeding, NEO is  
20    presented as a single, combined entity throughout this case and in all SFR schedules.  
21    Where appropriate, the detail for each of the four separate entities is presented in the  
22    schedules. The books and records of each entity are also available as needed. Collectively,

1 the four entities have 29,198 customers as of September 30, 2018; therefore, the SFR for  
2 “Small Utilities” applies in this proceeding.<sup>1</sup>

3 **Q. PLEASE DESCRIBE THE STIPULATIONS ASSOCIATED WITH CASE NO. 16-**  
4 **354-GA-AIS, THE MOST RECENT FINANCING CASE, AND CASE NO. 16-2251-**  
5 **GA-UNC, THE CASE ADDRESSING THE MERGER OF NEO’S PARENT, GAS**  
6 **NATURAL, INC., WITH FR BISON HOLDINGS AND NEO’S PROPOSAL FOR**  
7 **ADDRESSING THEIR REQUIREMENTS AS A COMBINED ENTITY.**

8 **A.** There are a number of stipulations that require certain actions by Brainard, Orwell, NEO  
9 and Spelman or some combination of these entities. For example, Stipulation 4 in Case No.  
10 16-2251-GA-UNC requires each of the corporate entities to maintain a common equity  
11 capital at levels equal to or greater than 45 percent of its total adjusted capital. In Case No.  
12 16-354-GA-AIS, for example, Stipulation 1 limits each entity’s access to the proceeds of  
13 the financing while Stipulation 2 requires each entity to file reports quarterly on the use of  
14 proceeds. In Case No. 18-1484 NEO indicated in its filing:

15 13. Each Ohio Utility will continue to comply with and report individually based  
16 on the requirements of the most recent financing case, Case No. 16-354-GA-AIS,  
17 and with the merger case of the Ohio Utilities with FR Bison Holdings, Case No.  
18 16-2251-GA-UNC, until such reporting may be changed at the conclusion of  
19 NEO’s next rate case.

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<sup>1</sup> See Ohio Adm.Code 4901-7-01, Appendix, Chapter III (defining “Small Utilities” as “more than 7,500 but less than 30,000 customers”).

1 In reviewing the stipulations, it appears that the most practical approach would be to simply  
2 require the combined NEO to conform with the intent of the stipulations by adopting the  
3 requirements as a unified entity. In the above examples this would mean that NEO would  
4 maintain a common equity capital at level equal to or greater than 45 percent of its total  
5 adjusted capital, NEO would have available the sum of the financing proceeds previously  
6 available to the individual entities, and NEO would report quarterly on the use of the  
7 proceeds. Approaching the stipulations in this manner seems consistent with the  
8 Commission's original intent and can be easily ordered without re-writing each item.

9 **.Q. PLEASE DISCUSS THE BASIS FOR EXISTING CUSTOMER RATES FOR EACH**  
10 **OF THE FOUR ENTITIES.**

11 A. The Commission set NEO's rates in Case No. 03-2170-GA-AIR, Orwell's rates in Case  
12 No. 87-706-GA-ATA, and Brainard's rates in Case No. 97-746-GA-ATA. The  
13 Commission established Spelman's rates in Case 11-4444-PL-UNC. The date certain and  
14 revenue requirement are available from NEO's last case but are not readily available for  
15 the other three companies.

16 **Q. PLEASE STATE THE PROPOSED TEST YEAR AND DATE CERTAIN IN THIS**  
17 **PROCEEDING.**

18 A. The test year is the twelve months ending June 30, 2019, with a date certain of September  
19 30, 2018. The test year represents three months of actual financial data for the months of  
20 July, August, and September 2018, and nine months of projected data through June 30,  
21 2019. The Commission approved the test year and the date certain in its Entry dated  
22 December 12, 2018.

1 **Q. PLEASE DESCRIBE THE PROCESS USED BY NEO TO DEVELOP THE NINE**  
2 **MONTHS OF PROJECTED DATA INCLUDED IN THE TEST YEAR**

3 A. NEO applied its budgeting process to develop the projected months of the test year. The  
4 test year date of June 30 falls in-between NEO's 2018 budget and 2019 budget and so a  
5 separate projection for the nine months was prepared. NEO's budgeting process starts with  
6 the latest twelve months of actual data available, which is then normalized for weather and  
7 other adjustments. For the test year, NEO used the twelve months ending September 30,  
8 2018, as the base, to which NEO applied the normalizing adjustments for the entire twelve  
9 months. Schedule C-2.1 presents the test year as the actual three months through  
10 September 30, 2018, with nine months of projected data added to complete the full twelve-  
11 month test year. With a few exceptions discussed later in my testimony, the adjustments  
12 in Schedule C-3 are designed to apply the normalizing adjustments to the actual data in  
13 the three-month period. The result on Schedule C-2 is an adjusted test year that fairly  
14 represents NEO's normalized on-going revenue and expenses.

