SURREBUTTAL TESTIMONY

OF

JAMES A. BUSCH

CASE NO. GR-2004-0209

MISSOURI GAS ENERGY

Q. Please state your name and business address.

A. My name is James A. Busch and my business address is P. O. Box 2230, Jefferson City, MO 65102.

Q. By whom are you employed and in what capacity?

A. I am a Public Utility Economist with the Missouri Office of the Public Counsel (Public Counsel).

Q. Are you the same James A. Busch who filed direct and rebuttal testimony earlier in this proceeding?

A. Yes I am.

Q. What is the purpose of your surrebuttal testimony in Case No. GR-2004-0209?

A. The purpose of my surrebuttal testimony is to address the rebuttal testimonies of Missouri Gas Energy (MGE or Company) witnesses F. Jay Cummings, Michael Noack, and John Hayes, intervenor Federal Executive Agencies (FEA) witness Gary Price, and intervenor (CMSU, UMKC, and MGUA) witness Donald Johnstone.

Q. How is your surrebuttal testimony organized?

A. My surrebuttal testimony is organized in the following manner. First, I will discuss the Class Cost of Service (COS) studies or rebuttal testimony concerning the class COS studies of witnesses Cummings, Johnstone, and Price. Second, I will discuss MGE's proposed rate design, including its alternative proposal of a weather normalization clause (WNC) as found in the rebuttal testimony of MGE witness Cummings. Finally, I will address the capacity release issue as described in the testimony of MGE witnesses Noack and Hayes.

CLASS COST OF SERVICE STUDIES

Q. Has any party filed a new class COS study in rebuttal testimony?

A. Yes. Witness Price for the FEA filed a new class COS study in his rebuttal testimony. This study generally accepted MGE's class COS study methodologies with a few changes in certain allocators.

Q. Have you had an opportunity to review his study?

A. I have reviewed the study as it was presented in his filed testimony. However, I have not received electronic copies of his workpapers at this time. Therefore, I would reserve the right to address any further concerns I may have with witness Price's class COS study in supplemental surrebuttal.

Q. Has witness Johnstone filed a class COS study for the intervenors CMSU/MGUA/UMKC?

A. No. Witness Johnstone has simply commented on the various class COS studies that were filed in direct testimony.

Q. Witnesses Price, on page 10, lines 1 – 3 of his rebuttal testimony, Johnstone, on page 20,lines 12 and 13 of his rebuttal testimony, and Cummings, on page 25, lines 3 – 9 of his rebuttal testimony, criticize Public Counsel for "ignoring or denying" the customer impact on mains cost. Do you have comment to their criticism?

A. Yes. As I discussed in my rebuttal testimony, dividing mains costs into customer-related and demand-related components leads to excessive costs to the low-use user. The best way to avoid this excessive cost problem is to simply allocate mains cost through a demand factor. This is what Public Counsel did in its cost study.

Furthermore, it is more appropriate to allocate mains costs only through a demand allocator for the following reason. The main is in the ground not to just serve one customer or to simply provide natural gas on a peak day. The main is in the ground to provide service on a daily basis to all existing customers and to be available for potential future customers. Public Counsel's method takes this into account by looking at demands throughout the year and determining the appropriate percentage for each customer class.

Q. Both witness Price and Johnstone criticize the other three parties for allocating gas inventories to the LVS class. Please respond.

A. First an LVS customer (an LVS customer is generally a commercial or industrial customer whose natural gas requirements at a single address or location that MGE expects will exceed 15,000 Ccf in one month of a 12 month billing period) can be either a transportation customer or a sales customer. Therefore it is appropriate to allocate some of the inventory costs to the LVS class. Second, there may be instances where a transportation customer receives more gas from MGE than it nominated. Thus, the transportation customer would be receiving benefit from the system and benefit from gas that was in storage. Since the potential for benefit is there, transportation customers should be allocated a portion of gas inventory. Third, a benefit to the entire system is the fact that MGE has storage capabilities. Therefore, all customers should share in the costs.

