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PUBLIC SERVICE COMMISSION

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Hearing

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Jefferson City, Missouri
Volume 2

In the Matter of Laclede Gas)
Company's Experimental Price) Case No. GO-2000-394
Stabilization Fund.)

VICKY RUTH, Presiding,
REGULATORY LAW JUDGE.

SHEILA LUMPE, Chair,
CONNIE MURRAY,
ROBERT G. SCHEMENAUER,
KELVIN SIMMONS,
M. DIANNE DRAINER, Vice-Chair,
COMMISSIONERS.

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P R O C E E D I N G S

JUDGE RUTH: Let's go ahead and go on the record, please.

Good morning. My name is Vickie Ruth, and I'm the Regulatory Law Judge assigned to this case. It's Case GO-2000-394 in the Matter of Laclede Gas Company's Experimental Price Stabilization Fund. It is February 2nd, 2001, and the time is 8:34.

We will begin with entries of appearance, and Laclede, would you please start.

MR. PENDERGAST: Thank you, your Honor. Michael C. Pendergast appearing on behalf of Laclede Gas Company. My business address is 720 Olive Street, St. Louis, Missouri 63101.

JUDGE RUTH: Staff?

MR. SCHWARZ: Good morning. Thomas R. Schwarz, Jr., P.O. Box 360, Jefferson City, Missouri 65102, appearing for the Staff of the Missouri Public Service Commission.

MR. MICHEEL: Douglas E. Micheel appearing on behalf of the Office of the Public Counsel and the Public, P.O. Box 7800, Jefferson City, Missouri 65102-7800.

JUDGE RUTH: Thank you.

This hearing has been scheduled to allow the parties an opportunity to more fully explain certain matters to the Commissioners. You will be given an opportunity to answer questions, and if you have witnesses that you need to call in order to more fully answer those questions, you'll be allowed to do so.

We're going to take a very brief three or four minute break while I call the Commissioners and tell them we're ready to begin.

MR. SCHWARZ: Will we have opening statements?

JUDGE RUTH: Yes. We'll go off the record for just a moment.

(AN OFF-THE-RECORD DISCUSSION WAS HELD.)

JUDGE RUTH: Let's go back on the record, please.

As I stated briefly before we took our break, this hearing has been scheduled to allow the parties to more fully explain certain matters to the Commissioners. In particular, the Commission requires a more thorough explanation of the alleged deficiencies of the Experimental Price Stabilization Plan, and it also requires a clarification of the financial gains and savings that Laclede alleges it has made under the experimental PSP.

We will begin with oral arguments from the parties, and then the Commissioners will have questions from the Bench. If you require a witness in order to answer the question, you're entitled to call one.

And let's begin, then, with an opening statement actually from Staff.

MR. SCHWARZ: Good morning. May it please the Commission?

I was struck by an observation in the Commission's agenda discussion, and I can't remember if it was last week or the week before, when the Commission was discussing the access charges for wireless telecommunications carriers.

At the end of that discussion, Chair Lumpe observed that the Commission had provided as many incentives as it could think of to get the parties to sit down and negotiate access rates, and that none of those incentives had realized the activities that the Commission wanted. Namely, you hadn't been able to get the parties to sit down and negotiate meaningfully on wireless access charges.

The thrust of that statement is that the incentives were not designed to produce the results that you intended. They certainly didn't achieve the results that you intended.

I would suggest that the PSP, the incentive hedging program that is currently in place for Laclede, suffers a similar fate. That is, it appears from the Commission's Report and Order in Case 98-484 that the Commission thought that it was eliciting guaranteed price protection for Laclede's customers. That is, that was a main purpose of the PSP.

It does not appear that the PSP is designed to achieve those results. There are specific design flaws in the PSP that provide for results that were unintended. A principal feature of the PSP is the determination in early March of a target strike price and a catastrophic price level. There is then a 90-day window.

Okay. The prices are determined, target strike price and catastrophic price level are determined in early March. There is then 90 days. At the end of that 90 days, Laclede has the option of terminating the guaranteed price protections that the parties have.

COMMISSIONER DRAINER: Excuse me. Do we have a copy of that?

MR. SCHWARZ: No. I can provide copies if you like.

COMMISSIONER DRAINER: It would be easier to follow you.

MR. SCHWARZ: In the intervening period, in those 90 days, prices can go up or prices can go down. They can, of course, stay the same. But the two possibilities that you need to deal with are prices going up or prices going down.

If at the end of 90 days prices have gone up, prices have moved against the consumer, Laclede is free to say, We choose not to provide protection, guaranteed protection for the customers at either the target strike price or the catastrophic price level.

That is precisely what happened in June of last year. Laclede sent the Commission a letter saying, Gee, the market has moved up, and we will not provide guaranteed price protection for consumers in the winter of 2000-2001.

That is a flaw in the design of the program. That is, it gives the LDC the opportunity, indeed the incentive, for 90 days to sit and watch and see which way the market moves, and if the market moves adversely to customers, to relieve itself of the obligation of providing guaranteed price protection.

On the other hand, the price can move down, the green line. Again, for 90 days the company sits and observes the market. What is the consequence, the design of the ability to sit and observe the market going down? Well, by definition you can now acquire protection at either of the two price levels for less cost than you could do 90 days earlier.

So by having the LDC do nothing but sit and watch, they are entitled to share in the customers' exposure to market risk which has now moved in favor of the customers. That is, Laclede will get a percentage either through cost reduction or through the ability to trade in a broader range than it would if it had been bound to guarantee protection at the levels of early March.

That is inherent in the design of the program, and it is precisely the kind of design that the Commission is entitled to address and correct under the terms of its Order in 98-484.

There is another flaw in the design of this program. That is, in the instance where prices are moving upward, moving against the consumer, come June 1st the LDC is entitled to abandon the guaranteed price protection for consumers. In that case, what happens next? What happens next?

In the current design of the program, Laclede is required to acquire at a certain price, at certain strike prices for certain percentages of their volumes for a certain amount of money price protection for customers. Well, lo and behold, in this particular rising market, those parameters were unattainable. That is, the market had moved so far against customers that the fallback position was an impossibility.

So in a market that's moving up, the LDC, as it's entitled to do under the design of this program, says no guaranteed price protection in the particular circumstances that we faced last summer, that they were unable to achieve the fallback position, and what happened was the Public Counsel, Laclede and Staff finally -- actually, what happened next was in early July Laclede filed a pleading saying, Gee, the fallback position is not achievable. We need to change the terms of the program to accommodate these new market conditions.

So Staff and the Public Counsel and Laclede negotiated, talked around things and finally reached an agreement in August for modifications to the program to -- under which Laclede then undertook to provide some price protection for customers, but that's another delay, June, July, August, before the parties reached agreement.

It wasn't, I think, until October that the Commission finally approved the modifications proposed by the parties, but certainly there was two and a half, three months before Laclede knew it had the agreement of the other active parties to a modification of the program to really permit them to go ahead and undertake price protection.

So that that time delay during -- again, the market is moving against the customer, that the existence of that fallback position which wasn't attainable worked against the interests of the customer, and that delay is inherent in the design of the PSP.

The PSP has a cost reduction feature. I'm not even sure how to categorize it. When I think of cost reduction, I mean the authorized costs of the program, and I don't know if this is -- this may be -- the number may be highly confidential.

JUDGE RUTH: Do you want to go --

MR. SCHWARZ: Yes, I would like to go highly confidential if we might.

JUDGE RUTH: Okay. Is there anyone in the audience that would need to leave?

MR. SCHWARZ: No.

(REPORTER'S NOTE: At this time, an in-camera session was held, which is contained in Volume No. 3, Pages 15 through 17 of the transcript.)

JUDGE RUTH: Sorry. Please proceed.

MR. SCHWARZ: No problem.

So it would seem that what Laclede is claiming is the same kind of trading profits that it would have claimed or could have claimed under the PSP portion of the incentive program is now being claimed as a cost reduction. In fact, the -- I mean, if you total up the cost, it's almost double or more than double of the amount of the maximum recovery amount that Laclede had been authorized.

I think that -- and no matter what happens for the year, the second year of the program, I think that for the third year of the program that is something that the Commission should address. If the customers aren't getting the guaranteed price protection that is the object of this program, then perhaps you should take a look -- not perhaps -- you should take a look at the ability to profit on the cost savings end of things.

Staff's proposal to remedy the design deficiencies in this incentive hedging mechanism is for the Commission to simply tell Laclede basically what they told MGE last fall, which is, Look, we're not going to set preapprovals, we're not going to set targets, and we don't want to confuse the acquisition of price protection for consumers with incentive -- incentives to the LDC to make profits.

The LDCs should be exercising their best judgment and securing price protection for customers in a changing market, in a market which even Laclede concedes is unprecedented. In those circumstances, the company should take the best interests of its customers as its guideline and exercise its best judgment and protect the customers accordingly.

The early years of price protection said -- directed the participating LDCs, go out, spend this amount of money, protect this amount of volumes at this particular price level. And in the market prior to the past year, that was something that was achievable.

The market fluctuations prior to 2000 were nothing compared to the price spike that we had just in December of the year 2000. I don't believe there's anyone in this room that can tell you right now that $4 or $5 or $6 in December of 2001 is going to be a good price for customers to pay.

That is something that the LDC is going to have to determine in the exercise of its best judgment. They're in the market every day. They're in the market all the time. They have expertise. They talk to suppliers. They talk to other LDCs. They have to be able to gauge the market and exercise their judgment.

It is Staff's position that it is impractical at this time to say, LDC, we expect X coverage for X dollars at this price. We don't think that in the current market conditions that's doable.

Staff's position is that, just as the Commission has told MGE, go forth and do right, it should give the same instructions to Laclede Gas Company.

If the Commission does not feel that it can take that step, the Staff would strongly urge the Commission to eliminate the 90-day window in which the LDC can speculate on market movements at no risk to itself and only risk to its customers. That is, the day that the TSP and the CPL are determined, that's the price level that's locked in for customers.

Staff will certainly be available to answer any questions the Commission might have. Thank you.

JUDGE RUTH: Thank you, Staff. Laclede, are you prepared to give your --

MR. PENDERGAST: Did you want us first?

JUDGE RUTH: I'm sorry. You're right. Public Counsel would be next.

MR. MICHEEL: May it please the Commission?

I guess for my opening I want to talk about the major deficiencies that exist currently in Laclede's current approved Price Stabilization Plan, and before I explain those current major deficiencies in the current PSP, I think it's important for the Commission to get a flavor of the background of the Price Stabilization Plan and how we got to where we are today.

I think the Commission's well aware that the original purpose of the Experimental Price Stabilization Plan that was approved by unanimous stipulation in Case No. GO-97-401 was to permit Laclede to purchase and hold financial instruments in its effort to reduce the volatility of the natural gas market.

COMMISSIONER DRAINER: Will you speak up a little bit, please, or closer to the mic? I couldn't hear you.

MR. MICHEEL: Yes. In GO-98-484, Laclede sought to modify the original PSP to add the opportunity to allow Laclede to profit from the program. This Commission, on a three to two decision, decided to allow the modifications proposed by Laclede in their Alternate Plan B.

This decision, in my opinion, essentially changed the program from one directed at price protection to one driven by profit motivation. Thus, the major deficiency, the overarching deficiency that occurs in the current PSP as approved by this Commission is the profit motive, and that profit motive is contrary to the purpose of the program, and the purpose of the program initially was to reduce the volatility of the natural gas market as it related to Laclede's captive customers.

The current program, in Public Counsel's opinion, only allows the company to participate in upside profits while avoiding all downside risks.

As Mr. Schwarz alluded to, the program structure has two distinct incentive mechanisms, each allowing the company the opportunity to profit. The first incentive mechanism is the price protection incentive, and that incentive is the incentive where the company sets the target strike price and a catastrophic price level and it can trade. If it purchases within that level, it has an opportunity to profit.

The second portion of the incentive is the overall cost reduction incentive. I've prepared -- the Office of the Public Counsel has prepared some handouts that I'd like to hand out to the Commission now to kind of follow along with the rest of what I'm doing. And I guess --

JUDGE RUTH: I'm sorry. I was just going to ask if we needed to go in-camera?

MR. MICHEEL: Some of the items on these handouts are highly confidential, and where I do specifically talk about the numbers, I will let you know and we need to go in-camera. But to the extent that I don't verbalize the numbers in my opening, I don't think it's highly confidential, although these papers that I've given you do contain highly confidential information and they are so marked. But I'd be willing to go in-camera if that's what you'd like to do.

COMMISSIONER DRAINER: Let me just ask, these are Laclede's numbers that are highly confidential. So I would just ask, as we did on the previous, that just afterwards you let us know whether or not you believe that this document needs to be highly confidential or that the numbers are considered highly confidential, because I know that the other -- the 4 million was not highly confidential.

MR. PENDERGAST: Yes.

COMMISSIONER DRAINER: It's in a pleading by you just recently.

MR. PENDERGAST: Yes.

COMMISSIONER DRAINER: So I just want to keep it as open to the public record as possible.

MR. MICHEEL: I agree with that, Commissioner, and on this initial sheet, the only numbers that I know that are for sure highly confidential are the TSP and the CPL.

COMMISSIONER DRAINER: All right. So we can follow without you stating it?

MR. MICHEEL: Yes. This essentially is just a time line, and I thought that it would be more appropriately -- more appropriate to graphically show the progression in the case rather than just speak to that progression, but I would like to point out a couple of highlights on the time line.

The first highlight, of course, is what the target strike price and the catastrophic price level was for the current program, and I'm not going to say that because that's HC, but the Commissioners can see that level.

The second bubble you'll see there is the fact that between 3/1 of 2000 and 5/5 of 2000, Laclede Gas Company had at least 39 out of 48 days to purchase the appropriate protection below the catastrophic price level.

Also on the time line we show the 6/1 where Laclede Gas Company opted out of the price protection incentive, and that's pursuant to the program as approved.

On 7/7, Laclede filed for their temporary revisions to the PSP, and as the Commission will recall, those temporary provisions were an increase in program funds to $10 million, to relax the 70 percent requirement for protecting flowing supplies, to allow Laclede to vary the protection it buys in some months up to as low as zero and to extend/expand the type of financial instruments that Laclede could utilize in the program.

The next bubble on there shows that Laclede began selling in and out of certain hedge positions on certain dates well before those positions had come to fruition or the contracts were in the last three days.

It also shows that on 9/1 that Laclede, Public Counsel and Staff entered into the Stipulation and Agreement that Mr. Schwarz talked about. And of the four recommended changes or revisions to the program that Laclede offered in July, the parties were able to agree to relax the 70 percent requirement and allow Laclede to get zero protection in certain months. And then the other item on that just shows when Staff filed to terminate the current PSP.

At this time I'd like to just discuss the major deficiencies in the price protection incentive, and that's the first part of the program.

With the price protection incentive, Laclede has the ability to bail out of that incentive within the 90-day window, and indeed, as that graph shows, Laclede bailed out of that on 6/1 via a letter.

The reason Laclede gave for exiting that part of the program was that the market was going up and it had moved against them essentially. The way this program is structured and the way the incentive part of this program is structured, the only incentive that Laclede has to opt out of that portion of the incentive program is when the market is going up, when prices are going up.

Of course, unfortunately, when market prices are going up, that's the time that the consumers need the protection provided or that was supposed to be provided by this program the most. By exiting the program as designed, by exercising their option to bail out at the 90-day window, the customers were left with the risk of rising prices and the lack of stability in that price.

In Public Counsel's opinion, that is the antithesis of the purposes of this program. We certainly believe that the 90-day out clause is a major deficiency in this program that needs to be corrected by this Commission.

I'd ask you to turn to the second handout in the packet there, and I just want to explain what that handout graphically demonstrates.

As you are aware, the current program sets a target strike price and a catastrophic price level. This graphically represents, based on the prices on the current dates, when Laclede could indeed have gotten into the market -- could have gotten in the market, excuse me, at certain prices and when it could have gotten into the market below the TSP or the CPL. So that's just a graphic representation of those 39 days that we talked about on the initial document.

In bailing out of the price protection incentive, Laclede Gas Company acted consistent with the actions of a profit-maximizing company, contrary to the purpose of the program. That act is not price protection but profit motivation.

The second portion of the incentive is the overall cost reduction incentive, and the overall cost reduction incentive allows Laclede Gas Company to trade in and out of positions on certain financial instruments and gives Laclede the opportunity to share in the profits from those trades.

In other words, if Laclede trades in and out of their positions before the last three business days of the contract's price, they get to share in those upside profits.

I would note in this situation, because Laclede bailed out of the price protection portion, any contracts that Laclede held up to the last three business days or during the last three business days of the program, 100 percent of the profits from the contracts went to the ratepayers.

There are some major deficiencies with the overall cost reduction incentive. As a result of the profit motivation given by the overall cost reduction incentive, ratepayers' cost of gas, in our opinion, is higher than it would have been absent the profit motivation.

And I'd ask that -- just to give you an example, or our view of an example, turn to the sheet that's got November activity here. And what this sheet shows is, based on information given to us from Laclede -- and I'm not going to talk specifically about the numbers because obviously the numbers are highly confidential, but these sheets show all of Laclede's trading activities up and until a certain date where we had the information.

And I'd ask that you turn to page 3 of this sheet, the January activity of Laclede, and I think you'll see a vivid example of where the profit motivation overcame the purposes of the program.

If you'll look down on the line date purchased 10/30/2000, 10/30/2000, the last two lines on that level, you will see under the date sold on 12/20/2000 that Laclede sold out of certain areas, certain contracts, and received a substantial profit on those sales, and those profits total almost $4 million. I'm looking at the January activity sheet, page 3, last two lines.

The way the overall cost reduction incentive is structured, essentially Laclede got the opportunity to share in 50 percent of those profits.

COMMISSIONER DRAINER: Excuse me. I want to ask you something. I'm trying to follow here. You're talking about profit. Your table here says gain. Is that the same thing as profit?

MR. MICHEEL: Yes.

COMMISSIONER DRAINER: Okay.

MR. MICHEEL: Those are synonymous. I'm

sorry. They had a gain on the sale of that option, and I view that as a profit.

COMMISSIONER DRAINER: All right. I just wanted -- you're trying to get me to follow the sheet, and I'm trying to follow the sheet and it doesn't have profit here anywhere, so --

MR. MICHEEL: I'm sorry. It's in the gain column. You'll see the last two lines there, they gained approximately $4 million.

COMMISSIONER DRAINER: So that's a net profit, you're saying net after cost?

MR. MICHEEL: Net after cost. And under the program they share those gains with the customers or those profits with the customers.

COMMISSIONER DRAINER: Okay. Thank you.

MR. MICHEEL: If you'll look up on the line to the fourth line under date sold, you'll see 12/21/2000 where they sold also out of certain positions, and you will see a gain there of a little over some $2 million.

The way the program is structured, because the company opted out of the price protection, that $2 million essentially goes 100 percent to the ratepayers.

Now, you may ask, how are the ratepayers harmed or disadvantaged by this trading? Well, absent the ability to share in the gain or the profit, ratepayers would have seen 100 percent of those gains credited against gas costs. For example, let's assume that gas costs $10, and Laclede is getting $5 for that gas from the ratepayers and $5 of that from their gain or profit from sale of the option. If they had held that option, ratepayers would pay $5, the gain would pay $5, and that would equal the $10.

The way the current program is structured, essentially -- and there are some sharing grids, but I'm just going to use 50 percent. It averages out to about 50 percent because it's a stairstep sharing grid -- ratepayers are going to pay $5. $2.50 from the gain or profit on sale of that option is going to go to the cost of that gas. $2.50 from that sale is going to go into Laclede's pocket as profit, and then Laclede is going to ask the ratepayer for the other $2.50 to equal the $10.

