

BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of SourceGas) Application No. NG-0060
Distribution LLC, Lakewood,)
Colorado, seeking approval of a)
general rate increase.)
) ORDER GRANTING APPLICATION
) IN PART
)
)
) Entered: March 9, 2010

BY THE COMMISSION:

On or about July 2, 2009, SourceGas Distribution LLC, Lakewood, Colorado (SourceGas or Company) filed an application seeking approval of a general rate increase. Petitions for Formal Interventions were filed by the Public Advocate, Black Hills Energy, and the Public Alliance for Community Energy d/b/a ACE. A Petition for Informal Intervention was filed by Constellation New Energy Gas. On August 18 and September 29, 2009, the Commission entered orders granting Petitions for Formal and Informal Intervention.

In summary, SourceGas seeks a total revenue increase of approximately \$9.3 million and an overall rate of return of 9.05%. SourceGas proposes increases in the fixed monthly customer charges for residential rate payers from \$10.00 to \$15.00; for small commercial ratepayers from \$12.00 to \$17.00; and for large commercial ratepayers from \$22.00 to \$110.00. Furthermore, SourceGas has proposed a two-tiered distribution rate schedule with an increase in the per therm rate for the first tier from \$0.35 to \$0.50 and a slight decrease for the second tier from \$0.1086 to \$0.1084. In addition to changes in the fixed and volumetric charges, SourceGas seeks approval of five revenue decoupling mechanisms including: a Weather Normalization Adjustment (WNA), Customer Adjustment (CA), Use Per Customer Adjustment (UPCA), Inflation Adjustment (IA), and Pipeline Infrastructure Cost Adjustment (PICA).

Hearing on this matter was held December 14 through 17, 2009. Dan Watson, Dr. Charles Moyer, Ben Breland, Russ Feingold, Thomas Sullivan, Larry Loos, William Meckling, Verlyn Engler, Jerrad Hammer, James Elliott, and Alan Lovinger presented live testimony on behalf of SourceGas in support of its Application. Dr. David Dismukes, Dr. J. Randall Woolridge, Alan Bartsch, and Michael Arndt presented testimony on behalf of the Public Advocate. In addition to live testimony, prefiled written and rebuttal testimony on behalf of the witnesses listed above and that of Gary Abbate on behalf of SourceGas was entered into the record. Various other documents were also entered into

the record in this matter and will be referenced when appropriate.

O P I N I O N A N D F I N D I N G S

"Every rate made, demanded, or received by any natural gas public utility shall be just and reasonable. Rates shall not be unreasonably preferential or discriminatory and shall be reasonably consistent in application to a class of ratepayers."¹

The commission, in the exercise of its power and duty to determine just and reasonable rates for natural gas public utilities, shall give due consideration to the public need for adequate, efficient, and reasonable natural gas service and to the need of the jurisdictional utility for revenue sufficient to enable it to meet the cost of furnishing the service, including adequate provisions for depreciation of its utility property used and useful in rendering service to the public, and to earn a fair and reasonable return upon the investment in such property.²

"Cost of service shall include operating expenses and a fair and reasonable return on rate base, less appropriate credits."³

With the exception of the items specifically addressed herein, the Commission grants SourceGas' Application subject to the adjustments and limitations discussed below.

BURDEN OF PROOF

At the onset, the Commission is compelled to note that SourceGas' general rate application was rife with conclusory statements with little to no substantive support. It is not the volume of information provided, but the quality and relevance of the information that is important to meeting the burden of proof. SourceGas' multi-layered corporate structure which required all costs to be allocated coupled with lack of availability of records added to the complication of many of the issues presented.

The burden of proof in demonstrating that proposed rates are just and reasonable rests with the utility. SourceGas has incorrectly argued that it submitted its application in compliance with the Commission's standard filing requirements and

¹ Neb. Rev. Stat. § 66-1825(1) (2003).

² § 66-1825(3).

³ § 66-1825(4).

therefore the burden of proof then shifts to the Public Advocate.⁴ This is a misapplication of the burden of proof in general rate applications. In order to prove its case, a utility must not only meet the filing requirements but must provide substantive support for the elements of its rate application. Mere conclusory statements are insufficient.

A major burden of proof issue presented in this case by the Public Advocate is the lack of a fully allocated cost of service study. SourceGas repeatedly responded by stating that it is not required to perform one. The question is not whether SourceGas performed a fully allocated cost of service study but is instead whether it presented sufficient evidence to demonstrate just and reasonable rates. Implicit in the standard of "just and reasonable rates" is that such rates comply with the Act, which includes a prohibition against subsidization across classes of ratepayers. While the presentation of a fully allocated cost of service study would seem to be the most efficient and clear means of meeting that burden with regard to subsidization across classes, no explicit requirement to conduct such a study currently exists.

ROLE OF COMMISSION CONSULTANT REPORT

The Commission also finds it necessary to define the role of the Commission consultants and advisory report in this matter. Analysis in the form of an advisory report was provided by Commission consultants. Parties were provided an opportunity to comment on the report. The advisory report is intended to assist the Commission in the technical analysis of the information provided by all parties. The report itself is not evidence in this matter. The Commission retains the sole responsibility for balancing the interests of ratepayers and the utility and for advancing the policy objectives set forth in the Act.

MOTION TO DISMISS

On December 11, 2009, the Public Advocate filed a Motion to Dismiss SourceGas' Application (Motion) alleging that the Company failed to conduct and provide a fully allocated cost of service study and therefore evidence provided in support of the rate application was insufficient to meet SourceGas' burden of proof. SourceGas filed a response to the Motion on December 14, 2010, contending that there is no requirement to file a fully allocated cost of service study. Due to the fact that currently Commission rules do not explicitly require the filing of a fully

⁴ See Post-Hearing Brief of SourceGas Distribution LLC, pg. 9.

allocated cost of service study, the Commission finds that the Motion should be overruled.

ALLOCATION OF COMMON PROPERTY AND COSTS

The allocation of common property and shared costs among SourceGas' affiliates, the multiple jurisdictions, jurisdictional and non-jurisdictional services and the various classes of service is an issue throughout this case. The Act specifically addresses the inclusion of allocated common property and expenses.

The rate base of the jurisdictional utility shall consist of the utility's property, used and useful in providing utility service, including ... reasonable allocations of common property, less such investment as may be reasonably attributed to other than investor-supplied capital unless such deduction is otherwise prohibited by law.⁵

Operating expenses shall consist of expenses prudently incurred to provide natural gas service including (a) a reasonable allocation of common expenses as authorized and limited by section 66-1819 ..."⁶

The Act also specifically prohibits subsidization, stating:

Subsidization is prohibited. For purposes of this subsection, subsidization means the establishment of rates to be collected from a ratepayer or class of ratepayers of a jurisdictional utility that (a) include costs that properly are includable in rates charged to other ratepayers or classes of ratepayers of the utility, or other persons, firms, companies, or corporations doing business with the jurisdictional utility, (b) exclude costs that properly are includable in rates charged to such ratepayers or classes of ratepayers, or (c) include costs that properly are chargeable or allocable to a nonregulated private enterprise engaged in by such jurisdictional utility.⁷

SourceGas relies upon its Cost Assignment and Allocation Manual (CAAM) for the allocation of common property and common

⁵ § 66-1825(6).

