

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Eastern Shore Natural Gas Company

)

Docket No. RP07 -

PREPARED DIRECT TESTIMONY OF
RONALD A. CRAIG

1 **Q. Would you please state your name, occupation, and business address?**

2 A. My name is Ronald A. Craig. I am Contract & Billing Administrator for Eastern
3 Shore Natural Gas Company (“Eastern Shore”). My business address is 417 Bank
4 Lane, Dover, Delaware, 19904.

5 **Q. Would you describe your education and relevant professional experience?**

6 A. I graduated in 1973 from the University of Delaware with a Bachelors Degree in
7 Business Administration. I have been employed by Eastern Shore since May 1977.
8 Since that time I have been involved in, among other things, contracts, billing, tariffs,
9 the preparation of studies concerning costs and rates, and various financial matters
10 contained in rate and certificate proceedings with the Federal Energy Regulatory
11 Commission (“the Commission”), as they pertain to Eastern Shore.

12 **Q. Have you previously submitted testimony before the Federal Energy Regulatory**
13 **Commission?**

14 A. Yes, I have submitted testimony in previous Eastern Shore rate proceedings.

1 **Q. Why has Eastern Shore submitted a filing at this time?**

2 A. Eastern Shore has initiated this proceeding in accordance with the terms of a
3 Stipulation and Agreement approved by the Commission in Eastern Shore's last
4 Section 4 rate case at Docket No. RP02-34-000. As stipulated in Article IX therein,
5 Eastern Shore is required to make a filing to revise its base tariff rates with a
6 proposed effective date of November 1, 2006. Article IX further stipulates that,
7 should Eastern Shore propose an increase in its base tariff rates, it may be filed at any
8 time between September 1, 2006 and November 1, 2006, with Eastern Shore
9 agreeing to up to a full five-month suspension of its effectiveness, pursuant to 18
10 C.F.R. §154.202.

11 **Q. Please briefly describe Eastern Shore's pipeline system and the services it**
12 **provides?**

13 A. Eastern Shore has operated interstate natural gas transmission facilities on the
14 Delmarva Peninsula since 1959. Eastern Shore provides open access firm and
15 interruptible transportation service to several local distribution companies ("LDCs"),
16 as well as a small number of industrial and power generation customers, with
17 operations on the Delmarva Peninsula. Eastern Shore also provides firm storage
18 service to several of its LDC customers. Currently, all of the gas transported by
19 Eastern Shore is received from Transcontinental Gas Pipe Line Corporation
20 ("Transco") and Columbia Gas Transmission Corporation ("Columbia") at points of

1 interconnection with those pipelines in Southeastern Pennsylvania and Northern
2 Delaware. Eastern Shore's system extends from its interconnections with
3 Transco/Columbia southward into Delaware and the Eastern Shore of Maryland. At
4 the end of the test period in this case, its system will be comprised of 366 miles of
5 mainline pipeline facilities (including looping) and compression facilities (totaling
6 10,220 horsepower) located at Daleville, PA., Bridgeville, DE., and Delaware City,
7 DE.. There are no physical storage facilities located on Eastern Shore's system;
8 storage service (under Rate Schedules GSS; LSS; and LGA) is provided to Eastern
9 Shore's customers via Eastern Shore's contracts with Transco in accordance with the
10 restructuring of services approved by the Commission in Docket Nos. CP96-97, et
11 al. Eastern Shore provides firm and interruptible transportation services on its
12 system under its FT, ST, T-1, and IT Rate Schedules, in addition to the GSS, LSS,
13 and LGA storage services mentioned above.

14 **Q. What is the purpose of your testimony in this proceeding?**

15 A. I will discuss Eastern Shore's overall cost of service, rate base, depreciation expense,
16 cost classification, and derivation of rates.

