

**Exhibit No.:**  
**Issue:** **Complaint and  
Counterclaim Issues**  
**Witness:** **Michael T. Cline**  
**Type of Exhibit:** **Surrebuttal  
Testimony**  
**Sponsoring Party:** **Laclede Gas Company**  
**Case No.:** **GC-2011-0098**  
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**LACLEDE GAS COMPANY**

**GC-2011-0098**

**SURREBUTTAL TESTIMONY**

**OF**

**MICHAEL T. CLINE**

1 **SURREBUTTAL TESTIMONY OF MICHAEL T. CLINE**

2 Q. Please state your name and address?

3 A. My name is Michael T. Cline and my business address is 720 Olive Street, St.  
4 Louis, Missouri 63101.

5 Q. Are you the same Michael T. Cline who filed direct and rebuttal testimony in this  
6 docket?

7 A. Yes.

8 Q. What is the purpose of your surrebuttal testimony?

9 A. The purpose of my surrebuttal testimony is to address a number of the assertions  
10 made in the rebuttal testimony submitted by Staff witness Charles R. Hyneman  
11 and OPC witness Barbara Meisenheimer. Specifically, I will address their claims  
12 that Laclede's Cost Allocation Manual (CAM) is contrary to the Commission's  
13 affiliate transaction rules (Rules) because it does not appear to explicitly require  
14 Laclede to conduct a fully distributed cost (FDC) analysis each time Laclede  
15 purchases or sells gas in transactions with its marketing affiliate, LER. In  
16 particular, I will demonstrate that such claims are inconsistent with literally years  
17 of acquiescence by both Staff and OPC in the very CAM provisions that they now  
18 claim are inadequate. I will also show that fair market price (FMP) is the only  
19 relevant basis for assessing the propriety of gas sales and purchases made by an  
20 LDC on the wholesale market, and that the attempts of the Staff and OPC witness  
21 to create the impression that FDC is meaningful in this context is completely  
22 meritless.

23 Q. Is this issue also being addressed by other Company witnesses?

1 A. Yes. Mr. John J. Reed of Concentric has also filed surrebuttal testimony on this  
2 issue on behalf of Laclede.

3 Q You said that the assertions made by Mr. Hyneman and Ms. Meisenheimer  
4 regarding this alleged deficiency in the CAM are inconsistent with Staff's and  
5 OPC's long acquiescence in these CAM provisions. Please explain what you  
6 mean.

7 A. It is all well and good for Mr. Hyneman and Ms. Meisenheimer to weigh in with  
8 their views regarding the CAM's alleged failure to satisfy the so-called FDC  
9 requirement of the Affiliate Transactions Rules, but I think it is fair to ask where  
10 they were nearly 10 years ago when these CAM provisions were first transmitted  
11 to them pursuant to the agreed-upon process approved by the Commission in Case  
12 No. GM-2001-342 for completing the CAM. As Mr. Buck explains in his  
13 surrebuttal testimony, the CAM, with these very provisions in it, was sent to both  
14 the Staff and OPC in December of 2001. The CAM provisions should have been  
15 reviewed by these parties at that time, particularly since their use for pricing gas-  
16 related transactions had also been endorsed by Staff and OPC as part of the  
17 settlement approved by the Commission in Laclede's 2001 rate case. And if for  
18 some unknown reason they weren't reviewed at that time, they certainly should  
19 have been reviewed by these parties in Laclede's 2002 rate case, during which the  
20 Staff explicitly asked the Company to once again provide the CAM and answer  
21 questions in connection therewith.

22 Q. Did Staff or OPC raise any concerns about the use of FDC on pricing gas supply  
23 transactions at that time?

1 A. No concerns were raised by these parties in either late 2001 or 2002. Nor were  
2 such concerns expressed in 2003 when Laclede had a lengthy meeting with Staff  
3 and OPC on how utilities should comply with the Affiliate Transactions Rules,  
4 nor in 2004 when Laclede submitted its revised CAM in compliance with the  
5 Rules, nor in 2005 when the Company had an extended discussion regarding its  
6 affiliate transactions with the Staff. In fact, as Ms. Meisenheimer herself  
7 observes, it wasn't until late 2007 that OPC first mentioned a concern about the  
8 CAM not explicitly mentioning FDC for certain gas supply transactions in an  
9 email from Ryan Kind to Laclede.