⁶ § 66-1825(7).

⁷ § 66-1825(10).

expenses among affiliates and jurisdictions.⁸ The CAAM was originally created to comply with a regulation of the Colorado Public Utilities Commission and revised for the Arkansas Public Service Commission.⁹ It does not specifically address Nebraska requirements and has never been reviewed or approved by the Commission. The CAAM was filed with the application, and testimony was offered stating what method was used to allocate various costs based upon the CAAM. Testimony was also provided regarding the three-factor allocator. However, no supporting evidence was offered to demonstrate that the methods described in the CAAM resulted in reasonable allocations to Nebraska of common costs and property and avoided any illegal subsidization.

For example, in response to questions from the Public Advocate regarding the allocations made by SourceGas regarding the costs associated with the call center and their allocation between regulated and non-regulated activities, Mr. James Elliott testified in relevant part:

Q: Why is revenue a fair allocator of the call center if the amount of revenue that's paid on those in the category of regulated services has nothing to do with how much usage is made by that entire group of service recipient of the call center?

. . . .

A: Essentially what revenue shows is kind of the business focus and how much focus, you know, the overall business has on the particular activity.

So, you know, whether - whether or not a particular customer calls the call center 7 percent of the time related to their nonregulated service, I don't think that's really relevant.

What it is is in reflecting the costs and shared costs is where the overall business focus of the utility is. And revenue is a fair allocator and a fair indicator of what that focus is.

Q: What are your reasons for saying revenue is a fair allocator of cost - of call center function?

⁸ Rebuttal Testimony of James Elliott, Ex. 27 at 17:22-24.

⁹ Ex. 27 18:6-10.

A: Well, the basis is is that the cost and - should follow whatever that business focus is. If the business spends 5 percent of its time focused on nonregulated issues, then 5 percent of the common costs, 5 percent of the shared costs should go towards the - that particular function. So it's, you know, purely as it relates to the amount of time spent on a particular activity that makes it a fair allocator.¹⁰

SourceGas attempted to draw a connection between revenues generated and costs incurred by attempting to characterize revenues as an indicator of "business focus".¹¹ However, SourceGas provided no support for how it determined the percentage of time "the business spends ... focused on nonregulated issues." The Public Advocate's witness, Mr. Bartsch testified and provided data to show that Nebraska ratepayers are subsidizing SourceGas' non-utility activities because costs are not being properly allocated.¹² SourceGas' "business focus" allocation is unreasonable. It is not based on any discernable cost-causation principles.

Therefore, to the extent that the Public Advocate was able to provide an alternate method for allocating these costs and other common costs, the Commission finds its information persuasive and adopts it. Using this alternate method, the Public Advocate recommends that the Company's proposed operating and maintenance costs for the call center be reduced by \$1,074,703 and the SAP related costs be reduced by \$468,108. The adjustments to rate base that result from applying the Public Advocate's alternate allocations are discussed below.

In the absence of an alternative, the Commission reluctantly accepts the remainder of the Company's allocations made pursuant to the CAAM. However, this in no way constitutes approval of the CAAM, and the Company is advised to fully support its allocation methodologies in its next application for a rate increase. Calculations of allocations are set forth in Attachment A to this order, incorporated herein by this reference.

CLASS COST OF SERVICE STUDY

SourceGas also submitted a customer class cost of service study (COSS) for jurisdictional customer classes served by its

¹⁰ Trans. at 840:24-25; 841:10-13, 24-842:11.

¹¹ Trans. at 842:284 - 843:3.

¹² See Pre-filed Direct Testimony of Albert D. Bartsch, Ex. 99 and Ex. 209.

Nebraska operations including the residential, small commercial and large commercial customers.¹³ With respect to costs associated with the service of high volume and agricultural ratepayers, SourceGas employs a revenue crediting methodology by which prior to determining rates for jurisdictional ratepayers, SourceGas credits the revenues received from high volume and agricultural ratepayers to the overall cost of service for Nebraska. SourceGas itself has conceded that it does not know whether any subsidization is or will occur under this method.¹⁴ Furthermore, SourceGas also stated that those jurisdictions in which they utilize the revenue crediting method do not have the same "jurisdictional/nonjurisdictional breakout".¹⁵ High volume and agricultural ratepayers may or may not be bearing the costs associated with their service.

The Act specifically prohibits subsidization between classes of ratepayers. For purposes of determining rates in this matter, we assume that the rates established pursuant to a settlement in the prior rate application (Kinder Morgan) were just and reasonable. No party raised an issue regarding subsidies with respect to that settlement. When SourceGas purchased Kinder Morgan, it adopted Kinder Morgan's Commission approved rates. The rates currently in effect resulted from that case.

In order to mitigate the possibility of creating a subsidy, the Commission finds that the Public Advocate's recommendation be adopted and that the same percentage rate increase approved by the Commission be imputed to nonjurisdictional ratepayers as that imposed on other classes of ratepayers. It is SourceGas' decision as to whether the rates for high volume or agricultural ratepayers need to be adjusted to meet its revenue requirement. The Commission will expect SourceGas in the future to provide evidence regarding the cost of service to all classes of ratepayers in order to ensure that no subsidy exists.

RATE BASE

"The rate base of the jurisdictional utility shall consist of the utility's property, used and useful in providing utility service, including the applicable investment in utility plant, less accumulated depreciation and amortization, allowance for

¹³ Ex. 3, Schedules 24-29; Ex. 27 at 16:23-17:1 stating "The cost of service presented in the Company's Application in this docket was made according to the Commission's rules and accurately reflects the cost of service related to SourceGas Distribution's Nebraska Jurisdictional operations."; Trans. at 870:16-18.

¹⁴ Trans. at 866:10-19.

¹⁵ Trans. at 864:2-8.

working capital, such other items as may be reasonably included and reasonable allocations of common property, less such investment as may be reasonably attributed to other than investor-supplied capital unless such deduction is otherwise prohibited by law."¹⁶

"The rate base shall ordinarily consist of those items which are used and useful in providing service to the public."¹⁷ In calculating its rate base, SourceGas seeks adjustments totaling approximately \$5 million. The Public Advocate has objected to four of the proposed adjustments: construction work in progress in the amount of \$2,132,353, treatment of unamortized rate case expenses totaling \$534,010, adjustments related to SourceGas' customer call center in the amount of \$137,887, and the SAP billing system in the amount of \$1,927,078. Additionally, the Public Advocate seeks an adjustment to reduce rate base for Accumulated Deferred Income Taxes (ADIT) in the amount of \$14 million, the ADIT balance which SourceGas did not retain after the acquisition of Kinder Morgan assets.