17 **Q. Are there additional witnesses offering testimony in this proceeding and, if so,**
18 **can you identify them and provide a brief description of their testimonies?**

19 A. Yes, there are five additional witnesses who are offering testimony in this
20 proceeding. They are:

1 Amanda Chi (ES-3) – Witness Chi is providing testimony describing adjustments to
2 operations and maintenance expense and Taxes Other Than Income.

3 Joseph D. Steinmetz – (ES-4) – Witness Steinmetz is providing testimony on Federal
4 and State Income Taxes and Deferred Income Taxes.

5 Paul R. Moul – (ES-5 and ES-6) – Witness Moul is providing testimony regarding
6 the appropriate return on equity.

7 Elaine B. Bittner – (ES-7) – Witness Bittner is providing testimony on the business
8 and regulatory risks faced by Eastern Shore.

9 Michael P. McMasters (ES-8) – Witness McMasters is providing testimony
10 discussing the cost of debt, proposed capital structure, and financial risks.

11 **Q. What statements and/or schedules are you sponsoring in conjunction with your**
12 **direct testimony?**

13 A. I am sponsoring the following statements and schedules: Statements A, B, C, D, E,
14 G thru G-6, H-2, I, J and supporting schedules.

15 **Q. Please describe the statements that set out the calculations for the cost of service**
16 **as filed herein.**

17 A. Statement A summarizes the overall cost of service for services provided for the
18 twelve-month test period ending March 31, 2007. Pursuant to Part 154 of the
19 Commission’s regulations the test period extends forward nine months from the end
20 of the base period. The base period in this proceeding is the twelve months ended
21 June 30, 2006. The test period ends nine months past this date or March 31, 2007.

1 As shown on Line 8, the total cost of service is \$26,019,906. The cost of service
2 consists of operations & maintenance expense, depreciation expense, federal and
3 state income taxes, taxes other than income taxes, and return, as developed in
4 Statements H-1, H-2, H-3, H-4, and B, respectively. Additional information
5 regarding the rate of return is included in the testimony of Eastern Shore's witness
6 Paul R. Moul, (ES-5). Also, reflected on Line 7 is an IT cost of service credit that I
7 will address later in my testimony.

8 **Q. Please explain Statement B.**

9 A. Statement B summarizes the test period rate base and return, as derived from
10 Statements C, D, E, and Schedules B-1, B-2, and F-2. The method used by Eastern
11 Shore conforms to Section 154.303 of the Commission's regulations that permits the
12 use of a base period rate base adjusted to reflect the conditions that are anticipated to
13 exist at the end of the test period. Furthermore, the test period rate base will be
14 adjusted as actual information becomes available through the end of the test period.
15 The rate base consists of net plant plus working capital, reduced by accumulated
16 deferred income taxes, and increased by regulatory assets. The overall rate of return
17 of 11.72% yields an overall return on rate base of \$9,590,016 as shown on Line 9.

18 **Q. Please describe Schedules B-1 and B-2.**

19 A. Schedule B-1 sets forth the accumulated deferred federal and state income taxes
20 deducted from the rate base as of March 31, 2007. The total deferred income taxes
21 deducted from rate base are \$9,808,720 by Eastern Shore witness Steinmetz (ES-4).

1 Schedule B-2 sets forth the balances for the regulatory assets and liabilities at the
2 end of the test period.

3 **Q. Please describe the contents of Statement C.**

4 A. Statement C provides a summary of the cost of plant for Accounts 101 through 107.
5 The total cost of plant claimed in rate base by Eastern Shore is \$118,622,550.
6 Schedule C-1 shows the projected Gas Plant balances as of March 31, 2007.
7 Furthermore, the test period cost of plant will be adjusted as actual information
8 becomes available through the end of the test period.

9 **Q. What is contained in Statement D?**

10 A. Statement D sets forth accumulated depreciation from Account 108 as of March 31,
11 2007. This total is deducted from total gas plant investment to determine total net
12 gas plant investment claimed in rate base. The test period accumulated depreciation
13 will be adjusted as actual information becomes available through the end of the test
14 period.

