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2 PUBLIC SERVICE COMMISSION

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4 TRANSCRIPT OF PROCEEDINGS

5 Oral Argument

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9
10 In the Matter of the PGA Filing of)Case No. GR-2006-0288
11 Laclede Gas Company for 2005-2006)

12
13 KENNARD L. JONES, Presiding
14 SENIOR REGULATORY LAW JUDGE
15 ROBERT M. CLAYTON, III, Chairman,
16 JEFF DAVIS,
17 TERRY JARRETT,
18 ROBERT S. KENNEY,
19 COMMISSIONERS

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1 P R O C E E D I N G S

2 JUDGE JONES: Okay. We are on the record with
3 Case Nos. GR-2005-0203 and GR-2006-0288 in the matter of
4 Laclede Gas Company's purchased gas adjustments for
5 2004-2005 and for 2005-2006.

6 I'll point out that although these matters are
7 being heard together with regard to this specific issue,
8 they have not been consolidated.

9 The arguments we will hear today are relevant to
10 the Staff of the Commission's request for information from
11 Laclede, and that has been ongoing and continues through
12 today.

13 And with that, we'll start with the Staff of the
14 commission. Oh, let me take entries of appearances first
15 from Staff.

16 MR. THOMPSON: Thank you, your Honor. Kevin
17 Thompson and Lera Shemwell for the Staff of the Missouri
18 Public Service Commission.

19 JUDGE JONES: And the Office of Public Counsel?

20 MR. POSTON: Marc Poston appearing for the
21 Office of Public Counsel and the public.

22 JUDGE JONES: And Laclede Gas Company?

23 MR. PENDERGAST: Michael C. Pendergast and Rick
24 Zucker on behalf of Laclede Gas Company.

25 JUDGE JONES: And that will start with Staff.

1 MR. THOMPSON: May it please the Commission.
2 I'm not going to waste a lot of your time. I know that
3 you're familiar with this matter. It's been heard in this
4 room before.

5 This is a discovery dispute, and it's a
6 discovery dispute that is occurring within the context of
7 a PGA/ACA case. And to quickly rehearse what that is, in
8 the world of natural gas, rates are treated somewhat
9 differently than they are in the area of electric and
10 water and sewer so that the commodity rate, that is, the
11 cost of the gas itself, is separate from all the other
12 costs of the gas company.

13 And the commodity cost is passed directly
14 through to the customer through the PGA/ACA process. And
15 it's an annual thing. The company will estimate what they
16 think the cost of gas will be for a -- a period of time,
17 and these clauses will vary from company to company.

18 And the estimated cost is then approved by the
19 Commission. And that's what people pay until the company
20 comes and changes it either up or down.

21 At the end of the year when the gas is being
22 used, we go into the ACA phase. And the ACA phase
23 includes a true-up where Staff does a prudent audit of the
24 actual costs, and the company's rolling balance is then
25 adjusted either in favor of the ratepayers or in favor of

1 the company, depending on whether those estimated costs
2 that were paid during the year when the gas was being
3 used, how closely it tracked the actual costs.

4 And this is done because the volatility in the
5 commodity costs are -- is so great that the company,
6 frankly, cannot have enough cash on hand to absorb the
7 swings in the commodity costs only to recover later in a
8 traditional rate case.

9 So this discovery request comes as part of a
10 prudence review. Laclede Gas Company has an affiliate,
11 LER, Laclede Energy Resources, I believe that is. And the
12 two companies engage in transactions.

13 Because they engage in transactions, Staff must
14 determine whether or not the transactions were prudent
15 from the point of view of the regulated company, Laclede
16 Gas Company.

17 The Commission has, as you know, affiliate
18 transaction rules. The standard in that rule is, "A
19 regulated gas corporation shall not provide a financial
20 advantage to an affiliated entity." It's just that
21 simple.

22 So the prudence review is simply to determine
23 whether or not a financial advantage has been provided.
24 As part of that prudence review, Staff has sought certain
25 documents. These documents, for the most part, have to do

1 with the sources of certain gas used by LER to fill
2 contracts with Laclede. So this is a transaction where
3 gas is flowing from LER to Laclede Gas Company in exchange
4 for money.

5 And Staff seeks documents on the origin of the
6 gas in order to determine the price at which LER acquired
7 it. In an audit, you go to original documents. Staff is
8 not saying today that we believe Laclede Gas Company or
9 LER has done anything improper.

10 We don't know that. We're simply seeking to
11 acquire certain documents in order to complete an audit.
12 The documents that we seek are relevant and necessary.
13 Thank you.

14 JUDGE JONES: Okay. And --

15 COMMISSIONER JARRETT: I have some questions,
16 Judge.

17 JUDGE JONES: Why don't we go ahead and do
18 questions --

19 MR. THOMPSON: Sure.

20 JUDGE JONES: -- from Staff while you're there.

21 MR. THOMPSON: Ms. Shemwell help me respond to
22 questions because she knows an awful lot more about this
23 than I do.

24 JUDGE JONES: All right. Thank you,
25 Mr. Thompson.

1 COMMISSIONER JARRETT: In going back through the
2 multitude of pleadings in this case, specifically, I was
3 looking at -- the first document I want to talk about is
4 the document that was filed by Staff on July 25th of 2008.
5 And by the way, I'm referring to the 2006 case.

6 And this document was entitled List of Documents
7 Required by Staff to Analyze Laclede's ACA Filings and
8 Motion for Order Directing Laclede to Produce.

9 MS. SHEMWELL: Commissioner, what was the date
10 on that, please?

11 COMMISSIONER JARRETT: July -- July 25th of '08.
12 And while she's looking for that, Counsel, let me
13 summarize my reading of that.

14 My -- my reading of that is the argument by
15 Staff was that there's allegations of imprudence of
16 Laclede's gas purchasing practices and potential
17 violations of the Commission's affiliate transaction rules
18 and that Staff needed these documents to properly analyze
19 the business dealings between Laclede and the one
20 affiliate that's at issue in this case.

21 MR. THOMPSON: Yes, sir.

22 COMMISSIONER JARRETT: Does that sound accurate?

23 MR. THOMPSON: I'm sure it's accurate, sir. I
24 was not involved in drafting it. I don't know that there
25 are allegations of improprieties. There's simply a need

1 to review certain documents to determine that there were
2 not any.

3 COMMISSIONER JARRETT: Okay. Then we had an
4 oral argument in this case on March 26th. All right? And
5 the transcript of that is Transcript Vol. II and, again,
6 in the 2006 case is the transcript I'm looking at. And
7 I'm looking at page 47 of that.

8 So I'll let Ms. Shemwell maybe find that. But I
9 want to go back to the affiliate transaction rule for a
10 moment that quoted the standard. You quoted the first
11 sentence of the standard. I want to continue on.

12 The second sentence says, "For the purposes of
13 this rule, a regulated gas corporation shall be deemed to
14 provide a financial advantage to an affiliated entity if,
15 No. 1, it compensates an affiliated entity for goods or
16 services above the lesser of, A, the fair market price,
17 or, B, the fully distributed costs to the regulated gas
18 corporation to provide the goods or services for itself."

19 So in that case, that is where the gas company
20 purchases the gas from the affiliate; is that right?
21 Is that what situation that applies to?

22 MR. THOMPSON: Yes, sir.

23 COMMISSIONER JARRETT: Okay. So if it purchases
24 the gas above the lesser of the fair market price or the
25 fully distributed costs to the regulated gas corporation,

1 then it has granted a financial advantage to the
2 affiliate?

3 MR. THOMPSON: That's correct.

4 COMMISSIONER JARRETT: Okay. And then No. 2
5 talks about the reverse, where the affiliate provides
6 something to the gas company. So if the fully distributed
7 cost -- or excuse me -- it transfers information, assets
8 or gas or services of any kind to an affiliated entity
9 below the greater of the fair market price or the fully
10 distributed costs of the regulated gas corporation.

11 MR. THOMPSON: Yes, sir.

12 COMMISSIONER JARRETT: And I guess that has to
13 do the with the allegation of the capacity issue?

14 MR. THOMPSON: Yes, sir.

15 COMMISSIONER JARRETT: Right. So, again, the
16 standard, under the rule, for both of these is it's either
17 the lesser of or the greater of the fair market price or
18 the fully distributed -- distributed cost?

19 MR. THOMPSON: That's correct.

20 COMMISSIONER JARRETT: Correct. Now, in the
21 March 26th oral argument, and I'm referring to page 47 of
22 Volume 2 of the transcript, Counsel for Staff stated, "The
23 primary purpose for this information that Staff is
24 seeking" -- and I'm starting on Line 2 of the -- of page
25 47 of page 47.

1 "The primary purpose for this information is to
2 determine whether Laclede paid too much to the affiliate
3 for gas and determine whether the affiliate -- determine
4 what the affiliate did with Laclede's capacity that was
5 released to the affiliate."

6 MR. THOMPSON: That's correct.

7 COMMISSIONER JARRETT: And Commissioner Murray
8 said, "And too much would be defined by the rule, would it
9 not?" And counsel said, "Not necessarily."

10 Now, where in that standard that you agree is
11 the standard under the rule is a "not necessarily" clause?

12 MR. THOMPSON: There is no such clause.

13 COMMISSIONER JARRETT: Okay. So was counsel
14 wrong when he said not necessarily?

15 MR. THOMPSON: I don't believe so, sir. No.

16 COMMISSIONER JARRETT: Okay. Then why was
17 counsel not incorrect?

18 MR. THOMPSON: Because it may be that the
19 affiliate transaction rule does not occupy or define the
20 entire universe of improper affiliate transactions.

21 COMMISSIONER JARRETT: Well, the rule addresses
22 whether a regulated gas corporation has provided a
23 financial advantage to an affiliated entity or vice versa;
24 isn't that right?

25 MR. THOMPSON: Yes, sir.

1 COMMISSIONER JARRETT: Okay. So what you're
2 saying is that a utility could completely comply with the
3 rule and still be imprudent?

4 MR. THOMPSON: Let me answer that with a
5 hypothetical, if I may. And I beg your indulgence.

6 COMMISSIONER JARRETT: All right.

7 MR. THOMPSON: Because I know you're not looking
8 for a narrative answer.

9 COMMISSIONER JARRETT: I'm just looking for a
10 goo -- for a good answer that I can understand.

11 MR. THOMPSON: Okay. And I hope I can provide
12 that. Suppose -- suppose that you have a regulated gas
13 company that has an unregulated marketing subsid --
14 affiliate, much as we have here. And suppose that the
15 unregulated affiliate sells gas under a contract to the
16 regulated entity.

17 And suppose that the contract specifies a
18 particular price per unit, and that price per unit is the
19 price at a certain location in the nation where gas is
20 traded as of a certain date. And suppose that the
21 unregulated entity is able to acquire cheaper gas with
22 which to fill that contract.

23 Now, from the point of view of a business
24 person, you would say, Well, that's business.
25 Buy low, sell high. That's what you do. And from the

1 point of view of contract administration, you would say,
2 Well, they met their contract. They provided the required
3 quantity of gas, and they were paid the bargained-for
4 price. Nothing irregular there. But --

5 MS. SHEMWELL: Is that a cell phone?

6 JUDGE JONES: Probably.

7 MR. THOMPSON: It ain't me. From the point of
8 view of a prudence auditor -- from the point of view of a
9 prudence auditor, that difference between the contract
10 price and the price at which the gas was acquired to fill
11 the contract, isn't that a profit that the ratepayers have
12 unnecessarily paid?

13 Because would it not have been possible for the
14 company, the regulated company, to acquire that gas itself
15 at the same location that the unregulated entity acquired
16 it?

17 That's one scenario. I'm not saying that
18 happened here.

19 COMMISSIONER KENNEY: Can I ask -- may I ask the
20 question slightly differently? And I think it's the same
21 thing that Commissioner Jarrett is getting at. And To my
22 mind, it's the crux of the issue, and I'm going to ask
23 Laclede the same question.

24 Is the analysis that Staff goes through for
25 purposes of a prudence review under an ACA the same or

1 different than the analysis that goes into determining
2 whether the regulated entity did or did not violate the
3 affiliate transaction rule? Is that -- do you understand
4 my question? It's a bit --

5 MR. THOMPSON: I believe I understand your
6 question. And I would think -- and, of course, I'm not an
7 auditor. But I think the two analyses are not necessarily
8 identical.

9 COMMISSIONER KENNEY: Okay. So is it Staff's
10 position that the regulated entity could comply with the
11 affiliate transaction rule but still have made an
12 imprudent decision for purposes of the ACA analysis?

13 MR. THOMPSON: I think so. I think it's
14 possible.

15 COMMISSIONER KENNEY: And is there case law to
16 that effect, or is that an economic question or is it an
17 auditing question? Where do we go to determine
18 definitively whether or not that is or is not the answer?

19 MR. THOMPSON: To go back to this
20 hypothetical --

21 COMMISSIONER KENNEY: Oh, I'm sorry.

22 MR. THOMPSON: -- it seems to me it would turn
23 on what is the fair market price. Is it the contract
24 price, or is it the price at which the unregulated
25 affiliate actually acquired the gas?

1 If the contract price is the fair market price,
2 then there's no violation of the rule. None at all. If
3 the fair market price is the well head price at which the
4 gas was acquired, then there is a violation of the rule
5 because the regulated entity paid more per unit.

6 COMMISSIONER KENNEY: And let me -- let me ask
7 another question, then. In your hypothetical, then, the
8 fair market price is the well head price. Are you arguing
9 that the regulated entity should have bypassed its
10 affiliated entity and purchased directly from the well
11 head and violate its contract?

12 MR. THOMPSON: What I'm saying is if we were to
13 acquire those documents and if we were to find out that
14 these transactions occurred, maybe we would argue that to
15 the Commission when we come to the final evidentiary
16 hearing, the determination state of this ACA case.

17 We're not there yet. We don't know that we will
18 find anything like that. But the hypothetical is to
19 illustrate why we're looking for these documents, why we
20 need the documents that show the original price.

21 COMMISSIONER KENNEY: And I'm sorry if I
22 encroached on Commissioner Jarrett's questions, so I'll --

23 COMMISSIONER JARRETT: No. Not at all.

24 MS. SHEMWELL: Might I add something? I think
25 that we do our analysis as well under Statute -- under

1 393.140(12), which says that when a regulated utility has
2 an affiliate, the Commission may inquire into and
3 apportion capitalization earnings. We're looking at these
4 as debts and dispenses fairly and justly to be borne by
5 the regulated utility as distinguished from the
6 unregulated affiliate.

7 So I believe that the Commission makes its
8 prudence determination under parts of the statute.

9 COMMISSIONER JARRETT: But, again, this is what
10 counsel argued, page 47 --

11 MR. THOMPSON: Yes, sir.

12 COMMISSIONER JARRETT: -- in March. "The
13 primary purpose for this information is to determine
14 whether Laclede paid too much to LER for gas and determine
15 what LER did with Laclede's capacity that was released to
16 LER." And I believe you said that was correct.

17 MR. THOMSON: Yes, sir.

18 COMMISSIONER JARRETT: Now you guys are arguing
19 something different than that. Now you're arguing that
20 this isn't about LER. It's about whether Laclede should
21 have gone to the well head and bought the gas independent
22 of buying it from LER. Are you not?

23 MS. SHEMWELL: I think we're stating the
24 evidence that we need to show prudence, What kind of --

25 COMMISSIONER JARRETT: I'm just asking -- this

1 is what counsel said in March as to what the purpose of
2 getting this information was.

3 MR. THOMPSON: I don't think counsel misspoke.

4 COMMISSIONER JARRETT: To determine whether --
5 to determine whether Laclede paid too much to LER for gas.

6 MR. THOMPSON: Yes, sir.

7 COMMISSIONER JARRETT: And what you're arguing
8 now is Laclede should have gone to the well head to
9 determine if -- if the fair market price was lower than
10 what LER was charging, and if it was, they should buy it
11 directly at well head and not from LER. That's completely
12 different from what counsel argued in March.

13 MR. THOMPSON: If the well head price was ten
14 and the contract price was 15, then we would say Laclede
15 did pay too much to LER for gas, that instead of buying
16 the gas from LER, Laclede should have gone and acquired
17 the gas. That would be more prudent.

18 COMMISSIONER JARRETT: Right. But that wasn't
19 the argument in March. I'll move on.

20 COMMISSIONER KENNEY: Not to belabor this, but
21 I'm -- I am -- I want to make sure I'm clear in my mind
22 that the affiliate transaction rule is a separate
23 determination from a prudence review.

24 MR. THOMPSON: Well, a prudence review is an
25 auditing function in which you compare -- you look at

1 actions that the company took, and you assess those
2 actions against the context within which they were taken
3 to determine whether the decisions that were made, whether
4 the actions that were taken were sensible, prudent at the
5 time they were taken.

6 COMMISSIONER KENNEY: So is it -- and would it
7 be accurate to say that the affiliate transaction rule
8 with a capital A and capital T as defined under the
9 regulations is one action, but then you're talking
10 generally about transactions between affiliated entities,
11 not as a defined term, but just as a part of analyzing
12 whether certain purchases were, in fact, prudent? Is that
13 correct?

14 MR. THOMPSON: Absolutely. There would be a
15 prudence review whether or not there had been any
16 affiliate transactions.

17 COMMISSIONER KENNEY: But in this particular
18 circumstance, certain transactions between affiliated
19 entities become relevant to your prudence analysis?

20 MR. THOMPSON: Because they occurred.

21 COMMISSIONER KENNEY: All right. All right.
22 All right. And so what Mr. Reed was arguing back in March
23 at page 47, Line 2, isn't necessarily contradictory or
24 inconsistent with what you're saying today?

25 MR. THOMPSON: I don't believe it is.

1 COMMISSIONER KENNEY: I think he said it's the
2 primary purpose, but not the sole purpose. Is that --
3 it's not inconsistent necessarily?

