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November 19, 2002

Mr. Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102

FILED⁴
NOV 19 2002

Missouri Public
Service Commission

Re: Case No. GT-2003-0117

Dear Mr. Roberts:

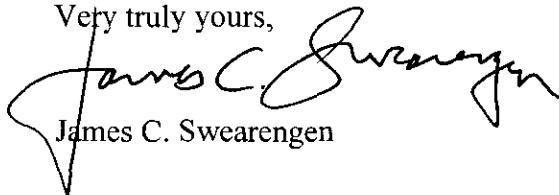
Enclosed for filing with the Missouri Public Service Commission in the referenced case on behalf of Laclede Gas Company please find an original and eight (8) copies of the direct testimony and schedules of Michael T. Cline, John Moten, Jr., and James A. Fallert.

Would you please see that this filing is brought to the attention of the appropriate Commission personnel.

A copy of this filing is being provided to all parties.

I thank you in advance for your cooperation in this matter.

Very truly yours,


James C. Swearengen

JCS/lar

Enclosure

cc: Dan Joyce
John Coffman
Ronald Molteni

Exhibit No.:

Issue:

**Financial Implications
Of Catch-Up/Keep-Up
Program**

Witness:

James A. Fallert

Type of Exhibit:

Direct Testimony

Sponsoring Party:

Laclede Gas Company

Case No.:

GT-2003-0117

Date:

November 19, 2002

FILED⁴

NOV 19 2002

**Missouri Public
Service Commission**

LACLEDE GAS COMPANY

GT-2003-0117

DIRECT TESTIMONY

OF

JAMES A. FALLERT

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Tariff Filing of)
Laclede Gas Company to Implement)
An Experimental Low Income Assistance) Case No.GT-2003-0117
Program called Catch-Up/Keep-Up)

AFFIDAVIT

STATE OF MISSOURI)
) SS.
CITY OF ST. LOUIS)


James A. Fallert, of lawful age, being first duly sworn, deposes and states:

1. My name is James A. Fallert. My business address is 720 Olive Street, St. Louis, Missouri 63101; and I am Controller of Laclede Gas Company.
2. Attached hereto and made a part hereof for all purposes is my Direct Testimony, consisting of pages 1 to 9, inclusive.
3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.



James A. Fallert

Subscribed and sworn to before me this 18th day November, 2002.



JOYCE L. JANSEN
Notary Public — Notary Seal
STATE OF MISSOURI
ST. CHARLES COUNTY
My Commission Expires: July 2, 2005

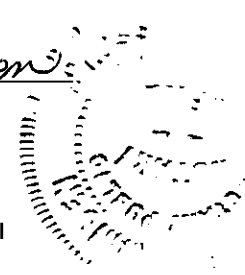


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DIRECT TESTIMONY OF JAMES A. FALLERT

General Information/Qualifications

1

2 Q. Please state your name and business address.

3 A. My name is James A. Fallert, and my business address is 720 Olive Street, St.
4 Louis, Missouri 63101.

5 Q. What is your present position?

6 A. I am Controller for Laclede Gas Company ("Laclede" or "Company").

7 Q. Please state how long you have held your position and briefly describe your
8 responsibilities.

9 A. I was appointed to my present position in February 1998. In this position, I am
10 directly responsible for the Company's customer accounting functions, and also
11 participate in the preparation and review of financial statements, budgets, and
12 financial plans.

13 Q. What is your educational background?

14 A. I graduated from Southeast Missouri State University in 1976 with the degree of
15 Bachelor of Science in Business Administration, majoring in administrative
16 management. In 1981, I received a Master's Degree in Business Administration
17 from Saint Louis University.

18 Q. Will you briefly describe your experience with Laclede prior to becoming
19 Controller?

20 A. I joined Laclede in July 1976, and held various staff and supervisory positions in
21 the Methods and Procedures Department, Internal Audit Department, and Budget
22 Department until April 1988, when I was promoted to the position of Manager of

1 Budget and Financial Planning. I held this position until being promoted to
2 Manager of Financial Services in February 1992. I was elected Controller
3 effective February 1, 1998.

4 Q. Have you previously filed testimony before the Missouri Public Service
5 Commission ("Commission")?

6 A. Yes, I have, in Case Nos. GR-90-120, GR-92-165, GR-94-220, GR-96-193, GR-
7 98-374, GR-99-315, GR-2001-629, and GR-2002-356.

8 **Purpose of Testimony**

9 Q. What is the purpose of your testimony?

10 A. The purpose of my testimony is to present evidence regarding the need for the
11 Company's proposed experimental Catch-Up/Keep-Up Program as evidenced, in
12 part, by the current arrearages being experienced by the Company's residential
13 customers, to comment on the possible benefits arising from the plan, and to
14 respond to suggestions that the plan could be funded through an Accounting
15 Authority Order ("AAO") as an alternative to the funding mechanism proposed in
16 the Company's plan.

