STATE OF MISSOURI

PUBLIC SERVICE COMMISSION

In the Matter of Laclede Gas)
Company's Tariff to Revise Natural) Case No. GR-99-315
Gas Rate Schedules.)

DEPOSITION OF MARK OLIGSCHLAEGER,

a witness, produced, sworn and examined on the 17th day of September, 2004, between the hours of 8:00 a.m. and 6:00 p.m. of that day at the offices of AmerenUE, 101 Madison Street, in the City of Jefferson, County of Cole, State of Missouri, before

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and Notary Public within and for the State of Missouri, commissioned in Cole County, Missouri, in the above-entitled cause, on the part of AmerenUE, pursuant to agreement.

Exhibit No. 157
Case No(s). GR-99-315
Date 9-24-04 Rptr TS

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ALSO PRESENT: Rosella Schad

SIGNATURE INSTRUCTIONS:

Presentment waived; signature requested.

EXHIBIT INSTRUCTIONS:

None marked.

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MARK OLIGSCHLAEGER, being sworn, testified as follows:

DIRECT EXAMINATION BY MR. LOWERY:

Q. Good morning, Mr. Oligschlaeger. My name is Jim Lowery, and as I think you know, I represent AmerenUE in this case. We're here this morning in the case involving Laclede Gas Company, Case No. GR-99-315, which has been remanded to the Commission from the Missouri Court of Appeals.

Could you please state your name for the record.

A. My name is Mark L. Oligschlaeger.

Q. Have you had your deposition taken before, Mr. Oligschlaeger?

A. Yes, I have.

Q. Just a couple preliminary matters before we start the substantive part of the deposition. If you don't hear a question that I ask, or understand it, would you please let me know?

A. Yes.

Q. And I'll try to rephrase or clarify it. If you want to take a break at some point, just let me know as well and we can do that as well.

Is there any reason that you know of that you might not be able to answer or understand any of the questions I'm going to ask you this morning?

A. No.
Q. You filed supplemental rebuttal testimony in this case on September 10th, correct?
A. Yes.
Q. Are you a depreciation engineer?
A. No, I am not.
Q. Are you a depreciation expert or analyst?
A. I would consider myself an expert generally in regulatory matters. I would just leave it at that.
Q. Not in depreciation in particular, though, in the field of depreciation?
A. I don't believe so.
Q. Is calculating depreciation rates, for example, a part of your job?
A. It has not been.
Q. Is it now a part of your job?
A. No, it is not.
Q. Schedule 2-1 of your testimony lists the cases in which you've testified over your career with the Staff, right?
A. Yes.
Q. And you've been with the Staff, what, a about 22 or '3 years?
A. 23 years.
Q. 23. Did you provide any testimony relating

to depreciation in any of the cases that you've listed in Schedule 2-1? And I'm referring to your Schedule in -- no. 2-1 is correct.

A. Not specifically, no.

Q. Did you in general address depreciation in testimony in some of those cases?

A. In some cases, in terms of policy testimony or looking at things like cash flow or earnings, looking at annual levels of depreciation expense may have entered into it, that kind of thing.

Q. You didn't -- I take it you did not address issues about what the appropriate way to calculate depreciation is, one method versus another, any of that testimony?

A. No.

Q. Or the appropriate way to determine net salvage percentages or net salvage allowances in any of those cases?

A. No.

Q. Whom would you consider to be experts in the field of depreciation?

A. I would consider our staff members that are part of the engineering and management services department that specialize in depreciation recommendations to be experts. I presume that the witnesses offered by the company and Public Counsel and other intervenors on depreciation matters would be considered as experts as well.

Q. You mentioned the staff members. Would that be Jolie Mathis, Greg Macias and Ms. Schad?

A. I'm not sure that's a comprehensive list, but I would agree that each of those three would be experts.

Q. Did I leave out Guy Gilbert, for example?

A. Yes, you did.

Q. Is there anybody else that you think I left out?

A. That's all I can come up with.

Q. Other than those Staff folks that you consider to be experts, and you indicated you would consider or that the experts that have been proffered by the companies on depreciation would be experts, any names come to mind, anybody that you know of that you consider to be experts that you're familiar with?

A. Beyond the universe of individuals who have submitted testimony in the Missouri PSC, no.

Q. Just to get an idea of where you fit into the organization at Staff, who do you report to?

A. I report to Joan Wandel, the manager of the auditing department.

Q. And who does she report to?

A. Bob Schallenberg, the utility services division director.

Q. And he reports to Robert Quinn?

A. The executive secretary, I think is his job title.

Q. And do you have some direct reports yourself?

A. All of the members of the Jefferson City auditing department report to me.

Q. Have you ever worked for a public utility?

A. No, I have not.

Q. Your entire career has been spent as a regulator; is that right?

A. Actually, I spent five months working for the firm of what was called at that time Dittmer, Brosch & Associates, now known as Utilitech, which is a consulting firm specializing in regulatory matters. That would be the period December '85 through April '86. Other than that, my entire professional career has been with the Commission.

Q. So you left the Commission for a little while, went to work for this consulting firm and then came back?

A. That is correct.
Q. **Did you work on any depreciation issues while you were at -- I don't remember the name of the company that you mentioned, but this other employer?**
A. Not that I recall.
Q. **Have you ever worked for any other industrial or commercial corporation or enterprise?**
A. No.
Q. **Have you ever worked in any job where you had responsibility for managing the cash flows of an organization?**
A. No.
Q. **What training in cash flow management do you have?**
A. Just the training that one receives and the experience one receives working as a regulatory auditor with the Commission.
Q. **Is that training just on-the-job training, in terms of these are things you learn as you're doing your job duties, or have you actually taken seminars relating to cash flow management or gone to classes or training relating to cash flow management of some kind?**
A. I don't recall any specific training classes or seminar that dealt with cash flow issues.
Q. **How about a job where you had**

responsibility for managing reinvestments of earnings or cash flow back into a company, have you ever had any of those kinds of responsibilities?

A. No.

Q. What training in managing the reinvestments of earnings or cash flows back into the company do you have? I take it you don't have any particular training in that area?

A. That is correct.

Q. Have you ever worked for a credit ratings agency?

A. No, I have not.

Q. Do the opinions of credit ratings agencies affect the cost of utility borrowings?

A. I don't know that their opinions do. I believe generally the ratings given to the debt offerings of a utility may affect the cost.

Q. So the credit ratings, A, AA, BBB-, whatever rating they may give, that would affect the cost of utility borrowings?

A. That is my understanding.

Q. Do you have any training in rating the creditworthiness of commercial enterprises like public utilities?

A. No, I do not.

Q. Have you ever worked for a large pension fund or insurance company or any other kind of large institutional investor of the type that might invest in debt of public utilities?

A. No.

Q. Is it fair to say that investors, those kinds of investors rely upon the ratings from credit agencies in making their decisions to subscribe to the debt of public utilities?

A. I presume to some degree investors would rely upon such ratings.

Q. Do you know whether they do or you just -- you think it's fair to make that assumption?

A. I think that's a fair assumption.

Q. You indicate in your testimony at page 2, lines 4 to 6, that you had received training at in-house and outside seminars on technical ratemaking matters, and I think you've probably already answered this to a large degree, but I take it that none of that training dealt with depreciation in particular or net salvage/cost of removal in particular?

A. Not that I recall.

Q. This may -- this may generate a long list. I'm not sure. But what training have you had? What kind of -- what training were you referring to in your

testimony?

A. Over the duration of my employment to the Commission, I've occasionally been allowed to attend outside seminars on various topics, as well as attend what I would call general regulatory seminars, such as actually the NARUC Subcommittee on Accounts meeting that I just spent several days with in St. Louis.

Also over the course of my employment the Commission from time to time has offered in-house training on various topics of interest in terms of ratemaking. That's a general thing. If you want me to get more specific --

Q. No. I think that will suffice.

Do you recall if any of that training talked about the issue of the use of cash flows from depreciation, including net salvage, in utility operations?

A. As a specific topic, I don't recall.

Q. Have you read the record in this case?

A. I have read the testimony that was filed both in the original stage of the GR-99-315 proceedings, on this particular issue.

Q. Okay.

A. As well as the testimony filed during this current phase of the remand proceeding. I'll supplement that by also saying that in 1999 I probably reviewed other portions of the case on other issues as well.

Q. You've read all the supplemental testimony filed here in the last month or so?

A. Yes.

Q. And you read Paul Adam's testimony from '99?

A. Yes.

Q. Ron White's testimony? No, he wasn't in this case. Mr. Kottemann's testimony?

A. Actually, Mr. White was.

Q. Mr. White was in the case also. All right.

A. And Mr. Kottemann's, but only as it applied to this specific issue.

Q. All right. Anybody else that you read re-- well, let me strike that.

You read the testimony from '99 recently?

A. Yes.

Q. In connection with preparing your supplemental rebuttal testimony?

A. Yes.

Q. Anybody else's testimony from '99 that I didn't mention or you didn't mention that you read relating to these depreciation issues that we have before us now?

A. No. That would have been Mr. Adam, Mr. Kottemann, Mr. White.

Q. When you say you read their testimony, you read their direct and their rebuttal and their surrebuttal if they filed those?

A. Yes.

Q. Have you read the hearing transcript?

A. No, I have not.

Q. None of it? Not even the part -- for example, did you read the hearing transcript when Mr. Adam testified or --

A. No, I have not.

Q. Or Mr. Kottemann or Mr. White?

A. No.

Q. Have you read any Data Request responses from Staff relating, for example, from Mr. Adam that he would have submitted responses to Data Requests back in '99 when this case was tried?

A. No.

Q. I take it you haven't read any Data Request responses from any of the other parties, then, in this case?

A. Unless they've been attached as schedules to their supplemental rebuttal testimony, but I don't recall whether they were or not.

Q. Only if they were part of the testimony that you reviewed --

A. Right.

Q. -- would you have done that?

Have you studied Laclede's depreciation and net salvage data -- related data in this case?

A. I've done -- in that respect, I've read the testimony I described earlier. I've not done any further analysis.

Q. You haven't studied, for example, in particular Laclede's estimates of net salvage that they proposed in the case?

A. No.

Q. Or how they were calculated, other than -- let me try to clarify that. Other than the methodology by which they may have calculated them, you haven't studied the estimates themselves?

A. No.

Q. Do you agree with Mr. Adam's prefiled testimony? And I'm talking about his direct, his rebuttal and surrebuttal.

A. I agree with his recommendations and conclusions.

Q. Does that mean there's things that he said that you don't necessarily agree with?

A. I don't recall any. If I was asked to write testimony, I might state things differently than Mr. Adam, but not necessarily disagree with him.

Q. You said that you agree with his recommendations and conclusions. What are those recommendations and conclusions that you agree with?

A. Specifically that it would be appropriate to treat Laclede's net salvage costs for ratemaking purposes based upon the recent outlays Laclede had made for that item.

Q. Anything else?

A. Not that I recall.

Q. You've read -- you said that you've read all the testimony that's been filed here in the last month or so. Do you agree with Mrs. Schad's testimony that's been filed in this case?

A. Yes, I do.

Q. Anything that you don't agree with?

A. No.

Q. I'd like to try to get some terminology straight. I don't think there's any confusion, but just for the record, I'm going to use some terms and I want to make sure you and I are on the same page when I'm using those.

When I say Staff's method or Staff's

approach or Staff's treatment of net salvage, I'm going to be talking about the method originally proposed by Mr. Adam that Mrs. Schad has adopted.

A. Okay.

Q. Is that fair?

A. That would be fair.

Q. And when I'm talking about the company's method or approach or the standard method or approach, I'm going to talk about -- I'll be talking about the method of dealing with net salvage that's been advocated by Laclede and AmerenUE in this case.

A. Okay. I understand that.

Q. Staff has proposed in a number of proceedings subsequent to this case, the GR-99-315 case, a different way of handling net salvage, in fact, to remove net salvage completely from the depreciation calculation. Are you familiar with that?

A. Yes, I am.

Q. Which approach do you believe is correct, the one advocated by Mr. Adam and adopted by Mrs. Schad in this case or the one that Staff has on numerous occasions suggested in subsequent cases?

A. I believe that substantively those approaches are identical. I do not have a problem with and would advocate treating the net salvage costs on a period expense basis.

Q. When you say on a period expense basis, is that Staff's subsequent method? Is that what you mean when you --

A. Yes.

Q. So if you don't think they're substantively different, then I -- is it fair to say that you wouldn't oppose use of Mr. Adam's method in future cases?

A. I think it leads to the same results. I'm an auditor, so perhaps I think it's more easily understood perhaps under the -- what you would call the subsequent Staff method.

Q. Is that why you think they're the same, one may be preferable to the other, that they're more easily -- that the subsequent method is more easily understood?

A. Again, I don't think there's a difference in the dollar values that are generated. In my mind, and this is a personal opinion, it's easier to understand when it's termed as a period expense.

Q. Mr. Adam's method includes net salvage as part of the depreciation calculation, correct?

A. That's my understanding.

Q. And the effect of that is that the accruals for net salvage that are part of the depreciation rate go

into the depreciation reserve, correct?

A. Yes.

Q. And that doesn't happen with Staff's subsequently recommended method, correct?

A. That is correct.

Q. Is that a good thing or a bad thing from your perspective?

A. I'm not sure it's either good or bad. If it is treated as an expense, there should be no impact on rate base or the depreciation reserve.

Q. Can you define depreciation for me?

A. I believe I state on page 4 of my supplemental rebuttal testimony that depreciation expense is a return to shareholders of capital previously invested by the utility in plant and assets.

Q. Where did you get that definition that you use in your testimony?

A. That is my definition. I believe it's consistent with other definitions I have seen used by the Staff.

Q. Are you familiar with the definition of depreciation in the Uniform System of Accounts?

A. I've read it, yes.

Q. Do you know what the concept of service value is?

A. I have read that definition as well in the Uniform System of Accounts and am familiar with it.

Q. Mr. Stout's testified in this case that Staff's method is inconsistent with the Uniform System of Accounts. Do you agree or disagree with him?

A. I am not sure that the Uniform System of Accounts dictates specifically how the net salvage component of the depreciation rate is to be calculated.

Q. I'm going to hand you the definition section from the Uniform Systems of Accounts adopted by FERC for gas utilities, and I'll direct your attention to -- it's on page 547, and it's 12B, the definition of depreciation. Could you just read the definition of depreciation up to the first period for the record.

A. Depreciation as applied to depreciable gas plant means the loss in service value not restored by current maintenance incurred in connection with the consumption or prospective retirement of gas plant in the course of service from causes which are known to be in current operation and against which the utility is not protected by insurance.

Q. Thank you. The concept of service value is included in that definition, correct?

A. I believe so.

Q. And can you define service value for me?

A. As I generally recall, the service value is the original cost -- as defined in the Uniform System of Accounts, is the original cost of the plant item in question less any net salvage.

