BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy's Purchased Gas Adjustment (PGA) Factors to be Audited in Its 2002-2003 Actual Cost Adjustment	)))	**Case No. GR-2003-0330**
In the Matter of Missouri Gas Energy's Purchased Gas Adjustment Tariff Revisions to be Reviewed in Its 2001-2002 Actual Cost Adjustment	)))	**Case No. GR-2002-348**

REPORT AND ORDER

Issue Date: October 2, 2007

Effective Date: October 12, 2007

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy's Purchased Gas Adjustment (PGA) Factors to be Audited in Its 2002-2003 Actual Cost Adjustment	)))	**Case No. GR-2003-0330**
In the Matter of Missouri Gas Energy's Purchased Gas Adjustment Tariff Revisions to be Reviewed in Its 2001-2002 Actual Cost Adjustment	)))	**Case No. GR-2002-348**

Table of Contents

APPEARANCES

Gary W. Duffy, and Janet Wheeler, Attorneys at Law, Brydon Swearengen & England, 312 East Capitol Avenue, Jefferson City, Missouri 65102, for Missouri Gas Energy.

Mark D. Poston, Senior Public Counsel, Office of the Public Counsel, Post Office Box 2230, Jefferson City, Missouri 65102, for the Office of the Public Counsel and the Public.

Steven C. Reed, Chief Litigation Attorney, Missouri Public Service Commission, Post Office Box 360, Jefferson City, Missouri 65102, for the Staff of the Missouri Public Service Commission.

REGULATORY LAW JUDGE: Morris L. Woodruff

REPORT AND ORDER

SUMMARY

The Commission finds that the Commission's Staff has failed to create a serious doubt about the prudence of MGE's decisions regarding the determination of appropriate natural gas pipeline capacity. Therefore, Staff's proposed disallowance regarding excess pipeline capacity is denied.

FINDINGS OF FACT

The Missouri Public Service Commission, having considered all of the competent and substantial evidence upon the whole record, makes the following findings of fact. The

Commission in making this decision has considered the positions and arguments of all of the parties. Failure to specifically address a piece of evidence, position, or argument of any party does not indicate that the Commission has failed to consider relevant evidence, but indicates rather that the omitted material was not dispositive of this decision.

Procedural History

In this consolidated proceeding, the Commission is considering Missouri Gas Energy's Actual Cost Adjustment for two years. Case Number GR-2002-348 was established on October 16, 2002, to track the over-recovery or under-recovery of MGE's natural gas costs for the Actual Cost Adjustment (ACA) period for 2001-2002. Case Number GR-2003-0330 was established on March 17, 2003, to review MGE's ACA for 2002-2003. The Commission consolidated the two cases for all purposes on April 12, 2005.

There were originally two contested issues in this consolidated case relating to adjustments that Staff asked the Commission to make to MGE's ACA balances. The first issue concerned an adjustment based on the alleged imprudence of MGE's contract with Mid-Kansas Pipeline Company and Riverside Pipeline Company for the interstate transportation of natural gas. The second issue concerned an adjustment based on Staff's contention that MGE imprudently purchased more pipeline capacity than it needs to serve its customers.

The first issue, regarding the alleged imprudence of the pipeline contract, was previously litigated in Commission Case Number GR-96-450, the case concerning MGE's 1996-1997 ACA. In its Report and Order in GR-96-450, the Commission found that Staff had failed to present competent and substantial evidence sufficient to raise a serious doubt

about the prudence of the pipeline contract. For that reason, the Commission rejected Staff's proposed disallowance for the 1996-1997 ACA. The Commission, however, found that it could not determine whether a stipulation and agreement from a still earlier case would preclude prudence reviews regarding that contract in future ACAs. Kansas Pipeline appealed that aspect of the Report and Order.

While that first issue was subject to appeal, the Commission could not address that issue in this case. Rather than wait for the results of that appeal, the Commission decided to set aside the question of the prudence of the pipeline contract and proceed to hear the other issue. Subsequently, the Commission held hearings concerning the second issue on August 28 and 29, 2006. Staff and MGE filed pre-hearing briefs on August 22, 2006. Staff, MGE and Public Counsel filed post-hearing briefs on October 23, 2006. Staff and MGE also filed proposed findings of fact and conclusions of law on October 23, 2006.

