Exhibit No.:	
Issues:	Rate Design
Witness:	Joel McNutt
Sponsoring Party:	MO PSC Staff
Type of Exhibit:	Surrebuttal Testimony
Case No.:	GR-2014-0007
Date Testimony Prepared:	April 3, 2014

MISSOURI PUBLIC SERVICE COMMISSION

REGULATORY REVIEW DIVISION

SURREBUTTAL TESTIMONY

OF

JOEL MCNUTT

MISSOURI GAS ENERGY

CASE NO. GR-2014-0007

Jefferson City, Missouri
April 2014

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy,) Inc.'s Filing of Revised Tariffs to Increase) its Annual Revenues for Natural Gas)	Case No.: GR-2014-0007

AFFIDAVIT OF JOEL MCNUTT

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Joel McNutt, of lawful age, on his oath states: that he has participated in the preparation of the following Surrebuttal Testimony in question and answer form, consisting of 10 pages of Surrebuttal Testimony to be presented in the above case, that the answers in the following Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true to the best of his knowledge and belief.

Joel McNutt

Subscribed and sworn to before me this 3rd day of April, 2014.

Notary Public

SURREBUTTAL TESTIMONY

OF

JOEL MCNUTT

MISSOURI GAS ENERGY

CASE NO. GR-2014-0007

Q. Please state your name, title, and business address.

A. Joel McNutt, Regulatory Economist, MO Public Service Commission, P.O. Box 360, Jefferson City, MO 65102

Q. Are you the same Joel McNutt that contributed as a witness to the Missouri Public Commission's Staff's ("Staff's") Class-Cost-of-Service and Rate Design Report ("Staff COS Report") filed on February 7, 2014, and filed Rebuttal Testimony on February 28, 2014?

A. Yes.

Q. Please summarize your surrebuttal testimony.

A. The purpose of my surrebuttal testimony is to address Missouri Gas Energy ("MGE") Witness Mike Noack's rebuttal testimony regarding MGE's modified proposal on the sculpted rate , and respond to the major themes of Office of Public Counsel's ("OPC's") witness Barbara Meisenheimer's rebuttal testimony on the Rate Design.

MGE Witness Michael R. Noack

Q. Does Staff agree with Mr. Noack's revised proposal to limit the customer charge during the winter months to $32.84, as presented in his rebuttal testimony, to accommodate concerns expressed by MGE's customers at the local public hearings over MGE's proposed "sculpted" seasonal rates? As Mr. Noack points out, this reflects a 75%

reduction in MGE's originally proposed seasonal winter customer charge while at the same time allowing the full $7 dollar decrease in customer charge over the summer months.

A. No. As stated in my rebuttal testimony, Staff remains opposed to MGE implementing "sculpted rates" in its current Straight Fixed Variable ("SFV") rate design and continues to assert that the Company has not provided any studies or empirical evidence to show that seasonal rates, at any proposed level, will have the desired effect of decreasing summer disconnects for MGE.

<u>Office of Public Council Witness Barb Meisenheimer</u>

Q. In her rebuttal testimony OPC witness Barbara Meisenheimer refers to "low use" customers and insists that these customers are overpaying and harmed by the SFV rate design. Is the term "low usage customer" defined by any formal description or understanding in the natural gas industry?

A. No. Staff points out that this is a generic term and that there is no formal definition to identify what qualifies a low usage customer. Every utility defines this term differently based on the utility's own customer base usage dynamics. Thus, it is hard to identify which customers fall into a "low usage" category according to OPC. Further, it is difficult to distinguish which customers, according to OPC, that might be disadvantaged by the SFV rate design. The SFV rate is designed so that MGE's customers pay only what it costs MGE to provide gas service. Customers of MGE should pay no more and no less than MGE's actual costs to provide them with gas service.

Q. Regarding warmer versus cooler-than-normal heating seasons, what are the benefits, if any, of OPC's proposed return to the past volumetric rate design?

A. There are no “benefits” to the customer or the company. Ms. Meisenheimer states in her rebuttal testimony that the SFV rate design relieves shareholders of the risk of warmer than normal weather. But she ignores that the utility’s customers are also protected from overpaying their cost of service in colder than normal weather.

Even though a customer might pay less during warmer than normal heating seasons under OPC’s proposed volumetric rate design, that customer would also pay significantly higher bills in colder than normal heating seasons such as in this past winter.

The Commission has supported the SFV rate design in MGE’s last two rate cases [GR-2006-0422 & GR-2009-0355], reasoning that the SFV rate design mitigates weather risk for both the Company and the customer. In addition, the Commission extended the SFV rate design to MGE’s SGS class in GR-2009-0355:

Report and Order, page 52:

> “The Commission finds this issue in favor of MGE. With SFV, high-use consumers will stop paying a disproportionate share of MGE’s operating expenses. Month-to-month volatility of bills will be reduced. Consumers still retain control over a majority of their monthly natural gas costs. Ratepayers interests will be aligned with the interests of the shareholders because of the removal of the disincentive for the utility to encourage natural gas conservation. MGE shall continue administering its Straight Fixed Variable rate design into its residential customers, and shall administer it to its Small General Service customers”.

