

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. GR-2013-0257, Summit Natural Gas of Missouri

FROM: Phil Lock, Regulatory Auditor – Procurement Analysis
Kwang Choe, Ph.D., Regulatory Economist – Procurement Analysis
Derick Miles, P.E., Regulatory Engineer – Procurement Analysis

/s/ David M. Sommerer 07/23/13
Project Coordinator / Date

/s/ Bob Berlin 07/23/13
Staff Counsel's Office / Date

/s/ Lesa Jenkins, P.E 07/23/13
Utility Regulatory Engineer II / Date

SUBJECT: Staff Recommendation in Case No. GR-2013-0257, Summit Natural Gas of Missouri 2011-2012 Actual Cost Adjustment Filing (formerly Missouri Gas Utility)

DATE: July 23, 2013

EXECUTIVE SUMMARY

On April 27, 2011 Southern Missouri Gas Company (SMNG) and Missouri Gas Utility (MGU) filed an application for authority from the Commission for SMNG and MGU to merge, with MGU as the surviving entity. The parties filed a Unanimous Stipulation and Agreement on September 15, 2011, which the Commission approved on September 28, 2011.

On February 2, 2012 MGU filed for a name change to Summit Natural Gas of Missouri (SNG, Summit or Company). On February 23, 2012, Summit filed tariff sheets to adopt MGU's Missouri tariffs. Those tariff sheets became effective on March 24, 2012.

On November 2, 2012, Summit (successor in interest to MGU) filed its Actual Cost Adjustment (ACA) for the 2011-2012 annual ACA period (September 2011 through August 2012) for rates to become effective November 17, 2012. The Procurement Analysis Unit (Staff) of the Missouri Public Service Commission has reviewed the Company's ACA filing. A comparison of billed revenue recovery with actual gas costs will yield either an over-recovery or under-recovery of the ACA balance.

**** Denotes Highly Confidential Information ****

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Staff conducted the following analyses:

- a review of billed revenue compared with actual gas costs,
- a reliability analysis including a review of estimated peak-day requirements and the capacity levels needed to meet these requirements
- a review of the Company's gas purchasing practices to evaluate the prudence of the Company's purchasing decisions for this ACA period; and
- a hedging review to evaluate the reasonableness of the Company's hedging practices for this ACA period.

Based on its review, Staff recommends the following adjustments to the Company's filed ACA balances:

Description NORTHERN SYSTEM	Summit's ACA Balance	Staff Adjustments	Staff Recommended ACA Balance
Beginning ACA Balance @ 9/1/11– (Over-recovered)/Under-recovered	(\$24,317)	\$0	(\$24,317)
Total Cost of Gas Delivered to City Gate	\$639,566	\$0	\$639,566
Total Revenue Recovery	(\$687,512)	(\$2,446)	(\$689,958)
Ending ACA Balance @ 8/31/12– (Over-recovered)/Under-recovered	(\$72,263)	(\$2,446)	(\$74,709)

Description SOUTHERN SYSTEM	Summit's ACA Balance	Staff Adjustments	Staff Recommended ACA Balance
Beginning ACA Balance @ 9/1/11– (Over-recovered)/Under-recovered	(\$3,951)	\$0	(\$3,951)
Total Cost of Gas Delivered to City Gate	\$629,659	(\$7,348)	\$622,311
Total Revenue Recovery	(\$687,776)	\$47,737	(\$640,039)
Ending ACA Balance @ 8/31/12– (Over-recovered)/Under-recovered	(\$62,068)	\$40,389	(\$21,679)

In summary, on the Northern System, Staff's accounting adjustments for the 2011-2012 ACA increase the filed over-recovery balance of \$72,263 by a total of \$2,446 to an adjusted over-recovery balance of \$74,709. On the Southern System, Staff's accounting adjustments for the 2011-2012 ACA reduce the filed over-recovery balance of \$62,068 by a total of \$40,389 to an adjusted over-recovery balance of \$21,679. These accounting adjustments are described in detail in Section II – Billed Revenue and Actual Gas Costs.

Staff's concerns/comments regarding reliability analysis and gas supply planning are addressed in that section of the memorandum. Staff recommends the Commission order the Company to respond to Staff's concerns/recommendations within 30 days.

Staff has no adjustments related to hedging; however Staff's concerns/comments are addressed in the Hedging section of the memorandum.

