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In the Matter of Missouri Gas Energy's Purchased Gas Adjustment Tariff Revisions to be Reviewed in its 2000-2001 Actual Cost adjustment.	)	Case No. GR-2001-382
In the Matter of Missouri Gas Energy's Purchased Gas Cost Adjustment Factors to be Reviewed in its 1999-2000 Actual Cost Adjustment.	)	Case No. GR-2000-425
In the Matter of Missouri Gas Energy's Purchased Gas Cost Adjustment Factors to be Reviewed in its 1998-1999 Actual Cost Adjustment.	)	Case No. GR-99-304
In the Matter of Missouri Gas Energy's Purchased Gas Cost Adjustment Tariff Revisions to be Reviewed in its 1997-1998 Actual Cost Adjustment.	)	Case No. GR-98-167

MORRIS L. WOODRUFF, Presiding,
SENIOR REGULATORY LAW JUDGE.

CONNIE MURRAY,
STEVE GAW,
BRYAN FORBIS,
COMMISSIONERS.

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P R O C E E D I N G S

JUDGE WOODRUFF: We're back for day two of this hearing in GR-2001-328, and when we left off yesterday afternoon, Mr. Langston was on the stand and Staff was cross-examining, so let's resume.

MR. SCHWARZ: Thank you, Judge.

MICHAEL LANGSTON testified as follows:

CROSS-EXAMINATION (CONT.) BY MR. SCHWARZ:

Q. Good morning.

A. Good morning.

Q. I'd like to start off by recapping a bit, if I might. Make sure that my memory jives with yours, if you would.

I think that yesterday, between yourself and Mr. Reed, we had established that by June of 2000 it was clear that the natural gas market at that stage was new and different from things that we had experienced before; is that correct?

A. I believe that was Mr. Reed's testimony.

Q. I think that we established that the weighted average cost of gas that MGE had in storage going into the winter of 2000-2001 was about 50 percent higher than it had been in previous years, about four and a quarter as compared to 2.50. I hope those aren't HC.

A. I think we used about $4.20 round numbers. It was a little different for each month, but that's correct.

Q. I think that we had established that the weather in November of 2000 was considerably colder than the weather in 1998 or 1999; is that correct?

A. I believe that was the second coldest November on record just for the month of November.

Q. And '98 and '99, in contrast, were warm Novembers?

Take a look at Ms. Jenkins' direct, Schedule 7-4.

A. That's correct.

Q. And isn't it -- isn't it true also, as she has them ranked there, that '97-'98 -- I guess '97-'98 was like the ninth warmest in that series, and then '98-'99 was third warmest, and '99-2000 was the warmest?

A. I'm sorry. What schedule are you looking at?

Q. 7-4 on Ms. Jenkins' direct. I'm sorry. Let me withdraw the question. It was misstated and I apologize.

Those are winters?

A. Yes, those are entire winters.

Q. I apologize. I apologize. However warm they were as set out in that November column?

A. Right. I believe that November of '97, just that month alone was actually slightly cooler than normal.

Q. I'm sorry. But certainly '98 and '99 were warm?

A. Yes, warmer than normal.

Q. I think that we have established that there was substantial volatility in the natural gas market in November and December of 2000; is that correct?

A. I'll agree with that.

Q. And I think that in answer to one of my questions about how you plan for storage, you indicated that you look at total demand by month in doing that?

A. Well, we look at -- I mean, we look at our normal projected demand, you know, each month across the season when we're doing our seasonal planning, and then each single individual month as we update the plan, we look at that time for that particular month.

Q. Right. You may recall that I asked you a series of questions about the difference, the cash flow consequence -- consequences of using storage as opposed to flowing gas?

A. I remember the series of questions, yes.

Q. Do you remember the answers? Did -- strike that. I will leave it at that. And I think that probably suits me as far as recapping yesterday.

Do you recall that there was a price stabilization program initiated in late spring of 1997?

A. Yes. I believe that was part of GO-97-409.

Q. Yes. And that was basically a three-year program; is that --

A. Right. That was part of an overall change to the PGA structure, as far as going to the seasonal PGA filings with one potential unscheduled filing in the winter, as well as implementation of this price stabilization.

Q. And do you recall what percentage of supply was to be hedged under that program?

A. I believe -- subject to check, I believe --

JUDGE WOODRUFF: I'm sorry. We can't let you say "subject to check." Either you know it or you don't know it, but we're not going to give you -- unless you're actually planning on going out and checking it. So just tell us what you know or what you don't know.

THE WITNESS: I don't recollect the exact number. My memory is that it was 26 million MMBtus across the entire winter.

BY MR. SCHWARZ:

Q. If I suggested it was 70 percent of flowing supply for each month, would that refresh your memory?

A. I think there was -- that may have been the basis of a calculation to come up with a number by month. Whether or not it was actually 70 percent of flowing gas on any particular month, I don't believe that that was an exact percentage number. The numbers were rounded by month. I think that was supposed to proximate 70 percent of flowing gas across the entire winter period.

Q. And was MGE authorized or mandated to obtain that, to hedge those volumes?

A. I don't recollect how that order was structured.

Q. If --

A. Let me also say, I'm not sure whether there was a settlement in that docket or not either, whether or not there was a stipulated agreement that that would, in fact, be implemented or not. So --

Q. I will suggest to you that it was a settled case. So this hedging plan was on top of the price hedge that storage provided to MGE's customers; is that correct?

A. It would have been in addition to storage.

Q. So --

A. And whether or not storage would have been a price hedge or not would -- well, according to Mr. Reed, it would be a price hedge period, whether or not the price hedge was above or below market price that was based on the prices during that particular year.

Q. Whether it was favorable to customers --

A. Correct.

Q. -- was sorted out by the facts?

So at least for those three years, if you can do the math in your head, about how much of MGE's supply was hedged, counting storage as a hedge as well?

A. A little over 60 percent.

Q. Okay. And that was under a program authorized by the Commission? That was authorized by the Commission?

A. To the extent that it was a settlement that the company and the Staff and OPC agreed to, to be implemented, the Commission approved the program that was agreed to be implemented by the parties.

Q. Have MGE's PGA tariffs ever given an assurance that 100 percent of its indexed based purchases would be recovered?

A. Well, the PGA tariffs, if we're talking about since the GO-97-409 docket where we filed seasonal rates, I believe is calculated based on a forecast of what expected overall commodity prices are by month and projected purchases as well.

To the extent there's any difference between what's paid for supplies and what's collected from customers during those relative periods, it's trued up in the annual, the ACA filing, and a surcharge is added to the following year. So I think the tariff's intent is for the company to recover their gas cost.

Q. But have MGE's PGA tariffs ever stated the company is authorized to purchase gas supply based on pipeline indexes, and that will be -- any such purchases will be considered prudently incurred and assured of recovery?

A. I think there's a lot of issues, in that prudence is obviously an issue that's determined in a hearing like this, after the fact, is the way it's set up at this point in time.

As far as recovery, I think to the extent that the purchases are included in the definition of cost of gas in the tariffs, then they're clearly to be recovered pursuant to the tariffs, subject to a prudence review. So I mean, you know, I think, are they to be recovered, yes, unless they're found to be imprudent.

Q. But there's no -- and there has never been any specific reference to index priced gas as opposed to fixed price gas as opposed to daily, you know, gas purchase in the daily market; there's never been any specific authorization for any of those types of purchases in the PGA tariffs, has there?

A. Well, the PGA authorizes the costs that can be included in that mechanism for recovery, and the cost of gas definitions are basically whatever price is paid for the commodity of the gas that's acquired. So if what you're talking about is different pricing mechanisms, whether or not the price that's paid is index or fixed price or any other structure that, you know, it could be a demand commodity supply purchase structure, whatever that might be.

That's simply a costing mechanism within the purchase contracts, but the cost of gas tariff language defines that the payments made for the purchase of the commodity can be recovered, which is as opposed to financial instruments where, at least from my perspective, the cost of gas definitions do not include gains or losses on option contracts, for instance, on the NYMEX.

Q. Is that a no?

A. I think I've explained my answer.

MR. SCHWARZ: Judge, I think I'm entitled to a yes or no answer and then the explanation, or at least a yes or no at the end.

JUDGE WOODRUFF: He's given you an explanation. Why don't you reask your question -- ask it again, and try and answer yes or no if you can. If you can't answer yes or no, just say, I can't answer yes or no.

BY MR. SCHWARZ:

Q. Has MGE's PGA tariffs ever specifically authorized recovery of index based purchases, fixed price purchases, daily market purchases, specifically saying that these types of purchases are authorized?

A. Yes, with the explanation that, as I interpret the tariffs, to the extent that the pricing mechanisms that you enumerated are for the purchase of the commodity of natural gas, then they are includable in the cost of gas provision within the PGA and recoverable.

Q. And to your knowledge, has Staff concurred in that consideration?

A. That commodity purchases are recoverable in the PGA?

Q. Yes.

A. Yes.

Q. And has Staff ever proposed a disallowance specifically because the purchase was based on index price or because the purchase was a fixed price or because the purchase was made in a daily or spot market?

A. Yes, I believe they have.

Q. Because of the type of purchase or because of the surrounding circumstances?

A. My recollection is they've challenged pricing mechanisms in a contract.

Q. And can you tell me when?

A. My recollection is they challenged the purchases of some ox-- purchases under our Tight Sands contract as a result of a pricing mechanism that was contained in the contract and a dispute over that mechanism.

Q. But that -- that had to do with the level of the price, didn't it?

A. No. I think it had to do with the cost included in the price calculation.
Q. But they have never disallowed a, for instance, a fixed price, because it was a fixed price and not because of the level or the circumstance?
A. Ever, you know, I don't know.
Q. Within your knowledge?
A. I don't have any experience. I don't recall.
Q. Do MGE's PGA tariffs indicate a preference for first-of-the-month index pricing over daily pricing or fixed price purchases?
A. The PGA mechanism simply defines -- no. The PGA tariffs simply define the payments that can be recoverable within the PGA mechanism. Again, any specific pricing mechanism under the contracts essentially represent how that payment is calculated.
Q. Does MGE ever pay a gas marketer or producer a premium over and above an index price?
A. Yes.
Q. Would the Duke contract be an example of that, in part?
A. For certain purchases, certain purchases below index, certain purchases above index. Depends on the delivery point under the contract.
Q. Did MGE seek Commission approval before it

entered its contract with Duke Energy?

A. Not for the contract itself.

Q. I don't think I'm going to get into any HC stuff. I will -- before you answer, if I am, please alert me.

Does the Duke contract allow fixed pricing as well as index pricing?

MR. DUFFY: Your Honor, could we have a clarification as to what the Duke contract is that we're talking about here and what time period it relates to?

JUDGE WOODRUFF: If you can clarify that, please.

THE WITNESS: The Duke contract was an arrangement that we entered into following a request for proposals that was sent out in 1999. The contract was essentially agreed to in early 2000 and codified in a contract that began September 1 of 2000 and runs through August 31st of 2003 and -- I'm sorry.

BY MR. SCHWARZ:

Q. No. That's fine. Does it provide for fixed pricing, as well as index pricing?

A. Not specifically.

Q. Could you expand on that a bit, without being HC?

A. There are pricing options within the contract that were designed to match the provisions in the fixed commodity price mechanism that was approved by the Commission in the tariffs that were filed by the company. To the extent that those provisions were exercised, then the company could effectively fix the price for all of its purchases under that contract, under defined pricing terms.

Outside the parameters of that and the specific index pricing, which is different by delivery point, the company and Duke have at times agreed to fixed price purchases at specific points for specific quantities for specific periods within the -- within the contract.

Q. Right. The testimony indicates that during this ACA period MGE had some fixed price gas. Was that done through the Duke contract or was that done --

A. That's correct.

MR. SCHWARZ: May I approach the witness?

JUDGE WOODRUFF: You may. Is this a new exhibit?

MR. SCHWARZ: Yes.

JUDGE WOODRUFF: Will this be HC?

MR. SCHWARZ: It's not marked HC.

JUDGE WOODRUFF: This will be 22.

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

BY MR. SCHWARZ:

Q. Have you had a chance to review Exhibit 22?
A. Yes, I have.
Q. And does that accurately state the function and role of reliability reports?
A. I believe the question asked about the company's gas purchasing practices during the '99-2000 ACA period. The information contained in the reliability reports is utilized as an example of the information that's utilized in those practices.
Q. And is that representation accurate?
A. Yes.
Q. You may recall -- well, we reviewed yesterday the Schedule 2 to Ms. Jenkins' surrebuttal, which was -- I'm not sure who it's from at this stage, if it's from Ken Hubbard or from Dave Twitchell. But you recall that?
A. The Schedule 2-1 through 2-4?
Q. Right. Would a similar document have gone to Duke for the November nominations with different numbers in it but the same kind of --
A. Generally speaking, our practice in most months was to send them electronically a copy of the document that would be similar to what's in 2-3, 2-4. You know, in this case there's a -- there's a cover memo that outlines a change as a result of some agreed volume and pricing changes. And on the memo itself, on the to -- where

it says to and from, it's from David Twitchell to -- Mark Homestead is -- works for Duke.

Q. Okay. Thank you. And do you know if the information that was sent to Duke in November would have been for a base case nomination?

A. Bear with me one minute. Generally what would have been sent to Duke would have been the information on my sheet MTL-16, page 15. Schedule MTL-16 to my direct testimony.

Q. Was that 15 --

A. MTL-16, which is the last schedule on direct, page 15.

Q. Thank you.

MR. SCHWARZ: I think I need to go in-camera for this next series of questions.

JUDGE WOODRUFF: All right. At this point we'll go in-camera. Anyone in the audience who needs to leave, please do so.

(REPORTER'S NOTE: At this point, an in-camera session was held, which is contained in Volume 5, pages 242 through 251 of the transcript.)

JUDGE WOODRUFF: And we're on the Internet. You can proceed.

BY MR. SCHWARZ:

Q. Did MGE ever conduct a specific analysis in terms of costs and risk to the use of swing supply as an alternative to storage, particularly with respect to storage use in November?

JUDGE WOODRUFF: And if you can clarify for me what swing supply is.

BY MR. SCHWARZ:

Q. Answer his question first if you would.

A. If I understand your question, swing supplies would be those supplies that you have a contractual right to take, typically on a firm basis, with pricing that's either determined in the day market with a premium, obviously, since you have essentially a right to call but no obligation to take.

So swing gas is gas that you are not obligated to purchase but you have an absolute right to purchase any time you elect to nominate it.

JUDGE WOODRUFF: Is it similar to a call option?

THE WITNESS: No. It's actually -- it is a purchase -- it's a sale commitment on the part of the seller and an option to purchase on the part of the purchaser of physical commodity.

JUDGE WOODRUFF: Okay. You can go ahead and answer Mr. Schwarz's question.

BY MR. SCHWARZ:

Q. Which was, did you ever do a specific analysis of -- particularly with respect to November of 2000, of the use of swing supply as an alternative to storage?

A. We -- I mean, we actually operated in that manner, you know, for a number of years. I mean, early in our purchase of our Missouri properties, which began in February of '94, we had several years where we purchased gas and we attempted to use swing supplies in such a manner with -- and our storage plans were for lower pulls of storage in November, while not on the same basis, I mean, not unlike the profile that Ms. Jenkins has proposed in this case.

But what we found is that it's -- it was very expensive. You know, prices are very volatile. So in the day market you're subject to substantial swings. So as a result, you know, certainly for those years, we always found that first-of-the-month purchases were going to be a lower price option.

So when you say analysis, I'd say basically what our experience showed was that that was consistently the case in our regard. So, you know, where we ended up was the fact that we thought it was much more valuable to essentially deal with the flexibility we needed through our storage pulls in November.

Q. And I -- if I understand your answer, that's accurate as to first-of-the-month nominations, but I'm -- my question went to when did MGE do an analysis in the month of November regarding whether the additional gas that it needed would come out of storage or come from swing supply?

Let me ask you this: Did you have swing supply available to meet a substantial portion of your November needs? I mean --

A. There's two questions there. The first one, as far as generically November issues of swing gas versus storage gas, essentially early on when we actually were operating under a plan where we would pull -- where we intended to pull less gas in November, we generally found that that swing gas was much more expensive than either first of the month or the actual gas in storage. And our experience was, you know, prices did have a tendency to decline from November, you know, forward.

So our experience was that that was an expensive option. We changed our storage take profile to deal with the operational issues that we had. In November of 2000, we operated under that -- that same plan. We did have the right under the Duke contract to pull incremental volumes. I mean, we could nominate daily volumes under that contract based on the pricing in the contract for the day purchases.

Q. And so it's my understanding from your answer that in November of 2000 you did have swing supplies available in November; is that correct?

A. Yes.

Q. Okay.

A. To purchase additional volumes.

Q. Right. Right. Which -- and so you were free or had the ability to substitute swing gas for storage gas during the month of November; is that correct?

A. Well, you also have to look at the first-of-the-month flowing gas. In other words, if you're going to -- if you still have to nominate a low level of first-of-the-month flowing volumes in order to make sure that you're not faced with a situation where you have to inject volumes into capacity that's not available, so -- you know, but once you set that level, then yes, you can then vary your storage takes or swing gas as you want to.

Q. Did MGE in November of 2000 consider that it was pulling more gas from storage than even its modified baseline provided for?

A. Our projections showed, you know, while it varies every day, I mean, every day we would run the numbers and, you know, obviously it would fluctuate. As we got to the end of the month, our perception was that we were basically very close to plan. Our projections were that we were pulling basically 4.5 compared to 4.15. So we were within 7, 8 percent, which is -- for a storage plan is not -- that's not very much.

Now, ultimately there were revisions to the allocations on the Williams system that we got later in December which gave us a very big adjustment, and that changed our perception immediately.

Q. And when did you get that information?

A. I believe that was December 13th. We probably had it available to us on the 14th.

MR. SCHWARZ: Could I ask for a five-minute recess, if I might?

JUDGE WOODRUFF: All right. Let's take a short break and come back at -- well, about 9:30.

(A BREAK WAS TAKEN.)

JUDGE WOODRUFF: We're back on the record, and you can proceed with your cross-examination.

THE WITNESS: Mr. Schwarz, if I could clarify that, the question that you were asking me previously, if you want to look at the actual data, it's on my Schedule MTL-16, page 54.

BY MR. SCHWARZ:

Q. 15, 64?

A. MTL-16, page 54. That shows you the date that we received those storage updates.

Q. What was the weather forecast at the end of November -- strike that.

What was the December weather forecast at the end of November when MGE was making its December nominations?

A. Forecast was for a warmer than normal period for the first week or so, with 8 to 14-day outlook of approximately normal.

Q. And when did you realize that the December weather was going to be colder than that?

A. We watched it, and on the 10th our forward 10-day forecast, which was past that time period, was showing that it was going to be significantly colder than what that forecast had originally indicated.

Q. Was the weather in the first ten days of December colder than it had been forecast at the end of November?

A. Yes. MTL-16, page 39 would have shown what we were looking at on December 7th, which would have six days of actual heating degree days and then ten days of forecasted heating degree days in general. The normal average heating degree days per day in December would be slightly over 34.

So you had three or four days at or slightly below that and a couple of days above that in the forecast, especially by the time you got out to the 12th was showing a cold front coming through. Basically, we looked at that through until the 10th, confirmed those forecasts were -- stayed valid and we purchased incremental supplies.

There may be another schedule in here. Actually, MTL-16, page 37 would show the December the 11th, which was essentially the first day that we had purchased incremental supplies, and it does show that beginning on the 10th, 11th time period there was a cold front that came through.

Q. If you had actually posted the Riverside -- I'm changing subjects entirely. If you had actually posted the Riverside Mid-Kansas capacity for release, there would have been no need for any hypothetical calculations on the part of Mr. Sommerer; is that correct?

A. I don't intend to be argumentative, but I guess our position is there's no reason to do any hypothetical calculations in any event. The capacity could not be released on Kansas Pipeline and, you know, we had -- we released --

MR. SCHWARZ: I'd ask -- this is nonresponsive.

JUDGE WOODRUFF: It is nonresponsive. On redirect you might be given an opportunity to explain that further, but right now you just need to answer his question.

BY MR. SCHWARZ:

Q. He can make his explanation after he answers the question. If you had actually posted the Riverside Mid-Kansas volumes for release, there would -- Mr. Sommerer would have no reason to do a hypothetical calculation; is that correct?

A. And I would agree that there's no reason for him to do a hypothetical calculation in any event.

Q. Is that a yes?

A. There's never been any need for Mr. Sommerer to do a hypothetical calculation.

JUDGE WOODRUFF: I think he's answered your question.

MR. SCHWARZ: Could you tell me what the answer is?

JUDGE WOODRUFF: He said there's no need for a hypothetical question or for hypothetical calculations.

MR. SCHWARZ: I asked a yes or no question. I'm still -- even with your explanation, I'm not sure if the answer was yes or no.

JUDGE WOODRUFF: Well, you can go ahead and answer yes or no, then. Was --

BY MR. SCHWARZ:

Q.   If you had posted the capacity for release, there would be no need for Mr. Sommerer to do a hypothetical calculation?