We think that's a major design flaw in this program because the program's goal was to reduce overall price volatility for the ratepayers.

I'd refer you to the next chart and just explain that a little bit and what costs it has on the chart. The first cost in the, I guess, darker blue is the cost of the options purchased. The maroon one is the overall gain. The yellow is the gain in the last three days where they held the contracts for the last three days, and the greenish blue is the gains upon which Laclede has an opportunity to profit or share in that gain.

And I would note that the title of this is Unrealized and Realized Gains, and the unrealized gains for this chart relate to the amount of money not credited to ratepayers. It's not that they didn't get a gain from the sale, but the unrealized gain column shows where the sharing occurs in the sale of those options. And that just graphically shows what has happened in this program up through January 4th, 2001.

The Office of the Public Counsel believes that the program's basis and the underlying purpose of this program was a good purpose, to protect price volatility from customers. However, we believe that the profit motivation placed into this program has, unfortunately, changed the focus of the program.

So we would ask that the Commission strip out the profit portions of this program and return the program to its roots and to its purposes as set out when the Commission initially approved this program in GO-97-401.

The other point that I would note about Laclede's ability to gain on this program I think is very important, and Laclede's ability to profit from this program grows as gas prices increase. So their ability to profit from selling the financial instruments gains or increases as gas prices increase.

Therefore, their ability to see benefits to their shareholders from this program increases as the pain and the prices to the ratepayers who are required to pay that for that gas increases.

I would submit to you that that is the antithesis again of this program. So we would ask that the Commission strip out the profit motivation from this program and allow the program to continue in its initial state the way it was approved in GO-97-401 and run its full three-year term.

I have Mr. Busch here. He is more than happy to answer any specific questions you may have. Of course, I'm available to answer any questions you have.

Thank you.

JUDGE RUTH: Thank you, Public Counsel. Laclede, are you ready to give your statement?

MR. PENDERGAST: Yes. Thank you. Good morning. May it please the Commission?

These are difficult times for energy consumers throughout the country and in the state of Missouri. Laclede is acutely aware of the extraordinary pressures that have been placed on family budgets as a result of the unprecedented increases in wholesale natural gas prices that we've experienced over the last ten months, and we're also aware and appreciative of the pressures that have been placed on those who have been entrusted with the rather thankless task of recognizing this economic reality in a manner that insures the ability of utilities to deliver critical service, all of which makes it even more difficult to understand why we would be here today arguing over whether to continue a program that has actually done something, and something pretty substantial, to mitigate this problem.

Laclede is proud of this Commission's record of being among the first in the country to actively promote the use of financial instruments as a means of mitigating the effects of wholesale price increases, and we're also proud of successful efforts of our gas supply personnel to use the tools you gave us to create significant benefits for our customers under very problematic circumstances.

Amid all the whirlwind surrounding the extraordinary run up in gas prices, the TPSP stands as a testament to both the Commission's foresight and the company's hard work.

Before addressing the various criticisms that have been leveled at the PSP and the alternative that has been proposed to take its place, I wanted to briefly address the Commission's questions from its January 30th Order regarding the exact nature of the benefits achieved under the PSP.

As we've said in our pleadings, we have so far managed to convert the $4 million that was initially authorized under the TSP to right around $28.5 million in financial gains. We've done that in two ways. You've heard about those two ways from both Mr. Micheel and Mr. Schwarz.

The first way, the first approximately $11.5 million of the overall amount was achieved by holding the financial instruments until the last three days before they were due to expire and then cashing them in at their existing value. This amount would have been attributable to the price protection incentive.

However, since the company did withdraw from this component of the incentive program, as it's already been noted this morning, all of those gains will be flowed through to the ratepayer.

The remaining $17 million was achieved by trading in and out of options during the month. In other words, rather than simply buying the option and holding it to its expiration, we traded them when market conditions appeared favorable.

Pursuant to the overall cost reduction incentive component of the PSP, the gains made as a result of these intra-monthly trades were to be treated as reductions to the cost of the program. Under that same component, the company would also be entitled to keep a share of the cost projections ranging from 40 to 60 percent depending on the level of the savings achieved.

In any event, regardless of what component you're talking about, we have converted $4 million that we have received or will receive in rates from our customers into $28.5 million in financial gains and savings for which we have already received cash payment.

I should emphasize that since the program is not over and we may purchase more instruments, this is not a final number. It does, however, represent where we are today. And we have provided both Staff and Public Counsel with the source documentation showing the cash transfers associated with these transactions and a summary of them.

I should note that you can also see that summary in Attachment B to Staff's response. I believe all of this information was also provided to Public Counsel. In fact, Mr. Busch was kind enough to point out a few slight discrepancies between the source material and our summary. We've corrected that, but that didn't change the overall results.

But given these results, we don't believe there can be any dispute regarding either our quantification of the overall benefits or the success of the program. It's astounding to us that one could characterize the PSP as having the kind of major deficiencies that would warrant its elimination.

In nearly 20 years of practice before this Commission, I cannot recall another program offhand that has produced the kind of returns six-fold for ratepayers that they will receive under the PSP. And if there wasn't, I can't believe that the Staff or anyone else would have recommended that the Commission get rid of it.

By virtually any measure, the PSP has been a resounding success compared to the hedging program that was being undertaken by Kansas Gas Service at around the same time as the PSP, a copy of which we included for the Commission's review in one of our earlier pleadings.

From what we have been able to determine, that utility was authorized to spend some $6 million for 50 percent more on its hedging program than we were, yet it expects to achieve a level of benefits that is substantially lower than what we have already achieved under the program.

Compare it to the results that were achieved on the other side of the state where the approach that's been recommended in this case is followed. From what we heard, there was no hedging program ever implemented and hence no hedging gains. I hope we can all agree that $28.5 million in hedging benefits is better than no benefits at all.

Compare it to the results that would have been achieved if Staff's hedging proposal in Case No. GO-98-484 -- that was the case in which the PSP was first approved by the Commission -- had been adopted instead of the PSP. As we've pointed out before, under the approach that was being recommended by Staff at that time, there could have been a $4 per MMBtu ceiling on the prices for the financial instruments that could have been purchased by the company.

Because of the market conditions that have existed, this ceiling would have precluded effectively the purchase of any financial instruments by the company, and hence there would have been no gains at all. Once again, $28.5 million in benefits is better than no benefits at all.

In view of these results, we believe it is simply impossible to conclude that the PSP has the kind of major deficiencies that would warrant its elimination, and according to the terms of the program, that's the standard that is to be used to justify any change in the program let alone a decision to eliminate it.

Moreover, we firmly believe that it would be a major mistake to abandon a program that has proved its value under very problematic circumstances for the standardless process that the Staff is advocating.

It is simply not reasonable to expect LDCs to spend amounts equivalent to a third or a half or even more of their entire net income for an entire year to buy price insurance for their customers on the hope that they may be able to eventually recover those amounts in rates in accordance with some unknown standard to be determined later.

And, quite frankly, what we've heard today has not done much to change that view. You have had both Mr. Micheel and Mr. Schwarz provide you with various calculations showing what could have been achieved under different scenarios back in March and April if the company had simply gone out and purchased all the instruments at that time, and if that's not an example of hindsight, I don't know what is, and it's a particularly unfair example of hindsight.

As Staff knows and Public Counsel knows, it was at that very time that they were submitting to the Commission a Stipulation and Agreement that proposed that a fixed price trigger be established for MGE that was around 2.50 or nearly $2.50 below what the price was that we were facing to purchase financial instruments.

Staff had also just recently indicated or criticized the company for not -- or for having purchased its instruments at strike prices around $4. By the time March and April rolled around, the strike prices were already well above that level. In addition, we had consultants -- and I'll, if I can approach the Bench, hand out.

We had our consultants and, of course, other sources of information showing us where prices were expected to go. And as you look at these prices now in hindsight, if only that had been the case.

But it's just a graphic demonstration of the fact that people thought the market at that time was overpriced, and we did not wait to purchase our instruments because we had some conception of making gains for ourselves but because we thought it was in the best interests of our ratepayers to wait until those prices came down, as Staff apparently thought they would, as Public Counsel apparently thought they would, and as the vast majority of analysts thought they would.

In any event, there are those kind of analyses that make it difficult, I think, for any gas utility to go out and, without any standards established beforehand, risk the kind of money, particularly in comparison to the average LDC's net income that would be required to do this kind of program and to take these kind of actions without the parameters established by the PSP.

At the same time, the Staff or Public Counsel do have concerns about certain mechanics of the PSP notwithstanding its benefits. We're willing, as we always have been in the past, to sit down and talk with them about such concerns.

Now is not the time, however, to jettison a program that has proven to be a resilient and effective mechanism for addressing the daunting problems posed by unprecedented changes in the wholesale market for natural gas, and I think it's important to recognize just how resilient this program has been.

Because this program was in effect, we were monitoring the market with a diligence and with a concentration that I suspect not every other LDC was, and we were following it, and when, because of that close scrutiny, we saw that the market was getting away, it was the company that came to the Commission and proposed that certain modifications be made, including an increase in the funding level that would have permitted us to go ahead and purchase more financial instruments, including the potential use of other instruments.

It was the company that had the flexibility under the PSP that was designed by this Commission that even with those run-up in market prices, instead of having an arbitrary $4 ceiling that we were constricted to and, therefore, couldn't do anything, as was the case with MGE, we had the flexibility, and I'll add with the help of Staff and Public Counsel, too, to go out and under very difficult circumstances realize very significant gains for our customers.

And in our view, that's a program that warrants continuation by the Commission and should really serve as a model not only for other LDCs in Missouri but for other LDCs across the country.

We want to make it clear -- and, therefore, we believe that Staff's recommendation and Public Counsel's as well should be rejected.

We want to make it clear, however, that we're anxious to work with the Commission and the Commission Staff and the Office of the Public Counsel to take whatever actions we reasonably can to relieve the financial burdens currently being experienced by our customers.

And to that end, we're willing to sit down and work with the parties on a filing to be made in the next week or so that would make various changes to our tariff that governs the PSP.

And what we would like to do is we would like to first of all have a mechanism for, instead of waiting until November to flow through the gains under the program, to speed that process up so that they can be returned to customers sooner rather than later.

We are certainly willing to sit down and talk to Staff if there are some reasonable things we can do to address their concerns and Public Counsel as well about the 90-day window and about the setting of the TSP to do that.

And we also want to go ahead and discuss with them additional funding for the program and an extension of the program for another year. And to make that additional funding possible, we're willing to take the gains that we would be entitled to under the cost reduction incentive component of the program and use those to supplement the hedging funds that would be available over the next two years. Right now it looks like that would be perhaps around $8 million. As I said, that may be subject to a little change.

But we would be willing to take that 4 million added to the 4 million that's already authorized under the program, to it for two years so that we have a more reasonable, more realistic opportunity of obtaining protection for our customers in the future.

We think those are the kind of common sense, constructive solutions that will help us to address this daunting problem we've all been facing. We hope we can sit down with Staff and Public Counsel and work something out along those lines.

But if we can't, we would certainly recommend that the Commission reject Staff's alternative and allow this program to go into its third year and hopefully produce benefits next year as it has this year.

Thank you very much.

JUDGE RUTH: We will now move to some questions from the Bench, and we'll begin with Chair Lumpe.

CHAIR LUMPE: I guess asking from Laclede first, in your sort of final statements there you talked about being willing to address some of the things that were considered to be design flaws by Staff and Public Counsel.

Is the 90-day window one of the things you would be willing to address and remove? And can I ask, was this analysis what led you to think you should opt out of the 90-day window?

MR. PENDERGAST: Let me answer the second question first, and then Mr. Neises I think can go ahead and answer the first question.

No, that wasn't the analysis that made us decide that we needed to go ahead and opt out of the 90-day window. What made us decide that was where actual gas prices had moved to relative to where the parameters for the program had been set.

What I tried to illustrate with that was at the time that Staff and Public Counsel have indicated the company could have made even greater gains by simply purchasing financial instruments, the market was already at very high, unusually high levels for summer prices, but they

were expected to decline and decline significantly.
So if you were going to be buying financial instruments, you would have tended to go ahead, as most people did, and wait. And what we were trying to illustrate by that is some of the information we were receiving from consultants that forecasted that those price declines were going to actually occur.
That's what motivated us to go ahead and wait, not out of any sense to go ahead and make some profit for the company, but to go ahead and make sure that we didn't buy instruments at a higher price than we needed to.
CHAIR LUMPE: I'm really curious about this consultant's projections. I mean, when we saw the prices go up in the summer, when we sent our letters out to state agencies and all legislators, et cetera, it was our assumption that they would continue to go up, and I don't know, I'm kind of glad we didn't have this consultant to go by.
MR. PENDERGAST: And I have to point out that this was in the spring. It was before the summer when the prices had been at those levels for quite some time.
CHAIR LUMPE: So this analysis was given to you way back in the spring?
MR. PENDERGAST: Yes.
CHAIR LUMPE: But they did -- they were

assuming that it would go up in the summer but then it would start going down; is that right?

MR. PENDERGAST: Yes.

CHAIR LUMPE: And Mr. Neises is going to address the 90-day window --

MR. PENDERGAST: Yes.

CHAIR LUMPE: -- whether that would be something that you would be willing to change?

MR. PENDERGAST: Certainly, your Honor.

CHAIR LUMPE: I assume Mr. Neises has to be sworn.

JUDGE RUTH: Yes. Would you like to sit at the witness box?

MR. NEISES: Surely, I'd be happy to.

(Witness sworn.)

JUDGE RUTH: Would you please state your full name for the record.

MR. NEISES: My name is Kenneth J. Neises. I'm Senior Vice President of Energy and Administrative Service, Laclede Gas Company.

JUDGE RUTH: Thank you. And when you're seated, please make sure your microphone's in front. I'm having a little difficulty hearing you.

MR. NEISES: Good morning. Could I first of all supplement the response which Mr. Pendergast gave to your --

CHAIR LUMPE: By all means. The more information I have the better.

MR. NEISES: What I would like to do is submit for the record a response to a data request which we had received from the Staff on the issue of why we opted out and the conditions that caused us to do that, and I'd like to submit that response for the record which gives you a full explanation of that. It's a one-page response if we could.

In addition, I would just like to add that the graph that was passed out to you that indicated what the projections of most analysts, I mean, those projections are generally consistent with what most analysts expected gas prices to do last year when they were looking at it in the spring.

And I would add that the Department of Energy, the division of that department which is responsible for these types of projections as well, their projection was no different than that of Goldman Sachs, of Risk Management, Inc. and of other analysts.

The point is that back in the spring, in March, April and May, while we were in the 90-day window, everybody expected prices to drop, including us, that it was the market was just totally overbought. And we had just come out of a very warm winter, if you recall, and for that reason was fully expected that prices would come down, that there should be adequate supplies and so forth. The letter or the response to the data request I think explains all this.

In response to the question on the 90-day window, if I could, I would like to explain to you first of all what the purpose of the 90-day window was and remains. That window, in my judgment, acted exactly as it should have.

The purpose of that window was that in the event -- and we all thought -- when I sat on this witness stand in support of that program when it was first proposed, I said that we needed to have a window for the reason that if the market were to take a radical move upwards after the target price was set in March, we would -- we could not operate under the price protection incentive of that program, because if it takes a radical move, we would have been at tremendous risk, a risk that the company could not bear.

We would go bankrupt if we would assure prices that were just -- or assure a particular price and then the market took this huge jump and there would be no way we could cover it.

And lo and behold, I did not dream when I designed that 90-day window that we would have to exercise it. I never thought that we were going see this kind of run-up in prices. It occurred so rapidly.

During the 90-day period, the big run-up occurred in the first week of May, about 60 days into the window, while we were thinking, everybody was thinking the price was going to go down. And suddenly, the beginning of May, in a matter of days, literally days -- we only had $4 million to cover. That's all that we were authorized.

In a matter of days, that number went to 12 million, that quickly, in order to buy the kind of coverage that we would have had to buy under the program that we would have been required to do. There's no way we could possibly deal with that. And the market just kept running, and now we all know where it ultimately went. So that's the purpose of the 90-day window.

Now, under normal circumstances, you know, this was sort of the 500-year flood, and what happened -- what I sat here thinking was, you know, I was just protecting in a very strange market, thinking it would never occur, and it did. And all I can say is thank God we had the 90-day window. That's the purpose.

The Chair asked the question, are we willing to deal with the 90-day window? The answer is yes. We're willing to shorten that period of time if that provides comfort, and we're prepared to do other things that I think should address the Staff's concerns.

As Mike Pendergast indicated, this is a resilient program. You know, we're -- the markets are -- in a free market, you know, a lot of things happen. But fundamentally we've got a program that we can make adjustments to, and they're not that -- it's not all that difficult.

I've instructed my staff, fully recognizing that these concerns are out there, to sit down and put -- we all put our heads together. We have ideas how to solve these problems and make this plan work in today's environment. We've got a totally different environment now.

We've got to address the dollar issue. $4 million today just isn't going to give us protection. Yet we all know we've got to provide some kind of protection. That's becoming increasingly clear to me as I attend the various investigations that are going on in the state.

We can't afford not to have protection. We can't let this happen again. But we would be foolish to sit back and think we can do that for $4 million when that value was set in a totally different age.

No. 2, we have to look at the 70 percent requirement. Can we really and is it right to say that we want to cover 70 percent? Maybe we can't afford to do that.

But I think -- and we have to look at different types of instruments. Instead of just looking at call options, which provide price protection which you have to pay for, which there's a premium involved in that, and that premium has gone up dramatically, where it used to cost 10 cents can cost 70, 80 cents or a dollar.

There are other measures such as what we call costless callers, and when you do that, what you do is you can establish a ceiling price which you give up and then you establish a floor, though, and the prices go below that floor, you've got to live with that reality, and you don't benefit or you can't -- you cannot then realize the benefits of that lower price below the floor.

But these are the kind of things that should not be that difficult to deal with, and we're prepared to do that so that we have a program within the context and the frame work that we have that I believe is workable for the future.

CHAIR LUMPE: Let me ask you another question, Mr. Neises. The $28.5 million that are in your pleadings and we've read that, where precisely does that fit into? Are you telling me that the customers would have paid $28.5 million more in their rates if you had not done the things you did? Was that shared? Where did that money go?

MR. NEISES: That money is presently in in accounts at Laclede Gas Company. That money has not yet been flowed through. And what we're proposing to do is -- first to answer your question, yes, these are real hard dollars. In other words, we had $4 million to spend, and we produced gains of 28 million. So there's -- that's cash that's sitting there now.

Okay. What we're proposing to do -- now, of the 28 million under this program technically, or under this, the way the tariff is written, we're entitled, the company is entitled to 8 million of that.

But what we're saying is, under the circumstances that we're under right now, recognizing that we need more money to fund this, the company's willing to take those $8 million and say, Let's spend that -- we'll put that money in to buy increased protection for the next two years. Add those 8 million -- or take four for one year and four for the next and add that to the existing four, and then we'll got $8 million to deal with. That'll improve that picture. The company won't keep that money.

CHAIR LUMPE: But it hasn't been spent?

MR. NEISES: No.

CHAIR LUMPE: It hasn't been relieving --

MR. NEISES: It has not. It has not. What we would like to do, if we could get a speedy resolution of this, our plan would be to file a rate reduction to flow through those dollars now, and that rate reduction would be -- that $28 million translates into about 11 cents, so that we could reduce our rates by approximately 11 cents when this money gets flowed through. That's not an insignificant amount. That's totally a result of the hedging program that we're talking about here today.