The appeal of the issue of the prudence of MGE's interstate pipeline contract with Mid-Kansas Pipeline Company and Riverside Pipeline Company followed a convoluted path through the appellate courts until it was finally resolved by a decision of the Missouri Supreme Court, issued on January 30, 2007.[1] The Supreme Court held that the Commission was precluded from considering the prudence of that contract by a stipulation and agreement approved by the Commission in an earlier case. In response to the Supreme Court's decision, Staff formally withdrew the Kansas Pipeline issue from this case in a notice of withdrawal of issue filed on May 18, 2007. The Commission is now free to decide the remaining issue.

[1] *State ex rel. Riverside Pipeline Co. v. Pub. Serv. Comm'n,* 215 S.W.3d 76 (Mo. 2007).

Proposed Disallowance for Excess Pipeline Capacity

Staff alleges MGE failed to properly plan for the amount of interstate pipeline capacity it needed to reserve to meet the needs of its customers. Because of that allegedly poor planning, Staff contends MGE imprudently failed to reduce its capacity on the Southern Star interstate pipeline when it renegotiated its contract with that pipeline in 2001. Staff claims MGE reserved a substantial amount[2] of decatherms per day in excess capacity on the Southern Star pipeline for the Kansas City and St. Joseph areas in both the 2001-2002 and 2002-2003 ACA periods. Staff calculated the cost of reserving that excess capacity in 2001-2002 as $2,041,931.[3] For 2002-2003, Staff calculated that cost as $2,015,661.[4] Based on these calculations, Staff proposed a disallowance for the two ACA periods totaling $4,057,592.

Background on Transportation of Natural Gas

When moving natural gas to its customers, a local distribution company (LDC), such as MGE, must use the services of an interstate pipeline to transport that gas from the production areas to the LDC's service area. At the time in question, MGE contracted with four interstate pipelines to transport the gas it needs to serve its customers: Southern Star Central f/k/a Williams Gas Pipeline – Central; Panhandle Eastern Pipe Line Company; Enbridge Pipelines; and Pony Express Pipeline.[5]

The amount of gas that can move through a pipeline is finite; only a certain number of gas molecules can been squeezed into the pipeline. When demand for gas is high, not

[2] The exact amount of capacity that Staff claims to be excessive is highly confidential.

[3] Jenkins Direct, Ex. 7, Page 37, Line 17.

[4] Jenkins Direct, Ex. 7, Page 38, Line 1.

[5] Kirkland Direct, Ex. 4, Page 10, Lines 16-21.

enough gas can be moved through the pipeline to satisfy the entire demand. Under those circumstances, the supply of gas to some users may have to be shut-off.

To avoid being shut-off, an LDC, or other shipper on the pipeline, can purchase reserved capacity on the pipeline. By purchasing reserved capacity, a shipper ensures that it will be able to move enough gas through the pipeline to meet its needs, even when demand for natural gas is high. Of course, reserving capacity on a pipeline costs money. Therefore, a shipper wants to purchase enough capacity to meet its needs, while not wasting money by purchasing too much capacity.

Design Day Demand

Firm capacity on the Southern Star pipeline, as on most interstate pipelines, is sold on a year-round basis. For that reason, MGE must plan to reserve enough pipeline capacity to transport the natural gas its customers will need on the one day during the year that the demand for gas will be at its highest. Since the greatest demand for gas in Missouri is for space heating in the winter, the day on which the demand for gas is likely to peak is the coldest day of the winter. Therefore, in order to determine how much capacity should reasonably be reserved, MGE must determine how cold a winter day can reasonably be anticipated and, more importantly, how much gas is likely to be used on that very cold day. MGE may be able to sell some of its unused pipeline capacity on days that demand does not peak, but having that capacity reserved and available is like an insurance policy protecting its customers' ability to obtain the gas they need when that very cold day arrives.

