EXHIBIT

Exhibit No.:	
Issue(s):	Rate Design
Witness/Type of Exhibit:	Meisenheimer/Rebuttal
Sponsoring Party:	Public Counsel
Case No.:	GR-2006-0422

REBUTTAL TESTIMONY

OF

BARBARA A. MEISENHEIMER

Submitted on Behalf of the Office of the Public Counsel

MISSOURI GAS ENERGY
(RATE DESIGN)

CASE NO. GR-2006-0422

November 21, 2006

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Missouri Gas Energy's Tariff Sheets Designed to Increase Rates for Gas Service in the Company's Missouri Service Area	))))	**Case No. GR-2006-0422**

AFFIDAVIT OF BARBARA A. MEISENHEIMER

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Barbara A. Meisenheimer, of lawful age and being first duly sworn, deposes and states:

1. My name is Barbara A. Meisenheimer. I am Chief Utility Economist for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony consisting of 29 pages.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

Barbara A. Meisenheimer

Subscribed and sworn to me this 21st day of November 2006.

NOTARY PUBLIC NOTARY SEAL STATE OF MISSOURI

JERENE A. BUCKMAN
My Commission Expires
August 10, 2009
Cole County
Commission #05754036

Jerene A. Buckman
Notary Public

My Commission expires August 10, 2009.

REBUTTAL TESTIMONY

OF

BARBARA MEISENHEIMER

CASE NO. GR-2006-0422

MISSOURI GAS ENERGY

Q. PLEASE STATE YOUR NAME, TITLE, AND BUSINESS ADDRESS.

A. Barbara A. Meisenheimer, Chief Utility Economist, Office of the Public Counsel, P.O. 2230, Jefferson City, Missouri 65102.

Q. HAVE YOU TESTIFIED PREVIOUSLY IN THIS CASE?

A. Yes. I filed direct testimony on the issues of class cost of service and rate design.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. In this testimony I will respond to the direct testimony of Staff witnesses Anne Ross, Michael Ensrud and Company witness Russell Feingold.

Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY.

A. My rebuttal testimony addresses the following issues;

1. The Company by way of the Straight-Fixed Variable Charge (SFV) proposal and Staff by way of the Delivery Charge (which is also a SFV) seek drastic rate design changes in this case that will substantially increase the rates for many low use residential customers. Both rate design proposals would collect all non-gas revenue in a flat fixed charge eliminating the current rate structure that recovers a portion of non-gas costs in a fixed customer charge and the remainder of costs through a volumetric rate. For good reasons, these types of rate structures were rejected by Staff's Senior Economist Dr. Michael Proctor just a few years ago. Dr. Proctor argued that such rate structures would be detrimental to low use customers. He was absolutely correct. Low use customers pay significantly more under the Staff and Company SFV proposals.

2. The Staff proposes to deny necessary winter heating to seasonal residential customers unless those customers pay the Company the same non-gas revenue as customers receiving year-round service. The Company proposal would recapture lost charges for customers who leave the system voluntarily for up to seven months but would not impose the charge for customers disconnected for non-payment. The Staff's proposal would eliminate a customer's ability to avoid current non-gas volumetric based charges by forgoing service for at least 12 months. The Company's proposal would eliminate a customer's ability to avoid current non-gas volumetric based charges by voluntarily forgoing service for at least 7 months.

3. As an alternative, the Company proposes to couple an increase in the customer charge with a weather normalization adjustment (WNA). The WNA would correct for revenue lost from customer conservation or warmer than normal weather by way of a variable adder to the non-gas volumetric rate. To customers attempting to lower their bill through conservation measures, the Company's WNA proposal would be more aptly labeled a conservation mitigation rate design.

4. In MGE's last rate case, this Commission rejected proposals to collect more than 55% of non-gas revenue through the fixed customer charge recognizing that the WNA the Company proposed in the last case would effectively create another fixed charge and impede customers' ability to benefit from conservation efforts. The SFV proposals by the Company and Staff will result in a 100% customer charge. Both the SFV and WNA proposals reduce the ability to benefit from conservation.

5. Both the Company and Staff rate design proposals insulate the Company from virtually all weather risk while proposing no meaningful protection for many customers from upward volatility of gas commodity prices that constitute the lion's share of a customer's bill. Further, these "weather proof" rate design proposals are not accompanied by proposals to significantly lower the Company's rate of return to reflect the elimination of risk. The Company has proposed to increase funding to its low-income weatherization program. Public Counsel supports the proposal for increased low-income weatherization. The Staff has proposed no conservation programs despite heavily relying on the promotion of conservation as a primary driver in proposing its rate design.

6. The Company WNA proposal is premature and not accompanied by a symmetric proposal for annual true-ups as was contemplated by the

Legislature in Senate Bill 179. If the Company experiences customer growth, the Company's WNA will recover more than the test-year revenue requirement established in this rate case.

