

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF SOUTH EASTERN INDIANA )  
NATURAL GAS COMPANY, INC. FOR )  
AUTHORITY TO CHANGE ITS RATES, )  
CHARGES, TARIFFS, RULES, AND )  
REGULATIONS; AUTHORIZATION OF THE )  
ISSUANCE OF LONG-TERM DEBT; AND )  
APPROVAL OF AN ALTERNATIVE )  
REGULATORY PLAN PURSUANT TO INDIANA )  
CODE § 8-1-2.5-6 FOR PURPOSES OF )  
IMPLEMENTING AN ENERGY EFFICIENCY )  
PROGRAM, ASSOCIATED FUNDING AND )  
DECOUPLING MECHANISMS, AND CHANGES )  
TO PETITIONER'S CALCULATION OF COSTS )  
FOR EXTENSION OF DISTRIBUTION MAINS )

CAUSE NO. 44128

APPROVED: NOV 7 2012

ORDER OF THE COMMISSION

**Presiding Officers:**

**James D. Atterholt, Chairman**

**Aaron A. Schmoll, Senior Administrative Law Judge**

On December 5, 2011, South Eastern Indiana Natural Gas Company, Inc. ("Petitioner") filed its Petition with the Indiana Utility Regulatory Commission ("Commission" or "IURC") seeking authority to change its rates, charges, tariffs, rules, and regulations; authority to issue long term debt; and approval of alternative regulatory plans to implement the Energy Efficiency Program and accompanying funding and decoupling mechanisms consistent with the Commission's Order in Cause No. 43995, and a separate plan to change Petitioner's current calculation used to determine costs to be recovered for the extension of distribution mains from its customers.

On January 6, 2012, in lieu of a pre-hearing conference order in this Cause, Petitioner and the Office of Utility Consumer Counselor ("OUCC"), (collectively, the "Parties"), jointly submitted a motion proposing an agreed test year, procedural schedule, and waiver of a pre-hearing conference, among other matters. On January 19, 2012, the Commission issued a docket entry establishing the test year and the procedural schedule in this Cause.

Pursuant to the proper notice, a public hearing was held on July 26, 2012, in Room 224 of the PNC Center, 101 West Washington Street, Indianapolis, Indiana. The Petitioner and OUCC were present and participated in such hearing, formally advising the Commission that they had reached a settlement in principle on all issues. No members of the general public appeared or sought to testify. Based on the Parties' request for additional time to reduce the settlement to writing and file the same with the Commission, this matter was continued to September 17,

2012. On September 7, 2012, the Parties pre-filed the Stipulation and Settlement Agreement (“Settlement”) and the settlement testimony of Duane C. Mercer, Kerry A. Heid, and Mark H. Grosskopf in support of such agreement. In addition, Petitioner filed its responses to the Commission’s docket entry of July 26, 2012.

On September 17, 2012, the Commission reconvened the hearing in this Cause. The Petitioner and OUCC appeared and offered into evidence their respective pre-filed testimony and exhibits, along with their respective settlement testimony and exhibits, and the Settlement (Joint Exhibit 1). The Parties waived cross-examination of all witnesses and all pre-filed evidence and exhibits were admitted into the record. No members of the public appeared or sought to participate therein.

The Commission having considered the evidence in this cause, including the provisions of the Settlement, and Petitioner’s response to the Commission’s docket entry, now finds as follows:

1. **Notice and Jurisdiction.** Due, legal, and timely notice of these proceedings was given and published as required by law. Petitioner is a public utility as defined in I.C. § 8-1-2-1. Petitioner is also an energy utility as defined in I.C. § 8-1-2.5-6. Thus, the Commission has jurisdiction over the Petitioner and the subject matter of this cause.

2. **Petitioner’s Characteristics.** Petitioner is a public utility, organized and existing under the laws of the State of Indiana. Petitioner provides natural gas service to customers in both rural and municipal areas in Dearborn and Ripley Counties, Indiana.

3. **Existing Rates, Test Year, and Relief Requested.** The Petitioner’s current base rates and charges are those established by this Commission on January 16, 2008 under Cause No. 43318-U. Based on a test year of July 31, 2011, as adjusted for changes fixed, known, and measurable and occurring within the 12 months following such date, the Petitioner proposes to change its base rates and charges. Through its case-in-chief, the Petitioner proposed to change its base rates and charges to increase its existing pro forma revenues by \$256,924 exclusive of the cost of gas. Petitioner proposes to allocate such increased revenue across the board to all customer classes and their respective current rates and charges. Petitioner also proposes to issue long term debt and to implement alternative regulatory plans for purposes of implementing an Energy Efficiency Program and a different distribution main extension calculation.

4. **Evidence of the Parties.**

A. **Petitioner’s Case-in-Chief.** Petitioner offered in its direct case-in-chief the testimony and exhibits of its witnesses Duane Mercer, Bonnie Mann, Earl Ridlen, Jason L. Wortman, Dr. John Boquist, and Kerry Heid. Mr. Mercer explained that he and his firm had been engaged to review Petitioner’s financial records and advise Petitioner on an appropriate level of revenue in light of its operating expenses and investment in utility plant. Mr. Mercer’s testimony indicates that Petitioner is not earning a reasonable rate of return on its investment and in fact is not earning the return authorized in Petitioner’s last rate case. Mr. Mercer suggested that Petitioner should be authorized to increase its rates and charges in order to produce an

additional \$256,924 in operating revenue exclusive of the cost of gas. Mr. Mercer noted this would result in an authorized net operating income of \$174,693 based on an 8.59% overall return on its existing rate base established through an original cost analysis of Petitioner's utility plant in service.

