

Request for Expressions of Interest  
City of Philadelphia – Philadelphia Gas Works  
Question Answer for the REI  
May 24, 2013

1. How much debt is currently outstanding under each of the PGW Ordinances (1975 and 1998)? Does the City have any plans to issue additional bonds under the 1975 Ordinance?

*The par amount of bonds outstanding under each of the PGW General Ordinances is presented in the table below.*

<b>PGW</b>	
<b>Bonds Outstanding by Ordinance</b>	
<i>as of June 1, 2013</i>	
<u><b>Ordinance</b></u>	<u><b>Bonds Outstanding</b></u>
1975 General Ordinance (Senior)	\$185,890,000
1998 General Ordinance (Subordinate)	\$907,550,000
	<u>\$1,093,440,000</u>

*In the 1998 General Ordinance, the City covenanted that it would not issue any additional bonds under the 1975 General Ordinance except to refund outstanding 1975 Ordinance Bonds.*

2. Is there an update available to the 6/15/11 Black & Veatch Engineering report?

*No, but the City has released an RFP to procure this service and expects to have a new report in time for the Capital Projects Commercial Paper Program.*

3. The last B&V report described the physical plant & equipment as being in “good” shape.

*The last B&V report stated the following on page 3 of their letter – “PGW is a competently managed and operated gas distribution utility. PGW and the System are organized, operated, and maintained at a level equal to or in excess of, regulatory requirements and generally accepted industry practices. The System is in good operating condition.*

4. In terms of PGW’s infrastructure and their replacement schedule for the cast iron pipes, is the company maintaining, gaining, or falling behind?

*PGW has a cast iron main replacement program that is focused on removing 18 miles of cast iron main from service per year. PGW recently started an accelerated cast iron main replacement program to remove additional miles of cast iron main from service per year. This additional program will be funded by a Distribution System Improvement Charge (DSIC) estimated to be approximately \$22.0 million per year. The DSIC charge will be implemented in July 2013.*

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5. What is PGW's line loss ratio? (Difference in what is metered at the City gate versus what is metered at the customer).

*PGW's line loss charge for the last three fiscal years was FY 2010 - 2.9%, FY 2011 - 3.3%, FY 2012 – 3.2%*

6. What is the average age of PGW's capital assets?

*PGW's depreciation rate is approximately 2.3%. This would approximate an average of 43.4 years for assets subject to depreciation.*

7. How much in capital expenditures are planned for the next five years? Is it \$500 million or \$100 million per year?

*Capital expenditures are estimated to be approximately \$100.0 million per year, ranging from \$94.0 million to \$106.0 million.*

8. As new debt is issued, when will PGW need to raise rates in order to remain in compliance with their rate covenant?

*PGW does not have a rate increase projected in its most recent five year forecast ending in August 2018.*

9. How does PGW compare with other natural gas retailers in terms of their efficiency ratios: gross margin, net income, etc?

*PGW does not have information related to its peers. PGW's information for the fiscal year ended 2012 is located on its website at [www.pgworks.com](http://www.pgworks.com).*

10. How does PGW compare to their peers in terms of OPEB and pension liabilities?

*PGW does not have information related to its peers. PGW's information for the fiscal year ended 2012 is located on its website at [www.pgworks.com](http://www.pgworks.com).*

11. Can you please provide the annual management letter from the auditor on internal controls?

*Answer is attached below.*

12. Can you please provide an updated mark to market on the Gas Works interest rate swaps?

*As of April 30, 2013, PGW's swaps had the following marks-to-market:*

*8<sup>th</sup> B – (\$11,974,851)  
8<sup>th</sup> C – (\$11,912,625)*

Request for Expressions of Interest  
City of Philadelphia – Philadelphia Gas Works  
Question Answer for the REI  
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*8<sup>th</sup> D – (\$17,869,231)*  
*8<sup>th</sup> E – (\$11,974,851)*

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**Answer to Question 11**

**Census Data for Actuarial Valuations**

Reference Number: 2012-01

Observation:

The Company experienced issues and delays relating to their census data being provided to the third-party actuaries for use in developing their OPEB valuation estimates and as a result caused delays for the KPMG engagement team in performing the requisite audit procedures over these estimates. Specifically, the issues and delays related to 1) instances where employees were missing from both the active and the retired files - due in part to a lag between when each file was produced and sent to the third party actuary; 2) instances of duplicate employees being contained within a given population - due to several factors including both the active & retired employee numbers being included and former employees who are also surviving spouses of other former employees being double-counted for OPEB benefits; and 3) instances of employees being included in the files received from the third party actuary who were not included on files provided to the engagement team directly from the client.

Recommendation:

We recommend the Company develop policies and procedures to ensure the consistency and integrity of the census data being provided to the third party actuary utilized to develop the valuation estimates and subsequently retained as support for such estimates.

Management Response:

PGW agrees with the recommendation and will develop the suggested policies and procedures for future census data compilations and transfers.

**Bank Reconciliations**

Reference Number: 2012-02

Observation:

As a result of our audit procedures over cash and cash equivalents, KPMG noted certain bank reconciliations were not prepared and/or reviewed in a timely manner as defined in the Company's internal control / process documentation. Specifically, certain bank account reconciliations were not completed until November, which exceeds the control stated deadline of 45 days after month-end, in this example, month-end being August 31.

Recommendation:

We recommend management review the bank reconciliation control documentation and reiterate the control process within operations and the accounting departments responsible for the execution of the control.

