Exhibit No.:	
Issues:	**MKP/RPC Pipeline Adjustment**
Witness:	**Howard E. Lubow**
Type of Exhibit:	**Rebuttal Testimony**
Sponsoring Party:	**Mid-Kansas Partnership/Riverside Pipeline Company, L.P.**
Case No:	**GR-96-450**

MID-KANSAS PARTNERSHIP/RIVERSIDE PIPELINE COMPANY, L.P.

REBUTTAL TESTIMONY

OF

HOWARD E. LUBOW

MISSOURI GAS ENERGY

A division of

Southern Union Company

CASE NO. GR-96-450

Jefferson City, Missouri
December, 1998

REBUTTAL TESTIMONY OF

HOWARD E. LUBOW

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REBUTTAL TESTIMONY OF HOWARD E. LUBOW

<u>I. Introduction</u>

Q. Please state your name and address.

A. My name is Howard E. Lubow. My business address is 8325 Lenexa Drive, Suite, 400, Lenexa, Kansas 66214.

Q. What is your present occupation?

A. I am the Executive Vice President, Chief Operating Officer, and Chief Financial Officer of Kansas Pipeline Operating Company (KPOC). I have been with the Company since July 1997. I was made Chief Operating Officer of the Company in January 1998. In my capacity as COO and CFO, I oversee the operations of the pipeline companies, including financial, regulatory, and accounting functions.

I also continue to serve as a public utility consultant and President of Overland Consulting, specializing in financial, management and regulatory services within the utility industry. My responsibilities are primarily related to the oversight of consulting services focused on management and financial audits, cost of service determination and allocation, litigation support, regulatory policy, financing studios, forecasting, rate design and valuation.

Q. Please describe your education and professional background and experience generally relevant to these proceedings.

A. My educational and professional experience in the public utility field is summarized in **Schedule HEL 1**.

In recent years, as President of Overland, I have been involved in a number of projects and regulatory reviews specifically relevant to the consideration of issues raised in this case. These include:

- A gas supply and pipeline procurement practices review of three LDCs with pipeline and/or supply affiliates (Mountain Fuel; Montana-Dakota Utilities and Wyoming Gas) on behalf of the Wyoming Public Service Commission.

- A financial and regulatory compliance audit of the Pacific Gas & Electric intrastate regulated gas Pipeline Expansion Project ($850 million construction cost) on behalf of the California Public Utility Commission. This project required a thorough review of CPUC pipeline competition, pricing and service policies, and specific issues associated with implementation.

- A cost of service and rate design analysis of Transok, an intrastate gas pipeline company, on behalf of the Oklahoma Attorney General. This analysis included policy testimony on optimal procurement criteria, and implementation of pipeline competition.

- A review of gas procurement policies and practices of Arkla, an LDC with sister company affiliate transportation and supply services, on behalf of the Oklahoma Corporation Commission. The project focused on policy issues affecting gas procurement in general, and as it specifically pertained to Arkla.

I have also provided testimony on behalf of KPOC in several proceedings before the Kansas Corporation Commission. I addressed various cost of service and financial issues in the Company's general rate proceedings in rebuttal testimony in Docket 190,362-U, dated September 1994. I testified on various cost of service, finance and rate issues regarding new gas supply and transportation contracts pending approval in Docket 192,506-U, dated May 1995. Finally, I addressed issues regarding the prudence of transportation and supply arrangements between Western Resources and Kansas Pipeline in Docket 97-WSRG-312-PGA, dated May 1997.

I have also been heavily involved in the Company's FERC Section 7 proceeding and other related matters over the last three years.

Q. What is the purpose of your testimony?

A. I will address the testimony of Staff witness, Mr. Mike Wallis and the issues he has brought before this Commission regarding the recommended disallowance of $4,532,449.60 in costs paid by Missouri Gas Energy (MGE) to MKP during the July 1, 1996 to June 30, 1997 time period. My testimony is organized as follows:

II. Overview of the Prudence Standard

Q. Mr. Lubow, have you or your consulting firm ever been retained to consider an appropriate definition of the prudence standard, and its application based on company specific circumstances?

A. Yes. Over the last 13 years, I have been involved in addressing both appropriate constructions of the prudence standard, and the application of such standards arising from specific decisions of utility managers. These reviews have included nuclear power projects, gas and coal procurement, and other decisions affecting utility operations. I have published articles, addressed utility conferences, and been quoted in trade publications regarding issues associated with the definition and application of prudence standards.

Q. Why is the formulation of a prudence standard necessary within the utility regulatory framework?

A. As a matter of public policy, a system of regulation is adopted to assure that utility rates, operations, and services are fair, just and reasonable. In the absence of a competitive marketplace, regulators must assure just and reasonable rates for consumers, utilities and investors.

While as a theoretical matter regulation is meant to substitute for competition, in practice it is not always a very close substitute or necessarily even a very good one. In this regard, Charles F. Phillips, Jr. in his book, <u>The Regulation of Public Utilities: Theory and Practice</u> (Second Printing 1985), at page 154 observes:

> (Regulatory) policies are shaped by various economic, social, and political pressures, so that regulation may seek other than competitive objectives (i.e., internal subsidies, lifetime rates). But even when economic objectives are sought, it is not easy to specify with any precision that competitive

standard which regulation should seek, for competition throughout the economy is imperfect. Consequently, as Lewis[1] has pointed out:

> It is probably true that regulation can never achieve more than a rough approximation of the results which perfect competition probably would have worked out in these industries – that is, it must be regarded as a "make-shift" for a condition of competition which never has existed and never can exist – and society must be prepared to accept some degree of maladjustment as inevitable.

Phillips points out that the goal of regulation as a replacement for competition also suffers from a practical limitation, specifically that regulatory agencies can neither acquire nor effectively utilize: "the range of data which influence a competitive market."[2] This inability of regulation creates "an inherent limitation which cannot be wholly overcome by an improvement in the regulatory structure or process."[3]

At least one aspect of this "regulation in place of competition" concept involves reviewing utility management decisions. This is because:

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[1] Ben W. Lewis, "Public Utilities," in L.S. Lyon and V. Abramson, Government and Economic Life, (1940) Volume II, at 625.

[2] Phillips, Id. At 154 quoting from former FCC chairman, Lee Loevinger's, Regulation and Competition at Alternatives," 11 the Antitrust Bulletin 101, 125 (1966).

[3] Id.

