Docket No. RP07-_______
Black Marlin Pipeline Company
Notice of Rate Change

STATEMENT P
ROBERT W. NEUSTAEDTER

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Black Marlin Pipeline Company) Docket No. RP07-_-000

PREPARED DIRECT TESTIMONY OF ROBERT W. NEUSTAEDTER

Q. Please state your name and business address.

A. Robert W. Neustaedter, 808 Travis Street, Suite 1107, Houston, Texas 77002.

QUALIFICATIONS

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

A. I am employed by Pace Global Energy Services, LLC ("Pace Global") as Project Manager. Pace Global is an international energy consulting company with its corporate headquarters located in Fairfax, Virginia. Pace Global has over 25 years experience providing energy consulting services to natural gas companies, electric utilities, independent power producers, financial institutions and industrial customers engaged in businesses in the energy sector. Pace Global has been specifically engaged to assist Black Marlin in the preparation of this rate case.

Q. Would you briefly describe your educational background and work experience?

A. In 1978 I graduated cum laude from Texas A&M University with a BBA degree in Finance. That same year I began my career with Tennessee Gas Pipeline Company ("Tennessee") as an analyst in its rate department. Between 1978 and

1993 I held various positions within the rate department with increasing levels of responsibility including Manager of Rates. In that position I was responsible for all rate, tariff and certificate matters for Tennessee including the preparation of major rate case filings for Tennessee and its FERC-regulated pipeline affiliates. In 1994 I became Manager of Strategy Development for Tennessee, with responsibilities for coordinating the development of the company's 5-year strategic plans; providing economic analyses of pipeline capital projects; and supporting the analysis and recovery of Tennessee's take-or-pay costs. In 1997 I joined Reliant Energy, now CenterPoint Energy ("CenterPoint"), as Manager of Regulatory and Policy Development. At CenterPoint I was responsible for supporting the company's retail marketing efforts and strategies and coordinated the consistent implementation of corporate regulatory and business policies across Center Point's strategic business units. In 1998 I joined Enron Corp. as Manager of Regulatory and Government Affairs where I managed the regulatory and government affairs activity for Enron's international and domestic business units, including Enron LNG. I supported the company's business origination efforts by performing regulatory due diligence and risk management activities and promoted wholesale and retail market opportunities through analysis of existing utility tariffs and regulations. In addition, I supported the company's international efforts, providing regulatory due diligence of the rules and regulations governing the energy sector in countries where Enron had business interests.

Q. Please go on.

A. After Enron's financial collapse in December 2001, I took the position of Project Manager, Regulatory Affairs for Panhandle Energy ("Panhandle"). In this capacity, I managed the regulatory affairs for Panhandle Energy pipeline companies, including Trunkline LNG. I directed the preparation and filing of all pipeline fuel rate applications with the FERC, performed cost and revenue studies and provided financial forecasts. In addition, I ensured compliance with FERC regulations and tariff requirements and monitored and analyzed the impact of FERC orders, industry initiatives and competitor filings. In November 2005 I assumed my current position with Pace Global in its Houston office with responsibilities for supporting the company's service offerings in the natural gas regulatory arena for pipeline, storage and local distribution companies.

Q. Is there anything else you wish to add?

A. Yes. I have been a guest lecturer at the American Gas Association sponsored rate schools at the universities of Wisconsin and Maryland where I taught fundamental and advanced pipeline cost allocation and rate design concepts and have been a past and current member of the Southern Gas Association Rate Committee.

Q. Have you previously testified in regulatory proceedings before this Commission?

A. Yes I have. I have presented testimony in various rate proceedings before the FERC for Tennessee Gas Pipeline and Midwestern Gas Transmission. In addition, I have testified before the Canadian National Energy Board and the California Public Utility Commission related to cases involving Tennessee Gas Pipeline.

EXHIBITS SPONSORED

Q. Would you please describe your responsibilities in this case?

A. I am responsible for development of the statements and schedules which support Black Marlin's Overall Cost of Service, including schedules developing Operation and Maintenance Expenses, Rate Base and Return, Depreciation, the creation and allowance for the amortization of Regulatory Assets, Income Taxes and Other Taxes, and the derivation of its rates for T-1, FTS and ITS services. In addition, as Black Marlin Witness Brennan discusses in his testimony, in the event the Commission does not grant Black Marlin's request for nominal suspension of its proposed rate increase, Black Marlin, in the alternative, is requesting that the Commission allow a portion of its proposed rate increase to be implemented December 1, 2006, with the full increase to be implemented May 1, 2007 after the full statutory 5-month suspension. My testimony will also support the derivation of the partial rate increase to be effective December 1, 2006.

Q. Please identify the Exhibits you are sponsoring.

A. I am sponsoring the following exhibits:

Exhibit No. BMP-20	Statement A
Exhibit No. BMP-21	Statement B
Exhibit No. BMP-22	Statement F-1 and F-2
Exhibit No. BMP-23	Statement C and Schedule C-1
Exhibit No. BMP-24	Statement D and supporting working papers
Exhibit No. BMP -25	Schedules B-1 and H(3)-2

Exhibit No. BMP-26	Schedule B-2
Exhibit No. BMP-27	Schedule E-2
Exhibit No. BMP-28	Statements H-1, H-2, H-3 and H-4
Exhibit No. BMP-29	Statement I and Schedules I-1, I-2 and I-3
Exhibit No. BMP-30	Statement J and Schedules J-1, J-1(a) and J-2
Exhibit No. BMP-31	Houston Ship Channel Project Estimates
Exhibit No. BMP-32	1998 and 1999 FERC Form 2-A Annual Report, Page 219
Exhibit No. BMP-33	Fifteenth Revised Sheet No. 4
Exhibit No. BMP-34	"Out-of-Pocket" Costs
Exhibit No. BMP-35	Classification of "Out of Pocket" Costs
Exhibit No. BMP-36	Partial Rate Derivation
Exhibit No. BMP-37	Alternate Fifteenth Revised Sheet No. 4

Q. Were the Statements and Schedules contained in the above-referenced exhibits prepared by you or under your supervision?

