

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the matter of the application of                     )  
Missouri Gas Energy, a division of                     )  
Southern Union Company, for approval to             )  
change its infrastructure system                     )  
replacement surcharge.                                     )

**Case No. GO-2009-0009**  
YG-2009-0008

**STAFF RECOMMENDATION**

**COMES NOW** the Staff of the Missouri Public Service Commission, in response to the Commission's July 23, 2008 Order Directing Filing of Staff Report, and states:

1. On July 2, 2008 Missouri Gas Energy (MGE) a division of Southern Union Company (Southern Union) filed an Application and Petition (Application) to change its tariffed rate for the Infrastructure System Replacement Surcharge (ISRS).

2. MGE requests an adjustment to ISRS rates for ISRS eligible gas utility plant projects through its ISRS rate schedule.

3. Commission Rule 4 CSR 240-3.265(11) states that "the staff of the Commission may examine information of the gas corporation to confirm that the underlying costs are in accordance with the provisions of Sections 393.1009 to 393.1015, RSMo, and to confirm" proper calculation of the proposed charge. The Staff "may submit a report regarding its examination to the Commission no later than sixty days" after the petition is filed.

4. In Case No. GO-2008-0113, MGE's previous ISRS revenues were calculated on ISRS plant that was placed in service during the period November 1, 2006 through September 30, 2007.

5. By this filing, MGE seeks to recover costs of ISRS-qualifying plant placed in service from October 1, 2007 through May 31, 2008.

6. These costs, reflected in the instant ISRS filing, are intended to generate an additional \$1,530,499 of annual revenue.

7. As the result of MGE's correction of certain cost reporting errors, MGE updated its requested ISRS revenues from \$1,530,499 to \$1,491,751. These errors are more fully explained in Staff's Memorandum attached hereto as Appendix A and incorporated by reference.

8. Based on its examination and calculations contained in its Memorandum, the Staff has determined that the Company's ISRS rates should be designed to recover an incremental revenue requirement of \$1,445,763. This is based on an ISRS net investment date of October 30, 2008, the approximate date MGE's ISRS from this case will go into effect. Staff made three adjustments to MGE's updated filing.

9. MGE's incremental ISRS revenues based on a net investment date of June 30, 2008 is \$1,473,453. MGE's ISRS rates are based on a total combined revenue requirement of \$2,785,641 which is a composite amount from this case and Case No. GO-2008-0113.

10. Please See Staff's attached Appendix B for the ISRS rates which should be approved.

**WHEREFORE** Staff recommends that the Commission issue an order in this case:

1. Rejecting the tariff sheet filed by MGE on July 2, 2008, (assigned tariff number YG-2009-0008);

2. Authorizing MGE to file a tariff to impose an Infrastructure System Replacement Surcharge that is sufficient to recover appropriate annual pre-tax revenues in the amount of \$1,445,763.

3. Authorizing rates consistent with those calculated by Staff as shown on Appendix
- B.

Respectfully submitted,

**/s/ Robert S. Berlin**

Robert S. Berlin  
Senior Counsel  
Missouri Bar No. 51709

Attorney for the Staff of the  
Missouri Public Service Commission  
P. O. Box 360  
Jefferson City, MO 65102  
(573) 526-7779  
(573) 751-9285 (FAX)  
Bob.berlin@psc.mo.gov

### **Certificate of Service**

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or electronically mailed to all counsel of record this 29<sup>th</sup> day of August 2008.

**/s/ Robert S. Berlin**

## **MEMORANDUM**

TO: Missouri Public Service Commission Official Case File  
Case No. GO-2009-0009 / File No. YG-2009-0008 – Missouri Gas Energy

FROM: Bret Prenger, Auditing Department  
Chuck Hyneman, Auditing Department  
Michael Ensrud, Tariffs/Rate Design - Energy

/s/ Steve Traxler  
/s/ Tom Imhoff      08/28/08      /s/ Robert S. Berlin 08/28/08  
Project Coordinator / Date      General Counsel's Office / Date

SUBJECT: Staff Report and Recommendation Regarding the Application of Missouri Gas Energy Seeking the Missouri Public Service Commission's Approval to Increase an Infrastructure System Replacement Surcharge

DATE: August 28, 2008

### **BACKGROUND**

On July 2, 2008, Missouri Gas Energy (MGE), a division of Southern Union Company, filed an Application and Petition (Application) to implement a change in MGE's Infrastructure System Replacement Surcharge (ISRS) with the Missouri Public Service Commission (Commission) with a proposed effective date of August 1, 2008. The Commission's Rule 4 CSR 240-3.265; Natural Gas Utility Petitions for Infrastructure System Replacement Surcharges allows Gas corporations to recover certain infrastructure system replacement costs outside of a formal rate case filing through a surcharge on customers' bills. MGE filed this tariff sheet to reflect a total revenue requirement of \$2,870,377. In this current ISRS filing, MGE seeks to recover an additional \$1,530,499 revenues from its customers.