Q. DO YOU HAVE COMMENTS REGARDING THE CLASS COST OF SERVICE STUDY FILED IN YOUR DIRECT TESTIMONY?

A. Yes. The parties have agreed to an equal percentage increase to customer classes, so class cost of service issues will have been resolved upon approval by the Commission. However, although I continue to believe that the RSUM method is reasonable, I do acknowledge that this Commission previously rejected it. It was not my intention to rehash issues in this case related to a mains allocation method that the Commission previously rejected. If the Commission does not accept the parties' resolution of class revenue responsibility, Public Counsel would support the use the Staff allocator in determining class costs.

Q. PLEASE SUMMARIZE THE STAFF'S BASE RATE DESIGN PROPOSALS.

A. Staff witness Anne Ross proposes that the Company's residential customers pay a fixed delivery charge designed to recover all district specific non-gas costs based on the Staff's proposed revenue requirement. (Ross Direct, Page 1, Line 19) The delivery charge would be calculated by dividing the annual residential class rate revenues by the number of bills. The effect would be that the Company would collect from each residential customer exactly the same non-gas revenue regardless of consumption. Based on Staff's revenue requirement, Ms. Ross calculates a delivery charge of $23.48. (Ross Direct, Page 13, Line 7)

Staff further suggests that it may be appropriate to split the small business class into a small and a medium general service class. However, Staff proposes that research is needed to determine a "fair" delivery charge on the smaller general service customers so the Staff proposes that all general service customers retain the existing rate structure consisting of a customer charge and volumetric charge. (Ross Direct, Page 16, Line 18 through Page 17, Line 12)

In addition to the delivery charge, Staff witness Michael Ensrud presents Staff's proposal for recouping all non-gas revenues associated with seasonal disconnects. It appears that the Staff proposes the charge would apply to only residential customers. Under the Staff's proposal a customer reconnecting within 12 months would be required to pay all delivery charges for the months the customer was disconnected. This would result in part-time customers paying the Company the same non-gas revenue as customers receiving year-round service. The Staff proposes that the policy apply even for involuntary disconnects

Q. WHAT RATE DESIGN DOES MGE PROPOSE?

A, The Company's primary proposal for residential rates is a Straight-Fixed Variable rate design that will collect all non-gas cost through a flat fixed $27.50 Basic Service Charge. The primary proposal for small general service is to increase the customer charge to collect a larger proportion of class costs. The remaining SGS cost would be collected through volumetric rates. The primary proposal for LGS and LV is to retain the existing rate structure.

As an alternative, the Company proposes an increase in the current customer charge coupled with a Weather Normalization Adjustment for the Residential, SGS and LGS classes. The WNA would correct for revenue lost from customer conservation or warmer than normal weather by way of a variable adder to the non-gas volumetric rate from October through May. The Company proposes a $15.50 Customer Charge for Residential customers and a $20.50 Customer Charge for SGS.

The Company proposes a seasonal reconnection charge for residential customers that would recapture charges from customers who leave the system voluntarily for up to seven months but would not impose the charge for customers disconnected for non-payment.

Q. IS THE STAFF DELIVERY CHARGE SIMILAR TO THE BASIC SERVICE CHARGE INCLUDED IN MGE'S PRIMARY RATE DESIGN PROPOSAL FOR A STRAIGHT-FIXED VARIABLE RATE DESIGN?

A. Yes. The Staff Delivery Charge appears to be conceptually the same as the Basic Service Charge contained in the Company's Straight-Fixed Variable proposal in that all non-gas cost will be collected through an unavoidable flat fixed rate.

Q. WHAT ARE YOUR PRIMARY CONCERNS WITH THE COMPANY'S PRIMARY SFV AND STAFF'S DELIVERY CHARGE PROPOSAL FOR RESIDENTIAL RATES?

A. I have a number of concerns with these residential rate proposals.

Q. PLEASE DISCUSS YOUR FIRST CONCERN.

A. The proposals will substantially increase the non-gas rates paid by low-use residential customers

Q. HAVE YOU PERFORMED AN ANALYSIS TO EVALUATE THE RANGE OF RESIDENTIAL CUSTOMER IMPACTS THAT COULD RESULT FROM THESE RATE DESIGN PROPOSALS?

A. Yes. Table 1 shown below is based on Staff's test-year residential base rate revenue. It compares non-gas recovery under the current rate structure to the range of impacts resulting from collecting all non-gas revenue through a fixed flat charge like those proposed by Staff and the primary Company recommendation.