Q. And do you know how net salvage is defined?

A. I believe net salvage is defined as the cost of removal associated with an asset netted against any salvage proceeds associated with the retirement, removal of the asset.

Q. So at least in the Uniform System of Accounts, the definition of depreciation, which includes the concept of service value, also includes service value, includes the concept of net salvage, which includes the concept of cost of removal, correct?

A. I believe that's accurate.

Q. And doesn't your definition that you gave on page 4 at lines 10 and 11 focus only on the original investment in the capital assets?

A. I would agree with that.

Q. So your definition is not consistent with the Uniform System of Accounts, is it?

A. To the extent the Uniform System of Accounts provides for what I would call an accrual or estimated level of cost to removal or net salvage to be included in the depreciation rate, then that would not be consistent.

Q. And it does provide for that, does it not?

A. Again, I am not personally convinced that the USOA provides for that kind of accrual approach to net salvage.

Q. But the definitions used in the Uniform System of Accounts as they pertain to depreciation clearly contemplate that service value is a part of depreciation and that net salvage is a part of service value, correct?

A. That net salvage be taken into account.

Q. Would it be fair to say that the company's method of treating net salvage is accounting for it on an accrual basis, whereas Staff's method is accounting for it on a cash basis?

A. In broad terms, I would agree with that.

Q. Do you know whether the Uniform System of Accounts recommends accrual or cash-based accounting?

A. Like all -- well, I shouldn't say all. Like most systems of accounting, it is based upon accrual accounting, but there may be exceptions for ratemaking purposes, though.

Q. General Instruction 11 of the Uniform System of Accounts mandates accrual accounting, doesn't it?

A. Yes.

Q. When was the last time that AmerenUE itself made a major acquisition?

A. I believe -- I believe they're in the process of making an acquisition of Illinois Power & Light.

Q. AmerenUE is making that acquisition?

A. Oh, I'm sorry. I'm sorry. Since the formation of AmerenUE, and I guess when I say formation, since the corporate structure was set up in the late '90s, I don't believe AmerenUE itself -- I'm not aware that AmerenUE itself has made those kind of acquisitions.

Q. You're not aware during the last, oh, roughly eight years or so AmerenUE itself making any major acquisitions?

A. I'm not aware of that.

Q. AmerenUE itself doesn't have any significant unregulated operations either, does it? Maybe none, but nothing of any real significance; is that fair to say?

A. That's my understanding.

Q. So on page 3, lines 4 to 16 -- 14 to 16, excuse me, when you indicate that cash flow can also be used by utilities for other activities, such as to finance mergers and acquisition transaction and for investment in nonregulated ventures, you're not saying that AmerenUE is

using cash flow for depreciation to finance AmerenUE acquisitions or to engage in unregulated operations, are you?

A. No. My suggestion there is in a parent company kind of structure, usually the cash flow is turned over to the parent company to make decisions on how to use the cash.

Q. Well, do you know what happens to the dividends that AmerenUE dividends to Ameren Corporation? I assume that's what you're referring to.

A. Yes.

Q. Do you know what happens to those?

A. I assume they're available for whatever use Ameren Corporation would determine is best.

Q. Do you know?

A. No. That's an assumption.

Q. If Ameren -- if all the dividends paid by AmerenUE --

MR. SCHWARZ: I'm going to object because this case doesn't involve AmerenUE. I think if the same situation applies at Laclede, that that might lead to admissible evidence, but there's nothing in this case that deals with dividend patterns or acquisition patterns of AmerenUE. So I don't think that this line of questions can lead to admissible evidence.

MR. LOWERY: Just to respond to that a moment, AmerenUE is an intervenor in this case, and Mr. Oligschlaeger has made a broad statement in his testimony about the use of cash flow by utilities, not limited to Laclede, and suggested that that cash flow's being used to finance certain mergers and acquisitions and unregulated ventures.

BY MR. LOWERY:

Q. So subject to Mr. Schwarz's objection, you can answer the question. Do you need us to read it back or try to restate it?

A. At this point, yes.

Q. If the dividends that are paid by AmerenUE to Ameren Corporation, if those dividends are in turn paid to Ameren shareholders, then isn't it true that the cash flows from AmerenUE are not financing Ameren Corporation unregulated operations or Ameren Corporation acquisitions?

A. Under the assumption that those dividends paid by AmerenUE to Ameren Corporation are in turn paid out as corporate dividends to shareholders, then those monies would no longer be available to Ameren Corporation for whatever purpose they could have been used.

Q. And you don't know whether or not that assumption is valid or not, do you?

A. I reviewed AmerenUE's most recent annual shareholders report, which had a 10K attached, and I do not believe there was a 100 percent payout of net income to dividend, in the form of dividends to shareholders. I believe some level of monies were retained.

Q. You might have lost me there. Was this were these Ameren monies that were retained or AmerenUE monies that were retained?

Let me try it this way: AmerenUE may not have dividended all of its cash flows, for example, to Ameren; there may be retained earnings at AmerenUE, correct?

A. There could be. I don't know that.

Q. There could be?

A. Yes.

Q. But we already talked about the fact that AmerenUE over the last several years hasn't made any acquisitions of its own of any significance, right?

A. Those are made at the corporate level, the parent company.

Q. Well, when you say they're made at the corporate level, that's a different corporation, though, is it not?

A. A parent company level.

Q. And we've already talked about the fact that AmerenUE itself doesn't engage in any significant

unregulated operations, right?

A. That's my understanding.

Q. So if there are retained earnings at AmerenUE, that's not the money we're talking about, is it? We're talking about dividends from AmerenUE to Ameren and what happens with that money. That's what my question is directed toward. Do you understand that?

A. Okay.

Q. So when you mentioned the 10K and you mentioned whether or not 100 percent may or may not have been dividended to shareholders, are you talking about whether or not 100 percent of the dividends from AmerenUE to Ameren may or may not have been dividended to shareholders or are you talking about Ameren's earnings in general, whether or not Ameren may have had certain amount of earnings and only some of them were dividended?

A. The specific information I reviewed had to do with total company Ameren.

Q. Ameren Corporation?

A. That is correct.

Q. What's dividend yield?

A. I'm not a financial analyst. It is my understanding that that's taking the current level of dividends, comparing it to the current stock price or recent average of stock prices.

Q. That's what I remember, but I'm sort of like you. It's the -- it's an expression of a rate, we take the current level of dividends, we take the stock price and that gives us a percentage, for example, 5 percent dividend yield?

A. Yes, that's my understanding.

Q. Is an attractive dividend yield one of the factors that equity investors consider in deciding whether to invest in a stock?

A. Based upon reading of financial analysis testimony over the years, I would agree with that.

Q. And in the utility industry, dividend yield in particular is something that -- let me try to rephrase that.

Utility stocks historically have been stocks that are invested in or that are seen as being attractive because they typically have pretty good dividend yields; is that fair?

A. That's my understanding, on a historical basis. There may be some changes to that in some aspects of the utility industry in recent years.

Q. Dividends are paid from cash flow; is that right?

A. That's correct.

Q. And lower depreciation rates are going to

result in less cash flow?

A. To the extent those are reflected in the rate levels directly, yes.

Q. If depreciation rates are lowered and rates are set based upon those lower depreciation rates, then cash flows are going to go down?

A. Yes, I believe so.

Q. Is that a paraphrase of what you said?

A. Uh-huh.

Q. And Staff's approach in this case results in lower depreciation rates than if the standard approach is used, correct?

A. In the situation where net -- where cost of removal exceeds salvage, yes, which I believe is generally the case today.

Q. Well, if we have the same data and we have cost of removal exceeding salvage -- exceeding salvage in a set of plan accounts and we use Staff's approach or we use the standard approach, if we use Staff's approach, the resulting depreciation rate's going to be lower?

A. Under those assumptions, yes.

Q. And if the resulting depreciation rate is lower and if that depreciation rate is used to set rates, cash flows are going to be lower, correct?

A. Yes.

Q. If a utility's stock is less attractive to investors than other utilities' stocks, will that affect -- will that mean that the cost of accessing the equity markets for the less attractive utility are greater than the cost of accessing the equity markets for the more attractive utility?

A. In a general sense, I would believe that to be true. Again, that's based on just reading financial analysis testimony filed in rate proceedings over the years.

Q. Which you've been doing for 23 or 4 years?

A. That's fair to say, yes.

Q. I mean, you do know something about this, correct?

A. Enough to be dangerous probably.

Q. Now, with regard to dividends, the cash for dividends typically comes from some or all of the return on equity recovered in rates, correct?

A. That's my understanding.

Q. So when you state on page 6, line 2 of your testimony that amounts associated with return on equity are also available to the utility for potential investment and construction activities, that's not necessarily accurate, is it?

A. I believe somewhere in my testimony I make it clear that the amounts of return on equity available to the company for investment purposes is net of any dividends paid out. So I think I'm agreeing with you.

Q. Okay. At least part of those funds are likely going to be paid out in dividends, correct?

A. Yes.

Q. On page 3 of your testimony, lines 17 to 19, you indicate that, in the context of this proceeding, the cash flow and net salvage issues pertain only to the amount of cash flow available to invest in long-term utility assets.

A. That's correct.

Q. Is that a fair statement of what you said?

A. Yes.

Q. Are you familiar with AmerenUE's capital investment commitments made in the EC-2002-1 settlement and the Order that approved it?

A. At the time I was familiar with or read the Stipulation & Agreement, yes.

Q. Would you agree that AmerenUE has essentially committed to make over $2 billion of infrastructure investments by, I think it's either 2006 or 2007?

A. I don't recall the exact amount. I would agree that -- significant is probably a fair term for their commitments, yes.

Q. It's more than a billion; do you recall that?

A. I don't, but --

Q. But it's very significant; is that fair?

A. Well, significant. I'll leave it at significant.

Q. Okay. Well, whatever the exact number is, and the record would reflect that, AmerenUE, in fact, has a requirement to outlay whatever that number is as a result of the Commission's Order adopting that settlement, correct?

A. I believe that would be the legal -- or I can't say legal -- the impact of the Stipulation & Agreement, yes.

Q. I mean, the Order says we'd better do that, correct?

A. I think there is a commitment there, yes.

Q. So when you say on page 4, line 6 to 7 of your testimony that depreciation, deferred taxes and return on equity are sources of cash because there is no contemporaneous required outlay of cash, utilities do have contemporaneous required outlays of cash, do they not?

A. They are not -- well, what I meant there is in terms -- you don't write a check for depreciation expense once you receive it in rates. You receive the money in rates under the rubric of depreciation expense and these other items, and then you have a choice of what you can do with it, and one of those is reinvesting in the company's infrastructure, which I believe you -- as I recall, was a commitment that UE made in the last Stipulation & Agreement.

Q. We may not have to take that dollar bill and spend it on infrastructure, might be a different dollar; that's what you're essentially saying?

A. You're committed to spend cash or -- from however that's obtained for the purposes described in the Stipulation & Agreement.

Q. But utilities do have required, in fact, legally required cash outlays, do they not? Certainly in the case of AmerenUE if we've committed to $2 billion of infrastructure investments and we're ordered to make those under an Order, we're required to make cash outlays for those, are we not?

A. Well, I don't want to make a legal conclusion, because I cannot. But from a practical perspective, I believe you are committed and should make those expenditures.

Q. And utilities have an obligation to provide safe and reliable service, correct?

A. Yes.

Q. And to the extent cash is required to do that, wouldn't Staff take the position that the utility had better spend the cash in order to make sure they're providing that service?

A. They need to do what it takes to provide safe and adequate service, including use of cash, yes.

Q. Direct your attention to page 4, lines 22 to 23, and page 5, line 1 through the word "no." And you're asked, is traditional ratemaking as practiced in this jurisdiction primarily based upon a utility's cash flow needs? And your answer is no, and then you go on to expand on that. That is your opinion, correct?

A. That's my opinion. I believe that is an accurate reflection of what our traditional regulation in the state is based on.

Q. I take it that while it's your opinion that a utility's cash flow needs is not the primary focus of traditional ratemaking, a utility's cash flow needs are nevertheless a relevant consideration that the Commission should consider in setting rates, is it not?

A. I would agree with that.

Q. Can you cite me to a Commission Order that indicates that your opinion on this issue that you expressed in the passage that I read is, in fact, the

policy of this Commission?

A. I cannot cite to a specific or a particular Order that indicates such. In my opinion, this is something that is generally understood.

Q. Is there any statute in Missouri that you can cite to that indicates that your opinion is the policy of the state, your opinion with respect to what the primary purpose of ratemaking is and is not?

A. No.

Q. And I take it there's no court decision that you can point to?

A. No.

Q. What about the rest of your answer on page 5, line 1 to 7, is there any Commission Order that states that it is the policy of this Commission that utilities should not receive cash in rates to pay for anything other than short-term cash expenses?

A. I don't believe that's the Commission's policy, that they only receive cash in rates to pay short-term cash expenses. There are other -- the utility receives cash in rates at levels that typically exceed their short-term cash expenses and those are available to the utility for its use.

Q. Well, on lines 3 and 4, you state that while the rate-setting process generally can be expected

to provide a utility with cash and rates to pay short-term expenses, then you go on and talk about the usual practice is to borrow or obtain equity for long-term investments. Is it not your testimony -- strike that.

Then it's not your testimony that cash flows provided in rates should only be used for short-term cash expenses? They can be used for other things and that's appropriate; is that your testimony?

A. That is my testimony.

Q. Are you familiar with the St. Louis County Water Company case?

A. I'm familiar with a number of such cases. Which one are you referring to?

Q. That's a good answer. The WR-2000-844 case decided in 2001 that dealt with depreciation and net salvage issues.

A. I have at the very least read the Report and Order for that case.

Q. In fact, this Commission in that case cited the need for cash flows to invest in utility infrastructure as at least one of the bases for adopting the standard approach in that case; isn't that fair?

A. I believe that's a fair characterization.

Q. Does Laclede have outstanding debt?

A. I would assume it does. I have not

specifically looked at that.

Q. What about AmerenUE, are you familiar with whether AmerenUE has outstanding debt?

A. Same assumption; I would assume they do.

Q. Do those two companies issue stock to raise equity capital?

A. Yes.

Q. So both Ameren -- assuming that those assumptions are correct, that they do have debt and they do issue stock to raise equity capital, which you think is probably correct, right?

A. Yes.

Q. Assuming those two facts are true, that means that AmerenUE and Laclede are, in fact, not receiving enough cash in rates today to meet all of their cash needs?

A. Just based on those facts, I can't say, because the timing of such debt issuances and the equity issuances aren't defined. It could be that they are currently cash sufficient but may not have been in the past at which time those issuances were made.

Q. Fair enough. Do you know whether they've gone to the equity and debt markets from time to time on an ongoing basis over the last few years?