And then what we would do -- so I'd want to give that benefit up front so we can get -- so we can move rates down now. That's the big issue, to get rates down now. It's very clear to me that that's what the Attorney General was -- the message he was sending the other day.

Now, then, but part of -- but part of our proposal is, though, when we come next year, that we can use or have the $8 million to spend. So that, in effect, we're giving the money to the ratepayers now, and then -- but we're -- but then we're saying, the next go around we need to spend a little more to get the kind of protection that we need.

CHAIR LUMPE: How do you respond to the charge and the perception that the risk is all on the ratepayer and Laclede has taken no risk for itself, it's all -- the ratepayer has all the risk?

MR. NEISES: No. 1, when this radical change occurred in the marketplace and we had to enter in this unusual situation where we had to -- where we had to opt out, it is true that the company at that point in time was shedding the risk, but it was something we had to do under the circumstances because we simply would not be a viable financial inst-- a viable entity had we taken that risk.

But the program, if we don't exercise our -- you know, if you don't have these kinds of events and the market is operating rationally, there's no reason why the company would opt out. I mean, this was just -- this is just an exceptional, unusual situation. It's unfortunate for many reasons that it has happened, but that's just the harsh reality.

As we would go forward, I wouldn't anticipate opting out. If you have a rational market, I see no reason why we should have to do that. And we now have -- we now know, you know, prices have moved and we're -- and we all kind of have an understanding at least of potentially what's going on, and when we're designing what we're doing the next year, we take that all into account.

CHAIR LUMPE: Why wouldn't we want to design something, though, that at least shared the risks? And we talked about the 500-year flood. I recall when we had the 500-year flood in '93 we had another one in '95. So sometimes there's no guarantee that this isn't going to the market for who knows how long.

Why wouldn't we want to at least share the risk?

MR. NEISES: The program does. There is a sharing of risk in the program. In other words --

CHAIR LUMPE: I didn't perceive that.

MR. NEISES: Well, it is there I mean, because if -- because the way the program is designed, that if we cannot buy options above that catastrophic price level after that window has expired, we're at risk.

And if through the program, if we -- and if we do not have coverage, if we're -- when we're making judgments through the program and we sell options, for example, which is what we did this past period, and the market moves against us and we don't have coverage at the end of the 70 percent requirement, we're at risk.

So once the window's passed, we're at risk. So we've got to have coverage or we make up the difference. It's just the window period where we don't have the risk.

CHAIR LUMPE: Thank you, Mr. Neises.

Can I ask some questions of Staff and Public Counsel, Staff first? Thank you, Mr. Neises.

Are you of the same position as I think I heard Public Counsel, let's go back to the hedging program that was originally established in, I guess the case was 401, that original one?

MR. SCHWARZ: No. Staff's position is that it is at -- it's no longer practical to specify a dollar amount to be spent, a particular price level to be hit, and the volumes that need to be covered.

The market changes -- for instance, in a month from today, the TSP and CPL for the winter of 2001-2002 will be determined under the current program. Just as last year in February people were expecting prices to go down, I would suggest to you that the price of gas in the last three weeks has dropped significantly. People may expect the price of gas to continue to go down.

The prices determined as the TSP and CPL in early March, there's no guarantee in the current market conditions that that's going to be a reasonable number for the company to hit as the market continues to move through April and May and June and August and when the -- when the electric, you know, the gas-fired electric generators kick on in June and July and August.

No, Staff -- Staff doesn't think that at this stage that it's appropriate to set in concrete at any particular point in time the definition of what's going to be a good price for consumers in the winter heating season. That's something that the company should have the flexibility.

I mean, Mr. Neises says that we should sit down and discuss things further. From our perspective, we don't know how the -- A, we don't know how long those discussions would take, we don't know what the market's going to do in the meantime, and we don't know if at the end of that period we will have reached a conclusion that you can say with certainty will be reasonable under the unfolding market conditions.

We think that the company should exercise its best judgment. Knowing that there are expectations that it will provide price protection for consumers and knowing those expectations, it should exercise its best judgment and obtain appropriate price protection. We no longer think that it's particularly viable.

CHAIR LUMPE: For either --

MR. SCHWARZ: For either side.

CHAIR LUMPE: -- the old one or the new one? I mean, the old price -- the old hedging program?

MR. SCHWARZ: Right. Right. And I would also point out that the current program also has a difference between the target strike price, which by definition protection at the target strike price can be achieved at the time it's determined.

I mean, you actually go out in the marketplace, look at prices and say, For X dollars this is the level that we can hit. And then there's an additional 50 cents added to that price to, in Staff's view, provide the company with some cushion from market vagaries in the achievement of those protections.

And so as far as the 90-day window, the 90-day window permits them, without risk, to sit and watch the market, and at the end of the 90 days, I mean, they don't have any risk during the 90 days and they don't have any risk at the end of the 90 days because at the end of the 90 days you get the letter that says, Gee, the market's moved against us. The company has no risk, not when the TSP is determined, not during the 90 days, not after the 90 days.

If you have any other questions, I think Mr. Sommerer --

CHAIR LUMPE: I just have one more, and that's for Public Counsel. Mr. Micheel, you seemed to imply that going back to the old hedging program would be acceptable and sufficient. Is that your position?

MR. MICHEEL: Yes, it is, Chair Lumpe. We're willing to strip out all the profit motive, and I think Mr. Neises' testimony graphically demonstrates how the profit motive has affected decisions in this program or the idea to avoid adverse conditions where Laclede has risks, okay, and that's the 90-day opt out.

I'm not saying that Laclede in bailing out of the price protection incentive acted inconsistent with the actions of a profit-maximizing company. That's what they should have done, bailed out. What I'm telling you is, that by putting that profit-maximizing motive in there, it's the antithesis of the purpose of this program, and the purpose of this program is price protection, not profit motivation.

Nowhere did I say that they acted incorrectly in getting out. What I'm saying is, by putting that up there and putting the profit motive in there, you've undermined the entire purpose of the program, which is price protection.

And by opting out in that 90 days and allowing that 90-day window to opt out, customers were left essentially holding the bag.

And, you know, Mr. Neises talks about the $28 million of savings, but I mean, $8 million of that is going right to their bottom line. That's the way the program is designed. So my clients are paying essentially $8 million more for gas costs than they would have been using traditional PGA ACA Ideals, which is dollar for dollar pass through.

As I tried to point out, the only way that they're making those profits, since they bailed out of the price protection portion of the program, is because the gas costs are going up and they bought the options at lower prices.

So in my view, my clients are being asked to pay more money as gas prices go up. And if you strip out that profit motivation and make it into a price protection program, which was its initial purpose, my clients would see $28 million total benefit from this program, not $20 million.

And you put that profit motivation in and, rightfully so, company managers are going to look at the company bottom line and protect the company. I don't begrudge them for that. That's what they're supposed to do, but in doing that it puts my clients at risk and completely obviates what the program was supposed to do.

CHAIR LUMPE: You disagree with Mr. Neises saying that the old hedging program would not have worked and would have put the plan in jeopardy?

MR. MICHEEL: I'm glad you asked that question. As you'll recall, when the company came in for the incentive PSP, the only part of that program that the Office of the Public Counsel opposed was the profit incentive making portion of that program.

So I understand Mr. Neises' claim that in, you know, GO-97-401 it was set at the $4 level, but in the subsequent case, GO-98-484, the Office of the Public Counsel took the position that this should just be an insurance program, not a profit center for the company.

So it was not our position that they should be stuck at the $4, and indeed, you know, we're always willing to talk to the company and make some changes to the program so it works better. What we object to is the profit center portion of the program, and that's what we objected to in GO-98-484, and you can look at our Briefs and you can look at what we said in that program. So to me, the $4 number is a red herring.

CHAIR LUMPE: Thank you. That's all I have.

JUDGE RUTH: Vice Chair Drainer?

COMMISSIONER DRAINER: Before I ask a question, I would like -- I think Mr. Pendergast had a response, and I would like for him to be able to give that.

MR. PENDERGAST: Thank you, your Honor.

I think it's just important to point a few things out, particularly relating to the comments you've heard about the structure of the PSP and the incentives it provides and the risks that it imposes. And I think it's important for the Commission to remember that the program was structured after considerable debate and after considerable modifications that were made to address concerns that we had heard to try and make the interests of our customers as consistent with the interests of the company and its shareholders, so that when we were successful in going out and lining up price protection at more favorable prices, we benefited and the customer benefited, so that when we were successful in going out and reducing the cost of the program, we benefited and our customers benefited.

And that's how the program was structured, and that's how the program was designed, and that's how the program works. And you've just had an illustration of that with the fact that we've produced $28.5 million worth of benefits, and it's a little difficult to have your motives questioned and to have why you're doing what you're doing questioned when you've just offered to try and reach an accommodation where any gains that you would have been entitled to receive under that program you're willing to go ahead and use to help line up price protection for customers in the future.

If you want to look at risk, that's $4 million of risk next year and it's $4 million worth of risk the year after that. And I think that's a substantial offer, and if somebody's looking at having additional risk in the program, we believe that that does that.

Thank you.

COMMISSIONER DRAINER: Stay there. And now let's -- now for my question.

MR. PENDERGAST: Certainly.

COMMISSIONER DRAINER: And let me go ahead and just express that I appreciate the time line that

Mr. Micheel showed with what's happened with this program through time, and historically where it began was with a Stipulation and Agreement with all the parties. Had the case, made some changes, and then there was a Stipulation and Agreement last September with all of the parties. And that was in September, and in October we approved the tariffs, and then everyone starts saying the sky is falling.

And I really would challenge anyone in here to tell me that this isn't like, if not a 500-year flood, that anyone in here could have told me we were going to have gas prices that were going to go over $5.

So this is -- this is serious, and yet I'm in here today because my Report and Order did say that if there were going to be corrections to the program, it had to be by February 15. And so I'm here on February 2nd, and I'm being asked to react, maybe because of my own bad judgment in putting the February 15th day, but I want us to calm down and act reasonably.

And so my first question about this is, is that February 15th date part of the tariff?

MR. PENDERGAST: It is part of the tariff and part of the program description.

COMMISSIONER DRAINER: Then what I want to know, is there any way that we can step back from a February 15th date where I'm real concerned about due process, because when we had the GO-98-484 case, I had witnesses on the stand, I had testimony, rebuttal testimony. Public Counsel had an opportunity, as Mr. Micheel said, to present evidence about their concerns. And it was a different time then. There were different prices then.

And I either have to say off with your heads or go forth and -- and I don't know because I don't have expert witnesses that can tell me what's going on, and I'm real concerned because I hear Laclede saying that you would be willing to have discussions. I hear Public Counsel saying that the old program as it was was good, but they -- I really don't hear a closed door there.

Have there been discussions? Have you had adequate time -- that's my first question. Have you had adequate time to have discussions on whether or not this program should be ditched? Have you had adequate time to have discussions with Staff, Mr. Pendergast?

MR. PENDERGAST: I would say that --

COMMISSIONER DRAINER: This is a yes or no question. Since they have filed to ditch this program, have you had adequate time to give them other proposals and discuss changes to the program?

MR. PENDERGAST: I would say the answer to that would be no.

COMMISSIONER DRAINER: Mr. Micheel, have you had adequate time to hear proposals from Laclede?

MR. MICHEEL: No. The first proposals I've heard from Laclede were sitting here today.

COMMISSIONER DRAINER: Mr. Schwarz, has Staff had adequate time to discuss proposals for changes to the program?

MR. SCHWARZ: No.

COMMISSIONER DRAINER: Then my question is, before I am asked to make a quick decision, which for me at least aging has told me that quick decisions aren't usually my best decisions, is there a way of dealing with that February 15th date and to give you the month of February to have discussions and bring a proposal back or to have witnesses and have a hearing on why it needs to go away versus having just the attorneys give me speeches today and have to bring the witnesses up on short notice with just handouts and asking us to come back by next Tuesday and give a decision?

And if we need to go to other questions, I know we'll have time for a break. Maybe we need to go to other questions. After we break, you can answer that.

MR. PENDERGAST: If we could have a few minutes to think about that and to see if we could come up with a helpful response.

COMMISSIONER DRAINER: And having that as my main question at this point, I would pass to other Commissioners for other questions and ask that after a break you-all tell me how you would answer that question.

MR. PENDERGAST: Very good. Thank you.

JUDGE RUTH: We have been on the record for at least an hour and a half. I think we'll go ahead and take a 15-minute break at this time.

We'll go off the record.

(A recess was taken.)

JUDGE RUTH: Let's go back on the record, please.

We took a short recess and it is now 10:34. Commissioner Murray, would you like to proceed?

COMMISSIONER DRAINER: I think they're going to answer my question.

JUDGE RUTH: That's right. Sorry.

COMMISSIONER DRAINER: Excuse me. Let's finish up with the procedure.

MR. PENDERGAST: Thank you, your Honor. We had some brief hurried discussions during the break here, and, unfortunately, I think I have to report that, based on those discussions, I think the parties are probably in agreement, and, you know, Mr. Schwarz and Mr. Micheel, please stand up and clarify it if I'm putting it inappropriately, but that additional time given where the parties' respective positions are would probably be unlikely to result in much progress towards agreement, and, therefore, additional time for that purpose would probably not be productive.

However, if the Commission would like some additional time to consider the matter or if it believes it needs additional time to gather more information, we'd certainly be willing to talk about a reasonable accommodation there.

We do obviously want to have something in effect sooner rather than later simply so that you have the maximum amount of time to take advantage of hopefully some opportunities that will appear. But if a few additional weeks would be helpful or we can assist in some other way, we'd certainly be willing to do that.

COMMISSIONER DRAINER: All right. Then the final part of this procedurally, I just wish to ask you and the other attorneys because this is a legal point, that the tariff, the Commission basically stated that it retained the right but not the obligation to review the program annually and, if necessary, revise it, revise it to correct any major deficiencies on or before February 15th of each year of the program.

And I would like the position on does that language mean that the Commission has rights to make changes to the program, and is one of the revisions that it can actually eliminate the program? Does that language allow the Commission to extend that far?

MR. PENDERGAST: I appreciate that question, and, you know, obviously the language itself would seem to suggest that what the Commission should be more focused on is revising it to correct deficiencies as opposed to simply eliminating the program in total.

I think our position has been that the program would have to be so irredeamably flawed that it could not be fixed and that ratepayers would be better off without it than with it to even possibly justify that kind of result.

So we think that if there are deficiencies, the appropriate response is to try and revise the program as opposed to just wholesale eliminate it.

COMMISSIONER DRAINER: I'm not sure you answered my question.

MR. PENDERGAST: I'm sorry.

COMMISSIONER DRAINER: Do you believe that your tariff allows us to, with this type of a hearing, allows us the -- that we have the authority to eliminate the program?

MR. PENDERGAST: I do not think it does at this point, and the reason I say that, you'll have to forgive me, but I don't believe that there has been competent substantial evidence presented, I don't believe there has been even informal information presented that would meet the standard under the tariff, which is that it has to have a major deficiency that needs to be corrected that would support that kind of -- that kind of decision.

COMMISSIONER DRAINER: Then would it be your position that the type of competent and substantial evidence that this Commission would have to rely on would call for just as whatever changes to the program, forgive me if I don't quote the right case, but GO-98-484, that we would have to have witnesses, the company and Public Counsel, any -- Staff, any other party that would wish to intervene would have to have the opportunity to do cross on the witnesses?

MR. PENDERGAST: I think that's probably correct.

COMMISSIONER DRAINER: Okay. Thank you. Mr. Micheel, would you respond to that, please?

MR. MICHEEL: Certainly, Commissioner. I think that this Commission has authority to revise the program however it sees fit, and that includes including a revision to end the program as we know it.

With respect to the second question about whether or not a hearing is necessary, that is not my reading of No. 7, the term of the program there. It just says, The Commission retains the right but not the obligation to review the program annually, if necessary revise it to correct any major deficiencies on or about February 15 of each year of the program.

Nowhere in that paragraph does it state that the Commission retains that right to do so after hearing. And the legal standard for a contested case, the magic words for a contested case are after hearing. And the contested case is where all parties get the rights that you're talking about, Commissioner, to present witnesses, to cross-examine witnesses, and things like that.

And to me, and this is off the cuff, but I don't see the words after hearing, which means the whole panoply that you get in a contested case hearing. So it would be my view that this proceeding is enough and that the Commission can, if it sees fit, revise the program how it sees fit based on the information it has or no information.

COMMISSIONER DRAINER: So because you-all agreed to that language, even the Public Counsel, any changes that we would deem appropriate you would have to accept because -- and would not say that you needed to have had more evidence on the record, because you'd say -- you're telling me there's no after hearing and we could do what we want.

MR. MICHEEL: Well, again, Commissioner, this is without doing any of the legal research, and obviously I'm retaining all my rights to do the legal research. I'm telling you --

COMMISSIONER DRAINER: So you're really telling me that this is -- you are -- this is your opinion at this point, but it's not firm?

MR. MICHEEL: Yes. And I would point out that that language that you have in there was drafted by Laclede Gas.

COMMISSIONER DRAINER: Okay. Thank you. Mr. Schwarz?

MR. SCHWARZ: Well, I would begin with a reference to the tariffs. What we have is an Experimental Price Stabilization Fund. That's how it's titled in Laclede's tariffs. So it's an experiment. It's not a final product. I don't think anyone has a right to expect that it's a final product.

The parties included in -- or Laclede included in its final proposal in GO-98-484 the tariff language that's in paragraph 7 on sheet 28G which gives the Commission the right to amend the proceeding.

But I'd ask you to consider further, what do you consider the program? If you consider the program really to be an experimental price stabilization fund, Staff is not proposing that that be eliminated. Staff is not proposing that Laclede should do no -- take no price protection steps or efforts on behalf of its customers.

What Staff is saying is that the particular terms of the current program which put the price protection function in opposition to the profit motive of Laclede Gas Company, it is that aspect of the program that should be eliminated.

So that, if you will, you should surgically remove those portions of the program that put in opposition the interests of the consumer and price protection with the interests of Laclede in profiting from providing that protection. So Staff is not suggesting that the --

COMMISSIONER DRAINER: Then what changes are you asking us to make or to direct Laclede to make to the Tariff Sheets 28E, F and G? What are the language changes that the Staff is asking us to make to those tariff sheets?

MR. SCHWARZ: I hesitate on the fly. I mean, I worked for years on tariff language, and I will tell you that --

COMMISSIONER DRAINER: Well, you're asking us to make a decision by February 15th.

MR. SCHWARZ: I understand, and I would say --

COMMISSIONER DRAINER: Well, no, you don't, because you haven't brought me what changes you're asking us to make.

MR. SCHWARZ: I haven't finished my answer either. I'm just cautioning that I haven't examined the tariff particularly. I think the elimination of paragraphs 3 and 4 in -- or sub 3 and 4 under the program, which would eliminate the profit conflict with the price protection, is basically what the Staff is seeking.

I have not read the tariffs closely enough to consider any other language changes, but clearly what Staff is proposing is the elimination of the profit drive and also modification of the idea that at any particular point in time you can determine what needs to be done to meet the market, that is saying that you have a fixed percentage of volumes at a fixed price for a fixed cost.

We think that needs to be modified, too. I can't tell you just off the top of my head where the --

COMMISSIONER DRAINER: And Mr. Sommerer, if you were put under oath, tell us what changes you'd want to the tariff sheet.

MR. SOMMERER: Should I take the stand?

JUDGE RUTH: Yes, please.

(Witness sworn.)

JUDGE RUTH: Please be seated and state your full name for the record and your position.

