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LACLEDE GAS COMPANY
MISSOURI GAS ENERGY

GR-2017-0215
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DIRECT TESTIMONY

OF

C. ERIC LOBSER

APRIL 2017

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DIRECT TESTIMONY OF C. ERIC LOBSER

Q. **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A. My name is C. Eric Lobser and my business address is 700 Market St., St. Louis, Missouri, 63101.

Q. **WHAT IS YOUR PRESENT POSITION?**

A. I am presently employed as Vice President - Regulatory & Governmental Affairs at Spire Inc.

Q. **PLEASE STATE HOW LONG YOU HAVE HELD YOUR POSITION AND BRIEFLY DESCRIBE YOUR RESPONSIBILITIES.**

A. I was elected to my present position in December 2014. In this position, I am responsible for directing and managing the state level regulatory and legislative work for Spire's five utilities in three states, including Laclede Gas Company's ("Laclede" or the "Company") two operating units in Missouri, Laclede Gas ("LAC") and Missouri Gas Energy ("MGE"). As part of my duties, I am responsible for the research, assessment and development of regulatory and legislative enhancements that will position our utilities to better meet our customers' needs and shareholders' expectations. I am also responsible for overseeing our efforts to plan and pursue implementation of those enhancements in the applicable regulatory or legislative forum.

Q. **WHAT WAS YOUR EXPERIENCE WITH LACLEDE PRIOR TO ASSUMING YOUR CURRENT POSITION?**

Q. I joined Laclede in 1991 as a Budget Analyst in the Finance area and was chosen to handle similar duties for operations departments as a Senior Administrative Assistant in the Administrative Services department in 1992. After the completion of the next budget cycle in late 1993 I moved to Customer Accounting to supervise the correction bill issues and billing of our large volume commercial and industrial customers and became Assistant to the Manager before moving on to the Treasury department in 1999 as a Senior Treasury Analyst. I served in that position until August 2001, when I was promoted into the newly created Planning Department, where I supported business planning, strategy development and analytical support for internal improvement projects, before advancing to the position of Managing Director – Strategic Planning and Corporate Development. In that position, I was responsible for researching, evaluating and pursuing business opportunities in line with Spire's short and long-term strategic business development objectives. My duties included conducting natural gas industry analysis, from "wellhead to burner tip", target assessments and financial modeling throughout the bid process, as well as due diligence and deal negotiation.

Q. WHAT IS YOUR EDUCATIONAL BACKGROUND?

A. I graduated from Boston College in 1990 with a Bachelor of Science Degree in Finance. I received my Masters in Business Administration from the University of Missouri – St. Louis, in 2000.

Q. **HAVE YOU PREVIOUSLY FILED TESTIMONY BEFORE THIS COMMISSION?**

A. No. I have not.

I. PURPOSE AND OVERVIEW OF TESTIMONY

Q. **WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A. The purpose of my testimony is to provide an overview of the main ratemaking and regulatory policy initiatives Laclede is asking the Commission to approve in these cases, consistent with the overall policy considerations discussed by Laclede witness Lindsey in his direct testimony. Specifically, I will address Laclede's proposals for: 1) further integrating its two Missouri operating units to increase consistency of treatment and reduce costs, both of which benefit customers, 2) enhancing opportunities for economic development, growing the customer base and further spreading costs for customers, and 3) enhancing regulatory structures to better align the interests of customers and the Company in areas such as costs and customer service.

As I and other Laclede witnesses will discuss, the continued integration of LAC and MGE through the application of more consistent regulatory practices provides our customers similar treatment regardless of service territory. It also allows us to further develop our shared services and business platforms to advance customer service and capture cost efficiencies. More consistent and effective processes results in tasks being performed in less time, with fewer resources, and better outcomes.

Growth has been one of the hallmarks of Spire over the last several years, creating significant scale and providing the opportunity for the benefits noted above. We believe this strategy should be extended locally to organic growth and economic development for the benefit of Missouri customers and the State. Expanded efforts to grow the customer base can provide additional benefits to current customers, by further spreading costs, and to new customers, by delivering them the benefits of an energy that is favorably priced, safe, extremely reliable, and environmentally friendly. Natural gas not only provides residential users with a superior way to heat their home and cook their meals, but can also be critical to attracting energy intensive business operations, and the jobs that accompany them.

Enhanced structures allow regulators to create an environment where the Company has the tools to better meet the needs of its customers. As I will discuss, these include ratemaking structures that better protect both customers and the Company from the financial effects of uncontrollable factors such as weather, and that provide more timely recognition of the costs incurred to provide service, thus enabling necessary and beneficial investment. They also include performance-based structures to hold management more accountable for the quality and cost of utility services, and synergy sharing concepts to promote further beneficial growth. All of these enhancements would work together to provide customers with benefits from better service and lower costs than would otherwise be the case under current structures.

II. BENEFITS OF FURTHER INTEGRATION

Q. HAS THE COMMISSION SEEN THE BENEFIT OF, AND SHOWN AN INTEREST IN, INTEGRATING THE OPERATING UNITS OF OTHER UTILITIES WITHIN THE STATE?

A. Yes. On September 28, 2016, the Commission approved the consolidation of Missouri Public Service and St. Joseph Light and Power rate districts into a common KCP&L Greater Missouri Operations Company rate structure in Case No. ER-2016-0156. Similarly, in an order effective June 25, 2016 in Case No. WR-2015-0301 the Commission approved the consolidation of Missouri American Water Company's rate districts from 19 districts to 3 with a goal of moving towards a state-wide pricing method.

Q. HOW WOULD LAC AND MGE CUSTOMERS BENEFIT FROM BEING TREATED ALIKE?

A. For the most part, Laclede customers, whether in eastern Missouri or western Missouri, are served under similar general terms and conditions, but some of the legacy tariffs and rates are naturally different due to different ownership and history. We believe we should treat our Missouri customers as consistently as possible. As part of the further integration of LAC and MGE, we are proposing changes to each of those operating unit's tariffs. Having uniform regulatory treatment permits employees at the respective operating units to undertake the same operational practices, which further enhances the quality of performance, supervision, compliance and governance. For the regulator, greater consistency in tariffs and practices followed by both operating units can also allow Commission Staff and OPC to more effectively and efficiently monitor and evaluate the utility's compliance with regulatory standards and requirements, as they no longer have to acquire knowledge of and apply a number of different and even inconsistent regulatory requirements. Customers, of course, are the ultimate beneficiaries of the more consistent, effective and efficient process created by these efforts.

Q. WHAT REGULATORY AND OPERATIONAL PRACTICES IS LACLEDE PROPOSING TO FURTHER INTEGRATE IN THIS CASE?

A. We have a number of proposals designed to bring greater conformity of regulatory treatment between the utilities. These generally relate to tariffs and rate designs of the two utilities, and several that address specific additional areas we've identified that can provide benefits to customers. Next, I will address a proposal to bring greater consistency in how the respective Purchased Gas Adjustment/Actual Cost Adjustment provisions work for the two operating units, which can provide benefits of reduced gas supply costs for the customer by enhancing the incentive structures. Finally, I will discuss the benefits our shared services model provides to our customers by providing Laclede with necessary services in an effective and efficient manner, thus helping to keep costs and rates reasonable.

a) More Consistent Tariffs and Rate Design

Q. HAS SOME PROGRESS ALREADY BEEN MADE IN ACHIEVING THESE GOALS?

A. Yes. With the assistance of the Commission, LAC and MGE were able to adopt and apply the same operational and regulatory practices in some areas in 2015, including budget billing, main extension policies, and procedures for estimating bills. Most of these changes were driven by the successful integration of MGE from its dated customer service information system to a common platform with LAC, on the new Customer Care & Billing system. In addition to these initiatives, LAC and MGE have also adopted consistent approaches to their ISRS filings, which has permitted both filings to be reviewed at the same time and any disputes addressed in a single hearing rather than multiple hearings.

Q. IN GENERAL, WHAT ARE SOME CHANGES LACLEDE IS PROPOSING TO MAKE LAC AND MGE TARIFFS AND RATE DESIGNS MORE CONSISTENT?

A. As described by Laclede witness Weitzel, we are reviewing all of the general terms and conditions as well as rate designs to make them as straight-forward and consistent as possible. For the terms and conditions, we are using Chapter 13 requirements and best practices from our two utilities as guideposts for this integration. For the rate designs, we are leveraging the use of a Revenue Stabilization Mechanism (RSM) to simplify the rate design, create more consistency, and reduce the reliance upon a high customer charge.