"Post test year adjustments are permitted for known and measurable rate base adjustments to test year where the utility accounts for any related impacts on all aspects of the jurisdictional utility's operations. Related impacts are those that reasonably follow as a consequence of the post test year adjustment being proposed, including a related impact of another post test year adjustment."¹⁸

Construction Work In Progress

SourceGas seeks an adjustment to rate base in the amount of \$2,132,353 related to items it has described as construction work in progress. Adjustments included are set forth in Exhibit No. 97 in SourceGas' response to PA-514. The evidence presented on all but the project labeled "Polk: 2008 Pipe Replacement" in the amount of \$1,006,804.94 and those projects related to the SAP billing system totaling \$1,298,274.09 consisted only of the title, a notation about the completion date and the amount attributable to the project. Minimal additional evidence regarding the Polk and SAP billing projects was presented by Mr. Elliott.

¹⁶ § 66-1825(6).

¹⁷ § Neb. Admin. Code, Title 291, Ch. 9 § 005.06D (2006).

¹⁸ § 005.06F

Pursuant to Neb. Rev. Stat. § 66-1817,

(1) Any jurisdictional utility property may be deemed to be completed and dedicated to commercial service if construction of the property will be commenced and completed in one year or less.

(2) The commission may determine that property of a jurisdictional utility which has not been completed and dedicated to commercial service may be deemed to be used and useful in the utility's service to the public.

The Act makes a distinction between construction projects commenced and completed within a year and those that are truly construction works in progress which will be put into service more than 12 months after the end of test year.

Adjustments to rate base related to construction work in progress are entirely within the Commission's discretion.¹⁹ The Commission has previously provided guidance regarding the nature of direct testimony utilities should provide in support of adjustments for construction work in progress including but not limited to: "a discussion of each project; why the utility has determined that the project is necessary to the provision of safe and reliable gas service; and how the project costs are being financed, whether through debt or internally generated cash. Additionally, the utility should describe why it is necessary for the project to be included in rates before it is complete and in service."²⁰

The Commission further suggested that evidence should include: "a list of all construction projects the utility is requesting to include in plant in service which should include a description of the project; location of the project; purpose of the project; date construction was begun; expected completion date; actual costs incurred as of the last day of the test year; and finally total expected cost of the project at completion."²¹ Conclusory statements alone without any explanation are inadequate. Utilities are reminded that these are discretionary adjustments and it is the utility's burden to demonstrate that they should be included.

¹⁹ § 66-1817.

²⁰ *In the Matter of Aquila, Inc. d/b/a Aquila Networks (Aquila), Omaha, seeking individual rate increases for Aquila's Rate Area One, Rate Area Two, and Rate Area Three.*, Application No. NG-0041, Order Granting Application in Part, pg. 5 (July 24, 2007).

²¹ *Id.*

Mr. Elliott testified that the Polk County project was to replace piping. He further stated that the expenses related to the SAP billing system and the Polk County project were currently used and useful.²² Additionally, Mr. Elliott provided rebuttal testimony outlining adjustments made to accumulated depreciation and states that no adjustments to revenues are necessary as the projects are not revenue producing.²³ The Company made no adjustments to its ADIT and has stated that none are made the first year. The Commission remains concerned that adjustments may be required to ADIT by IRS regulations in order to avoid any normalization violations. However, the Commission does not find a sufficient record exists to require any such adjustment.

The Commission finds that, although very slight, the evidence provided regarding the Polk project and those items related to the SAP billing system was sufficient to satisfy SourceGas' burden of proof and should be included in rate base in the amount of \$2,143,083. This amount reflects the Public Advocate's adjustment for the allocation of the SAP billing system to Nebraska operations.

With respect to the remaining adjustments labeled as construction work in progress, SourceGas failed to produce sufficient evidence. Conclusory statements alone without any explanation are inadequate.

Unamortized Rate Case Expense

SourceGas proposed to amortize the cost of the rate case over a two-year period and include one-half of its estimated rate case expenses in rate base in the amount of \$534,010. The remaining half is included in administrative and general expenses. The Public Advocate proposes that the expense be amortized over three years and that no amount be included in rate base.

On and after June 1, 2007, the commission by general rule and regulation shall authorize the recovery of the amount of any assessments or charges paid to the commission pursuant to this section and section 66-1840 in a general rate filing or through a special surcharge which may be billed on the monthly statements for up to a twelve-month period immediately

²² Pre-filed Rebuttal Testimony of James E. Elliott, Ex. 27 at 53:6-12.

²³ *Id.* at 53:13-54:13.

following their payment by the jurisdictional utility.²⁴

SourceGas' approach is permissible under the Act. The Commission recognizes that the two-year amortization period is short and may lead to an over-recovery of rate base expenses. However, in light of the small increase approved in this matter, it is unlikely that the utility will delay filing a new rate application for an extended period of time and the risk for over-recovery is slight. The Commission finds that the unamortized rate case expense in the amount of \$534,000 should be included in rate base.

Call Center Furniture

SourceGas proposes to include \$137,887 for furniture for its new call center in Arkansas in rate base. The Public Advocate recommended that the costs be excluded or in the alternative that the amounts be allocated differently. Mr. Breland testified regarding the company's decision and plans to bring the call center in-house.²⁵ The Commission finds that the amount be included as it is used and useful; however, as previously discussed in this order, the Commission finds that the Public Advocate's method of allocation be used.

SAP Billing System

SourceGas seeks two rate base adjustments of \$1,298,274 for construction work in progress and \$1,927,078 related to the SAP billing system. The rate base adjustment for construction work in progress was previously discussed. With respect to the remaining adjustment of \$1,927,078, the Public Advocate again recommended the amount be excluded or in the alternative that the amount be allocated differently. Mr. Breland describes the necessity and nature of the SAP billing system in detail in his direct testimony, filed with the Company's application.²⁶ The Commission finds that the amount be included as it is used and useful; however, as previously discussed in this order, the Commission finds that the Public Advocate's method of allocation be used.

Accumulated Deferred Income Tax

Both the Company and the Public Advocate agree that Accumulated Deferred Income Tax (ADIT) contained on SourceGas' books

²⁴ § 66-1841(6)(b).

²⁵ Ex. 8 at 32:23-33:21; 36:3-38:11.

²⁶ Pre-filed Direct Testimony of Bentley W. Breland, Ex. 8 at 30:3-9; 34:4-35:26; 36:3-39:10.

is appropriately deducted from rate base as cost-free capital. The disagreement arises regarding the amount of ADIT that should be properly deducted. When SourceGas purchased the utility distribution assets from the previous owner Kinder Morgan, approximately \$14 million of ADIT that was on Kinder Morgan's books did not transfer to SourceGas. The Public Advocate estimates that the balance of ADIT as of December 31, 2008, would have been approximately \$15 million rather than the \$1.3 million reflected by SourceGas in this proceeding if the \$14 million in ADIT had transferred to SourceGas from Kinder Morgan.

