STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

In the Matter of Aquila, Inc. d/b/a Aquila Networks L&P and Aquila Networks MPS, and Its Tariff Filing to Implement a General Rate Increase for Electric Service

Case No. ER-2004-0034

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Volume 15-A
(Continuation of Volume 15)

In the Matter of Aquila, Inc.)
d/b/a Aquila Networks L&P)
and Aquila Networks MPS, and)
Its Tariff Filing to) Case No.: ER-2004-0034
Implement a General Rate)
Increase for Electric Service)

KENNARD L. JONES, Presiding,
REGULATORY LAW JUDGE.

CONNIE MURRAY,
COMMISSIONER.

REPORTED BY:
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P R O C E E D I N G S

(EXHIBIT NO. 176 WAS MARKED FOR IDENTIFICATION.)

JUDGE JONES: All right. Where we left off was questions from the Bench of Dr. White. And I believe, Commissioner Murray, you can finish your questions.

COMMISSIONER MURRAY: No questions.

JUDGE JONES: Will there be recross from the Office of the Public Counsel?

MR. MICHEEL: No, Your Honor.

JUDGE JONES: Okay. From the Staff of the Commission?

MR. SCHWARZ: I have a couple questions.

JUDGE JONES: Okay.

RON WHITE, having been previously sworn, testified as follows:

RECROSS-EXAMINATION BY MR. SCHWARZ:

Q. Dr. White, is it fair to say that the principle differences, at least as far as dollars are concerned between Staff and the Company, are due to the use of -- the Company's use of remaining-life technique and the Staff's use of whole-life -- the Company's use of terminal dates on the lifespan property and the Company's forward-looking net salvage?

A. That's a fair statement.
Q. Is Missouri Aquila's largest operation -- regulated utility operations?
A. I want to say yes.
Q. So as far as -- as other states using remaining-life technique, for instance, those -- those states aren't as -- as big operations for Aquila as Missouri is; is that --
A. That would be true, I believe.
Q. I think Commission Murray asked just if there were -- you know, what in this depreciation process is certain.
Would you agree that the original cost, once a plan is placed, is known and certain?
A. I -- I certainly would. And what I was referring to was the parameters that enter into a depreciation rate. I mean, in that sense the recorded depreciation reserve is certain, too.
Q. And I think that in a line of questions about reserve imbalances you said that we refine our estimates as time passes.
Do you recall?
A. That's correct.
Q. Aren't you really making new estimates for a different population?

A. Not necessarily. The -- the context of the population that we discussed earlier -- let's take a full-line account, for example -- I'm still trying to estimate undoubtedly the parameters of the same parent population.

And -- and while I have a different sample, okay, the population remains the same.

Q. So that if Aquila's next rate case is in 2007, and you do a depreciation study then, you'll simply be -- be revie-- reviewing the current depreciation study, you don't be -- be --

A. Oh, no. No. That's not what I said. I said I'll have a different sample. That means in 2007 I will have additional retirement experience, additions, transfers, adjustments. I've changed the sample. I've changed -- I've reached in and I've grabbed a different handful now --

Q. But there's a different --

A. -- of my --

Q. -- population, too, isn't there?

A. No. The parent population is still the same that I'm trying to estimate the parameters from.

Q. So -- so -- and -- and maybe I'm confused about the remaining-life technique. My understanding was that -- that you are -- the remaining-life technique estimates the remaining life for the specific plant still in service at a date certain; is that correct?

A. We're -- we're -- we're confusing concept, again, now.

Q. Is that -- well, but is that correct?

A. May I have the question read back, please?

MR. SCHWARZ: Can you read that?

(THE COURT REPORTER READ BACK THE REQUESTED PORTION.)

THE WITNESS: No. It has nothing to do with the plant in service. The way Staff has calculated their depreciation rates -- all that we need to know is the weighted average age of plant that's in service.

The plant balance has nothing do with it. If I use a vintage group procedure, now the dollars amount -- amount in service by vintage-year placement enter into the calculation of the remaining life.

But remember that's in the phase of the depreciation study where we calculate the depreciation rate. What we were talking about earlier was the estimation of parameters -- estimating the service life, the projection curve, the projection life.

That has nothing to do with the calculation of remaining life that goes into the depreciation rate.

BY MR. SCHWARZ:

Q. But is the -- are the remaining-life estimates applicable to a specific population which is the surviving -- the -- the plant in service as of the date of the study?

A. Again, I -- I -- I'm not trying to be argumentative at all, only trying to understand concept. With a broad-group procedure where we assume that every vintage has the same average service life, all I need to know is the weighted average age of the plant.

I could care less about the dollars that are actually on the plant books. All I need to know is its age. If I know its age, I can estimate the remaining life.

Q. Well, going back to my example of -- of where you are in 2007, in 2007 you will have a study where the -- the -- the population of that study is different than the population of this study.

There will be plant that's been added in 2005, 2006; is that --

A. I think we're using the term "population" in two different senses. If you mean that my plant account is going to have a different composition to it, because of the age of the dollars, I've had additions, I've had retirements, I would fully agree -- I would fully agree.

From a statistical standpoint, looking at that plant account for estimating statistics -- projection curve, projection life, the statistical analysis that we do, it's a different sample. It's a different sample, not a different population.

Q. Well, how -- how do you use the term "population" then?

A. Ex-- exactly the way we discussed it earlier. I -- I -- I -- I described our plant account as being a sample from some parent population. I used the hat analogy and a handful of marbles in my hand. It's what's in the hat that's the population, and that's the parameter that I'm trying to estimate for depreciation rates.

That's why we use those survivorship functions. Those are probability distributions. We use probabilities to draw inferences about the parent population.

JUDGE JONES: Does that mean you're finished?

MR. SCHWARZ: Yes, sir.

JUDGE JONES: Okay.

COMMISSIONER MURRAY: Judge, I'm -- I'm sorry, but I forgot about --

JUDGE JONES: Go right ahead.

COMMISSIONER MURRAY: -- something else I forgot to ask him.

JUDGE JONES: That's fine.

COMMISSIONER MURRAY: I apologize. I hope this doesn't prolong things, but I did want to ask you something for clarification and forgot earlier.

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. In terms of interim net salvage and termin-- terminal net salvage, is there a rationale for treating those differently?

A. Not in the context of setting the depreciation rate. Interim net salvage, of course, refers to the cost removal and salvage that would be realized on complement (sic) parts of a larger facility.

The terminal net salvage is when all of the plant is conterminously retired -- a production plant, for example. The treatment in the depreciation rate calculation itself is the same.

Q. Okay.

A. The -- the magnitude of the rates may be quite different, and how they are combined to develop one rate to be used in the depreciation rate formula is -- is another question, but the treatment is the same.

Q. And that's what I wanted to know if there was any reason -- reason to treat them differently --

A. No.

Q. -- and you say no.

All right.

A. No.

COMMISSIONER MURRAY: Thank you.

JUDGE JONES: Will there be recross based on questions from the Bench?

MR. SCHWARZ: No.

JUDGE JONES: And now we move to redirect from Aquila.

MR. ENGLAND: No redirect, Your Honor.

JUDGE JONES: Thank you.

Dr. White, you may be excused.

THE WITNESS: Thank you.

(Witness excused.)

JUDGE JONES: We'll move to Aquila's second witness.

MR. ENGLAND: We'd call Davis Rooney, Your Honor.

JUDGE JONES: Mr. Rooney, will you raise your right hand, please?

(Witness sworn.)

JUDGE JONES: You may be seated.

MR. ENGLAND: Your Honor, before I begin my examination of Mr. Rooney, I've got some revised schedules that we'd like to have marked as separate exhibits, please.

JUDGE JONES: Okay. This will be Exhibit No. 180.

MR. SCHWARZ: I'm sorry, Judge. What was that number again?

JUDGE JONES: 180.

(EXHIBIT NO. 180 WAS MARKED FOR IDENTIFICATION.)

JUDGE JONES: You may proceed.

H. DAVIS ROONEY testified as follows:

DIRECT EXAMINATION BY MR. ENGLAND:

Q. Would you state your name for the record, please.

A. H. Davis Rooney, R-O-O-N-E-Y.

Q. And by whom are you employed?

A. Aquila.

Q. And what is your capacity with Aquila?

A. I'm director of financial management.

Q. And what is your business address, Mr. Rooney?

A. 10750 East 360 Highway, Raytown, Missouri.

Q. Mr. Rooney, did you cause to be prepared and filed in this docket three pieces of testimony, the first being the direct testimony of H. Davis Rooney?

A. Yes.

Q. I believe that's been marked for purposes of identification as Exhibit 38.

Do you have any corrections or changes to make at this time?

A. To my direct testimony, yes, I have two corrections. On page 3, line 4, replace the word "traditional" with "accrual," and on page 3, line 7, replace "this traditional" with "the accrual."

JUDGE JONES: Was the second, page 3, line 7?

THE WITNESS: Line 7, yes.

BY MR. ENGLAND:

Q. Actually on mine it begins at the very end of line 6 with the word "this" --

A. Okay.

Q. -- and then carries over to the beginning of the next line, 7, traditional.

So you're striking those two words, "this traditional"?

A. Yes.

Q. And inserting what again, please?

A. The accrual.

MR. MICHEEL: Could you give me the first one again? I'm sorry. I missed it.

MR. ENGLAND: (Indicating.)

MR. MICHEEL: Thank you.

BY MR. ENGLAND:

Q. Any other changes to your dir-- direct testimony, Mr. Rooney?

A. No.

Q. Turning your attention to what I believe has been marked for purposes of identification as Exhibit 39, your rebuttal testimony, do you have any changes or corrections to that?

A. Yes. As a result of the schedules you just introduced, I have some amounts that need to be changed in my testimony.

On page 12, line 16, replace $3.9 with $4.5; on page 12, line 17, replace $3.9 with $4.5; on page 12, line 18, replace $900,000 with $3.4 million.

And those are all the changes.

Q. And then turning your attention to an exhibit that's been marked just recently as 180, would you please identify that for the record, please? That's the two-page exhibit that was just marked when you took the stand.

A. These are the replacement Schedules 1 and 2 in my rebuttal testimony.

Q. Schedule HDR-2?

A. HDR-1 and HDR-2, yes.
Q. And they replace the -- or revise the comparably marked schedules attached to your rebuttal testimony?
A. Yes, they do.
Q. Thank you.
Have we taken care of any and all corrections to your rebuttal testimony and schedules?
A. Yes, we have.
Q. Okay. Turning your attention, then, to your surrebuttal testimony that's been marked, I believe, for identification as Exhibit No. 40.
Do you have any corrections or changes to that testimony?
A. No, I do not.
MR. ENGLAND: Okay. Your Honor, I think we've identified the exhibits that this witness is sponsoring, made the corrections we think are necessary, and I would offer at this time Exhibits 38, 39, 40, 180, and then I guess the redacted counterparts 1038, 1039 and 1040.
JUDGE JONES: Any objections?
(No response.)
JUDGE JONES: Exhibits 38, 39, 40, 180, 1038, 1039 and 1040 are admitted into the record.

(EXHIBIT NOS. 38 THROUGH 40, 180 AND 1038 THROUGH 1040 WERE RECEIVED INTO EVIDENCE.)

MR. ENGLAND: Thank you, Your Honor.

And I tender the witness for cross-examination.

JUDGE JONES: Will there be cross-examination from the Office of the Public Counsel?

MR. MICHEEL: No.

JUDGE JONES: Cross-examination from the Staff of the Commission?

MR. SCHWARZ: Yes, Judge.

JUDGE JONES: Okay.

CROSS-EXAMINATION BY MR. SCHWARZ:

Q. Good afternoon, sir -- evening, sir.

Your direct testimony says that you practiced in public accounting. By whom were you employed prior to joining Aquila?