The RSM has a number of customer benefits I will address in a later section on regulatory enhancements. There are also a number of specific areas Laclede has changed to bring consistency of regulatory treatment to its customers.

i) <u>Consistent Treatment of Bill Proration Practices</u>

Q. WHAT IS ONE OF THOSE AREAS?

A. Proration of bills that cover a period less than 26 days or more than 35 days.

Q. IS THIS CHANGE RELATED TO AN AGREEMENT BETWEEN MGE AND STAFF?

A. Yes. This is an issue that arose around the time of the update of MGE's billing system to the modern, more capable system at LAC. Currently, MGE has language in its tariffs explicitly stating that billing periods of less than 26 days ("short bills") will be prorated, but is silent on billing periods greater than 35 days ("long bills"). For its part, LAC's tariff is silent on proration for both short and long bills, but it prorates both long and short bills. Historically, the Commission has favored prorating both short and long billing periods, which makes perfect sense. Pursuant to a Stipulation and Agreement between Staff and MGE approved by the Commission in Case No. GC-2016-0149, MGE agreed that in its next general rate case it would file tariffs amending its tariff rule 7.02 (Sheet R-47) to clarify and confirm that it will prorate all monthly fixed charges on both short and long billing periods. The Stipulation and Agreement also stated that LAC would be permitted to file similar conforming tariff provisions. Such a balanced approach is a fair way of ensuring appropriate cost recovery for billing periods shorter or longer than the normal number of days in a billing cycle.

Q. HAS LACLEDE FILED SUCH CLARIFYING TARIFF PROVISIONS FOR BOTH ITS MGE AND LAC OPERATING UNITS?

A. Yes. Laclede witness Weitzel proposes in his testimony a single set of tariffed rules for MGE and LAC that includes language clarifying that both short and long billing periods will be prorated.

ii) <u>Consistent Treatment of School Transportation Program</u>

Q. **IS THERE ANOTHER AREA IN WHICH MGE AGREED WITH STAFF TO MAKE CHANGES TO MAKE REGULATORY TREATMENT MORE CONSISTENT**?

A. Yes. In recent MGE ACA proceedings, Staff raised concerns regarding the way in which MGE handles imbalances between nominations and deliveries to schools participating in the school transportation program ("STP"). In essence, the Staff has stated a desire to have any imbalances recognized and accounted for on a monthly basis while MGE has taken the position that such a process would require the installation of electronic metering at each school – something the Company cannot charge to schools or to other customers under the statute governing such programs. MGE and Staff agreed to increase the balancing fee charged by MGE in connection with the program and committed to revisit the issue in MGE's next rate case. LAC does not have similar issues because it is able to obtain daily reads from its meters and has moved its school transportation accounts to a calendar month cycle, to coincide with the interstate pipeline month, in order to make balancing more feasible.

Q. **DID MGE AGREE TO PROVIDE CERTAIN INFORMATION TO FACILITATE AN INFORMED EVALUATION OF THIS ISSUE IN THE RATE CASE?**

A. Yes. We agreed to provide a variety of information regarding the costs and potential benefits of installing and operating electronic meter reading equipment at each school so that each school's nominations and deliveries could be determined and reconciled on a monthly basis. Laclede witness Noack provides and explains this information as part of his direct testimony. We also agreed to provide our perspective on whether these costs and potential benefits justify the installation of such equipment. As Mr. Noack also explains in his direct testimony, while we believe there are benefits in providing greater consistency in the treatment of Missouri schools, whether on the eastern side of the state or the western side, and in providing them with sufficient, timely information to help their marketers balance gas supply needs so as not to inadvertently utilize gas supply or storage assets of sales customers, we are limited by statute in how we can assess the related expenditures for doing so. Given this constraint and the absence of any historical evidence suggesting that the schools have nominated their transportation volumes and created imbalances in a way that has adversely affected sales customers, there does not seem to be a sufficient justification for making such an expenditure at this time. We therefore believe other steps can and should be taken to address this concern with a view towards achieving greater consistency if and when there is a system wide change in how meter readings are collected. Nevertheless, we look forward to discussing the issue with the other stakeholders as this case progresses.

iii) <u>Consistent Treatment of Landlord/Tenant Billing Practices</u>

Q. IS LACLEDE PROPOSING TO RECONCILE OTHER AREAS NOT RELATED TO AN AGREEMENT?

A. Yes. Another item relates to how the two operating units assess utility charges when a rental unit is temporarily empty because the tenant has moved out and it has not yet been leased to another tenant. In LAC's service area, the landlord continues to be billed at the residential rate, including both the residential customer charge and the residential usage charges. At MGE, however, tariffs require that we bill the landlord at the higher rates for general service customers when the premise is vacant, and revert back to residential rates when it is reoccupied.

Q. HAS THIS PRACTICE OF CHARGING THE LANDLORD HIGHER RATES WHEN THE PREMISES IS TEMPORARILY VACANT RESULTED IN A FAIR AMOUNT OF CUSTOMER DISSATIFACTION?

A. That would be an understatement. MGE has received numerous complaints over the years from landlords, who believe it is not fair to charge them a higher rate simply to continue gas service to a property that is used only for residential purposes. The Office of the Public Counsel has also raised concerns in the past regarding the appropriateness of such a practice.

Q. WHAT KIND OF COST OF SERVICE ADJUSTMENT IS NECESSARY TO ACHIEVE THIS RESULT?

A. Charging landlords at the residential rate during periods when there is a vacancy will reduce the margin collected from those customers by roughly $2.1 million, based on an analysis of test year billings. To make up this deficiency, MGE is proposing that this amount be reallocated to the residential class and recovered in residential rates.

iv) <u>Consistent Treatment of One-Time Bill Payment Fees</u>

Q. WHAT IS ANOTHER REGULATORY/OPERATIONAL PRACTICE THAT LACLEDE HAS PROPOSED BE APPLIED ACROSS BOTH OPERATING UNITS THAT WOULD PROVIDE BENEFITS TO CUSTOMERS?

A. MGE currently embeds in its overall cost of service the credit card fees charged by third parties to accept and process one-time payments over the phone from customers on their utility bills. As a result, MGE customers do not have to pay an additional charge when they make such payments. In contrast, LAC charges its customers a fee to pay their bill by credit card – something increasingly rare to find in the non-regulated world. I would note that Laclede has worked very hard to reduce the level of these fees and help ensure its customers pay a charge that compares favorably to those at other utilities in other area. This case provides an opportunity; however, to create consistency and eliminate the separate fee for LAC customers, just as it has been eliminated for MGE's customers, by including an allowance in rates for that purpose.

Q. ASIDE FROM CONSISTENCY, ARE THERE OTHER REASONS FOR ELIMINATING THIS SEPARATE FEE?

A. Yes. Whenever possible, I think it is important for Laclede to offer their customers the kind and variety of service options that customers in a fully competitive market expect to receive. Like so many other businesses today that accept credit card payments over the phone without charging a separate fee, I think LAC needs to join MGE in making that option available to its customers.

Q. ARE THERE OTHER AREAS WHERE THE FEES CAN BE MADE MORE CONSISTENT BETWEEN LGC AND MGE?

A. Yes, there are a number of service fees that need updated costs, and at the same time it would make sense to make those fees as consistent as possible given the level of integration between the two utilities. This will be discussed further by Laclede witness Weitzel, but essentially we are proposing to use the same fees across Laclede's operating units, which are set at reasonable levels to provide benefits to those customers.

b) <u>Further Integrated, Enhanced and Consistent Customer Programs</u>

Q. IS LACLEDE PROPOSING ANY INTEGRATION-RELATED CHANGES TO ITS PROGRAMS FOR HELPING CUSTOMERS MAINTAIN UTILITY SERVICE AND USE THAT SERVICE MORE EFFICIENTLY?

A. Yes. Our main goal for proposing such changes is to make all of the related programs more successful in serving customer needs and providing the energy efficiency support and energy assistance funding to customers in need, as intended.