The day when usage is expected to peak is known as the design day because the system must be designed to be capable of meeting the demand for gas on that day. To

calculate the amount of gas it would need to supply on a design day, MGE undertook the following steps:

- Peak day demand from the prior year was identified and baseload was subtracted to calculate the heat load on this specific day.
- The HDD [heating degree days] for that day was identified and adjusted by MGE for wind.
- The heat load was then divided by the wind-adjusted HDD to calculate a heat load factor.
- The heat load factor was then applied to the MGE design temperature, which was a wind-adjusted 85 HDD.
- The baseload was then added to the heat load to produce the design day demand.[6]

In the context of these calculations, a peak day demand is the amount of natural gas actually used on the day in which the maximum amount of gas was delivered to customers in the previous year. Usually, that will be coldest day of the year.[7] Peak day demand is not the same as design day demand because the coldest day of a particular winter may not approach the coldest day that could occur. Baseload is the amount of gas that is likely to be used regardless of the outside temperature. It would include gas used in industrial processes as well as for home cooking and water heating to the extent that such usage is not affected by the weather. Heatload, in contrast to baseload, is the amount of gas usage that is dependent on the weather. Heating degree days are a measure of the amount by which the average temperature for the day is below 65 degrees, the level at which customers are likely to need to use gas to heat their homes. For example, a day in which the average temperature was 10 degrees would have 55 HDD.[8]

[6] Kirkland Surrebuttal, Ex. 6, Pages 13-14, Lines 21-23, 1-6.

[7] Reed Direct, Ex.1, Page 7, Lines 1-3.

[8] Jenkins Direct, Ex. 7, Page 12, Lines 8-11.

Staff's Challenge to MGE's Design Day Forecast

Determination of Coldest Day

Staff challenged the accuracy of several of inputs to MGE's calculations. First, in calculating the HDD for its forecasted design day, MGE looked at the coldest day reported at the Kansas City airport by Accu-Weather, Inc. That coldest day occurred on December 21, 1989, when the high temperature was 12 degrees below zero, the low was 23 degrees below, and the average wind speed was 14 miles per hour. That resulted in 83 HDD, which MGE adjusted to 85 HDD to account for the wind chill resulting from the high wind speeds.[9]

For its calculations, Staff used historical data from the National Oceanic and Atmospheric Administration's National Climatic Data Center to find a peak of 80.5 HDD occurring on December 22, 1989.[10] Staff did not adjust that figure to account for wind chill.

For purposes of the hearing, MGE engaged the services of an independent consulting firm, Concentric Energy Advisors, Inc., to perform its own evaluation of the design day forecasts of Staff and MGE. John Reed, Chairman and Chief Executive Officer of Concentric Energy Advisors,[11] testified that rather than use the coldest historical day, he calculated the coldest reasonably likely day by averaging the observed coldest day for the last 30 years, determining the standard deviation around that mean, and calculating a statistical value of 81.9 HDD as the coldest day likely to occur once in 100 years in Kansas City.[12]

---

[9] Kirkland Surrebuttal, Ex. 6, Page 14, Lines 27-32.

[10] Jenkins Direct, Ex. 7, Page 13, Lines 6-9.

[11] Reed Direct, Ex. 1, Page 1, Lines 12-15.

[12] Reed Direct, Ex. 1, Pages 27-28, Lines 20-23, 1-22..

Clearly, there are different ways to calculate the coldest day likely to be experienced in MGE's gas service area. The HDD figure used by MGE in calculating its design day gas needs is a few degrees higher than the figure used by either Staff or MGE's consultant, particularly because it is adjusted upward to account for wind chill. However, David Kirkland, MGE's Director of Gas Supply,[13] offered his expert opinion that industry standards permit the use of wind-adjusted temperatures in calculating design day gas needs.[14] Staff offered no evidence to rebut that opinion.

