

Poston, Marc

From: Kind, Ryan
Sent: Friday, November 16, 2007 2:51 PM
To: 'Pendergast, Mike'; Shemwell, Lera; Schallenberg, Bob; Imhoff, Tom; Sommerer, David
Cc: Poston, Marc; Trippensee, Russ
Subject: Follow-up to 10/26/07 Laclede affiliate issues meeting

Mike and others,

A couple of weeks ago members of Staff and OPC met with Laclede to begin discussing affiliate transaction and CAM issues pursuant to paragraph 23 of the Unanimous Stipulation and Agreement in Case No. GR-2007-0208. At that meeting you asked OPC to put together a list of the concerns that we have with Laclede's CAM and any changes that we would like to see in Laclede's annual filing schedule for information that is required by the Commission's Affiliate Transaction rule.

Regarding the annual filing schedule, as we have discussed previously, OPC would like for Laclede to begin making its annual filings for the year ending September 30 on December 15 (2 1/2 months after the end of Laclede's fiscal year). The date of Laclede's annual filings are addressed on page 1 of the CAM. Public Counsel believes that it would be necessary to obtain a variance from the affiliate rule to depart from the calendar year filings required by the rule and we would not oppose such a variance.

Subsection (3)(D) of 4 CSR 240-40.015 states as follows:

(D) In transactions involving the purchase of goods or services by the regulated gas corporation from an affiliated entity, the regulated gas corporation will use a commission approved CAM **which sets forth cost allocation, market valuation and internal cost methods**. This CAM can use benchmarking practices that can constitute compliance with the market value requirements of this section if approved by the commission. (Emphasis added.)

Here are the concerns that we have with the Laclede CAM.

1. The Laclede CAM contains a number of items that do not pertain to the rule requirement of setting forth "cost allocation, market valuation and internal cost methods." For the most part, we do not believe these additional items should be in the CAM unless they are necessary to clarify the cost allocation process or to comply with previous agreements and Commission orders regarding affiliate transactions and related subjects.
2. There appears to be a conflict between (or at least some ambiguity) the transfer pricing standards described on page 7 in IX.A.(i) and (ii) and the language in IX.C. regarding fully distributed costs. While the transfer pricing standards described on page 7 in IX.A.(i) and (ii) properly describe the affiliate rule standards in (2)(A) of 4 CSR 240-40.015, the language on pages 8 through 15 in section IX.C. appears to state that in all instances the fully distributed cost calculation methodology will be applied. For example, paragraph C. on page 8 states that "The fully distributed cost of an asset or service shall be identified and charged or allocated to the asset or service in accordance with these general principles, as more fully outlined below:" This sentence appears to require that charges and allocations be based on fully distributed cost, even when it should be based on a market evaluation pursuant to the affiliate rule standards in (2)(A) of 4 CSR 240-40.015. The above quoted sentence could be changed to state "The fully distributed cost of an asset or service shall be identified and CALCULATED in accordance with these general principles, as more fully outlined below:"
3. Similar to the problem identified in 2 above, on page 8 of the CAM in paragraph (i) it states "Costs incurred for materials or services that are specifically attributable to goods or services provided to an affiliate shall be charged directly to the books and records of the affiliate, using standard voucher account distribution procedures." This provision also seems to conflict with the affiliate rule standards in (2)(A) of 4 CSR 240-40.015 since it does not reflect the higher of cost or market standard in the rule. The same problem occurs in paragraph (ii) on page 9 of the CAM.
4. The language in and following the paragraph titled "Energy Related Goods and Services" on page 13 of the CAM also appears to be inconsistent with the affiliate rule standards in (2)(A)1. of 4 CSR 240-40.015. The paragraphs that follow this paragraph appear to state that when affiliates provide energy-related goods and services to Laclede they will be priced at market instead of the lower of market or the cost that the "fully distributed cost to the regulated gas corporation

to provide the goods or services for itself." Subsection (3)(D) of 4 CSR 240-40.015 requires Laclede to have a CAM that includes the "internal cost methods" that will be used to arrive at an estimate of the "fully distributed cost to the regulated gas corporation to provide the goods or services for itself." The Laclede CAM appears to use a pricing standard that essentially means an affiliate can charge Laclede the lower of market or market for any energy-related goods and services that it provides to Laclede.

5. The language on page 14 of the CAM about "gas supply sales" from Laclede to its affiliates does not include selling at the higher of cost or market as required by the affiliate rule standards in (2)(A)1. Instead, the language in the "gas supply sales" paragraph on page 14 of the CAM states that all sales from Laclede to its affiliates should be made at the "fair market price" even if Laclede's cost for the gas supplies exceeded the "fair market price."

6. The language on page 15 of the CAM about "pipeline transportation and storage capacity releases" from Laclede to its affiliates includes some recognition of the need to price such transactions at the higher or cost or market but the description of the fully distributed cost calculation does not provide sufficient detail where it refers to "an appropriate allocation of joint and common costs, given the nature, location and timing of the transaction."

7. Section XII. on page 16 of the CAM should also state that when Laclede enters into a non-complying affiliate transaction, it should file a notice of that transaction to the Commission and Public Counsel within 10 days of doing so as required by (10)(A)2.B. of 4 CSR 240-40.015.

Also, please remember that during our meeting on 10/26/07 Mike Pendergast stated that he did not believe that Laclede Gas makes any joint purchases of gas, pipeline capacity, or storage with LER but that he would check on this and get back to me to verify.

Thanks,

Ryan Kind
Office of Public Counsel