On July 2, 2008, the Commission issued its order, directing notice and setting an intervention date of July 22, 2008. The Commission indicated that it must issue its order regarding this application effective no later than October 30, 2008.

On July 8, 2008, the Commission suspended the proposed ISRS tariff until October 30, 2008.

On July 23, 2008 the Commission set a filing date of August 31, 2008 for Staff's Recommendation. This Memorandum is in response to that Order.

### **STAFF'S INVESTIGATION**

Staff members from the Auditing and Energy Departments participated in the Staff's investigation of the Application. The Staff's investigation into the Application included a review of the Application, the

supporting documentation, Missouri statutory sections 393.1009, 393.1012 and 393.1015 RSMo and all additional data provided by MGE.

## THE APPLICATION

In Case No. GO-2008-0113, MGE's current ISRS revenues were calculated on ISRS plant that was placed in service during the period November 1, 2006 through September 30, 2007. In MGE's current ISRS Application, Case No. GO-2009-0009, MGE seeks to recover costs of ISRS-qualifying plant placed in service from October 1, 2007 through May 31, 2008.

|  | MGE as filed |
|--|--------------|
| ISRS Plant in service Oct 2007 thru May 2008       | \$10,893,200 |
| Less: Plant retirements                            | \$0          |
| Deferred Taxes GO-2008-0113 at 6/30/08             | (\$107,045)  |
| Deferred Taxes GO-2009-0009 at 6/30/08             | (\$101,970)  |
| Accumulated Depreciation GO-2008-0113 at 6/30/08   | (\$173,545)  |
| Accumulated Depreciation GO-2009-0009 at 6/30/08   | (\$97,502)   |
| Total ISRS Rate Base                               | \$10,413,138 |
| Tax Grossed Up Rate or Return per GR-2006-0422     | 11.30%       |
| Return on ISRS rate base                           | \$1,176,498  |
| Correction of rate of return error on GO-2008-0113 | \$0          |
| Annual Depreciation Expense ISRS Plant Additions   | \$260,317    |
| Annual Depreciation Expense Plant Retirements      | (\$4,070)    |
| Property taxes GO-2009-0009                        | \$36,574     |
| Property taxes GO-2008-0113                        | \$61,180     |
| Total ISRS Revenues                                | \$1,530,499  |

## STAFF REVIEW

The Staff's review consisted of a review of MGE's Application, a review of selected plant workorders at MGE's headquarters in Kansas City, Missouri, responses to Staff data requests, and discussions with MGE personnel. Based on the Staff's review of MGE's ISRS plant workorders and discussions with MGE personnel, MGE agreed to remove \$177,413 in plant costs associated with a project that was revenue producing and thus did not qualify for ISRS treatment. MGE also agreed to correct the weighted cost of debt it used to calculate the return on ISRS rate base. MGE used a cost of debt rate that did not reflect the rate ordered by the Commission in its Report and Order in Case No. GR-2006-0422, as required by Commission Rule 4 CSR 240-3.265. Finally, MGE removed depreciation expense on plant included in its current GO-2008-0113 ISRS and incorrectly included in this Application. As a result of the correction of these errors, MGE updated its requested ISRS revenues from \$1,530,499 to \$1,491,751. This calculation is shown below:

|  |                    |
|--|--------------------|
|  | MGE corrected      |
| ISRS Plant in service Oct 2007 thru May 2008       | \$10,715,787       |
| Less: Plant retirements                            | \$0                |
| Deferred Taxes GO-2008-0113 at 6/30/08             | (\$107,045)        |
| Deferred Taxes GO-2009-0009 at 6/30/08             | (\$100,086)        |
| Accumulated Depreciation GO-2008-0113 at 6/30/08   | <u>(\$173,545)</u> |
| Accumulated Depreciation GO-2009-0009 at 6/30/08   | (\$96,495)         |
| Total ISRS Rate Base                               | \$10,238,616       |
| Tax Grossed Up Rate or Return per GR-2006-0422     | 11.19%             |
| Return on ISRS rate base                           | <u>\$1,145,778</u> |
| Correction of rate of return error on GO-2008-0113 | \$0                |
| Annual Depreciation Expense ISRS Plant Additions   | \$252,289          |
| Annual Depreciation Expense Plant Retirements      | (\$4,070)          |
| Property taxes GO-2009-0009                        | \$36,574           |
| Property taxes GO-2008-0113                        | <u>\$61,180</u>    |
| Total ISRS Revenues                                | \$1,491,751        |