Application of Kansas City's Coldest Day to the Entire System

Staff also challenged MGE's decision to calculate the design day gas needs for its entire system based on the coldest temperature observed at the Kansas City airport. Approximately 15 percent of the gas drawn through MGE's system at peak demand is delivered to the Joplin area.[15] Since Joplin is approximately 160 miles south of Kansas City, it does not get quite as cold in the winter. For that reason, Staff uses the coldest temperature recorded at Springfield, Missouri, approximately 70 miles east of Joplin, to determine a HDD of 72.1 for Joplin.[16] MGE's consultant, John Reed, also used Springfield data to represent MGE's Joplin service area in making his calculations because no NOAA weather data is available for Joplin.[17] Using a 1-in-100 year likelihood of occurrence calculation, Reed determined a design day HDD of 76.3 for the Joplin service area.[18]

[13] Kirkland Direct, Ex. 4, Page 3, Lines 10-11.

[14] Transcript, Page 152, Lines 14-21.

[15] Transcript, Page 72, Lines 21-24.

[16] Jenkins Direct, Ex. 7, Page 17, Lines 16-18.

[17] Reed Direct, Ex. 1, Page 28, Lines 11-12.

[18] Reed Direct, Ex. 1, Page 28, Lines 18-19.

Reed explained that his analysis used a separate design day temperature for the Joplin service area because he believes that to be the best practice. Based on Reed's advice as a consultant, MGE has followed that practice in its reliability calculations for the years subsequent to the years in question. However, Reed states that MGE's use of the weather at a single observation point to determine design day temperature for the entire system is "well within industry norms" for the analysis it performed.[19] Again, Staff offered no evidence to rebut that opinion.

Calculation of Heatload Factor

Staff also challenged the accuracy of MGE's calculations of the heatload factor, in other words, the amount of gas usage that is dependent upon temperature. MGE calculated the heatload factor by determining the amount of gas actually used on its system on the single coldest day of the previous years, and then subtracting the baseload, the portion of gas used that is not dependent upon variations in temperature.

Staff roundly criticized MGE's approach for using only one data point each year to determine the heat load factor.[20] In contrast to MGE, Staff performed a regression analysis utilizing total daily usage data, both baseload and heatload, for every winter day for four winters between November 1, 1997, and March 31, 2001, to estimate MGE's heatload.[21] This method allowed Staff to rely on many more data points in making its calculations.

John Reed, the consultant hired by MGE, agreed with Staff that the use of multiple data points to measure gas usage on cold days was preferable to using only a single data

[19] Transcript, Page 114, Lines 10-25.

[20] Jenkins Direct, Ex. 7, Page 20, Lines 8-11.

[21] Jenkins Direct, Ex. 7, Page 21, Lines 11-13.

point.[22] However, the data used must also be appropriate, not just voluminous. The design day demand analysis prepared by Reed's consulting firm used the three highest demand days that were also within the ten coldest days for the four winters for which data was available.[23]

The use of multiple data points does not by itself create reliable results. Staff uses many data points, but its approach suffers from a fundamental flaw in that its regression analysis was premised on input data that was not representative of the data that was to be forecasted with the regression analysis.[24] By using data showing the amount of gas used on every winter day, including days that were quite warm, Staff predicted the amount of gas likely to be used on an average winter day. But the regression analysis should be predicting the amount of gas likely to be used during the extremely cold weather of a design day. Thus, Staff's calculations tend to understate the amount of gas likely to be needed on a design day.

Calculation of Baseload Factor

The other factor needed to calculate a design day demand is the baseload, in other words, the amount of gas used on the system that is not related to the weather. MGE, the consulting firm, and most other LDC's around the country, simply use the amount of gas dispatched during the summer months, when demand for space heating is zero, to establish the baseload.[25] Staff contends that baseload could be different in the winter than

[22] Transcript, Page 46, Lines 19-24.

[23] Reed Direct, Ex. 1, Page 36, Lines 7-9.

[24] Reed Direct, Ex. 1, Page 37, Lines 15-17.

