

1 STATE OF MISSOURI  
2 PUBLIC SERVICE COMMISSION

3 HEARING  
4 September 15, 1999  
5 Jefferson City, Missouri  
6 Volume 3

7 In the Matter of 4 CSR 240-20.015 )Case No. EX-99-442  
8 Proposed Rule - Electric Utilities )  
9 Affiliate Transactions. )

10 In the Matter of 4 CSR 240-80.015 )Case No. HX-99-443  
11 Proposed Rule - Steam Heating )  
12 Utilities Affiliate Transactions. )

13 In the Matter of 4 CSR 240-40.015 )Case No. GX-99-444  
14 Proposed Rule - Gas Utilities )  
15 Affiliate Transactions. )

16 In the Matter of 4 CSR 240-4.016 )Case No. GX-99-445  
17 Proposed Rule - Gas Utilities, )  
18 Marketing Affiliate Transactions. )

19 BEFORE:

20 KEITH THORNBURG, Presiding,  
21 REGULATORY LAW JUDGE.  
22 CONNIE MURRAY,  
23 M. DIANNE DRAINER, Vice-Chair  
24 COMMISSIONERS.

25 REPORTED BY:

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1 P R O C E E D I N G S

2 JUDGE THORNBURG: We're going to go ahead  
3 and open the hearing today. Is there anyone that  
4 hasn't signed in yet that is a witness that is  
5 appearing here today or might appear?

6 Okay. My name is Keith Thornburg. I'm the  
7 regulatory law judge assigned to this rule making  
8 proceeding today. It's September 15, 1999 and we're  
9 convening a rulemaking hearing for proposed rules  
10 applicable to the gas utility industry.

11 The style of the proceeding -- we'll be  
12 handling two proposed rules today, and it's -- the  
13 style in the first case is in the matter of the  
14 Missouri Public Service Commission's proposed rule  
15 regarding affiliate transactions for gas utilities,  
16 Case No. GX-99-444, and the second proposed rule in  
17 the case is styled in the matter of the Missouri  
18 Public Service Commission's proposed rule regarding  
19 marketing affiliate transactions for gas utilities,  
20 Case No. GX-99-445. The proposed rule numbers are  
21 4CSR 240-40.015 and 4CSR 240-40.016.

22 I'd like to point out that this is a public  
23 hearing regarding proposed rulemakings. We are here  
24 today to take comments from the public regarding the  
25 proposed rules. Attorneys may appear today in a

1 representative capacity. If you are appearing as an  
2 attorney in a representative capacity, I will ask that  
3 you complete a written entry of appearance and that  
4 you also re-identify yourself and your clients on the  
5 record.

6           You will be allowed to make a brief opening  
7 statement if you desire, and then later in the hearing  
8 when we take comments, you'll be called on again if  
9 you have comments. And you may include in your  
10 comments facts, arguments or statements of issues that  
11 you'd like the Commission to consider.

12           I will if possible call on you in the  
13 same order as I call for opening statements. A  
14 Commissioner or I may question you. At the time you  
15 are called for comments you may present any witnesses  
16 that accompanied you today for the hearing.

17           Any person who wishes to appear and offer  
18 comments that is not acting as an attorney in a  
19 representative capacity will be sworn in, including  
20 attorneys that are appearing solely as a witness. If  
21 someone is here today and wishes to speak, he or she  
22 should sign the witness list. Because this is a  
23 rulemaking proceeding, objections to the testimony of  
24 the witnesses will not be ruled on or considered and  
25 the questioning will continue.

1           The order of opening statements and  
2 witnesses today will be proponents first and opponents  
3 second. I've prepared a list of participants, of  
4 proponents and opponents based on the preregistered  
5 participants. I'm going to work down that list first  
6 and then any persons registering today, I'll take  
7 them.

8           Some participants have indicated that they  
9 may request that their comments today be incorporated  
10 into the records for the utility industry affiliate  
11 transactions rules considered in Case No. EX-99-442 or  
12 the steam heating utility affiliate transactions rule  
13 considered in Case No. HX-99-443.

14           If that's the case, then the witness or  
15 attorney should indicate the cases where this is  
16 desired, and I'll instruct the court reporter to  
17 reproduce that testimony as an exhibit to the  
18 transcript for that respective rulemaking record.

19           It's my preference not to do this for  
20 opening statements unless that presents a hardship to  
21 one of the attorneys. If a witness has initially  
22 appeared and presented his comments and answered  
23 questions, it's possible that the Commission or I will  
24 ask questions of that witness later in the hearing.

25           Those comments won't automatically be

1 included into another record. Thus far, the comments  
2 of Robert Schallenberg, who testified on behalf of the  
3 Staff on Monday, September 13, 1999, have been added  
4 to the record transcripts for EX-99-442 and to today's  
5 proceedings in GX-99-444 and 445.

6 Mr. Schallenberg's comments are going to be  
7 labeled Exhibit B. The entire hearing transcript for  
8 Tuesday, September 14, 1999 in Case No. 99-442 will  
9 be made Exhibit A in the steam heating case HX-99-443,  
10 and it will also be the same Exhibit A in today's  
11 transcript for the hearing for GX-99-444 and  
12 GX-99-445.

13 If you later decide that you have hearing  
14 comments or opening statements in today's record that  
15 have not been incorporated into the record and you  
16 want them considered in another record later, you may  
17 make a written request to the Commission. You can  
18 identify that testimony and comments by the page and  
19 line number in the transcript, or if the material is  
20 not lengthy, you can quote it and just submit that  
21 request and we'll consider that.

22 At this time I'd like to call for  
23 on-the-record entries of appearance for the attorneys  
24 that are here today. You need only state your name  
25 and the clients that you are representing.

1                   For the Staff?

2                   MS. SHEMWELL: Lera Shemwell, representing  
3                   the Staff of the Missouri Public Service Commission.

4                   JUDGE THORNBURG: Thank you.  
5                   Office of Public Counsel?

6                   MR. MICHEEL: John B. Coffman and Douglas E.  
7                   Micheel appearing on behalf of the Office of the  
8                   Public Counsel and the public.

9                   JUDGE THORNBURG: Thank you.  
10                  Is there a representative from Mountain  
11                  Energy today?

12                  MR. SCOTT: Yes, your Honor. Victor Scott  
13                  from the law firm of Andereck, Evans, Milne, Peace and  
14                  Baumhoer here.

15                  Real quickly, your Honor, my client will be  
16                  making the statements again -- I apologize for this.  
17                  I request to be excused as I have other obligations  
18                  besides this hearing and since Mr. Barron will be  
19                  making the statement, I would like to be excused.

20                  JUDGE THORNBURG: Okay. We will be taking  
21                  opening statements when we open. If you can't remain,  
22                  that will be fine. I will take your witness.

23                  MR. SCOTT: I can make that statement, your  
24                  Honor.

25                  JUDGE THORNBURG: And do we have a

1 representative today for Enron?

2 (No response.)

3 JUDGE THORNBURG: Okay.

4 Any other proponent attorneys?

5 (No response.)

6 JUDGE THORNBURG: On the opponent's side is  
7 there a representative for AmerenUE today?

8 MR. NIEHOFF: William Niehoff for Ameren  
9 Corporation/Union Electric Company.

10 JUDGE THORNBURG: Thank you.

11 MGE?

12 MR. HACK: Robert Hack on behalf of Missouri  
13 Gas Energy.

14 JUDGE THORNBURG: Laclede Gas?

15 MR. PENDERGAST: Michael C. Pendergast on  
16 behalf of Laclede Gas Company.

17 JUDGE THORNBURG: Mr. Fischer?

18 MR. FISCHER: James M. Fischer on behalf of  
19 United Cities Gas, Greeley Gas Company, both divisions  
20 of Atmos Energy Corporation and Fidelity Natural Gas  
21 Inc. and Southern Missouri Gas Company, LP.

22 JUDGE THORNBURG: Okay.

23 Are there any opposing attorneys?

24 Yes, Mr. Cooper.

25 MR. COOPER: Dean Cooper on behalf of

1 Associated Natural Gas, Utilicorp United Inc., doing  
2 business as Missouri Public Service and St. Joseph  
3 Light and Power.

4 JUDGE THORNBURG: Thank you.  
5 Questions?

6 MR. PENDERGAST: Well, your Honor, I'd  
7 just -- if this is the appropriate time to dispense  
8 with it, you've had a number of objections noted over  
9 the last couple of days regarding the swearing in of  
10 witnesses, and I recognize that you're not going to  
11 rule upon those, but just so that we do it for this  
12 proceeding as well, I'd like to renew that objection  
13 on behalf of a number of the utilities here so that  
14 that will be a part of the record.

15 JUDGE THORNBURG: On behalf of your client?

16 MR. PENDERGAST: Well, certainly on behalf  
17 of our client.

18 JUDGE THORNBURG: Okay. And those similar  
19 objections were made in the hearing yesterday, and  
20 that record is going to be incorporated into this one.  
21 I will note that I didn't have the rule number  
22 yesterday. I may not still have it.

23 I believe it's 4 CSR 240-2.180(7) -- I  
24 didn't copy the whole thing. But it does provide that  
25 in rulemaking hearings persons testifying will be



1 sworn. And that's a rule that has been in effect a  
2 number of years.

3 And in unrelated proceedings the Commission  
4 is considering its procedural rule including this one.  
5 So if any attorneys here today want to offer comments  
6 in another proceeding considering the rulemaking rule,  
7 those will be welcome, and we'd be happy to consider  
8 those in that context also.

9 If there aren't any other questions, we'll  
10 take a short recess until 10:25 and I'll return with  
11 the Commission.

12 Thank you.

13 (A RECESS WAS TAKEN.)

14 JUDGE THORNBURG: Go back on the record now.

15 And this is -- the hearing has combined the  
16 two gas proposed rulemakings, gas affiliate and gas  
17 marketing, and at this time we'll take brief opening  
18 statements. I will remind the attorneys that we'll  
19 come back for your second round of comments. So the  
20 openings hopefully will be brief.

21 Ms. Shemwell for Staff.

22 MS. SHEMWELL: Thank you, your Honor.

23 Good morning. May it please the Commission,  
24 you've seen quite a parade before you of bright,  
25 capable, well-respected professionals in the two days

1 before you and I expect the same to continue today.  
2 This is an indication of the importance of these rules  
3 to the utilities and to their customers.

4 Yesterday I directed the Commission's  
5 attention to the annual reports of Ameren in KCPL in  
6 which they discussed their growing affiliate  
7 operations. Today I would call the Commission's  
8 attention to the annual reports of some of the gas  
9 utilities, for many of them also discuss their growing  
10 unregulated businesses as an increasingly important  
11 part of their operations.