MR. SOMMERER: My name is David Sommerer, and I'm the Manager of the Procurement Analysis Department at the Missouri Public Service Commission.

It's the Staff's policy that the program be terminated. Therefore, the only necessary tariff language that would need to be retained is any ultimate reconciliation of the funds that are already spent for the current winter.

Staff would propose that paragraph 6 be retained. That has the reconciliation language where it's carried over to the ACA and reviewed. We would not object to continuing paragraph 5, which allows for carrying costs to the extent there are differences between what's spent and what is received through this rate that the company has. That's Staff's position.

COMMISSIONER DRAINER: Thank you, Mr. Sommerer. Mr. Micheel?

MR. MICHEEL: Yes.

COMMISSIONER DRAINER: Does the Office of the Public Counsel have tariff language on their proposed changes to --

MR. MICHEEL: Certainly. It is our view that Sheet 28F, which is the sheet that contains the description of the Experimental Price Stabilization Fund and the incentive portions, should be out. I don't disagree with Mr. --

COMMISSIONER DRAINER: Excuse me. So it would be paragraph 3 would be eliminated?

MR. MICHEEL: Yes. Paragraph 4 would be eliminated.

COMMISSIONER DRAINER: Okay.

MR. MICHEEL: I don't disagree on 28G that we need to keep the carrying costs and the reconciliation portion.

And I think we probably would need to create some new tariff language, Commissioner, that indicates that the program was going to go forward for the third year on what I would call the insurance type basis where there is no profit incentive and certainly --

COMMISSIONER DRAINER: Go back to 28E then?

MR. MICHEEL: Yes.

COMMISSIONER DRAINER: So you would basically be going back and piffling one of the canceled tariff sheets on the original program and having that language reinserted?

MR. MICHEEL: Yes. I would have to look at those canceled sheets, Commissioner, and obviously I'd want to do that in concert with the Staff and Laclede, but we're proposing that the program go on without the incentive features of the program.

COMMISSIONER DRAINER: Thank you. I have no other questions.

JUDGE RUTH: Mr. Sommerer, you may step down.

MR. MICHEEL: Commissioner, there's one other thing that would need to be stricken. I'm sorry. If I may answer. There was the highly confidential letter that more fully described the program that was in the Commission's file, and I guess that would need to be modified to take out -- you know, it would still state what the required price protection was, but it would take out the sharing grids and those things. So that would also need to be modified.

COMMISSIONER DRAINER: And you could file with the Commission by three o'clock -- wait. Today's Friday. I was going to say three o'clock on Friday. But Monday you could file revised tariff sheets as you believe they would need to be worded to be placed into effect for the last third year?

MR. MICHEEL: I'd be more than willing to give it a shot.

COMMISSIONER DRAINER: Thank you.

JUDGE RUTH: Now we'll move to Commissioner Murray.

COMMISSIONER MURRAY: I guess this question would be directed to both Staff and to the Office of the Public Counsel, and I would direct it to the attorneys because I believe this is something that I want to know from a legal standpoint.

The flaws that you are alleging exist with the program as it is currently in place, are those flaws any different than what you argued when that program -- as it exists with the changes that were made in the last tariff, are those flaws any different than what you argued before this Commission at that time? Either one. I mean, I'd like to hear from both of you.

Are you raising anything new that we did not decide when we approved it?

MR. SCHWARZ: I do not believe so. I believe that we identified flaws in Case GO-98-484 that we perceived in the design of the program. I think that, like any other experiment, that we now have some observed behavior, some observed results, and we think that the observed results verify the problems that we perceived in the design phase of the program.

So, no, I don't think that we're advancing any arguments particularly that we didn't advance in GO-98-484.

COMMISSIONER MURRAY: So from at least Staff's standpoint, you are just relitigating the same issues?

MR. SCHWARZ: I don't -- I certainly wouldn't characterize it that way. It may appear that way. We think that, you know, part of the purpose of any experiment is you put something in place, you make your observations, and then you compare the observations to the experimental design.

We think now we're in that latter period, and I think that the empirical data supports the observations that were made at that time.

COMMISSIONER MURRAY: And I'll get to you in a moment, Mr. Micheel. But then in relation to that you are saying, and Mr. Sommerer just stated on the stand, that Staff's position is that the entire program as it exists should be discontinued?

MR. SCHWARZ: Staff -- and I don't understand Mr. Sommerer to have said that Staff opposes the company taking steps to provide price protection to its customers. I think certainly that we don't believe that that price protection should be obtained under the conditions and procedures described in the current program.

COMMISSIONER MURRAY: So basically what you would be saying is go back and take Staff's original position that was argued at the last time this Commission approved -- I don't have that date before me, but the last Report and Order from this Commission and the last tariff that was approved by this Commission, with Staff's recommendation and OPC's recommendation that that tariff complied with the Commission Order?

MR. SCHWARZ: I'm sorry. I didn't --

COMMISSIONER MURRAY: I'm sorry. That went on too long. I can understand why you didn't follow it.

Basically, then, what you would be saying is you want us to go back to where we would have been had we accepted Staff's argument in the previous case?

MR. SCHWARZ: I believe that that's correct. I'd defer to Mr. Sommerer as to exactly what Staff's position was.

COMMISSIONER MURRAY: And I don't think Mr. Sommerer needs to come to the witness stand. He's already been sworn, so --

MR. SOMMERER: Yes, the Staff's position on the original case was a buy and hold strategy, continue the existing program, and we didn't want to encourage the Commission to make a policy statement that Laclede should diversify its portfolio. That was part of Staff's original position.

The Staff's position in this case is for the Commission to order Laclede to take a similar approach that was set out in the MGE case in October where I believe the Commission said, and I know you dissented, that --

COMMISSIONER MURRAY: Thank you for remembering that.

MR. SOMMERER: Yes, I do. That MGE should go ahead and take steps to hedge and evaluate those business decisions on a going-forward basis without any preapproval.

COMMISSIONER MURRAY: Okay. Now I'm going to move to Mr. Micheel.

MR. MICHEEL: Thank you, Commissioner.

Indeed our position is a little different than our position in the underlying case, which was GO-98-484. In GO-98-484 we took the blanket position that the Commission should not allow the profit motive to infect this insurance program.

As I spoke here today in my opening statement or our initial arguments, I talked about major deficiencies that we saw in the current program. One of the major deficiencies that is different than an issue we raised in the 484 case is the ability of the company to opt out in that 90-day window.

And as you'll remember my opening argument or statement in this case, I recommended that if the -- if the program go forward, that the Commission strip out that 90-day window, and that allowing that 90-day window is a major deficiency in the current program.

And the reason I said that was a major deficiency is, when the market goes against them and they have some down side risk possibility, Laclede gets the opportunity to opt out of that window and then essentially, I think, and Mr. Neises agreed, that all the risk is off of the company there.

So our position from 484 to this case is different, Commissioner.

COMMISSIONER MURRAY: You did not oppose the 90-day window then in the prior case?

MR. MICHEEL: Not specifically, no. We said there should be no profit motive in the case. Okay. A blanket no profit. This is specifically saying this program as designed has this 90-day window, and it's in the attached letter, the highly confidential letter, and that should be done away with. So that's a specific difference.

COMMISSIONER MURRAY: Okay. As a follow-up to that, you heard Mr. Pendergast today indicate that the company was willing to look at that window and perhaps shorten it.

Has the Office of the Public Counsel considered talking with the company and seeing if there can be some arrangement that could be established in terms of a window that would be acceptable to Public Counsel?

MR. MICHEEL: Commissioner, I'm always willing to talk with companies. I settle more cases than I litigate. But I can tell you candidly that from the beginning the Office of the Public Counsel does not believe and still does not believe that there should be a profit incentive in this insurance program.

So if we're ordered to do so, we certainly will sit down and talk with the company. With respect to the proposals that Mr. Pendergast offered up here today, this is the first time, first opportunity that I've heard those proposals, and so certainly we're willing to consider those.

COMMISSIONER MURRAY: Thank you. I'll move on to the next Commissioner.

JUDGE RUTH: Commissioner Schemenauer.

COMMISSIONER SCHEMENAUER: Thank you, your Honor. I think I have a few questions maybe for Mr. Neises, and I think you can stay there. You've already been sworn in.

And I'm trying to get clear in my mind the operation of the hedging program for the options program. When you buy a contract in natural gas, is that like pork bellies, is it 10,000 CCF or 10,000 MCF? Is that --

MR. NEISES: Yes.

COMMISSIONER SCHEMENAUER: It's 10,000 CCF?

MR. NEISES: That is correct, I believe. MMBtu as opposed to a CCF.

COMMISSIONER SCHEMENAUER: So it would be 10,000 MCF?

COMMISSIONER SCHEMENAUER: MMBtu.

COMMISSIONER SCHEMENAUER: Okay. MMBtu. You indicated that the premium escalated from the 7, 8 cents it was up to over a dollar?

MR. NEISES: At times. I mean, it's fluctuating dramatically. In today's market, it fluctuates at levels that we had never experienced before.

COMMISSIONER SCHEMENAUER: In December I see it went up to $2.15.

MR. NEISES: Yes. I mean, it depends upon your -- if you're in -- if at any given point in time you're in the money, at that point in time the option -- the cost of acquiring an option is very high.

It becomes -- and if the option -- it can be penny for penny at that point in time in terms of the type of gain that you made, you would have realized. I mean, you have to effectively pay, be paying for that in the money option.

COMMISSIONER SCHEMENAUER: When you buy contracts, I mean, you're actually buying an option to take delivery of that amount of gas?

MR. NEISES: Yes. If you're buying the contract as opposed to a call option, yes, you're actually --

COMMISSIONER SCHEMENAUER: So you didn't actually buy contracts; you bought call options?

MR. NEISES: That is correct. We did not buy contracts.

COMMISSIONER SCHEMENAUER: So you didn't buy any contracts at all?

MR. NEISES: No, we did not, because under the program, the program is strictly limited to call options.

COMMISSIONER SCHEMENAUER: And is that a wise limitation to limit it to call options? I mean, wouldn't it have been wiser to have a mix?

MR. NEISES: My belief is, yes, that I would prefer greater flexibility. But when you start talking about buying the contract, you do introduce a host of other issues that it maybe becomes more complicated, because when you're buying the contract, then you are potentially subject to margin calls.

COMMISSIONER SCHEMENAUER: Right.

MR. NEISES: And those margin calls in an extremely volatile market, as we have experienced this past year, can be extremely significant. And indeed what we saw on the market, you could see on days when there were, you know, significant margin calls taking place there was a lot of selling taking place to cover.

And so it becomes very, very risky, but at the same time, we are advocating in a filing which you currently have before this Commission in connection with our Gas Supply Incentive Plan, to begin an experimental program that would allow us to gain more experience with buying the contract because it is a way of fixing prices.

So we're not adverse to moving in that direction and adding that component to an overall hedging program.

COMMISSIONER SCHEMENAUER: But if you bought a contract for $5 and the market was escalating, would you experience a margin call?

MR. NEISES: No.

COMMISSIONER SCHEMENAUER: Okay. Just if the market's going down?

MR. NEISES: That is correct.

COMMISSIONER SCHEMENAUER: That's the way I understand it. Okay. So now this -- from hindsight, if you would have purchased contracts at $5 or $6, you would not have had any margin calls?

MR. NEISES: In hindsight, I think that's generally true, yes, because the market was escalating upwards. We have had very few decline. We have not had any decline since last May where we've been down to those kinds of levels.

COMMISSIONER SCHEMENAUER: And I know it's always easier to see what kind of strategy you should have used after the time period has passed.

I'm trying to -- you said $28 million was your gain, and if all that flowed through to the ratepayers, it would only amount to 11 cents per CCF?

MR. NEISES: Yes. We could reduce our rates from -- they're currently 91 cents, and we could reduce them to 81, about 80 cents.

COMMISSIONER SCHEMENAUER: So on $10 gas, it would go down to 8.90, 8.80, something like that?

MR. NEISES: That's correct.

COMMISSIONER SCHEMENAUER: So the call, you know, the program that you're in, when the market gets so high, the savings that you achieve overall isn't very much, and nobody expected the price to get to $10. I know that.

But your preference would be to have the ability to have a mix in your portfolio of purchasing contracts, call options, callers, and I don't know if you use puts or not, but a mix to give you better -- not to give you, but to give your consultant a better strategy opportunity?

MR. NEISES: Yes. I think in -- you know, ideally, I think that those -- that one does need these arrows, additional arrows in your quiver to do an effective risk management program.

COMMISSIONER SCHEMENAUER: And I think one last question. Your consultant is Risk Management, Inc. or Goldman Sachs?

MR. NEISES: It's Risk Management, Inc. out of Chicago. They do extensive consulting in commodities.

COMMISSIONER SCHEMENAUER: Are they affiliated with you in any way?

MR. NEISES: No.

COMMISSIONER SCHEMENAUER: You don't own any shares in their company?

MR. NEISES: None whatsoever.

COMMISSIONER SCHEMENAUER: Do you know, the large industrial users that purchase gas on their own, I mean, I know they all have consultants. Do you have any idea what their experience has been this winter? Did they purchase hedging contracts? Did they buy their gas ahead of time?

MR. NEISES: Industrial, some do in terms of natural gas. I mean, I certainly read in the press. I only know from what I've read in the press. They do, and, of course, they know precisely -- in industrial, they know precisely how much they're willing to risk and how much they're willing to pay. They can make that determination and they live with it. They have no regulated body after the fact to decide, well, was that a good decision or not. I mean, they live with it.

Some certainly have to -- I know that some industrials had to hedge their gas this past winter, and indeed to the point where they made profits to the point where it was better to just take the profits and shut the business down this past winter, which will obviously have ripple effects throughout our economy as we go forward.

COMMISSIONER SCHEMENAUER: But I guess their incentive is to decrease their exposure to a market that has gone, it looks like it's going way up?

MR. NEISES: That's right. It's the same -- it's the same problem that we face.

COMMISSIONER SCHEMENAUER: And if I were an industrial user and in December I bought $5 gas for January and February and the price went higher, I've saved my company some money, but if the price had decreased, then I would have lost some money because if gas would have dropped to $3 and I had $5 gas, I'm going to have to pay for that $5 gas?

MR. NEISES: That's correct.

COMMISSIONER SCHEMENAUER: Okay. I think that's all I have. Thank you.

JUDGE RUTH: Commissioner Simmons, would you like to ask a question?

COMMISSIONER SIMMONS: Yes. Thank you, your Honor.

My first question goes to Laclede. Mr. Neises, I gathered through your earlier testimony that you helped construct this program; is that correct?

MR. NEISES: Yes, I did.

COMMISSIONER SIMMONS: As you constructed this program, was this the first one in the state of Missouri or the first one in the country?

MR. NEISES: I would say that it certainly was the first in the state of Missouri. There have been some incentive programs in other states with respect to risk management, but I can't say that it was identical to what we were proposing or have proposed here.

COMMISSIONER SIMMONS: So the program that you put in place was one that you developed yourself, you did not look at other programs and other parts of the country to construct this program?

MR. NEISES: We had -- I know we had looked at -- there were several others. I know there was one on the east coast and another program that I don't recall the state that we had looked at, yes.

COMMISSIONER SIMMONS: As you looked at those programs or as you looked at those programs carefully or closely, did you find that those programs had profit or incentive components in those programs?

MR. NEISES: Yes, my recollection was that those did.

COMMISSIONER SIMMONS: Were you aware of any of those programs that did not have a profit or incentive mechanism in those programs?

MR. NEISES: I really -- I'm sure there were some, but the reality is that most local distribution companies in the United States have not had hedging programs at all, and hence that is why you see prices -- why you see the problem that we have today is that most LDCs in this country have not been hedging and, therefore, it's becoming a very lively issue these days.

COMMISSIONER SIMMONS: Earlier you spoke about the $28.5 million, and I believe you talked about where that money is currently. What did you say or where did you say that money is?

COMMISSIONER SIMMONS: Well, the company -- the gains are being held by the company and is reflected on our -- in our accounts.

COMMISSIONER SIMMONS: And with --

MR. NEISES: But not on our -- they're not on our income statements or anything like that. They're presently being held for disposition in accordance with our tariff.

COMMISSIONER SIMMONS: And as they are being held, are they invested in any way kind of way? Are they invested in any way?

MR. NEISES: I'm not sure I can answer that question. I think that they -- I can't answer that question because that department is not under my supervision.

COMMISSIONER SIMMONS: I guess I'm getting to the point of trying to figure out if the $28.5 million is probably larger than $28.5 million if it had been invested in some form or fashion, and you don't have any knowledge of that?

MR. PENDERGAST: If I could address that?

COMMISSIONER SIMMONS: Sure.

MR. PENDERGAST: We don't have a special escrow fund that we put it in where we --

JUDGE RUTH: Would you repeat your answer using the microphone, please?

MR. PENDERGAST: I'm sorry. We don't have, to my knowledge, any kind of special escrow fund or anything of that nature that we put it in, but there are two things to note about it. No. 1, under the tariff we are required whenever there is a gain and it's under the carrying cost section, I believe, to go ahead and credit for the customers' benefit later on an interest charge, and I think it's prime minus one.

And, of course, temporarily while we have those gains it does enable the company to have some ability to offset some of its cash requirements. I think right now we're about 210 or $240 million out in short-term debt just trying to finance these huge gas purchases, and that does have a tendency to at least temporarily help us.

COMMISSIONER SIMMONS: Could you remind me if the $28.5 million was -- if the program was discontinued, where that goes or how that's distributed?

MR. NEISES: And I have not run the specific calculations because, as I say, this program isn't over until the end of February. But based on the dollars that we have today, roughly the 20 -- under the tariff, $20 million -- approximately $20 million, I believe, would be flowed through to our ratepayers, and $8 million would be eligible to be retained by the company.

COMMISSIONER SIMMONS: Okay. Next line of questions, Public Counsel. Earlier we talked about design flaws and the 90-day window. I think that you discussed, Mr. Micheel. I seemed to get the impression that the 90-day window was a problem.

Are you saying that there is a time frame that is more acceptable? Are you saying that that 90-day window is just totally unacceptable and there are no other days that you would look at? What do you mean by that?

MR. MICHEEL: What I'm saying, Commissioner, is what the 90-day window does is allowed Laclede to shed any risk in this program. And we talked about the whole idea of the incentive program is share the risk of increasing gas costs between the company and the ratepayer.

And the reason that we're objecting to the

90-day window now is it's clear that when you have an increase in market price like we had this winter, Laclede can note that and shed that risk, leaving the entire risk to be borne by the ratepayer.

And so I'm saying if we're going to give a true incentive where there are both risks and rewards to the company, then we need to give the company that risk.

COMMISSIONER SIMMONS: And again, do you see a time frame that's more receptive to what you just said?

MR. MICHEEL: Any time frame that you give the company, Commissioner, will allow the company to shed that risk and force it all down upon the captive customer.

And if I may, Commissioner, just to follow up, Mr. Neises indicated that their hedging program was the first hedging program in Missouri, and that's incorrect. Years ago AmerenUE, a natural gas company, came in, and this Commission approved a hedging program for them, and I think MGE's hedging program was approved prior to Laclede's.

But this is the first incentive hedging program, if that's the context that Mr. Neises was answering in.

COMMISSIONER SIMMONS: Okay. Thank you, sir. This question is for Staff. We're noticing today that Staff's position is to terminate this program, and I guess I'm going to ask this question. As you talk about terminating the program, are you saying that you want to close the door on this program indefinitely or do you see the door being opened at some other time if the Commission were to take a position to terminate the program?

