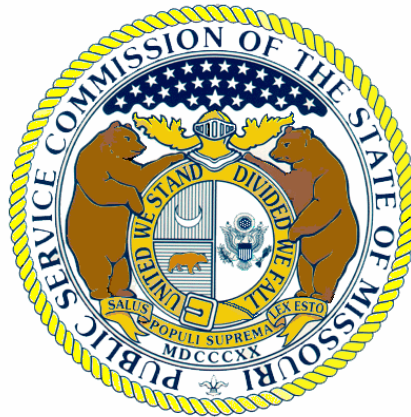


BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI



In the Matter of Laclede Gas Company's Tariff)
Designed to Permit Early Implementation of)
Cold Weather Rule Provision and to Permit)
Laclede to Collect Bad Debt Through the PGA)

File No. GT-2009-0026
Tariff No. JG-2009-0033

REPORT AND ORDER

Issue Date: April 15, 2009

Effective Date: April 25, 2009

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APPEARANCES

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For Laclede Gas Company.

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For the Office of the Public Counsel and the Public.

DEPUTY CHIEF REGULATORY LAW JUDGE: Morris L. Woodruff

REPORT AND ORDER

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The Missouri Public Service Commission, having considered all the competent and substantial evidence upon the whole record, makes the following findings of fact and conclusions of law. The positions and arguments of all of the parties have been considered by the Commission in making this decision. Failure to specifically address a piece of evidence, position, or argument of any party does not indicate that the Commission has failed to consider relevant evidence, but indicates rather that the omitted material was not dispositive of this decision.

Procedural History

On July 9, 2008, Laclede Gas Company filed a tariff revision that would modify the company's purchased gas adjustment (PGA) mechanism to allow Laclede to recover the gas cost portion of its bad debt write-offs from its customers through the PGA mechanism.¹ On July 17, the Office of the Public Counsel filed a motion opposing Laclede's proposal to include bad debt amounts in the PGA and asking the Commission to suspend the tariff. The Commission's Staff filed its own motion on July 22, in which it asks the Commission to suspend or reject Laclede's tariff.

Laclede's tariff carried an effective date of August 8. On August 5, the Commission issued an order suspending the tariff until December 6. Following a prehearing conference,

¹ Laclede's tariff would also have implemented certain provisions of the Commission's cold weather rule in advance of the winter heating season. Those provisions have been rendered moot by the passage of time while the tariff has been suspended, and the parties agree they do not need to be further addressed in this Report and Order.

the Commission, on August 28, adopted a procedural schedule proposed by the parties, and extended its suspension of the tariff for an additional six months, until June 6, 2009.

In compliance with the established procedural schedule, the parties prefiled direct, rebuttal, and surrebuttal testimony. The Commission conducted an evidentiary hearing on January 5, 2009. The parties, filed initial post-hearing briefs on February 13, followed by reply briefs, on February 27. In addition, the Missouri Energy Development Association (MEDA) filed an amicus brief on February 13.

Findings of Fact

Laclede proposes to modify its PGA tariff to allow for the recovery of what Laclede describes as the gas cost portion of its bad debt expense. To understand what that proposed modification would do, it is necessary to first understand how Laclede currently recovers its cost of bad debt, and second, to understand how the PGA tariff works.

Laclede, like any other business, has customers who either cannot or will not pay their bills. After a customer's account with Laclede is unpaid for six months, the company writes that account balance off as uncollectible, in other words, bad debt.² Bad debt is a legitimate cost of doing business, for which a utility is generally allowed to seek recovery from its customers through rates established by this Commission.

Currently, Laclede is able to recover its bad debt expense through its base rates. As part of an overall rate case, the Commission determines the amount of bad debt expense the utility is likely to incur. The Commission then considers that amount of bad debt

² Transcript, Page 78, Lines 1-14.

expense, along with the other expenses and revenues of the utility when establishing a rate that will allow the utility an opportunity to recover its cost of service from its customers.³

The amount the Commission chooses to allow Laclede to recover for bad debt expense through a rate case is, however, just an estimate of what those expenses will be. If the actual level of bad debt rises above the amount allowed in the rate case, Laclede runs the risk of under recovering its costs. Conversely, if bad debt levels drop below the amount allowed in the rate case, Laclede would be able to keep the extra revenue resulting from the over recovery of its costs. Laclede's proposal would relieve the company of a part of the risk of over or under recovery of bad debt expenses by allowing the company to recover part of those expenses from ratepayers through the existing PGA mechanism.

