BEFORE THE PUBLIC SERVICE COMMISSION

STATE OF MISSOURI

In the Matter of Missouri Gas Energy's Purchased Gas Adjustment (PGA) Factors to be Audited in its 2002-2003 Actual Cost Adjustment.	))))	**Case No. GR-2003-0330**

STAFF'S PROPOSED FINDINGS OF FACT
AND CONCLUSIONS OF LAW

COMES NOW the Staff of the Missouri Public Service Commission, by and through the Commission's General Counsel, and for its Proposed Findings of Fact and Conclusions of Law, states as follows:

Proposed Findings of Fact

The Parties:

1. Southern Union Company, which does business as Missouri Gas Energy (MGE), is a Local Distribution Company (LDC) that is in the business of purchasing natural gas and re-selling it at retail to some 500,000 residential and other customers in three Missouri service areas: Kansas City, St. Joseph and Joplin. Southern Union acquired its Missouri LDC operation from Western Resources in February 1994 (Kirkland Direct, at 10).

2. The Staff of the Missouri Public Service Commission (Staff) traditionally appears as a party in Commission proceedings and is represented by the Commission's General Counsel, an employee of the Commission

authorized by statute to "represent and appear for the Commission in all actions and proceedings involving this or any other law [involving the Commission.]"[1]

3. The Public Counsel is appointed by the Director of the Missouri Department of Economic Development and is authorized to "represent and protect the interests of the public in any proceeding before or appeal from the public service commission[.]"[2]

4. Enbridge Pipelines was formerly known as Kansas Pipeline Company (*Application for Intervention,* filed on April 11, 2003). Enbridge is an interstate supplier of gas transportation services that serves MGE's Kansas City service area (*Id.*). Enbridge did not file testimony or participate in the evidentiary hearing held herein.

The Issue:

5. Unlike the rates of such other public utilities as electric companies and water companies, the rates of LDCs are set in two separate proceedings. Rates reflective of all components of the cost-of-service except the commodity cost of natural gas are set in traditional rate proceedings, generally brought under the "file-and-suspend" method and based upon a historical test year. Rates reflective of the commodity cost of the natural gas that the LDC purchases and distributes to its customers, however, are set on an interim basis, subject to refund, in the annual Purchased Gas Adjustment (PGA) process. The PGA process allows the LDC to rapidly adjust its rates to account for gas price

[1] Section 386.071, RSMo 2000. All statutory citations, unless otherwise specified, are to the Revised Statutes of Missouri (RSMo.), revision of 2000.

[2] Sections 386.700 and 386.710.

volatility. The cost of the commodity is passed through to the LDC's customers at cost, with no mark-up. Following the close of each annual PGA, the prices paid by the LDC are subject to audit by the Commission's Staff in the Actual Cost Adjustment (ACA) phase. During the ACA phase, the Staff's Procurement Analysis Department (PAD) reviews all aspects of the LDC's purchasing, planning, hedging, transporting, and storing of gas. Staff may recommend that some part of the LDC's costs not be recovered from ratepayers due to imprudence. Where, as here, the Company refuses to accept Staff's recommendation, a contested case ensues.

6. On December 19, 2003, Staff filed its Memorandum and Recommendation for MGE's 2001-2002 ACA filing in Case No. GR-2002-348, later consolidated for all purposes into the present case (Reed Direct, at 4-5; Sch. JJR-1).[3] Staff's filing stated that its review:

> consisted of an analysis of the billed revenues and actual gas costs, for the period of July 1, 2001 to June 30, 2002. A comparison of billed revenue recovery with actual gas costs will yield either an over-recovery or under-recovery of the ACA, Refund, Take-or-Pay (TOP) and Transition Cost balances. The Staff also reviewed MGE's gas purchasing practices to determine the prudence of the Company's purchasing and operating decisions.

(*Id.*). Staff recommended a disallowance of $1,373,016 to reflect the excess gas costs for peak day reserve. (*Id.*).