MR. SOMMERER: I think that Staff is always open to improvements and new ideas. The current position obviously is that we think the company would have a lot more flexibility if it knew that we would evaluate fixed costs, fixed rate contracts and hedging the same way we do index pricing or spot market pricing. We'll take a look at it in a prudence review and just give the company the authority which we believe it already has to make the decisions in a timely way without any preapproval.

But we're always open to any programs we see out there from this state or other states that may benefit the customer.

COMMISSIONER SIMMONS: My next question may have already been asked or alluded to by one of the other Commissioners, but if we are indeed looking at this from not closing the door and the door could be open, is there a reason, other than what the tariff says, why we can't work together on trying to put something in place that may be more acceptable other than the February 15th date that it seems that we're under the gun for right now?

MR. SOMMERER: I think Staff is concerned that if nothing happens prior to February 15th, the third year of this program will continue as designed in the tariffs and will still have the profit incentive, will still have the 90-day window, will still have the ability for Laclede to make what we believe are more speculative sales early on rather than holding these options until they close, and so that would be the concern is, if there is no action, then we'll be looking at year three of this program.

COMMISSIONER SIMMONS: Last question for you. Have you at any point in time had an opportunity to look at other programs across the country and make any type of evaluations or determinations of whether or not those programs are models or whether those programs are very good programs and, if you had it your way, we would look at trying to do the same thing in Missouri?

MR. SOMMERER: One of the programs that we're trying to get additional information on is Kansas Gas Service Company. They have a what I believe is called option program where there's an amount of money that is allowed, and we want to see how that's operated this year and try and get some more details on that.

COMMISSIONER SIMMONS: That's all the questions I have. Thank you very much. Thank you, Judge.

JUDGE RUTH: Chair Lumpe, would you like to ask a question?

CHAIR LUMPE: Yes. For Mr. Neises, are you aware of any of the transportation companies in Missouri that -- or in your territory that have closed down and sold their gas as we've heard in other -- as I've heard about in other states? Are you aware of any that -- you alluded to that some of them have made more money by closing down. Are you aware of any of your customers?

MR. NEISES: I have a recollection -- it was not one of our customers, but my recollection is that there was an article I read in the Wall Street Journal, I believe, about a company in, I thought it was in southern Missouri where that had happened, but they were not a customer of ours.

CHAIR LUMPE: I had heard about three companies in Iowa that had done that, and they were able to shut down, pay their workers and still make more money than if they were producing the product. I was just curious whether you had any of those customers, but you are not aware of any?

MR. NEISES: I'm not aware of any. I think another point in that same vein is that while some companies found themselves in that position and were, I guess, lucky, a lot of companies also find themselves in the same position in terms of industrial. Utilities are competitive, and they're paying these very high prices, and -- but also they're fortunate that they have an alternative fuel. When prices got up in the 6.50, $7 range, they shifted off to No. 2 diesel.

CHAIR LUMPE: Is there any incentive for companies to become transportation companies and try to go buy their own in markets such as this? In other words, could you be losing customers because they would say, Well, we're paying too high there, we'll try it on our own?

MR. NEISES: I suppose so. However, from our general experience has been that we still buy gas as efficiently as anybody out there, and the only advantage they really have is the fact that they escape the taxes, the state taxes.

CHAIR LUMPE: Which may be a big advantage.

MR. NEISES: Exactly. In today's environment, it's a very big advantage.

CHAIR LUMPE: Would you just answer for me, and I probably should know this, the 28.5 million, what generated that 28.5 million, what investments, what --

MR. NEISES: I think that is an excellent question, because I don't think that that's fully appreciated in this room.

Essentially what generated it was the very concept that brought us here in the first place several years ago when we instituted this program. We had been operating under a buy and hold kind of program that Mr. Sommerer alluded to and would prefer to go back to, which is simply once you buy the option you hold it until liquidation.

We changed that in this program. Our argument was that the company should have the ability to exercise its judgment while it is holding an option to sell that option and take its profits or gains and share those gains when that happens with its customers and its ratepayers and its shareholders, and that's what we did.

When we saw -- when we were holding an option and the value of that option, we may have paid 10, 15 cents for that option, and when the price -- when the value of that option, let's say it could have been 30 days or 20 days or whatever prior to expiration was worth 2, $3, I had a decision to make; do I take my 2 and $3 right now for my ratepayers. And I had that ability in this program, take the gains right now as opposed to risking those gains which could -- which if the prices come down, we -- the ratepayer would lose. The option could expire, worthless.

So we exercised our judgment, and believe me, this was -- we were in effect, throughout this winter, we were -- the stress and the day-to-day decision-making that we had to undergo was tremendous.

We would come in every day and watch the value of these options, make judgments as to what is happening, is the weather remaining cold, are the fundamentals there that are going to see this option continue to increase in value, or is it such that we're seeing the weather looking 15 days out and seeing a warming trend feeling, Well, what can happen here is the value of these options could reduce, and so, therefore, get out.

We were successful in doing that. That's where the $28 million --

CHAIR LUMPE: From the ability to sell within the last three days?

MR. NEISES: No. It's the ability to sell prior to that.

CHAIR LUMPE: Prior to the last three days of the options?

MR. NEISES: When we're making -- yes. Exactly.

CHAIR LUMPE: Yeah. I really wasn't quite sure where you had generated that total amount from.

Okay. Thank you.

MR. NEISES: Now, excuse me. Some of it was, not the total 28. That was the 17. Some of it was generated because we made the decision to hold it to the very end, and when we held it to the other end, that fell into the other category.

CHAIR LUMPE: Okay. Thank you. That's all I have.

JUDGE RUTH: Vice Chair Drainer?

COMMISSIONER DRAINER: Okay. First of all, it just came to me. Mr. Neises, this program is -- if it needs to be in-camera, tell me. But when we approved this program, did we approve it for a hundred percent of your buying of gas for the winter months or is this just a percentage of your overall purchasing?

MR. NEISES: The program was designed to cover 70 percent of our flowing gas, which excludes the storage volumes which makes up about a third of our gas supply.

COMMISSIONER DRAINER: So it's a third, about a third?

MR. NEISES: In the winter months, yes.

COMMISSIONER DRAINER: Okay. Now, let's talk about what this program's done for the last year, then, and let's look at the 28 million profit again. About 8 is the company's, you said, of that 28. 8 million is the company's profit?

MR. NEISES: As the tariff is currently written. And as I have said, the company is willing to take those dollars and invest them for the future in this program.

COMMISSIONER DRAINER: Now, the 20 million that go then -- approximately that goes back to the customers goes back at the end of the ACA period at the end of the year, correct?

MR. NEISES: That is correct, under the tariff.

COMMISSIONER DRAINER: That's part of the reconciliation is this money will go back to the customers on the ACA factor.

If you had not had this program, would -- can you tell me that, in your opinion, would the customers have a $20 million reduction in their rates?

MR. NEISES: I do not believe they would.

COMMISSIONER DRAINER: Would they through this past year have experienced more than a $20 million reduction in their rates?

MR. NEISES: I do not believe so.

COMMISSIONER DRAINER: You do not believe your buying practices would have resulted in savings to the customers in more than $20 million?

MR. NEISES: All other things being equal, no.

COMMISSIONER DRAINER: Thank you.
Mr. Sommerer, as the expert witness for Staff --

MR. SOMMERER: Yes.

COMMISSIONER DRAINER: -- do you disagree with Mr. Neises that the customers are going to receive approximately a $20 million reduction in their ACA factor at the end of this period?

MR. SOMMERER: I believe the Staff would say that it should be $28 million. We have a disagreement about whether the profit should go to Laclede. But given that, given that issue, I would say that certainly at least $20 million in the ACA.

COMMISSIONER DRAINER: That's the way the program's set up, correct?

MR. SOMMERER: That's right.

COMMISSIONER DRAINER: So you don't refute that that's the way the program's set up and they will receive the 20 million?

MR. SOMMERER: And we would -- we retain the right to disagree with the company on the additional 8 million.

COMMISSIONER DRAINER: Well, answer my question first and I'll give you a chance to go further. Okay?

MR. SOMMERER: Sure.

COMMISSIONER DRAINER: Okay. So then can you tell me as an expert witness for Staff that, without this program you believe that Laclede's buying practices without the program would have resulted in adjustments to their PGA or the ACA that would have resulted in greater than

$20 million?
MR. SOMMERER: Yes, I am convinced of that.
COMMISSIONER DRAINER: And what would be the amount that they -- that the customers would have saved greater than 20 million?
MR. SOMMERER: I believe approximately $44 million in addition to the 20 million.
COMMISSIONER DRAINER: And that 44 million would have gone back to them in what part of their bill?
MR. SOMMERER: I think it would have, the way that the tariffs are written, would have flowed back through the ACA.
COMMISSIONER DRAINER: It would have flowed back through the ACA, which is adjusted annually, correct?
MR. SOMMERER: That's correct.
COMMISSIONER DRAINER: All right. Well, we have -- so you're telling me at the end of this year, Staff would have done a prudency review that would have looked at their buying practices and would have said that there needed to be a $44 million reduction?
MR. SOMMERER: The results of the review aren't complete, but I think that certainly is a potential.
COMMISSIONER DRAINER: Tell me why.
MR. SOMMERER: Because we believe that Laclede had the opportunity under this program to lock in at strike

prices.

COMMISSIONER DRAINER: Excuse me now. We're not talking -- this program's gone.

MR. SOMMERER: Okay.

COMMISSIONER DRAINER: Because you're asking me to get rid of this program. So I'm saying if there had not been this program. I mean, what I know as a fact that you haven't refuted is that the customers will receive a $20 million reduction in the ACA at the end of this year, more or less, and you've agreed with that.

Now, I'm saying that -- and Mr. Neises has said that he believes without this program there would have been less, that he could not have told me they would have received that profit.

Now, what I'm asking you is, without this program, what would have been the -- what would be the adjustment to the ACA? And you told me 44 million without the program.

MR. SOMMERER: That's correct.

COMMISSIONER DRAINER: So don't talk about the program and strike prices and all that because that doesn't exist anymore.

MR. SOMMERER: Right. If the company would have put ceilings in their gas contracts, which are similar to call options, it certainly is an alternative, then they could have obtained those ceilings, I believe, at similar prices that were available in the market, in the call option market, in February, March and April of the year 2000.

Had they made that decision to diversify their portfolio, to put some limit on the gas index that's embedded in their gas supply contract, it could have resulted in $44 million worth of savings.

COMMISSIONER DRAINER: And so is it your position that they have been imprudent in their buying practices because of having the PCS or PSP to protect them?

MR. SOMMERER: We want to look at all the facts and circumstances, and we don't have all the data in from other states or other LDCs, and I think that's one of the issues we want to look at is what were available, what were other LDCs doing, what would reasonable people have done given the facts and circumstances at the time they made the decision.

But at this point we do believe there's a very strong argument that Laclede could have had a great deal more savings with reasonable -- reasonably available purchasing practices.

COMMISSIONER DRAINER: Is it your position based on the information you have on Laclede and other companies in Missouri that Laclede has acted less prudently in what its ACA adjustment would be because the others do not have that? Do you want to answer that, Mr. Schwarz? Please do.

MR. SCHWARZ: Laclede is operating under the PSP this year. Its actions must be gauged under the PSP this year. So that it's kind of the flip of your earlier comment to Mr. Sommerer. We can't judge them as though they were outside the PSP for the current heating season. We have to judge them according to the terms of the PSP for this year. So that will be something that is taken into account.

COMMISSIONER DRAINER: Well, I understand that that's what will have to be taken into account as far as the actual ACA, but what I'm asking, because I'm being asked to eliminate, that I have to look -- you're asking me to look to the future, and that their actions have resulted in $20 million. It could have been more.

And if I get rid of this, then what you're expecting is that, instead of potentially a 20 million profit to the ratepayers, it would be, you said 44 million. So it's almost double. I mean, it's double, that their buying practices and their behavior in the market you're expecting to result in greater savings through an ACA review?

MR. SOMMERER: Given the evidence that I've looked at to date, that's correct.

COMMISSIONER DRAINER: All right. Thank you. And then I would like either Mr. Neises or Mr. Pendergast to respond to that.

MR. PENDERGAST: I'd like to respond first. If Mr. Neises would like to say something --

JUDGE RUTH: Could you move the microphone to you, please?

MR. PENDERGAST: I'll try and respond first, and I think you just had a demonstration of why utilities are so reluctant to go out and make decisions without firm parameters to guide how those actions and results of those actions will be determined.

We're essentially being accused here of being imprudent for not having gone out and purchased gas in March and April, that's what Staff's calculation was based on, at prices that were well in excess of $4, $4.50, $4.70.

At that very time, Staff had negotiated an arrangement with another LDC where it was saying the most reasonable trigger price we can come up with right now is $2.50. Staff had just gotten done about a month before criticizing the company because we had gone out and bought call options at $4 an MMBtu, and at that point, less than a month later we were forced into having to buy them at 4.70 if prices didn't decline.

I think it's just absolutely untenable to have those kind of careless accusations thrown about by somebody and by a staff that was completely unwilling to recognize the reasonableness of any prices higher than 2.50 or any prices higher than $4.

COMMISSIONER DRAINER: All right. Thank you. Did Mr. Neises have anything to respond to?

MR. NEISES: The only thing I would add to that, I totally agree with Mike on this point. But as the man who is in charge of gas supply during this period, I have to say that during the period from March through April, that that was part of the 90-day window.

A factor that weighed very, very heavily on my mind for not buying options at that point was the fact that just two months before a Staff recommendation was made and said that we shouldn't -- we were criticized for buying options at $4 strikes the year before.

Well, now I would have had to buy strikes or options at 4.70 to 5.20, which was in excess of what we had just been criticized for buying the year before, and I was very concerned about that.

The point I want to make is that the criticisms that are leveled against the company in various recommendations are taken very, very seriously by the company, and so we were very -- I was very concerned about that, that it was a clear feeling at the company that we shouldn't be going out buying strikes up in the 4.50, 4.70, $5 level, and so, therefore, we did hold off.

By the time May rolled around, as I explained in the response to that data request that you have before you, I recognized that something was afoot. I felt that the market was running away, and in a way I think we were -- we felt that far earlier than anybody else. I know that for a fact.

And it was at that point that I directed my staff to begin covering a minimum of 50 percent of our volume, and it was only -- and it was within -- and we started, and we didn't get a lot done because the market ran away. It ran so rapidly after that that we couldn't get it done. And that's all I have to add.

COMMISSIONER DRAINER: Would your behavior or your judgment in managing the purchase of gas have been any different without this program?

MR. NEISES: If we had not had the program, I am sure that I would have -- I'm not sure I understand the question. Would you repeat the question?

COMMISSIONER DRAINER: Well, you know, Mr. Sommerer made the statement that without the program there would have been a $44 million benefit to the ratepayers and somehow the current program acted as a screen that caused less profit to come back to the ratepayers over this past year.

When you look at your purchasing practices under the program and the profit, you know, hindsight is 20/20, and you know how you operated before the program and you know how you've operated in the program. And in your opinion as the manager, would there have been differences in your decisions?

MR. NEISES: The answer with respect to going into the market in that March/April period, it would have been no different. If we hadn't had this program or if we had the program the Staff would have had in the past, I still would not have gone in the market during that period.

COMMISSIONER DRAINER: Okay. Thank you. And I really have one final question, but before I ask it I really want to ask Mr. Schwarz if he would like to make a comment?

MR. SCHWARZ: I think that both Mr. Pendergast and Mr. Neises mischaracterized the situation significantly. First of all, Laclede was operating under Laclede's program last spring. The market had told Laclede, this is your target strike price. This is a catastrophic strike price. The language is Laclede's. If customers pay this price, it's a catastrophe.

Laclede's program says -- and Laclede behaved perfectly rationally in adhering to the terms of its approved program, but the program itself said, Wait 90 days and see what happens, and at the end of the 90 days you can shed all risk of upward price movement onto the customers and avoid all upward price risk for Laclede Gas Company.

That's what the program permitted them to do, and Laclede acted rationally and within the bounds of the program to do so.

Now, Laclede's gas purchasing department is hired by Laclede, and their salaries are paid by the ratepayers to manage the portfolio for the benefit of the customers. It is perfectly rational for Laclede to want the customers to bear all the risk of upward price movement.

I don't think that you can quibble with the fact that, particularly in the immediate historic circumstances that we've had, that upward price movements are probably sufficient to overwhelm Laclede Gas Company. But if Laclede knows that it's facing those kinds of risks, its behavior will be different than if it is in a position to shed all those risks to the ratepayers.

And that's what we're talking about here today; on a going-forward basis, what is the best way for the management of the customers' risk.

And it's easy to say that the focus today is, in hindsight, what would have happened if Laclede had done this and what would have happened if Laclede had done that, but the plain fact of the matter is that Laclede was operating under the PSP. Its behavior under the PSP was predictable by the design of the PSP and was perfectly legitimate within the parameters of that program.

What Staff is suggesting is that the design of that program is such that the ability to shed all that risk onto the ratepayers is detrimental to the ratepayers. It's not saying that, at least's Staff position isn't, that Laclede should guarantee a $2 price to its customers. What Staff is saying is that Laclede should be bound to manage its customers' portfolio in a manner that a prudent person would manage the risk in that portfolio.

It is the customers' risk, and Laclede is basically the agent of the customers for acquiring that gas. That's what they're paid to do. That's part of the regulatory bargain. That's why there are no competitors. I mean, that's part of the regulatory compact is that Laclede manages that portfolio for its customers.

And what Staff is here today to say is, on a going-forward basis, there is a much better way to manage that risk than the PSP. The PSP by its design shifts risks in a rising market to ratepayers, and Staff doesn't think that that's right, and whatever -- whatever the ultimate outcome of this year's activity under the PSP, we think it's predictable, whether the market goes up or the market goes down from this point forward, that there's a better way to manage that risk.

And the chips are going to fall where they may on the operation of the PSP for this year, and you're not done with that. That will happen in the blessed ACA yet to come. So you'll be revisiting that issue ad nauseam I'm sure.

The question today is what's -- what's worthwhile on a going-forward basis, and Staff's position is that a program that shifts all risk to the customer is not in the customers' best interests.

COMMISSIONER DRAINER: Okay. Let me ask finally just -- again, I look at the time lines, and all three parties here signed a Unanimous Stipulation & Agreement in September to go forward with those changes, and then the Commission approved it in October, and two months later, on December 22nd, the Staff then asked to have just the program eliminated.

And I am talking time line, but I mean, I truly would be surprised if there -- if there was legislation that a position could be given by any party and the Commission had to make a decision based on that recommendation that all parties had to get their information in to the Commission and it had to be decided in 45 days, that rocket docket, that really -- I would be surprised if any party wanted that for everything to happen, for it to be that quickly, and we are talking that quickly on this.

So why in September, instead of a Unanimous Stipulation & Agreement, why didn't you come to us then and say, Whoa?

MR. SCHWARZ: Well, I will speak from Staff's perspective. Between June and September, what we were focusing on is, I don't want to say a bandaid approach, but we're looking at what can be done. The guaranteed price protection for customers that perhaps people might have been relying on earlier in the year has disappeared. What can be done to moderate the possible impacts of the market changes on the effects that are going to impact on customers under the program that we have now in year two of the PSP? What can we do to possibly better the results for this winter?

Now, I'm not here to tell you that what we agreed to turned out to be a panacea, turned out -- I mean, I don't think even then anyone anticipated $9.95 gas for an entire month. But what was done then was an attempt to deal with year two of the PSP. We're in the middle of this thing. We don't have much time. We have to focus on what can be done for customers this year.