Q. WHICH CUSTOMER PROGRAMS ARE YOU REFERENCING?

A. These programs include energy efficiency programs that are available to all customers who want to use natural gas in a more efficient way and save on their utility bills in the process. The other programs are aimed at helping our most vulnerable customers, and include low-income weatherization, our red-tag, and energy affordability programs. The first two low income programs are currently offered by LAC and MGE, while the energy affordability program is currently offered only by LAC.

Q. WHAT CHANGE IS LACLEDE PROPOSING TO THESE PROGRAMS?

A. First, we are proposing that all of these programs be offered on a consistent basis throughout the service territories of both LAC and MGE. To that end, we are consolidating the programs and incorporating them in a single set of Standard Rules and Regulations that would be equally applicable to both LAC and MGE.

Q. HOW WOULD CUSTOMERS BENEFIT FROM THIS CONSOLIDATION OF PROGRAMS?

A. It will assist us in providing information in a more comprehensive manner and through more unified messaging. This, in turn, should increase both the awareness and effectiveness of the program offerings, thus affording customers enhanced access to the resources necessary to better manage their energy consumption, pay outstanding bills, and have access to qualified repair programs for critical appliances they depend upon. The bundling of these efforts would help customers reduce usage, lower their bills, and stay more current on their accounts. At the same time, it would better ensure customers have properly functioning, safe, reliable and efficient appliances for heating their home, water and meals. Retaining customers and supporting safe, energy efficiency measures benefits all customers.

Q. HAS LACLEDE ALREADY MADE PROGRESS ON CONSOLIDATING THESE PROGRAM OFFERINGS?

A. Yes. LAC and MGE have already made significant progress in combining and coordinating the governance of their energy efficiency programs by having the energy efficiency collaborative discuss and make recommendations for both programs on a joint basis. Combining the cost and governance of these other programs, as well as other related programs proposed to be offered in the future, makes sense as well, and the tariffs we have submitted in this case reflect that approach. Laclede witness Weitzel goes into further detail about these integration efforts and proposed enhancements. We believe the cost of these customer programs should be combined and appropriately allocated to both operating units based on where program resources are applied.

Q. ARE THERE ALSO CUSTOMER SERVICE PRACTICES LACLEDE IS PROPOSING TO MAKE MORE UNIFORM?

A. Yes. The first relates to those tariff provisions governing Laclede's low-income energy affordability programs. Currently, the LAC operating unit has a low-income program in place, but it has been a number of years since the MGE operating unit offered such a program.

Q. IS THERE A VALID REASON FOR OFFERING SUCH A PROGRAM IN ONE SERVICE TERRITORY BUT NOT THE OTHER?

A. No there is not. Unfortunately, we have vulnerable customers with limited resources in both service territories who could benefit from such a program and there is really no rationale for offering such an assistance program in one area but not the other. I should note that since it acquired MGE, Laclede has pursued a number of initiatives to help its low income customers obtain energy assistance, including the introduction of its Dollar-Help Program in MGE's service territory, an initiative that has significantly increased the level of contributions provided by MGE's customers to help others with their energy bills. We have also been strong supporters of efforts by Community Action Agencies and others to obtain State UtiliCare funding and federal LIHEAP funding. The reintroduction of an energy assistance program in the MGE service area would be a helpful compliment to these initiatives, particularly in light of some of the concerns as to whether the federal budget will provide for energy assistance funding for LIHEAP.

Q. ASIDE FROM REINTRODUCING AN ENERGY ASSISTANCE PROGRAM IN THE MGE SERVICE AREA, IS LACLEDE PROPOSING ANY CHANGES TO THESE PROGRAMS?

A. Yes. As discussed in greater detail by Laclede witness Weitzel, Laclede is also proposing to simplify the energy affordability program. This would be achieved by providing a year round credit to the fixed monthly charge paid by such customers, similar to a program recently approved for Empire District Electric Co., instead of having a series of usage-related credits which vary depending on the customer's income level. This should make the program easier to administer by our Community Action and other social agency partners in addition to making it easier for customers to retain service during non-winter periods. We are also proposing to provide additional support for the Community Action Agencies who help administer the programs so they can both identify low-income customers who are more likely to succeed in the program, as well as provide more comprehensive assistance to such customers on the steps necessary to be successful. We are also proposing that the arrearage repayment portion of the program be simplified and expanded to help customers restore service by facilitating arrearage payments necessary to cover the gap between LIHEAP grants received by a customer and what the customer requires to restore service under the Cold Weather Rule. We believe these modifications are essential to ensuring the programs achieve their intended goals.

Q. IS THE COMPANY PROPOSING CHANGES TO THE RED-TAG PROGRAM?

A. Yes. Based on the input we have received from our Community Action Partners, we are proposing the maximum amount provided to any single qualifying customer for repairs necessary to resume safe operations be increased from $450 to $1,000, with limitations per each “red-tagged” item. We believe this change will permit more customers to effectively address appliance repairs and restore service, while reducing the likelihood customers will either operate equipment in an unsafe manner or use other heating equipment that can pose a significant safety risk and is less energy efficient.

c) <u>More Consistent and Enhanced PGA Structures</u>

Q. YOU MENTIONED LACLEDE IS ALSO PROPOSING TO BRING GREATER CONSISTENCY TO THE TERMS AND OPERATION OF MGE’S AND LAC’S RESPECTIVE PGA AND ACA CLAUSES. WHAT RECONCILING MODIFICATIONS IS LACLEDE PROPOSING?

A. As discussed in greater detail by Laclede witness Weitzel, the Company has made a number of proposals in this case to update and bring greater consistency to how the respective PGA/ACA Clauses of MGE and LAC operate. The goal of these changes is to make them as consistent as possible, as a likely initial first step in eventually fully integrating their overall rates. Such a change in the future would provide our Missouri customers, whether MGE or LAC, a more diverse, robust gas supply portfolio with beneficial access to certain assets and pricing across the state. In the meantime, consistency between the two would also be administratively less burdensome for the Company and the Commission than the current distinct processes that occur at different times of the year. Several of these modifications are consistency changes, while others proposals are enhancements to produce more beneficial outcomes.

<u>i) Consistent Treatment of the PGA and ACA</u>

Q. PLEASE BRIEFLY DISCUSS LACLEDE’S PROPOSAL RELATING TO CREATING A MORE CONSISTENT PGA AND ACA.

A. One simple change that can be made is to use the same review periods for both, by changing MGE's program date to LAC's date, which coincides with the fiscal year as well as the beginning of the heating season. Another relatively small but meaningful fix would be to update the standard volumes used in the calculation with those approved in each general rate proceeding to update to more accurate, current levels and reduce the systematic mismatch of volumes used in the PGA/ACA rate calculation and the determinants approved in the most recent general rate proceeding. A couple other changes that would create similar structures between LAC and MGE are enabled by the Revenue Stabilization Mechanism and rate design changes noted previously. Currently MGE utilizes a single PGA rate, but LAC has a more complex approach with multiple PGA rates by both rate class and rate block due to its weather mitigated rate design. The changes proposed in this case would have LAC adopt the more straight-forward approach used by MGE, with adjustments as necessary for rates such as its Interruptible sales class, creating a more simple structure with better transparency because it's easier to understand, which improves the Commission's ability to administer and review it.

ii) Consistent Treatment of Natural Gas Storage Inventory Costs

Q. WHAT OTHER MODIFICATIONS ARE BEING PROPOSED BY LACLEDE TO BRING GREATER CONSISTENCY TO THE PGA/ACA PROVISIONS OF MGE AND LAC?

A. Currently, MGE recovers the cost of maintaining its gas storage inventories in its base distribution rates. LAC, on the other hand, recovers these gas inventory costs through its PGA/ACA mechanism. We are proposing LAC take the same approach as MGE, which is more standard in the industry and helps remove another area of inconsistency between the utilities. We have accordingly included the necessary adjustments to LAC's PGA/ACA balances and cost of service to reflect the addition of the average storage inventory costs in rate base, consistent with the approach taken for MGE. These adjustments are discussed and sponsored by Laclede witness Keathley in his direct testimony.

