Exhibit No.:
Issue: ** ______________ **
Witness: David M. Sommerer
Sponsoring Party: MoPSC Staff
Type of Exhibit: Direct Testimony
Case No.: GR-2004-0273
Date Testimony Prepared: September 8, 2006

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

DAVID M. SOMMERER

LACLEDE GAS COMPANY

CASE NO. GR-2004-0273

Jefferson City, Missouri
September 2006

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

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DAVID M. SOMMERER

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GR-2004-0273

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DIRECT TESTIMONY

OF

DAVID M. SOMMERER

LACLEDE GAS COMPANY

GR-2004-0273

Q. Please state your name and business address.

A. David M. Sommerer, P.O. Box 360, Jefferson City, Mo. 65102.

Q. By whom are you employed and in what capacity?

A. I am the Manager of the Procurement Analysis Department with the Missouri Public Service Commission.

Q. Please describe your educational background.

A. In May 1983, I received a Bachelor of Science degree in Business and Administration with a major in Accounting from Southern Illinois University at Carbondale, Illinois. In May 1984, I received a Master of Accountancy degree from the same university. Also, in May 1984, I sat for and passed the Uniform Certified Public Accountants examination. I am currently a licensed CPA in Missouri. Upon graduation, I accepted employment with the Commission.

Q. What has been the nature of your duties while in the employ of the Commission?

A. From 1984 to 1990 I assisted with audits and examinations of the books and records of public utilities operating within the State of Missouri. In 1988 the responsibility for conducting the Actual Cost Adjustment (ACA) audits of natural gas utilities was given to the Accounting Department. I assumed responsibility for planning and implementing these audits and trained available Staff on the requirements and conduct of the audits. I participated in most of the ACA audits from early 1988 to early 1990. On November 1, 1990, I transferred to the Commission's Energy Department. Until November of 1993, my duties consisted of reviews of various tariff proposals by electric and gas utilities, Purchased Gas Adjustment reviews, and tariff reviews as part of a rate case. In November of 1993, I assumed my present duties of managing a newly created department called the Procurement Analysis Department. This Department was created to more fully address the emerging changes in the gas industry especially as they impacted the utilities' recovery of gas costs. My duties have included managing the five member staff, reviewing ACA audits and recommendations, participating in the gas integrated resource planning project, serving on the gas project team, serving on the natural gas commodity price task force, and participating in matters relating to natural gas service in the State of Missouri. In July of 2006, the Federal Issues/Policy Analysis Section was transferred to the Procurement Analysis Department. That group analyzes filings made before the Federal Energy Regulatory Commission (FERC).

Q. Have you previously testified before this Commission?

A. Yes. A list of cases and issues in which I have filed testimony is included as Schedule 1 of my testimony.

Q. Did you make an examination and analysis of the books and records of Laclede Gas Company (Company, Laclede) in regard to matters raised in this case?

A. Yes. I have examined these records in the context of the issues I am addressing in this case.

Q. What matters will you address in your testimony?

A. I am sponsoring the Staff's position regarding Laclede's decision to rely on ** ____ ____ **

Q. What knowledge, skill, experience, training, or education do you have in these matters?

A. I have been assigned and testified in many Purchased Gas Adjustment (PGA) and ACA proceedings. I have reviewed numerous ACA filings and have evaluated the purchasing practices of various Local Gas Distribution Companies (LDCs) in Missouri. I have also attended conferences and seminars related to the natural gas futures market and other natural gas issues.

Q. What is the purpose of your direct testimony in this case?

A. I will provide support for the Staff's disallowance of certain ** ____ ______________________________ **

Q. What areas of this case have you reviewed?

A. I have reviewed Laclede's decision to rely on ** ________ ** for the 2003-2004 ACA period. The particular ACA review related to the 12 months ending September 30, 2004. The Staff's Recommendation memorandum in this case is attached as Schedule 2.

EXECUTIVE SUMMARY

Q. Please provide an executive summary of Staff's disallowance?

A. Staff is asserting that it was imprudent for Laclede Gas Company to pay an approximate doubling of ** ______________________________ ____

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______________ ** resulted in over $2,000,000 of excess costs as compared to the ** ____________________________ **

<u>ACA PROCESS</u>

Q. What is the purpose of the ACA review?

A. The Procurement Analysis Department conducts an Actual Cost Adjustment (ACA) Review annually at the end of each ACA period. The ACA process has a number of purposes. A primary purpose of the ACA process is to reconcile the company's actual gas costs with what it charged customers (its billed revenues). In its purchased gas adjustment (PGA) filings the Company estimates its gas costs for the upcoming year. In the ACA, the estimate is reconciled with the actual cost of gas. In this function the Procurement Analysis Department Staff reviews the gas purchases of the LDC to ensure that the claimed costs are properly attributed to the period under review and that the pipelines and natural gas suppliers have charged or invoiced the LDC for the volumes nominated and received at the proper contract rates. A comparison of billed revenue recovery with actual gas costs will normally yield either an over-recovery or under-recovery of the ACA balances.

