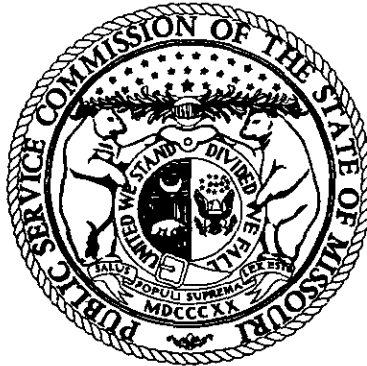


**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**



In the matter of Associated Natural
Gas Company's Tariff Revisions to be
Reviewed in its 1995-1996 Actual Cost
Adjustment.

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Case No. GR-96-227

REPORT AND ORDER

Issue Date: January 26, 1999

Effective Date: February 5, 1999

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Associated Natural)	
Gas Company's Tariff Revisions to be)	<u>Case No. GR-96-227</u>
Reviewed in its 1995-1996 Actual Cost)	
Adjustment.)	

APPEARANCES

Gary W. Duffy, Attorney at Law, Brydon, Swearengen & England, P.C., P.O. Box 456, 312 East Capitol Avenue, Jefferson City, Missouri 65102-0456, for Associated Natural Gas Company.

Jeffrey L. Dangeau, Attorney at Law, P.O. Box 1408, Fayetteville, Arkansas 72702, for Associated Natural Gas Company.

Cherlyn McGowan, Assistant General Counsel, P.O. Box 360, Jefferson City, Missouri 65102, for Staff of the Missouri Public Service Commission.

Douglas E. Micheel, Senior Public Counsel, P.O. Box 7800, Jefferson City, Missouri 65102, for Office of Public Counsel.

REGULATORY LAW JUDGE: Morris L. Woodruff

REPORT AND ORDER

Procedural History

This case was established to consider Associated Natural Gas Company's (ANG's) Actual Cost Adjustment (ACA) for the year ending October 31, 1996. ANG submitted tariff sheets designed to revise the ACA factors for each of its three Missouri districts. Those tariff sheets were

approved on October 30, 1996 on an interim, subject to refund basis. In the same order the Commission directed its Procurement Analysis Department (Staff) to conduct an audit of the ACA period and submit its recommendation by August 1, 1997. Staff conducted the required audit and submitted its recommendation on August 4. Staff recommended several adjustments to ANG's ACA filing. On September 4, ANG filed a response to Staff's recommendations. The only recommendation with which ANG disagreed concerns Staff's proposal to reduce ANG's SEMO District gas costs by \$254,476 to eliminate an alleged double recovery in ANG's 1995-1996 ACA filing of Liquefied Natural Gas (LNG) and Natural Gas Pipeline of America (NGPL), non-S2 storage withdrawal dollars. The double recovery allegedly occurred as a result of ANG's change in ACA recovery methodology with regard to storage injection and withdrawals.

An Order Adopting Procedural Schedule was filed on November 21. Direct Testimony on behalf of Staff and ANG was filed on November 24, Rebuttal testimony was filed on behalf of both parties on January 23, and Surrebuttal testimony was filed on behalf of both parties on March 2.

A hearing was held on April 7. Staff and ANG submitted initial briefs on May 11, and reply briefs on June 1. Although the Office of the Public Counsel entered its appearance at the hearing, it chose not to participate further in the hearing and did not submit post-hearing briefs.

Findings of Fact

The Missouri Public Service Commission has considered all of the competent and substantial evidence upon the whole record in order to make

the following findings of fact. The Commission has also considered the positions and arguments of all the parties in making these findings. Failure to specifically address a particular item offered into evidence or a position or argument made by a party does not indicate that the Commission has not considered it. Rather, the omitted material was not dispositive of the issues before the Commission.

