

The Midwest Gasser

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Midwest's GR-96-285 Stay Order Is Upheld by Court of Appeals, Supreme Court

At the earliest moment possible under the moratorium agreement under which it purchased KPL's Missouri gas distribution system, Missouri Gas Energy ("MGE") applied for a \$27 million increase for its service territory. Although MGE's own study showed that transportation customers were being overcharged under the current rates, MGE's filing proposed only a moderate reduction for transportation customers, and advocated several transportation-adverse proposals. Based on these adverse proposals and anticipating that the Missouri PSC Staff and Office of Public Counsel would propose to transfer even more costs from the residential customers to transporters, Midwest intervened with the support of several committed companies and submitted a cost of service study showing that transportation customers were still significantly overcharged, and by greater amounts than shown even by the MGE study. As expected, in their testimonies, the PSC Staff proposed shifting over \$8 million to transporters and Public Counsel proposed to shift \$5.9 million to transporters.

The Commission held an extensive hearing on revenue and service quality issues. The parties negotiated a compromise of the class cost of service and rate design issues and presented it to the Commission. The Commission rejected the compromise, then failed to hold a hearing on the issues covered by the rejected settlement. Instead, the Commission imposed what it characterized as an "equal percentage" increase to all classes including transport customers.

Midwest successfully appealed this denial of due process. In addition to finding for Midwest and reversing the Commission, at Midwest's request the circuit court in Jefferson City issued a stay requiring MGE to pay into court the funds it collected from transport customers in excess of the prior rates.

MGE's requests for immediate review of the stay order were completely rejected, first by the Missouri Court of Appeals, then

by the Missouri Supreme Court. MGE then took a direct appeal of the stay order. The case was briefed and argued last October.

On May 11, 1999 the Court of Appeals affirmed Midwest's stay in all respects. MGE sought reconsideration or transfer of this decision, but this request was denied by the Court of Appeals. Following that denial, MGE then petitioned the Missouri Supreme Court to review the Court of Appeals' decision. On August 24, 1999, the Supreme Court denied further review thus finally upholding the stay and impoundment order.

Pursuant to this stay, the amount of 1.87 cents per dekatherm of natural gas transported continues to be held in escrow with the circuit court. This fund now amounts to roughly \$830,000 and

For this reason it will be important for Midwest counsel to have your company's current address and contact person. A form for updating that information is enclosed.

continues to grow each month. Although we expect that MGE will continue to resist, when the matter is finally concluded, we believe that the bulk of this money will be returned to the transport customers who

paid it to MGE.

Midwest Wins Reversal of MGE's GR-98-140 Rate Case

In a June 18, 1999 decision, the Circuit Court of Cole County, Missouri reversed the Commission's Report and Order in GR-98-140 insofar as it imposed a further increase on transportation customers based on the rates that were held unlawful by the same court in GR-96-285 (see article above). Midwest had filed its appeal contending that the Commission's decision had simply perpetuated the error it made in GR-96-285 by applying a percentage increase to those earlier unlawful rates.

MGE and the Commission earlier sought to block Midwest's appeal, claiming that the PSC's decision wasn't final because partial rehearing had been granted to MGE on issues that would have increased rates by an additional \$2.2 million annually. However, the Circuit Court rebuffed these claims. When it determined to continue to process Midwest's appeal, MGE and the PSC sought a writ of prohibition with the Court of Appeals.

When that failed, they tried again at the Supreme Court without success.

In another part of the decision, the court rejected MGE's appeal that the Commission had not authorized enough revenue. MGE appealed this part of the Circuit Court's order. That appeal is now pending at the Court of Appeals.

“Steal Your Gas” Provision Removed from MGE Tariff

One of the holdovers from early days of transportation with KPL was the “steal your gas” provision. That's our term for it. The "politically correct" name for the provision was the “deferred delivery option.” The provision allowed KPL (and its successor MGE) to confiscate the transporter's natural gas supplies if “human needs” customers' supplies ran short. The utility was to compensate the transporters by paying them the difference between the diverted gas and the alternate fuel the transporter had to use.

No one then or now wishes hospital operating rooms or schools to freeze. In the narrow circumstances of FERC Order 436 and the Williams Natural Gas settlements then in place, Midwest reluctantly agreed to the provision as a result of the Missouri Commission's failure to require its own Staff to live up to the Stipulation and Agreement in GO-85-264. Agreement to the provision had become necessary to bring Order 436 open access transportation to Missouri. Midwest counsel also felt that the provision was unlikely to be used.