Q. What is the difference between a transportation customer and a sales customer?

A. A sales customer is a customer that relies on MGE to purchase its natural gas for it and provide transportation. A transportation customer is a customer that generally only uses MGE for the transport of natural gas to its premises. It is responsible for the purchase of its gas supplies from a third party.

WEATHER NORMALIZATION CLAUSE

Q. Has MGE offered an alternative to its weather mitigation rate design?

A. Yes it has. MGE has now offered a weather normalization clause (WNC) for the Commission's consideration if the Commission decides against MGE's proposed weather mitigation rate design as offered in witness Cummings's direct testimony.

Q. How does the WNC work?

A. As discussed in MGE witness Cummings rebuttal testimony, the WNC adjusts the non-gas portion of the customer's bill to account for deviations from "normal" weather. This means that no matter what the actual weather is, the customer will pay as if the weather was normal.

Q. What is normal weather?

A. In a rate case proceeding, the Commission determines what is considered to be normal weather (i.e. a normal amount of HDDs or Heating Degree Days per year) for the determination of the appropriate per unit rate to charge customers. Historically, this Commission has favored using thirty years of weather data to determine normal weather.

Q. Does this mean that a customer may pay more for natural gas than the tariffed rate?

A. Yes. If the weather in a month is warmer-than-normal, an adjustment will be made to the customer's bill to adjust the volumes up to normal. Thus, when compared to a standard rate design, the customer is paying more for natural gas service under the WNC due to the upward weather adjustment.

Q. Please provide a numerical example.

A. Please refer to Schedule JAB-S1 for the complete calculation. First, assume that MGE is still operating under its current rate design structure. Second, assume that the non-gas volumetric rate is $0.15 per Ccf. Third, assume that the customer uses 150 Ccfs in a given billing cycle in the Kansas City area. The volumetric charge to this customer would normally be $22.50. Now assume that the WNC has been implemented. Looking at Schedule JAB-S1, you can see that when there is a 10% reduction in HDDs (Heating Degree Days) that leads to a weather adjustment of approximately 14.6 Ccfs. Multiplying the weather adjustment by the $0.15 per Ccf volumetric charge results to an adjustment of approximately $2.19 on the customer's bill. This additional $2.19 added to the $22.50 means that the effective rate paid per Ccf increases to $0.1646 per Ccf ($24.69/150 Ccfs).

Q. Does the WNC apply to each customer class?

A. No. The WNC is to apply only the residential and small general service customer classes.

Q. Is the concept of a WNC new?

A. No. MGE has tried unsuccessfully in the past to have the Commission approve a WNC. Also, Laclede Gas Company has unsuccessfully proposed a WNC in past rate proceedings.

Q. In the past, has the Commission ruled on lawfulness, justness, and reasonableness of a WNC.

A. Yes it has. In Case No. GT-95-429, In the Matter of Missouri Gas Energy's Tariff Revision Designed to Implement a Weather Normalization Clause, the Commission found that the WNC is unjust, unreasonable, and contrary to law and should be rejected (Report and Order, Case No. GT-95-429, page 5). It further stated that since the Commission found the proposed WNC tariff to be unlawful, it could not be approved on an experimental basis (Report and Order, Case No. GT-95-429, page 5).

Q. Are there any other cases in which the Commission ruled against a proposed WNC?

A. Yes. In Case No. GR-96-285, In the Matter of Missouri Gas Energy's Tariff Sheets Designed to Increase Rates for Gas Service in the Company's Service Area, the Commission found that the approval of the WNC would be a de facto abdication of the Commission's responsibility to set rates and that the fact that the WNC technically adjusts volumes rather than rates does not cure this fundamental problem. Thus, the Commission will not approve the WNC (Report and Order, Case No. GR-96-285, page 61).