> Management of unregulated business subject to the free interplay of competitive forces have no alternative to efficiency. If they are to remain competitive, they must constantly be on the lookout for cost economics and cost savings. Public utility management, on the other hand, does not have quite the same incentive. Regulation must make sure that the costs incurred in the rendition of the services requested are necessary and prudent.[4]

This does not mean that the regulator should require public utilities to seek prior approval of managerial decisions nor that the regulator should actively interfere in day-to-day management decisions. Indeed, as Alfred Kahn observes:

> Effective regulation of operating expenses and capital outlays would require a detailed, day-to-day, transaction-by-transaction, and decision-by-decision review of every aspect of the Company's operation. Commissions could do so only if they were prepared completely to duplicate the role of management itself. This society has never been willing to have commissions fill the role of management and doubtless with good reason: it is difficult to see how any company could function under two separate, coequal managements, each with an equally pervasive role in its operations. Therefore, when the controlling decisions are made, they are

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[4] New England Power Co., 31 F.E.R.C. para. 61,047 (1985), at 61,083 (quoting Midwestern Gas Transmission Co., 36 F.P.C. 61 (1966), at 70, aff'd 388 F.2d 44 (7th cir. 1968) cert. denied, 392 U.S. 928 (1968).

> made in the first instance by private management itself. Regulation can do little more than review the major decisions after the fact, permitting here and disallowing there. In these circumstances they have been unable as a general practice to substitute their judgements for those of management; and often when they have tried, the courts have denied them the authority to do so, except in cases of obvious and gross mismanagement.[5]

Q. Is it ever possible to consider every detail that should have been considered by the decision maker?

A. No. The decision-making process can be very complex. It is never possible to go back in time and take into account every fact considered by the decision-maker, every fact that the decision maker should have considered but did not, the atmosphere and conditions under which the decision was made and numerous other factors. All that the Commission can do is to reconstruct, on the basis of limited data, the major and some of the minor factors involved in making the decision. The inability to reconstruct every detail that should have been considered by the decision maker is not particularly significant because the prudence process should not attempt to second guess management judgments concerning minor factors. Indeed, second-guessing based on minor factors is frequently merely an attempt to bootstrap hindsight into the analysis based on an adverse outcome that occurred after the decision was made. In fact, Staff

[5] Kahn, The Economics of Regulation: Principles and Institutions (1970), at 29.

representative Thomas Shaw agreed that it would be inappropriate to micro-manage the decision of MGE by dictating what the company could or should have done in early 1995, when the Mid –Kansas II Agreement was executed (See **Schedule HEL 2-1**, Deposition Transcript of Thomas Shaw, page 19, lines 17-23).

Q. What is the specific nature or need for a prudence standard?

A. For many years most commissions have resolved this question with respect to rate base items by determining whether the investment was "prudent." The genesis of this test is generally attributed to Justice Brandeis' opinion in Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Commission, 262 U.S. 276 (1923). Brandies' concurrence was premised upon the basis that the Missouri PSC order under review prevented the "utility from earning a fair return on the amount prudently invested…" (Id. At 289). He then defined "prudent investment" in a footnote that has been frequently quoted during the last 70 years:

> The term prudent investment is not used in a critical sense. There should not be excluded from the finding of the base, investments which, under ordinary circumstances would be deemed reasonable. The term is applied for the purpose of excluding what might be found to be dishonest or obviously wasteful or imprudent expenditures. Every investment may be assumed to have been made in the exercise of reasonable judgment, unless the contrary is shown.

Q. Please state for the record what you believe is an appropriate definition of the prudence standard.

A. For reasons I will further address, I believe the definition provided by the FERC in New England Power Co., 31 F.E.R.C. 61, 047 (1985), sets forth the test most consistent with sound public policy. In this case, FERC concluded that "the most helpful test" in resolving issues of "prudent investment" is the "reasonable man" test, which it defined as follows:

> In performing our duty to determine the prudence of specific costs, the appropriate test to be used in whether they are costs which a reasonable utility management (or that of another jurisdictional entity) would have made, in good faith, under the same circumstances, and at the relevant point in time. We note that while in hindsight it may be clear that a management decision was wrong, our task is to review the prudence of the utility's actions and the costs resulting therefrom based on the particular circumstances existing either at the time the challenged costs were actually incurred, or the time the utility became committed to incur these expenses.[6]

At least two important concepts appear in the portion of NEPCO quoted above. The first is the concept of evaluating management decisions by a "reasonable

[6] NEPCO, Id. At 61,084.

utility management" standard and the second is the inappropriateness of using hindsight in reviewing management decision. The "reasonable man" standard does not depend on what a particular person considers reasonable under the circumstances, but rather on a standard of reasonableness imposed by the public, utilizing the information available at the time such judgement or action is taken.

Q. Has the Missouri Public Service Commission embraced a similar definition of the prudence standard?

A. Yes. In *Union Electric*, 27 Mo P.S.C. at 194 (quoting Consolidated Edison Company of New York, Inc. 45 P.U.R.4th 331 (1982)), the Commission explained that:

> The company's conduct should be judged by asking whether the conduct was reasonable at the time, under all the circumstances, considering that the company had to solve its problem prospectively rather than in reliance on hindsight. In effect, our responsibility is to determine how reasonable people would have performed the tasks that confronted the company.

Thus, the Missouri Commission has also embraced the guiding principles expressed in *NEPCO*.

Q. Given an appropriate framework and definition of the prudence standard, please address the process and requisite evidence associated with potential findings by this Commission with regard to particular determinations of what constitutes prudent behavior.

A. Based upon my previous involvement in regulatory proceeding involving the application of the prudence standard, as well as my review of commission actions regarding what constitutes prudent behavior, the following evaluation process is normally followed.

- **Identify the various elements of the decision or decisions to be examined. What were the stated objectives and alternatives considered. What were the risks and consequences of choices available, and how were they weighed.**
- **Determine for each of the decision making elements identified whether the utility performed each of them and, if it did, the manner in which it did so.**
- **Ascertain how a reasonable utility manager would have performed each of these elements under the same or similar circumstances.**
- **Determine whether or not the decision making process, including the method of selection, was reasonable. If it was, the resulting decision was prudent.**
- **In considering the prudence of a decision, the Commission must avoid considering the consequences of the decision.**

Q. In your construction of the process required by regulators to evaluate the prudence of particular utility decisions or actions, you have raised the subject and relevance of applying the use of hindsight in evaluating management conduct. Please address the efficacy of the application of hindsight as a foundation for any conclusions regarding the prudence of utility management decisions and related actions.

A. **The outcome of a decision does not determine whether the decision was a prudent one. A prudent decision may produce negative results attributable to uncontrollable external factors while an imprudent decision may fortuitously lead to a favorable outcome. Thus, the Commission's focus must be on the circumstances at the time of the decision, and must avoid consideration of the consequences.** In evaluating the reasonableness of a decision, its outcome is irrelevant. The focus of a regulatory inquiry should be upon the reasonable foreseeability or risk that a specific decision will result in a negative or unfavorable outcome and whether the undertaking of such risk was reasonable under all of the circumstances that existed at the time the decision was made. Certainly all actions involve some potential risk of an unfavorable outcome; it is the likelihood and the potential extent of the negative outcome which decision making must focus upon. In evaluating the prudence of an individual decision, the Commission must assess the extent to which management evaluated each of the alternatives open to it, and considered the possible benefits and the respective risks.