A. Arthur Anderson.

Q. And how long were you there?

A. I was there nine years.

Q. Okay. Were you a partner?

A. I was a senior ma-- a senior manager.

Q. Okay.

A. I think they -- I think maybe the right term would be "experienced manager" when I left, so --

Q. And what were your jobs as controller of -- well, let me ask you, what is West Plains -- what is the West Plains or what was the West Plains Energy Division?

A. The West Plains Energy Division is the electric operations of Aquila in Kansas and Colorado.

Q. And what were your duties with them?

A. As controller I supervised the accounting department of -- of both of those states' operations and prepared analysis and -- and supervised the -- the accounting operations.

Q. Okay. In order to achieve intergenerational equity, do you need to know the costs that are to be divided among and between the various generations?

A. You need to have an estimate, yes.

Q. Well, but you need to know the costs that are to be divided, do you not? I mean, es-- estimates won't result in intergenerational equity, will they?

A. Yes, they can.

Q. How -- if the estimates turn out not to be historically accurate, you know, as -- as things eventuate, how can you achieve intergenerational equity?

A. Suppose that you have an estimate that per year you need, say, $100 of expense to collect from your ratepayer, and it turns out that it should be $101, and the alternative is to use zero. 100 would be closer to 101 and would be closer to intergenerational equity than zero.

Q. So it's closer.

But in order to achieve intergenerational equity, you actually have to distribute the costs equally among the different generations of ratepayers; isn't that correct?

A. I don't think perfection is necessary to achieve an adequate level of intergenerational equity.

MR. SCHWARZ: I didn't ask that.

I'd ask that he answer my question.

JUDGE JONES: Answer his question.

THE WITNESS: May I hear it again, please?

BY MR. SCHWARZ:

Q. In order to actually achieve intergenerational equity, you actually have to divide the costs among -- the actual costs among the different generations of ratepayers?

A. Yes.

Q. Now, I'll follow up. Given that not all costs are known at any particular point in time, is it necessary to make estimates to achieve a measure of intergenerational equity?

A. Yes, it is.
Q. Okay. And has Aquila, to your knowledge, ever conducted a study to determine that the amounts it collected in rates for costs of removal or net salvage actually equaled the costs to remove a particular vintage of property that has been completely retired?
A. No, it has not.
Q. Assuming for the moment that the accrued reserve for Account 311 structures and improvements at the Jefferson -- or Jeffrey Energy Center on 12/31/01 was $12,530,615, can you tell me how much of that was accrued for cost of removal, and how much was accrued as recovery of the Company's original investment in that account?
A. That's for -- for the Jeffrey --
Q. Right.
A. -- Energy Center?
No, I cannot.
Q. When plant is retired, the retirement will reduce the account balance; is that correct?
A. Yes.
Q. It will also reduce the reserve for depreciation by the same amount; is that --
A. Yes.
Q. And the reserve for depreciation will also be

reduced by any co-- net cost of removal over and above the -- any salvage; is that --

A. Under current methods?

Q. No, under the method proposed by the Company.

A. Yes.

Q. Okay. Has Aquila ever been unable to book the retired plant to the account at the time plant was retired, because there wasn't a sufficient accrual in the reserve?

A. I don't think those are mutually exclusive, so I guess the answer would be no.

Q. If -- if -- if you're not -- I take it you're not clear what I was asking.

A. Yeah.

Q. Let me --

A. Ask again.

Q. -- try again.

Has Aquila ever retired plant and there not be a sufficient accrual in the reserve to accommodate that re-- retirement; that is --

A. You're -- you're asking --

Q. -- the -- the property that was retired was, say, $100, but there was only $50 in the reserve?

A. I believe that has happened before. It's not frequent, but it has happened.

Q. Has -- has it been significant amounts, do you know?

A. I -- I don't know.

Q. In your rebuttal testimony on page 6 in my version -- I think I may have printed this off of EFUS, so the lines may not exactly match -- there's a -- a question that be-- on my version on line 10, Question: How can harm arise?

Are you there?

A. Yes. At line 4, yes.

Q. Right.

A. I guess there's the same question on line 10, so --

Q. Oh, so there is.

I'm looking at the line 10 ques--

A. Okay.

Q. -- question.

And I think you indicate that lenders and investors might note in-- instability; is that --

A. Yes.

Q. Do you think that since 2001, when the depreciation practices changed, that lenders and investors in Aquila have been more affected by the depreciation change or by the problems with Aquila's non-regulated activities?

A. I -- I guess I don't know for certain on that. I would --

Q. Well, let me ask you, which is -- which to lenders and investors would -- would be a larger dollar problem?

A. Well, I expect that the non-regulated activity was the larger dollar in the past.

Q. Again, on page 6 in my version on line 21 you say that you believe a $13 million per-year change in cash flow and a 40 percent change in depreciation is -- is noteworthy.

Do you think that -- well, let me ask you this: Is that in reference to the rates and revenues that were sent in 2001 and are currently in place, or is that in reference to the 1997 rates and revenues?

A. That was in reference to the 1997 rates then.

Q. And do you -- do you think that currently investors and creditors are looking at Aquila's books and records from 1997 or from current books and records?

A. I think they're looking at current books and records.

Q. I noticed that on HDR-1 and HDR-2 you source your information from the FERC Form 1; is that correct?

A. Yes, it is.

Q. Neither Ms. Schad nor Dr. White did so; is that -- that your understanding?
A. Yes, it is.
Q. Page 16 you give an ex-- an example about the costs of removing a pole. And you say, if the pole cost $1,000 to install it, it will cost about $750 to remove. And I -- I think that's based on prior studies.
If -- if you have two poles and it costs $1,000 to install each of them, and one of them -- they were installed at the same time, and one of them retires next year and the other one retires in 20 years, do you think it'll cost the same to remove them?
A. No. My understanding of the calculation of that average rate that I used to calculate that is that it accounts for the differences in the values that accrue over time for those removals.
Q. At page 17 of your rebuttal you mention the St. Joe Water case, where a lifespan plant was retired, and note that Public Counsel tried to have those costs disallowed.
Are you -- are you there?
A. Yes.
Q. What was the com-- what was St. Joe Water's

position in that case?

A. I believe it was they were seeking recovery of that.

Q. And what was Staff's position?

A. I believe Staff was -- was seeking to allow them to recover that.

Q. And what did the Commission order?

A. I believe the Commission ordered that they wouldn't recover that in that initial case.

MR. SCHWARZ: I'd ask that the Commission take notice of its decision in 2000-281.

JUDGE JONES: You do realize that we aren't bound by our previous --

MR. SCHWARZ: No, I understand.

JUDGE JONES: Okay.

MR. SCHWARZ: But just as to the facts of what happened.

JUDGE JONES: All right.

Commissioner Murray, do you have questions of Mr. Rooney?

COMMISSIONER MURRAY: Is Mr. Schwarz finished?

MR. SCHWARZ: No, I -- yeah. Oh, sorry. I should have --

COMMISSIONER MURRAY: He just wanders off now and then.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good evening, I guess it is.

A. Good evening.

Q. Let's see the questions that I have for you. The exhibit, 180, that was just entered, that's a substitute for one of your schedules, right?

A. Yes.

Q. Okay. And that is to demonstrate that using Staff's method for treatment of net salvage, that even if a new rate case were filed every year, there would be an underrecovery amounting to the -- the columns -- the last two columns; is that right -- is that what those last two columns are showing?

A. Yes.

Q. And the -- the column showing 10 percent lost return, what do you mean by that?

A. Under the rate-base method, the over or underrecovery would be included in rate base, and would be allowed a return either to the benefit of the ratepayer or the -- the benefit of the Company, depending on whether it was an over or underrecovery.

In this case the example or the illustration shows an underrecovery by the Company. And I've calculated what the -- the lost return would also be compared to had it been included in -- included in rate base under the rate-base method.

Q. Okay. So over the years that were cited there, that would be the total of lost return?

A. Yes.

Q. On page 49 of your surrebuttal testimony, you speak on line 10 about references that Ms. Schad makes in her testimony. And you indicate that you have had outstanding recovery requests -- or discovery requests, rather, on Staff's calculations that you had not received.

Have you received those?

A. We have.

Q. And did you respond to the question that you were asked there?

A. Based upon the responses that I've gotten, I'm still not in a position to fully reconcile that number. And I -- I think that there are some differences that still exist between Staff's calculation of that 14.5, and what I think may be a more appropriate number, but we -- we haven't resolved that at this point.

Q. Okay. When did you receive the discovery?

A. I think I received it on the same -- same day or the -- or the evening before I filed this testimony.

Q. You indicate on line 16 and 17 that gross salvage is a reduction of the Company's cost and is

given to the ratepayers as a benefit.
Do you see that?
A. Yes.
Q. So in your example of a $1,000 utility pole that there's an estimated cost of removal of $750, if the -- if rather than the cost of removing it, there were a gross salvage value of $750 at retirement, would the effect of that be that only $250 would go into rate base and be depreciated over the life of the asset, or how would that be treated?
A. Yes, there would be a reduction of the depreciation rate, so that you would have net reduction in depreciation to take -- take into account that expected salvage amount.
Q. And you would also have an -- a reduction in the total cost of the asset that would go into rate base; is that right?
A. The total cost of the asset would still go into rate base, because the salvage hadn't been received yet. But the depreciation would be lower -- the amount of the return of investment would be lower during the life of the asset in anticipation of the salvage that would be received at the end.
Q. Okay. So you would get the return on the initial investment of $1,000 until it was retired, and

then -- walk me through, again --

A. Yea.

Q. -- what would happen to the 750?

A. The -- the Company invests $1,000 and they're looking for a return of that $1,000. If they expect $750 of salvage at the end of the life of the asset, then they would -- they would collect from the ratepayer $250. And then at the end of the life when they actually salvaged that pole, they would receive the other $750 from the effect of salvaging that pole.

So over the life of the asset they would receive $1,000, their original investment back, 250 from the ratepayer and 750 from salvaging the pole at the end of its life.

Q. And you're speak -- you're talking about the return of?

A. Yes.

Q. And they would also earn the return on their initial $1,000 --

A. Yes.

Q. -- investment?

A. Having laid out $1,000 to install the pole, they would get return on that $1,000 until they got return of the $1,000. So they would receive return on their investment until it -- until it was returned.

Q. And under the method of treatment of net salvage that you're recommending, any investment in an asset such as that, the Company would receive -- be able to earn a return on that investment, including whatever cost of salvage there was, is that correct, if it was a net salvage?

A. If -- if it was a -- if it was a net salvage, it would -- after they received the salvage, it would be a reduction of the rate base. If it was a net cost removal, it would be an increase to rate base until they collected it.

Q. Okay. I'm not asking my question very well.

If you had an asset that, let's just say, cost $1,000 and then the cost of removal was $500, and there was no positive salvage value, $1,500 would go into rate base; is that correct?

A. Initially only $1,000 would go into rate base, because that was the initial cash outlay. The -- under what I'm proposing the depreciation rate would be somewhat higher over the life of the asset in order to collect the $500 from the ratepayers, such that at the end of the life of the asset you will have collected $1,500 from -- over the life of the asset, you'll have collected $1,500 from the ratepayer to pay for the $500 to return the $1,000 that you initially invested and to pay for the $500 that you would incur at the end of the life of the asset to retire the -- to retire the asset.

So the -- the rate -- each -- the ratepayer in each year would be paying for a portion of not only the cost of that asset serving them, but also the cost that it will ultimately take to retire that asset at the end.

Q. Okay. And that is only reflected in the depreciation accrual, it's not reflected in the rate base -- the cost of retirement; is that what you're telling me?

A. It's -- yes. It's accrued in the -- through the depreciation accrual.

Q. Okay.

A. At the -- at the end of the life of the asset then the accrual is matched against the actual expenditure. And if there's any net difference, that would remain in rate base to be amortized back as either a benefit to the ratepayer if it was -- if we overcollected or as a -- as a future amount to be collected from the ratepayer if we undercollected.