12 Regulation is the balancing of diverse  
13 interests, and that is what those appearing before you  
14 are asking you to do. Staff's proposed rule is a  
15 moderate, balanced approach that takes a middle ground  
16 and protects utility companies without being unduly  
17 burdensome upon the utilities. The Commission is not  
18 required by law to take the least restrictive approach  
19 to achieve its goals, but instead is charged with  
20 taking a reasonable approach when regulating the  
21 utilities.

22 Staff respectfully suggests that the  
23 proposed rule is a reasonable approach that is also  
24 very close to being the least restrictive rule, that  
25 balances the competing interests of the utilities and

1       their customers.

2               The issue between the Staff and the industry  
3       is whether or not the regulated utilities can transfer  
4       benefits, many of which have been achieved because of  
5       their monopoly status, to their affiliates for free or  
6       for less than full value.  If the answer to that  
7       question is yes, then the Commission should adopt one  
8       of the utility's proposed rules.  If the answer is no,  
9       that the utility should get value for the benefits  
10      that they have, then adopt Staff's rule.

11              The reason for Staff's rule and the need  
12      for the required record keeping is so that Staff can  
13      assure the Commission that such transfers are not  
14      occurring.  The rule is necessary to prevent such  
15      subsidization.

16              Thank you.

17              JUDGE THORNBURG:  Thank you.

18              Mr. Micheel?

19              MR. MICHEEL:  May it please the Commission,  
20      we're here today to take comments on two proposed  
21      rules.  The first rule is GX-99-444.  This rule is  
22      virtually identical to the proposed electric rule  
23      EX-99-442, and for the reasons given by Public Counsel  
24      in the proceeding yesterday, Public Counsel urges that  
25      the Commission adopt the rule GX-99-444 with

1 modifications proposed by Public Counsel's initial and  
2 reply comments.

3           However, I did want to comment specifically  
4 on GX-99-445. This rule pertains to the marketing  
5 affiliated transactions and contains a code of conduct  
6 for transactions between regulated local distribution  
7 companies and their marketing affiliates.

8           First, I think it's important to point out  
9 that all major local distribution companies currently  
10 operating in the State of Missouri have unregulated  
11 marketing affiliates. Utilicorp United, which does  
12 business in Missouri as Missouri Public Service, has  
13 Utilicorp Energy Solutions. Southern Union Company,  
14 which does business in the State of Missouri as  
15 Missouri Gas Energy, has Mercado, Inc. Ameren, the  
16 parent company of AmerenUE, has Ameren Energy and  
17 Laclede Gas Company has Laclede Energy Resources.

18           Public Counsel wishes to emphasize the  
19 importance of the nondiscrimination standards of  
20 conduct found in the proposed rules. Such standards  
21 would promote the development of a competitive gas  
22 marketplace and ensure nondiscrimination in services  
23 provided to the utilities' affiliates and any  
24 alternative gas marketers, including but not limited  
25 to cost allocations, cross-subsidization and

1 information sharing.

2 Comments have been filed by the opponents in  
3 numerous LDCs asserting that no, quote, real world,  
4 closed quote, evidence has been offered to demonstrate  
5 the need for such rules. Indeed, many commentators  
6 today may echo that claim. Such claims should not  
7 persuade the Commission that these rules are  
8 unnecessary.

9 Perhaps one commentator before the Federal  
10 Energy Regulatory Commission in Case No. RM87-5-000  
11 which was entitled notice of inquiry into alleged  
12 anti-competitive practices related to marketing  
13 affiliates of interstate pipelines said it best when  
14 he stated, we do not know to what extent, if any, the  
15 consumer has been exploited by pipelines as a result  
16 of the creation of affiliated marketers.

17 We do know, however, that the potential for  
18 such abuse exists and that serious allegations of such  
19 abuse have been made in a number of cases before the  
20 Federal Energy Regulatory Commission. It is the  
21 responsibility of the FERC to assure through  
22 regulation that the potential for abuse is not, in  
23 fact, realized.

24 That commentator was Kenneth J. Nysis  
25 (phonetic sp.), the current senior vice-president of

1       Laclede Gas Company. The FERC subsequently adopted  
2       standards for conduct for interstate pipelines with  
3       marketing affiliates.

4               In this proceeding, we do not know to what  
5       extent, if any, ratepayers have been harmed as a  
6       result of the affiliated gas marketers. We do know,  
7       however, that the potential for such abuse exists and  
8       that the Staff has made serious allegations of such  
9       abuse in cases before the Commission. It is the  
10      responsibility of the Commission to assure through  
11      regulation that the potential for such abuse is not,  
12      in fact, realized. That is what these rules would  
13      prevent.

14              Adopting these rules as modified by Public  
15      Counsel would be an appropriate course of action. We  
16      have one commentator today, Ryan Kind. I think you're  
17      all familiar with him and I would ask that his  
18      comments be incorporated into both the electric and  
19      steam dockets.

20              JUDGE THORNBURG: Thank you.

21              Are there any other proponent attorney's  
22      opening statements.

23              Mr. Scott?

24              MR. SCOTT: Thank you, your Honor. I'm  
25      Victor Scott with the law firm Andereck, Evans, Milne,

1 Peace and Baumhoer, and I'm here representing Mountain  
2 Energy, an independent gas marketer who supports the  
3 rule. As an independent gas marketer, they are in  
4 direct competition with some of the regulated entities  
5 who have market affiliates. And as such, I will be  
6 here today presenting Mr. Peter Barron who had filed  
7 comments and has participated in several of the rate  
8 cases before this Commission.

9 After the presentation of Mr. Barron and  
10 for cross-examination of the questions, at this time I  
11 would request that the Commission grant me leave to  
12 miss the remaining portions of today's hearing as I  
13 have other obligations to attend to.

14 JUDGE THORNBURG: Since Mr. Scott has been  
15 asked to be excused, are there any questions for him  
16 at this time?

17 Commissioner Drainer?

18 COMMISSIONER DRAINER: No.

19 JUDGE THORNBURG: Thank you.

20 MR. SCOTT: Thank you.

21 JUDGE THORNBURG: And you may be excused.

22 Any other proponent's attorneys?

23 Mr. Niehoff?

24 MR. NIEHOFF: Yes, sir. We don't have any  
25 additional statement to make. We have made statements

1 the last two days and we ask that those be considered.

2 Thank you.

3 JUDGE THORNBURG: Thank you.

4 Mr. Hack?

5 MR. HACK: Good morning. I will be very  
6 brief. For the record, I'd like to recite MGE's  
7 joining in the objection to the swearing of witnesses  
8 later on today. We don't have substantial additional  
9 comments to make. I would for the Commission's  
10 information let them know that Mercado is Spanish for  
11 the word "market." That's our marketing affiliate's  
12 name.

13 And we know Commissioner Drainer had some  
14 questions yesterday. We do not have another witness.  
15 So I'll try to address those questions to the extent I  
16 understand them if you would like.

17 COMMISSIONER DRAINER: I appreciate that.

18 MR. HACK: I regret to inform you that we  
19 did not provide an estimate of fiscal impact to the  
20 Staff in response to the two rules we're here  
21 discussing today. We don't have substantial quarrel  
22 with the fiscal estimates that they put together in  
23 the rule.

24 I would note, however, that there are  
25 impacts, cost impacts, on unregulated entities and



1 affiliated entities that are not included in those  
2 cost estimates and, you know, I think those need to be  
3 considered.

4 On the variance question, you know, I guess  
5 our primary point would be draft the rule well so you  
6 don't need a variance. To the extent that you want to  
7 permit variances, I think it's our position that it  
8 should be clearly authorized, whether it's partial,  
9 entire, blanket, however it might be characterized.

10 Other than that, I'd be happy to answer  
11 questions.

12 JUDGE THORNBURG: And will you be here later  
13 in the hearing?

14 MR. HACK: Yes, I will.

15 JUDGE THORNBURG: We'll come around for a  
16 second round of questions.

17 MR. HACK: Thank you.

18 COMMISSIONER DRAINER: Thank you.

19 JUDGE THORNBURG: Mr. Pendergast?

20 MR. PENDERGAST: Thank you. If it please  
21 the Commission, I'm Mike Pendergast on behalf of  
22 Laclede Gas Company. I, like Mr. Hack, would like to  
23 begin by responding to the questions that were asked  
24 by Commissioner Drainer yesterday, and in the interest  
25 of brevity, I think it might be helpful to distribute

1 the letter that we sent to the Staff last November on  
2 the subject of fiscal impact on Laclede, so that the  
3 Commission will go ahead and have a copy of that and  
4 it will save me from going over it again in detail, if  
5 that would be acceptable to your Honor.

6 JUDGE THORNBURG: You may approach and do  
7 so, if you would provide a copy to the court reporter  
8 also.

9 MR. PENDERGAST: As we indicated in the  
10 letter that you have before us, it simply was  
11 impossible for us at the time last November to provide  
12 a specific qualification of the rule's impact because  
13 of what we think is the ambiguity of the rule's  
14 various provisions and the uncertainty over how those  
15 provisions might be applied, a problem that I think  
16 Public Counsel has also noted in its remarks.

17 But if literally applied, we indicate in our  
18 letter and we maintain today that the proposed rules  
19 could potentially cost Laclede and its customers  
20 literally millions of dollars on added expenses for  
21 foregone revenues, and I think the most remarkable  
22 thing about that is, I don't believe that's a result  
23 that is intended by Public Counsel, Staff and  
24 certainly not by our Commission.

25 I think the real problem is that the

1 proposed rule, although it's called an affiliate  
2 transaction rule, actually purports to cover not only  
3 transactions between affiliates and their separate  
4 corporate -- or between utilities and their separate  
5 corporate affiliates, but also transactions between  
6 any unregulated business operations of the utility and  
7 its regulated business operations.

8           And to this day I still don't have a very  
9 good understanding of what an unregulated business  
10 operation means. I think it's important for the  
11 Commission to understand that every year both Laclede  
12 and the other utilities, I suspect, in this room  
13 engage in literally thousands of transactions that  
14 involve the transfer of goods and services that are  
15 unregulated by this Commission.

16           Just to give you a couple of examples,  
17 and we note them in the letter, vehicles wear out,  
18 equipment wears out, you sell them for scrap, you  
19 sell them to somebody else who doesn't mind having a  
20 10-year-old or a 15-year-old vehicle. That is a  
21 transfer of a good and service. The terms and prices  
22 of that aren't regulated by the Commission. The  
23 Commission doesn't tell us who we can sell it to and,  
24 nevertheless, those transactions are done.

25           We provide joint trenching services, or at  
19

1     least have in the past, for other utilities, where  
2     when we go out and we put in facilities, gas  
3     facilities, if there are compatible facilities from  
4     another company, generally telephone lines and that  
5     sort of thing, we work out arrangements where we'll  
6     bury them at the same time, saves the telephone  
7     company some money, because they pay us less than it  
8     would cost for them to go ahead and do the work, and  
9     it also saves us some money because we get a  
10    contribution to the cost of putting in those  
11    facilities.

