Exhibit No.:	
Issue:	True-up
Witness:	James A. Fallert
Type of Exhibit:	True-up Testimony
Sponsoring Party:	Laclede Gas Company
Case No.:	GR-99-315

LACLEDE GAS COMPANY

GR-99-315

TRUE-UP TESTIMONY

OF

JAMES A. FALLERT

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's)
Tariff to Revise Natural Gas Rate Schedules.) Case No. GR-99-315

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 part hereof for all purposes is my true-up testimony, consisting of pages 1 to 10 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.

Ja. A. Fallert

James A. Fallert

Subscribed and sworn to before me this 1st day of October, 1999.

Betty J. Baumgartner

BETTY J. BAUMGARTNER NOTARY SEAL NOTARY PUBLIC STATE OF MISSOURI

BETTY J. BAUMGARTNER
NOTARY PUBLIC—STATE OF MISSOURI
ST. LOUIS COUNTY
MY COMMISSION EXPIRES MAR. 25, 2000

TRUE-UP TESTIMONY OF JAMES A. FALLERT

General Information

Q. Please state your name and business address.

A. My name is James A. Fallert. My business address is 720 Olive Street, St. Louis, MO.

Q. Are you the same James A. Fallert who previously filed direct, rebuttal, and surrebuttal testimony in this case?

A. Yes.

Purpose of Testimony

Q. What is the purpose of your true-up testimony?

A. The purpose of my testimony is to: (1) summarize the true-up issues that have been resolved by the active parties, (2) present Laclede's position regarding issues which were not settled, and (3) comment on the reasons why the minimum revenue requirement level as currently recommended by the parties is substantially less than the level reflected in the First Amended Partial Stipulation and Agreement filed with the Commission on September 3, 1999.

Settled Issues

Q. What issues have the parties reached agreement on in this true-up proceeding?

A. Laclede and Staff have reached agreement on the following issues which were listed in the Commission's ORDER ESTABLISHING TRUE-UP AUDIT AND HEARING of September 21, 1999:

(a) revenues associated with customer changes as of August 1, 1999.

Note: This item has been partially settled. Revenues associated with customer load changes have been settled, but revenues associated with customer annualization remain at issue.

(b) rate base component changes and associated depreciation and property taxes as of August 1, 1999;

(c) changes in employee levels and benefits costs, including costs associated with the August 1, 1999 contract wage increases, for union employees in the Laclede and Missouri Natural divisions, and changes in management salaries,

(d) the effect of any change in the Commission's annual assessment for fiscal year 2000;

(e) costs associated with maintenance agreements for computer systems that are in service;

(f) changes in rate case expenses;

(g) verifiable cost changes associated with the calculable increases in facility locates;

(h) changes in deferred balances and amortizations associated with the tracking mechanisms and accounting authorizations granted to Laclede in its last two rate case proceedings, based on the parties' positions on this issue.

Note: The dollar amounts associated with this item were previously agreed upon by the parties as part of the Partial Stipulation and Agreement filed in this case.

Q. What is the impact of these agreed upon trued-up amounts on the overall revenue requirement level recommended by the parties before resolution of the litigated issues in this proceeding?

A. Based on Staff's midpoint 9.5% return on common equity, the revenue requirement agreed upon by the parties after the inclusion of these true-up amounts would be $5,139,000, before resolution of the remaining issues in this case.

<u>Remaining Issues</u>

Q. What true-up issues have not been settled?

A. The parties have not been able to reach agreement on two issues that pertain to the true-up: (1) the proper level of annualized customers to be included in the true-up, and (2) the proper amount of short-term debt to be included in capital structure.

<u>Customer Annualization</u>

Q. Please describe the issue regarding customer annualization.

A. Both Company and Staff agree that the number of customers should be increased in the true-up to reflect annualized levels at July 31, 1999. However, because the number of customers changes seasonally, simply using the number of customers at July 31, 1999 would understate the correct number of customers over an annual period. (The actual customer count declined from 634,337 at March 31, 1999 to 625,506 at July 31, 1999.) Laclede and Staff employed different methods in their direct cases to arrive at the March 31, 1999 annualized level and agreed to split the difference between the two methods as a means of settling this issue in this proceeding.

Q. Do you agree with how Staff applied its customer annualization methodology for true-up purposes?

A. No. It is obvious that the manner in which Staff applied its methodology in the true-up has produced an obviously inflated customer level and needs to be adjusted.

Q. How many customers would Staff's true-up adjustment add?

A. Staff's adjustment would add 2,645 customers between March 31 and July 31, 1999, which would imply an annual rate of increase of 7,935 customers.