Q. So if -- if that is the case -- it doesn't go into rate base, then the Company is not earning a return on the cost of removal, is that correct, but only a cost of -- only a return of the cost of removal?

A. Under that, yes -- under that example, yes.

Q. And is that the proposal that the Company is making here?

A. Yes.

Q. So when you talk about rate-base accounting for treat-- rate-base accounting treatment of net salvage, why do you call it rate-base accounting?

A. Well, the -- because the amounts are being matched up in rate base. And if there's a mismatch, that amount remains in rate base.

So perhaps when -- when you asked your question about the $1,000 and the $500 of removal costs and you say, well, is the $500 in rate base -- if we're collecting for that cost of removal over the life of the asset, then that collection of the cost removal is reducing rate base.

And by reducing rate base, it's reducing the cost to the customer during the -- while we're collecting it. And then when the actual cost removal is incurred at the end of the life of the asset, that's matched up against the amount that we collected.

So -- so if there's a mismatch in that, that remains in rate base. Because by the -- by the end of the life of the asset, the asset -- the rate base will be reduced by $500 for having collected the cost of removal. And when the cost of removal is incurred, that will be matched against the $500 that was collected over the life of the asset.

Q. Okay.

A. And if there was a net difference, that would remain in rate base. And that's why it would be considered a rate-base treatment. It's really dealing with the -- the net difference.

Q. Okay. But you're depreciating the initial cost of the asset over the life of the asset as well, and deducting that from rate base --

A. Yes.

Q. -- annually?

A. Yes.

Q. So the rate base is al-- already being reduced by the initial -- by the accrual of the original cost of the asset?

A. Yes, it is.

Q. And if you were both accruing the depreciation for the original cost plus depreciation for the cost of removal and reducing rate base by both of those amounts each year, won't you exhaust the rate base account for that asset prior to its for-- or prior to trying to remove it?

A. If -- if there were only one account -- if there were only one asset, that might be true. But in -- where you have a -- like a -- poles where you have assets constantly being added and retired, that -- that is not occurring.

What you're doing is you're spreading the cost of that $500 of removal over the life of the asset to the customers. And when you incur that $500 at the end, that's also being added to rate base.

So ultimately you have $1,500 of costs that you reported and $1,500 of recovery that you reported.

Q. On page 3 of your rebuttal testimony at line 19 the statement, the ratepayers receive the Company's cost of capital as return on any overcollected money through the reduction of the Company's rate base until they receive return of their money through lower depreciation rates -- would you explain that sentence?

A. Yeah.

If we overcollect, say $100, that gets -- is a subtraction to rate base. And so as a subtraction to rate base the cost of capital to the ratepayers -- the cost of the return-on component of ratemaking is reduced by the return on that $100 in our rate cases.

As a reduction of our reserve -- or as a reduction of rate base that's reflected in our reserve, ultimately that will flow through the depreciation study, as Dr. White testified, through the process of doing updated depreciation studies. And that will result in a lower depreciation rate at some point in the future that gives return of that $100 back to the ratepayer.

So during the time that we have overcollected it, the ratepayer receives a return on the money that we overcollected. And when the rate -- depreciation rates reflect that overcollection through a reduction of the depreciation rate, then that's where the ratepayer gets a return of their money.

Q. For some reason it's not registering with me how the ratepayer can be receiving a return on.

A. If I had a $1,000 investment and a 10 percent return, we would have a revenue requirement of the return on that $1,000 of $100.

Had I overcollected $100, I would only have $900 of rate base. And at 10 percent return on that 900 the -- the cost to the ratepayer of that rate base would only be $90 instead of 100.

So the ratepayer would receive the benefit of a $10 reduction in their revenue requirement, as a result of that lower rate base. And the -- and the cost of service treatment where that doesn't go into rate base if I overcollect that -- that $100, then that doesn't ever give a benefit back to the -- that benefit never gets back to the -- to the ratepayer either in return of or return on.

So their -- their return on is reflected in a reduction of their cost of money -- in a reduction of the return on rate base, because rate base has been reduced.

Q. On page 7 of your rebuttal testimony the answer that you give beginning on line 1 -- it goes through line 8?

A. Beginning on line 1?

Q. Yes. Through -- through line 8. I'm on page 7.

A. Yes.

This was dealing with how net salvage has been treated historically?

Q. Yes.

And I was wondering if -- the example that you give there, could you -- would you just mind walking through that?

A. Well, line 1 actually starts the question on line 23 of the previous page, which has to go with the -- the magnitude of net salvage.

And the magnitude of net salvage can -- can --

here I'm just noting that -- that it can fluctuate significantly from year to year, changing from close to zero to $3 million in any given year. And my comparison was just that -- that that's sizable in comparison to the amount of rate change that occurred in our last rate case.

The next question there was, how has net salvage been treated in the past? I simply looked back at FERC Form 1's for various years, and noted that it had been treated in a -- am I on the right page or --

Q. I don't believe so.

A. Page 7 of the rebuttal?

JUDGE JONES: You all may have different versions.

COMMISSIONER MURRAY: We may have.

BY COMMISSIONER MURRAY:

Q. But I -- I'll -- I'll tell you the question -- the question began on line -- on page 6, and it -- well, actually the question only said, is net salvage noteworthy?

MR. SCHWARZ: Page 14, line 6 in my version.

COMMISSIONER MURRAY: Well, all of the versions are very different then. It's on page 6 of my copy.

BY COMMISSIONER MURRAY:

Q. And the answer refers to ER-97-394?

A. Yes, I -- I've got that here now. Where I -- where I say that Staff Witness Ms. Schad had quantified her view of Staff's previous accrual recommendation in that case at $13 million --

Q. Yes.

A. -- and that this amount did not include any amounts for terminal salvage.

I was pointing out -- as-- asking whether or not it's a sizable number, and I was pointing out that -- that $13 million was about 40 percent of Staff's recommended depreciation rate in this case. And I was pointing out that it -- that the net salvage number has been -- is a -- is a sizable number and has been a sizable number in prior cases.

Q. Okay. And that's what you were attempting to point out there.

And why -- what is the rationale or -- or, if you know, for the separating out terminal salvage in 3-- in ER-97-394?

A. Well, I think -- I think that it was -- simply that it was a -- that it was a -- a -- a large number and it was being distinguished from the day-to-day-type retirements or cost removals that -- that occur on an ongoing basis in the -- in the -- in most of the other mass accounts.

I -- I -- I think there was some discussion in that case about separating it out, because -- because it was a -- more of a fixed event in the future than -- than an ongoing event currently.

Q. The Report and Order stated, the Commission finds that terminal net salvage costs are speculative and not known and measurable and, therefore, may not be included in current rates. The Commission adopts the proposed Staff adjustment.

So apparently the adjustment was only for the terminal net salvage and not for the incremental net --

A. Yes, it --

Q. -- salvage?

A. Yes, it was.

Q. And is that something that's unusual to separate those in that -- that manner?

A. I guess I -- I don't know if it's unusual, but I know that -- that the salvage cost or the net cost removal cost is viewed similarly for purposes of depreciation as a cost that will ultimately be paid -- or will ultimately be incurred by the Company at the end of the life of the -- of the asset as other cost removals are.

So I -- I guess -- Dr. White had also

testified that he didn't see any distinction between those two.

Q. And you don't see any distinction either, in terms of the way they should be treated?

A. No, because it -- it is a cost of serving the current customer that that property will -- that that asset is serving the current customer, and this will be a cost incurred at the end of the life of that asset.

And so it should also be a cost collected from the current customer, because it's -- it's part of the cost of serving the current customer.

Q. On page 10 of your rebuttal you -- you indicate that rate-base treatment is compatible with both the accrual amount and the average annual amount.

So that regardless of whether the Commission allows the accrual amount or the average annual amount, it should be treated in a traditional rate-base manner?

A. Yes.

Q. Is that right?

A. Yes.

Q. Do you know -- and did you review Case No. ER-97-394 in preparation for your testimony?

A. Yes, I did.

Q. Do you know how the Commission treated the terminal net salvage costs that apparently -- well, do

you know how they treated --
A. In -- in -- in ER-97-394 they excluded those costs from the -- from the calculation of the depreciation rate and the -- and the cost removal accrual.
Q. And they had excluded it from any treatment in rate base?
A. That wasn't -- wasn't clear. I would say the answer to that would be no. That had we incurred terminal net salvage, I think we would have charged that to the rate base. So it -- it was not -- that's still where it would have been charged.
Q. Okay. So that was left unclear in that?
A. I -- I think that since the rest of the net salvage was being charged to rate base, that would have been the -- that -- it would have been the place we would have charged that.
Q. Okay. And I'm assuming that decision -- that Report and Order in ER-97-394 was a departure from the way that the Commission had been treating terminal net salvage in the past. Do you know?
A. In terms of including it in the depreciation rate, I don't know whether it was a departure or not. They had been allowing -- prior to that, they'd been allowing the actual costs occurred, and in their -- in

their calculation of the depreciation rate.

So I think that we have had some terminal salvage on some of our plants. I think one of our -- Richard Green plant we had some terminal salvage. We haven't completely removed that plant, but we've taken it out of service and been removing -- and had some removal costs.

So those would have been recovered through the method, but it would not have been included in the depreciation rate itself. So it would have been included as a rate-base method and charged a rate base and included in the calculations of recovery for the future.

COMMISSIONER MURRAY: All right. I -- I think that's all I have.

Thank you.

QUESTIONS BY JUDGE JONES:

Q. I just want to make sure I understand the difference between Aquila's position and Staff's. It seems that you all are in disagreement over the speculative nature of -- of net salvage; is that a fair statement?

A. Yes.

Q. Well, if the Company purchases something for a million dollars and it has a 20-year life and Aquila speculates that it may be able to salvage $250,000 20 years from now, it's Aquila's position that ratepayers today should pay for that $250,000 20 years from now?

A. Are -- are we talking salvage or cost --

Q. Yes.

A. -- of removal?

Q. Well, cost of removal.

A. Cost of removal, yes.

Q. Well, now, since you brought up salvage, if it's -- if the salvage is -- I guess there are two ways to look at salvage. They can be greater or less than cost of removal.

If it's greater than cost of the removal, then -- then you have a profit, so to speak, and you'll -- you'll make money when you get rid of it.

How does that affect the ratepayers 20 years now from today?

A. Yeah, I -- I think the important thing to note about the rate-base treatment is -- is that you're matching the estimate with the actual. And that any difference that occurs between the estimate and the actual is carried forward and -- and balanced in the future.

So, for example, if we estimated that the $250 of cost removal and it turns out to be over 200, we don't come out ahead by $50 on that. The $50 difference is held in the depreciation reserve on the rate -- on -- in rate base until --

Q. No, I don't mean your estimate's off.

A. Oh, okay. I'm sorry.

Q. I mean, if it cost -- if it cost is $250,000 to re-- to remove the product, get rid of it, but the salvage is 275,000 so you make $25,000, how does that -- does that benefit ratepayers?