12               We -- and in the past -- and I'm sure other  
13    utilities have temporarily rented out unused office  
14    space -- we really substream capacity to third  
15    parties, and in all of these transactions, the price  
16    at which we do that isn't regulated by the Commission.  
17    The materials under which we do it isn't regulated by  
18    the Commission, although the Commission may have  
19    tariffs that determine how the revenues are ultimately  
20    allocated to our customers.

21               And I think it's just important for the  
22    Commission to understand that the revenues from all of  
23    these transactions are accounted for above the line.  
24    And in many instances, none of these transactions or a  
25    few of them involve affiliates. Sometimes they will

1 but most of the time they don't. They involve totally  
2 unrelated parties.

3 But because they're not regulated as to  
4 terms or price, is that an unregulated business  
5 operation that is intended to be covered by the rule?  
6 And if it is, it raises the question of whether or not  
7 we can make those kind of transactions under  
8 circumstances where the market value for that old  
9 vehicle may be below its fully distributed cost, where  
10 the capacity we're releasing may be below what we paid  
11 for, where the joint trenching fee that we collect may  
12 be below the fully distributed cost.

13 That may be all that the market's willing to  
14 pay but it's below the fully distributed cost.  
15 Nevertheless, all of these incremental revenues  
16 benefit our customers. And we don't think it makes  
17 sense under those circumstances, particularly since  
18 they're accounted for up the line, you have the full  
19 ability to go ahead and ask us any information you  
20 want about those transactions and you have the full  
21 ability to determine how you want to allocate those  
22 revenues to make them subject to this type of rule.

23 I know that there is a provision in  
24 the rule that permits a variance, but it just seems  
25 counter-intuitive and counter-productive that you

1     should have to go ahead and go through an elaborate  
2     variance procedure in order to do routine utility  
3     transactions that utilities have been doing for years,  
4     where there's never been any hint of somebody trying  
5     to hide revenues in some unregulated affiliate, and  
6     where the Commission has full access to any  
7     information that it needs to go ahead and make a  
8     determination of how those revenues should be treated.

9             Now we proposed a fix for that in the  
10    modified rule that we attached to our comments. That  
11    fix was to go ahead and basically say an unregulated  
12    service includes a service where the utility is  
13    booking revenues that are generated utilizing utility  
14    assets below the line.

15            In other words, in an instance where a  
16    utility is trying to say, these aren't regulated  
17    revenues, we're taking them below the line and  
18    potentially trying to take them beyond the  
19    Commission's jurisdiction. Under those circumstances  
20    it might be appropriate to go ahead and have some sort  
21    of requirement, but where it's above the line we don't  
22    think it is, and we think that it would be very  
23    helpful and avoid a lot of confusion, a lot of burden  
24    in the past to go ahead and give serious consideration  
25    to adopting that particular change.

1           With regard to the second question, as far  
2   as the variance is concerned, I think whatever rule  
3   you adopt, if, in fact, you do adopt a rule, you  
4   should have a variance provision included in it that  
5   allows you to go blanket variance or a variance from  
6   all or part of the rule's provisions.

7           Mr. Matthews will be testifying or at  
8   least providing comments later on about a real-life  
9   example of how the Commission can approve and  
10  implement alternative structures that I think gets at  
11  the heart of what this whole proceeding is about. And  
12  that's namely the concern that utilities have the  
13  obligation -- or have a profit motive to try and take  
14  revenues and put them in unregulated operations and  
15  benefit those unregulated operations or unregulated  
16  affiliates so that they will go ahead and increase the  
17  amount of financial benefit they get to the bottom  
18  line.

19          This Commission has recently adopted a set  
20  of plans for a number of LDCs in this state, and those  
21  incentive plans provide an opportunity for LDCs to go  
22  out, and in a way that makes the shareholder's  
23  interest consistent with the customer's interest, try  
24  and maximize the revenues or minimize the costs  
25  associated with their activity in a particular area.

1 And when you have that kind of mechanism in place, you  
2 have to ask yourself, is there any financial incentive  
3 anymore to try and benefit an unregulated provider of  
4 the same kind of service.

5 And I think Mr. Matthews will come up and  
6 show you a real-life example of why you don't need to  
7 have that concern. So having a variance provision to  
8 permit exceptions where you have those alternative  
9 mechanisms in place to us makes a lot of sense.

10 Finally I'd just like to note that as  
11 Mr. Micheel kindly shared with you, we don't minimize  
12 for a moment this Commission's legitimate interest  
13 in making sure that utilities do not take unfair  
14 advantage of their competitive relationships with  
15 affiliates, that they don't abuse those particular  
16 relationships in some way that would be detrimental to  
17 the customers.

18 We believe that ten years ago when we filed  
19 the comments that Mr. Micheel indicated and that  
20 Mr. Matthews will also address in his testimony, at  
21 the very time that FERC was opening up the wholesale  
22 market, interstate pipelines were taking on massive --  
23 well, they were implementing programs where they had  
24 marketing affiliates to sell gas.

25 We are certainly willing to go ahead and



1 recognize that reasonable rules can be put in place  
2 today. While we don't think that any evidence has  
3 been produced that would suggest that there is a  
4 problem it needs to be addressing, nonetheless, we  
5 have proposed a modified rule that does have  
6 reasonable restrictions included in them.

7 And I think it's really appropriate to  
8 take a look at what remedy you're pursuing in this  
9 case, because while it's true that you have legitimate  
10 interest in looking at this, it's equally true that  
11 whatever the scope of the remedy is, it ought to be  
12 proportionate to the scope of problem.

13 And to my knowledge, the only specific  
14 instance that has been raised over the last several  
15 years regarding affiliate abuses involving LDCs was in  
16 the MoPub ACA case, and in that case, you specifically  
17 looked at the evidence, you specifically looked at the  
18 allegations, there was cross-examination, there was a  
19 thorough illumination of the various contentions, and  
20 this Commission came forward and said that they found  
21 absolutely no evidence of an improper relationship  
22 going on there.

23 And I think, you know, if there was  
24 something improper going on there, when you have a  
25 company like Enron who was here yesterday that has

1 assets that are 30 times the assets and the revenues  
2 of every LDC in this room combined, if we were doing  
3 something funny out there or doing something  
4 inappropriate, believe me, they have the resources to  
5 come in and tell you that.

6 And I think that in the absence of people  
7 doing that, you have to take a hard look at how  
8 extensive and how much you think we need to change our  
9 business practice.

10 I appreciate that and we'll be happy to  
11 answer any questions you might have.

12 Thank you.

13 JUDGE THORNBURG: Mr. Pendergast, did you  
14 want this letter offered as an exhibit to the  
15 transcript?

16 MR. PENDERGAST: That would be fine, your  
17 Honor.

18 JUDGE THORNBURG: That will be the first  
19 numbered exhibit today. And the court reporter may  
20 require a couple more copies.

21 (EXHIBIT NO. 1 WAS MARKED FOR IDENTIFICATION  
22 BY THE COURT REPORTER.)

23 JUDGE THORNBURG: Mr. Fischer, did you have  
24 some brief opening remarks?

25 MR. FISCHER: Yes.

1 JUDGE THORNBURG: You may proceed.

2 MR. FISCHER: May it please the Commission,  
3 my name is Jim Fischer and I'm here today representing  
4 United Cities Company and Greeley Gas Company, which  
5 are both divisions of Atmos Energy Corporation located  
6 in Dallas, as well as Southern Missouri Gas Company  
7 and Fidelity Natural Gas Inc.

8 United Cities and Greeley both filed  
9 comments together, and so did Missouri Gas Company and  
10 Fidelity file separate joint comments to address the  
11 concerns of the rule, but these particular companies  
12 won't be presenting witnesses here today, but at an  
13 appropriate time I will have a few comments regarding  
14 the -- that will highlight their concerns about the  
15 rules.

16 Yesterday during the electric rulemaking  
17 Commissioner Drainer asked a couple of questions  
18 relating to the cost of implementation and whether the  
19 variances should be on a transaction-by-transaction  
20 basis or on a company-by-company basis, and I'd like  
21 to just briefly respond to those.

22 In the initial comments of Fidelity  
23 and Southern Missouri Gas Company, we proposed an  
24 automatic exemption for small LDCs with 10,000  
25 customers or less.

1           Fidelity has 900 customers and Southern  
2       Missouri Gas Company has approximately 5,500  
3       customers.

4           In addition, at Atmos Energy Corporation  
5       suggested an automatic variance or exemption for any  
6       transactions of multi-jurisdictional utilities that do  
7       not impact the Missouri operations. In other words,  
8       if Atmos is -- one of its affiliates is doing a  
9       transaction in Tennessee, it wouldn't be appropriate  
10      that we have to do all of the things under the rule if  
11      it doesn't have any impact under -- for Missouri.

12           We continue to believe that those would make  
13      sense and would be workable approaches. For a small  
14      LDC, for example, like Fidelity, it's not uncommon for  
15      the same personnel to work for both the regulated gas  
16      company and do limited amounts of marketing work for  
17      the marketing affiliates.

18           While they already allocate their time  
19      between the companies, it would be impractical to  
20      expect them, as the rule seems to suggest, to have,  
21      quote, no more access to employees of the regulated  
22      gas company than as provided to any unaffiliated  
23      entity.

24           It would also be difficult and otherwise  
25      impractical to physically separate all personnel who

1 are employed in the marketing affiliate of these small  
2 companies from those personnel employed in the  
3 regulated distribution company.

4 The enforcement of that kind of requirement  
5 for a small LDC may effectively amount to an outright  
6 prohibition from them getting into that market or at a  
7 minimum at least requiring them to hire additional  
8 personnel and separate them into a new office to do  
9 marketing functions. This regulation, therefore, for  
10 a small LDC could result in the loss of economies of  
11 scale that could benefit the gas corporation  
12 ratepayers. And I think if it's applied to small LDCs  
13 and their marketing affiliates, it could mean the  
14 ratepayers might be deprived of an economic supplier  
15 or a choice that they have today.

16 It's also unrealistic and unworkable to  
17 require a small LDC to make available general  
18 administrative services such as accounting, legal or  
19 human resources or other administrative services to  
20 outside entities merely because such services are  
21 available to their regular -- or to their affiliated  
22 marketing affiliate.

23 That's really doubtful in my opinion that  
24 they would -- that any outside entity would really  
25 want the human resources functions of these small

1 companies to be available to them if they're -- if  
2 they are competing with their marketing affiliate.

3 From a small LDC perspective it would appear  
4 that an exception from the various affiliated  
5 transactions and marketing rules would be appropriate  
6 and a practical approach for resolving the concerns of  
7 the small local distribution companies, and therefore  
8 I'd urge you to take a hard look at that -- that part  
9 of the comments of Fidelity and Southern Missouri Gas  
10 Company. In addition, the question about  
11 multi-jurisdictional utilities and transactions that  
12 don't impact Missouri should also be adopted.