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[3] The Commission consolidated Case Nos. GR-2002-348 and GR-2003-0330, relating to the 2001-2002 and 2002-2003 PGA/ACA periods, respectively, for all purposes. *In the Matter of Missouri Gas Energy's Purchased Gas Adjustment (PGA) Factors to be Audited in Its 2002-2003 Actual Cost Adjustment,* Case No. GR-2003-0330 (*Order Consolidating Cases and Establishing Procedural Schedule,* issued April 12, 2005) at p. 1-2 ("*Consolidation Order*").

7. On December 28, 2004, Staff filed its Memorandum and Recommendation for MGE's 2002-2003 ACA filing in the present case (Reed Direct, at 5-6; Sch. JJR-2). Staff recommended a disallowance of $2,015,661 to reflect the excess gas costs for peak day reserve (*Id.*). Staff also corrected the recommended disallowance for the 2001-2002 ACA to $2,041,931 (*Id.*). Thus, the disallowance at issue in these consolidated cases aggregates to $4,057,592.[4]

8. The responsibility of an LDC with respect to transportation capacity is to ensure that sufficient capacity is available to meet its customers' requirements on the coldest day that is reasonably likely to be experienced (Jenkins Direct, at 6; Tr. 1:138-139). This is termed the "design day" (Kirkland Direct, at 6 n. 2) or the "peak day" (Jenkins Direct, at 2). The cost of this amount of capacity, and no more, is fairly chargeable to the ratepayers (Jenkins Direct, at 2, 6). Staff contends that some of MGE's transportation capacity costs for 2001-2002 and 2002-2003 should be disallowed because MGE reserved capacity in excess of that necessary to meet its customers' requirements on the coldest day reasonably likely to be experienced (Jenkins Direct, at 3, 4).

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[4] Exclusive of other proposed disallowances based on costs incurred for transportation over the Kansas Pipeline. The Commission stated, in its *Consolidation Order,* "[T]he Commission has decided to move forward with other issues while waiting for an appellate decision on the Kansas Pipeline issue." *In the Matter of Missouri Gas Energy's Purchased Gas Adjustment (PGA) Factors to be Audited in Its 2002-2003 Actual Cost Adjustment,* Case No. GR-2003-0330 (*Order Consolidating Cases and Establishing Procedural Schedule,* issued April 12, 2005) at p. 2 ("*Consolidation Order*").

Rebutting the Presumption of Prudence:

<u>Inadequate Capacity Serving Joplin</u>

9. MGE's expert, John Reed, testified that his calculation of the design day requirement of MGE's Joplin service area significantly exceeded the firm transportation capacity actually available to MGE to serve Joplin (Tr. 2:70). MGE's own prediction was higher than Reed's and the design day capacity shortfall for Joplin was thus correspondingly greater (Tr. 2:71). MGE's management knew the amount of capacity available (Tr. 2:65), and knew that the capacity serving Joplin was insufficient (Tr. 2:73). MGE was thus in violation of its admitted responsibility "to make certain that we have a system . . . such that we can meet our delivery obligations" (Tr. 1:138-139; testimony of MGE witness Kirkland). MGE's witness Kirkland admitted that inadequate capacity posed a risk of "potentially severe human and economic consequences if curtailments and/or outages occur" (Kirkland Direct, at 6, 9). MGE's own witness, John Reed, testified,

> The consequences of being short on a peak day, a design day when it actually occurs are nearly catastrophic in many cases in terms of loss of service, in terms of the property damage, the economic damage and in terms of the cost of having to go out and relight the system, pilot light by pilot light, valve by valve, meter by meter. I've studied outages like that on gas distributions. It's something that should be avoided at nearly all cost.

(Tr. 1:119).