A.   Okay. I guess the problem I'm having is with the premise of your question, if we had posted a release. So the first part is, was there a need to post capacity? No. Was there a need for Mr. Sommerer to do a hypothetical calculation? No.

Q.   If you had posted it, he still would -- he definitely would not have had to do a hypothetical calculation; is that correct?

MR. DUFFY: I'm going to object because he's asking us to -- asking the witness to speculate what Mr. Sommerer may or may not have done, depending on some action that MGE may or may not have taken.

JUDGE WOODRUFF: I'm going to sustain the objection.

MR. SCHWARZ: That's not --

JUDGE WOODRUFF: I sustained the objection. Please move on.

MR. SCHWARZ: That's not the question that was asked.

JUDGE WOODRUFF: But I sustained the objection. Please move on.

MR. SCHWARZ: I have nothing further.
JUDGE WOODRUFF: All right. Thank you.
Then we'll come up to the Bench for questions, and I do have a few.
QUESTIONS BY JUDGE WOODRUFF:
Q. First of all, there's been a term that's been used frequently in this, and as frequently is the case in these, everybody in the room knows what it is but it doesn't necessarily appear in the record.
Can you tell me what heating degree days are and how are they calculated?
A. Heating degree days are generally the -- a measure of the difference between the average temperature during a day and 65 degrees Fahrenheit. So in other words, if you look at the high and low temperatures for a day and the high is 50 and the low is 30, so the average is 40, then that particular day will have 25 heating degree days, or the difference between that average of 40 and 65.
Now, that's a somewhat simplified explanation, because I think the Weather Service has a little more involved calculation, but that's essentially how it's applied.
Q. And it's used to measure basically how cold a day is?
A. How cold on average the day is.

Q. Okay.

A. But there's a similar measure for cooling degree days, over on the summer electric side.

Q. And it's measuring how people have to turn on their heat, I assume?

A. That's correct. It's a measure of how much natural gas may be consumed for heat.

Q. Okay.

A. Or it helps measure that.

Q. Okay. Now, earlier in your testimony you mentioned that in October MGE had entered into an interruptible storage contract. So you can inject more storage -- gas into storage; is that right?

A. Exactly. We have a -- we had a maximum storage quantity contract on the Williams Central system. October was very warm. So our demand was lower than our expectation, and so we entered into a short-term interruptible -- essentially a contract with Central to acquire some short-term additional storage space so that we could, in fact, inject that gas in October.

Q. And that wasn't anything you planned in advance? You wound up having extra gas?

A. Yes. Our -- you know, our option would have been to either dump that gas in the off-system market or -- or to do what we did, which was try to obtain some additional storage and put it in storage.

Q. Is that storage contract expensive?

A. No. It was -- it was at their tariffed rates, which I think were about the same as what we were paying for other storage capacity at the time. I'd have to confirm that with the invoices.

Q. Okay. Now, you did that in October. Is there a reason you couldn't do that in November?

A. In November, I mean, once we started pulling -- obviously, the first gas that we pulled was the gas out of the interruptible storage, and then that agreement terminated. And then as we pulled more gas, we actually had storage capacity available under our own storage contracts. So we wouldn't have needed to maintain additional storage capacity as we were withdrawing gas out of storage.

Q. The reason I ask the question is, you indicated that you need to under-nominate November supplies so that you have this shock absorber, I think was the term that was used, for gas so that if in November you have abnormally warm weather, you have someplace -- you don't have to be injecting gas or dumping it on the market.

A. Okay.

Q. I'm asking would such contracts be available in November on a more general basis?

A. And generally, no. I mean, we were able to obtain 500,000 MMBtus of storage capacity compared to 16,500,000 round numbers of capacity we currently have under contract. So we're essentially acquiring roughly 3 to 4 percent more capacity than we currently had under contract.

We were able to do that only because Central actually had that quantity of capacity available and we had made the commitment to them that we, you know, would not attempt to have that gas in storage for very long.

As a general rule, the Central storage, all of their storage is fully contracted for. So their ability to provide that type of additional capacity is subject to how the rest of their customers are filling storage.

Q. And I believe you mentioned also that with the type of storage you use, that there's a turn-around point, is that right, where gas is no longer being injected and then comes out and you can't inject easily?

A. The tariff provisions on the Williams Central system are that from April 1 through October 30th is the period in which gas is injected into storage. November 1 through March 31st is the period at which gas is withdrawn from storage. There are differences in the summer months, April through October.

The quantity that you can inject in your storage capacity every day starts out fairly high and then, as the Central storage facilities fill up, then the injection quantity declines. So that you start out in April and in our case we have about 120 to 130 million cubic feet a day of injectible capability into storage. By the time we get to October, that's down closer to 40 million cubic feet per day. So, you know, it gets cut by at least a factor of three on the injection cycle. So --

Q. Is that just a technical reason or is that everybody's trying to get it in at the last minute?

A. It's a technical reason. As you inject gas into the reservoir facility itself and pressure builds up within the reservoir, then your ability to inject more and more into the higher pressure reservoir becomes more and more limited.

Q. Okay. Now, let me ask you about the nomination of November supplies. I got the impression from your testimony that MGE was planning to nominate only the base load, not including the heating element of demand. Is that correct?

A. What we -- what we were doing is nominating a flowing gas level that -- and let's see if we can kind of define some terms here. Base load can be used in a couple of different manners. An absolute base load amount is essentially the quantity of natural gas that is taken on a daily basis in total by our customers when there is absolutely no heating demand at all. So we measure that typically during the middle of the summer, so there's no demand. That number's quite low.

This particular year, our forecast was that the base load quantity would be roughly 47,600 MMBtus per day. On a monthly basis, what we look at is -- and particularly in the wintertime, like in November, we'll look at what is our total customer demand for the month at the warmest or lowest demand period that we have experienced.

Q. And that's based on historical heating degree days?

A. Heating degree days and actual customer consumption. And so we know that that's kind of a level of demand that we can expect as a minimum across the month. That number at this point in time would have been about 4, 400,000 MMBtus, or roughly 140, 145,000 MMBtus per day or a little less.

Q. That was in November you're talking about?

A. In November. So we set our flowing volumes at less than that so that we would pull -- you know, even if we had an absolute warm November, all of our flowing gas would flow to customer demand and our -- and we would have a smaller storage pull, even if we had a warm -- very warm -- historically warm November.

Now, beyond that, we also did look at what the daily impact would be. So when you said we set our first-of-the-month nomination, we do look at how far is that over our absolute base load amount, because you can have periods in November when you have no heating degree days, and early November can be very warm. I mean, average temperature is over 65 degrees.

And in that event, then we have to look to what type of flexibility do we inherently have in our upstream transportation storage portfolio in order to deal with that gas. And so that's why we're cautious with how much flowing gas we turn on on the first of November, particularly because storage tends to be full.

Q. All right. So now you've nominated this base amount of flowing gas at the first of November, and it turned out to be a cold November. Do you have the option of purchasing more flowing gas on a daily basis?

A. We do.

Q. And did you do that in this November of 2000?

A. No, we didn't, mainly because our forecast of what our storage withdrawals were were not significantly above what our plan levels were.

Q. Okay.

A. So until -- until we got to some updated storage numbers, which were in December, we thought we were relatively close to our November plan.

Q. That leads into my next question. How did that happen? You were estimating how much gas you were taking out of storage, is that --

A. Correct.

Q. What is that based on?

A. There's these sheets in my testimony where we attempt to calculate based on the heating degree day forecast. We have the base load amount that we know our customers take, plus we have -- we estimate a heat rate factor, which is a measure of, based on how cold it is, what type of consumption per heating degree day is going to be utilized within our service territory.

And so we track that, and we track it based on what the telemetry and the measurement stations tell us, you know, actuals have occurred each day and we update the sheets to kind of show actuals.

We recalculate what those numbers are each day. We try to basically step forward with our estimates to essentially estimate what our total demand is and what our overall storage consumption will be.

Q. So you knew what your volumes were flowing and you knew what amount estimate of --

A. Estimate.

Q. -- what was actually going through your system?

A. Correct.

Q. And whatever wasn't flowing was coming out of storage?

A. That's correct.

Q. Okay. And did Williams give you a preliminary report or something on storage? I think that was mentioned yesterday.

A. Not a preliminary report. They gave us their numbers on December 13th.

Q. Okay. Did they give you something before that also? I thought I heard that in your testimony yesterday, something towards the end of November, the preliminary report or something. Maybe I misunderstood.

A. I mean, we have -- we had our report that -- I mean, we had our forecast that we were utilizing as of the -- you know, projected through the end of November. So we were -- we were looking at, you know, as of the end of the month, where do we think we're going to be.

Q. That's what you were using when you made your decision about how much flowing gas to purchase in December?

A. That's correct. And then through the month of November, to the extent that we were seeing that we weren't going to be -- we didn't think we were going to be significantly off our storage plan, then we didn't feel the need to hit those spots.

Q. December 13th, I believe you said it was, you got the report from Williams?

A. Correct.

Q. And that showed that you'd used a lot more gas out of storage than you thought?

A. Correct.

Q. And how did that happen, do you know?

A. That's an allocation process that Central utilizes. We try to determine what generated that, that change. They obviously never had a satisfactory answer for us on that. My expectation is that it probably had to do with measurement error that they had recalculated, as well as potentially the impacts of the failure of third parties to nominate.

Q. Explain that last statement for me.

A. We have transport customers that are located behind our system. We have telemetry on their -- on all those meters.

Q. These would be industrial using you for transport?

A. Correct. And they acquire their own supplies. They nominate their supplies with their suppliers. Their suppliers nominate on the Central system to move it to our citygate. So we see those numbers.

At the end of the month, though, Central goes back and they determine whether or not all of that gas was, in fact, delivered by the suppliers, you know, versus the actual consumption, and if there's any differences, then they -- they make adjustments on those citygate deliveries. It's generally referred to in previous cases here as burner tip balancing. It's essentially a -- a balancing provision for the transport customers on our system.

Q. So the transport customers pay you for what gas they use?

A. Actually, they pay their suppliers for the gas and they just pay us for the transportation service.

Q. Okay. But you're saying you think they used some of your storage gas; is that --

A. At the -- based on the nominations, we didn't see that there was a major issue, but Williams goes back and redoes an allocation of everything delivered to our citygate. They never told us specifically that that was it. I'm just telling you what my opinion was. We could never verify what the absolute cause was.

We also inquired about measurement errors. Measurement errors occur -- gas is measured through typically long tubes called orifice meters. It's essentially just a piece of pipe with a metal disc with a very precise hole right in the middle of the disc. And there's very precise calculations of how pressure can drop across this plate.

And essentially, depending on the flow of the gas, you have to change these plates out to make sure that the instrument measures correctly, and you have -- also have to have the correct diameter of this hole in your calculations in order to properly measure. If someone goes out and changes the plate and you don't change the calculation of the diameter of this hole, then you can generate measurement errors.

Again, we inquired about that, and we couldn't get any satisfactory answers. In any event, there was a revision to the numbers.

Q. Okay. And does MGE have any recourse against the pipeline company or anybody else for this shortage or --

A. No. No. That's just an error on their part.

Q. And did this cost MGE money? I mean, if this gas disappeared, is this a loss to MGE, aside from the argument about whether or not that storage could be used later in the year?

A. I mean, that's the primary impact. I mean, obviously to the extent that, as a result of measurement or whatever, obviously if we're -- we're looking at forecasted numbers to tell us, well, gosh, we're pretty close to what our plan was. Obviously had we known that, you know, we were going to be another 10 percent off or more, I mean, we could have obviously taken some steps there. But the main impact is just the overall impact on inventories.

Q. Okay. Now, you said you made a decision in December to under-nominate flowing gas because you thought the prices were going to drop, and in December the prices went up. I believe you also said that you did the same thing in February, and then in February the prices did drop?

A. Yes.

Q. Do you know roughly how much MGE saved by making that decision in February? If it's highly confidential, you don't have to give me an exact figure.

A. We haven't calculated that. What we did is we looked at our forecast, similar to what we did in December, and again consciously decided to reduce our flowing supplies at first-of-the-month price by 20 million a day. As we progressed through the month, prices did fall.

At the same time, we saw that our demand was lower than we had projected. So we ultimately elected not to purchase any additional incremental supplies because at that point in time our projected takes from storage for February was consistent with what that February monthly plan was.

So compared to past purchasing, if we had purchased for 20 million at the first of the month, the first-of-the-month index prices for February were something over $8. First-of-the-month prices by March were probably 6, 6.50. I mean, we can get some exact numbers, but we would essentially save the difference. If we had made the commitment to purchase it, then we would have been obligated to purchase it in first-of-the-month increments.

Q. Now, it's my understanding that very little gas was taken from storage in January; is that right?

A. Yes.

Q. I think the chart was -- I don't know if it's a highly confidential number or not, percentage, but it was a much smaller percentage than any other month of your anticipated take?

A. Right. It was -- compared to our original plan, as we got through December and, you know, we saw that the storage balance was adjusted, once we got the Williams information, you know, then we were planning -- we planned to increase our flowing gas in January and reduce our storage -- our projected -- our planned storage withdrawals for January to about half of what we had previously planned.

If you want to go in-camera I can give you the exact numbers.

Q. I'm assuming they are in the testimony somewhere?

A. They are. They are. Actually, January turned out to be warmer than normal, and as a result, our pulls from storage ended up being about 10 percent of what we had originally planned for that month, even after our adjustments.

Q. Okay. Although January was warmer, the price was still high, though; is that right?

A. The price was high at the first of the month. Shortly after the first of the month, prices did finally begin to decline.

Q. So they peaked early in January?

A. Yes, either around the 1st or shortly -- 2nd, 3rd certainly.

Q. How high did they get?

A. I want to say prices were in the high $9 or just over $10.

Q. Okay. So by the end of the month they'd dropped to 8?

A. Correct.

Q. Okay.

A. A little over 8, I believe.

Q. Now, I had a question about reliability. You indicated that reliability is one of the reasons why you have storage of gas. I'm wondering about your definition of reliability. Does reliability include both the need to make sure everybody has enough gas as well as the need to make sure you don't have too much gas? Is it two parts of the equation?

A. Let me say, the way I view it, reliability is making sure that you always serve the customers' demands. Having too much gas is essentially an economic issue. If you have excess gas, then you either have to -- you have to have someplace to go with it. I mean, you know, pipelines can't just kind of save it for you unless you have a storage contract with them.

So you either have to have storage capacity to put that excess gas into or you have to take as it's flowing and sell it elsewhere. It's not something that you can typically save or defer.

Q. Now, I want to talk a little bit about the price stabilization plan that was in effect for that winter but which was never triggered because price was set too low. Were there any incentives in that program for MGE?

A. Let me just make sure I understand. There were -- the price stabilization fund was the call option program that had been implemented in three previous years. The fixed commodity price incentive was the incentive mechanism that had the trigger price that was set at a low level.

Q. Okay. I'm not really -- I was confused about that, too. Why don't you tell me about both of them?

A. Okay. The fixed commodity price incentive program that was -- there was a stipulation filed, I think, April 28th, and then it was amended May 15th, I believe, to add the OPC. That was filed with the Commission, and the Commission approved it August 1.

That program essentially stated that if the price declined to trigger price level, that MGE would fix the price of all of its flowing supplies for a term of two years.

Q. And that was just to buy the gas with fixed prices. It wasn't call options, that sort of thing?

A. Essentially MGE was committing to essentially fix the price that flowed through the PGA for those commodities. Obviously, our intention was to essentially cover that pricing risk with our supply contracts or financial active -- hedging activity.

Q. Could be either one?

A. Either one. From our perspective, the agreement had a provision that if the trigger price wasn't reached within 60 days after approval, that the parties could meet and talk about adjusting it to a market level, which was subject to agreement of the parties. That agreement was never reached. So, therefore, that particular fixed commodity price mechanism was not implemented.

Of course, we had tariffs in place that

provided for it, but it was subject to agreement with the Staff and the OPC. That's separate from -- the stipulation that we filed essentially said, if you don't get the fixed commodity price implemented by -- it's in here. I think it was September 1 or there was a date in here -- that if you didn't get the fixed commodity price implemented, then you could implement the price stabilization fund mechanism consistent with the previous year's program.

What occurred there was the previous year's program included limitations on the price level that could -- that you were authorized to obtain. There would be set dollar amounts and set volume that was covered by that program.

And at the time, when we realized that we weren't going to get the fixed commodity price implemented because prices were high and we couldn't get an agreement on upping this trigger price, then we came back to the Commission and we asked for a modification of the terms of the price stabilization fund program from the previous year that we had agreed to seek to implement in this stipulation, that the Staff opposed those changes and the Commission denied that application, I think, October 26th.

Q. The changes would have -- of the prices that you could use purchase options at?

A. I'm trying to remember. I think we sought to modify the -- the profile or the volumes that we had covered by the program. I don't -- can't remember if we proposed any changes to the dollar amounts that we would spend to do that. And then, of course, we needed to increase the cap price or the call option price that we would obtain as a result of market prices.

Q. Okay. To change focus a little bit here, going back to posting capacity for release, is there any cost for MGE of posting these items on the electronic bulletin board of the pipeline?

A. No. Just personal time and effort in coordinating with the pipeline to get the items posted.

Q. Okay. And I assume it would not be a totally unsubstantial amount of money to have the personnel to do that. Is that -- what would be involved in actually doing that?

A. Most pipelines have an electronic bulletin board area in which you -- you essentially outline the terms of your -- the capacity that you want to release and what terms you want to release them for.

A portion of that bulletin board typically is public information, and a portion can be confidential. In other words, there can be terms that you specify, you know, that aren't necessarily revealed. Some bulletin boards are all public information, some are not.

You have to enter all those fields, and in most all cases we pretty much have to talk to the pipeline about exactly how that data is being entered, because it's not a very straightforward process. Every pipeline has a little different methodology for it.

Q. I understand they're all required to have this. Are they actually used very often?

A. On some pipelines, yes. On others not. Frankly, the postings we have made on the Kansas Pipeline system, which were not until after we understood the Staff's concern in this case, ours was the first capacity release posting that had ever been made on Kansas Pipeline.

On the Williams system, on the other hand, there is a fairly regular posting activity on that system. Similarly on Panhandle Eastern, there's a pretty active capacity release market. On Kinder Morgan, probably not as active, but they -- you know, they do have regular capacity release activities.

JUDGE WOODRUFF: I believe that's all the questions I have, so we'll go to recross.

KPC?

MR. KEEVIL: No questions.

JUDGE WOODRUFF: City of Joplin counsel is not here, so they waive.

Public Counsel?

MR. MICHEEL: No questions.

JUDGE WOODRUFF: Staff?

MR. SCHWARZ: No questions.

JUDGE WOODRUFF: All right. Redirect?

They're going to be videotaping us for a training program for the Commission. So if you see somebody with a camera, that's what it's about.

Go ahead.

MR. DUFFY: I was going to say, how am I supposed to indoctrinate these?

MR. SCHWARZ: Do we get, like, Screen Actors Guild minimums or something?

JUDGE WOODRUFF: Again, talk to the Commissioners.

REDIRECT EXAMINATION BY MR. DUFFY:

Q. Okay. Mr. Langston, I think I'd like to start out by messing up this microphone.

I'd like to start out and take you back to Mr. Schwarz's initial questions yesterday afternoon. He asked you some questions about Mr. Bush's testimony and the general topic of normalizing costs and whether Mr. Bush was attempting to come up with a normalized storage withdrawal plan.

Can you just briefly summarize, did -- what was the purpose of showing Mr. Bush's testimony in your testimony?

A. Mr. Bush testified in a rate case that MGE had filed. The purpose of his testimony was to come up with a storage injection/withdrawal profile against which prices would be calculated and an inventory cost would be calculated that would be included in a working capital adjustment for the company in their -- in their rate case.

The -- from that standpoint, to the extent that the intention was to normalize cost and to normalize the storage profile that underlied the economic calculation, the point was to point out the differences between the normal November withdrawal level proposed by Mr. Bush in the rate case versus the normal level proposed by Ms. Jenkins in this case.

Q. So if I understand what you're saying and the import of all that, it's that Mr. Bush's normalization of storage withdrawals that he performed in that rate case is very similar or comparable to the storage withdrawal plan MGE has, but both of those are then significantly different from what Ms. Jenkins has come up with in this case.

Is that accurate, that your plan's more closely aligned with what Mr. Bush showed than what Ms. Jenkins is saying?

A. You know, I think the -- there could be some discussion about that. His plan was not exactly like MGE's plan. His November withdrawal level was substantially higher than that proposed by Ms. Jenkins, and the point of including that in my testimony was simply to point out that the Staff had taken one position regarding our storage withdrawal in November in our rate case and is taking a different proposed normal for November in this case.

And in both time periods, our storage assets, our storage capacity and withdrawal capabilities have not substantially changed during those time periods.

Q. Ms. Allee, I think, in her prepared testimony, or maybe Ms. Jenkins, I can't remember which, said that by you talking about or by you including Mr. Bush's testimony, you were comparing apples to oranges.