10 Q. Did Mr. Kind articulate how FDC would come into play when pricing such gas  
11 supply transactions?

12 A. No. Mr. Kind simply mentioned the concern without giving any insight into how  
13 FDC would be applied in the context of gas supply transactions. Unfortunately,  
14 more than three years later, Ms. Meisenheimer hasn't shed any additional light on  
15 the subject. Instead of articulating exactly how an FDC calculation would be  
16 done in the context of such transactions or why it would produce a more favorable  
17 result for customers than FMP, she simply observes that the Rules mention FDC  
18 and that sometimes FDC can be different from FMP. That says nothing about the  
19 issue. It completely fails to respond to either Laclede's December 10, 2010  
20 Answer or its March 22, 2011 direct testimony on the subject.

21 Q. Have other members of the Staff addressed the issue of what FDC means in the  
22 context of such transactions?

1 A. Yes. As I have testified previously, Mr. Sommerer has previously testified that  
2 FDC is not even a consideration in evaluating gas supply transactions because  
3 LDCs are not in the business of producing gas and as a result FDC would only  
4 add administrative costs on top of FMP, the competitively determined acquisition  
5 price of the gas purchased by the LDC. This has been subsequently confirmed by  
6 Mr. Hyneman himself who in response to Laclede's First Set of Data Requests  
7 has given a definition of how FDC costs would be calculated. Similar to Mr.  
8 Sommerer's testimony on this issue, this shows once again that an FDC  
9 calculation would only add additional costs onto the price at which gas supplies  
10 were acquired – a result that assures that FDC, if it is even applicable, would be  
11 the same or greater than FMP.

12 Q Does this recognition on the part of the Staff explain why it did not take issue  
13 with the gas supply-related pricing provisions of the CAM in 2001, 2002, 2003,  
14 2004, 2005 and later?

15 A. It is certainly one explanation and, I believe, the most likely.

16 Q. Does this mean that Laclede has ignored FDC or not taken it into account when  
17 pricing these transactions as Mr. Hyneman and Ms. Meisenheimer allege?

18 A. Absolutely not. To the contrary, Laclede thoroughly considered FDC in  
19 developing the gas supply pricing provisions in the CAM. And, with Staff's and  
20 OPC's full acquiescence over many years it has reflected in those pricing  
21 provisions the commonly understood reality that FDC will not produce a more  
22 favorable result for customers than FMP – an outcome that is also fully consistent  
23 with the views recently expressed by Mr. Sommerer and Mr. Hyneman. Given

1           these considerations, it is fatuous to claim that the CAM is deficient because it  
2           does not pretend that the Company should perform a calculation each and every  
3           time it buys gas when everyone knows or should know that such a calculation is  
4           meaningless because it will not produce a more favorable result for customers  
5           than that obtained under FMP.

6    Q.    Is this reliance on FMP also consistent with how the Commission determines the  
7           reasonableness of gas costs in other contexts?

8    A.    Yes.  When the Staff reviews the reasonableness of the prices paid by Laclede to  
9           other suppliers during an ACA audit it looks at whether they are reflective of the  
10          market price for gas supplies for the locations and periods over which the supplies  
11          were purchased.  It does not look at the marketer's *costs*.  Literally thousands of  
12          gas supply contracts, purchases and sales have been deemed reasonable based on  
13          this market test.  When the Commission determines whether Laclede is eligible  
14          for incentive sharing under its tariffed Gas Supply Incentive Plan, it looks at  
15          whether the prices paid by the Company meet or beat a mix of competitively-  
16          determined market indices, not the suppliers' *costs* of producing, gathering or  
17          pooling gas supplies.  Again, the Company has been allowed on a number of  
18          occasions over the past 15 years to retain a share of the savings achieved by its  
19          superior procurement of gas supplies based solely on how the prices it paid  
20          compared to the prices being offered in the competitive wholesale marketplace.

21   Q.    Does the Company's PGA tariff look at the underlying costs incurred by suppliers  
22          in determining what costs are eligible for recovery through the PGA?