Management Response:

PGW accepts this recommendation. PGW will conduct periodic meetings, at least quarterly, involving the Treasury Department and the Accounting and Reporting Department to identify and address reconciling items to comply with PGW's control standard.

Request for Expressions of Interest  
City of Philadelphia – Philadelphia Gas Works  
Question Answer for the REI  
May 24, 2013

**Construction Work in Process**

Reference Number: 2012-03

Observation:

As part of KPMG's audit procedures over the classification of utility plant assets as under construction versus in service, we observed delays of several months between the documented completion of certain projects (as evidenced by signed Capital and Special Job Authorization project summaries) and the accounting entries to move the project from under construction to in-service, triggering depreciation on the project and related capital assets. We identified \$22.8 million related to 107 projects that remained in CWIP at year-end although the projects had no spending in fiscal 2012.

Recommendation:

We recommend the Company develop policies and procedures to ensure the accuracy and timeliness of the recording of completed capital asset projects from under construction to in use through management review of all projects in service.

Management Response:

PGW accepts this recommendation. Accounting and Reporting Departmental management personnel will review monthly reports to ensure the oldest completed projects are transferred to in-service in a timely manner.

**Revenue Bonds**

Reference Number: 2012-04

Observation:

The Company entered into multiple transactions in September 2011 related to the remarketing, refunding and defeasance of certain Revenue Bonds. The Company inadvertently omitted required disclosure regarding the economic gain or loss upon the refunding of the Sixteenth Series, First Series A, First Series C, Second Series, and Third Series Bonds.

Recommendation:

We recommend the Company develop policies and procedures to ensure that all future transactions related to the Company's Revenue Bonds are reviewed to ensure that they are appropriately accounted for and accurately disclosed by the Company. This includes any impact to the derivative instruments hedging the variable interest rate of the Eighth Series Revenue Bonds.

Management Response:

PGW accepts this recommendation and will develop policies and procedures to ensure that all future transactions related to the Company's Revenue Bonds are reviewed to ensure they are appropriately accounted for and accurately disclosed by the Company.

Request for Expressions of Interest  
City of Philadelphia – Philadelphia Gas Works  
Question Answer for the REI  
May 24, 2013

**Information Technology – Passwords and System Access**

Reference Number: 2012-05

Observation:

The default passwords for the following default database users specific to the Oracle Financials production database were not changed: apps, applsys, po, ap, and gl. This creates a risk such that user ID's may be used anonymously without creating an audit trail.

In addition, KPMG noted there is no process in place to regularly change the passwords for the SYS and SYSTEM accounts in the BCCS and Oracle Financials databases. KPMG noted that the passwords were updated on the below dates:

- Oracle Financials database: SYS and SYSTEM last updated on 5/29/2010
- BCCS database: SYS last updated on 7/9/2007 and SYSTEM last updated on 10/28/2004.

KPMG noted that the passwords to these accounts are shared amongst all Database Administrators (DBAs), as such all DBAs terminated since the last update date still have knowledge of the passwords to these powerful database IDs.

One BCCS database user (LSPIEGEL) is assigned to the DEFAULT profile, which is intended for system/service accounts. As such, no password requirements are applied to the user's account.

Lastly, KPMG noted that no minimum length requirements are enforced by the BCCS database and, therefore, do not meet the requirements set forth in the Company's Password Policy for End Users document.

We noted the existence of a compensating control in that in order to gain access to the Oracle and BCCS production database, a user must first authenticate to the PGW network.

Recommendation:

We recommend the Company determine whether password parameters are appropriate, and ensure its formal policies reflect its actual practices.

Management Response:

PGW accepts this recommendation. Information Services will review actual practices to ensure that they are in compliance with formal password policies.

**Information Technology – Test Documentation**

Reference Number: 2012-06

Observation:

KPMG noted that, although test script documentation existed for all selected tests, there were inconsistencies in the manner in which tests were documented and completed. Specifically, KPMG noted multiple instances wherein documentation did not contain adequate testing procedures, expected/intended results, and/or actual results of testing (e.g. screenshot, report, reconciliation, verbiage, etc.). System changes that are not adequately tested could negatively impact the production environment, thereby adversely affecting the integrity of financial data. Additionally, changes may not satisfy business requirements and/or may result in unintended consequences including the inability to identify issues/defects typically found during testing.

Recommendation:

We recommend the Company ensure consistency in the manner in which testing procedures, expected results, and actual results are adequately documented.

Request for Expressions of Interest  
City of Philadelphia – Philadelphia Gas Works  
Question Answer for the REI  
May 24, 2013

Management Response:

During the upgrade project in excess of 2,500 test scripts were executed. All were documented with the tester name, date of script execution and the test results. Each test iteration was reviewed and signed off by the module leads (PGW and contractor) and project managers (PGW and contractor). In signing they attested to the completeness and accuracy of the test results. At the completion of the final iteration, user acceptance testing, module leads and managers, in addition to attesting to the completeness and accuracy of the test results, signed that the system was ready for go-live.

Data validation was ensured by the execution of “data validation reports” prior to system upgrade and after system upgrade. The results of the reports were documented and the results verified to ensure data accuracy and data integrity.

PGW does not agree that the system was not adequately tested or that the integrity of the data was not ensured by PGW. PGW does agree that in future Oracle upgrades we will endeavor to provide documentation as noted in the observation to the maximum that is feasible.