Another purpose of the ACA process is to examine the reliability of the LDC's gas supply, transportation, and storage capabilities. For this analysis, Staff reviews the estimated peak day requirements and the capacity levels to meet those requirements, peak day reserve margin and the rationale for this reserve margin, and natural gas supply plans for various weather conditions.

A third purpose of the ACA process is to review the LDC's gas purchasing practices to determine the prudence of the Company's natural gas purchasing and operating decisions. Staff will consider the financial impact on customers of the LDC's use of its gas supply, transportation and storage contracts in light of the conditions and information available when the operational decisions were made.

Q. What is the review period for this ACA case?

A. The Staff's review included an analysis of billed revenues and actual gas costs for the 2003-2004 ACA for the period October 1, 2003, through September 30, 2004.

TERMINOLOGY

Q. Please provide an overview of the terminology that will be used in this case.

A. First, it will be helpful to provide some definitions of certain terms that will be used in this case, and some discussion of the basic terminology. This case will involve the pricing of the natural gas commodity. It is important to note the difference between natural gas transportation and natural gas commodity. Natural gas is hauled or transported from the producing zones in the U.S. to the market areas via a system of interstate pipelines. The major producing areas that serve the Midwest include the Gulf Coast, both on shore and offshore, the South Texas area, the Arkoma and Anadarko basins in Arkansas, Oklahoma and Kansas, and the Rocky Mountain areas of Colorado and Wyoming. Tariff rates for transportation of the gas through long haul interstate pipelines are regulated by the Federal Energy Regulatory Commission (FERC). The natural gas commodity itself has been unregulated since 1993. LDCs such as Laclede must negotiate and contract with pipelines or marketers for their natural gas transportation. LDCs must negotiate and contract with gas producers and marketers for their gas supply.

Since at least the late 1980s a practice arose for pricing the natural gas commodity through the use of an index. A natural gas index was supposed to represent a market price for natural gas for a particular time period and for a specific location. Natural gas industry publications such as "Inside FERC's Gas Market Report", and "Natural Gas Intelligence" would take samples of natural gas commodity prices from many different production areas and would associate these samples to a particular interstate pipeline. The samples could be for deals that were designed to last 30 days in order to develop a monthly index, or, for only daily transactions in order to develop a daily index.

The general concept was to have a representative sample of actual gas trading that was done at a particular location for a specific time period. Those trades would have been "fixed price" deals. A fixed price simply means a price that does not fluctuate after it has been set. Thus, the price is known with certainty. Fixed priced deals sometimes imply a contract of longer duration, but in fact, a fixed price could be fixed for 30 days or even one day. A fixed price is known "upfront". Obviously, a fixed price deal for one year provides much more certainty than a fixed price that is set for 30 days.

The spot market is another concept that is important to understand in the context of pricing of natural gas contracts. The spot market generally refers to a short-term gas transaction, often only for a few days of gas supply.

Index pricing is a common practice used by LDCs to set the commodity price for natural gas that it buys from producers/marketers. An index for FOM would be found by referring to a recognized industry publication that publishes indices for various locations throughout the country. The FOM is established each month and represents a sampling during "bid-week", the last few days prior to the beginning of the month the gas flows, of actual transactions for natural gas at a specific location.

In a similar manner, a "daily index" is calculated for each day that gas flows in order to provide the industry with an indication of what daily market prices are for a particular location. In both instances, what the LDC will eventually pay for the gas is an absolute unknown, until after the gas index is published. Therefore, a typical pricing provision might refer to an FOM index or a Gas Daily index for a particular pipeline location. The pricing provision could be in place many months in advance of the actual delivery and therefore, many months prior to the actual price being known.