Evidence Presented

Staff alleges that ANG has double recovered \$254,476 for natural gas withdrawn from LNG and NGPL non-S2 storage between December 1, 1995 and October 31, 1996. Staff proposes to decrease ANG's SEMO District gas costs by that amount when calculating ANG's ACA adjustment.

The ACA adjustment is designed to permit a gas utility to pass along to consumers the actual costs it incurs for purchase of natural gas. For the period in question, ANG included in its actual cost the value of natural gas which it removed from storage in its LNG and NGPL non-S2 storage facilities after December 1, 1995. Prior to December 1, 1995, ANG had employed an "up-front" ACA recovery method under which it passed on to consumers its cost of gas that was injected into LNG and NGPL non-S2 storage at the time the gas was injected into storage. Beginning on December 1, 1995, ANG changed to an "as withdrawn/consumed" recovery method.

Staff agreed with ANG's decision to change its recovery method because ANG already used the "as withdrawn/consumed" method with regard to its other storage accounts and that method is also used by the majority of other Local Distribution Companies in Missouri. However,

Staff asserted that ANG should only be allowed to recover under the new "as withdrawn/consumed" method for those gas supplies injected into storage after the changeover date of December 1, 1995. Allowing ANG to recover for the gas supplies injected prior to the change over date would allegedly permit ANG to recover the cost of the previously injected gas both at the time of injection under the former "up-front" recovery method as well as at the time of withdrawal under the new "as withdrawn/consumed" method.

ANG responded to Staff's position by submitting the Direct Testimony of Mark S. Kidd. Mr. Kidd's testimony asserted that there had been no double recovery. Mr. Kidd testified that the amount of natural gas that ANG has in storage varies greatly over the course of a year. The company purchases extra gas during the warm weather months, when prices and demand are low, and injects it into storage. Then during the cold weather months, when prices and demand are high, the company withdraws some of the gas from storage to meet peak demand and to reduce the price that it would otherwise need to pay for gas on the market at that time. From September 1982, through November 1995, ANG included in its ACA recovery the cost of gas injected into LNG and NGPL non-S2 storage. Beginning December 1, 1995, ANG began including the cost of LNG and NGPL non-S2 withdrawals in its ACA recovery. Kidd testified that ANG was concerned about the possibility of over- or under-recovery at the time it decided to change from an "up-front" recovery method to an "as withdrawn/consumed" method. However, ANG does not agree that any over-recovery has occurred.

ANG argues that in order to prevent an over- or under-recovery, the actual costs recovered by ANG under the old "up-front" recovery method must be compared to the costs that ANG would have recovered under the new "as withdrawn/consumed" method if that method had been in use throughout the period. ANG made such calculations and they show that for the period of September 1982 through November 1995, injections actually recovered totaled \$5,166,804 and withdrawals from storage totaled \$5,174,736. Thus, changing to the "as withdrawn/consumed" recovery method on December 1, 1995 resulted in an under-recovery by ANG in the amount of \$7,932. Put another way, ANG's calculations alleged that it had a beginning inventory of gas in storage on September 1, 1982 of \$835,859. Injections of \$5,166,807 were added to that amount and then withdrawals of \$5,174,739 were subtracted. The result is an ending inventory balance of \$827,927 as of November 30, 1995. The value of ANG's inventory of gas in storage was thus reduced by \$7,932 and ANG has allegedly under-recovered by that amount.

In response to the Direct Testimony of Mark S. Kidd, the Staff filed the rebuttal testimony of Michael J. Wallis. Wallis' testimony argued that prior to July 8, 1982, the date when ANG began recovering its procurement gas costs through the ACA true-up mechanism, ANG had already recovered approximately \$663,000 of Missouri allocated storage withdrawal costs in an up-front fashion¹. Staff argued that this up-front recovery

¹A portion of the value of ANG's natural gas storage inventory, specifically a portion of the inventory in ANG storage, would be used outside Missouri and would not be allocated to Missouri ratepayers.

