

REPORT OF
MUNICIPAL GAS COMMISSION
OF MISSOURI
DECEMBER 31, 2007 AND 2006



CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

2005 West Broadway, Suite 100, Columbia, MO 65203
OFFICE (573) 442-6171 FAX (573) 777-7800

3220 West Edgewood, Suite E, Jefferson City, MO 65109
OFFICE (573) 635-6196 FAX (573) 644-7240

www.williamskeepers.com

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Municipal Gas Commission of Missouri

We have audited the accompanying balance sheets of the Municipal Gas Commission of Missouri ("MGCM"), as of December 31, 2007 and 2006, and the related statements of revenue, expenses and changes in fund equity; and cash flows for the years then ended. These financial statements are the responsibility of MGCM's management. Our responsibility is to express an opinion on the financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Municipal Gas Commission of Missouri as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The Management's Discussion and Analysis on pages 2 through 6 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Williams-Keepers LLC

July 29, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the annual financial report provides an overview and analysis of the financial activities of the Municipal Gas Commission of Missouri ("MGCM") for the years ended December 31, 2007 and 2006. We encourage you to consider the information presented here in conjunction with additional information presented in the basic financial statements which follow this section.

MGCM's purpose is to provide for financing, acquisition and operation of natural gas production, transmission and distribution facilities and resources and for the joint purchase of natural gas to meet the requirements of its member municipalities. MGCM was established in 1988, under the Missouri Joint Municipal Utility Commission Act.

Overview of the Financial Statements

The basic financial statements are prepared using proprietary or enterprise fund accounting. Proprietary funds account for governmental operations that are designed to be self-supporting from fees charged to consumers for the provision of goods and services or where the government has decided that the periodic determination of revenues, expenses, and net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. The accounting and financial reporting practices of proprietary funds are similar to those used for business enterprises and focus on capital maintenance and the flow of economic resources through the use of accrual accounting.

The basic financial statements, in addition to Management's Discussion and Analysis, are comprised of the Balance Sheet; the Statement of Revenue, Expenses and Changes in Fund Equity; the Statement of Cash Flows; and the Notes to Financial Statements. The financial statements are prepared on the accrual basis in accordance with U.S. generally accepted accounting principles.

The Balance Sheet presents MGCM's financial position as of the end of the year. Information is displayed on assets and liabilities, with the difference between the two reported as fund equity. The fund equity of MGCM reflects the resources available as of the end of the year to support member activities. Over time, increases and decreases in fund equity measure whether MGCM's financial position is improving or deteriorating.

The Statements of Revenue, Expenses and Changes in Fund Equity presents information detailing the revenues and expenses that resulted in the change in fund equity that occurred during the current year. All revenues and expenses are reported on an accrual basis. This means that the revenue or expense is recognized as soon as the underlying event giving rise to the change occurs, regardless of when the actual cash is received or paid. Thus, revenues and expenses are reported in this statement for some items that will not result in cash flows until future periods. For example, gas purchases that occurred during the year will be reflected as an expense, whether or not they have been paid as of the end of the fiscal year.

The Statements of Cash Flows presents the cash inflows and outflows of MGCM categorized by operating, noncapital financing, and investing activities. It reconciles the beginning and end-of-year cash balances contained in the Balance Sheet. The effects of accrual accounting are adjusted out and noncash activities, such as depreciation, are removed to supplement the presentation in the Statement of Revenue, Expenses and Changes in Fund Equity.

The Notes to Financial Statements follow the above basic financial statements and provide additional information that is essential to a full understanding of the data provided in the financial statements.

Financial Analysis

The following tables present summarized financial position and results for the years ended December 31, 2007 and 2006. Additional details are available in the accompanying basic financial statements.

Balance Sheet Analysis for 2007

| | <u>2007</u> | <u>2006</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|-----------------------------------|---------------------|---------------------|--------------------------------|------------------------------|
| ASSETS | | | | |
| Accounts receivable | \$ 3,056,407 | \$ 2,880,957 | \$ 175,450 | 6.1% |
| Other current assets | 1,040,353 | 1,408,281 | (367,928) | -26.1% |
| Total current assets | <u>\$ 4,096,760</u> | <u>\$ 4,289,238</u> | <u>\$ (192,478)</u> | <u>-4.5%</u> |
| LIABILITIES | | | | |
| Accounts payable | \$ 2,706,174 | \$ 3,621,334 | \$ (915,160) | -25.3% |
| Other current liabilities | 530,606 | 36,677 | 493,929 | 1346.7% |
| Total current liabilities | <u>3,236,780</u> | <u>3,658,011</u> | <u>(421,231)</u> | <u>-11.5%</u> |
| Advances from members | <u>98,968</u> | <u>98,968</u> | - | 0.0% |
| Total liabilities | <u>3,335,748</u> | <u>3,756,979</u> | <u>(421,231)</u> | <u>-11.2%</u> |
| UNRESTRICTED FUND EQUITY | <u>761,012</u> | <u>532,259</u> | <u>228,753</u> | <u>43.0%</u> |
| Total liabilities and fund equity | <u>\$ 4,096,760</u> | <u>\$ 4,289,238</u> | <u>\$ (192,478)</u> | <u>-4.5%</u> |

