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In the Matter of Missouri Gas Energy's Tariff Sheets Designed to Renew for an Additional Year the Price Stabilization Fund and Capacity Release Incentive Mechanism.) Case No. GO-2000-231

LEWIS R. MILLS, Presiding,
DEPUTY CHIEF REGULATORY LAW JUDGE.

SHEILA LUMPE, Chair,
CONNIE MURRAY,
ROBERT G. SCHEMENAUER,
COMMISSIONERS.

REPORTED BY:

KELLENE K. FEDDERSEN, CSR, RPR
ASSOCIATED COURT REPORTERS, INC.

APPEARANCES:

ROBERT J. HACK, Attorney at Law
3420 Broadway
Kansas City, Missouri 64111

FOR: Missouri Gas Energy.

DOUGLAS E. MICHEEL, Senior Public Counsel
P.O. Box 7800
Jefferson City, Missouri 65102-7800

FOR: Office of the Public Counsel and the Public.

THOMAS R. SCHWARZ, JR., Deputy General Counsel
P.O. Box 360
Jefferson City, Missouri 65102

FOR: Staff of the Missouri Public Service Commission.

P R O C E E D I N G S

JUDGE MILLS: Let's go on the record.

We're here this afternoon for an on-the-record session in Case No. GO-2000-231, in the Matter of Missouri Gas Energy's Tariff Sheets Designed to Renew for an Additional Year the Price Stabilization Fund and Capacity Release Incentive Mechanism.

Let's do entries of appearance beginning over here with Mr. Hack.

MR. HACK: Robert J. Hack appearing on behalf of Missouri Gas Energy, 3420 Broadway, KC, MO 64111.

JUDGE MILLS: Mr. Schwarz?

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

JUDGE MILLS: Mr. Micheel?

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

JUDGE MILLS: Thank you. Is there anything we need to take up on the record before I get the Commissioners and they can ask their questions?

MR. HACK: Not to my knowledge.

JUDGE MILLS: Hearing nothing, we're off the record.

(Discussion off the record.)

JUDGE MILLS: Let's go back on the record.

We're back on the record in GO-2000-231, and we're ready for questions from the Bench of the parties. Let's begin with the Chair.

CHAIR LUMPE: I think my questions are basically those that I read in the paper, so I'll just start with those.

The Commission wanted to know, and I would like to know, have you done any hedging for this year already?

MR. HACK: And this is Mike Langston who is our Vice President of Gas Supply, and I'll ask him to answer some of those questions, and that's a good one for Mike.

JUDGE MILLS: I was going to say, let's follow this procedure. If the attorneys, if it's a fairly general question, the attorneys can answer it on behalf of their clients, just go ahead and answer from where you stand. If you want to bring an expert, we'll bring the expert forward, swear him in and he or she can answer questions from there.

MR. HACK: How about I'll give it a shot, and then if Mike wants to be sworn he can tell me? How's that?

Right now we're not hedging in Missouri. We are hedging -- Southern Union is hedging in El Paso pursuant to specific municipal ordinance authority down there.

CHAIR LUMPE: So you did hedge last year prior to the last year's heating season, but then for this year's heating season you have not done any hedging?

MR. HACK: We hedged for the last heating season and the heating season before that pursuant to specific tariff authority that we're seeking to renew right now, exactly the same way.

CHAIR LUMPE: Is there a reason you waited until this late to ask for that authority?

MR. HACK: We have been since December of last year engaged in discussions with the Staff regarding the whole -- and Public Counsel -- regarding the whole issue of the regulatory treatment of gas costs. And as you know, I think, our EGCIM expired at the end of June, and through the discussions we have been attempting to negotiate along the lines of a fixed price commodity PGA.

And we saw the price stabilization fund and the fixed price commodity PGA as kind of mutually exclusive concepts. So we were hopeful, and maybe we're guilty of being overly optimistic, of reaching agreement on the fixed price commodity.

When it became apparent that that was not possible prior to this winter heating season, we filed to renew the price stabilization fund. And frankly, we were also trying to take into consideration your decision in the Laclede case 99-303 which came out on September 9.

CHAIR LUMPE: The cap, and I think that's probably confidential so I won't mention it, but there was mention in there that the cap was raised. Is that a function of having waited so long or --

MR. HACK: Basically, it's a function of -- this is a good one where I think I want to get Mike up on the stand. If I could call Mr. Langston to the stand.

JUDGE MILLS: Sure. Please come forward.

(Witness sworn.)

JUDGE MILLS: Thank you. You may be seated.

