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Service Commission

Exhibit No.:

Issue: Sharing of Merger Savings

Witness: Janis E. Fischer

Sponsoring Party: MoPSC Staff

Type of Exhibit: Rebuttal Testimony

Case Nos.: ER-2004-0034 and

HR-2004-0024

(Consolidated)

Date Testimony Prepared: January 26, 2004

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

REBUTTAL TESTIMONY

OF

JANIS E. FISCHER

AQUILA, INC.

**d/b/a AQUILA NETWORKS-MPS (Electric)
AND AQUILA NETWORKS-L&P (Electric & Steam)**

**CASE NOS. ER-2004-0034 AND HR-2004-0024
(Consolidated)**

*Jefferson City, Missouri
January 2004*

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Case No(s) ER-2004-0034
Date 2/23/04 Rptr KF

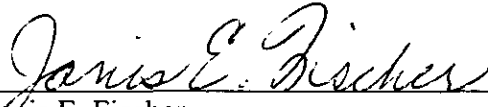
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Aquila, Inc. d/b/a Aquila Networks)
L&P and Aquila Networks MPS to implement a) Case No. ER-2004-0034
general rate increase in electricity.)
)
)
In the matter of Aquila, Inc. d/b/a Aquila Networks)
L&P to implement a general rate increase in Steam) Case No. HR-2004-0024
Rates.)
)

AFFIDAVIT OF JANIS E. FISCHER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Janis E. Fischer, of lawful age, on her oath states: that she has participated in the preparation of the following rebuttal testimony in question and answer form, consisting of 22 pages to be presented in the above case; that the answers in the following rebuttal testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.



Janis E. Fischer

Subscribed and sworn to before me this 23rd day of January 2004.





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

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**TABLE OF CONTENTS OF
REBUTTAL TESTIMONY OF
JANIS E. FISCHER**

**AQUILA, INC. d/b/a AQUILA NETWORKS-MPS (ELECTRIC)
AND AQUILA NETWORKS-L&P (ELECTRIC AND STEAM)
CASE NOS. ER-2004-0034 AND HR-2004-0024**

(Consolidated)

PURPOSE OF REBUTTAL TESTIMONY 5
SUMMARY OF CASE ORDERS..... 7
MASSACHUSETTS GUIDELINES..... 15
KANSAS CORPORATION COMMISSION ORDER..... 17
IOWA UTILITIES BOARD RPU-02-5 20
STAFF’S CONCLUSIONS 21

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21

REBUTTAL TESTIMONY

OF

JANIS E. FISCHER

AQUILA, INC. d/b/a AQUILA NETWORKS-MPS (ELECTRIC)

AND AQUILA NETWORKS-L&P (ELECTRIC AND STEAM)

CASE NOS. ER-2004-0034 AND HR-2004-0024

(Consolidated)

Q. Please state your name and business address.

A. Janis E. Fischer, Governor Office Building, PO Box 360, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am a Regulatory Auditor with the Missouri Public Service Commission (Commission).

Background of Witness

Q. Please describe your educational background.

A. I graduated from Peru State College, Peru, Nebraska in December 1979, and received a Bachelor of Science degree in Education (Basic Business) and Business Administration. In May 1985, I completed course work and earned a Bachelor of Science degree in Accounting. I passed the Uniform Certified Public Accountant examination in May 1994 and received my license to practice in March 1997.

Q. Please describe your work background.

Rebuttal Testimony of
Janis E. Fischer

1 A. Prior to my employment at the Commission, I worked from February 1988
2 through November 1994 as the office and accounting supervisor for the Falls City, Nebraska
3 Utilities Department (Falls City Utilities Department).

4 I also was employed as a staff accountant with the accounting firm of Cuneo,
5 Lawson, Shay and Staley, PC, in Kansas City, Missouri, from November 1994 through
6 October 1996. Prior to that, I worked in the business office of the Falls City Community
7 Hospital and as the accountant for the Sac and Fox Tribe of Missouri.

8 Q. What has been the nature of your duties while employed by the Commission?

9 A. Since I began employment with the Commission in October 1996, I have
10 directed and assisted with various audits and examinations of the books and records of public
11 utilities operating within the state of Missouri under the jurisdiction of the Commission. I
12 assumed my present position of Regulatory Auditor IV in December 2001.

13 Q. Have you previously filed testimony before this Commission?

14 A. Yes. Please refer to Schedule 1, attached to this rebuttal testimony, for a list
15 of the major audits and issues on which I have assisted and filed testimony.

16 Q. With reference to Case Nos. ER-2004-0034 and HR-2004-0024, have you
17 examined and studied the books and records of Aquila Networks-Missouri Public Service
18 (MPS) and Aquila Networks-Light & Power (L&P) relevant to the filing in this case?

19 A. Yes, with the assistance of other members of the Commission Staff (Staff). I
20 have examined the Company's filing, data request responses and prior case proceedings
21 relevant to this case, and in particular with the area regarding which I am providing rebuttal
22 testimony.

Rebuttal Testimony of
Janis E. Fischer

1 Q. What knowledge, skill, experience, training or education do you have in
2 regulatory matters?

3 A. My knowledge is based upon my work prior to being employed by the
4 Commission and being assigned a variety of issues in a number of Commission cases over
5 the past seven years. Specifically with regard to Aquila cases, I filed testimony in the
6 Aquila, Inc. (when it was called Utilicorp United, Inc.) and St. Joseph Light & Power
7 Company (SJLP) Case No. EM-2000-292 (merger case) and MPS' 2001 general rate increase
8 application designated as Case No. ER-2001-672. I have also filed testimony on the issue of
9 merger savings and tracking of merger costs and savings in the unconsummated merger of
10 UtiliCorp United, Inc. and The Empire District Electric Company in Case No. EM-2000-369;
11 and the unconsummated Western Resources Inc. and Kansas City Power & Light Company
12 merger in Case No. EM-97-515.