A. Yes, they were.

COST OF SERVICE

Q. Please explain Exhibit No. BMP-20.

A. This exhibit, which is also Statement A of the filing, shows Black Marlin's Total Cost of Service for the twelve months ended June 30, 2006 ("Base Period"), as adjusted for known and measurable changes for the nine months ending March 31, 2007 ("Test Period") and reduced by Other Revenues resulting in the Net Cost of Service of $2,966,836. The Net Cost of Service consists of Operation and

Maintenance Expenses; Depreciation and Amortization Expense; Income and Other Taxes; an allowance for Regulatory Asset Amortization; Return on the Test Period Rate Base; and Credits to the Total Cost of Service.

Q. Will you now please explain Exhibit No. BMP-21?

A. This exhibit, which is also Statement B of the filing, is a summary of the Test Period Rate Base and reflects the annual Return on that Rate Base computed at 13.80 percent. The Test Period Rate Base includes Gas Plant in Service, a deduction for the Accumulated Provision for Depreciation and Amortization of Gas Utility Plant and Accumulated Deferred Income Taxes, and an allowance for working capital. In addition, and explained later in my testimony, Black Marlin is including in Rate Base the deferral of certain operation and maintenance costs as a Regulatory Asset. Such costs are related to pigging operations performed during the Base Period and associated costs expected to be incurred by Black Marlin prior to the end of its Test Period.

Q. Please explain Exhibit No. BMP-22, which includes Statements F-1 and F-2 of the filing.

A. Statement F-1 is a description of the percentage rate of return being claimed and the general reasons therefor. Statement F-2 shows the capitalization being used and the overall rate of return claimed. Black Marlin Witness Olson, in his testimony, supports the capital structure being used, as well as the cost of equity being claimed by Black Marlin which is used to calculate its overall rate of return of 13.8 percent.

Q. Please explain Exhibit No. BMP-23 , which reflects Statement C and Schedule C-1 of the filing.

A. Statement C summarizes the beginning and ending balances and the changes in the plant accounts during the twelve months ended June 30, 2006 and the adjustments to plant accounts expected during the Test Period.

Q. Column D of Statement C shows $598,837 of plant additions during the Base Period. Please explain what these additions relate to.

A. The $598,837 of plant additions relate to costs incurred by Black Marlin to modify its system to accommodate "smart" pigging operations performed during the Base Period as referenced above.

Q. Is Black Marlin proposing any adjustments to Gas Plant in Service?

A. Yes. Black Marlin is proposing to reduce Gas Plant in Service by $2,222,000, which represents the acquisition premium paid by a previous owner, previously booked to Account 114, which was included in Account 101 upon sale of Black Marlin to Williams Field Services.

Q. Please continue.

A. In March 1999, the Blue Dolphin group acquired Black Marlin from Enron Corp. See 93 FERC ¶61,188 (Nov. 21, 2000). Related to that transaction, the Blue Dolphin group recorded $2,222,000 as an acquisition premium in Account 114, representing the amount paid over original net book value. The acquisition premium was to be amortized over 15 years with the amortization amount booked below the line to Account 425. In January 2001, Williams Field Services

("WFS") acquired Black Marlin from the Blue Dolphin group. Reconciliation of Black Marlin's historical FERC Form 2-A Annual Reports and Accounting Exhibit S to the certificate application, filed on September 17, 2001, in Docket No. CP01-442, concerning the WFS acquisition, reveals that at that point in time the Blue Dolphin acquisition premium, less the accumulated amortization of the acquisition premium, was incorrectly included as a part of Net Plant.

Q. Was WFS aware at that time that Blue Dolphin's acquisition premium was included in Gas Plant in Service?

A. No it was not. As consistently reported in Black Marlin's FERC Form 2-A Reports filed since the acquisition by WFS, the accounting records available to WFS from that time were very limited. In addition, the FERC Form 2-A Reports filed by the Blue Dolphin group for the years 1999 and 2000 (the period in which the Blue Dolphin group had ownership of Black Marlin) and which identified the original and proper accounting of the Blue Dolphin group acquisition premium, were not filed until June 21, 2001, six months after WFS acquired Black Marlin. Furthermore, WFS relied on the Blue Dolphin group's Net Plant representation as provided by them for inclusion in the Accounting Exhibit S to the certificate filing in Docket No. CP01-442, which now has been found to include Blue Dolphin's acquisition premium.

Q. What is FERC's policy with respect to the inclusion of acquisition premiums in pipeline rate determinations?

A. FERC's policy, as a general rule, is to allow utilities to recover in rates only the cost to the first person devoting property to public service net of any previously accumulated provision for depreciation. This is otherwise known as the "original cost concept". Utilities are required to separately recognize in Account 114 any amounts paid for utility property above the original, depreciated cost. Generally, amounts recorded to Account 114 are amortized below the line to Account 425. Both accounts 114 and 425 are typically excluded from rates. However, the Commission has allowed exceptions to the rule when the purchaser can demonstrate specific dollar benefits resulting directly from the sale. Black Marlin is not proposing to include such costs in its rate base at this time.