The flexibility of the gas supply will have a bearing on how it is priced. ** __

**

Q. How does Laclede price its various supplies?

A. ** **

Q. What is a ** **

A. **

**

Q. What is another way to price "swing supply"?

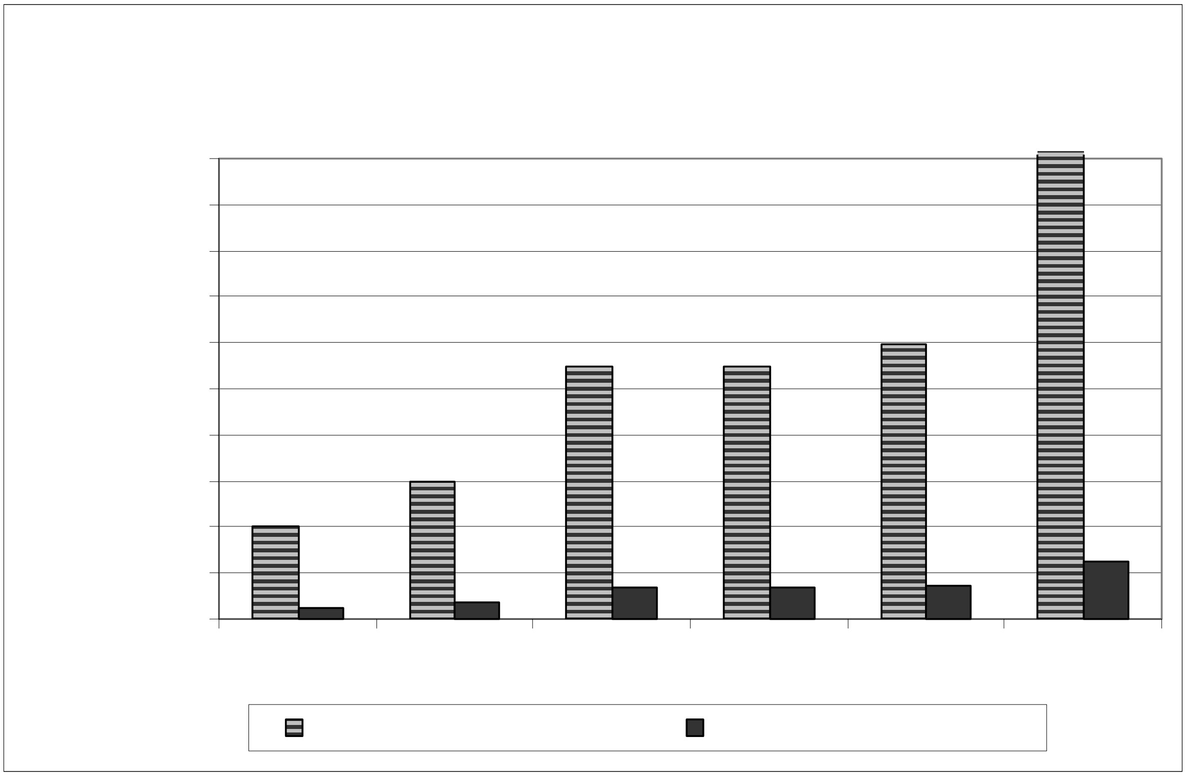
A. ** **

RECOMMENDED DISALLOWANCE

Q. Why has Staff calculated a disallowance in this case?

A. From the 2002/2003 ACA to the 2003/2004 ACA, ** ** for each of the ACA periods 1998/1999 through 2003-2004 are shown in the chart below. (The details are provided in the attached Schedule 3.)

** Chart is Highly Confidential in it Entirety



** ____
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During Laclede's most recent rate case, the Staff asked whether the Company had performed a ** ____
____
____________________________________ **

Q. Did Laclede provide a study?

A. Laclede produced a ** __________________ ** that showed "savings" from the choice of an ** ____ ** attached as Schedule 4. Staff received the ** ________________ ** in response to Data Request (DR) No. 225 in the Laclede Gas Company rate case, GR-2005-0284. It was immediately apparent that the study was outdated and contained data from the mid-1990s, at least seven years prior to the fly-up in ** ____________________ ** Laclede prepared an update of its ** _____ ____________________________________ ** attached as Schedule 5. No study had been performed during the intervening 9 years.

Q. Is it your experience that the gas industry changed from the time of the ** ____________ ** until the 2003-2004 ACA?

A. Yes. The supply and demand fundamentals, pricing, trading, and a host of other factors changed. The Enron collapse had not occurred. Supply and demand was not perceived as being nearly as tight in the mid-1990s. Gas demand for electric generation was changing during this time period. In the mid-1990s prices at the New York Mercantile Exchange (NYMEX) hadn't seen the $10/MMBtu experienced in the winter of 2000/2001.

Q. Did Staff review Laclede's ** _____________ ** regarding ** __________ ________________________________ **

A. Yes. Although the document was only available in hard copy (the electronic spreadsheet was not available), the Staff reviewed the methodology. ** ________________ ____ _______________ ** First it calculated the costs of using an ** __________________ ____ ____ **

Then *the same volumes* were used to apply the ** _________ ** that prevailed during the time period Laclede ordered the gas. The difference between the two scenarios was compared and was declared to be savings.

