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Issues: Revenue Requirement
Differences; Corporate Cost
Allocation Study
Witness: Mark L. Oligschlaeger
Sponsoring Party: MoPSC Staff
Type of Exhibit: Direct Testimony
Case No.: GR-2004-0209
Date Testimony Prepared: April 15, 2004

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

MARK L. OLIGSCHLAEGER

FILED

JUL 13 2004

**Missouri Public
Service Commission**

MISSOURI GAS ENERGY

CASE NO. GR-2004-0209

*Jefferson City, Missouri
April 2004*

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy's)
Tariffs to Implement a General Rate)
Increase for Natural Gas Service)

Case No. GR-2004-0209

AFFIDAVIT OF MARK L. OLIGSCHLAEGER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Mark L. Oligschlaeger, being of lawful age, on his oath states: that he has participated in the preparation of the following direct testimony in question and answer form, consisting of 10 pages to be presented in the above case; that the answers in the following direct testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Mark L. Oligschlaeger
Mark L. Oligschlaeger

Subscribed and sworn to before me this 14th day of April 2004.



Toni M Charlton

TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004

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1 Commission. I have also been responsible for the supervision of other Commission
2 employees in rate cases and other regulatory proceedings numerous times. I have received
3 training at in-house and outside seminars on technical ratemaking matters since I began my
4 employment at the Commission.

5 Q. With reference to Case No. GR-2004-0209, the Application by Missouri Gas
6 Energy (MGE or Company) to increase rates charged to its natural gas customers, have you
7 examined the books and records of MGE?

8 A. Yes, with the assistance of other members of the Commission Staff (Staff).

9 Q. What is the purpose of your direct testimony?

10 A. The purpose of my direct testimony is to highlight for the Commission some
11 of the major issues causing the difference between MGE's requested amount of rate relief in
12 this proceeding, and the Staff's recommended revenue requirement. I also address a
13 corporate cost allocation study issue that has recently arisen between MGE and the Staff.

14 **REVENUE REQUIREMENT DIFFERENCES**

15 Q. What is the Staff's recommended rate change for MGE as a result of its audit
16 of the Company's books and records?

17 A. Based upon its audit of the books and records of MGE, the Staff's
18 recommended revenue requirement for the Company in this case is \$330,953, calculated at
19 the Staff's recommended midpoint return on equity in this case, sponsored by Staff witness
20 David Murray of the Financial Analysis Department. The Staff's revenue requirement is
21 based upon a test year of the twelve months ended June 30, 2003, with an update of known
22 and measurable changes through December 31, 2003, as ordered by the Commission earlier
23 in this proceeding. The Staff's revenue requirement also reflects the impact of an

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1 "Allowance for True-up" amount of \$2.5 million, which is discussed in the direct testimony
2 of Staff Auditing witness Charles R. Hyneman.

3 Q. What amount of rate relief is MGE seeking in this proceeding?

4 A. On November 4, 2003, MGE filed tariff sheets with the Commission seeking
5 to implement a general rate increase for natural gas service in an annual amount of
6 \$44,875,635.

7 Q. What explains the difference between MGE's and the Staff's filed revenue
8 requirements in this case?

9 A. The Staff has performed a preliminary reconciliation of MGE's and the Staff's
10 filed cases. (All amounts cited in this testimony regarding value of issues are subject to
11 change, pending the Staff's filing of a case reconciliation on April 26, 2004, as ordered by
12 the Commission.) Based upon this preliminary reconciliation, the rate of return area is the
13 largest issue area in this proceeding. The Staff believes the differences between the parties in
14 the area of rate of return in this case are worth approximately \$23 million in total.

15 Q. Why is the rate of return/capital structure issue so significant in this case?

16 A. There are two main subcomponents to this issue: 1) use of different capital
17 structures; and 2) differences in recommended return on equity. Differences between the
18 parties in both of these areas are significant in terms of revenue requirement.