Q. Is the utility decision making process subject to objective and precise analysis?

A. The decision making process, by its very nature, involves a degree of subjectivity and consequently lacks precision. To suggest that there cannot be more than one reasonable decision out of any array of possibilities would be an attempt to require that a decision be the "optimum" one which could have been made, thus ascribing to the decision making process a precision which it obviously lacks. Any other result would place the utility in the role of being a guarantor of its decision and imposing a standard of perfection, neither of which is appropriate. Thus, if a utility has selected from reasonable options available to it, the utility's decision should be found to be prudent, even if the decision turns out badly.

Q. Does the prudence standard require perfection?

A. No. The prudence standard requires that the alternative selected be among those that a reasonable utility management might have selected given the information that was known or should have been known at the time.

Q. Is there typically more than one prudent alternative?

A. Yes. Decisions, particularly those involving long-term commitments, require judgments concerning factors that are subject to considerable uncertainty. Each decision maker intuitively makes judgments concerning those uncertainties based on their own values, experiences and expectations. For example, some decision makers may be more risk adverse than others. As a result, there frequently is more than one prudent alternative that reasonably could have been selected by management.

Q. Does the prudence standard require the selection of the alternative with the lowest price?

A. No. All of the consequences of each of the available alternatives should be considered including non-price factors such as risk avoidance, service quality and supply flexibility.

Q. As a matter of sound public policy, are there adverse consequences associated with the application of unreasonable standards by regulators on the evaluation of utility decisions?

A. Yes. Good utility management should involve some risk taking. Always taking what appears to be the safest or least risky course of action does not necessarily result in the lowest costs to the ratepayer. Creativity and innovation by management necessarily means that it is engaging in new, and possibly untested activities where, no matter how well conceived, there always exists some risk of failure. In an environment where large penalties may be imposed by regulators as a result of what actually is, or may be perceived to be, an unreasonable construction or application of standards for utility conduct, utility managements will necessarily conclude that there is more risk in deciding to act affirmatively than in avoiding a decision or deciding not to act.

Q. How has the prudence standard been applied by MPSC Staff in these proceedings?

A. Based upon Mr. Wallis' testimony and Staff's responses to Data Requests of MKP/Riverside, it is evident that Mr. Wallis and Staff have failed to properly consider the meaning or application of the prudence standard, as addressed earlier in my testimony. The analysis and conclusions are based on a review of the ***results*** of these procurement decisions rather than the process by which the decisions themselves were made. As I have previously addressed, the courts, if not otherwise considered by regulatory agencies directly, have carefully avoided assessing utility decisions on the basis of the hindsight after the fact evidence provided by Staff in this proceeding.

III. Prudence of the Mid-Kansas II Agreement

Q. What are the fundamental objectives of the gas procurement function?

A. LDC's should employ practices and procedures that result in the procurement of gas in an optimal manner, consistent with safe, adequate and reliable service, while achieving overall minimum costs.

Q. On what basis should the reasonableness of gas procurement policies be evaluated?

A. In terms of gas supply and transportation choices, an appropriate portfolio can be defined as the lowest cost mix of gas supply, transportation and storage services that are sufficiently reliable to meet customer needs on a peak day and annual basis over time, but flexible enough to adapt to changing market conditions. Thus, any gas portfolio should be assessed in terms of economy, reliability, and efficiency.

Q. What general assessment criteria should be considered in any specific review of gas procurement activities?

A. In considering the relative achievement of the general objectives identified, a number of questions should be addressed including:

- Do the current supply and transport portfolios contain the appropriate mix of long term and short term contracts and high and low load factor supplies.
- Do current gas supply contracts offer adequate protection for peak periods.
- Can alternative supply and transportation sources offer comparable peak protection at lower expected costs.

Q. Does Staff's analysis, which examines one specific contract within MGE's overall portfolio, promote sound gas procurement strategies within the State of Missouri?

A. No. The overreaching statutory requirement for this Commission is to ensure that charges for natural gas are just and reasonable. In an era where local distribution companies are expected to compile portfolios of gas supplies and transportation;

some short, some medium and some long term contracts, some with fixed prices, some indexed prices and some reflecting spot market prices, an analysis that relies upon the hindsight review of one or a few of those contracts and labels them imprudent is antithetical to the very rationale for creating a portfolio of contracts in the first place. If a local distribution company could forecast the future perfectly, it would not enter into a portfolio of diverse contracts. The LDC would select one contract or a number of identical contracts. The primary justification for a diverse portfolio is based upon the limited ability to forecast significant variables that impact the procurement function in this industry. The measure of success of a portfolio of contracts is how well the mix of contracts serves the purpose or purposes the portfolio was intended to serve. In other words, is the local distribution company's portfolio designed to limit short-term price volatility, ensure effective competition, or create a diversity of supply sources?

Q. Assuming an appropriate construction and application of prudence standards, do you have an opinion of the prudence of the Mid-Kansas II Firm Gas Sales Agreement executed by MKP and MGE on February 24, 1995 (Mid-Kansas II Agreement)?

A. Other witnesses address the specific circumstances associated with the decision making process and the resulting decisions to enter into the Mid-Kansas II Agreement. Based upon this testimony, exhibits supporting such testimony, my review of documents available at the time of these agreements, and my knowledge of the industry environment at the time of this agreement, the decision to enter into the Mid-Kansas Agreement was clearly prudent.

Q. Were there any considerations that led the parties to recommit to a long-term agreement at this time?

A. Yes. A long-term agreement was essential to position MKP and its affiliates as a credible long term competitive alternative to WNG. The Mid-Kansas II Agreement put MGE in the position of having continued leverage over the pricing of WNG services. In order to provide that leverage it was necessary to maintain a viable threat that MKP and its affiliates could expand its pipeline capacity. Maintaining that threat required a pipeline that was financially sound and capable of financing expansion.

Q. Was MGE's decision to execute the Mid-Kansas II Agreement reasonable, from a gas supply management perspective?

A. Yes. Gas supply risks are managed by maintaining a portfolio of gas supply arrangements with differing durations and pricing terms. The gas industry restructuring imposed by FERC policy during this period, presented considerable uncertainties regarding the cost and availability of pipeline services. Contracting with a supplier that had proven its ability to provide reliable low cost gas provided a modest hedge.

Q. Does Mr. Wallis' analysis consider the advantages of the MKP alternative in the context of MGE's supply portfolio?

A. No. Mr. Wallis does not even discuss MGE's gas supply portfolio as it existed at the time the decision was made. Portfolio analysis is fundamental to consideration of gas supply procurement decisions. A decision that may be prudent in the context of one gas supply portfolio may be imprudent in another. Staff's failure to consider the Mid-Kansas II Agreement in the context of MGE's existing gas supply portfolio colors its conclusion. Even more remarkable, Mr. Wallis assumes that for purposes of calculating MGE's disallowance that 100% of the 46,332 MMBtu delivered by MKP would be delivered by WNG, even though that assumption means increasing MGE's reliance upon WNG, at a time when supply diversity was an explicit public policy objective being promoted throughout the natural gas industry. In fact, MGE has clearly indicated that decreasing their reliance upon WNG, during the period in question, was one of their objectives in constructing a prudent gas supply portfolio (See **Schedule HEL 3**, Deposition Transcript of Michael T. Langston, page 38, lines 23-25 and page 39, lines 1-2).

