Exhibit No.:
Issue: Hedging Decisions
Witness: Randal T. Maffett
Sponsoring Party: Southern Missouri Gas Company, L.P. d/b/a Southern Missouri Natural Gas
Type of Exhibit: Rebuttal Testimony
Case No.: GR-2006-0352

SOUTHERN MISSOURI GAS COMPANY, L.P.
D/B/A SOUTHERN MISSOURI NATURAL GAS

REBUTTAL TESTIMONY

OF

RANDAL T. MAFFETT

Jefferson City, Missouri

October 19, 2007

BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of Southern Missouri Gas Company, L.P.'s Purchased Gas Adjustment Factors to be Reviewed In Its 2005-2006 Actual Cost Adjustment.)	)))	Case No.GR-2006-0352

AFFIDAVIT

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Comes now Randal T. Maffett, having been duly sworn, upon his oath and states that he has caused to be prepared the attached written testimony in question-answer form and attached exhibits to be presented in the above-captioned proceeding; that the answers and information contained therein are true and correct to the best of his knowledge, information and belief.

Randal T. Maffett

Subscribed and sworn to before me this 17th day of October, 2007.

Grace Raven
Notary Public
STATE OF TEXAS
My Comm. Exp. Nov. 16, 2010

Notary Public

My Commission Expires: 11/16/2010

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

REBUTTAL TESTIMONY
OF
RANDAL T. MAFFETT

CASE NO. GR-2006-0352

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Randal T. Maffett. My business address is 1001 Fannin, Suite 550, Houston, Texas 77002.

Q. ARE YOU THE SAME RANDAL T. MAFFETT THE PRESENTED DIRECT TESIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my testimony is to respond to the direct testimony of Commission Staff ("Staff") Witness Kwang Y. Choe in this proceeding. Essentially, Mr. Choe has alleged that Southern Missouri Natural Gas ("SMNG" or "Company") engaged in imprudent natural gas hedging practices for the winter months, November 2005 through March 2006. In addition, Mr. Choe asserts that SMNG failed to effectively hedge for the winter periods of 2005-2006 in violation of 4 CSR 240-40.018. Mr. Choe recommends that the Commission disallow between $220,000

and $378,000 from the Company's gas costs for the winter months, November 2005 through March 2006.

Q. WHAT IS THE BASIS OF STAFF'S CONCLUSIONS?

A. Mr. Choe identifies three primary issues in support of his conclusions. First, he asserts that SMNG failed to follow its Gas Supply Plan dated August 26, 2005. Second, he alleges that SMNG failed to follow Commission Rule 4 CSR 240-40.018, Natural Gas Price Volatility Mitigation. Third, he noted that SMNG fixed only the basis discount or differential from the New York Mercantile Exchange (NYMEX) when fixing a price for natural gas.

Q. WHAT ARE THE PRIMARY FINDINGS OF YOUR REBUTTAL TESTIMONY?

A. The primary conclusion of my rebuttal testimony is that Mr. Choe has not presented reasonable and supported evidence regarding SMNG's hedging decisions that would lead one to doubt the prudence of those decisions, under the circumstances that were known at the time of the decisions.

Mr. Choe has asserted that SMNG should have purchased fixed price contracts on specific dates, in addition to the basis hedges that SMNG utilized, and alleged that SMNG's failure to lock in prices was imprudent; however, Mr. Choe has failed to demonstrate that such decisions were in

fact unreasonable or imprudent based on generally-accepted prudence standards.

- Mr. Choe did not rely upon information and circumstances that existed at the time the decisions were made to support his analysis;
- Mr. Choe apparently failed to understand that the use of basis swaps or basis hedging was always a part of SMNG's Gas Supply Plan of 2005;
- Mr. Choe apparently failed to understand that SMNG considered the various pricing structures, mechanisms, and instruments contained in 4 CSR 240-40.018(2), including natural gas storage, fixed price contracts, call options, collars, outsourcing/agency agreements, futures contracts, financial swaps, and other tools utilized in the market for cost-effective management of price and/or usage volatility, as required by Commission's rule on Natural Gas Price Volatility Mitigation.
- Mr. Choe failed to mention that Staff witness David Sommerer was unwilling, based upon information that was available at that time, to recommend that SMNG lock-in fixed price contracts in the face of rising natural gas prices when Staff was given that opportunity in September, 2005;
- Mr. Choe's conclusions are the result of hindsight and ignore generally-accepted prudence standards utilized by

the Commission in ACA cases.

Therefore, Mr. Choe's proposed disallowance is unfounded and should be disregarded by the Commission.

STAFF ALLEGATION REGARDING SMNG'S GAS SUPPLY PLAN

Q. DO YOU AGREE WITH MR. CHOE'S SUGGESTION THAT SMNG FAILED TO FOLLOW ITS GAS SUPPLY PLAN FOR HEDGING?

A. No. As I explained in my Direct Testimony, SMNG was following its Gas Supply Plan during this ACA period. As was specifically mentioned in SMNG's Gas Supply Plan (dated August 26, 2005, p. 2), it was always SMNG's Plan to "continue to evaluate and monitor opportunities to use financial derivative contracts such as call options, basis swaps, costless collars and knock-out options as a means to provide better price stability to its customers." (Schedule RTM-R-1, page 2)(emphasis added).

SMNG personnel looked at the unique markets circumstances that existed during the summer and fall of 2005, and decided that using basis swaps (also known as "basis differential hedging") was a more reasonable and appropriate strategy than securing 60-75% of the winter heating season load at record high prices. SMNG never intended to execute basis swaps and

nothing else, however. SMNG fully intended on locking in its winter gas prices as called for in its Gas Supply Plan. By locking in basis differentials in favorable markets, SMNG had the opportunity to secure larger discounts from the NYMEX futures index and secure a lower overall price for its customers. However, the destruction that resulted from two hurricanes, Rita and Katrina, caused natural gas prices to spiral even higher to all time highs during the summer and fall of 2005, and effectively delayed SMNG's ability to lock-in prices using fixed price contracts.

Had the Company ignored its commitment to review the viability of basis swaps in its Gas Supply Plan and proceeded to mindlessly lock-in 60-75% of its winter heating-season gas supplies using fixed price contracts, it would have been locking-in some of the highest natural gas priced supplies in its history. Based upon the fundamentals in the gas market that existed at that time, and following its Gas Supply Plan of 2005, SMNG management felt that the most prudent course of action was to lock-in record high basis differentials, and then exercise those basis differential hedges when the natural gas prices moderated. SMNG followed this plan, and as result, SMNG's customers benefited from the use of these basis hedges.

Ultimately, SMNG executed basis differential hedges on two separate occasions; one at NYMEX minus 59 cents on July 26, 2005 and another at NYMEX minus 98.5 cents on September 2, 2005. Subsequently, on October 27, 2005, December 27, 2005, and January 3, 2006, SMNG entered into several fixed priced contracts for a substantial portion of its expected natural gas requirements for the winter load, and effectively utilized the basis differential hedges secured in July and September, 2005, to obtain a lower price for its customers for the winter.

Q. DOES MR. CHOE TAKE INTO ACCOUNT THE UNIQUE MARKET CONDITIONS THAT EXISTED AT THE TIME SMNG MADE ITS HEDGING DECISIONS IN THE 2005/2006 ACA PERIOD.

A. No. Mr. Choe merely recites SMNG's previous experience with fixed price contracts during typical winters, including 2002-2003, 2003-2004, and 2004-2005, without acknowledging the huge impact that the unique markets conditions of the summer and fall of 2005 had on SMNG's ability to prudently lock-in fixed price contracts at reasonable rates, as it had done in previous years. Mr. Choe also failed to acknowledge that evaluating and monitoring the opportunities to use basis differential hedging techniques were always part of the SMNG Gas Supply Plan of 2005.