The PGA mechanism allows Laclede to recover the costs it incurs to purchase natural gas, as well as certain other gas related costs, from its customers by means of a separate charge on the customer's bill. Laclede can change the amount of that PGA charge several times throughout the year to reflect changes in the amount it must pay to purchase and transport natural gas over the interstate pipelines to serve its customers. Laclede's PGA charges are subject to an Actual Cost Adjustment (ACA) by which Staff reviews the company's gas purchases for prudence and adjusts the company's rates to ensure those gas costs are simply passed through to customers dollar for dollar. Roughly 75 percent of the costs included in a customer's bill are related to gas costs and thus are flowed through the PGA.⁴

Laclede recovers its non-gas related costs through base rates and those costs are not passed through the PGA mechanism. Base rates are designed to allow the company to

³ Buck Direct, Ex. 3, Page 3, Lines 5-20.

⁴ Cline Direct, Ex. 1, Page 4, Lines 12-14.

recover its investment, as well as operating and maintenance costs it incurs to deliver gas through its distribution system to a customer's home or business.⁵ Unlike PGA rates, Laclede can change its base rates only by filing a rate case.

Currently, Laclede recovers its bad debt expense through its base rates. However, Laclede's proposed tariff would allow it to recover a portion of its bad debt expense through the PGA mechanism. To justify this change, Laclede claims a portion of its bad debt expense is really a gas cost and would include that gas cost portion of its bad debt expense for recovery through the PGA mechanism. Since approximately 75 percent of a customer's bill is for recovery of gas costs, Laclede would assume that approximately 75 percent of its bad debt expense is related to its gas cost and would recover that 75 percent of its bad debt expense through the PGA rather than through base rates.

The recovery mechanism described in Laclede's tariff is, however, more complicated than would be necessary to simply ascribe 75 percent of bad debt expense to gas costs to be recovered through the PGA. The added complexity is necessary because Laclede is proposing this tariff change outside of a general rate case. In Laclede's last rate case, File No. GR-2007-0208, some amount was included in Laclede's base rates to reflect the company's bad debt expense. If Laclede were allowed to simply recover 75 percent of its bad debt expense through the PGA, it would double recover all, or at least a part of the amount of bad debt expense included in base rates in the last rate case.

In an attempt to get around that double recovery problem, Laclede would assume that \$8.1 million are already included in base rates for recovery of the gas cost portion of bad debt, and would track fluctuations above and below that amount for recovery or refund

⁵ Cline Direct, Ex. 1, Page 3, Lines 10-20.

through the PGA mechanism. However, Laclede's last rate case was resolved through a stipulation and agreement among the parties. That stipulation and agreement was a "black box" settlement in which the parties simply agreed upon an overall amount that Laclede should be able to recover, but did not reach an agreement on the amount of any specific component of that settlement amount. As a result, there was no specific level of bad debt included in that stipulation and agreement.⁶

Laclede's proposed tariff would allow it to recover a portion of its bad debt expense through the PGA mechanism on the assumption that such bad debt expense is a merely another aspect of the company's cost to purchase natural gas. However, bad debt expense is not a part of Laclede's cost to purchase gas. Laclede does not make a payment to anyone when it incurs bad debt, rather it merely makes an accounting entry to recognize a loss of revenue.⁷ An increase or decrease in Laclede's level of bad debt has no effect on the amount its wholesale gas suppliers charge Laclede for the natural gas it purchases.⁸ Simply put, bad debt is not a gas cost.⁹

This distinction is important because, as will be explained more fully in the Conclusions of Law section of this Report and Order, the only costs a gas utility can recover through the PGA are those costs over which the utility does not exercise substantial control. Laclede's current PGA tariff allows it to recover the commodity and related transportation costs it must incur to obtain the natural gas it supplies to its

⁶ Transcript, Page 44, Lines 20-25.