Do you believe that's a fair characterization?

A. I don't think so. Certainly the -- the purpose of Mr. Bush's testimony was designed at coming up with a plan that was then going to be applied. In fact, I think Ms. Allee did the economic calculations that were applied against the storage plan to come up with the working capital proposed in that case.

From the standpoint that we're dealing with a working capital adjustment in one rate case versus a -- an ACA proceeding, that certainly is an apples to oranges process. But to the extent that in both cases the intention is to look at what a normal storage plan is and particularly normal withdrawals for November, then Mr. Bush should have had the same objective.

Q. And that would have been apples to apples then?

A. Correct.

Q. There was a notation made or discussion that MGE did not file a reliability report for the time period of 1999 to 2000. Can you explain why no report was filed for that time period?

A. The reliability reports that were -- the first three that were filed by MGE were filed as a result of Commission order following implementation of the case GO-94-318 incentive mechanism. The case that essentially implemented the reliability report filing obligation was GO-96-243, and essentially ordered MGE to file reliability reports as of July 1 prior to each year of the implementation of the incentive mechanism, which was a three-year process.

So MGE filed for the years of '96-97, '97-98 and '98-99. The incentive mechanism terminated on June 30th of 1999, and so ended the obligation to file reliability reports. So the following year MGE did not file a reliability report, since at that point in time the only obligation was to file for those three years.

Following that, in another case, you know, the

Staff expressed an interest to continue to receive that information. The Staff always had obtained that information through Data Request and ACA proceedings such as this, but I think they had a preference for having it, you know, at least that information in a document.

So there was an agreement. I believe it was a stipulation entered into between the company and the Staff that that information would be provided in a different forum, you know, less information than what had previously been provided. And from our standpoint the focus was slightly different.

Q. So that obligation or agreement to supply reliability reports started after 2000 and it continues today or that's also gone away? What's the current status of that?

A. It's my understanding that -- I don't remember the exact time in which the agreement was reached. It was reached prior to -- I mean, the first report that was filed following the agreement to provide the information was the one that was filed July 1 of 2000. And reports were filed for July 1 of 2001 and also July 1 of 2002. My understanding is the July 1, 2002 report was the last one obligated to be filed pursuant to those agreements.

Q. And is that the last one that has been filed, to your knowledge?

A. Yes, it is.

Q. You were active in GO-94-318 from which the concept of a reliability report first emanated; is that right?

A. Yes.

Q. Based on your knowledge, was the Commission Order that directed MGE to file this reliability report based upon some concern with how you were managing withdrawals of storage gas?

A. I believe the main stated concern that the Commission had was that if they were giving us a com-- natural gas commodity-based incentive plan, which was price based, that the company would then seek to take risks with reliability and, for instance, take all of its purchases to the spot market or the day market or somehow not have adequate gas supply resources under contract to be able to flow gas on a consistent and reliable basis to the customers.

Q. And consequently to be able to make money under this incentive plan?

A. Correct.

Q. At the risk of jeopardizing reliability to the customer?

A. Correct.

Q. Okay. Go ahead. I'm sorry. I interrupted you.

A. So the reliability reports were really designed to address what our, you know, longer term or, you know, essentially at least an annual period supply requirements would be, what's the -- what -- what gas supply resources we had under contract, what gas supply resources needed to be placed under contract for this to come here, and deliverability associated with that, that sort of thing.

Q. So prior to this first reliability report, there were no reliability reports even though there were ACA cases?

A. Not as such, that I'm aware of.

Q. Okay. And when you -- when MGE describes storage withdrawals in the reliability reports, was MGE attempting to document its storage withdrawal plans or something else?

A. We were trying to, you know, essentially layer in a fairly conservative withdrawal, you know, structure across the winter period. The objective was to make sure that we came up with a conservative estimate of the supplies that we needed to enter into a contract month by month, also compared to the deliverability that we needed month by month.

So that once you know what the deliverability you need on a daily basis as a maximum, plus the quantity that you need to be able to purchase across the month, then you can outline a supply purchase plan by month that would consist of base load and swing supplies, if that's what you elect to purchase.

Q. Has MGE's total storage capacity changed materially since 1998 or -- or is the -- well, let's go back to 1996. Has it changed materially over the six, seven years, total I mean?

A. Not more than 3 or 4 percent.

Q. Okay. So would it be fair to say that the total amount of storage that MGE would have disclosed or addressed in reliability reports would have been the same as they would have discussed in perhaps responses to data requests in ACA cases?

A. Correct.

Q. Would the format or the manner in which the withdrawals from that storage were addressed, would they be identical in the reliability report and in responses to data requests in ACA cases?

What I'm trying to get at is, there seems to have been raised on previous questions that the numbers that MGE showed for storage withdrawal in their reliability reports differ from what you called your plan, and so I'm trying to explore why that is, if that's, in fact, the situation.

A. During the first -- during the incentive mechanism period, what we were really looking at doing is focusing on the supply. You know, we understood the reliability issue to be primarily supply driven, that we maintain adequate gas supplies under contract for a reasonably long term and we had adequate deliverability of heat for any projected peak for a day within a month. That was the focus.

You know, there very well -- I'm sure were times in which, you know, we may have outlined in the reliability report, you know, we did as a conservative measure to try to make sure that we were going to have adequate flowing supplies under contract for a month, you know, that very well could be different from the actual storage plan we entered into a seasonal winter with, you know, as we moved into that winter.

Q. If the numbers are different for the same time period in the reliability report compared to what your plan was, was that some intention to mislead somebody about what your plans really were?

A. No. Our intention was to try to address the Commission's issues to make sure we had adequate flowing supplies under contract and deliverability to meet customer demands. You know, the title reliability report was an effort to make sure we had gas to serve customer needs, whatever that situation was.

Q. Do you remember Exhibit 17HC that was talked about yesterday, this document (indicating)? Do you have that? Or I can supply you one if you don't.

A. Yes, I have it.

Q. Okay. I think you were asked some questions about the table on the lower half of that page, entitled MGE 2000-2001 storage withdrawal. Do you see that?

A. Yes.

Q. And this is HC, so I'm not trying to elicit HC information, but I guess what I wanted to know generally was, does that document or does that table show what you thought your storage was at different points in time under your storage plan?

A. The --

Q. Does it reflect what MGE actually knew about where its storage was at any particular point in time, if that helps?

A. The row that's labeled "plan" was essentially our kind of planned month-by-month withdrawal quantities entering into the winter season.

As to what our storage balances actually were, as to any point in time, that -- we would have been looking at the daily reports that are -- I believe we talked about earlier that were attached to my direct testimony.

Q. Okay. So you -- on that basis, you have apparently some general idea from daily reports what your storage withdrawal is, but those are estimates as opposed to actual amounts; is that right?

A. That's correct.

Q. And there are estimates that you calculate based upon what you think the temperature is and what you assume the demand to have been and other factors; is that right?

A. Yes. I mean, our forecast demand is based on estimates. We attempt to get actuals by taking actual physical meter volume readings, and then we update the report every day for actuals for the previous -- previous time periods. So it's a combination of actuals for, you know, the historical days in the month from whatever day you're looking at it and a forecast of at least ten days forward, which include all these estimates.

Q. Okay. Let me see if I can get a layman's understanding. I've got a mental picture of a control room for an electric utility, and there's a big meter or digital readout on the wall and that shows what all of their power plants are producing at any given moment in time.

And so my assumption -- and you're an electrical engineer. Maybe you can tell me. My assumption is the electric company knows from minute to minute what the demand is on its system; is that right?

A. You know, I'm not familiar with the electric utility operations.

Q. Now, do you know -- do you have -- does the gas company, does MGE have something like that, so that you know from minute to minute or day to day what the actual demand on your system is, or do you have to use estimates to calculate what that demand actually is?

A. We have -- there's telemetry, what's called telemetry units on every citygate station that serves our distribution system. We monitor what flows through those measurement stations. That information is generally updated hourly with about a two or three-hour lag, so we can get a rough idea.

These rough volume measurements do have to be adjusted by certain calculation factors for Btu content and some other things, and verified that the actual measurement calculation in the software and in the computer system is properly calculating. But subject to those changes, we have a, you know, a reasonable idea of what our demand is on the system at any point in time with the two or three-hour delay.

So we monitor that constantly, every single day, plus we have -- we forecast based on what the weather is, what that demand is every single day. So we're constantly looking at what was actuals for the day before, what's happening today versus what we projected was supposed to happen today, what was the weather today versus what we thought it was going to be today, what's the change in the forecast going forward today versus what we thought it was yesterday.

It's constant, you know, updating for actuals that you have, updating for new forecasts that you have, that sort of thing. So it's --

Q. You gave an answer to Judge Woodruff about Williams giving you a recalculation of these volumes on December 13th that I got the impression from your testimony that you were not expecting a calculation of that significance and deviation. So that's why -- so let's talk for a second about that.

Did you have any warning from Williams that they were going to do a revision of the magnitude they did?

A. No.

Q. And can we put into perspective how great of a magnitude of a correction this was?

A. It was probably about the second largest correction that I've seen on the Central system for MGE's properties.

Q. Let's try to put this into perspective. When you saw this, was this -- was your reaction, okay, that will be fine, we'll deal with that, or more towards, my God, Williams has just thrown a grenade at me, or somewhere in between?

A. Yeah, it was -- it was fairly -- it was a very significant change, which was in the absolutely wrong direction for us at that point in time. So, yeah, we immediately started looking at what were our options to try to deal with the storage.

Unfortunately, by the time we got the information, prices in the day market were extremely high and, you know, we felt that somewhat limited our options. It was not going to be very economic for us to try to deal with at that point in time, but we did increase our planned flowing gas in January.

Q. So is it fair to say that you went through some sort of a contingency planning at that point, once you knew that the storage withdrawals had been actually greater than you were able to estimate, and you and your people had discussions about, what if we do this, what if we do that? Is that accurate or not?

A. Yes, it's accurate.

Q. And what options did you have at that point?

A. Our options were that we had already begun purchasing some incremental supplies, based on our previous, you know, issues with the 20 million a day that we had short

December 1. Our options were a greater level of incremental supply or to look to nominate additional volumes January 1.

Q. And which did you pick?

A. We elected to purchase more volumes January 1.

Q. And was that a reasonable thing to do, based on what you knew at the time?

A. I think so. We were looking at some -- some daily prices that were, you know, over $11 for the incremental supplies that we were purchasing. You know, while we were certainly at unprecedented levels, we could not imagine that prices would be higher than those levels in January.

Q. Did you -- in retrospect, did you do anything wrong in reacting to that notice from Williams? I mean, would you have done it differently if you had to do it over again?

A. No, I don't think so.

Q. Did the fact that the weather in November and December 2000 -- I believe it's been testified to that that was the coldest 60-day period on record. Was that a contributing factor to this situation, do you believe, or not?

A. Relative to the Williams adjustment, I can't say whether or not that really was affecting their allocations and their measurement. I wouldn't think the weather would have -- would -- I think there was some other error that occurred on the Central system. Certainly relative to our overall storage demand, it was directly driven by weather during that time period.

Q. I'm trying to get a picture here. We have weather at record cold. We have this significant change from Williams. Are these things -- are these factors coming together at the worst possible time for you, in terms of planning for things, or are they totally unrelated and you could deal with either one of them?

I'm trying to get a feel for whether this was a -- you know, what was the -- how would you characterize this period in the interaction at least?

A. Well, where -- as we were coming out of the end of November and our original estimate showed that we were not far off of our storage plan, and we made a small adjustment for December which we felt would accommodate that. By the time we got into December, it was much colder than we had expected there, plus we had the storage adjustment from Williams. We were then looking at some overall major impacts on our storage inventories.

Now, from a reliability standpoint, again, while we have limitations on our injections in the Williams storage as the season goes forward, we don't have any limitations on our withdrawal capability in Williams storage. So we weren't concerned about our ability to meet a peak day, even in the event of this cold weather. So the cold weather in and of itself was not going to be reliable, our deliverability, our ability to take gas out of storage.

What we were concerned about was overall inventory levels, which were, at that point in time, below our planned levels. So, you know, our options were to, you know, take steps to then adjust what our planned storage withdrawal levels were going forward, which we did.

Q. So you tried to preserve the storage gas that you had in storage for the possibility of further unexpected occurrences later on, and instead you substituted that with some sort of flowing or daily supplies or swing supplies; is that right?

A. Right.

Q. That was the plan to try to deal with it?

A. Yes.

Q. Mr. Schwarz asked you some questions on cross-examination and the implication I got from them, these were the questions about, well, what are the cash flow implications of taking gas from storage as opposed to going out and buying, I'll call it fresh gas in the market.

And the implication that I got from Mr. Schwarz's questions were that MGE's management somehow perceived that it was in a cash flow crunch and that maybe you were given some direction to protect the cash flow problems that MGE was having, and so --

MR. SCHWARZ: I'm going to object to his characterization of my questions.

MR. DUFFY: Well, I'm asking a question based upon my understanding and my implication of what I got from his questions, and then I'm going to ask the witness whether that implication that I thought -- that I got is accurate or not.

JUDGE WOODRUFF: I'm going to overrule the objection, because it's a question from counsel, and I'm going to allow him to go ahead and answer the question that he wants to ask. If you have an objection to the response from the witness, make it at that time.

Go ahead and answer the -- go ahead and complete your question.

MR. DUFFY: Okay. I'll try to pick up, I think, where I left off.

BY MR. DUFFY:

Q. I got the impression that the tenor of Mr. Schwarz's questions were that MGE was in a cash flow problem, that maybe you were given some directions from management to try to alleviate that problem and, therefore, you were given directions to pull gas from storage to better MGE's cash flow position, as opposed to going out and buying new gas which might, under some scenario, hurt MGE's cash flow at that time.

Now, as I said, that was simply my impression from listening to those questions. My question to you is, were there any cash flow implications or were there any -- did you make storage withdrawal decisions in November based upon cash flow considerations or did you make them based upon other considerations?

A. No. We don't ever make storage -- operational storage withdrawal decisions based upon cash flow issues.

Q. Has management ever told you even to do something like that?

A. No.

Q. Do you remember whether there was a cash flow problem at that time or not?

A. You know, Southern Union has a whole cash management group. They would have been responsible for that. I have no idea what the status of Southern Union's cash flow was.

Q. You gave several responses to the questions on cross and from the -- maybe from the Bench, I don't remember -- at least on cross, to MTL-16, which is attached to your direct testimony. Do you remember that?

A. Yes.

Q. What was the -- your intent or what was the purpose of including all of the stuff that's in MTL-16, just briefly?

A. It was an attempt to try to, you know, outline kind of key decision points that we were facing as we got information throughout the winter period and, you know, at least the significant changes that we made as we stepped through the winter, whether it be to flowing gas, storage plans, that sort of thing.

Q. Would it be fair to say it was an attempt to show -- well, let's back up.

You gave that document to the Staff early on in this ACA process, or at least before we were filing testimony, didn't you?

A. Yes.

Q. And was your intention to show the Staff what MGE knew, when it knew it, and what it did about what it knew when it knew it?

A. Yes.

Q. And why did you give that to the Staff in that particular format at the time that you did?

A. You know, my view is that what the Staff's questioning here is our decision process regarding our -- on the storage issues regarding our use of storage. To that end -- and also some of the decisions that were made relative to November, December, January particularly.

In that regard, I was attempting to outline, well, you know here's the steps that we took and, you know, from our perspective, all of the steps and decisions we made were reasonable at the time. Were they all correct? No. But they were reasonable at the time we made them, based on what we knew.

Q. Okay. You were asked a question about the price stabilization program, and I believe you cited it as Case No. GO-97-409. And I heard, I think, an answer -- maybe it was in the question -- that it was a three-year program. Do you remember that?

A. Well, no. Let me --

Q. Well --

A. If I stated that, that was an error.

Q. Okay. Was it, in fact, a three-year program or was it a program that got renewed each year for three years or something different?

A. The price stabilization fund program was implemented annually. I mean, it was only implemented for a one-winter-season period, and then it had to be terminated on its own terms. So it had to be reauthorized each year, and it was for a -- it was ultimately authorized for a total of three individual annual periods or three individual winter seasons.

Q. So if there was implication previously in anybody's question or answer that it originally was intended to be a three-year program, that would be wrong?

A. Yes. If I -- if I stated that, I misspoke. The original incentive mechanism that was authorized in GO-94-318 was for a three-year program which ran from July 1, '96 through June 30th of '99. I may have gotten those two terms messed up.

Q. I'll jump back to the reliability report topic, just briefly, because you were asked some questions, I think, about what was marked as Exhibit 22. And my question is, do any of the reliability reports that MGE has provided contain a description or a representation of the process on how MGE dispatches either flowing supplies or manages its storage?

In other words, are they intended to be a depiction of an operating manual of how this occurs or something else?

A. No, it's not intended to be an operating document.

Q. Pardon me if I asked this before, but I want to take you back again to December 13th, 2000 and December 14th, when you got this notice of a revision from Williams. Was there any warning that that was going to happen before that happened?

A. Well, I mean, we were constantly pressing

Central to -- to get us the information of what the actual storage allocations were. So we were expecting to get the storage report, but we were not expecting the revisions that were contained therein.

Q. Was the report late?

A. Yes. We had generally received it a little bit earlier previous to that time.

Q. But nobody at Williams told you, look out, this big number's coming at you?

A. No.

MR. DUFFY: Just a second. That's all the redirect I have.

JUDGE WOODRUFF: All right. Before you step down, there's a couple exhibits that we need to deal with as well.

Exhibits 21HC and 22 were not offered?

MR. SCHWARZ: I would offer them at this time.

JUDGE WOODRUFF: All right. Exhibit 21HC and 22 have been offered into evidence. Are there any objections to their receipt?

MR. DUFFY: I don't think I have, but let me just make sure. Okay. Those were those DR responses, right?

JUDGE WOODRUFF: Yes.

MR. DUFFY: No, I have no objection to them.

JUDGE WOODRUFF: All right. 21HC and 22 will be admitted into evidence.

(EXHIBIT NOS. 21HC AND 22 WERE RECEIVED INTO EVIDENCE.)

JUDGE WOODRUFF: And we've also got 19HC and 20HC.

MR. SCHWARZ: I have spoken to MGE and counsel and have -- physically the documents on Exhibit 19HC I distributed yesterday to the Commission and the court reporter and to the other parties full copies of those reports.

What we will actually ask to be submitted is the cover page to provide an identification, and with respect to 19HC, then pages 11 through 16 of that document, which remain highly confidential but don't have the additional proprietary problems.

JUDGE WOODRUFF: So counsel for KPC can see those?

MR. SCHWARZ: He can see those, and I've got those.

And with respect to 20HC, it's the cover page and then pages 8 through 12. No. Excuse me. 11.

JUDGE WOODRUFF: Are you going to make new packets of documents to distribute?

MR. SCHWARZ: I can do that. The Commission --

JUDGE WOODRUFF: They're all sitting right here.

MR. SCHWARZ: Oh, if you've got them right there, I would be glad to do so.

MR. DUFFY: I was going to ask about how do we go about retrieving -- since we're essentially substituting a couple of pages for 40 or 50 pages, are we going to retrieve the ones that were -- that are not going to be the exhibit so there's no confusion?

JUDGE WOODRUFF: I think that would be best to retrieve all the documents. And I'll ask the court reporter when she's not typing to do that for you. And I believe I have all the copies here that were given to the Bench. So then after the break -- by the way, we're going to take a break in a moment here -- we can go ahead and replace those.

MR. SCHWARZ: If it's suitable, we can do that over the lunch hour.

JUDGE WOODRUFF: That will be fine. That will be fine. Okay.

MR. KEEVIL: If I can interrupt just briefly. I haven't seen the revised thing, so I don't know if I will have any objection to --

JUDGE WOODRUFF: I'm not asking for objections at this time. We'll deal with that after we actually get the revised copies. So we'll deal with 19 and 20 later on.

You can step down.

(Witness excused.)

JUDGE WOODRUFF: We'll take a break. We'll come back at 11:05.

(A BREAK WAS TAKEN.)

JUDGE WOODRUFF: We're back on the Internet and we're back on the record. We had just concluded the testimony of Mr. Langston, and I believe Staff can call their first witness.

MR. SCHWARZ: Staff calls Mr. John Herbert.

(Witness sworn.)

JUDGE WOODRUFF: You may be seated. You may inquire.

JOHN HERBERT testified as follows:

DIRECT EXAMINATION BY MR. SCHWARZ:

Q. Would you state your name for the record, please.

A. John H. Herbert.

Q. And what is your occupation?

A. Independent consultant, adjunct professor of statistics and adjunct professor of finance, first at Virginia Tech, secondly at Johns Hopkins University.

Q. And you are testifying on behalf of the Staff of the Public Service Commission in this case?

A. Correct.

Q. And did you cause to be prefiled in this case what has been marked Exhibit 6, the direct testimony of John Herbert, Exhibit 7, which is the rebuttal testimony of John Herbert, and Exhibit 8, which is the surrebuttal testimony of John Herbert?