Q. What observations do you have about the ** _____________ **

A. Besides the study being woefully stale, it contained certain flaws that were recognized in Laclede's own footnotes to the study. ** ________________________________ ____ ____ _______ ** Mr. Jaskowiak is no longer employed with Laclede Gas Company. He works for Laclede Energy Resources (LER), an affiliate of Laclede Gas Company. ** __________ ____ ____ ____ **

Q. Why does Staff have a concern with ** ________________________________ ____ **

A. ** ____ ____ ____ ____ ____ ____ ** Thus, the savings calculated in Laclede's study are overstated.

Q. Did Mr. Jaskowiak or Laclede Gas Company discuss the methodology used in this ** ______________ ** with the Staff?

A. No.

---

[1] ** ____ **

NP

Q. **

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A. **

NP

**

Q. Does Staff have any additional concerns with Laclede's ** **

A. Yes. **

**

Q. What observations do you have about the ** **

A. ** **

Q. How did the Staff quantify its adjustment?

A. **

________ ** Attached as Schedule 6, is Staff's workpaper summary of how the disallowance was derived. ** ____ ________ ** The result is Staff's proposed disallowance of $2,424,020.

Q. ** ____ **

A. ** ____ **

Q. ** ____ **

A. ** ____ **

Q. Do you have a graph on how total ** ____________________ ** increased over time?

A. Yes, it is provided earlier in my direct testimony and is attached as Schedule 3.

Q. Prior to deciding on the ** ____ **

A. Yes. ** ____ **

Q. You mentioned the term "off-system sales" previously. Please explain that term.

A. The term relates to the practice of selling excess gas supply when it is not needed by customers in Laclede's service territory. ** ____

**

Q. What is your understanding of the advantages that Laclede argues for ** **

A. My understanding is that Laclede believes the ** **

Q. Are there any other advantages that Laclede has referenced?

A. ** **

Q. Has the Staff given Laclede a "credit" to recognize the benefit of off-system sales?

A. No. **

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__________ **

Q. What do you mean "likely bias" towards an ** _______________ **

A. ** ____
____
____
____
___________________________ **

Q. Does the customer enjoy benefits from off-system sales?

A. To some extent, yes. However, if only $2 million is imputed in a rate case, while the pricing philosophy costs something in excess of this level, it is not apparent how much the customers have gained. In addition, Laclede's marketing affiliate, LER, ** ______
____
____
____
___________________ **

Q. Do you have any other recommendations related to this issue?

A. Yes. The Staff recommends that prior to each winter heating season, Laclede prepare a cost/benefit analysis regarding ** _________________________________ ** The study should: ** **

Q. Does this conclude your direct testimony?

A. Yes.

CASES WHERE TESTIMONY WAS FILED

DAVID M. SOMMERER

COMPANY	ISSUES	CASE NO.
Missouri-American Water Co.	Payroll	WR-85-16
Great River Gas Company	Payroll, Working Capital	GR-85-136
Grand River Mutual Telephone	Cash Working Capital	TR-85-242
Associated Natural Gas Company	Revenues, Gas Cost	GR-86-86
Empire District Electric Company	Revenues	WR-86-151
Grand River Mutual Tel. Company	Plant, Revenues	TR-87-25
Great River Gas Company	Lease Application	GM-87-65
KPL Gas Service Company	ACA Gas Costs	GR-89-48
KPL Gas Service Company	ACA Gas Costs	GR-90-16
KPL Gas Service Company	Service Line Replacement	GR-90-50
Associated Natural Gas Company	Payroll	GR-90-152
United Cities Gas Company	PGA tariff	GR-90-233
United Cities Gas Company	PGA tariff	GR-91-249
Laclede Gas Company	PGA tariff	GR-92-165
United Cities Gas Company	PGA tariff, Billing Adjustments	GR-93-47
Western Resources Inc.	PGA tariff, Billing Adjustments	GR-93-240
Union Electric Company	ACA Gas Costs	GR-93-106
Missouri Public Service	Cost of Gas	GA-95-216
Missouri Gas Energy	Incentive Plan	GO-94-318
Missouri Gas Energy	PGA Clause	GO-97-409
United Cities Gas Company	PGA Clause	GO-97-410
Missouri Gas Energy	ACA Gas Costs	GR-96-450
Missouri Gas Energy	Complaint Gas Costs	GC-98-335

COMPANY	ISSUES	CASE NO.
Laclede Gas Company	Price Stabilization	GO-98-484
Laclede Gas Company	PGA Clause	GR-98-374
Laclede Gas Company	Complaint PGA	GC-99-121
Laclede Gas Company	Incentive Plan	GT-99-303
Laclede Gas Company	ACA Gas Cost	GR-98-297
Laclede Gas Company	Incentive Plan	GT-2001-329
Laclede Gas Company	Price Stabilization	GO-2000-394
Laclede Gas Company	Inventory, Off-System Sales	GR-2001-629
Laclede Gas Company	Inventory, Off-System Sales	GR-2002-356
Laclede Gas Company	ACA Price Stabilization	GR-2001-387
Laclede Gas Company	Low-Income Program	GT-2003-0117
Missouri Gas Energy	ACA Hedging/Capacity Release	GR-2001-382
Missouri Gas Energy	Pipeline Discounts, Gas Supply	GM-2003-0238
Aquila, Inc.	PGA Process, Deferred Gas Cost	EF-2003-0465
AmerenUE	Transfer of Gas Services	EO-2004-0108