had occurred because prior to July 8, 1982, the Purchased Gas Adjustment (PGA) tariffs then in effect would have allowed ANG to recover the cost of gas injected into storage by charging its Missouri customers an estimated PGA rate. That rate was based on the Company's average cost of gas, which was determined by using the most recent supplier invoices without a reduction for gas injected into storage. In support of this argument, Staff attached a copy of Missouri PSC PGA tariff sheet number 44 which served as ANG's PGA clause for the SEMO District for the period of June 2, 1978 to July 8, 1982. Staff asserted that this tariff sheet would have permitted ANG to recover all of the cost of gas injected into storage prior to July 8, 1982.

ANG did not accept Staff's position and submitted the surrebuttal testimony of Mark S. Kidd. In his surrebuttal testimony, Kidd analyzed the operation of tariff sheet 44. Kidd pointed out that tariff sheet 44 does not make any specific mention of the treatment of gas in storage. However, he asserted that tariff sheet 44 provided for recovery of gas costs from customers as consumed rather than recovery as purchased as alleged by Staff. Calculations using similar assumptions in three different scenarios, attached to his testimony as Schedule MSK-9, illustrate Kidd's understanding of the operation of tariff sheet 44.

Kidd's surrebuttal testimony also indicated that ANG had changed its position with regard to the date that the ACA mechanism commenced and its effect on the value of gas in storage on that date. Kidd indicated that his previous calculations had assumed a starting date of September 1, 1982 but that tariff sheet 44 showed that the ACA mechanism would have

gone into effect on July 8, 1982 which is the date that tariff sheet 44 was canceled. Using this new date, Kidd contends that a positive adjustment for gas costs of \$19,522 should be ordered by the Commission to compensate ANG for the additional value of gas in storage.

Staff submitted the surrebuttal testimony of Michael J. Wallis. In that testimony, Mr. Wallis again emphasized Staff's contention that ANG had, prior to July 8, 1982, recovered its storage withdrawal costs in an up-front fashion. He testified that ANG accomplished this by charging its Missouri customers an estimated PGA rate which was based on ANG's average cost of gas, determined by using the most recent supplier invoices, including gas supplies injected into storage.

An evidentiary hearing was held on April 7, 1998. At the hearing, Michael Wallis testified on behalf of the Staff and Mark Kidd testified on behalf of ANG. Mr. Kidd reiterated his interpretation of tariff sheet 44 as providing for recovery by ANG of gas costs as the gas was consumed and not as it was injected into storage. Mr. Kidd did agree that supplier invoices from a gas pipeline prior to July 8, 1982 would have included the cost of gas purchased as well as transportation and storage costs in one lump sum cost of gas figure. Mr. Wallis testified that tariff sheet 44 would have included storage costs as part of the invoiced cost that was the basis for establishing a rate. He stated that it was Staff's position that the value of the gas in storage as of July 8, 1982 was recovered at the time it was purchased by ANG.

Discussion

Burden of Proof

The Missouri Supreme Court has stated that "[t]he law in this state as to the burden of proof is clear and designed to assure that hearings on contested matters provide the parties with predictable rules of procedure. The party asserting the positive of a proposition bears the burden of proving that proposition." Dycus v. Cross, 869 S.W. 2d 745, 749 (Mo. banc 1994). In this case, the Staff is asserting that ANG is double recovering the value of the gas it has in storage. Therefore, according to the rule set out in Dycus, the Staff has the burden of proving its assertion.

Section 393.150.2, RSMo (1994), does state that "[a]t any hearing involving a rate sought to be increased, the burden of proof to show that the increased rate or proposed increased rate is just and reasonable shall be upon the gas corporation," In this case, ANG is, in effect, seeking to increase its rate through the PGA/ACA process. Therefore, it does, in general, have the burden of proving that its proposed rate is just and reasonable. However, the existence of Section 393.150 does not establish that ANG has the burden of proof as to all issues. Requiring ANG to prove the negative of Staff's assertion regarding double recovery would violate the rule set forth in Dycus.