At the end of a fiscal year the level of accounts receivable from member municipalities as well as the level of cash and cash investments is generally largely a function of the timing of member payments, with the general level of gas prices also having some influence. Cash and cash investments at December 31, 2007 decreased by 82% from the amount at December 31, 2006, from \$860,766 to \$151,196. For 2007, more gas in storage was purchased to try to mitigate the rising costs of gas. Although \$200,000 was borrowed on MGCM's line of credit to help finance these purchases, they also drew down cash balances. Primarily because of this, gas in storage, which is included in other current assets in the above table, increased by \$348,442 from December 31, 2006 to December 31, 2007. Although for 2007 there was an intentional increase in the level of gas in storage because of the market, changes in total storage gas volumes can typically also result because of normal operational issues such as weather and unanticipated gas sales volumes. The unit value of gas in storage is influenced by gas market prices and the timing of purchases. The combination of all of these factors can cause significant changes in the total dollar value of gas in storage from year to year.

In addition to the borrowing on the line of credit for \$200,000, other current liabilities include funds held for members totaling \$293,929 as of December 31, 2007. Funds held for members represents collections from three member cities related to a tariff case filed with the Missouri Public Service Commission. MGCM is disputing certain billings for natural gas transportation service for the cities, pursuant to Public Service Commission Rule 13.045. This liability consists of billings to members for the amounts MGCM considered to be overcharges on transportation costs. MGCM incurred legal costs on behalf of MGCM members in a successful effort to have the Missouri Public Service Commission set aside these overcharges. Further information is provided in Note 6 to the financial statements.

The change in fund equity from 2007 is explained after the table summarizing the Statement of Revenue, Expenses, and Change in Fund Equity.

Balance Sheet Analysis for 2006

| | <u>2006</u> | <u>2005</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|-----------------------------------|---------------------|---------------------|--------------------------------|------------------------------|
| ASSETS | | | | |
| Accounts receivable | \$ 2,880,957 | \$ 3,372,866 | \$ (491,909) | -14.6% |
| Other current assets | 1,408,281 | 865,347 | 542,934 | 62.7% |
| Total current assets | <u>\$ 4,289,238</u> | <u>4,238,213</u> | <u>\$ 51,025</u> | <u>1.2%</u> |
| LIABILITIES | | | | |
| Accounts payable | \$ 3,621,334 | \$ 3,650,074 | \$ (28,740) | -0.8% |
| Other current liabilities | 36,677 | 36,677 | - | N/A |
| Total current liabilities | 3,658,011 | 3,686,751 | (28,740) | -0.8% |
| Advances from members | 98,968 | 98,968 | - | 0.0% |
| Total liabilities | 3,756,979 | 3,785,719 | (28,740) | -0.8% |
| UNRESTRICTED FUND EQUITY | 532,259 | 452,494 | 79,765 | 17.6% |
| Total liabilities and fund equity | <u>\$ 4,289,238</u> | <u>\$ 4,238,213</u> | <u>\$ 51,025</u> | <u>1.2%</u> |

At the end of a fiscal year the level of accounts receivable from member municipalities as well as the level of cash and cash investments is largely a function of the timing of member payments, with the general level of gas prices also having some influence. Cash and cash investments at December 31, 2006 increased by 12% from the amount at December 31, 2005, from \$769,116 to \$860,766. Gas in storage represented 13% and 2%, respectively, of total current assets at the end of 2006 and 2005. Changes in total storage gas volumes resulted because of normal operational issues. Because of a decrease in receivables from members at the end of 2006 as compared to the end of 2005, total assets did not change significantly.

The change in fund equity from 2006 is explained after the table summarizing the Statement of Revenue, Expenses, and Change in Fund Equity.

Statement of Revenue, Expenses, and Change in Fund Equity Analysis for 2007

| | <u>2007</u> | <u>2006</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|---|-------------------|-------------------|--------------------------------|------------------------------|
| OPERATING REVENUES | | | | |
| Gas sales | \$ 13,015,965 | \$ 12,783,653 | \$ 232,312 | 1.8% |
| Management fee | 71,429 | 65,616 | 5,813 | 8.9% |
| From members for legal fees | 62,060 | 25,077 | 36,983 | 147.5% |
| Total operating revenues | <u>13,149,454</u> | <u>12,874,346</u> | <u>275,108</u> | <u>2.1%</u> |
| OPERATING EXPENSES | | | | |
| Gas purchases and related costs | 12,789,066 | 12,680,217 | 108,849 | 0.9% |
| Management fee | 84,000 | 82,742 | 1,258 | 1.5% |
| Other expense | 15,013 | 30,543 | (15,530) | -50.8% |
| Total operating expenses | <u>12,888,079</u> | <u>12,793,502</u> | <u>94,577</u> | <u>0.7%</u> |
| NONOPERATING REVENUES (EXPENSES) | | | | |
| Interest income | 28,529 | 25,422 | 3,107 | 12.2% |
| Interest expense | (497) | (18) | 479 | 2661.1% |
| Total nonoperating income | <u>28,032</u> | <u>25,404</u> | <u>2,628</u> | <u>10.3%</u> |
| Increase in fund equity | 289,407 | 106,248 | 183,159 | 172.4% |
| Fund equity, beginning of the year | 558,742 | 452,494 | 106,248 | 23.5% |
| Fund equity, end of the year | <u>\$ 848,149</u> | <u>\$ 558,742</u> | <u>\$ 289,407</u> | <u>51.8%</u> |