That's a different question from the one we're addressing today, which is how do you want to address the similar situation for the upcoming heating season.

COMMISSIONER DRAINER: But I would still ask why -- if you knew you were doing a bandaid for year two, why when you're looking at year three it took to the end of December to come to the Commission and say, The revision we want is to eliminate it?

MR. SCHWARZ: All I can say is the press of other business. I mean, there's been a lot going on, and --

COMMISSIONER DRAINER: Okay. I just -- thank you. I just wondered if you had something more you need to tell me. And I guess just a final point would be that Mr. Pendergast seems to need to respond.

MR. PENDERGAST: Thank you.

First of all, I want to apologize for being a little excited there earlier, and I will try and do better. I --

COMMISSIONER DRAINER: Well, I guess if you will, I will too. So will Tim.

MR. PENDERGAST: I just wanted to say a few, you know, brief words. We've had a lot of discussion about what maybe the company could have done or should have done under various hypothetical scenarios.

And I think it's very important to go ahead and keep in mind that you had three pretty good cases, three pretty good control groups here over the last six months. They're all relatively large local distribution companies, they're all located here in the midwest, and they all were in some way impacted by either having a hedging program or not having a hedging program.

And what you saw with those three companies was one company that went out and, under the incentive program that you approved, took $4 million and converted it into $28.5 million. That would be us.

You saw another company that operated under the approach that Staff had recommended you take, and for whatever reason, and maybe they had good reasons, but decided that either the risks were too great or prices were not such that it was a wise thing to do, wound up with no hedging program whatsoever and, therefore, no hedging gains.

And then you had Kansas Gas Service that did have a hedging program and, as Staff and Public Counsel would suggest, one that I don't believe had an incentive feature. And they wound up, from what we've been able to read in the press, spending 50 percent more than we did and deriving fewer benefits than we did. 20 million is what I heard reported in the press.

And I think if you're talking about experiments and you're talking about giving those experiments their due, when you have three test cases like that and you have the kind of results that I'm sure the people in Kansas -- and I'm sure the people in Topeka would just as soon trade places with our customers when it comes to those benefits. It just seems to us intuitively not to make a great deal of sense to get rid of a program like that, and particularly not at a time like this.

The only thing that has happened since we tried to sit down and negotiate and did come up with that Stipulation and Agreement is we've seen how these three companies' results were achieved and we've achieved $28.5 million worth of benefits for that, benefits which we're prepared to go ahead and give back to our customers in their totality if we can go ahead and make adequate provision for the future.

Thank you.

MR. MICHEEL: Commissioner, I just haven't had a chance to weigh in on this entire discussion, and I'd just like to add my two cents.

COMMISSIONER DRAINER: Okay. We've all said we're going to kind of be calm, so you will, too, right?

MR. MICHEEL: I'm always calm, Commissioner. Calm is what I'm about.

First of all, I think what this shows is -- let's go back to the beginning, and the beginning is 1962 when this Commission approved the first PGA, and then a little further down the line we implemented the ACA, and the whole reason we have the PGA ACA --

COMMISSIONER DRAINER: I really want you, though, to stick to answering the questions I asked. So my first question was with respect to the 20 million, and is it your position that the ratepayers will, with the ACA adjustment, receive --

MR. MICHEEL: Right. I'm answering those questions, but in order to answer that question appropriately, it's important to get the background.

COMMISSIONER DRAINER: But I really -- I know about the PGA ACA process, and I did limit them to some yes/nos and sticking with it. I would like for you to also stick with this year and what you believe. Without this program, would we have had -- in your opinion or your expert witness' opinion, would there have been greater than a $20 million adjustments to the ratepayers' bills?

MR. MICHEEL: Yes, customers are going to receive the $20 million benefit. Okay. But the problem with that is the whole idea of the PGA ACA is that it's going to be a dollar for dollar pass through and this company is not going to have any ability to make a profit on their gas costs.

Okay. So now we enter into all these incentive programs that give the company the incentive to profit when the underlying purpose of the PGA ACA always has been you're going to do the best job possible. And this catastrophe just shows the underlying weaknesses of the PGA ACA clause in general.

As Mr. Schwarz pointed out, my clients pay the salaries of the gas department. I have no doubt that Mr. Neises and his team worked long and hard this winter. I have no doubt that you as a result of this crisis have worked long and hard, and you're not getting any bonuses from the taxpayers. That's your job.

And that's the basic premise of the ACA PGA. They're not supposed to be getting any bonuses. And that goes back to the fundamental problem with this.

The customers should be seeing the $28 million reduction completely, and this company, due to the regulatory bargain that the PGA ACA has given it and the fact that my clients pay their salaries, should be out in that market doing everything prudently possible to get the lowest gas cost for captive consumers.

COMMISSIONER DRAINER: All right. And that would be why your position is that there's a 20 million but, all things being held equal, it should be the entire 28 million. And I guess that would also be why your position would be that the original Stipulation & Agreement that the Office of the Public Counsel signed on, the original did not have that profit margin in it, and you believe that if that were in place, it would have allowed the 28 million to go to the customer?

MR. MICHEEL: Yes. And let's not forget, Commissioner, that that seed money that Laclede took to the poker table, that $4 million, that came from the ratepayers, not from the shareholders.

And one other comment and then I'll be finished. Mr. Pendergast gave the hypothetical of three companies. I think we should add a fourth company into this hypothetical. I think we should talk about the AmerenUE, the third largest LDC in this state that does not have an incentive program and has not come in for an unscheduled PGA filing. We need to ask all of ourselves, why did they do that?

COMMISSIONER DRAINER: Can you tell me what their current PGA factor is?

MR. MICHEEL: I don't have it off the top of my head, but it's well below $9.10 or $9.80. It's $6 and -- $6.80 or something like that.

And I guess my only point is apparently that company has been able to do something in its gas purchasing practices that have allowed it to keep under the threshold for filing one of these unscheduled filings, and they don't have an incentive.

COMMISSIONER DRAINER: Thank you.

MR. MICHEEL: Thank you.

COMMISSIONER DRAINER: Thank you for your response. And before I pass it, then, was there any response to Mr. Micheel since we've allowed everyone before?

MR. PENDERGAST: Your Honor, just very briefly. Mr. Micheel did mention AmerenUE, and I certainly don't want to question anything that they've managed to do, but when I talked about my three test cases, I did talk about them being local distribution companies and not being combination companies with rather large electric assets.

And when it gets back to the issue of what risk you can afford to take and what risk you can't under the parameters of the program, if we take a risk and it turns out badly, it can easily be half of a $25 million net income or even the entire net income.

When your net income's more in the range of $250 million and you have half the gas customers or less than we do, it is a little bit easier perhaps to go ahead and take some risks. Sometimes it may turn out and sometimes it may not, but there is a distinction there.

JUDGE RUTH: Staff, did you have a comment?

MR. SCHWARZ: No.

JUDGE RUTH: Okay. It is 12 o'clock. I think we will break for lunch. We will take an hour and a half and start back up promptly at 1:30.

Off the record.

(The noon recess was taken.)

JUDGE RUTH: Let's go back on the record, please.

We're continuing the Laclede hearing. It's 1:35, and we will start back up with some questions from Commissioner Murray.

COMMISSIONER MURRAY: Thank you. I think I'll direct this at Staff to begin with, and I'd like to just have you just walk through something with me regarding this incentive price stabilization program, and I'd like you to correct me anywhere that I'm making a misstatement about the program.

It was set up to establish a mechanism whereby -- the way it is today I'm talking about -- whereby the company is given an incentive to hedge by being allowed to retain some of the savings above certain levels that are calculated by a formula, but in order to participate in that incentive, the company has to guarantee any increases above a certain level, also calculated by a formula. Am I correct so far?

MR. SCHWARZ: So far.

COMMISSIONER MURRAY: Mr. Micheel is dying to say something.

MR. MICHEEL: Unless they opt out.

COMMISSIONER MURRAY: Yes. That's my next point. And in order to participate -- well, let's put it this way. The company has the option, then, during that 90-day period to opt out?

MR. SCHWARZ: That's correct.

COMMISSIONER MURRAY: And when they opt out, they do not have to -- they no longer have to guarantee a floor, basically, or a ceiling rather to the ratepayers?

MR. SCHWARZ: That's correct.

COMMISSIONER MURRAY: But is it also true that they no longer share in the savings beyond that level calculated by that formula?

MR. SCHWARZ: Under paragraph -- subparagraph 3, that's correct.

COMMISSIONER MURRAY: So basically, they just opted out of the incentive program at that point?

MR. SCHWARZ: Yes.

COMMISSIONER MURRAY: So then if -- the company would be back where it would have been without the program whereby it can still hedge, correct?

MR. SCHWARZ: Yes.

COMMISSIONER MURRAY: But in the event that the company's crystal ball is not perfect and the prices go down, it locks in prices and then the prices go down, there's a good chance that the company would not be able to recover any of that amount from the ratepayers, is that correct, any of the amount below -- between what they paid and what the real prices -- what they locked in and what the real prices turn out to be?

MR. SCHWARZ: I don't know that I would agree with that. That is, that is something that would be examined in the context of what information did they have at the time they made that decision, and at the time they made that decision, with the information that they had, was it reasonable and prudent?

COMMISSIONER MURRAY: Okay.

MR. SCHWARZ: And I think that the company is -- the consequence for the company is that it's no longer operating under the incentive solution, but the consequence for the customer, there's a consequence for the customers as well when the company opts out, and that's that the customers no longer have available the price ceiling.

COMMISSIONER MURRAY: Ceiling?

MR. SCHWARZ: Right.

COMMISSIONER MURRAY: Which was an offset to the risk -- which was an offset to the company being able to share in any savings in the program?

MR. SCHWARZ: Limiting the customers' risk is the primary purpose of the program.

COMMISSIONER MURRAY: Now, and when you talked about whether the company would be able to recover the difference between what they might have locked in versus what the actual cost turned out to be if its costs were lower, and Mr. Sommerer -- I'm sorry, your named slipped my mind for a moment -- stated that he thought that the Staff might be saying that the company or the ratepayers would have been entitled to an additional $44 million.

What I'm understanding the rationale here to be, and correct me if I'm wrong, is that the Staff would be saying that the company was imprudent not to have locked in a rate somewhere in the February or rather the March period somewhere before when the rates started to increase dramatically, and that the company's not locking in at that point was imprudent and, therefore, that 44 million would have come from disallowances, not cost savings, but disallowances to the company or, in other words, the charging that off to the shareholders.

Is that where that 44 million that you've talked about earlier would be coming from?

MR. SCHWARZ: Well, I think that the -- the $44 million, which would be in addition to the 20 or 28 million that the company earned under the PSP, would have resulted from, you know, a buy early and hold strategy.

I didn't understand Mr. Sommerer to say that, given that the PSP was in effect, that Staff would be making such a prudence adjustment. The company was entitled to operate under the PSP. I mean, that was its tariff and it was entitled to do so. And until such time as --

COMMISSIONER MURRAY: Let me stop you because the questions were from Vice Chair Drainer if the PSP had not been in place, and the Staff was asked the question, as I recall, what would the ratepayers have been entitled to additionally had that not been in place?

And as I understand the rationale in assuming that the ratepayers would have been entitled to that much additional, that it would have been through prudence disallowances?

MR. SCHWARZ: That is correct. But I didn't understand Mr. Sommerer to say that the Staff would be proposing such.

COMMISSIONER MURRAY: Okay. I may have misstated that, but what I'm talking about was the exchange between Vice Chair Drainer and Mr. Sommerer.

MR. SCHWARZ: Right.

COMMISSIONER MURRAY: And that was related to if the PSP had not been in place and the additional amount that the customers would have been entitled to.

And if that were the case, it appears that Staff would just go after, on the basis of prudence, any amount that was beyond that time period in which most analysts were saying that the price of natural gas was going to be at a level way below what it turned out to be. Now, am I wrong about that?

MR. SCHWARZ: I'd defer to Mr. Sommerer. I'm not sure I remember the questions clearly enough.

MR. SOMMERER: Even though most analysts appeared to be saying that the market would be below $4, it's always prudent to hedge if you have a supply portfolio that's totally indexed based.

And I think what Staff is concerned about is if you have no hedging or very little hedging and you have an exposure with a market-based index with your entire gas supply.

COMMISSIONER MURRAY: So you're saying because of the incentive program that was in place, you're saying that is the only thing that kept the company from hedging during that time period, in your opinion?

MR. SOMMERER: In my opinion, I think that was an important factor in their decision not to do any material hedging. In years past they had a buy and hold program. The original program had no incentive mechanism, and the company in those circumstances hedged approximately 70 percent of their volumes.

COMMISSIONER MURRAY: In a different market situation than exists today?

MR. SOMMERER: It was a different market

situation in terms of price, but it was still the same exposure with the gas supply contracts. In other words, those contracts were index-based then and they're index-based now.

COMMISSIONER MURRAY: Okay. I'm going to let some other people respond. I'd like to get Laclede's response. Is Laclede prepared to respond?

MR. PENDERGAST: Ken, would you like to take it?

MR. NEISES: I think I had indicated earlier that the company under the circumstances that existed in March and April would not have hedged at the prices then prevailing. Based upon the market information that we had at hand, we would not have gone out and bought call options at that point in time whether or not this program was in place.

The fact of the matter is that the price was at a historical high, and it did not seem prudent to go out and hedge when a market is at historical high when you're being advised and that most analysts are suggesting that it is inordinately high and that the market is going to correct. That being the case, the prudent action was not to hedge, wait for the correction.

Furthermore, if you hedge that early, there is a huge premium that you have to pay for what is known as time decay. When you're hedging that far in advance, i.e. March for the following winter, you pay a very dear premium for that length of time that you're going to be hedged. And as the months -- as the months go by, that premium reduces.

So I think we could be arguing clearly, if that market had done what everybody was expecting and we had hedged, I think a far better case could have been made that we were imprudent if, in fact, that market did turn down in the face of everything that we knew at that point in time. And as we sit here today, of course it's clear in terms of what the runup ultimately was.

So my short answer is that this -- and I am -- I say to you, the truth is as I sit here that I would not have done anything different, and it was not this program, it was not this 90-day window. The accusation is being made that somehow it's the 90-day window. The 90-day window had nothing to do with it.

It appears -- the hypothesis that has been presented here is that somehow this 90-day window is the cause of everything, and it really isn't, because we simply would not have acted any differently in this -- in an environment whether this program was not -- whether it was in place or not during this period of time.

COMMISSIONER MURRAY: Mr. Neises, with the fact that you opted out with that 90-day window, at that point there was no guarantee of a ceiling to the ratepayers, correct?

MR. NEISES: That is correct.

COMMISSIONER MURRAY: And at that point there was also no incentive to the company; is that correct?

MR. NEISES: That's correct. In terms of that price incentive provision, we could neither make any money nor could we lose any money at that point in time under that provision. Now, we opted out of that provision.

The cost reduction provision remained in place, and the whole idea behind the cost reduction is to give the company an incentive to try to reduce that $4 million that the ratepayers are going to have to pay for this hedging program, and we did that. They effectively got free insurance because we wiped out the $4 million.

COMMISSIONER MURRAY: Okay. Let me pursue that just a little bit further because I'm still just a little bit confused about what was still in place after the opt out. The provision of the sharing grid and the provision of the ceiling to the ratepayers, that was gone?

MR. NEISES: That was gone for that component of the program, right.

COMMISSIONER MURRAY: But then --

MR. NEISES: So that when -- just if I could add, so that when we on the 11.5 million or whatever it is, when we took those options to liquidation, the company shares in none of that.

COMMISSIONER MURRAY: Okay. And now --

MR. NEISES: Those gains.

COMMISSIONER MURRAY: In terms of any hedging that the company did after that, did or did not do after that, and in terms of your ACA adjustment, are you subject to the same kind of prudence review that you would have been subject to had this program not been in place with the provisions that are still remaining, or is there some kind of a curtailment of that prudence review?

MR. NEISES: No. It's the company's position that there is no prudence review after -- you know, when this program was put in place, the regulatory compact effectively was that when there's an incentive program in place, that the company has an incentive to do everything it can, and at that point in time with that -- with that understanding and as the incentives are supposed to take the place of that, because the company is attempting to do everything it can, it has a motivation to do what is right under a given set of circumstances.

COMMISSIONER MURRAY: I'm still not sure I understand.

MR. NEISES: Well, I tried to --

COMMISSIONER MURRAY: Let me ask Staff, and then, Mr. Micheel, I'm sure you're wanting to comment, too. In terms of any prudence review for the period in time after the company opted out from the 90-day window, how does the program, the portion of it that is in place, how does that affect any prudence review?

MR. NEISES: It's the company's position that under the program there are no prudence reviews.

COMMISSIONER MURRAY: Okay. And I'd like --

MR. NEISES: He's the lawyer here in terms of if he has a different opinion.

MR. PENDERGAST: I was just going to say, I think she was directing that question to Staff.

MR. NEISES: I'm sorry.

COMMISSIONER MURRAY: Well, I will hear from Staff, and then if there's anything else you want to add to that, I'll be happy to hear it.

Mr. Sommerer?

MR. SOMMERER: I don't think the prudence reviews are removed under the hedging incentive program, and I don't see anything about the word prudence in the tariffs or in the program description.

I do believe that under the company's Gas Supply Incentive Program, which is a separate set of tariffs, prudence reviews are curtailed under certain circumstances.

If the company is able to buy below a certain market index price, there's a real question on whether the Staff can go forward with a prudence review, and that's under the Gas Supply Incentive Plan rather than the hedging.

COMMISSIONER MURRAY: Now, are you saying that under this Price Stabilization Plan, that even if they had not opted out, that they would not be immune from a prudence review?

MR. SOMMERER: I think the company if they wouldn't have opted out would have had some fairly significant guarantees, price guarantees. So it would be very unlikely that there would be a prudence review.

I'm not certain of the answer to your question in terms of if there were some costs that Staff believed imprudent and the company had not opted out, I'm uncertain about our ability to do a prudence review in that particular case.

COMMISSIONER MURRAY: Let me go back to Mr. Pendergast and ask you, from a legal standpoint in terms of the tariff, where does it -- in your opinion, where does it prohibit a prudence review?

MR. PENDERGAST: Sure. And I think a tariff's just like statutes. You have to harmonize them and read them together, and I think if you read the PSP tariff that applies to our edging program and you read the Gas Supply

Incentive Plan tariff provisions, and I believe Mr. Micheel has pointed this out as well, the Gas Supply Incentive Plan which really borrowed from what the Commission first approved for MGE a number of years ago, of course, had benchmarks, and as long as you were within those benchmark levels, your gas costs were considered prudent. And if you fell outside those benchmark levels, they were, I believe, deemed imprudent.

And then you had a hedging program that came along that had its own internal incentives, if you will, to attempt to provide incentives relating to hedging on how costs will be treated.

And it would be our view that, to the extent that those provisions were not operable because the company opted out of them, that you fall back to the general, if you will, tariff provisions that basically say, as long as your gas costs are within these specified limits, and I believe they have been, that they would not be subject to a prudence review.

COMMISSIONER MURRAY: All right. Is there anything that Public Counsel wants to add to that?

MR. MICHEEL: I don't disagree with Mr. Pendergast in that the GSIP, if they're within 110 percent of their benchmark, the Commission has essentially given them safe harbor from any sort of prudence review.

That's part and parcel of why we didn't ask for an emergency ACA in Laclede's case, and I think I filed something pointing that out to the Commission. It's something that we look long and hard at.

I'm not certain with respect to prudence as it relates to the hedging. I haven't thought about that question, Commissioner.