IV. Reliance on MPSC Actions

Q. Approximately how many regulatory proceedings have you participated in over your consulting career?

A. I do not maintain a record of my previous testimonies before regulatory agencies, or forms of involvement in regulatory proceedings. However, I believe that 200 would be a reasonable estimate.

Q. Who was your client in these proceedings?

A. I have been retained by utilities, state governmental agencies, and major customers. The majority of my consulting participation has been with state regulatory agencies, such as the Kansas Corporation Commission.

Q. Aside from your involvement as an expert witness in regulatory proceedings, have you had occasion to provide policy advice to senior commission staff, or to commissioners directly?

A. Yes. I have provided such services on numerous occasions.

Q. Are regulatory commissions bound by previous actions or orders within their jurisdiction in situations where the historical or factual circumstances have not changed?

A. Though technically not bound to legal doctrines such as res judicata, sound public policy requires consistency in the exercise of regulatory oversight of utility matters. As such, case specific actions of regulators found in historic orders should be considered binding. The absence of commitment and consistency to historic regulatory actions is not in the public interest. Utilities have an obligation to provide safe, adequate and reliable service to their customers. This requires significant, long term capital commitments. The cost of raising capital is largely a function of the risk perceived by investors that the utility will not be able to honor its commitments. Adhering to established precedents lower the level of risk perceived by investors, which in turn lowers the cost of attracting capital. In addition, a perceived risk that regulators will disregard the prudence standard in favor of a hindsight analysis test will result in less favorable terms. Thus, the long term cost of utility service is increased when utility decisions and actions are arbitrarily revisited or negated.

Q. You indicated previously that you have worked directly with utility commissioners and senior commission staff members in the review of utility issues and the formulation of regulatory policy. Have you ever advocated the reversal of past commission orders or findings regarding utility management decisions, or factual positions stated by regulators?

A. No. I typically attempt to exercise care that I review and carefully apply historic policy and findings contained in regulatory orders, regulations, or other sources of policy or company specific issues. My recommendations are in light of, not in spite of, existing regulatory policy guidelines and issue specific findings. It has been my experience that regulators are equally concerned with the consistent and equitable treatment of regulated utilities in their deliberation of issues brought before them.

Q. Is the Staff's recommendation in the public interest?

A. No. There is no legitimate basis to consider Staff's recommendation which turns the prudence standard on its head and focuses on a year to year review of price results, rather then evaluating the affected utility's decision making process. When MKP/Riverside inquired as to the basis for Staff's proposed disallowance, Staff did not claim the costs incurred by MGE were imprudent. Instead Staff merely states that their rationale for the proposed cost adjustment was that "MKP/RPC's total costs are higher than WNG's total costs." (See **Schedule HEL 4**, Staff's response to MKP/RPC's Data Request No. 36). That rational does not constitute a basis for disallowance. Utilities make many decisions every year which result in an array of prices from different suppliers. It would be rare indeed that utilities had identical prices from alternative suppliers in any one year. The mere existence of a price difference or a perceived price difference, cannot be the basis for a determination of imprudence. Staff witness Thomas Shaw concurred that price differentials do not provide a basis for disallowing a utility's costs. (See **Schedule HEL 2-2,** Deposition Transcript of Thomas Shaw, page 76, lines 1-16). Moreover, considering that Staff failed to recommend a disallowance of Panhandle Eastern Pipeline transportation costs that exceeded WNG's, on a per unit basis, Staff has applied their "price difference" standard in an arbitrary fashion (See

Schedule HEL 5, Staff's Response to MKP/RPC Data Request No. 26). In my review of Mr. Wallis' testimony, I found no evidence or alleged facts that even question MGE's decision making process at the time of the execution of the Mid-Kansas II Agreement. Staff failed to analyze the decision making process of MGE and has not presented any evidence as to the cause of what they allege are excessive costs. Staff presents no evidence concerning the surrounding circumstances existing at the time of MGE's execution of the Mid-Kansas II Agreement. In short, Staff has failed to present any evidence concerning the cause of what they believe to be excessive gas costs.

Q. Can you address the implications of the Staff analysis and related recommendations on other Missouri utilities?

A. The Staff recommendations, if logically followed, would require this Commission to review any contract or investment, regardless of its terms or conditions, that exceeds the lowest cost spot price for energy. Contracts that exceed the lowest cost in a portfolio at any given time would be written down to the lowest cost option. Energy costs, at least in the short run, would decrease substantially. The effect of the proposed recommendations on other utilities would trigger substantial civil litigation with supplier vendors regarding the application of contract terms. Where utility investments are disallowed, the investments would be written down, and defaults under commitments with lenders would quickly develop.

Q. Have you participated in specific proceedings in any other jurisdiction where the factual background was similar to the circumstances in this case?

A. As I indicated earlier, to the best of my knowledge, given the background of this case, Staff's analysis and recommendations regarding the Mid-Kansas II contract is unprecedented. However, the general background, and even the specific factors leading to contracting between these parties is not unique. Overland Consulting issued a report entitled "Independent Audit of Cost Segregation For the Pacific Gas & Electric Company's Pipeline Expansion Project" dated September 1994 and updated in October 1995. The Pipeline Expansion Project (PEP) was a 413 mile intrastate transmission pipeline from the Oregon/California border to the Southern California market area. This pipeline went into commercial operation in November 1993. Its regulatory history, however, originated in December 1988, when the CPUC initiated an investigation "to determine whether additional interstate natural gas pipeline capacity is needed to serve the requirements of California and, if such need is found, in what form it should be met."[7] Decision 90-012-016, dated February 7, 1990, provides the following description of the pipeline policy adopted by the CPUC:

> ...we believe that the time is right for us to guide and work with, rather than command and restrain, the competitive forces engaged in the pipeline market. First, regarding our LDCs, we have developed an appropriate

[7] CPUC Decision 90-02-016, page 5.

> record in this proceeding for modifying our prior position on additional capacity and for providing the guidance that the LDCs management needs. We fully expect the LDCs to exercise their own judgement to evaluate the pipeline capacity that best suit each utility's situation. Second, the condition we have announced for our willingness to support any given interstate pipeline project into California are crafted in large part to ensure appropriate assignment of costs to cost-causers. These conditions send a key message to potential users and sponsors of additional pipeline capacity. These conditions also protect the interest of the core ratepayers. Having established these conditions, this Commission has fulfilled its regulatory obligations and enabled competitive forces to work in ways ensuring that private risk taking will serve the public good.