17 **Need for the Program**

18 Q. You indicated that the need for the Program was evidenced, in part, by the current
19 arrearages being experienced by the Company. Please define "arrearages".

20 A. Arrearages are amounts that have been billed to customers for gas service, but that
21 such customers have not paid as of the delinquent date for the invoice on which
22 the service was billed. Arrearages indicate by how much customers have fallen
23 behind on payment of their bills.

1 Q. What is Laclede's recent experience with arrearages for its residential customers?

2 A. As of September 30, 2002, 110,324 residential customers were in arrears by a
3 total of \$18,523,000. A total of 21,080 of these customers' accounts have been
4 finaled, meaning that they are not currently receiving gas service. Arrearages
5 applicable to these finaled customers totaled \$9,927,000 as of September 30,
6 2002.

7 Q. Do these figures include accounts that have been written off?

8 A. No. Customer account balances are no longer included in arrearages at the point
9 where they are written off.

10 Q. What do these statistics suggest to you?

11 A. There are a substantial number of customers who have had difficulty keeping their
12 gas bills current and who are either in threat of having their gas service
13 discontinued or have already been disconnected. There appears to be a significant
14 need for relief of these arrearage amounts among Laclede's customers. With over
15 \$18 million currently in arrears, the \$6 million program proposed by the
16 Company certainly appears to be a reasonable and proportionate response to an
17 existing need.

18 **Benefits of the Program**

19 Q. Have you calculated the impact that this program will have on the Company's
20 uncollectible accounts?

21 A. Because there are so many unknown variables regarding whether, when and on
22 what terms the Program may be approved and how customers will receive and
23 responded to the experimental incentives provided by the Program, it has not been

1 possible to develop a definitive estimate of the Program's impact. Indeed, if the
2 impact of the Program could be definitively assessed in advance there would be
3 little, or no, need to conduct an experiment. However, the Program should serve
4 to reduce uncollectible expense and I believe an amount of about \$2.0 to \$3.0
5 million represents a reasonable estimate of this potential impact.

6 Q. Why is an estimate of \$2.0 million to \$3.0 million reasonable when there may be
7 up to \$6.0 in funding available under the Program?

8 A. First of all, up to \$.6 million of the \$6 million is earmarked for customer outreach,
9 bill counseling, conservation, weatherization, etc. But even if the remaining \$5.4
10 million is fully utilized by customers in the Program, I still wouldn't expect that
11 uncollectible accounts would be reduced by that amount.

12 Q. Why not?

13 A. I believe it is reasonable to expect that some of the customers who would take
14 advantage of the Program may have found a way to pay all or a portion of their
15 arrearages and maintain service even in the absence of the Program. In addition,
16 some customers participating in the Program will fail or not be able to meet their
17 payment obligations under the Program despite the more affordable terms
18 provided by the Program. Given these considerations, I believe it is reasonable to
19 estimate a bad debt impact that is in the mid-range of total Program funding.

20 Q. Does this mean that the Program is a losing proposition and that some of the
21 Catch-Up/Keep-Up amounts are being wasted?

22 A. No. The Program is only available to customers who meet certain income
23 guidelines. The fact that some of these customers may have been able to scrape

1 together the money to pay their arrearages, probably by cutting back on other
2 essentials, doesn't mean that they don't have a need for help. In fact, these are the
3 type of customers that we are trying to help with this Program: people who want
4 to make an honest effort to keep up with their bills but have fallen behind because
5 of a combination of their income level and gas bills, and the demands imposed by
6 their other financial needs.

7 Q. What benefits would you expect a successful Catch-Up/Keep-Up Program to have
8 for the Company's customers who do not participate?

9 A. All of the Company's paying customers pay for the bad debts of those who don't
10 pay, since these bad debts are ultimately recovered as a cost of service through the
11 ratemaking mechanism. By fostering a habit among poor pay customers of
12 keeping up with their monthly payments, the Program is designed to reduce the
13 level of these bad debts in the long run. Concurrently, the cost of taking
14 collection action against these customers should decline and the amount of
15 working capital devoted to carrying their arrearages should decrease. These
16 benefits will also eventually flow to all customers in the form of reductions to
17 these elements in the Company's cost of service.