13 Unfortunately, on the question of cost  
14 implementation, we were unable to really obtain very  
15 good estimates and we didn't file anything on the  
16 fiscal note. Obviously if a small LDC does have to  
17 hire a new guy to do the marketing and obtain office  
18 space somewhere else, that would add additional costs.

19 In addition, while the small LDC already  
20 allocates their costs, the creation of a elaborate  
21 cost allocation manual would certainly have a  
22 significant cost to that company as well. At an  
23 appropriate time I'll have some additional comments  
24 about the rule.

25 Thank you.

1 JUDGE THORNBURG: Thank you.

2 If you need to ask a question there,  
3 Commissioner Drainer.

4 COMMISSIONER DRAINER: If you don't mind, I  
5 would like to ask you one question.

6 You did not reference as some of the other  
7 companies have that you are opposed to the swearing in  
8 of witnesses.

9 MR. FISCHER: I haven't taken a position on  
10 that in the pleadings. I think there was a case some  
11 years ago that indicated under this particular statute  
12 it requires the taking of evidence, and that implies  
13 competence and substantial evidence that is subject to  
14 cross-examination, and I know the Public Counsel's  
15 Office has gone to court years ago and gotten that  
16 kind of a ruling from the court. But we didn't as a  
17 small company take a position on the swearing of  
18 testimony.

19 COMMISSIONER DRAINER: Okay. Thank you.

20 JUDGE THORNBURG: Mr. Cooper, did you have  
21 any comments or statements today?

22 MR. COOPER: Just very briefly, your Honor.

23 My name is Dean Cooper. I'm here today in  
24 opposition to the rule on behalf of Associated Natural  
25 Gas, Utilicorp United Inc. which does business as

1 Missouri Public Service, and St. Joseph Light and  
2 Power.

3 I'll make no opening statement at this time  
4 other than to refer you to our written comments that  
5 have been filed previously in these dockets and would  
6 state for the record that my clients do join in the  
7 objections to the form of the proceeding that have  
8 been previously stated here today, as well as in the  
9 electric and heat cases earlier this week.

10 That's all I have. Thank you.

11 JUDGE THORNBURG: Thank you.

12 Are there any other opponent attorneys for  
13 opening statements here today?

14 All right.

15 Ms. Shemwell, did you have a witness list to  
16 present today?

17 MS. SHEMWELL: We do. Thank you. Before we  
18 start with witnesses, just a small issue. Something  
19 I'd like to raise.

20 There has been some discussion of adopting  
21 other rules, perhaps SEC rules, and we believe that  
22 this Commission could not adopt those rules  
23 respectively or it would be an unlawful delegation of  
24 Commission authority. I have some case law on that.

25 I believe Ameren's proposed rule which has



1       been discussed a couple of times has some sentences in  
2       it that say that the SEC rules will be adopted  
3       respectively. We would encourage the Commission not  
4       to do that, and just to support that position, here is  
5       some case law, if I may offer that.

6               JUDGE THORNBURG: I'd really rather you read  
7       these citations than take this as an exhibit to -- and  
8       you're merely offering these to the Bench?

9               MS. SHEMWELL: Yes, in support of that.

10              JUDGE THORNBURG: Are some of these  
11       addressed in your written comments, the same  
12       authority?

13              MS. SHEMWELL: I don't believe so. There  
14       has been some discussion about the fiscal notes. And  
15       we would want to call Lena Mantle to the stand.

16              (EXHIBIT NO. 2 WAS MARKED FOR IDENTIFICATION  
17       BY THE COURT REPORTER.)

18              (Witness sworn.)

19              JUDGE THORNBURG: Thank you.

20              You might briefly introduce yourself, and I  
21       realize most of us know you, but start up with that  
22       and your prepared comments and we'll have questions to  
23       you.

24              MS. MANTLE: My name is Lena M. Mantle. I  
25       work for the Staff of the Public Service Commission.

1 And Commissioner Drainer had some questions on the  
2 fiscal notes that the Staff attached to the rules, and  
3 we wanted to give the Commissioners some background  
4 information on how we developed those costs.

5           You've heard from some of the utilities  
6 already. And basically I wanted to go over -- we  
7 sent out letters requesting estimates of fiscal  
8 impacts to the 3 steam utilities, the 5 electric  
9 utilities, and then also 12 gas utilities. So that's  
10 a total of 20 letters that we sent out asking for  
11 estimate of impacts. We got 12 replies: 1 from  
12 TriGen, Kansas City, the only steam company that  
13 replied, 4 electric companies did reply and then 7 gas  
14 companies.

15           Out of those 1 electric and 6 gas companies,  
16 said there would be an impact but they couldn't  
17 estimate how much and that it depended -- as you heard  
18 from Mr. Pendergast, that it depended on the rule that  
19 was adopted and it also depends on the number of  
20 transactions each utility does and also the number of  
21 affiliates. And we saw that too in the range of the 4  
22 responses that we did get. 3 gas utilities said it  
23 could be millions of dollars but couldn't narrow it  
24 down any more than that for us.

25           The range we got was from \$1,000 from

1 St. Joe Light and Power, and on the other extreme we  
2 had, as Mr. Niehoff said yesterday, we had 72 million.  
3 So we had quite a wide range. Of course, that 72  
4 million as he explained was estimating with structural  
5 and functional separation, of which we don't believe  
6 this rule as proposed requires. So we kind of had to  
7 throw that one out as not a real good estimate for us  
8 to work from.

9 So we had 4 responses out of the 20 that we  
10 felt we could work with. St. Joe sent in 2, 1 for the  
11 gas and 1 for electric, that said 1 to \$10,000 the  
12 first year, 3 to 5,000 ongoing, and that's reflected  
13 in the exhibit that Ryan Kind offered yesterday, that  
14 showed that St. Joe light and Power didn't do many  
15 affiliate transactions.

16 Empire District Electric Company sent us a  
17 response of \$100,000 the first year and then \$50,000  
18 each year after that.

19 TriGen Kansas City sent us an estimate of  
20 243,009 in year one and then \$183,457 on an ongoing  
21 basis. So we had a range, but then we had it from  
22 only 3 utilities, so that was a concern too.

23 Staff met, those of us working on the steam  
24 rule, the electric rule and the gas rule, and we  
25 discussed these responses. The ones that didn't reply

1 was as much a response as those that did, that they  
2 didn't take enough time to or didn't think the impact  
3 was great enough that they could shed some time  
4 writing us a letter.

5 We took that into consideration. We took  
6 into consideration what we thought the utilities  
7 should already be keeping, some of these should be  
8 being kept on an ongoing basis now.

9 We looked at how much personnel we thought  
10 it would take, programming, setting up new accounts,  
11 and from that we estimated the \$100,000 per utility  
12 for the first year and \$75,000 each year after that.

13 Staff will be glad to make you copies of  
14 these replies we got from utilities. You've already  
15 got the one from Laclede. But if the Commission would  
16 like to see those, we'd be glad to make those for you.

17 That concludes my comments.

18 JUDGE THORNBURG: Commissioner Drainer?

19 COMMISSIONER DRAINER: I have no questions,  
20 but thank you for your input.

21 JUDGE THORNBURG: Commissioner Murray?

22 COMMISSIONER MURRAY: I have no questions.

23 Thank you.

24 JUDGE THORNBURG: Thank you.

25 Ms. Shemwell, did you want this witness's

1 testimony preserved?

2 MS. SHEMWELL: We would appreciate that,  
3 your Honor.

4 JUDGE THORNBURG: If that gets expensive I  
5 may just incorporate this transcript today with the  
6 other records. In fact, if no one has any issue with  
7 that, we'll just do that and it will -- I think that  
8 will be easier for the court reporter.

9 I don't hear anybody expressing a problem  
10 with that, so we'll make today's record and we'll  
11 attach that the same as we did yesterday's record to  
12 the steam heating record.

13 Thank you.

14 MS. SHEMWELL: Thank you.

15 JUDGE THORNBURG: Did you have another  
16 witness today?

17 MS. SHEMWELL: Judge, we have Mr. Thomas  
18 Imhoff here. He doesn't have an opening statement but  
19 he could answer questions about what other states have  
20 done if the Commission or the Judge has questions.

21 JUDGE THORNBURG: Commissioner Drainer?

22 COMMISSIONER DRAINER: I have no questions.

23 JUDGE THORNBURG: Any questions,  
24 Commissioner Murray?

25 COMMISSIONER MURRAY: No questions.

1 JUDGE THORNBURG: We'll just note that Tom  
2 Imhoff was available today. I think we have the  
3 information that we need and the written comments.

4 MS. SHEMWELL: Okay.

5 JUDGE THORNBURG: Did you have any --

6 MS. SHEMWELL: Mr. Mike Wallace is also  
7 available to answer specific questions about the gas  
8 marketing rule, although he also has no opening  
9 comments.

10 JUDGE THORNBURG: Again, do we have any  
11 questions for Mr. Wallace today?

12 COMMISSIONER DRAINER: I have no questions.

13 JUDGE THORNBURG: Commissioner Murray?

14 COMMISSIONER MURRAY: I probably have one.

15 MS. SHEMWELL: We'll call Mr. Mike Wallace  
16 to the stand then.

17 JUDGE THORNBURG: Thank you.

18 Mr. Wallace?

19 (Witness sworn.)

20 MICHAEL J. WALLACE testified as follows:

21 JUDGE THORNBURG: You may briefly introduce  
22 yourself and then I believe we have some questions for  
23 you.

24 MR. WALLACE: My name is Michael J. Wallace.  
25 I work here at the Commission in the procurement

1 analysis department.

2 JUDGE THORNBURG: Commissioner Murray?

3 QUESTIONS BY COMMISSIONER MURRAY:

4 Q. Good morning, Mr. Wallace.

5 A. Good morning.

6 Q. I just wanted to know if you could explain  
7 why you think there is a need for marketing affiliate  
8 rules in addition -- why you think that the affiliate  
9 transaction rules would cover marketing affiliates as  
10 well.

11 A. Well, there's -- there's two sets of rules  
12 as you indicated, 240-40.015 and 240-40.016, and the  
13 only difference in the rules is the codes of conduct  
14 and some definitions. As to why there is two rules,  
15 that might be a question for Mr. Schallenberg as to  
16 why it was done that way.

17 But as far as why we need the codes of  
18 conduct, I think that that is necessary because we  
19 have a PGA process with gas that affiliate marketers  
20 are involved with those costs, and also, customers may  
21 be dealing with affiliate marketers at some point in  
22 the future, if we unbundle or something like, that to  
23 actually purchase their gas.