A. I'm not aware of the timing of those kinds of issuances over the last several years, no.

Q. Well, if we assume that the internally generated cash is not sufficient to meet their current cash needs, in that scenario the utilities will have to go somewhere else to get that cash, correct?

A. That is correct.

Q. And the two likely sources or maybe the only two sources are either the equity markets or to go to the debt markets?

A. That's true.

Q. On page 6, line 7 to 8, you accuse the companies of a falsehood, do you not?

A. No, I wouldn't agree with that. What I stated is these claims seem to be based upon the assumption that utilities should not have to use external sources of funding. That is false. To the extent the utilities, in fact, believe that they should not have to use it, I would disagree with that opinion, but I would not say that's a factual falsehood, no.

Q. Well, can you cite me any testimony from the companies in this case where one of their witnesses suggested that they should never have to borrow funds or raise equity in the equity markets?

A. I don't believe any such testimony is filed.

Q. And while you don't know the particular timing of the debt or equity issuances, you did agree that they -- those two utilities typically have borrowed money and have issued stock from time to time, correct?

A. Let -- let me state, when you -- referring specifically to Ameren, I'm aware that Ameren has certainly engaged in those activities as part of their merger and acquisition approach.

In terms of AmerenUE, whether they issue debt separately or whatever, I'm not familiar with what those activities may have been.

Q. You don't know one way or the other --

A. I do not.

Q. -- whether AmerenUE itself has issued debt?

A. That's correct.

Q. Let me ask you if this is fair. Isn't it fair to say that what the company's witnesses have testified to is that Staff's approach will reduce the cash flows that they have been receiving via depreciation and net salvage, which will require them to get cash that they used to get via depreciation and net salvage elsewhere?

A. That's correct.

Q. Not that they should get all of their cash needs from depreciation and net salvage; they haven't testified in that regard, have they? They haven't married

that suggestion, have they?

A. They have not stated that directly, no.

Q. Well, how have they stated it indirectly?

A. And what I was referring to on page 6 is, I think both Mr. -- I believe it was Mr. Sherwin, maybe Mr. Cooper for Laclede and Mr. Baxter for UE compared their current construction expenditures to the current level of depreciation expense received in rates with, in my mind, the implication that since there was a shortfall of depreciation compared to the construction, that that constituted a problem of some sort. That is what I was addressing.

Q. Could just have easily been, though, a contention that today, under the standard approach, we're getting X amount of cash flow, and if you go to Staff's approach we're going to get less cash flow, and so we are going to lose a certain amount of cash flow that we used to have available to make infrastructure investments, correct?

A. And I would agree that's an impact of our position on net salvage.

Q. Whose expectation is it that external funding be used to invest in long-lived assets? Is that your expectation, your opinion?

A. It's an expectation based on past

experience that all major utilities have rate base investment, which means they have gotten funds from external sources to invest in long-term assets.

Q. **Forgive me if I'm asking the same question again, but I think you've already testified, though, that it's not your expectation that that be the only source of investment in long-lived assets?**

A. Utilities typically would invest both internally-generated funds and externally-provided funds in long-term assets.

Q. **You talk about rate base at page 6, lines 11 to 13 of your testimony. Do you recall that or can you see that as you look at your testimony?**

A. Yes, I do.

Q. **What effect do depreciation accruals have on a utility's rate base?**

A. All other things being equal, they would reduce it.

Q. **So if under the standard approach the depreciation accruals are higher than under the Staff's approach, the reduction in rate base, all things being equal, is going to be greater under the standard approach, correct?**

A. That is correct.

Q. **And if rate base goes down more under the**

standard approach than the revenue requirement associated with it, the return on rate base is going to go down more as well, correct?

A. When that is isolated to consider only rate base impacts, that is correct.

Q. If the rate base goes down by a million dollars more under the standard approach, and let's just keep it simple, say the rate of return is 10 percent, revenue requirement's going to go down by $100,000 more in that example, correct?

A. That's correct. That does not take into account the additional monies provided in rates for the higher depreciation rates earlier by the customers.

Q. And reduction of rate base by the amount of the depreciation accruals, that has been the practice that the Commission has followed for a very long time, correct?

A. I believe that's true.

Q. What is the service life of a utility asset?

A. It depends from asset to asset.

Q. Well, I didn't mean literally. In general, what is -- not 50 years versus 30 years, but in general, what does service life mean?

A. Oh, I'm sorry.

Q. That's okay. My question wasn't a good one

obviously.

A. How long -- the service life of a particular asset is how long it is in service and providing a benefit to the utility and its customers.

Q. What is intergenerational equity?

A. It's my understanding of the term that that is the appropriate charging of costs in rates to different generations of customers.

Q. Each generation of customer should pay the full cost that the utility incurs to provide them service. Is what I just said the same thing as what you just said in your mind?

A. General terms, yes.

Q. What is your definition of a generation of customers?

A. I'm not aware that there's any kind of standard definition of that as it specifically applies to utility ratemaking and intergenerational equity.

I would say at a minimum probably you would consider customers under one level of rates compared to another set of customers under a different level of rates via a general rate proceeding to be two different generations of customers.

Q. When you said at a minimum, what did you mean? You said at a minimum you would consider customers

under one set of rates versus customers under another set of rates.

A. What I mean is that, for example, if Laclede typically files a rate case every two years or AmerenUE files every five years or whatever the case may be, that it could be legitimate to view that set of customers in effect for the first two years for Laclede as a different set of customers for the next two years under a different level of rates.

Q. Okay. I understand what your definition is. I just wasn't sure why you qualified it with at a minimum. There wasn't any particular reason?

A. Well, that's -- using that example, if Laclede is operating under the same set of rates for two years, would I look at one year's customers as a different generation than the next year's? Probably not. This is a matter of art and not science, probably.

Q. Would you agree that it's unfair for a past -- for past or future generations of customers to subsidize the rates of today's customers?

A. As a general matter, yes.

Q. Should the Commission take the potential for subsidization of that type into account when it sets rates?

A. As one of the considerations facing it, yes.

Q. Should it consider that in making decisions about how depreciation and net salvage is going to be treated?

A. Yes.

Q. Is it fair to say that one of the things regulators try to do is match the costs associated with the utility asset with the revenues generated by that asset?

A. That is fair.

Q. That's the matching principle?

A. Yes.

Q. And you generally support that principle in ratemaking?

A. Yes.

Q. And that's a principle the Commission should consider when it sets rates?

A. Yes.

Q. If the Commission believes that a part of the cost of an asset is the cost to remove or otherwise retire that asset, then does it not make sense for the customers who are served by that asset to pay the ratable share of the entire cost of the asset over its service life?

A. As long as those costs can be reasonably and accurately quantified, yes.

Q. And when can those cost be reasonably and accurately quantified, to use your terms?

A. Typically in the ratemaking process, that is done by use of actual expense levels, as opposed to use of estimated levels into the future. I'll just leave it at that. Generally, it's using actual known costs.

Q. To the extent -- and I'll just ask you to assume this, not necessarily to agree with it. To the extent that the standard approach has been used in the past for utilities, then, in fact, estimates of net salvage have been used in ratemaking in this state, have they not?

A. That is correct.

Q. So when you use the word typically, what were you referring to?

A. The way most costs -- and I wasn't limiting it to net salvage or cost of removal. Most costs, the way most costs are treated in the ratemaking process.

Q. How do you know that Staff's approach will in no way create a cash flow detriment, as you allege on page 8 of your testimony?

A. Well, actually, there may be a short-term differential between the rate -- the cash received in rates for cost of removal and salvage activities compared to the actual cost outlay. So with that caveat, ignoring that, which is typical of all items of expense that a utility incurs, the intent of the Staff's approach is to provide them the cash -- provide the utilities the cash they need to in turn expend on a current basis on cost of removal activities.

Q. If the Staff's approach were adopted prospectively and permanently, let's say, then the cash flows over the long term are going to be less than if the standard approach -- well, strike that.

I think we talked earlier about that cash flows -- maybe we didn't. Are cash flows one of the important factors that credit ratings agencies look at in rating companies in general but utilities in particular?

A. I can't speak about in general. For utilities, I believe that they look at cash flows, yes.

Q. Certainly for utilities, the cash flows that utility has -- that utilities have is an important factor in that credit ratings agency's determination of what the credit rating is going to be?

A. I believe I could generally agree with that.

Q. It's one of the more important factors, isn't it?

A. I believe that's what Mr. Fetter's

testimony says, and I have no reason to doubt that.

Q. You don't have any reason to doubt that Mr. Fetter is correct about that?

A. On that point, yes.

Q. And regardless of -- well, let me back up.

on page 10, lines 14 to 15, I think you suggest that credit rating agencies are not focused on setting just and reasonable rates. That's not their focus, is your point, correct?

A. That's correct.

Q. Regardless of whether or that's true or not, if credit ratings agencies perceive that Missouri's policy on depreciation is less favorable than other states' policies on depreciation, that's going to increase the likelihood that Missouri utilities will have lower credit ratings relative to other utilities in other states, is it not?

A. Taken in isolation, I would agree that measures that would reduce the cash flow of Missouri utilities compared to out-of-state utilities would be looked at less favorably by the credit rating agencies.

Q. Particularly since cash flow is an important consideration for utilities in terms of how credit ratings agencies view them, correct?

A. Yes.

Q. And if your credit rating is lower, if a utility's credit rating is lower, then in general its cost of borrowing is going to be higher, is it not?

A. That's my general understanding.

Q. And that in turn is going to cause customer rates to be higher to the extent customer rates reflect borrowing costs; is that not true?

A. All other things being equal, that is true.

Q. And if a utility is in general less creditworthy in the views of the credit ratings agencies or in the views of investors in general, the attractiveness of its stock to equity investors is probably going to be somewhat less as well, is it not?

A. Can you repeat that question?

Q. A utility that is less creditworthy than another utility, its stock in general is going to be less attractive than the stock of other utilities that are seen as more creditworthy, true?

A. Credit rating agencies, as I understand it, look at the debt instruments of a utility, not necessarily the equity securities that they may issue. So what you say has a certain amount of plausibility. I'm not sure I could have the knowledge to fully -- or to agree with you.

Q. Well, let me try it this way. I agree with you that credit ratings agencies issue ratings related to

the debt of a utility, but isn't it a fact that equity investors look at the -- look at the overall creditworthiness of a company as well in making decisions as to whether to invest in Company A versus Company B?
A. I think it's reasonable to assume that equity investors would also have an interest in cash flow.
THE WITNESS: Can I take a break?
MR. LOWERY: You bet.
(A BREAK WAS TAKEN.)
BY MR. LOWERY:
Q. Mr. Oligschlaeger, before we took a break, we'd been talking about the creditworthiness of utilities and the effect of credit ratings on borrowing costs and those types of things. Do you recall that discussion?
A. Yes.
Q. And I think you agreed that if, at least all other things being equal, if credit ratings are lower for a utility, that their costs of borrowing are going to be higher?
A. That's my understanding.
Q. And I think you agreed with the general proposition, though you didn't necessarily have personal firsthand knowledge, but you agreed that it was reasonable to suggest that if a utility is less creditworthy, that its stock may be less attractive as well?

A. That's possible.

Q. Assuming that a utility has lower credit ratings and thus higher borrowing costs and that its stock is less attractive, utilities in that situation are going to incur higher costs in raising funds externally than they otherwise would; is that fair to say?

A. As a general understanding, I think that would be accurate.

Q. And in the context of this discussion, we were talking about the fact that it's reduced cash flows that are driving those lower credit ratings and higher costs, correct?

A. In the context of this discussion, yes.

Q. How credit rating agencies perceive depreciation policy in this state is a relevant consideration that the Commission ought to consider, is it not?

A. One of the considerations, yes.

Q. On page 11, lines 11 to 13, you state, our belief, and when you say our belief, you mean Staff's belief; is that correct?

A. Yes.

Q. You state Staff's belief that downgrades in credit ratings in recent years are because of voluntary initiatives by utilities to expand into nonregulated

activities.

Do the downgrades issued by Moody's or S&P for Laclede cite as reasons for those downgrades expansion into nonregulated activities?

A. Well, what I was referring to my testimony was particularly the maintenance of an investment grade rating, and I believe that there are other utilities in the state that have had a problem maintaining those ratings, and those were the reasons stated here in the testimony. I wasn't referring specifically there to Laclede or AmerenUE.

Q. Okay. Well, but back to my question. Moody's and S&P have downgraded Laclede; you're aware of that?

A. I don't believe there's -- I'm aware of that. I don't believe that's an investment grade rating problem.

Q. But they have been downgraded?

A. My knowledge of that is just based on the other testimony filed in this proceeding.

Q. So I take it you don't know what the reasons for the downgrade of Laclede's debt, what reasons were given by Moody's and Laclede -- or Moody's and S&P?

A. Other than what was discussed in the testimony in this proceeding.

Q. You've not alleging that expansion into nonregulated activities was one of the reasons given with respect to Laclede?

A. No, I'm not alleging that.

Q. Are you alleging that Ameren's credit ratings have in some way suffered as a result of expansion into nonregulated activities?

A. I'm not aware of that.

Q. Are you referring really when you made those statements in your testimony, are you really referring to a company like Aquila?

A. On page 11, lines 10 through 13, yes, Aquila was my primary point of emphasis there, yes.

Q. Is it your contention that Ameren and Laclede have conducted themselves in a manner similar to Aquila?

A. No, it is not.

Q. And you're not contending that Ameren or Laclede have a financial profile that's similar to Aquila's in any way?

A. No, I'm not.

Q. You disagree with Mr. Fetter's contention that credit ratings agencies tend to view Staff's approach as more risky because of the greater chance that cost of removal amounts will ultimately not be recovered, correct?

A. I disagree with his perception that there is a significant risk that the Commission would deny rate recovery of prudent cost of removal expenditures.

Q. Let me try to rephrase what I think you just said. The reason you disagree with Mr. Fetter is because you think that he is suggesting that the Commission won't properly allow the recovery of prudently incurred expenses; is that what you think he's suggesting?

A. I believe the use of such terms as rate shock in that regard leads me to believe that that is his suggestion.

Q. Well, assume for a minute that future commissions will allow recovery of all prudently incurred expenses, but that the credit rating agencies don't believe that future commissions will allow recovery of all of those prudently incurred expenses.

Is it fair to say that the credit ratings agencies may nevertheless downgrade the utility regardless of all of the good intention of the current Commission?