15 **Q. WILL NEO PROVIDE ACTUAL DATA FOR THE ENTIRE TEST PERIOD IN**  
16 **THIS PROCEEDING?**

17 A. Yes. Within three months after the end of the test year, NEO will file a comparison of the  
18 twelve-month actual income statement for the test year versus the partially projected  
19 income statement. Further, NEO will explain any material differences between the  
20 projected and actual data to the extent necessary.

21 **IV. STANDARD FILING REQUIREMENTS**

22 **A. Revenue Requirement**

23 **Q. PLEASE DESCRIBE SCHEDULE A-1, THE FINANCIAL SUMMARY.**



1 A. **Schedule A-1** is an overall financial summary of the Application, including rate base,  
2 operating income, rate of return, and the proposed revenue increase. Specific references  
3 are made to the various supporting schedules. As shown on line 3, the current earned rate  
4 of return on rate base of 2.82% is significantly below the level required to provide NEO  
5 with a fair and reasonable rate of return. Line 4 shows NEO's requested rate of return on  
6 rate base of 8.66%, which is further detailed in Schedule D-1 and is supported by the  
7 testimony of NEO witness Greg Schieg. Line 9 reflects the proposed revenue increase of  
8 \$3,526,053, which is consistent with the increase derived from the noticed rates in the  
9 proposed tariffs in **Schedule E-1**.

10 Q. PLEASE DESCRIBE **SCHEDULE A-2**, GROSS REVENUE CONVERSION  
11 FACTOR.

12 A. **Schedule A-2** presents the calculated Gross Revenue Conversion Factor used to determine  
13 the overall revenue increase on **Schedule A-1**. The Gross Revenue Conversion Factor uses  
14 the current statutory federal income tax rate of 21%, as reflected on line 6.

15 B. Rate Base

16 Q. PLEASE SUMMARIZE NEO'S RATE BASE.

17 A. **Schedule B-1**, line 14, shows the jurisdictional rate base for NEO to be \$47,659,758 as of  
18 the September 30, 2018 date certain. There are several supporting schedules referenced by  
19 **Schedule B-1**, including **Schedule B-2** (Plant in Service), **Schedule B-3** (Reserve for  
20 Accumulated Depreciation), **Schedule B-5** (Working Capital Allowance), and **Schedule**  
21 **B-6** (Other Rate Base Items).

22 Q. IS NEO INCLUDING CONSTRUCTION WORK IN PROGRESS ("CWIP") IN  
23 RATE BASE?

1 A. No. NEO did not include CWIP in rate base.<sup>2</sup> As such, Schedules A-3, B-4, B-4.1, B-4.2  
2 and B-9, all of which concern or otherwise relate to CWIP, are not applicable and have  
3 been omitted.

4 **Q. IS ALL THE PLANT IN SERVICE USED AND USEFUL IN PROVIDING**  
5 **UTILITY SERVICE IN THE STATE OF OHIO?**

6 A Yes. In the adjustments described below, certain pipeline assets of Spelman have been  
7 removed from rate base because they are either located in Kentucky or they are not used  
8 and useful in Ohio. All remaining plant in service is used and useful in the state of Ohio.

9 **Q. ARE ALL OF NEO'S OPERATIONS SUBJECT TO THE JURISDICTION OF THE**  
10 **COMMISSION?**

11 A Yes. All of NEO's operations are subject to the jurisdiction of the Commission.  
12 Importantly, there are no revenues or costs associated with the assets located in Kentucky  
13 or with the assets in Ohio that are not used and useful and so none are included in test year  
14 revenues or expenses. Therefore, schedules B-7, B7.1 and B7.2, all of which relate to  
15 jurisdictional allocation factors, are not applicable and have been omitted.

16 **Q. HAS THE PLANT IN SERVICE BEEN IDENTIFIED BY ACCOUNTS AND**  
17 **SUBACCOUNTS IN ACCORDANCE WITH THE FERC UNIFORM SYSTEM OF**  
18 **ACCOUNTS AND NEO'S CONTINUING PROPERTY RECORDS?**

19 A. Yes. **Schedule B-2** summarizes by major property groupings the plant in service as of the  
20 date certain, September 30, 2018. **Schedule B-2.1** details the Company's jurisdictional  
21 plant in service by account and subaccount as of the date certain. Except for the

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<sup>2</sup> CWIP was also not included in the final result of NEO's last rate case, i.e., Case No. 03-2170-GA-AIR.

adjustments shown in column (H) of **Schedule B-2.1** and as described below, NEO's gas distribution operations are wholly under this Commission's jurisdiction and no allocation of amounts is needed on **Schedule B-2.1**.