Q. PLEASE ELABORATE UPON THE UNIQUE MARKET CONDITIONS THAT EXISTED IN THE SUMMER AND FALL OF 2005.

A. As I explained in my Direct Testimony, during the spring and summer months of 2005, NYMEX gas prices began approaching record high levels. However, the market fundamentals did not support the record high NYMEX prices. Fundamental market indicators were suggesting that the natural gas market was ready for a major correction to lower the price of natural gas. Natural gas storage levels were at all-time record highs indicating the lack of demand during the previous months. The winter of 2004 had been relatively mild and, as a result, storage withdrawals were significantly behind schedule leaving what ultimately was a record high surplus gas left in storage at the beginning of the spring injection season. Summer temperatures were also relatively mild across most of the country therefore electric air conditioning demand was substantially lower than expected. With record storage surplus and the lack of current electric generation demand, fundamentals indicated storage would be full much sooner than normal creating a glut of gas in the market.

Therefore, we concluded that these strong bearish signals of an oversupplied market would result in a major downward price correction. However, NYMEX prices were continuing to increase

to levels substantially higher than previous years without any fundamental support. If SMNG had locked-in its natural gas price during this period, as it had done in previous years, SMNG would have been locking-in at what were then record high prices and trying to compete with propane that was still being priced at steep discounts.

Q. DOES MR. CHOE DISCUSS THE MARKET CONDITIONS THAT EXISTED AT THE TIME SMNG EXECUTED ITS HEDGING PLANS?

A. No. While Mr. Choe testified that many factors, including "weather, oil prices, drilling rig counts, the level of electric generation from natural gas-fired combustion turbines, national storage levels for natural gas, the level of economic activity, war, and the psychology of the natural gas market participants," affect the price of natural gas (Choe Direct, p. 3), he does not attempt to analyze these factors or other fundamental market conditions that existed in the summer and fall of 2005. He provides the Commission with no insight into the market conditions that existed at the time SMNG made its hedging decisions and his analysis, by his own admission, is based 100% on hindsight.

Q. DOES MR. CHOE ACKNOWLEDGE THAT THE HURRICANES KATRINA AND RITA HAD A DRAMATIC IMPACT UPON THE PRICE OF NATURAL GAS?

A. Not directly. On page 3 lines 13-16 of his Direct Testimony, Mr. Choe identifies the factors that he believes affect natural gas prices. While he mentions "weather", he does not analyze the devastating impacts the hurricanes of 2005 had natural gas prices during the ACA period in this case.

Q. ON PAGE 6 OF HIS DIRECT TESTIMONY, MR. CHOE STATES THAT "THERE WAS LITTLE EVIDENCE TO WARRANT THAT THE NATURAL GAS PRICES WOULD FALL LATER ON [AFTER THE SUMMER OF 2005]". DOES HE PROVIDE ANY SUPPORT FOR HIS ASSERTION?

A. No. As I mentioned earlier, he does not discuss the fundamental market indicators that existed at the time SMNG was making its hedging decisions that clearly demonstrated to SMNG that a substantial market correction was likely to result in lower natural gas prices later in the season. Schedule 1 attached to Mr. Choe's testimony confirms, however, that a huge market correction was about to occur in January, 2006, as we were anticipating.

STAFF'S ALLEGATION CONCERNING THE GAS PRICE VOLATILITY MITIGATION RULE

Q. MR. CHOE ALSO ALLEGES THAT SMNG FAILED TO FOLLOW COMMISSION RULE 4 CSR 240-40.018. HAS THIS ALLEGATION BEEN DEALT WITH BY THE COMMISSION IN ANY OTHER PROCEEDING?

A. Yes. On October 21, 2005, the Office of the Public Counsel filed a Complaint against SMNG alleging that the Company had failed to comply with 4 CSR 240-40.018 in Case No. GC-2006-0180. Staff also participated in this proceeding.

On April 11, 2006, the Commission issued an Order Approving Unanimous Stipulation And Agreement in Case No. GC-2006-0180 which resolved all disputes between SMNG, Public Counsel, and the Staff regarding the allegation that SMNG had failed to comply with 4 CSR 240-40.018 in 2005. (Order Approving Unanimous Stipulation And Agreement, Case No. GC-2006-0180 (April 11, 2006). As a part of the settlement of the case, the complaint was dismissed, and the case was closed.

Q. WHAT COMMITMENTS WERE MADE AS A PART OF THE SETTLEMENT OF CASE NO. GC-2006-0180 RELATED TO SMNG'S HEDGING PRACTICES?

A. SMNG has committed, as a part of the settlement in Case No. GC-2006-0180, to follow a practice of purchasing fixed price contracts as follows:

> The Signatory Parties agree that SMNG's initial gas supply purchasing and hedging strategies plan to be filed on April 1, 2006, for the 06-07 winter heating season shall adhere to the following requirements: (1) SMNG will secure a minimum of 20% of normal winter heating-season gas supply at fixed prices or otherwise hedged against market exposure, no later than April 30, 2006, unless good cause is shown for deviating from this benchmark; (2) SMNG will secure a minimum of 40% normal winter heating-season gas supply at fixed prices or otherwise hedged against market exposure, no later than July 15 of 2006, unless good cause is shown for deviating from this benchmark; (3) SMNG will secure a minimum of 55% of normal winter heating-season gas supply at fixed prices or otherwise hedged against market exposure, no later than October 1, 2006, unless good cause is shown for deviating from this benchmark.
>
> (Unanimous Stipulation And Agreement, p.3, Case No. GC-2006-0180).

SMNG successfully completed this plan in the 2006-2007 winter, and has developed similar hedging plans for the upcoming winter of 2007-2008, and has now hedged its gas supplies for the upcoming winter.

Q. DID SMNG MAKE OTHER COMMITMENTS IN THE UNANIMOUS STIPULATION AND AGREEMENT THAT WAS APPROVED BY THE COMMISSION IN CASE NO. GC-2006-0180?

A. Yes. SMNG agreed to initiate a rebate program designed to encourage the installation of new energy efficient, ENERGY STAR® qualified natural gas furnaces in the Company's service area. In addition, SMNG agreed it will permit customers to enter into payment arrangements that would recover any arrearages above the minimum payment required under the

Commission's Cold Weather Rule, 4 CSR 240-13.055 to be re-connected to the natural gas system over an eighteen (18) month period rather than the twelve (12) period required by 4 CSR 240-13.055.

Q. NOTWITHSTANDING THE COMMITMENTS SMNG MADE RESOLVE CASE NO. GC-2005-0180, DO YOU BELIEVE THAT SMNG FOLLOWED THE REQUIREMENTS OF 4 CSR 240-40.018?

A. Yes. As I explained in my Direct Testimony, SMNG considered the various pricing structures, mechanisms, and instruments contained in 4 CSR 240-40.018(2), including natural gas storage, fixed price contracts, call options, collars, outsourcing/agency agreements, futures contracts, financial swaps, and other tools utilized in the market for cost-effective management of price and/or usage volatility. Because of its size and financial capabilities, there were only a limited number of hedging techniques that were realistically available for SMNG to utilize, and SMNG utilized the tools that it believed were most appropriate, under the unique circumstances that existed in the summer and fall of 2005.

STAFF'S PROPOSED HEDGING ADJUSTMENT

Q. PLEASE DESCRIBE YOUR UNDERSTANDING OF STAFF'S PROPOSED HEDGING ADJUSTMENT IN THIS CASE?

A. According to Mr. Choe's testimony and the Staff Recommendation filed in this case, the Staff is proposing one of three alternative adjustments based upon three sets of assumed conditions. Scenarios I and II assume that SMNG would have locked in the record high natural gas prices that existed on 7/26/05 and 9/2/05 in addition to the basis hedges that were locked in on those dates. Under Scenario I, SMNG would have locked-in 100% of its winter supplies, while Scenario II assumes that SMNG would have locked-in 50% of its normally required volumes for the winter. Scenario III assumes that SMNG would have locked in 54% of the normal winter volumes on 8/11/05 and 8/24/05 and also applied the actual basis differentials that SMNG had secured on 7/26/05 and 9/2/05.

Staff's proposed adjustment(s) are based upon a comparison of what the cost of gas hypothetically would have been had SMNG utilized the purchasing strategies assumed in the Scenarios, rather than using the Company's actual hedging and purchasing plan.

Q. DOES STAFF OBJECT TO SMNG'S USE OF BASIS DIFFERENTIALS?

A: No. According to Mr. Choe, Staff is not critical of SMNG's decision to use basis hedges for the winter months of November, 2005 through March 2006. In fact, Staff's proposed adjustments assume that SMNG obtained and utilized these record high basis discounts.