19 Q. What are the different capital structures being recommended by MGE and the
20 Staff in this case?

21 A. In its filing, MGE recommended a capital structure of 43.3% common equity,
22 46.1% long-term debt, and 10.5% preferred equity. This is the capital structure that results
23 when one takes Southern Union's actual capital structure at June 30, 2003, and then

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1 eliminates all debt associated with Southern Union's Panhandle Energy (Panhandle)
2 properties. (The equity associated with Panhandle remains in MGE's proposed capital
3 structure.)

4 The Staff's capital structure as of December 31, 2003, is Southern Union's
5 consolidated capital structure of 61.1% long-term debt, 25.4% common equity, 6.2%
6 preferred equity and 7.35% short-term debt. (The short-term debt in the Staff's
7 recommended capital structure is the amount in excess of Southern Union's current
8 construction requirements.) As a consolidated capital structure, the Staff's recommendation
9 reflects both the debt and the equity associated with Panhandle Eastern.

10 The Staff is estimating that the revenue requirement difference caused by MGE and
11 the Staff's different capital structures in this case as being worth approximately \$16.3
12 million.

13 Q. What is the difference in recommended return on equity between MGE and
14 the Staff?

15 A. The Company recommended a return on equity of 12.00%. The Staff has
16 recommended a range of equity returns between 8.50% and 9.50%. The difference in
17 revenue requirement between the MGE's recommended return on equity and the Staff
18 midpoint return on equity recommendation is approximately \$6.7 million.

19 Q. What Staff witness is addressing rate of return matters in this proceeding?

20 A. Staff witness David Murray of the Financial Analysis Department is
21 sponsoring the Staff's position on these matters.

22 Q. What are the other major issues, measured in dollar value, between MGE and the
23 Staff in this proceeding?

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1 A. I have listed below some of the major revenue, expense and rate base issues
2 between the Company and the Staff, based upon each party's direct testimony filing. The
3 revenue/expense issues listed below all have an approximate income statement difference of
4 approximately \$1 million. The rate base issues listed below involve a rate base valuation
5 difference of at least \$5 million.

6 **Revenues**

7 - Capacity Release Revenues

8 - Load Attrition Adjustment

9 **Expenses**

10 - Depreciation Expense

11 - Corporate Allocations

12 - Bad Debt Expense

13 - Pensions/PPA Amortization

14 **Rate Base**

15 - SLRP Deferrals

16 - AMT Credit

17 - Cash Working Capital (Revenue Lag)

18 Q. In the revenues area, what is the difference between the Company and the
19 Staff concerning capacity release revenues?

20 A. The Staff has included a normalized level of capacity release revenues in its
21 case of approximately \$1.34 million, while MGE has not included any of these revenues in
22 its case. Capacity release revenues represent revenues received by gas utilities for release of

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1 unused pipeline capacity to third party users. This item is discussed in the direct testimony
2 of Staff witness Anne M. Allee of the Procurement Analysis Department.

3 Q. What is the difference in revenues concerning "load attrition?"

4 A. The Company has included an adjustment in its case to reduce revenues by
5 approximately \$1.63 million to account for what it asserts to be reduced usage of gas by its
6 customers over time. The Staff has not proposed any adjustment for load attrition in its case.

7 Q. What is the issue between the Company and the Staff on depreciation
8 expense?

9 A. There are two subcomponent issues: depreciation rates and treatment of cost
10 of removal. These issues' total value is approximately \$3.9 million.

11 Concerning depreciation rates, the Company has recommended that one-half of the
12 value of the shift in depreciation rates called for in a depreciation study performed for MGE
13 in 2000 by Black & Veatch be implemented in this case, although it offered no such study in
14 its testimony. The Staff recommends that the depreciation rates agreed to by the parties of
15 MGE's last rate proceeding, Case No. GR-2001-292 should be maintained in this proceeding,
16 and that continuing property record data problems associated with MGE's acquisition of its
17 Missouri service territory from Western Resources, Inc. in 1994 makes the quality of any
18 current MGE-specific depreciation rate analysis suspect. This matter is addressed in the
19 direct testimony of Staff witness Jolie L. Mathis of the Engineering and Management
20 Services Department.