13 I have reviewed the Staff Auditing Department position papers, training manuals and
14 technical manuals dealing with accounting issues in this case. In addition, I have reviewed
15 Commission Report And Orders, testimony and transcripts of recent Commission cases. I
16 have also attended in-house and Commission sponsored training throughout the seven years
17 of my employment with the Commission.

18 In addition to knowledge gained while employed at the Commission, my work at a
19 municipal utility company for over six years has given me additional expertise related to the
20 daily operations of an electric and natural gas utility. A small municipal utility operation
21 provides employees the opportunity to gain knowledge in many aspects of utility operations.
22 While with the Falls City Utilities Department, I completed water and electric rate reviews,
23 developed procedures for PCB monitoring and disposal, implemented a program to verify the

Rebuttal Testimony of
Janis E. Fischer

1 accuracy of remote water meters, supervised office staff and handled customer complaints. I
2 assisted with the acquisition of Falls City's natural gas distribution system from Kansas
3 Power and Light Company, predecessor company of Western Resources, Inc. After the
4 acquisition, I compiled asset records for the natural gas distribution system for the utility,
5 nominated gas supplies for the municipal power plant, negotiated prices for gas purchased
6 from marketers, monitored gas transportation customer loads and billed transportation
7 customers.

8 I was appointed by the Falls City Board of Public Works (Board) to the Nebraska
9 Public Gas Agency (NPGA) Board and later was elected Secretary and then Vice
10 Chairperson of the NPGA Board. NPGA is comprised of members from Nebraska, Kansas,
11 Iowa and Wisconsin municipal natural gas systems which collectively purchase natural gas
12 and acquire natural gas wells to supply gas to NPGA member municipal gas systems and
13 power plants at reduced costs. As a member of the NPGA Board, I reviewed annual budgets
14 and natural gas purchases for member communities. I participated in management salary
15 negotiations and the development of incentive compensation programs for management and
16 other employee groups. In addition I participated in NPGA's negotiations to purchase gas
17 wells, reviewed terms and conditions for the issuance of revenue bonds and attended
18 meetings with NPGA's lobbyist and future planning sessions.

19 While employed as a staff accountant with Cuneo, Lawson, Shay and Staley, I
20 assisted in various audits, compilations and reviews of corporations and prepared individual
21 and corporate state and federal tax returns. I researched tax issues for international client
22 business operations and interacted with various clients. I completed pension plan audits,

Rebuttal Testimony of
Janis E. Fischer

1 health care plan compliance audits for several unions in the Kansas City area, a stock
2 brokerage firm audit and a nursing home audit.

3 In addition, my prior work experience in the area of accounting included assisting in
4 preparing monthly financial statements, reconciling cash receipts to customer payments,
5 completing accounts payable functions and maintaining investment records for a non-profit
6 hospital. While employed as the accountant for the Sac and Fox Tribe of Missouri, my
7 responsibilities included maintenance of all accounting records of federal and state
8 governmental grants and contracts. I compiled monthly financial statements, completed
9 payroll functions and corresponded with the Bureau of Indian Affairs and the United States
10 Department of the Interior on a quarterly basis regarding the status of grants and contracts
11 administered by the Sac and Fox Tribe.

12 **PURPOSE OF REBUTTAL TESTIMONY**

13 Q. What is the purpose of your rebuttal testimony?

14 A. I am responding to the direct testimony of Aquila witness Mr. Vern J. Siemek
15 on the issue of Merger Savings. Mr. Siemek, at pages 11 and 13 of his direct testimony,
16 states:

17 ...[T]here are many recent precedents for sharing the savings
18 from mergers or acquisitions....All acknowledge that the savings
19 created by acquisitions are equitably shared in some ratio between the
20 customers and the shareholders that created the savings.

21 Clearly, many jurisdictions have realized the equity of sharing
22 acquisition-related savings with shareholders to reward the companies
23 and to help offset the costs of accomplishing the transactions that
24 created the savings.

25 Mr. Siemek then includes quotes from thirteen public utility commission orders
26 issued by ten jurisdictions that allegedly approved sharing of merger savings. I will respond

Rebuttal Testimony of
Janis E. Fischer

1 to Mr. Siemek's characterizations of these orders. I will also briefly address a 2002 Aquila
2 rate proceeding in Iowa that included merger savings sharing issues.

3 Q. Did the Missouri Commission approve sharing of merger savings between
4 customers and shareholders in the UtiliCorp United Inc. and St. Joseph Light & Power
5 Company merger, Case No. EM-2000-292?

6 A. No, the Commission did not approve the sharing of merger savings between
7 customers and shareholders. The Commission's Report and Order in Case No. EM-2000-292
8 also included no findings related to rate recovery, the sharing of merger savings, limitations
9 on rate case filings, rate caps, base rate freezes or rate case moratoriums.

10 Q. Have you reviewed the orders cited in Mr. Siemek's direct testimony?

11 A. Yes, I have reviewed all the public utility commission orders cited by
12 Mr. Siemek. My review included reading portions of each order pertaining to merger
13 savings and then reading additional sections that provided explanation of the issues specific
14 to that case, historical overviews of the filings in the case and the commission's explanation
15 of how it reached its decision. I also read the section of each order from which Mr. Siemek
16 quoted.

17 Q. What was the conclusion you reached about the statements made by
18 Mr. Siemek in his direct testimony regarding the sharing of merger savings in other
19 jurisdictions, as quoted above?