Ms. Mann offered testimony and exhibits describing and supporting the various pro forma adjustments to Petitioner's test year operating results that were used to establish Petitioner's requested revenue requirement in this case. Petitioner's witness, Mr. Ridlen, explained various adjustments to Petitioner's test year related primarily to various taxes required from the Petitioner. Petitioner's pro forma adjustments to current operating revenue and operating expenses included: an adjustment to eliminate Gas Cost Adjustment ("GCA") revenues; an adjustment to recognize unaccounted for gas; an adjustment to eliminate the cost of natural gas purchased from base rates; an increase in payroll; an increase in pension and 401(k) expenses; recovery of rate case expense; a recovery of expenses associated with the ARP in Cause No. 43995; a reduction for rebates associated with the Normal Temperature Adjustment ("NTA") that will become part of the Energy Efficiency Program ("EEP"); an estimated increase in outside services for future decoupling mechanism filing; an adjustment to cover the cost of increased postage; an adjustment for various insurance cost increases; an adjustment to remove charitable contributions; an adjustment in depreciation; and adjustments to recover the current IURC fee, appropriate bad debt expense, and various flow through taxes.

Petitioner also offered the testimony of its Vice President, Jason L. Wortman. Mr. Wortman described the overall change in rates Petitioner was seeking exclusive of the cost of gas. He also described Petitioner's request to issue long term debt. Mr. Wortman, along with Mr. Mercer, described Petitioner's request to implement the EEP and the associated funding and decoupling mechanisms in keeping with the Commission's order in Cause No. 43995. Finally, Mr. Wortman, along with Mr. Mercer, explained Petitioner's request for an alternative regulatory plan to change the calculation to be used in future cases of distribution main extensions.

Dr. Boquist described his review of the Petitioner, his analysis of a proxy group of regulated natural gas utilities, his opinion as to the current economic condition faced by the Petitioner, and his opinion as to Petitioner's cost of equity capital and a reasonable return on such equity investment. Dr. Boquist discussed risks faced by this Petitioner, including unique risks associated with its size, lack of marketability, and competition from alternative energy sources within its service territory.

Finally, Mr. Heid offered testimony and exhibits reflecting the allocation of Petitioner's proposed revenue requirement across the board to all Petitioner's current customers. Mr. Heid also offered testimony about the Energy Efficiency Rider ("EER") proposed for the Petitioner which would provide the Energy Efficiency Funding Component ("EEFC"), and the Sales Reconciliation Component ("SRC") as previously accepted by the Commission for this Petitioner and certain other gas utilities in Cause No. 43995.

**B. OUCC's Case-in-Chief.** The OUCC offered in its case-in-chief the testimony and exhibits of its witnesses OUCC analysts Mark Grosskopf, Heather Poole, Bradley Lorton, and Jon Dahlstrom. The OUCC accepted a number of Petitioner's proposals and

proposed revenue requirement adjustments. However, the OUCC also suggested different pro forma adjustments including: an adjustment to pro forma payroll and corresponding pension and 401(k) expense; an adjustment to rate case expense and the amortization period for its recovery; an adjustment to health, dental, and life insurance expenses; a change in the Alternative Regulatory Plan (“ARP”) expense associated with the EEP in Cause No. 43995, as well as the amortization period for its recovery; a change in the rebates formerly associated with the NTA to be associated with the EEP; a change in the estimated amount for future outside services associated with the decoupling mechanism; a change in test year professional fees; elimination of additional miscellaneous and administrative general expenses; a reduction in depreciation expense based on adjustments to Petitioner’s utility plant in service; a lower bad debt expense estimate; and adjustments to various flow through expenses, including taxes, the IURC fee, and bad debt expense based on pro forma revenue increases.

Mr. Grosskopf and Ms. Poole explained each of these different adjustments through their respective testimony and exhibits. Mr. Lorton testified Petitioner’s cost of equity and an appropriate return on its equity investment should be lower than that proposed by the Petitioner. Mr. Dahlstrom raised a number of questions about the application of Petitioner’s revenue requirement to its current rates and charges. Mr. Dahlstrom also objected to Petitioner’s proposed implementation of its EER and its main extension calculation.

**C. Petitioner’s Rebuttal.** In its rebuttal case, Petitioner offered testimony of its witnesses Mr. Mercer, Ms. Mann, Mr. Ridlen, Dr. Boquist, and Mr. Heid. Mr. Mercer initially focused his rebuttal on the OUCC’s position as to rate case expenses, both in the amount as well as the amortization period. Describing the actual expenses incurred in the Boonville Natural Gas rate case, Cause No. 43342, and the Indiana Utilities rate case, Cause No. 44062, Mr. Mercer disagreed with the OUCC’s position as to the amount of rate case expense. With respect to the amortization of such rate case expense, Mr. Mercer stated that this Petitioner is anticipating a return to the Commission for a base rate case in three or four years. Mr. Mercer also explained his disagreement with the OUCC’s adjustment to the Petitioner’s capital structure. He stated Petitioner’s capital structure did not include the debt referenced by the OUCC because such debt was paid off before Petitioner filed its case-in-chief. Mr. Mercer offered testimony in opposition to the OUCC’s proposed return on equity, focusing on the Commission’s decision and the OUCC’s testimony in the Westfield Gas case, Cause No. 43624. Mr. Mercer asserted that, unlike Westfield Gas, this Petitioner was not owned by a creditworthy parent and the current equity markets reflect that the economy has improved since that case. Finally, Mr. Mercer offered rebuttal testimony to the OUCC’s objections to Petitioner’s requested changes in the main extension calculation. He stated that the main extension calculation proposed by Petitioner is the same as that proposed by Indiana Utilities and Midwest Natural Gas in their recent proceedings.

Ms. Mann offered rebuttal testimony on various OUCC adjustments reflecting disagreement with the OUCC over rate case expense, amortization of rate case expense, payroll adjustments, adjustments to pension and 401(k) expenses, amortization of expenses associated with the ARP in Cause No. 43995, adjustments for future decoupling expenses, adjustments for professional fees, and adjustments for miscellaneous administrative and general expenses. Ms. Mann noted agreement with the OUCC as to adjustments for health, life, and dental expenses;

bad debt expenses; and adjustment for depreciation expense. Ms. Mann pointed out that a number of other adjustments proposed by the OUCC were necessitated by other particular operating expense adjustments the OUCC had proposed. Thus, Ms. Mann noted that payroll taxes, utility receipts taxes, federal and state income taxes, and working capital are different only because the OUCC used different operating expenses which in turn affected these various adjustments. She acknowledged that the methodologies used by the Petitioner and the OUCC on these adjustments were the same.