Q. Please explain Schedule C-1.

A. Schedule C-l shows Black Marlin's individual plant cost balances at June 30, 2006, projected plant adjustments and the resulting Test Period balances. Column (D) of Schedule C-1 shows the $2,222,000 reduction to Gas Plant in Service allocated pro-rata among the various transmission accounts (corresponding to the same $2,222,000 increase that was allocated pro-rata among the respective transmission sub-accounts).

Q. Will you now refer to Exhibit No. BMP-24, which is Statement D and the working papers supporting Statement D of the filing?

A. Statement D summarizes the beginning and ending balances and changes in the accumulated provisions for depreciation and amortization accounts for the twelve months ended June 30, 2006. The adjoining columns reflect the projected changes for the Test Period. The resulting projected balance at the end of the Test Period of $23,466,811 as shown on Line 7, Column (I) has been carried forward to Statement B, Line 2.

Q. What does Statement D (Working Papers) Page 1 of 2 show?

A. Statement D (Working Papers) Page 1 of 2 shows in more detail the Test Period adjustments to the Accumulated Provision for Depreciation and Amortization ("Depreciation Reserve") reflected in Columns (G) and (H) of Statement D.

Q. Please explain the adjustments reflected in Statement D (Working Papers) Page 1 of 2.

A. Adjustment No. 1, as reflected in Column (B), shows the adjustment to the Depreciation Reserve for nine months additional depreciation expense and Negative Salvage allowance from June 30, 2006 to the end of the Test Period based upon the depreciable plant balance as of June 30, 2006 and using the FERC- approved book depreciation and negative salvage rates.

Q. Please explain Adjustment No. 2 as reflected in Columns (C) through (G).

A. Adjustment No. 2 addresses various adjustments to the depreciation reserve covering prior periods to properly restate the Depreciation Reserve as of June 30, 2006.

Q. Please explain the adjustment reflected in Column (C).

A. Column (C) shows the adjustment to the Depreciation Reserve to reflect the proper recording of depreciation expense and negative salvage credited to the Depreciation Reserve for the period January 1, 2001 through June 30, 2006.

Q. Please elaborate.

A. Depreciation expense for the period January 1, 2001 through June 30, 2006, and credited to the Depreciation Reserve, was incorrectly calculated using a depreciation rate of 2.42 percent. Black Marlin's rate settlement approved in Docket No. RP98-274 (Black Marlin's last rate case) by Commission order dated December 30, 1998, established the depreciation rate for Transmission Plant, effective January 1, 1999, as 2.40 percent plus an allowance for Negative Salvage of .25 percent for a total depreciation rate of 2.65 percent. The adjustment in Column (C) reflects the additional depreciation expense and negative salvage that should have been taken and credited to the Depreciation Reserve equal to the difference between the approved 2.65 percent and the 2.42 percent depreciation rate erroneously booked.

Q. Please explain the adjustment reflected in Column (D).

A. As described previously, the accumulated amortization associated with the Blue Dolphin acquisition premium originally booked to Account 425 was incorrectly booked to Account 108, Depreciation Reserve. Just as Gas Plant in Service is being reduced by the $2,222,000, so should the previously accumulated amortization associated with the $2,222,000 be reversed out of the Depreciation Reserve.

Q. How was the $271,568 "Prior Acquisition Premium Amortization" amount as reflected in Column (D), Line 1 determined?

A. The Blue Dolphin $2,222,000 acquisition premium originally was being amortized over 15 years resulting in an annual amortization amount equal to $148,133 or $12,344 per month. Blue Dolphin amortized the acquisition premium for 22 months (March 1, 1999 through December 31, 2000) before selling Black Marlin to WFS, resulting in an accumulated amortization reserve amount of $271,568.

Q. Please describe the $323,857 "Prior Acquisition Premium Depreciation" adjustment reflected in Column (E).

A. Upon classification of the Blue Dolphin acquisition premium as Gas Plant in Service, starting in January 2001 and continuing through June 30, 2006, depreciation expense was taken on the $2,222,000 using the 2.42% depreciation rate and booked to the Depreciation Reserve. As part of the adjustment to reverse out the effect of the $2,222,000, any depreciation expense booked to Account 108, Depreciation Reserve should be reversed out as well.

Q. How was the $323,857 adjustment reflected in Column (E) determined?

A. Depreciation expense credited to the Depreciation Reserve associated with the $2,222,000 for the period January 1, 2001 through June 30, 2006 was calculated as follows: $2,222,000 x 2.65% x 5.5 years = $323,857.

Q. If depreciation expense was originally booked at 2.42 percent on the $2,222,000 acquisition premium, why did you reverse it using a depreciation rate of 2.65 percent?

A. The adjustment reflected in Column (C), correcting for the difference between the 2.42 percent and 2.65 percent depreciation rates, included the $2,222,000 acquisition premium, thereby restating the depreciation reserve at the 2.65 percent basis. Therefore, the adjustment to reduce the reserve associated with the $2,222,000 acquisition premium should be calculated using the 2.65 percent rate.