**Q. PLEASE DESCRIBE THE ADJUSTMENTS TO PLANT IN SERVICE.**

A. **Schedule B-2.2** provides further detail of the adjustments to plant in service. As referenced previously, certain assets of Spelman are in Kentucky. In addition, certain portions of the Spelman pipeline in Ohio are not contiguous, and thus, are not considered to be used and useful in this case. Accordingly, the adjustments reflected in **Schedule B-2.2** remove the original cost of these items from plant in service. The total reduction to plant in service is \$1,226,562, as shown in column (H) of **Schedule B-2.1**, which reflects the total plant excluded from rate base. **Schedule B-2.5** clarifies that no additional property was excluded from rate base as of the date certain.

**Q. PLEASE DESCRIBE SCHEDULE B-2.3, THE PLANT IN SERVICE ROLLFORWARD.**

A. **Schedule B-2.3** provides a roll-forward of the gross additions, retirements, and transfers to/from plant in service from June 30, 2003 (i.e., the date certain in NEO's prior rate case) to September 30, 2018 (i.e., the date certain in this proceeding). **Schedule B-2.3** includes the plant in service of Brainard, Orwell, NEO, and Spelman. In the absence of a firm date certain for Orwell and Brainard, June 30, 2003, has been used as a starting point for the data in **Schedule B-2.3**. Spelman is included beginning in 2011, the year it was acquired.

1   **Q.    HAS THE COMPANY INCLUDED LEASED PROPERTY IN ITS RATE BASE?**

2   A.    No. As shown on Schedule B-2.4, the Company has no leased property as of the date  
3       certain. Further, as illustrated by Schedule B-3.4, NEO does not have any related  
4       accumulated depreciation.

5   **Q.    PLEASE DESCRIBE SCHEDULES B-3 AND B-3.1 RELATED TO THE**  
6       **ACCUMULATED DEPRECIATION RESERVE.**

7   A.    Schedule B-3 details the current accumulated depreciation reserve as of September 30,  
8       2018, for each account and subaccount. Schedule B-3.1 illustrates the adjustments to the  
9       accumulated depreciation reserve to account for the removal of certain Spelman pipeline  
10      assets as explained above.

11   **Q.    PLEASE DESCRIBE THE DEPRECIATION EXPENSE CALCULATION IN**  
12       **SCHEDULE B-3.2.**

13   A.    Schedule B-3.2 calculates depreciation expense using the rates and service lives approved  
14       by the Commission. The rates and service lives are different for the assets of NEO, Orwell,  
15       Brainard and Spelman; consequently, Schedule B-3.2 not only presents the depreciation  
16       expense for all four entities combined (titled, "TOTAL OHIO"), it also includes separate  
17       pages for each of the four stand-alone entities. Test year depreciation expense is adjusted  
18       to match this calculated depreciation expense on Schedule C-3.10.

19   **Q.    PLEASE DESCRIBE SCHEDULE B-3.3, THE ACCUMULATED**  
20       **DEPRECIATION ROLLFORWARD.**

21   A.    Schedule B3.3 details the depreciation reserve accruals, retirements and transfers from  
22       June 30, 2003 (i.e., the date certain in Case 03-2170-GA-AIR) to September 30, 2018 (i.e.,  
23       the date certain in this proceeding) by account and subaccount.

1 **Q. PLEASE DESCRIBE THE WORKING CAPITAL ALLOWANCE IN SCHEDULE**  
2 **B-5.**

3 A. As shown on Schedule B-5, the Company proposes to include three items in rate base as a  
4 working capital allowance: 1) a cash component calculated at one eighth of adjusted  
5 jurisdictional operating and maintenance expense; 2) a thirteen-month average of materials  
6 and supplies inventory; and 3) a thirteen-month average of gas in storage and pipeline  
7 imbalances. Schedule B-5.1 demonstrates both the date certain and the thirteen-month  
8 average of both inventories. Schedule B-5.2 indicates no adjustments were made to  
9 working capital items.

10 **Q. PLEASE DESCRIBE THE OTHER RATE BASE ITEMS INCLUDED IN**  
11 **SCHEDULE B-6.**

12 A. Schedule B-6 describes other items that are included in determining rate base, including  
13 reductions for customer deposits, customer advances for construction, regulatory liability  
14 for accrued removal costs, deferred income taxes, and excess deferred income taxes – all  
15 as of the date certain. In addition, the unamortized balance of rate case costs was included  
16 in Schedule B-6. Finally, Schedule B-6 also itemizes reductions for the same items over  
17 a thirteen-month average for the test year.