Q. WHAT IS YOUR UNDERSTANDING OF WHAT STAFF IS CRITICIZING ABOUT SMNG'S HEDGING ACTIVITIES?

A. As I understand Mr. Choe's testimony, Staff objects to the fact that SMNG did not lock-in the record high natural gas prices that occurred during the summer and fall of 2005. Mr. Choe has picked alternative sets of dates (i.e. 7/26/2005 and 9/2/2005, and 8/11/2005 and 8/24/2005), and made assumptions that if we had hedged on these specific dates, and if we had hedged assumed volumes, then our gas costs would have been lower. Staff then compares the cost of gas under these assumptions to the actual cost of gas as experienced by SMNG during the ACA period.

Q. DOES MR. CHOE ACKNOWLEDGE THAT HE IS USING 20/20 HINDSIGHT WHEN MAKING HIS PROPOSED ADJUSTMENTS?

A. While Mr. Choe does eventually acknowledge that his analysis is done after the fact with the benefit of 20/20 hindsight,

this critical and very fundamental fact is relegated to the very end of his testimony. This use of hindsight is a fatal flaw in Staff's approach to this entire case.

In reality, commodity markets are dynamic in nature and are constantly changing in response to market fundamentals. The decisions that SMNG and all LDCs make are based upon the best available information at the time of the decision, and unfortunately, we do not have the benefit of knowing what tomorrow's prices will be.

Q. ARE THERE INSTANCES IN WHICH THE COMPANY COULD HAVE HEDGED ITS GAS PRICES FOLLOWING MR. CHOE'S PROPOSED METHODOLOGY, AND THE RESULT WOULD HAVE BEEN THAT THE COMPANY'S GAS COSTS WOULD HAVE INCREASED?

A. Absolutely. Mr. Choe acknowledges that SMNG could have locked in prices for the winter volumes on many different dates prior to the winter season. However, he stated that Staff did not evaluate every conceivable date that SMNG could have locked in price, but merely selected three scenarios based upon when SMNG executed the basis differentials, or when it may have executed fixed contracts in previous years under substantially different market conditions.

Q. IF YOU ASSUME THAT SMNG WOULD HAVE LOCKED-IN FIXED PRICES ON DIFFERENT DATES THAN ASSUMED BY STAFF, WOULD THE RESULTS BE SUBSTANTIALLY DIFFERENT?

A. Yes. Like Mr. Choe, I now have the benefit of 20/20 hindsight and there are numerous examples of how SMNG could have locked in its gas prices consistent with Mr. Choe's suggested "prudent" approach to hedging using fixed price contracts, and ended up with higher gas costs overall. For example, Schedule RTM-R-2 demonstrates that if SMNG had locked in 35% of its winter supplies on August 25, 2005 and another 35% of its winter supplies on September 28, 2005, then SMNG's theoretical gas costs, under those circumstances, with seventy percent of its winter supplies hedged, would have been $363,642 higher than its actual gas costs for this ACA period.

Q. IF SMNG HAD PURCHASED FIXED PRICE CONTRACTS ON AUGUST 25, AND SEPTEMBER 28, 2005, FOR A TOTAL OF SEVENTY PERCENT (70%) OF ITS WINTER SUPPLIES, WOULD SMNG HAVE BEEN CONSISTENT WITH THE SMNG GAS SUPPLY PLAN OF 2005, AND STAFF'S APPARENT VIEW OF A "PRUDENT" HEDGING PLAN?

A. Yes. Under those assumptions, the Company would have been completely in compliance with both its filed Gas Supply Plan of 2005, and Staff's suggested "prudent" approach, yet it

would have cost SMNG's customers over $363,000 more than SMNG's actual experience!

Q. ARE YOU ACKNOWLEDGING THAT THE COMPANY'S GAS COSTS WERE NOT NECESSARILY AS LOW AS THEY COULD HAVE BEEN, BUT THAT THEY WEREN'T NEARLY AS HIGH EITHER?

A. Yes. As Mr. Choe's analysis shows, we could have reduced our costs (assuming we had the benefit of 20/20 hindsight), but we could also have significantly increased them by locking in fixed prices on other dates during this period. I have concluded that SMNG's actual gas costs were somewhere in the middle of the various combinations of costs that would have resulted from the various hedging strategies that could have been utilized.

Q. MERELY BY CHANGING THE ASSUMED DATES THAT THE FIXED PRICE CONTRACTS WERE PURCHASED, ARE YOU SUGGESTING THAT THE CONCLUSIONS WOULD HAVE BEEN DIFFERENT?

A. Absolutely. With 20/20 hindsight, it is possible to consider what would have been the absolute best time to lock-in, and what would have been the worst time to lock-in prices. However, this is not what the Commission should do when reviewing the prudence of the Company's actions. The SMNG

decision makers did not have this type of "perfect knowledge" about what prices were going to do when the hedging decisions were being made.

Q. DID STAFF EVER COMMUNICATE TO SMNG THAT IT BELIEVED THAT SMNG SHOULD LOCK-IN PRICES AT RECORD HIGH LEVELS DURING THE SUMMER OR FALL OF 2005?

A. No. Staff never communicated to SMNG that it believed the company should lock-in prices using fixed price contracts during the summer and fall of 2005, based upon the contemporaneous information that was available at that time.

Q. DID SMNG EVER REQUEST STAFF'S OPINION OF WHETHER IT SHOULD LOCK IN PRICES DURING THIS PERIOD?

A. Yes. During the hearings held in Case No. GR-2005-0279 on September 29, 2005, Staff witness David Sommerer was given the opportunity to recommend to SMNG whether to lock in its gas supply at that time (i.e. September 29, 2005), based upon the information that was then available to Staff. He declined to make any recommendations about whether the Company should lock in its winter supplies at that time, and testified that he did not know whether the prices would continue to go up for the rest of the winter. He also confirmed that had the Company locked-in the prices at that time that those prices would have

been more than twice the prices of the previous winter (Schedule RTM-R-3, Case No. GR-2005-0279, Tr. 158-160).

Q. IN YOUR OPINION, HAS STAFF PROVIDED EVIDENCE OF IMPRUDENCE IN THIS PROCEEDING?

A. No. In my opinion, Staff has not met any of the criteria for a finding of imprudence that I discussed in the Direct Testimony. First, Staff has not relied upon the information and circumstances that were available at the time of the hedging decisions were being made by SMNG. Second, Staff has not demonstrated that SMNG's actions and decisions were not within a reasonable and generally-acceptable range of behavior. Lastly, Staff was unwilling to communicate to SMNG that it believed SMNG should lock-in record high natural gas prices, when only contemporaneous information was available.

Q. DO YOU BELIEVE THAT SMNG'S HEDGING PRACTICES WERE PRUDENT UNDER THE CIRCUMSTANCES THAT WERE KNOWN AT THE TIME SMNG MADE ITS HEDGING DECISIONS?

A. Yes. Given the unique circumstances that existed at the time the decisions were being made, I believe that SMNG acted prudently in managing its gas supplies and hedging practices.

1 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY AT THIS TIME?**

2 A. Yes sir, it does.

GAS SUPPLY PLAN

SOUTHERN MISSOURI GAS COMPANY, L.P.

AUGUST 26, 2005

(This document is no longer considered confidential)

Schedule RTM-R-1

GAS SUPPLY PLAN
SOUTHERN MISSOURI GAS COMPANY, L.P.

August 26, 2005

I. OVERVIEW

The new millennium has brought about numerous changes to the natural gas industry including, but not limited to the collapse of many of the former major energy merchants, growth in the number of speculative financial traders, a dramatic shift in the overall supply and demand balance (gas-fired electric generating plants and LNG facilities) and the increased speed and availability of critical market-based information. All of these have had profound impacts on the challenges facing Southern Missouri Gas Company (SMGC) but most noticeably on price volatility and availability of supply.

SMGC's primary goals and objectives with respect to its gas supply requirements are as follows:

1) Reliability
2) Price stability and cost effectiveness
3) Flexibility
4) Plan for future growth, and
5) Regulatory compliance

Most industry "experts" are seemingly unable to agree upon the future direction of the natural gas industry, other than the fact that change will be more impulsive (faster-paced), more dramatic (bigger peaks and valleys) and more constant. Additionally, because of its rural-based markets, SMGC also faces very stiff and very real competition from the propane industry which is unregulated and has distinct competitive advantages versus natural gas.