Q. Please explain the "Removal Costs" adjustment shown Column (F) in the amount of $1,851,076.

A. In 1998-1999, as a result of the widening and deepening of the Houston Ship Channel as proposed by the Federal government, Black Marlin replaced its existing 16" line that crossed the channel, burying the new line at a deeper depth. The project involved digging up and removing the original line. Preliminary cost estimates for removal were estimated at approximately $.9 million as shown in Exhibit No. BMP-31. It appears the actual cost of removal for the old line totaled almost $1.1 million, which is reflected as the sum of the amounts recorded as cost of removal in the FERC Form 2-A Annual Reports for 1998 and 1999, as set forth in Exhibit No. BMP-32. However, upon careful review of Black Marlin's FERC Form 2-A Annual Report for 1999 (prepared by its previous owners - the "Blue Dolphin group"), I found that a *credit* in the amount of $925,538 was made to the Depreciation Reserve for removal costs associated with the Houston Ship Channel facilities. Proper accounting for removal costs entails *debiting* the Depreciation Reserve, as correctly recorded for removal costs incurred in 1998 and shown in the 1998 FERC Form 2-A Annual Report (prepared by Enron Corp. - the owners of Black Marlin at that time), as excerpted in Exhibit No. BMP-32. Reversing the mistaken credit entry and properly debiting the Depreciation Reserve for removal costs results in a correcting entry of $1,851,076.

Q. Please describe the adjustment for "Negative Salvage" shown in Column (G).

A. The "Negative Salvage" adjustment reclassifies $934,240 of the Depreciation Reserve to a sub-account specifically related to Negative Salvage. The allowance for Negative Salvage and the reserve for depreciation for Offshore Transmission plant are currently accounted for in one account.

Q. Is Black Marlin required to separately account for Negative Salvage?

A. Yes. Section 154.312(d) of the Commission's Regulations states that "any authorized negative salvage must be maintained in a separate sub-account of account 108."

Q. Why hasn't Black Marlin maintained a sub-account of the Depreciation Reserve to account for Negative Salvage?

A. Again, when WFS acquired Black Marlin from Blue Dolphin, there were very limited accounting and property records that were available. The plant property accounting information that was available did not reflect a separate sub-account for Negative Salvage.

Q. What is the basis of your adjustment to the Depreciation Reserve to establish a separate sub-account for Negative Salvage?

A. As shown on Statement D (Working Papers) Page 2 of 2, I started with a beginning balance for Negative Salvage as of October 31, 1992 in the amount of $151,239 as reflected in Black Marlin's rate case filing in Docket No. RP93-70.

Q. Why did you begin there?

A. The rate case filing in Docket No. RP93-70 was the only document I found that separately stated a balance for Black Marlin's Negative Salvage reserve.

Q. Why did you use the balance at October 31, 1992?

A. The rate case filing in Docket No. RP93-70 utilized a twelve-month Base Period ending October 31, 1992 with a Test Period ending July 31, 1993. I used the balance at October 31, 1992 because it represented an actual book balance.

Q. Didn't Black Marlin file a rate case more recent than the filing in Docket No. RP93-70 that you could have utilized?

A. Although Black Marlin filed a subsequent rate case on June 30, 1998 in Docket No. RP98-274, the Depreciation Reserve as reflected in that filing did not separately identify a sub-account related to Negative Salvage.

Q. Please continue with your explanation.

A. As I mentioned, I started with a known balance for Negative Salvage as of October 31, 1992. For the period November 1, 1992 through December 31, 1996 I calculated an allowance for Negative Salvage by multiplying the approved .25 percent Negative Salvage rate by the Offshore Transmission depreciable plant balance as of the end of October 31, 1992 (the Base Period as reflected in Docket No. RP93-70) - again, so as to utilize an actual, unadjusted plant balance.

Q. Why did you use the Offshore Transmission Plant balance from the RP93-70 rate case to calculate an allowance for Negative Salvage for the period November 1, 1992 through December 31, 1996?

A. I did not have available to me the actual offshore transmission plant balances for that time period. In addition, the plant balances in Black Marlin's FERC Form 2-A Annual Reports during that time period included certain onshore facilities that were subsequently sold, so I could not use FERC Form 2-A Annual Reports as a source.

Q. Could there have been additions and retirements to plant during that time period that would have affected the amount of Negative Salvage claimed?

A. Yes. However, because Offshore Plant only increased $432,456 between October 31, 1992 and December 31, 1996, any impact would be negligible. Even if the $432,456 increase in plant balances occurred in November 1992, the impact for the entire period would be less than $6,000. Based upon that result, the end result was reasonable.

Q. Please continue.

A. For the period 1997 through 2000 I calculated the allowance for Negative Salvage by multiplying the Negative Salvage rate by the average of the beginning and ending Transmission Plant balances as reflected in Black Marlin's FERC Form 2-A. For the period January 1, 2001 through June 30, 2006 I calculated the allowance for Negative Salvage based upon the actual balances for Offshore

Transmission Plant reflected on Black Marlin's books, exclusive of the $2,222,000 Blue Dolphin acquisition adjustment previously discussed.

Q. Does the "reclassification" of Transmission Plant Depreciation Reserve dollars to Negative Salvage affect Black Marlin's overall depreciation reserve used in the calculation of Rate Base?

A. No, it does not. The allowance for Negative Salvage is a component of the overall Depreciation Reserve which is subtracted from Gas Plant in Service to arrive at Net Plant for Rate Base purposes. The overall impact of the adjustment is simply to properly classify amounts recorded in the Depreciation Reserve between Negative Salvage and Transmission Plant.

Q. Please explain Exhibit BMP-25, which consists of Statement B-1 and H-3(2) of the filing.

A. Statement B-1 shows Accumulated Deferred Income taxes which are an adjustment to rate base.

Q. Why are there no monthly entries or balances associated with deferred taxes prior to June 30, 2006?

A. Beginning in 2004, the sum of the balances in Black Marlin's Accounts 190 and 282 resulted in an overall deferred tax asset on its books. However, because of Black Marlin's tax net operating loss history, it was determined that the potential for realization of the Property, Plant and Equipment deferred tax asset was less than 50 percent. In accordance with Financial Accounting Standards 109 paragraph 27, a valuation allowance was established beginning in 2004, offsetting the full amount of the deferred income tax liability. With this rate case, Black Marlin is anticipating sufficient levels of taxable income that will, in effect, reverse the valuation allowance going forward.