MICHAEL LANGSTON testified as follows:

QUESTIONS BY CHAIR LUMPE:

Q. Mr. Langston is it?

A. Yes, ma'am.

Q. Would you like to respond to that question?

A. We -- the price cap was increased primarily because, at the time that we filed the tariffs, we went to the market and got a quote of what could be done immediately prior to the time that we filed the tariffs, and what we found is that that was higher than what -- than what we had in our filing last year.

So not knowing what the market would do between the time that we filed tariff sheets and the time that the Commission would act on our request, we frankly increased the cap levels to make sure that we could act within what we expected the market to do during that interim time period.

Q. So it was partially a result of having waited this late? In other words, had you been able to do this last summer, you may not have needed to raise the cap?

A. We may still actually purchase these instruments at substantially below. The cap only served as an outside boundary as to the authority that we were seeking to be granted by the Commission. It doesn't indicate the price that we expect to actually purchase the instruments at depending again on the time of approval.

Obviously you can -- the market was substantially lower in March of '99 than it was throughout the late summer and into the fall. So you can say it would have been lower, say, in March, but it may not necessarily have been lower later on in the summer.

Q. In August, do you remember?

A. You know, I don't remember the exact status of the market at those different points in time.

Q. I had a question and it left me.

Could you tell me what potential impact to the ratepayer there might be because of the increase in the cap? I think I heard you say there could be none, but there could be -- could be and, if so, what might there be?

A. We sought some quotes last night of the status of the market. Were we able to actually implement these transactions as of the close of business last night, we could have actually obtained price levels that were essentially between the levels that we achieved last year and the levels that we achieved the year before. So we would have been essentially right in the same range.

However, the market was up over 10 cents as of 11 o'clock this morning. So, you know, so much depends on the timing of these instruments.

Q. And you would look at that timing in doing your purchasing or your hedging?

A. Yes, ma'am.

Q. Would you be the correct person to -- I have a question on the capacity release item. Would you be the proper person to ask that?

A. I believe so, yes.

Q. Okay. What struck me was that your program is sort of the reverse of Laclede's. In other words, at the beginning they share less, and then the more they save the more they share. And yours seems to be the reverse; at the first you share 50 percent and then you share less and less. Why is that a better incentive to share less than to share more?

A. Honestly, when we filed this, we looked at in the Laclede Order it simply reauthorized the tariff authority that they had had in their capacity release portion of their incentive mechanism.

This reflects the same capacity release incentive that we had in our incentive mechanism when it was done. This was the result of the litigated case in GO-94-318 that reconciled different positions that the parties had in the case.

Q. Was your EC--

A. ECGIM, yes, ma'am.
Q. Was it put in place before Laclede's?
A. Yes, it was.
Q. Okay. So that it's possible that someone looked at yours and said it might be a better incentive to do it this way than that way?
A. Yes, ma'am. And we also have significantly different capacity contracts. Laclede has a large number of what I would call upstream capacity arrangements on systems that feed their main pipeline supplier. Our capacity arrangements are primarily on the main line transmission systems that serve our service territory. So we do have some very different structural contract arrangements.
Q. But do you think in theory that if you get to share more the more you save that that is a better incentive?
A. We're certainly more for all -- for more incentive. Given the status of the market on the systems that serve our area, we feel like our current structure is reasonable, is a reasonable compromise between the company's interests and ratepayers' interests. We certainly can restructure that incentive.
Q. If you were to reverse the -- instead of

starting at 50 and going down, start at -- I forget what the bottom number is and going up?

A. That certainly would provide us a greater portion of the sharing of any capacity release revenues generated.

CHAIR LUMPE: Thank you. Those are my questions.

JUDGE MILLS: Commissioner Murray?

COMMISSIONER MURRAY: Thank you.

QUESTIONS BY COMMISSION MURRAY:

Q. Good afternoon. The hedging authorization ceased on May 1st, '99; is that correct?

A. I believe that's correct.

MR. HACK: With our summer PGA filing.

BY COMMISSIONER MURRAY:

Q. And I just want to make sure I understand what you said, Mr. Hack, that MGE has not done any hedging since May 1, '99; is that correct?

A. For the Missouri properties, that's correct.

Q. Okay. I wasn't quite clear on the time period in there.

COMMISSIONER MURRAY: I think my other questions have been asked. Thank you very much.

JUDGE MILLS: Commissioner Schemenauer?

COMMISSIONER SCHEMENAUER: Thank you.