In this environment our challenge is to formulate a gas procurement strategy which will allow SMGC to better serve its customers, mitigate its risks and maintain a position of flexibility from which to take advantage of favorable market dynamics. This illustrates the need for SMGC to not only remain proactive and creative in developing new strategies, products and services, but also the need to improve its efficiencies and its ability to anticipate, analyze and respond to ever-changing market conditions.

The following document serves as a written guideline which SMGC will utilize to meet its challenges in the coming years. It is constantly open to review and will be changed as necessary to anticipate and meet new challenges as they arise.

II. GAS SUPPLY GOALS & OBJECTIVES

Reliability
Previously, SMGC has had NAESB contracts with only two suppliers. However, under its new ownership and with a new strategy focused on growth, SMGC has executed two additional new NAESB agreements putting SMGC in a better position to:

a) reduce its overall gas cost through more competitive bid processes
b) diversify its supply and potential credit risk
c) reduce the potential impact of unforeseen supply disruptions, and
d) improve its position to mitigate dramatic price spikes during peak heating season

SMGC will also continue to evaluate the operational and cost effectiveness of building and utilizing propane/air injection facilities to meet peak day needs as well as provide operational stability to its system.

Price Stability & Cost Effectiveness
By expanding and diversifying its choice of suppliers, SMGC will also be better positioned to take advantage of favorable market movements and continuously secure gas supplies which provide better price certainty and remain more competitive with propane. SMGC will continue to evaluate and monitor opportunities to use financial derivative contracts such as call options, basis swaps, costless collars and knock-out options as a means to provide better price stability to its customers.

Flexibility
SMGC must also constantly monitor and analyze opportunities to diversify its access to new physical supplies. In conjunction with its market growth strategies, SMGC will analyze new opportunities to expand its interstate pipeline capacity as well as evaluate opportunities to build new pipeline interconnects. Additionally, SMGC will continue to evaluate and implement use of storage if and when available and economically feasible.

Plan for Future Growth
As SMGC continues to expand its current market penetration and its service to new markets, its supply and transportation requirements will continue to change. SMGC will continuously need to monitor its transport and supply options by maintaining regular communication and strong working relationships with Southern Star Central Gas Pipeline (SSCGP) as well as other southwest Missouri transporters in order to stay abreast of and involved in potential capacity expansion projects as well as utilize capacity release and/or sharing arrangements. As stated above, SMGC will continue to monitor and evaluate opportunities to diversify its physical supply options such as building new pipeline interconnects.

Regulatory Compliance
Historically, SMGC has had a very good working relationship with the MPSC and its Staff and will continue to work to improve the communication between both. In addition

to filing its annual Gas Supply Plan, SMGC will work harder to incorporate the Commission's expertise and feedback on a more dynamic, real-time basis which will provide additional sources of ideas and suggestions as well as hopefully streamline and reduce the overall cost of the annual ACA process.

III. CURRENT MARKET FUNDAMENTALS

Market Participants

As stated earlier, the natural gas market has experienced dramatic changes in recent years including the loss of many major market participants such as Enron, Dynegy, Williams, Aquila, Mirant, et al. While many of these were heavily involved in speculative trading, they were also major sources of supply as well as price discovery. Additionally, many of these same market participants were the major market-makers for longer term supply contracts as well as many of the financial risk management products. Their demise has also re-emphasized the importance of credit requirements in a commodity based market which has resulted in tighter and more expensive collateral requirements.

SMGC has also seen the introduction and rapid growth in the number of speculative financial traders such as hedge funds which do not add any value to the market itself but instead have created more price volatility as well as increased the frequency and magnitude of price shifts. The magnitude of funds under management and the immense liquidity it provides gives the fund managers significant influence in price direction as well as frequency, tenor and overall size of price movements.

Supply & Demand Balance

Since 2000, the continual decline in U.S.-based natural gas reserves along with the growth in natural gas-fired electric generating plants has created a shift in the overall supply and demand balance. The impact on the gas market has been increased price volatility as well as constraints on interstate pipeline and storage capacity and increased competition for limited physical supply. Peaking electric plants in particular can have dramatic impacts on intra-month as well as intra-day gas prices.

This shift in supply and demand has also generated significant upward movements in the price of both crude oil and natural gas which, in turn, has spurred an increase in oil and gas exploration. As a result there are numerous new players in the producing sector of the industry which will increase the number of supply options for SMGC. However, this potential new supply still faces the challenge of a finite amount of pipeline capacity to transport it from the supply regions to the end-use markets.

Additionally, there have been numerous LNG projects announced over the past few years which will create new market dynamics but will also face some of the same challenges, namely pipeline capacity constraints. Due to their physical and financial size, these projects also face significant hurdles with respect to geographic location, capital sourcing, permitting and environmental opposition which will render many of them

unfeasible. While their ultimate impact will be long-term, so is the lead time for construction and operational commissioning. Ultimately, LNG will become a major source of natural gas supply in the U.S. and it, too, will create change in the marketplace with respect to pricing, pipeline projects, storage and supply optionality.

Market Information

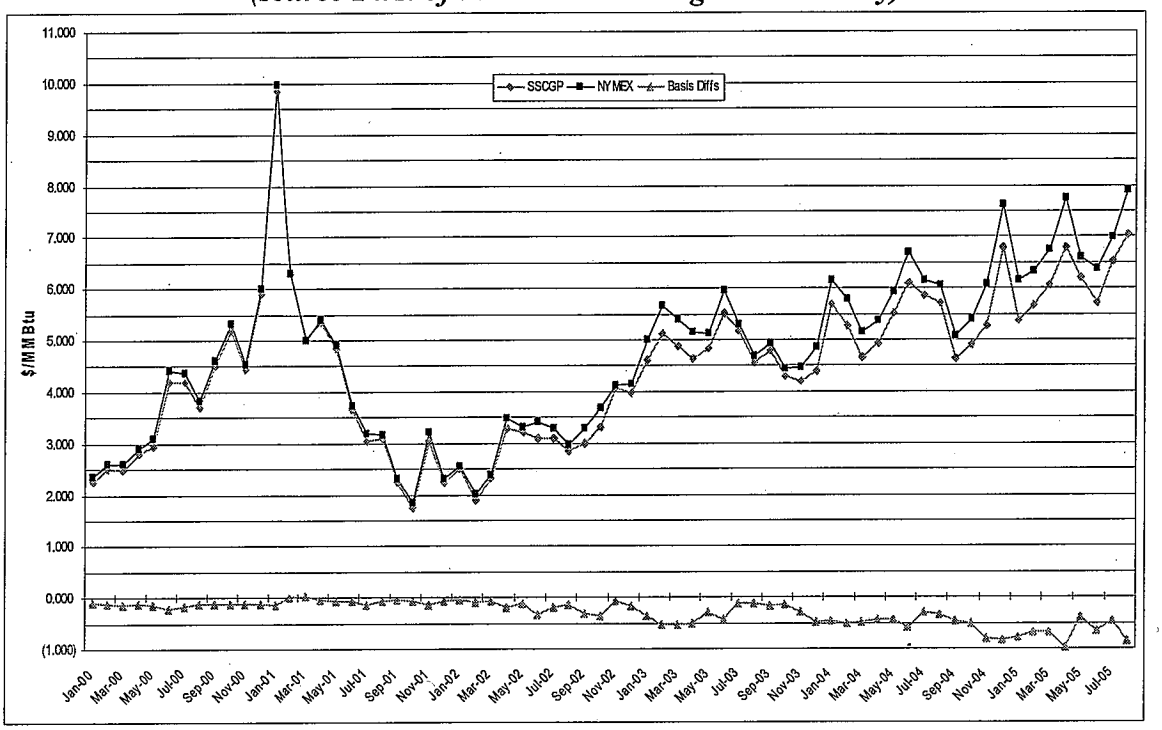
With the growth and technological advances of the internet, SMGC has seen a tremendous impact on the speed and efficiency with which market information can be transferred, processed and transacted. For example, EIA storage numbers, rig count information, weather reports, etc… as well as numerous economic indices are now reported in "real time" and with the growth in speculative market participants, the impact on gas pricing is both immediate and, in some instances, dramatic.

