

Exhibit No..
Witness: John B. Snell
Issue: Price Stabilization
Fund; Hedging Practices
Type of Exhibit: Surrebuttal Testimony
Sponsoring Party: Laclede Gas Company
Case No.: GO-98-484

SURREBUTTAL TESTIMONY

OF

JOHN B. SNELL

LACLEDE GAS COMPANY

Case No. GO-98-484

FILED
AUG 5 1998
Missouri Public
Service Commission

St. Louis, Missouri

August, 1998

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's)
Tariff Sheets designed to extend for an)
additional year the experimental price)
stabilization fund.)

Case No. GO-98-484

A F F I D A V I T

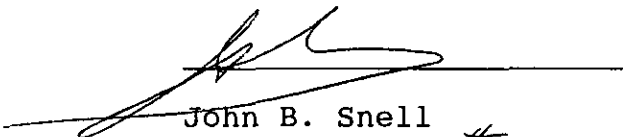
STATE OF ILLINOIS)
) SS.
COUNTY OF COOK)

John B. Snell, of lawful age, being first duly sworn,
deposes and states:

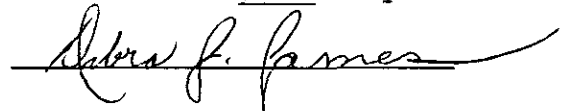
1. My name is John B. Snell. My business address is
Chicago Board of Trade Building, 141 West Jackson Blvd.,
Suite 1800A, Chicago, Illinois 60604; and I am President of
Risk Management, Incorporated.

2. Attached hereto and made a part hereof for all
purposes is my surrebuttal testimony, consisting of pages 1
to 12, inclusive.

3. I hereby swear and affirm that my answers contained
in the attached testimony to the questions therein propounded
are true and correct to the best of my knowledge and belief.


John B. Snell

Subscribed and sworn to before me this 4th day of
August, 1998.





SURREBUTTAL TESTIMONY OF JOHN B. SNELL

1 Q. Please state your name and business address.

2 A. My name is John B. Snell, and my address is Suite 1800A,
3 141 West Jackson, Chicago, Illinois 60604.

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

5 A. I am the president of Risk Management Incorporated (RMI).

6 Q. What is the business of RMI?

7 A. RMI offers risk management services to public utilities
8 and other businesses through consulting and brokerage
9 services. These services help clients determine the
10 need for and means of controlling or reducing risk. The
11 primary focus of RMI is to provide to clients an
12 awareness of how risk management can be used to provide
13 positive benefits in increasingly complex markets, and
14 to match the physical needs of a client's business with
15 a distinctive strategy tailored to the client's needs.

16 Q. Please describe your educational background and work
17 experience.

18 A. After receiving a Bachelor of Science degree in Finance
19 from the University of Illinois in Champaign, I received
20 a Master of Science degree in Industrial Management from
21 Georgia Tech. I have worked in risk management for over
22 20 years, designing risk management strategies directed
23 to clients' specific needs. My career began as a
24 commodity analyst at Merrill Lynch, where I worked with
25 major corporations in hedging agricultural products.
26 After leaving Merrill Lynch, I worked independently as a

1 broker and consultant, and 11 years ago I formed the
2 company presently known as RMI. For the past 18 years,
3 I have worked with a discrete number of multi-national
4 corporations with billions of dollars of products and
5 supplies subject to market risk, creating and
6 implementing strategies to reduce or control the risks
7 to which those companies are exposed. Through RMI, I
8 have been providing consulting services to utilities
9 since shortly after gas futures became available on the
10 New York Mercantile Exchange (NYMEX) in the spring of
11 1990.

12 Q. Please describe briefly the services you provide to
13 utilities in these areas.

14 A. Our consulting services are directed toward assisting
15 the customer in understanding the benefits that risk
16 management can provide to a company, and developing and
17 using risk management strategies. This includes the
18 preparation of company policies and procedures for a
19 risk management program, a series of workshops and
20 conferences to provide in-depth training of key
21 personnel who will be responsible for trading
22 operations, the development of pilot programs, the
23 gradual expansion of the original pilot programs to
24 include more comprehensive risk management, the
25 evaluation of incentive programs to address the
26 implementation and execution of hedging programs,
27 positioning software to track and interrelate physical
28 transactions with financial transactions, and

1 step-by-step documentation of pricing decisions and
2 rationale, including a recap of expected results. When
3 requested, we assist in the filing of a proposal,
4 assembling exhibits and providing testimony before
5 regulatory commissions on the role of risk management
6 for utilities.