20 A. Mr. Siemek implies that there is a wide or general acceptance in other
21 jurisdictions supporting Aquila's position in this case. However, Mr. Siemek refers to public
22 service commission orders from only ten jurisdictions. Considering ten out of fifty-one
23 jurisdictions does not constitute anywhere near the majority of jurisdictions concerning the

Rebuttal Testimony of
Janis E. Fischer

1 rate treatment of merger savings. Also, a review of these orders indicated there were
2 significant differences in both the circumstances under which the merger savings sharing was
3 ordered, compared to Aquila's current situation, and that the manner of merger savings
4 sharing was often significantly different than that proposed by Aquila in this proceeding.

5 Q. Did Mr. Siemek base his assertions upon a fair indication of the specifics of
6 each case?

7 A. No. In a deposition of Mr. Siemek dated December 30, 2003, he stated that he
8 just skimmed the orders he quoted from and relied on to support his direct testimony. Of the
9 thirteen orders quoted, eight actually are from contested merger cases or rate cases resulting
10 from mergers; two represent stipulation and agreements accepted by the commissions; one
11 order is from a petition to reduce retail rates; and one order is from a case seeking approval
12 of an alternative form of rate regulation.

13 **SUMMARY OF CASE ORDERS**

14 Q. Do the state jurisdictions cited in the orders quoted by Mr. Siemek face
15 similar situations as Missouri has in ruling on merger and acquisition issues?

16 A. No. Of the ten state jurisdictions quoted, four have proceeded with total
17 deregulation. Three of the states quoted (California, Massachusetts and New York) had
18 utility rates in the top 20 percent in the nation. Several of the state commissions quoted by
19 Mr. Siemek have stated in merger case orders that they promote mergers and acquisitions in
20 an effort to reduce utility rates. Massachusetts, whose commission was quoted four times by
21 Mr. Siemek, has Guidelines and Standards for Acquisitions and Mergers of Utilities
22 (Guidelines) adopted to standardize the approval process.

Rebuttal Testimony of
Janis E. Fischer

1 Q. Please comment on the California Public Utility Commission, Case
2 No. A.90-09-043, GTE Corporation, cited on page 11, lines 19-21 of Mr. Siemek's direct
3 testimony.

4 A. The California GTE merger case cited by Mr. Siemek involves telephone local
5 exchange carriers under incentive regulation that include price cap indexing and an economic
6 benefits sharing mechanism. The Public Utility Code of California 854(b)(2) provides that,
7 before authorizing a merger, the Commission shall find that the proposal:

8 Equitably allocates, where the commission has ratemaking authority,
9 the total short-term and long-term forecasted economic benefits, as
10 determined by the commission, of the proposed merger, acquisition, or
11 control, between shareholders and ratepayers. Ratepayers shall receive
12 not less than 50 percent of those benefits.

13 The California GTE merger case is not remotely similar to the merger between
14 Aquila and SJLP because of the differences in the regulatory treatment required by the Public
15 Utility Code of California to that traditionally practiced in Missouri.

16 Q. Please comment on the District of Columbia Public Service Commission,
17 Case No. 951, Baltimore Gas and Electric Company, Order No. 11075 case cited on page 11,
18 lines 23-26 of Mr. Siemek's direct testimony.

19 A. The District of Columbia (D.C.) Commission in the Baltimore Gas and
20 Electric Company case cited by Mr. Siemek approved a four-year base rate cap. The amount
21 of estimated net merger savings (1997-2006) to be shared was \$1.805 billion, of which D.C.
22 ratepayers were to receive 19.1 percent, or \$345 million. The shared savings were to be
23 distributed monthly as a credit to ratepayers over the period of the four-year cap. Total costs
24 to achieve the merger were \$146 million, representing approximately 7.5 percent of the
25 estimated merger savings. In contrast to the D.C. Commission, the Missouri Commission did
26 not order a rate cap or freeze in the Aquila-SJLP merger case. Nor did this Commission

Rebuttal Testimony of
Janis E. Fischer

1 require Aquila to immediately share, reduce rates or otherwise provide any purported
2 benefits resulting from the merger to the customers of either MPS or L&P.

3 Although Mr. Siemek uses ellipses to indicate his omission of words, the quote on
4 page 11, lines 23-26 of his direct testimony is out of context. I have included the quote in its
5 entirety and underlined the text quoted by Mr. Siemek:

6 We believe that the public interest of the District of Columbia will best
7 be served by a plan of merger which includes: (1) A cap on base rates
8 for four years, as opposed to the two and one-half-year freeze
9 proposed by the Applicants (2) A Plan for District ratepayers to
10 recover 75% of the District's share of net merger savings estimated to
11 occur over the period of the four-year cap, as opposed to a 50% share
12 as proposed by the Applicants (3) a credit to be computed annually and
13 distributed monthly to District ratepayers totaling \$94.5 million over
14 the period of the four-year cap. [emphasis added]

15 Nothing was or has been presented to the Staff during Case No. EM-2000-292, Case
16 No. ER-2001-672 (MPS's last electric rate case in Missouri), or in this rate case to indicate
17 that the merger savings in the Aquila-SJLP merger are anywhere near the magnitude of those
18 in the Baltimore Gas and Electric Company case.

19 Q. Please comment on the Louisiana Public Service Commission, Docket
20 No. U-19904, Entergy Corporation, Order No. U-19904 case cited on page 12, lines 1-5 of
21 Mr. Siemek's direct testimony.