Q. Did the Commission find anything else about the WNC in its Report and Orders?

A. Yes. In the GR-96-285 Report and Order the Commission stated the following:

> It is clear to the Commission that approval of the WNC proposed by MGE would benefit MGE insofar as the variability of its revenues resulting from weather changes would be reduced, thus reducing MGE's business risk. The WNC would shift **virtually all** weather-related risk onto ratepayers. In the event that the Commission would authorize a WNC similar to the one proposed herein, the Commission would seriously consider a downward adjustment to return on equity as proposed by OPC. Also, there may be other conditions that would have to be implemented along with the WNC. … On balance, the Commission finds that the **WNC would be a detriment to ratepayers because weather-related risks would be assumed by ratepayers,** and ratepayers are already able to levelize their payments by entering into a levelized payment plan.

(Report and Order Case No. GR-96-285, pages 60 and 61, emphasis added)

Further in Case No. GT-95-429, the Commission determined the following:

> The Commission agrees with OPC and Staff that the institution on the WNC tariff could affect the company's rate of return by reducing its risk. If the rate of return were to change, the matching of revenues and expenses approved by the Commission in the company's last rate case would be abrogated and the effective rate structure changed without a reconsideration of all relevant factors.

> The Commission further finds that approval of the WNC tariff would result in a de facto change in MGE's rates. Under the weather normalization clause a customer would pay for more gas than he actually used in an unusually warm month. In that month, the customer would have paid an effective per unit rate for his actual usage greater than MGE's current tariffed rate. In an unusually cold month

> the customer would pay for less gas than he actually used. In that month, the customer would have paid a lower per unit rate for his actual usage than MGE's current tariffed rate.
> (Report and Order, Case No. GT-95-429, pages 3 and 4)

Q. Does Public Counsel oppose the implementation of a weather normalization clause for MGE in this proceeding?

A. Yes it does.

Q. Why?

A. Public Counsel opposes MGE's proposed WNC for many of the same reasons that the Commission articulated in its denials of previous attempts by MGE to implement a WNC.

Q. Does Public Counsel agree with the findings of the Commission regarding WNC's detriment to the public?

A. Yes. Public Counsel still believes that a WNC, or the weather mitigation rate design proposed by MGE in its direct testimony, would be a detrimental to the ratepayers of MGE. I will show this later in my testimony. Public Counsel still believes that both proposed weather mitigation tools shift "virtually all weather related risk" to the consumers. Public Counsel still believes that if the Commission does decide to implement one of these weather mitigation tools that it must consider a reduction in MGE's authorized rate of return due to the reduction in business risk the Company will now be faced with.

Q. Does witness Cummings agree with earlier Commission decisions concerning the reduction of variability in the Company's revenue stream?

A. Yes. On page 37, lines 9 – 11, witness Cummings states, “The Company benefits from a WNC through significantly reducing the variability of its revenue stream and improving its opportunity to reach the revenue levels that the Commission will use to set rates in this case.”

Q. Would approval of a WNC, like approval of MGE’s earlier proposed weather mitigation rate design, reduce MGE’s risk?

A. Yes. Both rate design proposals have the same major component, and that component is to reduce the variability of MGE’s earnings due to changes in the weather. As discussed in my rebuttal testimony, this one-sided transfer of risk is of benefit only to the Company, while it leaves all weather-related risk on the ratepayers.

Q. Are you aware of any other businesses that have any sort of weather clause that ensures relatively constant returns?

A. No. I am not aware of any business that has a clause that guarantees earnings regardless of the weather, or other risks. For example, assume that a baseball team expects 30,000 customers per game. These fans will pay for a ticket, parking, and concessions, to provide revenues to the owners. Further assume that due to a forecast for rainy weather, only 5,000 brave souls decide to endure three hours of rain soaked baseball. The team not only loses money due to a lack of ticket sales, but it also loses money from less parking and fewer concession sales. The owners of the team, seeing the lower level of attendance, do not have the ability to go to its fans that did not attend the game due to the weather and demand that they pay for a product that was not consumed. Nor do the owners raise ticket prices for the next game to make up for the loss of the previous game. It is simply one of the risks the owners take.