7 Q. Have you provided such assistance to gas utilities other
8 than Laclede Gas Company (Laclede)?

9 A. Yes, I have helped over 20 utilities throughout the
10 country initiate risk management programs. In addition
11 to conducting numerous presentations for staff members
12 of regulatory commissions, I have also submitted
13 testimony on two separate occasions in Rhode Island, and
14 once in Illinois on behalf of gas utilities. I am also
15 preparing to testify in the Province of Ontario,
16 Canada. I spoke at the New England Gas Association
17 Annual Conferences in April of 1997 and April 1998. I
18 also spoke at a statewide conference sponsored by the
19 Missouri Public Service Commission in May of 1997, and
20 in July of 1997 I presented a full day's program to the
21 Subcommittee on Gas at the NARUC national convention in
22 San Francisco. In December of 1997, at the invitation
23 of the NYMEX, I spoke at a one day conference of NARUC
24 members.

25 Q. Have you reviewed the rebuttal testimony filed in this
26 proceeding by Commission Staff witnesses David Sommerer
27 and James A. Busch?

28 A. Yes, I have.

1 Q. Do you agree with the Staff witnesses' conclusions that
2 Laclede's proposed revisions to its Price Stabilization
3 Plan (PSP) are illogical and would be detrimental to
4 ratepayers?

5 A. No. ** _____
6 _____
7 _____
8 _____
9 _____
10 _____
11 _____
12 _____

13 ** It would
14 provide Laclede the ability and incentive to acquire
15 price protection for its customers at an optimal cost.

16 Q. Mr. Sommerer and Mr. Busch have characterized Laclede's
17 proposal as an "elaborate plan" with many "speculative
18 elements." Do you agree with these characterizations?

19 A. No. ** _____
20 _____
21 _____
22 _____
23 _____
24 _____
25 _____
26 _____
27 _____

28 ** With regard to the
allegation that Laclede's proposal is speculative, I

1 completely disagree. By definition a speculator is a
2 market participant who **_____

3 _____** for the sole purpose of making a profit.

4 **_____

5 _____** in
6 conjunction with a physical transaction that will occur
7 at a later date. Laclede will need to ultimately pay
8 for the cost of gas associated with its physical
9 contracts and, unlike a speculator, it must be involved
10 in assessing price risk associated with a constantly
11 changing gas market. Since Laclede's program is
12 entirely designed to provide price protection for
13 physical natural gas Laclede needs to purchase in the
14 winter period, it is not a speculative program.

15 Q. Do unregulated companies employ **_____**
16 programs to hedge their positions in commodities markets?

17 A. It can happen, but virtually every company that hedges
18 its physical position in an unregulated environment
19 retains the flexibility to **_____** in
20 response to changing market conditions. In my opinion
21 it is not the most efficient strategy for any company to
22 implement a **_____** strategy that ignores
23 changes that might occur in the market.

24 Q. Even if Laclede's proposed Incentive PSP does not
25 technically constitute speculation, doesn't it subject
26 Laclede's ratepayers to unreasonable financial risks as
27 indicated by the Staff?

28 A. Absolutely not. **_____

1 _____
2 _____
3 _____**.

4 Since under Laclede's program the very most that
5 ratepayers would have to contribute toward the purchase
6 of such instruments in any given year is **_____

7 _____,**
8 plus any transaction costs, this amount represents the
9 very most ratepayers would have to pay for price
10 protection in a given year. Of course, under the
11 proposed PSP, Laclede will have a financial incentive to
12 reduce, and even eliminate, this cost to its
13 ratepayers. In my opinion, Laclede's customers are
14 subject to a substantially greater risk of paying more
15 for price protection under the existing program, since
16 Laclede is prohibited from adjusting its position in
17 response to changing market conditions **_____

18 _____**.

19 Q. On pages 9-10 of his rebuttal testimony, Mr. Busch
20 argues that giving Laclede the flexibility **_____

21 _____** will lead to the potential that
22 ratepayers may be "unhedged and vulnerable to unlimited
23 adverse price movements," and that ratepayers could "get
24 nothing for their **_____**." Do you agree with
25 Mr. Busch's statements?

26 A. No. Under Laclede's proposed program, the volumes that
27 must be protected could never be **_____

_____. **. Laclede
would be absolutely required to ** _____

_____. **, no matter what. Laclede would also be
required to guarantee a certain level of price
protection to its ratepayers regardless of ** _____
_____ ** it purchases to provide the
required protection.