Q. YOU MENTIONED "ENHANCEMENTS TO PRODUCE MORE BENEFICIAL OUTCOMES". WHAT OTHER CHANGES ARE BEING PROPOSED?

A. Yes, next I will address a couple changes to our PGA/ACA tariffs to better reflect current market conditions, as well as enhance the Company's opportunities to create beneficial outcomes for customers through lower commodity costs, which account for over half of their bill.

iii) <u>Enhancements to Off-System Sales and Capacity Release</u>

Q. PLEASE DISCUSS LACLEDE'S PROPOSAL RELATING TO OFF-SYSTEM SALES AND CAPACITY RELEASES.

A. Currently both MGE and LAC have provisions in their PGA clauses that provide for a sharing of the net margins associated with the sale of gas or the release of pipeline capacity by the utility to customers located off their distribution systems. These sales are made by optimizing underutilized pipeline capacity and/or gas supply entitlements that are temporarily unneeded to serve traditional, on-system customers receiving regulated natural gas service.

Q. ARE THERE DIFFERENCES BETWEEN MGE'S AND LAC'S OFF-SYSTEM SALE/CAPACITY RELEASE PROVISONS?

A. Yes. Both sharing structures permit the utility to retain a modest but increasing share of the net margins achieved from such transactions as the level of those net margins increase. This sharing percentage begins at 85% for the customer and 15% for the utility at the lower tier of sales and caps out at 30% for the utility with still 70% going to customers even at the highest tier of sales. The effective average for both over the last several years has been about 24%. The primary difference between the LAC and MGE sharing structures is that the margin thresholds for MGE are lower than LAC's based on lower level of sales MGE has historically achieved, based principally on market forces. Such market forces can also meaningfully change the future opportunities that will be available to LAC and MGE to achieve the margins necessary reach the arbitrary levels of the current sharing mechanism.

Q. WHAT CHANGES TO THESE PROVISIONS IS LACLEDE PROPOSING IN THIS CASE?

A. First, we are proposing both MGE and LAC operate under one sharing mechanism, rather than two, whether the PGA is combined or not. Given the fact that the same gas supply personnel are responsible for making off-system sales and releasing capacity for both MGE and LAC and the degree to which the growing abundance of natural gas supplies has moderated the differential in capacity values between MGE and LAC, we believe that combining these efforts under a single sharing mechanism makes sense. Second, we are proposing that the margin thresholds for the sharing tiers in the mechanism be eliminated in favor of a single sharing percentage of 25%, which would apply equally to all off-system sales and capacity releases in the future. The proposed percentage is based on the historic effective rate and its adoption would eliminate the artificial and arbitrary levels currently in place. Laclede witness Weitzel discusses these modifications and the reasons that warrant their adoption in greater detail in his direct testimony.

Q. HOW WOULD THE MARGINS REALIZED FOR CUSTOMERS UNDER THE NEW SHARING MECHANISM BE ALLOCATED BETWEEN MGE AND LAC CUSTOMERS?

A. Over a similar timeframe, LAC has earned the majority of these incentives, and we would propose an allocation approximately reflecting such historic levels. Going forward, if the Commission deems it appropriate, an adjustment could be made to reflect any systematic change in margin levels achieved by each operating unit's gas supply assets.

iv) <u>Enhancements to the Gas Supply Incentive Plan</u>

Q. WHAT IS THE COMPANY PROPOSING IN TERMS OF HOW LACLEDE'S GAS SUPPLY INCENTIVE PLAN SHOULD BE TREATED?

A. Both LAC and MGE have had a gas supply incentive plan ("GSIP") in effect in the past. In fact, MGE was the first Missouri local distribution company to have such a plan approved. Today, however, only LAC has a GSIP in effect, and it is rarely triggered because of changing market conditions and price levels, with limitations in the plan we believe should be changed.

Q. DOES THE COMPANY BELIEVE LAC'S GSIP SHOULD BE APPLIED CONSISTENTLY TO BOTH OPERATING UNITS?

A. Yes. The fundamental rationale for implementing and maintaining such an incentive plan – namely to encourage superior performance in the cost-effective acquisition of gas supplies – is equally applicable to the gas procurement activities of both LAC and MGE.

Q. IS LACLEDE PROPOSING ANY CHANGES TO THE GSIP IN THIS PROCEEDING?

A. Yes. We are proposing four substantive changes. Similar to the changes we are proposing to simplify the off-system sales/capacity release mechanism, we are recommending that the gas cost tiers governing when the GISP triggers a sharing of savings be eliminated in favor of a single sharing mechanism using the current sharing percentage of 10%. This modification simply recognizes that it is important to achieve reductions in the cost of gas regardless of whether gas prices are historically low or historically high and through whichever element of gas supply presents the best opportunity for savings. Second, we are removing hedging impacts from the calculation of savings, since hedging is focused primarily on achieving protection from price volatility rather than securing the lowest possible price. Third, we are proposing to add a provision that provides incentives for achieving future negotiated discounts or savings in the cost of third-party pipeline capacity. Again, Laclede witness Weitzel discusses the details and rationale for these modifications in his direct testimony.

v) Enhancements to Research & Development Funding

Q. IS LACLEDE ALSO PROPOSING TO IMPLEMENT R&D FUNDING IN ITS PGA/ACA THAT SUPPORTS ENERGY EFFICIENCY AND GAS SAFETY?

A. Yes. We are proposing the Commission approve an allowance in rates to support an ongoing contribution by Laclede, on behalf of both operating units, to the Gas Technology Institute ("GTI").

Q. **WHAT IS GTI AND WHAT BENEFITS DOES IT PROVIDE TO THE COMPANY'S CUSTOMERS THAT WOULD WARRANT THE APPROVAL OF SUCH AN ALLOWANCE?**

A. GTI was formed in 2000 by combining two major research and technology firms which had served the natural gas industry for many years. One was the Institute of Gas Technology which since 1941 had assisted the natural gas industry in training graduate engineers. The other was the Gas Research Institute which was founded in 1976 in response to the Federal Power Commission encouraging increased gas research and development. Today, GTI provides a wide variety of services to the natural gas industry, including research and development of new technologies impacting all aspects of the natural gas supply and distribution chain, analytical and technical support, program management and training. Examples of innovations developed through GTI that have directly benefitted natural gas customers, include more energy efficient, lower cost and environmentally-friendly appliance innovations for both business and low-income residential applications, tools and techniques to support pipeline integrity, emissions / leak detection and third-party damage prevention.

Q. **HAVE NATURAL GAS CONSUMERS PREVIOUSLY FUNDED SUCH EFFORTS THROUGH THEIR RATES FOR NATURAL GAS SERVICES?**

A. Yes. For many years, the customers of LAC, MGE and other local distribution companies funded such activities, at least indirectly, by paying for GRI assessments included in the rates charged by interstate pipelines. That practice eventually ended when the pipelines were taken out of the merchant function as a result of FERC Order 436. But the principle that natural gas consumers benefit from the kind of work done by GTI –

and that it is therefore appropriate to recover the cost of such work from those consumers – has been well established. We believe GTI funding is a more cost effective and efficient approach to developing very meaningful enhancements to energy efficiency and environmental benefits than LAC and MGE can pursue on their own.

Q. **HAVE COMMISSIONS IN OTHER STATES AUTHORIZED THE INCLUSION OF GTI CONTRIBUTIONS IN THE RATES CHARGED BY THE GAS UTILITIES THEY REGULATE?**

A. As of the end of 2016, 30 utility commissions had authorized the inclusion of GTI contributions in rates for utilities. We believe that this Commission should as well and propose such modest costs be included in the PGA/ACA for LAC and MGE, and believe it would be a great complement to our customer-specific efforts related to standing energy efficiency programs in base rates.

d) Benefits of Further Integration through our Shared Services Model

Q. **WHY IS IT IMPORTANT TO FURTHER INTEGRATE THE OPERATIONS OF LACLEDE'S TWO OPERATING UNITS?**

A. It has now been three and a half years since Laclede completed its acquisition of MGE, but the full implementation of Spire's shared services model has only been in place for the last year and a half and is still evolving, adapting and improving with three sibling utilities added to the family. One of the major benefits of an acquisition of this nature is the opportunity it provides to compare and contrast the various regulatory and operational practices that affect how service is provided to customers and adopt those that are most conducive to providing quality customer service in an efficient way. An acquisition also provides an opportunity to integrate and share administrative costs over a greater customer base so that customers can share in the lower per-customer cost of these business functions.