In its Certificate Decision, the CPUC recognized that the allocation of risk was fundamental to its determination that the PEP was economically justified when it found that recovery of pipeline cost of service was subject to the demand for pipeline capacity. That having been said, the CPUC concluded that, "We will not second guess the decision of Expansion Project shippers to choose transportation over the Expansion at its rate instead of alternatives."[8] As the MPSC committed to fostering pipeline competition in the late 1980s[9] and early 1990s, so did the CPUC. It did so in an environment where a number of interstate pipelines were interested

[8] CPUC Decision 90-12-119, page 95.
[9] In MPSC Case No. GO-85-264, the commission compelled local distribution companies to provide open access transportation service in furtherance of established federal policy, thereby increasing competition in

in expanding their pipeline capacity into California. Ultimately, various pipeline expansions were constructed and put into commercial operation; including the Pipeline Expansion Project.

V. Financial Consequences of MPSC Staff Recommendations

Q. Could you explain how a proposed disallowance of MGE's costs affects MKP/Riverside?

A. Article 4.4(a) of the Mid-Kansas II Agreement provided:

> Should any regulatory authority having jurisdiction over Buyer [MGE] at any time deny Buyer the right to recover any amount paid to Seller [Mid-Kansas] hereunder, Buyer shall notify Seller of such denial within thirty days thereof, and Seller shall reimburse Buyer for the amount of such denial, with interest, with such reimbursement retroactive to the first day of service for which recovery is denied. Such funds will be paid by Seller to Buyer at the times and in the same manner as Buyer is required to refund such amounts to its customers (regardless of whether or not such denial may at such times be subject to appellate review).

Q. Have you considered the implications of Staff's recommended disallowance of $4,532,449.60 on the financial condition of MKP/Riverside?

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the gas industry. Additionally, in GA-89-126, the commission ruled that two suppliers would be beneficial to end users and transportation customers in the St. Louis market.

A. Consistent with the assertion of jurisdiction over our pipeline assets, FERC directed the consolidation of the Riverside and other pipeline assets earlier this year. The consolidated net income of our pipelines, excluding extraordinary items, for the twelve months ended December 31, 1997, was approximately $7.8 million. The consolidated net income of the pipelines for the eight-month period ended August 1998 was approximately $4.1 million. Our 1998 budgeted net income is $4.8 million. We are currently developing our 1999 budget, however, I expect that it will reflect a net income level which is lower than 1998. Therefore, the proposed disallowance, if imposed by this Commission, will virtually wipe out our 1999 expected earnings.

Q. How material is a $4.5 million write-off in relation to the total equity of these companies?

A. As of August 1998, the total equity of these companies was about $17.1 million. Therefore, a write-off of $4.5 million would represent an immediate reduction of our capital in excess of 25%.

Q. What impact would the proposed $4.5 million refund have on your compliance with long-term debt obligations?

A. Our long-term debt covenants require, among other things, that we maintain a "Debt Service Coverage Ratio" of 1.15 times or greater. A refund of $4.5 million, in combination with an expected decline in our 1999 earnings, could put the pipelines into default. Clearly, the proposed staff disallowance, if approved by the Commission, will have a material adverse financial impact on the Company.

<u>VI. Conclusion</u>

Q. Could you please summarize your conclusions

A. The arguments propounded by Staff testimony are without merit or foundation for the following reasons.

- Staff's analysis ignores any review of the decision making process or the decisions to enter into the agreements.
- Staff's analyses and recommendations are predicated on the <u>results</u> of the decisions and actions associated with the Mid-Kansas II Agreement; an approach that has been consistently rejected by regulators and courts.

For the above reasons, as well as other factors previously addressed in my testimony, Staff's recommended disallowance should be rejected.

Q. Does this conclude your testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of the Missouri Gas Energy's Gas Cost Adjustment Tariff Revisions to Be Reviewed in its 1996-1997 Annual Reconciliation Adjustment Account	))))	Case No. GR-96-450

AFFIDAVIT OF HOWARD E. LUBOW

STATE OF KANSAS)
) ss.
COUNTY OF JOHNSON)

Howard E. Lubow, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Rebuttal Testimony in question and answer form, considering of 29 pages to be presented in the above case; that the answers in the foregoing Rebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Howard E. Lubow

Subscribed and sworn to before me this 30 day of November, 1998.

FELICIA A. BODY
NOTARY PUBLIC
STATE OF KANSAS
MY APPT. EXPIRES 6/2/2002

Notary Public

My commission Expires: 6/2/2002

HOWARD E. LUBOW

General

Mr. Lubow has over 28 years of public utility experience with more than twenty-five years as a public utility consultant and four years as an employee of the Kansas City Power & Light Company. Since July 1997, Mr. Lubow has served in various senior executive capacities with the Kansas Pipeline Operating Company, and its affiliates. Throughout his career, his consulting engagements have encompassed a broad spectrum of management, organizational and regulatory issues for electric, gas, water, pipeline, and telephone utilities. These assignments have included focused management audits, analysis of utility diversification and acquisition plans, prudence studies, accounting systems design, cost of service determination and allocation, utility property valuation, rate of return determinations and rate design issues. Mr. Lubow has been involved in more than 150 regulatory and civil litigation proceedings and has testified in approximately twenty jurisdictions throughout the country.

Education

- Bachelor of Business Administration - Accounting, 1968, University of Missouri - Kansas City. Minor in economics.

- Graduate studies in quantitative and systems analysis, 1968-1970, University of Missouri - Kansas City.

Experience

- Directed a comprehensive review of the operation of a telecommunications incentive plan, based upon a revenue sharing mechanism, over a three-year period. The study reviewed quality of service measures, capital expansion programs, work force reductions, and other major elements of operating expense for the review period. provided policy options regarding modifications to the incentive plan for prospective consideration.

- Performed several REA workout studies.

- Performed a financial and market feasibility study of a fiber optic network designed to provide scada requirements for a large multi-state electric utility interested in selling capacity to telecommunications carriers and high volume customers.
- Developed business plan and other related materials for telecommunications reseller in its initial public offering. Provided ongoing financial and regulatory services, including development of all SEC filings.
- Performed a valuation study of a $300 million cellular satellite venture used in initial funding requirements for a consortium member. This work also involved due diligence developed for funding by current and new investors.
- Performed a valuation analysis of a cable TV operation. Developed a continuing property records system in connection with the valuation analysis.
- Sponsored the overall development of utility revenue requirements, jurisdictional and class cost of service studies and rate design issues in numerous electric, gas, water and telecommunication cases throughout the country.
- Developed utility valuation studies relied upon in determining full cash values for property tax purposes. The analysis included applications of the stock and debt method; direct and yield capitalization methods; and analysis of market transactions. These valuation studies have been relied upon in administrative and civil proceedings. Complete cost of capital analyses were developed based upon applications of the DCF and CAPM models.
- Directed an analysis of switching and other LEC facilities required and costs associated with the provision of interexchange services to an alternative service provider in the Phoenix, Arizona area.
- Performed a comprehensive due diligence analysis of a large capacity fiber optic network connecting Seattle and Vancouver, which included an analysis of market demand and pricing assumptions, competition, and anticipated construction and operating costs.