A. Yes.

Q. How?

A. That goes back in as a reduction of rate base. So the re--

Q. Well, but it reduces rate base when?

A. At the time that it's in-- at the time that it is incurred at the end in the --

Q. 20 years from now?

A. Well, if -- if your estimates were accurate --

Q. Right.

A. -- it would --

Q. Assuming that.

A. -- it would benefit them over the life of the asset. So if -- if you -- if you estimated that you were going to come out ahead 25,000 --

Q. Uh-huh.
A. -- then your depreciation rate would be lower over the life of the asset by a total of $25,000.
Q. Okay.
A. So they would benefit over the life of the asset for that estimate.
JUDGE JONES: Okay.
Will there be recross?
MR. SCHWARZ: Yes.
RECROSS-EXAMINATION BY MR. SCHWARZ:
Q. You had a -- a series of questions from Commissioner Murray that I'd like to expand on.
The Company calculat-- calculates the depreciation expense based on -- for regulatory purposes, based on the original cost of the plant and service; is that correct?
A. Yes.
Q. That is, unlike the rate base for purposes of depreciation calculation, the depreciation rate is charged against the original cost of the property until such time as that plant is retired; is that correct?
A. Yes.
Q. So -- so that -- that's a distinction between the base -- against which depreciation is calculated and rate base? Rate base is actually reduced every

month by the depreciation expense?
A. Yes, it is.
Q. Okay.
A. And it's increased by any new additions or --
Q. Correct.
A. -- retirements that accrue --
Q. Right.
A. -- also.
Q. The return on the rate base that ratepayers get isn't actually realized until there's -- until the next rate case, though, is that correct; that is, there's regulatory lag that --
A. That's true.
Q. -- offsets?
A. But it is held until that time.
Q. Right.
Let me ask you this: Assume that we have a situation -- a lifespan plant -- a generating plant and the -- the Company's proposed depreciation approach is used.
And assume further that it's right on the nose -- that after the 45-year life of the plant, the amount -- right amount has been accrued to give the shareholders the return of the investment, and it has accrued the proper amount of cost of removal. And

let's just say $30 million.

But we get to the end of the period and they -- they've got to spend the $30 million, but they don't actually have it. So the Company borrows $30 million and tears the plant down.

Would the ratepayers be responsible for the interest and amortization of the principal of that loan?

A. I'm not sure I understand your -- your question completely. The --

Q. At -- at the -- at the end of the -- at the time that the lifespan property is removed, the accruals have been perfect, the cost of removal is $30 million, but the Company doesn't have $30 million in cash, so it borrows $30 million to tear down the plant.

Should the ratepayers have to pay for the amortization of the principal and the interest on that loan?

A. I think the question is, where did the 30 million go? Because if you had the -- if you collected the 30 million, right now what would happen is, because our capital investment is higher than our depreciation rates, that 30 million would be invested in new capital.

And as a reduction of rate base, you'd have a period of time where the ratepayer would be paying less than the cost of investing in that new capital. And then it would restore that when you actually incurred it at the end.

So I think you would borrow that money at the end to reflect your increase in rate base, because that would be the balance of -- your rate base would go up by 30 million, and you would balance that to reflect your investment in the remaining plant.

Q. No, you don't invest $30 million. You're going to purchase power.

A. And we're not recovering that in cost of service?

Q. Yeah, but there's no investment in rate base -- I mean, there's no plant investment. Instead of building a new plant, you simply purchase power. Setaris parapis (phonetic sp.). There's -- there's no additional increase in -- in the Company's investment?

A. Well, you're comparing a cost-of-service item with a rate-base -- with a rate-base item. The $30 million is being collected in depreciation as a rate-base item, and you're comparing that to a cost-of-service item. I can't see that comparison making sense.

So we should compare a rate-base item with another rate-base item, which what you would do with the 30 million, typically, if you collected depreciation, I mean, in theoretical treatment of -- of ratemaking is the -- if you're collecting a dollar of depreciation, you should be refunding -- assuming a 50/50 capital structure, should be returning 50 cents to your equity investor and 50 cents to your bondholder or reinvesting that dollar in -- in new capital, cuz it's a -- it's a rate -- it's a rate-base item.

Q. Well --

A. I mean, that's -- that's what the depreciation reflects is a return of investment.

Q. But the -- but there's no requirement that the shareholders with that return of investment make additional investment in plant. I'm -- I'm -- I'm saying, don't assume that -- that there's been an additional $30 million invested in -- in rate base.

A. Well, then -- then the -- then the rate base would simply go down by 30 million, and you would reduce your equity and your debt by 30 million. Because you had a -- by collecting the depreciation, your rate base has gone down by 30 million.

When you do your capital structure against that reduced rate base of 30 million, your equity and debt for ratemaking purposes go down by 30 million. That's the reflection of taking that 30 million and paying off your debt and equity.

Q. Well, I won't -- I won't push it.

The Company does have a lot of expenses that aren't rate-base expenses; isn't that correct? Insurance, postage?

A. The cost-of-service items, yeah.

Q. Yeah.

A. They're not rate base.

MR. SCHWARZ: That's all.

JUDGE JONES: Thank you, Mr. Schwarz.

Okay. We'll have redirect from Aquila now.

MR. ENGLAND: Thank you.

MS. WHEELER: There's no paper left in there.

MR. ENGLAND: There's none?

JUDGE JONES: There may be a way to flip it over.

MR. SCHWARZ: I thought those numbers were the same in this case.

MR. ENGLAND: I'm looking for a page that doesn't come through.

JUDGE JONES: Now, Mr. England, we -- we do have use of the overhead projector over there now, if you'd like to --

MR. ENGLAND: Oh, no. You have to understand my technical limitations, Your Honor.

JUDGE JONES: It's just a matter of turning the lights on, and then I can put it on this screen over here. Really.

We'll -- we'll go off the record for a second and do that so everyone can see what's going on.

(A RECESS WAS TAKEN.)

JUDGE JONES: Okay. We're back on the record.

REDIRECT EXAMINATION BY MR. ENGLAND:

Q. Mr. Rooney, I want to take you through an example, which I think was sort of what you were talking about with Commissioner Murray.

And on the screen is projected a piece of paper that I've -- I've got four columns. The first is year, the second is plant less reserve equals rate base, the third column is 10 percent return and the fourth column is depreciation.

Do you understand that?

A. Yes.

Q. As I understand the hypothetical that you were discussing with Commissioner Murray, at the beginning of Year 1, we'll say, you invest $1,000 in plant.

A. Yes.

Q. So that's your rate base, right?

A. Yes.
Q. At -- assuming a 10 percent return, that would be?
A. $100.
Q. Thank you.
And further assuming that it will cost you net $500 to remove this piece of plant, what would be your depreciation in the first year --
A. Would --
Q. -- over a 10-year life?
A. Would be $150.
Q. Now, in Year 2, what's your rate base?
A. It's going to be $850.
Q. And why is that?
A. Having collected $150 of depreciation, you would have put a credit to your accumulated depreciation reserve, which is a reduction of rate base for $150.
So your original gross plant would be 1,000, your accumulated depreciation reserve would be $150 for a net rate base of $850.
Q. Okay. What's my return at 10 percent in Year 2?
A. Would be $85.
Q. Okay. And what's my depreciation?

A. Would be 150 again.

Q. Okay. And I hate to do this to you, but what happens now in Year 3? We're gonna go through the whole --

A. 7--

Q. -- life.

A. $700, $70, $150.

Q. Year 4?

A. 550, 55, 150.

Q. Year 5?

A. 400, 40, 150.

Q. Year 6?

A. 250, 25, 150.

Q. Oops. Year 7?

A. Be 100, 10, 150.

Q. Year 8?

A. Negative 50, negative 5, 150.

Q. Year 9?

A. Negative 200, negative 20, 150.

Q. Year 10?

A. Negative 350, negative 35, 150.

Q. And then at the beginning of Year 11 -- or at the end of Year 10 --

A. You'd have --

Q. -- what's your rate base?

A. -- negative 500.

Q. And that same year you spend, as I understand, 500 to take it out of service?

A. So you would -- you would replace that 500 with zero, having spent it at the beginning of the year.

Q. So is that a rough depiction of that particular plant with those assumptions --

A. Yes, it is.

Q. -- over that 10-year life?

A. Yes, it is.

MR. ENGLAND: Okay. Thank you.

Your Honor, for purposes of the record, it might be best to have this marked as an exhibit, and I can have copies made and distributed.

JUDGE JONES: Okay.

MS. WHEELER: 181.

JUDGE JONES: 181.

(EXHIBIT NO. 181 WAS MARKED FOR IDENTIFICATION.)

BY MR. ENGLAND:

Q. One other -- one or two other questions, Mr. Rooney.

Commissioner Murray asked you about the '97 case, and I think you indicated that in that case the Commission disallowed recovery of the net salvage associated with -- what was it?

A. Term-- terminal salvage.

Q. Thank you. Terminal salvage.

But was -- was there an allowance for what I'll call the traditional or normal net salvage on mass accounts?

A. Yes, there was, and an accrual of it.

MR. ENGLAND: Okay. Thank you, sir.

I think that's all the questions I'd have, and would offer Exhibit 181.

JUDGE JONES: Any objection to Exhibit 181?

(No response.)

JUDGE JONES: Okay. Exhibit 181 is admitted into the record.

(EXHIBIT NO. 181 WAS RECEIVED INTO EVIDENCE.)

JUDGE JONES: Well, I think -- I think that concludes the testimony of Aquila's witnesses. Now we'll move on to Staff's witnesses.

Mr. Schwarz?

MR. SCHWARZ: I'm sorry. We ask to take Ms. Schad at this stage.

JUDGE JONES: Ms. Schad, will you raise your right hand, please?

(Witness sworn.)

JUDGE JONES: Thank you.
ROSELLA L. SCHAD testified as follows:
DIRECT EXAMINATION BY MR. SCHWARZ:
Q. Good evening. You have caused to be filed in this case direct testimony, rebuttal and surrebuttal?
A. Yes.
Q. And also, what did we call it, revised direct, rebuttal and surrebuttal?
A. Yes.
Q. And, for the record, your direct is marked Exhibit 101, the revised is marked -- direct is 1101, rebuttal is 102, revised rebuttal 1102, surrebuttal 103 and revised surrebuttal 1103; is that correct?
A. Yes.
Q. And have you -- did you file a correction that's been marked 1146?
A. That's a corrected Schedule 4 --
Q. Right.
A. -- and I don't have that exhibit, no.
MR. SCHWARZ: Is that -- okay. Excuse me, Judge. It is 146, not 1146.
BY MR. SCHWARZ:
Q. Do you have any corrections to be made to your testimony?
A. Yes. On that exhibit you just mentioned,

146 --

Q. Yes.

A. -- there is a reversal that should occur there. It's -- under the net cost of removal -- the second one down where it's a negative 232,538, that will be positive.

And I don't have the sequential effect of what that does to the 1.7 million there, but it -- it will have a -- it should have a small incremental change to that. So I will leave with the -- the 232,538 should be a salvage positive number on that.

And then if we're ready, I'll give the others. In my direct on page 10, line 13 --

Q. Just a moment.

Yes.

A. -- the word "not" should be placed between "does appear."

Q. Okay.

A. Okay. In the rebuttal page 19, line 20 --

Q. Rebuttal page 19, line 20.

A. -- the word "whole" should be replaced with "remaining."

Q. Okay.

A. On surrebuttal page 11, line 1 --

Q. Yes.

A. -- the Item No. 3 should be Item No. 4 so it'll correspond to the -- the schematic of the schedule.

In line 2 the word "revenue" should be replaced with "expense," and on line 3 on the same page the Item No. 4 should be 3, again, to match with the schedule.

That's all the corrections I have.

MR. SCHWARZ: Very well.

I think under our protocol I would offer those exhibits and tender Ms. Schad for cross.

JUDGE JONES: Okay. Staff Exhibits 101, 102, 103, 1101, 1102 and 1103 are admitted into the record, and Exhibit 146 shall be admitted into the record.

(EXHIBIT NOS. 101 THROUGH 103, 146 AND 1101 THROUGH 1103 WERE RECEIVED INTO EVIDENCE.)

JUDGE JONES: Let's see. Will there be any cross from Aquila?

MR. ENGLAND: Yes, sir.