22 A. The Louisiana Commission in the Entergy Corporation case cited by
23 Mr. Siemek approved a five-year base rate ceiling and required a tracking mechanism for
24 merger savings, as stated in this quote from the Order:

25 The essential terms of the joint proposal include the following:

26 1. All fuel savings will be flowed through the fuel clause to
27 ratepayers, subject to any offsets required by the Louisiana Light &
28 Power Company (LP&L) protection mechanism, or a FERC protection
29 mechanism discussed in the next section.

Rebuttal Testimony of
Janis E. Fischer

1 2. There will be a five-year rate ceiling at Gulf States Utilities
2 Company's (GSU's) current base rates.

3 3. A tracking mechanism will be established to measure O&M
4 savings. The tracker will be based on a benchmark of projected O&M
5 costs, reflecting a 1992 normalized level of costs, increased in each
6 year by the Consumer Price Index and one-half of GSU's sales growth.
7 Savings will be the difference between the normalized O&M expense
8 in any future year and the benchmark.

9 4. The company will be permitted to include 60 percent of the
10 O&M savings actually achieved in any year as a cost of service item to
11 reduce the amount of any rate decrease.

12 5. There will be an annual cost of service review. A rate rider
13 will be used to reduce rates below the current level--entitled "merger
14 savings credit".

15 6. The company may request a rate increase after the fifth year,
16 but may not include shared savings as a cost of service item to support
17 the rate increase.

18 7. The rate cap is subject to "force majeure" and the sharing
19 formula contains special provisions, which are explained in the joint
20 regulatory proposal.

21 Q. Please comment on the Nevada Public Service Commission, Docket
22 No. 98-7023, Nevada Power Company, case cited on page 12, lines 7-12 of Mr. Siemek's
23 direct testimony.

24 A. The Nevada Commission in the Nevada Power Company merger case
25 approved a three-year rate freeze after which time a general rate case would determine if
26 resulting merger savings were adequate to allow recovery of costs associated with the
27 merger. The Nevada Commission also included these terms and conditions in its Compliance
28 Order:

29 Before the merger shall be considered fully and finally approved,
30 Nevada Power Company and Sierra Pacific Power Company shall take
31 the following actions, consistent with the terms and conditions of this
32 Compliance Order: (a) file individual rate cases to establish actual
33 revenue requirements pursuant to NRS 704.986 and the regulations

Rebuttal Testimony of
Janis E. Fischer

1 adopted by this Commission, which revenue requirements shall be
2 frozen for a period of three years; (b) unbundled costs by
3 functionalizing and allocating costs of services as ordered in Docket
4 Nos. 97-11018 and 97-11028; (c) divest generation assts as specified
5 in a plan of divestiture filed with the Commission.

6 Q. Does Mr. Siemek accurately represent the Nevada Public Utilities
7 Commission's decision in the Nevada Power Company Docket No. 98-7023 case?

8 A. No. The costs of the merger of Nevada Power Company with Sierra Pacific
9 Power Company as stated throughout the Order, were only marginally below the estimated
10 merger savings. Therefore the Commission's main concern was to hold ratepayers harmless:

11 Given the uncertain benefits associated with this merger, the
12 Commission finds that it is not appropriate to place on ratepayers the
13 risk that they will have to pay for merger costs without receiving
14 merger benefits. Utility management designed the transaction,
15 arranged the terms and incurred the costs. The Joint Applicants have
16 not persuaded the Commission that the transaction will enhance the
17 Joint Applicants' ability to fulfill their legal obligation to serve
18 ratepayers at reasonable cost. Rather, it appears that the Joint
19 Applicants entered into the transaction to advance their competitive
20 interests. That goal is not necessarily inconsistent with the public
21 interest, but it is not one for which ratepayers of the Joint Applicants'
22 noncompetitive services should bear risks. Under these circumstances,
23 the risk that merger savings will be insufficient relative to merger costs
24 is a risk that should be borne by the company's shareholders. The
25 Commission therefore will establish a procedure that affords the
26 shareholders a reasonable opportunity to recover these costs, upon a
27 showing that merger savings are sufficient to justify these costs.

28 Q. Is Mr. Siemek's use of a quote on page 13, lines 9-11 of his direct testimony
29 from the Kentucky Public Service Commission, Case No. 98-474, Kentucky Utility
30 Company (KU), appropriate for demonstrating that the Kentucky Commission has allowed
31 the sharing of acquisition-related savings to offset merger-related costs?

32 A. No. The case was intended to determine the alternative form of rate
33 regulation to be used by KU. The Kentucky Commission in merger Case No. 97-300
34 directed KU and Louisville Gas and Electric Company (LG&E) to file their respective

Rebuttal Testimony of
Janis E. Fischer

1 detailed plans to address future regulation by September 14, 1998, or by the consummation
2 of the merger, whichever was later. Beginning on page 18 of the Case No. 98-474 Order, a
3 discussion of earnings sharing mechanisms (ESMs) and their use when an industry is
4 beginning the transition from a monopolistic industrial structure to a more competitive
5 structure can be found. A discussion of the Commission's optional ESM plan continues on
6 page 21 of the Order. Mr. Siemek's quote is taken from this section of the Order. Case
7 No. 98-474 had nothing to do with the merger of KU and LG&E, Case No. 97-300. The
8 quote included in Mr. Siemek's direct testimony refers to the Commission's optional
9 earnings sharing mechanism (ESM) plan, not the sharing of merger savings. The ESM was
10 not intended to include merger savings.

11 Q. Do you have any comments regarding Mr. Siemek's use of the Iowa Utilities
12 Board, Docket No. RPU-91-6, IPS Electric, a Division of Iowa Public Service Company case
13 on page 13, lines 13-23 of his direct testimony?