Q. Witness Cummings, on page 36, lines 10 – 23, and page 37, lines 1 – 7, of his rebuttal testimony describes the so-called benefits to residential consumers of the proposed WNC. Do you agree with his statement?

A. No.

Q. Why?

A. The so-called benefits or "premiums" witness Cummings describes are de minimus to the overall bill of an average MGE customer. A majority of the costs that a residential consumer faces come from the Purchased Gas Adjustment (PGA) rate that consists of the gas costs plus transportation costs.

Q. Can you provide an example of the de minimus benefits an average customer would receive from the WNC?

A. Yes. For my example, I used the average residential use used by witness Cummings found on page 31 of his direct testimony. I then took the average use and increased it by 10% for a colder-than-average year, and decreased it by 10% for a warmer-than-average year. Table 1 shows the results of my analysis.

TABLE 1

Average

	Use	Delivery Charge	Customer Charge	Non-Gas Costs	PGA	Total Bill
Jan	176	$ 20.10	$ 10.05	$ 30.15	$132.10	$ 162.25
Feb	168	$ 19.19	$ 10.05	$ 29.24	$126.09	$ 155.33
Mar	138	$ 15.76	$ 10.05	$ 25.81	$103.58	$ 129.39
Apr	91	$ 10.39	$ 10.05	$ 20.44	$ 68.30	$ 88.75
May	49	$ 5.60	$ 10.05	$ 15.65	$ 36.78	$ 52.42
Jun	21	$ 2.40	$ 10.05	$ 12.45	$ 15.76	$ 28.21
Jul	16	$ 1.83	$ 10.05	$ 11.88	$ 12.01	$ 23.89
Aug	14	$ 1.60	$ 10.05	$ 11.65	$ 10.51	$ 22.16
Sep	16	$ 1.83	$ 10.05	$ 11.88	$ 12.01	$ 23.89
Oct	26	$ 2.97	$ 10.05	$ 13.02	$ 19.51	$ 32.53
Nov	48	$ 5.48	$ 10.05	$ 15.53	$ 36.03	$ 51.56
Dec	116	$ 13.25	$ 10.05	$ 23.30	$ 87.06	$ 110.37
Yearly Total		$ 100.41	$ 120.60	$ 221.01	$659.74	$ 880.75
Percent of Total		**11.40%**	**13.69%**		**74.91%**	

10% Greater-Than-Average-Use

	Use	Delivery Charge	Customer Charge	Non-Gas Costs	PGA	Total Bill
Jan	193.6	$ 22.11	$ 10.05	$ 32.16	$145.31	$ 177.47
Feb	184.8	$ 21.11	$ 10.05	$ 31.16	$138.70	$ 169.86
Mar	151.8	$ 17.34	$ 10.05	$ 27.39	$113.94	$ 141.33
Apr	100.1	$ 11.43	$ 10.05	$ 21.48	$ 75.13	$ 96.62
May	53.9	$ 6.16	$ 10.05	$ 16.21	$ 40.46	$ 56.66
Jun	23.1	$ 2.64	$ 10.05	$ 12.69	$ 17.34	$ 30.03
Jul	17.6	$ 2.01	$ 10.05	$ 12.06	$ 13.21	$ 25.27
Aug	15.4	$ 1.76	$ 10.05	$ 11.81	$ 11.56	$ 23.37
Sep	17.6	$ 2.01	$ 10.05	$ 12.06	$ 13.21	$ 25.27
Oct	28.6	$ 3.27	$ 10.05	$ 13.32	$ 21.47	$ 34.78
Nov	52.8	$ 6.03	$ 10.05	$ 16.08	$ 39.63	$ 55.71
Dec	127.6	$ 14.58	$ 10.05	$ 24.63	$ 95.77	$ 120.40
Yearly Total		$ 110.45	$ 120.60	$ 231.05	$725.72	$ 956.77
Percent of Total		**12.54%**	**13.69%**		**82.40%**	

