Exhibit No.:
Issues: *Revenue Requirements*
Affiliate Transactions
Witness: *Amanda C. McMellen*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Surrebuttal Testimony*
Case No.: *GR-2014-0086*
Date Testimony Prepared: *August 8, 2014*

MISSOURI PUBLIC SERVICE COMMISSION

REGULATORY REVIEW DIVISION
UTILITY SERVICES -AUDITING

SURREBUTTAL TESTIMONY

OF

AMANDA C. MCMELLEN

SUMMIT NATURAL GAS OF MISSOURI, INC.

CASE NO. GR-2014-0086

Jefferson City, Missouri
August 2014

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AMANDA C. MCMELLEN

SUMMIT NATURAL GAS OF MISSOURI, INC.

CASE NO. GR-2014-0086

Q. Please state your name and business address.

A. Amanda C. McMellen, 200 Madison Street, Suite 440, Jefferson City, MO 65102.

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

A. I am employed by the Missouri Public Service Commission ("Commission") as a Utility Regulatory Auditor V.

Q. Are you the same Amanda C. McMellen who has filed direct testimony, rebuttal testimony and portions of the Missouri Public Service Commission Staff's ("Staff") Cost of Service Report in this case?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my testimony is to address the rebuttal testimony of Summit Natural Gas of Missouri, Inc. ("SNG" or "Company") witness Tyson D. Porter concerning operation and maintenance (O&M) expenses, and reserve for depreciation and depreciation expense; Office of the Public Counsel ("OPC") witness Keri Roth regarding Missouri Gas Utility's ("MGU") purchase of Southern Missouri Natural Gas ("SMNG") at a bargain purchase discount. I will also address the rebuttal testimony of Barbara A. Meisenheimer related to the economic risk impact of the Company's service expansion efforts on customers, Affiliate Transaction Rule and the bargain purchase discount.

EXECUTIVE SUMMARY

Q. What topics are addressed in this piece of testimony?

A. My surrebuttal testimony will address several topics. First, there are a few updates to Staff's direct filed revenue requirements. Staff had the opportunity to review additional information after the filing of direct and rebuttal testimony. After analyzing this information, additional costs that were previously excluded due to lack of documentation are now included in Staff's cost of service based upon further analysis and review. Second, I respond to Ms. Meisenheimer's rebuttal testimony where she addresses her concerns that the economic risk of SNG's expansion of gas service into new systems has been shifted to the customers. Staff believes that in the Company's Gallatin and Rogersville districts there has been no sufficient evidence to show that these systems are not currently economically viable. In the Branson and Warsaw districts, Staff believes that the most appropriate way to address any current uneconomic impact of offering utility service in these areas is by proposing "excess capacity" adjustments to the installed plant in service in these districts. In contrast, OPC has chosen to recommend denying all rate increases for each district based upon Ms. Meisenheimer's assertions that the customer and sales targets in the original CCN projections have not been met. Last, I address OPC's concern regarding the Affiliate Transaction Rules as it pertains to the MGU purchase of SMNG. Ms. Meisenheimer believes that due to the Affiliate Transaction Rules MGU should record the value of the SMNG properties at the purchase price (bargain purchase discount). Ms Roth agrees and believes that if the assets are valued at the bargain purchase discount price there is also a tax benefit to the seller that should be taken into account as well. Staff believes that the Affiliate Transaction Rules are intended to apply to transactions between regulated and non-regulated entities. Therefore, MGU's purchase of the SMNG assets should be recorded at the original net book value ("NBV") of the assets.

REVENUE REQUIREMENT UPDATES

Q. How does Staff respond to SNG witness Mr. Porter's testimony regarding costs booked to Account 923, Outside Services?

A. Staff still believes that the information it initially requested was not provided by SNG at the time of Staff's direct filing. Although Staff Data Request (DR) No. 0045.1 does specifically ask for a "list" of invoices, Staff had discussions with the Company, prior to issuing this data request, explaining what additional information we would need to complete the review where Staff specifically requested actual invoices. Furthermore, the information that SNG submitted as a response to DR No. 0045.1 was only the general ledger entries for Outside Services which Staff believes does not constitute a detailed list necessary to perform a review of these expenses.

Q. Has Staff subsequently had a chance to review the actual invoices for Outside Services?

A. Yes. Staff has reviewed the invoices provided and updated the adjustments to include these costs in Account 923, Outside Services.