I also -- you had asked some questions about when the company got out of the price protection plan and they didn't get a chance or an opportunity then to profit from that plan, but that doesn't answer the problem that we have with that price protection plan, and that's that it's asymmetrical.

In other words, the company only has upside potential to profit and none of the downside risk. And it's our view if we're going to give the company a real incentive, then they should have a real opportunity to bear some of the risk also, not just opt out.

So I would just answer your questions a little differently than some of the other parties and tell you that my concern is a little bit with the asymmetrical nature of the risk, and how the 90-day opting out makes the risk asymmetrical.

COMMISSIONER MURRAY: But let me ask you this.

Assuming they didn't opt out, I mean, once they opt out, there's no program, so it's like they lost the risk, they lost the reward. So it's not one-sided. They took both away, the risk and the reward.

But had they stayed in, they had to provide a guaranteed ceiling to the ratepayers in order to stay in; isn't that correct?

MR. MICHEEL: Not necessarily a guaranteed ceiling. What they -- I guess it would be guaranteed in the sense that they would have to buy up to the program limit.

Okay. But the whole purpose of the program is to provide ratepayers protection against price volatility. Once you opt out of that portion of the program, Commissioner, the protection given to the ratepayers in the program isn't there anymore.

COMMISSIONER MURRAY: But you're going back to opting out again, and I'm talking about if it's in place, and I'm saying that there's a rate ceiling for the ratepayers the way I understand it. Is that not true?

MR. MICHEEL: Well, there's various sharing grids, Commissioner, and I think --

COMMISSIONER MURRAY: But the maximum that the ratepayers will be charged is set?

MR. MICHEEL: Is the CPL, yes.

COMMISSIONER MURRAY: Yes. So the ratepayers are protected. They can't be charged any more than that if the program is in place. And if the company is able to save beyond that, the ratepayers pay even less than that.

MR. MICHEEL: For those amount of volumes that they would do that, yes, I mean, but the PGA price would still go up because we're just talking about the 40 percent of the volumes, flowing volumes in the winter. So with that caveat, based on this stipulation, I do not disagree.

COMMISSIONER MURRAY: Mr. Schwarz?

MR. SCHWARZ: If I might, it seems to me that there is an anomaly. That is -- and my understanding of the PSP is that in return for a cap on the agreed-upon volumes, that the company would be permitted to share in any profits from trading in financial instruments. In return for providing that price ceiling, they were going to share in trading profits.

Well, the company opted out of that, but it seems to me that there -- what they're now claiming to share from as a cost reduction is trading profits. So I'm -- I'm not quite sure what the bargain is down below. That is, the maximum recoverable amount which is talked about in the cost portion of the program is $4 million. This program cost 8 million, 8 1/2, $9 million.

And I know it's -- the terms and definitions in that cost reduction program, I think we'll be having some considerable discussions in the appropriate ACA case about that. But it seems to me anomalous that the calculations, at least as it appears to me, that the company has made is exactly the same kind of calculations they would have made had the guaranteed price ceiling still been in place.

So I'm -- and I don't know that I would characterize that as a prudence review. I haven't really given thought to whether a prudence review would be available under the program. But I certainly think that there's some question about how it's structured.

But I emphasize again that what we're talking about is what should be in place for the next heating season, and I think that the focus shouldn't be so much on what were the possible consequences, what will be the possible consequences under the events that have unfolded in the last 11 months as how do you want events to unfold in the next 11 months.

COMMISSIONER MURRAY: Okay. So then let me follow up with this. If the company is still sharing through the cost reduction incentive, what sharing ended when they opted out?

MR. SCHWARZ: The obligation to put in place a price ceiling.

COMMISSIONER MURRAY: What sharing ended?

MR. SCHWARZ: The same -- the same kinds of sharing, the sharing in the benefit of transactions that I think they're now claiming under the cost reduction program.

COMMISSIONER MURRAY: Mr. Pendergast wants to respond to that.

MR. PENDERGAST: Yeah, if I could. Both the price protection incentive component as well as the overall cost reduction incentive component, those two separate components had their own specific sharing grids, had their own specific allocations of risk.

And under the price protection incentive component, it was based on where your actual financial instrument prices fell in comparison to benchmarks that were made up of a target strike price and a catastrophic price level, and depending upon whether you were above or below one of those you would get to share.

The overall cost reduction incentive amount was based on a sharing grid that took into account the $4 million expenditure of the program and then as you got additional profits made from not buying and holding until the last three days but trading in per month or conceivably just not spending the money. As those savings increased, you would get either 40 percent or if you got them above, I think, 6.6 million or so, 60 percent. So both of them had their own internal sharing grids.

COMMISSIONER MURRAY: And so you were then discussing the cost reduction incentive just with your last remarks?

MR. PENDERGAST: Yes. Yes.

COMMISSIONER MURRAY: Okay. Mr. Micheel, I thought you were wanting to say something.

MR. MICHEEL: No. I think Mr. Pendergast gave a correct description of how the price protection incentive works and where they have the opportunity to earn a profit in trading in and out.

And I would just say that, you know, the $11 million we're talking about that goes only to ratepayers here, that's for contracts that they did not sell, I mean did not sell before the last three trading days.

COMMISSIONER MURRAY: Under the cost reduction incentive?

MR. MICHEEL: Well, yes. And that's only in effect under the cost reduction incentive, that portion. The ratepayers only get a hundred percent of that because they opted out of the price protection incentive.

COMMISSIONER MURRAY: Otherwise it would have been under the sharing grid?

MR. MICHEEL: Yes.

COMMISSIONER MURRAY: So the opting out affected both the cost reduction incentive?

MR. PENDERGAST: If I could, just real

briefly, the $11.5 million were the results, the financial implications of those that we held until the last three business days, and that would have been under the price protection incentive, and since we opted out of that, all 11.5 million of those go to the ratepayer.

The 17 million were the gains that were achieved by trading during the month, trading in and out of options, and pursuant to the terms of the program, those were supposed to go ahead and go to reduce the overall cost of the program, and that's the 17 million that was subject to the overall cost reduction sharing grid which, as I told you, had the 40 and 60 percent depending on how high the level was.

MR. MICHEEL: Commissioner, I have a sheet that kind of has all these numbers on it if that would help to pass out.

COMMISSIONER MURRAY: I think it would help. I don't know if you have copies of it.

MR. MICHEEL: I do. I probably should have passed it out.

COMMISSIONER MURRAY: Did you want to show it to the other counsel?

MR. MICHEEL: Sure.

COMMISSIONER MURRAY: Would you like to explain this?

MR. MICHEEL: Yes. What it has on the sheet is essentially --

COMMISSIONER MURRAY: We're in highly confidential numbers apparently.

MR. MICHEEL: Yeah. I wasn't going to say the numbers out loud, I didn't think. But what it has is essentially the starting balance of the fund on page 1, which is $4 million, and that's an amount provided by ratepayers, and then we just show the iterations of the trades and the proceeds and how they shake out.

And when you go to the second page there, you'll see that 11 million number, and you'll see the 17 million number that we've been talking about, and that roughly adds up to the 28 million number that we've been talking about.

And then you can see the breakdown there where, based upon the sharing grid of the overall cost reduction, you know, what Laclede's profit potential is, and you have the 11 million, the ratepayer share with the asterisk there because that's because they opted out of the price incentive program. You see the --

COMMISSIONER MURRAY: Yes, I see it.

MR. MICHEEL: Okay. And then you get to that 28 million number.

COMMISSIONER MURRAY: Okay. And the only

thing that -- I appreciate your providing this. The only thing I can say is that this probably demonstrates again that it's difficult in a proceeding this quickly to be asked to make major revisions in a program that's in place when we have a few days to do so.

And I think Vice Chair Drainer pointed that out earlier, that it's kind of a Catch 22 for us. The clause that's in the tariff as well as in our Order that we issued in this case that we could review, has the right but not -- the Commission has the right but not the obligation to review the program annually and revise it to correct major deficiencies on or before February 15.

I don't know what the parties were thinking of when language was placed in there that way. I don't know if it was an attempt to have us -- I can't imagine it was an attempt to throw out the program at somewhere along the way before it was ended because I don't think that's what the language says.

I don't think the revision includes discontinuance. I looked up the word revision in Black's Law Dictionary, and I don't see anything that would include a discontinuance when you're looking at revising something. And I would think the parties in putting that language in would have been very careful about language as they generally are in contractual language.

So I guess my problem is that I'm trying to express here, it's not really a question, but I think it's a problem for the Commission to have -- to be asked at this stage in this program not only to make major revisions but we're even being asked to discontinue it on very short notice without a full evidentiary hearing, which is totally impracticable.

I mean, you don't enter into an incentive program or experimental program with the expectation that you're going to have major evidentiary hearings in the middle of it to see if it's going to continue its full term.

So I just have a real problem with what it is that Staff and OPC expect us to do on such short notice with the little bit that we have before us. And either one of you can respond, and then it's time for me to pass the mic. I apologize for keeping it so long.

MR. MICHEEL: Commissioner, we would hope, consistent with my opening statement, that the Commission would strip out the profit portions of this incentive program and let the program go on the way it was designed in the GO-97-401 case as an insurance program. That's what we hope to accomplish.

MR. SCHWARZ: Staff certainly understands and shares the Commission's frustrations in having to deal with big problems in a very short time frame.

I think it's safe to say that no one really anticipated at the time we're back dealing with GO-98-484 that we would have a target strike price that was set at twice the typical, the historical if you will price of natural gas. And even last spring and summer, I don't know that anyone would have anticipated seeing prices double from that level.

But it's part of the nature of the times that we live in that change is accelerating and the time with which to deal with those changes is shrinking.

I think that you need to look at the PSP as that, a price stabilization program. And if you eliminate the incentive aspects of it, you're still left with a price stabilization program.

I mean, I think that you can view it as a modification by the elimination of the profit mechanism. You still have a price stabilization effort. It's substantially different, but the times are substantially different, and we've had -- I mean, we've had the intervening historical experience.

COMMISSIONER MURRAY: Okay. I'm going to have to pursue this just a little bit further because I do not understand what it is that Staff is alleging would still be in place if we do what you're asking. What kind of price stabilization would be there?

MR. SCHWARZ: The price stabilization would be a directive from the Commission to the company to exercise its best judgment in light of changing market conditions to stabilize prices for the customers.

COMMISSIONER MURRAY: Isn't that what the company is directed to do anyway? I mean, how is that different? How are we providing any kind of special price stabilization by telling the company that you're supposed to exercise your best judgment for the ratepayers?

MR. SCHWARZ: Well, I think it would make explicit the expectation that --

COMMISSIONER MURRAY: You think they don't know we expect that?

MR. SCHWARZ: I don't think the company would say that in the absence of an explicit directive from the Commission, that they would be facing the expectation that they would engage in pursuit of financial instruments.

I certainly think that there is some value in having such an explicit statement. I think you heard the company say that if they purchased financial instruments and there was an experience of a market decline, that they would expect a disallowance of the costs of that effort, and I think that an explicit statement from the Commission that you expect a proactive approach to the management of the portfolio should go a long way to ameliorate those concerns on the part of the company.

COMMISSIONER MURRAY: But it seems to me like what you want us to tell them is we want you to go out -- we want you to have a crystal ball and we want you to make perfect judgment, and if you don't, we're going to disallow it, but you better try hard to make it perfect. And if you guess wrong, even if you go along with what all of the analysts are saying, the Staff is going to come back and say, Disallow it.

MR. SCHWARZ: I don't think that that's a fair characterization. I don't -- and particularly in the presence of an explicit declaration from the Commission that you expect this activity, I don't think it would be well to say that what the Commission is requiring is perfect foresight. I don't think the Commission expects that.

I think that if Staff were to advance the position in an ACA case that, gee, the company missed the low point of the market by a nickel or a dime or 50 cents, that we'd get very far with the Commission, and, frankly, I don't think we should. I don't think that's the purpose of it at all.

I'm sure that -- well, certainly there hasn't ban an ACA case adjustment that we've litigated where the company didn't feel justified in asserting its position, just as the Staff felt justified in making the proposed adjustment. And frankly, we win some, we lose some, and we go on.

COMMISSIONER MURRAY: That's an interesting point you bring up. Have you won any disallowance cases against Laclede in the last --

MR. SCHWARZ: I don't know that we've brought any. We had the ACA case with Laclede on off-system sales and a certain bundled supply and transportation contract that I won't name by name because I think that may be HC. We did bring that one.

COMMISSIONER MURRAY: Did you win it?

MR. SCHWARZ: No, ma'am.

COMMISSIONER MURRAY: You haven't won any in the last -- any disallowances in the last --

MR. SCHWARZ: Not against Laclede, that's correct. We've won some others.

COMMISSIONER MURRAY: So the Commission has found that their purchases have been prudent?

MR. SCHWARZ: I'm not sure that Staff has made any allegations other than that their -- and I'm not sure that that was exactly prudence. I think we were arguing over the meaning and nature of the contract. I don't think that was a prudence challenge.

MR. MICHEEL: Commissioner, if I may, as you'll recall, Laclede has had their Gas Supply Incentive

Plan in place for a number of years now, and that limits some of the prudency arguments that either the Staff or Public Counsel or any other party can make, again as long as they're within the 110 percent of the benchmark.

So I suspect, Commissioner, in all candor, that's probably part and parcel why you haven't seen as many proposed adjustments because, quite frankly, if they're below that 110 percent, we're out of luck.

COMMISSIONER MURRAY: Thank you. Mr. Pendergast, and then I'm going to have to pass this on to Commissioner Simmons.

MR. PENDERGAST: Commissioner, if I just could briefly respond. I think there was some discussion with regard to what kind of a response Staff is looking for from the Commission with let's eliminate the program and let's just tell you to go out there and do the best job you can and sort of emphasize that hedging's important and we'll take a look at it afterwards to see whether you did a good job.

I would submit to you that turning down this program at this time and rejecting it would send just the opposite message. I mean, we can sit and talk about incentives and risk allocations and how it might have gone a little bit differently here and how it might have gone a little bit differently there, but I think the average LDC and, quite frankly, our average customer is going to look at this and he's going to say, You turn $4 million into $28.5 million, and you did that even though other incentive programs going on at the same time were not producing anywhere near that level of benefits, even though the approach that just says go out and do what you can led to no hedging being done elsewhere at all, and if in the midst of all that the Commission comes in and says, I'm sorry, but 28.5 from 4 isn't good enough, that's not our view of a reasonable, productive, effective hedging program, I think that sends a very bad message, and I think that makes people sit there and think, you know, what am I supposed to do and how'm I supposed to do it?

Quite frankly, we thought after we came through the Stipulation & Agreement and we were fortunate enough to get at least a portion of that thing worked out, that when we were able to go ahead and do these trades and were able to get these gains, because we wanted to show the Commission this program could work, and we had finally gotten about $28.5 million worth of benefits, that Staff would be overjoyed, that Public Counsel would think, Hey, that's a pretty good result, and that rather than getting a recommendation to close down the program, there wouldn't have been any recommendation at all.

And so I just think that in the broader

picture you have to take into consideration what turning down a program with this kind of cost/benefit result would suggest to people that maybe don't have as good and as fine an appreciation for alternative scenarios of what could have been.

Thank you.

COMMISSIONER MURRAY: Thank you.

COMMISSIONER DRAINER: Can I ask for a clarification on a couple of Commissioner Murray's? These are very quick clarifications. Mr. Micheel?

MR. MICHEEL: Yes.

COMMISSIONER DRAINER: This is just with respect to what you handed out, and I won't talk numbers, but I just want to understand some of the symbols.

Next to all the dates there's an X or normally like a time sign, but I don't know what it's supposed to -- why it's there. Can you tell me why it's there?

MR. MICHEEL: Can I turn this over to Mr. Busch? He created the chart.

COMMISSIONER DRAINER: Sure. Have him sworn in. I don't believe he's sworn in yet.

MR. MICHEEL: That's correct.

COMMISSIONER DRAINER: I didn't think you'd get through the day without getting sworn. You don't have to come up, but you do have to be sworn in.

(Witness sworn.)

JUDGE RUTH: Would you please state your name for the record.

MR. BUSCH: My name is James A. Busch. I'm an economist with the Office of the Public Counsel.

COMMISSIONER DRAINER: Okay. Mr. Busch, if you would just tell me what all the Xs next to the dates symbolize, their function.

MR. BUSCH: For the most part, this sheet was provided by Laclede Gas Company as showing the balance that they started with, and there is a column that's missing that says costs, and it shows what they paid and how that's affected the overall balance, when they made a sale and how that increased the balance.

I also then got backup information from Laclede. That X just symbolizes that I've got that data for that date.

COMMISSIONER DRAINER: So it was a checklist item?

MR. BUSCH: Yeah. It was just a checklist for me so I can look at this list and the backup data provided by the company and then I know every --

COMMISSIONER DRAINER: Okay. And then on the last page where you have the asterisk, that's just to go to the footnote; is that correct?

MR. BUSCH: Yes. The asterisk after the 11.5 million --

COMMISSIONER DRAINER: Is that confidential? It's not. Okay. What is confidential on here?

MR. PENDERGAST: Well, I think primarily what we're interested in keeping confidential, and we've tried to make this as transparent as possible, is just when and how the TSP and CPL were set.

COMMISSIONER DRAINER: Well, I guess then again I'm just going to ask that you look at this document and tell us whether it needs to be kept confidential for the record.

MR. PENDERGAST: Sure. I will.

COMMISSIONER DRAINER: So that's just next to those dollars and it tells you the footnote. But then if I take that column and I take the next column, those are added up to give me the sum, correct?

MR. BUSCH: Yes. The two numbers, starting with the 8 million, is just the -- how the 17 million is broken down according to the sharing grid for the --

COMMISSIONER DRAINER: Okay. But then go over one.

MR. BUSCH: Oh, yeah. Then going over one, that's a total column. I'm sorry. Yes, that's how you get to the 28 million.

COMMISSIONER DRAINER: Okay. Thank you. Thank you for your answer.

MR. BUSCH: Thank you.

COMMISSIONER DRAINER: And finally, because the gas supply incentive program has been mentioned throughout the day, I want one final clarification, because Mr. Micheel was talking to Commissioner Murray about that and a safe harbor that it creates, et cetera, and this is a yes/no.

Okay. Was that program originally initiated as part of a settlement in a Laclede -- a rate case? Tim, maybe -- Mr. Schwarz, I'm sorry, would you answer that, because I believe you can answer for all parties on this?

MR. SCHWARZ: My recollection is that the original GSIP was adopted by Stipulation and Agreement in Laclede's general rate case GR-96-193.

COMMISSIONER DRAINER: Okay. Now --

MR. SCHWARZ: Which would --

COMMISSIONER DRAINER: So that was part of that, and that was part of the Stipulation and Agreement among all parties, correct?

MR. SCHWARZ: Yes.

COMMISSIONER DRAINER: Okay. And the Office of the Public Counsel in that, Mr. Micheel, although you did not support it, you did not oppose it and did sign on the

Stipulation and Agreement?

MR. MICHEEL: That would be correct.

COMMISSIONER DRAINER: Okay. Thank you. I have no other questions. I appreciate your answers.

JUDGE RUTH: Commissioner Simmons, would you like to ask questions?

COMMISSIONER SIMMONS: Yes. Thank you.

I'd like to go back to a line of questioning that I opened up with earlier today and kind of narrow the scope of that questioning, and I'll start with Laclede, go to Staff and then end up with Public Counsel.

Earlier, Mr. Neises, I believe that you said that the 90-day window was not the problem with this program, and so -- or at least I characterize your statement as being that. Is it your position that, yes or no, the 90-day window issue is not a problem and that it should not be eliminated from this program?