21 As for cost of removal, the Staff is following its current practice of treating actual
22 cost of removal/salvage amounts as a component of expense, as opposed to MGE's
23 recommended approach of accruing for estimated future cost of removal as a component of

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1 depreciation rates. Staff witness Hyneman in this case sponsors the Staff's cost of removal
2 position.

3 Q. What is the issue concerning allocation of Southern Union corporate costs in
4 this proceeding?

5 A. The Company has recommended inclusion of an estimated \$4.1 million in
6 allocated corporate costs from Southern Union as part of its rate request in this case. The
7 Staff has proposed a number of adjustments to the test year Southern Union allocated costs,
8 including recalculation of the general allocator to exclude a customer numbers component,
9 removal of excessive directors' salary and office expenses, exclusion of lobbying related
10 allocated costs, and removal of excessive corporate aircraft costs. The Staff's total
11 adjustments in this area, sponsored by Mr. Hyneman, total approximately \$2.4 million.

12 Q. What is the difference in this case concerning bad debt expense?

13 A. Staff Auditing witness Paul R. Harrison sponsored a five-year average of past
14 bad debt write-offs to develop a normalized level of bad debt expense to include in rates.
15 MGE used a three-year average of bad debt write-offs for its recommended rate allowance.
16 The difference between these two approaches is approximately worth \$1.3 million in
17 expense.

18 Q. What were the positions of the parties concerning pension expense in this
19 proceeding?

20 A. The Company's case was based upon the FAS 87 level of accrued pension
21 expense, which when annualized totaled a little under \$1 million. The Staff filed its case
22 consistent with its current pension position of using the Minimum ERISA amount, which for
23 MGE is zero.

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1 There is also a difference between the parties concerning amortization of the prepaid
2 pension asset in rate base. The Company has proposed to amortize this amount over six
3 years, with the Staff advocating seven years. This difference is worth approximately
4 \$400,000 in expense.

5 Staff witness Hyneman is sponsoring the Staff's position on pension related matters
6 in this case.

7 Q. What is the issue concerning SLRP deferrals in rate base in this case?

8 A. MGE has included \$18.3 million of unamortized Service Line Replacement
9 Program accounting authority deferrals in rate base in this case. The Staff has excluded the
10 unamortized balances of SLRP deferrals from rate base in accord with Commission
11 precedent for MGE, set in Case No. GR-98-140.

12 Q. What is the rate base issue concerning the Alternative Minimum Tax Credit?

13 A. This credit results from the alternative minimum tax payments Southern
14 Union has paid to the Internal Revenue Service in recent years. The Company has placed
15 this credit in rate base where it effectively is an offset to the Deferred Income Tax balances.
16 The Staff does not believe that the AMT credit should be in rate base at all until it is shown
17 that the AMT payments are directly related to MGE financial results, and not the results of
18 MGE's parent company, Southern Union. Staff witness Harrison addressed this matter in his
19 direct testimony in this proceeding.

20 Q. What are the rate base differences between the Company and the Staff
21 concerning cash working capital?

22 A. The primary differences in this area relate to the revenue lag component of the
23 CWC lead/lag study. The Company filed a billing lag of over six days, while the Staff has

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1 sponsored a billing lag of slightly over three days, which is more in line with the billing lags
2 of other large energy utilities in this state. In relation to the collection lag, the Company
3 calculated that lag through an accounts receivable turnover computation, and derived a lag of
4 over 25 days. The Staff has chosen to modify MGE's turnover calculation by removing the
5 impact of bad debts on the computation, and came up with a collection lag of slightly under
6 23 days.