When FERC Order 636 was issued, the provision became obsolete and Midwest targeted it for removal. Order 636 terminated the interstate pipelines' gas sales functions, required local distributors to become entirely responsible to provide reliable gas supplies for their retail customers, and equalized access to the interstate pipeline. With those changes, any rationale behind such a provision fell away.

Despite this, the provision remained in KPL's tariff and was carried over to MGE's. Midwest sought to have it removed in GR-96-285 (see above). MGE opposed removal, characterizing

it as a "last resort" supply for its customers. The Commission, however, failed to decide the issue. On Midwest's appeal, the court reversed the Commission on this issue and told the Commission that parties were entitled to have disputed issues decided.

The issue arose again in GR-98-140. MGE again clung to its old arguments. Although the Commission made other errors which are the subject of separate appeals from that case, on this point it agreed with Midwest and ordered MGE to remove the provision from its tariff, thus bringing this anomaly to an end.

Midwest was present at the "birth and "death" of this provision in KPL's/MGE's tariffs. Unfortunately, the provision was copied from the KPL tariffs into the transportation tariffs of several other gas distributors in Missouri, including Union Electric. Midwest was successful in negotiating its elimination from the UE tariffs roughly two years ago in a case involving that utility.

A similar provision was implemented in the KPL Kansas tariffs, and still exists in the tariffs for Kansas Gas Service, KPL's Kansas successor. The provision makes no greater sense in that jurisdiction than it did in Missouri and it should be removed there also. The provision was never used.

Is "Bypass" Still Available? When Should It Be Used

By pass is the word that the local gas distributor doesn't want you to know exists. As many of you know, "bypass," or "alternative sourcing" simply refers to the process of obtaining a direct connection to a nearby interstate pipeline and thereby eliminating the cost that the LDC adds to the gas stream.

There are three important reasons to consider a bypass. First, the elimination of the LDC margin and extraneous charges from your transportation costs can be beneficial. In MGE's service territory in Missouri, that margin amounts to as much as 40 cents per Dth. In addition, the Missouri Commission has incorrectly allowed MGE to pass on to transporters part of the Gas Supply Restructuring charges that it incurs to provide

service to its sales customers. These charges have, at times, added as much as 15 cents per Dth to the LDC transportation rates. Direct connection to the interstate pipeline avoids these costs.

Second, a viable bypass opportunity puts significant economic pressure on the LDC to retain your business through a discount.

Third, the task of balancing gas supplies, takes and deliveries is significantly simplified. Midwest counsel has assisted a number of companies in bypassing their local distribution company and is not aware that any of these customers are unhappy with the results they obtained.

There are some other questions that are common:

Q. I like the marketer/broker I'm currently working with. Would I have to give them up?

A. No. In fact, several aspects of that relationship might be improved as a result of the direct connection. In any event you would likely gain access to an additional set of service providers from which you could select future service.

Q. How much does a bypass cost? What would my hurdle cost or payback period be?

A. The cost varies, based on the distance that you would have to cover to install the pipe, costs of easements and the like. The critical question is how near your property is to an interstate pipeline. The cost of the tap itself will vary from pipeline to pipeline, but runs around \$10,000-20,000. Depending on the arrangement you negotiate with the pipeline, legal costs may vary but would probably run around \$10,000, more if the LDC puts up a fight. Given those numbers, and assuming (1) that the installation of the direct connection would cost around \$50,000, (2) that your usage is about 250,000 Dth annually, and (3) the LDC charges avoided are about 40 cents per Dth, payback would be in the range of 1 year.

Q. What would I give up to do this?

A. Based on the experience of a number of companies, nothing. However, if you perceive that LDC services provide value to your company in terms of reliability, supplier of last resort, backup services, etc., you would probably give up those services. On the other hand, corresponding services are often available at the same or lower cost either from the pipelines themselves or from marketers or brokers. As a direct customer of the pipeline, additional flexibility to your service options can be provided on a negotiated basis.

Q. What are some examples of these services?

A. They include: Direct access to storage services that can permit you to "hedge" with lower cost supplies or use other risk management devices; longer duration, more customized arrangements with suppliers; arrangements with suppliers for standby services only on an "as needed" basis; and direct access to capacity release transactions which can lower even the pipeline's firm transportation charges.