<u>Inadequate Planning Methodology</u>

10. Natural gas is transported from the production fields to LDCs like MGE over interstate pipelines (Jenkins Direct, at 6). Each pipeline has a finite

capacity and an LDCs must reserve whatever fraction of that capacity is necessary to obtain the gas needed to serve its customers (Jenkins Direct, at 6). The LDC's task is more complex where, as here, the LDC has customers in several service areas that are served by different pipelines (Jenkins Direct, at 10). In that case, the LDC must reserve sufficient capacity for each of its service areas because excess capacity in Kansas City and St. Joseph cannot be used to serve Joplin (Kirkland Rebuttal, at 38). The process of reserving sufficient transportation capacity involves contracts that often extend for several years; consequently, each LDC must accurately forecast the gas volume that it will need in each of several future years and enter into sufficient contracts to obtain that volume (Jenkins Direct, at 7-8). If an LDC contracts for too little capacity, it will not have sufficient gas and it will have to pay premium prices and penalties to obtain what it needs (Jenkins Direct, at 2). On the other hand, if the LDC contracts for too much capacity, the regulatory authority will seek to disallow its recovery of the associated costs from its customers (Jenkins Direct, at 2, 6-7).

11. In forecasting the volume of transportation capacity that it needs in future years, the LDC must plan for the coldest day that is likely to occur in each year, because that is the day that the greatest volume of gas will be required (Jenkins Direct, at 2, 12). There are various ways of doing this and the Staff has never insisted that the LDCs use any particular method (Tr. 3:249). However, Staff *does* insist that the method adopted by any LDC be reasonably reliable (Jenkins Direct, at 20). Staff's expert, Lesa Jenkins, testified that MGE has not adopted a reasonably reliable method (Jenkins Direct, at 4, 11-12).

12. The tools available to an LDC in making these forecasts are usage and weather data drawn from records of past years, growth estimates, and mathematical tools for analyzing the data (Jenkins Direct, at 7, 12). The coldest day that may be expected in each service area is referred to as the "peak day" (Jenkins Direct, at 2) or "design day" (Reed). MGE uses Heating Degree Days (HDD) in its planning process; a Heating Degree Day is the number of degrees Fahrenheit by which the average temperature on a given day, at a given location, deviated from 65^{o} (Jenkins Direct, at 12). Thus, for example, a day on which the average temperature is 15^{o} F is rated at 50 HDD. The design day that MGE must plan for, consequently, is the highest HDD day recorded for each of its service areas (Jenkins Direct, at 12).

13. MGE has three, non-contiguous service areas arrayed in a north-to-south pattern: St. Joseph, Kansas City and Joplin (Jenkins Direct, at 10). MGE engaged in total system capacity planning rather than planning by service area even though, due to the configuration of the pipelines that served it, MGE was required to have a separate supply plan for each service area (Jenkins Direct, at 10, 19). Likewise, MGE used a Kansas City peak day figure in planning for its system rather than a peak day value from each service area (Jenkins Direct, at 12). In selecting its peak day from the Kansas City data, MGE was not even accurate – it used too high a figure (Jenkins Direct, at 11-13, 17). Staff expert Jenkins testified that this was a material error that had significant results in the form of some tens of thousands of dekatherms of excess capacity (Jenkins

Direct, at 17).[5] Each one degree increase in HDD requires an additional 10,200 to 10,600 dekatherms of capacity per day at 30 to 40 cents per day per dekatherm (Tr. 3:141, 143). MGE's own witness, John Reed, testified that the historical peak day is important for planning purposes and that MGE should have known that figure (Tr. 1:51).

14. MGE contended that it used a regression analysis to support its choice of demand day for planning purposes (Jenkins Direct, at 13-14). That analysis relied on a data set consisting of the single coldest day that occurred each year for each of 30 years (Jenkins Direct, at 14). Staff's expert, Lesa Jenkins, testified, "I think that one data point is insufficient and, yes, I think that's sloppy (Tr. 2:220) . . . I don't believe that it was reasonable to use one data point, so in that sense -- that one data point didn't tell anything" (Tr. 2:221). Although characterized by MGE as a "regression analysis," it is nothing of the sort (Jenkins Rebuttal, at 17; Jenkins Surrebuttal, at 13). MGE's own witness, John Reed, testified that the method used by MGE was theoretically inferior to that used by Staff (Tr. 1:47). By selecting only a single cold day from each of 30 years, MGE ignored many other cold days that occurred during that period (Jenkins Direct, at 14). A quite different result can be obtained, for example, by using the 30 coldest days that occurred during the 30 year period (Jenkins Direct, at 15). Staff expert Jenkins testified,

> "I don't believe that it's appropriate. I don't believe it's appropriate to use one data point. You can't determine what the shape of the line is with one data point. . . . You can't do a

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[5] The actual numbers are Highly Confidential (HC).