14 A. Yes. Mr. Siemek does not actually quote from this case. According to his
15 response to questions in his deposition on December 30, 2003, he relied upon his Iowa
16 counsel for the statements made in his direct testimony. The RPU-91-6 case was filed by the
17 Consumer Advocate Division of the Iowa Department of Justice as a request to reduce rates
18 for IPS Electric. The 30 basis points allowed for "management efficiencies" adjusted the rate
19 of return from 9.81 percent to 9.93 percent. A direct quote from the Order indicates that
20 Mr. Siemek is mistaken:

21 It is important to note that the management efficiency rules were
22 adopted prior to any utility mergers taking place in Iowa. The benefits
23 which flow from appropriate mergers were not specifically
24 contemplated nor addressed as appropriate for consideration in making
25 a management efficiency award.

Rebuttal Testimony of
Janis E. Fischer

1 Mr. Siemek asserts that “[t]he incentive management award effectively gave IPS
2 Electric a means to share in the synergies created by the merger via a higher return on
3 equity.”

4 Q. Do you have any comments regarding the use of the New York Public Service
5 Commission, Case No. 01-M-0075, Niagara Mohawk Holdings, Inc., quoted on page 13,
6 lines 4-7 of Mr. Siemek’s direct testimony?

7 A. Yes. This was a stipulated case in which a provision was “that the proposal is
8 explicitly conditioned upon our acceptance of it in its entirety.” The New York Commission
9 Staff noted that the proposal was offered as a complete package that was fair and equitable
10 overall and that no term should be viewed in isolation. The proposal included a write-off of
11 \$851 million of expected stranded costs, which along with expected merger savings produced
12 a significant up-front electric rate reduction. A more comprehensive statement appears at
13 pages 6-7 of the New York Commission Opinion:

14 In addition to reflecting the treatment of stranded costs, the rate
15 reductions also reflect the assignment to ratepayers of 50% of the
16 electric portion of the forecast efficiency gains and synergy savings
17 (net of costs to achieve) agreed to by the parties. Synergy savings over
18 the term of the plan are set at about \$130 million per year, allocated 62
19 percent to New York, and efficiency gains are set at \$60 million per
20 year, allocated 100 percent to New York. The imputed levels flow to
21 ratepayers regardless of whether they are achieved in fact; the
22 treatment of savings in excess of the imputed levels is discussed
23 below.

24 While the New York case related more to an incentive plan rather than to a merger
25 savings sharing plan, a key element to the Opinion was that customers received rate
26 reductions immediately. That certainly was not the case with the Aquila-SJLP merger.

27 Q. Do you agree with Mr. Siemek’s inclusion of a quote on page 12, lines 45-46,
28 continuing on page 13, lines 1-2 of his direct testimony from the Illinois Commerce

Rebuttal Testimony of
Janis E. Fischer

1 Commission, Case No. 00-0476, Illinois-American Water Company, Order dated May 15,
2 2001, as a comparison to the Aquila-SJLP merger?

3 A. No, I do not. Again, Mr. Siemek has taken a portion of an Illinois
4 Commission Order and quoted it out of context. A more complete quote with the portion
5 used by Mr. Siemek underlined follows:

6 The Commission concludes that the shared savings plan (SSP) should
7 be rejected for several reasons. First, the SSP would allow the
8 opportunity to recover the Acquisition Adjustment from ratepayers.
9 The SPP would inappropriately require ratepayers to compensate
10 Illinois-American for its decision to pay approximately \$66.6 million
11 over book value for Citizens' utility assets. The Commission views
12 the Acquisition Adjustment as a merger transactional cost that is not
13 directly associated with the utility's provision of service. The
14 Acquisition Adjustment is a cost associated with the "business end of
15 the deal". Accordingly, the Acquisition Adjustment is not recoverable
16 from ratepayers under the standard recently followed by the
17 Commission in Docket Nos. 98-0555 (Ameritech/SBC) and 98-0866
18 (GTE/Bell Atlantic).

19 The next issue to be addressed is the allocation of Acquisition savings.
20 Section 7-204(c) of the Act provides that the Commission shall not
21 approve a reorganization without ruling on the allocation of savings
22 resulting from the proposed reorganization. In its Orders in Docket
23 Nos. 98-0855 (Ameritech/SBC) and 98-0866 (GTE/Bell Atlantic), the
24 Commission concluded that there should be a 50/50 sharing of net
25 merger savings between ratepayers and shareholders. In this case,
26 there are no costs approved for netting against savings. The
27 Commission believes that a fair treatment in this case of the savings
28 attributable solely to the Acquisition is a 50/50 sharing between
29 shareholders and ratepayers. The Commission shares the concerns
30 expressed by Staff and IWC regarding the difficulty in measuring
31 Acquisition savings. Illinois-American has not presented a specific
32 methodology for quantifying Acquisition savings. The Commission
33 believes that it would be unworkable to litigate the appropriate
34 quantification methodology in the next rate proceeding. Therefore,
35 Illinois-American is required to file, within 90 days of the date of the
36 Order in this proceeding, a petition seeking approval of a specific
37 methodology for quantifying Acquisition savings. [Emphasis added]

38 Q. Did you review the petition seeking approval of a specific methodology for
39 quantifying acquisition savings filed in response to the Illinois Commission Order?

Rebuttal Testimony of
Janis E. Fischer

1 A. Yes, I did. The Illinois-American Water Company case is not applicable to
2 the Aquila-SJLP merger case. Expenses recorded during 1998 served as the base year for
3 determining acquisition savings. The Illinois Commission set out the methodology for
4 calculating the acquisition savings in the prior cases listed in the quote above. A schedule
5 provided in Case No. 02-0690 included calculations for acquisition savings/sharing by
6 district in five categories of costs: (1) labor and labor-related; (2) management fees; (3) rate
7 case expense; (4) non-Citizens [Illinois-American Water Company acquired Citizens Lake
8 Water Company (Citizens)] rate area long-term debt; and (5) Citizens rate area long-term
9 debt. Savings in these five categories only were eligible for sharing.