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the PGA filing for Laclede Gas Company.	))	Case No. GR-2004-0273

STAFF RECOMMENDATION

COMES NOW the Staff of the Missouri Public Service Commission and files its memorandum with recommendations in this case. Staff states:

1. On October 31, 2004, Laclede Gas Company (Laclede or Company) filed a tariff sheet to adjust its charges for natural gas which is proposed to become effective November 15, 2004.

2. The Procurement Analysis Department (Staff) has reviewed Laclede Gas Company's (Laclede or Company) 2003-2004 Actual Cost Adjustment (ACA) filing and the results of Staff's analysis are contained in Appendix A to this pleading. Both HC and NP versions are being filed.

3. Staff audited and evaluated the Company's gas purchasing practices to determine the prudence of the Company's purchasing and operating decisions. Staff conducted a reliability analysis of estimated peak day requirements and the capacity levels needed to meet those requirements; peak day reserve margin and the reasons for this reserve margin; and a review of normal and cold weather requirements. Staff also reviewed MGE's hedging for the period to determine the reasonableness of the Company's hedging plans and risk management strategy.

4. In addition, Staff reviewed the Company's level of producer demand charges for reasonableness.

5. Staff recommends that the Company be required to respond to Staff's recommendations within thirty (30) days, and make several adjustments to the ACA balance as detailed in Staff's memorandum.

WHEREFORE, the Staff recommends that the Commission accept Staff's recommendations as set out on pages 11-13 of the attached Appendices.

Respectfully submitted,

DANA K. JOYCE
General Counsel

/s/ Lera L. Shemwell

Lera L. Shemwell
Senior Counsel
Missouri Bar No. 43792

Attorney for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
(573) 751-7431Telephone)
(573) 751-9285 (Fax)
lera.shemwell@psc.mo.gov

Certificate of Service

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or electronically mailed to all counsel of record this 29th day of December 2005.

/s/ Lera Shemwell

MEMORANDUM

TO: Missouri Public Service Commission Official Case File, Case No. GR-2004-0273, Laclede Gas Company

FROM: Dave Sommerer, Manager - Procurement Analysis Department, Utility Services Division
Anne Allee, Regulatory Auditor - Procurement Analysis Department, Utility Services Division
Lesa A. Jenkins, P.E., Regulatory Engineer - Procurement Analysis Department, Utility Services Division
Kwang Choe, Ph.D., Regulatory Economist – Procurement Analysis Department, Utility Services Division
Jim Busch, Regulatory Economist – Economic Analysis Section, Energy Department, Utility Operations Division

/s/ Dave Sommerer 12/29/05	/s/ Thomas R. Schwarz 12/29/05
Project Coordinator / Date	General Counsel's Office / Date

SUBJECT: Staff's Recommendation in Case No. GR-2004-0273, Laclede Gas Company's 2003-2004 Actual Cost Adjustment Filing

DATE: December 29, 2005

The Procurement Analysis Department (Staff) has reviewed Laclede Gas Company's (Company or Laclede) 2003-2004 Actual Cost Adjustment (ACA) filing. This filing was made on October 29, 2004, and is docketed as Case No. GR-2004-0273. The filing contains the Company's calculations of the ACA and Refund balances. The Staff's review included an analysis of billed revenues and actual gas costs for the period October 1, 2003 through September 30, 2004.

Laclede Gas Company serves approximately 632,000 residential, commercial and industrial customers in the St. Louis metropolitan area and the surrounding southeastern counties.

Staff conducted a reliability analysis for Laclede, including a review of estimated peak day requirements and the capacity levels to meet those requirements, peak day reserve margin and the rationale for this reserve margin, and a review of normal and cold weather requirements. The Staff also reviewed Laclede's gas purchasing practices to determine the prudence of the Company's purchasing and operating decisions.

RELIABILITY ANALYSIS

The Company is responsible for conducting reasonable long range supply planning and the decisions resulting from 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 reviews the LDC's plans and decisions regarding estimated peak day requirements and the capacity levels to meet those requirements, peak day reserve margin and the rationale for this reserve margin, and natural gas supply plans for various weather conditions.