7 The total difference between the Staff's and MGE's CWC recommendations is worth
8 approximately \$8.9 million in rate base. These issues are addressed in the direct testimony of
9 Staff Auditing witness Dana E. Eaves.

10 Q. What explains the remaining differences between the Staff and MGE on the
11 appropriate amount of rate relief for the Company from this case?

12 A. There are a number of revenue, expense and rate base issues of lower dollar
13 value between the Staff and MGE in this proceeding.

14 **CORPORATE COST ALLOCATION STUDY**

15 Q. Does the Staff have any other issues that need to be addressed in this case?

16 A. Yes. Case No. GM-2003-0238 was a case filed by Southern Union seeking
17 Commission approval of the acquisition of Panhandle Eastern Pipeline Company. This
18 transaction was approved by Commission Order on March 27, 2003. The Commission
19 approved a Stipulation And Agreement in that Order, for which Section III.3.G required that
20 a study be done within six months of the closing of the transaction. The transaction was
21 closed in June 2003. The study was to be done by Southern Union regarding the specific
22 impacts of the acquisition and operation of Panhandle on Southern Union's administrative

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1 and general expense and cost allocation methodology. The provisions of the Stipulation And
2 Agreement specifically set out the details of the study that was to be performed.

3 Q. Does the Staff believe that Southern Union has adequately completed this
4 study?

5 A. No. The Staff does not believe that such a study has in fact been adequately
6 completed. While Southern Union has provided some information to the Staff, including a
7 Cost Allocation Model and a Joint and Common Costs Model, the Staff does not believe that
8 the specific study contemplated by the Stipulation And Agreement has actually been
9 performed. Accordingly, the Staff recommends that, as part of any Commission Order in this
10 case, that Southern Union be ordered to complete this study and provide it to the parties to
11 Case No. GM-2003-0238.

12 The Staff proposes that, during the prehearing to this case, MGE, the Staff and other
13 interested parties meet to discuss the topics outlined in Section III.3.G of the Stipulation And
14 Agreement in Case No. GM-2003-0238. It is hoped that the result of the meeting will be an
15 agreement on what specific information will be provided in the study consistent with the
16 Stipulation And Agreement in Case No. GM-2003-0238. The Staff further proposes that
17 MGE/Southern Union complete and file its study with the Commission as part of this case no
18 later than the operation-of-law date for this proceeding.

19 Q. Does this conclude your direct testimony?

20 A. Yes, it does.

21

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<u>COMPANY</u>	<u>CASE NO.</u>
Kansas City Power and Light Company	ER-82-66
Kansas City Power and Light Company	HR-82-67
Southwestern Bell Telephone Company	TR-82-199
Missouri Public Service Company	ER-83-40
Kansas City Power and Light Company	ER-83-49
Southwestern Bell Telephone Company	TR-83-253
Kansas City Power and Light Company	EO-84-4
Kansas City Power and Light Company	ER-85-128 & EO-85-185
KPL Gas Service Company	GR-86-76
Kansas City Power and Light Company	HO-86-139
Southwestern Bell Telephone Company	TC-89-14
Western Resources	GR-90-40 & GR-91-149
Missouri-American Water Company	WR-91-211
UtiliCorp United Inc. / Missouri Public Service	EO-91-358 & EO-91-360
Generic: Expanded Calling Scopes	TO-92-306
Generic: Energy Policy Act of 1992	EO-93-218
Western Resources, Inc./Southern Union Company	GM-94-40
St. Louis County Water Company	WR-95-145
Union Electric Company	EM-96-149
St. Louis County Water Company	WR-96-263
Missouri Gas Energy	GR-96-285
The Empire District Electric Company	ER-97-82
UtiliCorp United, Inc./Missouri Public Service	ER-97-394
Western Resources, Inc./Kansas City Power & Light Company	EM-97-515
United Water Missouri, Inc.	WA-98-187
Missouri-American Water Company	WM-2000-222