A. It's the credit rating agency's perceptions that would govern that, yes.

Q. Not the intentions of the Commission itself?

A. That's difficult to answer. The intentions of the Commission are not always very clear.

Q. I would agree with that.
A. But, no, it -- again, their perceptions of what is likely or possible to happen in the future I assume would govern that judgment.
Q. And put another way, the point is not what commissions may or may not do, but what the credit rating agencies perceive they may do or not do?
A. That's correct.
Q. And if they perceive, they being the credit rating agencies, if they perceive the creditworthiness of the utility negatively because of adoption of Staff's approach, the credit ratings are going to be negatively impacted, correct?
A. That's correct.
Q. You imply on page 9 of your testimony that utilities don't have incentive to operate efficiently if the standard approach is followed. Is that a fair characterization of what you discuss on page 9?
A. I would state that they don't have as much incentive as under the Staff's approach to operate in an efficient and productive manner.
Q. Well, didn't you suggest elsewhere in your testimony that utilities want cash flow provided by depreciation rates that include net salvage to pay dividends, to invest in unregulated activities and in

other activities? If the utilities want cash for those things, then what makes you think that the utilities are going to spend more for cost of removal or retirement than they should?

A. I disagree with the assumption in your question that I stated that utilities want that particular cash flow for that purpose. I think what I stated is that they could use it if they wished, that there were no impediments to that use. I'm not making a judgment in terms of Laclede and AmerenUE's desire for the additional cash flow under this approach.

The point on efficiency is quite simple. If you pre-collect a cost in rates, you have less incentive to be efficient in terms of carrying out those activities than -- as opposed to whether -- as opposed to if an approach is taken using historical average in which the utility might be able to beat that average in terms of its actual cost experience.

Q. Do you have any evidence that AmerenUE or Laclede have incurred more cost of removal or retirement costs than they should have prudently incurred?

A. No.

Q. That they've been inefficient in the way that they go about incurring removal or retirement costs?

A. No.

Q. Even though for many years they've operated under the standard approach, you don't have any evidence to that effect, do you?

A. I haven't particularly done a review or research of that point, but I'm not aware of any evidence of that.

Q. So your statement about incentives is sort of a generalized statement; it isn't backed up by any particular evidence that AmerenUE or Laclede have not had the right incentives to be efficient in terms of removal or retirement activities?

A. It is a general statement based upon the inherent attributes of traditional regulation as practiced in the state. It was not based upon any specific knowledge of or allegations that AmerenUE or Laclede have not operated in a reasonably prudent and efficient fashion in these activities.

Q. Well, if utilities in general or AmerenUE or Laclede in particular, if they blow the funds that they accrue for net salvage via depreciation rates on unnecessary cost of removal or retirement activities, they're not going to have those funds for investing in new plant or to pay dividends or invest in some kind of other activities, are they?

A. They would not have those funds for any other purpose, yes.

Q. Because it seems that the premise of your testimony or at least one of the premises is that utilities desire this cash flow to use for these -- to use for these other kinds of activities.

You, in fact, indicate in your testimony, do you not, that that cash flow's available for unregulated operations, dividends, these other types of activities, correct?

A. They're available for those purposes. They're available to reinvest in plant or other utility-type activities.

Q. So if one of your premises is that utilities would like to have the cash to use for those activities, don't they have an incentive not to incur unnecessary removal or retirement costs?

A. Well, my testimony is not to say that utilities have no incentive whatsoever to be efficient under what you call the standard approach. I'm just making a generalized statement. I believe greater efficiency is served by the Staff's approach.

Q. But you have no evidence or no instances that you can cite to me that indicate that the standard approach has created a disincentive to be efficient in cost of removal or retirement?

A. I'm not aware of any prudency or efficiency problems in that area for either --

Q. But this -- I'm sorry.

A. -- for either of those, Laclede or AmerenUE.

Q. This efficiency theme, then, is really -- it's your theory or your supposition about what might or might not be true?

A. It's a general theory or supposition that I believe, that I think is reasonable.

Q. That's not based on any evidence?

A. As it applies -- no evidence, but from Laclede's or AmerenUE's actual cost of removal activities, yes.

Q. Well, now I have to ask another question. Do you have evidence of another utility that indicates that use of the standard approach has caused them to be less efficient than you think they should have been?

A. No.

Q. So you don't have any evidence of any utility that indicates that the standard approach has created the wrong incentive in terms of being less efficient in cost of removal or retirement activities?

A. No. This is stated as a general belief.

Q. If the standard approach continues to be

used and Staff thinks that too much is being spent on cost of removal or retirement, can't Staff point that out to the Commission in a rate case?

A. Yes.

Q. Isn't it fair to say that the Commission would have the power to force a utility to absorb imprudently incurred retirement or removal costs?

A. I'm not sure how that would work given the prepayment approach that is implicit within the standard. I guess prospectively you could reduce depreciation rates to take into account allegations of that sort. That doesn't impact, I don't think, the past precollections that may not have been used efficiently or prudently.

Q. Well, are you aware that Staff has discussed in testimony on numerous times -- on numerous occasions amortizing accruals over time, in effect returning what Staff views as overaccruals to customers?

A. As it applies to depreciation reserve?

Q. Yes.

A. Yes, I am aware of it.

Q. So that's a mechanism, isn't it, that in effect causes the utility to absorb those costs as opposed to ratepayers?

A. That is possible.

Q. I mean, isn't it fair to say that the

Commission has the power, if utilities come in later and say, you know, we need more money for cost of removal or retirement even though we've already collected it applicable to particular plant, we need more money, we want more money, isn't it -- isn't it within the power of the Commission to look at those expenses and say, you were imprudent in what you did with the money you've been accruing all of these years and, therefore, we're not going to allow you more money, your shareholders are going to have to bear that cost?

A. I presume the Commission has that power.

Q. On pages 9 and 10 of your testimony, you do not disagree with the company's contention that customer rates will be lower in the long run under the standard approach, do you?

A. I believe that revenue -- I do not believe it has been established that customer revenue requirements will be lower under the standard approach.

Q. Well, the question you were asked was as follows: In general terms, the company's witnesses claim that precollection of net salvage costs in rates will result in lower overall customer rates in the long term. Is this valid? And you do not say in your answer whether the company's claim is valid or invalid, do you? Rather you go on to argue in your answer that the customer's

cost of capital may be more than the utility's cost of capital, so that the return on rate base the customer enjoys may not be a good deal for the customer. Is that your basic point?

A. My basic point there is, if in fact rates might be lower under the standard approach in the long run, that does not take into account the financing costs the customers themselves face when such rates for net salvage are precollected from them, compared to the Staff's approach.

Q. You don't know whether, as you put it, the customer's cost of capital is more than the utility's or not, do you?

A. As I state, I think it's counterintuitive to believe that customers can obtain capital cheaper than companies like Laclede and AmerenUE, but that is based on -- I haven't done a specific study of what the average customer's cost of capital is, and I'm not sure that that would be easy or practical to do in any case.

Q. You have a theory that their cost of capital may be higher, but you don't know whether it is or not?

A. I believe that's a reasonable theory and assumption.

Q. But it is a theory and an assumption on

your part?

A. Yes.

Q. If a gas customer pays a few dollars more per year in his gas rates as a result of the standard approach and if those few extra dollars would have been sitting in a checking account or a savings account or a CD that earns 1, 2, 3, 4 percent, that customer's cost of capital, in fact, is a heck of a lot less than the utility's, is it not?

A. Under the specific assumptions you just gave, that would be true. I wouldn't agree those are the only relevant assumptions.

Q. There's certainly customers that have that exact situation, do they not?

A. Some customers, I'm sure.

Q. Because when depreciation accruals go into the depreciation reserve and reduce rate base, customers essentially earn the rate of return of the utility on those monies, do they not?

A. That is the way the rate process works, yes.

Q. And that's going to be more than those customers can earn in a savings account or a CD in most instances, is it not?

A. That is true, but those are not the only sources that would establish a customer's cost of capital.

Q. **But they certainly are one source --**

A. One source.

Q. **-- that would establish it?**

A. Yes.

Q. **And you haven't studied the weighting of various sources, have you?**

A. No, I have not.

Q. **Do you agree with the Commission's decision in the St. Louis County Water case, 2000-844 case we talked about earlier?**

A. As it relates to net salvage issue?

Q. **Yes.**

A. Okay. I would agree that a company's infrastructure capital requirements are a relevant consideration to take into account in establishing a rate decision regarding net salvage.

Q. **Did the Commission in your view make the right decision about net salvage in St. Louis County Water Company?**

A. I did not -- was not involved in that case to the degree necessary to have really looked at St. Louis County Water's infrastructure requirements and so on. So I really can't say I agree or disagree with the specifics of that decision.

Q. The standard approach was used in that case; is that your understanding?

A. The Commission ordered something along the lines of the standard approach, yes.

Q. They ordered depreciation rates that had been determined using the standard approach, correct?

A. With a net salvage component and the depreciation rate, I believe so.

Q. And the net salvage component in the depreciation rate was calculated in the manner using -- not in the manner -- using the standard approach to calculating that, correct?

A. That is my understanding.

Q. And in order to use the standard approach, net salvage estimates are used, were they not? They were used in that case? You had to use estimates of net salvage in order to use the standard approach in the St. Louis County Water case?

A. Based upon my reading of the Order, I believe that's correct.

Q. Specifically, the future net salvage costs in that case and under the standard approach in general were and are estimated by taking the ratio of the dollars of cost of removal or retirement experienced in each account over the original cost of the assets that are

retired in each account; is that your understanding?

A. That's my understanding in general of the standard approach. I really can't comment as to whether that was specifically done in the County Water rate case.

Q. You don't know whether it was or was not?

A. No, I do not know.

Q. You know that Bill Stout was the witness for County Water in that case?

A. Yes.

Q. You've read Mr. Stout's testimony in this case?

A. Yes.

Q. And you know that he advocates using the standard approach and calculating net salvage as I just described it, correct?

A. Yes.

Q. Is it probably a fair assumption that that's how it was done in St. Louis County Water?

A. That's a fair assumption. I've not read his testimony in that case.

Q. In any event, the ratio I just described, it produces a net salvage percent for each account; is that right?

A. I believe so.

Q. And that net salvage percent, together with

informed judgment of the depreciation analyst, is then used to come up with the depreciation rate; is that correct?

A. I think that's generally accurate.

Q. And those rates were adopted by the Commission in that case?

A. In that case.

Q. So the Commission in that case at least sanctioned the use of estimates and net salvage, did it not?

A. Yes, while stating that the Staff's approach also had its merits and will continue to be considered in other cases.

Q. I understand that qualification, but the Commission did sanction the use of estimates in that case?

A. I believe so.

Q. So estimates of future net salvage in the Commission's view are not necessarily -- let me strike that.

Using estimates of net salvage in the Commission's view is sometimes okay, correct?

A. Under certain circumstances, yes.

Q. And I think your testimony in your supplemental rebuttal testimony was that there are circumstances where that would be okay with you?

A. Yes, if a company can demonstrate it has a particular cash flow concern or problem of the nature, perhaps similar to the nature of County Water's, that should be taken into consideration.

Q. Which means there are going to be circumstances, as you just described, where using future estimates of net salvage are okay with you?

A. In terms of an overall balancing of the various policies the Commission has to take into account, yes.

Q. So there's no Commission order or rule that says, thou shalt not use estimates of future net salvage, is there?

A. Not that I'm aware of.

Q. There's no Commission order or rule that says that net salvage amounts must be known and measurable, as Mrs. Schad discusses in her testimony?

A. I'm not aware of a Commission order that states that is the only and singular consideration.

Q. Do you know what terminal net salvage is?

A. I have a general, very general understanding that that is the net salvage associated with final demolishment or removal of major assets such as electric generating stations and so on.

Q. Associated with what's sometimes also

called life span property? You've heard that term?
A. Yes, I believe that's true.
Q. Terminal net salvage is not what we're talking about in this case, correct, to your understanding?
A. I don't -- I frankly don't know whether the companies are -- Laclede in the '99 rate case was seeking terminal net salvage or not. I don't believe so.
Q. Okay. Do you know what I mean by the term "mass property"?
A. Yes.
Q. Is it your understanding, to the best you can understand from reading the record or preparing for this case, that what is at issue in this case at this time on this remand is Laclede's mass property accounts?
A. I know it involves the mass property accounts. I really can't say that it doesn't involve non-mass property accounts. I don't know.
Q. Do you have an opinion with respect to whether the approach Mr. Adam -- well, strike that. I've already asked you that.
Are you offerings any opinions in this case with respect to what the appropriate net salvage percentages should be, the actual numbers should be in this case for Laclede?

A. No.
Q. Or what the overall depreciation rates for Laclede should be?
A. No.
Q. You make a proposal near the end of your testimony to segregate net salvage accruals from other corporate funds if the Commission were to continue the standard approach, correct?
A. Yes.
Q. Has the Commission ever required such a segregated fund with respect to depreciation or net salvage for Laclede?
A. For Laclede, no, or not that I'm aware of.
Q. For AmerenUE?
A. Unless one considers nuclear decommissioning to be a subset of cost of removal, other than that, no.
Q. The nuclear decommissioning fund is a function of federal statute, state statute, I believe, is it not?
A. Yes.
Q. So putting that aside, not for anything else at AmerenUE that you know of?
A. Not that I'm aware of.
Q. For any electric utility in Missouri, and

again ignoring nuclear decommissioning, for example, KCPL?

A. Not that I'm aware of.

Q. Any other gas utility in Missouri?

A. Same answer, I'm not aware of any.

Q. How would your segregated fund work?

A. This is one area that I did not develop in great detail. I believe that would be subject to further discussion, review and analysis to determine the exact mechanism that would be used to safeguard the funds. It could work similar to the current procedures used for pension and post-retirement benefit funds, but there probably are other approaches as well that could be considered.

Q. Well, the idea that you have, and correct me if I'm wrong, for using a separate fund is that you want to make sure that the funds are available, right?

A. For the intended purpose, which is payment of cost of removal or net salvage.

Q. That those funds are sitting there, and when we've got to retire or remove a piece of plant, you take a dollar out of that fund and you use it for that?

A. That was my thought process, yes.

Q. So I take it you would recommend investing in, relatively speaking, conservative investments, investing those funds in conservative investments to make sure they're going to be available?

A. I really didn't have a recommendation along those lines. As a general policy, I believe that would be reasonable.

Q. And if that is reasonable as a general policy and that's how it ends up being implemented, if it were implemented, those types of investors likely won't earn what the customers earn on the rate base reduction that is experienced because of the accruals in the depreciation reserve? They're not likely to earn that level of return on that segregated fund, are they?

A. That is possible.

Q. Well, isn't it likely that they won't earn that level of return, if we're investing in bonds for example?

A. I would agree under that specific example it would not be likely.

Q. Okay. There will probably be costs associated with setting up a segregated fund, correct?

A. I assume there would be.

Q. Probably trustee fees?

A. If the trustee route is used, yes.

Q. Well, if you're going to have segregated funds, you've got to have some type of custodian or trustee, some fiduciary that is essentially managing those

funds, don't you? Else it's not really segregated, is it?

A. Well, again, when I wrote this, I didn't mean to preclude other possible processes other than pension and OPEB type procedures that are used. Quite frankly, I'm not sure of the realm of total possibilities and so on. If a trustee is used, then there are certain costs associated with that.