Staff has the following comments and concerns regarding the Company's reliability information:

1. Reserve Margin

The reserve margin for early to mid-winter is high, but as storage is drawn down, the Laclede withdrawal capacity decreases and, thus, the reserve margin decreases. Staff disagrees with the pipeline capacity value (MMBtu/day value) used by Laclede in the reserve margin calculation and uses a higher pipeline capacity figure/number. Laclede asserts that excess reserve is needed because of potential failure of a component in the propane facilities, but the deliverability calculated for these facilities already is reduced for startup problems and/or operational inefficiencies. However, even with the revision in pipeline capacity, the late winter reserve margin estimate is reasonable at this time.

2. Pipeline Capacity – Upstream

To support the quantity of upstream pipeline capacity needed, Laclede states that it considers: 1) geographic diversity of supply, 2) the availability of the firm flexible type supplies that it requires in its gas supply portfolio, 3) cost of supply in comparison to other options the Company may have from time to time, 4) access to supplies during late cold peak days when Mississippi River Transport (MRT) storage and on-system peak shaving resources are limited, and 5) transport availability in the long term (Data Request No. 107-HC).

Laclede states that certain supply areas are dominated by producers that only offer baseload-type services so it has to be careful not to rely too heavily on these areas when structuring its portfolio (Data Request No. 107-HC). Such a review should include a summary of the upstream pipelines that can provide the transportation for the firm flexible type supplies desired by Laclede, with a breakout for both the summer and winter months. However, Laclede provided no details to support which supply areas are dominated by producers with baseload only service.

Laclede indicates that it must consider how the supply basis varies in summer versus winter and where physical supply is needed to meet winter peak needs. It must also consider where supply is needed to fill MRT's storage in the summer months. The Company states that physical constraints require it to take large quantities of supply in certain areas of its system in the winter months but will only allow small quantities to be taken in the summer months when system requirements are low. Laclede further states that during the summer months, the Company needs large quantities in the field to maintain MRT storage injections. (Data Request No. 107-HC) However, Laclede provides no specific information explaining how the upstream pipelines were evaluated for 2003/2004 to assure that the stated conditions were met for the winter months and for the summer months with acceptable cost. For example, between 2002/2003 and 2003/2004 Laclede dropped its capacity subscription from 100,000 MMBtu/day to 80,000 on Natural Gas Pipeline Company of America (NGPL) and increased its capacity from 60,000 MMBtu/day to 80,000 on Trunkline while maintaining the same capacity on Center Point Energy and Gulf South. Laclede provided no analysis supporting these changes.

Laclede states that it is the most vulnerable to daily peak sendout situations late in the winter season when on-system peak shaving resources and Laclede's storage in MRT's Unionville storage site are potentially depleted. Laclede asserts that it must have access to flowing supplies on upstream pipelines given the limited amount of supply that is directly connected to the MRT system. Laclede provides an Excel worksheet to support these statements (Data Request No. 107-HC), but the worksheet does not explain what gas can be sourced on MRT or on each of the upstream pipelines in this late winter analysis. Nor does the worksheet explain why Laclede split the upstream capacity among the various pipelines for the 2003/2004 ACA period. The lack of information raises the question of how Laclede evaluated the cost of sourcing the supply on each pipeline. The lack of information makes evaluation of the Company's prudence much more difficult.

Staff recommends that Laclede provide more details of its analysis for subsequent ACA reviews to address these issues and that this information for 2004/2005 and 2005/2006 be submitted no later than June 1, 2006. If Laclede does not have such an analysis for the 2004/2005 or 2005/2006 ACA periods, Staff recommends that the Commission order Laclede to provide, no later than June 1, 2006, a more detailed analysis prior to the 2006/2007 ACA period.

3. School Aggregation

Laclede excludes basic transportation and interruptible customer requirements in its peak day estimate because there is no obligation to provide back-up gas supplies for these customers. However, Laclede includes requirements for School Aggregation Service, a service similar to basic transportation, in both its pipeline capacity and peak day requirements, even though schools obtain capacity through Laclede capacity release and are responsible for their own supply. Capacity release for the school aggregation program is 19.01 MMcf/day (19.39 BBtu) for November through March and 8.45 MMcf/day (8.62 BBtu/day) for April through October. Laclede has developed estimated requirements for schools for each month of November through May. Using these Laclede factors and an expected historical peak cold day of minus eight degree Fahrenheit, estimated peak day usage for these schools is 23.2 MMcf. Released capacity only covers 81.9% of school peak day needs and schools are only paying for this level of capacity for five months of the year. The remaining seven months of the year, schools are paying for capacity equal to 36.4% of peak day needs. The downstream capacity (MRT, Southern Star, and Panhandle/ Missouri Pipeline Company) for firm customers (mainly residential and small commercial customers) is paid for 12 months a year. Thus, these firm customers (mainly residential and small commercial customers) are carrying the extra load for schools for all the months that schools are not covered for peak day capacity.