18 **Q. PLEASE FURTHER DESCRIBE THE REGULATORY LIABILITY FOR**  
19 **ACCRUED REMOVAL COSTS.**

20 A. This amount represents the accumulated regulatory liability for accrued removal costs on  
21 the books of Orwell and Brainard related to the negative salvage accrual rate included as  
22 part of the depreciation accrual rates approved by the Commission in Case No. 03-1913-  
23 GA-AAM for Orwell and Case No. 04-1719-GA-AAM for Brainard. The presentation as

1 a regulatory liability (as opposed to netting with accumulated depreciation) conforms to  
2 the Generally Accepted Accounting Principles (GAAP) presentation.

3 **Q. PLEASE FURTHER DESCRIBE THE LINE ITEMS FOR ACCUMULATED**  
4 **DEFERRED INCOME TAXES AND EXCESS DEFERRED INCOME TAXES.**

5 A. As illustrated by Schedule B-6, accumulated deferred income taxes of approximately \$2.6  
6 million were deducted from rate base as of the date certain. Additionally, as a result of the  
7 Tax Cuts and Jobs Act of 2017 (“TCJA”), Schedule B-6 shows \$2.3 million of excess  
8 deferred income taxes (EDIT) were deducted from rate base as of the date certain. The  
9 EDIT balance includes amounts related to both normalized assets and non-normalized  
10 assets.

11 **Q. HOW ARE CONTRIBUTIONS IN AID OF CONSTRUCTION REFLECTED IN**  
12 **THE COMPANY’S ASSET RECORDS AND IN RATE BASE?**

13 A. As shown on Schedule B-6.2, all contributions in aid of construction received by the  
14 Company are netted against plant in service reflected in Schedule B-2.1.

15 **C. Operating Income**

16 **Q. PLEASE DESCRIBE SECTION C OF THE APPLICATION REGARDING**  
17 **OPERATING INCOME.**

18 A. Section C presents the Company’s operating income for the test year, describes adjustments  
19 necessary to reflect the fair, reasonable, and recurring items that are proper for establishing  
20 an ongoing level of expenses and revenue, and reflects the pro forma adjustments resulting

1 from the requested increase. Section C also incorporates schedules containing statistical  
2 data relating to the income statement.

3 **Q. PLEASE DESCRIBE THE PRO FORMA INCOME STATEMENT THAT IS**  
4 **SCHEDULE C-1.**

5 A. **Schedule C-1** is the jurisdictional pro forma income statement showing the adjusted  
6 revenues and expenses under existing customer rates and the impact of the proposed  
7 revenue increase. Column (D) of this schedule shows that under current rates the  
8 Company's rate of return on rate base is 2.82%. Column (F) shows the rate of return of  
9 8.66%, which reflects the impact to the current adjusted operating income from the  
10 proposed rates included in the Company's proposed tariffs in **Schedule E-1**. The rate of  
11 return of 8.66% is the Company's requested rate of return as illustrated on **Schedule D-1**  
12 and as discussed by NEO witness Greg Schieg.

13 **Q. PLEASE DESCRIBE SCHEDULE C-2, ADJUSTED TEST YEAR OPERATING**  
14 **INCOME.**

15 A. **Schedule C-2** in column (E) identifies the Company's jurisdictional revenue and expenses  
16 for the test year (i.e., the twelve months ending June 30, 2019). Column (F) contains  
17 adjustments to those revenues and expenses, as detailed in **Schedule C-3** and as discussed  
18 later in my testimony. Column (G) contains the jurisdictional adjusted revenue, expenses

and net operating income during the test year and provides the source for certain of the adjusted revenue and expenses identified in column (D) of **Schedule C-1**.

**Q. PLEASE DESCRIBE SCHEDULE C-2.1, OPERATING REVENUES AND EXPENSES BY ACCOUNT.**

A. **Schedule C-2.1** details by account the operating revenues and expenses for the test year in accordance with the Uniform System of Accounts. The amounts on this schedule reflect the unadjusted test year amounts, including the actual results for July, August and September 2018 and the projected amounts for the remaining nine months of the test year. The costs included are all incurred to support the NEO customer base and contain both the combined NEO's direct costs and allocated costs for shared services provided by NEO's indirect parent, HUI.