A. Correct.

Q. Do you have any corrections to that testimony?

A. No.

Q. If I asked you the same questions today, would your answers be essentially the same?

A. Yes.

Q. And are those answers true and correct to the best of your information, knowledge and belief?

A. Yes.

MR. SCHWARZ: I would offer Exhibits 6, 7 and 8 into the record at this time.

JUDGE WOODRUFF: Exhibit 6, 7 and 8 have been offered into evidence. Are there any objections to their receipt?

(No response.)

JUDGE WOODRUFF: Hearing none, they will be received into evidence.

(EXHIBIT NOS. 6, 7 AND 8 WERE RECEIVED INTO EVIDENCE.)

MR. SCHWARZ: And I tender the witness for cross-examination.

JUDGE WOODRUFF: Thank you. And for cross-examination, then, we will begin with City of Joplin, and counsel for Joplin is not here.

Public Counsel?

MR. MICHEEL: No questions. Only friendly ones.

JUDGE WOODRUFF: KPC?

MR. KEEVIL: No questions at this time, Judge.

JUDGE WOODRUFF: MGE?

MR. DUFFY: Yes, your Honor.

CROSS-EXAMINATION BY MR. DUFFY:

Q. Good morning, Mr. Herbert.

A. Good morning.

Q. I want to focus on how prices are set in the first-of-month market and the intra-month market. Would you agree that first-of-month prices are, at least partially, a function of market participants' expectations regarding supply and demand?

A. It's a combination of their knowledge of supplies relative to expected demands.

Q. After first-of-month price has been set, if actual demand turns out to be less than expected, would you agree, all other things being equal, that this would be expected to put downward pressure on intra-month gas prices, as compared to first-of-month prices?

A. Depends on the conditions, the supply conditions in the market.

MR. DUFFY: That's all the questions I have. Thank you.

JUDGE WOODRUFF: All right. Thank you. I have a few questions from the Bench.

QUESTIONS BY JUDGE WOODRUFF:

Q. From reading your testimony, I get the impression that your philosophy is that hedging should be -- is an essential element for any gas company in dealing with supply and prices. Is that a fair characterization?

A. It's an important thing for them to consider. The larger the company, the more depth the Staff has, of course, the greater the likelihood you expect them to have in place a strong price risk management program.

Q. Okay. I also got the impression that you believe hedging is important to -- based on the amount of volume, not just on the price that you can get the hedging at. Is that fair?

A. Very much so.

Q. So that a company should -- should hedge even if the price at the time is high, assuming there's going to be volatility?

A. Exactly. It's pretty hard not to assume volatility.

Q. Okay.

A. So yes.

Q. There's always volatility?

A. Most definitely.

Q. When did you first -- when were you first engaged by the Commission Staff?

A. Almost two years ago.

Q. Okay. So that would have been after the winter of 2000-2001 that we're talking about?

A. Correct.

Q. Do you know if your current -- if your philosophy on hedging was Staff's philosophy on hedging before the winter of 2000-2001?

A. Was my philosophy of hedging similar before 2000?

Q. I'm not asking your philosophy. I'm asking what Staff's philosophy on hedging was before that watershed winter?

A. Well, the impression I have was that they also thought that hedging was important.

Q. Okay. Now, there's been some testimony in this case that there was some negotiations between Staff, Public Counsel and MGE in the summer leading into that winter of 2000-2001 about whether or not prices -- the trigger price should be upped on the -- on the gas -- I forget what it's called -- the gas price protection.

A. I can never get -- I tend to forget the names of things. I can remember --

Q. You know what I'm talking about?

A. -- details beautifully, yeah.

Q. Do you have any opinion as to whether Staff might have or should have been able to or should have agreed upon the higher price, a higher trigger price?

A. No, I have no opinion on that.

Q. Okay. Now I want to ask you about your 30 percent hedging guideline or standard or whatever you want to call it. Why was 30 percent chosen?

A. In a meeting I pushed for 70 percent of normal, because I considered that to be sort of a real rough indicator of what would be requirements during a warmest heating season month for most utilities. Then the point was made, well, we're trying to come up with something that's reasonable and considered for all companies, because at that time we'd just been talking about this sort of thing.

And so, then, more or less lower numbers were considered, and then the 30 percent normal number when it was mentioned, my problem with that is there'd still be a lot of exposure of customers, and exposure is the volumes, what's at risk. And nonetheless, since I had limited knowledge of all the companies at that time, basically said that seems to be a reasonable lower bound. It's something certainly that's worth considering.

Q.   So 30 percent isn't any sort of magic number? It could be 29 or 31 or --

A.   Yeah. My experience with other companies, for example, it's higher. Or I think that's -- yes.

Q.   Okay. There's also been some question about applying that 30 percent standard monthly rather than overall. Can you explain why you believe it should be applied monthly rather than overall?

A.   Yeah, because the exposure varies by month. That's one reason. Another reason, there's always an opportunity, there's always a chance that instead of, for example, a fixed price contract, the company would enter into futures contracts in the future, and to fix the price up there, it's essential that the volumes that you purchase be consistent with the volumes under that hedging contract, that futures contract.

So volumes which vary by month, and to me it's analogous to if I have a house that's 2,000 square feet, everything else being equal, I know that my exposure is higher than -- to a variety of damages, tornadoes, fire, what have you, than someone that has a household of 1,000 square feet. I have more risk exposure, and that's why I expect it to cost me more for that insurance.

Q. Okay. Now, if -- for example, it's my understanding in February of that winter of 2000-2001, prices were dropping throughout the month. Is that fair? Is that correct?

A. I've got a figure, several of them, in my testimony.

Q. I'm not really concerned about exact figures, but is that generally true that prices were dropping in February?

A. I believe so, yes.

Q. Okay. So if the company had purchased hedging instruments at the first of February, they would have not finished in the money in that the prices were dropping, so their hedges would have -- with the benefit of hindsight, their hedges would have been unnecessary. Is that fair?

A. Yeah, they wouldn't -- maybe say -- or just elaborate slightly. The natural position for the utility under that futures contract would have been to be buying before February for the right volumes of gas to be hedged. Then prices slide throughout February. You can view that closing out of that futures position of selling at that time, and the prices, as you characterized it, had declined. So you'd be selling at a price which was lower than what you bought. So in that sense, that time, prices declined.

Q. Is it analogous to buying fire insurance and not having a fire?
A. Yeah.
Q. And obviously there's a value in having fire insurance even if you don't have a fire?
A. Exactly.
JUDGE WOODRUFF: I don't believe I have any other questions. So we'll go to recross. Again, Joplin's not here.
Public Counsel?
MR. MICHEEL: No questions, your Honor.
JUDGE WOODRUFF: KPC?
MR. KEEVIL: No questions, Judge.
JUDGE WOODRUFF: MGE?
MR. DUFFY: Could I have just a minute?
JUDGE WOODRUFF: Sure.
MR. DUFFY: No questions, your Honor.
JUDGE WOODRUFF: Redirect?
REDIRECT EXAMINATION BY MR. SCHWARZ:
Q. I'd like to expand a little bit, if I might, on the Judge's question about the February hedging. If the company had purchased a call option for February gas, that's based on the first-of-the-month price; is that correct?
A. If it purchased a call option?
Q. Right. For --

A. The call option would have been whatever the relevant price is, whatever the strike price would have been in that call option. So that's -- and then it's a matter of whether or not when February rolls around the price is above that or below that strike price. And I guess you can view it as the price you can call the gas at.

Q. But that's determined at the first of the month. So a call option, a February call option, February 1st you know if it's finished in the money or out of the money; is that correct?

A. No. Well, it's actually prior to -- right, the options contract closed out prior to the futures contract. And this is different for the gas industry, by the way. This goes on simultaneously. So for February delivery, okay, for February delivery, the contract would close out end of January sometime. So it's whatever the relevant price at that time is. Now, that's near mid week first of the month. So there is some overlap.

Q. But by February 1st you're going to know if that call option finished in the money or not?

A. You would know prior to that, because the contract -- in other words, you would complete or you would close out that contract prior to February 1. You would know what February's delivery prices are, but you know that the end of January.

MR. SCHWARZ: I have nothing else.

JUDGE WOODRUFF: All right. You may step down.

And Staff can call its next witness.

MR. SCHWARZ: Staff calls David Sommerer.

(Witness sworn.)

JUDGE WOODRUFF: You may inquire.

DAVID SOMMERER testified as follows:

DIRECT EXAMINATION BY MR. SCHWARZ:

Q. Would you state your name for the record, please.

A. David Sommerer.

Q. And by whom are you employed?

A. The Missouri Public Service Commission.

Q. And what is your position with the Commission?

A. I'm the manager of the procurement analysis department.

Q. And are you the same David Sommerer who caused to be filed Sommerer direct, Exhibit 9NP and 9HC, Exhibit 10, rebuttal, and Exhibits 11NP and HC, which are your surrebuttal testimony?

A. Yes.

Q. Do you have any corrections?

A. No.

Q. If I ask you the same questions today as are contained in your prefiled testimony, would your answers be the same?

A. Yes.

Q. Are those answers true and correct to the best of your information, knowledge and belief?

A. Yes.

MR. SCHWARZ: I would offer Exhibits 9NP and 9HC, Exhibit 10 and Exhibits 11NP and 11HC.

JUDGE WOODRUFF: I show 10 as being both NP and HC. Am I incorrect?

MR. DUFFY: I think there's just one.

MR. MICHEEL: You're incorrect, Judge.

JUDGE WOODRUFF: I am incorrect. Okay. I must have been in -- all right. It's just 10, not 10NP and HC?

MR. SCHWARZ: Correct.

JUDGE WOODRUFF: Okay. Exhibit 9NP and 9HC, Exhibit 10, Exhibit 11NP and HC are offered into evidence. Are there any objections to their receipt?

(No response.)

JUDGE WOODRUFF: Hearing none, they will be received into evidence.

(EXHIBIT NOS. 9NP, 9HC, 10, 11NP and 11HC WERE RECEIVED INTO EVIDENCE.)

MR. SCHWARZ: I tender the witness for

cross-examination.

JUDGE WOODRUFF: All right. And for cross-examination, we'll begin with -- again, Joplin's not here.

Public Counsel?

MR. MICHEEL: No questions.

JUDGE WOODRUFF: KPC?

CROSS-EXAMINATION BY MR. KEEVIL:

Q. I don't know whether to try to adjust this thing or just give up. Give up.

Okay. Good morning, Mr. Sommerer.

A. Good morning, Mr. Keevil.

Q. I only have a couple of questions for you, I hope. My questions pertain to the Staff's proposed capacity release adjustment. And first let me ask you if you recall having your deposition taken in this case back in, looks like December of last year?

A. Yes.

Q. All right. Do you recall -- strike that.

Let me just tell you that at that time --

MR. KEEVIL: Counsel, do you have a copy of that?

MR. SCHWARZ: I don't know that I brought a copy of his deposition.

MR. DUFFY: Are you talking about the

deposition?

MR. KEEVIL: Yeah.

MR. DUFFY: I have some copies.

MR. KEEVIL: Well, this is -- I don't think it will be a problem. Let's try it and see.

BY MR. KEEVIL:

Q. Mr. Sommerer, let me propose or submit to you that during your deposition I posed a question to you in regard to the capacity release adjustment that -- and I'll see if I can quote from the deposition here.

MR. SCHWARZ: What page are you on?

MR. KEEVIL: This is page 148, toward the bottom, beginning on line 15 or 16.

BY MR. KEEVIL:

Q. My question to you at the deposition, Mr. Sommerer, was that it doesn't seem to me that Staff really cared or would have cared whether MGE released capacity on Kansas Pipeline or on Williams Pipeline. The point you were trying to make is, there should have been a capacity release. And my question was, is that fair, meaning is that a fair statement of Staff's position, and your answer was, that's correct.

Do you recall that, Mr. Sommerer?

A. Yes.

Q. If I were to ask you that question here today,

would your answer be the same?
A. Yes.
Q. Now, as I understand it, also in relation to that adjustment, Mr. Sommerer, the amount of the adjustment was quantified based on a release of capacity on the Williams pipeline system; is that correct?
A. That's correct.
MR. KEEVIL: I think that's all I have. Thank you, sir.
JUDGE WOODRUFF: All right. Then for MGE?
MR. DUFFY: Your Honor, I have a fair amount of cross for Mr. Sommerer. I'm wondering if we couldn't take the lunch break at this point, since I would get into it and then we'd have to break.
JUDGE WOODRUFF: Very well. It's now 11:30.
We'll take a break for lunch and come back at one o'clock. Thank you.
(A BREAK WAS TAKEN.)
JUDGE WOODRUFF: We're back after lunch and Mr. Sommerer is on the stand, and MGE is about to begin its cross-examination.
You may proceed.
MR. DUFFY: Thank you.
CROSS-EXAMINATION BY MR. DUFFY:
Q. Good afternoon, Mr. Sommerer.

A. Good afternoon, Mr. Duffy.

Q. In the May 31st, 2002 Staff official case filing, the Staff said that, quote, MGE should have posted for release to other shippers its idle capacity on Kansas Pipeline Company, KPC, for the months of April through October, unquote, for the ACA period in question in this proceeding, right?

A. That's correct.

Q. You generally describe the capacity release process on pages 4 and 5 of your direct testimony?

A. Yes.

Q. You said there on page 4 that the Federal Energy Regulatory Commission requires that capacity release transactions be posted for bid on the interstate pipeline's electronic bulletin board unless certain conditions are met?

A. That's correct.

Q. The FERC regulates the rates and terms and conditions of service of what we are calling the KPC pipeline in this case, right?

A. That's right.

Q. You talked in your direct testimony on page 5 about MGE paying a reservation charge to reserve a level of capacity on KPC and that MGE pays these charges each month of the year, regardless of whether MGE uses the capacity, right?

A. That's correct.
Q. The capacity that MGE has on KPC is approximately 46,000 decatherms a day?
A. That's correct.
Q. And just for reference purposes, a decatherm is what in terms of MMBtus for round general purposes?
A. A decatherm is usually considered equivalent to an MMBtu.
Q. The reservation charges or capacity charges that you talked about are determined by the FERC, correct?
A. That's correct.
Q. And they're determined in a rate case at the FERC in a process similar to how this Commission sets rates for utility companies?
A. Yes.
Q. So just as customers of MGE must pay the rates set by this Commission for MGE's gas service, MGE must pay the charges that the FERC sets for capacity reservation on KPC?
A. That is correct.
Q. MGE uses that KPC capacity in the winter in order to bring natural gas into Kansas City to serve MGE's customers?
A. That's correct.
Q. MGE is then a shipper or transporter on the

KPC pipeline?

A. That's also correct.

Q. But MGE has not been using that pipeline in the summer months because there is not as much demand for natural gas in Kansas City in the summer as there is in the winter, right?

A. That's correct.

Q. And the FERC created this capacity release process to try to address the situation where a shipper could offer its reserved but temporarily idle capacity to other people when the shipper did not need it for its own purposes, correct?

A. That's also correct.

Q. Would you agree with me that that process is generally like subletting an apartment -- subletting an apartment that you're renting?

MR. SCHWARZ: I'll object. That calls for a legal opinion on the part of the witness.

JUDGE WOODRUFF: Overruled.

THE WITNESS: I think you can make an analogy to that circumstance, yes.

BY MR. DUFFY:

Q. A shipper can either post a public notice that he's willing to let someone else use its capacity for a certain period or it can make a private deal with someone

else to use it, correct?
A. That's correct.
Q. You told me in your deposition that we took back in December, I think, that the primary reason you proposed this disallowance is because you discovered that MGE was no longer using the KPC capacity in the summer, and you questioned whether there was an opportunity to release the capacity in the capacity release market. You said you wanted to know if there was some value that could be derived from that pipeline since it was not being used; is that correct?
A. That's correct.
Q. You also told me in the deposition that it took several years' worth of data before you became convinced that the pipeline was not being used in the summer months; is that right?
A. I'd like to refresh my recollection on that. Do you have a page?
Q. I do. Look at page 22, lines 1 through 12, if you have that handy. And I'll be glad to read the question again after you've read lines 1 through 12 on page 22 of your deposition.
A. I agree with the question. That's correct.
Q. You also told me in the deposition that the Staff was aware in previous ACA periods that this capacity

was not being used?

A. That's correct.

Q. Your proposed adjustment regarding a capacity release on Kansas Pipeline Company necessarily assumes that there was someone out there that would be willing to purchase MGE's idle capacity on that pipeline during the summer months?

A. Yes.

Q. Let's take a look briefly at your direct testimony, and I want to look at Schedules 2-1 and 2-2. Let's look first at Schedule 2-1. Are you ready?

A. I'm there.

Q. Okay. On Schedule 2-1 there is a date stamp showing the Staff received that document on May 1, 2002, correct?

A. That's correct.

Q. On Schedule 2-2, which is apparently an attachment to that, that's a letter from the management of what we're calling Kansas Pipeline Company or KPC in this proceeding; is that correct?

A. That's correct.

Q. Do you recognize that Joan Schnapp, the signatory to that letter, as being a witness for KPC in Case No. GR-96-450 that we tried back in November of 2001?

A. Yes.

Q. Ms. Schnapp's letter there on Schedule 2-2 says there has never been a capacity release transaction on KPC since its inception as an interstate pipeline on June 1, 1997, doesn't it?
A. That's correct.
Q. And on Schedule 2-1, the response tells you that MGE posted capacity on KPC for release in 2002 and got no responses to that posting, correct?
A. That's correct.
Q. So according to the date stamp on Schedule 2-1 the Staff has known for more than a year now that there has never been a capacity release on KPC since its inception as an interstate pipeline in 1997 and that MGE got no responses when it posted that capacity for release on KPC; is that correct?
A. That's correct to the extent that this request is current through today.
Q. So the Staff knew at the time the Staff memo was filed in this case back on May 31st, I think we said, May 31st, 2002, that there had never been a capacity release on KPC and there had never been a response to an MGE posting offering to release that capacity; is that right?
A. That's correct.
Q. You admitted in your deposition back in November that you had no evidence, no documentation,

information or anything that shows somebody out there wanted or even asked for this KPC capacity that you say MGE should have released; is that right?

A. I'd clarify that I believe the deposition was in December rather than November, but subject to that change, that's my recollection of the response, yes.

Q. Okay. I was supposed to say deposition in December. If I said November, I misspoke and I apologize.

In that May 31st memo to the case file of the Staff, it said that, quote, another option would have been for MGE to post a nonrecallable release of capacity on Williams pipeline and source the replacement gas on KPC, unquote; is that correct?

A. That's correct.

Q. So you're saying that MGE should have posted for nonrecallable release its Williams capacity and then utilized its KPC capacity for the same amount of volumes instead; is that correct?

A. To the extent that it would have been economical to do so, that is my testimony, yes.

Q. When you included that language in the Staff memo of May 31st, it didn't have any qualifier about to the extent that it was economical to do so, did it?

A. That's correct.

Q. For your proposed disallowance in this case regarding the capacity release issue, you made the assumption that MGE could have received 75 percent of the maximum Williams tariff rate as revenue for the capacity that MGE could have released on Williams, correct?

A. I would clarify that by saying that was 75 percent of the maximum Williams reservation rate.

Q. Why did you give me that clarification when I referred to it as the Williams tariff rate?

A. Williams has two or three tariffed rates. They could have a commodity rate, a rate for fuel or a percentage for fuel and a reservation charge.

Q. So you wanted to be more exact that you're focusing on the reservation or capacity charge, as opposed to some other rate?

A. Exactly.

Q. Would it be okay if I referred to that, with your clarification, as the Williams maximum tariff rate in the rest of my questions?

A. That would be fine.

Q. To support your assumption MGE would have obtained 75 percent of the maximum tariff rate for releasing its Williams capacity and utilizing its KPC capacity, you attached Schedule 2 to your surrebuttal testimony; is that correct?

A. Schedule 2 to my surrebuttal testimony is a listing of Williams capacity release transactions for that time period.

Q. And I assume that you attached it in order to support your assumption and your position that MGE could have obtained 75 percent of the Williams maximum tariff rate? That was the purpose why you attached it, to show that could occur?

A. That's correct.

Q. Let's look at the Schedule 2 to your surrebuttal, and it's comprised of, what, 47 pages of what's designated HC material; is that right?

A. Yes.

Q. And is it true that this document purports to be all of the transactions that are listed on the Williams electronic bulletin board, all of the capacity release transactions on that bulletin board for a specific one-year period of time?

A. That's correct.

Q. And that one-year period of time matches the ACA period in GR-2001-382?

A. Yes.

Q. And that would be July 1, 2000 through June 30, 2001?

A. July 2000 through June 30 of 2001.

Q. Okay. In Schedule 2 -- and I'm not asking you to reveal anything that may be considered highly confidential here. In Schedule 2 to your surrebuttal, the fifth column on all of those sheets has a heading that reads biddable, yes/no, does it not?

A. That's correct.

Q. A Y designation in that column means that the capacity was posted for bidding, and an N means that the capacity was released as a prearranged transaction; is that correct?