> regression with one data point. In my experience in working with statistics in the classes that I've taken, they're generally encouraging you to look at at least 30 data points. And in fact, MGE did look at more data points but they only looked at 12 and they only looked at three a year for four years as a follow-up. That's what the consultant did. I still don't think that's sufficient values, and I communicated that with the company, but they were not willing at the time to move off of the 12 data points."

(Tr. 3:254-255).

15. MGE used the peak day figure it had selected to develop a heat load factor; it then used the heat load factor with a base load factor to forecast the daily capacity required to meet peak day demand (Jenkins Direct, at 19-20). "Heat load" is a measurement of the gas required for heating purposes in cold weather in addition to the "base load" volume that does not vary throughout the year (Jenkins Direct, at 19-20). While heat load is temperature-sensitive, base load is not (Jenkins Direct, at 19-20). In performing this analysis, MGE ignored available daily usage data for each service area (Jenkins Direct, at 19). Instead, MGE developed its heat load factor by evaluating usage on only one cold day each year (Jenkins Direct, at 20; Jenkins Surrebuttal, at 14). MGE developed its base load factor by evaluating usage in the summer months when there are no HDD days (Jenkins Direct, at 20). However, in developing its base load factor, MGE failed to correct for the very significant amount of gas used in July and August by its electric utility customers to meet the temperature-sensitive air-conditioning load (Tr. 2:256). Consequently, MGE's estimate of the non-temperature sensitive base load based upon its uncorrected summer usage data was more than double the figure calculated by Staff using a regression analysis (Tr. 1:87).

16. Although he testified that MGE reached an appropriate result, MGE's own witness, John Reed, did not testify that MGE's analytical methods were reasonable (Tr. 1:45). Reed testified, "I'm not trying to offer a defense or critique of the company's methodology" (Tr. 1:46). Reed presented his own analysis that, according to him, represented "best practices" (Tr. 1:112). Notably, Reed analyzed each of the three service areas separately, as Staff did; MGE did not (Tr. 1:47).

Excess Transportation Capacity

17. For both the 2001-2002 and 2002-2003 ACA periods that are at issue in this case, Staff's calculations reveal a significant capacity excess in the Kansas City and St. Joseph service areas (Jenkins Direct, at 18; Kirkland Direct, at 5). That excess represents unnecessary capacity the cost of which Staff proposes should be disallowed from the costs that MGE is permitted to recover from its ratepayers (Kirkland Direct, at 5).

Inadequate Documentation

18. MGE was unable to produce, on request, the regression analysis supporting its 2001-2002 Reliability Report (Jenkins Surrebuttal, at 13). MGE's own witness, John Reed, testified that he had never seen it (Tr. 2:61), despite having been involved in MGE's planning function since 1995 (Tr. 1:107). Company witness Kirkland admitted that it was lost (Tr. 1:130). Jenkins characterized this situation as "sloppy" (Tr. 2:220-221).

Imprudence:

19. Staff expert Lesa Jenkins testified that "prior to making contract decisions impacting the 2001/2002 ACA period, MGE did not perform separate analyses for the three major service areas of Kansas City, Joplin and St. Joseph" (Jenkins Direct, at 19).