Mr. Ridlen described the content of engagement letters from London Witte Group in response to concerns raised by the OUCC. Mr. Ridlen discussed the ability of Petitioner's management's to review invoices from London Witte Group and maintained those invoices and the amount requested were reasonable in light of the alternative firms in the State of Indiana that offer similar accounting services.

Dr. Boquist offered testimony focused on the conclusions reached by the OUCC as to the return on equity. He stated that the OUCC's proposed 9.0% return on equity is well below that previously proposed for Westfield Gas in Cause No. 43624. He asserted various elements of risk that Petitioner is facing were different from the elements of risk of the proxy group. Dr. Boquist asserted that absent an adjustment for Petitioner's size, debt, and lack of a parent company as existed for Westfield Gas, the OUCC's recommendation in this Cause was too low. Dr. Boquist noted his disagreement with the OUCC's contentions regarding inflation, the effect of decoupling, and the OUCC's references to macro-economic trends. Dr. Boquist recommended the return on equity he originally proposed in Petitioner's case-in-chief.

Mr. Heid expressed a number of concerns to the proposals of the OUCC. Mr. Heid asserted the OUCC's proposal on avoided cost lacks support in Commission orders or other proceedings. He asserted that the proposed monthly customer service charge is similar to the monthly customer charge collected by other gas utilities operating in the State of Indiana. With respect to the EER, he suggested that such rider, which includes both the EEFC and the SRC, follow the conclusions previously reached by the Commission in Cause No. 43995. Finally, witness Heid noted that the main extension methodology proposed by this Petitioner is the same methodology being proposed by Indiana Utilities and Midwest Natural Gas.

**D. Settlement and Settlement Testimony.** Petitioner offered the settlement testimony of its witnesses Mr. Mercer and Mr. Heid. Mr. Mercer's settlement testimony explained that the Petitioner and the OUCC had reached an agreement as to all operating expense adjustments; all issues related to Petitioner's capital structure and the cost of Petitioner's capital; and all issues associated with the Petitioner's rate base as of the test year. Mr. Mercer noted that the Parties' Settlement was filed with this Commission as the Parties' Joint Exhibit 1. Finally, Mr. Mercer pointed out that he and his colleagues have prepared settlement schedules in the same format of the original schedules in this case which numerically describe the Settlement of the Parties as to all operating revenue, operating expense, rate base, and costs of capital for this Petitioner going forward.

Mr. Heid's settlement testimony and exhibits describe that the Parties have agreed on how Petitioner's increased revenue will be applied to Petitioner's customer classes and their

respective rates and charges. He noted the Parties' compromise includes an increase in the current monthly customer service charge for all customer classes. The proposed charge of \$11 for residential and general sales service customers, and \$28 for school transportation customers falls well within the range of similar charges collected by other national gas companies. Mr. Heid noted that Petitioner's current general service rate class will be separated into a residential rate class and a non-residential rate class to eliminate any confusion in the application of the EER, which will only apply to residential customers. The non-residential rate class will retain the general service designation. Mr. Heid's settlement testimony also noted that the rates and charges of the residential rate class and new general service (i.e., non-residential) rate class will be identical other than the elimination of the "Over 256 therm" rate block from the residential rate class. Mr. Heid also provided tariff language for the EER and the main extension calculation.

The result of the Parties' compromise indicates that Petitioner's current rates and charges should be changed in order to increase Petitioner's operating revenue by \$162,770 exclusive of the cost of gas. The Parties also agree Petitioner should be authorized to issue long term debt as originally requested; to implement an alternative regulatory plan for purposes of implementing the Energy Efficiency Program with its associated funding and decoupling mechanisms; and a separate alternative regulatory plan to change Petitioner's calculation associated with extending distribution mains.

In keeping with their compromise, the Parties have also reduced their Settlement to writing, Joint Exhibit 1. The Settlement indicates that the Parties have resolved all issues and specifically describes the resolution of a number of the issues for which they originally had disagreements. The Settlement also asks that this Commission accept and approve the settlement and base our final order in this case on the terms of such Settlement.

**5. Discussion and Findings.** Settlements presented to the Commission are not ordinary contracts between private parties. *United States Gypsum, Inc. v. Indiana Gas Co.*, 735 N.E.2d 790 (Ind. 2000). When the Commission approves a settlement, that settlement "loses its status as a strictly private contract and takes on a public interest gloss." *Id.* (quoting *Citizens Action Coalition v. PSI Energy*, 664 N.E.2d 401 (Ind. Ct. App. 1996)). Thus the Commission "may not accept a settlement merely because the private parties are satisfied; rather [the Commission] must consider whether the public interest will be served by accepting the settlement." *Citizens Action Coalition*, 664 N.E.2d at 406. Furthermore, any Commission decision, ruling, or order, including the approval of a settlement, must be supported by specific findings of fact and sufficient evidence. *United States Gypsum, Inc.*, 735 N.E.2d at 795. The Commission's own procedural rules require that settlements be supported by probative evidence. 170 I.A.C. 1-1.1-17(D). Therefore, before the Commission can approve the Settlement, we must determine whether the evidence in this cause sufficiently supports the conclusions that the Settlement is reasonable, just, and consistent with the purpose of Ind. Code ch. 8-1-2, and that such Settlement serves the public interest.

The Parties, through their respective pre-filed testimony and exhibits, have provided the Commission with substantial evidence supporting their original positions and their compromise offered through the Settlement in this Cause. The evidence recognizes the appropriateness of

adjusting Petitioner’s base rates to recognize various increased operating expenses, including: increases in payroll; increases in pension and 401(k) expense; increases in FICA taxes associated with payroll; adjustments to recover costs incurred by Petitioner in participating in Cause No. 43995; an adjustment to recover estimated costs associated with future filings regarding the decoupling mechanism that flow from our order in Cause No. 43995; adjustments to recognize that energy efficiency rebates will continue but be part of the EEP rather than the NTA; an adjustment to recognize the depreciation expense for Petitioner’s depreciable plant has increased due to changes in its utility plant in service; an adjustment to recognize the increase in postage; increases in insurance costs; increases in bad debt; decreases in the test year expense associated with professional fees; various miscellaneous and general expenses; deduction of synchronized interest from state taxes. The evidence also reveals that the Parties have agreed on rate case expense and its amortization because of this settlement. The Parties agreed to cost of capital and to Petitioner’s rate base as of its test year. The Parties also agreed to upward IURC fee adjustment as well as an update to the IURC fee for pro forma proposed revenue based on the current IURC fee.