4 MR. THOMPSON: Well, what Mr. Reed said was we
5 want to find out if Laclede paid too much to LER for this
6 gas. And the hypothetical that I gave you was to explain
7 in more detail how it is that Laclede might have paid too
8 much to LER for the gas.

9 COMMISSIONER KENNEY: All right.

10 COMMISSIONER JARRETT: Counsel, wouldn't your
11 argument in your hypothetical mean gas companies couldn't
12 enter into hedging contracts? Because they enter into
13 these contracts, they may pay a higher price for the gas.

14 MR. THOMPSON: Yes, sir.

15 COMMISSIONER JARRETT: But in order get some
16 long-term stability, they pay more for the gas.

17 MR. THOMPSON: Right.

18 COMMISSIONER JARRETT: So under your
19 argument --

20 MR. THOMPSON: And that's viewed as prudent.

21 COMMISSIONER JARRETT: Well, under your
22 argument, if the contract is a certain price, if they can
23 go somewhere else and buy it lesser than under the
24 contract, then that's not prudent. I mean, isn't -- isn't
25 that the same argument you're making?

1 MR. THOMPSON: I think there's some differences.
2 First of all -- I don't know when they made this contract.
3 And I'm sure Lera could probably tell you. The other
4 thing is, is that I think it's a heightened scrutiny when
5 the transaction is between a regulated entity and an
6 affiliate, an unregulated affiliate.

7 COMMISSIONER JARRETT: Right. And we have
8 standards for that. It's in the rule.

9 MR. THOMPSON: Yes, sir.

10 COMMISSIONER JARRETT: Right.

11 MR. THOMPSON: As Lera pointed out with the
12 reference to the statute, the rule isn't the only
13 consideration.

14 MS. SHEMWELL: Commissioner Jarrett, may I say
15 that hedging is not typically done with an affiliate.
16 Here the concern is that the affiliate is performing much
17 the same service as the regulated.

18 Laclede has other affiliates, and they do
19 completely separate business. In this case, LER is
20 selling -- acquiring and selling gas. And that's what
21 Laclede does. It acquires and sells gas.

22 COMMISSIONER JARRETT: Right. But, again, if
23 we're talking about the relationship between Laclede and
24 its affiliate, that's handled under the rule.

25 MS. SHEMWELL: Among other things. Yes.

1 COMMISSIONER JARRETT: Right. One other
2 question I had was about the CAM, the Cost Allocation
3 Manual. There was a lot of discussion about the CAM in
4 the last oral argument in March.

5 And again, going back to transcript Vol. II,
6 page 49, starting at line 21, Commissioner Murray starts a
7 -- an inquiry of counsel about how the CAM provides for
8 dealings with the affiliate. And counsel for Staff says,
9 Yes, that's right.

10 And then over on page 50, Commissioner Murray
11 says, "And it says the higher -- depending on whether it's
12 sale of purchase, the higher of the fair market value or
13 fully distributed cost?" Counsel, "Right." Counsel,
14 "Yes. Or the lower of these two things."

15 So I take it from that exchange that Laclede's
16 CAM is consistent with our rule on that?

17 MS. SHEMWELL: No.

18 MR. THOMPSON: Ms. Shemwell will speak to that.

19 COMMISSIONER JARRETT: At least on that -- at
20 least on that issue.

21 MS. SHEMWELL: Let me speak to the CAM. The CAM
22 -- the rule says Commission approved CAM. This CAM has
23 never been Commission approved.

24 COMMISSIONER JARRETT: When was it -- when was
25 it submitted to the Commission for approval?

1 MS. SHEMWELL: It has never been submitted to
2 the Commission for approval.

3 COMMISSIONER JARRETT: Okay.

4 MS. SHEMWELL: There was a CAM that was
5 submitted to the Commission before the affiliate
6 transaction rules went into place. And Laclede said --
7 and it was submitted in that case. Or it was to be
8 submitted in that case --

9 COMMISSIONER JARRETT: Okay.

10 MS. SHEMWELL: -- in 2001. Laclede's CAM has
11 never been submitted. We do not believe that their CAM
12 actually contains the same pricing provisions as are
13 required in the affiliate rule.

14 COMMISSIONER JARRETT: So, again, Mr. Reed was
15 incorrect when he said that?

16 MS. SHEMWELL: Did he say the CAM complied with
17 the affiliate rules?

18 COMMISSIONER JARRETT: That's what -- I'll read
19 it again. And, again, I'm looking on page 49 and 50.
20 Commissioner Murray, "So if there is -- and at this point
21 I'd like to know, is there a specific way that the Cost
22 Allocation Manual provides for dealings with an affiliate,
23 correct?" Mr. Reed, "Yes. That's right."

24 Over to page 50, line 1. Commissioner Murray,
25 "And it says the higher, depending on whether it's the

1 sale or purchase, the higher the fair market value or
2 fully distributed cost." Mr. Reed, "Right. Yes."

3 So all I'm asking is, is -- at least in that
4 respect, is the CAM consistent with the rule?

5 MS. SHEMWELL: No.

6 COMMISSIONER JARRETT: So Mr. Reed was wrong?

7 MS. SHEMWELL: I believe Mr. Reed -- to the very
8 limited extent Commissioner Murray posed that, I suppose
9 that the answer could be yes. My complete answer would be
10 that, technically, it does not comply with the
11 Commission's affiliate rules.

12 We have to reserve the right, Commissioner, to
13 learn and grow and read and study. And we continue to do
14 so.

15 COMMISSIONER JARRETT: Seems to be a lot of that
16 between March and now. Just a moment. I believe in the
17 oral argument -- and I'll try not to put words in
18 Mr. Pendergast's mouth, but I believe he argued that Staff
19 wasn't judging this from fair market value standard.
20 Staff wanted to look at this as the affiliate's lowest
21 cost of gas from anywhere in its portfolio, so not a fair
22 market value standard. You just have to look at whatever
23 the -- whatever the lowest cost gas is in the portfolio.
24 Is that -- would you agree with that?

25 MR. THOMPSON: I wasn't here during that

1 argument, sir.

2 COMMISSIONER JARRETT: Okay. Well, I'll ask you
3 now. Do you agree with it, assuming that what I said was
4 accurate?

5 MR. THOMPSON: Yes, sir.

6 COMMISSIONER JARRETT: You do agree with that?

7 MR. THOMPSON: Yes, sir.

8 COMMISSIONER JARRETT: So it's not a fair market
9 value standard?

10 MS. SHEMWELL: Actually --

11 MR. THOMPSON: Go ahead.

12 MS. SHEMWELL: I would suggest that what Staff
13 wants to look at is the fair market value. The
14 transaction between Laclede and its affiliate is not an
15 arm's length transaction. So that does not establish fair
16 market value.

17 A transaction between independent parties with
18 no affiliation looks -- will establish the fair market
19 value. We are looking at what the fair market value is.
20 The fair market value of gas, Commissioner Jarrett, can
21 change from day to day, certainly from location to
22 location.

23 There are many, many influences on what the fair
24 market of gas is, especially in today's market. We do
25 want to assure that, in fact, what Laclede is buying from

1 LER is the lowest price at which Laclede could have
2 acquired the gas itself.

3 Our question is, would it have been prudent for
4 Laclede to do the transaction itself rather than buying
5 gas from LER? If they had purchased from a third party,
6 might they have bought the gas cheaper? Did they pay LER
7 more?

8 We're looking -- and that's the fair market
9 price is the transaction between LER and a third party,
10 not the transaction between Laclede and its affiliate.
11 There can't be a presumption of prudence when a utility is
12 dealing with its affiliate because the Supreme Court said
13 in the ATMOS case, "When there is an affiliate, the
14 utility has the opportunity and the incentive to benefit
15 its affiliate to the detriment of its customers."

16 That's the ATMOS case that the Supreme Court
17 approved the Commission's affiliate transactions rules. I
18 have copies if you'd like to see it.

19 COMMISSIONER JARRETT: Okay. So fair market
20 price -- if I'm -- if I'm understanding you correctly, the
21 fair market price can mean one thing under the affiliate
22 transaction rule, but another thing under prudence review?

23 MS. SHEMWELL: I think fair market price is fair
24 market price. It's how you establish the fair market
25 price that we're trying to get to. What is the fair

1 market price? That's the documents that we seek to show
2 what is the fair market price for the transactions between
3 Laclede and LER. And we cannot assume when it's an
4 affiliate transaction that that establishes fair market
5 value because they're affiliated entities. It's a third
6 party transaction.

7 Those are presumed prudent, as in any rate case.
8 When Laclede goes out and buys from anybody, there's a
9 presumption of prudence until someone raises a substantial
10 question about it.

11 With an affiliate, there can't be a presumption
12 of prudence because, just as the Supreme Court said in
13 ATMOS, there's the opportunity as well as the incentive to
14 give a benefit to the affiliate.

15 And here's why. When Laclede makes off system
16 sales, it has to share all of that with its customers.
17 And when it makes off system sales, 80 percent of that
18 goes back and reduces customers' rates, cost of gas, and
19 Laclede keeps 20 percent.

20 When LER makes an off-system sale, 100 percent
21 of that goes to the holding company. So there is a strong
22 incentive to benefit LER to give that financial advantage.
23 All we're asking is show us that you didn't. Just produce
24 the documents to show us that, in fact, when you dealt
25 with LER, it was similar to, very close to the same trans

1 -- the same as the transaction would have been with a
2 third party.

3 And what we're saying is, when LER -- for
4 example, Laclede makes an off system sale, if LER turns
5 around and almost immediately makes a similar sale to a
6 third party and there is a substantial gain on it, our
7 question is, why didn't Laclede make that transaction
8 itself? Because it's customers have paid for everything
9 for Laclede to make the off-system sales. It's paid for
10 the personnel, the gas, the capacity, the computers,
11 everything.

12 So off-system sales, that activity, is
13 completely supported by consumers, and consumers should
14 get the benefit. If, in fact, it's shifted to LER so that
15 LER can get the benefit, that goes back to the company and
16 none of it is shared with customers.

17 That's our question. And that's how we show
18 fair market value is to look at a directly comparable
19 transaction between independent parties.

20 COMMISSIONER JARRETT: But isn't that a
21 hindsight review?

22 MS. SHEMWELL: It's got to be based on what they
23 knew at the time. If they sold to LER and LER was able to
24 make a -- a similar sale, then -- I mean, it couldn't have
25 been six months later. The sale has to be fairly

1 contemporaneous. But the question is why wouldn't Laclede
2 have made the sale?

3 COMMISSIONER JARRETT: Right. But wouldn't that
4 be a hindsight review, what you just described?

5 MS. SHEMWELL: We're having -- I don't know any
6 other way to look at fair market value. They're required
7 to make the sale to LER at fair market value. How do we
8 determine fair market value? At the time. What was the
9 fair market value on the date they made the sale?

10 What -- and if, in fact, they made the sale to
11 LER at \$2 less than the fair market price on that day,
12 it's what they knew on that day. So I don't see it as
13 hindsight.

14 COMMISSIONER JARRETT: Okay. Now. Laclede has
15 to provide, according to our rule, record-keeping
16 requirements, provide a whole slew of information on or
17 before March 15th of every year. I assume -- I assume
18 that's an annual deal, right?

19 MS. SHEMWELL: Yes.

20 COMMISSIONER JARRETT: And they provide a list
21 of all goods or services provided to or received from
22 affiliated entities, the -- the amount that they've paid.
23 So Staff already has records regarding all of the
24 transactions Laclede made with the affiliate and the price
25 they paid, right?

1 MR. THOMPSON: Right.

2 MS. SHEMWELL: In total. In total.

3 COMMISSIONER JARRETT: Right.

4 MS. SHEMWELL: Not individual.

5 COMMISSIONER JARRETT: Okay. But they have the
6 dates?

7 MS. SHEMWELL: Yes.

8 COMMISSIONER JARRETT: So you don't have on a
9 day-to-day basis, Laclede paid this amount for this
10 purchase?

11 MS. SHEMWELL: No. I suspect that's in those
12 thousands and thousands of documents that Mr. Pendergast
13 described the last time, the last oral argument.

14 COMMISSIONER JARRETT: Okay. And that's not
15 provided -- a full and complete list of all of the
16 affiliate transactions they're taking; is that right?

17 MS. SHEMWELL: In total. It's in total. The
18 list comes in in total.

19 COMMISSIONER JARRETT: I don't understand. What
20 does that mean, by total?

21 MS. SHEMWELL: The total amount of transactions.

22 COMMISSIONER JARRETT: So it comes in --

23 MS. SHEMWELL: It's not these invoices.

24 COMMISSIONER JARRETT: LER, it just says 50
25 transactions?

1 MS. SHEMWELL: I haven't actually reviewed that
2 lately. May I ask someone who may have?

3 COMMISSIONER JARRETT: All right.

4 MS. SHEMWELL: It doesn't tell you the number of
5 transactions. It just tells you the dollars. Or just
6 tells us the dollars because it's submitted. It's not
7 filed, I don't think.

8 COMMISSIONER JARRETT: So when the rule says a
9 full and complete list of all affiliate transactions
10 undertaken and the amount of all affiliate transactions by
11 affiliated entity and account charged, that's just totals?

12 MS. SHEMWELL: That's correct.

13 COMMISSIONER JARRETT: Do you think that's what
14 the rule says?

15 MS. SHEMWELL: Well, it sounds like it could
16 require more.

17 COMMISSIONER JARRETT: And how long has that
18 rule been in effect?

19 MS. SHEMWELL: 2003.

20 COMMISSIONER JARRETT: Okay. And Staff has just
21 been accepting those kind of reports since 2003?

22 MS. SHEMWELL: I would suggest that, yes, every
23 company reports in a different way. Some have very few.
24 Some have many. But yes.

25 COMMISSIONER JARRETT: And then there's also in

1 the rule all kinds of records that affiliated entities
2 have to keep and the company, the gas company, has to make
3 available to the Commission; is that correct?

4 MS. SHEMWELL: Yes, sir.

5 COMMISSIONER JARRETT: Okay. Is Staff saying
6 that any of these records in No. 5, records of affiliated
7 entities, Laclede is refusing to provide?

8 MS. SHEMWELL: They're refusing to provide
9 records of their affiliate entities in those transactions.

10 COMMISSIONER JARRETT: There's eight of them
11 listed here. Could you tell me which one of the eight
12 that they're refusing to provide?

13 MR. THOMPSON: No. 1. Documentation of the
14 costs associated with affiliate transactions that are
15 incurred by the parent or affiliated entity and charged to
16 the regulated gas corporation.

17 COMMISSIONER JARRETT: Okay. And they're not
18 providing that? You were asking for documents that LER
19 had with other entities other than Laclede; isn't that
20 correct? Isn't that what the problem is?

21 MR. THOMPSON: Yes, sir.

22 COMMISSIONER JARRETT: No. 1 doesn't apply to
23 that.

24 MR. THOMPSON: I guess it would depend on how
25 narrowly you would read that one.

1 COMMISSIONER JARRETT: Well, it -- it -- it is
2 transactions between the affiliate and the regulated gas
3 corporation, isn't it, and charged to the regulated gas
4 corporation? So that's not even at issue here, is it?

5 You're looking for documents where the affiliate
6 has made transactions with other entities. That's my
7 understanding. Am I wrong?

8 MS. SHEMWELL: If you look under C, records
9 identifying the basis, which is fair market value of fully
10 distributed costs to records and books or accounts and
11 supporting records in sufficient detail to permit
12 verification of compliance.

13 COMMISSIONER JARRETT: With this rule.

14 MS. SHEMWELL: Yes.

15 COMMISSIONER JARRETT: But aren't you arguing
16 that what you're looking for is really beyond this rule?

17 MS. SHEMWELL: I think what we're suggesting is
18 that we're trying to determine prudence. And the
19 Commission may look at whether or not Laclede Gas, as a
20 regulated entity, has made prudent purchases.

21 COMMISSIONER JARRETT: And I asked this once.
22 I'll ask it again. So I think what I understood
23 Mr. Thompson to say is that Laclede could comply with
24 every letter in spirit of this rule and still be
25 imprudent. Is that what you're saying?

1 MS. SHEMWELL: Well, I think it's possible.
2 Certainly, compliance with the rule would get them a long
3 way to showing prudence. We don't know. We don't know
4 what they've done.

5 We're not saying yet that they've been
6 imprudent. We're suggesting we need documents to
7 determine that. And the documents we're asking for would
8 show fair market value in a very accurate way.

9 And they are required to describe the basis
10 used, fair market value or fully distributed costs. We're
11 looking for documents that show fair market value.
12 They've offered some substitutes, but those substitutes do
13 not actually demonstrate the fair market value.

14 As I said, it can change day to day, the fair
15 market value. It's dependent on many things, where it's
16 delivered, capacity, time of year, many things. So we're
17 looking for documents that actually demonstrate the fair
18 market value, and that is LER's dealings with a third
19 party will determine -- will establish fair market value.

20 There might be some alternatives. And if they'd
21 like to put those forward, we'd be happy to see any
22 documents they have that shows the fair market value of
23 the transaction.

24 But we're saying that the best evidence, the
25 best evidence, is either what LER paid for the gas from

1 Laclede, bought from it, what LER actually paid for that
2 gas that it's supplying to Laclede.

3 We can only know that by looking at the amount
4 for which they purchased it. LER's purchase of the gas
5 establishes the fair market value. LER's sale to Laclede
6 does not establish the fair market value.

7 So we're looking for those documents that prove
8 fair market value. If they produce those under the rule
9 and we see that, yes, they were paying LER a reasonable,
10 prudent price, a fair market value for the gas, what they
11 could have acquired it for themselves or they have sold to
12 LER at what they could have sold it, sold the gas to a
13 third party.