Natural Gas Pricing

As the graph below (Chart 1) provides an historical view of first of the month natural gas prices for both NYMEX futures contracts and the cash index for SSCGP. Some of the more interesting facts are as follows:

- Increased price volatility
- Widening in basis differentials (NYMEX vs. SSCGP)
- Significant upward trend in overall pricing, and
- Increased frequency in dramatic price shifts

Chart 1
SSCGP Index v. NYMEX
(source First of the Month Postings in Gas Daily)



All of these factors help illustrate an overall shift in market fundamentals and the need for companies in today's natural gas market to be well-informed and able to react very quickly to constantly changing market signals.

IV. SMGC MARKET ANALYSIS & SYSTEM REQUIREMENTS

Historical Market Perspective

After an initial period of meteoric growth due to the penetration of a new market, the last five years have seen SMGC's Residential (RS & OG rate classes) and Commercial (2GS rate class) markets become very stable with predictable average annual growth rates of 1.25% and 3%, respectively. SMGC has observed a customer class migration away from the OG class toward the RS class but it has not produced a significant impact upon our load profile. Overall SMGC's three customer classes' demand levels have become very predictable. SMGC has recently created a five year database which has proved to be an effective tool to predict demand levels by customer class based upon the customer count in each class, and the number of heating degree days expected. *(See Charts 2 and 3 below)*

Chart 2
SMGC Monthly Throughput

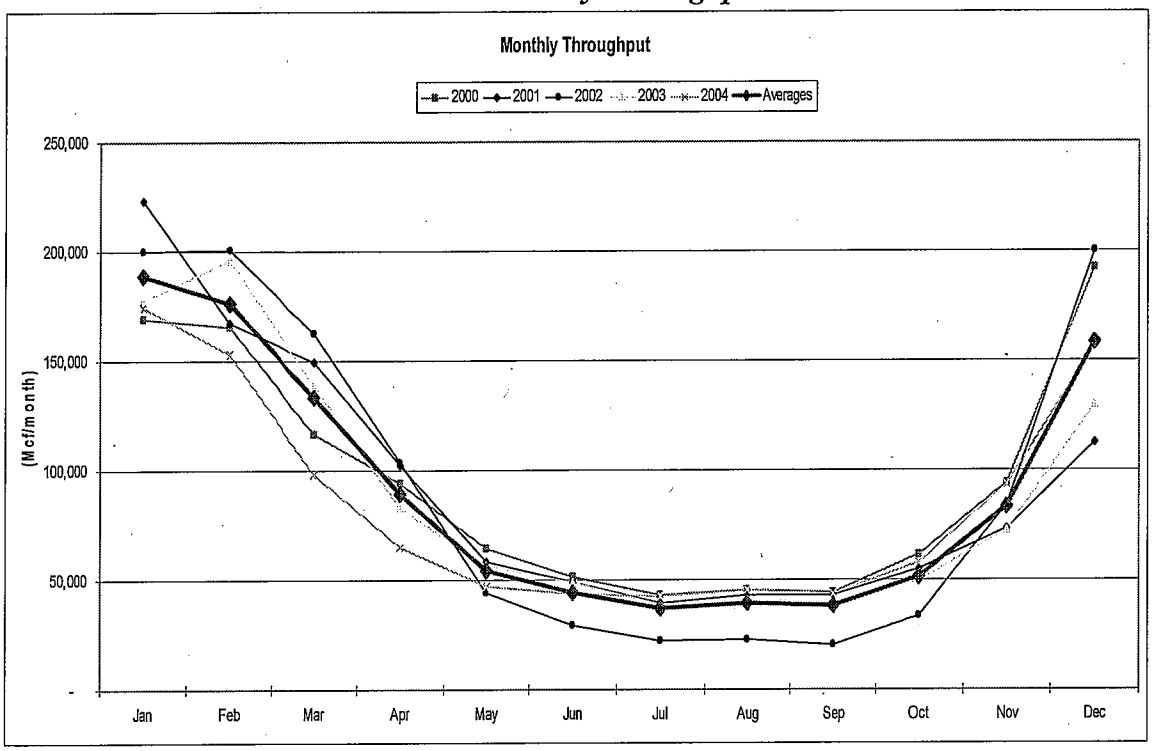
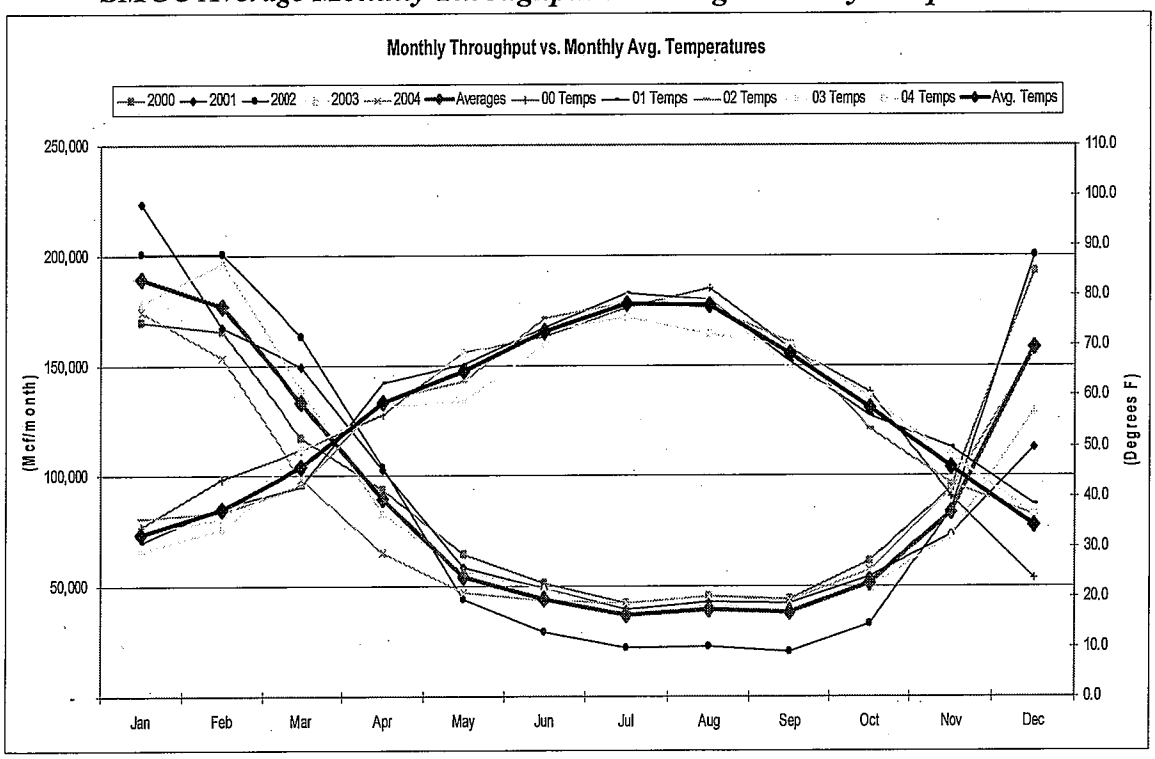


Chart 3
SMGC Average Monthly Throughput v. Average Monthly Temperatures



Significant Changes

SMGC's customer classes have seen significant change over the same period driven by several of its larger industrial customers switching from firm sales to transport gas as well as others switching part or all of their process load to alternative fuels. This has resulted in a net decrease in peak day needs of approximately 1,100 MMbtu/day. The relatively small growth experienced from these two customer classes plus the additional load for existing customers has only served to offset approximately 350 of the 1,100 MMbtu/day lost.