Based upon the evidence of record, including the Petitioner’s direct and rebuttal cases, the OUCC’s direct case, and the settlement testimony including schedules and attachments, and the Parties’ Settlement, we find the Petitioner’s current rates and charges are insufficient. We, therefore, find that Petitioner should be authorized to increase its rates and charges in order to produce additional operating revenue net of the cost of gas of \$162,770 in order to provide the Petitioner with the opportunity of earning a net operating income of \$146,221 which reflects the opportunity to earn approximately 7.54% on Petitioner’s original cost rate base as of the test year of \$1,939,266, as shown in the table below:

<b>Revenue Requirement</b>	
<b>Description</b>	
<b>Rate Base</b>	\$ 1,939,266
<b>Times: Rate of Return</b>	7.54%
<b>Net Operating Income</b>	146,221
<b>Less: Adjusted Net Operating Income</b>	(49,890)
<b>Increase in Net Operating Income</b>	96,331
<b>Times: Revenue Conversion Factor</b>	1.6897
<b>Recommended Revenue Increase</b>	<u>\$ 162,770</u>
<b>Overall Percentage Increase</b>	<u>18.51%</u>

This represents an approximate 7.21% increase in Petitioner’s total revenues inclusive of gas costs and represents an approximate 18.51% increase in the non-gas portion of Petitioner’s operating revenues.

We further find that the Parties’ proposed allocation of this increased revenue to increased monthly customer charges and thereafter on an across-the-board basis to the volumetric rates of Petitioner’s customer classes is reasonable. We agree with the Parties that the separation of Petitioner’s existing general service rate class into a residential and non-

residential (new general service) rate class is reasonable and will allow Petitioner to more easily apply the EER, including the EEFC and the SRC. We also agree with the Parties that the elimination of the “Over 256 therm” block is reasonable for the new residential rate class. However, as we noted in *Indiana Utilities*, Cause No. 44062 (IURC September 5, 2012),

Petitioner must move towards straight-fixed variable rate pricing in order to continue implementing a decoupled rate design. This will require Petitioner to file a cost of service study in its next rate proceeding in order to increase the amount of fixed costs recovered through Petitioner’s customer charges. With the addition of the SRC to Petitioner’s rates, which reduces Petitioner’s risk in earning its authorized margins, we believe it is imperative for Petitioner to demonstrate that its rates are cost-based.

Further, as we noted in our investigation in Cause No. 43180, we encourage utilities to continue to move toward straight-fixed variable rate design, and the implementation of the SRC is a step in that direction.

We also agree that the Petitioner should be authorized to issue long term debt in an amount up to \$250,000 for a period of up to ten years at a fixed interest rate of up to 6.50%. We also find the Parties’ inclusion of Petitioner’s existing long term debt as of the end of the test year reasonable, in the amount reflected in Petitioner’s capital structure in Joint Exhibit 1. We further find that the Settlement is in the public interest, and as such, find that the Settlement should be approved, and will incorporate the attached Settlement as part of this Order.

Finally, the parties agree that the Settlement should not be used as precedent in any other proceeding or for any other purpose, except to the extent necessary to implement or enforce its terms. Consequently, with regard to future citation of the Settlement Agreement, we find that our approval herein should be constructed in a manner consistent with our finding in *Richmond Power & Light*, Cause No. 40434, (IURC March 19, 1997).

**IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION that:**

1. The Stipulation and Settlement Agreement, attached, is hereby approved.
2. Petitioner is authorized to increase its rates and charges in accordance with our findings in Paragraph 5 of this Order to produce an additional \$162,770 in annual revenue beyond that provided by Petitioner's current rates and charges.
3. Petitioner is authorized to implement the Energy Efficiency Program previously approved in Cause No. 43995, including the recovery of Petitioner's share of joint energy efficiency program costs and SRC recovery, subject to the terms of our final Order in Cause No. 43995 and in accordance with our findings in Paragraph 5 of this Order.
4. Petitioner is authorized to implement the alternative regulatory plan for main extension cost recovery in accordance with our findings in Paragraph 5, above.

5. Petitioner shall file with the Commission under this Cause, prior to placing into effect the rates and charges and Terms and Conditions for Gas Service authorized herein, tariff schedules set out in accordance with the Commission's rules for filing utility tariffs. Said tariffs, when filed by Petitioner and upon approval by the Commission's Natural Gas Division, shall cancel all present and prior rates and charges concurrently when said rates and charges herein are approved and placed into effect by Petitioner.

6. Petitioner is authorized to issue long term debt in the amount and on the terms found in Paragraph 5 above. Following the closing on such debt issuance, the Petitioner shall make a compliance filing with the Commission under this Cause concerning the final terms of such loan(s) within sixty (60) days after closing consistent with our findings in paragraph 5, above.

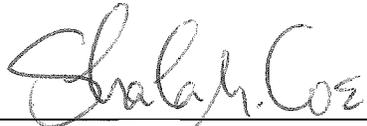
7. Petitioner shall file a cost of service study in its next base rate case.