MR. NEISES: I do not believe -- no, I do not believe it needs to be eliminated.

COMMISSIONER SIMMONS: Okay. Same line of questioning, although this time to Staff, and I'm going to ask Mr. Sommerer to give me a response to that. Is it your belief that the 90-day window issue is a problem, and is it something that should be eliminated from this program?

MR. SOMMERER: Yes.

COMMISSIONER SIMMONS: You are now sworn in, Mr. Busch, so I'm going to ask Mr. Busch the same question as it relates to the 90-day window. Is it a problem and should it be eliminated from this program?

MR. BUSCH: Yes.

COMMISSIONER SIMMONS: That's all the questions I have.

COMMISSIONER DRAINER: Can I follow up on a question? And I would ask Mr. Neises, based on the answers that were given by Staff and the Office of the Public Counsel, if the 90-day paragraph from the -- that's in the document, the letter, they call it a letter but it's really the description, if that were removed from the program, does that in effect void any benefits from the program? Does it make the program not workable or is it a still workable program?

MR. NEISES: The reason -- to answer that question, you have to understand the reason for that window, and the reason for the window is that it is literally to protect the company from severe financial consequences, and I say severe, because the window calls for a radical change in the market. In other words, a sudden rise or something has occurred in this past year, and in that event, if we don't get ourselves covered or if a situation arises as it did this year, we have to have some protection.

I would hope that in the normal -- in a normal marketplace, there wouldn't be a need for a 90-day window, but we're simply dealing with such an irrational market that you need that in order to protect the company so we don't get ourselves in a situation like the California utilities got themselves into and all of the mess that has been created as a result of that. That's all it's about.

And my hope, as I expressed earlier at the beginning, was that we'd never have to invoke that window, and I only invoked that window after much, much thought and realization that it was the last thing that I -- I had to do it.

I am prepared to say that the company, if it would help people, would be willing to reduce the time frame to, for example, 60 days, take 30 days off of it, so it -- so it becomes a narrower window and puts more risk on us. That's all I have to say on the issue. Thank you.

COMMISSIONER DRAINER: Well, I appreciate your answers, but I want to be clear on what I'm hearing is you had mentioned earlier that the 90 days was something that you would change, and I want to be clear what you're saying is, although you believe there needs to be a window, adjusting it to 60 days is something that the company thinks does not then void the program. To go to totally, though, not have a window, again, does that void the program?

MR. NEISES: I think to go with no window at all would void it. To go to a 60-day would be -- would be an adjustment that would not void the program in my judgment.

COMMISSIONER DRAINER: Thank you. No other questions.

COMMISSIONER SIMMONS: I need to follow up for just a second. I'm going to ask this question to Staff and then probably Office of the Public Counsel.

Based on the last statement that was just made, would it be your opinion that a 60-day window and a program that had a 60-day window or even a 30-day window, that it voids the program or it modifies it?

MR. SCHWARZ: I would not be overly comforted by a modification which would permit the shifting of risk of rising prices to the customers. So whether it's 60 days or 90 days or 15 days, it seems to me that the differential between the target strike price and the catastrophic price level provide significant cushion for the company.

And if you look at the handout that OPC did later -- or did earlier today, it would appear that, I mean, there was some movement up and some movement down, but there was a considerable period of time where the movement was very small.

So no, the option of the company to shift the upward price risk to the customers is the facet that's disturbing.

COMMISSIONER SIMMONS: Public Counsel, would you like to respond to that?

MR. MICHEEL: Yes, Commissioner. I guess any closure or shortening of that window would be a modification, to answer your first question.

Does it alleviate the problems that we see with intertwining the profit motive in an insurance program? No.

COMMISSIONER SIMMONS: Thank you.

CHAIR LUMPE: I think part of Commissioner Simmons' question also was, I don't know how to state it, but if we were to eliminate that window, does that void the program? The company said to eliminate the window voids the program. The program doesn't exist without the window. Would you agree with that? Is there anything left?

MR. SCHWARZ: Well, there is still the difference between the target strike price and the catastrophic price level. As far as if the Commission issues an Order, I assume that the General Counsel's Office would seek to enforce that Order should the company seek to review the Order. I don't know that compliance with Commission Orders is voluntary.

MR. MICHEEL: I don't think that that would end the program at all. It would just merely take out that window. I think what Mr. Neises is saying -- and if I'm wrong, Mr. Neises, correct me -- that the company wouldn't be willing to take the risk if the window was gone, but it certainly would not eliminate the program.

It would only modify the program, taking out that one provision. The two incentive provisions, the price protection provision and the overall cost incentive program would still be in effect, yes.

CHAIR LUMPE: Thank you.

MR. NEISES: May I respond to that?

JUDGE RUTH: Yes.

MR. NEISES: The reason that I say that a total elimination of the 90-day window would void the program is because it is a critical component in the program, a critical component. And if you eliminate any critical component, I think you're voiding the program.

The reason it's critical is because the company must be protected from a severe disruption in the marketplace that could potentially bankrupt it.

COMMISSIONER DRAINER: Well, I just need to go ahead and express a concern. Attorneys can offer opinions. It's your expert witnesses that can offer evidence, and we have very little expert witnesses speaking, and I'm not in any way, please, dressing you down and do respect your opinions.

But I do believe that your expert witnesses -- Mr. Busch, I think you should be responding for Public Counsel to Mr. Neises' statements. He's a witness for Laclede. And I think, Mr. Sommerer, you should be responding for Staff, and it should not be just left to your attorneys to give us opinions.

We need evidence. And again, we're on a very short time line, and I do think we should be hearing from your witnesses.

I'm sorry. Commissioner, you had something to ask.

COMMISSIONER MURRAY: My memory is so short. If I could just remember what it was I wanted to ask. It's gone right now. I'll think of it in a minute, though, but if everyone is finished, I do have another question or two.

JUDGE RUTH: Go ahead.

COMMISSIONER MURRAY: Unless you wanted Mr. Sommerer and Mr. Busch to respond.

COMMISSIONER DRAINER: No. I just thought I needed to express that concern because I thought we were on a very short time line, as we've mentioned before, and I weigh very heavily the evidence given to me by witnesses, and I think they need to be speaking to the issues.

COMMISSIONER MURRAY: I have a short question here that I wanted to pursue on Mr. Schwarz' statements earlier today. You mentioned that the cost reduction feature was not clearly described in the tariffs and that was one of the things that you objected to.

I pulled out the Staff rec regarding that tariff, and the Staff rec did say that the Staff has reviewed the October 5 filing and is of the opinion that the filing implements the agreement of the parties and complies with the Commission Order. Therefore, Staff recommends the Commission approve the October 5 tariff filing.

When did Staff develop a problem with the language in the tariff?

MR. SCHWARZ: If I might, the particular language that we were talking about remained from Case No. GO-98-484, and the Staff's task in reviewing the tariffs on a compliance filing is whether it complies with the Commission Order, and in this case that Order had been supplemented by the filings, I think, subsequent.

You know, the Commission requested that description, summary description, and Staff's function in the compliance filing is to review the tariffs with the substance of the Commission Order.

COMMISSIONER MURRAY: Which basically incorporated the agreement of the parties?

MR. SCHWARZ: No, not in GO-98-484.

COMMISSIONER MURRAY: I'm talking about GO-2000-394.

MR. SCHWARZ: That's correct. And the provisions of paragraph 3 and paragraph 4, I think it is, of the tariffs were not the subject of that agreement.

COMMISSIONER MURRAY: Okay. So at the filing of the tariff for GO-98-484, did Staff object to the tariffs not complying?

MR. SCHWARZ: No. Staff's job was to see if the tariffs complied with the Commission Order in that case, which was -- that was a contested case order, and the Staff simply checked to see if the tariffs reflected the decision of the Commission.

COMMISSIONER MURRAY: But your statement earlier today was that the cost reduction feature was not clearly described in the tariffs.

MR. SCHWARZ: I think that the import of the language of the cost reduction program will be the subject of -- you know, exactly what does that mean will be the subject of an ACA case, yes.

COMMISSIONER MURRAY: So basically you didn't think it was clearly described in the Commission Order?

MR. SCHWARZ: That's correct.

COMMISSIONER MURRAY: I really want to remember the question that I had for Mr. Neises. It was related to the 90-day window and the elimination of the 90-day window. I know what my question was.

If the 90-day window were completely eliminated, then the Commission -- correct me if I'm wrong, and anybody can correct me if I'm wrong, but it's my understanding that the Commission cannot force a company to enter into an experimental or an incentive type program of this nature.

In other words, is it -- am I correct that the Commission could not remove the 90-day window and say, Laclede, you must abide by the terms of this program without that window?

MR. NEISES: I would agree with you.

COMMISSIONER MURRAY: Anybody else disagree?

MR. MICHEEL: Yes.

COMMISSIONER MURRAY: You disagree?

MR. MICHEEL: Yes.

COMMISSIONER MURRAY: You think the Commission can force a company into an experimental incentive program without their consent?

MR. MICHEEL: I think that this Commission has authority to regulate the rates and activities of investor-owned natural gas utilities, yes.

COMMISSIONER MURRAY: Staff?

MR. SCHWARZ: I think that in this specific instance, Laclede has acceded to modifications to the experiment that the Commission deems appropriate. That's in the tariff, and I think that that is certainly an additional basis to the one as stated by Mr. Micheel.

COMMISSIONER MURRAY: I do have another question about the contention that the company has the option at the time that the target strike price is established of locking in at that time. I believe that was stated earlier as being one of the reasons that you don't think the 90-day opt-out period is appropriate. Is that correct, Mr. Sommerer?

MR. SOMMERER: That's correct.

COMMISSIONER MURRAY: Okay. Then is what you're saying that -- and here again, I'm not sure that I understand this correctly, but I thought that on a monthly basis the target strike price changed, and that -- well, let me put it this way.

Are you saying that at the time the program is implemented, that the company should, if they want to protect themselves or they have the option to protect themselves by locking in at that target strike price for every amount that they're going to lock in during the period of the program?

MR. SOMMERER: I think that certainly should be a guaranteed price level because the company has this profit incentive built in, and the other side of that equation should be that catastrophic price guarantee.

And if you look at all of the formulas in the tariffs, they're really driven off of the catastrophic price level and the target strike price. In other words, the company doesn't make any money if it holds the options until the last three days unless they can beat the catastrophic price or the target strike price.

So it was kind of a baseline or a benchmark, and it was almost as if they were trying to use the old buy and hold as the benchmark, almost as a minimum acceptable performance. And to the extent they could be more flexible and beat that old buy and hold strategy, then I believe the company felt like they should participate in some of the gain.

COMMISSIONER MURRAY: Okay. But now that target strike price and the catastrophic price are established at the time the program goes into effect or are those recalculated on a monthly basis?

MR. SOMMERER: Every March the target strike price and the catastrophic price level is calculated.

COMMISSIONER MURRAY: For purposes of this incentive program?

MR. SOMMERER: That's correct.

COMMISSIONER MURRAY: And that is held

throughout that year of the program, then?
MR. SOMMERER: That's right.
COMMISSIONER MURRAY: So basically what you're saying is if they want to protect themselves, they should lock in the beginning, and then if the prices go down, they're safe, but if the prices -- okay. If the prices go up and they've locked in at that target strike price, then both the ratepayers and the shareholders gain under the program if the prices go up after they lock in the target price?
MR. SOMMERER: If the prices go up, the customer has guaranteed protection.
COMMISSIONER MURRAY: That the customer does not pay above the catastrophic price level?
MR. SOMMERER: That's right.
COMMISSIONER MURRAY: And the customer also shares in any gain from locking in below?
MR. SOMMERER: To the extent -- that's the price incentive feature, to the extent that in the last three days, when you finally get to the options expiration, the company was able to obtain strike prices lower than the target strike price, they could share in some of the savings.
COMMISSIONER MURRAY: Now, let's take the other scenario. They've locked in at the target strike

price in the beginning and the prices go down. The company is protected, but the ratepayers are at risk?

MR. SOMMERER: Well, the customers still have that protection of the target strike price to the extent the company has locked in at that price. If prices have come down, the probability is that prices -- options are going to be less if prices have come down. The company might be able to get price insurance for a lesser price, but there is some risk in getting out of that position. And the longer that you're out of the position, out of any sort of cap, the more risk there is for the customer.

But certainly there is a potential to the extent that prices go way down, option prices are going to go down as well, and the company theoretically for the same amount of money could get greater protection.

COMMISSIONER MURRAY: So wouldn't it be better to let the company exercise judgment rather than say that there's only one way to protect themselves and that's to lock in at the target strike price that was established in the beginning?

MR. SOMMERER: That's what Staff's position is. We want the company to exercise their best judgment, but we don't think that should require preapproval or a profit incentive.

COMMISSIONER MURRAY: And am I correct that

Staff is just not in favor of incentive regulation?

MR. SOMMERER: I think as long as it's fair for the customer and it's designed appropriately, there's nothing wrong with incentive regulation. I think it's really difficult to apply within a hedging program because we believe the most important goal by far should be an effective hedge for the customer.

COMMISSIONER MURRAY: Okay. Anybody else have any responses? If not, I think -- I think I'm going to call it quits.

COMMISSIONER DRAINER: Let me just ask a couple real quick questions. The original PSP program, the original one before the Commission's changes to the program, was that a Stipulation and Agreement?

MR. SOMMERER: I believe it was, yes. I think it was.

COMMISSIONER DRAINER: So although -- although you just told Commissioner Murray that you have concerns about hedging programs, you did and were a party to a Stipulation and Agreement that began an original PSP, correct?

MR. SOMMERER: That was the old buy and hold strategy, but yes, we were part of that stipulation.

COMMISSIONER DRAINER: Okay. I just have -- as Commissioner Murray said, I think I'm about ready to quit, too. I just have a couple cleanups.

In the September Stipulation & Agreement between the Office of the Public Counsel and Staff and the Company, there were changes to the program that every one of the parties agreed to, correct?

MR. SOMMERER: That's correct.

COMMISSIONER DRAINER: Then, Mr. Sommerer, did you file any direct testimony attached to Staff's first pleading to eliminate the third year of the program?

MR. SOMMERER: No, I did not.

COMMISSIONER DRAINER: Mr. Busch, did you file any direct testimony with OPC's pleading to support Staff's position to eliminate the third year of the program?

MR. BUSCH: No, I did not.

COMMISSIONER DRAINER: Mr. Neises, were you or any member of your staff provided the opportunity to have -- to review testimony and, therefore, rebuttal on why the program should not be changed or eliminated in its third year?

MR. NEISES: We were not provided with any.

COMMISSIONER DRAINER: Opportunity?

MR. NEISES: Opportunity.

COMMISSIONER DRAINER: And Mr. Pendergast?

MR. PENDERGAST: Yes.

COMMISSIONER DRAINER: As an attorney for

Laclede, were you or any member of your staff provided an opportunity to cross-examine any witnesses that asked to have this program eliminated?

MR. PENDERGAST: No, we were not.

COMMISSIONER DRAINER: I have no other questions.

JUDGE RUTH: Commissioner Simmons, do you have any further questions?

COMMISSIONER SIMMONS: I do not. Thank you.

JUDGE RUTH: Then that will conclude the questioning from the Bench. I have a couple of housekeeping items that I'd like to clean up. We'll go ahead and, unless someone desperately needs a break, we'll just go ahead and take care of this.

First of all, earlier Vice Chair Drainer had asked the Office of the Public Counsel if you'd be willing to file some proposed tariff sheets implementing some of your language. She asked if you could do that by Monday at 3 p.m. I'd like you to go ahead and attempt to file those Monday at 3 p.m.

She'd asked a similar question of Staff. Your proposal might be very similar, but I'd like you to also file proposed tariff language as to what it is you would want removed from the tariff and file it separately or with the Office of the Public Counsel if you prefer, and those would be -- they need to be in Monday by 3.

Then I want to identify a few of the handouts that the parties have used even back in the opening statements. The court reporter, I believe, was provided a copy of the graph that was used by Staff. Do you want one put in the record?

MR. SCHWARZ: Ask her. I can't remember. That was three hours ago.

THE REPORTER: I didn't get one.

JUDGE RUTH: Let me ask you, Mr. Schwarz, would you like one placed in the record for the Commissioners to be able to review? You have the option of either just placing it in for demonstrative purposes or actually offering it as an exhibit into the record.

MR. SCHWARZ: I am not offering it as an exhibit.

JUDGE RUTH: Then let's go ahead and mark one just for demonstrative purposes as Exhibit 1, demonstrative purposes only, and it's the graph that Staff used.

Then the Office of the Public Counsel had a packet of, I believe, eight pages actually, and some of these pages may -- yes. They're marked actually confidential. The Commissioners would like for this to be placed in at least as an exhibit for demonstrative purposes.

So let me ask you, pages -- it says two. It's actually the third page, and then two, three, four, five, those are all marked as confidential. Should those be highly confidential?

MR. PENDERGAST: Your Honor, we made a commitment to go ahead and take a look at those and, I think, a couple of others and determine whether or not there were any pages there that we thought needed to remain confidential.

If we could just have the weekend to take a look at those and get back to you on Monday before three o'clock, say, and if there's anything on any of the exhibits that are being marked that we think need to remain confidential, we'll point that out to you.

JUDGE RUTH: Okay. Thank you. Then I'll mark it as Exhibit 2, the packet, for demonstrative purposes only, and it will not be placed into the record until I hear further from Laclede as to whether portions need to remain highly confidential.

And then Laclede had shown the graph that was Risk Management, Inc. and Goldman's recommendations or predictions. I'm going to mark this as Exhibit 3 for demonstrative purposes, and I assume that is not highly confidential.

MR. PENDERGAST: That is not highly confidential.

JUDGE RUTH: And the last item, I just wanted to clarify with the Office of the Public Counsel. I believe it was the Office of the Public Counsel that provided this data request.

MR. PENDERGAST: No. That was us, and we would like to make that a demonstrative exhibit.

JUDGE RUTH: Okay. That would be Exhibit 4 and it's marked highly confidential.

MR. PENDERGAST: Yes, and we would like that to remain highly confidential.

JUDGE RUTH: It will be marked highly confidential at this time. Did you give a copy of that to the court reporter? If not, would you do so after the hearing, make arrangements to get one to her?

MR. PENDERGAST: Certainly.

JUDGE RUTH: I do not have any further housekeeping items.

MR. MICHEEL: Judge Ruth, we had this sheet also. I figured you'd want them all in.

JUDGE RUTH: Yes. So that one will be -- we'll make it Exhibit 5. And I'm going to call it highly confidential unless Laclede tells me otherwise Monday.

MR. PENDERGAST: We'll look at that one, too.

JUDGE RUTH: That's the two-page document prepared by the Office of the Public Counsel that lists option summary.

Okay. Then I have nothing further. That will conclude the hearing. The transcript should be ready Monday. If you need the disc copy, please be sure and talk to the court reporter.

We're off the record now. Thank you very much.

(EXHIBIT NOS. 1 THROUGH 5 WERE MARKED FOR IDENTIFICATION.)

WHEREUPON, the hearing of this case was concluded.

EXHIBITS INDEX

	Marked	Rec'd
EXHIBIT NO. 1 Graph used by Staff	173	*
EXHIBIT NO. 2 OPC Timeline of Laclede Gas Company Activity	173	*
EXHIBIT NO. 3 Price Projections at end of February 2000	173	*
EXHIBIT NO. 4HC Staff Data Request No. 5005-23	173	*
EXHIBIT NO. 5 Laclede Gas Company Option Summary	173	*

*Marked for demonstrative purposes.