Q. ARE THERE OTHER BENEFITS FROM ADOPTING BEST PRACTICES IN REGULATORY AND OPERATIONAL ACTIVITIES AND APPLYING THEM CONSISTENTLY ACROSS BOTH OPERATING UNITS?

A. Yes. Such an approach produces tangible benefits for the utility, its customers and the regulator. For the utility, swapping ideas between utilities better enables continual improvement efforts, and having a single, robust and capable technology platform better enables our shared services to work together and have access to more robust and capable technology platforms.

Q. **WHAT ARE SOME OF THE OTHER BENEFITS OF SHARED SERVICES?**

A. Growth and added scale can be very beneficial to an organization and help spread costs, but only to the extent they can effectively and efficiently share resources, knowledge, capabilities, systems, platforms, facilities and services. As witness Flaherty demonstrates in his testimony, Spire's shared services provide direct benefits to Laclede and its customers in terms of lower costs and more reliable operations. Providing these services from a "center-led" model, such as Spire's, is inherently more efficient than distributing them among the operating companies. It reduces redundancies and provides knowledgeable, capable and efficient support in shared service functions that are complementary in nature to the operating company, who are active in managing the combined costs and performance results of this partnership. Based on the results of this study, absolute costs for shared service functions for Laclede have dropped significantly on an inflation-adjusted basis, and have also been meaningfully reduced even on a nominal basis since the acquisition of MGE and adoption of the shared service model.

Q. WHAT IS LACLEDE PROPOSING TO HELP INTEGRATE THE COST STRUCTURES OF LAC AND MGE?

A. Despite being owned by the same company and operating in the same state, MGE has a lower cost structure than LAC, and has further benefited from the acquisition. As noted above, since the acquisition by Laclede, there has been a significant reduction in O&M costs for MGE, particularly for shared services functions. Additionally, there has been a significant increase in investment in pipeline replacement at MGE, which has helped to also meaningfully reduce MGE's effective tax rate. Laclede is proposing to combine the assets and liabilities associated with MGE's and LAC's pension and post-retirement medical benefits, but only those that have occurred since the acquisition by Laclede, using the balances established during MGE's last rate case. On a going forward basis for Laclede, the costs of funding these benefits and paying down the net asset that has accumulated for these items would also be combined and allocated to the two operating units, as described in the testimony of Laclede witness Buck.

Q. IS THIS APPROACH FAIR TO THE CUSTOMERS OF BOTH OPERATING UNITS?

A. I firmly believe it is fair, given the relative cost levels achieved through this approach. While the costs of the pension and other post-retirement medical benefits would be higher for MGE than would have otherwise been the case if MGE had not been owned by Laclede, a number of other areas of cost are significantly lower than they would have otherwise been absent the acquisition and integration into Laclede, from the M&A

synergies, to the lower effective tax rate benefit generated by increased emphasis on accelerated pipeline replacement, which improved the pace of MGE upgrades from around a century to one that is closer to two decades. Notably, the employees providing the vast majority of shared services to LGC and MGE for more than three years now work for Laclede. This is a comprehensive approach to combining cost structures that have a meaningful difference, based on significant benefits generated for customers of both the utilities, which also helps bring their overall cost of service closer together on a timelier basis.

Q. ARE THERE OTHER PROPOSALS LACLEDE HAS RELATED TO ITS SHARED SERVICES?

A. Yes. Some members of Staff suggested that in order to be technically in compliance with its Commission-approved Cost Allocation Manual and the Affiliate Transactions Rules, Laclede must seek a waiver from the requirements for asymmetric pricing. We believe we are already complying with this requirement, to the extent it is even applicable to corporate support and other similar services, since our Human Resources department takes great effort to ensure wages and benefits are market-based and since our Supply Chain department undertakes RFPs and competitive bidding efforts to ensure purchases are priced competitively. In addition, we have allocation processes that charge the fully distributed rate – so our allocations represent both market-based prices and fully-distributed costs. However, out of an abundance of caution, however, during the pendency of this case we will pursue such a waiver to alleviate any concerns Staff might have if further discussions with Staff indicate that this concern persists.

Q. SHOULD THERE BE CONCERNS ABOUT LACLEDE'S COMPLIANCE WITH OTHER ELEMENTS OF THE CAM OR AFFILIATE TRANSACTION RULES?

A. No. As discussed at length in the direct testimony of Laclede witness Flaherty, Laclede and its affiliates have gone to considerable lengths to ensure that these and other costs are being appropriately allocated between all affiliated entities based on well-recognized allocation principles such as those set forth in Laclede's CAM. In fact, we have even established a separate service company for accounting purposes so that these allocations can be performed in as transparent and effective manner as possible. Our allocation process is an appropriately structured, reasonable and straight-forward mechanism that links costs to those benefiting entities, and the use of shared services has created significant benefits to LAC and MGE, as noted by Laclede witnesses Lindsey and Flaherty.

III. <u>BENEFITS OF GROWTH AND DEVELOPMENT</u>

Q. WHY IS LACLEDE SEEKING TARIFF CHANGES RELATED TO CUSTOMER GROWTH AND ECONOMIC DEVELOPMENT?

A. As noted earlier, further efforts to grow the customer base provides benefits to current customers by further spreading the utility's relatively fixed costs, and provides new customer the benefits of reasonably priced natural gas to their homes or businesses. Attracting large commercial and industrial businesses in Missouri is an economic benefit to the State, which also brings further growth opportunities and the added benefit of additional revenue support from those new businesses to help reduce rates for Laclede's current customers. Similarly, extending Laclede's distribution facilities to unserved or newly developing areas helps organically generate new residential and commercial load, serve new customers and provide additional rate benefits to current Laclede customers.

a) <u>Enhanced Economic Development Tariffs</u>

Q. IS LACLEDE SEEKING TARIFF CHANGES RELATED TO IT'S ECONOMIC DEVELOPMENT RATES?

A. Yes. Currently, MGE has tariff provisions that permit it to offer economic development and flexible rates where necessary to attract or retain customers. We believe it is important for utilities to play a vigorous role in encouraging the kind of customer growth or expansion and economic development, which can benefit both current customers as well as the economic health of the communities in which they operate, as long as such efforts are done in a judicious manner. The same thing is true for efforts to retain customers that might otherwise choose to bypass the Company or otherwise leave the jurisdiction for more attractive opportunities, resulting in the loss of revenues to cover costs that would then have to be paid by other customers. That said, the current MGE program has had very limited use over the years, lacks flexibility and contains a disincentive for the Company. We are therefore proposing changes to the economic development rider and flex rate programs.

Q. WHAT MODIFICATIONS TO MGE'S TARIFFS IS LACLEDE PROPOSING?

A. First, for both programs we are proposing rates be based on the actual revenues received from customers receiving a discounted rate rather than some imputed level of revenues, with a requirement that the terms of any negotiated rate contract cover all incremental costs incurred to serve the customer and make some contribution to the Company's fixed costs. It should also be shown that the economic development rider or discounted rate was necessary to retain or attract the customer given the competitive alternatives available to the customer. Meeting these requirements will ensure other customers are not adversely affected, but instead are affirmatively benefitted from these transactions. Any discounted rate contract would be submitted to Staff and reviewed prior to being effective and approved.

Q. WOULD YOU PROPOSE THAT SUCH TARIFFS BE ADOPTED BY LAC?

A. Yes. These improvements are beneficial to all stakeholders. As such it would be beneficial for the LAC service territory as well – to better meet the unique needs of certain customers and grow the Company's customer base, which then helps reduce the rates of other customers and improve economic development in the area, resulting in the potential for further growth and benefit for all stakeholders.

b) <u>Enhanced Extension Tariffs for Unserved Areas</u>

Q. WHAT DOES LACLEDE PROPOSE FOR TARIFF ENHANCEMENTS TO CREATE CUSTOMER GROWTH, SO CURRENT CUSTOMERS CAN BENEFIT FROM FURTHER SPREADING OF COSTS AND MISSOURI RESIDENTS HAVE ACCESS TO THE BENEFITS OF NATURAL GAS SERVICE?