8. This Order shall be effective on and after the date of its approval.

**ATTERHOLT, BENNETT, LANDIS, MAYS AND ZIEGNER CONCUR:**

**APPROVED: NOV 7 2012**

**I hereby certify that the above is a true  
and correct copy of the Order as approved.**



---

**Shala M. Coe**  
**Acting Secretary to the Commission**

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

PETITION OF SOUTH EASTERN INDIANA )  
NATURAL GAS COMPANY, INC. FOR )  
AUTHORITY TO CHANGE ITS RATES, )  
CHARGES, TARIFFS, RULES, AND ) CAUSE NO.: 44128  
REGULATIONS; AUTHORIZATION OF THE )  
ISSUANCE OF LONG-TERM DEBT; AND )  
APPROVAL OF AN ALTERNATIVE )  
REGULATORY PLANS PURSUANT TO INDIANA )  
CODE § 8-1-2.5-6 FOR PURPOSES OF )  
IMPLEMENTING AN ENERGY EFFICIENCY )  
PROGRAM, ASSOCIATED FUNDING AND )  
DECOUPLING MECHANISMS, AND CHANGES )  
TO PETITIONER'S CALCULATION OF COSTS )  
FOR EXTENSION OF DISTRIBUTION MAINS )

STIPULATION AND SETTLEMENT AGREEMENT

South Eastern Indiana Natural Gas Company, Inc., (hereafter "Petitioner") and the Indiana Office of Utility Consumer Counselor (hereinafter "OUCC") have, through their respective representatives, discussed the evidence of record and the potential for compromise of all issues in this cause. The result of such discussions between the Petitioner and the OUCC (hereinafter collectively the "Parties") is a settlement on all issues as described by this Stipulation and Settlement Agreement (hereinafter the "Settlement").

The Parties believe that the evidence of record supports the terms of this Settlement. The Parties acknowledge that the terms and conditions of this Settlement are a result of negotiations and compromise between the Parties relative to the position each has taken or would take in further proceedings in this Cause. In the interest of efficiency, saving the limited resources of the regulatory bodies involved, and recognizing the reasonableness of the results produced by this Settlement, the Parties herein stipulate and agree as follows:

1. **Rate Increase.** Based on the test year ending July 31, 2011, as adjusted for matters that are fixed, known, and measurable, and occurring within 12 months of the test year, Petitioner proposed in its direct case filed January 20, 2012, that its operating revenue should be increased exclusive of the cost of gas by \$256,924. The OUCC proposed in its direct case filed May 17, 2012, that operating revenue be increased by \$103,091 exclusive of the cost of gas. The Parties now agree that Petitioner should be authorized to increase its base rates and charges for purposes of natural gas service to its various customers to produce additional annual operating revenue, exclusive of the cost of gas, by \$162,717. This represents an increase of approximately 7.21% over adjusted test year operating revenue, including the cost of gas.

2. **Proforma Adjustments.** Petitioner proposed in its direct case various adjustments to its test year results as set forth numerically in Petitioner's Exhibit DCM-1, Exhibit C, and accompanying schedules. The pro forma adjustments were further described by Petitioner's witnesses Mercer, Mann and Ridlen. The proposed pro forma adjustments related to both operating revenue and operating expenses, and included: adjustments to eliminate revenues recovering gas commodity costs and the cost of natural gas purchased from base rates; adjustment to revenue to recognize unaccounted for gas; an increase in payroll, net of amount capitalized; flow through changes to pension and 401(k); recovery of rate case expense; recovery of expenses associated with an alternative regulatory plan (ARP) where Petitioner and other utilities requested an Energy Efficiency Program (EEP) in Cause No. 43995; reduction for rebates associated with the NTA that will become part of the EEP going forward; estimated increase in outside services for decoupling (decoupling expenses); changes in the IURC fee; increase in postage; increases in various insurance costs; removal of charitable contributions; increase in depreciation relative to an increased utility plant in service; recovery of appropriate

bad debt expense; recovery of increased FICA taxes due to payroll increases; reduction in property tax; and recovery of various other taxes that are associated with and flow from Petitioner's proposed increased revenue, including utility receipts tax, state income tax, and federal income tax. Petitioner also sought to establish the value of its rate base; and the elements of and costs associated with its capital structure.

With the filing of the OUCC's case-in-chief on May 17, 2012, the OUCC suggested different adjustments relating to various proposals described in Petitioner's direct case-in-chief, including those related to payroll and corresponding pension and 401(k) expense; rate case expense and the amortization period for its recovery; health, dental and life insurance expenses; a reduction in the EEP expense and a change in the amortization period for its recovery; a different reduction for the rebates formerly associated with the NTA to be associated with the EEP going forward; a different estimated amount for outside services associated with decoupling expenses; a lower bad debt expense estimate; a change to accrued professional fees; elimination of miscellaneous administrative and general expenses; a reduction in depreciation expense based on suggested adjustments to utility plant in service; and the corresponding impact of these different adjustments and changes on various flow through taxes such as payroll tax, utility receipts tax, state income tax, and federal income tax; as well as other flow through pro forma proposed rate adjustments such as the IURC fee and bad debt expense. Through negotiation and compromise, the Parties have resolved all of these pro forma differences and stipulate to the following pro forma adjustments:

**Payroll Expense.** The Petitioner, as part of its direct case, proposed to adjust its test year operation and maintenance expenses for purposes of annualizing increases in payroll net of the

amount of payroll capitalized by \$13,128. The OUCC, following its review of Petitioner's books and records and Petitioner's responses to both formal and informal discovery, suggested Petitioner's payroll recovered in rates should be reduced by (\$17,091) to account for a reduction of what the OUCC described as unsupported bonus payments; and the appropriate allocation of the payroll costs of one employee shared with an affiliated entity. Following further exchange of information, including recognition of capitalized payroll, the Parties have compromised on pro forma payroll and agreed to an upward payroll adjustment of \$378 as reflected in the Settlement Schedule C-1, Adjustment 3(a).

**Pension and 401(k) Expense.** The Petitioner initially proposed in its direct case that the flow through effect of its payroll adjustment would be an increase in pension expense of \$1,313 and an increase in 401(k) contributions of \$330. With the agreed payroll expense reflected above, including the reallocation of the expense of a shared employee, the Parties now agree that the appropriate flow through pension expense is an upward adjustment of \$3,063 and the appropriate 401(k) expense is an upward adjustment of \$818 as reflected on Revised Schedule C-1, Adjustment 3(b) and 3(c).