**Q. PLEASE FURTHER EXPLAIN THE ALLOCATED COSTS.**

A. HUI manages the shared services and allocates associated expenses among all HUI companies. Internally, we refer to the shared services as HUI Services. HUI Services is not a service company and is not a separate legal entity. Included within HUI Services are the salaries and expenses of corporate officers and administrative staff, auditing, legal and other professional outside services, engineering services, information technology services, and salaries and expenses of HUI accounting staff. The costs associated with the shared services are allocated among the HUI companies on the basis of the "4-factor formula", which originated with the Montana Public Service Commission in 1993. The allocation methodology is designed for shared costs. Direct charges for services provided to subsidiary companies are not subject to the formula; instead, these types of expenses must be supported by time sheets, invoices, or other direct evidence of cost. The 4-factor



1 formula has been consistently applied and accepted by the Montana Public Service  
2 Commission, the Maine Public Utilities Commission, and the North Carolina Utilities  
3 Commission. The 4-factor formula used for allocation of HUI Services is specified in the  
4 Support Services Agreement as part of the Stipulation Settlement in Case No. 16-355-GA-  
5 UNC, which was approved by this Commission.

6 **Q. HOW IS THE 4-FACTOR FORMULA CALCULATED AND HOW IS IT**  
7 **UPDATED?**

8 A. The 4-factor formula is calculated using the average of each entity's percentage of the 1)  
9 total operating and maintenance expense (exclusive of shared costs), 2) net plant, 3)  
10 number of customers, and 4) number of employees. The 4-factor formula is updated for  
11 all HUI entities on an annual basis during the budgeting process, using the latest data  
12 available for expenses, net plant, customers and employees. This updated allocation  
13 formula is applied at the start of each calendar year. For the unadjusted test year, **Schedule**  
14 **C-2.1** on page 3, line 48 shows the combined NEO's portion of HUI Services costs as  
15 \$2,127,187. This represents the actual three months and the projected nine months of the  
16 test year. Please reference my later testimony related to **Schedule C-3.9** for information  
17 on the adjustments to the test year and the net combined NEO costs of HUI Services.

18 **Q. PLEASE DESCRIBE SCHEDULE C-3, ADJUSTMENTS TO REVENUES AND**  
19 **EXPENSES.**

20 A. **Schedule C-3** summarizes the adjustments which are detailed in **Schedules C-3.1** through  
21 **C-3.11** and **C-4** through **C-9**. The adjustments are needed to present an annualized and  
22 normalized test year that reflects the annual effect of expenses and revenues. As described  
23 earlier in my testimony, with two exceptions, the adjustments provide normalizing effect

1 to the actual three months. The projected months are already normalized. The exceptions  
2 are income tax expense, and rate case expense, which are presented as adjustments to the  
3 full test year amounts.

4 **Q. PLEASE DESCRIBE SCHEDULE C-3.1, ADJUSTMENTS TO NORMALIZE**  
5 **REVENUE.**

6 A. **Schedule C-3.1** normalizes the revenue for the three months of July, August and  
7 September 2018 for weather and other known changes and includes adjustments to the base  
8 revenue and also to the revenue and costs related to gas cost recovery. Workpaper WPC3.1  
9 referenced by Schedule 3.1 provides details of the adjustments. For the base revenue,  
10 unbilled revenue included in the actual three months of July – September 2018 is removed.  
11 The projected months of the test year include no unbilled revenue or unbilled volumes.  
12 The monthly service charge is normalized based on the average customer count during the  
13 test year and the sales volumes are normalized for weather. For Brainard, base revenue is  
14 adjusted to reflect the loss of one of its largest customers, who has switched to a competing  
15 utility company for its gas service. Finally, the revenue recorded in the actual three months  
16 for Spelman has been removed as it will no longer be billing for the use of its assets. The  
17 total adjustment to base revenue is a reduction of \$171,591.

18 The gas cost related adjustment is applied equally to both gas cost revenue and gas  
19 costs and the effect on the revenue requirement is zero. The adjustment removes the  
20 unbilled revenue related to the actual three months of the test year and then adjusts the gas  
21 cost rate to the test year average and applies it to the normalized sales volumes. The total  
22 gas cost related adjustment to both revenue and costs is \$313,451.

1 **Q. PLEASE DESCRIBE THE METHODOLOGY USED FOR THE WEATHER**  
2 **NORMALIZATION ADJUSTMENT.**

3 A. NEO's service territory takes in large portions of the State of Ohio with differing weather  
4 patterns and degree days, As a result, we calculated the weather normalization on a  
5 customer by customer basis. We used the average usage for July and August as the base  
6 use for each customer. We weather normalized the heat sensitive use for each customer  
7 using the degree days appropriate for their location. For NEO standalone this was either  
8 Lancaster or Strasburg (Akron Canton), For Orwell, this was either Cleveland Area or  
9 Youngstown and for Brainard, Youngstown was used. The volume normalization pages  
10 of workpaper WPC3.1 show the summary of this calculation for each of the three entities.