Q. Ms. Meisenhiemer also asserts in her rebuttal that “Staff’s position on this issue does not reasonably balance the interests of the Company and its customers”. Do you agree:

A. No. The SFV rate design achieves a balance of interests because it protects both the customer and the company from the effects of changing weather. In the context of this case, Staff agrees with the assessment made by Company witness Mr. Russell Feingold in his rebuttal testimony in GR-2009-0355, “Weather is beyond the Company’s control as recognized by regulators throughout the U.S.”

And;

> “When SFV rates are properly designed and implemented, circumstances such as changing weather conditions, additional customer conservation prompted by customer initiatives, gas utility initiatives and even electric utility initiatives, and price elasticity have less impact on the expected revenue than under volumetric rates. However, even with SFV rates, there is no certainty of revenue for the utility. Recognizing that revenue is only part of the equation for determining if there is a reasonable opportunity for the utility to earn its allowed rate of return, it is obvious that where fixed costs are such a significant part of the total costs and that variable costs are essentially matched dollar for dollar through the utility’s gas cost adjustment mechanism, any rate design that causes significant variations in revenue cannot provide the utility with a reasonable opportunity to earn its allowed rate of return.”

Q. Has Public Counsel offered any new evidence in support of its position that consumers are somehow better served by linking their cost of service payment to the variability of the winter heating season?

A. No. Staff has seen no new studies or evidence that would support Public Counsel’s position to return to the past volumetric rate design. Staff maintains that introducing a volumetric component into the existing SFV rate design would introduce more risk and fluctuations both in terms of “revenue” to the Company and “cost” to the customer. Neither of which are desirable outcomes and neither of which promote Company stability or protect customers from overpayment.

Q. What, if any, are the usage patterns and correlation between low income and high income natural gas customers in Missouri?

A. OPC improperly relies on the U.S. Energy Information Administration’s (“EIA”) 2009 Residential Energy Consumption Survey (“RECS”) and corresponding statistical evidence of a nine (9) state region. This survey shows a positive correlation between household income and natural gas usage in a nine (9) state Midwest region, of which 8 of the 9 states are north of Missouri. Upon further analysis of the 9 state region represented in this survey, a selective isolation of data related to only Missouri natural gas users shows that income has no significant correlation with consumption in that sample. In addition, there exists no correlation of this 9 state region to MGE's assigned Missouri service territory. As shown in Diagram 1 and 2 below.

