

Exhibit No.:
Issues: *Tariff Proposal*
ACA Process
Witness: *David M. Sommerer*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Rebuttal Testimony*
Case No.: *GT-2009-0026*
Date Testimony Prepared: *October 24, 2008*

MISSOURI PUBLIC SERVICE COMMISSION
UTILITY SERVICES DIVISION

REBUTTAL TESTIMONY

OF

DAVID M. SOMMERER

LACLEDE GAS COMPANY

CASE NO. GT-2009-0026

Jefferson City, Missouri
October 2008

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1 A. From 1984 to 1990 I assisted with audits and examinations of the books and
2 records of public utilities operating within the state of Missouri. In 1988, the responsibility
3 for conducting the Actual Cost Adjustment (ACA) audits of natural gas utilities was given to
4 the Accounting Department (now referred to as the Auditing Department). I assumed
5 responsibility for planning and implementing these audits and trained available Staff on the
6 requirements and conduct of the audits. I participated in most of the ACA audits from early
7 1988 to early 1990. On November 1, 1990, I transferred to the Commission's Energy
8 Department. Until November of 1993, my duties consisted of reviews of various tariff
9 proposals by electric and gas utilities, Purchased Gas Adjustment (PGA) reviews, and tariff
10 reviews as part of a rate case. In November of 1993, I assumed my present duties of
11 managing a newly created department called the Procurement Analysis Department.
12 This Department was created to more fully address the emerging changes in the gas industry
13 especially as they impacted the utilities' recovery of gas costs. My duties have included
14 managing the five member staff, reviewing ACA audits and recommendations, participating
15 in the gas integrated resource planning project, serving on the gas project team, serving on
16 the natural gas commodity price task force, and participating in matters relating to natural gas
17 service in the state of Missouri. In July of 2006, the Federal Issues/Policy Analysis Section
18 was transferred to the Procurement Analysis Department. That group analyzes filings made
19 before the Federal Energy Regulatory Commission (FERC).

20 Q. Have you previously filed testimony before the Commission?

21 A. Yes, I have. The cases in which I previously have filed testimony are
22 included as Schedule 1 of my rebuttal testimony.

EXECUTIVE SUMMARY

Q. What is the purpose of your Rebuttal Testimony in this case, Case No. GT-2009-0026?

A. The purpose of my testimony in this case is to rebut the testimony of Laclede Gas Company (Laclede or Company) witnesses Glenn W. Buck and Michael T. Cline by addressing the inappropriateness of Laclede's proposal to recover bad debt write-offs through the Company's Purchased Gas Adjustment/Actual Cost Adjustment (PGA/ACA) mechanism.

I recommend denial of the proposed tariff change for several reasons including: the tariff language is vague, and moves away from a long-standing "as billed" approach to PGA costs and revenues. The provision will add to the complexity of the ACA audit, which is already weighed down with difficult discovery issues, and affiliated transaction concerns.

Q. How has bad debt expense been treated?

A. Traditionally, bad debt expense has been analyzed, and set in a general rate case and included in base rates. Laclede's bad debt expense was included in base rates in its last rate case, GR-2007-0208. Carving some arbitrary amount of uncollectible costs from base rates for purposes of further protecting the Company from risks associated with over/under recovery of non-gas costs outside a rate case is inappropriate.

TARIFF PROPOSAL

Q. Has the Company proposed tariff language to address their proposal?

A. Yes, here is an excerpt from the proposed tariffs.

3. The amount of gas cost revenues recovered each month for the sales classes shall be the product of the actual therm sales of each sales class and the gas cost revenue recovery

1 components for such sales class, minus the net write-offs
2 adjustment described below. Such revenue recovery
3 component shall be equal to the CPGA applicable to such sales
4 class.

5 4. The net write-offs adjustment shall be derived by
6 subtracting one-twelfth of the gas cost portion of the annual net
7 write-offs recovered through the Company's non-gas rates
8 from the gas cost portion of the Company's actual net write-
9 offs in each month. The gas cost portion of the Company's
10 annual net write-offs recovered through the Company's non-
11 gas rates shall be determined in the Company's most recent
12 general rate case. For purposes of application of this paragraph
13 after the resolution of Case No. GR-2007-0208 and after the
14 effective date of this tariff sheet, the gas cost portion of the
15 Company's annual net write-offs recovered through the
16 Company's non-gas rates shall be \$8,100,000. The gas cost
17 portion of the Company's actual net write-offs in each month
18 shall be determined by multiplying such net write-offs by the
19 percentage of gas cost revenues to total revenues for all sales
20 customers for the period to which the write-offs apply.

21 Q. In general, what do you believe the proposed language means?

22 A. My understanding is that it is meant to establish what the level of the "gas cost
23 portion" of net write-offs recovered through the Company's non-gas rates was in the last
24 ratecase. The tariff provision then compares that item to an item called the "gas cost" portion
25 of Company's actual net write-offs.