24 COMMISSIONER MURRAY: Okay. I believe  
25 that's all of the questions I have.

1 Thank you.

2 JUDGE THORNBURG: Thank you.

3 Ms. Shemwell, did you have any additional  
4 witnesses or comments at this time?

5 MS. SHEMWELL: We do not.

6 Thank you, your Honor.

7 JUDGE THORNBURG: Mr. Micheel?

8 MR. MICHEEL: Yes, your Honor. I just have  
9 some brief comments and then we'll present Mr. Kind.

10 I felt compelled to respond to  
11 Mr. Pendergast's parade of horrors as it related to  
12 selling automobiles and the unused office space and  
13 trenching, and just point out to the Commission some  
14 specific definitions that are contained in the rules  
15 that I think take care of those problems.

16 I think first of all, if you look at the  
17 definition under 1B under the definitional section of  
18 an affiliate transactions, it says the transactions  
19 between the regulated gas corporation and any  
20 affiliate. So to the extent that a gas utility is  
21 selling an automobile to a salvage company or renting  
22 unused space to someone that is not affiliated with  
23 the company, these rules do not apply. They'd only  
24 apply if it was -- if it was an affiliated transaction  
25 between the company.



1           The same would be with trenching. I  
2     think the example that Mr. Pendergast gave was they  
3     have some sort of joint trenching agreement with  
4     Southwestern Bell, and I don't think Laclede is a  
5     sub -- or Southwestern Bell is a sub of SBC Corp yet,  
6     but you never know the way the mergers are going.

7           I guess the other example he gave was the  
8     capacity release. I think that that issue -- I think  
9     it's fairly -- I think they probably do release some  
10    capacity to their affiliated marketer, and we all just  
11    have been through GT-99-303 and heard a lot of  
12    evidence there. But I think that the variance  
13    sections of the rule would take care of any problems  
14    that would arise there, and I'm specifically looking  
15    at subsection 2 of the variance rule that is under  
16    10A-2, that when it says, when to the best of its  
17    knowledge or belief compliance with the standards  
18    would not be in the best interests of regulated  
19    customers and complies with certain procedures.

20           The way capacity release is -- is dealt  
21    with, local distribution companies have to reserve  
22    enough capacity to meet severe weather or their  
23    largest peak day, and sometimes they don't have that  
24    particular peak day capacity as a sum cost. They've  
25    paid for that capacity upfront and the idea of

1 releasing the capacity is to get some value for that  
2 capacity.

3 I think that the variance procedures here  
4 set out specifically a way that that problem could be  
5 averted. I think the rules take care of that problem.  
6 And I also think that with respect to most LDCs, our  
7 good friends at Laclede in particular, that how  
8 capacity release is going to be treated is something  
9 that is already tariffed. It's a tariffed issue.

10 So I don't think that necessarily those  
11 parade of horrors are going to occur unless it's  
12 transactions with an affiliated company as defined by  
13 the rule. And I think if there are any problems, that  
14 the variance procedures can take care of those  
15 problems.

16 I present Mr. Kind at this point.

17 JUDGE THORNBURG: Commissioner Murray, did  
18 you have any questions to follow up on Mr. Micheel's  
19 statement?

20 COMMISSIONER MURRAY: I don't believe so.  
21 Thank you.

22 JUDGE THORNBURG: You may proceed with this  
23 witness.

24 (Witness sworn.)

25 RYAN KIND testified as follows:

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1 JUDGE THORNBURG: Please be seated.

2 You did introduce yourself briefly  
3 yesterday, but you might reintroduce yourself briefly  
4 today, and if you have prepared comments, we'll take  
5 those and we have some questions for you.

6 MR. KIND: Thank you. My name is Ryan Kind  
7 and I'm the chief energy economist at Missouri Office  
8 of Public Counsel. I have been involved in numerous  
9 cases involving gas utilities, which is, of course,  
10 the subject that we're on today.

11 I do have a little bit less to say than  
12 yesterday. I'm going to try not to re-cover the same  
13 ground, although I do want to probably return to one  
14 issue that was discussed yesterday to elaborate on it  
15 further.

16 First of all, the issue of the need for the  
17 rules, some Commissioners have expressed concern that,  
18 you know, why is there a need for the rules now, and I  
19 addressed that yesterday in both a general sense with  
20 respect to the entire energy industry, and  
21 specifically with respect to the electric industry,  
22 and I just wanted to provide a little bit of  
23 additional detail on that subject today with respect  
24 to the gas industry.

25 And I believe the situation is no different

1     for gas utilities than it is for electric utilities.  
2     There is a significant amount of diversification going  
3     on. I think this is probably pretty obvious in the  
4     case of our two large combined gas and electric  
5     utilities that we have in Missouri, those being  
6     Utilicorp United and Union Electric, both of which  
7     engage in a wide range of non-regulated activities.

8             I might add an increasingly wide range in  
9     recent years. As OPC noted in its initial comments in  
10    this docket, the most recent Laclede annual report  
11    states that, we will continue and expand efforts to  
12    sell not only gas appliances but energy-related  
13    services, some of which may involve unregulated  
14    operations.

15            The other large LDC on the other side of the  
16    State, MGE, which is a division of Southern Union, in  
17    Southern Union's 1997 annual report, they discuss  
18    seeking investment opportunities in cogeneration and  
19    pipeline transportation, as well as a discussion of  
20    expanding sales in nontraditional markets.

21            Now I want to talk a little bit about one of  
22    the specific provisions in the Commission's proposed  
23    gas marketing rule, that being the section on time  
24    which is Section 2K. Some utilities have opposed this  
25    provision on the grounds that it is duplicative of

1 Federal antitrust laws.

2 Public Counsel does not see a problem with  
3 this, even if there is some duplication, and we think  
4 that a similar prohibition administered by the  
5 Missouri Commission is advisable to ensure that  
6 Missourians that could be harmed by time arrangements  
7 do not need to resort to Federal litigation to address  
8 that problem and have it resolved. And, in fact,  
9 hopefully just having such a provision in the Missouri  
10 rule will prevent such activities from occurring in  
11 the first place.

12 I'd also note that some of the people who  
13 have commented on this proposed time provision have  
14 gone so far as to assert that offering discounts on  
15 bundles of services that include regulated monopoly  
16 services is somehow a legitimate trade practice, and I  
17 really never had heard this before.

18 I think I heard it in someone's comments  
19 yesterday. This makes absolutely no sense to me. And  
20 makes sense for the reason that only the regulated  
21 monopoly can provided regulated services, and if the  
22 regulated monopoly is then allowed to offer a bundle  
23 of regulated and nonregulated services at a discount  
24 price, it's obvious that it's using an unfair and  
25 unearned advantage to compete against others.

1                   Next I want to talk about some of the  
2           information that we've accumulated from discovery in  
3           this case, some specific information regarding gas  
4           utilities and I'm going to go over a summary similar  
5           to the one that I went through yesterday for electric  
6           utilities. And this summary contains a slightly fewer  
7           number of questions, and that's just because I did  
8           not -- just because of an oversight. I did not ask  
9           every single one of the same questions that I'd asked  
10          to electric utilities, to all of the gas utilities,  
11          and so I've only provided information here where I  
12          had information from all of the utilities.

13                   As you can see, there really is some pretty  
14       similar responses, a similar pattern to what we saw  
15       for the electric industry yesterday in terms of  
16       utilities making use of many of their monopoly assets  
17       in order to promote and further the profitability of  
18       their own regulated businesses.

19           And I just want to reiterate like I said  
20       yesterday, that this per se is not a bad thing. It's  
21       just a matter of when there is preference involved,  
22       and these assets are offered only to their unregulated  
23       affiliates, which I believe to be the case in  
24       Missouri.

25 And as you would note, that the monthly bill  
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1 is used by several utilities in Missouri to either  
2 bill for or promote their unregulated products,  
3 customer lists again have been made available to the  
4 unregulated affiliates of Missouri gas utilities, just  
5 as they have for many of our electric utilities.

6 And as the bottom line indicates, there is a  
7 significant number of affiliate transactions taking  
8 place at almost all of the four largest gas utilities  
9 in Missouri. You would note that I did not gather any  
10 other -- any information on gas utilities other than  
11 these four. There are, of course, additional gas  
12 utilities. I just -- it was a pretty -- a pretty  
13 large job just to gather this much information from  
14 this many utilities. So I sort of stopped at these  
15 four.

16 Just one last point to kind of follow up on  
17 one of the questions that Commissioner Murray had  
18 yesterday about the information that I'd presented on  
19 the electric sheet. Commissioner Murray asked me  
20 yesterday whether the responses on the electric  
21 summary that I presented, you were interested in  
22 seeing if in my opinion just by looking at that  
23 summary, I could say that something harmful was  
24 happening, something detrimental to consumers.

25 And I know I -- I think I felt like it

1 was -- it was really difficult for me to answer that  
2 question. I didn't want to state that, yeah, I  
3 definitely felt there was one, when I just hadn't  
4 really given it enough thought to feel like I was  
5 really firm in that being the appropriate response.  
6 But after further reflection, I think that that is the  
7 way I would answer that question today, that this  
8 information alone indicates that some harm has  
9 occurred. And I would like to explain why I believe  
10 that to be the case.

11 I believe that to be the case because as  
12 this information shows, certain valuable utility  
13 assets have been shared with or utilized for the  
14 benefits of affiliated entities. That's the  
15 information that I see revealed in these top five  
16 questions.

17 And I think it is fair to assume that  
18 without having an affiliate rule in place requiring  
19 that there be no preference in access to utility  
20 assets, that the same access just has not been  
21 provided to competitors of utilities' affiliated  
22 entities and, in fact, it seems to me that absent a  
23 rule, if utilities were to do -- do otherwise, in  
24 other words, if they were to provide access, that they  
25 would be ignoring their fiduciary responsibility to



1       their shareholders.

2               Sharing an advantage with their competitors  
3       would necessary -- it's not something that is going to  
4       be beneficial to their bottom line. And given that I  
5       believe this preferential treatment has occurred, I  
6       think the current and future nonregulated markets have  
7       not and will not operate in an optimally efficient  
8       manner and that outcomes from those markets for  
9       consumers in terms of the price and quality of  
10      products will be poorer than they would be if no  
11      preferential treatment had occurred.

12              And I think that this harm exists today even  
13      with no unbundling in the electric industry and with  
14      only partial unbundling in the gas industry. And I  
15      think this harm will only be magnified if further  
16      unbundling occurs in the gas industry for small  
17      customers.

18              And just one last explanation of that is  
19      that since unbundling of the gas commodity from the  
20      distribution service will probably, according to what  
21      most experts believe who I read in the trade press  
22      and inquiring to what I myself believe, unbundling of  
23      the gas commodities from distribution service will  
24      probably be followed by a rebundling that includes a  
25      package of formerly regulated -- of the formerly

1 regulated commodity with unregulated products. And  
2 the formal -- former monopoly provider of the gas  
3 monopoly is likely to have a competitive advantage in  
4 offering a rebundled package of services due to the  
5 activities that are shown on this data request only.