CROSS-EXAMINATION BY MR. ENGLAND:

Q. Good evening, Ms. Schad.

A. Good evening.

Q. I have a few questions about -- your background and experience, I think, are on page 1 of your direct testimony.

A. Okay.
Q. Lines 16 through 26, I think you have a quick summary of your educational work experience.
Do you see that?
A. Yes.
Q. If I'm reading that correctly, you joined the Missouri Public Service Commission Staff in 1999?
A. Yes.
Q. Is it fair to say that prior to that time, you had no specific education or work -- work experience in developing depreciation rates for utility companies?
A. That is correct.
Q. So all your education and work experience in this area has been since your employ with the Missouri Public Service Commission in 1999?
A. Yes.
Q. Okay. On page -- again, page 1 of your direct, line 23, you indicate that you have completed training in depreciation concepts.
Do you see that?
A. Yes.
Q. Could you describe those -- that training, rather, for me, please?
A. Yes. The -- the initial training was with an entity in Michigan to go over depreciation parameters

and the -- the basis for what those play in the development of the depreciation system and the -- the construct of a depreciation methodology.

I've -- they include also training at Gannet Fleming with the use of the software, and also depreciation concepts there regarding parameters.

Q. The -- the first one you mentioned, something about Michigan, did that have a name?

A. It did. I believe it was Depreciation Programs, Incorporated. It was on page 3 of my direct.

Q. Okay. So the three training were sponsored by Depreciation Programs, Inc., Gannet Flemming and Depreciation Concepts?

A. Let me see. Let's go back. Deprec-- okay. On page 3 the Depreciation Programs, Inc., the Society of Depreciation Professionals and the Gannett Fleming Evaluation and Rate Consultants.

Q. Okay. They're -- okay. I'm sorry. I see them now. They're on lines 7 through 8 on your -- page 3 of your direct?

A. Yes.

Q. Okay. Then you indicate that you've attended numerous industry seminars. Can you give me the names or describe for me those industry seminars that focused on depreciation?

A. Okay. I would include in that the -- the seminars that STP, the Society of Depreciation Professionals, have provided on an annual basis to their members or to depreciation analysts.

Q. Any others?

A. Specific to depreciation --?

Q. Uh-huh.

A. -- and actually using the technique, no.

Q. Okay. Thank you.

Is it fair to say that you have neither written nor lectured on the subject of utility depreciation?

A. That would be correct.

Q. Okay. Now, you -- it appears you have -- and I'm looking at your Schedule 1 -- you have presented testimony on a number of occasions on the issue of depreciation as shown by Schedule 1; is that correct?

A. Yes.

Q. And in -- and in some of that, apparently, was not depreciation, but it looks like the majority of it was -- that testimony?

A. Yes.

Q. Okay. Have you ever been subject to cross-examination on any of this testimony that you indicate on Schedule 1?

A. No.
Q. Is it fair to say -- and again, I'm basing this question on what I see on Schedule 1, so correct me if I'm wrong -- but is it fair to say that the -- this would be the first electric utility for which you have had primary responsibility for the performance of a depreciation study?
A. I'm gonna quanti-- qualify that.
Q. Sure.
A. I did the initial work on the 291 -- 299 -- ER-2001-299 case with Empire. I did -- I did do that initial work on that.
Q. But another Staff member took it over --
A. Yes.
Q. -- for purposes of testimony and presentation?
A. Well, for purposes of my absence.
Q. Okay. And then can you tell me do you have any specific experience in the design construction or operation of an electric utility company?
A. My experience with the construction at Callaway.
Q. That was limited to the nuclear plant, then?
A. Yes.
Q. Okay. And that was, I think, indicated in your direct testimony approximate two-year period of

time immediately graduating engineering school?

A. That's right.

Q. What exactly were your responsibilities at Callaway?

A. The responsibilities there were as a liaison between staff of Union Electric and any other entity that was involved at the plant, whether it was Daniels, the construction company, Bechtel, Snuffs, which was the design unit. It was the -- the liaison position that was it -- that was staffed on site.

Q. Okay. Thank you.

I -- I think you'll agree with me that one of the big issues between the Staff and the Company in this case is the way in which the parties handle cost of removal or, as it's sometimes been referred to as, net salvage for depreciation services --

A. Yes.

Q. -- correct?

A. Uh-huh.

Q. And again, I -- my understanding is Staff proposes to use what I call an expensing method where they propose to expense net salvage, based on a 5-year average of actual cost of removal, correct?

A. Yes. I mean, we -- we are -- and Staff witness Cary Featherstone can address that specific mechanism of the 5-year average.

Q. Yeah, I didn't want to -- I -- I didn't mean to get into it any deeper than that.

A. Oh, okay.

Q. But it's just based on a 5-year average of actual cost of removal incurred or experienced by the Company?

A. Yes.

Q. Okay. The Company, on the other hand, proposes to accrue an amount for future net salvage as part of the depreciation rate, would you agree with me?

A. Yes.

Q. Thank you.

It's my understanding that there is only one other state, other than Missouri, that currently follows the method or the approach that Staff uses to expensing net salvage, and that state is Pennsylvania; is that your understanding as well?

A. That is my understanding.

Q. And all other states follow the accrual method?

A. I can't confirm that, because I don't know.

Q. Okay. Would you agree with me that a majority of states follow the accrual method?

A. Again, I'd have to say that I can't confirm that.

Q. Okay. Are you aware of any authoritative texts on the issue of depreciation that advocate the expensing of net salvage, as proposed by Staff?

A. I read texts that have a -- have mentioned that it can be. I -- I don't have those texts here in front of me. But that there are alternatives to accruing it.

Q. And I -- I was drawing a distinction between mentioning and advocating --

A. Okay.

Q. -- recommending.

Do these texts recommend it or do they just mention that as a -- a way that some people or some state commissions do it?

A. I -- I think I'll stay with the mention.

Q. Okay. Of the industry seminars on depreciation that you've attended, which I believe were sponsored by the Society of Depreciation Professionals, do they recommend or advocate the use of the expensing method that Staff proposes?

A. I can't say they recommended it.

Q. Okay. I know that Gannet Fleming does not advocate expensing and, in fact, witnesses from Gannet Fleming have come and testified here on behalf of the

accrual, would you agree with me?
A. I would agree.
Q. Okay. What about depreciation programs, do they advocate the expensing or the accrual method?
A. I don't believe that there was a moment of advocation in the presentation as such.
Q. What --
A. I mean, I don't -- I don't believe that they advocate accrual or advocate processes in that manner.
Q. Okay. How about depreciation concepts, do they advocate it, recommend it --
A. Now --
Q. -- promote it?
A. -- you were referring to concepts as different than programs?
Q. I -- I drew a distin-- I thought there were two different ones when you gave me an answer earlier. Maybe --
A. I don't --
Q. Help he out here. I --
A. I don't -- I don't think --
Q. -- may have mischaracterized your answer.
A. I think the concepts are incorporated in the semi-- I mean, at the locations of the training. I don't think that one of the trainings has a name -- is

an entity of depreciation concepts.

Q. Okay. Let me look, then, on page 3, line -- I guess it's lines 7 and 8. We've covered that, the Society of Depreciation Professionals?

A. Right.

Q. They sponsor training and seminars; is that --

A. That's correct.

Q. Okay. And I'm sorry. I hate to repeat myself. If I -- if I am, I can't remember.

Did you say they do or do not advocate the expensing of net salvage?

A. They neither advocate or deny that possibility.

Q. Okay. Is it fair to say that the traditional approach to determining whole-life depreciations has been to accrue an amount for net salvage in the depreciation rate?

A. Yes.

Q. As the Company has proposed in this case?

A. That I would say, no. Within our own history here we have had times, and they -- they were not consistent. They were -- they were and then they moved away from it, and then they came back to where that accrual was, a current basis.

Q. Okay. We'll talk about that later, but I was concerned about what the Company has done.

How is the Company's proposal to accrue for net salvage different from the traditional approach that we talked about?

A. One way is the final costs of removal in the sense that that may or may not -- depending on how you want to determine what net salvage percentage you want to put into a -- a traditional depreciation rate is gonna determine whether or not you include terminal -- terminal salvage.

Whether you want to include a future salvage, there's -- there's many ways that you can develop a percentage, and we still call it net salvage percentage.

Q. I -- I was -- I was being a little broader in my --

A. I -- I know, but --

Q. -- in my question.

Insofar as just generally accruing for net salvage -- future net salvage as part of the depreciation rate, the Company's approach is consistent with what we've discussed as the tra-- traditional approach, isn't it?

A. I still can't say that it is, because there's still that defining difference on a future versus a current.

Q. Okay.

A. A traditional can be just a current level.

Q. But a -- but a -- accrued is part -- I guess I -- let me focus more clearly on --

A. Running it through the depreciation rate.

Q. Correct.

A. Yes.

Q. Okay. The -- the Company, then, is traditional in that sense?

A. Traditional in that sense.

Q. Okay. Thank you.

Looking back at Schedule 1 to your direct testimony and the cases where you've performed -- or depreciation studies, have you ever developed depreciation rates using the traditional whole-life approach that we've talked about -- just talked about?

A. Not on those listed on this sheet.

Q. Okay. Would it be fair, then, to say that your whole work experience, then, in this area has been to developed -- or has been, rather, to develop depreciation rates using Staff's expensing method for net salvage?

A. No. Actually on the Ameren gas case I worked on rates that included in that salvage percentage that was on a current basis to -- but that's not on this case, because I wasn't the primary one, so --

Q. I understand. And that -- and -- and that -- but that was a fair answer, because my question was broader than what was listed on here.

Can you give me the -- the -- the case number or the year of that Ameren gas case?

A. It's listed on page 3, line 1. GR-2000-512.

Q. So with the exception, then, of the Ameren case, GR-2000-512, all of your other experience has been to develop depreciation rates, based on the expensing method, correct?

A. Yes.

Q. Okay. Now, your advocacy, if you will, or recommendation of an expensing method, is that a result of your own personal experience and opinion or is it because of your employment here at the Staff and that's pretty much how they do things?

A. It's mine.

Q. Have you ever -- oh, I'm sorry.

With respect to the Ameren gas case --

A. Yes.

Q. -- can you tell me how that net salvage was handled in that case?

A. I believe the end result was to include it, pending finalization of a Laclede case in the courts.

Q. In-- include it where?

A. In the rates.

Q. Okay. So it was -- it was accrued as part of the depreciation rate in the Ameren case -- net salvage, that is?

A. Yes.

Q. Okay. Has Ameren gas since that time been in for a rate case?

A. Yes.

Q. And is that the same method that Staff is recommending in the subsequent rate case?

A. No.

Q. Staff is recommending the expensing method?

A. Yes.

Q. Okay. Let's talk a little bit about service lives, if we can.

A. Okay.

Q. I understand that's another major difference between the Staff and the Company in this case, right?

A. Yes.

Q. Would you agree with me that generally speaking the longer the average servi-- service life, the lower the depreciation rate and the smaller the depreciation expense for accrual?

A. Yes.

Q. And, conversely, the shorter the average service life, the higher the depreciation rate and the larger the depreciation expense or accrual?

A. Yes.

Q. In this case, would you agree with me, that Staff is generally proposing longer average service lives than the Company and thus lower depreciation rates and accruals?

A. I guess I see that Staff is not compressing the average service lives as much, therefore, resulting in what is more accurate. It is a display of the average service lives of the plant in place, rather than just saying I'm lengthening the Company's.

Q. No, I didn't say you were lengthening. I said you were proposing, relatively speaking, longer lives than -- than the Company.

A. They are longer lives.

Q. Okay. And as a result lower depreciation rates and accruals?

A. Yes.

Q. Now, as I understand it, Staff is also proposing a change in the average service lives which were used to develop the current or presently authorized rates -- depreciation rates, excuse me --

correct?

A. Are we recommending longer lives?

Q. No, I was just --

A. Sorry.

Q. You're -- you're reading me -- you're way ahead of me on this.

My first question is, you're proposing a change in the average service lives that underlie the current or presently authorized depreciation rates?