- Conducted an analysis of the adequacy of depreciation rates for a large independent telephone company located in Texas in order to assess the relationship of capital recovery in light of technological obsolescence.

- Developed and directed a three day nationally attended conference entitled "Competitive Strategies in the Local Exchange Marketplace".

- Directed and developed a two day training seminar for the Kentucky Public Service Commission addressing energy and telecommunications issues raised in rate filings, and utility planning and forecast models required in considering the use of projected test year data.

- Supervised and directed a group of PSC Staff members in the review of a rate filing relying upon the use of a projected test year.

- Directed a comprehensive financial and regulatory base period audit of a large gas transmission and distribution company in connection with implementation of an incentive regulation plan. Reviewed savings resulting from force reductions of 1,200 employees and implementation of aggressive cost reduction programs.

- Performed a study of an LDC's gas supply and transportation procurement practices in a post Order 636 operating environment, where the LDC's transportation and supply services continued to be provided by affiliated companies. The parent reorganized its pipeline transmission and gas supply services into a separate company, transferring jurisdiction from state regulators to the FERC. Developed a model to quantify an optimal supply and transportation mix for state ratemaking purposes.

- Performed a review of intrastate pipeline issues including the use of a straight fixed-variable cost methodology; regulatory treatment of stranded costs; pipeline competition issues; and the merits of a corporate restructuring and related effects on cost of service and changes in corporate operations.

- Developed a revenue requirement analysis of an intrastate gas transmission pipeline company addressing issues including: proper recognition of net operating loss carryforwards for ratemaking purposes; treatment of deferred start-up costs; application of criteria for consideration of acquisition premium in rates; and the recognition and relationship of financial criteria in the ratesetting process.

- Directed a comprehensive review of the $850 million PG&E gas transmission pipeline expansion project recently placed into commercial operation. This study included a review of regulatory considerations in recognizing construction and operating costs in light of competition in the California pipeline markets, and based upon the Commission intended allocation of risks among regulated customers, project shippers and the pipeline owner.

- Directed a review of gas procurement policies and procedures, and addressed the impact of FERC Order 636 for three Wyoming LDCs. This study addressed the relationship of gas pipeline and LDC affiliate organizations associated with the gas supply and transportation functions, and the impact of the affiliated organizational structures on gas prices measured against other utilities in the region.

- Reviewed impacts of FERC Order 636 on gas utility distribution companies including staffing and other operating requirements, changes in gas procurement and storage policies, and effects on marketing plans. Also reviewed various pipeline compliance filings, analyzing impacts on firm and non-firm customers.

- Reviewed electric and gas utility fuel procurement policies and procedures, organization and internal controls in various engagements. Developed recommendations resulting in significant benefits to utilities under review.

- Performed fuel audit investigations in several jurisdictions addressing such issues as economic dispatch procedures, fuel acquisition policies, affiliated mine or pipeline operations, captive mine development and compliance with Commission rules and regulations. These studies included the review of prices and returns produced from affiliated operations vs. third-party options and market prices available.

- Reviewed gas supply issues including procurement policies, supply mix, affiliate transactions, and contract provisions in the context of both cost of service and management review proceedings. Provided policy analysis regarding considerations and benefits of increased gas supply and pipeline competition.

- Participated in three FERC interstate pipeline rate proceedings addressing cost of service issues, including appropriate classification and allocation methodologies. Also addressed construction costs, overhead, and pipeline operations issues in a major oil pipeline docket.

- Performed a detailed analysis and presented testimony regarding the relative economic benefits of the operation of a LNG plant vs. meeting seasonal peak demands through pipeline contract commitments.

- Developed gas transportation pricing criteria and implementation guidelines in the development of tariff service offerings for several gas LDCs.
- Developed numerous gas cost service studies, and related rates design recommendations for local distribution companies, as well as pipeline suppliers. Testimony regarding such studies was presented before various state commissions, as well as the FERC.

- Responsible for gas distribution company revenue requirements in over twenty-five cases, addressing accounting, cost allocation, operations, and rate design issues. These cases generally included an analysis of gas production, gathering, and transmission systems owned by the LDC parent.

- Developed a damages model for a gas utility in civil litigation arising from acquisition of a defective distribution system caused by improper installation practices. Measured incremental construction and operating costs associated with pipe replacement program.

- Performed an analysis of the value of helium and helium extraction costs for litigation before the Federal District Court of Kansas. Review involved analysis of four major pipeline systems; construction and operating costs associated with pipelines and extraction plants; and analysis of incremental costs and revenues related in by-product liquid extractions.

- Developed a risk analysis model used to associate the relationship between cost recovery and changes in class consumption patterns for a gas distribution company.

- Developed a quantitative model to estimate jurisdictional and class-peak consumption for distribution gas companies.

- Performed an overview of regulatory considerations in the oversight of holding company formations and operations. This project was conducted on behalf of a PUC to analyze issues associated with holding company formations, utility diversification, and affiliated interest oversight and controls. The four largest electric utilities in the state were included in the study. The final report covered policy issues, as well as more detailed discussions of monitoring procedures and recommended filing requirements.

- Developed diversification guidelines for utilities in several jurisdictions. Addressed regulatory concerns and limits that might be implemented to control contingent adverse consequences to utility ratepayers.

- Performed an overview of regulatory considerations in the oversight of holding company formations and operations. This study addressed appropriate regulatory guidelines and oversight policies for utility and nonutility operations.

- Conducted a valuation analysis of electric and gas properties used by an electric utility in a tender offer in a $200 million plus transaction.

- Conducted a valuation study of an electric cooperative relied upon in court proceedings affirming a contested acquisition of an investor-owned electric utility.

- Developed regulatory and valuation models employed in the due diligence and offer price of over $150 million for natural gas distribution properties.

- Directed reviews of two major utility subsidiary gas intrastate pipeline systems, addressing cost of service, operating issues, and appropriate accounting for overheads and affiliated transactions from regulated electric utility parent companies.

- Developed a financing plan and reorganization of corporate structure for an electric utility having gas properties and a separate gas subsidiary. This project included preparation of SEC U-1 filings, filings with regulatory agencies and testimony to address the impact of the proposed financing and reorganization on cost of capital and rates.

- Responsible for the independent analysis of the feasibility and economics of consolidation of two major electric utilities. This in-depth twelve month study included a detailed review of the scope of services and basis of pricing such services among affiliates. The study addressed a number of affiliate interest issues including: the basis of pricing and level of capacity and/or energy supplied by affiliate vs. third-parties; the services provided by an affiliate "service" company vs. internal resources or purchases from third-parties; and the consideration of management resources devoted to non-utility functions and the basis of compensation for such resource transfers.