10% Lower-Than-Average-Use

	Use	Delivery Charge	Customer Charge	Non-Gas Costs	PGA	Total Bill
Jan	158.4	$ 18.09	$ 10.05	$ 28.14	$118.89	$ 147.03
Feb	151.2	$ 17.27	$ 10.05	$ 27.32	$113.48	$ 140.81
Mar	124.2	$ 14.19	$ 10.05	$ 24.24	$ 93.22	$ 117.46
Apr	81.9	$ 9.36	$ 10.05	$ 19.41	$ 61.47	$ 80.88
May	44.1	$ 5.04	$ 10.05	$ 15.09	$ 33.10	$ 48.19
Jun	18.9	$ 2.16	$ 10.05	$ 12.21	$ 14.19	$ 26.39
Jul	14.4	$ 1.64	$ 10.05	$ 11.69	$ 10.81	$ 22.50

Aug	12.6	$	1.44	$	10.05	$	11.49	$ 9.46	$	20.95
Sep	14.4	$	1.64	$	10.05	$	11.69	$ 10.81	$	22.50
Oct	23.4	$	2.67	$	10.05	$	12.72	$ 17.56	$	30.29
Nov	43.2	$	4.93	$	10.05	$	14.98	$ 32.42	$	47.41
Dec	104.4	$	11.93	$	10.05	$	21.98	$ 78.36	$	100.33
Yearly Total		$	90.37	$	120.60	$	210.97	$593.77	$	804.74
Percent of Total			**10.26%**		**13.69%**			**67.42%**		

My analysis shows that in an average year, based on MGE's current tariffed rates, an average residential customer will have an annual bill of $880.75. Of this amount, $100.41, or 11.4%, will be from the delivery charge. Another $120.60, or 13.7%, will be from the monthly customer charge. The remaining 74.9%, or $659.74, is due to the PGA rate. Thus, the proposed WNC merely affects the portion of the bill that makes up only 11.4% of the customer's total annual bill.

Q. What is the dollar impact of MGE's proposed WNC on an average use customer?

A. Assuming warmer-than-normal weather leads to lower usage and colder-than-normal weather leads to greater usage, the difference in the annual delivery charge between a warmer-than-average year and average year is approximately $10 per year per average customer. The difference in the annual delivery charge between a colder-than-average year and the average year is also approximately $10 per year per average customer. However the respective differences in PGA costs are is approximately $66 per year per average customer. In other words, an average customer would be paying or receiving an extra $10, depending upon actual weather conditions, to protect the Company from revenue variations, while still being subject to the full effect of the PGA rate. This is hardly a benefit to the consumers or a way to make gas service somewhat more affordable as witness Cummings characterizes it in his rebuttal testimony. On the contrary, this weather normalization clause, like the weather mitigation rate design proffered in MGE's direct testimony is simply another proposal to protect the Company without providing the ratepayers with equal protection.

Q. How does the weather normalization clause protect the Company but not the ratepayer?

A. The Company is protected since its revenues are derived from the non-gas rates that consumers pay. These rates are the volumetric and customer charges on a typical residential bill. On the other hand, the ratepayers are not protected because they still have to pay the actual gas and transportation costs. From the Company perspective, these costs are flowed to the consumers from the suppliers and pipeline companies via a dollar-for-dollar pass through. Therefore, the Company is not profited or harmed by these costs.

Q. Does the proposed WNC affect PGA rates?

A. No.

Q. Has MGE offered to reduce its return on equity upon implementation of either its proposed weather mitigation rate design or the WNC even though both proposals have the effect of reducing MGE's business risk?