Q. How does Staff respond to Mr. Porter's testimony regarding Corporate Overhead Allocations?

A. Staff believes that with the Corporate Overhead Allocations information that was available at the time of its direct filing there was nothing Staff could rely on to show

how SNG's Distrigas formula was applied. Staff had several subsequent discussions with the Company and recently reviewed additional information showing how costs are assigned using the Distrigas formula.

Q. Has Staff made any changes based on the additional information provided?

A. Yes. After extensive review of the additional information provided, Staff has included the costs identified by Mr. Porter in Accounts 874, 879, 903, 920 and 923.

Q. Has Staff made any changes to depreciation reserve?

A. Yes. As addressed in Mr. Porter's testimony, Staff inadvertently omitted making adjustments to depreciation reserve for the shared assets between Warsaw and Lake of the Ozarks. Depreciation reserve for Accounts 376 and 378 for the Warsaw district have been updated to reflect this oversight.

Q. How does Staff respond to Mr. Porter's testimony regarding franchise agreements?

A. After reviewing Account 302, Staff believes this is an account that should be amortized, and not depreciated as the Company is currently doing. Staff has now made adjustments correcting the depreciation reserve, depreciation expense and amortization expense for this item, and added the accumulated amortization as a reduction to rate base. These franchise agreement costs are amortized based on use of an estimated 20-year life.

Q. Does Staff have any additional updates to the revenue requirement?

A. Yes. Based on several discussions with the Company, Staff has updated billing determinants for all districts. The update in billing determinants also reflects updated revenue amounts. The new billing determinants and associated revenues are included in Schedule ACM-1.

ECONOMIC RISK IMPACT ON CUSTOMERS

Q. Does Staff agree in general with Ms. Meisenheimer's rebuttal testimony that no increase should be granted to any of SNG's districts because they have not achieved certain feasibility study projections as of this date?

A. No. Staff believes that these districts may still be economically viable even with lower levels of volumes than originally projected.

Q. Has Ms. Meisenheimer presented any evidence showing what specific economic feasibility problems relate to which specific CCN applications?

A. No. Ms. Meisenheimer uses totals per district in her analysis to show how the Company has not met projections. She has not identified what particular CCN cases are allegedly the root of the problem she identifies.

Q. Does Ms. Meisenheimer provide any kind of target, other than original feasibility projections, to show where these districts could be economically viable?

A. No. Ms. Meisenheimer chose instead to propose in her rebuttal testimony that no increase be granted to any district because SNG did not meet original CCN feasibility projections. She provides no other options except to deny all increases.

Q. What is Staff's position?

A. In general, a Company can still be economically viable even if they do not meet the projections included in their CCN feasibility studies. Feasibility studies provide a projection of what a utility can possibly do (targeted levels), not a minimum level necessary to justify economic viability. The language contained in the orders approving the CCNs in question does not state that no increase be granted if the specified levels are not reached. Further, even if Ms. Meisenheimer's complaints about economic feasibility are valid, Staff asserts a better solution would be a targeted adjustment to eliminate the alleged uneconomic impact through an "excess capacity" or a revenue imputation adjustment.

Q. How does Staff respond to Ms. Meisenheimer's rebuttal testimony regarding the Gallatin system, in particular?

A. The Gallatin system is different than any other systems that are currently part of SNG. The first application case (No. GO-2005-0120) filed for Gallatin was for MGU to take over two municipal systems, the cities of Gallatin and Hamilton. These two systems were in dire need because no gas supply contracts were in place for that winter season. MGU quickly filed to acquire these systems to make sure these customers would have gas service.

Q. Did Staff and MGU encounter any problems during Case No. GO-2005-0120 concerning valuation of the assets purchased by MGU?

A. Yes. Documentation was not available from the municipalities to provide an accurate net book value of the assets. Therefore, the value of Gallatin system (cities of Gallatin and Hamilton) is booked at purchase price instead of the original net book value by agreement of the parties to that proceeding.

Q. What is Staff's position regarding the Gallatin system?

A. Staff believes that although Gallatin may not have fully met its CCN feasibility projections the system is still economically viable and should recover the full cost of service. The data presented by Ms. Meisenheimer shows that the current sales volumes achieved by SNG for this district are only a modest amount below what was originally estimated for this district.

Q. How does Staff respond to Ms. Meisenheimer's rebuttal testimony regarding the Rogersville system?

A. Staff believes, based on our calculation of annualized and normalized sales volumes (1,888,994 Mcf) for this area in this proceeding, that the Rogersville system has exceeded the sales target requirements (1,797,000 Mcf) agreed to in Case No. GA-94-127. The portion of the Rogersville system subject to the revenue imputation conditions established in Case No. GA-94-127 forms the bulk of the Rogersville system.