A. Yes.

Q. Okay. And, generally speaking, you're recommending longer average service lives than under-- what -- than those that underlie the -- the current rates, correct?

A. They are slightly --

Q. Okay.

A. -- although minimal.

Q. At page 5 of your direct testimony, lines 2 and 3 you state that, the ASL -- which I understand is ster-- excuse me -- understand means average service life -- is determined by an analysis of records of actual annual additions and retirements by vintage (year of placement), correct?

A. Yes.

Q. And then at page 6, lines 9 through 15 you discuss how an account's average service life or ASL may change over time.

Do you see that?

A. Yes.

Q. For example, you indicate that technology changes, environmental regulations, regulatory requirements or accounting changes can modify an account's average service life, correct?

A. Yes.

Q. Okay. Now, let me take you to your Schedule 3-1 attached to your direct testimony -- page 2 of that schedule. I believe you show certain summary data down there at the bottom of that schedule.

A. Yes.

Q. Do you see that?

A. Uh-huh.

Q. As I understand, the only -- and -- and you make several -- and you make certain comparisons. And I'm gonna focus right now on a comparison between your proposal in this case and the existing accruals under presently authorized depreciation rates.

A. Yes.

Q. So with that comparison in mind, would you agree with me that the only difference between existing rates -- depreciation rates, that is -- and those proposed by Staff in this case is a change in the average service life?

A. No -- well, yes and no. I am not truncating the average -- I am not truncating for a lifespan plant for the production, which the lives for the current plant were.

Q. Okay. That -- that has the effect of changing the life, correct?

A. Yes.

Q. Okay. So I guess maybe I'm being a little too general, but that -- that seems to me to fall under the category as the main change between present and proposed, as far as Staff is concerned, is a change in the average service lives?

A. Yes.

Q. Okay. At the very bottom there you show MPS Electric and Common Utility plant summary figures.

Do you see that?

A. Yes.

Q. Under existing rates, which is about the middle of the page -- or I guess the first number in that -- well, it's not the first. It's the second. But there's a figure of 32 million.

Do you see that?

A. Yes.

Q. That's the current annual accrual under existing rates. As I understand it, under your proposed rates, the current annual accrual would be 27-and-a-half million roughly?

A. Yes.

Q. Okay. Or -- or approximately a $4-and-a-half million reduction in annual accruals for MPS Electric and Common Utility plant, right?

A. Yes.

Q. Okay. Now, you mentioned a minute ago that you didn't have much change between what's currently authorized and what you're proposing in this case, I think, did you not?

A. There was more in this case than just that summation.

Q. Right.

And -- and I'm gonna turn the page, and I think this is where -- I think these are the numbers maybe you were referring to -- or I think you were referring to.

Again, at the very bottom of this schedule you have total MPS Electric Utility plant of roughly -- and -- and -- and current accruals of roughly 32.6 million, correct?

A. Yes.

Q. And under your proposed rates, 31.9 million?
A. Right.
Q. Roughly a difference of 700,000.
And where you make up the almost $3.8 million of the difference we talked about on the prior page is here in corporate plant, correct?
A. Yes.
Q. And that's because -- not so much because you've changed lives, but because you are implementing rates for depreciable accounts that hadn't -- that previously did not have any depreciation rates, right?
A. Right.
Q. In fact, where you are proposing rates, where we do have rates for the corporate account, your rates are lower, indicating longer service lives?
A. Okay. Say that again.
Q. Sure.
For those five accounts where we do have rates under the present depreciation rates, you're proposing lower rates, which would indicate that you're using longer service lives, correct?
A. Yes. But the other thing to take into consideration on when you say that those plant dollars did not have a depreciation rate --
Q. Uh-huh.

A. -- I would agree to the extent that that is true. Although if you look back in time, the computers were all caught up in the -- in a different grouping -- in a different function up in common general.

So they -- and I'm not for sure where one set went to and the other one came to. But at one point in time the computers were all up in another function, and then those dollars have sort of decimated away.

And then the dollars have -- have shown up more down in corporate. You know, why that occurred, I -- I don't know.

Q. Neither do I.

I think without belaboring -- well --

A. I mean, because that I -- I -- I tried to stay away from just looking at that -- just picture in time, because I could see that, you know, dollars were kind of moving. So I didn't think it was fair to just focus on that point by itself.

Q. Oh, okay. Well, and that -- and that's fine.

I -- but my question -- and I think you answered it is, for those accounts where we presently have rates, your proposed rates are less, indicating longer service lives, correct?

A. Yes.

Q. Okay. Schedule 3.2 shows similar analyses for the St. Joe properties?

A. Yes.

Q. And -- and up until a day or two ago I didn't know if I was gonna be able to talk about those numbers.

A. Okay.

MR. ENGLAND: I -- I guess it's okay now, Your Honor?

JUDGE JONES: Yes, it is.

BY MR. ENGLAND:

Q. Okay. Again, my understanding is for the St. Joe Electric and Common Utility plant, which is page 2 of 3.2, current accruals are 11.6 million, your proposal is 8 million, roughly?

A. Yes.

Q. And so that would be a 2.6 -- excuse me -- $3.6 million reduction in accruals?

A. With the clarification that that's not just a life change. That's a change that -- also with cost of removal not being in the depreciation expense.

Q. You're -- you're right. Thank you.

So it's a -- it's a two-fold effect?

A. Yes.

Q. Different lives, less cost of removal?

A. (Witness nodding.)

Q. Okay.
A. Yes.
Q. And the same with -- again, on the -- on the very last page -- the third page of that schedule total, St. Joe Light & Power Electric plant -- or electric utility plant -- excuse me -- current accruals are 11.8, your proposal is 9.5 or 9.6?
A. I'm sorry. Again?
Q. Yes.
Current accruals on the third page, last -- last line are 11.8 million; is that right?
A. Mine are? I'm sorry?
Q. No. Present rates.
A. Okay. Yes.
Q. And yours would be 9.6, approximately, million?
A. I must not be on the same page you are.
Q. Okay. It's the third page where you just --
A. Okay.
Q. -- sort of have a half of page of data.
A. Okay.
Q. And I'm looking first under the column that says, annual accrual current depreciation rates at 9/30/03.
A. Yes.

Q. And that would be 11.8 million?

A. Yes.

Q. And then the next column -- or the column next to it, annual accrual Staff proposed depreciation rates at 9/30/03. That would be 9.6 million?

A. Yes.

Q. Okay. So the -- the reduction, to the extent you have it in the MPS side, would be due primarily to changes in service lives?

A. Yes.

Q. And the reduction on the St. Joe side would be a combination of lengthening service lives and eliminating cost of removal?

A. Yes.

Q. Okay. Thank you.

I'm gonna try to do a little more here with these numbers and hope I get the right answers. It just remains to be seen.

In your surrebuttal testimony, page 3, lines 22 through 23 -- I -- I'm sorry. Did I say page 3?

A. Uh-huh.

MR. SCHWARZ: Yes.

MR. ENGLAND: I -- I misspoke. Page 2. I can't read my own handwriting.

THE WITNESS: Okay.

BY MR. ENGLAND:

Q. Lines 22 and 23 you say that there -- the three specific areas of difference -- and I assume you're talking between Company and Staff --

A. Yes.

Q. -- are depreciation expense for cost of removal, service lives and amortization of the accumulated depreciation reserve?

A. Yes.

Q. Okay. Now on the next page, I think you attempt to quantify those differences. And for purposes of cost of removal you quantify that at 7 million?

A. Yes.

Q. I think that's on line 2.

For the average service lives, you have quantified that at 6.5 million; is that correct?

A. Yes.

Q. And then on the reserve amortization, it appears that that's zero; is that right?

A. Yes.

Q. So would you agree with me really the two big areas of difference between the Company are cost of removal and service lives?

A. Yes.

Q. Okay. And I think that the -- the net difference, if I -- if I can use that term, between Company and Staff on cost of removal is really 7 million that we've got built, if you will, into our depreciation rates, and the 1.5 million that you're allowing as an expense item for a net of $5.5 million, correct?

A. Yes.

Q. That's the true difference, if you will, between Staff and the -- and Company on the cost-of-removal issue?

A. For MPS.

Q. For -- thank you. For MPS.

So the -- the total difference, depending on how you look at it between the two parties is -- is 13-and-a-half million if you don't look at your expensing of cost of removal; or if you do, it's a $12 million difference?

A. Yes.

Q. Okay. Thanks.

So let me get this straight. If the Commission chooses to adopt Staff's lives, but adopts Company's accrual for net salvage, it would generally increase Staff's annual depreciation expense for MPS by roughly $5.5 millon?

A. Yes.

Q. Okay. Thank you.

I want to talk a little bit about cost of removal or net salvage, as it's been -- sometimes been called.

As I understand, the sole reason that Staff does not accrue an amount for cost of removal and include it in the depreciation rate is because these are future costs and they are not known and measurable; is that right?

A. Can you repeat that?

Q. Sure.

The sole reason that Staff does not accrue an amount for cost of removal and include it in the depreciation rate is because these future costs are not known and measurable?

A. Or certain to occur, even at all.

Q. It -- it -- how -- how do you distinguish that from not known and measurable? Isn't that the not known part?

A. Yes.

Q. Okay. And, I mean, for example, at -- and I'll -- and this is where I think we're talking about some terminal cost of removal.

In your rebuttal page 3, lines 22 and 23 -- are you there?
A. Yes.
Q. You state, estimated future final costs of -- of removal for fossil fuel plants are an issue, because these costs are not known and measurable at this time, correct?
A. Right.
Q. Am I correct to assume that if future final costs of removal are known and measurable at this time, it would in Staff's opinion be appropriate to accrue them now and include them in a current depreciation rate?
A. No. I think that, even given that scenario, that the idea that something future in that regard is -- is known, i'm not for sure how I'm going to see that number today.
Q. Well, I'm -- I'm asking you to assume that they are known and measurable today.
A. I think that -- I think the cost of removal is itself characteristic of an expense, and I think it -- it probably should be expensed rather than come through the accrual.
Q. So if we knew and could measure today the cost of removal that we're going to incur in the future, you

would include that as a separate ex-- line-item expense item?

A. The de-- the depreciation is a mechanism to recover original cost, and that's not one of the components in that concept alone. So in that regard, it would be a separate line item.

Q. What -- what definition are you quoting from when you say depreciation is limited to the recovery of original cost?

A. Let's see how I have that. On page 4 of my direct I'll read lines 11 through 15. Depreciation is the loss not restored by current maintenance, which is due to all factors causing the ultimate retirement of the property.

These factors embrace wear and tear, decay, inadequacy and obsolescence. Annual depreciation is the loss that takes place in a year; thus annual depreciation expense dis-- distributed over the life of each asset yields the full recovery of the original cost of utility's assets.

Q. I see that.

It -- but that's that your testimony, that's not something authoritative text definition of depreciation, is it? I see no attribution there.

A. You do not.

Q. So -- so that is your definition of depreciation, correct?
A. Yes.
Q. Okay. Let me get back to my original question.
I thought we established that the only reason you didn't include future costs of removal in your depreciation rate or accrue for it was because they weren't known and measurable.
So is that -- didn't we establish that a -- a little while ago?
A. If I said it's the only reason, then I would like to expand that to include that it is an expensed item that we're going to -- we're going to recover original cost only through the depreciation mechanism.
Q. Okay. Let me ask you this question then: If future cost of removal is known and measurable, would you include it in a line item of expense for cost of removal?
A. I believe so.
Q. Based on those future known and measurable --
A. Well, if I can, I would defer that to someone that's handling an expense item. I'll defer that to Mr. Featherstone.
Q. Well -- and I think this may have been more of

a semantic argument. But would you agree with me that at least, as far as Staff is concerned, the only time you're going to really know and be able to really measure the actual cost of removal or net salvage is after the plant is taken out of service?

