BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Verified Application for Authority to Issue and Sell First Mortgage Bonds, Unsecured Debt and Preferred Stock, in Connection with a Universal Shelf Registration Statement, to Issue Common Stock and Receive Capital Contributions, to Issue and Accept Private Placement Securities, and to Enter Into Capital Leases, all in a Total Amount Not to Exceed $600 Million	)))))))))	**Case No. GF-2009-0450**

STAFF'S REPLY BRIEF

COMES NOW the Staff of the Missouri Public Service Commission (Staff) pursuant to the Commission's April 28th Post-Hearing Briefing Schedule and submits its Reply Brief in response to *Laclede Gas Company's Proposed Findings Of Fact And Conclusions Of law* and the *Initial Brief of Laclede Gas Company*. (Laclede Gas Company is hereinafter referred to as "Laclede" or Company")

Laclede raises no new arguments in support of its modified $520 to $600 million application for authority. Laclede continues to rely on policy arguments, instead of facts, for support of its proposed authority – policy arguments that are founded on tales of the unknown and "what if" scenarios. Staff replies as follows:

Laclede's Proposed Condition to "Float" the Amount of its Long Term Debt Authority based on indices of rate base and capital structure valuation is not permitted under Sect 393.200.1

Laclede seeks a long term debt authority based on a "floating" index giving the Company a level of authority that would not exceed the lesser of the value of Laclede's regulated rate base, which is devoted to public use, or an amount equal to 65% of Laclede's capital structure. In its Initial Brief, Laclede states these conditions, at current rate base valuation, would allow it a debt authority of $280 million. At hearing Laclede

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testified that number was $275 million based on then current conditions. Whatever that number is, under Laclede's proposal, its long term debt authority would "float" on the changing valuation of its rate base and capital structure. If the Commission grants Laclede this condition, it would be giving the Company a "blank check" – amount to be filled in later. Laclede asks the Commission simply to "trust me" – let the Company choose the purpose, amount, and timing of encumbering its assets. A "blanket authority" approach to indebtedness cannot be read into the governing statute, Section 393.200.1. The Commission may not cede its statutory oversight of the Company's financial health to the sole discretion of Company management.

In this regard, the Company's proposal to let its long-term debt authority float on the valuation of the Company is contrary to both the statute and the evidence adduced in this proceeding. Laclede has supported only $100 million of long-term debt authority and no more.

Under no reading of the Section 393.200.1 can the Commission set a debt authority based on a floating index - certainly not a "free floating" index that would authorize encumbering regulated utility assets for unknown purposes and amounts. For the Commission to float Laclede's debt authority on the value of its rate base and capital structure would be to loosen the reins of regulatory oversight and would put utility assets at risk of unnecessary encumbrances. That could pose a detriment to the ratepayer.

Again, Staff asserts it is statutorily impermissible under Section 393.200.1 for the Commission to grant an authority that would allow a public utility to pledge and encumber its regulated assets - assets that are dedicated to serving Missouri ratepayers - for undetermined purposes of "flexibility" in unspecified amounts. The statute requires

the utility to identify to the Commission reasonable and necessary "purposes" as defined by the statute and described in the order. "Flexibility" is not a "purpose" under the provisions of the statute.

As addressed in detail in Staff's Initial Brief in Staff's proposed Condition 1, Laclede only supports a long term debt authority of $100 million based on the record evidence.

If, in the future, Laclede identifies a new purpose, or an emergency need, it may file an application for authority and request expedited treatment. In future applications, Staff suggests the Company identify specific purposes and reasonable amounts necessary to meet those purposes.

Use of Funds From Operations (FFO) to Offset Projected Capital Expenditures

In its Initial Brief, Laclede challenges Staff's use of Laclede's FFO (internally generated funds) as an offset to the Company's projected capital expenditures over the period of the requested authority. Laclede contends Staff used an unsupported "formula" when it deducted FFO from the Company's projected capital expenditures. That simply is not so.

As Staff explained in its brief, it applied Laclede's FFO because: (1) ** _____

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_____ **, (2) Laclede told the American Gas Association Financial Forum in May 2009 that in 2008 it self-funded its capital expenditures and had free cash leftover, and (3) Laclede did not provide any information to Staff about any other intended uses of its FFO.

The "formulaic" approach that Staff used is not of its own "invention." Staff and Laclede used the exact same approach. Staff considered Laclede's FFO in just the same way Laclede did in its communications to ** _____ ** the American Gas Association. Laclede's communications to these groups affirm the appropriateness of the assumptions Staff witness Marevangepo used in estimating the amount of total external capital Laclede may need to issue.

Mr. Marevangepo also allowed the Company some flexibility by recommending that all of this capital could be funded with debt under the proposed $100 million limitation. He testified that, had Laclede identified any purposes for its FFO, he would have considered them. Now, at this late stage in the proceeding, Laclede has laid claim to its FFO to pump up its requested authority. But the record is clear. Laclede still has not identified any amount of its FFO for any other statutory purpose other than offsetting its planned capital expenditures – just as it ** _____ ** and told the American Gas Association.