6 And that concludes my comments. I'd be glad  
7 to answer any questions you'd have today.

8 QUESTIONS BY COMMISSIONER MURRAY:

9 Q. It sounds like you're saying any competitive  
10 advantage is a detriment to the ratepayer.

11 A. No. I'm really not -- I'm not saying that.  
12 I'm saying any competitive advantage that has solely  
13 been gained as a by-product of the regulated utility  
14 service, because that's a competitive advantage that  
15 is not available to others, and if you're not going to  
16 have -- I don't believe you're going to have effective  
17 and sustained competition in that situation.

18 And, in fact, I think that that kind of  
19 situation could hinder competition from other  
20 developing as it would make others more reluctant to  
21 enter such a market.

22 Q. Do you think that it's possible that  
23 customers would like to receive services from their  
24 utility that they're accustomed to receiving service  
25 from, they trust, they've always had good service,

1     they're pleased with the rates, that they might like  
2     to know if their utility was able to offer them a  
3     bundle of other services and that they would be  
4     willing to have the utility be able to tell them that  
5     they're associated with another entity and to provide  
6     them a bundle of services?

7             Do you think it's possible that the  
8     customers might want that?

9             A.     I would acknowledge that it's a possibility,  
10    and I think that that is a probable benefit of that  
11    type of activity that would need to be balanced and  
12    weighed against the possible harm that consumers would  
13    receive.

14            Q.     And do you think that we should not -- we  
15    probably should not do something that would make it so  
16    difficult for the utility to provide those types of  
17    services to its customers that they just would refuse  
18    do it?

19            Would you agree with that?

20            A.     Well, I don't know what you mean as to what  
21    might cause the difficulty to be so great that they  
22    would refuse to do it. Because I know, for example,  
23    that I don't believe any of the provisions in OPC's  
24    rule would cause that to happen because there are  
25    similar provisions in place in other states.

1           Q.     Just answer the question without relating it  
2     to something.

3                     Just do you think that we should probably  
4     not try to -- not do something that would make it so  
5     difficult for the utility, either costly or burdensome  
6     with record keeping or something, that would actually  
7     prevent the utility from pursuing offering other  
8     services to its customers?

9           A.     Um, just assuming something means any  
10    possible range of things, of regulations that could  
11    be imposed, there is certainly some regulations  
12    that -- that should not be imposed for that reason  
13    that you mentioned.

14          Q.     I just have another question here about  
15    something you just said.

16                    On offering -- you said that I believe --  
17    and correct me if I misunderstood you -- but the  
18    offering discounts on regulated services that are tied  
19    to unregulated services, and I think you went ahead  
20    and said the reverse, offering discounts on  
21    unregulated services tied to regulated services would  
22    be --

23          A.     No, I really did not intend to state that  
24    and the rule doesn't -- I don't believe it restricts  
25    that.

1           Q.     Okay.  So you only are saying that when a  
2     discount is offered on a regulated service tied to an  
3     unregulated service, that that is improper?

4           A.     Correct, yes.

5           Q.     Okay.  I'm trying to think of a telephone  
6     industry at the time you were saying that and thinking  
7     about the fact that we see services that are offered  
8     that are discounted to -- that customers can receive  
9     rates based upon taking a package, like taking more  
10    than one service from a telephone provider and they  
11    can get a better rate than somebody that is only  
12    taking one service.

13                   Now you're not indicating that that type of  
14    thing is improper?

15           A.     Well, I think, for example, what you might  
16    be suggesting is that, for instance, I think perhaps  
17    South -- Southwestern Bell may have a policy where  
18    they would offer a discount on local service for  
19    taking some optional services.  And to me there is a  
20    big distinction between what -- and I don't think that  
21    there is -- you know, probably a big problem with  
22    that, given that I really have much more limited  
23    knowledge in the telephone industry admittedly than I  
24    do the energy industries.

25                   But the reason I would suggest that there

1 is probably not a problem with that is because as a  
2 result of the deregulation of the telephone industry,  
3 one of the parts of that deregulation is to ensure  
4 that competitors also can offer local service. It's  
5 no longer a monopoly service. And so at the point at  
6 which there is no longer a monopoly service and you're  
7 offering discounts, then that -- I don't think that  
8 would necessarily be a problem.

9 And the only clarification I would make is  
10 just even in the transition, though, from monopoly to  
11 a competitive service, at some point in that  
12 transition there may -- there may be some concern  
13 when -- even though it's not necessarily any longer a  
14 monopoly service, you still don't have -- you don't  
15 yet have effective competition in the form of monopoly  
16 service.

17 COMMISSIONER MURRAY: Okay.

18 I believe that's all of my questions. Thank  
19 you.

20 JUDGE THORNBURG: Commissioner Drainer?

21 COMMISSIONER DRAINER: No questions.

22 JUDGE THORNBURG: One question.

23 QUESTIONS BY JUDGE THORNBURG:

24 Q. Mr. Kind, in this chart of examples you  
25 have, for instance, the monthly utility bill to bill

1 for unregulated products or the monthly utility bill  
2 to promote unregulated products, is the issue you see  
3 with respect to the use of that technical and physical  
4 ability to generate these billings, or is it the  
5 customer data that is the issue?

6 A. I think it's a combination of both, and it's  
7 also just the -- it's not the technical -- it's partly  
8 the technical ability that just having a billing  
9 system that is -- that's capable of efficiently  
10 reaching every single customer in a geographic area,  
11 because you're sending a bill to 100 percent of the  
12 households, that -- that's part of the issue.

13 Q. Is it the billing system or the access to  
14 customer data?

15 A. Well, it's -- um, I don't know that that  
16 particular example is -- is so much in access to  
17 customer data, because the customer data there is just  
18 all of the addresses of all of the households in a  
19 certain geographic area. And really anybody can get  
20 that information, probably.

21 What is more of a concern with access to  
22 customer data is when you're talking about getting  
23 customer name, address, usage histories and credit  
24 histories. Those -- that kind of information combined  
25 can allow competitors to target certain market

1 segments that are most profitable and cherry-picked  
2 markets.

3 JUDGE THORNBURG: Okay. Thank you.

4 MR. KIND: You're welcome.

5 JUDGE THORNBURG: Mr. Micheel, do you have  
6 any other witnesses or comments to present?

7 MR. MICHEEL: No, not at this time, your  
8 Honor.

9 JUDGE THORNBURG: Would you like the  
10 one-page document that Mr. Kind referred to entered as  
11 an exhibit to the record?

12 MR. MICHEEL: If that's your preference, we  
13 can do that, your Honor.

14 JUDGE THORNBURG: All right. That will be  
15 more clear if we do that.

16 MR. MICHEEL: Okay. I provided three copies  
17 to the court reporter if that's what you want to do.

18 JUDGE THORNBURG: Next marked exhibit number  
19 for this transcript, probably No. 2.

20 THE COURT REPORTER: No. 3.

21 (EXHIBIT NO. 3 WAS MARKED FOR IDENTIFICATION  
22 BY THE COURT REPORTER.)

23 JUDGE THORNBURG: Mr. Scott, do you wish to  
24 present any comments or witnesses at this time?

25 MR. SCOTT: Yes, your Honor. I have Peter  
56

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1 Barron to present an opening statement.

2 JUDGE THORNBURG: Mr. Barron, if you'll come  
3 forward.

4 (Witness sworn.)

5 PETER BARRON testified as follows:

6 JUDGE THORNBURG: Please be seated. You  
7 might briefly introduce yourself and give your  
8 prepared comments and we may have some questions for  
9 you.

10 MR. BARRON: My name is Peter Barron. I'm  
11 director of business development and regulatory  
12 affairs for Mountain Energy Corporation. Thank you  
13 for the opportunity to address the Commission.

14 Yes, we feel that a rule is necessary.  
15 Almost every jurisdiction that we deal in, the  
16 marketing affiliates of the regulated LDC is the  
17 predominant marketer. First of all, I am a salesman.  
18 I am not an attorney. I'll leave the details and the  
19 legal precedents that will make up these rules to the  
20 attorneys.

21 As a salesman, I sell against market  
22 affiliates, and I know what market affiliates can and  
23 cannot do. Since 1986 Mountain Energy and its  
24 predecessor Mountain Iron have bucked the industry by  
25 not being affiliated with a producer, a pipeline or an

1 LDC.

2 Since 1986, our selling process has not  
3 changed. We identify the LDC with the transport  
4 opportunities. We prospect, cold call, many calls are  
5 required to make the proper contact with the decision  
6 maker. We get the volume requests signed by the end  
7 user. We get the LDC to reply to the request. We  
8 present to the end user.

9 We make -- I'm sorry -- we -- I can't read  
10 my notes. I'm sorry.

11 We gain the confidence of the end user in  
12 that Mountain Energy will provide a secure and  
13 reliable gas supply to the end user and we  
14 differentiate Mountain Energy from our competitors in  
15 getting the end users business.

16 By comparison, the market affiliate walks in  
17 to the end user, and the person doing this many times  
18 is the former salesman of the LDC. They walk in.  
19 They already have the information of the marketing of  
20 the -- I'm sorry -- of the end users use profile and  
21 they walk in and say, we are part of the LDC. We're  
22 the same company. They walk in. They hand -- the  
23 first thing they hand out is the LDC's annual report.

24 Many times this person already has the end  
25 users knowledge, friendship and confidence. They

1     already give -- immediately get the nod from the LDC.  
2     And many times those persons are who get the business.

3             I can remember one time back in 1997 before  
4     Williams opened up walking into Truman Medical Center,  
5     having a meeting on why they could not transport  
6     across then KPL. The representative of that -- of the  
7     LDC of KPL had a list in his possession of all of the  
8     large industrial customers in the Kansas City,  
9     Missouri area, including their annual usages and  
10    peak-day volumes.

11            Two months later when Williams did open up,  
12    and I believe that was in August of '88, they -- that  
13    person was transferred to the marketing affiliate. In  
14    gas selling you have to be the first one in the door  
15    in order to get the business. Gas selling, you have  
16    to be -- sell smart. You have to sell quickly and you  
17    have to gain the customer's confidence in your ability  
18    to supply their needs.

19            96 percent of the business stays with  
20    whoever that first person was in the door. If you get  
21    their business, you have a 96 percent chance of  
22    retaining that business year after year.

23            That means there is only a 4 percent chance  
24    of knocking off someone else. In several instances in  
25    the Kansas City area, there is the appearance that the

1 LDC gives preference to the marketing affiliate,  
2 especially in new connections, in new customers coming  
3 in.

4           Someone comes in and builds a new plant,  
5 they call the LDC, saying, we need to talk about  
6 connecting, you know, getting gas service into this  
7 plant. That person is very busy with all of the  
8 aspects of construction, getting equipment in,  
9 getting -- you know, hiring people to run that plant.  
10 Here comes the utility saying, you know, okay, we're  
11 going to put this line in. Oh, by the way, we can  
12 save you money on your natural gas.