Q. And there's likely to be fund expenses?

A. Yes, under that assumption.

Q. Do you know if the real rate of return, the returns on that fund after inflation and whatever expenses may exist, whether that real rate of return is going to keep up with the future cost of removal that will be incurred?

A. I don't know that.

Q. You would have to estimate the return in such a fund to figure that out, wouldn't you?

A. I believe that's done currently with the pension and the OPEB fund, similar type of assumptions.

Q. You would have to estimate it, though?

A. Yes.

Q. You've got to use estimates to do that?

A. Well, yes. And under that assumption you'd be collecting the amounts based on estimates of future expenditures as well as estimates of the earnings associated with segregation of funds.

Q. What evidence do you have that supports your apparent contention that Laclede will not pay the costs of removal or retirement later when those cash lays are required absent a requirement that a segregated fund be established?

A. Well, my assumption is that Laclede will do what is necessary to meet its obligations to the public as a utility in terms of its cost of removal expenses and it would be -- as such, it would obtain its funds from some source to do so.

Q. Then why have a segregated fund?

A. Because if the cost is important enough to pre-collect from customers long in advance of the actual necessary cash outlay, then it is important enough to make sure that the funds are used for the intended purpose, which is to fund cost of removal activities.

Q. What does it matter to a customer whether Laclede uses those exact dollars or other dollars that you've just said you would expect Laclede would come up with and use to engage in the cost of removal activities? Why does it make any difference to the customer?

A. Well, if I'm a customer and I know I'm paying more in rates to a company for cost of removal activities but those funds are not actually being used for cost of removal activities, that may be an area of concern.

Q. **Why?**

A. Because I would presume as a customer that my -- the monies I pay in to a utility are being used for the purposes for which they're intended. If I'm paying for cost of removal and it turns out the utility does not actually use those amounts for cost of removal activities, as a customer I would say, why am I -- why am I making these payments to Laclede or AmerenUE?

Q. If a customer -- if customer rates takes into account what fuel and purchased power costs are going to be and it turns out that fuel and purchased power costs are less, some of those funds weren't used for what the customer was paying for either, were they?

A. True, but we're not talking about the many years, possibly many years duration between receipt of the funds by the utility and their actual use by the utility.

Q. If, in fact, the cost of using a segregated fund is greater than -- well, let me back up.

If on a total return basis the real rate of return in the segregated fund is less than the return that the customer is getting because of the rate base treatment of net salvage today, and if Laclede would come up with the money anyway, as you expect, to pay these cost of

removal costs, isn't a segregated fund costing the customer more in the long run?

A. Under those set of assumptions, I would agree, but there are other factors or considerations beyond just that kind of dollar for dollar comparison.

Q. But those kinds of -- that set of assumptions could very well be correct, could it not?

A. That is possible.

Q. And you haven't analyzed whether it's correct or not?

A. I've not -- that is correct.

Q. Yet you are recommending a segregated fund if the Commission continues the standard approach, correct?

A. Under the alternative that the Commission finds that a return to the standard approach for Laclede is appropriate, I believe these kinds of considerations should be considered, yes, by the Commission.

Q. Laclede has paid cost of removal and retirement costs for decades, have they not?

A. I believe so.

Q. Without a segregated fund?

A. I'm not aware of any segregated fund in use for that purpose.

Q. Does everyone on Staff agree with the

approach to net salvage recommended by Mr. Adam in this case?

A. Obviously I have not taken a poll or personally talked to every Staff member about this particular issue. Of those Staff members I have discussed this with or within a management position within the agency, I believe there is a concurrence with the Staff approach.

Q. How about Staff's subsequently adopted approach, same question?

A. Same answer.

Q. Does everybody agree? Same answer?

A. Same answer.

Q. Do you or to your knowledge any Staff members -- or have you or to your knowledge any Staff members had any second thoughts about whether Staff's approach is the appropriate approach?

A. I'm not aware of any.

Q. So once you -- once Staff made that decision, Staff is convinced this is the right approach?

A. To my knowledge. I mean, there may have been second thoughts as you suggest. I'm just not aware of them.

Q. Does Staff ever internally debate the merits of its approach, whether it's on the right track

with its approach? Does it debate the issue today, or recently has that debate taken place?

A. Many times informal discussions take place among members of the Staff in which these kinds of issues are discussed. In terms of is there any formal mechanism for the Staff to gather and say, let's say, do we want to continue with our current report -- approach to net salvage, I don't think there's that kind of specific.

Q. Let me ask it this way: Can you relate to me any discussions that you're aware of where someone on Staff in the last couple of years has said -- has raised questions about whether or not Staff's approach is the correct approach?

A. If they have, I am not aware of it.

Q. Do you personally believe in Mr. Adam's approach?

A. Yes, I do.

Q. And I take it you personally believe in Staff's subsequently adopted approach?

A. Yes. I believe they're equivalent.

Q. How did you come to have that belief yourself personally?

A. Initially just based upon my knowledge in general of the issue and the reliance upon what I would consider to be somewhat speculative estimates for establishing this level of cost in rates, it is my belief that an appropriate regulatory policy is to base recovery of this item on known and measurable historic numbers.

Q. This may be a hard hypothetical for you to agree with, since you don't agree with it, but let's assume that you didn't believe in Mr. Adam's approach or Staff's approach. Would you be permitted to file testimony to the company supporting whatever other approach you believed in?

A. As a general matter, no. If I -- if I was requested to file testimony in support of a particular approach which I personally did not agree with, then the proper course of action would be to explain my disagreement, and presumably another Staff member would then be approached to file the necessary testimony.

Q. So if Staff has a policy on a particular issue, then Staff witnesses are not allowed to file testimony contrary to that policy; is that fair?

A. They're not -- wouldn't be allowed to file testimony contradicting the Staff approach, I believe, as a general rule, yes.

Q. And who makes that decision?

A. In terms of who files testimony?

Q. Who makes the decision that we're not going to let Mr. Oligschlaeger file testimony on that issue

because his belief is not in accordance with Staff's current policy on that issue?

A. That would be -- if that situation ever arose, and it has not arisen with me, I believe that decision would be made at the division director level, possibly going up to the executive secretary.

Q. Probably Bob Schallenberg or perhaps Mr. Quinn?

A. Depending on the issue, Mr. Henderson may be involved.

Q. If it's within his area, it would be Mr. Henderson, but within your area it's probably going to be Mr. Schallenberg?

A. Yes.

Q. I take it you know that in AmerenUE and Laclede's testimony they have discussed a number of safeguards associated with the standard approach. You are generally familiar with that testimony, having read it?

A. Yes.

Q. One safeguard that they cite is that utilities are required by the Commission's rules to file new depreciation studies periodically. Do you agree that that's true, that they are required to file depreciation studies periodically?

A. That's my understanding.

Q. Do you know how often?

A. I believe five years.

Q. When they file those depreciation studies, they're including information of cost of removal by vintage, what the depreciation reserve is, all of the various backup data that deals with those plant accounts, correct?

A. I would assume that that happens. I'm not directly involved in those proceedings.

Q. So every five years the calculation of net salvage that they're using is updated, correct?

A. That's what I presume would happen.

Q. Wouldn't you agree that the fact that there's a specific requirement for a specific detailed study to be submitted to the staff every five years provides some measure of protection to customers?

A. Some measure. I would say an insufficient measure, but some measure.

Q. It is at least -- you believe it's an insufficient safeguard, but it is at least a safeguard to some extent, is it not?

A. You can correct estimates going forward or further refine them, yes.

Q. Another safeguard the companies have cited is the fact that the depreciation reserve acts as a

balancing account; is that correct?

A. They have stated that in testimony.

Q. Can you explain your understanding of how that works?

A. Well, the more monies provided to the company up front for cost of removal and net salvage activities, that is booked to the depreciation reserve and rate base is lowered by those amounts.

Q. And you can make adjustment to those depreciation rates going forward, can you not?

A. To a company's authorized depreciation rate?

Q. Yes.

A. Yes, that happens.

Q. And as we talked about before, there could be amortization of under or overaccruals, could there not?

A. There could be.

Q. Because you're tracking the accruals in an account, are you not?

A. On an overall basis. It is not split out between the net salvage component or the life component.

Q. Do you know whether or not, if a depreciation analyst wanted to look at the records, whether or not you could go back and split it out?

A. I don't know.

Q. And regardless of whether you can split it out or not, you can track in the depreciation reserve the total amount collected or total amount accrued for depreciation and net salvage from customers, can you not?

A. I believe so.

Q. So doesn't that allow you over time to balance or true-up that account?

A. Well, the depreciation reserve reflects the accruals for a particular account over time. To the extent you change the rates on a going-forward basis, then the reserve would be reflected in a similar manner. I'm not sure that's answering your question.

Q. Well, if you change the depreciation rates, you either raise them or lower them, you lower them if the accrual seems to be too high, you raise them if the accrual seems to be too low, or you may amortize over or under-accruals?

A. Uh-huh.

Q. Don't those two mechanisms over time allow you to true-up the total amount accrued for net salvage versus the total amount that's going to be -- strike that -- the total amount collected for depreciation and net salvage to the total amount accrued or the total amount that's going to be spent from that account? Can't you true that up over time by using those two mechanisms?

A. Again, you can refine the estimates going forward. I don't think a true-up per se is possible 'til the actual monies related to net salvage are spent.

Q. But you can make adjustments to bring that depreciation reserve more or less in line with the accruals over time at various points in the process, can you not?

A. Yes.

Q. A third safeguard cited by the companies is the fact that the depreciation reserve is an offset to rate base, and the Commission's longstanding practice has been to offset rate base with that depreciation reserve, right?

A. That's correct.

Q. Did you talk to anyone else on Staff about the content of your testimony before you drafted it? And I'm not asking for any attorney/client privileged kind of communications, so exclude those.

A. The discussion I had with other Staff members regarding this testimony before it was drafted would have been with Ms. Schad, Mr. Schallenberg and Mr. Schwarz.

Q. Did you receive, other than Mr. Schwarz, any substantive direction from Ms. Schad or Mr. Schallenberg in terms of your testimony?

A. They were provided copies of my draft testimony. I believe Ms. Schad had some comments in regard to my draft.

Q. Well, to the best of your recollection, what were her comments? And I'm not talking about if she found a misspelled word or she didn't like your grammar, which maybe she did.

A. They weren't extensive in any case. To the best of my recollection, I believe there's one sentence in here somewhere that was inserted largely at the suggestion of Ms. Schad. Without trying to be difficult, I really at this point don't remember which it was.

Q. You don't remember what it dealt with?

A. No, I do not.

Q. Fair enough.

MR. LOWERY: That's all I have.

CROSS-EXAMINATION BY MR. PENDERGAST:

Q. Good afternoon, Mr. Oligschlaeger.

A. Thank you.

Q. You indicated in response to some questions from Mr. Lowery that because customers are prepaying or the company is precollecting for these net salvage costs far in advance of when they're incurred, that you believe your mechanism is appropriate to ensure that those amounts that are collected will be there to pay the net salvage

costs when they're incurred. Is that basically correct?

A. That's accurate.

Q. I'd like to try and put that in perspective a little bit. On the other side of the ledger, the utility fronts a tremendous amount of money in order to provide service to its customers; is that correct?

A. They make shareholder investments to provide service, yes.

Q. Right. And would you generally agree with me that what the shareholder fronts to provide service to the customer dwarfs what the company is precollecting from the customer for these net salvage costs?

A. Yes, because most utilities have significantly positive rate base, which means shareholder investment is greater than the customer investment, so to speak.

Q. So for a utility like Laclede, if you look at their regulated base, you would expect their regulated rate base to be larger by many fold than whatever it's accrued for net salvage, would you not?

A. I think that's safe to say as a general proposition, yes.

Q. Okay. Can you tell me why it would be inappropriate for the utility having prepaid out all this money in order to go ahead and provide service on the

theory that some day customers will pay it back, why it's not necessary for those utilities to have some special mechanism in order to ensure that that money will be there at the end?

A. Why is it necessary that that special mechanism be there?

Q. No. Why is it not necessary for them to have a special mechanism to ensure that the customer will be paying that money when it becomes due?

A. That's kind of a broad question. I believe the assumption has been that utility service is a captive kind of monopoly service in which utilities don't have a meaningful choice, and to the extent that they desire to have that service, they will have to be paying rates into your companies on an ongoing basis.

Q. But isn't it true that the Commission has the ability to determine what those rates will be and whether those rates will be adequate enough to provide for a return on that investment?

A. The Commission makes the decision on what an adequate return is, yes.

Q. The utility can't unilaterally go to its customers and say, this is how much I need or how much I think I need and I want you to pay it up, they have to seek Commission approval to do that; isn't that correct?

A. That is certainly true.

Q. And in your view, is the fact that there is a commission there that has the authority to determine what kind of recovery is reasonable sufficient guarantees for the utility that it will, in fact, get a return of and a return on its investment?

A. I think it's accurate to say that utilities can reasonably expect a return on their -- or return of their investment. In terms of the return on their investment, certainly over time most utilities have recovered a return on. Their perception of whether that is adequate or reasonable may be different than what the Commission has ordered. I'm not sure that hits at what you're saying.

In general terms, yes, I believe companies can be able to rely upon the Commission that they will be able to recover their costs, including a return on and of investment.

Q. Okay. And that's for the much larger category of costs that we've been talking about that the utility fronts in order to provide service; is that correct?

A. Yes.

Q. When it comes to the smaller category of costs that we're talking about having been precollected

for net salvage costs, is it your testimony the customer cannot, however, rely on the Commission and its ability to exercise its oversight on how much the utility can collect in order to make sure that they'll be protected for whatever money they fronted?

A. To the extent those funds are not protected and the companies would come back to the Commission and say, help us out, certainly the Commission would have to make a decision or judgment whether that was appropriate or prudent under the circumstances.

Q. So is it your testimony, then, that unlike the case with utilities that you think can reasonably rely on the Commission to ensure that they will recover their investment, the customer cannot rely on the Commission in its general exercise of its regulatory responsibilities and oversight to make sure that they won't overpay for these costs or that once these costs have been incurred, that the utility will actually spend the money for that purpose; is that your testimony?

A. The Commission has general jurisdiction over your operations and how they are conducted, whether prudently or imprudently. That includes cost of removal and net salvage activities.

Q. Yes, and I understand that, and I appreciate that. We both agree with that. What I am

asking you is, you believe it's reasonably appropriate for utilities to assume that because of the Commission's oversight and regulatory powers, that they will recover their investments and that that is a sufficient enough mechanism that nothing further is necessary.

And my question to you is, when you look at the customer and you look at what he has prepaid if you will for recoveries far out in the future, is it your testimony that that same Commission oversight is not sufficient, like it is with the utility's investment, for those customers, that something additional is necessary?

A. I'm still not sure I'm totally understanding. Companies when they are collecting net salvage cost in rates under the standard approach typically invest those monies in utility operations. It's possible they may invest them in non-utility operations.