18 Q. Are there other potential benefits that may accrue to the Company's other
19 customers?

20 A. Yes. Currently, the Company incurs annual costs of about \$2.9 million for its
21 collection function, and an additional \$.9 million to reconnect customers who
22 have been disconnected for non-payment. To the extent participating customers
23 respond positively to the Program's mix of financial incentives and affordable

1 rates and keep current on their utility bills, the Program should also enable the
2 Company to reduce some of the expenses associated with these
3 disconnection/reconnection and collection activities. Once again, these are cost
4 savings that will ultimately flow to the Company's other customers in the form of
5 reductions to these elements of its cost of service. In addition, the Program will
6 also provide the Company with an incentive to obtain the most favorable level of
7 discounts possible from its out-of-state pipeline suppliers -- a result that will
8 benefit all customers.

9 Q. Does this mean that if the Program is approved that customers will see an absolute
10 decline in the cost of serving them or the rates they are charged for service?

11 A. All else being equal, customers should see a decline in the cost of service for the
12 areas affected by the Program. However, it is important to note that the actual
13 amount of bad debt expense being experienced by the Company is currently well
14 above the amounts that have been reflected in rates. For example, while the
15 Company received an allowance for bad debts of approximately \$8 million in its
16 most recent rate case, the actual level of bad debts experienced by the Company
17 for the fiscal year ended September 30, 2002, totaled some \$11.3 million. Factors
18 such as gas prices, the impact of weather-related usage on customers'
19 consumption of purchased gas volumes, availability and amount of governmental
20 energy assistance, and general economic conditions may also have a significant
21 impact on bad debt expense. In addition, the Company will continue to
22 experience payroll and benefit-related increases for the personnel who perform
23 disconnection and collection activities and some of these personnel may be

1 deployed to do other work in the event the Program results in a reduction in the
2 amount of time they require to work on these activities. The point is, however,
3 that regardless of whether there is an absolute reduction in the Company's cost of
4 service, the Program will nevertheless contribute to a relative reduction in costs
5 for these specific areas and functions compared to what those costs would have
6 been in the absence of the Program.

7 **Accounting Authority Order**

8 Q. Certain parties have suggested that, in lieu of the funding mechanism
9 recommended by Laclede, the Company should proceed with the Program on its
10 own and seek an AAO to recover any costs associated with the Program. Is this a
11 practical alternative?

12 A. No, an AAO is not an acceptable funding alternative for the Program.

13 Q. Why not?

14 A. There are three basic reasons: (1) lack of cash flow to fund the Program under an
15 AAO mechanism, (2) the lack of full recovery inherent in AAO mechanisms as
16 typically implemented in Missouri, and (3) the risk of future differences amongst
17 parties regarding the appropriate recovery of amounts deferred under the AAO
18 mechanism.

19 Q. Please explain your concerns regarding cash flow.

20 A. An AAO mechanism would force the Company to fund any incremental costs
21 associated with the Program up front. In view of the cash flow difficulties that the
22 Company has faced (and which are well documented in the testimony from our
23 recent rate case, Case No. GR-2002-356), and the resulting credit rating

1 downgrades that the Company has experienced, it would be unwise to place
2 additional pressure on the Company's cash flow situation. This is particularly
3 true in light of the fact that Case No. GR-2002-356 included a rate moratorium.

4 Q. You mentioned your concern that AAO mechanisms do not provide for full
5 recovery of deferred costs. Please elaborate.

6 A. The typical mechanism for return of dollars deferred pursuant to AAO
7 mechanisms has resulted in recovery of 50% or less of the original dollars on a
8 present value basis. These returns have occurred even for AAOs related to
9 programs of unquestioned importance, such as the gas safety replacement
10 program. Laclede cannot afford to implement a program of the magnitude of the
11 Catch-Up/Keep-Up Program under such circumstances.

12 Q. Why is the ultimate recovery under AAO mechanisms typically so low?

13 A. The Staff and Public Counsel have typically recommended recovery periods of 10
14 to 15 years (or longer) with no recognition of the deferred balances in rate base.
15 This amounts to a long term interest free loan from the Company's shareholders
16 to its customers. On top of this, these parties have typically advocated that rate
17 base during this 10 or 15 years be reduced by the deferred taxes related to the
18 deferrals, despite the fact that they advocate that the deferrals themselves be
19 excluded from rate base. The net effect of this approach is that the Company's
20 ultimate recovery of amounts deferred in an AAO is only a fraction of the value
21 of the original dollar deferred.

22 Q. Do you have any other concerns regarding the use of an AAO to fund the Catch-
23 Up/Keep-Up Program?

1 A. Yes. Absent very specific language, the amount of dollars deferred through an
2 AAO mechanism that are ultimately deemed recoverable could vary widely based
3 on the viewpoints of the parties determining those amounts. I would be
4 concerned that using an AAO in this instance would subject all of the parties
5 involved to a considerable degree of uncertainty as to the amounts that would be
6 recoverable.

7 Q. Does this conclude your testimony?

8 A. Yes.