Staff argued in its initial brief that an exception to the Dycus rule should apply in this case. Staff claimed that ANG should have the burden of proving that it has not already recovered the value of the stored gas because the evidence that would be required to prove that ANG

has already recovered the value of the gas through operation of tariff sheet 44 is in the exclusive control of ANG. The exception to the burden of proof rule cited by Staff certainly does exist. However, Staff's argument must fail because there was no showing that ANG had exclusive or even primary control over any documents or other evidence relevant to the determination of the issues in this case. There is no indication in the record that the Staff requested that ANG produce any documents that were not produced. In fact, ANG's expert witness, Mark S. Kidd, testified that he had based his analysis of the operation of tariff sheet 44 on documents that he reviewed at the offices of the Commission. Far from establishing that there were any documents or other evidence in the exclusive control of ANG, Staff's witness, Michael Wallis, testified that there were no missing documents.

Allegation of Double Recovery

Staff's initial position, as set forth in direct testimony of Michael J. Wallis, was that the fact of ANG's double recovery for gas sold out of storage was essentially self-evident. Wallis testified that "[p]rior to December 1, 1995, ANG would have recovered the amounts in its LNG and NGPL non-S2 storage accounts by (1) including the entire . . . commodity gas cost amount in its ACA filing and (2) excluding from the ACA filing the subsequent withdrawal, from storage of the . . . commodity gas amount which had previously been injected into storage." On December 1, 1995, ANG switched to an accounting system whereby it recovered the amounts in storage by including in its commodity gas amount in its ACA filing the value of the gas withdrawn from storage. Thus, Staff argued

that ANG included the value of the gas in its ACA filings both at the time the gas was injected into storage and at the time it was withdrawn from storage, resulting in a double recovery by ANG.

ANG through the rebuttal testimony of Mark Kidd argued that what seemed to be a double recovery in fact was not so. ANG contended that it had injected and withdrawn essentially equal values of gas since 1982 when the ACA mechanism first went into effect. Therefore, ANG would have recovered essentially the same amount under the ACA mechanism whether it used the "as injected" or the "as withdrawn" method of accounting for the value of gas in storage. Therefore, there was no double recovery and ANG should be able to recover the value of gas as withdrawn after December 1, 1995 to the extent that the recovered gas was being taken from the balance that existed in 1982, when the ACA mechanism went into effect.

ANG's theory is premised on the existence of a pre-existing balance of gas in storage at the start of the ACA process in 1982. Staff did not attempt to refute ANG's calculations regarding the interaction between the "as injected" and "as withdrawn" methods. Instead, Staff argued that the value of the pre-existing balance of gas in storage had already been recovered by ANG prior to the inception of the ACA process.

As the basis for this theory, Staff cited the operation of tariff sheet 44, which was the PGA mechanism in effect for ANG for the period of June 2, 1978 to July 8, 1982. Staff argued that tariff sheet 44 allowed ANG to recover its storage withdrawal cost in an up-front fashion by charging its Missouri customers an estimated PGA rate which was based on the Company's average cost of gas - determined by using the most recent

supplier invoices - to compute the appropriate adjustments to its rates. Staff pointed out that tariff sheet 44 does not state that ANG was to use the most recent supplier invoices less storage injections. Therefore, ANG would have been allowed to include the value of all gas purchased, whether stored or sold, in its PGA rates.

Staff's position is persuasive. From June 2, 1978 to July 8, 1982, tariff sheet 44 served as ANG's PGA Clause for the SEMO District and it controlled ANG's recovery treatment of storage injection and withdrawal costs during that period. As of July 8, 1982, the date tariff sheet 44 was canceled, ANG had fully recovered its storage costs incurred up to that date. In order to understand the fact of this recovery, it is important to understand that tariff sheet 44 operated in a pre-FERC Order 636 environment in which all components of gas supply and service were provided by the pipeline and appeared on the pipeline invoices.