Table 1

Average Monthly CCF	Current Customer Charge	Current Volumetric Rate	Current Non-Gas Revenue	Flat Charge at Current Revenue	Percentage Change
25	$11.65	$0.13187	$14.95	$21.45	43%
50	$11.65	$0.13187	$18.24	$21.45	18%
75	$11.65	$0.13187	$21.54	$21.45	0%
100	$11.65	$0.13187	$24.84	$21.45	-14%
125	$11.65	$0.13187	$28.13	$21.45	-24%
150	$11.65	$0.13187	$31.43	$21.45	-32%
175	$11.65	$0.13187	$34.73	$21.45	-38%
200	$11.65	$0.13187	$38.02	$21.45	-44%
225	$11.65	$0.13187	$41.32	$21.45	-48%
250	$11.65	$0.13187	$44.62	$21.45	-52%
275	$11.65	$0.13187	$47.91	$21.45	-55%
300	$11.65	$0.13187	$51.21	$21.45	-58%

As illustrated in Table 1, the lowest use customers would pay 43% more while the highest use customers pay 58% less.

Q. ARE THE USAGE LEVELS ILLUSTRATED IN TABLE 1 CONSISTENT WITH THE RANGE OF USE FOR ACTUAL MGE CUSTOMERS?

A. Yes. In an updated response to Staff Data Request No. 134 Staff witness Tom Solt obtained a stratified sample of actual residential customer use data categorized by levels of annual use ranging from those using up to 25 CCF to those using over 600 CCF. The range of average monthly use illustrated above (25 to 300 CCF) is consistent with the range of average monthly use for customers from the Data Request Response sample. I want to be clear that this example is specifically designed to show the impact on low and high use customers.

Q. HOW DOES YOUR EXAMPLE OF CUSTOMER IMPACTS DIFFER FROM MR. FEINGOLD'S EXAMPLES SHOWN ON PAGE 2 OF SCHEDULE RAF-11 OF HIS DIRECT TESTIMONY?

A. Mr. Feingold's Schedule includes commodity revenue from PGA rates which are not at issue in this case. By adding in commodity revenue, Mr. Feingold's results mask the percent increase in the non gas rates that are the issue.

Q. HAS THE STAFF PREVIOUSLY REJECTED PROPOSALS TO RECOVER ALL NON-GAS COSTS THROUGH A FIXED CHARGE DUE TO CONCERNS REGARDING THE POTENTIAL DETRIMENT TO LOW USE CUSTOMERS?

A. Yes. The detrimental impact on low use customers of full non-gas recovery through a fixed flat rate like the Staff's proposed Delivery Charge and the Company's primary proposal was foreseen by Staff witness Dr. Michael Proctor in his Surrebuttal in Laclede Gas Case No.

GR-2002-356. In testimony responding to Laclede's proposed weather mitigation rate design proposal, Dr. Proctor explained: "While the Staff favors using rate design as a weather mitigation measure, because of the detrimental impact on small users, the **Staff was not willing to recommend recovering all of the non-gas costs in** either **the customer charge**, first block rate or a combination of these rate components...." The Staff and Company primary proposals have exactly the effect that Dr. Proctor rejected because they are mechanisms designed to collect all non-gas costs through a monthly customer charge.

The Staff had access to the same data I did from which I concluded the delivery charge would be detrimental to low use customers. I assume Staff reviewed the information since Staff requested it from the Company. Despite access to this information, the Staff fails to explain its complete turn-about in policy and why the detrimental impact to small users identified by Dr. Proctor is no longer a concern to Staff.

Q. HAS THE COMMISSION REJECTED EXCESS RECOVERY OF NON-GAS REVENUE THROUGH A FIXED CUSTOMER CHARGE?

A. Yes. In MGE's last rate case, No. GR-2004-0209, this Commission rejected proposals to collect more than 55% of non-gas revenue through the fixed customer charge. The Staff Delivery Charge and the Company's primary proposal would collect 100% of non-gas revenue through the fixed customer charge. Both proposals should be rejected.

Q. WHAT IS ANOTHER CONCERN WITH THE STAFF'S DELIVERY CHARGE AND COMPANY'S PRIMARY PROPOSAL?

A. The proposals would collect all non-gas revenue in a flat fixed charge eliminating the current non-gas rate structure under which customers who use more pay more. At page 15, line 10, Staff witness Ross's testimony in GR-2006-0387, she acknowledged that customers may feel that such a structure is unfair.

Q. MS. ROSS AND MR. FEINGOLD SUGGEST THAT CUSTOMERS ARE USED TO RATE STRUCTURES LIKE THE STAFF DELIVERY CHARGE AND COMPANY PRIMARY PROPOSAL FOR OTHER SERVICES THEY BUY SUCH AS CABLE TELEVISION, PHONE SERVICE AND TRASH SERVICE. ON PAGE 38 OF HIS TESTIMONY MR. FEINGOLD SUGGESTS ADDITION EXAMPLES OF INTERNET ACCESS, HOME ALARM SYSTEMS, AUTO LEASES AND LOANS AND APARTMENT RENT. PLEASE RESPOND TO CLAIMS THAT THE CHARGE FOR THESE SERVICES IS LIKE THE STAFF'S DELIVERY CHARGE AND THE COMPANY'S PRIMARY PROPOSAL.