10 **MASSACHUSETTS GUIDELINES**

11 Q. Are the facts surrounding the utility merger cases in Massachusetts relied on
12 by Mr. Siemek to support Aquila's merger savings sharing proposal similar to the facts in
13 this case?

14 A. No. The Massachusetts Department of Public Utilities (DPU) (the
15 predecessor to the Department of Telecommunications and Energy (DTE)) Guidelines and
16 Standards for Acquisitions and Mergers of Utilities (Guidelines) dated August 3, 1994
17 defines the DTE's position related to utility mergers:

18 ...In light of concerns over high utility rates which in part may be the
19 result of duplicative facilities, functions, and services among
20 Massachusetts utilities, the Department has sought to reexamine its
21 current policy towards mergers or acquisitions and determine whether
22 the public interest may better be served by specific policy changes that
23 enhance efficient delivery of utility services in Massachusetts.

24 ...The Department believes that cost-effective mergers are one of
25 several means by which utilities may be able to reduce their cost of
26 service, improve service reliability, and enhance their financial
27 strength. [Emphasis added]

Rebuttal Testimony of
Janis E. Fischer

1 Massachusetts is a high cost per kilowatt-hour state (U.S. Department of Energy
2 statistical data). States that have high costs may be compelled to adopt policy in an attempt
3 to reduce rates and improve economic development opportunities in their states. Missouri is
4 not considered a high cost state and is not in same situation as Massachusetts and such other
5 states.

6 Mr. Siemek, on page 12, lines 14-19 of his direct testimony quoted from the Eastern
7 Enterprises (Eastern) acquisition of Essex County Gas Company (Essex) Order dated
8 September 17, 1998. The applicants presented evidence of an estimated \$47.1 million
9 acquisition premium, related to the earnings per share dilution that would be experienced by
10 Eastern shareholders. The DTE considered the factors in the Guidelines in assessing rate
11 treatment of merger savings. Essex is a small gas local distribution company at the end of an
12 interstate pipeline system. The DTE stated in its Order that Essex would be increasingly
13 challenged to respond to a competitive market dominated by larger utilities and that
14 ultimately the ratepayers would be losers if the merger did not take place. With respect to
15 effect on rates, the DTE stated:

16 The resulting net savings, and alternatives to the merger, the
17 Department found that approval of a 10-years freeze of base rates will
18 yield benefits to Essex's ratepayers and results in just and reasonable
19 rates. Further, the Department recognized that the proposed merger
20 would provide Essex's ratepayers with guaranteed savings in gas costs
21 that would be unavailable absent the merger. Based on our evaluation
22 of the Rate Plan, the Department also concludes that the five percent
23 rate reduction and 10-year rate freeze, in conjunction with the
24 opportunity for Eastern's shareholders to recover the costs associated
25 with the merger, represents a fair allocation of the benefits between
26 shareholders and ratepayers.

27 Significant among the specifics of the Massachusetts decision was a 10-year rate
28 freeze and an immediate rate reduction. This is a completely different circumstance than
29 what this Commission encountered with the Aquila-SJLP merger and Aquila's present

Rebuttal Testimony of
Janis E. Fischer

1 proposal. A condition of the approval was finding the Eastern/Essex transaction to be
2 “consistent with the public interest” or a “no net harm” standard. Under the Guidelines, the
3 extent to which recovery of the acquisition premium is permitted depends on the “no net
4 harm” analysis.

5 Q. Have there been other Massachusetts merger cases where the Guidelines were
6 applied?

7 A. Yes, the Guidelines were applied to another merger case in Massachusetts that
8 Mr. Siemek quotes. Mr. Siemek quoted on page 12, lines 35-38 of his direct testimony the
9 Colonial Gas Company (Colonial), DTE Case No. 98-128, Order dated July 15, 1999. In that
10 case, the DTE decided that a ten-year base rate freeze and a 2.2% reduction in the burner tip
11 price of gas for Colonial ratepayers was appropriate. A base rate freeze holds the base rate to
12 the same constant level of charge over the period the freeze is in effect. This is in contrast to
13 a base rate cap that only limits the maximum base rate to the current base rate charge.

14 As of the date of this rebuttal testimony, none of these companies to which
15 Massachusetts applied its Guidelines have completed a rate case proceeding to determine
16 actual merger savings. While the DTE’s Guidelines set standards for Massachusetts utility
17 mergers, the standards are not applicable to the present Missouri rate case.

18 **KANSAS CORPORATION COMMISSION ORDER**

19 Q. Please comment on the Kansas Corporation Commission (KCC), Docket
20 No. 99-WPEE-818 RTS, UtiliCorp United, Inc., Order relied on by Mr. Siemek on page 12,
21 lines 40-43 of his direct testimony to support the merger savings sharing proposal.

22 A. The KCC required that Aquila demonstrate that quantifiable savings were
23 created by the acquisition of Centel before it would allow recovery of the acquisition

Rebuttal Testimony of
Janis E. Fischer

1 premium. The acquisition premium was determined to be \$56 million and the merger
2 savings that the KCC approved Aquila to apply to the acquisition premium in the
3 proceedings was \$2,350,000.