15 **Q. Please explain Statements E, Schedules E-1 and E-2.**

16 A. Statement E reflects the components of working capital shown in Statement B as an
17 addition to rate base. Schedule E-1 states that Eastern Shore does not claim a
18 separate allowance for cash working capital. Schedule E-2 shows Eastern Shore's 13
19 monthly balances, from June 2005 through June 2006 for Materials and Supplies
20 (Account 154) and Pre-Payments (Account 165). The average of these 13 monthly
21 balances is \$607,511. Pre-payments have been adjusted to reflect the annualization

1 of additional insurance costs and property taxes, increasing the average balance by
2 \$79,376 to a total of \$686,887.

3 **Q. Please explain Statements F-1 through F-4.**

4 A. Statements F-1 through F-4 are sponsored by Eastern Shore witness Michael P.
5 McMasters (ES-8).

6 **Q. You stated earlier in your testimony that you were the sponsor of Statement G. Can**
7 **you explain it in further detail?**

8 A. Yes. Statement G, Page 1 of 4, shows a summary of Eastern Shore's base period
9 transportation revenues. Base period transportation revenues are shown by major
10 rate component; i.e. demand/reservation and commodity, and by the ACA surcharge
11 component. Base period revenues are further detailed by rate schedule (FT, ST, IT
12 and T-1) and rate zone (One and Two), where applicable. Statement G, Page 2 of 4,
13 summarizes Eastern Shore's test period transportation revenues. Test period
14 revenues are also shown by major rate component, i.e. demand/reservation and
15 commodity, and by the ACA surcharge component. Test period revenues are also
16 detailed by rate schedule (FT, ST, T-1) and rate zone (One and Two), where
17 applicable. Statement G, Page 3 of 4, summarizes Eastern Shore's base period
18 transportation billing determinants. Base period billing determinants are categorized
19 as demand/reservation and commodity and are further detailed by rate schedule (FT,
20 ST, IT, and T-1) and rate zone (One and Two), where applicable. Statement G, Page
21 4 of 4, details Eastern Shore's test period transportation billing determinants. Test

1 period billing determinants are also categorized as demand/reservation and
2 commodity and are further detailed by rate schedule (FT, ST, T-1) and rate zone
3 (One and Two), where applicable. Schedule G-1 sets forth the base period billing
4 determinants, billing rates and resulting transportation revenues, by month, by
5 customer, by rate schedule and rate zone. Schedule G-2 shows the test period billing
6 determinants, billing rates and resulting transportation revenues in the same format
7 as Schedule G-1.

8 **Q. Would you please explain Schedules G-3 through G-6?**

9 A. Schedule G-3 summarizes the proposed adjustments to the base period actual billing
10 determinants. The proposed adjustments reflect (1) an increase of 352,600 dts of
11 demand/reservation billing determinants over the base period based on annualizing
12 the demand/reservation billing determinants of the FT, ST and T-1 transportation
13 contracts in effect at March 31, 2007; (2) an increase of 1,649,107 dts of commodity
14 throughput over the base period commodity throughput under Rate Schedules FT
15 and ST; (3) the elimination of actual base period Rate Schedule IT throughput; and
16 (4) an increase of 10,231 dts of commodity throughput over the base period
17 commodity throughput under Rate Schedule T-1. I will discuss the reason for
18 making the IT elimination adjustment later in my testimony.

19 **Q. Please continue.**

1 A. Eastern Shore has not adjusted for any “at-risk” revenue, thus making Schedule G-4
2 not applicable. Schedule G-5 specifies “Other Revenues,” and G-6 is also not
3 applicable, because Eastern Shore has recorded no “Miscellaneous Revenue”.