Diagram 1

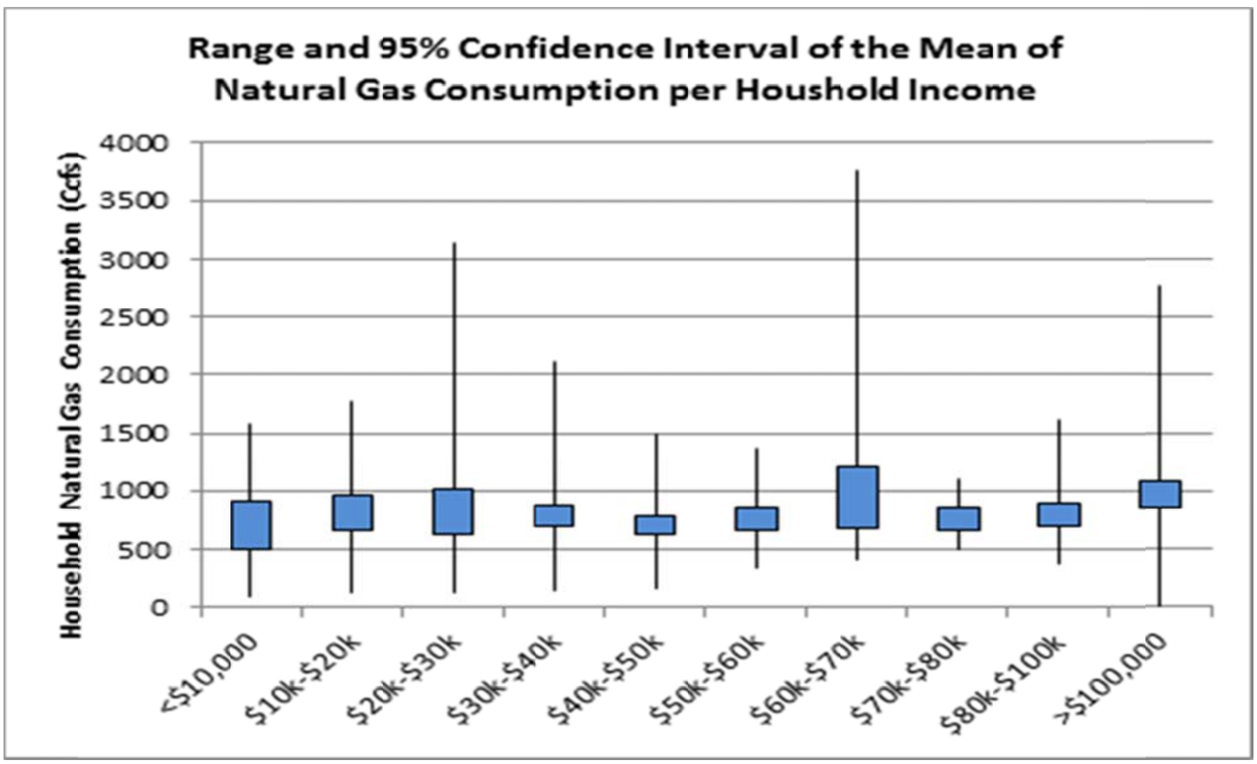
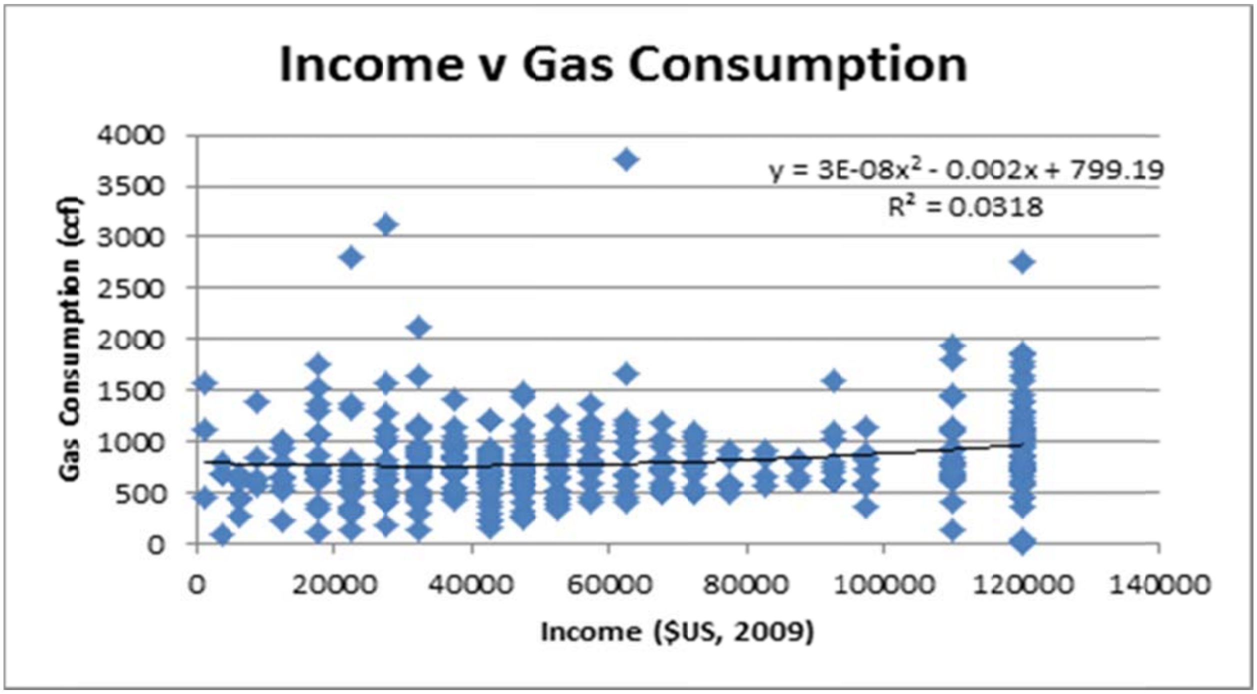


Diagram 2



(Source: http://www.eia.gov/consumption/residential/data/2009/)

Q. Explain the variable gas portion, Purchased Gas Adjustment ("PGA") component of customer's bill and its relationship to overall cost of service as it relates to the SFV rate design?

A. Under the SFV rate design all fixed costs are recovered in a fixed customer charge and variable costs are collected through a variable charge. As MGE witness Mike Noack points out in his rebuttal testimony for this case, approximately two thirds of a customer's total bill is directly related to gas commodity costs which are collected through a usage fee that varies with the amount of gas usage. Staff contends that the two thirds portion of the annual gas bill that represents the gas commodity sends a proper price signal to MGE customers that wish to adjust their gas consumption.

Q. What is Staff's position on including a volumetric component in the Residential and Small General Services ("SGS") Class?