[25] Reed Direct, Ex. 1, Page 33, Lines 4-13.

it is in the summer[26] and for that reason used the previously described regression analysis to determine winter baseload as well as heatload.[27]

Unfortunately, Staff's calculations do not reflect reality. Staff's estimate of baseload demand for Kansas City derived from its calculations are only about half of the actual demand on the system during the summer months when heatload is not a factor.[28] At the hearing, Staff speculated perhaps the summer baseload was affected by the use of natural gas by electric generating plants.[29] Staff, however, offered no evidence to support that speculation. Indeed, MGE has no interruptible load, which would be indicative of gas use by an electric power plant, on its system.[30]

Furthermore, the consultant hired by MGE tested Staff's regression equation by applying it to predict the amount of gas used on twelve actual high-demand cold-weather days in the past. That test revealed that Staff's equation under predicted the amount of gas actually used on those high-demand cold-weather days. For five of those twelve cold days, the under-prediction would exceed the reserve margin allowed by Staff's formula.[31]

In summary, Staff's calculations of the amount of gas MGE would need to meet design day requirements is flawed and understates the amount of gas likely to be needed. The separate forecast prepared by MGE's consultant, using best practices and avoiding the weaknesses that Staff identified in MGE's forecast, predicts gas usage that is very close to

[26] Jenkins Direct, Ex. 7, Pages 19-20, Lines 21-23, 1.

[27] Transcript, Page 255, Lines 18-24.

[28] Reed Direct, Ex. 1, Page 34, Lines 10-16.

[29] Transcript, Page 256, Lines 16-23.

[30] Transcript, Page 131, Lines 21-25.

[31] Reed Rebuttal, Ex. 2, Page 27, Lines 6-19.

the usage predicted by MGE.[32] Therefore, there is no basis for the Commission to conclude that MGE has overestimated the amount of gas it needs to meet design day demand or that MGE has contracted for surplus pipeline capacity.

The Determination of Appropriate Pipeline Capacity Requires More Than Just a Formula

Even if the Commission were to accept Staff's calculations and find that MGE had more pipeline capacity than indicated by those calculations, that finding would not establish that MGE had acted imprudently, and would not justify the disallowance proposed by Staff. The planning process for determining how much pipeline capacity should be purchased is more complicated than simply plugging some numbers into a formula and then buying the amount of capacity needed to match the results of the formula.

MGE, like other LDCs, must make decisions about how much pipeline capacity to reserve years in advance. Those decisions must take into account a number of factors, including "competitive market factors, economics, reliability, supply basin diversity, pipeline diversity, regulatory considerations and pipeline tariff requirements."[33] Natural gas pipeline companies periodically add capacity in large blocks that may not match the immediate needs of the LDC.[34] Therefore, an LDC must purchase capacity to meet its future needs when that capacity is available.

Staff contends its formula showed that MGE had more capacity than it immediately needed and proposed a disallowance based on that formula. Staff did not conduct any deeper evaluation of MGE's planning process. Indeed, Staff did not allege that any

[32] Reed Direct, Page 45, Lines 4-15.

[33] Kirkland Direct, Ex. 4, Page 8, Lines 9-11.

[34] Kirkland Direct, Ex. 4, Page 8, Lines 11-14.

particular action by MGE was imprudent, other than to argue that MGE could have reduced its capacity by the amount specified by Staff when it renegotiated its contract with Southern Star Central pipeline effective June 2001.[35]

MGE explained that capacity on Southern Star Central is low cost capacity that has access to different supply basins. It is the only pipeline that serves all three of MGE's service regions, affording MGE certain administrative and operational benefits across those regions.[36] Furthermore, if MGE had relinquished pipeline capacity on Southern Star Central to comply with Staff's formula, it also would have been required to relinquish a portion of its valuable gas storage capacity on that pipeline.[37]

In addition, at all relevant times, Southern Star Pipeline was fully subscribed. That means any capacity MGE relinquished to comply with Staff's formula would likely be sold to another shipper and would no longer be available to MGE to meet future needs.[38] As demand for gas increases, MGE will likely need additional capacity.[39]

Even assuming that MGE could repurchase the relinquished capacity in the future, the cost of repurchasing that capacity would likely increase because Federal Energy Regulatory Commission (FERC) policy requires that any future pipeline capacity expansion be priced at a higher incremental rate charged to new customers.[40] Staff admittedly did not consider this fact in its analysis.[41] As David Kirkland explained for MGE, "Staff is

---

[35] Jenkins Direct, Ex. 7, Pages 29-30, Lines 21-23, 1-10.