Determining Peak Day Requirements

In order to establish its gas supply needs for any given day SMGC can apply the number of customers in each of the 2GS, RS, and OG classes to a Base Load factor for that class (established in our data base), add to this the customer count applied to a Degree Day Factor for the class (also established in our data base) which is then applied to the expected number of Heating Degree Days and the result is our predicted consumption for each customer class for the given day. We then treat each of our LGS and LV customers individually as their needs can be more focused on their current levels of production than on HDDs. Adding all of the above gives us a forecasted gas requirement for a day based upon HDDs and other known contributing factors. (See Example Below)

Example #1:

Assume a 2GS customer count of 783
Assume a forecast of 72 HDDs
Baseload Factor .24918732Mcf/customer/day
Degree Day Factor .03151986698Mcf/Customer/degreee day
Thus ((783 x BF) + (783 x DDF x 72)) gives
((195) + (1,777) = 1,972 Mcf for the 2GS class for a 72 HDDay

Assume an RS customer count of 4,573
Assume the same 72 HDD
Baseload Factor .0451599Mcf/cust./day
Degree Day Factor .01224875409Mcf/cust/HDD
Thus ((4,573 x BF) + (4,583 x DDF x 72)) gives
((207) + (4,042) = 4,249 Mcf for the RS customer class for a 72 HDDay

Assume an OG customer count of 2,343
Assume the same 72 HDD
Baseload Factor .0323376Mcf/cust./day
Degree Day Factor .01020336974Mcf/cust/HDD
Thus ((2,343 x BF) + (2,343 x DDF x 72)) gives
((76) + (1,721)) = 1,797 Mcf for the OG customer Class for a 72 HDDay

This Totals 8,018 Mcf for a 72 Heating Degree Day for the above three classes
Add this to the 1,880 Mcf estimated daily demand for a 72 HDD for the LGS and LV classes assuming maximum levels of production
For a Grand Total Peak Day Calculated need of 9,898 Mcf.

Meeting Peak Supply Requirements

SMGC's gas supply plans include the pre-month purchase of a daily baseload of its estimated monthly requirements given normal HDD occurrence, and considering pre-month weather patterns. SMGC will supplement any needed intra-month gas on the spot market. SMGC will regularly monitor and utilize all available weather forecasts, and other load forecasting tools available to identify potential spot purchase requirements, and execute these purchases while simultaneously monitoring gas price market fundamentals to help ensure the lowest possible prices and the availability of gas. SMGC also has in place a peak-day call option contract for 5,000 MMbtu/day for any ten days on the Southern Star Central Gas Pipeline system to ensure adequate supplies even on peak days when additional gas supply may be more difficult to find.

Capacity Requirements & Reliability

SMGC has recently participated in an open-season for additional pipeline capacity on the SSCGP system to increase its reserve margin, and facilitate future growth. That prospective project is currently stalled due to the withdrawal of some participants, but SMGC is continuing to work with SSCGP independently to evaluate and secure additional firm capacity at cost effective pricing. SMGC has also recently received a quote for a Propane-Air Peak Shaving Plant as a possible alternative to obtaining additional capacity and are in the process of reviewing its feasibility as well other structural options. SMGC is also exploring a Peak Shaver sharing arrangement with neighboring LDCs who are faced with the same limited capacity dilemma which may prove to be the most cost effective method of assuring our continued reliability while facilitating continued organic growth. As a last resort, SMGC has available as a resource, approximately 2,000 MMbtu of usable line pack without adversely impacting system operations or integrity.

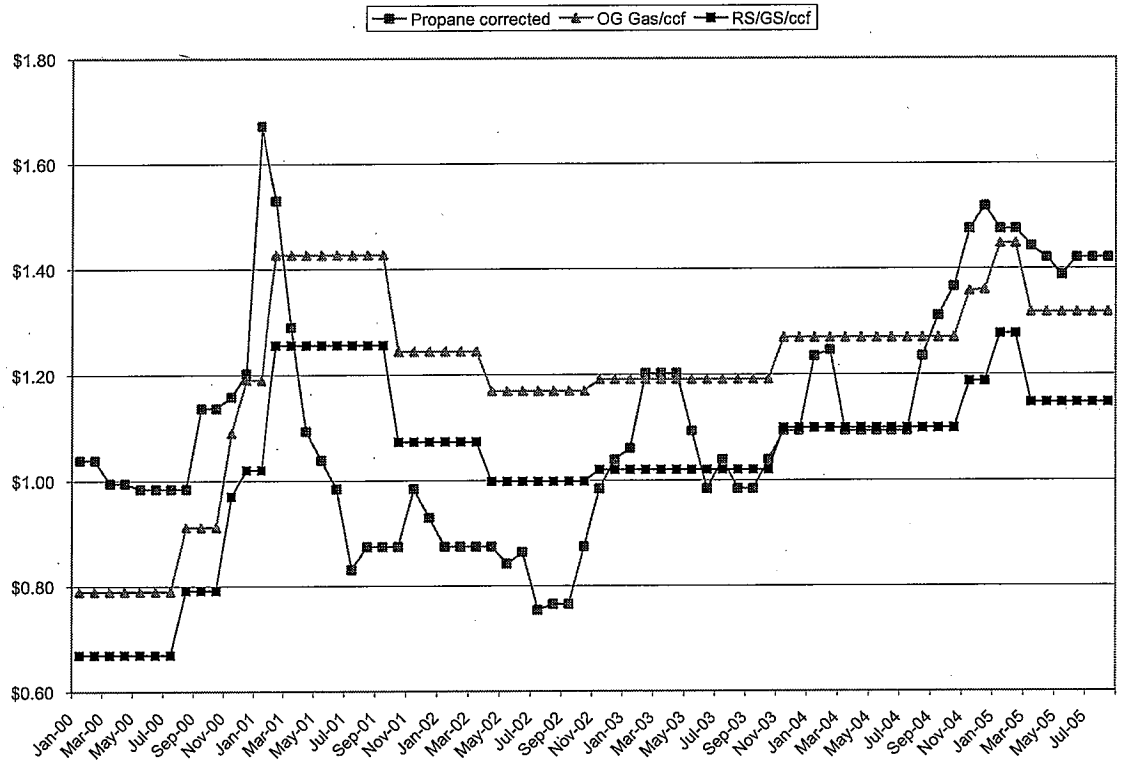
Competition

An important consideration in SMGC's overall gas supply plans and strategies is its ability to maintain competitiveness with local propane retailers. As unregulated fuel providers, propane dealers have the ability to offer multiple price structures as well as loss-leader pricing to undercut SMGC's tariffs on short term and/or on a customer by customer basis. They can also force their rental tank customers, and others who have no alternate fuel supply options, to subsidize any particular customer(s) as competition dictates. The following chart indicates historical local retail propane prices (corrected to 100,000 btu/unit) vs. our OG and our RS and 2GS rate (excluding customer service charges on RS & GS). On many occasions SMGC has inspected homes currently being served by propane and found their infrastructure to be substantially below regulated safety code. SMGC has experienced a number of situations whereby it has incurred the cost of upgrading a home to MPSC-regulated safety code only to have the homeowner switch back to propane . Finally, propane dealers have no restrictions with respect to the promotional practices they can employ to retain customers. Recently, SMGC experienced a situation where it wanted to bid on supplying natural gas to one of the

school districts in its service territory and was told "…don't even bother bidding, it won't be considered…"

As a direct result of the competition SMGC brought to our service area, local propane dealers were forced to initiate pre-purchase programs which allow their customers to fix their winter pricing by hedging their winter gas supply and pre-paying in the prior summer. The unregulated nature of our competitors' business creates an unlevel playing field and a difficult environment for SMGC to compete in and maintain compliance with the gas industry's regulations. As Chart 4 below illustrates, SMGC has recently gained a competitive price advantage, and it is uniquely poised to again make advancements into its market, and begin to consider market expansions. Its challenge then becomes identifying appropriate expansions, marketing them successfully, and at the same time assuring continued reliability to all of its customers by maintaining an adequate, but not excessive, capacity reserve margin.

Chart 4
SMGC Tariffs vs. Retail Propane Pricing



V. STRATEGIES FOR MEETING GOALS & OBJECTIVES

The management of SMGC has determined the best strategy to meet our goals and objectives is as follows:

(1) **Secure 60-75% of winter heating-season gas supply and 25-50% of summer baseload at fixed prices.** SMGC management will constantly monitor the market to identify the best opportunities to lock in prices and volumes for each respective season. For the winter heating season, we believe the optimum strategy is to transact in a series of 3-5 physical transactions as well as evaluate and procure, as feasible, peak day call options to cover extreme changes in load requirements. Summer baseload volumes generally are not sufficient to warrant the additional cost or administrative burdens of multiple transactions.