⁷ Transcript, Page 72, Lines 3-9.

⁸ Transcript, Page 77, Lines 3-12.

⁹ Solt Rebuttal, Ex. 8, Page 4, Line 19.

customers. When it incurs those gas costs, Laclede must pay the price established by a national and international market over which Laclede can exercise little or no control.¹⁰

In contrast, Laclede can exercise substantial influence over the level of bad debt expense it recognizes on its balance sheet by being more or less aggressive in its collection efforts.¹¹ For example, Laclede could be more aggressive in following through with disconnection of customers who fail to pay their bills.¹² Similarly, Laclede can use collection tools such as social security number identification to prevent customers from presenting a fraudulent identity to obtain service, customer security deposits, and can use collection agencies, to obtain payment of bills.¹³

Of course, Laclede cannot completely control the level of bad debt expense it must incur. The level of bad debt is also influenced by factors outside Laclede's control, such as natural gas prices, weather, levels of available energy assistance, and the general economy.¹⁴ Furthermore, Laclede's ability to aggressively collect bad debt is limited by Commission rules, such as the Cold Weather Rule, which are designed to allow consumers a greater ability to retain gas service, even when they are having difficulty paying their bills.¹⁵ Nevertheless, bad debt expense is of a different character than gas expenses that are currently passed through to customers under the PGA mechanism. The impact of that difference will be further discussed in the Conclusions of Law section.

¹⁰ Transcript, Page 60, Lines 1-5.

¹¹ Transcript, Page 42, Lines 2-5.

¹² Transcript, Pages 158-159, Lines 8-25, 1-2.

¹³ Kremer Rebuttal, Ex. 7, Page 5, Lines 3-13.

¹⁴ Cline Direct, Ex. 1, Page 5, Lines 7-20.

¹⁵ Kremer Rebuttal, Ex. 7, Pages 5-6, Lines 16-22, 1-10. The applicable Commission rules are found in 4 CSR 240.13 (Chapter 13).

Conclusions of Law

1. Laclede is a gas corporation and a public utility, as those terms are defined by Section 386.020(18) and (43), RSMo Supp. 2008. As such, the Commission has jurisdiction over Laclede pursuant to Sections 386.250(1), RSMo 2000, and 393.140, RSMo 2000.

2. Section 393.150, RSMo 2000 allows the Commission to suspend a tariff filed by a gas utility for 120 days, plus six months, beyond the date the tariff would otherwise become effective.

3. Laclede's current PGA mechanism is established in the company's tariff. The Commission first approved a PGA tariff for Laclede in a report and order issued in 1962.¹⁶

4. Section 393.270.4, RSMo 2000 provides: [i]n determining the price to be charged for gas, electricity, or water the commission may consider all facts which in its judgment have any bearing upon a proper determination of the question"

5. Missouri's courts have interpreted the provision of Section 393.270(4) that allows the Commission to consider all facts in setting rates, as requiring the Commission to consider "all relevant factors" when setting rates.¹⁷

6. In the 1979 *Utility Consumers Council of Missouri* decision,¹⁸ the Missouri Supreme Court struck down a Commission decision that allowed electric utilities to recover their fuel costs through operation of a fuel adjustment clause. In doing so, the court held

¹⁶ *In the Matter of the Application of Laclede Gas Company to Put into Effect a Purchased Gas Adjustment Clause*, 10 MO P.S.C. (N.S.) 442 (1962).

¹⁷ *State ex rel. Utility Consumers Council of Missouri, Inc. v. Pub. Serv. Comm'n*, 585 S.W.2d 41, 56 (Mo banc 1979)

¹⁸ *Id.*

that a fuel adjustment clause would violate the statutory prohibition against single-issue ratemaking, in part because such a clause would alter rates without a consideration of “all relevant factors”.¹⁹

7. The fuel adjustment clause for electric utilities the *Utility Consumers Council of Missouri* court found to be contrary to Missouri statutes is similar to the PGA clause utilized by Missouri’s natural gas distribution companies, including Laclede. Not surprisingly, a few years after the *Utility Consumers Council of Missouri* decision, the legality of PGA clauses for gas utilities was also challenged.