**FICA.** As with pension expense, FICA expense is a flow through expense based on annual payroll expense. The Parties have agreed to the method of calculation and the appropriate tax rate. With the

above changes in payroll, the Parties agree that Petitioner's pro forma FICA expense should be adjusted upward by \$2,342 as reflected on Settlement Schedule C-1, Adjustment 6(a).

**ARP Expenses Associated with EEP.** The Petitioner proposed recovery of its cost in participating with other small gas utilities in the ARP initiated to establish the EEP, along with funding and decoupling mechanisms. Such ARP was filed under Cause No. 43995 and resulted in an order from the Commission on November 30, 2011. Petitioner's proposal was to recover its actual costs incurred, using a three year amortization period by way of an upward adjustment to its test year operating expenses. Petitioner's adjustment provides for the annual recovery of \$4,600. While agreeing that recovery was appropriate, the OUCC used a slightly lower amount based upon the estimated costs described in Cause No. 43995 and the OUCC's belief that a seven year amortization period was more appropriate. Following discussion, the Parties agree to compromise this issue by using the estimated costs described in Cause No. 43995 as the appropriate amount to be recovered, and that an amortization period utilizing five years, similar to the amortization period for rate case expense recovery, is a reasonable compromise. The resulting adjustment agreed to by the Parties is an upward adjustment of \$2,730 reflected on Settlement Schedule C-1, Adjustment 4(C).

**Rebates to be Included in EEP.** The Petitioner in its direct case proposed to remove (\$3,100) from test year operating expenses because such expenses were to be incurred in the future through the EEP, rather than the NTA. Following its review of Petitioner's books and records, the OUCC suggested that Petitioner's actual test year expense for rebates under the NTA which are to be transferred to the EEP was (\$3,127), and thus suggested that this amount be removed from the test year. The Parties agree on a downward adjustment of (\$3,127) to the test year as reflected on Settlement Schedule C-1, Adjustment 4(D), because such rebates will be included in the EEP and its associated funding mechanism described below as part of the Energy Efficiency Rider.

**Decoupling Expenses.** The Petitioner described future filings that this Petitioner will be required to make as part of the EEP as required under Cause No. 43995. Petitioner's witnesses estimated an initial cost, requiring an adjustment to test year expenses of \$3,250. The OUCC proposed a different adjustment, \$1,934, based upon its belief that Petitioner would be sharing reporting and regulatory costs in any future filings with other small gas utilities. Following discussion among the Parties, the OUCC agrees that some costs will be incurred and relate solely to work that will be required of this Petitioner. The Parties have agreed that

Petitioner's test year should be adjusted upward by \$3,250 as reflected in Settlement Schedule C-1, Adjustment 4(E).

**Depreciation Expense.** The Petitioner, in its direct case, proposed an upward adjustment to annual depreciation expense for its depreciable plant in the amount of \$12,494. The OUCC proposed a recalculated depreciation expense following the OUCC's suggested adjustments to Petitioner's utility plant in service to eliminate those assets of Petitioner's utility plant that were replaced or fully depreciated. Through its rebuttal testimony, Petitioner indicated its agreement with the OUCC's position as to changes in Petitioner's utility plant in service with respect to depreciable assets. Therefore the Parties agree that depreciation expense should be adjusted upward in the amount of \$5,423 as reflected on Settlement Schedule C-1, Adjustment 5.

**Postage.** Petitioner's direct case-in-chief proposed to adjust its postage expense upward to reflect an increase in the postage rates. The OUCC indicated it had reviewed the adjustment and had no objections. Therefore, the Parties have agreed to an upward postage adjustment of \$280 as reflected in Settlement Schedule C-1, Adjustment 4(F).

**Insurance Costs.** In its direct case, Petitioner proposed upward adjustments for various insurance expenses, including an adjustment of \$1,065 to cover the increased cost of property,

workers' compensation, casualty, and general liability insurance coverage. Petitioner also proposed an upward adjustment of \$4,090 to reflect the increase in health, life, and dental insurance coverage. The OUCC indicated no objection to Petitioner's property, workers' compensation, casualty, and general liability insurance test year expenses or adjustments. However, the OUCC proposed a different adjustment for health, life, and dental insurance coverage, both as to test year expenses and pro forma adjustments. The result of the OUCC's adjustment is an upward adjustment of \$4,010. The Parties agree that Petitioner's proposed upward adjustment of \$1,065 and the OUCC's proposed upward adjustment of \$4,010 should be used in this cause for various increased insurance costs as reflected on Settlement Schedule C-1, Adjustments 4(A) and (B).

**Bad Debt.** The Petitioner proposed to increase its test year operating expenses based on a three year average of bad debt expense. The OUCC agreed with this methodology but proposed an updated three year average. The Parties have agreed that the OUCC's update is appropriate. Accordingly, bad debt expense should be adjusted upward by \$2,040. In addition, the Parties are in agreement that with the increase in revenue to Petitioner following the Commission's order in this cause, an additional increase of \$578 based on a current effective rate of 0.003553 is

appropriate. Such adjustments are reflected in Settlement Schedule C-1, Adjustment 4(H) and Settlement Exhibit (C), respectively.

**Professional Fees.** The Petitioner proposed no adjustment to professional fees in its case-in-chief. The OUCC proposed a downward adjustment of (\$1,954) in professional fees based upon its belief that the Petitioner in its test year had accrued certain professional fees which ultimately were not incurred. The Parties have now agreed to the OUCC's downward adjustment as reflected on Settlement Schedule C-1, Adjustment 4(i).

**Miscellaneous Administrative and General Expense.** The Petitioner proposed to remove certain administrative and general expenses to eliminate charitable contributions from test year operating expenses (\$26,150) as reflected in its direct case-in-chief, Schedule C-1, Adjustment 4(g). In addition to this amount, the OUCC proposed to adjust additional expenses for lobbying dues, holiday gifts, penalties or fines in the amount of (\$806). The Parties have now agreed to both adjustments as reflected on Settlement Schedule C-1, Adjustments 4(g) and (j).