11 **Q. PLEASE DESCRIBE SCHEDULE C-3.2, ADJUSTMENTS TO MCF EXCISE TAX.**

12 A. **Schedule C-3-2** removes the Mcf excise tax expense of \$3,543 included in the actual three  
13 months of the test year. The projected months of the test year include no Mcf excise tax  
14 expense.

15 **Q. PLEASE DESCRIBE SCHEDULE C-3.3, ADJUSTMENTS TO METER READING**  
16 **EXPENSE.**

17 A. NEO currently hires an outside contractor to perform its meter reading functions. A new  
18 contract was recently signed and the net adjustment of \$12,661 is needed to update the  
19 meter reading costs in the actual three months to reflect the increased cost reflected in the  
20 new contract. A portion of the meter reading expenses for the actual three months is  
21 incorrectly included in account 875. This adjustment also moves these amounts to the  
22 correct account, account 902.

1 **Q. PLEASE DESCRIBE SCHEDULE C-3.4, ADJUSTMENTS TO RENT EXPENSE.**

2 A. NEO has leased a building in Churchtown for the purpose of establishing a local base of  
3 operations for the system to serve customers in the Churchtown area. This adjustment  
4 normalizes the actual three months of rent expense for the related operating lease cost.

5 **Q. PLEASE DESCRIBE SCHEDULE C-3.5, ADJUSTMENTS TO PROPERTY AND**  
6 **LIABILITY INSURANCE EXPENSE.**

7 A. This adjustment updates the actual three months to reflect an increase in property and  
8 liability insurance based on the most current invoices. The projected months of the test  
9 year include the property and liability insurance expense based on the most current  
10 invoices.

11 **Q. PLEASE DESCRIBE SCHEDULE C-3.6, ADJUSTMENT FOR RATE CASE**  
12 **EXPENSE.**

13 A. Based on the details provided in Schedule C-8, the adjustment for rate case expense adds  
14 the annual amortization of the costs of this proceeding, assuming a five-year amortization  
15 period.

16 **Q. PLEASE DESCRIBE SCHEDULE C-3.7, REMOVAL OF DEFERRED RENT**  
17 **EXPENSE.**

18 A. Included in the actual three months of the test year is amortization expense related to the  
19 cost of NEO's Enterprise Resource Planning system, SAP, which expired on September  
20 30, 2018. The adjustment in Schedule C-3.7 removes this amortization expense (i.e.,  
21 \$79,624) from the test year expense. The projected months of the test year do not include  
22 any amortization expense.

1 **Q. PLEASE DESCRIBE SCHEDULE C-3.8, ADJUSTMENT TO OUTSIDE**  
2 **SERVICES.**

3 A. This adjustment updates the three actual months of the test year to reflect the normalized  
4 on-going level of outside services costs, reflecting a reduction of \$116,438 to test year  
5 expenses. The projected months of the test year also reflect the normalized on-going level  
6 of outside services costs.

7 **Q. PLEASE DESCRIBE SCHEDULE C-3.9, ADJUSTMENT TO HUI SERVICES**  
8 **COSTS.**

9 A. The adjusted test year total of HUI Services costs is \$5,888,077. Applying the 4-factor  
10 formula calculated for 2019, the combined NEO's portion of the allocation is 36.9887% or  
11 \$2,177,926. The Schedule C-3.9 adjustment is further described by the summary page of  
12 workpaper WPC3.9 which on page 2 updates the three actual months of the test year for  
13 the 2019 4-factor formula percentages and then applies normalizing adjustments to reflect  
14 the on-going level of HUI Services costs.

15 **Q. PLEASE DESCRIBE SCHEDULE C-3.10, ADJUSTMENT TO DEPRECIATION**  
16 **EXPENSE.**

17 A. As noted earlier in my testimony, the calculations in Schedule B-3.2 result in an adjustment  
18 to test year depreciation expense. For the actual three months of the test year, this  
19 adjustment totals \$14,342 and is reflected on Schedule C-3.10. The adjustment also  
20 removes amortization of intangible assets not included in rate base.

1 **Q. PLEASE DESCRIBE SCHEDULE C-3.11, ADJUSTMENT TO PROPERTY TAX**  
2 **EXPENSE.**

3 A. This adjustment updates the three actual months of the test year to reflect normalized  
4 property tax expense and is based on the most recent property tax invoices. The projected  
5 months of the test year also reflect the normalized amounts based on the most recent  
6 invoices.