## STAFF'S REVENUE CALCULATION

Based on its review, the Staff has determined that the appropriate incremental revenue requirement annual increase for the pending ISRS Application is \$1,445,763 based on ISRS plant placed in service during the period October 1, 2007 through May 31, 2008. These costs are shown below:

|   | Staff              |
|---|--------------------|
| ISRS Plant placed in service Oct 2007 thru May 2008 | \$10,715,787       |
| Deferred Taxes GO-2008-0113 at 10/31/08             | (\$129,078)        |
| Deferred Taxes GO-2009-0009 at 10/31/08             | (\$77,862)         |
| Accumulated Depreciation GO-2008-0113 at 10/31/08   | (\$337,900)        |
| Accumulated Depreciation GO-2009-0009 at 10/31/08   | <u>(\$180,591)</u> |
| Total ISRS Rate Base                                | \$9,990,355        |
| Tax Grossed Up Rate or Return per GR-2006-0422      | 11.19%             |
| Return on ISRS rate base                            | <u>\$1,117,996</u> |
| Correction of rate of return error on GO-2008-0113  | (\$10,833)         |
| Annual Depreciation Expense ISRS Plant Additions    | \$252,289          |
| Annual Depreciation Expense Plant Retirements       | (\$11,535)         |
| Property taxes on GO-2009-0009 plant due 12/08      | \$36,739           |
| Property taxes on GO-2008-0113 plant due 12/08      | <u>\$61,108</u>    |
| Total ISRS Revenues                                 | \$1,445,763        |

The total difference between MGE's incremental updated ISRS revenues of \$1,491,751 and the Staff's proposed level of \$1,445,763 is \$45,998. This difference is shown in the chart below and explained in the description of the Staff adjustments:

|   | Staff        | MGE          | Difference |
|---|--------------|--------------|------------|
| ISRS Plant placed in service Oct 2007 thru May 2008 | \$10,715,787 | \$10,715,787 | \$0        |
| Deferred Taxes GO-2008-0113 at 10/31/08             | (\$129,078)  | (\$107,045)  | \$22,033   |
| Deferred Taxes GO-2009-0009 at 10/31/08             | (\$77,862)   | (\$100,086)  | (\$22,224) |
| Accumulated Depreciation GO-2008-0113 at 10/31/08   | (\$337,900)  | (\$173,545)  | \$164,355  |
| Accumulated Depreciation GO-2009-0009 at 10/31/08   | (\$180,591)  | (\$96,495)   | \$84,097   |
| Total ISRS Rate Base                                | \$9,990,355  | \$10,238,616 | \$248,261  |
| Tax Grossed Up Rate or Return per GR-2006-0422      | 11.19%       | 11.19%       | 11.19%     |
| Return on ISRS rate base                            | \$1,117,996  | \$1,145,778  | \$27,782   |
| Correction of rate of return error on GO-2008-0113  | (\$10,833)   | \$0          | \$10,833   |
| Annual Depreciation Expense ISRS Plant Additions    | \$252,289    | \$252,289    | (\$0)      |
| Annual Depreciation Expense Plant Retirements       | (\$11,535)   | (\$4,070)    | \$7,465    |
| Property taxes on GO-2009-0009 plant due 12/08      | \$36,739     | \$36,574     | (\$165)    |
| Property taxes on GO-2008-0113 plant due 12/08      | \$61,108     | \$61,180     | \$72       |
| Total ISRS Revenues                                 | \$1,445,763  | \$1,491,751  | \$45,988   |

Adjustment 1 – correction of weighted cost of debt used in current ISRS (GO-2008-0113) decreasing ISRS revenues in the amount of \$10,833. As described above, MGE used this incorrect weighted cost of debt in this Application. MGE also used the incorrect rate in calculating its current ISRS surcharge. This adjustment reduces ISRS revenues in this case to account for the over-collection due to the error in the current ISRS.

Adjustment 2 – the Staff included the annual depreciation expense on ISRS plant retirements in the amount of \$11,535, as required by Commission Rule 4 CSR 240-3.265 (1)(E), which requires that the amount of ISRS depreciation expense be reduced by the annual depreciation expense on related facility retirements. In its application MGE did not include the annualized level of expense but only the amount that would be theoretically included in a depreciation reserve for retirements. The amount MGE included represents the amount of retirement depreciation expense recovered in base rates since the new ISRS plant was placed in service.