1 A. No. In defining the costs that Laclede may recover through the PGA process, the  
2 PGA tariff talks in terms of the commodity *charges* that Laclede pays to its  
3 suppliers, and makes specific reference to the use of “natural gas market indices”  
4 to determine the Company’s calculation of its current purchased gas adjustment.  
5 There is absolutely no mention of the costs that may underlie those charges.

6 Q Does the Commission’s web page also recognize that it is the market that  
7 determines the appropriate price for purchases of gas supply by an LDC?

8 A. Yes. As discussed by Laclede witness John J. Reed, the Commission’s web site is  
9 replete with references to the natural gas market as the mechanism that sets the  
10 price for gas supplies acquired by an LDC. In short, virtually every Commission-  
11 approved document, tariff, customer notice or other instrument that addresses the  
12 subject of how one can ensure that gas purchases made by an LDC have been  
13 appropriately priced uses FMP as the prevailing and, indeed, only standard.

14 Q. On pages 25-26 of his rebuttal testimony, Mr. Hyneman states that your “widget”  
15 example makes no sense to him. Why does he say that?

16 A. Because he doesn’t understand it. Although Mr. Hyneman agrees that Laclede  
17 does not produce natural gas itself, he fails to realize that, because of this, FDC is  
18 essentially rendered irrelevant for purposes of the asymmetrical pricing rules.

19 Q. What do you mean?

20 A. When a utility buys a product like natural gas from its affiliate, the Rules provide  
21 two options for setting the price of that affiliate transaction: FMP and FDC. The  
22 obvious purpose of FMP is to ensure that the utility does not disadvantage its  
23 customers by paying more than a fair price set by the market. The Rules add FDC

1 so that the utility will not buy the product (gas) from its affiliate at a market price  
2 if it could make or produce that product itself for less than that market price. So,  
3 if Laclede produced, pooled or aggregated its own natural gas in the field, and did  
4 so at a cost that was below the market price, the Rule would require Laclede to  
5 price its purchase of gas from its affiliate at FDC, rather than FMP. However,  
6 since Laclede, like most LDCs, does not perform the functions that are typically  
7 undertaken by a producer or marketer, the cost to Laclede of providing gas to  
8 itself is actually its cost to purchase gas from marketers in the wholesale market.  
9 Such wholesale cost, in turn, represents the fair market price of the gas to  
10 Laclede. Simply put, the cost is the market price.

11 As another Staff witness, Mr. David Sommerer, testified in the Atmos proceeding  
12 that I cited in my direct testimony, if FDC includes not only such fair market price  
13 but other direct and indirect costs associated with Laclede's purchase of the gas,  
14 by definition FDC will be equal to or greater than the fair market price. Mr.  
15 Hyneman may not care for the widget analogy, but there's no denying that FDC is  
16 meaningless in those instances where a company is not in the business of  
17 producing or providing the particular good or service under consideration, but  
18 must purchase it at a market price in order to acquire it. This is true whether that  
19 good is a widget or natural gas.

20 Q. On page 26, Mr. Hyneman somewhat facetiously indicates that Laclede has no  
21 problem calculating its cost of gas for PGA purposes; "only when it comes to  
22 affiliate transactions does Laclede seem to have a problem figuring out its cost to  
23 purchase or sell natural gas." Does this indicate a flaw in your position?



1 A. No. Again, the Affiliate Rules define FDC as a cost of the utility to produce the  
2 gas for itself. Since Laclede does not produce or aggregate natural gas for itself in  
3 the field, FDC is therefore not applicable. However, as indicated in the quote  
4 above from Mr. Hyneman’s testimony, Laclede certainly does have a “cost to  
5 purchase” natural gas, and Laclede has no problem figuring it out. Laclede’s cost  
6 to purchase gas is the price set by the wholesale gas market. The cost is the  
7 market.

8 Q. On pages 25 and 26 Mr. Hyneman would like the Commission to believe that  
9 your widget example falls apart because he believes that it implies that Laclede  
10 doesn’t manufacture anything. Do you agree?