And under that assumption, those funds themselves will not be used at a later point to pay the actual cost of removal of net salvage activities. Some other source of payment will have to be obtained by the utility in order to make those expenditures.

And it is my belief that given the precollection of costs from customers on an estimated, somewhat speculative basis by the companies under the standard approach, it is appropriate to then ensure that those monies will actually be there and be used for cost of removal activities 20 or 30 years later down the road.

Q. Okay. And your position is that it is not enough that the Commission will presumably still be in business, presumably still be regulating utilities, presumably still have the same authority it has today to determine who gets to collect what. That's not a sufficient protection, like it is a sufficient protection for the utility to get the return of its investment and the return on its investment; is that your testimony?

A. That -- it is my testimony that in that respect, net salvage if it's collected in rates on that matter, should be treated in a somewhat analogous manner to pensions and OPEBs, which are likewise required to be somewhat segregated, with the future cash payments to be paid.

Q. Okay. So the answer to my question would be that you don't believe standard Commission oversight and regulation is sufficient to protect the customer like it is sufficient to project the utility's expectation of getting a return on its investment?

A. My recommendation is that something more is required, and that is what I state in my testimony. It's the segregation of funds.

Q. Because you do not believe traditional

Commission oversight is appropriate or is sufficient?
A. Could be sufficient. I would recommend that additional measures be taken.
Q. It could be sufficient?
A. I cannot predict the future.
Q. Okay. And do you believe in predicting the future that it is relevant and appropriate to review the past and what has happened in the past?
A. In terms of predicting the future, there's not much else to base your prediction on.
Q. In fact, one of the most fundamental conventions of ratemaking is that we look to the past to try and predict the future; is that correct?
A. Yes.
Q. We use historical test years to try and predict the future or to determine what the rates will be when -- or costs and revenues and expenses will be when rates are in effect; is that correct?
A. In this jurisdiction, yes.
Q. Okay. And if we resort to the past in this particular instance for evidence of whether or not utilities have not fulfilled their obligations to pay for the cost of removing facilities that they have precollected funds for, what would that history tell us?
A. I am not aware of any particular problems

in terms of utilities not expending the funds they need to for cost of removal activities. On the other hand, Mr. Fetter's testimony creates the specter of what he calls rate shock in regard to these future expenditures, and that in and of itself, if that's true and that's valid, would lead to perhaps increased concern in regards to the future, as opposed to what our experience has been.

Q. Was it your understanding that his concerns about rate shock were being raised in terms of what might occur under Staff's approach?

A. Well, rate shock would be a concern under Staff's approach. I would think cash flow shock would still be a concern under the standard approach.

Q. Okay. Well, I think that's fair enough, but I'll have to think about it a little bit.

But if we're looking at the historical record, the historical record would essentially tell the Commission that, at least to your knowledge, there has never been an instance since 1913 where a utility has failed under the standard method to provide sufficient funds to pay its net salvage costs?

A. My institutional knowledge doesn't go that far, but as far as my institutional knowledge goes, I'm not aware of any such instance.

Q. Okay. And pursuant to our previous

discussion, do you believe that that is a factor that the Commission should take into consideration in determining whether a special mechanism is necessary?

A. It's certainly an argument that can be and probably will be raised for the Commission's consideration.

Q. My question was whether -- not whether it's an argument. My question was, given our previous discussion about the past being relevant for telling the future or giving us guidance for the future, is it your opinion that that's a factor that the Commission should take into consideration in determining whether a special mechanism is necessary if it goes to the standard method?

A. That's -- they should consider all factors that are relevant, and yeah, I would agree that the past is one of the relevant factors to be considered.

Q. Okay. Let me ask you about estimates, because I'm not clear what Staff's position is on estimates and when they should be used and when they shouldn't be used.

I believe you indicated in response to Mr. Lowery that it is appropriate or it may be appropriate to use estimates when there are cash flow considerations that warrant perhaps a precollection of net salvage costs. Am I remembering that correctly?

A. It is my testimony that what's called the standard approach of cost of removal/net salvage, which does include the use of estimates, could be taken into consideration by the Commission if there are special unique cash flow circumstances.

Q. Let me ask you this: Do you think that the reliability of a particular set of estimates is a factor that should be taken into account when the Commission determines whether to rely on them or not?

A. Whether the estimates are reliable or not?

Q. Yes.

A. Certainly.

Q. Okay. And as I recall, in response to Mr. Lowery, you indicated that you had not done any analysis of Laclede's net salvage estimates; is that correct?

A. That's correct.

Q. And am I to take from that that you have no opinion to offer on the reliability of those estimates?

A. As they specifically pertain to Laclede as compared to other companies, no, I have no opinion on that.

Q. Okay. And do you believe that this Commission, since you think reliability of estimates is a factor that should be taken into consideration in

determining whether to use those estimates, that this Commission should be -- should require that evidence be presented on what the reliability of these estimates are?

A. Certainly.

Q. Okay. Can you tell me where in the record of this case, stretching back five years until today, the Staff has presented evidence demonstrating a problem with reliability of the net salvage estimates utilized by Laclede?

A. I'm not -- I think as I established with Mr. Lowery, I certainly have not reviewed all of the record of this proceeding as it goes back to 1999. In terms of what I have reviewed, I'm not aware of that kind of analysis.

I'm also aware that Ms. Schad has testified that, in general, companies are not able to separately split out the net salvage accrual portion collected in rates compared to the other components of depreciation expense. I think that inability to separate those components would complicate any analysis of past historical accuracy.

Q. Well, are you aware of Mr. Stout's testimony in this case where he has indicated that the net salvage percentage, based on actual review over his many years of preparing and reviewing depreciation studies, has

tended to increase over time?

A. I'm aware of his testimony in that respect, yes.

Q. Okay. Do you have any reason to doubt that testimony?

A. I have no reason to doubt it.

Q. Okay. And assuming that that testimony is true and the Commission believes that testimony to be true, would that suggest that net salvage costs under the standard method, knowing what you know about the standard method and how it operates, has tended to understate net salvage costs or underestimate net salvage costs?

A. Based solely on what -- that is what Mr. Stout is suggesting. I don't have any separate base of knowledge to determine whether that is true or not. I don't know whether in the past it has undercollected.

Q. Okay. Well, let me ask you this: In your opinion, if the Commission were to conclude that Mr. Stout is correct and that the standard method tends to provide an estimate of net salvage costs which is estimate -- which is conservative and which, if anything, tends to understate the level of net salvage costs that will be actually incurred, under those circumstances, if the Commission were to make those conclusions, would you feel comfortable recommending to the Commission that they

continue to use the net salvage estimates derived under the standard method?

A. No, because that would assume that the future will be -- will follow the same path as the past, which obviously no one, Mr. Stout, myself or anyone, can determine.

Q. So is it your position, then, that the Commission just should not use any estimates at all because we can't tell for certain what the future is? Is that what your position is, the Staff's position is?

A. Well, I think as I stated earlier, my position is that estimates can be used as long as they are reasonable and capable of accurate -- can be -- let me restate this.

Estimates can be used in the ratemaking process. I would recommend they not be used unless there is evidence that they are -- can be considered reasonably accurate.

Q. Okay. And you've done no analysis of whether the estimates utilized by Laclede for determining net salvage are reasonably accurate or not?

A. I've done no analysis of Laclede's specific information.

Q. And you can't point me to anything in the record to your knowledge, based on your review of it, that

would demonstrate that they're not reasonably accurate?

A. Again, I haven't reviewed all the record, but I have not seen that kind of thing in the evidence.

Q. Okay. Well, we've talked in terms of estimates that are used in other areas. I think you mentioned pensions.

A. Right.

Q. Can you tell me whether net salvage estimates are more reasonably accurate than the estimates that are used in calculating pension expense?

A. That's kind of an apples to oranges comparison. I cannot say that. Of course, the ratemaking setup for pension expense is in part determined, I think, by federal statutes in terms of trust funds being set up. So there are other factors that play with pensions that are not present with net salvage.

Q. Okay. But you believe it's appropriate to use estimates in the pension area?

A. Again, I believe to some degree federal law would implicitly or explicitly require that. There I go being an attorney again. So I see -- yeah, I see that as a separate situation than net salvage.

Q. How about in terms of the estimates that are used in the DCF model for calculating a return on equity, do you know what those estimates are?

A. Not in any detailed knowledge, no.

Q. Well, how about in a superficial way?

A. I have a lot of superficial knowledge. I believe financial analysis look at estimates of going out some small short period of time into the future of estimates of earnings and dividends, payouts and so on, but that's very superficial.

Q. Do you know how long that period of time is?

A. I'm going to say one or two years, but I don't have a lot of confidence in that.

Q. Do you know how accurate those particular estimates are?

A. I don't have an opinion. It's easier to make an accurate estimate over one or two years, as opposed to 20 or 30 years, just in general.

Q. Okay. But you've done no analysis to try and determine the reliability of those particular estimates used for that pick purpose versus the reliability of net salvage estimates?

A. No, I have not.

Q. Okay. What kind of analysis have you done if you want to go to a longer horizon of the reliability of estimates used to determine service lives?

A. Can you repeat that?

Q. Yes. What can you tell me about the reliability of estimates used to determine service lives?

A. What I can tell you is that they are based upon an analysis of past historical record which leads to the creation of something called survivor curves on which these rates are based.

Q. Okay.

A. I've basically told you the extent of my knowledge on that.

Q. And would that also be true of net salvage estimates?

A. If they were based on an examination of the past historical record?

Q. Yes.

A. According to what I know, yes.

Q. Okay. What makes service -- estimates of service lives more reasonably accurate or reliable than estimates of net salvage costs?

A. Well, when considered in isolation, I'm not sure that there would be a difference between an estimate of net salvage, as opposed to service life. Of course, the net salvage calculation has two different unknowns, which is the actual cost to be incurred as well as the timing of the cost. With depreciation expense it's only the service life that is unknown, the cost being known up front. So in terms of that component of depreciation, I think it's logical to assume that can be somewhat more reliably estimated than the net salvage piece.

Q. And when you say assume, is that all it is is an assumption, or do you have something that you have studied or read that demonstrates that to you?

A. Logically, if I have to estimate a future cost and for one cost I have one unknown factor and for another cost I have two unknown factors, logically it would seem I have more risk of inaccuracy with the calculation that involves two unknown factors.

Q. Does that assume that the range of uncertainty for those two factors are the same?

A. I don't know that I made that assumption.

Q. Well, you can have something that has two unknown factors and another thing that has one unknown factor and the range of uncertainty on the thing that has one unknown factor can be substantially greater, can it not, than the one that has two unknown factors?

A. My implicit assumption was that there would be equal risk of uncertainty.

Q. Okay. And do you have any evidence to confirm that?

A. While I believe it is logical, I don't have any empirical evidence in front of me today to say this is it, this justifies that.

Q. Okay. Would it be fair to say, then, that looking at the record as a whole, when you talk about reasonably accurate estimates and whether net salvage estimates qualify for that characterization, you don't have any empirical evidence and you have done no study to make a determination of whether they do or do not?

A. Whether they do or do not what?

Q. Whether they do or do not qualify as reasonably accurate estimates?

A. That's based upon my general understanding of how the process works. In terms of have I done an analysis that I can provide you in the form of work papers to justify that, no.

Q. Okay. And you've certainly not done the kind of analysis that Mr. Stout has done and has reflected in his testimony; is that correct?

A. That's correct.

Q. Okay. Let me ask you, you mentioned something about incentives, and that by expensing net salvage utilities have a greater incentive to reduce costs; is that correct?

A. That's what my testimony states.

Q. Okay. Let me ask you this: If the Commission were to go ahead and expense rather than capitalize the capital budgets of utilities, for example, if the $50 million that Laclede spends every year or thereabouts on its capital programs, the Commission were to say, I want to expense that now and I want to just put $50 million on an ongoing level in rates to pay for that, would that give Laclede a greater incentive to reduce those particular expenses?

A. Yes and no. Yes in the sense that between rate cases Laclede would want to beat the historical level or the current level reflected in rates. No in the sense that perhaps there might be an opposite incentive in a rate case type proceeding to inflate that level of capital expenditures.

Q. That same yes and no applies to your net salvage example as well, does it not?

A. Let me think about that. Yes, as it generally would apply to all expense items.

Q. Okay. And, you know, given the fact that it would give the utility a greater incentive to reduce its -- or at least as much of an incentive to reduce that particular aspect of its costs as you say it would have to reduce its net salvage costs, would it be your recommendation that the Commission expense those capital items and allow Laclede to recover an ongoing level of $50 million in rates?

A. Well, no, and there are many reasons why that would not be appropriate.

Q. Please tell me what they are.

A. First of all, the utility must -- or the Commission must consider a number of different goals or policies in terms of setting its rate policies. For capital items, intergenerational equity is a consideration, as it is with net salvage. I'm not going to say that shouldn't be at all a consideration. And obviously long-term assets are placed in order to provide service for many years, hopefully, and those rates, it is fair that those rates be set to recover those costs over the period of time those assets are in use, are in use.

In terms of a practical matter, because utility construction budgets at least some of the times for some of the utilities tend to vary a lot from year to year, it simply wouldn't be practical from that to set rates based upon year-to-year construction budgets.

To use the extreme example, in the early 1980s when UE and KCPL had nuclear units, you might increase rates by 1.5 billion one year and decrease it back the next year. That I don't think would work very well.

Q. And is that because it would -- it would lead to an inappropriate recovery of costs from the

standpoint that you would have spikes and that customers might have to pay rates based on those spikes when, in fact, on an ongoing level costs went down so they'd be overpaying for service? Is that the kind of concern you're talking about?

A. That would be part of it.

Q. And that would be a bad thing? That would be something that from a policy standpoint you would think is unfavorable?

A. In general terms, yes.

Q. Okay. And is your concern about that unfavorable aspect of it based solely on what the magnitude of the costs are or do you believe that's unfavorable even if the costs are smaller?

A. Well, and again, particularly in terms of the capital budget being expensed, I think that's wrong in theory, as well as being wrong in practice or in its practical impact. So even if your construction budget was level from year to year, I do not think it would be appropriate to treat them as being expensed.

Q. Okay. And I understand that point as well, but from the standpoint of the volatility and the expenditures and not wanting to have a mismatch between what's being collected from customers and what's actually being incurred, is that a concern that is -- that you're

concerned about only because of the magnitude of the construction budgets or just in general?

A. If I understand your question, I think the answer is in general.

Q. Okay. And let me ask, I mean, is it your testimony that under the Staff's approach the utilities will be made whole for their net salvage costs?

A. For their cash outlays, yes, though as I stated earlier to Mr. Lowery, if you treat an item as an expense, there's always the chance you may under-recover the actual level in expense compare to what you outlay in cash or over-recover it, there may be those fluctuations.