A. Yes.

Q. So as a practical matter under Staff's criteria, you're never going to be able to collect future cost of removal through depreciation or through an expense item, because you're never gonna be able to know and measure it until after the fact?

A. In a current case we are including an expense item that is based on what it is incurring right now for this Company in this rate case as an expense item.

Q. Base on historical experience, correct?

A. That's correct, yes.

Q. My -- but my point is under your known and measurable test, criteria, whatever you want to call it, a company will never be able to collect future costs of removal today, because they are not known and measurable until after the plant is retired?

A. Correct.

Q. Sometime in the future, correct?

A. That's the only time we can know it.

Q. Okay. So --

A. If -- or if I --
Q. -- under that --
A. -- could -- if I could add that if -- if -- if an item is an event that is going to occur and you can quantify it just as we've done in this case current -- ongoing -- those costs that's gonna occur in the next two years or be costs that have not incurred yet, but we do have an amount and an expense for that.
Q. But you don't know what our cost of removal is gonna be next year or the year after, do you?
A. No.
Q. You've -- you've used an approximation based on five-year historical average of approximately 1.5 million --
A. Right.
Q. -- correct.
I guess what I'm getting at is under -- under Staff's criteria a company will never be able to accrue future cost of removal during the life of the plant that's going to create that cost of removal -- it's gonna have to be incurred after that plant's retired, correct?
A. Again, I -- I would say it's -- it's still similar to what's happening today simpl-- like to a maintenance cost that's being incurred, and it-- that's

in the rate case. Those maintenance costs are also what's just been incurred prior to this. And they will be an amount that's not the case for going forward.

Q. Maintenance -- maintenance costs are -- are day-to-day costs that -- that tend to be fairly stable, don't they, from year to year?

A. No, I wouldn't think so. I think that whenever you -- I would -- I would -- could see them being very similar to these costs of removal and maybe even a magnitude larger.

The vari-- the variability in the magnitude of maintenance costs could actually be more extreme than what we have with the cost of removal.

Q. Well, then under your analysis -- let me get back to the timing of this. The -- the actual cost of removal that is incurred at the time plant is retired from service won't be known until after retirement?

A. Correct.

Q. And it will -- it'd be impossible, under your analysis, to collect those dollars before retirement, correct?

A. Correct.

Q. Okay. If a company must wait to recover cost of removal after the plant is taken out of service, there is a very real risk that they may never recover those costs, because the plant is no longer used and useful, isn't there?

A. There is the possibility.

Q. In fact, that's exactly what happened with the Missouri-American case and the St. -- old St. Joseph Water treatment plant that's been talked about in this case, correct?

A. Well, in -- in that case that water treatment plant, although -- if we had been collecting dollars from those customers and just overcollecting year after year after year, they would be -- have been collected by the company. And at the end, the company sold the treatment plant.

Q. But that's not the case. It wasn't overcollected for years and years, it was undercollected for years and years. And there was a net original cost that was undepreciated at the time it was retired from service, correct?

A. For the -- for the cost of removal. They did not incur the cost to remove the -- the treatment plant. But had we been collecting for it, you know, as a final cost of -- of removal, then there would have been an inequity, because that plant was never removed.

It was -- under the company's ownership, it was not dismantled and the site reclaimed.

Q. There was investment in that plant, whether it was original investment or interim retirements and costs of removal throughout the life of that plant that were not collected, simply because there was roughly $2-and-a-half million of investment, as I understand, undepreciated at the time it was retired -- or $2-and-a-half million in the plant account undepreciated at the time it was retired, correct?

A. As to what occurred at -- on the original costs, I can't testify to that.

Q. Well, let -- let me get back to my original premise. Under your notion -- excuse me -- I'm sorry -- Staff's notion, Company will never collect its cost of removal until it's incurred, which is after retirement.

My question to you was, then there's a very real possibility that they may not get that cost of removal under the notion that the plant is no longer used and useful. And you -- I think you said that's a possibility, right?

A. That's a possibility.

Q. That doesn't seem fair to me. Does it seem fair to you?

A. The fairness lies that the reverse can happen as well.

Q. If it's overcollected, it goes to the reserve which goes to reducing rate base so the ratepayers get the benefit of the reduced rate base, correct?

A. The customers aren't being asked if they want to over-- be overcharged at this moment in time for something that may not occur.

MR. ENGLAND: The Company's not -- well, excuse me.

May I have my question read back, please?

(THE COURT REPORTER READ BACK THE REQUESTED PORTION.)

MR. ENGLAND: May I have the answer as well, please, because I don't believe it was responsive?

THE WITNESS: Yes. Does it -- it -- it would reduce rate base.

MR. ENGLAND: Thank you.

BY MR. ENGLAND:

Q. And you recognize that that's a benefit, do you not, in your testimony?

A. I -- I believe I do. I believe I also caveat that with the -- if we want to accelerate the reduction of rate base, then we should take that up as a different issue.

MR. ENGLAND: But at least -- I'm sorry.

Go ahead.

MR. SCHWARZ: I actually do have kids that I now need to pick up pretty quick. If -- and then I have to transport them home and -- and return.

I would anticipate 25 minutes to a half an hour to get that done.

JUDGE JONES: Does anyone have a problem with us breaking until 8:30?

MR. ENGLAND: Not if -- as a matter of fact, if we keep going, I could probably wrap up with Ms. Schad while --

MR. SCHWARZ: While I was gone.

MR. ENGLAND: -- while -- while Tim's gone.

No, I have no problem.

JUDGE JONES: Okay. Well, let's do that then.

Let's adjourn and -- and resume at 8:30.

MR. SCHWARZ: I appreciate the consideration.

(A RECESS WAS TAKEN.)

JUDGE JONES: Okay. We're back on the record with ER-2004-0034, and this is cross-examination of Rosella Schad.

You may proceed, Mr. England.

MR. ENGLAND: Thank you, Your Honor.

BY MR. ENGLAND:

Q. I can't quite remember where I left off, so I'll just move forward. If there's gap here, I apologize.

I'm gonna switch gears on what question we talked about before the break, but kind of a different hypothetical.

Ms. Schad, assuming a company could recover its actual known and measurable costs and removal after a plant is taken out of service, over what length of time would you think it would be appropriate to recover that cost of removal?

A. Are we talking about cost of removal that's associated with dismantlement and brown fill reclamation whole -- what were you talking about?

Q. I'm talking retirement and dismantling of a major power plant, so we're talking significant dollars.

A. I don't know what I would -- given as an exact number of years, cuz I would also be looking at the economic analysis the Company did to make that decision.

Q. Well, let's assume it was a crude point.

A. I think I would make that -- I think that decision for the number of years should be made closer to the actual time even in this scenario.

Q. So maybe two-, three-, four-, five-year recovery period?

A. No. As I said, I think something -- that only then should you decide two, three, four, five, six on the same, but at this time I wouldn't make that declaration.

Q. But you certainly wouldn't recommend it be recovered in one year, would you, it would be over some period of years?

A. I'd still make that declaration at that time.

Q. Well, then let's assume that it's going to be over a 10-year period of time. That's not a -- an unusual amortization period for extraordinary costs for ratemaking, is it?

A. No.

Q. Okay. Is it appropriate or equitable, in your opinion, to expect ratepayers 10 years after a plant is taken out of service to pay for it -- or at least to pay for the cost of service to pay for it?

A. I think that there have been instances where there's -- for other issues where there's similar occurrences where it's an amortization after the fact. I don't think that's unusual in this ratemaking business.

Q. So your answer is, yes, you think that would be equitable?

A. Relative to similar scenarios, I would answer that yes.

Q. It would violate the notion of intergener-- intergenerational equity, would it not?

A. Because it's a hypothetical, I really can't make that, because I'm making also the probability statement that that event would occur, on which I'm not prepared to do that.

Q. Now, my -- my assumption is that it's been retired, the costs have been prudently incurred, the recommendation is that they be recovered over a 10-year period of time and ratepayers in the 10th year after retirement of that plant would pay the last of those cost of removal costs, if you will.

Wouldn't that be a violation of the notion or concept of intergenerational equity?

A. To the extent that there could be some inequity, I would believe that there could be a portion that's inequitable --

Q. Okay.

A. -- but not where I'm going to say that I -- I believe that I think overall I'm -- I'm faced with a massive inequitable position.

Q. Okay. Would the Company also be allowed to recover its unamortized balance of the cost of removal in its rate base in that scenario?

A. Would it be my recommendation for that?
Q. Uh-huh.
A. Yes.
Q. Okay. And why is that?
A. It's at a point where it's known and measurable, and I wouldn't foresee any concern with that at that point.
Q. Well, it -- isn't it also fair for the rate -- or excuse me -- the shareholders to earn a return on the money that they've expended, if you will, in Year 1, but have to wait until Year 10 to fully recover?
A. Can you ask that question again?
Q. I'll try.
A. Okay.
Q. Wouldn't it also be fair for the shareholders to earn a return on those monies that they expend in Year 1 to remove the plant, because they have to wait until Year 10 to fully recover those costs?
A. Well, I think I would defer that question to someone who more works with the -- the return of that money.
Q. Well, let me put it into personal terms that maybe you and I can understand better.
Would you be willing to loan somebody

10 year-- or money for 10 years without any interest?
A. No.
Q. Thank you.
I want to talk about income treatment versus rate-base treatment. You --
A. Yes.
Q. -- devote some time to that, I think, in your surrebuttal testimony. Matter of fact, I believe it's on pages 9 through 17. And -- and as we've discussed in this case, Staff is proposing to expense cost of removal or give it as you call income treatment, correct?
A. Yes.
Q. Would you agree with me that one of the downsides to the income treatment proposal, as you've described it from a shareholder point of view, is that if the actual cost of removal exceeds the cost used in the revenue requirement, there will be a reduction in earnings?
A. I would bel-- I believe that would be the case.
Q. Matter of fact, I think you demonstrate that or show that in your Schedule 2-2 attached to your surrebuttal testimony?
A. Schedule 2-2?

Q. 2-2.
A. Okay.
Q. Where you -- you discuss the hypothetical of the actual net cost exceeding the net cost in the revenue requirement, and this dynamic results in decreased earnings to income?
A. Yes.
Q. Okay. And that would be a -- that would be a -- to use Martha Stewart's phrase or to -- to turn it around -- a bad thing from the shareholder's perspective, right -- a decrease in earnings?
A. I believe so.
Q. Thank you.
If there is a decrease in earnings under the expense method, the shareholder could never be made whole, correctly -- correct -- excuse me?
A. I believe that's the case with any expense item.
Q. Okay. If I understand, is it Exhibit 146 is a corrected --
A. Yes.
Q. -- Schedule 4 that was attached to your surrebuttal testimony?
A. Yes.
Q. And if I look at the column that says

under/overrecovery of Staff's method --

A. Yes.

Q. -- you indicate that under your method, historically applying that, the Company would have undercollected $1.7 million, roughly, of cost of removal?

A. Over a number of years.

Q. Okay. But nevertheless undercollected that?

A. Yes.

Q. Okay. And under the expense method, as we've discussed, they need it, they wouldn't be able to go back and get it on a retroactive basis, wouldn't they?

A. Not on an expense item. It would be like any other expense item.

Q. Okay. Now, with the rate-base treatment if actual costs of removal exceed the costs used in the revenue requirement, there will be no effect on earnings -- and I think you show that on your Schedule 3.2, correct?