26 Q. Has the Company defined "net write-off"?

27 A. No. A general accounting definition might be "when an account is
28 determined to no longer be collectible, or the company has ceased collection efforts on the
29 account, it is "written-off". That means the "accounts receivable" balance of the customer's
30 account is reduced to zero. (Financial Accounting, Third Edition, Walter B. Meigs, 1979).
31 The term "net" is generally understood to mean net of recoveries. The term "recoveries"
32 generally refers to collection of an amount previously written-off. Obviously, the company
33 has some control over when it writes off an account, when it determines an account is

1 uncollectible, and when it ceases collection efforts. When the company receives money for
2 an account that previously was written- off, there is no separate accounting on how much of
3 the recovery relates to “gas costs” and how much relates to “nongas costs”.

4 The Company’s approach in its tariff proposal is to go behind a settled rate
5 case stipulation, attempt to measure some level of expense it believes was included in the
6 settled rates, further subdivide the expense into a “gas cost portion” and a nongas portion,
7 and then track that estimate against an “actual” “gas cost portion” of net write-off amount,
8 which itself is an estimate. This adjustment is then netted against billed revenues.
9 More estimating takes place when some sort of subjective guess occurs as the Company tries
10 to determine the relationship between a calculated gas cost percentage of total revenues
11 during some time period and apply that percentage to an actual level of write-off for “the
12 period to which such write-offs apply”. It should be no surprise that this convoluted proposal
13 seems difficult to follow. It allows the Company great discretion in the determination of
14 what the final numbers will be.

15 Q. Is there some ambiguity with regard to the matching of a particular gas cost
16 percentage to actual write-offs for the period to which such write-offs apply?

17 A. Yes. Assume that the Company has calculated the gas cost percentage as 75%
18 for a particular month. It proposes to apply that percentage to the actual write-offs in that
19 month. However, the write-offs in a particular month likely related to service 9 months
20 before they are written off, or perhaps 12 months before they are written off, or some
21 combination of historical time periods. The Company’s language appears to allow
22 the Company to determine what the appropriate gas cost percentage is for write-offs that
23 likely vary in terms of when the underlying service was provided. It is an exercise in futility

1 to track such a vast array of time periods, which explains why the Company is repeatedly
2 using gross estimates, and then deeming those estimates to be actual amounts under the sole
3 theory that it declares it to be so. The PGA process already reconciles actual gas costs to
4 actual billed PGA revenues. It has done so for many years. An adjustment away from this
5 procedure moves away from the long-standing goal of only passing through actual and
6 prudently incurred gas costs to something more expansive, less tangible.

7 **ACA PROCESS**

8 Q. Isn't the ACA process a way to ensure a more accurate actual recovery of bad
9 debt expense?

10 A. No. The ACA process is already cumbersome. The Company files no
11 testimony to support its gas costs. The Company is under no obligation to point out major
12 decisions that impact gas costs prior to, during, or subsequent to an ACA period.
13 Once the ACA filing is made and the cost is claimed, it is incumbent upon the Staff or Office
14 of the Public Counsel (OPC) to identify the decisions that may be unreasonable, and the
15 excessive costs that may have resulted from those unreasonable actions.

16 Q. Are there other reasons why the ACA process is the wrong place to analyze
17 and recover bad debt expense?

18 A. Yes, Laclede's ACA reviews have increasingly become more complicated as
19 its unregulated marketing affiliate, LER, expands its operations. As an excerpt from Laclede
20 Group's 10k, filed with the Securities and Exchange Commission, points out "...*Those types*
21 *of transactions include sales of natural gas from Laclede Gas to Laclede Energy Resources,*
22 *Inc. (LER), ..., sales of natural gas from LER to Laclede Gas, and sales of propane and*
23 *transportation services provided by Laclede Pipeline Company to Laclede Gas.*"

1 In Laclede's case, affiliate transactions have placed additional burdens on the effectiveness
2 of the ACA reviews, where the interests of the LDC and marketing affiliate are not
3 necessarily aligned.

4 Q. Are there other reasons why the ACA process is the wrong place to analyze
5 and recover bad debt expense?

6 A. Yes. The entire sphere of credit and collection policies, procedures, and
7 practices become germane to the ACA review with Laclede's proposal. Although the
8 Company's tariff proposal does not specifically contemplate a review of the prudence and
9 reasonableness of the Company's collections process, given that the proposed adjustment
10 would pass through increases in those costs, it will be necessary to review those aspects of
11 the Company's operations. It should be plain that such a review moves far beyond the
12 already difficult task of reviewing gas procurement decisions and moves into an entirely
13 unrelated aspect of the Company's operations, "credit and collections". Not only would
14 those aspects be subject to review, but the associated accounting for write-offs, recoveries,
15 estimations and assumptions underlying the adjustments in this tariff proposal, will have to
16 be reviewed **each** ACA period.

17 **MR. CLINE'S TESTIMONY**

18 Q. On page 4, line 3 of his direct testimony, Mr. Cline asks, "How much is built
19 into the Company's existing rates for the recovery of the gas cost portion of bad debts?"
20 Do you agree with his response?