7 **Q. PLEASE DESCRIBE SCHEDULES C-4 AND C-4.1, RELATED TO INCOME**  
8 **TAXES.**

9 A. Schedule C-4.1 presents the unadjusted income tax expense for the test year while  
10 Schedule C-4 provides the adjusted income tax expense for the same period. The  
11 adjustments to the test year income tax expense reflects the synchronized interest expense  
12 and the 21% federal tax rate enshrined in the TCJA. The adjustment of \$370,056 is  
13 reflected on line 34, page 3 of Schedule C-3.

14 **Q. PLEASE DESCRIBE SCHEDULE C-5 RELATED TO FEES AND DUES.**

15 A. Schedule C-5 identifies the social organization and service club dues and fees. The dues  
16 for the American Gas Association and the Ohio Chamber of Commerce were adjusted to  
17 remove any costs/expenses related to lobbying. This reduction carries forward to column  
18 (M) on page 2 of Schedule C-3.

19 **Q. PLEASE DESCRIBE SCHEDULE C-6, CHARITABLE CONTRIBUTIONS.**

20 A. Schedule C-6 illustrates expenses for charitable contributions. The contribution to OH  
21 Partners Affordable Energy, which was made pursuant to a Commission-approved

1 Stipulation and Recommendation in Case No. 03-2170-GA-AIR,<sup>3</sup> is the only contribution  
2 included in test year expense.

3 **Q. PLEASE DESCRIBE SCHEDULE C-7, CUSTOMER SERVICE AND**  
4 **ADVERTISING EXPENSES.**

5 A. **Schedule C-7** enumerates customer service, sales and advertising expenses. Only the  
6 advertising expenses are separately itemized. All other expenses related to customer  
7 service are not individually documented in the Company's records.

8 **Q. PLEASE DESCRIBE SCHEDULE C-8, RATE CASE COSTS.**

9 A. **Schedule C-8** shows the estimated cost of this proceeding and provides the basis for the  
10 adjustment in **Schedule C-3.6** described earlier in my testimony.

11 **Q. PLEASE DESCRIBE SCHEDULES C-9 AND C-9.1 RELATED TO PAYROLL**  
12 **AND EMPLOYEE BENEFITS.**

13 A. **Schedule C-9** presents the unadjusted and adjusted payroll and benefits costs for the test  
14 year. The adjustments update the three actual months of the test year to reflect normalized  
15 payroll and benefits based on current approved positions and current payroll tax and benefit  
16 rates. These adjustments flow through to **Schedule C-3**, column (F). The nine projected  
17 months of the test year also reflect the normalized payroll and benefits. **Schedule C-9.1**  
18 reflects payroll and benefits statistical information for the test year and the most recent five  
19 years.

20 **Q. PLEASE DESCRIBE SCHEDULE C10.1 AND C10.2, COMPARATIVE DATA.**

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<sup>3</sup> See *In the Matter of the Application of Northeast Ohio Natural Gas Corp. for an Increase in its Rates and Charges for Natural Gas Service, et al.*, Case No. 03-2170-GA-AIR *et al.*, Opinion and Order (Nov. 10, 2004), at 5.

1 A. **Schedule C-10.1** presents comparative balance sheets as of the date certain and as of year  
2 end for each of the most recent calendar years. **Schedule C-10.2** identifies comparative  
3 income statements for the unadjusted test year and each of the most recent five years.

4 **Q. PLEASE DESCRIBE THE STATISTICS INFORMATION INCLUDED IN**  
5 **SCHEDULE C-11.1 THROUGH SCHEDULE C-11.4.**

6 A. **Schedule C-11.1** presents revenue statistics for the Company and each of the individual  
7 four entities by customer class for the most recent five years, as well as the test year.  
8 **Schedule C-11.3** provides sales volume information for the same periods for the Company  
9 and each of the individual four entities by customer class. **Schedules C-11.2** and **C-11.4**  
10 identify the same information on a jurisdictional basis but are inapplicable since all of the  
11 Company's operations are 100% jurisdictional.

12 **Q. PLEASE DESCRIBE SCHEDULE C-12, RELATED TO THE RESERVE FOR**  
13 **UNCOLLECTIBLE ACCOUNTS.**

14 A. **Schedule C-12** presents the analysis of the reserve for uncollectible accounts for the three  
15 most recent calendar years and the test year. The activity nets to zero as the Company's  
16 uncollectible accounts are tracked through either the percentage of income payment plan  
17 ("PIPP") riders or uncollectible expense riders.