Q. How does Staff respond to Ms. Meisenheimer's rebuttal testimony regarding the Branson and Warsaw systems?

A. Staff agrees with Ms. Meisenheimer that SNG has not met the feasibility projections for the Branson and Warsaw systems, and the shortfall in sales is material.

Q. What is Staff's position regarding the Branson and Warsaw systems?

A. As addressed in my rebuttal testimony, Staff did have concerns associated with these districts not meeting their earlier sales projections, and Staff worked with SNG for a possible solution to this problem. Staff has now calculated preliminary "excess capacity" adjustments to net rate base of $27.64 million for Branson and $6.97 million for Warsaw. The "excess capacity" adjustments are based on the mainline capacity usage factors ("usage factors") explained in Staff witness Lesa Jenkins' surrebuttal testimony. I calculated the adjustments by taking 100 percent less the usage factors to arrive at the actual reduction factors to apply to the plant and depreciation reserve balances. As part of Staff's recommendation, the amount of the Company's current plant and depreciation reserve balances that are deemed to be excess capacity should be moved into the "plant held for future use" account (Account No. 105) for possible recovery in a future case. Staff believes adoption of these adjustments would alleviate any concerns regarding the economic viability of the Branson and Warsaw districts. Therefore, Staff believes SNG should recover the full cost of service, less capacity adjustments, for these systems in this rate proceeding.

AFFILIATE TRANSACTION RULE

Q. Does Staff agree with Ms. Meisenheimer's rebuttal testimony that the valuation of the assets SNG acquired from SMNG in 2012 should be governed by the Affiliate Transaction Rule for gas utilities?

A. No. Staff believes these rules are not intended to regulate transactions associated with a merger between two regulated utilities. MGU and SMNG were both regulated by the Commission at the time of the merger (Case No. GM-2011-0354). In Staff's view, the asymmetric pricing rules included in Ms. Meisenheimer's rebuttal testimony page 21, line 1 through 17 are not intended to apply to a regulated entity transferring or acquiring assets from another regulated entity. The intent of these rules is to apply to regulated utilities doing business with non-regulated affiliates. These rules were put in place to prevent regulated utilities from subsidizing non-regulated affiliates.

Q. Do the asymmetric pricing rules make sense for two regulated utilities that merge?

A. No. The asymmetric pricing rules basically state that the selling utility should transfer assets at the higher of fully distributed costs (NBV) or fair market value ("FMV") and that the purchasing utility should acquire the assets at the lower of NBV or FMV. Unless the NBV and FMV are the same for a particular sale or merger transaction (and they were not for the MGU and SMNG merger transaction), it is obviously impossible for a selling company to transfer assets at a different value than the purchasing company acquires the assets for, because the merger results in only one surviving entity. Staff recommends that the appropriate regulation of a merger between two regulated entities is achieved by the application of the "net original cost rule," which provides that, as a general rule, only the original cost (i.e. the NBV) of utility plant to the first owner devoting the property to public service, adjusted for depreciation, should be included in a utility's rate base.[1]

<u>BARGAIN PURCHASE DISCOUNT</u>

Q. Does Staff agree with Ms. Meisenheimer and Ms. Roth that SNG should record the SMNG at the bargain purchase discount?

A. No. Staff has taken the consistent position that assets acquired in a sale or merger from another utility should continue to be booked at NBV, barring compelling circumstances. In this case, Staff is proposing excess capacity adjustments to address concerns that the customer growth to date for these districts is not sufficient to fully support the NBV of the plant in service installed in each area. No further adjustment to plant in service is necessary.

Q. Ms. Roth includes a quote from the Commission's Report and Order in Case No. ER-77-118 in support of OPC's position in this matter. How does Staff respond?

A. The quotation states a Commission policy that ratepayers are not entitled to any gain resulting from disposal of utility property, or that customers should absorb the loss associated with disposal of utility property. However, Staff believes that Ms. Roth's reference to the Commission's position in Kansas City Power & Light Case No. ER-77-118 in relation to the "bargain purchase discount" resulting from the MGU-SMNG transaction is misfounded. To Staff's knowledge, the Commission's position in Case No. ER-77-118 has never been applied to a sale or an acquisition of an entire utility company, or an entire system

[1] EM-2000-292, Re UtiliCorp United Inc., Second Report and Order, February 26, 2004, WL 431561, p. 2.

of assets. To Staff's knowledge, this position has been applied to cases involving sale or acquisition of individual assets or pieces of property. Therefore, in Staff's view the appropriate policy is to maintain the position of continuing to value acquired companies or systems of assets at their net original cost.