QUESTIONS BY COMMISSIONER SCHEMENAUER:

Q. Good afternoon, Mr. Langston.

A. Good afternoon.

Q. I take it from your responses to the Chair's questions you do not feel that it's too late to achieve any realistic savings for consumers through hedging strategies for this heating season?

A. We think that the instruments will -- would be able to provide price protection for our ratepayers for this winter.

Q. Even with the 10 cent increase you looked at today -- yesterday? Was it up earlier in the day and did they close lower? I know these things fluctuate.

A. They fluctuate very widely. There can be 20 to 30 cent movements in the market on any day, up one day, down the next day. So this 10 cent movement in the market this morning represents a very normal fluctuation in the price levels.

Q. There's been a lot of press from the Federal Government to expect 30 percent increase in heating costs this season for a variety of reasons. Some of them I don't think are applicable to natural gas, but do you think that's already been absorbed into the market, the natural gas market?

A. I can give you my personal opinion, which is all I can do.

Q. I understand.

A. It's not necessarily the company's position. Right now we're in what I generally think of as a shoulder period. It's between the period when you have high natural gas demand for electric generation for air conditioning and between the period you would have higher demand for natural gas for residential heating primarily. So this tends to be a point when prices will tend to trend down.

The actual increase in price to the consumer during the winter period is going to be substantially driven by the weather. We've had -- I think the weather in our service territory last year was 85 percent of normal, which is a substantially below normal type of weather profile in our service territory.

To the extent that there is normal weather across the nation, normal heating, heating demands, my expectation would be prices this winter for consumers would be higher than last winter.

Q. Are your reserves at approximately the same level they were last year at this time, your natural gas reserves?

A. When you say reserves, our storage levels --

Q. Your storage.

A. -- we are within a couple hundred thousand MMBtu's of our planned storage level as of the end of September and anticipate we're going to be in the 97, 98, 99 percent full range by the end of October, which is the end of the injection season. So yes, we are right on plan.

Q. So your inventories are about 200,000 --

A. Yes, sir.

Q. -- MMBtu's?

A. Out of about -- we are right at 15 billion cubic feet in inventory, which is only about 200,000 MCF difference from our plan. So we're within, what's that, 1.3 percent of our plan, which is a normal variation for us.

COMMISSIONER SCHEMENAUER: That's all the questions I have. Thank you.

JUDGE MILLS: Any of the Commissioners have questions for the other parties?

CHAIR LUMPE: Yes. I would like to ask Staff their opinion. Is it -- do you feel there's still a benefit that can be obtained for the ratepayers by hedging at this late?

MR. SCHWARZ: I would ask Mr. Straub to --

JUDGE MILLS: Mr. Langston, why don't you step down, and Mr. Straub, why don't you come forward?

(Witness sworn.)

JUDGE MILLS: You may be seated.

MICHAEL STRAUB testified as follows:

THE WITNESS: It's Michael W. Straub, S-t-r-a-u-b.

And to answer your question, yes, Staff is of the opinion that, even at the higher level at the cap, that we would prefer to have some protection for the coming winter than to have none.

QUESTIONS BY CHAIR LUMPE:

Q. Is part of that because you feel it's going to be an increase in the prices or that it's going to be a more difficult winter or colder winter, or does your assessment depend?

A. We believe that what could happen this winter could be very large in magnitude. I mean, it could swing a great deal. And as Mr. Langston indicated, it seems to be weather driven.

So after the winter of '96-'97, Staff has preferred to be hedged rather than to go into a winter exposed at the possibility of having extremely high spot market gas prices.

Q. And the increase in the cap you feel is reasonable?

A. We feel the cap would still be hedged at a level that's at or less than the PGA was in the '96-'97 winter period.

Q. Mr. Straub, are you the appropriate one to ask about the capacity release issue?

A. It depends on your question.

Q. Well, again, it's sort of the same question, that theoretically one would think the incentive would be that the more you get to save and the more you would have an incentive to save as opposed to if you got the boost right here that you had less and less incentive. Can you tell me why that theory, why that thinking of mine is wrong?

A. I don't think your thinking is wrong, and I think under general conditions generally you are correct, that an incentive mechanism that would allow the LDC to retain more of the savings the more that they were to release would give them the incentive to bring it closer to the edge or to operate their system more efficiently. So I think under general conditions your assessment is correct.

The reason Staff agreed to the current one are for the reasons that the company filed them, and that is that MGE's current plan was developed in the 318 case and it was approved by the Commission, and we didn't feel that now at this time would probably be a good time to try to change it, and the company appears to be satisfied with the plan as well.