18 **D. Rate of Return**

19 **Q. PLEASE DESCRIBE HOW THE COMPANY FUNDS ITS OPERATIONS.**

20 A. The Company finances its operations through internally generated funds and the proceeds  
21 from the issuance of securities. The Company's capital is presented as the combined total  
22 of the four individually merged entities: NEO, Orwell, Brainard, and Spelman. For each  
23 of the four entities, equity consists of common stock and additional paid-in-capital by HUI



1 through PHC. Debt financing for each of the four entities comes in the form of  
2 intercompany agreements between each of the four entities and HUI. Specifically, each  
3 of the four entities has an agreement with HUI for a short-term line of credit and NEO,  
4 Orwell and Brainard have separate agreements with HUI concerning long-term debt. All  
5 of these agreements were approved by the Commission in Case No. 16-354-GA-AIS. Now  
6 that the merger of the four entities into NEO has been approved by the Commission, after  
7 the merger is effectuated, the debt agreements will likely be merged into two agreements  
8 between NEO and HUI, one for short-term lines of credit and the other for long-term  
9 financing,

10 **Q. PLEASE DESCRIBE SCHEDULE D-1 AND THE COMPONENTS OF THE**  
11 **COMPANY'S CAPITAL STRUCTURE.**

12 A. As shown on Schedule D-1, the Company's capital structure as of the date certain consists  
13 of 64.47% equity and 35.53% long-term debt. The weighted average cost of capital is  
14 8.66%, which is based on the Company's embedded cost of debt of 4.72% and cost of  
15 equity of 10.83%. NEO witness Greg Schieg further expands on the cost of equity  
16 calculation and the reasonableness of NEO's capital structure.

17 **Q. PLEASE DESCRIBE SCHEDULE D-1.1 RELATED TO EQUITY.**

18 A. Schedule D-1.1 puts forth additional detail describing the components of the Company's  
19 \$35,831,416 of equity.

20 **Q. PLEASE DESCRIBE SCHEDULE D-2, SHORT TERM DEBT.**

21 A. Schedule D-2 describes the balance of the Company's short-term line of credit with HUI  
22 and the annual interest costs as of the date certain.

23 **Q. PLEASE DESCRIBE SCHEDULE D-3, LONG TERM DEBT.**

1 A. **Schedule D-3** describes the Company's long-term debt with HUI and the embedded cost  
2 of 4.72%. The annual interest cost shown in column (K) is comprised of interest of  
3 \$863,808 on the principal amount at the coupon rate of 4.23%, plus the amortization of  
4 debt issue costs and loss on reacquired debt totaling \$67,752, for a total annual interest cost  
5 of \$931,560. The carrying value in column (J) is calculated as the face amount of the debt  
6 outstanding of \$20,421,000 minus the unamortized debt issue costs of \$186,822 minus the  
7 unamortized loss on the reacquired debt of \$490,718 for a net of \$19,743,460. The  
8 embedded cost of debt of 4.72% is calculated as the annual interest cost of \$931,560  
9 divided by the carrying value of \$19,743,460.

10 **Q. HAS NEO ISSUED PREFERRED STOCK?**

11 A. No. NEO has no preferred stock as indicated in **Schedule D-4**.

12 **E. Rates and Tariffs**

13 **Q. PLEASE DESCRIBE SCHEDULES E-4 AND E-4.1, BASE OPERATING**  
14 **REVENUES BY RATE SCHEDULE**

15 A. **Schedules E-4** and **E-4.1** contain the summary and detail, respectively, by rate schedule,  
16 of the base operating revenues at the current and proposed rates. Current revenues, totaling  
17 \$15,050,450 (including \$94,152 of miscellaneous revenue), represent the adjusted test year  
18 totals, including changes made through **Schedule C-3**. Proposed revenues totaling  
19 \$18,576,400 (also including \$94,152 of miscellaneous revenue) use the same billing  
20 determinants (i.e., number of bills or customers, volumes) at the rates and charges proposed  
21 by NEO witness Charles Loy in his cost of service and rate design study. The increase  
22 shown on **Schedule E-4** is \$3,525,950 (\$18,576,400 minus \$15,050,450) which due to rate  
23 rounding is \$103 different from the \$3,526,053 shown on **Schedule A-1**.

1   **Q.     PLEASE DESCRIBE SCHEDULE E-5, TYPICAL BILL COMPARISONS.**

2   **A.     Schedule E-5** presents typical bill comparisons at various usage levels for each rate  
3         schedule at the current and proposed rates and charges.

4   **V.     CONCLUSION**

5   **Q.     DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

6   **A.     Yes, but I reserve the right to supplement my testimony.**

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Summary: Testimony Direct Testimony of Jed D. Henthorne electronically filed by Mr. Trevor Alexander on behalf of Northeast Ohio Natural Gas Corp. and Brainard Gas Corp. and Orwell Natural Gas Company and Spelman Pipeline Holdings, LLC