Supply nominated by the schools participating in the school aggregation program, versus the actual usage is shown below. In three of the six months where data was provided, the school nomination and the actual usage were more than 20% different.

Laclede School Aggregation Information	Nominations (therms)	Actual Usage (therms)	Nominations as % of Actuals
Nov-03	1,563,031	788,196	198%
Dec-03	2,797,804	2,315,868	121%
Jan-04	3,537,988	3,036,658	117%
Feb-04	3,027,811	3,436,059	88%
Mar-04	1,843,900	1,853,232	99%
Apr-04	775,840	997,455	78%
May-04	-		
Total	13,546,374	12,427,469	109%

4. Data for Volumes for Interruptible Customers

Although Laclede excludes volumes for interruptible customers from the peak day estimate, it uses estimated values, not actual values. In the 2002/2003 ACA review, Case No. GR-2003-0224, Staff commented on this lack of verification. Staff recommended that for subsequent ACA periods, the 2003/2004 ACA and forward, Laclede submit interruptible customer daily volumes for the winter months of December through February. Although Laclede responded that the interruptible customers account for deminimus amounts of the total purchases, it agreed to obtain the daily usage data for these customers for any periods of sustained cold weather in 2004/2005. Staff will review this information in the 2004/2005 ACA. If Laclede does not provide the data because there were no periods of sustained cold weather in 2004/2005, Staff recommends that Laclede submit, no later than June 1, 2006, this information for 2005/2006.

5. ** **

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6. **Targets for Physical Supply**

The Company's reliability report does not contain targets for actually acquiring physical supply. Having major portions of the physical supply not under contract until near the start of the heating season may pose a reliability issue. The reliability report should specify target dates for acquiring physical supply with consideration given to contracting for this supply earlier than just prior to the heating season.

GAS SUPPLY ANALYSIS

Based on its review of Laclede's gas purchasing practices Staff proposes adjustments reducing Laclede's cost of gas for Laclede's decisions regarding contracted volumes of ** ______________ **

1. ** ______________ **

** ______________ **

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Staff's review reveals a large difference in Laclede's baseload contracts for 2003/2004 compared to the prior ACA of 2002/2003.

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As shown below, Laclede did not follow its study when setting the baseload volumes for November through April and its baseload volumes for May through September are not consistent with the RFP.

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Laclede's decision to baseload less volumes of natural gas than called for in its study resulted in additional costs to its customers of $2,329,295. Staff recommends that these costs be disallowed for the 2003/2004 ACA period.

2. Swing Supply Demand Charges

Natural gas supply contracts may include a demand charge for the amount of gas a local distribution company (LDC) can nominate on any given day. Usually, baseload contracts have no demand charge or a relatively small demand charge, while swing contracts generally have the highest demand charges. ** ______________________________ ______________________________ **.

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** When added to the earlier adjustment of $2,329,295, the total adjustment is $3,322,773.

3. Cost/Benefit Analysis for Producer Demand Charges

Given the level of demand charges, ** **

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- **
- It should isolate and separately identify "off-system sales" so that costs and benefits related to on-system customers can be separately identified.

The Company should also, maintain, and make available for review, in electronically readable format, all workpapers that support the study. These workpapers should maintain full functionality with readable cell formulas, macros, or other program add-ins that were used in the spreadsheet calculations. Finally, the study should be a before-the-fact study that is completed in time to help the Company assess the cost/benefits of ** **

HEDGING

The Staff reviewed the Company's Risk Management Strategy and its hedging transactions applicable to the 2003-2004 ACA period. Weather during the winter period was warmer than normal. Laclede's hedged coverage comes from financial instruments and from storage withdrawals. The Staff also reviewed monthly hedged coverage.

1. Hedging Documentation

The Company provided a copy of its risk management strategy along with documentation of its hedging transactions. However, the Staff did not find sufficient details regarding the rationale for each of its hedging transactions. For example, the Company evaluation of the market conditions that either support initiating the hedge or liquidating the hedge position. Several other examples illustrate a lack of sufficient hedge documentation detail. **

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____________________ ** Since the Company tariffs allow the pass-through of prudently incurred hedging costs, Laclede should be obligated to provide justification and support for the reasonableness of those hedging expenditures. Therefore, the Staff recommends that for the 2004-2005 ACA period forward, the Company provide, for each hedging transaction executed, its rationale supporting its decision and a brief narrative of the interplay between the hedging purchase or liquidation and the Risk Management Strategy. This should include all reports that tie the Company's actual hedge results to the targets stated in the Company's risk management strategy and a specific identification of instruments that are used in conjunction to create a particular hedge strategy. The Staff further recommends this documentation should be maintained and be made available to the Staff during each ACA review.