Q. How was the deferred tax balance in Account 282 determined?

A. As shown in Schedule H-3(2), Black Marlin's Account 282 balance was determined by the reconciliation of Black Marlin's book and tax net plant balances as of June 30, 2006, resulting in a difference of net book plant over net tax plant of $28,847. Applying Black Marlin's effective tax rate to this difference generated a deferred tax liability balance of $10,096. The $10,096 balance was included as a reduction to Rate Base.

Q. Will you now turn to Exhibit BMP-26 , which is Schedule B-2 of the filing?

A. Schedule B-2 shows Regulatory Assets and Liabilities that are included in Rate Base.

Q. What costs are Black Marlin including as a Regulatory Asset?

A. As mentioned previously, Black Marlin conducted pigging operations on its system in late 2005. Certain modifications of the Black Marlin system were required in order to accommodate the pig. As reflected in Statement C, these costs were capitalized as Gas Plant in Service. As part of the pigging operation, Black Marlin additionally incurred operating and maintenance costs totaling $320,148 and, as a result of the analysis of the pigging operations identifying various anomalies requiring attention, will incur an additional $174,050. Typically, these costs would be expensed. However, the sum of the costs either incurred or projected to be incurred, totaling $494,198 represents almost 26 percent of the Test Period total operation and maintenance expense. Because these costs are unique to the start-up of this new pigging program, yet have value to Black Marlin and its shippers over the long term, Black Marlin is proposing to defer these costs through the creation of a regulatory asset to be amortized over a five-year period.

Q. Please explain Exhibit No. BMP-27, which is Schedule E-2 of the filing.

A. Schedule E-2 shows Working Capital claimed in Rate Base. Black Marlin has reflected as a Test Period adjustment an amount equal to $342,545 for Working Capital. This amount reflects the projected unamortized balance of a December 1, 2006 10-year lease pre-payment as of the end of the Test Period for the use of right-of-way through Texas state waters. Black Marlin's payment will be booked as a pre-payment in Account 165 - Prepayments Other. As the pre-payment is amortized it will be charged to Account 860 Operating Expense.

Q. Please turn to Exhibit No. BMP-28, which contain Statements H-1, H-2, H-3 and H-4 of the filing.

A. Statement H-1 shows Operation and Maintenance Expenses by FERC account by month, for the twelve months ended June 30, 2006, with the totals for the Base Period for each account shown in Column (O). The adjoining Columns (P) and (Q) show the adjustments and resulting Test Period Operation and Maintenance Expenses included in Black Marlin's Test Period Cost of Service. Total Test

Period Operation and Maintenance Expenses for Black Marlin of $1,904,110 shown on Line 45 have been summarized on Statement A, Lines 1 through 6.

Q. Do these Operation and Maintenance Expenses include costs assigned and allocated to it from entities other than Black Marlin?

A. Yes. Black Marlin's pipeline facilities are operated and maintained by Transcontinental Pipeline Company, an affiliate of Black Marlin. Administrative and staff functions are performed by various other affiliates on behalf of Black Marlin. The costs associated with these services have been charged to Black Marlin and included in Operation and Maintenance Expenses.

Q. What procedures are utilized by these entities to charge Black Marlin for the cost of the services?

A. Whenever possible, costs are directly assigned. When direct assignment is not possible, costs are allocated utilizing various bases including measurable benefits, dedicated resources and the Modified Massachusetts Formula.

Q. Please explain Parts A through G of Statement H-1.

A. Part A of Statement H-l summarizes the adjustments made to Black Marlin's Operation and Maintenance Expenses. A narrative explanation for each adjustment and support for the adjustment is contained in Parts B through G.

Q. Would you briefly explain each of the adjustments shown on Statement H-1, Part A?

A. Adjustment No. 1, a credit of $28,281, eliminates Black Marlin's Base Period Annual Charge Adjustment ("ACA") expenses. These expenses are collected through a separate surcharge pursuant to Section 18 of the General Terms and Conditions of Black Marlin's FERC Gas Tariff, First Revised Volume No. 1.

Q. Please explain Adjustment No. 2

A. Adjustment No. 2, a credit of $320,148, eliminates operation and maintenance costs incurred during the Base Period associated with the pigging of its system in 2005. As mentioned previously in my testimony, Black Marlin is proposing to defer these costs as a Regulatory Asset includable in Rate Base and amortized over five years.

Q. Please explain Adjustment No. 3.

A. Adjustment No. 3, in the amount of $290,155, adjusts the level of Black Marlin's corporate overhead costs allocable to Black Marlin from The Williams Companies and from Williams Energy LLC which are booked into Accounts 920 and 930.2. Such corporate overhead costs are allocated based upon the Modified Massachusetts Formula. The Williams Companies overhead costs are first allocated to Williams Energy LLC. Then Williams Energy LLC flows-through The Williams Companies overhead costs, along with its own corporate overhead costs, to Black Marlin (as well as the other business units under Williams Energy LLC) based upon the Modified Massachusetts Formula.

Q. Why are Accounts 920 and 930.2 understated in the Base Period?

A. For two reasons. One, due to an accounting oversight, corporate overheads attributable to Williams Energy LLC and allocable to Black Marlin were not charged to Black Marlin for 2005. Consequently, Accounts 920 and 930.2 are understated for the period July 2005 through December 2005. Secondly, Williams Energy LLC did not reflect any flow-through of The Williams Companies nor an allocation of its own corporate overhead costs for the period January through June, 2006. Therefore, an adjusting entry is necessary to reflect the proper accounting for these costs. Black Marlin is showing an adjustment to the Base Period for Account 920 in the amount of $93,569 and to Account 930.2 in the amount of $196,586 for a total adjustment related to corporate overhead costs in the amount $290,155.