Q. Are there any other costs that I can avoid or reduce by doing this?

A. In some cases, certain sales taxes and gross receipts taxes may be mitigated or avoided entirely, but this will depend on the jurisdiction and on how such taxes are imposed as well as the "nexus" of the tax or where the sale occurs. It is something that bears looking into in an overall consideration of a bypass, but may not be a determining factor.

At the FERC, bypass remains viable. Scarcely a month goes by without FERC approving a bypass transaction. We don't know if this situation will remain FERC's approach permanently, so this is something that you should consider if the savings will justify it. We will be glad to help you take an initial look at it if you wish.

**Midwest Active in
Settlement of Williams
\$180 Million GSR Cost
Docket at FERC;
Williams Agrees to
Absorb 40%**

Gas Supply Restructuring Costs, or “GSR” costs, have been a problem for the industry since Order 636 ordered interstate pipelines out of their “merchant” or gas purchasing and reselling functions. GSR costs are incurred by the pipeline to buy out, buy down or reform its gas purchase contracts.

On larger pipelines, these costs have been as much as \$2 billion. While Williams’ costs don't appear to be that high, but they are still significant to Williams' customers. On Williams’ system, virtually all the former LC and LI customers had switched to transportation by 1988 and the supplies that Williams kept were to provide service to the system supply customers. Thus, GSR costs that followed 1988 should not be charged to the former LC and LI customers.

Regardless, state commissions, and particularly the Missouri Commission, have sought to spread these costs to transportation customers through the PGA. Midwest unsuccessfully opposed that action at the Commission and the courts. However, as long as that illogical approach prevails, it is in those customers’ interest (as well as in the interest of all customers) to keep these costs as low as possible.

Williams recently filed to recover GSR costs on the last three of its most troublesome contracts. Litigation at FERC ensued and the matter was ultimately settled with Williams agreeing to absorb almost 40% of the total GSR costs. Midwest participated in this settlement, and submitted limited objections to FERC regarding the settlement. Although we did not oppose the absorption by Williams, we did oppose the method used to recover the balance. Williams “double-dipped” its recovery in such a way that transportation customers who have to move their gas across both Williams’ zones pay a greater share than the LDCs who can rely on storage. Unfortunately Williams' methodology was not detailed until after the settlement discussions had concluded, so Midwest had no choice but to submit a limited opposition to an otherwise generally favorable settlement.

FERC was eager to approve a settlement of complex and long-standing litigation and rejected Midwest's concerns. Although this error offsets some of the benefit of the settlement for certain transporters, the overall package is still preferable to having Williams recover substantially all these charges.

Kansas Gas Service Company Changes Its Transportation Tariff

The Kansas Gas Service Company submitted changes to its gas transportation tariff that will affect all current transportation customers and expand transportation eligibility. Following the filing, Midwest intervened and a settlement was reached. Pending final approval, the changes will have three significant effects.

Eligibility. Under the agreement, KGS will transport gas for any customer with a monthly demand of 1,500 Mcf, or an annual usage of 3,000 Mcf. Previous thresholds were 3,000 Mcf and 6,000 Mcf respectively. KGS estimates that 650 meters will become eligible for transportation service. If you currently are not a transporter or have a facility that was too small to receive transportation service, this change may be helpful.

Metering and Imbalance Penalties. KGS will now require electronic metering on all meters using in excess of 6,000 Mcf per year. Claimed justification is the need for more accurate and timely information to avoid system-wide problems during peaks. Customers are to pay between \$1,600 to \$3,400 per meter for the new equipment, a significant amount for smaller transportation customers. The expense is about one-half the comparable metering expense paid by Missouri customers some years ago. The payment can be financed over four years.

Transportation customers using less than 6,000 mcf per year, will face an optional mathematical formula to determine balancing penalties. This change largely benefits gas marketers by permitting load aggregation. Most marketers believe they will have greater ability to avoid penalties. This will make the contract between marketer and customer much more important as an allocator of risk.

Imbalance penalties are increased and the tolerance levels are decreased. KGS's penalties now mirror Williams' penalties.

School District Participation. KGS and Commission Staff committed to allow school districts to transport gas for all their facilities even though some of their facilities would otherwise be too small. While heralding allowing multiple-meter customers to aggregate load, KGS opposed further change as impractical. Midwest's historic position is that there is no reason for regulators to erect artificial barriers to transportation access. The work required to bring a transportation arrangement on line and operate it conscientiously often makes the option uneconomic for very small customers.