Adjustment 3 –In its Application, MGE only calculated the depreciation and deferred tax reserve at June 30, 2008, the month before its July 2, 2008 filing. However, Commission Rule 4 CSR 240-3.265 (12) requires that the Commission issue an Order with an effective date no later than 120 days after the utility files an ISRS petition. This would make the effective date of the customer surcharge from this case about October 30, 2008. The Staff used the October 30, 2008 date for the depreciation reserve and deferred tax reserve in its calculation of ISRS revenues, as that more closely reflects MGE's net investment in ISRS plant near the date the surcharge will go into effect.

The Staff recommends the Commission approve an incremental revenue requirement of \$1,445,763, based on an ISRS net investment date of October 30, 2008. This is the approximate date MGE's ISRS from this case will go into effect. MGE's incremental ISRS revenues based on a net investment date of June 30, 2008 is \$1,473,453. MGE's

ISRS rates are based on a total combined revenue requirement of \$2,785,641 which is a composite amount from this case and Case No. GO-2008-0113.

In this ISRS filing and in MGE's GO-2008-0113 ISRS filing, the Staff has had to make adjustments to remove costs related to plant work orders that do not meet the ISRS requirements under Commission Rule 4 CSR 240-3.265. The Staff has a concern about MGE's internal control procedures as it relates to its ISRS filings and has communicated its concern to MGE. For example, the Staff has determined that no employee of MGE's Regulatory Affairs Department performs a review of any of the ISRS workorders prior to filing an ISRS case. The Staff believes that, at a minimum, MGE Regulatory Affairs personnel should review the majority if not all of the plant workorders included in its ISRS petition. This simple procedure will reduce the likelihood of MGE's ratepayer from being charged excessive ISRS costs.

Shortly prior to filing its recommendation in this case the Staff noted an inconsistency between the method used by MGE in calculating its ISRS rate base (the asset side of the surcharge calculation) and depreciation expense (the expense side of the surcharge). Commission Rule 4 CSR 240-3.265 (1)(E) requires that depreciation expense on ISRS plant be reduced by the annual depreciation expense on plant retired as a result of the ISRS plant installed. The rule clearly contemplates a reduction in the surcharge for costs that are currently being recovered in base rates (depreciation expense on plant that is retired because of the ISRS). However, while the expense side of the ISRS calculation is covered by the rule, the asset or rate base side is not specifically addressed. To be consistent with what appears to be the intent of the Rule, a reduction on ISRS plant investment would be appropriate to reflect the financial return on the retired plant that is currently being recovered in base rates. While the Staff could have made some assumptions to calculate an approximate amount to reduce ISRS rate base in this case, it decided to address the issue in the next ISRS case where more time would be available to collect actual data.

## **THE ISRS RATE SCHEDULES**

Staff notes that MGE's initial filing was deficient and at odds with the traditional methodology of computing rates on a composite revenue requirement. MGE calculated different rates for each of the ISRS filings (GO-2008-0113 and GO-2009-0009) then added the computed rates from each case to develop their composite ISRS rate. The proper ISRS rates are derived from Staff's composite revenue requirement computed in both ISRS cases.

Staff's position is consistent with the Commission's determination in MGE's ISRS Case No. GO-2006-0556 when these two different methodologies in computing ISRS rates were presented. Staff's attached schedule reflects the ISRS rates that utilize the traditional ISRS methodology of calculating rates.

The Staff has verified that the Company has filed its 2007 annual report and is not delinquent on any assessment. The Staff is not aware of any other matter before the Commission that affects or is affected by this filing.



P.S.C. MO. No. 5

Eighth Revised Sheet No. 10, CANCELLING Seventh Revised Sheet No. 12

---

**RECOMMENDATION**

Based upon the above, the Staff recommends that the Commission issue an order in this case that:

1. Rejects the ISRS tariff sheet (YG-2009-0008) filed by MGE on July 2, 2008;
2. Approves the Staff's determination of the incremental ISRS surcharge revenues in the amount of annual pre-tax revenues of \$1,445,763; and
3. Authorizes MGE to file an ISRS rate for each customer class as reflected in Appendix B.