4 Q. Please summarize the details of the acquisition from Centel.

5 A. On September 27, 1991, in Docket No. 175,456-U, the KCC allowed
6 UtiliCorp to acquire the electric assets of Centel subject to stipulated conditions. Centel's
7 assets were transferred to UtiliCorp at or about net book value. However, Centel's eight
8 percent ownership interest in Jeffrey Energy Center was transferred to Wilmington Trust and
9 leased back to UtiliCorp. Aquila operates the former Centel properties as its West Plains
10 division. The stipulation in Docket No. 175,456-U set a two-year rate moratorium, a
11 reduction in UtiliCorp's initial rate tariffs, a refund to retail ratepayers within the West Plains
12 service territory and prohibited UtiliCorp from seeking rate recovery of any acquisition
13 premium beyond the level of savings generated by the acquisition. UtiliCorp did not propose
14 a method for identifying and quantify savings in the initial acquisition case. UtiliCorp
15 presented little evidence of cost savings apart from general and administrative cost reductions
16 in its prefiled testimony in Docket No. 175,456-U. The determination of any acquisition
17 premium, the recovery of such costs and the issue of an appropriate measuring mechanism
18 for the merger savings were deferred until the UtiliCorp's next rate case. UtiliCorp then filed
19 a rate increase case in Kansas for its West Plains properties designated as Docket
20 No. 99-WPEE-818-RTS.

21 Q. What were the merger savings issues in the subsequent KCC rate case, Docket
22 No. 99-WPEE-818-RTS?

1 A. UtiliCorp attempted to persuade the KCC to classify as “merger savings” as
2 many cost reductions it had experienced as possible. Of the eight categories of “merger
3 savings” UtiliCorp presented to the KCC, only one was approved partial treatment as a
4 “merger savings.” The following excerpts from the KCC Order on Application specifically
5 address the merger savings issues in the West Plains case:

6 Page 7, 17. The Applicant identified seven areas of claimed savings to
7 support the recovery of the acquisition premium and submitted that the
8 savings greatly exceeded any acquisition premium paid to Centel.
9 Staff and CURB examined each area of claimed savings and
10 contended that the Applicant failed to show a nexus between the
11 claimed savings and the Centel acquisition...

12 Page 8, 18. The largest claimed savings is based upon the position that
13 the Applicant was entirely responsible for the reduced coal costs at the
14 Jeffrey Energy Center... It appears that the primary reason for coal
15 cost savings is Western’s motivation to lower its coal costs and that the
16 Applicant benefited from Western’s efforts...Moreover, the Applicant
17 failed to carry its burden of proof with respect to these claimed savings
18 and failed to establish that the coal cost savings would not have been
19 created but for the Centel acquisition.

20 Page 9, 20. ...The third source of claimed savings is a Power Plant
21 Matrix Agreement, which resulted in staff reductions and increasing
22 plant capacity factors... The evidence does not show that these savings
23 would not have been realized but for the Centel acquisition or that the
24 savings related to a sharing of personnel with West Plains... It appears
25 that this type of employee reduction was in line with prudent utility
26 management.

27 Page 9, 21. The fourth source of claimed merger savings is power
28 plant savings from efficiency programs recently implemented by the
29 Applicant in 1998. Similarly, the Applicant claimed savings in a
30 general work force reduction implemented by the Applicant four years
31 after the Centel assets were acquired. It appears from the evidence
32 that these types of claimed savings are the result of good utility
33 management and consistent with industry standards. The evidence
34 does not establish that these recent corporate changes and restructuring
35 efforts were related to the Centel acquisition.

36 Page 11, 24. The final claimed cost savings is a general work force
37 reduction implemented by the Applicant starting in 1995. This
38 reduction is said to involve 60 positions and is claimed to reduce costs

Rebuttal Testimony of
Janis E. Fischer

1 by over \$4.6 million... It appears that the workforce reductions were
2 the result of general economic changes in the electric industry that
3 were forcing all electric utilities to make such work force reductions.

4 Page 11, 25. ...In addition, the Commission notes that West Plains
5 initially failed to provide adequate evidence and testimony to
6 document their claimed savings and this failure unfortunately
7 complicated and prolonged these proceedings. [Emphasis added]

8 **IOWA UTILITIES BOARD RPU-02-5**

9 Q. Have you reviewed the 2002 testimony of Mr. Siemek in Aquila's Iowa
10 Utilities Board (IUB) Case No. RPU-02-05?

11 A. Yes, I have. Mr. Siemek addressed this case in his deposition on
12 December 30, 2003. Mr. Siemek proposed in the IUB Case No. RPU-02-05 that the Iowa
13 Board allow Aquila to retain certain cost savings resulting from the Aquila-SJLP merger case
14 related to economies of scale. In other words, any reallocation of corporate costs resulting in
15 a net decrease in expense to Iowa would be attributed to the Aquila-SJLP merger.
16 Mr. Siemek proposed that only 75 percent of reductions in costs due to the allocation of
17 shared services to Iowa be reflected in the cost of service to ratepayers. The other 25 percent
18 would be retained by Aquila.

19 Q. What did the IUB decide in Case No. RPU-02-05?

20 A. A settlement was reached in Case No. RPU-02-05. Aquila in its application
21 asked for a permanent rate increase of \$9.3 million. The settlement approved by the IUB
22 approved an annual revenue increase of approximately \$4.25 million, less than half of the
23 amount initially requested by Aquila. The IBU did not address the merger savings sharing
24 issue in its Order.

1 **STAFF'S CONCLUSIONS**

2 Q. Do the cases cited by Aquila to support the Company's merger savings
3 sharing proposal indicate that other states have adopted the sharing of merger savings under
4 similar circumstances to the Aquila-SJLP merger?