Q. Why do you believe that this increase is inflated?

A. A comparison of the actual annual increases in general service customers between 1998 and 1999, as measured at the end of each of the four months between the March 31 update and the July 31 true-up, were as follows:

	1998	1999	Increase
April	627,756	632,079	4,323
May	6624,131	628,867	4,736
June	6620,913	626,444	5,531
July	6618,829	624,506	5,677

As the above figures indicate, the highest annual increase in customers experienced by the Company from March 31 to July 31 was 5,677. Given the disparity between these actual figures and the 7,935 customer increase implied by Staff's approach, it is simply not possible to conclude that Staff's approach is appropriate or reasonable.

Q. Why has the manner in which Staff applied its methodology for true-up purposes overstated customers at July 31?

A. An annualization method is needed because Laclede experiences a seasonal change in its customer levels each year, as some customers connect to the system for the heating season and then leave the system during the warm-weather months. As a result, no one month is representative of the average number of customers on the system. Therefore, an annualization adjustment is needed to calculate the average customers that would correspond to a particular month. Staff's method for dealing with this issue involves comparing the current month's customer level to averages of that month's number of customers for the past 10 years to yearly averages in those years. Staff then makes a winter/summer allocation of customers, again on a 10 year average basis. All of these averages are applied to the current month's customers to develop an annualized amount. The Company believes such a method is flawed because: (1) the 10 year averages may not be representative of what is actually happening during the period being studied, and (2) the method relies to too great a degree on a summertime customer level, which may be influenced by such events as collection activity which may, in turn, cause it to be unrepresentative of wintertime levels. Despite these flaws in its methodology, however, the Staff could have still produced a more reasonable and representative result had it simply rolled forward its 10 year averages as it moved forward to the true-up — an approach that would have been consistent with both Staff's methodology and the very purpose for which a true-up is held.

Q. Are there any other problems with the results of Staff's adjustment?

A. Yes. In addition to producing an overall customer level that is too high, Staff's adjustment produces an inconsistent and counter-intuitive result when examined on a divisional basis.

Q. Please continue.

A. Laclede's customers are divided into five divisions. The results of Staff's true-up adjustment on an annualized basis are compared below to actual annual customer changes for the year ended July 1999:

Division	Staff Adjustment	Actual July 1999 vs 1998
Laclede	7,606	1,426
St. Charles	779	3,446
Midwest	167	545
Missouri Natural	117	2
Franklin County	(734)	258
Total	7,935	5,677

Q. Do these results make sense?

A. No. Staff's adjustment would suggest that most of the Company's growth occurs in the Laclede division, but we know that this is not the case. Most of Laclede's growth occurs in St. Charles, as can be seen from the actual customer growth figures provided above.

Additionally, Staff's adjustment implies a decrease in customers in Franklin County. However, in reality, Franklin County is the Company's fastest growing division on a percentage basis. Overall, Staff's methodology overstated customer growth for the Company as a whole. Staff's methodology clearly cannot be relied upon to produce a reasonable result.

Q. How does Laclede make this adjustment?

A. Laclede has employed the same methodology for many years. This method was also utilized by Staff for many years, and the rationale was supported by both the Company and Staff for several rate cases. The Company continues to believe that its assumptions underlying its methods are more supportable than the assumptions which underlie the method used by Staff in this case. Specifically, we believe that the change in customers between winter months from one year to the next best represents the actual rate of increase because customer levels in non-winter months fluctuate due to seasonal effects such as weather and collection activity. On the other hand, customers tend to maintain service during the winter. The Company therefore determines the annual rate of increase based on the rate of increase experienced from the most recent January to January period, and extends this rate of increase to the appropriate update or true-up period. The Company applies this level of growth to the actual monthly test year customer levels, thereby maintaining the seasonal fluctuations experienced during the test year, and extends this same level of growth through the true-up period.

Q. How does Staff's true-up recommendation for customer annualization compare with the estimate included in the true-up allowance included in Staff's direct filed case?

A. Staff's true-up methodology produces a considerably greater negative adjustment to revenue requirement ($1,022,000) than did the method used by Staff to calculate the value of this component in the true-up allowance presented by Staff in its direct case (a negative $444,000). Even when averaged with Laclede's true-up calculation of a negative adjustment of $394,000, Staff's current recommendation has reduced revenue requirement by an additional $264,000 from that estimated in Staff's direct case.

Q. What is Laclede's recommendation regarding the proper amount to include for true-up of customer annualization?

A. Laclede calculates that revenues should be increased consistent with an increase of 1,403 customers between March 31 and July 31, 1999. This would equate to an annualized rate of increase of 4,209 customers which is consistent with the rate of increase actually experienced by the Company this past January when compared with the previous January. Laclede recommends that this adjustment be split evenly with a revised Staff adjustment which, consistent with the purpose of a true-up, would move Staff's 10 year average forward to the ten year period ended July 31, 1999.