The changes were approved in March, 1999. For more information or discussion of whether these tariff changes could affect your facilities, contact Midwest.

Kansas Ad Valorem Refunds Anyone??

Proceedings are under way that will create two separate opportunities for customers to obtain substantial refunds for past natural gas service. The first opportunity involves refunds of Kansas ad valorem taxes on natural gas produced in Kansas that were unlawfully passed through to end users by gas producers. The second opportunity (discussed in the following article) arises from the second phase of a settlement known as the Wyoming Tight Sands Settlement relating to gas purchased at unlawful rates in Wyoming.

Kansas Ad Valorem Tax Refunds. During 1983 through 1988, producers of natural gas in Kansas included in the price charged for their gas certain ad valorem taxes. The United States Supreme Court held that these taxes were improperly collected by the producers, and now the producers are being required to refund the taxes to the customers who bought gas during those years.

Refunds are being returned to all local distribution companies in Kansas and Missouri. In Kansas, the amounts involved to date are:

Kansas Gas Service Company	\$12 million
United Cities Gas Company	\$1.5 million

Earlier this year, the KCC asked for refund plans from the LDCs. Midwest intervened in those cases. KGS appears willing to refund to large customers, but unwilling to establish procedures to prove that it has done so. "Trust us," argues KGS. Midwest has been there before. KGS also contends that although it has these refunds in its hands, it is unwilling to give the money to its customers because KGS fears that at some later date it will be required to return some of the refunds to the producers. KGS has, however, refused to substantiate these claims or demonstrate how they apply to the funds KGS has already received. Midwest believes these fears are unfounded, since the amounts refunded to date are not subject to further litigation. Nevertheless, it is important that large customers maintain a presence before the KCC to assure that refunds are promptly and properly made to those customers who paid the bills.

United Cities originally proposed to **exclude** all transportation customers from their just refunds and Midwest opposed this proposal. As a result of Midwest's protest, United Cities modified its proposal to include transportation customers. Your participation may still, however, be necessary if you are to receive your share of the refunds.

**Missouri Customers
Fare Better; Receive
Significant Ad
Valorem Refunds
Through Midwest
Efforts**

Missouri customers have already received Ad Valorem refunds of about \$15 million of which transportation customers received over \$4 million, thanks to a collaborative effort by MGE, Midwest, Public Counsel and the PSC Staff. Although there may be further ad valorem refunds in the future, the agreement reached and approved by the PSC should cover those future refunds.

Refunds to current sales customers of about \$11 million have already been flowed back through the PGA. The refund to former LC and LI transportation customers was based on Midwest's Tight Sands litigation data including the percentages to be refunded to specific customers. Midwest's Board has authorized an assessment of the membership to help support its continuing work in Missouri.

The collaborative effort between Midwest and MGE included mutual sharing of data pursuant to a protective order and Midwest's help in locating specific Missouri recipients whose corporate identities had changed over the 18 year period since the Tight Sands data was assembled by KPL and Midwest during the Wyoming Tight Sands antitrust litigation.

Related Editorial Comment. Sadly, neither KGS nor the KCC appear to “get it” and Kansas customers of all classes remain “on hold” while KGS sits on the funds it has already received.

Midwest has worked for the interests of larger customers for nearly five decades and has seen the pendulum swing between its extremes multiple times. From that perspective, Midwest appreciates the political problems that regulators face. However, by refusing to: follow its own rules; honor its own protective orders; and require KGS to make proper proof of its contentions and data, KCC and its Staff position themselves as no more than handmaidens for the utility while Kansas ratepayers of all classes are denied refund of these overcharges. Moreover, in the past handful of years, KCC Staff has taken the inconsistent position of being a litigant before its own Commission, while simultaneously arguing that its role is to “balance the interests” of the other litigants before the same Commission. The KCC is the quasi-judicial agency that hears the evidence and makes decisions based on the record that the litigants assemble before it. Staff's role in a contested case is simply that of one of the litigants.

Ad Valorem refunds are not the only example where Missouri appears to be more concerned about its ratepayers than are Kansas regulators. In the still-pending merger between Western Resources and KCPL, KCC Staff signed onto a merger settlement that would have saddled Kansas ratepayers with paying more than a **\$1 billion** “acquisition premium” over the next four decades. **Across the state line, Missouri regulators refused to go along with such a deal.** Although the matter is not finally decided, ultimately the KCC was confronted with the Missouri settlement (by several parties including the **Midwest Utility Users' Association**) and appeared to have been embarrassed by its Staff's agreement compared to the far less costly deal that Missouri regulators had negotiated and approved.