A. They are over simplistic and inaccurate. Cable television and phone service are more like the traditional rate structure for gas services than they are like the all-you-can-eat charges proposed by Staff and the Company. Cable television and phone service include both fixed and a variable rate components. Even trash pick-up in certain cases costs more for greater use. Cable television and satellite television rates are set so that as I demand either more services "over the pipe" or "a larger pipe" I pay more. I can only subscribe to basic satellite or basic cable for a fixed minimum charge. In order to receive a greater variety of channels,

pay-per-view movies or high speed internet I pay additional incremental charges-the more services and capacity I demand, the more I pay. One might argue that in these cases, I am demanding services more akin to the gas commodity but again, this type of argument over simplifies the payment structure. Cable and Satellite companies are both retail service providers and access providers. In addition to charging you a monthly fee for a minimum bundle of broadcasting, they also receive compensation from other service companies that offer additional programming for an incremental charge. A portion of a customer payment of these incremental charges for additional programming flows back to the underlying access provider. This is also true with respect to phone service. For example, my telephone provider offers basic service that costs about $20 per month including fees and taxes. The same phone line is used to provide DSL, vertical and custom calling features and long distance service. Using my local company's long-distance or subscribing to custom calling features also increases my monthly charges. If I use a different provider for long distance service, a portion of the payment made directly to that provider flows back to my local phone company in the form of access rates that are generally charged as per minute rates to alternative providers using my local company's service lines. In the case of DSL it is even clearer that the more I use, the more I pay. Demand for higher speed access in the phone world is akin to demanding more capacity in the gas world. My local telephone company provides DSL over existing phone lines. To subscribe to access at 256 kbps costs $24.95, access at 1.5 Mbps costs $39.95 per month and access at 3.0 Mbps costs $49.95. The faster access I demand the more I pay. With respect to local service in Missouri, even the price for

local telephone service is not necessarily fixed. Local Measured Service, Extended Area Service and some tiers of the Metropolitan Calling Area Plans are all basic local services for which customers pay an additional rate to use the facilities more. Apartment rentals are also not like the all-you-can-eat Staff Delivery Charge and Company primary proposal. Generally in an apartment complex, apartments with more space cost more per month. Commercial rentals are often based on the square foot measurement of the space rented. In both cases, when I use more, I generally pay more. Auto leases and loans vary by the model of car and type and number of features demanded by the customer. One would not reasonably expect to pay the same lease payment or loan payment for a KIA as for a Lexus. Additionally, lease payments are often tied to mileage. If you exceed the contracted mileage, you may be required to pay more. Even the rate for trash service may not be as simple as one might believe. I live in a city where a minimum trash service is provided as a utility service through the City. However, this minimum service includes only once a week pick-ups and occasional collection of large items such as discarded appliances. I recently had the shingles on my roof replaced. When I contacted the City office to arrange for collection of the old shingles I found that I had to pay at least an extra $100 for use of a dumpster and hauling to the local dump. The larger the dumpster I would need and the longer it was needed, the higher the cost. Likewise, if I need a discarded appliance hauled away anytime other than during the regularly scheduled collections I must pay an additional $20. Even in the case of trash service, when I use more than the basic service, I pay more.

I would also like to point out that Cable TV and phone service policies even when provided in a monopoly environment are unlike the Company and Staff seasonal reconnection proposals. If I voluntarily disconnect and reconnect at a later date, I won't be back billed for the months I did not take service despite dedicated facilities still being in place to serve me.

Q. WHAT IS YOUR NEXT CONCERN REGARDING THE STAFF'S PROPOSED DELIVERY CHARGE PROPOSAL?

A. The Staff has made no recommendation to lower the Company's return to reflect lower risk.

Q. IN CASE GR-2002-356 WHERE A WEATHER MITIGATING RATE DESIGN WAS APPROVED, WAS REDUCED RISK CONSIDERED IN ESTABLISHING THE REVENUE REQUIREMENT?

A. Yes. In settling the Laclede rate case in which Laclede secured an experimental weather mitigation rate design the parties specifically considered reduced level of risk resulting from the rate design in crafting a settlement. As was explained in the Stipulation; "It is also understood that the impact of such weather mitigation rate design on the Company's risk has been given consideration in the settlement of the issues in this case."

Q. WHAT IS THE STAFF AND COMPANY STATED JUSTIFICATIONS FOR RECOVERING ALL NON-GAS COSTS THROUGH A FIXED RATE?

A. Ms. Ross lists what she refers to as two "significant current issues" affecting the natural gas distribution market that the Staff believes the delivery charge will address. The first she

claims is that it will remove disincentives for utilities to encourage and assist customers in making conservation and efficiency investments. She goes on to argue that the second issue the delivery charge will address is to reduce the effects of weather on utility revenues and customer bills and to provide utilities the "opportunity to earn their Commission-ordered non-gas revenue requirement - no more and no less- and insure that Residential customers pay for the price of providing their service-no more-no less ." (Ross Page 5, Line 9)

It is interesting to note that on Page 37, Lines 1-12, in which Mr. Feingold describes what he believes are the benefits to the Company and customers of full non-gas recovery through a fixed rate, he fails to include conservation benefits to consumers produced by the Company hopping on the conservation bandwagon as Ms. Ross predicts. At Page 16, Line 10, she postulates that once the utility's concern regarding revenue loss due to lowered sales has been addressed, the utility should be a creative, active and knowledgeable leader in the conservation effort.