8. In the *Midwest Gas Users’ Association* case,²⁰ the Court of Appeals distinguished the *Utility Consumers Council of Missouri* decision, finding that the nature of the gas costs passed to consumers under the PGA were fundamentally different from the electric costs that would have been passed to consumers of electricity under the rejected fuel adjustment clause.

9. In finding that the challenged PGA clause did not constitute improper single-issue ratemaking, the *Midwest Gas Users’ Association* court held that the cost of purchasing natural gas could be treated differently because natural gas is “a natural resource, not a product which must be produced with labor and materials.”²¹ As such, the gas utility cannot exercise meaningful control over the price it must pay for natural gas, and cannot offset those costs by implementing cost savings in other areas. In that way, the *Midwest Gas Users’ Association* court found that natural gas costs passed through to

¹⁹ Subsequently, in 2005, the General Assembly passed legislation that allowed electric utilities an opportunity to implement fuel adjustment clauses. That legislation is codified at Section 386.266, RSMo Supp. 2008.

²⁰ *State ex rel. Midwest Gas Users’ Association v. Pub. Serv. Comm’n*, 976 S.W.2d 470 (Mo. App. W.D. 1998)

²¹ *Id.* at 480.

customers under the PGA were akin to tax costs the Missouri Supreme Court allowed to be passed through to customers in a 1960 case, *Hotel Continental v. Burton*.²² Thus, if Laclede's bad debt costs are to be passed through the PGA they must be similar to the natural gas costs that were approved in *Midwest Gas Users' Association*, and not similar to the costs rejected in *Utility Consumers Council of Missouri*.

10. As the Commission explained in the findings of fact section of this report and order, Laclede's bad debt expense, which it seeks to recover under its PGA clause, is not a gas cost. Rather, Laclede can exercise substantial influence over the level of bad debt expense it recognizes on its balance sheet by being more or less aggressive in its collection efforts, subject to the limitations imposed by the Commission's regulations. In that way, Laclede's bad debt expense is more similar to the costs rejected in *Utility Consumers Council of Missouri*. As such, inclusion of those costs in the PGA is forbidden as single-issue ratemaking by the holding of the Supreme Court in *Utility Consumers Council of Missouri*.

Decision

Based on its findings of fact and conclusions of law, the Commission finds that Laclede's tariff that would allow Laclede to recover the portion of its bad debt expense ascribed to gas costs through its PGA clause is unlawful in that it would allow Laclede to recover bad debt expenses in a manner that would constitute improper single-issue ratemaking forbidden by the holding of the Missouri Supreme Court in *Utility Consumers Council of Missouri*. Furthermore, the Commission finds that Laclede's bad debt expense is not a gas cost such as can be recovered through the PGA under the exception to the

²² 334 S.W. 2d 75 (Mo. 1960).

single-issue ratemaking prohibition recognized by the *Midwest Gas Users' Association* decision. Therefore, the Commission must reject Laclede's tariff.

Staff and Public Counsel also challenged Laclede's tariff by arguing that even if bad debt expenses could otherwise be recovered through the PGA, the company could not modify its PGA tariff outside of a general rate case, and that even if it were legally able to recover its bad debt expense through its PGA tariff, it would be bad public policy to allow Laclede to do so. Because the Commission has found that Laclede cannot legally recover its bad debt expense through its PGA tariff, it will not reach the other proposed grounds for rejecting the tariff.

IT IS ORDERED THAT:

1. The tariff sheets filed by Laclede Gas Company on July 9, 2008, and assigned tariff number JG-2009-0033, are rejected.
2. This report and order shall become effective on April 25, 2009.

BY THE COMMISSION



Colleen M. Dale
Secretary

(S E A L)

Clayton, Chm., Murray, Davis, Jarrett,
and Gunn, CC., concur.

Dated at Jefferson City, Missouri,
on this 15th day of April, 2009.