(2) **Continuously monitor and track consumption vs. supply on an ongoing basis.** Intra-month purchases may be necessitated by colder than expected weather patterns and/or under-estimation of consumption. SSCGP requires SMGC to be within +/- 5% of its monthly throughput and can be required to balance on a daily basis within +/- 3% in extreme circumstances. Management utilizes a combination of monitoring its system receipts and

customer usage as well as monitoring multiple weather forecasters in an effort to optimize its intra-month requirements.

(3) **Manage and optimize pipeline imbalances to (a) avoid penalties and (b) take advantage of price movements for the following month.** During the last 7-10 days of each month, management will review and compare month to date consumption vs. supply data to determine whether or not SMGC's system will be within SSCGP's imbalance tolerance limits. Additionally, management will analyze and evaluate historical load data and current weather patterns to predict the following months expected consumption. By comparing this to any fixed price and/or fixed volume contracts, management will be in a position to determine its optimum strategy with respect to rolling over any projected imbalances and/or procuring additional gas supply.

(4) Managing and controlling pipeline transportation costs will be a high priority for SMGC management. Every effort will be made to reduce SMGC's overall transportation cost including actively marketing SMGC's unused firm transport capacity on SSCGP. Management will continuously monitor peak-day requirements and take any and all steps necessary to ensure reliability of supply to its customers. Additionally, management will seek to utilize capacity-sharing arrangements where possible as well as evaluate peak-shaving facilities such as propane-air injection systems, both internally as well as shared facilities with other local gas distributors. Finally, SMGC will continue to build a strong working relationship with SSCGP personnel to better monitor growth and expansion opportunities to meet SMGC's short and long-term goals and objectives. While SMGC will endeavor to reduce its overall transport costs, it should be noted that the market and value for recallable firm capacity on SSCGP's southwest system is essentially non-existent, particularly during summer months.

(5) **Monitor, analyze and evaluate the potential to utilize financial derivatives to better manage price volatility and avoid or minimize extreme price spikes.** Utilization of various financial instruments such as swaps, call options, costless collars, knock-out options, etc… is a way for SMGC to minimize dramatic price swings while simultaneously maintaining its flexibility with respect to procuring physical gas supply. As discussed earlier, the collapse of the merchant energy sector has heightened the market's awareness of the importance of bilateral credit collateral. As a result, SMGC's management must be very aware of and astute with respect to (a) the cost of credit support and (b) counterparty default risk. While utilization of financial derivatives can be a very efficient method of managing price risk, it also involves transferring physical performance risk (i.e., buying fixed price physical gas) into credit risk, since a derivative is by definition a swap of money and not physical gas.

(6) **SMGC management and relevant staff should attend various gas/energy industry seminars, trade shows and other functions.** Active participation in these events produces multiple positive benefits for SMGC including:
   (i) Staying up to date on market dynamics, new projects, major discoveries, global events, etc… that can have an impact on the domestic U.S. supply and demand balance and resulting prices.
   (ii) Promote a higher awareness and understanding of new market participants, products and services being offered.
   (iii) Expand SMGC's presence within the gas industry which will provide opportunities to expand its supplier relationships.
   (iv) Provide SMGC first-hand perspectives of changes in market requirements (such as credit support) as well as an opportunity to be proactive in the process.

VI. VENDOR SELECTION & CRITERIA

Currently, SMGC is aware of approximately six active market participants on the SSCGP system. Historically, SMGC has had existing contractual relationships with only two of them. As stated earlier, we recently executed two new NAESB agreements with two new suppliers who actively market on the SSCGP system. While SMGC will always be receptive to new market participants, physical and financial performance is always most important in order for SMGC to deliver the level of reliability it has always provided to its customers.

With respect to physical gas supply contracts (NAESB), SMGC will perform its own internal financial analysis of any and all potential suppliers. Additionally, SMGC will analyze all suppliers' historical performance and experience with both itself and other customer references. Finally, SMGC will target suppliers with a minimum credit rating of BBB- (S&P) or BAA3 (Moody's).

For financial derivatives, a counterparty's performance is purely financial since there is no "exchange" of physical commodities involved. Therefore, credit risk is of a much higher concern. As a result, SMGC will target counterparties with a minimum credit rating of A- (S&P) or Aaa3 (Moody's).

In the event a potential supplier or financial counterparty is not a publicly traded company or does not have its debt publicly rated, SMGC will utilize its own internal credit review process to determine a potential supplier's creditworthiness on a case by case basis. SMGC will determine whether or not such a supplier will be required to post credit collateral such as irrevocable or standby letters of credit and/or other instruments in order to ensure performance.

VII. SUPPLIER BID & AWARD PROCESS

Fixed Price Term Contracts (Physical & Financial) – Upon analysis and confirmation of favorable or opportune market conditions, Request for Proposals (RFP's) will be sent to pre-qualified vendors by telephone, fax or electronic mail. Such RFP will contain all pertinent data, including relevant deadlines, to allow potential bidders to provide timely and accurate responses. Contracts may, in addition to other factors, be awarded on a combination of price, creditworthiness, flexibility of supply, historical performance and existing relationships with SMGC. All information relating to these RFP's including all bids requested as well as all bids received will be permanently recorded in the Gas Control Manager's records.

First of the Month Cash Purchases (Physical) – First of the month purchases will be processed and evaluated identically to the Fixed Price Contracts discussed above. The same criteria will be used in awarding contracts as stated above and all information pertaining to RFP's, responses and contract awards will be permanently recorded in the Gas Control Manager's records.

Intra-month Spot Purchases – For reasons discussed earlier in this document, these purchases can be very time sensitive due to market or weather conditions and/or system load requirements. Typically, these transactions are conducted by telephone and all relevant information will be permanently recorded in the Gas Control Manager's records. While similar criteria will be used as in Fixed Price and First of the Month Purchases, availability of supply and deliverability can be given priorities in times of extreme market environments.

VIII. STAFFING/RESOURCES AND RESPONSIBILITIES

Currently, gas procurement and the management of our transportation contracts is the primary responsibility of the SMGC's Gas Control Manager. Historically, all analysis and decisions made with respect to gas purchases or balancing issues have been done by the Gas Control Manager with minimal input from the parent company. Going forward, we intend to expand the overall involvement of all SMGC management, including operations, finance and accounting, customer service and sales/marketing as well as that of SMGC's new owners. The benefits from expanding those involved are numerous, including:

- Creating and supporting a culture of information sharing
  - Improving interaction and coordination between Gas Control, Operations, Finance & Accounting, Sales & Marketing and Customer Service managers
  - Promoting sharing of ideas and identifying opportunities and/or challenges
  - Optimizing problem resolution

- Providing more employees opportunities to be involved and gain a better understanding of SMGC's overall business
- Eliminating information "silos"

➢ Creating a system of redundancy
- Protecting against an unforeseen resource shortfall
- Providing more flexibility to respond to market dynamics

➢ Creating a system of "checks and balances"

The Gas Control Manager will continue with the primary responsibility for all transportation contract management and gas supply functions and in circumstances requiring immediate action will be authorized and empowered to make any and all decisions necessary to preserve the operational integrity of SMGC's system as well as provide the highest and most reliable level of service to SMGC's customers. The Gas Control Manager will also be responsible for recording and maintaining all necessary records with respect to all gas purchases and contracts, and will work with the Finance & Accounting Manager with respect to any and all MPSC requirements and inquiries including, but not limited to, its annual ACA audit.