Q. Is Black Marlin proposing to increase corporate overhead costs over Base Period levels?

A. No. The purpose of the adjustments described above is only intended to reflect the proper level of costs that should have been booked in the Base Period for allocable corporate overhead costs chargeable to Black Marlin.

Q. Please explain Adjustment No. 4.

A. Adjustment No. 4 in the amount of $35,436, is to reflect the charging to expense the ten-year amortization of Black Marlin's pre-payment for the use of right-of-way as explained previously in my testimony.

Q. Please explain Adjustment No. 5.

A. Adjustment No. 5, in the amount of $56,154 is to adjust the level of Black Marlin's insurance premiums. Effective May 1, 2006, Black Marlin's property insurance increased to $109,452. The adjustment is the difference between the Base Period amount reflected in Account 924 and the $109,452.

Q. Please explain Adjustment No. 6.

A. Adjustment No. 6, in the amount of $433,333, reflects the three-year amortization of regulatory expenses projected to be incurred in this case assuming its full prosecution before an administrative law judge.

Q. Please turn to Statement H-2 in the filing.

A. Statement H-2 shows the computation of the Depreciation and Amortization Expense included in the Test Period Cost of Service. Columns (C) through (E) show the Gas Plant in Service balance at June 30, 2006, together with the adjustments and resulting Test Period balances, as previously set forth on Statement C. As shown in Columns (F) and (G), depreciation expense is computed at Black Marlin's per book transmission depreciation rate of 2.40 percent plus a negative salvage rate of 0.25 percent. These depreciation and negative salvage rates were approved and established by Commission order in Black Marlin's last rate case (Docket No. RP98-274). At this rate of depreciation, Black Marlin's test period net transmission plant of $1,734,680 (exclusive of negative salvage) will be fully depreciated in about three years.

Q. Did Black Marlin consider changing its existing FERC-approved Offshore Transmission and Negative Salvage rates?

A. No it did not. As stated above, Black Marlin's plant is almost completely depreciated. In addition, based upon the declines in throughput Black Marlin has experienced over the last several years and with little expectation of additional volumes being connected to its system, as discussed by Black Marlin Witness Dixon, Black Marlin sees no reason to adjust its depreciation rates.

Q. Please continue with your description of Statement H-2.

A. The depreciation rates in Column (G) are applied to the Test Period balances in Column (E) to compute the Test Period Depreciation and Amortization Expense reflected in Column (J). The adjustments shown in Column (I) are the differences between the Test Period Depreciation and Amortization Expense and Base Period Depreciation and Amortization Expense reflected in Column (H). The total Test Period Depreciation and Amortization Expense of $641,879 on Line 14 has been carried forward to Statement A, Line 7.

Q. Please explain the calculation of the Test Period Federal and State Income Taxes as shown in Statement H-3 of the filing.

A. Federal and State Income Taxes for the Test Period are computed on Statement H-3 on the basis of the 13.80 percent claimed rate of return reflected on Statement F-2. The computation of Income Taxes begins with the total amount of Return, Line 2, which is the product of the 13.80 percent claimed rate of return applied to the Test Period Rate Base on Line 1 and which equals the Return set forth on Statement A, Line 11. Because Black Marlin has no debt in its capital structure, there is no reduction to Total Return for interest expense. Because Black Marlin does not provide transportation service within the state of Texas, there are no state income taxes. Federal Income Taxes on Line 6 were calculated using the application of the statutory federal income tax rate of 35 percent to the Taxable

Return as shown on Line 4. The resulting product of $117,531 is carried forward to Statement A, Line 10.

Q. Please explain Statement H-4 of the filing.

A. Statement H-4 shows Other Taxes recorded for the twelve months ended June 30, 2006 in Column (B). The adjoining Columns (C) and (D) show that there are no adjustments to Base Period Other Taxes, resulting in Test Period Other Taxes of $112,425 shown on Line 7. This total has been carried forward to Statement A, Line 9.

Q. On line 13 of Exhibit No. BMP-20 (Statement A), Total Cost of Service is reduced by $126,220. What does the $126,220 represent?

A. The Revenue Credit amount of $126,220 represents Other Revenues collected by Black Marlin. Other Revenues, as discussed by Black Marlin Witness Dixon and reflected in Exhibit No. BMP-9, Line 254, are treated as a credit to the Total Cost of Service.

RATE DESIGN

Q. Would you turn now turn to Exhibit No. BMP-29?

A. Exhibit No. BMP-29 consists of Statement I and Schedules I-1, I-2 and I-3 of the filing.

Q. Would you please explain Statement I and Schedule I-1 in further detail?

A. Statement I, Explanatory Notes, summarize the procedures underlying the functionalization, classification, and allocation of the Net Cost of Service between services. Schedule I-1 explains that all of Black Marlin's facilities perform the same function which has historically been classified as Transmission.

Q. Please explain Schedule I-2.

A. Schedule I-2 shows the classification of the cost of service between fixed and variable costs and shows the assignment of fixed costs between the Reservation and Usage components using Straight Fixed-Variable ("SFV") principles of rate design. Under SFV all fixed costs are assigned to the Reservation component of the rate and all variable costs are assigned to the Usage component. Black Marlin has classified all its costs as fixed.

Q. Please explain Schedule I-3.

A. Schedule I-3 explains that Black Marlin does not directly allocate costs to rate schedules per se, but instead, derives rates based upon a system average cost.