A. We are proposing to add a provision that allows Laclede to finance extensions of its distribution system to bring the benefits of natural gas to areas that would go unserved with just the current main extension program. Natural gas can provide customers lower operating costs and better quality heating than other applications, and is also more environmentally friendly than most other energy options. Under our proposal, any incremental investment required to serve the customer – beyond the standard main extension allowance – would be recovered through a special system extension surcharge just to new customers serviced in that area, so current customers do not subsidize the arrangement, but instead benefit from that growth. The surcharge would be based on a financing period of up to 15 years using the same weighted cost of capital used to calculate the Company's ISRS charges for the service area in which the extension is being made. The energy savings for the new customers served by the extension would offset such a surcharge and provide the customer an overall net benefit that might otherwise not be available to them. As noted, such growth would also benefit current customers by spreading the Company's relatively fixed costs over a larger customer base.

IV. BENEFITS OF ENHANCEMENTS TO REGULATORY STRUCTURES

Q. **WOULD YOU PLEASE PROVIDE SOME BACKGROUND FOR YOUR STATEMENT THAT LACLEDE IS PROPOSING CERTAIN ENHANCEMENTS TO THE RATEMAKING PROCESS CONSISTENT WITH A RECENT CONSIDERATION OF SUCH MATTERS BY THE COMMISSION AND THE GERNERAL ASSEMBLY?**

A. Certainly. During the summer and fall of last year, the Commission and an Interim Committee of the Missouri Senate conducted workshops and hearings for the purpose of assessing what, if any changes, should be made to the ratemaking process in Missouri to, among other objectives, ensure sustained investment in utility infrastructure and improve the ratemaking process, but ensure that such efforts create benefits not just change. To that end, information was gathered from a wide variety of sources, including the Commission, its Staff, the Office of the Public Counsel, industry consultants, investor-owned utilities, the Energy Division of the Department of Economic Development and other environmental and consumer groups. At the same time, the Commission also conducted workshop to address many of the same issues with many of the same stakeholders.

Q. **DID THE SENATE INTERIM COMMITTEE MAKE RECOMMENDATIONS REGARDING POTENTIAL APPROACHES FOR ENHANCING THE RATEMAKING PROCESS?**

A. Yes. Based on the hearings it held and a comparison to the regulatory innovations instituted in other states, the Interim Committee issued a report in December, 2016, in which found that Missouri regulation was not keeping pace with the regulatory innovations being implemented in other states and that a modernization of the ratemaking process in Missouri could help to attract investment dollars and also benefit Missouri utility customers. To that end, the Committee recommended implementing a new regulatory framework that would include, among other things, a performance-based ratemaking approach to incentivize operational and customer service results; an annual review process that more closely matches revenues with costs; periodic reviews based upon enhanced reporting to verify information and set just and reasonable rates, the submission of capital expenditure plans, and approval of a revenue stabilization mechanism.

Q. WHAT RECOMMENDATIONS DID THE COMMISSION AND ITS STAFF MAKE?

A. Based on the workshops held by the Commission, the Commission Staff also presented a thoughtful set of recommendations in which it identified many of the same concepts as potential enhancements to the ratemaking process. Among those favorably mentioned were the use of performance metrics to encourage service quality, approaches to reducing regulatory lag that retain the Commission's jurisdiction and preserve incentives for the utility to operate efficiently, including the use of trackers or construction accounting on a case-by-case basis or discrete categories of plant, and the use of interim rates. For its part, the Commission recommended in its report that alternative ratemaking mechanisms be targeted to specific infrastructure needs and programs. The Commission also made a point to emphasize that any revisions to the process should preserve the Commission's jurisdiction and powers to make the fundamental ratemaking determinations necessary to ensure just and reasonable rates.

Q. HOW DID LACLEDE RESPOND TO THESE RECOMMENDATIONS?

A. We took them very much to heart, which is why we also support the Rate Case Modernization Act introduced in the Missouri Senate and House of Representatives, as Senate Bill 242 and House Bill 747, respectfully. This legislation takes a more comprehensive approach to these enhancements and includes some elements that currently don't have statutory authority, other than through the use of an experimental rate design program.

Q. IS LACLEDE PROPOSING THAT THE COMMISSION ADOPT SOME OF THE FEATURES OF THE RATE CASE MODERNIZATION ACT IN THIS PROCEEDING?

A. Yes. There are certain enhancements to the ratemaking process that the Commission already has clear legal authority to approve and that would contribute to regulatory enhancements and customer benefits, even if not a substitute for the more comprehensive approach in the legislation, for which the Commission may not have full statutory authority. As such, the regulatory enhancement proposals include, among others, proposals for: (a) stabilizing revenues and customer bills and enabling more customer-friendly rate designs; (b) recovering on a more timely basis costs for governments mandates and environmental requirements, as well as investments to better deliver quality customer service or implement critical IT business platforms to support the business; and (c) implementing performance management mechanisms to help ensure an appropriate balance of customer service, reliability and safety with cost management through a bilateral, balanced approach; and (d) sharing with our customers the benefits of growth achieved as a result of Spire's acquisitions.

a) Revenue Stabilization Mechanism (RSM)

Q. WHAT IS THE FIRST ENHANCEMENT BEING PROPOSED BY LACLEDE?

A. The first enhancement involves approval of an RSM. As noted in the initial section related to integration and consistent rate treatment, such a mechanism would help Laclede achieve more consistent, simplified rate designs for its two operating units. Additionally, it helps reduce the reliance upon a high customer charge, and allows Laclede to be more aggressive in pursuing energy efficiency programs for its customers. Finally, it would also provide residential and commercial customers with more stability in their bills, and would ensure that Laclede does not over- or under-recover its fixed distribution costs of providing utility service due to revenue variations that occur when such customers use more or less than was assumed when rates were established.

Q. WHY IS IT APPROPRIATE TO PREVENT SUCH OVER AND UNDER-RECOVERIES OF A UTILITY'S FIXED COSTS?

A. As this Commission has previously recognized in addressing this issue, the RSM represents a fair and balanced approach and is warranted for a number of reasons. First, from a pure cost causation standpoint, excessively tying the recovery of fixed costs to variable customer usage is inappropriate since most of these fixed costs do not, as their name implies, increase or decrease simply because customers use more or less gas due to variations in weather or other factors. Second, allowing over-recovery of costs during periods of high use is an unintended consequence of a volumetric rate design, but occurs at precisely the worst time as customers' bills are already high due to added gas use and such gas is likely to be at a relatively higher price given higher levels of demand – a double-whammy. Third, making recovery of such costs dependent on factors that are completely outside of the utility's control serves no valid economic or performance objective, but instead unnecessarily exposes the utility and its customers to random financial risks. Fourth, making recovery of fixed costs dependent on how much gas its customers use discourages the utility from pursuing energy efficiency programs to help customers reduce their usage, since lower usage exacts a financial disincentive on the utility.

Q. DOES THE COMMISSION HAVE THE LEGAL AUTHORITY TO APPROVE SUCH A MECHANSIM?

A. Yes. While I'm not a lawyer, it is my understanding that Missouri law already provides the Commission with explicit authority to approve a rate adjustment mechanism to address, between rate cases, the revenue impacts from changes in residential and commercial usage. RSMo 386.266.3 specifically states that *" . . .any gas corporation may make an application to the commission to approve rate schedules authorizing periodic rate adjustments outside of general rate proceedings to reflect the non-gas revenue effects of increases or decreases in residential and commercial customer usage* *due to variations in either weather, conservation, or both."* Up to now, however, the Commission has chosen to address this issue through various rate designs. These have included moving more of the utilities' fixed costs into a higher monthly customer charge and/or establish rate blocks where most fixed costs will be recovered once the customer uses a relatively modest amount of gas.

Q. HAS THIS RELIANCE ON VARIOUS RATE DESIGN SOLUTIONS ADEQUATELY ADDRESSED THE ISSUE OF FIXED COST RECOVERY?

A. It has certainly helped to mitigate the magnitude of the issue. But such approaches have their shortcomings. First, they still expose utilities and their customers to paying more or less than the actual cost of providing utility service. For example, there was over-recovery of those fixed distribution costs during the very cold winter of 2013/2014, and under-recovery of those costs during the warmer than normal winter of 2015/2016. Second, the reliance on higher customer charges to recover fixed costs has been vigorously opposed by some stakeholders in the ratemaking process. OPC and AARP have argued that a high customer charge is detrimental to low-income, low-use customers. Environmentalists and the Missouri Division of Energy have also advocated against a high fixed monthly charge, because it reduces the incentive to conserve energy.