In addition to the justifications of revenue stability for the Company and customers' paying "their costs" listed by Staff, on page 37 if direct testimony, Mr. Feingold lists bill stability, simplicity and understandability, fewer complaints, reduced rate case frequency, simplified forecast and adjustments lower ABC bill true-ups

Q. DOES PUBLIC COUNSEL BELIEVE THAT THE ABOVE ARGUMENTS ARE VALID REASONS TO IMPOSE FULL NON-GAS RECOVERY THROUGH A FLAT FIXED CHARGE?

A. No.

Q. PLEASE RESPOND TO THE CLAIM THAT A DELIVERY CHARGE WILL REMOVE DISINCENTIVES FOR UTILITIES TO ENCOURAGE AND ASSIST CUSTOMERS IN MAKING CONSERVATION AND EFFICIENCY INVESTMENTS.

A. The first point I would like to make is that full non-gas recovery through a flat fixed charge creates a trade off between dollars the customer could save under the current structure and those he might save associated with unspecified activities of the Company in the future. Today, a customer can reduce the **non-gas volumetric** and **commodity** portions of his bill by reducing consumption. He can also avoid **customer charges** by forgoing service. Full non-gas recovery through a flat fixed charge coupled with the proposal to allow the Company to recoup revenue from seasonal disconnects would eliminate any ability for a customer to reduce either **non-gas volumetric** or **customer charges**. Without requiring specific Company actions that will result in actual customer savings, the customer's incentive to conserve actually diminishes under the Staff and Company's primary proposals.

It is also not clear that any incentive created by granting a Company "guaranteed" recovery of non-gas costs will spur it to eagerly or even willingly pursue and promote widespread customer conservation that results in savings on the commodity portion of customers' bills. Instead, a Company would likely still have disincentives to encourage conservation and efficiency generally throughout its customer base unless it was also granted recovery of all conservation related costs as well as compensation for any net loss in

purchased gas cost. The Company has proposed additional low-income weatherization funding but has not proposed new conservation or efficiency programs for the broader customer base. Although Ms. Ross aggressively seeks to eliminate the customer's ability to influence the non-gas portion of their bills and devotes a substantial portion of her testimony extolling the benefits of conservation and efficiency, the Staff has made no specific conservation of efficiency proposals in this case. The Company and Staff proposals are one-sided benefiting the Company through guaranteed recovery and inaction while securing no benefit for the average customer in exchange. The proposals should be rejected.

One incentive to the Company associated with the delivery charge proposal is that it would still have an incentive to grow customer base and promote additional uses for gas services in order to generate return on additional investments. Encouraging more potential customers to use gas or existing customers to use more gas appliances will not lower commodity prices in the natural gas market.

Q. PLEASE RESPOND TO CLAIMS THAT FULL RECOVERY THROUGH A FLAT FIXED CHARGE WILL REDUCE THE EFFECTS OF WEATHER ON UTILITY REVENUES AND WILL PROVIDE UTILITIES THE OPPORTUNITY TO EARN THEIR COMMISSION-ORDERED NON-GAS REVENUE REQUIREMENT – NO MORE, AND NO LESS.

A. Contrary to witness Ross's apparent logic on this issue, the Commission's ordered non-gas revenue requirement is not a fixed or guaranteed level of revenue that a Company is entitled to recovery each year. Instead, the level of revenue requirement approved by the

Commission is a target level of costs including expenses, taxes and return on investment that an efficiently run company, barring unforeseen events has the opportunity to recover under long term average weather conditions. The Commission approved revenue requirement accounts for and is intricately related to potential weather variations that may affect costs and revenues from year to year. The process of normalizing demand determinates to account for weather and establishing a rate of return sufficient to attract investment despite the risk of weather variations are probably the two most obvious elements linking weather variations to revenue requirement. After the revenue requirement is determined, rates are set at a level anticipated to recover the target level of costs. However, the ratemaking process only reflects the anticipated cost and revenues at a snap shot in time. It does not guarantee or limit levels of either future costs or revenues and is not designed or intended to provide uniform recovery each year. Once rates are set, by efficiency or luck a Company has an opportunity to earn a return above that incorporated in the revenue requirement. Likewise, by inefficiency or luck a Company faces the potential to earn a return below that incorporated in the revenue requirement. This process mimics a competitive business environment by creating incentives for the Company to minimize costs.