A. No.

Q. Are there other problems with the WNC?

A. Yes. The WNC does not send the proper price signals to MGE's customers.

Q. Please explain.

A. Since the customer's monthly bill will be changed depending upon the outcome of that month's weather, the consumer will not know the effective volumetric charge he will be faced with prior to his consumption. Therefore, a consumer who may try to lower his bill by reducing his thermostat will not know the actual impact of his conservation efforts.

Q. What is another problem of the WNC?

A. Another problem would be the complexity to the consumer's bills if a WNC is implemented. Adding a charge to the bill to account for an increase or reduction based upon a previous period's weather will only confuse the customers who just want to know that the amount they are paying coincides with the number of Ccfs they used; no more, no less.

Q. Throughout his rebuttal testimony, MGE witness Cummings bemoans the need for the Commission to approve a rate design that would stabilize the Company's revenues from the impacts of the weather. Do you have any comments about these statements?

A. Yes. Witness Cummings claims throughout his testimony that MGE has not been able to earn its authorized rate of return. However, I am not aware of any source that states that a regulated utility is guaranteed a particular rate of return. The company is merely offered the opportunity to earn its rate of return. Furthermore, MGE first proposed a WNC in Case No. GT-95-429, to no avail. Since that time, operating without a WNC, MGE seems to have been able to maintain its ability to provide safe and reliable gas service at just and reasonable prices. I am unaware of any fundamental changes in the natural gas industry that have occurred recently that would prevent MGE from continuing to provide safe and reliable service at just and reasonable prices absent a WNC, or any form of weather mitigation rate design.

Q. Do you have any source that states that a public utility is not guaranteed a given rate of return?

A. Yes. From The Regulation of Public Utilities, by Charles F. Phillips, Jr., page 363, under the heading *No Guarantee of a Fair Return*, Phillips states:

> The Supreme Court also has stated that public utilities are not guaranteed a fair rate of return. In a 1933 case, the Court argued: The due process clause of the Fourteenth Amendment safeguards against the taking of private property, or the compelling of its use, for the service of the public without just compensation…. But it does not assure to public utilities the right under all circumstances to have a return upon the value of the property so used. The use of, or the failure to obtain, patronage, due to competition, does not justify the imposition of charges that are exorbitant and unjust to the public. The clause of the Constitution here invoked does not protect against such business hazards.

Q. On page 37, lines 16 – 21 of his rebuttal testimony, witness Cummings states that as a layman, he believes that the Commission has the authority to approve the implementation of the WNC as a "test case" or experiment. Do you believe the Commission should authorize MGE's proposed WNC?

A. No. MGE has tried twice in the past to get approval of a WNC from this Commission. Twice the Commission has ruled against the WNC, and on at least one occasion ruled that it was contrary to law. It is my belief that due to those findings, the Commission should not impose a WNC without agreement from all parties. At this time, Public Counsel does not agree to MGE's proposed WNC.

OFF-SYSTEM SALES/CAPACITY RELEASE

Q. What is the issue concerning capacity release and off-system sales revenues?

A. The issue regarding off-system sales/capacity release revenues has to do with the manner in which these revenues should be addressed. Both Public Counsel, in my direct testimony, and Staff, in the direct testimony of Anne Allee, have proposed to put any revenues associated with off-system sales and capacity release in MGE's cost of service. MGE, in the rebuttal testimony of Michael Noack, disagrees with this treatment and proposes to put these revenues in the PGA/ACA (Purchase Gas Adjustment/Actual Cost Adjustment) mechanism. Further, MGE proposes a sharing grid to divide any revenues from off-system sales/capacity release between the Company and the customers. This grid would give MGE a share of any of these revenues from the first dollar of either a capacity release transaction or off-system sale.

Q. Why does Public Counsel believe that off-system sales/capacity release revenues should be included in the cost of service?