Q. But if we were to put this in place for one year and you were to look at further incentive plans for the future, would you possibly consider reversing that or would you keep it the same way?

A. I think we would evaluate both of them, and I don't know if I could indicate which way Staff would end up going at this time. As Mr. Langston indicated, it is somewhat company specific. So he indicated the reasons why they're more comfortable with the current plan on their type of system versus Laclede's system as an example.

Q. And I know you alluded to some reason, but I'm not sure that I fully understand the significance of that difference, and perhaps if you were to be doing it in the future, making the significance of that difference apparent would be important.

A. Yes. I agree with you. I think it would be, and anything that we would come to agreement on I think we would provide an in-depth explanation of why the parties believe that particular type of mechanism is best.

CHAIR LUMPE: Thank you. I have no further questions.

JUDGE MILLS: Commissioner Murray?

COMMISSIONER MURRAY: I don't have any. Thank you.

JUDGE MILLS: Commissioner Schemenauer?

QUESTIONS BY COMMISSIONER SCHEMENAUER:

Q. I had one and then I lost it. I was going through the -- I was going through the capacity release sharing mechanism to see, based on the average, the consumers got 353,000 over that three-year period, and how much -- if the difference would be, if we reversed the sharing, and I guess if you made -- if you generated enough money in savings it would come out the same, but it didn't -- they didn't generate that much money in savings?

A. You are correct that there is a point to where both types of incentive mechanisms, whether there is declining or inclining, there is a point that you would reach to where they would both be about the same amount of money. I don't know if that -- if that would be proprietary or --

Q. I don't want to get into that. I was trying to get that in my mind, the difference.

A. And there is a point to where when you start releasing capacity, there is a point to where you get to where both plans would yield about the same for both sides, yes.

Q. And then the other question I had, based on the Y2K problem, do you anticipate any problem after the first of the year with domestic natural gas getting to the LDCs?

A. I can't think of any reason, but I certainly don't know how much the transportation system is computer driven. So I'm really not a good candidate to ask that question, but I haven't heard of any problems that have been discussed in the industry.

Q. Do you know if we -- if the country relies on any foreign imports of natural gas, outside of Canadian gas?

A. I don't know.

Q. Okay. It would just be the off-shore working routes probably, but it may create some apprehension toward the end of this year if there are some concerns that would drive the price up.

COMMISSIONER SCHEMENAUER: That's all I have. Thank you.

JUDGE MILLS: Are there questions for Public Counsel or for any other witnesses?

CHAIR LUMPE: Just one for Public Counsel, Mr. Micheel. Is your comfort level there because it's only one year?

MR. MICHEEL: Yes. And I think, Chair Lumpe, that you're absolutely correct in pointing out that the increasing block is a little more fair to ratepayers, I think.

And I can tell you that we did indeed litigate this particular incentive for MGE in GO-94-318 Phase 2, and I think it's safe to say that when we entered into the Stipulation and Agreement in the Laclede case which resulted in their gas supply incentive plan, that we specifically flipped the blocking around for that reason. And I think that the Staff and the Public Counsel believe that that was a little more effective way to do it and put the incentive the right way.

I think a couple reasons why I didn't say anything about this particular one; one, it was for a year. Two, the Commission, the way that the company had filed this, they bundled it up with their hedging request. I think generally we support the idea of hedging, and we didn't want to unnecessarily delay that by filing a motion to suspend these particular tariffs.

And, of course, you know what our position was in GT-99-303 about where capacity release revenues should be. That really hasn't changed.

CHAIR LUMPE: That's sort of why I needed to ask the question because I wanted to know where your comfort was coming from.

Mr. Langston was busy doing calculations over here. Was there something from that you wanted to share or would it be proprietary or --

MR. LANGSTON: We were just calculating the difference if we reversed the percentages from 50 percent to 10 percent declining to 10 percent to 50 percent with the same block rates. On average during the three years of our incentive, we had on average average capacity credits on our increases of just over $1.5 million. Of that the company participated in 354,000 of that.

If you reverse the percentages, if you had the same average capacity credit amount of a little over 1.5 million, our percentage -- our amount would move to 570,000. So that's -- that's the difference I was calculating.

CHAIR LUMPE: Okay. I thought you had something. Thank you.

JUDGE MILLS: Is there anything further? Is there anything further the parties wish to offer while we're on the record?

(No response.)

Hearing nothing, we're adjourned. Off the record.

WHEREUPON, the hearing of this case was concluded.