Q. So your testimony would be that you'll be made whole except for those circumstances where you won't be?

A. Well, you'll be made whole in the same way you're made whole for your other expenses.

Q. Okay. Well, let's talk about the way we're made whole for other expenses. You know, if there is volatility in a particular expense item, just like you were painting as far as volatility in the capital budgets and expenditures, it's not unusual to have a higher level of expense in one year and a lower level in the next; is that right?

A. That's correct.

Q. Let's say a utility's got net salvage costs of 5 million in year one and 9 million in year two and 5 million in year three. Under the approach that Staff is proposing, what level of net salvage costs will the utility be allowed to recover in its subsequent rate case?

A. In general terms, when you have a volatile level of expense, it will be appropriate to consider use of a multi-year average for that expense item.

Q. Okay. So let's say we use a multi-year average. I've now incurred 5, 9 and 5. Would you agree with me that's $19 million?

A. I can agree with that.

Q. Okay. And first of all, if the rate -- if the net salvage amounts have been set at 5 million in the prior case, okay?

A. Uh-huh.

Q. Will I ever recover that difference between 5 million and 9 million in year two?

A. If you didn't file a rate case, no.

Q. Okay. So let's say that I filed a rate case immediately after I had that 9 million.

A. Uh-huh.

Q. Will I be allowed to go back and recapture that 9 million?

A. You're say never allowed to recapture that shortfall or over-recovery in expense, but maybe that's too broad a statement. In general terms, no.

Q. So that's an instance where I'll be eating that $4 million, right, the utility will be?

A. In that particular case.

Q. And that won't exactly make me whole, will it?

A. Well, no, but in the future there may be cases where you will have less net salvage expense than what is the level set in rates.

Q. Okay. Let me ask you -- well, may, may not, right?

A. May, may not.

Q. Okay. But in any event, the one thing we know is that it's likely that the utility is not going to go ahead and recover whatever net salvage costs it has, no more, no less, under the expense approach; isn't that correct?

A. Consistent with traditional ratemaking, that is correct.

Q. And it's possible that a utility may have to absorb a significant amount of those net salvage costs; isn't that correct?

A. That is possible, as well as the possibility of over-recovery.

Q. Let me ask you this: And do you generally favor creating circumstances where there are possibilities for over and under-recovery? Is that a good thing in your opinion?

A. Let me answer it this way: I believe regulatory lag provides good incentives for a utility for efficient operations, and as part of regulatory -- the way regulatory lag works, that would incorporate both under-recoveries and over-recoveries of expenses or other rate elements compared to the level set in rates.

So the possibility of winners or losers, I think it's expressed in testimony, under or over-recovery does not bother me at all. I believe it has some efficiency benefits in the overall regulatory scheme.

Q. Okay. It doesn't bother you at all, but it does begin to bother you when the dollars are really big, right? Didn't you just have that discussion with the capital budget and your comments about the spikes and how, you know, you would lead to a mismatch between costs that are being incurred and what's being included in rates? There it bothered you, I thought, didn't it?

A. Well, probably should bother the utility, too, but my problem with expensing capital items is 95 percent theoretical and 5 percent practical, just to put that in perspective.

Q. I appreciate that, but I thought you gave me as one of your major reasons that capital budgets vary significantly, that there might be a significant spike, and that that would lead to a mismatch between actual costs and what customers paid. Now, is that a concern or not a concern?

A. Certainly it's a concern that probably would be greater with capital items because those are -- those are where the big dollars are.

Q. And would that be unfavorable from your standpoint? Would that be an unfavorable policy result?

A. To what, to expense?

Q. To have those big disparities between what's being incurred and what's being collected from customers.

A. As it relates to capital items, yes. As it relates to expense items, that's something that the company can accommodate through a rate filing to try to cure, if I understood you correct.

Q. So it's a concern when it comes to capital items and it's not a concern when it comes to expense items?

A. When there's great -- okay. Somewhere along the line I may have lost the train of where you're going, but if there's an item of expense that is highly volatile and subject to spikes, we have means within the rate process to try to accommodate that through, among other things, use of multi-year averages and so on.

Okay. So does it -- would it bother me that a utility's expenses spike that way? In general terms, normally they don't, but individual items of expense could, and we can accommodate that reasonably in the rate process.

Under the hypothetical situation where we expense the construction budget or capital items, that's less easily accommodated because of just the magnitude of the dollars involved.

Q. And how do you intend to accommodate that concern when it comes to net salvage costs?

A. Net -- well, net salvage costs to the extent they show a lot of volatility, we would, as I think we currently do, consider the use of multi-year averages to reflect that amount in rates.

Q. So in your view, the use of multi-year averages, even if under the example we gave it results in the utility incurring a not insignificant level of costs, it's in your view a sufficient remedy for that problem?

A. The fact that the utility may have to eat some portion of those costs --

Q. Yes.

A. -- under that approach?

Q. Yes.

A. Yes, recognizing the opposite possibility that the company may be able to over-recover those costs.

Q. Okay. Let me ask you about the over-recovery. You talked about regulatory lag. That basically means that there's usually a period between the time you incur costs and it's recognized in rates or some average is recognized in rates; is that correct?

A. I would agree that that -- well, between the time of a change in the company's financial picture and the time that is reflected in rates. It doesn't have to be an increase in expense. It could be opposite. Anything that impacts your financial levels that impact rates at the time that they are actually reflected in rates is regulatory lag.

Q. Okay. And can you tell me what the impact is on regulatory lag -- and just assume for me that you have a company that is generally experiencing an increase in net salvage costs over time, that they trend upwards. Under those circumstances, is use of historical averages, all else being equal, almost certain to result in an under-recovery of costs?

A. If you have a general trend upward in a cost, then depending upon the data that the Staff or the auditors would review, we would also, of course, consider use of last known measure of such an item. Now, it does get more complicated if you have a general trend upwards, as well as some volatility. Okay. That makes it a little bit more difficult.

Q. Well, let's assume that you use the last year of the three years. Okay? But you still have this general trends upwards. Okay? Isn't it fair to say that, under those circumstances, use of an historical expense related item to set a level of an average that's based on the lower part of the trend will result in an under-recovery, all else being equal?

A. All else being equal, yes.

Q. You indicated that there were basically three sources of cash flow, I believe, is that correct, one being return on equity, the other being deferred taxes and the third being depreciation in your testimony. Does that sound --

A. Customer supplied cash flow, yes.

Q. Customer supplied cash flow. And I think we've discussed that Staff's method tends to reduce cash flow, at least --

A. Compared to the company's method, yes.

Q. Right, compared to the standard method. And I think you would generally agree that a reduction in

cash flow for whatever reason is perceived negatively by rating agencies as opposed to certainly maintaining cash flow or increasing cash flow; would that be correct?

A. I would agree with that.

Q. And in looking at the three sources you've talked about, return on equity, would the same thing be true there? If you're getting less cash flow from your return equity, is that something that would be viewed unfavorably by rating agencies?

A. I'm quite confident rating agencies prefer higher returns on equity than lower returns on equity.

Q. So the extent you have lower returns on equity, that's going to be viewed as an unfavorable development as well; is that correct?

A. By the credit rating agency, I believe so.

Q. Okay. Can you tell me, since you pointed to these three sort of legs of the cash flow stool, where the Staff is in general terms with respect to its return on equity recommendations and how they compare to other jurisdictions?

A. I was involved in the current Missouri Gas Energy rate proceedings, so my knowledge is pretty much limited to the circumstances in that proceeding. I believe the Missouri Staff recommended return on equity in that proceeding was portrayed by MGE as being significantly below recent averages of returns granted by other jurisdictions.

Q. Well, do you have any reason to dispute that?

A. No.

Q. Okay. And isn't it true that, generally speaking, when it comes to the return on equity component that can also generate cash flow, that Staff has generally made recommendations that are below averages?

MR. SCHWARZ: I'm going to again inquire as to how this line of questions talking about return on equity has -- is tied in to the net salvage -- limited narrow net salvage issue in this case? I'm not sure that it's going to lead to any discovery or rather admissible evidence.

MR. PENDERGAST: Just to respond to that, it was Mr. Oligschlaeger that went ahead and in response to what we had talked about, the impacts of depreciation on cash flow and all the negative financial impacts flowing from that had said, wait a minute, you've got to look at what you get from return on equity, you've got to look at what you get from deferred income taxes. So I think I want to look at it.

Anything further, Tim?

MR. SCHWARZ: I think it should be limited to the discussions of return on equity in this case. I don't see -- I mean, he's identified it as another source of cash flow, but if -- but there's nothing material left in this case. There's no issue in this case on other sources of cash flow. It's just not an issue.

MR. PENDERGAST: Well, I think it is. I mean, I think it's an item that the Commission needs to take into consideration, particularly since it's been raised by Staff. And I think they need to take it into consideration because we have said that this depreciation policy has an adverse impact on our cash flows and on our financial condition, and we have had a Staff witness come in and say, oh, but you've got return on equity revenues to help with you that cash flow, no need to worry.

And I want to go ahead and probe that and see whether or not that's an additional source of negative development when it comes to our financial situation.

MR. SCHWARZ: But the only cash flows that are -- return on equity that are factors that are relevant to this issue in this case are the returns on equity that the Commission set in this case.

MR. BYRNE: Since there is no ALJ to rule on the objection, shouldn't he just answer the question?

MR. SCHWARZ: Well, I'm considering whether to direct him not to answer. All right?

MR. LOWERY: I don't believe it's appropriate for a lawyer to direct a witness to not answer a question based on a relevance objection in any deposition.

MR. SCHWARZ: It's not a relevance. It's a materiality.

MR. LOWERY: Or a materiality objection. It's not privileged.

MR. SCHWARZ: I pays my money and I takes my chances, and --

MR. LOWERY: I was going to suggest that you make your objection and then he answer the question, and if you want -- if it becomes an issue in the proceedings in terms of whether the question and answer used, then the ALJ can rule on the objection.

MR. SCHWARZ: We've -- go ahead. Answer the question.

THE WITNESS: Can you please repeat it?

MR. SCHWARZ: Read it back for him.

THE REPORTER: "Question: And isn't it true that, generally speaking, when it comes to the return on equity component that can also generate cash flow, that Staff has generally made recommendations that are below averages?"

THE WITNESS: And when you say below

averages, I assume you mean some measurement of the average return on equity findings of the jurisdiction s a whole?

BY MR. PENDERGAST:

Q. Yes.

A. Again, based upon my knowledge of the return on equity issue in the MGE rate case, there was evidence submitted that since the late 1990s that Staff's recommendations have tended to be below those kinds of national averages.

Q. Okay. And assuming that that's true, then wouldn't it also be true that, all else being equal, the amount of cash flow that utilities receive from that return on equity component you mentioned in your testimony, to the extent those recommendations have been reflected in lower Commission-authorized returns, it would be less than what other utilities on average are receiving?

A. I think that follows, yes, that the higher the return on equity granted, or actually the higher the return on equity earned, the more cash flow to the utility.

Q. And you recall a series of questions that you had with Mr. Lowery that talked about if you're getting less cash flow from depreciation than utilities in

other jurisdictions are getting, that you're going to be viewed less favorably by investors at least for that factor than utilities in others jurisdictions that are getting more cash flow?

A. Well, my assumption is, and I think it's reasonable, that investors are interested in return on equity determinations by this Commission and all commissions.

Q. And to the extent that they're lower than average, that would be a factor that, all else being equal, investors would tend to view negatively?

A. I believe that is logical.

Q. And would it also be logical that they would tend to view the circumstance even more unfavorably if you were getting less cash flow from the return component in addition to less cash flow from the depreciation component? Does it have a cumulative effect?

A. I think they would look at all factors impacting the cash flow, the two that you mentioned. There may be others, or there are others as well that they would examine in reviewing cash flow .

Q. But certainly they would tend to go ahead, would you agree, as a matter of logic, that they would tend to view more unfavorably a negative development or negative cash flow impact from two of those cash flow

producing areas than they would just one?

A. If there is less cash flow to the company as a result of two different regulatory decisions or policies than there would be just looking at one in isolation, yes, they would look at that more negatively.

Q. Okay. And in your testimony, I think you said the Commission should not, and I don't want to put words in your mouth, but essentially guide what it does solely by what rating agencies might think. Is that generally correct?

A. Yes.

Q. But do you think it's a factor they should take into account?

A. Rating agencies represent the debtors of your companies who are one of the interest groups and legitimate interest groups whose needs or whatever should be taken into account.

Q. But do you think they should take it into account for more reasons than just trying to look out for what the bondholders of Laclede may be -- may be experiencing? In other words, should they be concerned about potential impacts on your cost of capital?

A. That is a legitimate consideration.

Q. And that's a consideration that flows to a concern for the ratepayer potentially as well as for the

debtholder; is that correct?

A. That's correct.

Q. Okay. Let's talk about deferred income taxes a little bit. Is that a situation where the customer basically pays the utility a higher amount in rates for taxes at a given point in time than what the utility's actual liability for taxes is?

A. Yes.

Q. Okay. Now, why does that arise and why does that happen?

A. That arises because utilities are -- companies in general are allowed to take deductions for certain costs currently, speaking in general, than what they reflect on their books as current expenses, which means their taxable income is lower than their book income. But rates, again in general, are based upon book net income. Income tax expense in rates is based upon book net income. Therefore, they receive higher income tax expense rates than what the IRS and the State, whoever actually bills them for, so to speak.

Q. Okay. But why on the regulatory level do you recognize the higher book one, rather than the actual tax bill one?

A. In many cases it is because the current law or the Internal Revenue Code requires that we do so.

Q. And why does it require that you do so?

A. My general understanding is to provide a source of funds for investment for utilities. I believe that's the stated or the intended purpose.

Q. So to your knowledge, some policy determination has been made by somebody that's reflected in the tax codes or elsewhere that providing that additional cash flow to the utility for investment purposes is a worthwhile or good thing?

A. I think apparently it was a good policy decision to allow that -- those monies for investment purposes.

Q. Okay. How big can this deferred tax item get?

A. For major utilities, we're talking millions of dollars. It's a significant reduction to most utilities' rate base.

Q. How does it compare to net salvage cost?

A. Well, I think you're comparing an expense to a rate base item. A company's balance of deferred taxes it has received over time I think generally it could be expected to be much larger than its annual net salvage cost.

Q. Okay. And can you tell me, since customers are paying this amount in advance, okay, what specific

mechanisms have been established to make sure that when the tax liability is higher than what you're collecting in rates, the money will be there to pay Uncle Sam?

A. I don't think there is any specific measures the Commission has taken. I would imagine the IRS and the State have their own interest in that question in making sure those monies are available.

Q. Well, I guess what I'm asking you, has -- well, if they can't be collected from the utility or if they spent that, they can spend that money on something else, couldn't they?