A. Staff disagrees with the concept that a volumetric component in base rates is needed. Staff points out that at least 30 states throughout the U.S. have recognized the fundamental relationship of fixed cost pricing in utility ratemaking, and as a result have endorsed some form of decoupling [of the delivery charge from the gas usage charge]. Another 12 states are considering some form of decoupling. (Source: Revenue Regulation and Decoupling: A Guide to Theory and Application, June 2011;The Regulatory Assistance Project)

MGE witness Mike Noack points out in his rebuttal testimony that 25% of the customer's PGA gas commodity costs contain a fixed cost component. This fixed cost includes known demand charges or capacity reservation charges that are assessed by the Company's pipeline transporters. Mr. Noack points out that these fixed charges are not collected in a fixed delivery charge but are collected as an overall part of the actual gas commodity charge in the PGA. Therefore, as Mr. Noack correctly points out, low volume customers are actually paying less than they would pay if these PGA charges were purely treated as part of the fixed non-gas delivery charge.

Q. Ms. Meisenheimer discusses significant variations in usage that exist in MGE's Residential and SGS Class, and that those usage differences constitute different cost assessment among the Residential and SGS Classes. What is Staff's opinion on this matter?

A. Staff maintains the same position as Mr. Feingold expressed in his rebuttal testimony in GR-2009-0355:

> "A minimum installed size of distribution main will serve over 99 percent of the Company's residential customers given the average density of the Company's gas distribution system, its standard operating pressures, and the design day load characteristics of the customers served under the Company's RS rate class."

Mr. Feingold also testified that the same situation exists for the Company's SGS customers as well;

> "As I demonstrated in my direct testimony, the Company installs the same size meter, regulator, service line, and distribution main to serve virtually all SGS customers regardless of the monthly or annual volume of gas they use. The same situation exists for the Company's residential customers. This means that the size of the delivery service facilities is independent of gas volume and should, by Ms. Meisenheimer's own standard, be recovered through an SFV rate structure."

Staff contends that any variances in cost, born by the utility, to serve two different Residential or two different SGS customers are miniscule and cannot practically be recovered in a volumetric rate design. It is more equitable to recover these costs through a SFV rate design because these common costs are spread across each customer class because of the homogeneity of the Residential and the SGS customer classes.

Q. Ms. Meisenheimer states than several studies show that SFV rate design can negatively impact utility conservation and efficiency efforts. What is Staff's position on this matter?

A. Staff's position is that the tying of a portion of MGE's revenue directly to the amount of commodity it sells will have the adverse effect of dis-incenting utility efforts to promote energy conservation and energy efficiency programs. This fundamental principle goes against public policy because it creates an unnecessary barrier for the utility to promote energy conservation and efficiency.

Q. Ms. Meisenheimer cites in her rebuttal testimony certain conclusions regarding the SFV Rate Design that were published by the Not-For-Profit organization Regulatory Assistance Project ("RAP"). OPC's conclusion reflects a negative view of the SFV rate design. Does Staff agree with OPC's conclusions from this study?

A. No. Staff finds it curious that while the RAP study points out what it believes to be drawbacks with the SFV rate design, the study's ultimate conclusion favors SFV rate design:

> Conclusion:
>
> "Revenue regulation and decoupling provide simple and effective means to eliminate the utility throughput incentive, remove a critical barrier to investment in effective energy efficiency programs, stabilize consumer energy bills, and reduce the overall level of business and financial risk that utilities and their customers face.
>
> This guide has identified and explained key issues in decoupling for the benefit of regulators and participants in the regulatory process alike. Each utility and each state will be a little bit different, so there may not be a cookie-cutter approval that is right for all. However, the principles remain fairly constant: minor periodic adjustments in rates stabilize revenues, so that the utility is indifferent to sales volumes. This eliminates a variety of revenue and earnings risks, in particular those associated with effective investment in end-use energy efficiency, and can bring provision of least-cost energy service closer to reality for the benefit of utilities and consumers alike."

Staff agrees with this study's conclusion and recommends the continuation of the SFV rate design for MGE.

Q. OPC references Staff witness Dr. Michael Proctor's testimony from a previous rate case GR-2002-0356. OPC contends that Dr. Proctor states in his Surrebuttal testimony that Staff was unwilling to recommend recovering all of the non-gas costs in a fixed customer charge. What is Staff's opinion on this decision in GR-2002-0356?

A. Staff's recommendations from a 12 year old case involving another local distribution company ("LDC") are inapplicable to Staff's recommendations in this rate case. MGE's current rate design has been in effect since 2007 and has been approved by the Commission in two prior rate cases. OPC's comparison to a 12 year old rate case is not directly relevant and does not offer an "apples to apples" comparison and should not be considered.

Q. Does that conclude your rebuttal testimony?

A. Yes.