Neither of the Company's rate design proposals nor the Staff's delivery charge proposal is consistent with the purposes of utility regulation. Utility regulation does not create an "entitlement" for the utility to earn a Commission determined return that fully compensates the utility for its cost of service. If that were the case, there would be no reason

to determine an appropriate level of a risk adjusted return that should be included in a utility's rates. Instead, utility regulation is intended to mimic the outcomes and market environment that is faced by competitive firms. The use of utility regulation to simulate a competitive environment and encourage the benefits that would accrue if the industry were suitable for a competitive structure has been referred to as the competitive market paradigm. This paradigm was described by Dr. James Bonbright on page 93 of *Principles of Public Utility Rates* in the following manner:

> Regulation, it is said, is a substitute for competition. Hence its objective should be to compel a regulated enterprise, despite its possession of complete or partial monopoly, to charge rates approximating those which it would charge if free from regulation but subject to market forces of competition. In short, regulation should be not only a substitute for competition, but a closely imitative substitute.

While viewed by investors as undesirable, earnings uncertainty serves an important role in the efficient operation of competitive markets by providing inherent protections for consumers. Earnings uncertainty motivates competitive business entities to minimize costs and to strive for customer satisfaction. Eliminating earnings uncertainty in a regulated environment would have a similar detrimental affect on consumers as would eliminating earnings uncertainty in an unregulated market. However, in a competitive environment, consumers retain the ability to reduce or forgo purchases in response to excessive prices or poor service.

In recognition and in consideration of the service it provides as a natural monopoly, a local gas distribution company is granted an additional concession not ordinarily available in a competitive business environment. It is allowed to request a rate review to, when justified, realign revenue to costs. This concession together with other concessions made by the PSC and other governmental entities more than adequately addresses issues of potential under earnings. For example, direct pass through of costs such as those flowed through the PGA, have substantially shifted weather related risks to consumers. It is undesirable and unnecessary to shift all earnings risk to consumers.

Q. CAN YOU CITE ANY ANALYSIS BY A RECOGNIZED UTILITY INDUSTRY EXPERT THAT SUPPORTS YOUR BELIEF THAT UTILITY COMMISSIONS GENERALLY SET RATES AT A LEVEL WHICH ALLOWS UTILITIES THE OPPORTUNITY (AS OPPOSED TO A GUARANTEE) TO ATTAIN THEIR AUTHORIZED RETURN?

A. Yes, the following quote from page 202 of A. J. G. Priest's *Principles of Public Utility Regulation* supports this widely recognized regulatory principle:

> ...the utility's return allowance might be compared with a fishing or hunting license with a limit on the catch. Such a license does not guarantee that the holder will catch anything at all; it simply makes the catch legal (up to a specified limit) provided the holder is successful in his own efforts.

Q. PLEASE RESPOND TO THE CLAIM THAT FULL RECOVERY THROUGH A FLAT FIXED CHARGE WILL REDUCE THE EFFECTS OF WEATHER, STABILIZE CUSTOMERS' BILLS AND MAKE BILLS MORE UNDERSTADABLE.

A. I agree that that it will reduce the affect of weather on customers' bills but I disagree that mandatory imposition of such an affect as would occur under the Staff's delivery charge proposal or the Company's primary proposal is desirable. There are alternatives to these flat fixed rate schemes that can reduce undesirable effects of weather on customers' bills while preserving an individual customer's ability to control the charges they pay. Voluntary level payment plans can assist customers in budgeting for high costs associated with cold weather while retaining the ability to save by reducing or forgoing consumption when they choose to do so and by benefiting from reduced costs during periods of above normal temperatures. Under the Staff's proposal and the Company's primary proposal customers will be even more captive to a monopoly utility than they are today. They will have no ability to reduce the non-gas portion of the bill. Further, low use customers will likely pay substantially more whether or not they want or need the same level of service as high use customers. If they disconnect, when they return they will be forced to pay not only the Company's lost revenue from customer charges but also revenues currently recovered in volumetric charges. The traditional concept of those who use more should pay more will be eliminated with respect to non-gas cost.

I fully agree that the concept of a flat fixed rate will make the bill simpler and less complicated to calculate. From a fairness perspective, I disagree that the bill will be more understandable to customers or more desirable. These proposals are not customer friendly and should be rejected.

Q. PLEASE RESPOND TO CLAIMS THAT FULL-NON-GAS RECOVERY WILL ELIMINATE CROSS SUBSIDIZATION.

A. Both Ms. Ross and Mr. Feingold claim that the current rate design causes residential customers whose usage is greater than the average to pay more than the cost required to serve them, while allowing smaller customers to underpay their cost-of-service. With the exceptions of the service line and meter costs, the majority of an LDC's plant investments are best characterized as joint and common costs that are not attributable to any particular customer and must be allocated based on some reasonable mechanism. Ms Ross and Mr. Feingold focus on the value of service provided by the Company is in access to natural gas. This reasoning leads to a belief that each customer should be allocated the same level of costs not just for a meter and service line but for all LDC costs. From a rate design perspective, recovery of fixed costs through fixed rates is a recovery method of choice for firms with sufficient market power to impose flat fees or enough regulatory support to impose them. Rate designs that consist of a customer charge and volumetric charge are supportable based on recognizing that the value of service is both in having access to gas as well as in using gas so cost would not be uniformly allocated to customers. In my opinion, recovery through a customer charge and volumetric rate is reasonable and fair from both an economic and policy perspective. Historically, this Commission has determined that it is appropriate for those who use more to pay more. Public Counsel encourages the Commission to retain the status quo.