A. As explained in my direct testimony, Public Counsel believes that off-system sales and capacity release transactions are a normal part of MGE's business activities. Therefore, any revenues collected by MGE should be credited to ratepayers in base rates in order to offset any costs associated with these transactions.

Q. Has the Commission ever decided the issue of the appropriate treatment of off-system sales/capacity release revenues?

A. Yes. In Case No. GT-99-303, referred to in my direct testimony, the Commission found that off-system sales revenues should be included in base rates. The Commission did not make the same finding for capacity release revenues at that time.

Q. Why does Public Counsel include capacity release revenues in base rates?

A. Due to the interdependent nature of off-system sales and capacity release, Public Counsel believes both of these activities should be included in base rates.

Q. Briefly reiterate the interdependence between capacity release and off-system sales.

A. Capacity release occurs when the Company allows a third party to utilize its unused pipeline capacity. The Company has unused capacity because it has to insure sufficient capacity to meet peak day demands on its system. Off-system sales can be either the sale of excess natural gas, or a combination of excess natural gas and unutilized capacity. If these activities are treated in a dissimilar manner, the Company could focus its efforts on one activity to the detriment of ratepayers.

Q. MGE witness John Hayes discusses the Kern River pipeline expansion in May of 2003. What effect did this have on MGE's capacity release revenues?

A. I don't know the direct impact that the Kern River pipeline expansion had on MGE's capacity release revenues, but according to Table 2 below, it looks as if MGE's monthly capacity release revenues in June 2003 – December 2003 have generally increased.

**** Table 2**

	2001	2002	2003
Jan			
Feb			
Mar			
Apr			
May			
Jun			
Jul			
Aug			
Sep			
Oct			
Nov			
Dec			

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Q. Witness Hayes describes future impacts on MGE's ability to earn revenues through capacity release in the future. Do you have any comments on those statements?

A. Yes. In my preparation for this proceeding I sent out various Data Requests (DRs) to MGE. Attached, as Schedule JAB-S2, are my questions and MGE's responses to Public Counsel DRs 603 – 606. These DRs generally asked for any documentation, reports, analyses, and/or Board of Director minutes that discussed future potential off-system sales or capacity release. As you can see by MGE's responses, there was no documentation.

Q. After reading witness Hayes' rebuttal testimony, do these responses surprise you?

A. Yes. Natural gas pipeline projects do not spring up overnight. It takes up to one year from the time the new pipeline project has its initial open season (when potential shippers make initial capacity requests) to the pipeline Company files with FERC. It then takes time for the FERC to make its decision. Finally,

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construction of a major pipeline will take months to complete. In total, the process could take upwards of two or more years.

Furthermore, if these potential projects are going to impact MGE's ability to maintain a revenue stream, I would expect that the Company would have at least some documentation or analysis evaluating the potential impact the projects would have on the Company. Since MGE's response to my DRs were notably void of any such documentation or analysis to prepare any reports, I question the real impact they may have on MGE's ability to continue its capacity release revenue stream.

Q. Witness Hayes, on page 10, line 8 of his rebuttal testimony, mentions a potential pipeline called Western Frontier as possibly having an impact on MGE's ability to release capacity. What do you know about the Western Frontier pipeline?

A. Western Frontier is a pipeline project originally proposed by Williams Gas Pipeline (WNG) Company and filed with FERC in October of 2001. In June of 2002, WNG pulled its FERC application for the project. Currently, Williams is now called Southern Star Central Gas Pipeline (SSC), and is owned by AIG Highstar. SSC has reopened the proposed pipeline and has gone through an open season. However, an in-service date for this project is not proposed until 2006 or 2007, according to SSC. Furthermore, at this time, due to a lack of interest in this project, this project is not going forward. However, if market conditions change, SSC may have another open season.

Q. Also on page 10 of witness Hayes' rebuttal testimony, he mentions a pipeline project called Advantage being built by Kinder Morgan. What is the latest information on this project?