A. Certainly.

Q. Just like, you know, your concern about spending net salvage on something else, right?

A. Well, it's available for investment for any purpose.

Q. Okay. Available for any purpose. And then if they have to go ahead and pay that amount at some point in the future, they may have to borrow it, right?

A. They may have to borrow it, or if there's a crunch, they may decide not to make the expenditures for those activities that they otherwise would have.

Q. Okay. Just like they could with net salvage cost, right?

A. I'm sorry. I was talking about their net salvage cost.

Q. Okay.

A. I don't think you have the leeway not to pay taxes that are due.

Q. Well, you're under a statutory obligation to provide safe and adequate service, right?

A. That's correct.

Q. That's a legal obligation, too, isn't it?

A. I believe -- well, I don't know. It's my understanding that that is. I'm not an attorney.

Q. Well, but your point is that paying your tax bills is also a legal obligation, right?

A. And you will probably go to jail if you do not do so. Not you individually.

Q. I appreciate that advice.

But there are penalties for not fulfilling your statutory and commission duties as well; is that correct?

A. That is correct.

Q. And I guess what I'm trying to ask here is, for this what you think is a larger item where customers are prefunding something, can you explain to me why Staff under those circumstances has not proposed some sort of segregated account that those monies should flow into so that they'll be available later on when those tax

liabilities are greater than what's being plugged in rates?

A. Okay. You do not have legal discretion not to pay the incomes taxes that are payable when they are due. It is my understanding that there is some discretion in regards to the level of cost of removal activity a utility can undertake in most cases. Now, there are other -- nuclear decommissioning would be a contra example of that. But if there is a serious crunch, utilities have the option of going out and borrowing, obviously borrowing the money or getting it from equity sources.

But they also have the option of ramping it down, we won't spend that much. We have the option to leave this asset in place as opposed to fully remove it or whatever. There's a level of discretion with cost of removal activities than there is in income tax payments.

Q. Okay. And could you give me some examples of what that level -- what those discretionary items are?

A. Just in general, it is -- for example, most of the items for which utilities claim cost of removal expense in rates through the standard method are not accounted for for financial reporting purposes as liabilities, which means that they are not considered to be future obligations of the utility, okay, from a GAAP, from a financial reporting perspective. Some of the activities are, but most of them are not.

And that means that for financial reporting purposes, investors are not to assume that you will -- that you have a legal, or actually I think it goes beyond legal, an obligation to incur those costs in the future. Okay. That's -- that's what I'm talking about in general.

Q. So is your main concern, then, about whether or not you have a segregated fund, not whether the money will actually be available, but instead whether or not the utility will actually have to spend it on something? Is that what your concern is?

A. Well, no. My concern is that the money be available both to meet your future obligations for cost of removal, and that would create, I guess, a more beneficial atmosphere in terms of making sure the full level of cost of removal activities are taken out. Again, looking at Mr. Fetter's testimony where he raises the specter of sizeable and sharp increases in the future regarding those cost items.

Q. So your concern is, you want to make sure the money's available so that the utilities will be encouraged to spend it on those particular items; is that correct?

A. Well, if you do not need to spend it, and obviously the prudence of your future actions, I mean, utilities should determine whether they need to spend the money or not. But if you need to spend it, the money is there. If you don't need to spend it, then I guess the money would be segregated for future uses or maybe it can be refunded back. I don't know the mechanisms.

Q. I guess I'm just trying to understand, you know, the dynamics at work in that answer compared to the dynamics at work in your answer that said it's better to expense things and not provide for the money automatically being there so utilities will have an incentive not to spend unnecessary amounts when it comes to cost of removal that's ongoing. Can you reconcile those two for me?

A. First of all, it was not my testimony that it's better to expense things either in general or other. Capital items should be treated as capital items. Expense items should be treated as expense items in general.

At this point I'm kind of at a loss as to how to continue. I'm not sure exactly what your confusion is, what you're asking me.

Q. Well, I'm just trying to get at why you think a fund is necessary when it comes to net salvage costs but not when it comes to deferred taxes, and I thought you answered you thought one was more discretionary, namely incurring net salvage costs, than taxes. And in light of that, you thought it would be

better to have the money available there so that the utility would have no question about spending it on that, but then when it came to justifying your expense approach to net salvage, you said it would be better not to guarantee that the money is there because it acts as an incentive if you have a ceiling that the utility can spend. I'm just trying to get ahead where I can solve these two thoughts. They seem to be inconsistent to me.

A. Okay. Under an expensing approach in which you just recover the amount of your capital expenditures, as I think I explained before, that can have both positive and negative incentives to the company depending on where they are in the rate case cycle.

Okay. What my -- one of my concerns in terms of the segregation of funds approach is simply that the money be there for the intended purpose, because we assume that regardless there will be some level of net salvage activity you will have to undertake in the future, and the customers will be asked by you under the standard approach to significantly prefund that, yet at the same time those funds will not be there under the standard cash flow use that the utilities make of these precollections in rates.

I believe it's better public policy in general if an expense is prefunded, as it is for nuclear decommissioning, pensions and OPEBs, and as you are asking that it be for net salvage, that some sort of segregation or safeguarding of those funds be there so that they are used for their intended purpose.

Q. Okay. Let me ask you some questions about that particular concept.

MR. SCHWARZ: I'm ready for a lunch break.

(AN OFF-THE-RECORD DISCUSSION WAS HELD.)

BY MR. PENDERGAST:

Q. Utilities also borrow money from third parties, right? They go out in the capital markets, they issue debt, they -- they also get investments in the form of equity; is that correct?

A. Yes.

Q. Okay. And do you know whether or not utilities need to come before this Commission and request authorization to issue securities?

A. My general understanding to that is yes, but I'm not sure that's a blanket requirement or not.

Q. Okay. But assuming it's at least a requirement with respect to some utilities under some circumstances. And is it also your understanding that when a utility does that, it needs to specify what utility purposes the proceeds generated by those debt or equity issuances will be used for?

A. I don't know they're required to. The applications I've seen generally make somewhat general statements as to what the funds are intended to be used for.

Q. Do you know whether the Commission needs to find what they will be used for?

A. I do not know.

Q. Okay. Do you know whether Staff has expressed a concern before in financing applications regarding making sure that if the Commission authorizes debt and equity be issued, that those amounts will actually be used for utility purposes?

A. I think it's reasonable that they would have that interest. Again, I'm not sure to what extent that actually occurs.

Q. Okay. And do you know whether or not Staff has proposed various conditions to address that concern about whether this money that is being authorized by the Commission and it's being at least paid for, the debt cost and that sort of thing, a return on equity by the customer, assurances it will be used for those purposes?

A. I don't have firsthand knowledge. To the extent the Staff has those concerns, it is common we will seek conditions on those points.

Q. Okay. And do you have any opinion as to

whether or not those conditions are sufficient assurances that the money will be used for what its intended purpose was?

A. Because I don't have firsthand knowledge of the conditions, no, I do not.

Q. You did not evaluate those conditions in determining what conditions you wanted to come up with or thought you should come up with in terms of assurances that the amounts that were being paid by customers for net salvage costs will actually be used for that purpose?

A. No, I did not.

Q. Okay. Do you have any opinion as to whether that might be something that is worthwhile to examine as you further develop your approach to this area?

A. More knowledge is generally better than less knowledge in terms of any ratemaking recommendations. So I think I can agree in general, yes.

Q. I appreciate you going out on a limb.

A. Not all Staff members agree with that.

Q. You mention in your testimony the ISRS mechanism.

A. Yes.

Q. Do you know what portion of Laclede's capital expenditures that applies to?

A. In general terms, it applies to certain expenditures, I guess generally speaking infrastructure replacement, relocates, those non-revenue-producing capital additions, I believe, in general.

Q. **Do you know offhand what portion of Laclede's annual budget those expenditures would make up?**

A. No.

Q. **Okay. Do you know even with an ISRS whether there is a lag between the time expenditures are made and they're recovered in rates?**

A. I believe they have to be actually in service before the ISRS picks them up. So there would be some time lag.

Q. **Do you know what the processing time for an ISRS is?**

A. Not right off the top of my head. It's somewhat accelerated, a few months. That's about as specific as I can get.

Q. **Can you tell me -- you indicated that you supported Staff's removal of net salvage from the depreciation formula and its treatment as an expense; is that correct?**

A. Yes.

Q. **As opposed to what Mr. Adam had recommended in this proceeding?**

A. Well, again, I think substantively there is no difference. I think it's probably more straightforward if we just treat it as an expense, like other kinds of expenses where we look at historical averages, test year amounts and so on.

Q. Well, there's no difference other than you recall the discussion we had about being made whole?

A. Yes.

Q. Okay. Do you know if it was part of the depreciation rate and continued to be one whether that particular concern would still remain?

A. If net salvage levels were reflected in the depreciation rate?

Q. Yes.

A. To be honest, I have not thought of that, but that's possible.

Q. And if that was an impact of taking it out, would you view that as a substantive difference between the two?

A. It's possible.

Q. Would you agree with me generally that the only -- well, strike that.

The $50 million that Laclede spends every year on its capital budget is known and measurable; is that correct?

A. Not when it's a budget. After it is placed in service.

Q. Excuse me. That Laclede actually spends. Let's say they spent it. You're looking back at the prior year. You've got all the records. Is that a known and measurable amount?

A. Yes.

Q. Is a service life estimate a known and measurable amount?

A. In and of itself, no.

Q. Do you also support as part of removing net salvage from the depreciation formula then amortizing the difference between what has been collected under the standard method or theoretically collected under the standard method and what would have been collected under the Staff's method?

A. That's not something I've really considered, and I don't have an opinion on whether that would be appropriate or not.

Q. Okay. Would you generally agree with me that depreciation commences the moment you put a piece of property in service?

A. It's not necessarily the moment, but yes, it's instan-- more or less instantaneous.

Q. More or less?

A. Yes. You might wait 'til the end of the month, but --

Q. Yeah. But it's pretty contemporaneous?

A. Yes.

Q. And to the extent that you're accruing for net salvage costs, does the traditional approach and the traditional way of tracking those accruals assume that those accruals began immediately?

A. Yes.

Q. Would you necessarily be recovering anything from your customers immediately --

A. No.

Q. -- for those net salvage costs?

A. No. You would have to wait for the next rate proceeding.

Q. And for a typical gas utility, that wait can be anywhere from four or five months to two or three years; is that correct?

A. That's reasonable.

Q. Okay. And at that point you actually start to collect some of that net salvage from your customers, is that correct, under the traditional approach?

A. Yes.

Q. And just because you have rates in effect that reflect that net salvage level after six months or two years, it doesn't mean you'll necessarily collect that actual amount, that's going to depend on various circumstances, weather and so forth and so on; is that correct?

A. That's correct.

Q. Okay. Under those circumstances, if it comes time to amortize back amounts that have presumably been collected from customers in the past, in your view, do you need to take into account this lag where it wasn't actually collected from customers and you need to take a look at whether or not once it was included in rates it actually got collected from customers?

A. Again, that's a question I haven't thought about. In terms of your hypothetical scenario, there are also cases where companies continue to collect depreciation expense in rates for items of plant they they've retired.

So I think you would have to look at that whole picture to determine what the overall shortfall, if any, was before you would even make that kind of determination.

Q. Would you as a general proposition be comfortable returning to customers something that was never collected from them?

A. Well, as a general proposition, we don't attempt to set rates based upon measurements of when costs were collected in rates versus when they weren't collected in rates. That's a difficult determination, and ultimately that's determined by your overall return on equity, achieved return on equity. A company can be earning sufficiently, and at the same time they are adding plant and increasing its depreciation expense. You have to expand your analysis to look at were you actually recovering all your costs.

Q. Okay. So as a general proposition, you would feel comfortable returning to customers something that you never collected from them?

A. Well, again, I think the depreciation reserve would also reflect collection amounts in rates which you were no longer booking as an expense.

Q. Well, let's say you took all that into consideration and what you came up with was something that showed that a significant portion of this accrual amount was never collected from customers. Let's just assume that that's what you found. Under those circumstances, would it be your testimony that that should be returned to customers?

A. Again, I have not specifically looked at these kinds of amortizations, and I cannot express an opinion as to whether that would be appropriate or not.

MR. PENDERGAST: Okay. That's all I've

got. Thank you, Mr. Oligschlaeger.

MR. LOWERY: Thank you.

(PRESENTMENT WAIVED; SIGNATURE REQUESTED.)

CERTIFICATE OF REPORTER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

I, KELLENE K. FEDDERSEN, RPR, CSR, CCR, and Notary Public within and for the State of Missouri, do hereby certify that the witness whose testimony appears in the foregoing deposition was duly sworn by me; that the testimony of said witness was taken by me to the best of my ability and thereafter reduced to typewriting under my direction; that I am neither counsel for, related to, nor employed by any of the parties to the action to which this deposition was taken, and further that I am not a relative or employee of any attorney or counsel employed by the parties thereto, nor financially or otherwise interested in the outcome of the action.

____
KELLENE K. FEDDERSEN, RPR, CCR
Notary Public, State of Missouri
(Commissioned in Cole County)
My commission expires 3/28/05.

SIGNATURE PAGE

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

I, Mark Oligschlaeger, do hereby certify:

That I have read the foregoing deposition;

That I have made such changes in form and/or substance to the deposition as might be necessary to render the same true and correct;

That having made such changes thereon, I hereby subscribe my name to the deposition.

I declare under penalty of perjury that the foregoing is true and correct.

Executed the 22nd day of September, 2004, at Jefferson City, Missouri.

Mark Q. Oligschlaeger
MARK OLIGSCHLAEGER

Notary Public:
Sharon S. Wiles
My commission expires:

SHARON S WILES
Notary Public - Notary Seal
STATE OF MISSOURI
COLE COUNTY
MY COMMISSION EXP. SEPT 11,2006

ORIGINAL

KF/Mark Oligschlaeger
RE: Laclede Gas Company/GR-99-315

ERRATA SHEET

Witness: Mark Oligschlaeger
In Re: Laclede Gas Company/GR-99-315

Upon reading the deposition and before subscribing thereto, the deponent indicated the following changes should be made:

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Reporter: Kellene K. Feddersen, RPR, CSR, CCR

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September 6, 2004

THOMAS R. SCHWARZ, JR.
Mo Public Service Commission
P.O. Box 360
200 Madison Street
Jefferson City, MO 65102

In Re: Laclede Gas Company/GR-99-315

Dear Mr. Schwarz:

Please find enclosed your copy of the deposition of Mark Oligschlaeger taken on September 17, 2004, in the above-referenced case. Also enclosed is the original signature page and errata sheet.

Please have the witness read your copy of the transcript, indicate any changes and/or corrections desired on the errata sheet and sign the signature page before a notary public.

Please return the errata sheet and notarized signature page to Mr. Lowery for filing prior to trial date.

Thank you for your attention to this matter.

Sincerely,

Kellene K. Feddersen, RPR, CSR, CCR

Enclosure