**Taxes.** In its direct case-in-chief, the Petitioner indicated that various taxes would be required to be paid by Petitioner, with the specific amounts to be calculated based on the impacts from various elements of Petitioner's revenue requirement. The OUCC

agreed with Petitioner's description of the flow through nature of such taxes and also agreed with Petitioner's method of calculating pro forma taxes with the exception of the need to deduct synchronized interest from the state income tax expense calculation. The Parties agree that synchronized interest should be deducted from the state tax calculation and that the various taxes required of Petitioner are those reflected on the Settlement Schedules C-1 and C-2. The Parties indicate that it is their belief that these taxes are reasonable and should be included in the Commission's final order, using the same method of calculation used by the Parties and as reflected in the Settlement Schedules.

**Rate Case Expense and Amortization.** The Petitioner, in its direct case, proposed recovery of \$201,500 in rate case expense over four years in recognition of the expected time period these rates will be in effect. The OUCC proposed rate case expense of \$131,500 amortized over seven years. The Parties have now agreed, in light of the settlement of this particular case, that recovery of \$171,500 in rate case expense amortized over five years is a reasonable compromise of their respective positions as reflected on Settlement Schedule C-1, Adjustment 3(d). Petitioner has also agreed to change its rates in the future for purposes of eliminating this amortization following five full years of recovery if a new rate case has not been filed.

**IURC Fee.** The Petitioner proposed to increase its test year IURC fee expenses based on the current IURC fee of 0.11785100. The OUCC indicated it had reviewed the adjustment, but had no objections. Therefore, the Parties have agreed to an upward IURC fee adjustment of \$46 as reflected on Settlement Schedule C-1, Adjustment 3(e). In addition, the Parties also agreed to update the IURC fee for pro forma proposed revenue based on the current IURC fee rate of 0.11785100 as reflected on Settlement Schedule C-2, Adjustment (B).

3. **Rate Base.** In its direct case-in-chief, the Petitioner proposed a rate base calculated using the original cost of Petitioner's used and useful plant in service as of July 31, 2011, in the amount of \$3,672,540 less accumulated depreciation of (\$1,735,845) resulting in a net utility plant in service of \$1,936,695. Adding funds for working capital and materials and supplies, the Petitioner in its case-in-chief proposed a total original cost rate base of \$2,033,682. The OUCC indicated that its review suggests that Petitioner's utility plant in service value should be reduced to reflect the replacement of certain elements of plant and the complete depreciation of other elements. The OUCC recommends Petitioner's used and useful utility plant as of July 31, 2011, should include an additional adjustment for the removal of replaced meters or complete depreciation of (\$90,253) resulting in a net utility plant in service of \$1,846,442. The Petitioner has agreed to the OUCC's recommendation on utility plant in service. Based on the agreement of the Parties as to various operating expenses, the Parties also agree that the working capital component of Petitioner's rate base for purposes of setting rates should be \$74,182. They further agree that the materials and supplies component should be \$18,635. The result of the Parties'

settlement of these different issues of Petitioner's rate base is that the Parties now agree that Petitioner's rate base calculated on an original cost basis as of July 31, 2011, is \$1,939,259 as reflected on Settlement Exhibit D. The Parties also agree that this agreed original cost rate base should be used to determine an appropriate pro forma net operating income for this Petitioner.

4. **Cost of Capital.** The Petitioner, through its direct case, and the OUCC, through its direct case, each proposed a capital structure generally using the same elements. The only area of initial disagreement related to the OUCC's proposal to include existing long term debt in the capital structure since such debt had not been paid off as of the test year end. The Petitioner has agreed, through this Settlement, that \$158,290 of existing long term debt for its office building should be included in its capital structure at an interest rate of 6.25%. The Parties are in agreement that the remaining elements of the capital structure include common equity in an amount of \$1,863,291, new long term debt in the amount of \$250,000, customer deposits in the amount of \$121,460, and deferred tax in the amount of \$512,874. With respect to the costs of those other elements, the only initial disagreement related to the appropriate return on equity to be included in this capital structure. Originally, Petitioner proposed 10.89% as a return on equity. The OUCC proposed 9.00%. Following negotiations among the Parties, they have agreed that 10.10% represents an appropriate compromise return in recognition that all issues of this case have been settled by this Settlement. In light of the agreement of the Parties, the Parties believe the following table accurately reflects their agreement as to the Petitioner's capital structure and its various costs:

Description	Amount	Percent of Total	Cost	Weighted Cost
Common Equity	\$1,863,291	64.12%	10.10%	6.4762
New Long Term Debt	\$250,000	8.60%	5.50%	0.4732%
Existing Long Term Debt	\$158,290	5.45%	6.25%	0.3404%
Customer Deposits	\$121,460	4.18%	6.00%	0.2508%
Deferred Taxes	\$512,874	17.65%	0.00%	0.0000%
Total	\$2,905,915	100%		7.541

5. **Pro Forma Net Operating Income.** Based upon the agreement of the Parties as to Petitioner's rate base and Petitioner's cost of capital; and recognizing the Parties' agreement as all other elements of Petitioner's revenue requirements; the Parties agree the Petitioner should be authorized to earn 7.541% on its invested original cost rate base of \$1,939,259, thus authorizing Petitioner the opportunity to earn a net operating income of \$146,220.

6. **Cost of Service/Tariffs.** The Petitioner, in its direct case, proposed to allocate its revenue requirement across the board to all rates and charges. The OUCC, in its direct case, suggested that allocation across the board would be acceptable if Petitioner did not change the monthly customer service charge. Following extensive discussions among the Parties about Petitioner's current rate classes; a desire by the Parties to promote the EEP and encourage energy efficiency; and in recognition that Petitioner's residential customers do not typically reach the third block of the general service (GS) tariff used for both residential and commercial customers; the Parties have agreed that Petitioner should separate the current rate GS into a separate residential (RS) and a non-residential general service class which would include all other

customers (GS), with the RS rate including two blocks and the GS rate including three blocks. The Parties also recognize that Petitioner has no current customers under its School Transportation Service (STS). The Parties further agree that an increased monthly customer service charge is appropriate, but that the increases proposed by Petitioner should be reduced to \$11 for residential customers, \$11 for commercial customers, and \$28 for School Transportation Customers. Finally, the Parties agree that the remainder of the revenue requirement not anticipated to be collected through the monthly customer service charge should be allocated to both residential and commercial classes on an across the board volumetric basis. The Parties' agreements as to the appropriate allocation of its cost of service are reflected in Settlement Tariff KAH-4.