14 So we're looking for documents that prove that.
15 Our position is that the transactions of LER with the
16 third party are the best evidence of that. Laclede could
17 show --

18 COMMISSIONER JARRETT: I guess my confusion is
19 in -- and I think Commissioner Kenny, by his few
20 questions, agrees with me.

21 It's like we keep slipping in and out of the
22 rule. It's like we have the rule, and then we have
23 prudence. You know, if -- if the rule is fully complied
24 with, are they still -- could they still be imprudent?
25 Maybe. Maybe not.

1 So I don't -- I mean, all the company and the
2 public have to go by is the rule. And I -- and I --

3 MS. SHEMWELL: There's also statute that
4 requires a company not to engage in discriminatory
5 conduct.

6 COMMISSIONER JARRETT: Right. But if they
7 follow the rule, they're not engaging in discriminatory
8 conduct, are they?

9 MS. SHEMWELL: Commissioner, if they provide us
10 documents to demonstrate that they have complied with the
11 rule, we'll be a long way towards answering the question.
12 They have provided nothing.

13 We're asking them to provide evidence.
14 Mr. Pendergast stands up and says, We've complied with the
15 affiliate report rules. But we haven't seen it. We
16 haven't seen the documents, and we're looking for the best
17 evidence. We're looking for source documents.

18 COMMISSIONER JARRETT: All right. So what we
19 really are looking at, then, is whether they violated the
20 rule or not?

21 MS. SHEMWELL: That is not exactly the purview,
22 though, of a prudence review. While we think there's an
23 extraordinarily slim chance that they could comply with
24 the rule and still be imprudent, so we can't say
25 absolutely, that's a very slim chance. It's unlikely.

1 It's most likely that if they comply with the
2 rules, then they have made a prudent decision. But for me
3 to say 100 percent when there may be a half a percent
4 chance that something was imprudent, I don't want to tell
5 you 100 percent.

6 But if they can show us that they complied with
7 the rule -- but they also have to comply, again, with
8 non-discriminatory provisions under 393.140 that they
9 don't discriminate, that all charges are just and
10 reasonable, that they're giving their affiliate a benefit
11 and that their charges are not just and reasonable.

12 MR. POSTON: Can I add something?

13 JUDGE JONES: Sure. Mr. Poston. And this kind
14 of follows with what Lera just said. This is a
15 rate-making function when the Commission considers these
16 because these rates have not been considered to determine
17 whether they were just and reasonable.

18 And complying with the affiliate transaction
19 rule would get to the just part -- or a portion of the
20 just part because there's other rules. But there's still
21 that reasonable piece out there that -- that I think gets
22 at the prudence part of it.

23 It needs to be both just and reasonable under
24 393.130. So I think that's where -- yeah, there's the
25 affiliate transaction piece for the just part. But, you

1 know, the Commission's rate-making function goes beyond
2 that, and rates must be both just and reasonable.

3 COMMISSIONER KENNEY: Commissioner Jarrett, may
4 I?

5 COMMISSIONER JARRETT: Sure. Go ahead.

6 COMMISSIONER KENNEY: Let me -- correct me if
7 I'm wrong because it sounds like, I think, somehow along
8 the way, these issues have gotten conflated. Let's assume
9 that the regulated entity purchases no gas from an
10 affiliate.

11 MR. THOMPSON: Right.

12 COMMISSIONER KENNEY: The affiliate transaction
13 rule is not implicated, correct?

14 MR. THOMPSON: Right.

15 MS. SHEMWELL: Correct.

16 COMMISSIONER KENNEY: But you still have to
17 undertake a prudence analysis, correct?

18 MR. THOMPSON: Exactly.

19 COMMISSIONER KENNEY: So they're separate and
20 distinct from either other?

21 MR. THOMPSON: Right.

22 COMMISSIONER KENNEY: Correct?

23 MR. THOMPSON: Yes, sir.

24 COMMISSIONER KENNEY: This does not define in
25 total the scope of your discovery request; is that

1 correct?

2 MS. SHEMWELL: Yes, sir.

3 MR. THOMPSON: That is correct.

4 COMMISSIONER KENNEY: Okay. So the affiliate
5 transaction rule in compliance with or a violation of it
6 is one component of a prudence review. It's not the total
7 sum of a prudence review, correct?

8 MR. THOMPSON: Correct.

9 COMMISSIONER KENNEY: Okay. All right. I
10 understand, then. Thanks.

11 MS. SHEMWELL: Thank you.

12 COMMISSIONER JARRETT: Well, I'm looking at the
13 purpose under 4 CSR 240-40.015 Affiliate -- Affiliate
14 Transaction Purpose. This rule is intended to prevent
15 regulated utilities from subsidizing their non-regulated
16 operation. In order to accomplish this objective, the
17 rule sets forth financial standards, evidentiary standards
18 and record-keeping requirements applicable to any Missouri
19 Public Service Commission regulated gas corporation
20 whenever such corporation participates in transactions
21 with any affiliated entity except with regard to HVAC
22 services as defined in Section 386.754 RSMO Supp., 1998 by
23 the General Assembly of Missouri.

24 This rule and its effective enforcement will
25 provide the public the assurance that their rates are not

1 adversely impacted by the utility's non-regulated
2 activities. So aren't we really talking about the rule
3 and the scope of the rule?

4 MR. THOMPSON: I think we are. I think the rule
5 is certainly -- the prudence review is not identical to a
6 review of compliance with that rule. But a prudence
7 review where there had been affiliate transactions
8 necessarily implicates that.

9 COMMISSIONER JARRETT: Right. So I guess my
10 question is, what Staff is arguing is that the prudence
11 review goes beyond this rule?

12 MR. THOMPSON: That's correct.

13 COMMISSIONER JARRETT: Even though the purpose
14 says that the rule and its effective enforcement will
15 provide the public the assurance that their rates are not
16 adversely impacted by the utility's non-regulated
17 activities?

18 MS. SHEMWELL: But the Commission's
19 determination that a rate is just and reasonable also does
20 that. There are many things that may assure the public
21 that it is paying only just and reasonable rates.

22 The statutes requiring non-discriminatory
23 service, for example, the statutes that require them -- it
24 says all unjust and unreasonable rates are invalid,
25 393.130. So the Commission must assure just and

1 reasonable rates. This is one method of doing that.

2 But prudence review reviews all of the gas
3 transactions, not just those with affiliates.

4 COMMISSIONER JARRETT: All right. I don't think
5 I have any more questions right now. I'm sure after
6 Mr. Pendergast speaks, I may have some more questions of
7 him and then, also, of Staff.

8 JUDGE JONES: Commissioner Kenney, do you have
9 any questions of Staff?

10 COMMISSIONER KENNEY: No. I'm good. Thanks.

11 MS. SHEMWELL: Thank you.

12 JUDGE JONES: Thank you. Mr. Poston, I noticed
13 you jumped in. Are you wanting to give an opening or --

14 MR. POSTON: No. I don't have anything
15 prepared. Thank you.

16 JUDGE JONES: Okay. Mr. Pendergast?

17 MR. PENDERGAST: Thank you. I'd just like to
18 begin by noting that we did file a motion for the
19 Commission to rescind its prior order, and I won't go into
20 detail here since I went into detail there.

21 But, quite frankly, there were three
22 Commissioners that already voted, in our view, to deny
23 these motions for reconsideration. It was clear on the
24 record of the Commission's agenda meeting that that
25 determination was made. I, to this day, don't know why

1 that wasn't ultimately reflected in a final order that was
2 issued so that we wouldn't have to be here today.

3 The Commission's scheduling process is rather
4 opaque. It's difficult to determine why decisions are
5 made and why things are scheduled as they are. But I just
6 want to note from the very beginning that because we're
7 participating in this and we appreciate the opportunity to
8 do it, that we don't acquiesce to the justness and
9 reasonableness and lawfulness of being here today.

10 That said, what we really have here today is not
11 just a simple discovery matter. If it was a simple
12 discovery matter, it would have been resolved one way or
13 another a long time ago.

14 I think what we really have here today is a
15 test. And it's a test of whether the Commission is going
16 to comply with its own practices, procedures and rules or
17 its not going to and it's going to dismiss them and run
18 rough-shod over them out of some misdirected desire for
19 information.

20 We had a lot of talk about the standards, and I
21 think Commissioner Kenney and I think Commissioner Jarrett
22 got to the heart of the matter and it got to the heart of
23 the matter rather quickly.

24 And the standards we've been living under for
25 the last eight years since we had our holding company

1 reorganization and for the last seven years or six years
2 since the affiliate transaction rule became applicable to
3 us are what was in that CAM that was lawfully approved by
4 the Commission and what was in the affiliate transaction
5 rule.

6 And I'd like to direct your attention to a
7 hand-out I gave -- and I think you also have it,
8 Commissioner Jarrett. Maybe not. But at the time we had
9 our holding company -- and you had a lot of discussion
10 here about the cost allocation manual. And, really, the
11 cost allocation manual was borne in the holding company
12 docket that we had and was also woven into the affiliate
13 transaction rule as a way of making sure that the
14 standards you've talked about today are being complied
15 with.

16 At the time we had the holding company, there
17 was a lot of discussion among the Staff about, Well, how
18 do we protect ratepayers? How do we make sure ratepayers
19 aren't adversely impacted if we have transactions between
20 Laclede and its affiliates?

21 And as you can see on page 3, the discussions in
22 support of the stipulation and agreement that was
23 ultimately filed talked about the Cost Allocation Manual.
24 And in that, it said Staff Witness, Steven Rackers, filed
25 testimony that stated that the CAM should be maintained

1 and submitted to ensure that ratepayers were not being
2 harmed by any affiliate corporation transactions that
3 might take place after the proposed restructuring.

4 After extensive negotiation, substantially all
5 of the CAM suggestions sought by Staff were accepted by
6 the gas company.

7 In addition, compliance with the CAM procedures
8 was extended to all personnel of the gas company, would be
9 made a standard element of the company's code of conduct
10 applicable to employees.

11 Now, what we have here is the Staff coming
12 forward with a blueprint. And the blueprint says, This is
13 what you'll do, this is how you'll conduct your
14 transactions, this is how you will price your transactions
15 in order to ensure that ratepayers will be protected.

16 We fast forward six or seven years, and we have
17 Mr. Reed coming up on behalf of the Commission Staff and
18 saying, Not so fast. Not so fast. We may have provided
19 you a blueprint six or seven years ago. We may have said,
20 This is what you need to do in toward to go ahead and make
21 sure ratepayers are protected, but now there's something
22 else that we want to go ahead and say might be added to
23 the element.

24 We didn't tell you about it back then. We
25 didn't tell you about it until we filed an ACA

1 recommendation. But it's something different, something
2 new, something you haven't seen before, and that's how
3 we're going to go ahead and judge the propriety of your
4 actions that have already taken place under the blueprint
5 that we developed and we provided to you.

6 The same thing is true of the affiliate
7 transaction rule. It sets forth with great detail what
8 the standards of those -- you're supposed to follow in
9 pricing out your transactions, whether you're purchasing
10 from a utility or you're selling to go a utility.

11 We have complied with those transactions.
12 Contrary to Ms. Shemwell's statement, we have provided
13 thousands of pages of documents showing that we bought gas
14 at a fair market price and how we came up with a
15 determination it was a fair market price based on sales
16 that were being made by unaffiliated vendors.

17 We have provided lots of information showing
18 what our costs are. And the problem we have here is that
19 instead of the standard that's in the affiliate
20 transaction rule, which is basically a fair market price
21 because if we're going to buy stuff in the wholesale
22 market, you know, we don't have our own gas supply. We
23 don't have our own oil wells or gas wells. We have to buy
24 from a third party. So fair market price and cost of the
25 utility are essentially the same thing.

1 We have provided significant information to
2 Staff that shows that it was a fair market price, but
3 Staff has a different standard. And I think Mr. Thompson
4 said what that standard was today. It's the lowest cost
5 of gas in the affiliate's portfolio.

6 Well, read the CAM. You won't find that
7 standard in it. Read the affiliate transaction rule. You
8 won't find that standard in it. And the reason you won't
9 find it in it is because nobody would do affiliate
10 transactions under those circumstances.

11 If I'm a company and I'm going to sell you gas,
12 and every time I sell you gas, I have to go ahead and sell
13 it at the lowest cost of gas in my portfolio, and not only
14 the lowest cost of gas in my portfolio, but without any
15 profit, without my markup, who in the world is going to
16 make a sale under those circumstances? Nobody. Of course
17 nobody's going to do it.

18 And that's why Staff's standard for which
19 they're seeking the information to go ahead and prove up
20 is incontinence by affiliate transaction rule. It's not
21 in any way consistent with the CAM.

22 And, quite frankly, they should not be allowed
23 to pursue additional information to prove up that patently
24 unlawful standard. Do you have a question?

25 COMMISSIONER KENNEY: Well, I do. But I want to

1 let you finish first.

2 Mr. PENDERGAST: Okay. The same thing is true
3 on the sales side. On the sales side, they're saying,
4 Well, you know, you may have gone ahead and made a sale to
5 your affiliate. It may have been at a market price at the
6 time you went ahead and made it, but maybe the affiliate
7 took that and maybe it went ahead and made an additional
8 sale someplace else. If they did, we want to go ahead and
9 get whatever profit they made on that additional sale.

10 Once again, what company would ever buy from
11 another company if the deal was, okay, I'm going to sell
12 it to you, but if you make any money on it, if you sell it
13 to anybody else, we want whatever profit you made.

14 Nobody would go ahead and operate under that
15 kind of business. And that's why the standard for which
16 they're seeking information to prove is not contemplated
17 by the affiliate transaction rule, not contemplated by the
18 CAM because it would effectively make it impossible to do
19 transactions that the rules freely permit us to do.

20 And we summed it up in the last oral argument
21 that we had, and I think it bears repeating. The rule,
22 the CAM, basically provides that it's a fair market price,
23 whether it's a sale or whether it's a purchase. That is
24 the price that you have to go ahead and look at. That's
25 the documentation we have provided to show both the sales

1 and the purchases that we made involving LER were done in
2 that kind of fashion based on a fair market price.

3 And as I said, when it comes to purchases, Staff
4 wants to go ahead and make it the lowest cost of gas in
5 the portfolio, in the affiliate's portfolio. Nowhere to
6 be found in the rule.

7 And the problem with that is it's not in the
8 rule. Ours is. Theirs isn't. There's another part of
9 the rule that does say don't discriminate between
10 affiliates -- or between affiliated suppliers or marketers
11 -- unaffiliated suppliers and marketers.

12 Well, if we're going to go ahead and tell LER,
13 If we buy gas from you, you have to go ahead and give it
14 to us at the lowest cost of gas in your portfolio, but we
15 buy something from BP/Amoco and we say, Well, we'll buy it
16 from you at the market price regardless of what kind of
17 costs you have in the portfolio, are we discriminating?
18 Are we saying we're going to treat LER in a different
19 fashion, erratically different fashion than we are
20 BP/Amoco? Of course, we are.

21 And that's what Staff's proposed standard does.
22 It's not what our proposed standard does. Our standard is
23 consistent with the non-discrimination provisions in the
24 rule. Complies with the Cost Allocation Manual? Ours
25 does. Staff's does not.

1 As I said before, you can look throughout the
2 CAM. You can look throughout the affiliate transaction
3 rule. You won't see lowest cost of gas in the affiliate's
4 portfolio or whatever the affiliate makes on whatever you
5 sell them anywhere in those rules or that CAM.

6 Permits rational affiliate transactions to
7 occur? Ours does. If we buy something and it's a fair
8 market price, LER or anybody else we buy gas from has at
9 least an opportunity to make a profit. Under Staff's
10 approach, you can't.

11 And if we sell something to you, we're going to
12 go ahead and take the benefit of any profits you may make
13 on that later on. You can't do transactions under those
14 circumstances.

15 So our approach and our standard permits these
16 transactions to take place as contemplated by your rule.
17 Staff's standard does not. And is it in the interest of
18 the best -- best interest of the company's ratepayers? I
19 submit to you that it's not. And I'll show you why.

20 Here's what the real impact of having a
21 marketing affiliate like LER has been. Everybody
22 understands that not too long ago, credit markets were
23 very, very tight. Liquidity was very, very low.

24 LER, because it has had some success, has
25 generated cash, and that cash was loaned to Laclede at

1 extremely favorable rates. And it became a source of
2 revenue that we could use to make sure that we had plenty
3 of resources to purchase gas supplies, to hedge gas
4 supplies, so forth and so on.

5 It's been a reliable supplier to us in the few
6 instances that we've used them. They've never failed us.
7 They've never failed to deliver on the gas supply. And
8 they've been a market for our off system sales.

9 And you had a lot of discussion here about,
10 Well, we need to go ahead and look at whether or not LER
11 is taking capacity or gas sales that Laclede has made and
12 use that to go ahead and make sales that could have gone
13 to Laclede.

14 Well, let's take a look at it on a macro basis.
15 Now, if you take Staff at its word, you would think that
16 there's been some concerted effort to say, Let's release
17 capacity to LER. Let's go ahead and let them use our gas
18 supply assets so that they can go out and make some money
19 and they'll be able to go ahead and keep all that, whereas
20 if Laclede, the gas company, goes ahead and does it, you
21 know, we have to gift 70 percent back or 50 percent or
22 whatever the percentage was at the time.

23 Well, we've got the 2004-2005 ACA periods here,
24 the 2005-2006. And if you look at what our off-system
25 sales on the regulated side have done, you see that they

1 have not only gone up since 2003, but nearly doubled.

2 Now, you know, if you look at something like
3 that and you think there's been some big conspiracy to
4 migrate revenues from the gas company over to LER,
5 clearly, it was a very subtle conspiracy, presumably one
6 where everybody sat down and said, Well, let's do that,
7 but let's try and make it look good on the regulated side
8 by making sure that we increase and increase significantly
9 the off-system sales we're making on the regulated side
10 just so hopefully nobody will notice.