2. Hedge Effectiveness Testing

Based upon the information provided by the Company, it appears that Laclede does not test the hedge effectiveness of its financial instruments, although it does so for its marketing subsidiary, LER. Without measuring hedge effectiveness (required when the Financial Accounting Standards Boards Statement 133(SFAS) is applicable), there is a risk that the hedges that are established do not effectively protect the physical supply risk that is being hedged. ** ______________________________

______________________________ ** The Staff recommends that the Commission order the Company to test and document the effectiveness of its hedges in a manner consistent with the guidelines contained in the SFAS 133.

RECOMMENDATIONS

It is Staff's opinion that Laclede should do the following:

1. Establish the following account balances in its next ACA filing to reflect the (over)/under recovery of ACA and Refund balances to be (refunded)/collected from the ratepayers as of September 30, 2004:

   a. If the Company accepts the Staff recommendation for contracted volumes of ** ______________________ ** and the Staff recommendation for swing supply demand charges:

	Firm Sales non-LVTSS	Firm Sales LVTSS	Interruptible Sales	LP Sales	Firm Transportation	Vehicular Fuel	Refund
Beginning ACA Balance	$ 18,661,505	$1,032,722	$ (3,604)	$ 118,000	$ 464,331	$ 18,752	$ 348,488
Staff Adjustments:							
** ____ ____ **	$ (2,323,370)	$(5,925)					
Swing Supply Demand Charges	$ (990,951)	$ (2,527)					
Ending ACA Balance	**$ 15,347,184**	**$1,024,270**	**$ (3,604)**	**$ 118,000**	**$ 464,331**	**$ 18,752**	**$ 348,488**

b. If the Company rejects the Staff recommendation for contracted volumes of ** ____ ** and accepts the Staff recommendation for swing supply demand charges:

	Firm Sales non-LVTSS	Firm Sales LVTSS	Interruptible Sales	LP Sales	Firm Transportation	Vehicular Fuel	Refund
Beginning ACA Balance	$ 18,661,505	$1,032,722	$ (3,604)	118,000	$ 464,331	$ 18,752	$348,488
Staff Adjustments:							
** ____ ____ **	$ -	$ -					
Swing Supply Demand Charges	$ (2,417,854)	$ (6,166)					
Ending ACA Balance	**$ 16,243,651**	**$1,026,556**	**$ (3,604)**	**$118,000**	**$ 464,331**	**$ 18,752**	**$348,488**

2. Respond within thirty days to the school aggregation comments made by Staff in the Reliability Analysis Section.

3. Address the concerns in the Reliability Summary Section regarding support for the upstream pipeline capacity, data for volumes for interruptible customers, ** ____ ** and targets for physical supply. Submit information addressing these concerns by June 1, 2006.

4. Adjust the ACA balance by $2,329,295 for Laclede's decisions related to ** ____ **

5. Adjust the ACA balance for Laclede's decisions to price its swing contract supplies with ** ____ **

a. If the Company accepts the Staff recommendation for contracted volumes of ** ____ ** (recommendation number 4 above),adjust the ACA balance by an additional $993,478 for Laclede's decision to price its ** ____ **

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b. If the Company rejects the Staff recommendation for contracted volumes of ** ______________________________ ** (recommendation number 4 above) and accepts the Staff recommendation for ** ________________________ **, adjust the ACA balance by $2,424,020.

6. Provide a cost/benefit analysis for producer demand charges as recommended in item number three of the Gas Supply Analysis section of this recommendation. Provide an analysis for the 2006/2007 year to Staff by June 1, 2006.

7. Document and make available to the Staff, for each hedging transaction executed, the following information for the 2004-2005 ACA period forward:

a. For each hedging transaction executed, Laclede's rationale supporting its decision at the time of the transaction and a brief narrative of the interplay between the hedging purchase ** ___________ ** and the Risk Management Strategy. This should include all reports that tie the Company's actual hedge results to the targets stated in the Company's risk management strategy and a specific identification of instruments that are used in conjunction to create a particular hedge strategy.

b. Laclede's evaluation of the market conditions that either support initiating the hedge ** ___________ ** the hedge position.

c. ** ____ **

d. ** ____ **

e. A report of how much of the Company's monthly hedge targets ** ______________________ ** are actually achieved for that month and cumulatively.

For the 2004-2005 ACA, provide this documentation to Staff by June 1, 2006.

8. Test and document the effectiveness of its hedges in a manner consistent with the guidelines contained in the Statement of Financial Accounting Standard (SFAS) 133. For the 2004-2005 ACA, provide this to Staff by June 1, 2006.

9. Respond to the recommendations herein within 30 days.

SCHEDULE 3

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SCHEDULE 4

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SCHEDULE 5

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SCHEDULE 6

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