20. MGE's witness David Kirkland testified that capacity planning is a multi-year process that considers numerous variables and constraints, including supply diversity, operating and economic flexibility, the current portfolio, and the broader natural gas market (Kirkland Direct, at 6, 8; Kirkland Surrebuttal, at 2). Kirkland testified that "obtaining additional pipeline capacity is not like making a late-night trip to a gas station to fill up your car for a trip the next day" (Kirkland Surrebuttal, at 3). Additional capacity becomes available infrequently, usually at multi-year intervals (Kirkland Surrebuttal, at 3). Kirkland testified that MGE's primary focus in transportation planning is reliability, a surprising claim in view of the admitted inadequacy of MGE's capacity serving Joplin (Kirkland Surrebuttal, at 3; Finding of Fact 9). Kirkland testified, "MGE has negotiated over the years to where it now has contracted capacity on four different pipelines, access to three major natural gas supply basins, contracts for significant storage, and has integrated and leveraged its various capacity assets (Kirkland Surrebuttal, at 3).

21. MGE renegotiated its Southern Star transportation contract in 2000-2001 and did not reduce or increase the amount of available capacity (Tr. 3:171-172). The renewal became effective on June 15, 2001 (Kirkland Surrebuttal, at 6). A salient feature of the renewed contract, which was still in effect as recently

as this month, was the "no-notice" feature that accorded great flexibility to MGE (Kirkland Surrebuttal, at 6; Tr. 3:174). The Southern Star renewal negotiations were complex, as one would expect given the size of the negotiation (Kirkland Surrebuttal, at 10). The capacity renewal contract represented the most significant asset in MGE's transportation portfolio (Kirkland Surrebuttal, at 10). The storage component of the renewal contract, coupled with the TSS service, provided MGE with no-notice service (Kirkland Surrebuttal, at 11). "No-notice service" is the tool that provides the LDC with the ability to adjust the gas supply nominations to match the demand fluctuations associated with the deviation between forecast and actual weather with scheduling and balancing flexibility on the part of the pipeline (Kirkland Surrebuttal, at 11). If MGE did not have no-notice service, MGE would be exposed to pipeline imbalance penalties (Kirkland Surrebuttal, at 11). Additionally, the renewal allowed MGE to consolidate its several Southern Star contracts into one contract, thereby removing the possibility that some part of its capacity might be bid away by a competitor (Kirkland Rebuttal, at 39).

22. The renewed Southern Star contract had a term of five years (Jenkins Direct, at 4). When Staff projected MGE's design day demand over a five-year period, adjusted for expected customer growth, Staff found that even in the fifth year, when expected design day demand would be greatest, MGE's transportation portfolio included excess capacity in the amount of several tens of thousands of dekatherms (Jenkins Direct, at 27). It is this fifth-year excess capacity, termed "excess reserve margin," that Staff has recommended be

disallowed for each of the two ACA periods at issue in this case (Jenkins Direct, at 27, *especially* HC Chart on 28; 29). While the amount of the excess reserve margin in dekatherms is identical in each year, the dollar amount of the proposed disallowance varies because the reservation costs were different in each year (Jenkins Direct, at 37-39). MGE witness Kirkland admits that Staff's analysis is mathematically accurate (Kirkland Surrebuttal, at 16). MGE's witness Reed agrees that the analytical approach taken by Staff was the correct one: "First, both Staff and we agree that you should make a prediction for at least four to five years and make your capacity decisions based upon the projected requirements over that interval, not just at the beginning of that interval, and we've done that, Staff has done that" (Tr. 1:97).

23. Staff allows a certain reserve margin, equal to the standard error of the y-estimate, to account for variability in usage (Jenkins Direct, at 27). Staff used a five-year analytically horizon because MGE acquires pipeline capacity in "chunks" (Jenkins Direct, at 27). Because MGE makes contracts in blocks covering several years, more capacity at the beginning is acceptable in order to have sufficient capacity at the end (Jenkins Direct, at 29). However, Staff found that MGE had excess capacity at the end (Jenkins Direct, at 27, *especially* HC Chart on 28; 29).