13           By the time an outside affiliate or outside  
14 entity comes in trying to sell them, again,  
15 identifying the person who has the authority to make  
16 that decision, getting on their busy schedule and  
17 presenting, and then all of a sudden we find out,  
18 well, they're already with the marketing affiliate.

19           To see an example of this -- of the  
20 association between the marketing affiliates and the  
21 LDC, is go to any of the customer meetings that the  
22 LDC will host. Most of the time the LDC and the  
23 marketing affiliates -- I'm sorry -- the LDC personnel  
24 and the marketing affiliate people are all huddled  
25 together. They're -- whether they're talking socially

1 about their kids' baseball games or they're talking  
2 about business, they are after all one and the same  
3 company.

4 Last -- not last -- the market affiliate  
5 also benefits from the LDCs human resources services,  
6 health care contracts, computer systems and legal  
7 departments. Mountain Energy has to contract for all  
8 of these services individually out of our pocket.

9 If the market affiliate needs an attorney to  
10 review a contract, to enter into a transportation  
11 agreement, collect money, whatever the case may be,  
12 they have an entire legal staff available to them that  
13 makes -- that is already trained in the LDC's business  
14 and in the industry and is already paid by the  
15 ratepayers.

16 Mountain Energy in contrast has to get  
17 outside counsel, many times train them in the nuances  
18 of the business and then pay for them out of our  
19 pocket. If Mountain Energy needs computer systems or  
20 software, we have to, again, buy those out of our  
21 pocket. Many times those systems are already in place  
22 with the LDC.

23 Marketing affiliates also benefit from --  
24 I'm sorry -- from their LDC's health programs, their  
25 perks and options, none of which are available to an

1 outside firm.

2 Lastly, if Missouri wants to remain  
3 competitive with surrounding states, these rules which  
4 need to be moved forward in whatever form they take to  
5 ensure a competitive natural gas market for Missouri  
6 consumers.

7 Thank you.

8 JUDGE THORNBURG: Thank you.

9 Commissioner Drainer, any questions?

10 COMMISSIONER DRAINER: No questions.

11 Thank you for your comments.

12 JUDGE THORNBURG: Commissioner Murray?

13 COMMISSIONER MURRAY: I have none. Thank  
14 you.

15 JUDGE THORNBURG: Mr. Barron, thank you for  
16 being here today.

17 Are there any other proponent attorneys or  
18 commenters today?

19 Let's go off the record just a moment.

20 (Off the record.)

21 JUDGE THORNBURG: Mr. Niehoff, I'd like to  
22 give you another opportunity for comments or  
23 additional information you'd like to offer today.

24 MR. NIEHOFF: The only thing I have to offer  
25 today is a copy of our fiscal notes that we did submit

1 last November to the Commission. This has some  
2 testimony that we had submitted normally that I  
3 referenced yesterday, so I'd like to provide that to  
4 complete the record.

5 There are three of them there.

6 JUDGE THORNBURG: Mark these as the next  
7 numbered exhibit, No. 4.

8 (EXHIBIT NO. 4 WAS MARKED FOR IDENTIFICATION  
9 BY THE COURT REPORTER.)

10 JUDGE THORNBURG: Are there any questions  
11 for Mr. Niehoff?

12 Commissioner Drainer?

13 COMMISSIONER DRAINER: No. Thank you very  
14 much.

15 JUDGE THORNBURG: Commissioner Murray?

16 COMMISSIONER MURRAY: No, thank you.

17 JUDGE THORNBURG: Mr. Hack, did you have any  
18 statements or comments further to offer?

19 MR. HACK: No, thank you.

20 JUDGE THORNBURG: Any questions?

21 COMMISSIONER DRAINER: I just have a couple.

22 MR. HACK: Certainly.

23 COMMISSIONER DRAINER: Mr. Hack, from your  
24 comments that you filed, you had a proposed rule --  
25 oh, oh, I'm sorry. It was for the affiliate

1 transactions attached to your initial comments.

2 MR. HACK: Correct.

3 COMMISSIONER DRAINER: And I believe that  
4 would have been the same language that was proposed in  
5 Laclede's.

6 MR. HACK: Correct. And I believe maybe  
7 even some other companies also proposed.

8 COMMISSIONER DRAINER: And you think that --  
9 that should the Commission adopt your suggested  
10 proposed comment, that that would be adequate?

11 MR. HACK: Yes.

12 COMMISSIONER DRAINER: And there were no  
13 comments for the marketing affiliate transactions?

14 MR. HACK: Excuse me?

15 COMMISSIONER DRAINER: Well, I want to make  
16 sure I'm clear. I have your proposed comments for the  
17 affiliate transactions --

18 MR. HACK: Right.

19 COMMISSIONER DRAINER: -- which would have  
20 been 240.40.015, but I don't have any for 016, which  
21 is the marketing affiliates transactions.

22 MR. HACK: I think I understand the  
23 question.

24 COMMISSIONER DRAINER: Okay.

25 MR. HACK: One rule covers all activities.



1 And if you look at sub B on page 2 of the rule  
2 attached as Appendix A, that talks about specific  
3 nondiscrimination requirements applicable to natural  
4 gas marketing.

5 So our view is that affiliate transactions  
6 are affiliate transactions, and you can address the  
7 whole ball of wax in one rule and this rule does that.

8 COMMISSIONER DRAINER: That is what I wanted  
9 an answer to. You got it. Thank you very much.

10 MR. HACK: Okay.

11 JUDGE THORNBURG: Commissioner Murray?

12 COMMISSIONER MURRAY: No questions.

13 JUDGE THORNBURG: Thank you, Mr. Hack.

14 Mr. Pendergast, did you have any additional  
15 comments?

16 MR. PENDERGAST: Just a few, your Honor.  
17 Thank you.

18 JUDGE THORNBURG: You may come forward.

19 MR. PENDERGAST: I'd like to resist the  
20 temptation to get back in court here, but I do think a  
21 clarification is in order.

22 In response to my earlier comments, I think  
23 Mr. Micheel talked about the definitions in the rule  
24 and how those definitions in the rule seem to suggest  
25 that this only covers transactions between separate

1 entities.

2 My concern is that if you actually read the  
3 definitions, it says affiliated entity means any  
4 person, and then it goes on to list various kinds of  
5 persons that are covered by the rule. And I'm not at  
6 all clear that a person doesn't mean an actual  
7 employee of the utility as opposed to an actual  
8 separate legal entity. I don't think that's clear  
9 from the rule.

10 And secondly, in B, he did indicate that an  
11 affiliate transaction means any transaction between a  
12 regulated gas corporation and an affiliated entity,  
13 which once again could be a utility employee. But  
14 then it goes on to say, and shall include all  
15 transactions carried out between any unregulated  
16 business operation of a regulated gas corporation and  
17 the regulated business operation of a gas corporation.

18 That to me indicates that it's applicable to  
19 transactions regardless of whether there is a separate  
20 entity out there that is called an affiliate. I mean,  
21 they're talking about these transactions between, you  
22 know, the same -- within the same utility between a  
23 regulated and unregulated business operations. So,  
24 you know, I do think that ambiguity is in there and I  
25 do think that it stands to be addressed.

1           The only other comment I'd like to make, and  
2   I think perhaps there has been a little demonstration  
3   of why at times contested case procedures can be  
4   helpful, because, you know, we've had another exhibit  
5   filed today and we've had some additional readings of  
6   annual reports to indicate what the scope of  
7   unregulated activities may be by -- by utilities.

8           And I think it's important for the  
9   Commission to understand that at least when it comes  
10   to Laclede, only once in the last 5 years have the  
11   revenues we get from unregulated services exceeded 5  
12   percent. It didn't exceed 5 percent by very much and  
13   that wasn't in the last couple of years. The last  
14   couple of years it's been about 3 percent.

15          I think it's also important for the  
16   Commission to recognize is it talks about these  
17   marketing affiliates and how big they are and how many  
18   advantages they have.

19          LAR, our marketing affiliate, has one  
20   employee and he resides in a trailer somewhere in  
21   St. Louis County and I can't even tell you where that  
22   is, versus Enron that has \$30 billion worth of assets  
23   and, you know, to me it's akin to saying that we need  
24   to step in and protect a Wal-Mart so that it can  
25   compete with the local five and dime. I mean, you

1 know, it just does not bear a connection with reality  
2 when you say that there is a massive problem out there  
3 that needs to be addressed when you look at who the  
4 real players in this particular process are.

5 Finally, I think it has to be noted that on  
6 this handout -- and I don't question the accuracy of  
7 this handout at all that Mr. Ryan Kind provided -- but  
8 when we have these yes's down here on the side, all of  
9 those yes's, I believe, exclusively related to HVAC  
10 work, a business that my company has been in for more  
11 than four decades and probably longer than that, but  
12 that's the furthest that anybody can remember back.

13 That is something that we're entitled to be  
14 in that you've addressed with a separate rule, has  
15 been addressed with separate legislation and, yes, we  
16 do all of these things in connection with HVAC work.  
17 I think the answer would probably be no to every one  
18 of those except the last if we were talking about  
19 things that are actually addressed by this proposed  
20 rule which is not HVAC work.

21 And I think that if that is not being  
22 addressed by this rule, it's not entirely appropriate  
23 to go ahead and take what we do on the HVAC side into  
24 consideration, particularly when we're doing that in  
25 compliance with the law, and particularly when the

1 costs are being allocated properly for that.

2 I think it's also -- Commissioner Murray had  
3 asked a question about, well, maybe do consumers want  
4 us to do this? Well, we've been in the business for  
5 over four decades. I think that's a pretty good  
6 indication that they do.

7 I'd also note that when the HVAC legislation  
8 came up several years ago, the utilities -- and many  
9 utilities did it, so, you know, you need to look at it  
10 with that perspective, but we did a survey and we  
11 asked consumers across the State of Missouri whether  
12 they wanted us to be in that business, whether they  
13 wanted to have that choice, whether they wanted to  
14 offer that opportunity, and by substantial majorities  
15 they said they did.

16 And, you know, if we're here to protect the  
17 consumer interest, maybe it's appropriate to listen to  
18 what consumers have to say.

19 And finally, on the money that is down  
20 there, there have been many transactions. Most of  
21 them are HVAC, but some of them have been with LDR. I  
22 have Mr. Matthews here and he's going to come up and  
23 testify to you why those transactions with LDR have  
24 not only been not a situation that we've tried to go  
25 ahead and benefit our bottom line, but they have been

1       instead a situation where we have because of the  
2       consent mechanism we have benefited from LDR.

3               And we've taken just as much advantages as  
4       we can of LDR as we have any other marketer that is  
5       out there. So with that, I'll ask Mr. Matthews to  
6       come up, if that's okay with your Honor.