As part of its direct case, the Petitioner also proposed an Energy Efficiency Rider to initially implement an Energy Efficiency Funding Component (EEFC) of 83¢ per month per residential customer for purposes of funding its EEP and to implement a Sales Reconciliation Component (SRC) for all residential customers as its decoupling mechanism. Both the EEFC and the SRC flow from this Commission's order in Cause No. 43995. Following discussions with the Petitioner, the OUCC now agrees that the EEFC and the SRC should be implemented as proposed. The tariff the Parties propose be used to implement the EEFC and the SRC is as set forth in the language of Petitioner's settlement tariff KAH-4.

Finally, the Petitioner proposed that its current tariff be changed in order to mirror the existing Fountaintown tariff (except for the implementation of the EEFC and SRC which currently do not exist in the Fountaintown tariff but by prior agreement will in the future) due to the fact that this Petitioner is managed by the same officers who manage Fountaintown Gas. The

OUCG has indicated it has no objections to changing Petitioner's tariff in keeping with the tariff on file for Fountaintown Gas.

7. **Main Extension Policy.** The Petitioner, in its case-in-chief, proposed an alternative regulatory plan to change the calculation for main extensions from one involving gross revenue to one involving margin revenue. Petitioner also proposed that the three year average of revenue be changed to a six year average. The OUCG has indicated it has reviewed Petitioner's proposal and following further discussions with Petitioner, agrees that the main extension should be calculated on margin revenue and should use a six year period instead of a three year period. The Parties agree that the settlement tariff, KAH-4, appropriately describes the agreed main extension policy that this Petitioner should use following a final order from the Commission in this cause.

8. **Long Term Debt.** The Petitioner, in its case-in-chief, requested authority from this Commission to enter into new long term debt. The OUCG has indicated no objections to this request and both Parties have included new long term debt in the capital structure in this Settlement. The Parties agree that the Petitioner should be authorized as requested in its case-in-chief to issue long term debt in an amount up to \$250,000 for a period of up to ten years at a fixed interest rate of up to 6.5%. The Parties further agree that the Petitioner should report to the Commission, with a copy to the OUCG, on the final terms of any loan obtained through this authority within 60 days following the closing on such loan.

9. **Request for Prompt Approval by the Commission.** The Parties acknowledge that a significant motivation for the Petitioner to enter into this Settlement is the expectation that a final order will be issued promptly by the Commission authorizing increases in its rates and charges as reflected herein. The Parties have spent significant time and effort to resolve the

issues raised in this case. However, the Parties also recognize the insufficiency of Petitioner's current rates, as reflected by the prefiled evidence. Under these circumstances, the Petitioner requests prompt approval of this Settlement by way of a final order of the Commission.

10. **Sufficiency of the Evidence.** The Parties believe that the Petitioner's direct testimony and exhibits, the OUCC's direct testimony and exhibits, the Petitioner's rebuttal testimony and exhibits, the Parties' settlement testimony and exhibits, along with this Stipulation and Settlement Agreement, constitute substantial evidence sufficient to support this Settlement and provide an adequate evidentiary basis upon which the Commission may make findings of fact and conclusions of law necessary to issue a final order adopting and approving this Settlement.

11. **Settlement Effect, Scope, and Approval.** The Parties acknowledge and agree as follows:

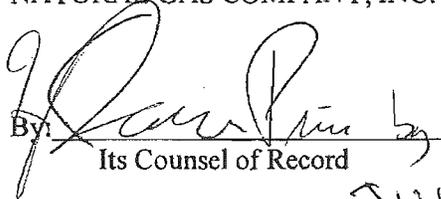
- (a) This Settlement is conditioned upon and subject to its acceptance and approval by the Commission in its entirety without change or condition that is unacceptable to any party. Each term of the Settlement is in consideration and support of each and every other term.
- (b) This Settlement is the result of compromise by the Parties within the settlement process. Neither the making of this Settlement nor any of the individual provisions or stipulations herein shall constitute an admission or waiver by any Party in any other proceeding; nor shall they constitute an admission or waiver in this proceeding if the Settlement is not accepted by the Commission.

The Parties hereto shall not use this Stipulation or the Order provided by this Stipulation as precedent or offer the same as an admission in any other proceeding or for any other purpose except to the extent necessary to implement or enforce its terms. In the event this Stipulation or resulting Order is offered for any purpose prohibited by this Agreement, the Parties agree that objections by the non-offering party are proper.

- (c) The communications and discussions among the Parties, along with the materials produced and exchanged during the negotiation of this Settlement, relate to offers of settlement and compromise, and as such, all are privileged and confidential. Such material cannot be used in this or any other proceeding without the agreement of the Parties herein.
- (d) The undersigned represent and agree that they are fully authorized to execute this Settlement on behalf of their designated clients who will thereafter be bound by this Settlement.
- (f) The Parties hereto will either support; or not oppose on rehearing, reconsideration, and/or appeal; an IURC order accepting and approving this Settlement in accordance with its terms.

Accepted and agreed this 7<sup>th</sup> day of September, 2012.

SOUTH EASTERN INDIANA  
NATURAL GAS COMPANY, INC.

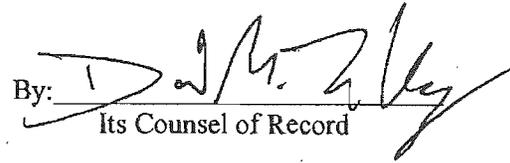
By:   
Its Counsel of Record

2194723\_11.

J.W.H.

Attorney No. 28660-29

INDIANA OFFICE OF UTILITY  
CONSUMER COUNSELOR

By:   
Its Counsel of Record