Q. Does the Staff testimony recognize at all the value of
permitting Laclede to adjust its position ** _____
_____ ** to reflect market conditions?

A. Yes. On page 26 of his rebuttal testimony, Mr. Busch
paradoxically recognizes that it is in the interest of
Laclede and its ratepayers for Laclede to ** _____

_____. **. This is the same
logic that supports Laclede's proposal to maintain the
flexibility to adjust its position after ** _____

_____. **. If Mr. Busch believes
it is in the ratepayers' interest for Laclede to have
such flexibility ** _____ **, it
should also be in the ratepayers' interest to retain
that flexibility ** _____ **.

Conversely, if Mr. Busch believes that it is
inappropriate to permit Laclede the flexibility to

1 respond to market conditions, he should be advocating a
2 requirement that Laclede ** _____

3 _____
4 _____**. His inconsistent,
5 "middle ground" position that Laclede should have the
6 flexibility to adapt to market conditions some of the
7 time, but not all of the time, makes no sense.

8 Q. On pages 5 and 6 of his testimony, Mr. Sommerer argues
9 that the Incentive PSP's goals of obtaining ** _____
10 _____** and minimizing the cost of
11 the program are inconsistent. Do you agree?

12 A. ** _____
13 _____
14 _____
15 _____
16 _____
17 _____
18 _____
19 _____
20 _____
21 _____
22 _____**. In an
23 analogous situation, when individuals purchase insurance
24 policies, they are faced with a similar "inconsistency"
25 -- there is a natural tension between the desire for low
26 premiums and low policy deductibles. But that
27 "inconsistency" does not mean, as Mr. Sommerer's

1 testimony suggests, that no one should ever buy an
2 insurance policy.

3 Q. On page 15 of his rebuttal testimony, Mr. Busch raises a
4 technical concern with Laclede's proposed method for
5 calculating **_____

6 _____
7 _____** there are generally not
8 enough data to make a determination as to what the value
9 would be. Do you agree with this statement?

10 A. No. Laclede proposes to obtain values used in the
11 calculation of the TSP from the NYMEX, because the NYMEX
12 is an unbiased provider of market pricing **_____

1 _____
2 _____ **.
3 Q. On page 16 of his rebuttal testimony, Mr. Busch
4 criticizes the proposed calculation of the CPL **_____
5 _____** above the TSP. He argues that no
6 support has been provided to show why **_____** was
7 chosen. Do you agree with Mr. Busch's criticism?

8 A. No. The establishment of parameters for a program such
9 as the one Laclede has proposed requires the use of
10 judgment. There is no precise formula that would
11 provide a mathematically verifiable calculation of the
12 CPL, just as there is no mathematical formula that
13 determines **_____

14 _____
15 _____**
16 (parameters which, incidentally, I understand were
17 developed by the Staff.) **_____

18 _____
19 _____
20 _____**.
21 Q. On page 16 of his rebuttal testimony, Mr. Busch raises
22 the specter that Laclede's cost of commissions and
23 transaction fees could rise dramatically if Laclede is
24 **_____**. Do you agree
25 with this assessment?

26 A. No. Although Laclede's transaction costs may increase
27 somewhat **_____

_____, **, the increase should not be substantial.
The parameters of the program would require Laclede to
act as a hedger, and so it would not be engaged ** _____

_____. **. In any event, the potential of a relatively
minor increase in transaction costs should not prevent
the Commission from implementing this program if it is
in the interest of Laclede and its ratepayers.

Q. Please summarize your testimony.

A. Laclede's proposed revisions to its PSP represent
significant improvements over the existing program.
Permitting Laclede ** _____

_____ ** on an equal footing with other
businesses that hedge their physical requirements for
various commodities with financial instruments. This
added flexibility will not make Laclede a "speculator"
or subject Laclede's ratepayers to unreasonable risk,
given Laclede's commitments ** _____

_____ **. It will simply give Laclede the tools
necessary to adequately manage price risk in a volatile
market, and provide Laclede with a financial incentive
to acquire coverage for its ratepayers at the most
reasonable total cost. The revised program is a
substantial improvement over the ** _____

_____ ** program that Laclede currently uses.
From a technical standpoint, contrary to the Staff's
assertions, the program will work. Specifically, it

1 contains a workable, objective method for calculating
2 the TSP, it sets the CPL at a reasonable level, and it
3 is unlikely to result in substantially increased
4 transaction costs. For all these reasons, the
5 Commission should approve the revisions to the program
6 proposed by Laclede.

7 Q. Does this conclude your testimony?

8 A. Yes, it does.