Q. WOULD APPROVAL OF THE PROPOSED RSM RESOLVE THESE SHORTCOMINGS?

A. Yes. As set forth in the Laclede's proposed tariffs in this case, the mechanism being proposed would provide better protection for customers and the Company from revenue impacts resulting from customer usage variations. In the process, it would reduce the disincentive to pursue energy efficiency measures for the Company's customers while providing greater flexibility to lower customer charges for residential and small commercial customers. In fact, as part of its proposal to adopt the RSM, Laclede is proposing that both LAC's and MGE's customer charges be reduced meaningfully from what the Companies would need absent an RSM It is also the anchor to a number of other proposed rate design improvements, simplifications and integration efforts.

Q. ARE THERE ISSUES THE COMMISSION SHOULD CONSIDER IN THE TIMING OF THE RSM IMPLEMENTATION?

A. Yes. As a general practice, it is easier to implement significant rate design changes at the beginning of the heating season. While I have set forth the significant benefits to customers of the company's proposed shift in rate design, implementing this change at the beginning of a low usage period (spring and summer) would significantly and adversely affect the revenues the Company had planned around. As such, Laclede is recommending in this case a phased in rate approach with a revenue neutral tariff design through the summer consistent with the current rate design, and transitioning to the company's modified tariff and RSM implementation just prior to the beginning of the heating season on October 1, 2018, as detailed in the testimony of Company witness Lyons. This approach will bring all the benefits to customers in the long term without negatively impacting the utility in the short run.

Q. IS THIS PHASED IN APPROACH TO RATE CHANGES A NEW APPROACH FOR MISSOURI?

A. No. In MGE's most recent previous rate case, the Commission approved a similar transition in rates with transitory rates in effect from May 1 through September, and permanent rates beginning in the fall.

Q. IN THE EVENT THE COMMISSION DOES NOT APPROVE THE PROPOSED RSM, DOES LACLEDE HAVE AN ALTERNATIVE PROPOSAL?

A. I want to emphasize that Laclede strongly supports the adoption of its proposal to implement an RSM pursuant to the legal authority that already exists for such a mechanism. Should the Commission choose not to approve such a mechanism, however, Laclede would alternatively propose to further increase the customer charges for both MGE and LAC, in addition to the ISRS roll-in, and implement a first block weather mitigation rate design for MGE. Again, this rate design is not as effective and has a number of detractors because of its financial impact on low-use and low-income customers, as well as reducing the incentive for energy efficiency. This alternative proposal is also addressed in greater detail in the direct testimony of Laclede witness Weitzel.

b) <u>Tracking of Certain Costs for Inclusion in Future Rates</u>

Q. WHAT IS THE SECOND REGULATORY ENHANCEMENT BEING PROPOSED BY LACLEDE?

A. The second enhancement involves provisions for tracking certain costs for inclusion in future rates. While not as effective as changing rates on a more timely basis, they do help reduce the unintended consequences of regulatory lag. The purpose of these tracking mechanisms is to more closely match the cost of providing utility service with what the Company ultimately charges for that service, and aligns with the Commission's view towards mechanisms defined around specific needs.

Q. WHAT COST ITEMS IS LACLEDE PROPOSING TO TRACK?

A. The costs we are proposing to track or defer and recover in LAC and MGE's next rate case include those prudently incurred costs, whether capital or expense, to (a) comply with any federal, state, or local environmental law, regulation, or rule, as authorized by Section 386.266; (b) comply with integrity management expenses, whether from physical or cyber threats, that may be required or mandated above current cost levels; and (c) complete major capital projects necessary to support the business and provide customer benefits, but that do not produce any new revenues to offset the costs and have significant investment requirements with relatively high depreciation rates. For such capital projects, these deferred costs would include the depreciation, taxes and carrying costs on the investments made by the Company from the time the related facilities or equipment are placed in service.

Q. WHY IS IT APPROPRIATE FOR THE COMMISSION TO PERMIT A TRACKING AND EVENTUAL RECOVERY OF THESE PARTICULAR COSTS IN A SUBSEQUENT GENERAL RATE CASE PROCEEDING?

A. Because all of these costs are incurred to either comply with existing governmental mandates, to protect and enhance critical infrastructure, or are necessary investments for the business to enhance service, increase capabilities or reduce costs, incurring such costs is in the customers' interests. Without timely cost recovery, however, such expenditures might be delayed, deferred or reduced unless Laclede inadvisably chooses to under-earn on its shareholders' capital until such costs are reflected in rates, and then only earn on the non-depreciated portion of the investment that still remains at such time. Moreover, none of the activities or investments giving rise to these costs generates any additional revenues for the Company to offset the expenditures being made.

Q. IS THERE AN EXISTING POLICY BASIS FOR AUTHORIZING SUCH TREATMENT OF THESE COST ITEMS?

A. Yes. In terms of the environmental compliance costs, existing Missouri law already authorizes the Commission to approve an adjustment mechanism that permits gas, electric and water utilities to changes rates between rate cases to reflect increases and decreases in such costs. Obviously, this statutory authority would indicate that the General Assembly believes that such environmental compliance expenditures are a category of costs that warrant special recovery treatment.

Q. WHAT ABOUT RECOVERY FOR THE OTHER ITEMS?

A. Integrity management and cyber security have also been the subject of special attention by the Commission over the last several years and rightly so. Protecting critical infrastructure from physical integrity issues and potential disruptions or damage due to cyber-attacks, as well as protection of sensitive customer information, is an increasing challenging endeavor given the growing sophistication and ubiquity of those seeking to engage in such attacks. To the extent significant expenditures are mandated or necessary to meet this challenge, there should not be a financial disincentive to making them. Permitting the deferral of depreciation, taxes and carrying costs on especially major projects needed for the business is a sound and fair way to address one of the significant deficiencies of the current process – namely the requirement to absorb such costs until a subsequent rate case is completed and the resulting diminution in the investment value that occurs, even though the facility is providing service to customers well before then.

Q. ARE THERE OTHER CONSIDERATIONS FOR COST RECOVERY THE COMMISSION SHOULD CONSIDER FOR MAJOR PROJECTS, SUCH AS THOSE FOR INFORMATION TECHNOLOGY PLATFORMS?

A. Yes, given that more and more systems are provided as "software as a service", we believe the Commission should also be receptive to regulatory structures adopted in other jurisdictions for such costs, which try to eliminate the "capital bias" related to such decisions by providing rate base treatment for pre-paid leases of such "cloudware" where it makes economic and business sense and provides benefits to customers.

Q. WILL SUCH STRUCTURES CREATE CONCERNS ABOUT "SINGLE-ISSUE RATEMAKING" OUTSIDE OF A RATE PROCEEDING WHERE ALL RELEVANT FACTORS ARE CONSIDERED?

A. No. Notably, Laclede is not proposing to go as far as the law would allow and is only recommending such environmental compliance costs be tracked, deferred and recovered in a future rate case. In short, this is a modest proposal that seeks to achieve the legislative purpose behind the statute, but in a way that tries to accommodate those stakeholders who express concerns whenever rates are adjusted outside of a rate case. Similarly, a tracker for incremental integrity management costs and the construction accounting treatment of capital-related costs for major projects to enhance customer service would go into regulatory deferral accounts that would then reviewed at the rate case to determine eligibility, prudence and inclusion in rates in the context of all relevant factors.

c) <u>Performance Metrics for Customer Service and Cost Management</u>

Q. HOW CAN THE COMMISSION BETTER SUPPORT FURTHER FOCUS ON CUSTOMER BENEFITS AND ACCEPTABLE PERFORMANCE LEVELS FOR CUSTOMER SERVICE, SAFETY AND RELIABILITY?