11 You would also go ahead and take it from Staff
12 that LER's fortunes have gone ahead and been fueled by its
13 reliance on sales and assets of Laclede Gas Company.

14 Let's put it in perspective. Here are LER's
15 sales to Laclede over the last four years. And in your
16 packet, I think you also have LER's purchases from
17 Laclede. And it's pretty comparable in nature.

18 As you can see, Laclede's -- or LER' sales from
19 Laclede have always been below 10 percent, and they've
20 been declining to where in 2008 they were below 1 percent.
21 The same thing is true if you look at it on the flip-side
22 and its purchases LER from Laclede.

23 I suggest to you that that doesn't sound like a
24 -- an arrangement where LER has in any way lived off the
25 assets of Laclede Gas Company. And it's these small blue

1 area right here, small blue area here that Staff is using
2 as a pretext based on its unauthorized and unlawful
3 standards to get access to all of the records of LER for
4 the other 95 percent of transactions that it's done with
5 third parties.

6 And I suggest to you that they haven't done
7 anything, anything to show that it's appropriate to do
8 that. But you don't have to take my word for it. From
9 the beginning of this proceeding, what we have said -- and
10 Staff came in with a couple of supposed transactions that
11 they thought were inappropriate.

12 And the thing that we ought to do, like we do in
13 every ACA proceeding is, let's have a hearing. Let's have
14 an evidentiary hearing where Staff can come in. They can
15 present these transactions. They can say why they think
16 it's inappropriate. We can go ahead and say why we think
17 it's consistent with the affiliate transaction rule, why
18 it's consistent with the CAM, why there was nothing rotten
19 in Denmark, why there was nothing inappropriate.

20 We'll have everybody subjected to the rigors of
21 cross-examination. It won't be just a bunch of attorneys
22 standing around talking about facts that aren't in
23 evidence. It will be an evidentiary hearing, and we'll
24 see whether there's any substance or any validity to the
25 examples that they've given.

1 You'll have a full factual record on which to
2 determine what the law really is, how the law really
3 applies and whether there's any reason to go forward and
4 have this mammoth investigation of an unregulated company.

5 Now, I have to ask you, why isn't that fair?
6 Why isn't that the appropriate thing to do? If Staff has
7 its theory and its brought forward examples of what it
8 thinks is inappropriate pricing, then let's have a hearing
9 and see whether there's any substance to those
10 allegations.

11 I submit to you that that's the fair thing to
12 do. That's the reasonable thing to do. That protects us
13 and gives us some due process in this process. And
14 there's absolutely no reason in the world why we shouldn't
15 pursue that particular approach.

16 I think it's time for Staff to come forward with
17 more than just ways of trying to suggest that the rules
18 aren't what they say or they're not complete or there's
19 something else out there that nobody knew about and nobody
20 was advised about and nobody was notified about that adds
21 to these standards.

22 I think it's time to go ahead -- and if Staff's
23 confident in what it's say, let's have an evidentiary
24 hearing and see whether there's any validity to what they
25 say or any validity to what we say. Thank you.

1 JUDGE JONES: Okay. Questions from the Bench?
2 Commissioner Jarrett? Commissioner Kenney?

3 COMMISSIONER KENNEY: Let me -- thank you. And
4 I'll ask some of the same questions. Let me back up and
5 -- the evidentiary hearing and -- why isn't this, what
6 we're here for today, simply a discovery dispute and
7 nothing more? Because, I mean, I'm framing it in my brain
8 as just that. And so I'm asking that question.

9 But then, secondarily, if we assume, as I'm
10 assuming, that this is a discovery dispute, the issues
11 that you're discussing will be held in abeyance for an
12 evidentiary hearing. The evidentiary hearing isn't
13 precluded by this proceeding that we're going through
14 today and what the outcome of this proceeding is.

15 MR. PENDERGAST: Well, it may not be precluded
16 ultimately from doing it, but the typical approach in an
17 ACA is Staff comes in and makes a recommendation.

18 In this case, they made a recommendation that
19 said, I think there should be a couple of disallowances
20 because you paid too much for gas notwithstanding what we
21 think was full compliance with the affiliate transaction
22 rule.

23 And to pursue this particular approach, we need
24 to go ahead and obtain all this additional information, do
25 an audit of a billion dollar company in order to go ahead

1 and see whether there's anything inappropriate here.

2 And I suggest to you, Commissioner, that's
3 putting the cart before the horse.

4 COMMISSIONER KENNEY: Well -- and let -- so let
5 me -- that begs the question, though. I mean, if that is,
6 in fact, what Staff is doing and they're asserting some
7 theory and they're making recommendations that certain
8 costs should be disallowed, by allowing access to these
9 documents, if that's what we ultimately do, we're not
10 passing judgment on the appropriateness or the
11 inappropriateness of this new standard that Staff is
12 coming up with, are we?

13 MR. PENDERGAST: No. What you're doing is
14 you're ignoring what your rules say. You're ignoring what
15 the CAM said. You're ignoring what the standards are and
16 you're saying, We're not going to go ahead and pay any
17 attention to them. We're going go ahead and allow the
18 party to pursue whatever information they want no matter
19 how inconsistent they happen to be with their own rules
20 and their own CAM that a utility has religiously and
21 faithfully relied upon for the last six or seven years.

22 And I don't think you should permit a fishing
23 expedition based on what I think are patently unlawful
24 standards.

25 COMMISSIONER KENNEY: Well, and that -- that's

1 two different statements there. And so let me ask you
2 this: I think you're right. We shouldn't allow fishing
3 expeditions if that's what this, in fact, is.

4 But isn't that different than saying that we are
5 -- that an ACA, in the contours of the information that
6 they are allowed to obtain, is limited by what's in the
7 CAM and the affiliate transaction rule?

8 MR. PENDERGAST: You know, Commissioner, I -- I
9 -- and I said it at the last oral argument. I think there
10 are a limited number of instances where the rule wouldn't
11 necessarily -- compliance with the rule wouldn't
12 necessarily bless a transaction. Let me tell you what I
13 think they are.

14 COMMISSIONER KENNEY: So you do agree -- so
15 Staff and Laclede are in agreement in that regard at
16 least?

17 MR. PENDERGAST: Certainly not in agreement on
18 what they say is a reasonable area to look into that may
19 not be covered by the rule. And let me tell -- you --

20 COMMISSIONER KENNEY: But the general
21 proposition that compliance with the affiliate transaction
22 rule does not automatically mean that you've complied with
23 the -- that you've been prudent.

24 MR. PENDERGAST: It -- it -- it does not --

25 COMMISSIONER KENNEY: You agree with that?

1 MR. PENDERGAST: I agree with that in a very
2 limited number of circumstances, one of which is decidedly
3 not this one. And let's give you a couple examples.

4 Let's say I go forward and I buy twice as much
5 gas as I really need. Okay? And the Staff comes in and
6 said, What did you buy all that gas all for? You didn't
7 need all that. You only needed half of it to go ahead and
8 serve your customer.

9 Now, whether I had gone ahead and bought it from
10 an affiliate or not, you know, just because I bought it
11 from an affiliate and it happened to be appropriately
12 priced, the fact that I bought twice as much as I need, I
13 think, would be still be a matter of prudence. That has
14 not been alleged in this case. That is not what Staff is
15 seeking information to.

16 The second area is if I bought gas, say, at a
17 very expensive pipeline and I said, I'm going to go ahead
18 and buy down here even though I could go ahead and take it
19 over there, and I'm going to go ahead and -- and do it no
20 matter what the economics are, I guess, whether I bought
21 if from an affiliate or not an affiliate, you could go
22 ahead and second-guess that and do a prudence.

23 The interesting thing about either of those is
24 you don't need affiliate records to go ahead and do a
25 prudence evaluation on that. You can determine whether I

1 bought too much gas just by how much gas I bought.

2 You don't have to go ahead and have affiliate
3 records to go ahead and determine, Well, you should have
4 bought it over on this pipeline rather than that pipeline.
5 You have plenty of records to go ahead and establish that.
6 You do not need this fishing expedition in order to get
7 that kind of information.

8 COMMISSIONER KENNEY: Let me ask another
9 question, then. Is the basis of Laclede's objection that
10 these documents that they're asking -- what's the basis --
11 I mean is it irrelevant? Is it overly broad and unduly
12 burdensome?

13 MR. PENDERGAST: It's irrelevant because they're
14 being asked pursuant to a standard that's directly
15 contrary to your rules. And there's no question about it.
16 That's been conceded. It's been admitted. And it's
17 directly contrary to the CAM. And there's no exception,
18 whether you want to call it prudence or anything else,
19 that justifies obtaining this kind of information for the
20 kind of standard that they're saying ought to be followed.

21 You don't have a standard that says lowest cost
22 of gas in the gas portfolio. And we don't need, you know,
23 even a hearing to make that determination.

24 COMMISSIONER KENNEY: But we're not -- we're not
25 blessing that standard.

1 MR. PENDERGAST: Well, if you go ahead and you
2 tell Staff based on a blatantly false, unsupported
3 standard like that they can go out and they can pursue a
4 massive audit of an unregulated company in order to try
5 and prove up that standard, I think everybody today can
6 sit there and look at the rule and say it ain't in there,
7 then I think you may not be blessing it, but you're
8 certainly putting a lot of people to a lot of burden for
9 what is patently an unreasonable exercise.

10 And -- and as I said, Commissioner, you know,
11 you don't have to make a determination today. Have an
12 evidentiary hearing where we can go ahead and sort through
13 these things, and we can all say what our view of the
14 affiliate transaction rule is and what our view of
15 prudence is and we can look at the transactions that Staff
16 has brought up.

17 And if after you do that and you determine,
18 Well, there's something fishy here, there's something
19 rotten in Denmark, then maybe you go ahead and do that.
20 I don't think you will.

21 But I think you either deny this outright or you
22 say, Staff, it's time to go ahead and put your allegations
23 to the test. Because I certainly haven't heard a cogent
24 defense of the standard that they've said they want to
25 pursue this information to obtain. Maybe you have. But I

1 haven't.

2 COMMISSIONER KENNEY: All right. I mean -- and
3 I just want to encapsulate this and put this -- you have
4 to forgive me. I'm thinking about this as a litigator, so
5 I'm trying to put this in the context of how this would be
6 argued in a traditional litigation context.

7 Is Laclede's argument that the CAM and the
8 affiliate transaction rule, in this context at least,
9 define the contours of the documents that Staff is allowed
10 access to?

11 MR. PENDERGAST: Yes. I would say that the CAM
12 and affiliate transaction rule affirmatively preclude the
13 kind of standard that Staff is relying on in order to
14 obtain the information that it says it wants.

15 COMMISSIONER KENNEY: But I'm thinking about
16 this in two different steps. I mean, this -- I'm not
17 putting a stamp of approval or casting an opinion about
18 the standard that Staff is putting forward. I just want
19 to know whether the documents are relevant to a prudence
20 review.

21 MR. PENDERGAST: No. And I don't think they're
22 relevant to a prudence review. And I think you ought to
23 go ahead and take to heart what Kevin Thompson here, when
24 he was a regulatory law judge, wrote in an AmerenUE case.

25 It says that it is true that the Commission is

1 authorized to require and examine the dealings with
2 regulated entities with their unregulated affiliates.
3 However, that authority applies to transactions between
4 the affiliates and the regulated entity.

5 It does not apply to transactions between the
6 unregulated affiliates and third parties absent a specific
7 showing of relevancy to transactions between the
8 affiliates and the regulated entity.

9 And what the Staff has done to show you
10 relevance is to come in and say, I've got a standard here.
11 It's a standard of lowest cost gas in the affiliate's
12 portfolio or it's a standard of, Let's follow the
13 affiliate around and see if it did anything with the
14 assets that you sold to them at the fair market price.

15 It doesn't even begin to comply with any
16 standard that you've authorized and any standard that
17 would make that information relevant. Doesn't even begin
18 to.

19 COMMISSIONER KENNEY: The -- the opinion that
20 you were just reading from, was that in the context of an
21 ACA review?

22 MR. PENDERGAST: No. That was in the context of
23 an Ameren case.

24 COMMISSIONER KENNEY: Okay.

25 MR. PENDERGAST: And it had to do with their

1 dealings with this an unregulated affiliate. And I just
2 have to quite tell you, quite candidly, that the ability
3 to go out and do prudence reviews and to say, The
4 affiliate transaction rules, well, they don't apply, or,
5 we can go ahead in the form of a prudence review come up
6 with any standard we want -- I mean, if we had known, I
7 guess, back in 2001 that here are the standards that we
8 have to meet, Here's how we have to conduct our
9 transactions and, oh, yes, at some point in the future,
10 somebody on Staff may come in and say, Well, I've got this
11 vague, ill-defined prudence standard that's going to go
12 ahead and change all of the standards that you've been
13 living by over the last six or seven years, and -- you
14 know, I don't know. Maybe we never would have done any
15 transactions at all.

16 But I tell you, that's a fundamental problem
17 with due process, advising parties what the rules of game
18 are. And what Staff is trying to do is change those rules
19 today. And you shouldn't let them do it.

20 MR. ZUCKER: Commissioner Kenney? Over here.
21 If I may supplement Mr. Pendergast's response?

22 COMMISSIONER KENNEY: Sure.

23 MR. ZUCKER: You've asked the question is
24 prudence the same as the affiliate transaction rule? How
25 close do they overlap in this case? Is there some

1 prudence -- is there some part of prudence that isn't part
2 of affiliate transaction rule?

3 And the answer is that, in this case, there is
4 not. They overlap 100 percent. And the prudence is the
5 affiliate transaction rule. And I'll tell you why.
6 That's because that in this case, Staff's done an audit.
7 They've looked for -- they spend a year doing it.

8 And what they've come up with a -- an allegation
9 that Laclede Gas Company paid too much when they bought
10 gas from LER. And so the sole issue here is the pricing
11 of an affiliate transaction.

12 And when that is the issue, the -- the
13 Commission has a rule that covers that issue specifically,
14 as you and Commissioner Jarrett have raised, and that rule
15 is the affiliate from action rule. It tells you --
16 between that and our CAM, it tells you exactly how those
17 transactions should be priced.

18 And that's exactly what this case should be
19 about. Did Laclede price these transactions in accordance
20 with the affiliate transaction rule? And the information
21 Staff's looking for has nothing to do with the affiliate
22 transactions that Laclede entered into.

23 COMMISSIONER KENNEY: I mean, I think -- it
24 occurs to me or it seems to me that Staff is conceding
25 that it's going beyond the list of standards that are set

1 forth in the affiliate transaction rule because they don't
2 overlap in their -- in their estimation. And so what I'm
3 trying to get my brain wrapped around, it seems to me what
4 they're arguing is that they need to see the documents
5 that demonstrate the transaction between LER and whomever
6 it bought the gas from. Is that your understanding of
7 what they're looking at?

8 MR. PENDERGAST: You know what? My
9 understanding of what they're looking at is they want to
10 find the lowest cost of gas in LER's portfolio so they can
11 go ahead and say, Instead of using fair market price, I
12 want to use that lowest cost of gas in your portfolio.

13 COMMISSIONER KENNEY: What --

14 MR. PENDERGAST: I mean, Mr. Thompson said that.
15 That's not in your rules.

16 COMMISSIONER KENNEY: I didn't -- let me make
17 sure I'm understanding because I didn't hear him say that.
18 Presumably, LER buys gas, right?

19 MR. PENDERGAST: Right.

20 COMMISSIONER KENNEY: Some of it it sells to
21 Laclede, and some to other folks, right?

22 MR. PENDERGAST: Right.

23 COMMISSIONER KENNEY: Are -- is Staff asking for
24 the underlying documents showing the purchases, LER's
25 purchases of the gas that it ultimately sold to Laclede,

1 or are they asking for the underlying documents of all of
2 LER's purchases, whether they sold to Laclede or somebody
3 else?

4 MR. PENDERGAST: They're looking for the
5 underlying documents of all purchases that were made by
6 LER from whatever source for whatever reason. You know,
7 we provided them with documents showing what LER -- what
8 they purchased from on the pipeline that we were providing
9 this from.

10 You know, they -- they wanted more than that.
11 They wanted to go ahead and see all LER invoices. They
12 wanted to see all of LER's sales information, 95 percent
13 of which involves transactions with other parties.

14 They want to go ahead and see what LER did with
15 any capacity that we went ahead and released to them. And
16 they want to do it, as I said before, pursuant to a
17 standard that's unlawful and unauthorized by the rules
18 that you have gone ahead and adopted.

19 COMMISSIONER KENNEY: Are they making an
20 allegation that any of those transactions are
21 inappropriate, or are they just wanting to determine
22 whether or not they are appropriate?

23 MR. PENDERGAST: My -- my --

24 COMMISSIONER KENNEY: It seems that they can't
25 make a determination one way or the other until they

1 actually see the documents.

2 MR. PENDERGAST: They can make a determination
3 because we have shown them time and time again what the
4 market-based price was for these transactions from
5 unaffiliated suppliers and unaffiliated purchasers at the
6 same time that they made these transactions with LER.

7 Now, that's the fair market kind of indicia
8 that's provided for in our CAM. It's provided for in the
9 affiliate transaction rule. And that's what's relevant.

10 What isn't relevant is, Can I find someplace
11 where LER would serve a heck of a lot more customers than
12 just Laclede, may have bought gas for somebody other than
13 Laclede and attributed that lowest price gas to the
14 regulated gas company?

15 Once again, it's not in your rules. And the
16 reason it's not in your rules is because nobody would do
17 business under those circumstances. And that's the
18 standard Staff's trying to apply.