21 A. No. Mr. Cline's response to this one question should be enough to reject
22 Laclede's proposal. His analysis is clearly making assumptions about the level of a single
23 expense in a settled rate case. The parties did not agree to exact levels of expenses, but made

1 their own judgments as to the reasonableness of the overall level of increase. His analysis
2 could be done for virtually any expense, but it is unlikely the parties to the stipulation would
3 agree to particular expense levels assumed to be in rates. Mr. Cline, in a matter of fact
4 manner implies that “gas cost portions” of expenses can be calculated by making a few
5 simplifying assumptions.

6 Q. Do you agree with Mr. Cline’s statement on page 6, line 6 of his direct
7 testimony where he says... “The Company should be entitled to be kept whole for all of the
8 gas costs it incurs, and customers should be entitled to pay only for gas costs that were
9 actually incurred, no more and no less.”?

10 A. No. The statement overlooks the principle that only prudently incurred gas
11 costs should be passed through. Furthermore, the idea of keeping Laclede whole could be
12 expanded to all other expenses, placing all risks on customers, and that is not the goal of
13 regulating a monopoly utility company. Given the uncertainty of what the gas portion of bad
14 debt expense from the last rate case really is, and the further uncertainty about how various
15 percentages will be applied to net write-offs, it is impossible to design a mechanism that will
16 keep either party whole.

17 **MR. BUCK’S TESTIMONY**

18 Q. Do you agree with Mr. Buck’s Direct Testimony where on page 6, line 21,
19 he says... “The cost of natural gas is highly volatile and effectively beyond the utility’s
20 control, as the Commission has acknowledged in the recent Empire and Aquila rate cases
21 where fuel adjustment clauses have been authorized.”?

22 A. No, not entirely. Although gas costs are certainly volatile, they are not
23 effectively beyond the company’s control. The Company has the ability to dispatch supplies

1 from cheaper sources, and has an incentive plan that was designed to reward that very
2 activity. Of even greater import is the responsibility of the Company to hedge gas costs, an
3 issue not raised by Mr. Buck or Mr. Cline. Hedging can limit the exposure to gas price
4 increases, and is an area Laclede has responsibility for. If there is a correlation between bad
5 debt expense and gas prices, as Laclede suggests, then the traditional treatment of bad debt
6 expense in a general rate case aligns the interests of the customers and the Company, by
7 making both averse to gas price increases.

8 Q. Does this conclude your rebuttal testimony?

9 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

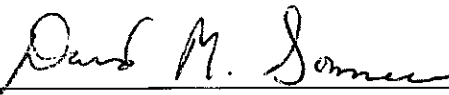
OF THE STATE OF MISSOURI

In the Matter of the Laclede Gas Company)
Tariff Filing to Recover Bad Debt Expenses) Case No. GT-2009-0026
Through the PGA and to Modify Cold Weather)
Rule Provisions.)

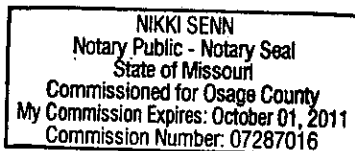
AFFIDAVIT OF DAVID M. SOMMERER


STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

David M. Sommerer, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Rebuttal Testimony in question and answer form, consisting of 9 pages to be presented in the above case; that the answers in the foregoing Rebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.


David M. Sommerer

Subscribed and sworn to before me this 23rd day of October, 2008.




Notary Public

CASES WHERE TESTIMONY WAS FILED**DAVID M. SOMMERER**

COMPANY	CASE NO.	ISSUES
Missouri Gas Utility	GR-2008-0060	Carrying Costs
Laclede Gas Company	GR-2007-0208	Gas Supply Incentive Plan, Off-system Sales, Capacity Release
Laclede Gas Company	GR-2005-0284	Off-System Sales/GSIP
Laclede Gas Company	GR-2004-0273	Demand Charges
AmerenUE	EO-2004-0108	Transfer of Gas Services
Aquila, Inc.	EF-2003-0465	PGA Process, Deferred Gas Cost
Missouri Gas Energy	GM-2003-0238	Pipeline Discounts, Gas Supply
Laclede Gas Company	GT-2003-0117	Low-Income Program
Laclede Gas Company	GR-2002-356	Inventory, Off-System Sales
Laclede Gas Company	GR-2001-629	Inventory, Off-System Sales
Laclede Gas Company	GR-2001-387	ACA Price Stabilization
Missouri Gas Energy	GR-2001-382	ACA Hedging/Capacity Release
Laclede Gas Company	GT-2001-329	Incentive Plan
Laclede Gas Company	GO-2000-394	Price Stabilization
Laclede Gas Company	GT-99-303	Incentive Plan
Laclede Gas Company	GC-99-121	Complaint PGA
Laclede Gas Company	GR-98-297	ACA Gas Cost
Laclede Gas Company	GO-98-484	Price Stabilization
Laclede Gas Company	GR-98-374	PGA Clause
Missouri Gas Energy	GC-98-335	Complaint Gas Costs
United Cities Gas Company	GO-97-410	PGA Clause
Missouri Gas Energy	GO-97-409	PGA Clause

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