Q. Ms. Roth notes that SMNG, the original owner of the assets in question, may have received a tax benefit associated with selling its assets to MGU at a loss in 2012. Please comment.

A. Whether or not the former owners of the SMNG assets received favorable tax treatment upon disposal of the assets does not seem relevant to the question of what rate base valuation the new owners of the assets should receive related to the acquisition.

Q. Does this conclude your surrebuttal testimony?

A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Summit Natural Gas of Missouri Inc.'s Filing of Revised Tariffs To Increase its Annual Revenues For Natural Gas Service	))))	Case No. GR-2014-0086

AFFIDAVIT OF AMANDA C. MCMELLEN

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Amanda C. McMellen, of lawful age, on her oath states: that she has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 10 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.

Amanda C McMellen

Amanda C. McMellen

Subscribed and sworn to before me this 8th day of August, 2014.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: December 12, 2016
Commission Number: 12412070

D Suzie Mankin

Notary Public

Summit Natural Gas of Missouri, Inc.
Case No GR-2014 -0086
Pro forma Revenues

Line No		Customer Charge Revenue			Commodity Charge Revenue				
		Monthly Charge Note 1	Annual Bills	Annual Revenue	Charge per Ccf Note 1	Average Annual Usage Mcf	Annual Volume Mcf	Annual Revenue	Total Annual Revenue
1	Gallatin								
2	GS- residential	$ 15.00	15,845	$ 237,675	$ 0.4449	67.74	90,802	$ 403,979	$ 641,654
3	GS-commercial	15.00	2,421	36,315	0.4449	104.58	21,129	94,002	130,317
4	CS	24.53	601	14,743	0.5027	776.25	38,848	195,290	210,032
5	LVS	81.77	12	981	0.5027		20,929	105,208	106,189
6	ISS	204.42		-	0.4415			-	-
7	TS	204.42	60	12,265	0.5027		32,252	162,133	174,398
8			18,939	$ 301,979			203,960	$ 960,611	$ 1,262,591
9	Warsaw								
10	GS- residential	$ 15.00	10,296	$ 154,440	$ 0.5500	50.56	43,781	$ 240,797	$ 395,237
11	GS-commercial	15.00	2,355	35,325	0.5500	95.39	18,860	103,729	139,054
12	CS	30.00	413	12,390	0.6000	1,039.94	35,262	211,569	223,959
13	LVS	100.00	192	19,200	0.6000		66,488	398,928	418,128
14	TS	200.00		-	0.6000			-	-
15			13,256	$ 221,355			164,391	$ 955,023	$ 1,176,378
16	Rogersville								
17	GS-residential	$ 10.00	58,192	$ 581,920	$ 0.4660	60.68	298,701	$ 1,391,949	$ 1,973,869
18	GS - residenital - optional	-	56,338	-	0.7060	49.40	234,070	1,652,531	1,652,531
19	GS-commercial	15.00	13,299	199,485	0.4630	199.89	226,416	1,048,306	1,247,791
20	GS-commercial - optional	-	4,352	-	0.7030	80.60	29,787	209,401	209,401
21	LGS	50.00	1,191	59,550	0.4300	1,796.13	175,939	756,538	816,088
22	LVS	300.00	192	57,600	0.4180		134,542	562,387	619,987
23	TS (note 4)	300.00	228	68,400	3.6000		789,539	2,842,339	2,910,739
24			133,792	$ 966,955			1,888,994	$ 8,463,451	$ 9,430,406
25	Branson								
26	GS-residential	$ 10.00	4,361	$ 43,610	$ 0.4660	59.70	21,926	$ 102,173	$ 145,783
27	GS - residenital - optional	-	1,339	-	0.7060	32.84	3,527	24,898	24,898
28	GS-commercial	15.00	2,075	31,125	0.4630	285.13	49,225	227,911	259,036
29	GS-commercial - optional	-	367	-	0.7030	75.52	2,041	14,347	14,347
30	LGS	50.00	1,361	68,050	0.4300	1,176.89	133,580	574,393	642,443
31	LVS	300.00		-	0.5180			-	-
32	TS (note 4)	300.00	96	28,800	4.6000		251,594	1,157,332	1,186,132
33			9,599	$ 171,585			461,892	$ 2,101,054	$ 2,272,639

Notes: (1) charges taken from current tariff.

Schedule ACM-1