During the acquisition proceeding before this Commission, Ben Breland testified on behalf of the companies that the ADIT balance would transfer to SourceGas.²⁷ Mr. Breland later learned that the ADIT balance would not transfer because of the federal income tax treatment of the sale transaction.²⁸ SourceGas did not inform the Commission when it learned that the information provided on the ADIT balance at the NG-0039 proceeding was incorrect. In the interest of full disclosure and openness, the Company should have considered informing the Commission of the error; however, the practical affect of such knowledge by the Commission at that time would have been negligible. The Company has made the Commission aware of the ADIT balance situation in direct testimony for this proceeding, acknowledging that Mr. Breland's testimony regarding the transfer of ADIT in NG-0039 was incorrect.²⁹

The Public Advocate urges us to find that SourceGas failed to retain the benefit of the ADIT balance in the acquisition from Kinder Morgan for Nebraska consumers and therefore acted in an imprudent manner. He argues \$14 million should be deducted from the Company's revenue requirement for what he characterizes as a failure.

The Commission declines to make such a finding. The Commission notes that in the acquisition by SourceGas of Kinder Morgan's utility distribution assets, SourceGas was one of two parties negotiating the details of the acquisition. SourceGas did not have exclusive control to determine how the acquisition was structured. To say the Company acted imprudently by not structuring the sale to maximize ADIT for SourceGas' customers ignores the practical reality of negotiating an agreement. Neither the Public Advocate nor the Commission was privy to those negotiations. If the ADIT had been handled differently, the final agreement on many points may have ultimately been

²⁷ Trans. at 489: 19-25.

²⁸ Trans. at 491: 8-19.

²⁹ Id.

different. It would be speculative to surmise what, if anything, SourceGas could or should have done regarding the ADIT balance. Simply because the Public Advocate does not favor the outcome does not make the structure of the acquisition imprudent.

The Public Advocate, in the alternative, recommends the \$14 million loss of ADIT be considered an acquisition premium and deducted from rate base, as SourceGas agreed in the NG-0039 stipulation approved by the Commission not to seek any acquisition premiums from ratepayers.³⁰ Commission rules define acquisition adjustments as "the difference between the purchase price of an acquired operating unit or system and the depreciated original cost of the acquired property."³¹ The loss of ADIT does not meet the definition of an "acquisition adjustment" and therefore should not be treated as such.

Finally, the Public Advocate suggests the Commission remove basis points from the Company's approved return on equity in this proceeding as a kind of punitive measure for not retaining the ADIT balance from Kinder Morgan and not informing the Commission at the time the Company learned the ADIT balance would not transfer.³² We are not inclined to do so. We see no direct link between the treatment of ADIT in an acquisition of a utility distribution system and the appropriate return on equity in a general rate increase filing.

For the reasons articulated above, we will not adjust the ADIT balance included by the Company in this filing. It shall remain \$1.3 million.

All rate base adjustments are set forth in Attachment B to this order, incorporated herein by this reference.

COST OF SERVICE

"Operating expenses shall consist of expenses prudently incurred to provide natural gas service including (a) a reasonable allocation of common expenses as authorized and limited by section 66-1819 and (b) the quantity and type of purchased services regulated by the Federal Energy Regulatory Commission."³³

³⁰ *Id.* Approved (February 27, 2007).

³¹ § 005.06A4.

³² See Post-Hearing Brief of the Public Advocate at pg. 42.

³³ § 66-1825(7).

Ad Valorem Taxes

SourceGas seeks to include all Ad Valorem taxes it paid to the State of Nebraska on its Nebraska utility assets. The amount of these taxes has increased significantly since SourceGas' acquisition of Kinder Morgan's assets.³⁴ The Public Advocate argues that the increase in taxes is the result of SourceGas having paid more than net book value for the utility plant it purchased from Kinder Morgan. Therefore, he recommends that the Ad Valorem tax amount included in rates should be reduced to the 2008 amount paid because the increased tax amount is related to the acquisition premium SourceGas paid, and should not to be recovered from ratepayers.³⁵

While it is true the Ad Valorem taxes owed by SourceGas to the State of Nebraska increased significantly after the purchase from Kinder Morgan, the taxes are assessed by the State, and are due and payable on SourceGas' public utility property used and useful in providing service to its customers. As previously stated, Commission rules specifically define acquisition adjustments as "the difference between the purchase price of an acquired operating unit or system and the depreciated original cost of the acquired property."³⁶ Adopting the Public Advocate's proposal to treat additional taxes as an acquisition adjustment would take an unreasonably broad view of "purchase price" in the Commission's definition of acquisition adjustment, requiring us to interpret "purchase price" to include taxes that accrued after the purchase.

The State of Nebraska determines the value of the utility assets and assesses taxes accordingly. Nothing in the record before us provides any validity to the Public Advocate's claim that SourceGas overpaid for Kinder Morgan's utility assets in Nebraska. The State's valuation of the assets purchased by SourceGas from Kinder Morgan increased after the sale, resulting in a corresponding increase in the tax liability owed by SourceGas to the State of Nebraska. These taxes are a reasonable and necessary cost assessed by a non-related party and should be recoverable by SourceGas in its rates.

Income Taxes

SourceGas seeks recovery of income taxes calculated at the maximum federal income tax rate of 35 percent.³⁷ The Public

³⁴ Trans. at 428:21.

³⁵ Prefiled Direct Testimony of Michael L. Arndt, Ex. 93 at 52:8-10.

³⁶ § 005.06A4.

³⁷ Prefiled Direct Testimony of James M. Elliott, Ex. 22 at 33:23.

Advocate raises two issues regarding SourceGas' calculation of income tax. First, SourceGas Distribution as a wholly-owned subsidiary does not pay federal income taxes. Second, the owners of SourceGas Distribution, Alinda and Aircraft Services Corporation, file a consolidated federal income tax return which includes SourceGas Distribution among other subsidiaries. The Public Advocate raises the possibility that there may have been some consolidated tax savings to the Company as whole, a portion of which should have been assigned to SourceGas Distribution. The Company did not file the consolidated tax return schedules in this case. The Public Advocate recommends that SourceGas Holdings, LLC, the direct parent of SourceGas Distribution, be required to file the consolidated schedule of its parent companies in its next rate case.³⁸

Income taxes paid by a utility are a necessary and reasonable cost and should be included in SourceGas' rates. In the current proceeding, the Company submitted a 35% federal income tax based on its estimated income if granted the rate of return proposed by the Company in this case. However, as discussed by the Commission below, the federal income tax owed on SourceGas' taxable income should be adjusted to reflect the rate of return finally determined in this proceeding. Therefore, based on the final results as outlined in this order, the applicable federal income tax rate should be 34 percent.³⁹ The adjustment to the revenue requirement shall be made pursuant to the applicable federal rate.