19 MS. SHEMWELL: Staff is trying to apply a
20 prudence standard. It --

21 COMMISSIONER KENNEY: What Mr. Pendergast just
22 described, is that the standard that Staff is attempting
23 to apply? I mean, are you looking into all of LER's sales
24 -- or purchases rather, and then its ultimate sales to
25 other entities other than Laclede and trying to determine

1 whether -- whatever the lowest price that it paid
2 irrespective of who it ultimately sold to? Is that the
3 price you're trying to attribute purchases -- sales to
4 Laclede? Did I restate what you just articulated?

5 MR. PENDERGAST: I think pretty fairly.

6 MR. THOMPSON: We're trying to determine what
7 LER spent to acquire the gas that it sold to Laclede in
8 fulfillment of those contracts.

9 COMMISSIONER KENNEY: So are the underlying
10 documents you're trying to obtain just the documents that
11 would reflect the gas that LER purchased that ultimately
12 sold to Laclede or all of LER's purchases irrespective of
13 to whom it ultimately was sold?

14 MR. THOMPSON: I think we're trying to get all
15 purchase information for four months out of the two-year
16 period.

17 COMMISSIONER KENNEY: All -- all of LER's
18 purchases irrespective of to whom it was ultimately sold?

19 MR. THOMPSON: Well, the gas mixes.

20 MS. SHEMWELL: Spongeable.

21 MR. THOMPSON: I mean, it's not -- you can't say
22 that this molecule that was acquired in Texas eventually
23 wound up with Laclede while this other molecule from
24 Louisiana wound up somewhere else.

25 MR. PENDERGAST: And Mr. Thompson is quite

1 right. It is just a portfolio of gas supply sources from
2 different areas. And that's why the exercise is going to
3 be even more futile and even more irrelevant regardless of
4 whether it's done pursuant to a standard that you've
5 authorized, which you didn't.

6 They're going to go ahead and see a lot of gas
7 that was bought for different purposes at different
8 places. And -- and what is that going to mean in the
9 context and in terms of whether what we purchased from LER
10 at the time with unaffiliated suppliers being used to show
11 what the benchmark price was was a fair market price or
12 not? How -- how is that possibly relevant to anything?
13 Can you answer that question?

14 COMMISSIONER DAVIS: Whoa, whoa. I want to get
15 in here just for a second. And tell me -- I mean, why --
16 I mean, why -- why is the weighted average cost of the gas
17 relevant?

18 MS. SHEMWELL: We're trying to establish fair
19 market value. What's the fair market value of what
20 Laclede bought from LER?

21 COMMISSIONER DAVIS: If they -- but -- the fair
22 market -- I mean, when we -- I'm just trying to think of
23 how to -- how to articulate this question here. But when
24 we -- Commissioner Kenney, forgive me, but you're -- I
25 mean, it certainly seems like -- you have market data. I

1 mean, doesn't that market data -- I mean, you know the
2 difference between -- between Henry Hub, the ICE market --
3 I mean, we know what those market prices are. So how is
4 this -- how is this different, Ms. Shemwell?

5 MS. SHEMWELL: Under the contract for LER,
6 Laclede has established a price that is Nimex minus 10
7 cents. LER is likely buying gas from Mid-Continent, which
8 is much lower. If it's lower, then Laclede has not -- is
9 not buying at a fair market value. Laclede could buy from
10 another supplier out in the Mid-Continent at -- at a lower
11 price.

12 So to buy from LER when the price is much higher
13 than they could otherwise acquire it or higher than the
14 fair market value is the question. Now --

15 COMMISSIONER KENNEY: And can you determine that
16 without looking at the underlying purchases by LER?

17 MS. SHEMWELL: No.

18 COMMISSIONER KENNEY: Okay.

19 MS. SHEMWELL: Because there is no index price
20 for St. Louis.

21 MR. PENDERGAST: What you can look at is --

22 MS. SHEMWELL: The fair market price for St.
23 Louis is not Nimex.

24 MR. PENDERGAST: But let me tell you what you
25 can look at. What you can look at is a BP/Amoco contract

1 we gave you for the same location where we went ahead and
2 bought gas from LER. And that BP contract will show that
3 the pricing considerations that LER sold the gas to us for
4 were the same as BP/Amoco, an unaffiliated supplier was
5 willing to provide. Ms. Shemwell said, We've got to look
6 at the St. Louis market because BP -- or Laclede -- or
7 excuse me -- LER had the ability to go ahead and deliver
8 to the St. Louis market and maybe, just maybe, they could
9 have gotten gas from a cheaper source.

10 Well, then let's look at the St. Louis market.
11 And what we have provided to Staff is the contract that
12 LER has with unaffiliated purchases, the School
13 Aggregation people that was put out for a competitive bid
14 because the schools have to go ahead and do that.

15 And it just so happens that the price that LER
16 charged Laclede was at or below the prices that LER was
17 charging all of these schools, 280, 300 schools, at or
18 below.

19 Now, you know, why doesn't the inquiry end there
20 under your rule? I think it should. And --

21 COMMISSIONER KENNEY: What you just described,
22 is that defined by the affiliate transaction rule?

23 MR. PENDERGAST: Yeah.

24 COMMISSIONER KENNEY: LER's sales to other third
25 parties? Is that encompassed by the affiliate transaction

1 rule?

2 MR. PENDERGAST: We -- we had already provided
3 Staff with information on the MRT Westline that showed
4 that this was a reasonable deal if you purchase down
5 there.

6 We had purchased down there religiously for the
7 last seven or eight years. Staff never alleged that we
8 shouldn't be purchasing from there. But in an additional
9 effort to try and appease them and show them some
10 additional information to set them at ease, we gave them
11 that as well.

12 COMMISSIONER KENNEY: You see what I'm getting
13 at, though?

14 MR. PENDERGAST: I do see what you're getting
15 at.

16 COMMISSIONER KENNEY: You've already provided
17 them documents that are outside of the scope of --

18 MR. PENDERGAST: We've gone above and beyond,
19 and we've been rewarded with --

20 COMMISSIONER KENNEY: Yeah. Let me -- let me
21 finish my question.

22 MR. PENDERGAST: Yes.

23 COMMISSIONER KENNEY: What you just described to
24 me, the sales that you were just describing to me, in
25 order to demonstrate the relevant St. Louis market, were

1 those sales governed by the affiliate transaction rule?

2 MR. PENDERGAST: Is that something we were
3 required to provide under the affiliate transaction rule?

4 COMMISSIONER KENNEY: Right.

5 MR. PENDERGAST: Probably not. Probably --

6 COMMISSIONER KENNEY: So you're -- you're -- you
7 will concede, then, that you -- Laclede is willing to
8 provide documents that fall outside of the contours of
9 what's required under the affiliate transaction rule?

10 MR. PENDERGAST: What I will concede,
11 Commissioner, is that in an effort to go above and beyond,
12 what we're required to do to satisfy Staff is this is an
13 above-board transaction, and if you look at it six ways
14 from Sundays, belts and suspenders, that this provides you
15 with all the fair market information anybody could
16 possibly need.

17 And -- and I don't think that having been
18 forthcoming like that, our reward should be to go ahead
19 and say, Well, we want to see everything that you have.

20 COMMISSIONER KENNEY: And I think you're right.
21 You shouldn't be penalized for doing what you're -- what
22 you describe as extra. What I'm asking you or what I
23 guess I'm getting at, though, is that the discovery
24 process for the purposes of an ACA review are not limited
25 by what's set forth in the affiliate transaction rule.

1 MR. PENDERGAST: I think in this particular
2 instance, it absolutely is because the affiliate
3 transaction rule says that parties are entitled to get --
4 I mean, you know, you don't necessarily have any
5 jurisdiction over LER. Okay? I mean, you know whether
6 it's informational or otherwise.

7 The jurisdiction that you do have comes from
8 your lawfully approved affiliate transaction rules. Those
9 affiliate transaction rules not something in a PGA or
10 something a prudence review -- I'm sorry go ahead.

11 COMMISSIONER DAVIS: Okay. Before you get to
12 the talking too fast, now, the Commission did approve --
13 what was it is? There is -- there is -- there is some
14 order that gives us a little more authority to look into
15 the dealings of LER than just the affiliate transaction
16 rule. Would you agree with that statement,
17 Mr. Pendergast? I mean, was it the --

18 COMMISSIONER KENNEY: Stipulation?

19 COMMISSIONER DAVIS: Yeah. The stipulation that
20 settled that case back in --

21 MR. PENDERGAST: Oh, if you're talking about the
22 2000 -- actually, what that stipulation says, if you go
23 through it, is we were reorganizing the company.

24 COMMISSIONER DAVIS: Right.

25 MR. PENDERGAST: It was separate utility,

1 remained a separate utility. And there's very clear
2 language in there that says that this isn't supposed to go
3 ahead and impact the scope of the Commission's authority
4 over LER or any other affiliate above and beyond what's
5 under existing law.

6 What it did say is that we would not object on
7 the grounds of relevancy if, in fact, we were saying
8 something was irrelevant because of the restructuring that
9 took place. But nothing here is a basis that we're using
10 to go ahead and say it's irrelevant because of the
11 restructuring that took place.

12 It's irrelevant because your affiliate
13 transaction rules say that this is the standard, and the
14 Staff's using a different standard to get this
15 information.

16 It also said, as I said earlier, it had had a
17 CAM that was designed to protect ratepayers in the event
18 of affiliate transactions were done. I just read earlier
19 from the Staff's suggestions in support of that where the
20 Staff wrote that Steve Rackers had proposed CAM provisions
21 in order to protect ratepayers, Laclede had agreed to all
22 of those provisions.

23 And, quite frankly, that's what we've lived
24 under and complied with. And what I'm saying is now Staff
25 wants to come up with a totally new standard than what

1 they developed back in that holding company docket.

2 And I think it's entirely inappropriate to do
3 that after the fact. If you want to change the affiliate
4 transaction rules on a going forward basis, you want to
5 change our CAM on a going forward basis, you know, we can
6 all have that discussion. But you shouldn't do it on a
7 retroactive basis. And that's basically what they're
8 trying to do.

9 MS. SHEMWELL: The standard is and always has
10 been are the charges just and reasonable, 393.130. Are --
11 always the standard, and that continues to be the standard
12 in rate cases.

13 MR. PENDERGAST: You can't read away specific
14 rules and specific requirements and specific standards by
15 saying there's some general concept out here saying just
16 and reasonable rates or prudence and -- and that makes all
17 those specifics go away. You just can't do that.

18 COMMISSIONER KENNEY: We need to read these all
19 together in context, I -- to my mind.

20 MR. PENDERGAST: I agree.

21 COMMISSIONER KENNEY: So I guess that gets back
22 to my initial point. Can we read the affiliate
23 transaction rule in isolation and say that that is what
24 governs the scope of discovery in an ACA review?

25 MR. PENDERGAST: I --

1 COMMISSIONER KENNEY: I'm really asking that
2 rhetorically. Let me ask a different question.

3 Didn't the Commission originally grant this
4 Motion to Compel?

5 MR. PENDERGAST: Yeah, they did.

6 COMMISSIONER KENNEY: And what happened?
7 Because I'm just -- I did a little time line for myself,
8 and it looks like in September of '08, we granted it.
9 October of '08, rather. And then there was motion to
10 reconsider.

11 MR. PENDERGAST: Right. And -- and --

12 COMMISSIONER KENNEY: And didn't they come --
13 didn't -- at some point, didn't Staff narrow the amount of
14 documents that it was asking for?

15 MR. PENDERGAST: Staff went ahead and said,
16 Well, just give us two months or four months instead of
17 twelve months. But from the standpoint of wanting to see
18 records of all sales from transactions, what margins you
19 made on them, records of all capacity, you know, it was
20 still a very broad, I want to come in and I want to look
21 at every invoice that your unregulated company has.

22 I want to look at every sale they've made
23 including all the sales, 95 percent of customers that
24 weren't Laclede Gas Company. So did they narrow it from a
25 number-wise? Yeah. Did they narrow it from a scope-wise?

1 Not too much.

2 COMMISSIONER KENNEY: But, I mean, they narrowed
3 the time that they wanted to examine?

4 MR. PENDERGAST: I think they said, We'll take
5 several months in each ACA period. I don't know whether
6 it was two or four. I don't have it in front of me right
7 now.

8 But the way these contracts work, you now, many
9 of them are for an entire year. That doesn't really
10 narrow it substantially. But more importantly, whether
11 it's a lot of information or a little bit of information
12 -- and it's a lot, it's a lot. You know, the thing is,
13 they want it for a standard that I think we've talked
14 about today, that isn't contemplated by your rule.

15 And you can't, in the guise of prudence or you
16 can't in the guise of just and reasonable rates, say,
17 We're going to go ahead and rejigger those standards that
18 we've gone ahead and -- and had in effect while we do
19 these transactions. It's just not appropriate.

20 COMMISSIONER KENNEY: Did I hear Staff
21 acknowledge that that was, in fact, the standard that they
22 were attempting to apply?

23 MS. SHEMWELL: I'm sorry. The affiliate
24 transactions rule is the standard?

25 COMMISSIONER KENNEY: No. The standard that

1 Mr. Pendergast was just describing, that you're looking at
2 whatever the lowest -- and can you restate it? Because I
3 don't think I ever got a clear answer.

4 MR. PENDERGAST: Sure. The purpose from LER is
5 looking for the lowest cost of gas in LER's supply
6 portfolio without any markup for profit or for the risk
7 and efforts undertaken by LER to line up that gas supply
8 and provide it to us. And for a sale, it's not what the
9 market price was at the time you made the sale, but,
10 instead, did LER take that someplace else and use that
11 capacity to make a sell to somebody else? And if they
12 did, we want that money.

13 MR. THOMPSON: No. That's not the standard that
14 Staff is seeking to apply, sir.

15 MR. PENDERGAST: Well, that's what I said their
16 standard was at the last oral argument, and nobody
17 disagreed with me. Maybe finally they are, and maybe
18 finally we'll find out what their standard is because I
19 don't know.

20 MR. THOMPSON: You might -- you might have been
21 talking too fast for anyone to follow.

22 MR. PENDERGAST: Okay. Well, perhaps.

23 COMMISSIONER KENNEY: All right, gentlemen. I
24 don't want to cause a ruckus between you two. Just keep
25 talking --

1 MR. THOMPSON: I apologize.

2 COMMISSIONER KENNEY: Just keep talking to us.
3 All right. So -- and I guess -- I'll ask this question of
4 Staff or -- have you -- are you trying to determine a
5 standard or are you just trying to get the information so
6 that you determine whether these were prudent purchases or
7 not?

8 MR. THOMPSON: We're -- we're trying to
9 determine the prices at which they acquired the gas.

10 COMMISSIONER KENNEY: Okay. For a finite period
11 of time?

12 MR. THOMPSON: For a finite period of time.

13 COMMISSIONER KENNEY: All right.

14 MR. THOMPSON: And we want to compare that to
15 the price -- the contract price at which they sold certain
16 amounts of gas to Laclede.

17 COMMISSIONER KENNEY: Is that, what he just
18 described, in your mind, relevant to the ACA review and
19 the prudence analysis?

20 MR. PENDERGAST: No. It is -- it's not relevant
21 to either, not in this case. The reason it's not relevant
22 is under the CAM and under the affiliate transaction rule,
23 we have to demonstrate that we purchased gas from LER at
24 competitive, fair market price.

25 It doesn't matter what LER's costs are as long

1 as we can show it's consistent with what other vendors
2 were selling it for. That's where the inquiry should end.
3 And if you go further than that and you say, We want to
4 look at their cost and see if there was a more favorable
5 cost in there, you're treating them in a discriminatory
6 fashion inconsistent with your rule. You're treating them
7 under a standard inconsistent with what's in your rule and
8 basically telling us, Don't do any more transactions like
9 that.

10 COMMISSIONER KENNEY: Let's assume for the sake
11 of this argument that that's -- that they want to examine
12 these underlying transactions. That, to your mind, is
13 going to automatically lead to a disallowance of those
14 purchases?

15 MR. PENDERGAST: No. I don't think it will
16 automatically lead to a disallowance. They've proposed a
17 disallowance based on the standards that not authorized by
18 the affiliate transaction rule.

19 And now what they're trying to do is, you know,
20 on the pretext of that unlawful, unauthorized standard get
21 information to try and, I guess, prove it up. And I don't
22 know why they should be allowed to prove up the standard
23 that -- that you have not authorized, that you have --
24 that is directly contrary to what you have authorized. I
25 mean, I think it's about as simple as that.

1 COMMISSIONER KENNEY: So in order for -- I guess
2 what you're saying is that it's irrelevant because it goes
3 beyond what's authorized by the affiliate transaction rule
4 and the cost allocation rule?

5 MR. PENDERGAST: I'm saying it's irrelevant, and
6 three Commissioners said it was irrelevant, and they did
7 that back on May 27th. That should have been the final
8 matter on it. You know, we shouldn't even be here today,
9 to be quite frank.

10 COMMISSIONER KENNEY: But that order denying the
11 Motion to Compel was an initial order granting it, and it
12 didn't set forth any specific rationale.

13 MR. PENDERGAST: I know. And we've --

14 COMMISSIONER KENNEY: So we don't know why they
15 denied it. And that's what I'm trying to get at.

16 MR. PENDERGAST: I mean -- we -- we -- we've
17 referenced that in our pleading. We've said it was
18 unfortunate that it didn't go ahead and provide more
19 information. We submitted Proposed Findings of Fact and
20 Conclusions of Law that the Commission could have utilized
21 for that.

22 They said based on the arguments of counsel, we
23 determined that it's not irrelevant. And those are the
24 arguments I made then, and it's the arguments I'm making
25 today. So I'm assuming that's what the Commission relied

1 on.