7               JUDGE THORNBURG: Let me make sure we didn't  
8       have any questions for you while you're here.

9               Commissioner Drainer?

10              COMMISSIONER DRAINER: Yes. As long as  
11      you're here.

12      QUESTIONS BY COMMISSIONER DRAINER:

13              Q. I did want to ask you the same question I  
14      asked Mr. Hack, so with respect to the comments  
15      that -- the proposed rule that you attached to your  
16      comments, you would believe that that takes care of,  
17      as Mr. Hack would say, the whole ball of wax?

18              A. Yes, yes. Because we had a specific set of  
19      provisions, admittedly less expansive than what is in  
20      the proposed rule for both marketing and also for the  
21      other aspects of the rule.

22              COMMISSIONER DRAINER: Thank you very much.

23              JUDGE THORNBURG: Thank you.

24              Commissioner Murray?

25              COMMISSIONER MURRAY: No questions.

1 JUDGE THORNBURG: Thank you.

2 If Mr. Matthews will come forward.

3 (Witness sworn.)

4 JUDGE THORNBURG: If you'll please be  
5 seated.

6 If you'll briefly introduce yourself and  
7 we'll hear your prepared comments, and then we may  
8 have some questions.

9 MR. MATTHEWS: Good morning. My name is  
10 Steve Matthews. I work for the Laclede Gas Company as  
11 the director of gas supply.

12 My comments today will focus on those  
13 portions of the proposed rule relating to standards of  
14 conduct for marketing affiliates.

15 I'd like to begin by noting that Laclede  
16 takes with the utmost seriousness its obligations to  
17 be fair and evenhanded in all of its dealings with  
18 marketers of natural gas, whether they be affiliates  
19 or unaffiliated companies.

20 Virtually from the time that interstate  
21 pipelines began marketing gas on an unregulated basis  
22 through various affiliates, Laclede raised with the  
23 FERC the need to ensure that customers would not be  
24 harmed by any competitive abuses.

25 As part of our comments in this proceeding,

1 we have also proposed for your consideration  
2 reasonable standards of conduct to prevent any  
3 favoritism or undue discrimination in how Missouri  
4 LDCs deal with their marketing affiliates and other  
5 unregulated suppliers.

6           Given the absence of any complaints or other  
7 indications that Missouri LDCs have actually abused  
8 their relationships with affiliated marketing  
9 companies, it is difficult to see a need for even  
10 these more reasonable standards of conduct. At a  
11 minimum, however, Laclede believes the standards it  
12 and other utilities have proposed are more than  
13 adequate to deal with any potential abuse.

14           This is particularly true in light of the  
15 gas supply incentive plan that has been approved for  
16 Laclede. As I understand it, the primary rationale  
17 for pursuing standards of conduct reflected in the  
18 proposed rule is the concern that LDCs may have a  
19 financial incentive to use their regulated assets in a  
20 way that would unfairly benefit their marketing  
21 affiliates since increased sales by that affiliate may  
22 translate into increased unregulated profits for the  
23 LDC.

24           Under our incentive program, however,  
25 Laclede has an incentive to maximize the revenues and



1 minimize the costs in all of its transactions without  
2 regard to whether such transactions involve affiliated  
3 or unaffiliated marketing companies, since both the  
4 company and its customers get to share in the benefits  
5 produced by such actions.

6 Under such circumstances I simply don't  
7 believe that the rationale for the proposed standard  
8 of conduct holds true, and that's been borne out by  
9 our experience under the incentive plan. In fact, one  
10 of the primary strategies we followed under the plan  
11 to achieve additional revenues for our customers was  
12 to lock in multi-month -- lock in -- excuse me -- for  
13 multi-month periods the price paid to the company for  
14 capacity we released to various marketing companies.

15 When the value of that capacity subsequently  
16 declined, the locked-in price allowed us to collect  
17 more from the marketer than we otherwise would have  
18 under a month-to-month market-based arrangement.

19 Notably when you look at the marketers who  
20 contributed to these additional sources of revenue,  
21 you'll find the company extracted a significant amount  
22 of revenue from Laclede Energy Resources on behalf of  
23 its jurisdictional customers.

24 This is one real-life example of how the  
25 structure currently in place makes the proposed

1 standards of conduct unnecessary. Given the absence  
2 of anything that would point in the opposite  
3 direction, we believe that the proposed standards  
4 submitted by the utilities in their initial comments  
5 are more than sufficient in the event the Commission  
6 ultimately determines there is, in fact, an actual  
7 need to establish additional guidance in this area.

8 Thank you.

9 JUDGE THORNBURG: Commissioner Drainer?

10 COMMISSIONER DRAINER: I have no questions,  
11 but I thank you very much for your comments today.

12 JUDGE THORNBURG: Commissioner Murray?

13 COMMISSIONER MURRAY: I don't have anything.

14 Thank you.

15 JUDGE THORNBURG: Thank you.

16 Mr. Fischer, at this time we'll take  
17 additional comments.

18 MR. FISCHER: Thank you, your Honor.

19 I think I may be the last thing standing in  
20 the way of lunch, so I'll try to be brief, but my  
21 clients did ask me to make some specific comments.  
22 Some of them will sound familiar from my opening  
23 statement, but I'd like to highlight a couple of areas  
24 that they have concerns about.

25 As a general matter, I think my clients

1 would ask the Commission to keep in mind that it's  
2 really full competition that will result in lower  
3 prices and the highest quality of service to the  
4 ratepayer. Handicapping the ability of a utility or  
5 its affiliated company to compete with competitors out  
6 in the marketplace and discouraging affiliated  
7 transactions will not necessarily achieve that goal.

8 One of the specific areas that they're  
9 concerned about is the use of the name and logos by  
10 affiliates. My clients feel that it's unnecessary to  
11 require physical separation between the utilities and  
12 the marketing affiliates. That is just going to add  
13 an unnecessary cost, and as I mentioned in my opening  
14 statement, it's very difficult and burdensome for  
15 small utilities that have small marketing operations  
16 to use the same personnel and somehow have them sit in  
17 separate offices. And I'm afraid the rules may end up  
18 requiring that they actually hire a new person or have  
19 a new office that they don't currently use. This  
20 would be inefficient.

21 Section 2H was proposed rule provides that  
22 the nonregulated employees will have no more access to  
23 employees of the regulated gas corporation than the  
24 non-affiliated entity. I think that standard is  
25 rather vague and overbroad, and as such, it's not

1 clear how a small company can comply with it or how it  
2 will be enforced for that matter.

3 Secondly, there's simply not a basis in the  
4 records, I don't think, for the generic conclusion  
5 that interaction between utility employees and their  
6 affiliates constitutes or somehow will result in  
7 noncompetitive behavior. Again, for small utilities,  
8 this would be impractical since the same employee that  
9 does some limited marketing functions may also be  
10 employed by that public utility. I just don't know  
11 how you separate that. Unfortunately, this rule would  
12 probably result in them just having to abandon their  
13 marketing efforts even though they are rather limited.

14 Section 2L of the proposed rule provides  
15 that a marketing affiliate shall not in any way relate  
16 to the consuming public that it's part of the  
17 regulated entity. United Cities, Greeley and Southern  
18 Missouri Gas and Fidelity all would oppose that  
19 particular standard. That restriction is unnecessary  
20 since there is no evidence that merely by using a  
21 related name provides a huge competitive advantage to  
22 an affiliate.

23 Certainly most consumers want to know who  
24 they're dealing with, and it would be helpful in  
25 assessing questions of reliability of service and

1 other non-price-type factors to know who you're really  
2 dealing with.

3 Certainly unregulated competitors will be  
4 using their widely recognized names and logos without  
5 restriction. I think if you go to Houston today or  
6 around the country, you're going to see some of these  
7 competitors' names showing up on stadiums and many  
8 other places that are quite conspicuous, and certainly  
9 in the telecommunications areas the use of names  
10 similar to the regulated telecommunications companies  
11 are quite common and help consumers to know who  
12 they're dealing with.

13 And then the last area, I think we've heard  
14 a lot over the last couple of days about the  
15 asymmetrical pricing concerns. United Cities and  
16 Greeley also share those concerns. They're concerned  
17 that the -- as a theoretical proposition, the rule  
18 where it says there should be a financial advantage  
19 isn't a problem but the way it's defined is where the  
20 problem occurs.

21 The pricing standards provide that a  
22 regulated gas company shall be deemed to provide a  
23 financial advantage to an affiliate if it purchases  
24 goods or services from the affiliate above the lesser  
25 of the fair market prices or the fully distributed

1 costs, and we've had a lot of discussion about that.

2 That definition is -- from our perspective  
3 is the problem. The asymmetrical pricing provisions  
4 will discourage what would otherwise be market-based  
5 transactions from occurring, and we don't think that  
6 would necessarily be a good idea. And we've heard a  
7 lot about specific examples. I won't go through  
8 those.

9 For many years in the telecommunications  
10 area this Commission has recognized the principle that  
11 a utility should cover its long-run incremental cost  
12 and provide some contribution to the telephone  
13 company's fixed cost and -- depending on the market  
14 conditions. Those principles were embodied in the old  
15 case of 18309 that we've used for years. I think  
16 those kind of principles are more appropriate to hear  
17 than trying to mandate a fully distributed cost  
18 standard, and I'd ask the Commission to think about  
19 that as you look at that standard.

20 This kind of approach I think would continue  
21 the goal that the Commission is trying to encourage  
22 here, that keeping transactions going forward to make  
23 economic sense. But I'm afraid the fully distributed  
24 cost standard is going to discourage transactions  
25 which would otherwise happen and not harm the utility

1 or its ratepayers.

2 With that I'd conclude my remarks and answer  
3 any questions you might have.

4 JUDGE THORNBURG: Commissioner Drainer?

5 COMMISSIONER DRAINER: Well, first I wanted  
6 to thank you for pointing us back to 18309. That's a  
7 good one.

8 MR. FISCHER: For the record, that was about  
9 the first case I was ever involved with, so I haven't  
10 forgotten it.

11 COMMISSIONER DRAINER: Secondly, I also  
12 wanted to thank you for pointing out, you said the  
13 name, because isn't that truly a two-edged sword, that  
14 on one hand although some might argue that it's an  
15 advantage to have it, on the other hand, if the  
16 affiliate messes up, it can hurt the parent company.

17 MR. FISCHER: I would agree.

18 COMMISSIONER DRAINER: So thank you. I  
19 appreciate your remarks.

20 JUDGE THORNBURG: Commissioner Murray?

21 COMMISSIONER MURRAY: No questions. Thank  
22 you.

23 JUDGE THORNBURG: Are there any other --

24 Mr. Cooper, did you have any comments?

25 MR. COOPER: No, your Honor.

1 JUDGE THORNBURG: Thank you.

2 Are there any other opponents, either  
3 attorneys or witness commenters?

4 (No response.)

5 JUDGE THORNBURG: Did anyone have any  
6 questions or matters that need to be addressed before  
7 we adjourn?

8 (No response.)

9 JUDGE THORNBURG: With that, we will be  
10 adjourned.

11 Thank you.

12 WHEREUPON, the hearing was adjourned.

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