It is speculation as to whether consolidated tax savings were realized by SourceGas' parent due in any part to the operations of SourceGas Distribution. The Public Advocate recommended the Commission order SourceGas in its next general rate case filing to file a consolidated income tax return to evaluate any consolidated tax savings that may have been realized by the entire family of companies. We, however, decline to require a consolidated income tax return of SourceGas' parent companies be filed in any future rate case proceeding. The Commission will instead estimate the taxable income the Company would report if it filed federal income taxes on its own and apply the appropriate federal tax levy to that amount to determine the fair and reasonable amount of federal taxes to be included in the revenue requirement by SourceGas Distribution. In the absence of a federal income tax return filed by SourceGas Distribution, we find this is the most reasonable way of determining the appropriate federal tax expense.

³⁸ See Post-Hearing Brief of the Public Advocate at pg. 51.

³⁹ 26 U.S.C. § 11 (West 2010).

The income tax calculations are set forth in Attachment C to this order, incorporated herein by this reference.

Fines and Penalties

The Public Advocate pointed out that SourceGas has included in its revenue requirement \$255 in fines. The Commission diligently searched the record for any information provided by the Company regarding these fines and penalties and was unable to find any supporting evidence regarding the fines sought to be recovered by the Company. The Commission was provided with no explanation regarding when the fines were imposed, by whom, and for what infraction or violation committed by the Company. Indeed, the Commission has no information that the fines sought to be included by the Company were related to its Nebraska operations or regulated activities. Therefore, the \$255 for fines shall not be included in the Company's revenue requirement.

Outside Services

SourceGas has included \$2.08 million in expenses for outside services.⁴⁰ The \$2.08 million in costs for outside services were allocated to SourceGas Distribution from its affiliates. The Public Advocate recommends excluding this amount in its entirety or, in the alternative, allowing the Company to recover the amount included in the previous rate case of \$215,663.⁴¹

The Commission cannot rely upon the outside services figure from the prior rate case as SourceGas Distribution along with its parent companies and affiliates are separate and distinct from Kinder Morgan and its affiliates, the Company operating the utility in Docket No. NG-0036.⁴² We have no evidence to rely upon in making a determination that the outside services required by SourceGas and the outside services used and recovered by Kinder Morgan in the last rate case are the same.

We are therefore left with the \$2.08 million figure and can find no support or basis in the record for that figure. The Company merely states that these costs were assigned to Federal Energy Regulatory Commission (FERC) Account 923 and evaluated by the Company to ensure the amount accurately reflected Nebraska.⁴³ No information was provided by the Company as to what criteria

⁴⁰ Prefiled Direct Testimony of Michael L. Arndt, Ex. 93 at 49:20-22.

⁴¹ See Docket No. NG-0036, *In the Matter of the Application of Kinder Morgan, Inc., Lakewood, Colorado, seeking approval of a general rate increase*, Order Approving Stipulation, (December 27, 2006).

⁴² *Id.*

⁴³ Prefiled Rebuttal Testimony of James M. Elliott, Ex. 27 at 72-73.

or basis was employed by the Company to evaluate those expenses and how they reflect Nebraska was never explained or presented. The Commission is unable to make a determination as to the reasonableness and necessity of the costs included by the Company for outside services based on the information provided by the Company. Further, as discussed in the allocation section, the Company gave us no supporting documentation regarding the allocation used to finally arrive at the \$2.08 million figure assigned to SourceGas Distribution to support the appropriateness of the figure. Therefore, the cost for outside services sought by the Company shall be excluded from the revenue requirement of the Company.

Cash Incentive Bonuses

SourceGas seeks recovery of \$159,459 in cash incentive bonuses paid to SourceGas employees. This figure was also allocated to SourceGas Distribution by its affiliates. The Public Advocate recommends that these amounts be disallowed.⁴⁴

The Company provided no evidence or information on the record as to how the bonuses were determined, who within the Company structure received the bonuses, nor how the allocation of the cost of the bonuses among affiliates was determined. The Company merely states the bonuses are based on evaluations of individual, department, and Company performance. The Company evaluated financial, customer service, employee responsiveness, safety and initiative.⁴⁵ The Commission has insufficient information on the record to ascertain how the bonuses were computed and even if the bonuses allocated to SourceGas Distribution's Nebraska operations relate to employees, departments, or SourceGas Distribution or were based on the performance of the entire family of SourceGas companies. Nothing provided indicates if any bonuses sought to be recovered were for anything related to service in Nebraska. Therefore, the Commission finds that the \$159,459 of bonuses sought by the Company will not be included in the revenue requirement.

Contributions and Donations

SourceGas initially sought to include \$2,172 in the cost of service related to charitable contributions and donations. The Public Advocate recommended the entire amount be removed from the cost of service for ratemaking purposes. In rebuttal testimony, the Company agreed that the \$2,172 for contributions

⁴⁴ Prefiled Direct Testimony of Michael L. Arndt, Ex. 93 at 51:1-3.

⁴⁵ Prefiled Rebuttal Testimony of James M. Elliott, Ex. 27 at 73:18-21.

and donations should be excluded.⁴⁶ Therefore, the \$2,172 of charitable contributions and donations shall not be included in SourceGas' cost of service for ratemaking purposes.

Depreciation Expense

The depreciation expense sought by the Company is based on all of the items proposed by SourceGas to be included in its rate base. Depreciation expense should therefore be adjusted to reflect only those items determined to be correctly included in rate base in this proceeding as outlined in this order. The depreciation expenses reflected by the Company for the items included in rate base are reasonable. Therefore, the expenses shall be adjusted to include only those items the Commission approved to be included in rate base in this proceeding. The adjustments are reflected in Attachment E to this order.

RATE OF RETURN

"In determining a fair and reasonable return on the rate base of a jurisdictional utility, a rate-of-return percentage shall be employed that is representative of the utility's weighted average cost of capital including, but not limited to, long-term debt, preferred stock, and common equity capital."⁴⁷

"The Commission must allow each utility a reasonable opportunity to earn a reasonable rate of return, which is expressed as a percentage of invested capital, and must fix the rate of return in accordance with Neb. Rev. Stat. §§ 66-1825(3) and (5)."⁴⁸ In evaluating each case, the Commission "must consider the utility's cost of capital, which is the weighted average of the cost of the various classes of capital used by the utility."⁴⁹

The classes of capital include debt and equity. "The cost of debt capital is the actual cost of debt."⁵⁰ "The cost of equity capital must be based upon a fair return on its value."⁵¹

Capital Structure

Mr. Breland discusses the Company's proposed capital structure.⁵² Schedule 12 of Exhibit 3 "sets forth SourceGas' actual

⁴⁶ *Id.* at 74.

⁴⁷ § 66-1825(5).

⁴⁸ § 005.05A.

⁴⁹ § 005.05A2.