2 COMMISSIONER KENNEY: Again, as I said at the
3 beginning, I appreciate you all coming out here because
4 it's primarily for my purposes. So what I'm asking,
5 irrespective of what was argued before and what the
6 initial order, are you saying that it's irrelevant because
7 it goes beyond what's required by the affiliate
8 transaction rule and the cost allocation manual?

9 MR. PENDERGAST: I'm saying it's irrelevant not
10 only because it goes beyond what's required by the CAM and
11 what's required by the affiliate transaction rule, but
12 because it presumes a standard that's directly contrary to
13 the one that appears in those rules and that CAM.

14 It cannot be reconciled with the standards that
15 you say ought to be used to govern these transactions.
16 And I'm saying that you can't overcome that by just
17 saying, Well, it's a prudence review or just and
18 reasonable rates. Your standards are what they are.

19 COMMISSIONER KENNEY: All right. So what we
20 would have to determine, then, is that, in this particular
21 case at least, a prudence review is defined and is limited
22 to what's set forth under the affiliate transaction rule
23 in the CAM?

24 MR. PENDERGAST: As Mr. Zucker said, in this
25 particular instance where the only issue is whether the

1 purchase from the affiliate was done at a proper price,
2 what you would have to determine is our rules and the --
3 and the company's CAM says what that price ought to be,
4 and that's what they have proven up. And that's --

5 COMMISSIONER KENNEY: That's what it says it
6 should be for purposes of compliance with the affiliate
7 transaction rule, right?

8 MR. PENDERGAST: You know, for purposes of the
9 affiliate transaction rule, which is, as Commissioner
10 Jarrett pointed out, designed to go ahead and prevent any
11 appropriate subsidization, which as the CAM pointed out,
12 Mr. Rackers testified to seven or eight years ago is
13 designed to ensure that ratepayers are adequately
14 protected.

15 And I'm sorry. I can't go ahead and agree with
16 the concept that, suddenly, we have a new definition of
17 what it takes to go ahead and protect ratepayers that was
18 un contemplated at that time that we wrap in a general
19 rubric of prudence and that's fundamentally different than
20 what you were living and operating under in good faith all
21 these years.

22 COMMISSIONER KENNEY: I don't think it's
23 fundamentally different. I think that it's just -- it's
24 not the only -- it's not the only governing -- governing
25 document for purposes of a prudence review.

1 And I guess this goes back to my original
2 question. It sounds like that we've conflated the
3 analysis for prudence review with the analysis for the
4 affiliate transaction rule. And that seems to be the
5 fundamental disagreement. I just want to make sure I'm --

6 MR. PENDERGAST: I think it is. And, quite
7 frankly, just to be candid about it, I think it's a
8 purposeful osfutation. I think people are trying to move
9 away from what it says in the affiliate transaction rule,
10 what says in our CAM, what those clear standards are by
11 throwing up the word "prudence" and saying, Well, you
12 know, we've got prudence here and that might be somehow
13 different.

14 And when you ask them to get more specific on
15 what they really mean by that, they come up with the
16 standard lowest cost of gas in the portfolio or whatever
17 the affiliate made when it sold gas to somebody else that
18 you can't tie back to anything.

19 You know, that is the standard that is in the
20 mind of David Summer, the Staff witness who proposed these
21 disallowances. It is not in your rules. It is not in the
22 CAM. And we shouldn't be required to provide a lot of
23 information pursuant to a rule that is blatantly
24 inconsistent with the rules that you have -- you've
25 approved and that we were supposed to live by.

1 They need to live by them, too.

2 COMMISSIONER KENNEY: I think I understand
3 Laclede's position.

4 MR. PENDERGAST: Thank you.

5 THE COURT REPORTER: Excuse me. I need to
6 change paper.

7 JUDGE JONES: okay. Go ahead.

8 (Break in proceedings.)

9 JUDGE JONES: Okay. Commissioner Kenney?

10 COMMISSIONER KENNEY: I want to make sure I've
11 encapsulated your position in easily digestible terms, and
12 this is just for my own education.

13 Mr. PENDERGAST: Sure. Appreciate that.

14 COMMISSIONER KENNEY: It's inconsistent -- or
15 it's irrelevant -- the information Staff seeks in
16 Laclede's information is irrelevant because it's
17 inconsistent with the CAM and the affiliate transaction
18 rules?

19 MR. PENDERGAST: Because it --

20 COMMISSIONER KENNEY: Is there an independent
21 basis that Laclede could argue for its irrelevancy,
22 separate and apart from the CAM on the affiliate
23 transaction rule?

24 MR. PENDERGAST: Yeah. I guess I would just
25 argue if there was no CAM and there was no affiliate

1 transaction rule and we could go ahead and demonstrate, as
2 I think we have, and we could prove that we made these
3 purchases from LER, here is the information we provided to
4 show you that it was made on a fair market value basis
5 based on what other marketers were willing to go ahead and
6 sell gas to you -- to us, that it was fully competitive
7 and reasonably priced from that standpoint.

8 I would think under those circumstances, whether
9 there was a CAM or not, looking at what LER may have gone
10 ahead and paid for that gas supply would be irrelevant.

11 COMMISSIONER KENNEY: So Laclede's position,
12 then, would be to -- the definition or the way to
13 determine fair market value would be the price that
14 Laclede paid from other non-affiliates, not what its
15 affiliate paid for the gas in the first instance?

16 MR. PENDERGAST: Absolutely. I think that's the
17 fair market test that is in our CAM. I think it's the
18 fair market test that is supported by the affiliate
19 transaction rule.

20 And, you know, quite frankly -- you know, I'm
21 not the first one to -- to say this. This isn't the first
22 time Staff has tried to come up with different standard.
23 Back -- as far back as the late '90s, they wanted to have
24 Utilicorp that was releasing capacity to their affiliates
25 have those capacity releases basically counted for at the

1 full maximum rate.

2 And at that time, the Commission said, No, this
3 is a fair market price. That's what the market was going
4 to pay for that capacity at that time. And if we charged
5 them the full fair market -- or not fair market -- the
6 full capacity release rate, they probably wouldn't have
7 purchased it and ratepayers would be worse off.

8 By the same token, if we had to live under an
9 environment where LER could only do business with us if it
10 was willing to give us the lowest cost in its portfolio or
11 go ahead and remit to us any profits it makes on anything
12 we sell them at fair market price, they would not go ahead
13 and ever do business with us.

14 And our customers would be the losers in that
15 circumstance because that's one more market for off-system
16 sales, which, as I showed you before, have increased
17 tremendously during the period when we were supposedly
18 migrating them over to LER. They just wouldn't be there
19 as a potential customer. And I don't think that would be
20 good for anybody. And it certainly wouldn't be consistent
21 with your rules.

22 COMMISSIONER KENNEY: Okay.

23 JUDGE JONES: Commissioner Jarrett?

24 COMMISSIONER JARRETT: Go ahead.

25 COMMISSIONER DAVIS: Okay. So, Ms. Shemwell, I

1 mean, you're basically telling me that Staff cannot
2 calculate the difference between sales and the
3 Mid-Continent and sales in the Nimex market?

4 MS. SHEMWELL: We can.

5 COMMISSIONER DAVIS: Okay. So --

6 MS. SHEMWELL: We just don't know what they were
7 at the time.

8 COMMISSIONER DAVIS: Well, if you -- if you can,
9 then -- then why can't -- why can't you calculate that?
10 Because it -- it seems to me that I have seen graphs in
11 the past that talk about the spread between Mid-Continent
12 Gas and Nimex or Henry Hub.

13 And, obviously, it's a lot -- in the past, it
14 has been a lot more than -- than 10 cents per million BTU.
15 So I'm still not sure what -- what the --

16 MR. THOMPSON: The piece that's missing, sir, is
17 where was LER actually acquiring the gas? We know what
18 the index prices were at the various locations. We know
19 what the gas was selling for. But what gas did they buy?

20 MS. SHEMWELL: There's no Mid-Continent index at
21 -- okay. They've set their price in the contract based
22 generally on Nimex minus 10 cents.

23 COMMISSIONER DAVIS: Right.

24 MS. SHEMWELL: So that's what they're paying
25 LER. Our question is, did LER buy gas much more cheaply

1 somewhere else? And Laclede could have bought that same
2 gas much more cheaply from a different marketer or from
3 someone else.

4 MR. PENDERGAST: If I could just respond to
5 that. Why don't we ask BP/Amoco when it makes a sale to
6 us whether or not they bought gas significantly more
7 cheaply from someplace else than what they sold to us at
8 market price at a particular time and location and tell
9 BP/Amoco that if they did buy that gas or buy some gas at
10 a cheaper location, we want them to go ahead and adjust
11 the contract price?

12 COMMISSIONER DAVIS: Okay, Rowdy. I'll get to
13 you in a minute here.

14 COMMISSIONER KENNEY: I mean, the reason we
15 don't do that, though, is we subject affiliate
16 transactions to a heightened scrutiny as a general
17 practice. And I don't mean affiliate transactions as
18 defined in the general regulations. I'm using it with a
19 little a and little d.

20 When we -- by definition, we wouldn't give that
21 transaction because between BP and Laclede the same
22 position we would give the transaction --

23 MR. PENDERGAST: I agree with you completely,
24 Commissioner, and that's why we have affiliate transaction
25 rules. That's why we have asymmetrical pricing standards

1 that are designed to go ahead and make sure that those
2 prices are reasonable.

3 And that's what we've lived with. And you also
4 have non-discrimination rules. And if you can't make a
5 BP/Amoco do that, you shouldn't make an affiliate do that
6 because you're treating them in a highly discriminatory
7 fashion if you do. I'm sorry, Commissioner.

8 COMMISSIONER DAVIS: All right.

9 COMMISSIONER KENNEY: Sorry about that.

10 COMMISSIONER DAVIS: It's -- it's all right.
11 I interrupted you earlier. All right. Let me switch
12 gears and go back to Mr. Pendergast here. Let's talk
13 about the release of pipeline capacity for a second.

14 Now, obviously, if Laclede releases capacity to
15 LER and then LER turns around and sells that capacity at a
16 -- at a -- at a marked up price, I mean, that's -- that's
17 a problem, isn't it?

18 MR. PENDERGAST: Oh, I think, you know, LER or
19 any other vendor out there is going to go ahead and take
20 whatever -- I mean, they're buying it from us for a
21 reason, whether it's capacity or gas supply. And that's
22 so that they can serve other customers.

23 COMMISSIONER DAVIS: Okay. But we're -- I mean,
24 you know, we're not talking about you selling gas to
25 Mr. Poston over here. I mean, we're talking about, you

1 know, Ken Nices and Ken Nices.

2 So it's like, you know, if I'm -- hypothetically
3 speaking, if -- if, you know, it's Ken Nices says, Well,
4 you know, here I am at Laclede. I'm going to release this
5 pipeline capacity to LER, and then LER is going to turn
6 around, I mean -- I mean, I'm not -- I mean, I'm not sure
7 that that passes the reasonable person's standard,
8 Mr. Pendergast. So tell me -- tell me why you think I'm
9 wrong on that.

10 MR. PENDERGAST: No. I'm not saying that that's
11 not a reason to go ahead and have a legitimate concern.
12 No. 1, I think that's why you have rules that say when you
13 release that capacity or you sell it, it has to be at a
14 fair market price.

15 No. 2, I think you can look at what we have
16 provided to you. And we provided you with performance
17 bonus information that shows that the gas supply people
18 who make these determinations right up to Mr. Nices, that
19 when they get evaluated as to whether they're going to be
20 compensated and whether they're going to go ahead and have
21 a bonus, it's whether they have maximized off-system sales
22 for the regulated gas company.

23 Staff asked for that information. We provided
24 it to you. George Godat or whoever makes those sales
25 doesn't get rewarded if LER makes more money. He gets

1 rewarded if Laclede Gas Company makes more money in its
2 off system sales.

3 And, secondly, I think we ought to have -- if
4 we're going to have an evidentiary hearing have Mr. Godat
5 come in here and tell you how he makes sure he maximizes
6 his off-system sales revenue, how he makes sure that he's
7 not giving capacity away when he could go ahead and bundle
8 it with gas supply and get more money to not only benefit
9 the company but benefit himself.

10 And I -- and we have those protections in place.
11 And I've shown you the macro information on how our off
12 system sales have grown throughout this period when we
13 were supposedly migrating them over to LER.

14 COMMISSIONER DAVIS: Right.

15 MR. PENDERGAST: And at the very least, doesn't
16 that justify having a hearing?

17 COMMISSIONER DAVIS: Okay. So is it your
18 opinion that what this is all about is Staff looks at LER
19 and they say, Oh, my, here is this LER, and they are
20 making obscene amounts of money, and we think that, since
21 this is all, in essence, underwritten by the -- the
22 regulated utility that the ratepayers ought to be entitled
23 to a bigger slice of that action? Is that -- is that --
24 is that what -- is that your impression of their -- of
25 what they're ultimately thinking? Or is it something

1 else?

2 MR. PENDERGAST: Well, that does sound like a
3 Staff thought process to me. And, you know, I -- I would
4 imagine that if LER was losing money or LER was hardly
5 making any money, I don't know if we would even be here.

6 I'm absolutely confident that if we had done
7 this same transaction that we did with with LER with
8 anybody else at the same price we wouldn't be here today.
9 I think it's because LER has had revenues grow and it has
10 been successful that Staff has tried to go ahead and make
11 the case that it's due to Laclede allowing them to use
12 Laclede's assets or selling things to them at a price that
13 wasn't appropriate.

14 And all I can say to that is if you look at how
15 much business LER has actually done with Laclede, whether
16 it's on sales or purchases, it's a very small component of
17 their overall business.

18 COMMISSIONER DAVIS: Okay. But let -- let me
19 ask another question. Let me ask it this way: Should the
20 prudence of a contract between Laclede and LER be judged
21 at the time the contract is signed, or should it be, you
22 know, three years down the road?

23 MR. PENDERGAST: I think under the prudence
24 standard, it ought to be evaluated based on what was known
25 and what the circumstances were at the time it was entered

1 into.

2 And I don't think that's really what the Staff's
3 disallowance in this case does. I think it's a
4 retrospective review. I think they want to go ahead and
5 look back in time and see if they can find, you know,
6 other instances where LER may have --

7 COMMISSIONER DAVIS: You know, I mean, as I
8 understand it, one of the purposes of LER is to assume
9 risk.

10 MR. PENDERGAST: Sure.

11 COMMISSIONER DAVIS: Okay. But, really, when --
12 when you sign a gas contract to purchase gas for Nimex
13 minus 10 cents -- I mean, to me, that doesn't seem like
14 LER is assuming a whole lot of risk.

15 I mean, you know, basically, I mean, you're just
16 saying, Hey, they can beat the -- the -- the average
17 monthly price by -- by 10 cents a million CCF or whatever;
18 is that correct?

19 MR. PENDERGAST: Yeah. Actually, the
20 transactions under consideration in these two ACA
21 proceedings, they took place and they were at a Nimex
22 minus something or other, nine or ten. And that was the
23 year where we had Katrina.

24 We had prices blow out. And if you talk to LER,
25 they'll tell you that they lost money on it. And we --

1 they wanted to renegotiate the contract. And we
2 ultimately had real problems doing that.

3 And we finally made an arrangement that was less
4 favorable to them than what other suppliers were getting
5 at the same time. You know, it was based on the BP/Amoco
6 purchases that we were making at the time.

7 We gave them the same pricing deal that BP/Amoco
8 was giving us. And, you know, from our perspective,
9 that's pretty good evidence that it was a fair market
10 price down in Westline off of MRT.

11 MR. ZUCKER: Commissioner, let me supplement
12 that answer. You asked when -- at a price of Nimex minus
13 ten it doesn't sound like LER is taking a lot of risk.

14 The answer is, the price that -- the price by
15 itself doesn't tell us anything. What tells us whether
16 the -- the utility ratepayer is being protected is whether
17 that price meets other comparable prices. Right?

18 That's what the rule is. This is pretty simple.
19 You want to make sure the ratepayer isn't paying more than
20 a market price. So you look at comparables, right?
21 Just like they do in the real estate market when you buy
22 -- when you buy a house.

23 And so the question isn't what -- what Nimex
24 minus ten is. The question is what are -- what are the
25 comparables? And that's the question that Staff should be

1 asking, not what did LER pay for gas out in the field at
2 the well head that they later brought to some other
3 location and sold to Laclede.

4 What LER paid for their gas is irrelevant to
5 whether our not Laclede paid a price higher than the
6 comparables would dictate.

7 COMMISSIONER KENNEY: And in order to determine
8 what's comparable, you're comparing LER -- LER's sales to
9 Laclede as compared to BP's sales to Laclede?

10 MR. ZUCKER: Right.

11 COMMISSIONER KENNEY: In order for it to be a
12 full -- a full and accurate --

13 MR. ZUCKER: Comparison.

14 COMMISSIONER KENNEY: -- comparison, don't we
15 need to know the underlying -- I mean, how do we know that
16 the BP sales and the LER sales are, in fact, comparable?

17 MR. PENDERGAST: Well, I think -- I think you
18 have to go ahead and -- and assume that the operating
19 assumptions behind the fair market test is that the fair
20 market is going to go ahead and provide a competitive
21 reasonable price.

22 Because if other people are willing to sell it
23 or willing to buy it at the same price you're selling it
24 or buying it from the affiliate, then that's good evidence
25 that it's a reasonable price.

1 And, you know, I don't know where you go if you
2 start looking behind that and you start saying, Well, I
3 know what people in the marketplace were charging and
4 demanding for it. But what was their cost structure like?
5 And where were they getting their gas from and how much?
6 And what's the difference between that and what they were
7 selling it for? I think you're just in a complete morass
8 at that point.