STAFF'S TECHNICAL DISCUSSION AND ANALYSIS

Staff's discussion of its findings is organized into the following five sections:

- I. Overview
- II. Billed Revenue and Actual Gas Costs
- III. Reliability Analysis and Gas Supply Planning
- IV. Hedging
- V. Recommendations

Each section explains Staff's concerns and recommendations.

I. OVERVIEW

On the Southern System, Southern Star Central Gas Pipeline (SSCGP) provides gas to an average of 1,033 sales customers in the central portion of the state including the counties of Benton, Pettis, Morgan, Camden and Miller. On the Northern System, ANR Pipeline Company (ANR) serves an average of 1,503 sales customers in the Northwest Missouri counties of Caldwell, Daviess and Harrison. ** _____ ** is the only transportation customer served on the Northern System.

II. BILLED REVENUE AND ACTUAL GAS COSTS

Revenue Recovery – Total Company

Summit books its revenues on an accrual basis. In doing so, they included unbilled revenues in the PGA revenue recovery of their filing. According to Summit's PGA tariffs (Sheet 48), there

shall be a monthly comparison of the actual “as billed” cost of gas to the cost recovery recorded on the books and records of the Company. Staff requested that Summit provide monthly billed sales volumes by customer class. To meet this requirement, Summit removed the unbilled revenues from its initial filing and restated its revenue recovery on an “as billed” basis (per Data Request No.1). The revenue recovery should be reduced from \$687,512 as originally filed, to \$684,616, a decrease of \$2,896 on the Northern System. On the Southern System, the revenue recovery should be reduced from \$687,776 as originally filed, to \$640,039, a decrease of \$47,737.

Gas Supply-Southern System

Gas was purchased from **_____** during June 2012. The gas was delivered on the former SMNG transportation contract for consumption by SMNG sales customers, but the costs were not included in SMNG’s cost of gas. Instead, the costs were inadvertently included in MGU’s cost of gas. These costs totaled \$7,348. The cost of gas should therefore be reduced by \$7,348 for sales customers on MGU’s Southern System.

Imbalances-Northern System

_____ incurred cash-out charges as a result of Negative Imbalances with Summit. Negative Imbalances occur when the transporter **_____** has used more gas than they had delivered to Summit. This occurred during the months of September 2011 and August 2012. During those months, Summit shall charge the transporter, in addition to applicable transportation charges and fuel assessments, an amount equal to the product of the absolute value of the Negative Imbalance volume and the Cash-out Rate. The cash-out rate and pricing options are defined in Summit’s tariffs (Sheet 29A). The cash-out amounts, billed to **_____** as “Gas Supply Charges”, was inadvertently left out of the PGA revenue total. Revenue recovery should therefore be increased by \$5,342 (\$4,582 + \$760) for sales customers on the Northern System.

ACA Approach for Interest Calculation – Northern System

During the months of April 2012 to August 2012, the average monthly ACA balance for each month exceeded the \$50,000 threshold required for interest calculation. No interest calculation was made by Summit. Staff calculated the interest during those months and the amount was not material so no adjustment was made. During future ACA’s, Staff recommends that Summit calculate the interest on all monthly ACA balances that exceed the monthly threshold of \$50,000.

Bids

When Summit purchases swing volumes, written documentation was not always provided. Bids were obtained by verbal or e-mail communication. In order for the Staff to conduct a thorough

and complete review of Summit's verbal communication processes, complete written documentation must be provided by Summit to substantiate its verbal communications.

III. RELIABILITY ANALYSIS AND GAS SUPPLY PLANNING

As a gas corporation providing natural gas service to Missouri customers, SNG is responsible for conducting reasonable long-range supply planning to meet its customer needs. SNG must make prudent decisions based on that planning. One purpose of the ACA process is to examine the reliability of the Local Distribution Company's (LDC's) gas supply, transportation, and storage capabilities. For this analysis, Staff reviewed the LDCs' plans and decisions regarding estimated peak-day requirements and reviewed the LDC's pipeline capacity levels to meet those requirements. Staff reviewed the peak day reserve margin and the rationale for this reserve margin and the natural gas supply plans for various weather conditions.

Staff offers the following comments and concerns regarding the supply planning process:

HDD selection for both systems:

Staff's review of heating degree day (HDD) data does not correspond with the Company's selection of a peak HDD. Staff recommends the Company review its sources for peak HDD selection prior to its peak day modeling for the 2013/2014 ACA period and provide the source data in the ACA review.