11 A. Absolutely not. Unlike gas supply, Laclede does produce a distribution service,  
12 namely the delivery of wholesale purchased natural gas through Laclede’s  
13 network of mains and services to customers’ homes and businesses. However, the  
14 costs to provide such service are in no way relevant in any FDC calculations in  
15 this case, since it is gas supply, not distribution service that Laclede purchases  
16 from LER.

17 Q. On page 26, Mr. Hyneman concludes that, in pricing a purchase of gas from its  
18 affiliate, Laclede is required by the Affiliate Rules to consider the question of  
19 which is lower, FDC or FMP. Do you agree?

20 A. Yes. As stated above, and in my direct and rebuttal testimonies, Laclede has in  
21 fact thoroughly considered the question and found that because it doesn’t produce  
22 or aggregate gas for itself in the field, FMP represents the proper pricing standard,  
23 because the FDC to obtain gas is never going to be lower than FMP.

1 Q. In addition to her comments regarding FDC, on page 4, lines 10-17 of her  
2 surrebuttal testimony, Ms. Meisenheimer also disagrees with what she  
3 understands to be the definition of fair market price on page 8 of Laclede's CAM.  
4 Is Ms. Meisenheimer correct?

5 A. No. First, FMP is not at issue in this case; rather, Staff's complaint herein is that  
6 gas supply affiliate transactions under Laclede's CAM do not account for FDC.  
7 Second, even if FMP was at issue, the relevant FMP in this case would be the  
8 FMP described on page 13 of the CAM pertaining to gas supply transactions, not  
9 the generic FMP identified by Ms. Meisenheimer on page 8 of the CAM. The  
10 FMP on page 13 has terms that are specific to gas supply pricing, which should  
11 not pose a problem for Ms. Meisenheimer. Third, the FMP provision Ms.  
12 Meisenheimer identified has been part of the CAM since 2001, and was agreed to  
13 at that time by Staff and OPC. While OPC has established a practice of un-  
14 agreeing to matters that it has previously agreed to, its position on this provision  
15 is an unnecessary and misleading distraction to the resolution of the issues in this  
16 proceeding. In any event, Laclede does not agree with Ms. Meisenheimer's  
17 interpretation of the provision on page 8 of the CAM.

18 Q. On page 11, lines 15-17, Ms. Meisenheimer suggests that prior to Laclede's  
19 corporate reorganization, when LER was a subsidiary of Laclede, Laclede was  
20 able to provide gas to itself through LER. Do you agree?

21 A. No. LER has always been a separate, non-regulated marketing affiliate of  
22 Laclede. LER has never performed the gas acquisition function for Laclede, as  
23 Ms. Meisenheimer suggests, either prior to or after the 2001 corporate

1 reorganization. Instead, LER, like any other marketer with whom Laclede  
2 contracts for gas supply, is in the business of buying gas from and selling gas to  
3 various parties. Since Laclede and LER have entirely different corporate  
4 identities, different business strategies and objectives and different MPSC-  
5 jurisdictional status, it is inappropriate to conclude that when Laclede buys gas  
6 from LER, Laclede is merely providing gas to itself. As such, there is no  
7 justification for using LER's cost for Laclede's FDC, much less using LER's cost  
8 as the FMP. Consistent with what I stated in my direct testimony, Laclede does  
9 not produce gas, and cannot provide gas to itself without going to the "wholesale"  
10 market and buying that gas from a marketing entity like LER. Therefore, to the  
11 extent FDC is even applicable, the cost Laclede incurs to acquire gas from that  
12 wholesale party, whether it is LER or an unaffiliated marketer, would form the  
13 basis for Laclede's FDC.

14 Q. You stated that LER has never performed the gas acquisition function for  
15 Laclede. But hasn't LER sold gas to Laclede?

16 A. Yes. Like many other marketers who have sold gas to Laclede on the wholesale  
17 market, LER has sold gas to Laclede, but only to a very modest degree. In fact,  
18 Laclede's purchases from LER as a percentage of Laclede's total requirements  
19 over the past five years have averaged less than 8%. Accordingly, any suggestion  
20 that LER is performing the gas supply acquisition function for Laclede has  
21 absolutely no basis in fact.

22 Q. Does this conclude your surrebuttal testimony?

23 A. Yes, it does.