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<u>COMPANY</u>	<u>CASE NO.</u>
UtiliCorp United Inc. / St. Joseph Light & Power Company	EM-2000-292
UtiliCorp United Inc. / The Empire District Electric Company	EM-2000-369
Green Hills Telephone Corporation	TT-2001-115
IAMO Telephone Company	TT-2001-116
Ozark Telephone Company	TT-2001-117
Peace Valley Telephone Company, Inc.	TT-2001-118
Holway Telephone Company	TT-2001-119
KLM Telephone Company	TT-2001-120
Missouri Gas Energy	GR-2001-292
The Empire District Electric Company	ER-2001-299
Oregon Farmers Mutual Telephone Company	TT-2001-328
Ozark Telephone Company	TC-2001-402
Gateway Pipeline Company, Inc.	GM-2001-585
Missouri Public Service	ER-2001-672
Union Electric, d/b/a AmerenUE	EC-2002-1
Laclede Gas Company	GA-2002-429
Aquila, Inc., d/b/a Aquila Networks-MPS-Electric and Aquila Networks-L&P-Electric and Steam	ER-2004-0034 & HR-2004-0024 (Consolidated)

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Company Name	Case Number	Issues
Western Resources	GR-90-40 and GR-91-149	Take-Or-Pay Costs
Missouri-American Water	WR-91-211	True-up; Known and Measurable
Missouri Public Service	EO-91-358 and EO-91-360	AAO
Generic Telephone	TO-92-306	Revenue Neutrality; Accounting Classification
Generic Electric	EO-93-218	Preapproval
Western Resources & Southern Union Company	GM-94-40	Regulatory Asset Transfer
St. Louis County Water	WR-95-145	Policy
Union Electric Company	EM-96-149	Merger Savings; Transmission Policy
St. Louis County Water	WR-96-263	Future Plant
Missouri Gas Energy	GR-96-285	Riders; Savings Sharing
Empire District Electric	ER-97-82	Policy
Missouri Public Service	ER-97-394	Stranded/Transition Costs; Regulatory Asset Amortization; Performance Based Regulation
Western Resources & Kansas City Power & Light	EM-97-515	Regulatory Plan; Ratemaking Recommendations; Stranded Costs
United Water Missouri	WA-98-187	FAS 106 Deferrals
Missouri-American Water	WM-2000-222	Conditions
UtiliCorp United & St. Joseph Light & Power	EM-2000-292	Staff Overall Recommendations
Utilicorp United & Empire District Electric	EM-2000-369	Overall Recommendations
Green Hills Telephone	TT-2001-115	Policy
IAMO Telephone Company	TT-2001-116	Policy

Company Name	Case Number	Issues
Ozark Telephone Company	TT-2001-117	Policy
Peace Valley Telephone	TT-2001-118	Policy
Holway Telephone Company	TT-2001-119	Policy
KLM Telephone Company	TT-2002-120	Policy
Missouri Gas Energy	GR-2001-292	SLRP Deferrals; Y2K Deferrals; Deferred Taxes; SLRP and Y2K CSE/GSIP
Empire District Electric	ER-2001-299	Prudence/State Line Construction/Capital Costs
Ozark Telephone Company	TC-2001-402	Interim Rate Refund
Gateway Pipeline Company	GM-2001-585	Financial Statements
Missouri Public Service	ER-2001-672	Purchased Power Agreement; Merger Savings/Acquisition Adjustment
Union Electric Company	EC-2002-1	Merger Savings; Criticisms of Staff's Case; Injuries and Damages; Uncollectibles
Laclede Gas Company	GA-2002-429	AAO Request
Aquila, Inc., d/b/a Aquila Networks-MPS-Electric and Aquila Networks-L&P-Electric and Steam	ER-2004-0034 and HR-2004-0024 (Consolidated)	Aries Purchased Power Agreement; Merger Savings