4 **Q. Please explain Statement H-1.**

5 A. Statement H-1 and its supporting schedules are sponsored by Eastern Shore witness
6 Amanda Chi (ES-3).

7 **Q. Please explain Statement H-2.**

8 A. Statement H-2 shows depreciation expense, as included on Statement A. The
9 depreciation rates utilized are the same as those agreed to and used in Eastern
10 Shore’s prior rate proceeding in Docket No. RP02-34-000, and are shown in
11 Appendix A, Schedule 4 of the Stipulation & Agreement approved in that
12 proceeding. These depreciation rates were applied to the March 31, 2007 depreciable
13 gas plant in-service balances to derive the annual depreciation expense included in
14 Eastern Shore’s cost of service. The test period depreciation expense will be adjusted
15 as actual information becomes available through the end of the test period.

16 **Q. Please explain Statement H-3.**

17 A. Statement H-3 is sponsored by Eastern Shore witness Joseph D. Steinmetz (ES-4).

18 **Q. Please explain Statement H-4.**

19 A. Statement H-4 is sponsored by Eastern Shore witness Amanda Chi (ES-3).

20 **Q. Please explain Statements I and J.**

1 A. With respect to Statements I and J, I would like to make two general comments.
2
3 First, Eastern Shore performs only a transmission function; consequently there are no
4 storage function or gathering function costs included in Eastern Shore's cost of
5 service. Second, Eastern Shore's proposed transportation rates continue to reflect a
6 straight fixed-variable ("SFV") cost classification and rate design methodology,
7 consistent with the Commission's policy for open access pipelines. Under SFV, all
8 fixed costs are classified 100 percent to the demand/reservation component of
9 transportation rates and all variable costs are classified to the commodity component
10 of transportation rates.

10 **Q. Is Eastern Shore proposing any change to the existing rate zones or its cost**
11 **classification, cost allocation, and rate design methodology underlying its**
12 **currently effective rates?**

13 A. No. Eastern Shore proposes the continued use of its existing two rate zones and the
14 same cost classification, cost allocation, and rate design methodology as was agreed
15 upon in its prior rate case in Docket No. RP02-34-000. Furthermore, pursuant to
16 Article XI of the Stipulation & Agreement approved in that proceeding, Eastern
17 Shore has retained the same zone rate differentials between the rate zones.

18 **Q. Please explain Schedule I-1.**

19 A. As stated above, Eastern Shore has only transmission facilities and its overall test
20 period cost of service is functionalized accordingly.

21 **Q. Please explain Schedules I-1 (A), I-1 (B) and I-1 (C).**

1 A. As stated above Eastern Shore only has a transmission function. Schedule I-1 (a),
2 therefore, references Schedule I-1. Schedules I-1 (b) and (c) are included to comply
3 with the Commission's regulations. Eastern Shore does not have incremental
4 facilities nor does it maintain records of costs by zones.

5 **Q. Please explain Schedule I-2.**

6 A. This schedule shows the classification of the test period cost of service between fixed
7 and variable costs which are, in turn, categorized between demand/reservation and
8 commodity. This schedule reflects the application of SFV principles to the costs that
9 make up Eastern Shore's cost of service. All fixed costs are classified 100 percent to
10 the demand/reservation component of rates. All variable costs, consisting of the
11 materials and other components of Account Nos. 853 and 864, respectively, are
12 classified to the commodity component of rates.

13 **Q. Please explain Schedule I-3.**

14 A. Schedule I-3 provides a brief narrative explanation with respect to the allocation of
15 cost of service on Eastern Shore's system.

16 **Q. Please explain Schedule I-4.**

17 A. Schedule I-4 is not applicable because Eastern Shore does not have any Transmission
18 and Compression of Gas by Others.

19 **Q. Please explain Schedule I-5.**

20 A. Schedule I-5 summarizes Eastern Shore's actual transportation receipts and
21 deliveries for the base period and as adjusted for the test period. The test period

1 receipts and deliveries have been adjusted to reflect estimated throughput for the test
2 period and also reflect the elimination of Rate Schedule IT deliveries during the base
3 period.