- Reviewed American Electric Power System Agreement to assess the reasonableness of fuel and purchased power costs incurred and allocated to its utility operating companies. The analysis also considered system dispatch and related fuel accounting issues associated with energy requirements of regulated customers versus wholesale transactions.

- Responsible for the development and implementation of phase-in plans utilized to defer initial costs of new generation facilities. Developed assessment criteria and related models to assign capacity from new plant additions between jurisdictional and nonregulated service.

- Developed and conducted a training program on the measurement of relative and absolute fuel productivity measures in ranking utility's effectiveness in fuel procurement and generation system operations.

- Conducted a feasibility study regarding the sale of a utility power plant used to provide steam heat and process steam to commercial customers through a downtown area distribution system. The feasibility study addressed energy alternatives and pricing options; cogeneration; and a financial and operating forecast assuming alternative case scenarios based upon various potential ownership structures. (1989)

- Developed a framework for implementation of competitive pricing for an electric utility facing higher costs due to nuclear plant additions. The analysis also encompassed an incentive rate program designed to induce greater use of excess capacity, as well as to improve the utility load factor.

- Analyzed and implemented economic dispatch models used to evaluate the effects of changes in generation capacity and fuel use.

- Conducted several comprehensive nuclear management and prudence reviews addressing construction, management, planning and economics issues.

- Directed a two-year study of the impacts on and options available to an electric utility due to the abandonment of a nuclear plant near completion. Presented a workout plan to regulators. Study involved a five-year forecast of financial results including construction expenditures and operating costs.

- Developed commercial operation date criteria and guidelines for nuclear power plants, which were supported by a national industry survey.

- Developed a financial analysis of a major municipal utility facing an extended outage of its nuclear power plant, with alternative pricing strategies, recognizing competitor pricing in adjacent service areas. Developed multi-year cost of service and revenue requirements models, and presented results to the Utility Board.

- Responsible for the development of budget and forecast models for a major municipal water utility in the midwest.

- Performed studies for municipalities to determine the feasibility of acquiring street lighting facilities, or in the alternative, pricing options other than PSC regulated tariffs.

- Conducted an industry survey of the effectiveness and relative benefits achieved from the use of uniform filing requirements in utility rate applications. The findings were published and distributed to the utility industry and regulatory commissions.

- Developed class cost-of-service studies including identification of direct assignments and review of distribution facilities, methodologies and criteria for the allocation of generation and bulk power facilities, and risk differentials associated with various classes of service.

- Directed an analysis of nuclear plant facilities performing an environmental protection function. Audit focused on identification of incremental costs incurred due to environmental requirements.

Publications and Presentations

- "The Use of Uniform Filing Requirements by State Regulatory Commissions - An Industry Survey," May 1980.

- "Regulatory and Accounting Implications of Phase-in Plans," NARUC Biennial Regulatory Information Conference, September 1984.

- "Rate Moderation Plan Considerations" Public Utilities Accounting and Ratemaking Conference, sponsored by the Texas Society of CPAs, April 1985.

- "Review of The Proposed Amendment to FASB Statement No. 71," Presentation to the Financial Accounting Standards Board, June 1986.

- "Regulatory Implications Associated with the Prudence Audit Process," NARUC Biennial Regulatory Information Conference, September 1986.

- "On the South Texas Project and Other Cases," The Advisory, March 4, 1987.

- "Regulatory Considerations Inherent in Assessing Utility Culpability" (Richard Ganulin coauthor), Public Utilities Fortnightly, 1987.

- "Framework for a Competitive Strategy," Southeastern Regional Public Utilities Conference, Atlanta, GA, September 1988.

- "Competitive Strategies in the Local Exchange Marketplace," a three-day telecommunications conference sponsored by Overland Consulting and the University of Missouri at Kansas City, September 1991.

- "Considerations Associated with the Review of Rate Applications Based Upon Projected Test Periods," a two-day training seminar conducted on behalf of the Kentucky Public Service Commission, December 1992.

- "Impact of Deregulation and Competition On Property Tax Valuation Within the Utility Industry," Western States Association of Tax Administrators, Austin, Texas, September 1995.

Work History

1997 – Present: **Kansas Pipeline Operating Company**
Executive Vice President, Chief Operating Officer, and Chief Financial Officer. As COO, responsible for the day-to-day operations of the pipeline companies. As CFO, in charge of the finance, accounting, and regulatory departments.

1991 - Present: **Overland Consulting**
President. Responsible for administration and review of management auditing, regulatory consulting, and litigation support services. Provide expert witness services in projects involving decision analysis, damages assessment, ratemaking, valuation, and accounting.

1983 - 1991: **LMSL, Inc.**

Chairman. Responsible for administration and review of regulatory services projects and research studies. Expert witness in regulatory proceedings. Director of special projects including management audits, financing feasibility studies, property acquisition and consolidation feasibility studies and development of innovative solutions to current regulatory issues.

1976 - 1982: **Drees Dunn Lubow & Company**
Partner - Utility Consulting Group. Responsible for projects for utility clients. Responsibility included financial and managerial analysis of public utility companies and the presentation of expert testimony before regulatory commissions.

1972 - 1976: **Troupe, Kehoe, Whiteaker & Kent**
Senior Regulatory Consultant. Responsible for special services work for utility clients, including accounting systems design, cost of service determination and allocation, budgeting and rate designs. Performed fair value determinations, developed cost analysis studies, curtailment requirements analysis, and forecasts of utility operations.

1968 - 1972: **Kansas City Power & Light Company**
Senior Accountant. Analyzed accounting and reporting procedures, taxes and costs of operations. Assisted in the preparation of the Federal and State income tax returns and the Annual Report to stockholders.

PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of Missouri Gas Energy's Gas Cost Adjustment Tariff Revisions to be Reviewed in its 1996-1997 Annual Reconciliation Adjustment Account.	) Case No. GR-96-450) October 28, 1998) Jefferson City, Mo.

DEPOSITION OF THOMAS SHAW,

a witness, produced, sworn and examined on the 28th day of October, 1998, between the hours of 8:00 a.m. and 6:00 p.m. of that day at the law offices of Brydon, Swearengen & England, 312 East Capitol, in the City of Jefferson, County of Cole, State of Missouri, before

KELLENE FEDDERSEN, CSR, RPR
ASSOCIATED COURT REPORTERS, INC.
714 West High Street
P.O. Box 1308
JEFFERSON CITY, MO 65109
(573) 636-7551

and Notary Public within and for the State of Missouri, commissioned in Cole County, in the above-entitled cause, on the part of MGE, taken pursuant to agreement.