Laclede's claimed $279 million of "unreimbursed" expenses related to net plant additions are already supported by financing and are not eligible under Section 393.200.1 for additional financing

As Staff discussed in its initial brief, the evidence of record leaves no doubt that the claimed $279 million of "unreimbursed" expenses for net plant additions from 2004 to 2009 are already secured by financing. Laclede continues to ignore the limiting phrase "…not secured or obtained from the issue of stocks, bonds, notes or other evidence of indebtedness of such corporation…" That phrase immediately follows and modifies the purpose "… *for the discharge or lawful refunding of its obligations* or *for the*

reimbursement of moneys actually expended from income, or from any other moneys in the treasury of the corporation…" (emphasis added)

Though arcane in wording the statute's meaning is clear. "Unreimbursed" expenses from income or the treasury are eligible for financing if and only if they are not already secured by the issue of stocks, bonds, notes or other evidence of indebtedness. Without this limitation, a utility could simply trot out a five year schedule containing the same expenditures and use it year after year to justify additional authority.

For example, under Laclede's view, the Company could file an updated 2005 to 2010 schedule containing nearly the same expenditures as the 2004 to 2009 schedule and use that to secure additional financing authority for expenditures that are already supported by financing. The phrase "…not secured or obtained from the issue of stocks, bonds, notes or other evidence of indebtedness of such corporation…" prevents an illogical and absurd result.

The Differences of Debt and Equity Issuances cannot be ignored under Section 393.200.1

Laclede argues that Section 393.200.1 does not distinguish purpose by the type of indebtedness. Staff agrees. But that does not make all types of indebtedness equal. The power to issue debt is the power to encumber assets. Section 393.180 specifically addresses the issuance of long term debt and distinguishes it by its encumbering of utility property. The placement of liens on regulated utility assets is deemed a "special privilege" (Section 393.180) which brings with it the scrutiny of Commission oversight to protect utility assets dedicated to serving the ratepayer. When liens are placed against assets, there becomes a potential for harm to those served by those assets that the Commission cannot ignore.

As Laclede witness Waltermire testified at hearing, in contrast, equity does not create liens against regulated assets. As the Chief Financial Officer of Laclede Gas and Laclede Group, Mr. Waltermire should know because he is a key decision maker on whether to issue debt or equity and what financial "vehicle" the Company should use to meet a certain need. He is also primarily responsible for submitting Laclede Group's Form 10-K with the SEC.

Equity has striking differences from debt. For example, the issuance of common equity is self-dilutive. Unless the Company is in a high earnings growth mode, which Laclede is not, the more shares issued, the more the share price declines. A downward movement in share price caused by the Company issuing new shares would not sit well at all with shareholders. The number of shares issued or outstanding is governed by the expectations of shareholders.

With equity, amount and timing of dividend payments are at the sole discretion of management. In bad economic times, Company management may decide to reduce or even stop paying dividends. In contrast, issuance of debt causes financial risk, the issuance of equity does not, but equity issuance can dilute shareholder value.

Long-term debt contractually obligates the Company to pay interest to debt holders. In an economic downturn, the Company cannot disregard its legal duty to make interest payments at the contractually set rate. It cannot forgo interest payments without consequences any more than an individual who has a home loan can forgo mortgage payments. In the homeowner's case, the object of the loan – the home - is also the collateral supporting the mortgage. In Laclede's case, the collateral supporting its debt is its plant, equipment and property.

Long-term debt is also treated differently in a general rate case. In a rate case there is no controversy over how much interest is paid to service outstanding long-term debt because the interest rates are set by contract. Not so with common equity. The Commission sets the amount of return on equity that the utility is permitted to recover and that amount must be determined by the Commission to be just and reasonable.

Conclusion

Under Staff's Conditions, the Company is free to issue common equity up to $500 million, subject to the $100 million debt limitation (combined total $600 million) and the limitations in Case No. GM-2001-341, requiring the Company to stay within a specified range of a target debt–to-equity ratio (65% debt maximum to 35% equity minimum) and maintain an investment grade credit rating. Staff's proposed Conditions afford Laclede great discretion on whether to issue common equity or long term debt.

The power to put liens on property and to encumber assets that collateralize mandatory interest payments is a matter that could, under a variety of circumstances, bring significant harm to the Company and its customers. That power requires the greatest oversight of the Commission under the governing statute Section 393.200.1 and Section 393.180. The Commission should approve Laclede's Application only if it also adopts Staff's twelve Conditions.

WHEREFORE, the Staff prays the Commission accept its Reply Brief as directed by the Commission and renews its recommendation that the Commission approve Laclede's Application for financing authority with Staff's proposed twelve Conditions.

Respectfully submitted,

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Certificate of Service

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or electronically mailed to all counsel of record this 28th day of May, 2010.

/s/ Robert S. Berlin