Revenues from 2007 total gas sales were approximately 3.5% greater than comparable revenues for 2006. Overall volumes of natural gas consumption for fiscal year 2007 of 1,424,763 MMBtu surpassed 2006 sale volumes by approximately 8.5% as a result of demand and 476 more heating degree days during the 2007 fiscal year. In 2007, Management purchasing strategies utilized more of available gas storage capacities during times of lesser demand and falling natural gas prices in order to subsidize higher winter natural gas prices. As a result of management purchase strategies and timeliness of cheaper natural gas market prices, members realized an all-in delivered commodity price of \$9.07 MMBtu, approximately \$0.66 cheaper than the 2006 all-in delivered price.

Legal fees for 2007 and 2006 are from collections from members to pay legal costs associated with the tariff dispute previously discussed. A corresponding amount of legal expense was incurred.

Natural gas sales during 2007 followed proportionately with operating expenses for natural gas purchases. MGCM delivered 1.383 Bcf of gas requirements to its members in 2007 compared to 2006 gas requirements of 1.274 Bcf. Although members' natural gas consumption increased 8.5% from fiscal year 2006 to 2007, total expenses for natural gas purchases exceed comparable 2006 amounts by less than 1%. MGCM members saw an average cost per MMBtu of \$7.59 for 2007 compared to \$7.97 for 2006 fiscal year.

Management believes short-term supply and demand price volatility for natural gas is likely to continue into 2008, but the average cost of natural gas during the 2008/2009 heating season is projected to be greater than during the 2007/2008 heating season due primarily to supply and demand. Management expects to continue to

utilize natural gas storage hedging practices again in 2008, while exploring other industry hedging strategies.

Statement of Revenue, Expenses, and Change in Fund Equity Analysis for 2006

| | <u>2006</u> | <u>2005</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|---|-------------------|-------------------|--------------------------------|------------------------------|
| OPERATING REVENUES | | | | |
| Gas sales | \$ 12,783,653 | \$ 12,073,878 | \$ 709,775 | 5.9% |
| Management fee | 65,616 | 70,854 | (5,238) | -7.4% |
| From members for legal fees | 25,077 | - | 25,077 | N/A |
| Total operating revenues | <u>12,874,346</u> | <u>12,144,732</u> | <u>729,614</u> | <u>6.0%</u> |
| OPERATING EXPENSES | | | | |
| Gas purchases and related costs | 12,680,217 | 11,974,095 | 706,122 | 5.9% |
| Management fee | 82,742 | 97,400 | (14,658) | -15.0% |
| Miscellaneous expense | 30,543 | 13,734 | 16,809 | 122.4% |
| Total operating expenses | <u>12,793,502</u> | <u>12,085,229</u> | <u>708,273</u> | <u>5.9%</u> |
| NONOPERATING REVENUES (EXPENSES) | | | | |
| Interest income | 25,422 | 11,191 | 14,231 | 127.2% |
| Interest expense | (18) | (77) | (59) | 76.6% |
| Total nonoperating income | <u>25,404</u> | <u>11,114</u> | <u>14,290</u> | <u>128.6%</u> |
| Increase in fund equity | 106,248 | 70,617 | 35,631 | 50.5% |
| Fund equity, beginning of the year | <u>452,494</u> | <u>381,877</u> | <u>70,617</u> | <u>18.5%</u> |
| Fund equity, end of the year | <u>\$ 558,742</u> | <u>\$ 452,494</u> | <u>\$ 106,248</u> | <u>23.5%</u> |

As the table above shows, gas sales increased close to 6% for 2006. Because the margin on gas sales was very comparable to 2005, the increased sales resulted in an increase of only \$3,653 in the margin on sales. Members contributed \$25,077 to costs of litigation in 2006 filed on their behalf pertaining to overcharges on gas transportation costs. The costs of the litigation of a comparable amount which are included in "other expense" in the above table account for 60% of the increase in other expense. The rest of the increase was due to write-off of an old receivable for taxes MGCM paid on gas in storage for which management has determined MGCM is unlikely to receive reimbursement.

Request for Information

This financial report is designed to provide the reader a general overview and analysis of the financial activities of MGCM. Questions or requests for more information should be directed to Duncan Kincheloe, General Manager, Municipal Gas Commission of Missouri, 1808 I-70 Drive SW, Columbia, MO 65203 (573-445-3279).