Are you saying that they did not act imprudently? Or if they did act imprudently, I want you to tell me what they did that in your mind was imprudent.

A. What I thought I said is that MGE was aware of the concerns of the stacked reservation charges. They knew what the rates of the alternative pipeline suppliers are for a similar type of service. They were aware that dockets were pending before the Missouri Public Service Commission regarding the prudence of the contracts they were holding at that time.

And MGE took it upon themselves to renegotiate that contract knowing the fact that capacity was available on these other pipeline systems and knowing what the rates were on these pipeline systems.

Q. So what should MGE have done as opposed to what they did do?

A. I'm not in a position to micromanage the company and be fully aware of all the litigation and potential considerations that's being thrown back and forth between the parties to resolve litigation that's pending between themselves.

Q. What aspect of what MGE did do in this particular time period is imprudent in your mind?

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DEPOSITION OF MICHAEL T. LANGSTON,

a witness, sworn and examined on the 27th day of October, 1998, between the hours of 8:00 a.m. and 6:00 p.m. of that day at the law office of Brydon, Swearengen & England, 312 East Capitol Avenue, in the City of Jefferson, County of Cole, State of Missouri, before

KRISTAL R. MURPHY, CSR, RPR, CCR
ASSOCIATED COURT REPORTERS, INC.
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Notary Public, within and for the State of Missouri, in the above-entitled cause, on the part of the MGE, taken pursuant to agreement.

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Q. Is it generally safe to say that under Riverside I agreement the advantages you described earlier of the pricing provisions and the volume -- the volume limitations being lifted and the TRANSOK lease option are also embodied in the Riverside I agreement?

A. The first -- certainly, the commodity is not present in the transportation agreement, but all of the other terms and conditions are present there.

Q. Okay. I believe in earlier testimony today you indicated -- or a question was asked, describe the acquisition by MGE of Western's LDC assets as going into effect, I believe, in February of 1994; is that correct?

A. As mentioned, either January 31, '94, or February 1 of '94. I don't remember the exact date.

Q. Is it generally safe to say that at the time you acquired the Western Resources Local Distribution Company assets in Missouri that Western, and now MGE, was reliant, heavily reliant, on Williams Natural Gas transportation services?

A. Yes.

Q. In your duties for MGE during that time frame, did you have as one of your goals a desire to move away from reliance upon Williams as a supplier

just to diversify your transportation portfolio?
A. Yes.
Q. Okay. I maybe didn't write it down fast enough, so I apologize. Earlier, did you describe or identify the other local distribution companies that MGE or Southern Union own and operate? If you didn't, could you just briefly run down those?
A. Well, besides Missouri Gas Energy, we have Southern Union Gas Company, which is our division that operates properties primarily in Texas. We also have an ownership interest in the Piedras Negras distribution system in Mexico. There is only a minority interest in a company that's generally referred to as Conagas. I don't know that I can give you the Mexican name.
Q. Without pinning you down to exact numbers, do you know approximately how many residential customers Southern Union or its divisions serve as a local distribution company?
A. Approximately, a million.
Q. And how many total cities, would you estimate? More than ten? Less than 50? I'm just trying to get a ball park.
A. More than 100.
Q. More than 100. Okay. In your job

MKP/RPC DR No. 35

Identify all Staff members involved in Staff's examination of MGE's gas purchasing practices.

Staff's Response

Mike Wallis was the Staff person who examined MGE's gas purchasing practices during 1996/1997 ACA period

MKP/RPC DR No. 36

Please provide Staff's rationale for its MKP/RPC Pipeline Adjustment, and identify the Staff members involved with the formulation of such rationale.

Staff's Response

MKP/RPC's total costs are higher than WNG's total costs as shown in the Staff workpaper provided in response to MKP/RPC DR No. 1 and MGE's response to Staff DR No. 23. Please see Staff's response to MKP/RPC DR No. 19.c for a list of Staff members.

MKP/RPC DR No. 37

Identify and describe all options, futures, or similar contracts of MGE related to the 1996-1997 ACA period and the results of each.

Staff's Response

There were none to Staff's knowledge.

MKP/RPC DR No. 38

Provide all analysis, calculations, correspondence, documentation memoranda, tariff sheets, workpapers, or any other material used in the analysis of MGE's gas purchasing practices.

Staff's Responses

Please see Staff's response to MKP/RPC DR No. 15.

MKP/RPC DR No. 39

Provide the Staff's definition of "prudence", and identify by citation any and all Commission dockets where the definition of "prudence" has been applied.

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Q. I assume it's not your testimony that you expect an LDC to have transportation rates with various suppliers that are always identical; is that a safe assumption?

A. It would be a very rare occasion that they all would be identical, yes.

Q. So more often than not there is some differences between the transportation rates paid by the same LDC for -- or to different pipelines for firm transportation service?

A. That is not uncommon at all.

Q. So it's not your testimony that's imprudent, the fact that there is a difference, by itself that there are differences in reservation charges paid by the LDCs?

A. That's correct.

Q. Okay. Can you describe for me at what level you -- a difference becomes imprudent? Is it when there's a 10 percent difference, 15 percent difference, 20 percent? Where do you draw the line?

A. I think what we attempted to do when I was in the Procurement Analysis Department was any time a -- because if we hadn't challenged the contract when it was executed, and a lot of times we came in and some of the contracts were in like the fourth year of

Staff's Response

The requested information is available for review in the Commission's public records room and/or the Staff's offices in the Truman Building.

<u>MKP/RPC DR No. 24</u>

Provide copies of MGE's (or its predecessor's monthly PGA filings, and the workpapers and documents supporting such filings, covering the 1991 through 1996 ACA periods.

Staff's Response

The requested information is available for review in the Commission's public records room and/or the Staff's offices in the Truman Building.

<u>MKP/RPC DR No. 25</u>

List any and all gas suppliers who provided sales service to MGE at prices in excess of WNG during the 1996-1997 ACA period, and identify and explain all the reasons Staff did not recommend an adjustment to reduce MGE's gas costs resulting from the purchase of that gas.

Staff's Response

During the 1996/1997 ACA period, MKP/RPC and PEPL are the only other entities that can be compared to WNG in terms of transportation costs. Staff, in its adjustment, has recognized the lower gas supply costs on MKP/RPC versus WNG by including a $3,166,310.47 offset to the higher MKP/RPC transportation costs. In addition, Staff would note that WNG does not provide sales service.

<u>MKP/RPC DR No. 26</u>

List any and all natural gas transportation suppliers who provided transportation service to MGE at prices in excess of WNG during the 1996-1997 ACA period, and identify and explain all the reasons Staff did not recommend an adjustment to reduce MGE's gas costs resulting from the purchase of that transportation.

Staff's Response

PEPL was slightly higher than WNG in terms of FERC transportation rates. Staff did not propose an adjustment in this regard because the difference in rates between PEPL and WNG was not material in comparison to the MKP/RPC rates versus the WNG rates.