[36] Kirkland Rebuttal, Ex. 5, Page 40, Lines 10-14.

[37] Kirkland Rebuttal, Ex. 5, Page 41, Lines 1-4.

[38] Kirkland Rebuttal, Ex. 5, Page 40, Lines 14-16.

[39] Reed Direct, Ex. 1, Page 45, Lines 18-19.

[40] Reed Surrebuttal, Ex. 3, Pages 6-7, Lines 17-24, 1-3.

[41] Transcript, Pages 202-203, Lines 14-25, 1-10.

suggesting that MGE reduce the most flexible capacity asset it has, which is also low-cost, to achieve a short term capacity reduction but at a potentially much higher long-term cost."[42]

The long-term cost of underestimating pipeline capacity needs could be very high indeed. Aside from the possible need to repurchase capacity at higher rate, the cost of failing to reserve enough pipeline capacity to supply the natural gas needed to meet customer needs on a truly cold day could be catastrophic, both in terms of dollars, as well as in human life. A shortage of capacity could require the curtailment of gas deliveries to some customers or even loss of service to all customers in an area.[43] If service were lost to an area, MGE would have to undertake a costly and time consuming process to shut off service lines, relight pilot lights, and check for leaks, before restoring service.[44] During this process, customers would be sitting in cold homes in what could be sub-zero temperatures. MGE's consultant estimated that such a capacity shortfall in the Kansas City area could cost MGE several hundred million dollars.[45]

CONCLUSIONS OF LAW

The Missouri Public Service Commission has reached the following conclusions of law.

Jurisdiction

[42] Kirkland Rebuttal, Ex. 5, Page 40, Lines 19-22.

[43] Kirkland Direct, Ex. 4, Page 9, Lines 8-11.

[44] Reed Rebuttal, Ex. 2, Page 35, Lines 4-19.

[45] Reed Rebuttal, Ex. 2, Page 37, Lines 1-8.

MGE is a public utility, and a gas corporation as those terms are defined in Section 386.020(18) and (42), RSMo 2000. As such, MGE is subject to the Commission's jurisdiction pursuant to Chapters 386 and 393, RSMo Supp. 2006.

Burden of Proof:

Section 393.130.1, RSMo Supp. 2006, requires that all charges made or demanded by any gas corporation be just and reasonable. Section 393.150.2, RSMo 2000, provides that in any hearing involving a rate increase, the gas corporation proposing such rate increase has the burden of proving that the proposed increased rate is just and reasonable. The Commission has also held that the gas corporation has the burden of showing that the gas costs that it proposes to pass on to ratepayers through operation of its PGA tariff are just and reasonable.[46]

The Prudence Standard:

It is not, however, sufficient to state that MGE, as the gas corporation, has the burden of proving that its gas costs are just and reasonable. The fact that Staff is challenging the prudence of incurring some of those costs brings into effect an additional standard, the prudence standard.

The Commission established its prudence standard in a 1985 case involving the costs incurred by Union Electric Company in constructing its Callaway nuclear plant.[47] In determining how much of those costs were to be included in Union Electric's rate base, the

[46] *In the Matter of Tariffs filed by Western Resources, Inc., d/b/a Gas Service, a Western Resources Company, to Reflect Rate Changes to be Reviewed in the Company's 1992-1993 Actual Cost Adjustment,* 3 Mo. P.S.C. 3rd 480, 488 (1995).

[47] *In the Matter of the Determination of In-Service Criteria for the Union Electric Company's Callaway Nuclear Plant and Callaway Rate Base and Related Issues. In the Matter of Union Electric Company of St. Louis, Missouri, for Authority to File Tariffs Increasing Rates for Electric Service Provided to Customers in the Missouri Service Area of the Company,* 27 Mo. P.S.C. (N.S.) 183, 192-193 (1985).