4 **Q. Why have you eliminated IT deliveries from your test period?**

5 A. Eastern Shore has included an IT Cost of Service Credit of \$250,000 in its test period
6 cost of service. Such amount was agreed to in Eastern Shore's prior rate proceeding
7 and is reflected on Statement A. Such credit, which reduces the proposed firm
8 transportation rates, is in addition to the proposed continuation of the current IT
9 Revenue Sharing tariff provision which requires Eastern Shore to credit 90% of its
10 net interruptible revenues in excess of \$250,000 to its firm transportation customers
11 through an annual refund. It is, therefore, appropriate to exclude IT deliveries from
12 the test period.

13 **Q. Please explain Statement J.**

14 A. Statement J, Page 1 of 2, shows a comparison of the estimated firm transportation
15 revenues by rate schedule (Statement G, Page 2 of 4 and Schedule G-2) against
16 Eastern Shore's test period cost of service as reflected in Schedule I-2. As shown
17 thereon, Eastern Shore's proposed firm total operating revenues equal \$26,019,906
18 as compared against a total proposed cost of service of \$26,019,906. Statement J,
19 Page 2 of 2, shows a summary of Eastern Shore's estimated firm transportation
20 revenues, computed utilizing test period billing determinants as applied to Eastern
21 Shore's proposed firm transportation rates and its current firm transportation rates,

1 respectively. As shown there, Eastern Shore's proposed firm transportation rates
2 generate an annualized increase of \$5,589,048 in total operating revenue.

3 **Q. What is shown on Schedule J-1?**

4 A. Schedule J-1 is a summary of the test period billing determinants used to derive rates
5 for Eastern Shore's firm transportation service under Rate Schedules FT, ST and T-1,
6 respectively. The billing determinants shown are taken from Schedule G-2.

7 **Q. Please explain Schedule J-2.**

8 A. Schedule J-2, Page 1 of 2, details the rate derivation formula utilized to determine
9 Eastern Shore's proposed Reservation Rates for Rate Schedules FT, ST and T-1,
10 respectively. The formula incorporates the existing reservation rate zone differential,
11 the test period reservation billing determinants, and the test period cost of service
12 classified as reservation. Schedule J-2, Page 2 of 2, details the rate derivation
13 formula utilized to determine Eastern Shore's proposed Commodity Rates for Rate
14 Schedules FT, ST and T-1, respectively. This formula incorporates the existing
15 commodity rate zone differential, the test period commodity billing determinants,
16 and the test period cost of service classified as commodity.

17 **Q. How are Eastern Shore's rate schedule IT rates determined?**

18 A. Consistent with Commission policy and precedent, Eastern Shore has designed
19 interruptible rates equal to the 100 percent load factor rates of the firm FT Zone 1
20 and FT Zone 2 rates, respectively. As shown on Statement J, the Rate Zone 1 IT rate
21 of \$0.3931 is the 100% load factor rate of the firm Rate Zone 1 FT rate, and the Rate

1 Zone 2 IT rate of \$0.6734 is the 100% load factor rate of the firm Rate Zone 2 FT
2 rate.

3 **Q. Does this conclude your testimony?**

4 A. Yes.

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BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Eastern Shore Natural Gas Company) Docket No. RP07-____-000

AFFIDAVIT OF RONALD A. CRAIG

Ronal A. Craig, being duly sworn according to law, on oath
deposes and says: that he is the witness whose testimony appears on the
preceding pages entitled “PREPARED DIRECT TESTIMONY OF RONALD A.
CRAIG” in this proceeding; that, if asked the questions which appear in
the text of the aforesaid testimony, affiant would give the answers that are therein
set forth; and that affiant adopts the aforesaid testimony as his sworn testimony
in these proceedings.

Ronald A. Craig

Subscribed and sworn to before me this _____ day of October, 2006.

Notary Public