A. That is correct.

Q. The sixth column heading reads maximum rate, does it not? It says max rate on EBB?

A. Yes.

Q. The figures in that column represent the maximum tariff rate that the releasing shipper is required to pay?

A. That's correct.

Q. The seventh column reads, min rate on EBB. That represents the actual rate at which the capacity release transaction was consummated, doesn't it?

A. That's correct.

Q. If there is no information in the seventh column, then the capacity was released at the maximum rate?

A. That's my understanding, yes.

Q. Conversely, if there is information in the seventh column, the transaction was conducted at less than the maximum tariff rate?

A. Yes.

Q. Williams has a market area and a production area for which it has separate rates?

A. That's correct.

Q. That is the distinction that appears in the tenth column called area?

A. Yes.

Q. A P in that column stands for production area and an M stands for market area?

A. Yes.

Q. Generally, would you agree that Wichita is about the boundary between the production and the market areas on Williams?

A. That's my recollection, yes.

Q. The 13th column in that schedule reads recall code. The information that is provided by Williams in that column is whether the capacity is recallable or nonrecallable, correct?

A. That is correct.

Q. You have pointed out that the recall codes are noted on the last page of each month; for example, on Schedule 2-4. Isn't it true that either an O designation or an N, as in Nancy, designation in the recall code column represents a nonrecallable transaction?

A. That is not correct.

Q. An O represents a transaction whereby the replacement shipper has the right to put the capacity back to the original shipper, doesn't it?

A. An O represents a recallable release where, at the option of the replacement shipper, the capacity can be reput to the releasing shipper.

Q. So are you telling -- so is an O a recallable transaction or a nonrecallable transaction, in your mind?

A. If you could allow me just a few seconds to double check that, I believe the O represents capacity that's recallable by the releasing shipper and reputtable at the option of the replacement shipper.

Q. So is O recallable or nonrecallable?

A. Recallable.

Q. Is N recallable or nonrecallable?

A. Nonrecallable.

Q. From the perspective of a releasing shipper such as MGE, wouldn't an N and an O transaction both be considered nonrecallable?

A. Not in my opinion, no.

Q. The 14th column has a heading, begin term. That information is the beginning date of the capacity release transaction; is that right?

A. That's correct.

Q. Did your counsel provide you with a document that we provided to your counsel yesterday morning in which we attempted to locate some transactions off of your Schedule 2 and sorted by whether they had a recall code of N and a recall code of O?

A. I believe I have that document in front of me.

Q. Okay. Does that show that there were five transactions that had a recall code of N, which means -- and I believe you agreed -- those are nonrecallable transactions?

A. I have agreed that those are nonrecallable transactions with a recall code of N, but the five transactions look to me to be short of the total number, if this is an attempt to summarize the total transactions that have a recall code of N.

Q. How many transactions had a recall code of N on your Schedule 2?

A. I haven't counted them, but they are numerous.

Q. If you then put in a criteria that the transaction occurred during this ACA period, would that reduce the number?

A. Yes, I think it would.

Q. Let me put it this way: Did you find any -- what transactions did you find on your Schedule 2 that you think met the criteria that you posed that MGE should have posted nonrecallable capacity on Williams during this ACA period? How many transactions did you find that you contend were similar or substantially similar to ones that MGE could have participated in?

A.   Generally speaking, I use this schedule to support the fact that nonrecallable releases tended to be released at the maximum Williams rate, and I didn't specifically concentrate on the specific time period, although there are some transactions that do cover the ACA period.

But I really pulled this schedule or downloaded this schedule from the Williams bulletin board in order to show that the majority of releases that are coded nonrecallable occur at a maximum rate.

Q.   With what you just said, are they also biddable? Did you determine how many of those met that criteria and also are biddable?

A.   No, I did not.

Q.   Do the one, two, three, four, five that we listed on this document that you've seen, are those all listed as biddable, meaning they have a Y in the posted biddable column and they also have an N in the recallable code column?

A.   For those five transactions that you have listed on that document, it appears that the releases were biddable.

Q. Do you have reason to believe there were other transactions in your Schedule 2 that were both biddable and had an N for nonrecallable and at least occurred during the ACA period in question here? Do you know of any?

A. I think there are examples of both. If you look at Schedule 2-1 -- and I think in order to be specific about it, I probably will have to -- I can give you some offer numbers.

Q. Well, why don't you give me an offer number so we can at least see what you're talking about?

A. Okay. If you take a look at the section of releases from Offer 225 through 257, it's about seven, seven or eight, you'll notice that the release was at maximum, and the biddable designator shows that it was nonbiddable or prearranged release. And the recall code, if you go over to that, there's an example of nonrecallable.

Q. Well, you just said that these were prearranged. These were not posted on the electronic bulletin board, and the basis for your disallowance is that MGE didn't post it on the electronic bulletin board.

So these are not comparable to what you said MGE should have done, because these were prearranged transactions; isn't that right?

A. I think that posting can be broader than that. Williams requires -- actually, FERC rules require that posting occurs for nonbiddable releases to the extent they're greater than 30 days in length.

Q. What was the size of those transactions?

A. The greatest level or size or volume associated with the transaction would be 157. There were several transactions that were 14.

Q. But the transaction we're talking about that you think MGE should have done was 46,000, was it not?

A. That's correct.

Q. So 46,000 is not comparable to 14 or 157, is it?

A. That's correct.

Q. When you were developing your proposal to include in the Staff recommendation in this case filed on May 31, 2002, was the material in your surrebuttal Schedule 2 available to you?

A. My recollection is it was, yes.

Q. When you made your proposal, did you evaluate what the financial result would have been if MGE would have released 46,000 decatherms of its Williams capacity on a nonrecallable basis at less than 15 percent of the maximum rate on Williams and used an equivalent volume of its KPC capacity?

A. No, I did not.

Q. The analysis you performed in Schedule 4 of your direct testimony made the assumption that MGE could have obtained 75 percent of the Williams maximum rate, correct?

A. That's correct.

Q. Are you aware that the Commission filed a Notice of Proposed Rulemaking with the Secretary of State of Missouri on May 1, 2003 in which it proposes to adopt a new rule entitled Natural Gas Price Volatility Mitigation?

A. I'm generally aware of that rulemaking, yes.

MR. DUFFY: Could I have an exhibit marked, your Honor?

JUDGE WOODRUFF: You certainly may. This will be 23.

(EXHIBIT NO. 23 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY MR. DUFFY:

Q. Do you have in front of you what's been marked for purposes of identification as Exhibit No. 23?

A. Yes.

Q. Does that appear to be a copy of some official documents of the Public Service Commission and a text of a proposed rule entitled 4 CSR 240-40.018, Natural Gas Price Volatility Mitigation, and bearing a received date stamp of the Secretary of State May 1, 2003?

A. Yes.

Q. Is this the document that -- or does this represent what you understand to be the Commission's Notice of Proposed Rulemaking that we just talked about?

A. Yes.

MR. DUFFY: I would move the admission of Exhibit 23 at this time.

JUDGE WOODRUFF: Exhibit 23 has been offered into evidence. Are there any objections to its receipt?

(No response.)

JUDGE WOODRUFF: Hearing none, it will be received into evidence.

(EXHIBIT NO. 23 WAS RECEIVED INTO EVIDENCE.)

BY MR. DUFFY:

Q. The purpose of the proposed rule states, this rule represents a statement of Commission policy that natural gas local distribution companies should undertake diversified natural gas purchasing activities as part of a prudent effort to mitigate upward natural gas price volatility and secure adequate natural gas supplies for their customers; is that right?

A. That's correct.

Q. It then continues by listing various pricing structures, mechanisms and instruments to hedge the price of

natural gas, correct?
A. That's correct.
Q. These include both physical and financial mechanisms, do they not?
A. Yes.
Q. And this proposed rule, the Commission has provided some specific guidance with regard to natural gas supply planning by including types of pricing structures or mechanisms that a gas company can use to provide a balanced portfolio. Would you agree?
A. I would agree with that, yes.
Q. To your knowledge, has the Commission ever previously issued an Order in which it stated that its policy was that all gas companies in Missouri should undertake diversified purchasing practices that included both physical and financial hedging mechanisms?
A. I'm unaware of that type of generic order.
Q. Was the authorization of the use of financial hedging instruments generally done prior to the winter of 2000-2001 on a company-by-company basis?
A. I may need a little bit of clarification on that. The purchased gas adjustment clauses for each company in Missouri that's regulated by the Commission varies somewhat, but they tend to have a lot of similar terms and conditions as well.

And it's Staff's position that those PGA clauses gave authorization to the companies to purchase gas supply and authorized hedging. That includes, in the Staff's opinion, financial instruments, as long as they were related to hedging.

Q. Are you aware of any Commission Order issued prior to the winter of 2000-2001 in which the Commission specifically authorized the use of financial hedging options similar to those outlined in the proposed rule for all gas companies in Missouri?

A. No.

Q. Would you agree, then, that prior to the winter of 2000-2001, there was no specific Commission Order, policy statement or other pronouncement by the Commission applicable to all Missouri gas companies which authorize the use of financial hedging mechanisms to mitigate price volatility, other than your comment about you think tariffs did that automatically?

A. With the clarification that tariffs are approved by the Commission. But with that clarification, I would say there was no general overall order that addressed that issue.

Q. Was there any rulemaking prior to the winter of 2000-2001 that outlined for all Missouri gas companies how the Commission would evaluate their hedging activities in an ACA proceeding?

A. No.

Q. Staff has suggested in this proceeding that MGE should have hedged at least 30 percent of its normal monthly volumes for the winter of 2000-2001, correct?

A. That is correct.

Q. Now, we discussed this at some length in the depositions we took back in December, and I believe you told me then, to the best of your recollection, the Staff developed this 30 percent level for hedging sometime in the spring of 2002; is that correct?

A. That's correct.

Q. You couldn't remember a specific time period other than the spring of 2002?

A. That's correct.

Q. Therefore, that 30 percent level was never communicated to the gas companies in Missouri prior to the winter of 2000-2001, correct?

A. That's correct.

Q. So those gas companies had no knowledge that there was going to be a minimum level of hedging considered for prudence purposes when it came time to look at that winter in an ACA proceeding, correct?

A. I would say the gas companies had no knowledge of the 30 percent or any particular percentage, but I would say that they did have knowledge that there were price stabilization funds in effect that had 70 percent targets and that the Staff had a longstanding position that companies should diversify their gas supply portfolio as exhibited in a couple of different documents.

Q. And the proposed rule that was filed by the Commission on May 1, 2003, is there anything in it that states that the Commission will be evaluating the conduct of gas companies in mitigating natural gas price volatility on the basis of having hedged at least 30 percent of each winter month's normal volumes?

A. No.

Q. In that proposed rule, has the Commission mentioned any specific percentage that it deems to be a minimum hedging percentage?

A. No.

Q. Prior to the issuance of this proposed rule, did the Commission ever issue an order in which it stated that it would evaluate conduct in mitigating natural gas price volatility on the basis of hedging at least 30 percent of each winter's normal volumes?

A. No.

Q. Prior to the issuance of the proposed rule, did the Commission ever make any kind of specific announcement of a specific percentage that it deemed to be a minimally prudent hedging percentage?

A.   No.

Q.   When I took your deposition on December 10th, 2002 -- and if you want to look at it, it's on page 94 and also 95 -- I asked you, what was the imprudence finding for MGE that caused you to apply the 30 percent in this case? And you said, the concern was that MGE did not have a documented hedging plan in place for that winter. Was that your testimony?

A.   That's correct.

Q.   And then I asked you, and is there some requirement by rule or statute that MGE have a documented hedging plan in place prior to a winter? And you responded, no. Is that right?

A.   That's correct.

Q.   And I also asked you in your deposition about page 108, lines 3 through 8, if I understand what your testimony is, you first had to make a threshold finding of imprudence for a company, and if you made that finding of imprudence, then you applied the 30 percent, is that right? And you responded, that's correct. Do you remember that?

A.   Yes.

MR. DUFFY: That's all the questions I have for this witness.

JUDGE WOODRUFF: All right. Come up to

questions from the Bench, then. Commissioner Murray?

COMMISSIONER MURRAY: Thank you.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good afternoon, Mr. Sommerer.

A. Good afternoon, Commissioner.

Q. I guess I'd like to start with, do you have Mr. Langston's testimony before you, specifically his direct testimony?

A. I have his direct testimony, but not his related exhibits or schedules.

Q. Okay. I don't think I'm going to ask anything from those. I'm just going to be looking at the testimony.

On page 32, he refers there to a deposition that was taken of you, and that was concerning the trigger price for the FCP stipulation, I believe; is that correct?

A. That's correct.

Q. And the quote that is given there on that page from your deposition, the part that's highlighted and bolded, would you read that aloud, please?

A. Yes. It says, based upon the concern that to the extent that market prices did go back down to that level, it may be locking in a price that was historically high and indeed higher than what current market conditions would dictate. In other words, somehow the $3.75 would catch the market on a downturn as it continued to go down, and then be locked in for the customers for two years at $3.75.

Q. And it's my understanding that Staff did refuse to agree to adjust the strike price to $3.75; is that correct?

A. They refused to adjust the trigger price, that's correct.

Q. Trigger price. Okay. And looking back on that, would you evaluate Staff's refusal to agree to adjust that trigger price to $3.75 as an imprudent decision?

A. I think it was prudent, given the facts and circumstances that were known at that time. MGE really wasn't offering to lock in prices at 3.75. If that was a real offer to lock in the customer's price at 3.75, the Staff would have jumped on that opportunity, but the prevailing price was a lot higher than that, the forward price, the price that was available if you were going to lock in a fixed price. That price was something like $5 to $6. I don't recall the exact level, but it was well north of or a lot higher than $3.75.

So the Staff's concern was, if the trigger is raised to $3.75 and at some point the market comes back down to 3.75, it could just as likely continue down to $3 or $2.50 if the market has come off from its historically high levels where the market was trading when this was being discussed and, therefore, the customers would have locked in at $3.75.

And as it turns out, the following year prices did for several months, quite a few months, drop down less than $3.75. So the customers would have been locked in to 3.75 and then given up -- up the opportunity to participate in lower gas prices.

Q. And the price -- the market price at the time of this deposition, what did you say it was?

A. It's my recollection it was between $5 and $6. It would be very much dependent upon when those discussions were taken -- taking place, and I don't recall exactly what the timing was, but it was an extremely volatile market and it was in the late fall of the year 2000.

Q. So your fear was that the market was going to go below 3.75?

A. That was a concern, yes, that the market could potentially go for an extended period of time.

Q. And, therefore, you were not willing to make adjustment above the $2.25 that had been agreed to previously; is that right?

A. That is correct.

Q. And you would evaluate that decision as having been prudent because you're not looking at what actually turned out; is that correct?

A. That's part of the basis, yes.
Q. And you would agree that it would not be fair to evaluate your decision based upon what actually happened later, would you not?
A. I agree.
Q. On page 37 of Mr. Langston's testimony, he references the Unanimous Stipulation & Agreement between Laclede, Staff and OPC that was signed on September 1st, 2000. Do you see that?
A. Yes.
Q. And is it true that was less than a month prior to MGE's filing?
A. That's correct.
Q. And is it also true that Staff supported Laclede's hedging settlement?
A. We supported that September 1st, 2000 settlement, that is correct.
Q. And then that was just before MGE filed to modify their price stabilization fund. Is that also correct?
A. That is also correct.
Q. And Staff took a position against MGE's filing; is that right?
A. That is correct.
Q. Can you explain that inconsistency, or if it

is not an inconsistency, can you explain why not?

A. Yes. I think the two programs were dramatically different. Laclede was operating in an incentive-based program which was still partially effective. Laclede still had the obligation, as the Staff understood it, to cover a certain amount of winter volumes with its program. Laclede was also involved, actively involved in obtaining certain hedges during the course of the summer of 2000.

MGE was in a situation where their plan had expired September 30th, they had no hedging in terms of call options, there weren't any incentive aspects related to the plan, there weren't ever any guarantees with those traditional price stabilization funds which MGE was asking to extend in terms of volume coverage.

And so the reason why Staff entered the Laclede Stipulation & Agreement was we really believe there might be an incentive for Laclede to obtain very high strike prices in order to meet the 70 percent guarantee, one of the guarantees that still existed from the Laclede program, and we did not feel that it would be beneficial from the customer standpoint to have $10 strike prices at some high level of funding requirement just in order to meet the letter of the tariff. And so that's why the Staff supported the September 1st, 2000 Stipulation & Agreement.

It did not support the MGE application because we believed the market was in a very dynamic mode, as it had been throughout the summer. It was extremely late. We had believed that there was enough time that was originally built into the stipulation in MGE's Case No. GO-2000-705 with an expiration date of September 30, 2000, that MGE could have had an opportunity to do some hedging.

And as Staff stated in its response or its memo, we believe that it was more appropriate that MGE take the tools that it had, that we believed it already had authority to use pursuant to its purchased gas adjustment clause, and make those decisions subject to a subsequent prudence review.

Q.   I'd like to talk to you just a little bit about Staff's storage utilization proposal in this case, and if you knew that your proposal for first-of-the-month flowing supplies would result in some years with an excess on most days in November, would you always recommend your methodology?

A.   I would prefer to defer that question to Staff Witness Jenkins. It's really more related to her area of expertise.

Q.   Now, you indicated that you thought that MGE had the full authority to go ahead and do the type of hedging that you're suggesting?

A. That's correct.

Q. And is there anything you can point to that the Commission has said that would substantiate that?

A. I will simply point the Commission to MGE's tariffs, which haven't changed greatly in terms of what they define as gas cost, and that definition is fairly general. It includes a list of typical items that are considered to be gas costs, gas supply commodity cost, transportation cost, storage cost, and I believe the language says includes, but is not limited to. So Staff used to the extent you're using storage clearly, storage is a physical hedge. That goes without saying.

You also have fixed prices that are available in the physical market, and we think that it's very clear that those PGA tariffs are so general, they don't refer to index pricing or spot market pricing. They simply say, you have the authority to pass through any particular pricing provision subject to a prudence review, subsequent prudence review.

Q. How did the price stabilization program differ, in that it was specifically brought to the Commission for approval?

A. That's correct. That program started back in 1997, and it related to three of the largest LDCs, local gas distribution companies in the state; AmerenUE, Missouri Gas

Energy and Laclede. In 1997, those three parties came forward, signed a Stipulation & Agreement which contained very specific terms on what the funding levels would be and what the goals would be in terms of coverage, what type of financial instruments would be used.

Q. Did that also provide for some statements to the recovery of the costs of price stabilization?

A. Yes. Those stipulations and agreements typically authorized the recovery of a charge, a price stabilization factor. It tended to be around 4.7 cents an MCF, and that was authorized as part of the purchased gas adjustment factor.

Q. So without that specific authorization, is it your understanding that the recovery of costs of entering into any kind of price stabilization would be very much open to disallowance?

A. I think it would be reviewed like any other element. The Staff has always preferred a diversified pricing approach, and so you can use a fixed gas price to hedge your gas supply, and to us that carries the same risk as an index price.

I know that Missouri Gas Energy in the past has been concerned because they view index pricing as being more closely related to market pricing and fixed pricing being something that can be above the market at any given time or below the market at any given time, and I think they were concerned about that risk.

But in Staff's view, we have always viewed any particular pricing provision as something that the company's management determines subject to an ultimate prudence review.

Q. On page 34 of Mr. Langston's direct testimony, bottom of the page, he says, in referring to Staff's opinion, being able to rely on Staff's opinion or the company going forward on an understanding as to what authority it had, it says, as Mr. Sommerer is abundantly aware, the Commission, not Staff, sets natural gas policy and precedent in Missouri. Do you agree with that statement?

A. Yes, I agree.

Q. And do you also agree that GO-2001-215, issued on October 26th, 2000 -- and I'm on page -- the bottom of page 35 of Mr. Langston's testimony -- that that case did not address Staff's proposed tariff language?

A. I agree.

Q. And that did not specifically grant MGE authority to purchase financial instruments?

A. The tariff language was not approved, and that language did make it more clear about tariff authorization for financial instruments.

Q. And that Order did not grant that; is that correct?

A. That's correct.

Q. And that Order did not grant MGE the ability to recover the cost of any financial instruments?

A. that Order basically said that it understood that there might be 4.7 cents remaining in MGE's purchased gas adjustments, but if the Staff wanted to remove it, the Commission believed that that would require a specific motion or filing by the Staff to remove it.

It's my understanding that subsequent to that time -- and this is very close to the Commission's order date, perhaps the next day -- MGE voluntarily made a filing, a substitute filing for its winter PGA, specifically removing that 4.7 cents. I believe that was the day after the Commission had issued its Order.

Q. And that 4.7 cents represented what?

A. That was the estimate of the funding level for the historical call option programs, the price stabilization fund. That was the rate that was associated with that, that fund.

Q. And that was removed from the tariff?

A. That rate was removed with MGE's substituted winter filing for the year 2000.

Q. Do you philosophically agree that if -- that it is good Commission policy to enable the utilities that the Commission regulates to have a clear understanding of what the Commission wants in terms of methodology to be followed, in terms of things that the Commission would find acceptable versus things the Commission would find not acceptable?