Commission adopted a standard for determining the prudence of costs that had been established by the United States Court of Appeals, District of Columbia, in a 1981 case.[48] The standard adopted by the Commission recognizes that a utility's costs are presumed to be prudently incurred, and that a utility need not demonstrate in its case-in-chief that all expenditures are prudent. "However, where some other participant in the proceeding creates a serious doubt as to the prudence of an expenditure, then the applicant has the burden of dispelling those doubts and proving the questioned expenditures to have been prudent."[49]

The Commission, in the Union Electric case, further recognized that the prudence standard is not based on hindsight, but upon a reasonableness standard. The Commission cited with approval a statement of the New York Public Service Commission that:

> . . . the company's conduct should be judged by asking whether the conduct was reasonable at the time, under all the circumstances, considering that the company had to solve its problem prospectively rather than in reliance on hindsight. In effect, our responsibility is to determine how reasonable people would have performed the tasks that confronted the company.[50]

Since its adoption, the Commission's prudence standard has been recognized by reviewing courts[51] and has been accepted by all parties as the standard to be applied in this case.

---

[48] *Anaheim, Riverside, Etc. v. Fed. Energy Reg. Comm'n,* 669 F.2nd 799, 809 (D.C. Cir. 1981).

[49] *Union Electric*, 27 Mo. P.S.C. (N.S.) 183, 193 (1985).

[50] *Union Electric*, at 194, quoting *Consolidated Edison Company of New York, Inc*., 45 P.U.R. 4th 331 (1982).

[51] *See. e.g. State ex rel. Associated Natural Gas Company v. Pub. Serv. Comm'n*, 954 S.W.2d 520, 529 (Mo. App. W.D. 1997).

DECISION

After applying the facts as it has found them to its conclusions of law, the Commission has reached the following decision regarding the issue identified by the parties.

Staff contends that MGE imprudently failed to properly analyze its pipeline capacity needs and for that reason failed to reduce its capacity to a level established by Staff's analysis. On that basis, Staff urges the Commission to disallow over $4 million of MGE's costs for the two ACA periods under review.

Staff seems to base its proposed disallowance on the premise that MGE must prove that it properly documented its planning process and therefore acted imprudently in determining whether to reduce its pipeline capacity during these ACA periods. However, MGE's actions are presumed to be prudent, and it is Staff's burden to overcome that presumption of prudence by demonstrating a serious doubt about the prudence of those decisions. Staff has not met that burden.

Staff attempted to raise a serious doubt about MGE's planning process by contending that the company's planning process was sloppy and undocumented. In fact, MGE was able to demonstrate that its method of determining its capacity needs was documented and was well within the norms of the industry. The reasonableness of MGE's calculations were further demonstrated by the independent "best practices" evaluation performed by Concentric Energy Advisors, which demonstrated a capacity need in line with the need calculated by MGE. On the other hand, Staff's flawed calculations seriously underestimated the amount of pipeline capacity that MGE would need on a very cold day.

At most, Staff showed that MGE's decisions about pipeline capacity were conservative. Perhaps MGE's service area will never again experience the extreme cold temperatures that would create the gas demand predicted to occur on a design day. Perhaps MGE could save an average customer a few dollars per year by reducing its pipeline capacity. However, the cost of running short of gas on a design day is so staggeringly high that a conservative approach is the prudent approach.

Staff has failed to create a serious doubt about the prudence of MGE's actions and its proposed disallowance will be denied.

IT IS ORDERED THAT:

1. The disallowance proposed by Staff regarding excess pipeline capacity is denied.

2. MGE shall establish the appropriate account balances for its 2001-2002, and 2002-2003 actual cost adjustments.

3. This Report and Order shall become effective on October 12, 2007.

BY THE COMMISSION

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Murray, Clayton, Appling
and Jarrett, CC., concur;
And certify compliance with the
Provisions of Section 536.080, RSMo.

Dated at Jefferson City, Missouri,
on this 2nd day of October, 2007.