5 A. No. As can be seen from the above review of the merger cases cited by
6 Aquila as identified by Mr. Siemek in his direct testimony, they generally do not show
7 similar facts and circumstances surrounding the merger of Aquila-SJLP. Many of the other
8 state commission orders relied on by Mr. Siemek concern rate moratoriums and several
9 involved immediate rate reductions. These considerations are not relevant to the Aquila-
10 SJLP merger. Aquila did not reduce rates as part of the merger. The Commission did not
11 impose a rate freeze on Aquila. Aquila has been free to file for rate increases as soon as
12 Aquila believed it was necessary, as evident by its 2001 MPS rate increase filing and its
13 filing on July 3, 2003, in these cases and its filing on August 1, 2003, for a rate increase for
14 Aquila's natural gas operations in this state, Case No. GR-2004-0072.

15 In short, the cases from other state commissions do not support the merger saving
16 sharing proposal identified in Mr. Siemek's direct testimony and, as such, the Commission
17 should not place any reliance on them.

18 Q. Did the Staff's review of merger and acquisitions in other state jurisdictions
19 play a significant role in determining the Staff's position on merger related matters in the
20 Aquila-SJLP merger case, Case No. EM-2000-292, MPS's last electric rate case, Case
21 No. ER-2001-672, and the current rate proceeding?

22 A. No. The Staff's analysis of merger and acquisition orders in other
23 jurisdictions shows a wide variety of circumstances, proposals and resolutions to issues

Rebuttal Testimony of
Janis E. Fischer

1 arising in these transactions. While the commission orders provide historical details of each
2 case, the comprehensive review of documents that would be needed to fully assess the
3 situation throughout the states was not undertaken principally because of the size of the task.
4 My conclusion would be that each merger and acquisition should be viewed on its own
5 merits. As stated earlier in my rebuttal testimony, differences resulting from deregulation,
6 utility rates, quality of service, utility company stability and state requirements imposed by
7 rules and regulations influence state commission decisions. The Missouri Commission
8 should base its decision related to the sharing of merger savings in this case based upon the
9 circumstances specific to this case.

10 Q. Does this conclude your rebuttal testimony?

11 A. Yes, it does.

CASE PROCEEDING PARTICIPATION

JANIS E. FISCHER

PARTICIPATION		TESTIMONY
COMPANY	CASE NO.	ISSUES
Osage Water Company	ST-2003-0562 & WT-2003-0563	Test Year, Accounting Schedules, Revenues and Cost of Removal and Salvage
Union Electric Company d/b/a AmerenUE	GR-2003-0517	Direct - Rate Case Expense, Legal Expense, Corporate Franchise Tax, Cost of Removal and Salvage, Pensions and OPEBs
Laclede Gas Company	GR-2002-356	Direct - Pensions and OPEBs, Rate Base Asset, Incentive Compensation
Missouri Gas Energy, Division of Southern Union Company	GR-2002-292	Direct - Pensions and OPEBs, Other Employee Benefits, SERP, COLI Amortization
Missouri-American Water Company	WO-2002-273	Rebuttal - Security Costs, Accounting Authority Order Staff Criteria
Citizens Electric Company	ER-2002-217	Direct - Test Year, Accounting Schedules, Revenues, Purchased Power and Transmission, Other Revenues, Uncollectibles Expense
Union Electric Company d/b/a AmerenUE	EC-2002-1	Surrebuttal - Incentive Compensation
Missouri Public Service, Division of UtiliCorp United, Inc.	ER-2001-672 EC-2002-265	Direct - Pensions and OPEBs, Merger Transition/Transaction Costs, Merger Savings-SJLP, Revenues, Uncollectibles
Missouri Public Service, Division of UtiliCorp United, Inc.	ER-2001-672 EC-2002-265	Rebuttal - Merger Transition/Transaction Costs, Merger Savings-SJLP, Revenues, Uncollectibles
The Empire District Electric Company	ER-2001-299	Direct - Payroll, Pensions and OPEBs, Payroll Related Benefits, Payroll Taxes, Outside Services, Merger Costs, Miscellaneous Expenses True-up Rebuttal - Chemicals, Property Taxes
The Empire District Electric Company	ER-2001-299	Rebuttal - Payroll Expense, Bonuses and Incentive Pay
The Empire District Electric Company	ER-2001-299	Surrebuttal - Payroll Expense, Bonuses and Incentive Pay
The Empire District Electric Company	ER-2001-299	Supplemental Surrebuttal - Incentive Awards
The Empire District Electric Company	ER-2001-299	True-up Direct - Payroll, Payroll Taxes, Payroll Related Benefits
KLM Telephone Company	TT-2001-120	Direct - Revenue Requirement
UtiliCorp United, Inc./ Empire District Electric Company	EM-2000-369	Rebuttal - Merger Savings, Acquisition Adjustment, Tracking of Merger Savings

PARTICIPATION		TESTIMONY
COMPANY	CASE NO.	ISSUES
UtiliCorp United, Inc./ St. Joseph Light & Power Company	EM-2000-292	Rebuttal - Merger Savings, Acquisition Adjustment, Tracking of Merger Savings
Osage Water Company	WA-98-236 WC-98-211	Rebuttal - Financial Viability, Organizational Costs
Western Resources/ Kansas City Power & Light Company	EM-97-515	Rebuttal - Merger Savings, Tracking of Merger Savings, Transaction Costs, Costs to Achieve
Union Electric Company d/b/a AmerenUE	GR-97-393	Direct - Cash Working Capital, Materials/Supplies, Prepayments, Federal/State Income Tax Offset, Purchased Gas Offset, Interest Expense Offset
The Empire District Electric Company	ER-97-81	Direct - Dues and Donations, Advertising, Rate Case Expenses, PSC Assessment, Non-Health Insurance, Miscellaneous Expenses