⁵⁰ § 005.05A2(a).

⁵¹ § 005.05A2(b).

⁵² Ex. 8 at 21:15-22:6.

capital structure as of December 31, 2008. Test year common equity comprises approximately 49.96% of SourceGas' capital structure, with the remaining approximately 50.04% representing long-term debt."⁵³ Neither SourceGas nor the Public Advocate propose an alternate equity ratio. Given the record developed, an equity ratio of 49.96 percent is reasonable for SourceGas Distribution LLC.

Cost of Debt

Mr. Breland's Schedule 13 of Exhibit 3 "sets forth the calculations of SourceGas' actual average cost of long-term debt, with consideration given to all of the individual debt instruments secured by SourceGas."⁵⁴ He develops an average cost of long-term debt equal to 6.005 percent. SourceGas does not specifically address the cost of long-term debt for SourceGas. The Public Advocate writes that "SourceGas has used a long-term debt cost of 6.005 percent. I will use this long-term debt cost rate."⁵⁵ Given the record developed, a cost of long-term debt equal to 6.005 percent is reasonable for SourceGas Distribution LLC.

Cost of Equity Capital

Both SourceGas and the Public Advocate develop a set of comparable companies and use financial data for those companies to estimate a cost of equity capital for SourceGas. SourceGas includes in its group of comparable companies "the twelve-firm grouping of natural gas utilities that is followed by *Value Line*."⁵⁶ The Public Advocate begins with a set of natural gas distribution companies that meet the following selection criteria:

(1) Listed as a natural gas Distribution, Transmission, and/or Integrated Gas Companies in *AUS Utility Reports*; (2) listed as a Natural Gas Utility in the Standard Edition of the *Value Line Investment Survey*; and (3) an investment grade bond rating by Moody's and Standard and Poor's.⁵⁷

The Public Advocate then excludes from this group New Jersey Resources and UGI due to their "low percentage of revenues from regulated gas operations,"⁵⁸ ending up with a group of

⁵³ *Id.* at 21:18-24.

⁵⁴ *Id.* at 22:14-16.

⁵⁵ Pre-filed Testimony of J. Randall Woolridge, Ph.D., Ex. 116 at 17:17-18.

⁵⁶ Pre-filed Direct Testimony of R. Charles Moyer, Ph.D., Ex. 15 at 10:13-14.

⁵⁷ Ex. 116 at 16:1-5.

⁵⁸ *Id.* at 16:11.

nine comparable companies. All nine are in SourceGas' group. The only difference between the two sets of comparable companies is whether New Jersey Resources, UGI and NiSource should be included. Comparative results for a variety of measures are very similar.⁵⁹ Hence, in this particular case, it appears to be of little practical consequence whether SourceGas' group of 12 comparable companies or the Public Advocate's group of nine comparable companies is used.

SourceGas uses its comparable group to develop an estimate of the cost of equity capital using Discounted Cash Flow (DCF) analysis, the Capital Asset Pricing Model (CAPM) and a Comparative Earnings (CE) standard. The Public Advocate uses the DCF and CAPM to generate an estimated return on equity capital.

The Public Advocate develops equity return estimates in the range of 7.2 to 9.05 percent. In considering the appropriate rate to choose from this range, the Public Advocate chooses "an equity cost rate at the upper end of the range, 9.0%, in recognition of recent capital market conditions."⁶⁰

SourceGas averages estimates from the CAPM, DCF and comparable returns model to get an estimated cost of equity capital equal to 10.1 percent. SourceGas then adds 250 basis points to generate an estimated cost of equity equal to 12.6 percent. However, it lowers that estimate to 12.1 percent, "recognizing that the current capital market environment reflects unusually high, and hopefully temporary, required return premiums for a company's more junior sources of capital."⁶¹

The company discusses SourceGas LLC in relation to its group of comparable companies. It argues that "SourceGas LLC is riskier than the average firm in the grouping"⁶² because SourceGas LLC has a capital structure with 50.04 percent long-term debt and the comparables have an average long-term debt ratio of 46.2 percent. It also establishes that parent company SourceGas LLC has a lower bond rating than the average for the

⁵⁹ For example, the table below shows averages for a variety of relevant measures using the SourceGas group of comparable companies and the Public Advocate's group.

Measure	SourceGas Group	Public Advocate Group
Long-Term Debt (Ex. 18)	46.21	44.78
Beta (<i>Id.</i>)	0.70	0.69
Comparative Earnings (Ex. 19)	11.2	11.1
Dividend Yield (<i>Id.</i>)	4.84	4.66
Dividend Growth Rate (<i>Id.</i>)	5.29	5.28

⁶⁰ Ex. 116 at 2:15-16.

⁶¹ Ex. 15 at 11:12-14.

⁶² *Id.* at 16:18-19.

group and has lower revenues than the average for the group. SourceGas then argues that "[t]hese data lead to the conclusion that SourceGas Distribution is a considerably riskier firm, from the standpoint of rate of return analysis, than the average of the firms in the *Value Line* grouping. Hence, the cost of equity estimates that are derived from an analysis of the twelve firms in the *Value Line* grouping need to be increased when applied to SourceGas Distribution."⁶³

To make this adjustment, SourceGas asserts that "utilities with an A/A- bond rating [the average bond rating for his comparable group] can expect that investors will demand about a 6.54 percent yield on their bonds."⁶⁴ In comparison, it argues that "utility companies with a Bal/BBB- bond rating [the split bond rating held by the parent company SourceGas LLC] can expect to pay about 9 percent when issuing bonds."⁶⁵ Subtracting the lower value from the higher value, SourceGas argues "[t]he difference between 9 percent and the 6.54 percent required yield on the bonds of the *Value Line* sample companies leads to approximately a 2.5 percent required equity risk premium above the cost of equity for the *Value Line* sample."⁶⁶

The Public Advocate objects to this additional premium for several reasons.⁶⁷ Primarily, his objection is that the bond ratings are ratings for SourceGas Distribution LLC's parent company, SourceGas LLC, and not for the regulated distribution company itself. Consequently, the ratings reflect the credit worthiness of the parent company and not the distribution company.

We find SourceGas' adjustment untenable for several reasons. The additional risk premium is based on the bond ratings of the parent company SourceGas LLC and not the risk profile of SourceGas Distribution, LLC. In Exhibit 194, the bond rating company Standard & Poor's explains its rating of SourceGas LLC bonds. Standard & Poor's writes that the rating "reflects the company's excellent business risk profile and highly leveraged financial risk profile. The ratings are based on the consolidated credit profile of SourceGas Holdings LLC."⁶⁸ Two implications are apparent. First, the "excellent business risk profile" suggests that SourceGas Distribution, LLC is in a relatively low risk position with respect to its mix of customers and revenue expectations. The second is that the

⁶³ *Id.* at 17:8-13.

⁶⁴ *Id.* at 17:20-22.

⁶⁵ *Id.* at 17:24.