At this point, KCC Staff's capitulatory settlement appears to have been rejected.

**Wyoming Tight Sands
Refunds Flow to
Missouri Customers;
Kansas Customers
Face Battle**

In an almost parallel situation, Missouri customers of all classes received roughly \$3 million of annual Tight Sands Settlement Proceeds during the late summer of 1999. Roughly 28% of this was distributed to former LC and LI customers based on Midwest's individual customer Tight Sands data and the analysis developed by Midwest's consultant George Donkin during the Wyoming Tight Sands antitrust litigation. During 1981 to 1987, gas supplied to its service area by Williams or its predecessors was purchased by Williams from Wyoming under contracts that were challenged initially by Midwest at FERC. Later, others joined this effort in a federal court lawsuit that culminated in a settlement in both jurisdictions in 1992. That settlement included below-spot market gas purchase contracts for the LDC and refunds over a twenty-year term for their customers.

Through separate settlements initiated and supported by Midwest in both states, the first ten years of these annual settlement payments were commuted to their present value through a financing mechanism. Their present value was then distributed to all Missouri ratepayers shortly following the settlement of the Tight Sands litigation. That financing mechanism has been paid off and the first of the remaining annual payments has been received both by MGE and KGS.

In Missouri, working cooperatively and sharing a common data base, MGE and Midwest saw to the prompt distribution of these refunds to the appropriate parties and confirmed the earlier settlement that established a mechanism for the remainder of the annual refunds.

In Kansas, however, the story is different. Despite having the same contracts as MGE in Missouri, KGS wanted to divert a significant portion of the former LC and LI customers' shares of the annual refund payments to current sales customers. KGS refused to recognize that this arrangement had been confirmed, settled and approved nearly eight years before.

This time, at least KCC Staff took the right view, noted that the original 1992 settlement was unambiguous in addressing the handling of the post-financing refunds, and recommended to the KCC that KGS's proposal be rejected. KGS argues that the below-spot purchase contracts have become too expensive because additional sales customers have switched to transportation. However, this overlooks the windfall that KGS obtained through the commutation and financing vehicle and discounted gas prices during that period. More importantly, the KCC itself was a signatory party to the gas purchase contracts which are only a part of the Tight Sands settlement package that was approved by the federal court and on the basis of which the federal court and FERC actions were settled. The KCC continues to consider this matter, while interest accumulates on the amount of these refunds in KGS's hands.

The **Midwest Gas Users' Association** is an unincorporated voluntary association founded over forty years ago to advocate the interests of large commercial and industrial interruptible users of natural gas in the Midwest through intervention in federal and state utility rate cases and related regulatory matters affecting the interest of these customers. Midwest assumed a seminal role of leadership in the initiation of natural gas transportation on the Williams system, Panhandle Eastern Pipe Line and Kansas Pipeline.

Midwest is active in state and federal jurisdictions consistently advocating these interests and the principles of cost-based rate regulation. Historically supported by assessments on refunds received by members, Midwest supplements its historic funding with member commitments for specific cases.

For information regarding participation in Midwest, contact any of the following:

Stu Conrad	(816) 753-1122
J. D. Finnegan	(816) 753-1122
Ed Peterson	(816) 753-1122
Dennis Kies	(913) 341-5651

or write the Association's office at: 3100 Broadway, Suite 1209, Kansas City, Missouri 64111. This newsletter is the official publication of the Association and is distributed to its members, to participants in Association interventions, and to those anticipated to be interested in matters of concern to large commercial and industrial natural gas users and transporters. The opinions expressed herein are those of Midwest, but do not necessarily represent the views of any particular Association member or case

participant. Permission to quote is given, provided that the quotation is sufficient in length to reflect the context of the quotation and acknowledgment is given to Midwest.

40037

RESPONSE FORM:

Please correct our company's address on your records to the following (you can also attach a business card to this sheet):

Company Name: _____
Attention: _____
Address: _____

City: _____
State: _____
Email: _____
Fax: _____

Please return to:

Midwest Gas Users' Association
3100 Broadway, Suite 1209
Kansas City, Missouri 64111
Fax: (816) 756-0373

Email: mgua@fcplaw.com