Staff's review of National Oceanic and Atmospheric Administration (NOAA) data for the St. Joseph Rosecrans airport for the period of January 1981 through August 2012 shows a peak of 83HDD occurring on December 25, 1983. The Company used a peak HDD for the St. Joseph Rosecrans airport of 79HDD in its peak day requirements predictor model. The Company stated that it does not know which 30 year period from which it obtained its peak heating degree day.

For the Warsaw area, the Company used 72HDD for its peak day obtained from the Lakeside weather station. This peak day is different from the NOAA peak of 81HDD for Sedalia, Missouri, occurring on December 23, 1989. The Company has previously indicated it is considering using the Sedalia weather station for the Warsaw area because of the lack of availability of data for the Lakeside station.

Southern System Peak Supply:

For the Warsaw area, SNG has no contracted storage. Thus, all gas supplies serving the Warsaw area are currently flowing supplies. It is important for the Company to have flexible supply plans for the Southern system because there is no contracted storage to allow for the swing changes in weather that require more or less flowing supply.

SNG had fixed baseload contracts with various suppliers for fixed deliveries that varied quantity by month. For the month of January, in which a peak day may occur, the Company contracted

for baseload gas that would fulfill 30% of the estimated peak day requirements for the Warsaw area system. The Company also has a swing contract for the Southern System that would fulfill 27% of the estimated peak day requirements. However, the baseload and swing contracts would only fulfill 57% of peak day requirements for January. The Company's 2011/2012 gas supply plans do not comment on how it would fulfill a peak day for the Southern system.

The Company's response to a similar Staff concern in the 2010/2011 ACA, GR-2012-0115, indicated the Warsaw system could become responsible for a portion of the storage to its other territory previously known as Southern Missouri Natural Gas. However, the SNG plans for SNG Southern System supply do not yet include these plans and do not include details for how the costs of the other system storage would be allocated.

Although cold weather requirements were not an issue for this ACA because of the warm winter, the Company's gas supply plans must include an explanation for how it would meet cold day and peak day requirements for its Southern System as a matter of establishing system reliability.

Northern Storage:

Because this was one of the warmest winters on record, the Company used only 33% of storage MSQ. A review of the invoices showed there were no penalties as a result of the storage not being withdrawn to 20% by April 1st, which is the threshold required by its pipeline tariff. Also, the Company had no storage plan in effect, relying only on filling its storage by November 1st and making withdrawals to meet its 20% (per ANR tariff) by April 1st. Because this practice affects reliability, Staff recommends the Company develop a storage injection and withdrawal plan as it has done in prior ACA periods. Staff recommends the Company provide this storage plan as part of its Fall Hedging Presentation no later than 11/1/2013 for the 2013/2014 Winter Season.

IV. HEDGING

Summit's winter hedging plans are primarily designed to achieve a reliable natural gas supply and to protect its customers against price spikes. Annually, the hedging plan for the Northern System calls for the Company to fill storage as close to capacity as possible by November 1. Additionally, fixed price purchases are a part of the hedging plan for the Northern System.

For the Southern System, the hedging plan utilizes fixed price purchases. The Southern System has no contracted storage capacity.

Summit's maximum storage quantity (MSQ) represents about 40% of normal winter weather requirements for the Northern System. For delivery during the winter periods, November 2011 - February 2012, Summit purchased fixed price volumes in May 2011. These fixed price volumes, combined with storage at the beginning of the winter season, represents 83% of customers' normal winter weather requirements for the Northern System.

For the Southern System, Summit purchased its fixed price volumes in May 2011 for delivery in November 2011 through March 2012. The fixed price volumes represent about 87% of normal winter weather requirements.

Conclusion

In addition to the analyses above of Summit's overall hedging practice for this winter's ACA period (2011-2012), Staff offers the following comments about the Company's hedging practice for this winter's ACA period:

1. It is important for the Company to evaluate the expected level of its customers' natural gas requirements that are reasonably protected (hedged) under warmer than normal, normal, and colder than normal weather scenarios. Additionally, the Company should evaluate its hedging strategy in response to the changing market dynamics as to how much the existing hedging strategy actually benefits its customers while achieving the goal of price stability. Although Staff is not suggesting that the Company develop its hedging strategy in order to beat the market, part of the Company's hedging plan should address changing markets and the possibility of less volatile market prices.
2. A part of Summit's hedging practice essentially calls for purchasing gas whenever it is less expensive compared to the current storage Weighted Average Cost of Gas (WACOG), and injecting the gas into storage. However, this market-timing approach of filling storage can lead to a situation where Summit waits too long for natural gas prices to go down (though Staff recognizes Summit's past efforts in reducing gas costs by utilizing this method). In addition, the Company should consider placing some hedges well in advance of the winter to allow sufficient time to avoid concentrating hedge placements too close to the fall and winter timeframe.