Q. Please detail the schedules and statements contained in Exhibit No. BMP-30.

A. Exhibit No. BMP-30 consists of Statement J and Schedules J-1, J-1(a) and Schedule J-2 which support the derivation of rates.

Q. Please explain Statement J.

A. Statement J is a comparison, by rate schedule, of operating revenues as shown on Schedule G-2, supported by Witness Dixon, with the allocated cost of service as shown in Schedule I-2.

Q. Please explain Schedule J-1.

A. Schedule J-l is a summary of billing determinants used to derive transportation rates and which tie to customers' total billing determinants as shown on Schedule G-2.

Q. Please explain Schedule J-1(a).

A. Any discount adjustment to billing determinants are required to be shown in Schedule J-1(a).

Q. Has Black Marlin adjusted its billing determinants to take into account transportation discounts to any of its customers?

A. No, it has not. As explained by Black Marlin Witness Dixon, by the time the proposed rates go into effect, Black Marlin will have terminated all rate discounts.

Q. Please explain Schedule J-2.

A. Schedule J-2 reflects the derivation of rates for Rate Schedules T-1, FTS and ITS. The rates for service under Rate Schedules T-1, FTS and ITS are derived from the reservation and usage costs (as set forth on Schedule I-2, Line 66) and the design determinants (as shown on Schedule J-1, Line 4). As explained by Mr. Dixon, the only transportation service utilized, and projected to be utilized by shippers, is interruptible service under Black Marlin's Rate Schedule ITS. For rate design purposes, Black Marlin has imputed Reservation billing determinants assuming a 100 percent load factor. Because Black Marlin's Reservation rates are stated on a daily basis, the Reservation billing determinants are equal to the Usage billing determinants. These allocated costs and design determinants are used to develop the system average unit transportation rates as shown on Schedule J-2, Line 3.

Rates for Rate Schedules T-1 and FTS are directly derived from the system average unit transportation rate for Reservation and Usage. As shown on Line 6, the Rate Schedule ITS rate is designed on a 100 percent load factor basis of the Rate Schedule system average rate. The resultant Rate Schedule T-1, FTS and ITS rates are reflected on Fifteenth Revised Sheet No. 4, as contained in Exhibit No. BMP-33.

PARTIAL RATE INCREASE

Q. Please explain Exhibit No. BMP-34.

A. As discussed by Black Marlin Witness Brennan, Black Marlin is in dire financial condition. In the event Black Marlin's request for nominal suspension of its proposed rate increase is not granted, Black Marlin requests that the Commission allow a portion of its proposed rate increase to go into effect after 30 days notice and nominal suspension, subject to refund. The partial rate increase will allow Black Marlin an opportunity to recover its "out-of-pocket" costs. Exhibit No BMP-34 sets forth those costs Black Marlin considers as "out-of-pocket", which consists of its operation and maintenance expenses, administrative and general costs, and taxes other than income.

Q. Please explain Exhibit No. BMP-35.

A. Exhibit No. BMP-35 shows the costs reflected in Exhibit No. BMP-34 classified between fixed and variable, with 100 percent of the fixed costs assigned to the Reservation component and 100 percent of the variable costs assigned to the Usage Component, consistent with Straight Fixed-Variable rate design principles.

Q. What does Exhibit No. BMP-36 show?

A. Exhibit No. BMP-36 shows the calculation of rates for Rate Schedules T-1, FTS and ITS determined on the same basis as reflected in Schedule J-2, based upon the "out-of-pocket" costs reflected in Exhibit Nos. BMP-34 and BMP-35 and the Test Period billing determinants reflected in Exhibit No. BMP-7. The resultant Rate Schedule T-1, FTS and ITS rates are reflected on Alternate Fifteenth Revised Sheet No. 4, as contained in Exhibit No. BMP-37.

Q. Does this conclude your testimony?

A. Yes it does.

VERIFICATION

THE STATE OF VIRGINIA	)	
	)	SS
COUNTY OF FAIRFAX	)	

ROBERT W. NEUSTAEDTER, being first duly sworn, deposes and saith that he is the same ROBERT W. NEUSTAEDTER whose Prepared Direct Testimony accompanies this verification; that such testimony was prepared by him; that he is familiar with the contents thereof; that the facts set forth therein are true and correct to the best of his knowledge, information and belief; and that he does accept the same as his sworn testimony in this proceeding.

Robert W. Neustaedter

ROBERT W. NEUSTAEDTER

SUBSCRIBED and SWORN to before me this 26th day of October 2006.

(seal)

My commission expires: April 30, 2009

Notary Public

STATEMENT OF RATES

Currently Effective Rates
For Transportation of Natural Gas
Under Rate Schedules Contained in This
FERC Gas Tariff, First Revised Volume No. 1

(Rates - ¢ per MMBtu)

Rate Schedule	Section	Description	Currently Effective Rates
T-1	3	Reservation Fee	106.22
		Commodity Rate	0.00
		Authorized Over-Run Rate	106.22
FTS	3	Reservation Fee	
		Maximum	106.22
		Minimum	0.00
		Commodity Rate	
		Maximum	0.00
		Minimum	0.00
		Authorized Over-Run Rate	
		Maximum	106.22
		Minimum	0.00
ITS	3	Commodity Rate	
		Maximum	106.22
		Minimum	0.00
ACA	3	Annual Charge Adjustment	0.16