9 COMMISSIONER KENNEY: Why isn't that enough?
10 And this is to Mr. Thompson and Ms. Shemwell.

11 MR. THOMPSON: It's not enough because LER is an
12 affiliate.

13 MS. SHEMWELL: The BP contract is not --

14 COMMISSIONER KENNEY: Let me ask the question
15 this way. If the goal is to determine whether Laclede is
16 purchasing gas at a reasonable price from its affiliate,
17 why isn't it sufficient to look to what Laclede was paying
18 to other non-affiliates? And if they are comparable, why
19 isn't that sufficient?

20 MR. THOMPSON: First of all, the goal is to
21 determine whether the price Laclede is paying for gas from
22 everybody is appropriate. It's a prudence review. So
23 we're not just looking at its transactions with LER.
24 We're looking at all of its transactions.

25 But when we come to the transactions with LER,

1 we have additional questions that we ask: Are they buying
2 gas from LER where perhaps they should have done something
3 else? And one way to look at that is to see if they are
4 paying an inordinate margin to LER.

5 COMMISSIONER KENNEY: So that's more than a fair
6 market test. I mean, that's greater than a fair market
7 test.

8 MR. THOMPSON: No. That's a prudence test.
9 That's the prudence test.

10 COMMISSIONER KENNEY: Okay.

11 MR. THOMPSON: In other words, were the actions
12 taken by Laclede prudent?

13 COMMISSIONER KENNEY: So irrespective of whether
14 they pass a fair market test, it may still not be a
15 prudent purchase?

16 MR. THOMPSON: That's exactly right, as
17 Mr. Pendergast himself said.

18 COMMISSIONER KENNEY: And you don't agree with
19 that?

20 MR. PENDERGAST: I don't for the life of me
21 understand under those circumstances where it's
22 competitive with what other people were willing to sell it
23 to, why that doesn't end the discussion.

24 I mean, if you were looking at BP/Amoco and
25 determining whether our arrangement with them was

1 reasonable, you'd look at what other people were selling
2 gas for down in that particular location at that
3 particular time, and you would say, okay, it's in line
4 with those prices. Well, the same thing ought to be true
5 of your affiliate.

6 COMMISSIONER DAVIS: Okay. But --

7 MR. THOMPSON: Let's go back, if I could, just
8 for a moment, sir.

9 COMMISSIONER DAVIS: Okay. Can you go back and
10 restate your argument one more time before you restate
11 whatever you want to state?

12 MR. THOMPSON: Our concern is whether the
13 actions that Laclede took were prudent. Were they the
14 best actions Laclede could have taken at the time given
15 what they knew or should have known at the time?

16 COMMISSIONER DAVIS: Wait. You said best.

17 MR. THOMPSON: Right.

18 COMMISSIONER DAVIS: Is best really the
19 standard, or is it reasonable under the circumstances by a
20 person who knows all of the relevant facts and would be in
21 a similar position?

22 MR. THOMPSON: I think that best and reasonable
23 are -- are essentially the same in this circumstance.

24 COMMISSIONER DAVIS: No. Because if you say, I
25 bought gas at a reasonable price versus buying gas at the

1 best price, I think those are two entirely different
2 standards. Don't you, Mr. Thompson?

3 MR. THOMPSON: Well, it would have to do with
4 the duty owed by Laclede to its ratepayers.

5 COMMISSIONER DAVIS: Okay.

6 MR. THOMPSON: Now, if we're -- if we're looking
7 at whether the price was just and reasonable --

8 COMMISSIONER DAVIS: Isn't that -- I mean, isn't
9 that --

10 MR. THOMPSON: How is best and reasonable -- how
11 are they different? The ratepayers expect to be getting
12 gas at the best price.

13 COMMISSIONER DAVIS: I understand. But we're
14 not measuring ratepayer expectations here. I mean, the
15 problem is under your standard, Mr. Thompson. As I -- as
16 I -- as I understand the standard that you have just
17 articulate, you are encouraging these people to speculate
18 and take risks.

19 MR. THOMPSON: Well, let's back away from best,
20 then. Let's say reasonable.

21 COMMISSIONER DAVIS: Okay. Let's say
22 reasonable. I mean, because -- I mean, I'm concerned --
23 you know, right now, at -- you know, \$3 gas is not that
24 reasonable.

25 But the question is, let's say the economy picks

1 back up and the price of natural gas is \$7 next year.
2 Okay? Does Mr. Pendergast buy that \$7 gas, or does he
3 wait because he thinks the price might go down and then
4 it's -- are you going to come back up -- when the price
5 goes to ten, are you going to come in and say, Well, you
6 should have locked in at seven?

7 MR. THOMPSON: Well --

8 COMMISSIONER DAVIS: You know --

9 MR. THOMPSON: You know, the standard is what
10 they knew or should have known at the time they made the
11 decision.

12 COMMISSIONER DAVIS: And you say it was their --

13 MR. THOMPSON: Our concern, sir, is --

14 COMMISSIONER DAVIS: So would the standard be
15 reasonable under the circumstances using their best
16 judgment? Is that how you'd apply best?

17 I mean, I'm just trying to get this figured out
18 here. I mean, I just want to make sure you're not sending
19 Mr. Pendergast down to Harrah's with a wad of money to put
20 on black or red.

21 MR. THOMPSON: I would never send Mr. Pendergast
22 down to Harrah's. What I'm concerned with is Ken Nices at
23 LER selling gas to Ken Nices at Laclede Gas Company.

24 And I think that we owe it to the people of
25 Missouri to look closely at those transactions to make

1 sure that Ken Nices, in his two hats, is not gaming the
2 system to take their money in an unfair way.

3 You know, it could be that Laclede is the best
4 operated gas company in this country. That could be. I
5 don't know. We want to look at these documents to get one
6 more piece of information to help Staff determine whether
7 or not these actions were prudent at the time they were
8 taken.

9 MR. PENDERGAST: You know, and I don't really
10 disagree with -- with the fact that you have to give these
11 heightened scrutiny. You know, that's why we have an
12 affiliate transaction rule. That's why we have a CAM.
13 That's why we have special pricing provisions, to address
14 the very concerns that Staff has raised. That's why we
15 have the rule.

16 And having gotten the rules and having applied
17 the rules, you don't go ahead and make up new rules
18 because you're maybe dissatisfied with how they protect
19 the ratepayers.

20 If you want to change the rules as you go
21 forward, you change the rules, and as far as what a
22 reasonable man standard is, you know what we knew at the
23 time we did these transactions? We knew what your rules
24 were. We knew what the standards in those rules were. We
25 knew what the CAM was. We knew what the -- what the

1 standards in those CAMs were. We knew how those
2 transactions ought to be priced, what we ought to look at,
3 what we ought to do to support them.

4 What we didn't know was this new standard that
5 came along after the fact that's completely different from
6 what was in those rules. And, you know, whether you want
7 to talk about due process or reasonable expectations or
8 living by the rules and not having them changed in the
9 middle, you know, you don't go ahead and do that. You
10 just don't do it. And that's what Staff's trying to do
11 here.

12 COMMISSIONER KENNEY: I mean, but Staff's not
13 the final arbiter. I mean, we're going to determine it at
14 the end of day. I mean, really, what we're determining
15 here is whether Staff is going to have access to certain
16 information so that it can then make a recommendation to
17 us.

18 I mean, at the end of the day, we're going to
19 determine what standard applies and what to disallow and
20 what to allow.

21 MR. PENDERGAST: And -- and I agree. And all
22 I'm saying, Commissioner, is I think that Staff at this
23 point has conceded a standard that it's trying to pursue
24 that is inconsistent with your rules and the standards in
25 your rules, and those standards say your access to

1 affiliate information is only as far as needed to go ahead
2 and ensure compliance with these particular rules.

3 And -- and they're saying, No, I want to go
4 further because I've got a different standard than what is
5 in the rules. And I don't think they should be allowed to
6 go ahead and go on a fishing expedition based on a
7 patently unlawful, unauthorized standard.

8 JUDGE JONES: Commissioner Jarrett had some --

9 COMMISSIONER JARRETT: Yes. I just -- sort of.
10 I guess, to sort of bring this full circle and put it in
11 the context of discovery, what is the standard this
12 Commission uses for discovery?

13 MR. PENDERGAST: I think the standard they use
14 is the one that's in Civil procedure reasonably calculated
15 to lead to relevant information and under --

16 COMMISSIONER JARRETT: Lead to admissible
17 evidence, whatever.

18 MR. PENDERGAST: Yeah.

19 COMMISSIONER JARRETT: And I -- so Laclede's
20 position is that Staff's request is not reasonable
21 calculated to lead to admissible evidence because?

22 MR. PENDERGAST: Because it is pursuant to a
23 standard and presumes a standard, pricing standard, that
24 is directly contrary to the pricing standards that you had
25 in your rules, that we have in our CAM.

1 I mean, we're not coming upon this sui generis
2 as an entirely new issue where there's nothing out there
3 to determine what might be reasonable or what might be
4 unreasonable or relevant or irrelevant.

5 You have rules that -- that specify what those
6 things are. And I don't think you can change those rules
7 in mid-stream, whether it's for discovery purpose,
8 disallowance purposes or anything else and say, We're
9 going to let these guys go out and get a bunch of
10 information.

11 If they wanted to come in and say, You shouldn't
12 do transactions with affiliates if they have red-haired
13 employees, you know, I want to go ahead and do some -- I
14 want to do some investigation to see if you've got any
15 red-headed employees over at Laclede.

16 We'd all say that that's irrelevant. You can't
17 do that. Well, you can't go in and say, I want to get
18 this information to prove up a standard that's also
19 inconsistent.

20 COMMISSIONER JARRETT: I was red-headed, too,
21 once. And, Mr. Thompson, Ms. Shemwell, I want to give you
22 the chance. Your position is that your requests are
23 reasonably calculated to lead to admissible evidence
24 because?

25 MR. THOMPSON: Because they go to whether or not

1 these affiliated companies are -- are abusing their
2 relationship and gaming the system to make an inordinate
3 profit.

4 COMMISSIONER JARRETT: All right. That's all I
5 have. Thank you.

6 JUDGE JONES: Any other questions?

7 COMMISSIONER KENNEY: I do not.

8 MR. PENDERGAST: I meant no offense to anybody
9 that happens to have red hair. I just want to go on the
10 record and say that.

11 COMMISSIONER JARRETT: You might want to issue a
12 formal apology.

13 MR. PENDERGAST: I will. I will.

14 COMMISSIONER DAVIS: Let me just say that -- I
15 mean, I don't know how long we've been studying this
16 issue, but we've been studying it for quite -- quite some
17 time now.

18 And I'm not sure what the answers are. But I
19 think there are some changes that need to be made, at
20 least on a going-forward basis. But, you know, I am --
21 and that goes with Laclede.

22 I mean, the -- I mean, I don't know how you
23 respond to this, Mr. Pendergast, but the whole -- I mean,
24 the whole idea that, you know, Ken Nices is selling gas to
25 Ken Nices is very troubling.

1 You know, on the other hand, I'm concerned that
2 Mr. Thompson's, you know, standard is, you know, somewhat
3 -- you know, we want to -- I mean, this -- and,
4 Mr. Thompson, I want to hear what you have to say about
5 this.

6 But, I mean, certainly, it seems like if you
7 want to ensure that Laclede got the, quote, best price on
8 the gas at the time, I mean, to my -- that just seems --

9 MR. THOMPSON: I may have misspoken when I said
10 best.

11 COMMISSIONER DAVIS: Okay.

12 MR. THOMPSON: Reasonable. Fair. We
13 understand, as Mr. Pendergast said, LER wouldn't sell the
14 gas to Laclede if there wasn't some markup. I understand
15 that. I think Staff understands that.

16 The question is, how much markup? And -- and
17 our concern is not with the actions of LER, but with the
18 actions of Laclede. In other words, did they -- did they
19 buy gas from LER where they should have gone out and
20 sought gas elsewhere because a reasonable price would be
21 lower, significantly lower? That's all. And to know
22 that, we have to know what LER was obtaining the gas for.

23 COMMISSIONER DAVIS: I --

24 Mr. ZUCKER: Commissioner Davis, that is not the
25 complaint that they have filed.

1 COMMISSIONER DAVIS: Mr. Thompson, I am still --
2 I -- you're telling me that this is the only way -- I
3 mean, you're telling me that you can't get market data
4 from any other source, that you can't find -- you can't
5 determine whether these transactions -- that you can't
6 find the other transactions or other pricing information
7 anywhere else?

8 I mean -- you know, I mean, that -- when you say
9 market, I mean, that implies that there are other people
10 out there buying and selling. And it's like -- it's like
11 -- I mean -- I mean, my impression is you're trying to
12 apply a company specific standard here.

13 MR. THOMPSON: We -- we just want to know what
14 LER was obtaining gas for. What -- what were they paying
15 for gas?

16 COMMISSIONER DAVIS: Okay. And, once again, how
17 is that relevant? Not to beat the horse to death here.

18 MR. THOMPSON: It's relevant because the
19 contract that Ken Nices made with Ken Nices called for gas
20 delivered in St. Louis, which means he could use gas that
21 he got anywhere.

22 COMMISSIONER DAVIS: Right.

23 MR. THOMPSON: And the gas delivered in St.
24 Louis was to be priced at Nimex.

25 COMMISSIONER DAVIS: Minus 10 cents.

1 MR. THOMPSON: Minus 10 cents. Okay. Which is
2 a high price. So if he can obtain gas somewhere else more
3 cheaply -- do you understand?

4 COMMISSIONER DAVIS: I understand. But -- let
5 -- okay. Let me ask you -- let me ask you this,
6 Mr. Thompson.

7 MR. THOMPSON: Sure.

8 COMMISSIONER DAVIS: We have Laclede. We have
9 Missouri Gas Energy.

10 MR. THOMPSON: Right.

11 COMMISSIONER DAVIS: We have -- what is it?
12 Southern Missouri Gas? I mean, don't some of these other
13 gas utilities have similar contracts? I mean -- I mean,
14 it's -- it's my recollection that Southern Missouri or
15 somebody had one that was also, you know, minus ten or
16 maybe it was Industrial Consumers that had one that was
17 Nimex minus ten.

18 You know, we have lots of cases flying through
19 here, so I -- I don't have the data off the top of my
20 head. Maybe someone that's working for me will be
21 listening up there and will start plowing through things.
22 But I don't think they're going to be able to find it
23 before we leave here today.

24 But, I mean, that -- to your knowledge, Ms.
25 Shemwell, are there other contracts out there like this

1 one that were signed at the same time by other Missouri
2 utilities?

3 MS. SHEMWELL: If there are, we looked at
4 prudence, whether or not it was prudent to enter into that
5 contract. And let me say ATMOS has a gas marketing
6 affiliate. When it's an arm's length transaction, then
7 there's a presumption of prudence. When it's an affiliate
8 transaction, there can be no presumption of prudence
9 because what ATMOS -- the ATMOS case and what the Supreme
10 Court said in the ATMOS case.

11 COMMISSIONER DAVIS: Okay. So, hypothetically
12 speaking, Southern Missouri Gas doesn't have a marketing
13 affiliate?

14 MS. SHEMWELL: That's right.

15 COMMISSIONER DAVIS: And if they have a Nimex
16 minus ten contract that was signed within a month of
17 Mr. Nices signing a contract with Mr. Nices, you're saying
18 that that's wholly irrelevant?

19 MS. SHEMWELL: I'm saying that we will look at
20 the prudence of that. We will look at the prudence of all
21 of the contract.

22 COMMISSIONER DAVIS: Okay. But if Southern
23 Missouri's contract was prudent, then wouldn't that be
24 evidence that Laclede's is prudence?

25 MS. SHEMWELL: No, sir.

1 COMMISSIONER DAVIS: And why not again?

2 MS. SHEMWELL: Because Laclede is a very
3 different company from Southern Missouri Natural Gas.
4 They have different options. They buy from different
5 parts of the country. They have different suppliers.
6 They have storage.

7 Each gas company is quite different in how it is
8 supplied. Ameren buys from different suppliers than
9 Laclede. I mean, they're very different. They have
10 different considerations. They have different credit
11 ratings. So the credit rating may affect whether or not
12 Southern Missouri Natural Gas can get as good a price as
13 Laclede or not. There are many things that might affect
14 the prudence of a contract.

15 MR. PENDERGAST: You know, if I could just --
16 you're asking are there other indicia of these being
17 reasonable contracts out there. And, once again, I think
18 there is.

19 Once again, these purchases were made down on
20 the MRT Westline. Staff didn't say we shouldn't have been
21 buying gas down there. We bought it in conformance with
22 our historical purchases on the MRT Westline.

23 We priced the purchases from LER at the same
24 prices we were paying to BP/Amoco. We thought that
25 satisfied the fair market price. Staff said, Well, you

1 know, they had the ability to go ahead and maybe serve
2 that St. Louis market from some area that might have also
3 been cheaper. So we said, Okay, let us give you market
4 data for the St. Louis purchases during that very time.

5 It was a very robust set of data. It's what
6 hundreds of schools were buying gas under RFPs from more
7 than one marketer, from a competitive supply. And it just
8 turns out that what LER was selling gas to us for was at
9 or below the prices that had been competitively determined
10 in this RFP process by school purchases.

11 And, once again, how does that not establish the
12 reasonableness of this arrangement?

13 COMMISSIONER KENNEY: I think the more we talk,
14 the more questions I -- but what you just described
15 establishes perhaps that there was -- that establishes a
16 baseline for a fair market determination in that St.
17 Louis market.

18 MR. PENDERGAST: Right.

19 COMMISSIONER KENNEY: But that's -- in Staff's
20 estimation, that's a separate analysis from whether the
21 purchases in and of themselves were prudent purchases.

22 MR. PENDERGAST: And what Staff --

23 COMMISSIONER KENNEY: And I think that those are
24 two distinct analyses, right?

25 MR. PENDERGAST: Well, I don't think that

1 they're two distinct analyses in this particular instance
2 because the only way we could go ahead and purchase gas
3 was to go ahead and purchase it from a marketer or
4 producer out in the field.