Q. Does this recommendation mean you agree with Staff's methodology?

A. Absolutely not. As I explained above, Staff's methodology cannot be trusted to produce reliable results. However, we had previously agreed to split the difference between the two methodologies in order to settle this issue, and have continued that agreement in this recommendation. However, we believe that, to the extent that Staff's methodology is employed, it should at least be updated to the true-up period which produces a somewhat more believable result.

Q. What would be the impact of this recommendation on revenue requirement in this case?

A. If the Commission adopts Laclede's recommendation, the currently agreed upon minimum revenue requirement of $5,139,000 would be increased by $170,000 to $5,309,000.

Short-Term Debt

Q. Please describe the issue that remains regarding short-term debt.

A. Laclede issued approximately $24 million of common equity (after transaction costs) in May 1999 and $25 million of long term debt in June 1999, and used the proceeds of both to reduce short-term borrowings. These financings occurred subsequent to the March 31, 1999 update period in this case but before the July 31, 1999 true-up date, and are thus appropriately included in this true-up. Consistent with the purpose of the true-up in this proceeding, Laclede has adjusted short-term debt balances to reflect the impact of these financings. Staff and Public Counsel, however, propose no change to short-term debt balances despite the aggregate $49 million of additional financing in the form of the May 1999 equity issue and the June 1999 long term debt issue, which are specifically designed to reduce short-term debt. This issue was tried at the hearing and I would refer the Commission to the record for a more detailed description of the issues involved.

Q. Is Staff's position regarding the treatment of short-term debt in this true-up proceeding consistent with the position taken in its direct testimony?

A. No. Originally in its direct case, Staff recognized the impact of the long term debt issue on the Company's short-term debt levels as part of the true-up allowance sponsored by Staff witness Westerfield in her direct testimony. Inexplicably, in its actual true-up recommendation, Staff has abandoned its prior position by failing to recognize the impact of the long term debt issuance previously recognized by Staff for true-up purposes.

Q. What is the impact of this change in Staff's position?

A. The First Amended Partial Stipulation and Agreement reflected an agreed upon revenue requirement in the amount of $6,313,000, based, in part, on the original true-up allowance sponsored by Staff in its direct case. Rather than maintain the estimated $1,456,000 increase in revenue requirement that was included in this allowance for changes in capital structure, however, the Staff's recommendation at true-up actually includes a decrease in revenue requirement due for capital structure of $350,000. This, in turn, has contributed to an overall decrease in the agreed upon minimum revenue requirement from the $6,313,000 reflected in the First Amended Partial Stipulation and Agreement to the current minimum of $5,139,000. Most of this decrease in revenue requirement is attributable to Staff's change of position on the short-term debt issue.

Q. Does Staff's modification of its position on the short-term debt issue account for all of the change in its revenue requirement recommendations for capital structure between its direct case and the true-up?

A. No. It is important to note that although Staff has chosen to now omit from true-up the impact on capital structure of the previously recognized effect of the $25 million debt issuance, it has nevertheless picked up other capital structure changes during the true-up period that go in the opposite direction and negatively affect the Company's revenue requirement. As a result, the position advocated by Staff (and presumably Public Counsel) requires the Commission to believe that the Company's cost of capital could have declined between March 31, 1999 and July 31, 1999, despite the fact that the Company issued $24 million of equity during this time period. Such a result simply makes no sense and is fundamentally inappropriate.

Q. Does the "trued-up" capital structure, as proposed by Staff and Public Counsel, match the rate base the Staff is allowing the Company to earn a return on?

A. Unfortunately, not even remotely. The Staff's current accounting schedules indicate a capital structure of approximately $575.5 million, while the Staff is allowing a return on $533.0 million in rate base. In other words, the Staff's capital structure is $42.5 million greater than the rate base. For a Company such as Laclede, which has no material investments in other lines of business or gas distribution in other jurisdictions, that large a discrepancy between total rate base and total capital structure is patently unreasonable.

Q. Why are the Staff and OPC proposed capital structures so much greater than the rate base these funds are used to support?

A. Neither the Staff nor OPC adjusted the historical short-term debt balances for the full year effect of the aforementioned equity and debt issues. Such an annualization adjustment, similar to annualizing the full year effect of a payroll increase, is normally common practice in regulatory proceedings in this state. However, for this particular proceeding, both parties have chosen to ignore this practice.

Q. How does the Company's capital structure compare to rate base?

A. The Company's capital structure, utilizing the 12 months ended July, 1999 level of short-term debt adjusted for the annualization effect of the equity and debt issuances, approximates \$535.4 million, or \$2.4 million greater than the rate base supported in this case.

Q. If both the customer annualization and short-term debt impacts are properly reflected, what is the appropriate revenue requirement following true-up and before resolution of the remaining issues?

A. These adjustments would result in revenue requirement of \$7,634,000, before resolution of the remaining issues in this case.

Q. Does this conclude your true-up testimony?

A. Yes.