Do you agree that clarity and ability to rely on something, some signals from the Commission would be important?

A. I believe that certainly I would be in favor of that. As a Staff member -- and I think the rulemaking that the Commission has recently submitted to the Secretary of State's Office is an example where there's a positive communication and it's useful because the parameters are general. Some guidance is given, but it's not so restrictive as to force the company to hedge a specific percentage or use a specific tool or be allotted a certain amount of money for a certain amount of time.

So I would say that those indications or those policy statements are important and they're valuable, and I think the Staff would support them as they did with this rulemaking.

Q. And you support the generality of the rulemaking, in that it's not specific as to any certain level that has to be hedged, for example?

A. That's correct.

Q. So would it be accurate to say that you don't think that a minimum of 30 percent is a figure that should be applied across the board?

A. No. In fact, we're concerned that the 30 percent is a relatively low number that we use simply as a measurement standard for this ACA period. And, frankly, the 30 percent would not provide a lot of coverage on a going-forward basis or even for that time period.

Q. So could a company expect that Staff might challenge failure to hedge 70 percent in the next case?

A. Well, I know that the Staff has not announced any sort of measurement standard for subsequent ACA proceedings, and really all that we've emphasized here is that we've used the Commission's prudence standard, which is a fairly general standard. It doesn't have the kind of detail where you know as a utility company just exactly what amount to hedge, when, at what prices.

And we think that that would probably be entering into the realm of management discretion if we gave those kind of parameters, those kind of detailed parameters.

Q. But isn't that what you're doing after the fact, giving those detailed parameters after you know what happened?

A. Again, I wouldn't use the 30 percent so much as a prudence standard, but more a recognition of the reality that you do have to measure the damages. The Staff believed that there were imprudent actions in that period, and you have to come up with some way, whether that number is 50 percent or 10 percent, of trying to estimate, were there damages that took place because of the imprudent action.

Q.   So after the fact, for example, could you say the customers were damaged because the results that occurred from a lack of hedging would have turned out a whole lot better, the results would have been a whole lot better if the company had hedged 70 percent? You could say that, couldn't you, and say the damages therefore would be equivalent to 70 percent?

A.   In looking at the measurement of the damage, we really did have a range that we were evaluating in terms of what was the detriment, what was the negative aspect that affected the customers here, and that range was from 30 percent to 70 percent as I recall, maybe even higher, and the belief was that 30 percent reflected a reasonable standard, given the prices prevailing in that winter, given the fact that storage assets are maintained by a lot of the LDCs, and they tend to allow a company to physically hedge anywhere between 27 to 28 to 33 percent.

So we looked at storage and asked ourselves, if they would have only used storage on somewhat of a ratable basis, that would have provided a physical hedge. So we weren't even suggesting a very significant use of fixed prices here.

Simply saying to the larger utilities, as long as you have that storage asset and didn't use it early so you didn't have an alternative, then it would be adequate to basically use your storage on an even basis, but if you had an operational reason for using your storage more heavily, then there -- in Staff's mind there needed to be an alternative.

I think that's why the two issues are tied together. There's a storage aspect to Staff's adjustment and there's a hedging aspect to Staff's adjustment, and if for some reason -- and we've argued that they operated their storage inappropriately, but even if it was an appropriate use of storage, if you're out of storage by January the 1st, then that no longer offers you a physical hedge for January prices.

And what was very clear to Staff was that January was still a very cold month. There's a tremendous amount of winter left starting January 1st. The prices can be extremely high after January the 1st, and so there needs to be some sort of alternative in place if you don't have storage to use anymore as a physical hedge.

Q. And when you say some sort of alternative in place, how do you measure that?
A. Generally, I think we're back to that 30 percent measurement standard where we try to make a comparison between this minimum level on a monthly basis, considering how MGE actually operated its storage and the fixed price contracts that it was able to enter into, did it incur damages as compared to that measurement.
Q. When do you establish that measurement?
A. That measurement was established, to the best of my recollection, in the spring of 2002.
Q. After the time period we are considering?
A. That's correct.
Q. And did you use any hindsight in establishing it?
A. Clearly it was a retrospective review. It was common knowledge that gas prices were at record levels for that winter. There were tremendous amounts of concerns voiced by the Legislature, by the Attorney General's Office, by various members of the media, by individual customers, and so we already knew that there could have been some problems.
You can't make an adjustment or a judgment, a prudence judgment just because gas prices were high. So you know that you need to focus on that particular question from

an audit standpoint, from a prudence review standpoint. But the prudence review again is using those decisions that the company made, looking at them at the time those decisions were made and evaluating them in terms of reasonableness.

Q. Now, as I understand it, the company was assuming that at the first of November as well as the first of December that the prices were likely to come down from the levels that they were sometime during the month. Is that your understanding?

A. I think there were points in time, as I understand Mr. Langston's testimony, that he believed prices would moderate.

Q. And is it your testimony that that was a totally unreasonable assumption?

A. I don't believe that the Staff was convinced that prices were going down.

Q. I'm not saying you were convinced. I'm saying was it a reasonable assumption, a reasonable alternative that could have happened?

A. It was certainly a possibility that prices could have gone down based upon weather, for example. Weather is one of the major drivers. So if you're in late November and, you know, the gas market is fairly high, I think it was headed towards $6 around Thanksgiving, and December turns out to be the warmest December in history, even though the storage fields were extremely low on a national basis, that may have overcome that fundamental factor and resulted in lower prices.

Q. Okay. Now, let's assume that if the company's prediction there that those prices wouldn't moderate had come true and the winter had been exceptionally warm, December -- November and December had been exceptionally warm months instead of the coldest two consecutive November and December on record, would Staff's position be different than it is today?

A. I would say that to the extent that you didn't have any damages that resulted from MGE's decision-making process, we wouldn't be here today.

Q. So let's pursue that a little, because I think that relates to something that I was asking Mr. Reed about yesterday regarding hedging preventing spikes both upward and downward. Were you here, do you recall testimony on prevention of both upward and downward spikes?

A. I think I heard some of that testimony, yes.

Q. So do you agree with that, that hedging does prevent both upward and downward spikes in prices?

A. Generally, if you're looking at a fixed price instrument, that would certainly lock you in and prevent upward and downward movement or upward and downward volatility. If you're looking at a cap or a call option, it will eliminate some volatility on the upside up to the strike price or up to the cap, and then one of the benefits of a call option is you participate in downward movement. So you still have that volatility.

Q. But if you're talking about storage as a hedge, that works both upward and downward, does it not?

A. Your storage typically would be full going into the winter heating season, and that gas would have been injected in the summer at known prices or whatever the summer prices were. So that operates more like a fixed contract, whatever you're taking out of storage you're displacing your alternative supply.

Q. And it can -- it can operate to prevent upward spikes as well as downward spikes?

A. That's correct.

Q. And if it operated to prevent downward spikes, would it be Staff's position that the customers were damaged?

A. As long as we believe that it was a reasonable and prudent use of storage, the storage asset, then there wouldn't be a prudence disallowance.

Q. When would you determine whether it was reasonable or not?

A. That review is made during the course of the actual cost adjustment review.

Q. But what would you be looking at? I'm not -- actually didn't mean to ask you when you would be doing it, but based upon factors, at what point in time would you be looking at it?

A. You would want to evaluate it based upon the company's storage plans and the market that it was looking at and the various constraints it had through the pipeline contracts. So you would be looking at those decisions when they were made.

Q. And you would not have a problem with a result being prevention of downward spikes? That would not be what would cause you to call it imprudent if you so -- if you did so?

A. That's correct.

Q. I want to go back to the tariff language for a minute or two that you say provides the authority for MGE to do whatever kind of hedging that you promoted here. What about -- and I'm looking at page 40 of Mr. Langston's direct testimony. But he says it's his understanding that an LDC must have specific tariff language authorizing the utility to assess charges to customers, otherwise the utility is at risk for the claim that its actions were unlawful.

And just comment on that, if you would.

A. Which lines were you quoting again?

Q. I'm sorry. I was actually at 19 through 21.

A. And this is on page 40?
Q. Mr. Langston's rebuttal. I apologize. It's not direct.
A. I would generally agree with that statement where he says, it is also my understanding that an LDC must have specific tariff language authorizing the utility to assess charges to customers, except I would clarify it by saying that the purchased gas adjustment clause has a certain amount of specificity in that it lists the types of costs that are considered gas costs.
But it's common practice with all the local distribution companies in the state, including MGE, that there are charges that are subsets to the general list of items that are considered gas cost in the purchased gas adjustment tariffs.
And so I would simply add to that specific tariff language quote that he has by saying within the bounds of certain general provisions.
Q. Where are you adding that?
A. We're on page 40.
Q. Yes.
A. Line 19 and 20. It is also my understanding that an LDC must have specific tariff language, and I would add a parenthetical within the bounds of general provisions authorizing the utility to assess charges to customers.

And what I mean by that is simply to say that tariffs should be precise and they should be clear, but there would be quite a few gas costs that are disallowed if the Staff took the approach that the purchased gas adjustment tariffs only authorized what was specifically contemplated in one of the listed items.

In other words, if the tariff talks about gas supply commodity cost, to me that means anything that's contained in that wellhead contract, and that can often mean producer demand charges, premiums that are paid to producers, the wellhead commodity itself, fixed prices, index prices, daily prices. You could make the tariff very specific, and you could read Mr. Langston's quote that way that you need specific tariff language before you want to take an action.

But I think if you go overboard with it and make it be too specific, then it becomes impractical to implement. So that's the point, the clarification that I would make to his quote.

Q. I wanted to ask you, it appears that your recommendation of the 30 percent factor was just for that particular winter. Is that accurate?

A. That's right.

Q. And what rationale other than hindsight can you use to vary a minimum level of reasonableness from year to year?

A. I would say that that number is based upon judgment, and going back to what we looked at and deriving the 30 percent, we considered storage levels for the LDCs as being a physical hedge and providing some minimal amount of hedging to the extent you had storage for each month of the winter period. And we also looked at it in terms of will this number be greater than warmer than normal requirements?

We didn't want to have a number that was so high that there was a potential that it could result in an overhedging of the volumes. And so we did some analysis with respect to warmer than normal winters to make sure that that level, as compared to warmer than normal winter rather than a normal winter, didn't go up to a percentage that exceeded 100 percent of what you could really count on, even in mild winters.

And those parameters really won't change extensively from year to year. So I don't know if the Staff will change its level of damages. We haven't discussed it, and it would probably be beyond my call at this point, without consulting other Staff members on what kind of items should be looked at. But that's what we looked at for that winter.

Q. Did you have any part in the recommendation regarding capacity release issue?

A. That was my issue.
Q. Sorry. Finally get to your issue, and I don't have much to ask you about that, other than, is it true that this is the first time that Staff has raised this as an issue with MGE?
A. Yes.
Q. And can you explain to me, if failure to release capacity or attempt to release capacity on KPC was imprudent in that particular year, why it would not have been considered imprudent in other years?
A. I think the Staff was looking for a trend in MGE's operations, because there were years, if you go back far enough, that MGE did purchase gas during summer months from KPC, but those purchases were made under a different contract where there was a real supply benefit for flowing those volumes in the summertime.
And so I think the Staff needed to convince itself that this was truly an operating pattern, needed to see two or three summers before we went ahead and made that adjustment.
Q. And if you'd made that adjustment in the prior two summers, what would have happened?
A. We would have, I suspect, made the adjustment based upon the same theory that we're using and that there would have been a disallowance subject to the Commission

reviewing that.

COMMISSIONER MURRAY: Okay. Maybe that will be followed up by counsel, because I'd like to have some better explanation of that, but I won't -- I'm not prepared to get into it right now.

I think that is all, Judge. Thank you.

JUDGE WOODRUFF: All right. We're due for a break. We'll adjourn until 2:45.

(A BREAK WAS TAKEN.)

JUDGE WOODRUFF: We're back on the record, and Commissioner Gaw, you can ask your questions.

QUESTIONS BY COMMISSIONER GAW:

Q. I'm not sure I'm going to improve on it.

Okay. Mr. Sommerer, just to clear up a little bit here, the testimony that you've given really -- does it really address Issue No. 3 to any great extent, which is the issue on storage and --

A. No, it does not.

Q. You're dealing with Issues 1, is that right, and 2, or mainly 2?

A. Mainly 1, with some testimony on Issue 2.

Q. All right. To clarify a little bit on Issue 2, where are we on these positions of the amount that was hedged for the winter, winter period in issue here? Is Staff still maintaining that the number that MGE has that they are -- proffers that they hedged 38 percent of normal winter volumes is incorrect?

A. That's correct.

Q. All right. What percentage does Staff believe was actually hedged for that winter?

A. The Staff does agree with MGE's calculation, and I believe it was approximately 38 percent for the entire winter, when you include storage.

Q. So as far as the winter season is concerned, if we're looking at numbers here, some 30 percent figure, you're not disagreeing with MGE's position that they hedged 38 percent for the entire season?

A. Mathematically, I think that is correct.

Q. Okay. And that -- and I guess to clarify, Staff's position is that you ought to be looking at increments or a period of time within that winter season in determining whether an appropriate amount of hedging was employed?

A. That's correct.

Q. Rather than looking at the entire season?

A. Yes.

Q. Okay. Now, in regard to the method of hedging, of the amount that was hedged, percentage-wise or around about anyway, how much of that hedging was from fixed storage?

A. In terms of the 38 percent calculation?

Q. Uh-huh.

A. The overwhelming majority was from MGE's storage, but I would like to refer you to Staff Witness Anne Allee for the specific numbers.

Q. All right. And from your standpoint, if I get into areas here which really is not your part of the case, don't hesitate to say, I wish you'd inquire of another witness. Some of this blends in when I'm going through it, and so I may go over there into some other areas.

In looking at the figure of this 30 percent figure, is it Staff's position that that 30 percent is something that has -- is calculatable in advance?

In other words, in determining whether the figure ought to be at 30 percent as opposed to some other figure, is that a mathematical calculation that Staff is doing to determine it should be at 30 percent when you're assessing damages in this case, or are you pulling that number just out of -- out of the air and saying arbitrarily, looking at all the factors, we think this is a fair figure for the assessment of what damages there might have been?

A. I would be reluctant to use the word "arbitrarily."

Q. I am sure. So you can use your own words.

A. Okay. We considered two or three different factors in arriving at the 30 percent, and there was some subjectivity involved in arriving at that number. It's not a standard in terms of finding it published in any document. There's --

Q. Wait. I'm stopping you because I'm not really asking about whether -- what the standard is that's been stated. I think it's fairly well established there is no place we can look to find that 30 percent figure saying everybody agrees that all companies should use 30 percent or that there's been previously some pronunciation by the Commission or by the Staff that that 30 percent figure is what you ought to hedge. Am I not right?

A. That's right.

Q. There's nothing there that says any of that?

A. That's correct.

Q. My understanding is what Staff is saying in assessing what was done, that in the whole gamut of things that were done, there were certain things that Staff is alleging were done imprudently, first of all. That's a portion of it, right?

A. That's correct.

Q. And then the next portion is, if you agree that some parts of this decision-making were imprudent, then we have to figure out what's the consequence of that; is that right?

A. That is correct.

Q. And so Staff has then come up with this figure of 30 percent to say, this is what we would propose to the Commission that you look at to assess some sort of a damage or some sort of a -- not really a penalty, but something that indicates this is what we need to do, maybe this would be a fair figure to make consumers whole?

A. That's right.

Q. So in other words, if I were dealing with a case where somebody was injured in an automobile accident and they had their arm hurt and they no longer have full mobility of their arm and you say, what's a fair figure for the damages to my arm, in other words, is there a book you can go to to find out what that figure is, you know, where there's a book where you can find what that figure is?

A. I assume there are experts who would testify to what that figure is, but you know --

Q. Do you think there's a book you can go to to see what an arm's worth?

A. Obviously not.

Q. And so -- but still, in those cases, if it was a personal injury case, a jury would be asked what -- we can't assign a value to this, to a person's arm or to their life or to whatever. It's not like a car where there's a market value, but yet we've got -- you've got to do something here to help to make this person whole, and you can't give them back their arm. The only way we've got to do it is some sort of money; is that right?

A. That's correct.

Q. So in this case you're trying to come up with something to make consumers whole, and you don't have a book to say, this is what we believe the damages were in this book. It doesn't say a damage figure, something like that?

A. I would agree with that assessment, yes.

Q. All right. So then the question I have, then, in following that, the questions I have have to do with how you calculate whether or not that figure is appropriate under the circumstances. And I am -- I am -- I'm assuming, even though it's a question in this case, that you get beyond the question of whether it was an imprudent decision made or decisions made.

So if you're doing that and you're saying, okay, what is it that we should use to calculate what the damages were to the consumers because of imprudent decisions, help me to understand why this 30 percent figure is an appropriate figure to assess damages in this case. What factors are there that are objective, what factors are there that are subjective, and of the objective factors, what calculations are made in making that determination that 30 percent is an appropriate figure?

A. The 30 percent comes from the fact that a lot of LDCs in Missouri have storage. Storage tends to have the ability to supply anywhere from 27, 28, 33 percent of the entire wintertime needs. So it's a physical hedge.

And I think one of the biggest considerations that Staff had was we're not necessarily suggesting that the company had extensive fixed pricing in place. What we are suggesting is that a company that has storage should use that storage in such a way as to provide a fairly level amount or a reasonable amount of coverage for each one of the winter months.

And so to the extent that you are not able to achieve that 30 percent from storage, we would argue that you should have had some sort of replacement or some sort of surrogate for storage to take the place of the storage. So that was one of the threshold issues was storage is usually about 30 percent. That's a physical number. You can calculate it. The LDCs that have storage in Missouri have that available. And it's not really asking the Commission to make any more of a disallowance than for that minimal standard.

Q. Okay. The disallowance that you have, then, the 30 percent figure rather is based upon what you see other LDCs doing in the state?

A. Based upon their use of storage, that's correct.

Q. All right. And is it entirely based -- is it entirely based on what you're seeing and what you believe is normal business practice and good business practice in regard to storage alone, or is it storage plus other financial instruments and other things that can be done for hedging purposes?

A. I think the baseline really is storage to the extent that 30 percent number calculated a shortfall, because the storage asset was no longer there or no longer available. It was no longer there. Then the Staff viewed it reasonable to have a fixed price as an alternative to storage.

So that's where fixed pricing comes into play, but we're really not looking at any incremental fixed pricing over and above that 30 percent level. And, again, that's generally reflected by the storage asset.

Q. All right. And so -- and so I understand -- I know you've already said this, that you believe that it is prudent decision-making and prudent practice for MGE in this case to have a minimum of 30 percent hedging in their program going into a winter season?

A. That is correct.

Q. That's a policy that you're asking this Commission to see as the enunciation of what is prudent for

MGE?

A. That is a request to have the Commission value the loss of that arm at that level.

Q. All right. Now, if I were to -- if I were to go farther and say, okay, in this case you're not asking the Commission to also enunciate what's the maximum amount of hedging that should be done, or are you?

A. No, we are not.

Q. Okay. If I -- if I break this down a little further, though, if I'm looking at trying to understand, because there's a connection here between the injury and the damages, that seems to point -- see fingers pointing both directions. In other words, part of what I understand you to be saying in regard to how I determine whether something is prudent is to look at that 30 percent figure, as well as using that as an assessment of what the damages are?

A. That's correct.

Q. So I'm just trying to make sure I understand. If MGE would have utilized its stored gas each month according to what Staff is saying is the minimum amount of use that should have been done, does that mean that each month, November, December, January, there should have been 30 percent of the amount of gas that was being utilized for MGE's customers that was out of storage?

A. That's a question that probably is best directed towards either Lesa Jenkins or Anne Allee.

Q. Okay. That's fair. Is there a stated definition of imprudence that the Commission is bound by previous case law or something that is accepted, if you know?

A. Yes. I think that prudence standard has been enunciated in a couple of different cases by the Commission. Western Resources, Case No. -- and it might be Missouri Gas Energy Case No. GR-93-140, I believe, discussed the prudence standard.

Q. Okay. And do you know what that is generally? And if you want, we can just look at the case. I was just wondering if you had something that was quick.

A. I don't believe I have that Order, a copy of that Order or cite to it, but it's fairly clear in that Order.

Q. Okay. And, again, this is probably a question for other witnesses. The testimony from I believe it was Mr. Reed regarding the rationale for using storage in November, are you familiar with that or is that really something having to do with other witnesses for Staff?

A. Again, I think that's really a question of storage availability, and best asked of Lesa Jenkins.

Q. Okay. Refresh my memory a little bit, if you would, on the contract that exists with MGE and Kansas

Pipeline Company with regard to the amount of capacity that is -- that belongs to MGE on that line. I'm not really looking for specific volumes as much as I am an understanding of the relative volumes that pass on that pipeline compared to other pipelines that service MGE.

A. Right. That certainly isn't the largest pipeline that serves Kansas City. I think it represents approximately anywhere from 3 to 7 percent of the entire load. Williams is the largest pipeline by far, probably serving in excess of 70 percent of the load in Kansas City.