5 Like I said, we don't have our own natural gas
6 well. We don't own our own pipelines. we have to buy our
7 capacity and we have to buy our gas supplies from third
8 parties.

9 And so when you determine whether or not that
10 purchase you make from a third party was -- whether it be
11 an affiliate or not a affiliate is reasonable, you look at
12 what the market prices were that were being offered at
13 that time. And you don't go behind the veil and you don't
14 go ahead and start saying whether it's an affiliate or
15 non-affiliate, I need to know what, you know, cost went
16 into that or whether you might have been able to get
17 cheaper gas from someplace.

18 As long as we can go ahead and demonstrate, had
19 we bought it from another affiliated supplier would the
20 unaffiliated supplier -- would be the price be the same
21 because we were making those purchases, that ought to be
22 the end of the inquiry.

23 I mean, that's what your rule really provides
24 for. That's what the CAM provides for. It's a fair
25 market test. If you want to argue should we have been

1 buying less gas, if you want to go ahead and argue should
2 we have been buying gas some place else, you can do that.

3 But they didn't make those arguments. They were
4 just saying was this appropriately priced? I think you
5 paid too much. And I don't see how you can say that when
6 it's a fair market price as established by all sorts of
7 alternative prices that were being paid by unaffiliated
8 people.

9 COMMISSIONER KENNEY: What they're -- what Staff
10 is saying is that -- and correct me if I'm wrong -- it's
11 not whether the gas was appropriately priced, whether LER
12 priced it based upon what everybody else in the St. Louis
13 market was pricing it. Staff's inquiry isn't whether LER
14 appropriately priced the gas, but whether Laclede's
15 purchase from LER for that specific gas was a prudent
16 purchase.

17 MR. PENDERGAST: And -- and -- and --

18 COMMISSIONER KENNEY: It's a subtle nuance, but
19 it's different.

20 MR. PENDERGAST: But if it's appropriately
21 priced, then what basis would you have for saying it
22 wasn't a prudent purchase? If you're going to say we
23 didn't need to buy any gas at all, that might be one
24 thing. But they're not saying that.

25 If you're saying we should have gone ahead and bought

1 the gas from somebody else, that might be another thing or
2 from some other location, but they're not saying that. I
3 mean, what they're saying is you bought it from LER, and
4 because you bought it from LER, we're not going to accept
5 the fair market price that we would accept if you bought
6 it from anybody else.

7 And, you know, it's treating LER differently in
8 a discriminatory fashion, and it's inconsistent with your
9 affiliate transaction rule. And you can't wipe that away
10 by just saying, Well, we're really talking about prudence
11 here.

12 You know, if it was bought at a fair market
13 price and they're not saying we shouldn't have bought that
14 much gas and they're not saying we should have gone ahead
15 and bought it someplace else, that's the end of the
16 equation.

17 You can talk prudence all day long, but it
18 doesn't change the fact that there's really nothing else
19 to go ahead and look into.

20 JUDGE JONES: Mr. Poston?

21 MR. POSTON: Excuse me. I would just like to go
22 back and talk about the discovery standard is that admiss
23 -- or is it likely to lead to the discovery of admissible
24 evidence.

25 And I think to apply that standard, you need to

1 look at the overall standard. The Commission needs to
2 look at just and reasonable rates under 393.130.

3 And so -- so I think what you need to do is
4 consider is this evidence likely to lead to discovery of
5 admissible evidence to show the lawfulness portion of
6 this. Did it follow the affiliate transaction rule?

7 But you also need to look at is it admissible to
8 show the reasonableness? Is it reasonable for Laclede,
9 for Ken Nices to make transactions in a way that boosts
10 the profits of LER on the back of Laclede's ratepayers?

11 And I think that's where -- where I believe that
12 this evidence is truly admissible is that it's
13 unreasonable to do those kinds of transactions which --
14 which Commissioner Davis seemed to acknowledge when he
15 made the statement that there needs to be some changes
16 done if this is how transactions are being conducted.

17 MR. PENDERGAST: You know, and if changes want
18 to be offered and suggested, like I said, we're willing to
19 sit down and talk with them. But what I can tell you is
20 your rules explicitly permit corporate overheads to be
21 shared.

22 They clearly contemplate that at the end of the
23 day, somebody has to be at the end of the pyramid. We do
24 have steps in place to make sure that we do specific
25 transactions, that the gas supply personnel are separated

1 from LER personnel and that they both work in accordance
2 with their own interests.

3 The performance evaluation information we give
4 is probably the most robust indication of that. And --
5 and so, consequently, I think the measures are already
6 there in the rule to address those particular situations.

7 And if you want to rewrite the rule and you want
8 to have a different rule, then I think that's a discussion
9 we should have. We just shouldn't do it retroactively.

10 COMMISSIONER DAVIS: All right. Mr. Pendergast,
11 let me ask you this question: How much of a hardship
12 would it be to Laclede if we said Laclede cannot purchase
13 gas from LER anymore?

14 MR. PENDERGAST: You know, having just shown you
15 all this information about how small our purchases are
16 already, I -- how could I sit there and say it would be a
17 major burden? I can't say that it would be.

18 You know, I think it would be unfortunate from
19 the standpoint that they are a potential supplier and you
20 like to keep your portfolio suppliers as broad as you can.
21 But would we survive? Would we be okay? Sure.

22 COMMISSIONER DAVIS: Okay. Now, let me ask --
23 let me ask this question: I mean -- and you're going to
24 have to forgive me because I do not have intimate
25 knowledge of how natural gas purchasing transactions

1 contracts work.

2 But would it be possible to say, I mean, you
3 have to put this out for a -- a public bid to do like an
4 RFP where everyone -- you know, where there's a
5 transparent process where, you know -- and I don't know --
6 I mean, I understand the market moves quickly sometimes.
7 So I mean, that's my hesitance.

8 But, you know, is there an electronic means
9 where if -- you know, if Laclede were to post, say, you
10 know, we're looking for a -- a long-term, you know, gas
11 contract, a collar or whatever, that, you know, there
12 would -- there would be a -- an open, transparent process
13 going forward?

14 Because, I mean, my concern is -- I mean, we're
15 going to spend a year or two hashing out -- I mean, we've
16 already spent 13 months, and we're not there yet. And I'm
17 just wondering if there's something that we need to be
18 doing now to, you know, prevent having these issues on a
19 going-forward basis.

20 I mean, does that -- does that make sense,
21 Mr. Pendergast?

22 MR. PENDERGAST: It makes sense.

23 COMMISSIONER DAVIS: And so -- so -- can you do
24 an RFP so everyone in here would be assured that if -- if
25 LER gets the bid, then everyone knows --

1 MR. PENDERGAST: That makes absolute 100 percent
2 sense from my perspective. And I think one of the
3 unfortunate things, you know, about this having dragged on
4 for so long, I mean, we've been interested in sitting down
5 and talking with the Staff and talking to the Public
6 Counsel so that we can go ahead and come up with a very
7 kind of system that you're talking about.

8 I mean, it doesn't do us any good to run into
9 these disputes to not know what really what the rules of
10 the game are and what other people -- and I think there
11 are things that you can do.

12 We have ICE out there now. That's a -- a
13 bulletin board where if you want to sell gas or you want
14 to buy gas, you don't know who's on the other end of the
15 transaction, but you post it on ICE, and, you know, you
16 get bids and you get offers.

17 We use that extensively now. I think that's a
18 mechanism for substantially reducing, you know, any
19 concerns that anybody might be -- have because you don't
20 even know who is on the other side of the transaction.

21 When you do have somebody on the other side of
22 the transaction, that people were interested in a more
23 robust RFP process, I think that merits a lot of
24 consideration, and we ought to sit down and do it.

25 And we ought to start this today because, quite

1 frankly, we've been operating under rules now for the last
2 seven or eight years where we don't know what the rules
3 are. And, you know, they seem to change from our
4 perspective.

5 And I think sitting down and doing that -- and
6 if there are more definitive things that need to be done
7 with the affiliate transaction rule to spell out exactly
8 how you want to go ahead and account for these
9 transactions and how you ought to do them, I'm all for it.
10 I'd like to start working on that tomorrow.

11 COMMISSIONER DAVIS: Anyone else have a response
12 to that?

13 MS. SHEMWELL: Mr. Pendergast talks about us
14 changing the rules. But, Commissioner Davis, the statute
15 for rate cases has always been just and reasonable.
16 There's no question about that. So the affiliate rules
17 have specific requirements.

18 But the gas that they're -- the cost of the gas
19 that they're charging their customers still has to be just
20 and reasonable. Mr. Pendergast is not surprised by that
21 standard.

22 COMMISSIONER DAVIS: Okay. And I know that.
23 Well, I -- I'm moving on, Ms. Shemwell, to, you know,
24 areas that aren't necessarily the subject of the
25 evidentiary dispute. And it's like -- I mean, are you

1 perfectly content to keep litigating this issue and to
2 keep, I mean, litigating this issue with Mr. Pendergast
3 for years? I mean --

4 MR. THOMPSON: We would be happy to sit down
5 with Mr. Pendergast and work something out on a
6 going-forward basis.

7 MR. PENDERGAST: I think that would be great.

8 COMMISSIONER DAVIS: And honestly -- I mean,
9 honestly, I'm not -- I want to make sure that you know
10 that we're not asking you to work everything out. But,
11 you know, some proposals, some agreements and summaries
12 would be nice.

13 And if you have irreconcilable differences,
14 then, you know, just -- just like Office of Public Counsel
15 has proposed rules for pay stations, you know, they could
16 say, Here's our proposal. Here's Staff's proposal.
17 Here's Mr. Pendergast's proposal. Now, Commission, you
18 decide.

19 But it's like I'm, you know, I'm concerned that
20 -- that everyone is so focused on this case that -- I
21 mean, if you -- if you're truly concerned that the
22 ratepayers have been harmed, which I think is your
23 concern, then --

24 MR. THOMPSON: Our concern --

25 COMMISSIONER DAVIS: What do you do? Are you

1 just going to do nothing to stop the bleeding going
2 forward? Or do you think if you ultimately get a verdict
3 against Mr. Pendergast, then -- a year from now, then that
4 will stop it? I mean, is -- I'm just trying to figure --
5 I'm not asking you for your litigation strategy.

6 I mean, just -- I mean, what's ultimately in the
7 best interest of the -- of the rate-paying public here?

8 MR. THOMPSON: We would be happy to talk to
9 Mr. Pendergast about changes that would be made on a
10 going-forward basis. We're certainly not surrendering our
11 position with respect to the evidence that we're here to
12 talk about today.

13 COMMISSIONER DAVIS: Right.

14 MR. THOMPSON: I would have to talk with the --
15 the gas staff. I mean, many more people than I would be
16 involved --

17 COMMISSIONER DAVIS: Right.

18 MR. THOMPSON: -- in what Staff's position would
19 be -- what Staff's concerns would be. But we're always
20 willing to talk. But what would not change is in every
21 ACA period, there would still be a prudence review.

22 COMMISSIONER DAVIS: Right. Right. No one's
23 saying ditch the -- ditch the prudence review. But,
24 obviously, if we can just promulgate an emergency rule
25 here in six months that said, you know, Laclede can't buy

1 gas from LER anymore, that would at least solve the
2 problem.

3 I mean, you'd have the -- you'd have the ACA
4 arguments for every succeeding period up to that point.
5 But after that point, you wouldn't have the issue -- that
6 issue. You still might have other issues in the ACA,
7 correct?

8 MR. THOMPSON: Correct. And -- and I don't even
9 know that Staff's position is that transactions with LER
10 are always bad or that the sum total is bad. To do a
11 prudence review, we simply feel we need the information
12 we're seeking.

13 COMMISSIONER DAVIS: Okay. All right. And I'm
14 just trying to figure out if there is a larger problem
15 that needs to be solved.

16 MR. THOMPSON: Well, maybe. When we get to the
17 point of actually having the evidentiary hearing, that
18 would be more clear. At this point, we're simply
19 justifying why we want particular evidence.

20 COMMISSIONER DAVIS: Okay. So you're saying
21 that you've got to have -- you've got to have the receipts
22 in hand before you know that you don't like the idea of
23 Mr. Nices dealing with Mr. Nices?

24 MR. THOMPSON: I don't mean to be flippant, but
25 did you ever know an auditor that did not want the

1 receipts?

2 MR. PENDERGAST: As long as the company is
3 supposed to be regulating, no.

4 MR. THOMPSON: Well, you know --

5 COMMISSIONER DAVIS: Okay. Okay.

6 Mr. Pendergast. I'm looking at Mr. Thompson here. We --

7 MR. PENDERGAST: Sorry.

8 MR. THOMPSON: We want the receipts. We --

9 COMMISSIONER DAVIS: Okay. We understand that
10 you want the receipts.

11 MR. THOMPSON: Thank you, sir.

12 COMMISSIONER DAVIS: And I'm just trying to find
13 out, are there any other policy changes that we need to be
14 making here?

15 MR. THOMPSON: Could we address that at a later
16 time? Because I don't want to say something stupid.

17 COMMISSIONER DAVIS: Well, yeah. Obviously --
18 and I think yes. But, I mean, today is October 1st. I
19 mean, certainly, if Mr. Poston, yourself or anyone -- you
20 know, I'm -- I don't know what a reasonable amount of time
21 is.

22 But if you have other policy concerns, maybe you
23 can get them together and get them back to us in a month.

24 MR. THOMPSON: Well, we -- we will do that, sir.

25 COMMISSIONER DAVIS: Because I just -- I'd like

1 to -- to solve this -- I'd like to solve this problem once
2 and for all if we could.

3 MR. PENDERGAST: Chairman, apropos that, too, as
4 a result of our last rate case, there was a provision in
5 the rate case that talked about the Staff and Public
6 Counsel and Laclede sitting down and going through our
7 Cost Allocation Manual and trying to develop provisions
8 that would be satisfactory to everybody.

9 Now, since this whole thing has been going on
10 for the last 13 months, you know, we haven't really had
11 the opportunity, I guess, or the will to sit down and
12 continue those discussions.

13 I think we had a couple of meetings, and I think
14 getting back and -- and doing that would be something that
15 could potentially benefit everybody. But I -- I do think
16 that knowing what the rules are and reaching, you know, as
17 much consensus as we can on how you track transactions,
18 ICE, whether you make them available on an Internet bull
19 -- bulletin board that the Staff can have access to, so it
20 has nearly contemporaneous information, whenever you do a
21 competitive transaction what the competitive price was, I
22 think those are all worthy of discussion. And I think
23 it's a discussion we ought to have sooner rather than
24 later.

25 JUDGE JONES: Does anyone have any more

1 questions? Commissioner Davis? Commissioner Kenney? I
2 -- go ahead.

3 COMMISSIONER KENNEY: No. I don't have any more
4 questions. But it -- in -- assuming nobody else does, let
5 me, again, say that I appreciate the length of time that
6 you all have been battling this particular issue.

7 And I thank you again for indulging me for the
8 last few hours while I ask my questions. So -- and both
9 of you gave very good presentations, and I appreciate the
10 -- the caliber and quality of your lawyering.

11 MR. PENDERGAST: Thank you very much. And we
12 appreciate the opportunity to come here and talk to you
13 today.

14 JUDGE JONES: Okay. With that, then, we're off
15 the record and adjourned.

16 COMMISSIONER DAVIS: Judge, while we're still on
17 the record, I mean, are we going to do a directive
18 ordering filing or --

19 JUDGE JONES: No, no, no. No more filings or
20 nothing. We're just going to wait for the transcript to
21 come up have time to review that. It will be on agenda
22 for discussion.

23 COMMISSIONER DAVIS: Okay. Well, what about --
24 what about my request that if they have policy
25 suggestions, that's --

1 JUDGE JONES: Well -- well, quite frankly, I
2 don't think that's relevant to the discovery issue.

3 COMMISSIONER DAVIS: It's not relevant to the
4 discovery issue. So I guess, you know -- if you have a
5 motion to make or if you want an issue addressed by the
6 Commission, I guess I'm saying I'd appreciate that you do
7 it in the next 30 days.

8 And if you don't, then your silence, I guess,
9 can be construed as acceptance of the status quo with
10 regard to those rules. Is that fair?

11 MR. THOMPSON: That's fair, sir. And we will
12 file whatever policy suggestions we have within a month
13 from today.

14 COMMISSIONER DAVIS: Does that seem reasonable,
15 Mr. Poston?

16 MR. POSTON: Yes.

17 JUDGE JONES: Can you do that and start a
18 different docket, a new -- we don't want the --

19 MR. THOMPSON: A New docket.

20 COMMISSIONER DAVIS: Don't muddy up Judge Jones'
21 docket any more than it already is.

22 MR. THOMPSON: Yes, sir.

23 MS. SHEMWELL: Yes, sir.

24 COMMISSIONER DAVIS: Thank you.

25 JUDGE JONES: Okay. With that, then, we're

1 adjourned.

2 (The proceedings were concluded at 1:45 p.m. on
3 October 1, 2009.)

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REPORTER'S CERTIFICATE

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STATE OF MISSOURI)
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COUNTY OF OSAGE)

I, Monnie S. Mealy, Certified Shorthand Reporter,
Certified Court Reporter #0538, and Registered
Professional Reporter, and Notary Public, within and for
the State of Missouri, do hereby certify that I was
personally present at the proceedings as set forth in the
caption sheet hereof; that I then and there took down in
stenotype the proceedings had at said time and was
thereafter transcribed by me, and is fully and accurately
set forth in the preceding pages.

IN WITNESS WHEREOF, I have hereunto set my hand and
seal on October 5, 2009.

Monnie S. Mealy, CSR, CCR #0539
Registered Professional Reporter