Hypothetical Case

	Total Actual Monthly Volume	Total Projected Monthly Volume	35% NYMEX 8/25/2005	Basis Diff 8/25/2005	Adj SSCGP Price 8/25/2005	Theoretical Cost 8/25/2005	35% NYMEX 9/28/2005	Basis Diff 9/28/2005	Adj SSCGP Price 9/28/2005	Theoretical Cost 9/28/2005	Spot Gas Volume	WACOG Spot Gas Price	Theoretical Cost of Spot Gas	Theoretical Cost All Gas Purchases
Nov05	67,500	90,000	$ 10.379	$ (0.740)	$ 9.64	$ 303,629	$ 13.120	$ (0.760)	$ 12.36	$ 389,340	4,500	$ 10.59	$ 47,655	$ 740,624
Dec05	140,000	140,000	$ 10.739	$ (0.740)	$ 10.00	$ 489,951	$ 13.710	$ (0.760)	$ 12.95	$ 634,550	42,000	$ 8.84	$ 371,280	$ 1,495,781
Jan06	130,008	150,000	$ 10.999	$ (0.740)	$ 10.26	$ 538,598	$ 14.040	$ (0.760)	$ 13.28	$ 697,200	25,008	$ 8.64	$ 216,069	$ 1,451,867
Feb06	80,000	120,000	$ 10.974	$ (0.740)	$ 10.23	$ 429,828	$ 13.860	$ (0.760)	$ 13.10	$ 550,200	(4,000)	$ 6.87	$ (27,480)	$ 952,548
Mar06	80,000	90,000	$ 10.744	$ (0.740)	$ 10.00	$ 315,126	$ 13.440	$ (0.760)	$ 12.68	$ 399,420	17,000	$ 6.27	$ 106,590	$ 821,136
	497508	590,000				$ 2,077,131				$ 2,670,710	84,508		$ 714,114	$ 5,461,955

Actual Case

	Actual Monthly Gas Costs	"Theoretical" Gas Cost	Savings/(Loss)
Nov05	$ 840,795	$ 740,624	$ (100,172)
Dec05	$ 1,433,450	$ 1,495,781	$ 62,331
Jan06	$ 1,296,318	$ 1,451,867	$ 155,549
Feb06	$ 812,600	$ 952,548	$ 139,948
Mar06	$ 715,150	$ 821,136	$ 105,986
Totals	$ 5,098,313	$ 5,461,955	$ 363,642

Excerpt from transcripts in Case No. GR-2005-0279

September 29, 2005

(Cross-examination of David Sommerer)

Schedule RTM-R-3

BEFORE THE PUBLIC SERVICE COMMISSION

STATE OF MISSOURI

TRANSCRIPT OF PROCEEDINGS

HEARING

September 29, 2005

Jefferson City, Missouri

Volume 1

In the Matter of Southern Missouri Gas Company, L.P.'s Purchased Gas Adjustment Factors to be Reviewed in Its 2004-2005 Actual Cost Adjustment	))))	Case No. GR-2005-0279

KEVIN A. THOMPSON, Presiding
DEPUTY CHIEF REGULATORY LAW JUDGE.
JEFF DAVIS, Chairman
STEVE GAW
ROBERT M. CLAYTON, III,
LINWARD "LIN" APPLING,
COMMISSIONERS.

REPORTED BY:
TRACY L. THORPE, CSR, CCR
MIDWEST LITIGATION SERVICES

A. We believe that it follows the tariff requirements and that it has been filed consistent with those tariffs. It also reflects the company's best estimate of what its actual gas costs will be.

COMMISSIONER APPLING: Okay. Thank you.

THE WITNESS: Thank you, sir.

JUDGE THOMPSON: Thank you, Commissioner.

Recross based on questions from the Bench, Mr. Fischer.

RECROSS-EXAMINATION BY MR. FISCHER:

Q. Once again, just briefly, Mr. Sommerer. I've got a couple questions related, first of all, I think to the questions from Commissioner Gaw regarding Ameren's eastern system. We were the comparing PGA rate that was a little bit higher than what we proposed here.

Is it your understanding that under the PGA or under the purchased gas adjustment tariffs of all the LDCs in the state, they're required to do a winter filing?

A. That's correct.

Q. And is it your understanding that this case is involving Southern Missouri Gas's winter filing?

A. That's correct.

Q. Is this the first winter filing that's been done by LDCs?

A. That's correct.

Q. Would it be correct that you would expect if Ameren follows its PGA tariffs, that it will also be required to do a winter filing on that eastern system at some point later in the fall?

A. That's correct.

Q. Given the way you've seen prices going in the market, would you expect that that PGA rate for the eastern system of Ameren will be going down or up?

A. It's difficult to say at this point. They -- they made a summer filing. It was later than some other interim PGA filings that were made. In my opinion, they've done quite a bit of hedging, which means their portfolio is less subject to market volatility, so you may not see the types of increase that you would associate with those market prices.

Q. Is it also correct that Ameren is an electric company as well as a gas company and would, therefore, have more options available for hedging its gas supplies?

A. I think as a larger company, potentially they may have greater access to the futures market and financial instruments than Southern Missouri Gas would have.

Q. Now, earlier in your statements you indicated that small companies like Southern Missouri Gas Company really do have some limitations on their ability to hedge. You went through a list of things they really can't do. Believe one of

the areas that you did say we could do would be fixed price contracts; is that right?

A. That is correct.

Q. And if I understand your answers to Commissioner Gaw's questions, you went back to the year 2003 for some of the fixed price contracts that that -- that the company did at that time; is that right?

A. That's correct.

Q. Could you give me just briefly what the prices were in July 24th, 2003 that was fixed at that time? Do you have that?

A. I will be referring to the company's response to DR 70, which has been marked confidential in its entirety.

Q. Okay. That was in 2003. We can go in-camera. I don't think it would probably be confidential anymore. We'd waive that. If you'd like to read that into the record, I'd appreciate it.

A. July the 24th '03, $5; July the 24th, '03, $4.78; August 15th, '03, $5.11; August 15th, '03, $5.23; September '02, 2003, $5.04; October '07, 2003, $4.79.

Q. Okay. Now, have you been following the market this summer?

A. Yes.

Q. If a company had tried to lock in on July 24th of this year, would you expect the prices to range from in the

upper 8's to 9.50 or so?

A. What was the time period you were looking at?

Q. Around July 24.

A. It looks like NYMEX was trading around $8.50 at that time.

Q. And if you went further out in the winter, it was up to 9.54, wasn't it?

A. By mid-August it looked like the winter was trading anywhere from about 9.50 to 10.25.

Q. Okay. And if we went to September, which was another date that in 2003 there was a fixed price contract, would you agree that the NYMEX was trading at 11.60 to over $12?

A. From early September until the middle of September it looks like it traded from about 11.50 to perhaps 12.50.

Q. Do you happen to have yesterday's prices or some time earlier this week?

A. I have yesterday's prices for November through March.

Q. Around 13.00, 13.50 dollar level?

A. Around the 14 to 15 dollar level.

Q. Okay. Mr. Sommerer, would you recommend that the company lock in its gas supply at this time?

A. I would not make a recommendation either way

for the company's purchasing practices since they haven't been made and it's inappropriate for me to make that recommendation.

Q. In fact, in the Staff recommendation it indicates Staff does not render an opinion as to the gas purchasing practices of SMGC at this time; is that right?

A. That's correct.

Q. And you haven't changed your position on that?

A. No.

Q. Volatility means markets go up and markets go down; is that right?

A. That's correct.

Q. Is the Staff projecting that markets are going to continue to go up the rest of winter?

A. No.

Q. Do you think they're going to come down?

A. I don't know.

Q. Had the company locked in at the 8, 9 dollar range, would you agree that that would have been higher than the whole winter cost of last year?

A. Based upon my recollection, I think that would be the case, yes.

Q. And that would be -- if we locked in today, it probably be more than twice what it was last year; is that correct?

A. Depending on whether you included transportation, but I think those percentages are within the ballpark.

Q. It's an unregulated market. Correct?

A. The natural gas and wellhead market is unregulated.

Q. And you're confident that the numbers that are included in the PGA reflect the company's best judgment about what the prices are likely to be? That's the standard and that's -- and you're recommending approval of the PGA. Correct?

A. That's my belief, yes.

MR. FISCHER: Okay. I think that's all I have. Thank you.

THE WITNESS: You're welcome.

JUDGE THOMPSON: Thank you Mr. Fischer.

Mr. Wheatley.

MR. WHEATLEY: No questions, your Honor.

JUDGE THOMPSON: Thank you.

Ms. Shemwell, redirect.

MS. SHEMWELL: Thank you.

REDIRECT EXAMINATION BY MS. SHEMWELL:

Q. Mr. Sommerer, Commissioner Gaw was asking you questions about hedging practices. Are futures contracts a form of hedging?