A. The open season for this project on December 15, 2003. Furthermore, in the March 24, 2004 edition of the Pipeline and Gas Journal (http://www.kindermorgan.com/news/news_features.cfm), it states that **if** the project is built, it could provide capacity from the Rocky Mountains to the mid-continent. Any in-service date will not happen until at least early 2006.

Q. Will these proposed pipelines have an immediate effect on MGE?

A. No. These projects, with potential in-service dates of no earlier than early 2006 or 2007 should have no immediate impact on MGE. Since MGE's rates from this case will go into effect no later than October 4, 2004, if either one of these pipelines does actually materialize, MGE will have ample time to file another rate case to take those new realities into consideration.

Q. Did your recommendation for capacity release/off-system sales revenues assume MGE would continue its current level of capacity release?

A. No. My recommendation was based off of the information contained in Table 2 above. As you can see capacity release revenues were ** __________ * in 2001, ** __________ ** in 2002, and ** __________ * in 2003. This shows a three-year trend of increasing capacity release revenues. However, my recommendation was to build in only ** __________ * into base rates. If I was anticipating MGE to be able to continue its current level of capacity release revenues I would have either used the total revenues from year ending 2003

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(which coincides with the update period for known and measurable changes), or done a trend analysis which would have shown an increase in capacity release revenues over the past three years.

Q. Does MGE propose an incentive sharing mechanism if off-system sales/capacity release revenues are put back in the PGA/ACA mechanism?

A. Yes. MGE proposes a sharing grid that is similar to the one it had in its last incentive plan. The sharing grid can be found on page 29 of witness Noack's rebuttal testimony.

Q. Please comment on the proposed sharing grid.

A. First, under the proposal, MGE would be allowed to keep 15% of any capacity release/off-system sales revenues up to $300,000. This means that if MGE only did $1 worth of capacity release of off-system sales, MGE would still get $0.15. Public Counsel disagrees with the Company being able to profit from the first dollar of capacity release/off-system sales revenues. Public Counsel believes that since there is a built amount of off-system sales/capacity release revenues that MGE should be able to earn in the normal course of doing business, therefore, MGE should have to reach a threshold level of off-system sales/capacity release revenues before it is allowed to profit from those transactions. Second, the methodology proposed by Public Counsel is the ultimate incentive. Under Public Counsel's treatment of these revenues, once MGE attains the baseline amount of revenues, it keeps 100% of any additional revenues. This provides the Company with the proper incentive to stay active in the capacity release/off-system sales markets.

Q. Has the Commission ruled on any incentive plans similar to MGE's proposal in the recent past?

A. Yes. In Case No. GT-2001-329, a proceeding involving Laclede Gas Company, Laclede's incentive mechanism was allowed to expire. This mechanism included a sharing grid for capacity release similar to the one proposed by MGE in this proceeding.

Q. If the Commission decides in this proceeding to move capacity release/off-system sales revenues into the PGA/ACA mechanism, should the Commission adopt MGE's proposed sharing grid?

A. No. If the Commission decides to move these revenues to the PGA/ACA mechanism, the Commission should establish the same baseline amount of off-system sales/capacity release revenues that I proposed in my direct testimony. This way, MGE cannot unreasonably benefit from the first dollar of any capacity release or off-system sale.

SUMMARY

Q. Please summarize your surrebuttal testimony.

A. In summary, I believe that the methodology I utilized to allocate mains costs is the best way to identify the appropriate recovery from each class based on costs causation principles. Public Counsel opposes MGE's alternate rate design proposal of a weather normalization clause. Also, Public Counsel still opposes MGE's originally proposed weather mitigation rate design as well. Finally, Public Counsel believes that the appropriate recognition of capacity release/off-system sales revenues is in base rates.

Q. Does this conclude your surrebuttal testimony?

A. Yes.