Q. All right. And is there -- do you recall what the obligation is of MGE under the contract that deals with the Kansas Pipeline?

A. Yes.

Q. Tell me a little bit about that, please.

A. It's a long-term obligation. It's a long-term contract. They're obligated to pay reservation charges on a monthly basis. Those reservation charges have been the subject of previous Staff disallowances, and there are some subsequent cases that are still waiting to be heard, but the Staff has had some concerns about the contract. It is a long-term agreement regulated by the Federal Energy Regulatory Commission.

Q. The price being paid under that contract, Staff believes, does Staff have an opinion about the price that's being paid for that capacity?

A. We believe that the price that's being paid for the primary capacity is excessive.

Q. And help me to understand a little bit about the Staff's position in relation to MGE's position as to the marketability of that, of gas over that pipeline.

And what I'm asking you is, it's my -- it's my understanding that Staff has taken the position on one hand that it is a very expensive pipeline under that contract, or it is more expensive than some other choices; is that correct?

A. That is correct.

Q. I'm trying to understand Staff's position in argument with MGE's position that that pipeline is very difficult to market because it's so expensive. Help me to understand how those two -- I almost think that you-all have switched hats on this issue, and I'm trying to understand it under that scenario. Do you want to give me a little explanation?

A. Okay. The Staff's main concern here, which is really the threshold prudence question, is should MGE have posted or marketed that capacity. Clearly the capacity -- and there's testimony to this and Staff agrees with it -- in Mr. Langston's direct, I believe, that the Kansas Pipeline capacity is the most expensive capacity in that area. And since that's the case, we believe there really should be a diligent attempt made to go to the secondary market and try and remarket that capacity and get what you can from it.

And MGE did not post the Kansas Pipeline capacity, which we think was imprudent not to do that, and we also believe to the extent that even if MGE shows there's no market for the capacity because of its expense or its operational restrictions or whatever, there was an alternative that they should have been looking at, and that is, clearly they're flowing -- MGE is flowing gas in the wintertime. They're not flowing gas in the summer. It's idle capacity in the summer.

What about the idea of releasing Williams capacity which may have more value because it's more flexible because it has more delivery points for whatever reason, and then resourcing the gas that MGE no longer sources on Williams, source that on Kansas Pipeline.

Q. Okay. Let's break this down just a little bit so it's easier for me to understand. There is an obligation to pay for the capacity on the line, regardless of whether it's in use?

A. That's correct.

Q. With KPC?

A. That's correct.

Q. So whether it's in use or not, that amount --

there's an amount that has to be paid because there's a long-term contract to that effect?

A. Yes.

Q. Then what additional charges are there when gas actually flows through that pipeline, if it's coming to MGE, for instance?

A. If the gas flows to MGE, MGE would have to pay for the gas supply commodity, the actual wellhead price of gas.

Q. Right.

A. It would have to pay the variable transportation charges on KPC. It would have to pay the fuel charges on KPC. It would also obviously continue to pay the reservation, the fixed reservation charge.

Q. Ignore that. That's a constant, right? That has to be paid whether it's used or not?

A. That's correct.

Q. Okay. Of the other charges, in relation to what prices are from other pipelines in the vicinity, are there aberrations in comparison to the other -- those charges on other pipelines?

A. I agree with Mr. Langston's characterizations and testimony that the variable charges on KPC are quite a bit higher than the other pipelines in the area.

Q. Tell me, what do you mean by variable charge?

A. The variable commodity transportation rate. It's a FERC-regulated rate, but it's a variable rate paid on the volumes that you actually flow.

Q. So if I were trying to market -- if I were MGE and I am trying to market the KPC line, how -- how are you going to get somebody to use that line, if that's the choice, to use that line if the variable charges are higher than the alternatives?

A. I think to the extent that you establish there is no market on KPC, and that may be one of the reasons, then you go to that Alternative 2 and you try and package some Williams capacity on a nonrecallable basis and market it that way.

Q. Okay. Now, let's -- are you conceding the issue on KPC for purposes of this hearing to MGE or is that still an issue? Because I'm hearing you go to that next step, and I'm trying to understand if that -- if that first idea is no longer being proffered.

A. I think the first idea has become somewhat improbable, based upon what I've seen and in Data Requests that MGE has now made the attempt, they've tried to release the capacity.

The Staff's only issue with that would be, are you reaching out? Are you simply posting it or are you doing some sort of active marketing process on KPC? But we understand there are restrictions, certain operational restrictions on KPC.

Q. Let me ask you this as a sideline here: Is there a cost of posting that? Is there a cost to MGE that's -- or is it just, you know, we post it or we don't, it's the same cost to us?

A. I don't think there is any fee to make that posting. The only cost you would have would be the time -- the administrative time you have to make the posting.

Q. Okay. You don't know how much that's valued at or how much that costs?

A. No.

Q. Let's go to the second part of that, and that's the idea that you could sell some of your Williams capacity if you were MGE and I assume make up the difference on Kansas Pipeline. Is that what we're talking about?

A. Alternative 2 is where you try and market your Williams idle capacity and achieve enough of a credit in that market to overcome the additional cost you would have by flowing replacement gas on KPC.

Q. And have you calculated the amount that you'd have to get in marketing the Williams line in order to get over break even with the additional charges that you would incur for variable costs on KPC?

A. I have not calculated that specific number, no.

Q. So are we going to have that information here in making a determination whether or not -- whether or not there is a point at which time that becomes something that's in MGE's best interests?

A. I think MGE has offered testimony saying that at a 14 percent credit level, it clearly is uneconomic. And that's on one side of the break even. And Staff's at 75 percent, and that number's approximately $800,000 to the credit. So somewhere in between that 75 percent credit level and the 14 percent it can be calculated. I don't think it's on the record in this case.

Q. Again, we have got to have information in order to make that assessment. I would assume that whatever breakover point is, which we don't have in front of us, there is a market, true?

A. Well, you have to assume some credit amount, and that's been one of the difficult issues for this particular issue is, since the release didn't take place, how much could you achieve from a release that didn't take place? And so you have to look at the market activity during that time period. We looked at it a little bit before the time period, and what we noted was that for nonrecallable release, you typically achieved the maximum FERC rate. So that's in testimony. That's part of the record.

And the Staff chose 75 percent. We believe that was a conservative number. MGE has argued that it was somewhat arbitrary because we can't point to a specific transaction that occurs at 75 percent. And they argue that 14 percent is probably a more reasonable standard for the release credits that would have been achieved on the Williams system.

Q. All right. So you're saying that in the record there is evidence to support -- evidence to support the sale of the Williams capacity at 100 percent of the FERC approved rate?

A. That is correct.

Q. And Staff has given them a 25 percent discount?

A. That's correct.

Q. Is there evidence in the record to support the 14 percent figure?

A. That is also correct. MGE, I believe, made a calculation based upon recallable capacity releases, and I believe that number was approximately 14 percent, or that's what they used in their analysis.

Q. Am I looking at a difference between 14 and 100 percent, based upon whether its recallable or nonrecallable? Is that the only variable?

A. That is the range of alternatives that have been presented, I think, in terms of scenarios before the Commission. You have Staff's support for 100 percent, the actual mathematical calculation at 75 percent, and MGE's suggestion that 14 percent is a more reasonable number.

Q. I'm going to ask the question again, because you continue. Is the only variable in the evidence of prior transactions on the Williams line, whether its recallable or nonrecallable, or is there some other variable in there?

A. Those transactions can be affected by the term of the release, how long the release is, potentially how biddable or nonbiddable it is. I think Mr. Duffy was trying to bring that out in his cross-examination, and we recognize there's a spectrum of various terms there, various characterizations on whether it's biddable or nonbiddable. But what we're saying is, generally speaking, nonrecallable releases are valued at 100 percent of the maximum rate.

Q. Is that a matter -- are we talking about, again, summer months?

A. Yes. That's -- even throughout the winter months, it's my recollection 100 percent of the maximum rate for nonrecallable releases.

COMMISSIONER GAW: That's all I have. Thank you, Judge.

JUDGE WOODRUFF: I have a couple questions.

QUESTIONS BY JUDGE WOODRUFF:
Q. First, I want to talk a little -- ask you a few questions about the history of all this. It's been my impression in looking at this case and some other cases that the Commission had been preapproving hedging plans for the winter of 2000-2001, and I'm going to ask you, has the Commission preapproved a hedging plan since that winter?
A. No, it has not.
Q. Okay. So at some point there was a change in philosophy; is that fair to say?
My next question is going to be when did that happen?
A. Okay.
Q. Is that a change in Commission philosophy or in Staff's philosophy? I can see the Commission's changed in this order here, and I'll ask you about that in a minute, but when did Staff's philosophy change?
A. Right. I think that the Staff always had a fairly broad view of what kind of tools could be used for hedging, and we tried to work with the companies on a company-by-company basis.
And there are ten LDCs in Missouri, and originally the three largest LDCs had these price stabilization funds. But even the three largest LDCs took different paths and they took those different paths or

different alternatives to hedging at different time periods.

You had AmerenUE under the old price stabilization fund for two years, the 1997-98 winter and '98-99 winter. Then Ameren chose to do its own thing; in essence, hedge using its internal management prerogative, and it did hedge during both of those winters, but it chose not to renew the price stabilization fund.

Q. Okay. So Ameren kind of went the way Staff would like to go?

A. Ameren's position was more consistent with Staff's position later on. I mean, Staff's position was always, I think, flexible in terms of we're not going to go out and create a bunch of complaint cases forcing Atmos or Aquila, the medium-sized utilities to enter into price stabilization funds.

If we thought that was critical, I think you would have seen six or seven complaint cases saying, there's a serious problem here. But I think some of the smaller LDCs and the medium-sized LDCs chose to do whatever hedging they were going to do on their own without any sort of authorization of a fund with certain parameters.

Q. Do you know if those at least went out and bought the financial instruments to hedge?

A. I think those LDCs generally concentrated more on using physical hedges, storage and fixed prices and perhaps -- they're called -- I think they're called embedded calls, but they're actually caps within a gas supply agreement. So they were more comfortable dealing with the physical market and what the physical market had to offer.

Q. Okay. I'm sorry. I interrupted you. Go ahead.

A. Okay. I would certainly say that Staff supported Ameren's choice to go ahead and make its own decisions with regard to hedging. Laclede had its own price stabilization program. That was something that the Staff, frankly, didn't like and opposed. Laclede got authority for that program for three years running, and it was a little bit different than the traditional programs.

It had certain guarantees that were contained in the tariffs. It had certain incentive mechanisms that were part of the tariffs, and it was quite a bit different than the traditional price stabilization fund, which was a nonprofit -- we viewed it as a tool, really, to let the companies know that call options for this amount of money would be funded by the customer with some fairly broad parameters in terms of review.

Q. You mean as far as prudence review?

A. That's correct.

Q. Okay. So under that program, you could do a prudence review?

A. I think we could do a prudence review, and again, this assumes that the company wasn't operating under some other incentive plan, gas supply incentive plan.

Q. Like Laclede was?

A. Exactly. If you were under the traditional PGA clause with a prudence review under that kind of scenario, if you had a price stabilization fund, I think the Staff still had authority to review index pricing versus fixed pricing; in other words, the pricing choice. Did the company diversify, did it choose to put all its eggs in one basket and go with total index pricing? Those kind of decisions were subject to a prudence review.

Q. And do you know if any LDCs had purchased hedging through financial instruments prior to 2001 other than Laclede, which is a separate case?

A. I think across the board you had LDCs that were involved in hedging, but for the most part, I would think that hedging was more concentrated towards fixed prices and natural gas storage.

Q. And my next question was going to be, do you know if the Commission had done any prudence reviews on the question of purchase of financial instruments for purpose of hedging before that winter?

A. I think we, as the Staff, have reviewed those instruments in various ACA cases, but there weren't any prudence disallowances and the Commission had not reviewed any prudence disallowances regarding financial instruments.

Q. Now, I mentioned an Order that the Commission issued on October 26th of 2000. It's the Order denying application to renew price stabilization fund, Schedule 10-1 of, I believe it's your direct.

A. I'm there.

Q. Okay. In the text of that it indicates that Staff had filed a recommendation suggesting that MGE could go ahead and perform these -- use these financial instruments for the purpose of hedging and then would be reviewed in the prudence review. Is that the first time Staff had made that kind of recommendation?

A. In terms of that particular situation, it may be the first time that this Staff recommended that those instruments be reviewed for prudence later on. I'm thinking back to that summer. Laclede may have had a filing in July, and I know there was a response to that. This was after Laclede had opted out of the price protection incentive, and I think the company still wanted to do some sort of modification.

And in that recommendation the Staff may have said, given the dynamics of the marketplace, it may be best to go ahead and subject those instruments to a prudence review. That may have been an aspect.

Q. But that would have been in September 2000 at earliest?
A. Potentially it would have been earlier than that. I think Laclede had an application actually in July. So sometime in June or July of 2000 I think the Staff responded to that original recommendation, which ultimately resulted in the September 2000 Stipulation & Agreement with Laclede.
Q. Okay. So this Order that we're talking about issued in October of 2000, to your knowledge, that's the first time the Commission said MGE's business decisions regarding hedging will be subject to prudence review without giving prior approval; is that true?
A. I think that's accurate, yes.
Q. Okay. Let's shift gears a little bit, then. I wanted to ask you about prudence decisions here. Can you tell me precisely which decision of MGE was imprudent?
A. I think it was really two decisions. One is a storage-based decision which I'd rather defer to Staff Witness Jenkins.
Q. That's the same storage issues that were in the issues -- I think it's Issue 2 in this case. We've got 2 and 3.
A. I believe that's Issue 2 and 3.
Q. All right.

A. And the other issue was, as I explained in my testimony, MGE really, in Staff's opinion, had no formal hedging plan or detailed analysis on what it would do in terms of hedging alternatives. And so we think ultimately that is a fundamental imprudent decision on MGE's part.

Q. Now, going back to that decision we were just talking about, MGE had applied to review the price stabilization fund, but the Commission rejected that. Was that -- is it fair to characterize that as a hedging plan, as you described it?

A. That's where there's a major disagreement, I think, between Staff --

Q. Explain that to me then.

A. The Staff believes that a comprehensive hedging plan would perhaps include the price stabilization fund as a tool, because that involved an authorization but not a requirement to go out and acquire call options. Call options are certainly one instrument that can be used. Fixed prices are another instrument that can be used. Storage clearly is an instrument that can have a tremendous effect, not only on a seasonal basis, but a monthly basis.

And so both the FCP stipulation program, fixed commodity price program, and the price stabilization fund we viewed as potential tools that could be useful, but it wasn't the whole hedging plan in our opinion.

Q. It's in need of something more?

A. Exactly. Q. I don't know if you've done the calculations on this or not, but if MGE had been able to use their storage as they had planned before the season started, would they have met the 30 percent requirement for each month?

A. That's a question probably best asked of Anne Allee. She has the spreadsheet calculation.

Q. Okay. And as I understand your argument, there were only two months when they didn't meet the 30 percent threshold; is that right? That would be January and March?

A. That's correct.

JUDGE WOODRUFF: I believe that's all the questions I have. So we'll go to recross. And for recross, again, the City of Joplin's not here.

Public Counsel?

MR. MICHEEL: Yes, your Honor. Thank you.

RECROSS-EXAMINATION BY MR. MICHEEL:

Q. Mr. Sommerer, Commissioner Murray and Judge Woodruff asked you numerous questions about the price stabilization fund in GO-2001-215. Do you remember those questions?

A. Yes.

Q. And it's my understanding from your answers that the Staff made it abundantly clear in their recommendation and memorandum that the Staff believed that MGE had the authority to hedge its gas costs using financial instruments without the need for an extension of the price stabilization fund. Is that a correct understanding of your testimony?

A. That's correct.

Q. And is that what was essentially stated in the Staff recommendation in that proceeding?

A. Yes.

Q. Commissioner Murray asked you a question about who sets natural gas policy in the state. Do you remember that question?

A. Yes.

Q. And with respect to this price stabilization fund, was it the Staff of the Public Service Commission that determined that the price stabilization fund should not be extended or was it the Commission?

A. That was based on the Commission's Order.

Q. And so the Commission made a policy decision not to extend the price stabilization fund, not the Staff?

A. That's correct.

Q. Drawing your attention to your Exhibit -- or excuse me -- Schedule 10 to your direct testimony, I guess that's the Order in GO-2001-215. I'm looking at page 3 of 5 there, the first full paragraph on the page. Let me know if you get there.

A. Okay.

Q. Could you read the last two sentences of that paragraph into the record for me? It starts, Staff is correct.

A. Staff is correct when it states that MGE should apply reasonable purchasing practices based upon its own evaluation of risks and its gas supply portfolio. MGE's business decision also be subject to prudence review, as are MGE's other gas supply choices.

Q. And was that the Commission stating its belief on how it was going to review MGE's decisions with respect to hedging or not hedging?

A. Yes.

Q. Also, to be fair, attached page 4 of 5, there was a dissent in that Order. Is that -- my understanding correct about that?

A. That's correct.

Q. Did that dissent indicate anywhere in the body of the dissent that the company needed specific tariff authority to hedge or that it didn't have authority to hedge?

A. That does not appear to be contained within the body of the paragraph.

Q. And the main decision with the four other Commissioners, does that -- is there any statement in that Order that indicates that the company needed specific Commission authority to purchase financial instruments?
A. No.
Q. In fact, does it -- does your reading of the Order indicate the opposite?
A. That's correct.
Q. And just to clear up, Judge Woodruff asked you about other LDCs in the state of Missouri and what they're doing with respect to hedging. Do you recall those questions?
A. Yes.
Q. Is it your understanding that other LDCs have regularly hedged -- used financial instruments to hedge gas costs without explicit Commission authority to do so?
A. That's my understanding, yes.
Q. And is it also your understanding that this company's PGA tariffs don't specifically talk to the need to purchase or specifically authorize such things as index price contracts?
A. That's correct.
Q. Or fixed price contracts?
A. Correct.
Q. So it's just like you said, a blanket

expansive authorization for gas costs, including but not limited to?

A. That's correct.

MR. MICHEEL: Thank you very much, Mr. Sommerer.

JUDGE WOODRUFF: And KPC?

RECROSS-EXAMINATION BY MR. KEEVIL:

Q. Mr. Sommerer, is it your understanding that issues regarding the contract between the Kansas Pipeline Company and MGE have been bifurcated out of this hearing and held in abeyance pending final judicial resolution of appeals of Case GR-96-450?

A. That's my understanding, yes.

Q. Okay. I assume, therefore, that your capacity release, your proposed capacity release adjustment is not premised on what you stated earlier to be your belief that the price being paid under that contract is excessive or that the KPC capacity was the most expensive in the MGE area, but based on something else; is that correct?

A. That's correct.

Q. Okay. As you and I discussed when I was originally questioning you earlier today, I believe you indicated that your real concern here -- your real concern here is -- in regards to this proposed adjustment is that MGE had during the summer months of the ACA period excess capacity and that you didn't care whether they released KPC capacity or Williams capacity, as long as they posted some capacity for release, is that accurate?

A. That is correct.

Q. So just hypothetically, if the Williams contract and the Kansas Pipeline contract and Pony Express contract, whatever, were all the same price but were designed to meet MGE's winter load, during the summer they would have excess capacity under one of these contracts, correct?

A. Potentially that would be the case, yes.

Q. Okay. But, again, regardless of the cost embedded in each of the contracts?

A. That's correct.

Q. Okay. And in that situation, I assume it would still be your recommendation that they should attempt to release excess capacity when they have no need for it; is that correct?

A. That's correct.

MR. KEEVIL: Thank you. That's all.

JUDGE WOODRUFF: MGE?

RECROSS-EXAMINATION BY MR. DUFFY:

Q. Okay. Let's talk about Kansas Pipeline briefly. And I don't intend to go back through all the things we did before, but I think we have to establish a few things.

Did the Public Service Commission approve the assignment of what is now the KPC contract from Western Resources to Missouri Gas Energy as a part of its acquisition of those assets?

MR. SCHWARZ: I'm going to object. I'm not sure where this comes into, relates anything to --

MR. DUFFY: Well, Commissioner Gaw was asking him about the contract and the excessive costs under the contract, and I'm simply trying to establish what -- where did this contract come from. And I don't intend to belabor this point, but it was raised by Commissioner Gaw.

JUDGE WOODRUFF: I'll overrule the objection. You can proceed.

BY MR. DUFFY:

Q. Did you understand my question, Mr. Sommerer?

A. Yes, I think so. The Commission authorized or approved of the sale of those assets, and certainly as part of those conditions of sale there were certain assets that were transferred. The Staff's position has been that that did not, in Staff's opinion, mean that there was an approval of those contracts, but they did approve the sale.