⁶⁶ *Id.* at 18:5-9.

⁶⁷ Ex. 116 at 80.

⁶⁸ Attachment PA-198 at 7.

financial risk can be attributed to the parent of the parent company. SourceGas Holdings LLC is the parent of SourceGas LLC, which in turn is the parent of SourceGas Distribution, LLC. The credit rating company clearly states that its ratings are based "on the consolidated credit profile of SourceGas Holding LLC."⁶⁹ SourceGas provides no evidence that the credit profile of SourceGas Holdings, a very diversified company with operations in regulated and non-regulated markets, and the resulting bond rating of SourceGas LLC is reflective of the relative riskiness of the regulated entity, SourceGas Distribution, LLC.

Another concern is that the record creates some confusion as to what SourceGas is actually measuring. Upon questioning from the staff attorney during testimony, SourceGas stated that the group of split rating companies was "mostly industrial companies."⁷⁰ It is not at all clear that a regulated natural gas distribution utility whose parent company has a Bal/BBB bond rating faces the same risks as the universe of mostly industrial companies with the same split bond rating. SourceGas presents no research or any other evidence to substantiate this claim. Without such research or evidence in the record, there is no basis for SourceGas' suggested adjustment.

A third concern is that SourceGas uses relative returns on bonds and applies that margin to stocks. No research or evidence has been introduced into the record suggesting that any margin in relative bond yields is appropriate when measuring relative stock returns.

For these reasons, SourceGas' proposed additional risk premium is unjustifiable and should be excluded from the Company's estimate of allowable return on equity capital. Removing 250 basis points from SourceGas' original estimate of 12.6 percent generates an estimate of 10.1 percent return on equity.

Using the Public Advocate's recommendation and SourceGas' estimate minus additional risk premium, an estimate of the cost of equity capital is in the range of 9.0 to 10.1 percent. Further evidence, discussed below, supports that the midpoint of this range, 9.6 percent, is a fair and reasonable rate of return.

In its rebuttal testimony SourceGas argues that "a return in the range of 7.2 - 9.05 percent is not consistent with current financial markets. It is not consistent with my

⁶⁹ *ibid.*

⁷⁰ Trans. at 274:3-16.

understanding of the judicial principles detailed in my direct testimony."⁷¹ SourceGas continues,

In today's marketplace, SourceGas must pay over 8.6 percent for new issues of long-term debt (source: Wells Fargo Securities, October 2009). The Public Advocate's recommended range of cost of equity (7.2% to 9.05%) is largely outside the bounds of this bed-rock standard of reasonability. Even the specific recommendation of 9 percent is inconsistent with all standards of reasonable risk premium spreads between common stock and bonds for a company. Between 1926 and 2008, realized annual returns on stocks have exceeded corporate bond returns by 5.5%. A recommended return of 9% represents an equity risk premium of 0.4 percent, a number that is totally inconsistent with market history and expectations.⁷²

SourceGas' arguments are not supported by the record. There is no evidence establishing that 8.6 percent is an accurate estimate of SourceGas' cost of long-term debt. There is, however, ample evidence in SourceGas' Exhibit 17 and the Public Advocate's Exhibit 120 to suggest that SourceGas' cost of long-term debt will be in the range of 6 to 6.5 percent. Page 1 of Exhibit 120, for example, shows that since 2005, BBB-rated utility bonds have never yielded even 7 percent, except for the period of September 2008 through July 2009. As of late September 2009, BBB-rated bonds were yielding only 6 percent. The Value Line "Selected Yields" in SourceGas' Exhibit 17 show the same thing.

The Capital Asset Pricing Model shows the sector-specific spread between the market return and the risk free rate. Using SourceGas' estimated beta of 0.7 and a risk premium of 6.5 percent, the implied spread for the group of comparable utilities should be 4.6 percentage points. It must be noted that this is the spread over the risk free rate. If utility bonds are 150 to 200 basis points above the risk-free rate (as suggested by panel B of Exhibit 120), this suggests a spread between utility bond and equity returns of from 2.6 to 3.1 percentage points. Hence a return on equity capital of 9.6 percent is very consistent with current financial markets. It is consistent with *Federal Power Comm. v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) and *Bluefield Co. v. Pub. Serv. Comm.*, 262 U.S. 679 (1923) as well.

⁷¹ Pre-filed Rebuttal Testimony of R. Charles Moyer, Ph.D., Ex. 21 at 3:15-17.

⁷² *Id.* at 4:15-24.

Based on the previous analysis, SourceGas Distribution LLC - Nebraska should be allowed a cost of equity of 9.6 percent.

Rate of return calculations are set forth in Attachment D to this order and incorporated herein by this reference.

BASE RATE REVENUE REQUIREMENT

Based upon the above, the Commission finds that SourceGas is entitled to a base rate revenue requirement of \$38,341,178. Rates are designed to recover this amount, annually. Revenue requirement calculations are set forth in Attachment E to this order, incorporated herein by this reference.

HEAT PROGRAM

SourceGas currently offers its High-efficiency Assistance Tool (HEAT) program which provides rebates to customers who purchase and install certain natural gas heaters.⁷³ Mr. Gary Abbate testified that the purpose of the program was to meet competition from electric utilities by offering rebates similar to those being offered for the installation of electric heat pumps.⁷⁴ From 2007 through mid-2009 2,646 people have participated in the program and rebates totaling \$1,009,500 have been paid.⁷⁵ SourceGas has proposed adding water heater installations to the program.⁷⁶ The Commission finds that the addition of water heater installations as proposed should be approved.

RATE ADJUSTMENT MECHANISMS

SourceGas seeks approval of five revenue decoupling mechanisms including: a Weather Normalization Adjustment (WNA), Customer Adjustment (CA), Use Per Customer Adjustment (UPCA), Inflation Adjustment (IA), and Pipeline Infrastructure Cost Adjustment (PICA). SourceGas proposed these mechanisms to address the impacts of what it has termed as "major business challenges faced by gas distribution utilities operating in North America" that it asserts are not adequately addressed by traditional ratemaking.⁷⁷

⁷³ Pre-filed Direct Testimony of Gary J. Abbate, Ex. 86 at 19:1-4.

⁷⁴ *Id.*, 19:5-8.

⁷⁵ *Id.*, 21:5-16.

⁷⁶ *Id.*, 22:12-17.

⁷⁷ See Pre-Filed Direct Testimony of Russell A. Feingold, Ex. 45 at 8:4-10:13.

Weather Normalization Adjustment, Customer Adjustment and Use per Customer Adjustment

The WNA, CA and UPCA can be properly characterized as "decoupling" mechanisms intended to break the link between the utility's revenues and customer volumetric use.

The WNA is designed to address the variability of weather by correcting for deviations from normal weather which underlie the Company's base rates. Similarly, the UPCA adjusts for deviations from the weather-normalized use per customer upon which rates were based. The CA is designed to adjust for the numbers of customers served as compared to the number of customers included in the test year customer count supporting its base rates.