24. The Southern Star pipeline was fully subscribed in 2001 (Kirkland Rebuttal, at 38, 40-41; Kirkland Surrebuttal, at 12; Tr. 3:173). Additional capacity only rarely becomes available and, had MGE released capacity when it renewed its contract in 2001, it would not have been able to add it later for the same price,

if at all (Kirkland Rebuttal, at 40, 41; Kirkland Surrebuttal, at 12; Tr. 1:148). Southern Star is the only pipeline that serves all three of MGE's service areas (Kirkland Rebuttal, at 40). It is low-cost, flexible capacity that provides access to multiple supply basins; it is valuable and difficult to obtain (Kirkland Rebuttal, at 40, 41-42).

Proposed Conclusions of Law

I.

MGE is a gas corporation and a public utility within the intendments of § 386.020, RSMo, and is therefore subject to the regulatory jurisdiction of this Commission under Chapters 386 and 393, RSMo.

II.

In all rate cases, the burden of proof is on the utility to show that its costs are just and reasonable.[6] However, the presumption of prudence described below places the initial burden of going forward with the evidence upon the party challenging the utility's expenditures and the "utility need not demonstrate in its case-in-chief that all [its] expenditures are prudent."[7]

III.

The Standard:

The Commission has employed a "prudence standard" in resolving cases

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[6] § 393.150.2, RSMo 2000; *In the Matter of Missouri Gas Energy, supra,* 11 Mo.P.S.C.3d at 222; *In the Matter of Western Resources,* 3 Mo.P.S.C.3d 480, 488 (1995). A PGA/ACA case is, by definition, a rate case and the Commission's prudence review is an exercise of its ratemaking authority. *State ex rel. Midwest Gas Users' Ass'n v. PSC,* 976 S.W.2d 470, 479-483 (Mo. App., W.D. 1998).

[7] *In the Matter of Missouri Gas Energy, supra,* 11 Mo.P.S.C.3d at 222.

involving gas cost disallowances.[8] Under this standard, the Company's costs are presumed to have been prudently incurred until "some other participant in the proceeding creates a serious doubt as to the prudence of an expenditure, then the [Company] has the burden of dispelling these doubts and proving the questioned expenditure to have been prudent."[9] Thus, "Staff's burden is to show that [MGE] acted imprudently in making gas supply arrangements which caused higher gas costs than if prudent decisions had been made."[10] The Commission may only disallow a utility's recovery of costs from its ratepayers upon a finding (1) that the utility acted imprudently and (2) that the imprudence resulted in harm to the utility's ratepayers.[11]

Rebutting the Presumption of Prudence:

The rebuttal of the initial presumption of prudence can be as simple as showing the poor outcome of management's decision-making. Thus, "[i]n the Union Electric case, the Commission found that the showing of two billion dollars in cost overruns associated with the building of the Callaway nuclear plant was sufficient to raise serious doubts about the prudence of Union Electric's expenditures, thus shifting the burden to Union Electric to show that its

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[8] So described by the Commission, for example, at *In the Matter of Missouri Gas Energy,* 11 Mo.P.S.C.3d 206, 222-223 (2002).

[9] *St. ex rel. Associated Natural Gas Co., supra,* 954 S.W.2d at 528; *quoting In the Matter of Union Electric,* 27 Mo.P.S.C. (N.S.) 183, 193 (1985), *in turn quoting Anaheim, Riverside, Etc. v. Fed. Energy Reg. Com'n*, 669 F.2d 799, 809 (D.C. Cir. 1981).

[10] *St. ex rel. Associated Natural Gas Co., supra,* 954 S.W.2d at 529, *quoting In the Matter of Western Resources,* Case No. GR-93-140 (*Order Denying Motion to Strike Testimony,* issued December 9, 1994).

[11] *State ex rel. Associated Natural Gas Co. v. PSC,* 954 S.W.2d 520, 529 (Mo. App., W.D. 1997).

expenditures were prudent."[12] Thus, the presumption of prudence is rebutted, and the utility is obliged to show that its costs and conduct are just and reasonable, when the challenger points to facts that raise a serious concern that the ratepayers are being overcharged or otherwise exposed to an unreasonable risk.