Docket No. RP07-_____
Statement P
Exhibit No. BMP-34

Black Marlin Pipeline Company
Partial Rate Increase
Out-of-Pocket Costs

Line No.	Description	Statement or Schedule	Amount
	(A)	(B)	(C)
	Operation and Maintenance Expenses	H-1	
1	Transmission		$ 716,666
2	Customer Accounts		-
3	Customer Service & Informational		-
4	Sales		-
5	Administrative & General		1,187,444
6	Total Operation & Maintenance Expeneses		$ 1,904,110
7	Depreciation and Amortization Expense	H-2	$ -
8	Regulatory Asset Amortization	B-2	-
9	Taxes Other Than Income Taxes	H-4	112,425
10	Federal and State Income Taxes	H-3	-
11	Return	B	-
12	Total Cost of Service		$ 2,016,535
13	Revenue Credits	G-5	(126,220)
14	Net Cost of Service		$ 1,890,315

Docket No. RP07-______
Statement P
Exhibit No. BMP-35

Black Marlin Pipeline Company
Partial Rate Increase
Classification Of Out-of-Pocket Costs

Line No.	Description	FERC Account No.	Schedule Reference	Total	Fixed/ Reservation	Variable/ Usage
	(A)	(B)	(C)	(D)	(E)	(F)
	TRANSMISSION EXPENSES		H-1			
	Operation					
1	Operation Supervision and Engineering	850		$ 24,945	$ 24,945	$ -
2	System Control and Load Dispatching	851		-	-	-
3	Communication System Expenses	852		4,880	4,880	-
4	Compressor Station Labor and Expenses	853		-	-	-
5	Gas for Compressor Station Fuel	854		-	-	-
6	Other Fuel and Power for Compressor Sts.	855		-	-	-
7	Mains Expenses	856		558,807	558,807	-
8	Measuring & Regulating Station Expenses	857		-	-	-
9	Transmission & Compression of Gas by Others	858		-	-	-
10	Other Expenses	859		29,810	29,810	-
11	Rents	860		42,736	42,736	-
12	**Total Operation**			$ 661,178	$ 661,178	$ -
13	**Maintenance**					
14	Supervision and Engineering	861		$ -	$ -	$ -
15	Structures and Improvements	862		-	-	-
16	Mains	863		55,488	55,488	-
17	Compressor Station Equipment	864		-	-	-
18	Measuring & Regulating Station Equipment	865		-	-	-
19	Communication Equipment	866		-	-	-
20	Other Equipment	867		-	-	-
21	Total Maintenance			$ 55,488	$ 55,488	$ -
22	**Total Transmission Expenses**			$ 716,666	$ 716,666	$ -
23	**ADMINISTRATIVE & GENERAL EXPENSES**					
24	Administrative and General Salaries	920		$ 113,507	$ 113,507	$ -
25	Office Supplies and Expenses	921		-	-	-
26	Administrative Expenses Transferred-Credit	922		-	-	-
27	Outside Services Employed	923		143,057	143,057	-
28	Property Insurance	924		109,452	109,452	-
29	Injuries and Damages	925		-	-	-
30	Employee Pensions and Benefits	926		126,115	126,115	-
31	Franchise Requirements	927		-	-	-
32	Regulatory Commission Expenses	928		433,333	433,333	-
33	Duplicate Charges-Credit	929		-	-	-
34	General Advertising Expenses	930.1		-	-	-
35	Miscellaneous General Expenses	930.2		261,980	261,980	-
36	Rents	931		-	-	-
37	Maintenance of General Plant	932		-	-	-
38	Total A&G Expenses			$ 1,187,444	$ 1,187,444	$ -
39	**TOTAL O&M and A&G EXPENSES**			$ 1,904,110	$ 1,904,110	$ -
40	Depreciation and Amortization Expense		H-2	$ -	$ -	$ -
41	Regulatory Asset Amortization		B-2	-	-	-
42	Taxes Other Than Income Taxes		H-4	112,425	112,425	-
43	Federal and State Income Taxes		H-3	-	-	-
44	Return		B	-	-	-
45	**Total Cost of Service**			$ 2,016,535	$ 2,016,535	$ -
46	Revenue Credits		G-5	$ (126,220)	$ (126,220)	$ -
47	**Net Cost of Service**			$ 1,890,315	$ 1,890,315	$ -

Docket No. RP07-______
Statement P
Exhibit No. BMP-36

Black Marlin Pipeline Company
Rate Schedules T-1, FTS and ITS
Partial Rate Increase
Rate Derivation

Line No.	Description	Reference	Total	Reservation	Usage
	(A)	(B)	(C)	(D)	(E)
1	Net Cost of Service	Exhbit No. BMP-35	$ 1,890,315	$ 1,890,315	$ -
2	Design Determinants	J-1		2,793,051	2,793,051
3	Unit Rate			$ 0.6768	$ -
4	Rate Schedule T-1			$ 0.6768	$ -
5	Rate Schedule FTS			$ 0.6768	$ -
6	Rate Schedule ITS				$ 0.6768

STATEMENT OF RATES

Currently Effective Rates
For Transportation of Natural Gas
Under Rate Schedules Contained in This
FERC Gas Tariff, First Revised Volume No. 1

(Rates - ¢ per MMBtu)

Rate Schedule	Section	Description	Currently Effective Rates
T-1	3	Reservation Fee	67.68
		Commodity Rate	0.00
		Authorized Over-Run Rate	67.68
FTS	3	Reservation Fee	
		Maximum	67.68
		Minimum	0.00
		Commodity Rate	
		Maximum	0.00
		Minimum	0.00
		Authorized Over-Run Rate	
		Maximum	67.68
		Minimum	0.00
ITS	3	Commodity Rate	
		Maximum	67.68
		Minimum	0.00
ACA	3	Annual Charge Adjustment	0.16