The Commission is aware of the more rural nature of SourceGas' service area and the declining trends in rural populations to which it provided testimony. However, many reasons can exist for a decline of customers, which can include poor customer service and the impact of alternative energy sources. With respect to weather, the utility itself concedes that weather fluctuations can result in increases and decreases in any adjustment.

As a matter of policy, the Commission believes that decoupling mechanisms generally should only be considered when done in conjunction with the institution of a comprehensive energy efficiency program. SourceGas currently has no such program other than the HEAT program which is limited to offering appliance rebates. Therefore, the Commission finds that the proposed UPCA, WNA, and CA should be denied.

Inflation Adjustment

The IA adjusts rates based upon changes in inflation. It may be true that certain indices may show an increase or decrease in prices throughout the economy. However, such changes in prices do not necessarily flow directly, dollar for dollar, to a utility's costs. Further, it does not allow for cost savings that may result from increased efficiencies on the part of the utility or costs that may not change due to existing contracts. Finally, such an arbitrary adjustment does not encourage innovation and efficiency on the part of utilities. There is simply an insufficient nexus between changes in inflation and the actual costs incurred by utilities. Therefore, the Commission finds that the proposed IA should be denied.

Pipeline Infrastructure Cost Adjustment

Finally, the PICA is intended to allow the Company to recover pipeline infrastructure costs incurred after the test year and not included in the test year without the necessity of a new general rate application. The PICA is not intended to include those projects driven by load growth considerations.

In 2009, the Legislature enacted LB 685 [2009] which allows a utility to adjust its rates for infrastructure replacement projects that meet particular criteria.⁷⁸ LB 685 addresses projects similar to those intended to be covered by SourceGas' proposed PICA. The Legislature has opted to set forth specific criteria and processes for adjusting rates to address similar infrastructure projects between general rate filings. The Commission believes it ill-advised to adopt a separate and automatic adjustment that would short-circuit the process now in place. Therefore, the Commission finds that the PICA should not be approved.

RATE DESIGN

SourceGas has proposed a rate design similar to that currently used with a fixed customer charge and a two-tiered volumetric charge. The Commission did not permit the use of revenue crediting for purposes of allocating cost of service among regulated and unregulated ratepayers and imputed an increase to high-volume and agricultural ratepayers for the purposes of setting rates. Because the Commission cannot rely on the COSS filed by SourceGas, we have therefore set rates in an effort to retain the status quo with respect to the relationship between the various classes of ratepayers and between the volumetric and fixed charges. The resulting rates are set forth in Attachment F to this order, incorporated herein by this reference.

SourceGas had asserted that it was under-recovering costs from its large commercial class of customers and therefore a greater increase in the customer charge was warranted. However, as previously stated, the Commission is unable to rely on the COSS provided by SourceGas. Furthermore, the smaller increase in the customer charge is consistent with the Commission's gradualism approach.

Additionally, the rate design adopted by the Commission has maintained the second tier volumetric charge at the rate as it existed prior to this Application. Such an increase is

⁷⁸ See Neb. Rev. Stat. § 66-1865 (2009).

consistent with the Commission's intention to encourage energy conservation and will send the proper price signals to rate-payers.

COMPLIANCE

The Commission finds that a compliance conference should be scheduled by the hearing officer to allow all parties an opportunity to discuss the terms and practical effects of the order. Subsequent to the conference, SourceGas shall submit to the Commission a Compliance Filing which shall include at least the following information.

Interim Rate Refund Plan

As permitted by law, SourceGas implemented interim rates pending the consideration of its rate application.⁷⁹ SourceGas implemented the full amount of its proposed rate. As a result of the Commission's decision herein, ratepayers are entitled to a refund of any amounts paid over and above the rates approved herein.

SourceGas will be required to file a Refund Plan within thirty (30) days from the compliance conference referenced herein. That Refund Plan shall include a proposal for refunding the difference between the interim rate revenue collected and its final rates. The Commission reserves the ability to receive evidence regarding such Refund Plan and to enter a subsequent order regarding such Refund Plan as hereafter provided in this order.

Proration of Rate Changes

The Company shall prorate the application of the final rates to reflect the estimated customer gas usage that occurred before and after the effective date of the new rates. The Compliance Filing shall include detailed description of the proration method utilized by the Company to implement the final rates as contained in this order.

Tariff Sheets

Finally, within thirty (30) days of the compliance conference, SourceGas shall file any necessary tariff sheets with the Commission.

⁷⁹ Neb. Rev. Stat. § 66-1838(10)(b) (2003).

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O R D E R

IT IS THEREFORE ORDERED by the Nebraska Public Service Commission that the Application for Approval of a General Rate Increase is granted in part.

MADE AND ENTERED at Lincoln, Nebraska this 9th day of March, 2010.

NEBRASKA PUBLIC SERVICE COMMISSION

COMMISSIONERS CONCURRING:

Frank Sanders

Aime Boyle

//s// Tim Schram

Tim Schram

Vice Chairman

ATTEST:

Michael J. HSO

Executive Director

COMMISSIONERS DISSENTING:

//s// Rod Johnson

//s// Gerald L. Vap

COMMISSIONER ANNE BOYLE, CONCURRING:

It is with great reluctance that I concur with the majority. My preference would be to deny any increase; however, a small amount is warranted. With this concurrence, I expect that the carrier will not file another rate case for some time given the costs borne by ratepayers for this case. Rarely, if ever, has a carrier come before this Commission requesting an increase in rates with so little support for the request which has resulted in such enormous cost to its ratepayers.

It is the utility's burden to demonstrate that its requested rates are just and reasonable. The applicant submitted a case to the Commission requesting a significant increase but failed to include evidence to prove their case. Lack of evidence was so overwhelming, the Commission majority allowed SourceGas only a small percentage of their request. Since Nebraska statutes allow a proposed rate to go into effect soon after a case is filed, SourceGas ratepayers have been drastically overcharged each month awaiting the outcome of this case. These are complex matters requiring a great deal of time and attention on the part of not only the parties involved but the Commissioners, Commission staff and consultants.

The Commission now must determine the amount to be credited to customers for monthly proposed rates that were unjustified. Although ratepayers have paid the increase each month, they do not receive a cash refund, only a credit on their bill going forward. The Commission can require un-retained funds be set aside for useful purposes. Yet, some consumers have overpaid and will never receive a refund because they have moved and cannot be located.

Finally, some of the costs may have been justified, but with no evidence the Commission had no way to allow those costs. As a result, SourceGas could choose to file another request for an increase much sooner than would have been needed. As a result, if that occurs, ratepayers will again be responsible for costs that would not have been necessary had this case been supported by evidence.

MADE AND ENTERED at Lincoln, Nebraska this 9th day of March, 2010.

NEBRASKA PUBLIC SERVICE COMMISSION

BY:

Commissioner Anne Boyle