Q. PLEASE RESPOND TO THE ARGUMENTS THAT FULL RECOVERY THROUGH A FLAT FIXED CHARGE WILL SIMPLIFY REVENUE FORCASTS AND ADJUSTMENTS AND WILL REDUCE RATE CASE FREQUENCY.

A. I acknowledge that if the Commission allows full recovery through a flat fixed charge, the administrative burden on the Company and Staff may diminish. However, these are ancillary effects that should not be the basis of adopting a rate making policy that significantly impacts consumers.

Q. WHAT ARE YOUR COMMENTS REGARDING THE STAFF'S SMALL GENERAL SERVICE RATE DISCUSSION?

A. The Staff suggests a split of the small general service class, and imposing a delivery charge on the smaller customers might be appropriate based on further research. The Staff provides no details specifying when the split should occur or what evaluation needs to be performed. While Public Counsel does not oppose evaluating the need for a split of the SGS class, we would oppose any rate change outside of a rate case and will likely oppose any proposal to impose a Delivery Charge on the smaller customers.

Q. PLEASE RESPOND TO THE CLAIM THAT THE EXISTING RATE DESIGN CREATES UNNECESSARY VOLATILITY IN CUSTOMER BILLS BY COLLECTING A LARGER PORTION OF CUSTOMERS' COST-OF-SERVICE IN THE WINTER.

A. I do agree that the current rate structure does increase the possibility of higher recovery of non gas costs in colder than normal winters. However, I do not consider creating an inescapable fixed delivery charge to be a better option. As I explained earlier in this testimony, the delivery charge proposal could substantially increase the non-gas recovery on some low use customers' bills with no ability to avoid the increase by curbing use.

Q. IN SUPPORT OF THE PROPOSED DELIVERY CHARGE WITNESS ROSS REFERENCES A NARUC RESOLUTION THAT IDENTIFIES COMPANIES IN OTHER STATES THAT HAVE ENERGY EFFICIENT TARIFFS AND DECOUPLING TARIFFS THAT NARUC CITES AS POTENTIALLY PROMOTING ENERGY EFFICIENCY AND ENERGY CONSERVATION AND SLOWING THE RATE OF DEMAND GROWTH OF NATURAL GAS, ESPECIALLY IN THE SHORT TERM. HOW DOES THE RATE DESIGN IN THE STATES LISTED COMPARE TO THE STAFF'S RATE DESIGN PROPOSAL IN THIS CASE?

A. I reviewed information for each company listed in the resolution; Northwest Natural Gas in Oregon, Baltimore Gas & Electric, Washington Gas in Maryland, Southwest Gas in California, Piedmont Natural Gas in North Carolina, States Power in North Dakota, Atlanta Gas Light in Georgia and Oklahoma Natural Gas. Only one has opted for a delivery charge mechanism like that proposed by the Staff that would collect all non-gas costs through a uniform fixed rate. In that case the parties stipulated to present the North Dakota Commission with two options. The first option included a traditional customer charge,

volumetric rate and a higher overall revenue requirement. The second option included a delivery charge and lower overall revenue requirement.

Q. WOULD YOU CHARACTERIZE THE CUSTOMER CHARGE IS "FIXED" FOR ATLANTA GAS LIGHT IN GEORGIA?

A. Yes. Based on a description of the calculation of the customer charge available on the Atlanta Gas Light website, it is my understanding that the customer charge is constructed of a flat rate element and an element based on the demand characteristics of a particular household. While residential customers pay for all non-gas charges in a flat rate, it is not a common fixed rate paid by all customers as would occur under the Staff proposal or the Company's primary proposal.

Q. PLEASE DESCRIBE THE COMPANY'S PROPOSED WEATHER NORMALIZATION ADJUSTMENT.

A. As an alternative to its proposal for a Straight-Fixed Variable rate design for residential customers, the Company proposes to couple an increase in the customer charge with a weather normalization adjustment (WNA). The WNA would correct for revenue lost from customer conservation or warmer than normal weather by way of a variable adder to the non-gas volumetric rate.

Q. DOES IT APPEAR THAT THE COMPANY'S PROPOSED WEATHER NORMALIZATION ADJUSTMENT WILL ADJUST FOR CHANGES IN CONSUMPTION DUE TO BOTH WEATHER VARIATIONS AND CONSERVATION?

A. Yes, it does. The Company proposes to annually adjust the heat sensitive factor which appears to be set in a manner that would reset the WNA rate factor per Ccf to recover all per customer sales revenues deviations from those established in the last rate case. This would result in any customer savings resulting from weather and conservation being factored in as an upward adjustment in the billing cycle WNA.