Hedging Recommendations

Staff recommends, for the 2012-2013 ACA period and beyond, that Summit:

- (a) Establish and maintain a current and consistent hedging policy with stated objectives based on month-specific normal weather requirements while also considering the impacts of warmer and colder than normal weather scenarios,
- (b) Consider a combination of various alternatives such as storage withdrawals, call options, and other fixed price purchases for effective hedging during the winter months, and
- (c) Continue to document its reasoning for executing any hedging transactions or decisions, whether by means of storage, fixed price contracting or other financial hedging instruments.

V. RECOMMENDATIONS

The Staff recommends that Summit:

1. Adjust the balances in its next ACA filing to reflect the Staff recommended ending (over)/under recovery ACA balances per the following table:

TABLE 1

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A) ** ____ ** cash-out charges

B) (\$684,616) – (\$687,512) Restate to billed revenues

Description SOUTHERN SYSTEM	Summit's ACA Balance	Staff Adjustments	Staff Recommended ACA Balance
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A) Gas Supply adjustment

B) Restate to billed revenues

2. Respond to Staff's recommendations in Section II – Billed Revenues and Actual Gas Costs.
3. Respond to Staff's recommendations in Section III – Reliability Analysis and Gas Supply Planning.
4. Respond to Staff's recommendations in Section IV – Hedging.
5. Respond to recommendations included herein within 30 days.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI


**In the Matter of Summit Natural Gas of Missouri, Inc.'s)
Purchased Gas Adjustment)**

File No. GR-2013-0257

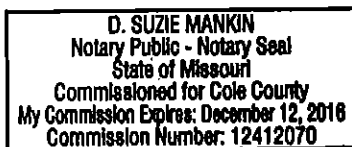
AFFIDAVIT OF PHIL S. LOCK

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Phil S. Lock, being of lawful age, on his oath states: that as a Utility Regulatory Auditor III in the Procurement Analysis Unit of the Utility Services Department, he has participated in the preparation of the foregoing memorandum consisting of 9 pages to be presented in the above case; that he has knowledge of the matters set forth in the Memorandum pertaining to *Billed Revenues and Actual Gas Costs*; and that such matters are true and correct to the best of his knowledge and belief,


Phil S. Lock

Subscribed and sworn to before me this 23rd day of July, 2013.



Shuzi Hankin
Notary Public

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Summit Natural Gas of Missouri, Inc.'s)
Purchased Gas Adjustment)

File No. GR-2013-0257

AFFIDAVIT OF KWANG Y. CHOE

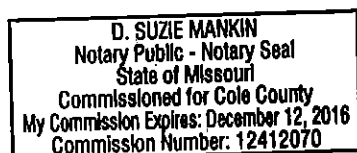
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Kwang Y. Choe, being of lawful age, on his oath states: that as a Regulatory Economist II in the Procurement Analysis Unit of the Utility Services Department, he has participated in the preparation of the foregoing memorandum consisting of 9 pages to be presented in the above case; that he has knowledge of the matters set forth in the Memorandum pertaining to *Hedging*; and that such matters are true and correct to the best of his knowledge and belief,

Howard E. Orr

Kwang Y. Choe

Subscribed and sworn to before me this 23rd day of July, 2013.



Suzie Hankin
Notary Public

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI


In the Matter of Summit Natural Gas of Missouri, Inc.'s)
Purchased Gas Adjustment)

File No. GR-2013-0257

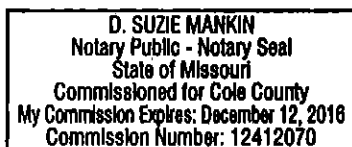
AFFIDAVIT OF DERICK MILES, P.E.

[illegible]

Derick Miles, being of lawful age, on his oath states: that as a Utility Regulatory Engineer I in the Procurement Analysis Unit of the Utility Services Department, he has participated in the preparation of the foregoing memorandum consisting of 9 pages to be presented in the above case; that he has knowledge of the matters set forth in the Memorandum pertaining to *Reliability Analysis and Gas Supply Planning*; and that such matters are true and correct to the best of his knowledge and belief,


Derick Miles, P.E.

Subscribed and sworn to before me this 23rd day of July, 2013.



Shuzellankin
Notary Public