In the present case, those facts are (1) MGE's admission that its available firm capacity serving its Joplin service area was insufficient to meet the design day requirement for that service area (Finding of Fact 9); (2) MGE's inadequate planning methodology (Findings of Fact 10-16), (3) resulting in its contracting for more pipeline transportation capacity than it reasonably needed (Finding of Fact 17), and (4) its surprising inability to produce basic records documenting its planning activities (Finding of Fact 18). All of these matters raise serious questions such that the Commission finds that the presumption of prudence has been rebutted.

Imprudence:

Once the initial presumption of prudence is rebutted, the utility must prove that the costs in question were prudently incurred, given what it knew or should have known at the time the decisions were actually made. The standard is reasonable care requiring due diligence.[13] "The Commission will assess management decisions at the time they are made and ask the question, 'Given all the surrounding circumstances existing at the time, did management use due

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[12] *Id.,* at 223.

[13] *In the Matter of Missouri-American Water Co.,* 9 Mo.P.S.C.3d 254, 280-281 (2000); *Union Electric*, *supra,* 27 Mo.P.S.C. (N.S.) at 194.

diligence to address all relevant factors and information known or available to it when it assessed the situation?'"[14] The Commission has stated:[15]

> [T]he company's conduct should be judged by asking whether the conduct was reasonable at the time, under all the circumstances, considering that the company had to solve its problem prospectively rather than in reliance on hindsight. In effect, our responsibility is to determine how reasonable people would have performed the tasks that confronted the company.

Staff charges that MGE's imprudent conduct was its decision to renew its Southern Star transportation contract in 2001 without a change in capacity, even though it knew it was adding other capacity on another pipeline. Ironically, this decision resulted in excess capacity for the Kansas City and St. Joseph service areas, while MGE knew that it had insufficient capacity to serve its Joplin service area (Finding of Fact 9).

Staff contends that the decision to renew the Southern Star contract was imprudent because it was done without first performing a comprehensive analysis of its capacity requirements. Reasonable care and due diligence require that one determine how much capacity is actually needed before entering into a multi-year transportation contract. Staff has shown that MGE's planning process was inadequate in several respects and the Commission finds that MGE's renewal of the Southern Star transportation contract at the pre-existing capacity was indeed imprudent because made in the absence of a sound forecast of capacity requirements.

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[14] *Union Electric*, *supra,* 27 Mo.P.S.C. (N.S.) at 194.

[15] *In the Matter of Missouri Gas Energy, supra,* 11 Mo.P.S.C.3d at 222-223, *citing Union Electric*, *supra,* 27 Mo.P.S.C. (N.S.) at 194, *quoting Consolidated Edison Company of New York, Inc.,* 45 P.U.R. 4th 331 (1982).

However, Staff need not show that MGE renewed its Southern Star contract without knowing whether or not it actually needed all of the capacity thereby obtained. It is also inappropriate to charge ratepayers for capacity that a utility acquires knowing full well that it is in excess of current needs. The Commission finds that MGE had a strong motivation to retain its Southern Star capacity because that capacity was low-cost, flexible and difficult to acquire (Finding of Fact 24). For this reason, the Commission doubts that MGE ever seriously considered reducing its capacity on that pipeline. Capacity that is in excess of reasonable requirements is not "used and useful" and thus cannot be charged to the ratepayers.[16] Rather, it is an investment against future need made by the shareholders and thus chargeable to them.

The Harm to the Ratepayers:

The excess capacity demonstrated by Staff cost money and that cost, if charged to the ratepayers, constitutes an undeniable harm to them. Consequently, the cost of the excess capacity, as calculated by Staff, must be disallowed from recovery.

Respectfully submitted,

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[16] *In the Matter of Missouri-American Water Company, supra,* 9 Mo.P.S.C. 3rd at 283-284 (portion of cost of new St. Joseph water treatment plant excluded from rate base because not used and useful in that capacity of new plant was in excess of system's current need).

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/s/ Kevin A. Thompson
Kevin A. Thompson