Before the Federal Energy Regulatory Commission (FERC) issued Order 636, interstate natural gas pipeline companies provided local distribution companies with a bundled gas supply, transportation and storage. FERC Order 636 required interstate natural gas pipelines to unbundle their gas supply service from their transportation and storage services. Prior to FERC Order 636, components of gas supply service included fixed and variable storage charges, fixed and variable transportation charges and all gas supply costs, irrespective of whether that gas supply flowed directly to the city gate or was injected into storage. Thus, fixed and variable storage charges would have been included on pipeline supplier invoices in the pre-Order 636 environment

in which tariff sheet 44 operated. When ANG changed its recovery mechanism for LNG and NGPL non-S2 gas on July 8, 1982, it had already recovered the gas cost associated with those volumes injected into storage prior to that date. To allow it to recover those costs again when the gas was removed from storage after December 1, 1995 would indeed result in double recovery.

Conclusions of Law

The Missouri Public Service Commission has arrived at the following conclusions of law:

Associated Natural Gas Company, a division of Arkansas Western Gas Company, is a gas corporation as defined under Section 386.020(18), RSMo (Supp. 1997)

Associated Natural Gas Company, a division of Arkansas Western Gas Company, is an investor-owned public utility engaged in the provision of natural gas service in the State of Missouri and is, therefore, subject to the jurisdiction of the Missouri Public Service Commission under Chapters 386 and 393, RSMo.

Associated Natural Gas Company, a division of Arkansas Western Gas Company, has the burden of proving that the increased rate or proposed increased rate is just and reasonable. Section 393.150.2, RSMo (1994).

The Staff of the Missouri Public Service Commission has the burden of proving its assertion that Associated Natural Gas Company's SEMO District gas costs should be reduced by \$254,476 to eliminate an alleged double recovery, in ANG's 1995-1996 ACA filing, of Liquefied Natural Gas (LNG) and Natural Gas Pipeline of America (NGPL), non-S2 storage

withdrawal dollars which allegedly occurred as a result of ANG's change in ACA recovery methodology with regard to storage injection and withdrawals. Dycus v. Cross, 869 S.W. 2d 745, 749 (Mo. banc 1994).

IT IS THEREFORE ORDERED:

1. That Staff's proposal to reduce Associated Natural Gas Company's SEMO District gas costs by \$254,476 to eliminate an alleged double recovery is affirmed.
2. That Associated Natural Gas Company's request to increase its SEMO District gas costs by \$19,522 is denied.
3. That any pending motions or objections not specifically ruled on in this order are hereby denied or overruled.
4. That this Report and Order shall become effective on February 5, 1999.

BY THE COMMISSION



**Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge**

(S E A L)

Lumpe, Ch., Crumpton and Schemenauer, CC.,
concur and certify compliance with the
provisions of Section 536.080, RSMo 1994.
Murray and Drainer, CC., dissent with opinion

Dated at Jefferson City, Missouri,
on this 26th day of January, 1999.

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the matter of Associated Natural Gas)
Company's Tariff Revisions to be Reviewed)
in its 1995-1996 Actual Cost Adjustment.)

Case No. GR-96-227

**DISSENTING OPINION OF COMMISSIONER CONNIE MURRAY AND
VICE CHAIR M. DIANNE DRAINER**

We respectfully disagree with the opinion of the majority in the Report and Order. We are not convinced that the evidence presented is sufficient to support the findings of the majority. We found the evidence presented by Associated Natural Gas Company's witness to be more persuasive, just and reasonable with respect to the 1995-1996 Actual Cost Adjustment. For this reason, we respectfully dissent.

Respectfully submitted,


Commissioner Connie Murray


Vice Chair M. Dianne Drainer

Dated at Jefferson City, Missouri,
on this 26th day of January, 1999.