A. Laclede proposes working with the Commission and other stakeholders to establish performance metrics in key areas of customer service, safety, reliability and other areas to ensure an acceptable level of customer service is maintained and better align the interests of Laclede and its customers. Laclede already monitors a variety of service, safety, reliability and other operational results and has previously provided the Commission Staff with a number of such performance metrics. Historic performance levels in such areas would be used to establish an appropriate benchmark to both monitor future results on a periodic basis and hold the utility accountable or incentivize superior operational results. This performance-based mechanism would establish a band of acceptable performance based on a reasonably achievable level of performance determined by analyzing past results across a reasonable number of metrics. Between four to six metrics would be chosen based on desired areas of focus for customer benefits, with each metric worth an amount equal to five basis points multiplied by the equity component of rate base established in this proceeding, plus or minus, to create bilateral accountabilities and incentives. For each metric selected, a regulatory deferral account would be debited or credited for that amount if the Company's performance for the year resulted in exceeding or falling short of the band. The sum of the amounts would be deferred in that regulatory account for recovery or refund at the next rate proceeding. In order for the incentive to operate appropriately, this mechanism would of course be independent of such rate proceeding's revenue requirement.

Q. COULD SUCH A MECHANISM ALSO WORK FOR ENHANCEMENTS TO COST MANAGEMENT FOR THE BENEFIT OF THE CUSTOMER?

A. Yes. A balance of both cost management and service quality would further align the interests of the Company and the customer, and Laclede is proposing the implementation of such a mechanism.

Q. WHAT IS LACLEDE PROPOSING?

A. Stakeholders agree that cost management is good for customers, but differ on the approach that will best incentivize activities to produce such benefits. Laclede is proposing that a benchmark be created, based upon prior year O&M costs for LAC and MGE, fixed at that level and then inflated by CPI-U each year, as a comparison point to what ongoing levels of cost are actually achieved by the respective business unit. A reasonable and symmetrical range would be placed around this benchmark, similar to the proposal for customer service metrics, and performance that achieves ongoing cost levels below this range would be incentivized by putting 50% of the difference between the achieved results and the benchmark range into a regulatory deferral mechanism for recovery at the Company's next rate case. Similar to the customer service incentive, cost levels that are higher than the range would create a financial accountability for the company and 50% of ongoing O&M costs that exceed the benchmark band would be deferred for a reduction in rates at the next rate case. Again, as with the customer service incentive, this mechanism would be independent of the revenue requirement in the next rate case.

Q. ARE THESE PERFORMANCE METRICS FOR CUSTOMER SERVICE AND COST MANAGEMENT APPROPRIATE AND FAIR TO STAKEHOLDERS?

A. Yes. They are fair and appropriate for several reasons. First, these incentive mechanisms better align the interests of the Company and its customers, similar to how the competitive marketplace rewards superior performance and punishes below standard results. When the Company is able to produce results that create benefits for the customer, they are appropriately incentivized, and when they produce results that are below standard, they also hold it accountable. It is also similar to how companies structure their employee compensation, by making incentives part of that compensation to elevate execution. Second, it creates a better and more transparent discipline to review and assess performance on a timelier basis, with reviews and determinations made on an annual basis. Reporting would be provided during the year to provide the Commission with a better sense for how the company is performing in these key areas, and the Company will be further incentivized to take action sooner to improve results.

d) <u>Treatment of Acquisition Costs and Synergies</u>

Q. HOW IS LACLEDE PROPOSING TO TREAT ANY SYNERGIES AND RELATED COSTS ASSOCIATED WITH THE ACQUISITION OF MGE?

A. The Company is proposing treat the costs to achieve and resulting synergies related to Laclede's acquisition of MGE consistent with the terms of the Stipulation and Agreement approved by the Commission in the MGE Acquisition Proceeding, Case No. GM-2013-0254. This approved, non-traditional structure recognizes the benefits of activities by the Company, which benefit customers through lower costs.

Q. WHAT DID THOSE TERMS PROVIDE?

A. The Agreement provides that the Laclede could include in rates 50% of the one-time transition and other costs incurred to achieve the synergies made possible by the acquisition. Laclede was also permitted to continue rate base treatment of one-time capital costs associated with facilities or other assets retired prior to the end of their useful life as a result of integrating the two companies. The right to include these one-time costs to achieve was contingent on the overall level of synergies achieved being sufficient to cover such costs.

Q WAS THE OVERALL LEVEL OF SYNERGIES ACHIEVED BY LACLEDE SUFFICIENT TO COVER ONE-HALF OF THE COSTS TO ACHIEVE?

A. Yes, by a wide margin. As has been reflected in the quarterly synergy reports provided to Staff and OPC over the past three and a half years, Laclede had achieved synergies in excess of one-time costs to achieve, both operating expense and capital, well before the end of the test year in these cases. These synergies consisted of a wide variety of items, including eliminations of redundant costs, supply chain and procurement savings from the added scale, benefits produced by the sharing of best practices between the two utilities, as well as other items. Such costs to achieve these ongoing cost-savings benefits for customers are therefore fully eligible for inclusion in rates in this proceeding and pursuant to the terms of the Stipulation and Agreement they will be amortized over a five-year period.

Q. WHAT ABOUT TREATMENT OF SYNERGIES RESULTING FROM THE UNRELATED ACQUISITIONS OF ALABAMA GAS CORPORATION AND ENERGYSOUTH INCORPORATED?

A. The Company believes it has created meaningful benefits for its Missouri customers through Spire's acquisitions and growth outside the jurisdiction of its LAC and MGE territories. A review of the shared services costs for LAC and MGE prior to and after these acquisitions shows a significant benefit has occurred based on Spire's growth. Essentially, without even being a party to the transactions or bearing any of the costs for the acquisitions, LAC and MGE customers have benefited from the investments in growth by Spire Inc. by having a cost structure that is far lower than it would have been otherwise.

Q. IS THERE ANYTHING IN THE CURRENT REVENUE REQUIREMENT FOR SUCH TREATMENT?

A. No. We would like to work with parties to determine how this may be included in this rate case, whether through some retention mechanism or a one-time incentive adder to Laclede's ROE.

Q. HOW WOULD THIS BE APPROPRIATE AND FAIR TO STAKEHOLDERS?

A. It is fair and appropriate for a number of reasons. First, it recognizes that Laclede's corporate parent, Spire Inc., devoted significant financial resources necessary to complete both transactions. Missouri ratepayers were not at risk nor were they required to support the premium required to purchase the companies, the transaction costs incurred to complete the transactions, or the costs incurred to achieve the synergies. Such an approach is appropriate because it recognizes benefits already received. Additionally, it provides a precedent as an incentive to pursue future transactions that can also serve to reduce the overall cost of utility service. Such treatment also recognizes that unlike the MGE acquisition, Spire has not had an opportunity to fully enjoy the benefits of the cost savings it created for its customers due to the required timing of this rate case by the ISRS statute.

Q WOULD THIS STILL ENSURE MISSOURI CUSTOMERS RECEIVE BENEFITS FROM THOSE ACQUISITIONS?

A. Without question. Not only have Missouri customers already received the benefit of our ability to stay out of a rate case longer as a result of these savings, but they would also be receiving the benefit of costs savings achieved in reducing the cost of corporate support and other shared services. Additionally, they would benefit customers long-term when this treatment ends at the next rate case. Such treatment, if approved by the Commission, would maintain the appropriate incentive to further pursue growth and cost reductions that provide significant benefits to Missouri customers.

Q. **DOES THIS COMPLETE YOUR DIRECT TESTIMONY?**

A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Request to Increase its Revenues for Gas Service	)))	File No. GR-2017-0215
In the Matter of Laclede Gas Company d/b/a Missouri Gas Energy's Request to Increase its Revenues for Gas Service	)))	File No. GR-2017-0216

AFFIDAVIT

STATE OF MISSOURI	)	
	)	SS.
CITY OF ST. LOUIS	)	

C. Eric Lobser, of lawful age, being first duly sworn, deposes and states:

1. My name is C. Eric Lobser. I am Vice President, Regulatory & Governmental Affairs for Laclede Gas Company. My business address is 700 Market St., St Louis, Missouri, 63101.

2. Attached hereto and made a part hereof for all purposes is my direct testimony on behalf of Laclede Gas Company and MGE.

3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.

C. Eric Lobser

Subscribed and sworn to before me this 3rd day of April 2017.

Marcia A. Spangler
Notary Public

MARCIA A. SPANGLER
Notary Public - Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires: Sept. 24, 2018
Commission # 14630361