Q. WILL THE WNA HAVE A SIMILAR AFFECT AS THE STRAIGHT-FIXED VARIABLE PROPOSAL ON CUSTOMERS INCENTIVES TO CONSERVE?

A. Yes. The Company's WNA proposal would reduce the incentive to conserve.

Q. DO YOU ANTICIPATE THAT CUSTOMERS WOULD BE CONFUSED BY A RATE THAT APPEARS TO CHANGE EACH BILLING CYCLE DEPENDING ON THE ACTUAL HEATING DEGREE DAYS VARIATION FROM NORMAL HEATING DEGREE DAYS?

A. Yes. Customers will likely be resistant to a rate that appears to increase in warmer than normal weather.

Q. CAN A WNA BE IMPLEMENTED AT THIS TIME?

A. No. I have been advised by Public Counsel's legal staff that a WNA adjustment can not be implemented prior to the Commission establishing rules regarding the WNA requests. The Company's request is premature.

Q. DOES SENATE BILL 179 MANDATE WNAS?

A. No. In adopting SB 179 the Legislature did not mandate a WNA. Neither did it mandate a flat fixed rate recovery mechanism for residential rates.

Q. DO YOU HAVE CONCERNS WITH THE WNA AS IT RELATES TO SB 179?

A. Yes. The Company WNA proposal is not accompanied by a symmetric proposal for annual true-ups as was contemplated by the Legislature in Senate Bill 179. If the Company experiences customer growth, the Company's WNA will recover more than the test-year costs established in this rate case. However, there is no mechanism in the Company proposal to compare the revenues that might result from customer growth to growth in costs.

Q. AS PART OF ITS ALTERNATIVE PROPOSAL, THE COMPANY PROPOSES A CUSTOMER CHARGE SET AT $15.50. DO YOU AGREE WITH THIS RECOMMENDATION?

A. No. In the event that the Commission approves an increase in the customer charge, it seems reasonable to limit the increase to no more than the residential class revenue increase. This would be consistent with the Commissions decision to allow 55% fixed rate element recovery in the last MGE rate case and maintain the fixed/volumetric balance for residential.

Q. DESCRIBE CASES WHERE THE COMMISSION HAS BEEN ASKED TO APPROVE A WEATHER MITIGATION ADJUSTMENT?

A. Missouri Gas Energy (MGE) asked this Commission to approve a weather mitigation clause in Case No. GT-95-429. Its request were denied. As a result of the Stipulation and Agreement in Case No. GR-2002-0356, Laclede operates under a weather mitigation rate

design. MGE sought a weather mitigation rate design in GR-2004-0209. However, the proposal was was rejected by the Commission.

Q. WHY DID THE COMMISSION DENY MGE'S PAST REQUESTS FOR A WEATHER MITIGATION ADJUSTMENTS?

A. The Commission found in Case No. GT-95-429 that "the weather normalization clause tariff, as proposed, is unjust, unreasonable, and contrary to the law and should be rejected." In GR-2004-0209, the Commission found that the Company's weather normalization proposal would change rates unlawfully, would contradict good public policy and rejected the proposal even on an experimental basis.

Q. WOULD THE PROPOSED WEATHER NORMALIZATION ADJUSTMENT RESULT IN AN EFFECTIVE CHANGE IN THE RATES THAT ARE CHARGED DURING BILLING PERIODS WHEN THE WEATHER IS NOT PRECISELY NORMAL?

A. Yes, such effective changes in rates would occur in nearly every winter billing period for nearly every residential and small general service customer.

Q. WILL THE WNA DILUTE SIGNALS FOR CONSUMERS TO CONSERVE?

A. Yes. Since the WNA will make it virtually impossible for customers to know the margin rate that they are effectively being charged prior to consumption, it will be more difficult for consumers to make both long-run and short-run choices regarding the amount of gas that

they will consume. The long run decisions that consumers make about the size and level of energy efficiency of the structure that they will inhabit and the efficiency level of gas furnaces and other gas-fueled appliances will not be based on readily available prices for utility service. Likewise, the lack of readily available prices for utility service will make it more difficult to make decisions regarding short-run decisions like where to set the furnace thermostat.

Q. WILL THE WNA MAKE BILLS HARDER FOR CUSTOMERS TO CALCULATE?

A. Yes. Currently, it is fairly simple for a residential customer to calculate the charges that will apply for the margin portion of their bill. The customer only needs to know the customer charge and the block rates that apply for the current season. Public Counsel sometimes gets inquiries from customers about how to calculate the margin rates that appear on their monthly bills and we post these rates for all of the Missouri investor owned gas utilities on our web site (http://www.mo-opc.org/gas/gasbill.htm) in order to help customers understand how their monthly bills are calculated. If the WNA is approved, customers could calculate the margin charges that would appear on their monthly bill only if they also knew the actual and normal heating degree days.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.