MISSOURI GAS ENERGY

Missouri Gas Energy

CASE NO. GO-2009-0009

FILE NO. YG-2009-0008

Company's Total ISRS Revenues

\$2,785,641

ISRS RATE DESIGN

| Customer<br>Rate Class | Number<br>of Customers | Customer<br>Charges | Ratio To Res.<br>Cust. Charge | Weighted<br>Customer# | Customer<br>Percentage | ISRS<br>charge | ISRS<br>Revenues   |
|------------------------|------------------------|---------------------|-------------------------------|-----------------------|------------------------|----------------|--------------------|
| Residential            | 446,682                | \$24.62             | 1.0000                        | 446,682               | 79.7541%               | \$0.41         | \$2,221,664        |
| Small General Service  | 67,237                 | \$18.39             | 1.3476                        | 90,609                | 16.1780%               | \$0.56         | \$450,660          |
| Large General Service  | 311                    | \$108.91            | 7.9828                        | 2,483                 | 0.4433%                | \$3.31         | \$12,348           |
| Large Volume Service   | 494                    | \$835.95            | 41.0944                       | 20,301                | 3.6246%                | \$17.03        | \$100,969          |
| TOTAL                  | <u>514,724</u>         |                     |                               | <u>560,074</u>        | <u>100.0000%</u>       |                | <u>\$2,785,641</u> |

APPENDIX B

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**


In the Matter of the Application of )  
Missouri Gas Energy, a division of )  
Southern Union Company, for approval )  
to change its infrastructure system )  
replacement surcharge. )

Case No. GO-2009-0009

**AFFIDAVIT OF MICHAEL J. ENSRUD**

**STATE OF MISSOURI** )  
                                  ) ss  
**COUNTY OF COLE** )

Michael J. Ensrud, of lawful age, on oath states: that he has participated in the preparation of the foregoing written memorandum, to be presented in the above case; that the information in the attached written report was given by Missouri Gas Energy (MGE); that he has knowledge of the matters set forth in such memorandum; and that such matters are true to the best of his knowledge and belief.

  
Michael J. Ensrud

Subscribed and sworn to before me this 28<sup>th</sup> day of August, 2008.



SUSAN L. SUNDERMEYER  
My Commission Expires  
September 21, 2010  
Callaway County  
Commission #06942086

  
Notary Public

**BEFORE THE PUBLIC SERVICE COMMISSION**  
**OF THE STATE OF MISSOURI**

|  |   |                       |
|--|---|-----------------------|
| In the Matter of the Application of Missouri | ) |                       |
| Gas Energy, a Division of Southern Union     | ) | Case No. GO-2009-0009 |
| Company, for Approval to Change its          | ) |                       |
| Infrastructure System Replacement Surcharge  | ) |                       |
|  | ) |                       |


AFFIDAVIT OF CHARLES R. HYNEMAN

STATE OF MISSOURI                    )  
  )  
COUNTY OF Jackson                )     ss.

Charles R. Hyneman, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Staff Recommendation in memorandum form, to be presented in the above case; that the information in the Staff Recommendation was developed by him; that he has knowledge of the matters set forth in such Staff Recommendation; and that such matters are true and correct to the best of his knowledge and belief.

  
\_\_\_\_\_  
Charles R. Hyneman

Subscribed and sworn to before me this 27<sup>th</sup> day of August, 2008.

  
\_\_\_\_\_  
Notary Public

BEVERLY M. WEBB  
Notary Public - Notary Seal  
STATE OF MISSOURI  
County of Clay  
My Commission Expires 4/14/2012  
Commission # 08464070

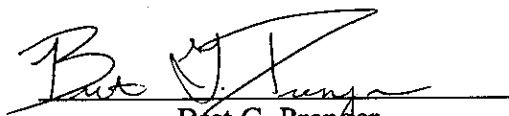
**BEFORE THE PUBLIC SERVICE COMMISSION**  
**OF THE STATE OF MISSOURI**

|  |   |                       |
|--|---|-----------------------|
| In the Matter of the Application of Missouri | ) |                       |
| Gas Energy, a Division of Southern Union     | ) | Case No. GO-2009-0009 |
| Company, for Approval to Change its          | ) |                       |
| Infrastructure System Replacement Surcharge  | ) |                       |
|  | ) |                       |

**AFFIDAVIT OF BRET G. PRENGER**

|                          |   |     |
|--------------------------|---|-----|
| STATE OF MISSOURI        | ) |     |
|                          | ) | ss. |
| COUNTY OF <u>Jackson</u> | ) |     |

Bret G. Prenger, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Staff Recommendation in memorandum form, to be presented in the above case; that the information in the Staff Recommendation was developed by him; that he has knowledge of the matters set forth in such Staff Recommendation; and that such matters are true and correct to the best of his knowledge and belief.

  
Bret G. Prenger

Subscribed and sworn to before me this 27<sup>th</sup> day of August, 2008.

  
Notary Public

**BEVERLY M. WEBB**  
Notary Public - Notary Seal  
STATE OF MISSOURI  
County of Clay  
My Commission Expires 4/14/2012  
Commission # 08464070