Q. Wasn't the assignment of that contract a part of the sale agreement which the Commission looked at and approved?

A. Certainly the allocation of that contract to Missouri Gas Energy was something that was reviewed and the Commission approved the sale.
Q. Okay. The contract lasts 'til when?
A. My recollection it lasts until 2009, but I believe a copy of the contract is in Mr. Langston's testimony.
Q. 2009 is my recollection also. So now, the charges that you said were excessive, those charges are set by the Federal Energy Regulatory Commission, aren't they?
A. After the middle of 1998, I think that's an accurate statement.
Q. Are you aware that the FERC rates paid on the Kansas Pipeline system have been reduced in November 2002 as a result of a FERC order?
A. Yes.
Q. Did that FERC rate case drastically reduce the demand or reservation rates paid by MGE?
A. It appears that that's the intent, although I'm also aware of certain appeals that are underway, and I do not know if that's a final rate.
Q. Do you know whether MGE attempts to market its available capacity during the summer months?
A. They have a history of marketing their capacity on Williams pipeline, and I believe Kinder Morgan

as well.

Q. Relative to the potential -- to the potentiality of releasing capacity on the Williams and KPC systems, did your review show that for each month of the summer MGE was unable to release all of its available Williams capacity?

A. My review didn't concentrate on that aspect.

Q. So you have no knowledge of MGE's actual results in attempting to release its available capacity on Williams in the summer?

A. My recollection is that Mr. Langston has indicated that there was some capacity that they had posted which was not picked up by a customer. So I'm aware of that much of the issue.

Q. So you have no reason to doubt what Mr. Langston said in his testimony about those capacity release attempts on Williams?

A. That's correct.

Q. Are you aware from Mr. Langston's testimony that MGE did, in fact, post Williams capacity for release on a nonrecallable basis and received no bids, even though MGE negotiated recallable releases at rates higher than the rate posted for nonrecallable releases?

A. I am aware of that, yes.

Q. Let's talk for a moment about this notion that

MGE has automatic authority under the tariffs to include and recover the costs of financial instruments. My question to you is, is the Staff the only party who has ever challenged a utility making charges to customers on the basis that the tariff didn't allow the charge? In other words, is the Staff the only party that can recommend disallowances or challenge tariff revisions before the Commission?

A. No.

Q. Public Counsel could do that if they wanted to, right?

A. That's correct.

Q. A municipality could do that if they wanted to, correct?

A. If they have been recognized as an intervenor, yes, that's correct.

Q. Okay. In fact, a complaint statute of the Commission allows lots of people if they meet the criteria to file a complaint and challenge a provision, right?

A. That's my understanding, yes.

Q. Do you remember a bunch of cases that we had several years ago in front of the Commission in which the Federal Energy Regulatory Commission created a thing called taker pay charges and there was a big controversy about whether those charges actually came down to the LDCs, whether they could pass them on to the customers because they weren't charges that were authorized specifically as gas costs?

A. I do recall there were a series of cases regarding that issue, yes.

Q. And there were a bunch of people in here arguing to the Commission that the LDCs ought to eat those costs because they weren't specified as allowable charges in the tariffs, right?

A. I think that was one of the issues, yes.

Q. So no matter whether the Staff believes that the company has the authority to recover these charges or not, and even if the Staff says, yes, you have that authority and you have our blessing, there are going to be people coming out of the woodwork saying, we don't want those charges passed through because they're not in the tariff, and we can spend a week or so in hearings in front of the Commission litigating that issue; isn't that right?

A. I think certainly there is a risk with any tariff provision that it can be challenged by a proper party.

Q. And we've had instances where people have done that, right?

A. That's correct.

Q. Commissioner Murray asked you about Staff's decision not to agree with MGE to increase the trigger price to $3.75, and you stated that you did not agree since MGE was not offering to fix the price at 3.75. Do you remember that?

A. Yes.

Q. Do you have Mr. Langston's direct testimony up there, by any chance?

A. I have his direct, but I don't have his attached schedules.

Q. I want you to look at his Schedule MTL-12, page 3, and let me see if I can find that and give that to you, or maybe your --

MR. HACK: I have it.

BY MR. DUFFY:

Q. Do you have in front of you a -- what's marked as Schedule MTL-12, which I think is a three-page document?

A. Yes.

Q. And that's a letter from Robert J. Hack to Thomas R. Schwarz, Jr., dated September 26, 2000?

A. That's correct.

Q. On page 3, I'll ask you the question, then I'll give you the opportunity to see if you agree that it's reflected on there. On page 3 of that, does that indicate that MGE offered to fix the price only through the winter period or a much shorter period than two years?

A. I assume you're referring to the statement where it says, to address this concern, MGE offered the possibility of fixing the commodity costs within the PGA on the basis of current market conditions only for this winter season?

Q. Yes.

A. Yes, I see that.

Q. Okay. So you'd agree with me, then, that MGE offered to fix the price just for that one winter period and not lock it in for a much longer period?

A. I think that's accurate, yes.

Q. Why did the Staff not agree to that shorter term?

A. I think for the same reason that I discussed with Commissioner Murray, that when this was being considered, the prevailing gas prices were fairly high and extremely volatile, and that would have been at a price in excess of 3.75. We don't believe that would have been a prudent decision.

Q. Because you think prices were going to go down and you didn't want to lock in, even for the one winter period?

A. We believe that potentially at $5 and $6, that prices potentially could go down, and to lock in 100 percent of the supply would not be appropriate.

Q. The fixed commodity price agreement included a provision regarding extensions of the price stabilization plan, including associated cost recovery, correct?

A. Could you provide a cite for that provision?

Q. Give me a second. I'll give you a citation to your direct testimony, Schedule 5-14.

A. I'm there.

Q. Okay. The question was, the fixed commodity price agreement included provisions regarding extensions of the price stabilization plan, including associated cost recovery. Do you agree?

A. I would agree with that, yes.

Q. The Staff supported this agreement, did it not?

A. Yes, it did.

Q. And this agreement in Case No. GO-2000-705 was filed with the Commission in the April/May 2000 time period and approved in August 2000, right?

A. That is correct.

Q. And about two months after that, the Staff opposed MGE's proposal to modify or extend the price stabilization plan, right?

A. That is correct.

Q. Am I wrong or is that a 180-degree change in the Staff's position in that two-month period?

A. When you consider the context of the market conditions, I don't think it's inconsistent. Certainly the Staff was in favor of the price stabilization fund to the extent there was time to implement it and market conditions were reasonably favorable so that it could be implemented. But by the time that MGE had requested an extension, approximately September 26th, it had come very close to the expiration date of the price stabilization fund.

The reason why September 30th was inserted into that provision was to encourage MGE to take steps during the late spring and summer of 2000 to hedge their supplies. And the Staff again, as it said in its response to the company's application at that late juncture, believed that it would be inappropriate to set up a predetermined formula and preapproval.

Q. Well, the stipulation was filed late April, early May, right?

A. That's correct.

Q. So MGE did what it could do to get it filed in time for all these things to happen, right?

A. Well, I would point out that MGE did not ask for any sort of expedited approval or make a motion for expedited approval.

Q. Well, whether it did or -- whether it did that or not, the Commission didn't act on it until August, after it was filed in May, right?

A. That is correct.

Q. Now, are you saying, then, that the Staff's decision to do a 180-degree turn is because the Commission took too long to act on it or because gas prices went up dramatically in the meantime?

MR. SCHWARZ: I'll object to the characterization of 180-degree turn. The witness has already indicated that he, at least, does not concur with that.

JUDGE WOODRUFF: I'll sustain that objection as to the exact language of the question, if you'd like to rephrase it.

BY MR. DUFFY:

Q. Is the Staff's change in position from supporting the stipulation at one point in time to opposing the stipulation at another point in time, is the reason for that your perception that the Commission took too long to act on the application since it was submitted in May and the Commission didn't act 'til August, or was it the fact that gas prices shot up dramatically or was it some combination of those two things or was it something else we haven't talked about?

A. I think it was really timing, timing in connection with market conditions, that by the time you get to late September and if you are in a volatile market and gas prices are high, which is the connection to gas cost, premiums for call options may be extremely high or strike prices may be extremely high. It was the Staff's belief that it was more appropriate to advise the company to take whatever steps the company believed necessary to hedge its portfolio.

Q. And you don't see any inconsistency in that position and the Staff support of the Laclede stipulation in the same late time period?

A. No, I do not.

Q. There were some questions from Commissioner Gaw about how this 30 percent related to the termination of damages or economic harm, whatever you want to call it here.

My question to you is, in developing its assessment of damages based on this 30 percent number, did the Staff examine the amount of its recommended disallowance in this case in relation to MGE's net operating income for the 2000-2001 ACA year?

A. I don't think there was a specific evaluation. There may have been some discussion about the magnitude of various adjustments, but it was in a very generalized way.

Q. Are you aware that adoption of Staff's disallowances in this proceeding, even without considering the Mid-Kansas/Riverside issue that we're not at hearing here about, that that would drive MGE's net operating income for 2000-2001 below zero?

A. We have not evaluated that aspect.

Q. So you weren't aware of that?

A. No.

Q. Commissioner Murray was asking you questions about the fact that it apparently took a couple years of no capacity release or it took a couple years of the fact that MGE wasn't scheduling gas on KPC in the summertime before the Staff decided to propose its disallowance in this case, and she indicated that maybe Public Counsel could develop that.

Do you still have a copy of your deposition up there with you?

A. Yes.

Q. In order to address her concerns, I'm going to propose that maybe I'll read the question and you read the answer out of the deposition for a short excerpt here and hopefully that'll address what she wanted to know about. Please turn to page 22 in the deposition.

A. I'm there.

Q. Okay. What I'm going to do is, I'm going to read the question that I asked at the deposition, and I'd ask then that you read the answer that you gave, and that way we'll get it in the record here. And what we're going to do is we're going to go over -- we're going to do that page 22 and we're going to go over through the top half of the next page, 23. Okay?

So the question I asked was, why, given that this situation has existed for perhaps a couple of ACA periods, is your adjustment showing up in this ACA period as opposed to a previous ACA period?

A. Answer: Well, as I indicated before, it took several years' worth of data before I became convinced that the pipeline was not being used during the summer months on MGE's system.

Q. So I guess what you're telling me is, you could have made this proposal in prior ACA periods if you had felt like it?

A. The review probably was -- was done. I know that Staff has tracked the volume, those monthly volumes every year, since they specifically relate to the other adjustment the Staff makes. However, the Staff did not notice the trend for that idle capacity until sometime during the review for the most recent ACA period.

Q. So you may have thought that the idle capacity was an anomaly in the previous periods?

A. That's possible, yes.

Q. But you did not investigate in those previous periods whether it, in fact, was an anomaly or not?

A. I would simply say that Staff noted that the volumes weren't being taken, but simply went no further than that.

Q. What was it that triggered you to do it in this case, as opposed to the previous ACA cases? Or was there something or was it just a gradual recognition that there's -- you suddenly discovered there was a trend there?

A. I think it's the latter. It's a gradual recognition of the trend.

Q. Okay. Thank you.

Now let's get into the topic of capacity releases on the Williams system. Let's look again at your deposition on page 41. Are you there?

A. I'm there.

Q. Okay. What I want to do is, I want to read the question I asked you that appears on lines 10 through 13, and then I'd like you to read your answer that appears on lines 14 through 25.

Here is the question I asked: Explain to me the factual basis for your assumption MGE would have obtained 75 percent of the Williams maximum rate if they had released capacity on the KPC system.

A. It was generally an extrapolation of what I had looked at on the Williams system. The releases on the Williams system that were done on a nonrecallable basis were at 100 percent of Williams' maximum rate. To me that set the upper boundary of what that release could have attained in the marketplace. The lower boundary, in my opinion, was approximately 50 percent, and that was simply based upon the fact that nonrecallable releases were anywhere from 10 to 20 percent, and there would be some additional value over and above the amount for nonrecallable releases.

Q. Okay. Now, with regard to that schedule you attached to your surrebuttal that listed all of those transactions on Williams in the ACA period, even if you were to assume that there were actually transactions on Williams that were nonrecallable and at the maximum tariff rate, weren't almost all of those transactions either conducted prior to the ACA period in question or very, very small quantities not comparable to the 46,000 decatherms MGE would have had to release?

A. Well, clearly there isn't an example of a number that approaches 46,000 in terms of a nonrecallable release. I will say or point out on Schedule 2-21 -- and I just happened to turn there randomly -- but this may appear in other months --

MR. DUFFY: Hang on just a second. Let me get that.

MR. SCHWARZ: Excuse me. Which page?

MR. DUFFY: 2-21.

BY MR. DUFFY:

Q. Is that what you said?
A. That's correct.
Q. Okay. Go ahead with your answer.
A. On 2-21, you do see a release that takes place there for 2,500 in the production area, 1,800 in the market area --
Q. Let's stop you. Give me the offer number on that page, so I can find what you're talking about.
A. The offer number is 644 and 645.
Q. Okay. Go ahead with your answer then.
A. And that release does appear to take place within the ACA period.
Q. Okay. But it didn't begin within the ACA period, did it? It's not in the summer months because it shows that it started on December 1st, 2000. The last time I checked, December wasn't a summer month.
A. That's correct. Let me see when that -- it looks like that release takes place on a monthly basis, so let me see when it started.
I'm not sure when that started, but if you go to April of 2001 --
Q. Give me a schedule number, please.
A. Schedule 2-36.
Q. And then give me an offer number.
A. Offer No. 1000068, and 1000069.

Q. Okay. Go ahead, then.
A. That looks like a similar release. It might not be for quite the same amount, but it certainly does touch upon that ACA period. It's nonrecallable. It's for a more significant level of volumes.
Q. That one doesn't appear to have started in the summer, does it?
A. It starts in February; however, it goes until June of 2001. So it does include some late spring months.
Q. February is late spring?
A. No. April and May I classify as being late spring.
Q. But your proposal was that this release would be in the summer months, and this isn't the summer months specifically, is it?
A. We've used the term "summer months" for shorthand, but I think the disallowance does go to April and May or includes April and May.
Q. What are the volumes on that?
A. Volumes are 2,500.
Q. And you think 2,500 is comparable to 46,000?
A. I would simply say it's not an insignificant amount of volumes, but certainly it is not comparable to 46,000.
Q. Let me ask it this way: With regard to

everything that appears in your Schedule 2, are there any transactions that are, No. 1, biddable, No. 2 -- and by biddable I mean nonprearranged -- No. 2, nonrecallable, and 3, they actually took place and were made during the summer months of this ACA period? Are there any that fit those three criteria?

That means they'd have to have a Y in the biddable column, and under our review an N, meaning nonrecallable in the recall, and it begins sometime in the summer of 2000, meaning July through October -- or June through October. Are there any that fit that criteria?

A. I haven't made an extensive line by line analysis. That would take some time. But based upon some spot checking, I have not seen anything that fit that particular criteria.

MR. DUFFY: Those are all the questions we have. Thank you.

JUDGE WOODRUFF: All right. Redirect?

REDIRECT EXAMINATION BY MR. SCHWARZ:

Q. Mr. Sommerer, you're aware that from the testimony and your review of the records that MGE did do some fixed prices in this ACA period; is that correct?

A. That is correct.

Q. And they did so without any specific tariff authorization during this ACA period; is that correct?

A. That's correct.

Q. Commissioner Murray asked you a question that involved assuming that the prices through the month did drop and asked if Staff's position would be different in that case, but isn't it true that when you're considering hedging from a perspective of protecting customers from price spikes, that the real risk is that prices will increase rather than they'll drop? Would you agree?

A. That's correct.

Q. Commissioner Murray asked you some further questions about storage, and I think you indicated that storage works like a fixed price; is that correct?

A. That's correct.

Q. Do you recall that? And would you agree that there are operational considerations that require LDCs to use storage whether the ability to work as a financial hedge or anticipation that it will be a substantial financial hedge is present, for operational purposes LDCs need storage to meet their consumers' demands in the winter?

A. Certainly the operational aspects are one of the primary drivers for how storage is used.

Q. Commissioner Gaw asked you if the 30 percent was calculatable in advance. Do you recall that?

A. Yes.

Q. I want to explore that a little bit, if I might. If an LDC submitted a reliability report, supply and transportation and storage plan for the upcoming heating season, if they submitted that plan in January of -- you know, before the heating season, would you expect that that plan might need to be changed as market conditions change during the year?

A. Yes.

Q. And that might be possible all the way up to September, October, November, as market conditions change; would that be correct?

A. That is correct.

Q. And once you get into the heating season itself, the company might still need to adjust its operations to reflect the changing market conditions and weather patterns as those unfold; would that be correct?

A. That is correct.

Q. And as the LDC would get into the operational stage, the execution stage of the plan as its execution changes, it would then have to modify the plan for the balance of the heat season to take that into account; is that correct?

A. Yes, that's correct.

Q. I want to ask you to think about the various data tables and so forth that are in evidence in this case. Do you think it would be possible to calculate the break-even point on the Williams -- you know, release of capacity on Williams and utilization of the Mid-Kansas/Riverside transportation?

A. Given the data that's on the record, I think that is possible, yes.

Q. I'm not going to ask you to do it now.

MR. KEEVIL: Judge, just for clarification, I guess I would object to the -- during the ACA period that that relates to, it was Kansas Pipeline Company, as opposed to Mid-Kansas/Riverside.

MR. SCHWARZ: I apologize.

JUDGE WOODRUFF: The clarification is noted.

MR. KEEVIL: Thank you.

BY MR. SCHWARZ:

Q. You recall a question, I think from Mr. Duffy, about a bunch of cases on the taker pay with people arguing that they couldn't be charged because it wasn't in the tariff?

A. Yes.

Q. And did the Commission ultimately reject those contentions and permit the taker pay cost to be recovered?

A. That was my recollection, was that they considered taker pay a gas cost recoverable pursuant to the purchased gas adjustment clause.

Q. Do Missouri local distribution companies

routinely act as Staff might recommend to them informally?
A. No.
MR. SCHWARZ: I think that's all.
JUDGE WOODRUFF: All right. Then you may step down.
Before we go on, during lunch you produced copies of these Exhibits 19 and 20HC, which were laid on my desk. Do you want to offer those at this time?
MR. SCHWARZ: I would. And for the record, I would like to say that Exhibit 19HC is now a cover sheet with -- of the reliability report, and then pages 10 through 16 of the '98-99 reliability report, and that Exhibit 20HC is the cover of that document, and then pages 7 through 11. And I -- with that clarification, I would like to offer Exhibits 19HC and 20HC.
MR. DUFFY: It's not that I don't doubt him. But I've not seen a copy of what he just talked about. So I'd like to see that.
MR. KEEVIL: Mr. Duffy, you just said, it's not that I don't doubt him.
MR. DUFFY: Well, that means that I don't trust him then.
(Laughter.)
MR. DUFFY: My concern was, I've not been given a physical copy of what you're offering here, and I'd

just like to have one before it gets admitted.

JUDGE WOODRUFF: And I don't have to rule on it today. If you want a chance to look at it, we can wait until tomorrow morning to rule on it. I'll defer ruling on that until tomorrow until everyone's had a chance to look at it.

The next witness on my list, then, would be Lesa Jenkins. And I'm assuming we're probably not going to finish her in 35 minutes. I see nods of agreement out there. So I suggest we just wait until tomorrow morning to start with Lesa, Ms. Jenkins.

MR. DUFFY: Your Honor, I've had a chance to look at these, and we don't have objections to Exhibits 19HC and 20HC in their reduced form.

JUDGE WOODRUFF: Okay. Mr. Keevil, do you have any objection?

MR. KEEVIL: In the reduced form in which Mr. Schwarz has now offered, I have no objection. I do have one question.

The cover page says highly confidential, then only certain pages within the -- only the ones with tables on them have highly confidential on each given page. And my question -- maybe it should be directed to Mr. Duffy instead of you, Mr. Schwarz, but do you know, is the whole thing highly confidential or is it just those pages that have highly confidential stamped on the pages?

MR. SCHWARZ: It was provided to us -- to the Staff, I should say, pursuant to earlier agreements and understanding -- I mean, it's not stamped as HC as provided under the Protective Order in this case. So my understanding would be that unless otherwise noted, it's all HC.

MR. DUFFY: MGE's position is the entire contents, except for the first page and cover page, should be treated as highly confidential. So whatever we have to do to accomplish that result in this record, if that means stamping each page HC on the exhibits that the court reporter has, we can do that, but we need the contents kept highly confidential.

JUDGE WOODRUFF: Okay. For purposes of this hearing, then, the entire contents of 19HC and 20HC are highly confidential. If you wish to go ahead and stamp those copies in the official file, that would certainly be a good idea.

Okay. Let's go ahead and rule on them, then. 19HC and 20HC have been offered into evidence. Are there any objections to their receipt?

(No response.)

JUDGE WOODRUFF: Hearing none, they will be received into evidence.

(EXHIBIT NOS. 19HC AND 20HC WERE RECEIVED INTO EVIDENCE.)

JUDGE WOODRUFF: And as I previously indicated, rather than starting with Ms. Jenkins this afternoon, we'll go ahead and start with her in the morning. So at this time we'll adjourn until 8:30 tomorrow morning. Thank you.

WHEREUPON, the hearing of this case was recessed until May 14, 2003.

I N D E X

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