A. Yes.

Q. And you conclude in your surrebuttal testimony at page 17, lines 9 through 12, that either income or rate-base treatment can be used to collect net cost of removal on a current basis --

A. Yes.

Q. -- correct?
So is it fair to say that Staff is ambivalent as to whether this item is expensed or treated -- given rate-base treatment -- excuse me?
A. No.
Q. Well, I don't see a preference in that testimony. It appears to me that either way is acceptable to Staff.
A. I -- can you tell me what page that is again?
Q. Sure.
Page 17, lines 9 through 12.
A. Uh-huh. I think I made a statement that it can be used. I would say that as a rate base as it's presented in this, it -- it's more like a tracker, if you would.
And I think in -- when it comes to what would we want to do with that tracker, the tracker really should probably exist only for something that's of a significant type item that has a lot of variation.
I don't think that -- given that if we have rate-base treatment or income treatment, we would still go forward with what we're proposing here with the income treatment.
Q. I'm not sure that -- that -- that you've answered my question. My question is: It appears that

you're ambivalent over those two methods, rate-base treatment or income treatment. At least from this testimony I don't see an expression of preference for one over the other.

Did I miss something?

A. I think that the inference is in the -- in the fact of what we're doing is our presence. The statement doesn't say one way or the other in and of itself. It just says that both can be used.

Q. Well, given the fact that the rate-base treatment results in no harm to the ratepayer or the shareholder because of the tracking mechanism that you talk about, wouldn't it be more equitable to do the rate-base treatment?

A. I think the depreciation needs to be re-- remain as -- as an item that's the original cost. And we can track original costs in that recovery of something that's original cost, and we can track it over time as to how well we're -- we're -- we're assigning life and keep the depreciations simply for depreciation -- the recovery of that original cost.

I don't think that the tracker is necessarily something that -- that has a benefit. If we've -- we've talked about that it is in a reserve and it can affect rate base.

But we -- I -- I guess my view on the rate base is that we will -- if we -- if we want to work with rate base, we should just do that separately.

Q. Well, but my question was: Given the fact that the rate-base treatment has a tracking mechanism to make the ratepayer or the shareholder whole, depending on over- or underrecovery, isn't it a more equitable mechanism than the income approach?

A. I think the -- I -- I'm gonna say no. I think the equitable is -- if over the years you're -- you're trying to recover those original costs -- or I'm sorry -- if you're trying to recover re-- removal costs, I think that it's more appropriate to view it as a -- something similar to a maintenance cost, and -- and -- and view the equity in that manner.

Q. Well, I'm -- I'm -- I'm -- for purposes of my question I'm accepting the fact that we're not gonna put it in the depreciation rate.

A. Okay.

Q. But I'm saying that for the purposes of accounting for it, we're gonna account for it as a rate base -- a separate rate-base item so that if there is over- or underrecovery, that can be brought forward, as you point out, in your testimony --

A. It can be done --

Q. -- under the rate-base method.
A. -- that way.
Q. And isn't that more equitable, then there are no winners or losers?
A. So your question is, then, so would it be the equity of it?
Q. Yes, ma'am.
A. Okay. I would say the -- the rate base if -- if you want to retain it -- a tracker for any kind of equity, it -- it lends itself to that.
Q. To more equitable treatment, correct, of both shareholders and ratepayers?
A. Because this -- I mean, I -- I guess I'm seeing it as -- equity is that the Company's cost of service is evaluated each time they come in for a rate case, and that their costs are being reviewed and -- and recovered through rates analyzed at the time of a rate case.
So I -- I'm not seeing that -- in -- in the magnitude that we're seeing of cost of removal relative to other expense items, I -- I don't think that the equity there is -- is a proportion to make that kind of a statement.
Q. Well, what -- whether it's one dollar or a million dollars, the fact is, that if under the

rate--base treatment if there's over/underrecovery, you can adjust for it on a go-forward basis in the next rate case and no one gets hurts. As we've seen, there's no harm to earnings.

Under the income approach, as you've indicated in your -- in your testimony, there is a very likelihood of actual net cost of removal not equaling that that was put in the revenue requirement and somebody's gonna win and somebody's gonna lose, right, and -- and they can't be made whole?

A. I -- I would agree to the extent that there are -- there is a mechanism to be made whole for -- for whatever amount. That would be -- the tracker could do that.

Q. Okay. And if you're struggling with the word "equity," insert the word "fair." It's more fair, isn't it?

A. I think fair, because I can -- I can also have the other occur, as far as the cost removal on ex-- on expensing that they could -- they could also time their -- their costs out in the field.

So where the earnings don't -- I mean, they're -- so that earnings are not reduced. I -- I can see the other side of that occurring as well.

Q. That's my point.

Nobody loses under the rate-base method.

MR. SCHWARZ: I -- I think she's finally answered this question.

JUDGE JONES: I -- I -- I tend to agree.

MR. ENGLAND: Sorry. I'll move on.

BY MR. ENGLAND:

Q. Let me talk about -- now, we've talked about the rate-base treatment. Let -- let me talk about accruing an amount for net salvage -- future net salvage as part of the depreciation rate.

A. Okay.

Q. And I think -- and you say there on lines 10 through 12, it's not necessary to do that, basically.

A. That's correct.

Q. Okay. But you'd agree with me that that's what Pete Love did in the Company's '93 rate case that you cite in your rebuttal testimony page 14, lines 10 through 16, right?

A. I agree.

Q. Okay. And that's the way Staff handled cost of removal in a 1999 Laclede Gas rate case that we've talked about here previously, correct?

A. Yes.

Q. Okay. And that's the way it was done for this Company in its '97 rate case, correct?

A. As a part of the depreciation rate?

Q. Yes.

A. Yes.

Q. Okay. And would you agree with me by including net cost of removal in the depreciation rate, it has the same effect as the rate-base treatment we've been talking about?

A. Yes.

Q. Okay. Would you agree with me -- I'm so-- I'm sorry. I'm gonna switch gears on you.

Would you agree with me that the Company's rate base has increased since its last rate case?

A. I believe so.

Q. Do you know by how much -- ballpark?

A. Oh, I don't know without looking at the number.

Q. But you -- but you do know or believe that it has increased?

A. Yes.

Q. Okay. And the fact that the rate base has increased since the last case would indicate that expenditures on utility plant have exceeded -- exceeded -- excuse me -- depreciation accruals for the same period of time, correct?

A. Please repeat that question.

Q. Sure.
The fact that rate base has increased since the last case indicates that plant investment has exceeded depreciation accruals for that same period of time?
A. Plant additions have exceeded depreciation accrual if rate base has --
Q. Greater now than it was then, right?
A. Let's see. Let me think about what else could add to the -- I believe that to be the case.
Q. Okay. At surrebuttal testimony page 2, lines 15 through 16 you note that total annual depreciation expense proposed by the Company is approximately 45.5 million for the MPS properties.
Do you see that?
A. Yes.
Q. By comparison, Staff's proposed annual depreciation expense is 32 million?
A. Yes.
Q. Roughly the difference of 13-and-a-half million we talked about earlier?
A. Yes.
Q. Or if you take into consideration your expensing amount of $1-and-a-half million the net difference is 12?

A. Yes.

Q. Okay. Now, you're familiar with Mr. Stam's testimony filed in this case, correct?

A. Yes.

Q. You've responded to it in both your rebuttal and surrebuttal testimony.

I assume you saw where he testified that the Company plans to spend between $60 and $70 million a year on plant? That was his direct testimony page 17, lines 22 through 23.

Do you recall that?

A. I don't know, but I could look it up again.

Q. Do you have any reason to doubt it?

A. No.

Q. Okay. Well, let's just assume that for purposes of my next question.

Assume the Company is gonna be spending on average $60 to $70 million in new plant a year. Even under Company's proposed annual depreciation accrual or expense of 45.5 million, capital expenditures will more than exceed the annual accrual of 45.5 million, correct?

A. Yes.

Q. Okay. So would you agree with me that the Company will have to look to external sources of capital, such as debt or equity, in order to fund the remainder of its capital budget on an annual basis?

A. I don't think I would be able to answer that question --

Q. Okay.

A. -- how you look for your funding.

Q. Where do you -- do you have any idea where the Company is gonna get the -- the difference between $60 and $70 million that it's gonna spend on capital additions and the 45.5 million that it'd generate with internally generated funds?

A. I don't think that I would be able to answer that question.

Q. Okay. Would you agree with me that if the capital expenditures of 60 to 70 million and annual accruals are only 45.5 million, that the Company will not have excess money from its depreciation to spend on other things besides capital expenditures?

A. I guess I'm not gonna be able to say what they do with their monies from the depreciation.

Q. Not even from just a common sense, very high-level look at it -- if they're gonna spend 60 to 70 million and they're only going to generate --

MR. SCHWARZ: I'm gonna object. It was asked and answered.

JUDGE JONES: Yeah, I agree.

Move on, Mr. England. It's too late to ask the same question twice.

MR. ENGLAND: Okay. Fair enough, Your Honor. I won't try a third time then.

That's all I have. Thank you.

Thank you, Ms. Schad.

THE WITNESS: Thank you.

JUDGE JONES: Commissioner Murray, do you have questions?

COMMISSIONER MURRAY: Yes, I do, Judge.

Thank you.

This is later than we've usually been in the hearing room, I believe.

QUESTIONS BY COMMISSIONER MURRAY:

Q. I wanted to ask you on page 4 of your direct testimony at line 11 you give a definition of depreciation there.

A. Yes.

Q. Where did you get that definition?

A. I can't give you the exact text. I'm sure that over time I have recovered that, and I -- and I -- I can't tell you, you know, the exact -- an exact source that would say those words in that mechanism.

I -- I also have worked with depreciation on the outside of this arena, and I believe that that's how I saw -- except for it being in a regulatory environment, the depreciation was as I stated there.

Q. Have you reviewed authorities on depreciation that define it differently?

A. I believe the -- the ones that may define it differently might view it more as a -- or state it more -- rather than as a physical context, more as the -- more maybe of it as a statement, not -- not in regard to its physical aspect like an engineer would read it.

Q. Okay. Did you read the definition that the Commission used in Case ER-97-394, which you cited elsewhere in your testimony?

A. I bel-- I believe I would have read that.

Q. Would you have any reason to doubt that the Commission stated -- and this is on page 190 -- the Commission states, depreciation is a system of accounting that aims to distribute the cost or other basic value of tangible capital assets less salvage over the estimated useful life of the unit (which may be a group of assets)?

A. I -- I wouldn't have any reason to doubt that that would be as it's stated.

Q. Would you disagree with that definition?

A. No.
Q. Even though it includes in the definition less -- the words "less salvage"?
A. I -- I think that where the -- and -- and maybe I can say confusion that I see that develops -- is that -- the idea is that you want to be able to be sure to not overcharge.

So that in the arena that there existed probably for a fair number of years, you wanted to be sure that you recovered and -- and brought back original costs, but there was a salvage.

And that's why they call it -- that's why it was never termed cost of removal. Because it was really thought of as just that you're gonna go less than 100 percent by some degree.

So you -- you enter in a term net salvage, and there may have been a minimal amount of cost of removal to -- in order to create or in order to actually possess that salvage.

But the idea wasn't, as -- as I see it, that we get into an arena for cost of removal that is -- that can be percentagewise much more than -- than the salvage.

So that the -- if that was the case, the cost of removal -- in fact, we see it many times -- it is similar to like a maintenance cost or it can actually get caught up into the new capital costs.

So if they -- if they go to let's say like pull a pump -- you know, like if you have something go bad, you don't -- you don't write a contract to a company to say, I'm going to pull the pump, and that's worth so much of the contract. And then while I'm there, I'm gonna put in the new one. And then there's some salvage.

I mean, the -- the actual -- we see things happening in a couple of arenas. And the one that I'm trying to explain is that sometimes that, like, cost of the old plant actually gets absorbed into almost the -- the capital of new -- of placing new plants.

So -- so that can happen. Or if it's actually just simply a contract for -- for doing no more than -- than simply removing an item, it -- it is more like an -- like a maintenance item.

And I think, if you will, that that definition that's presented there -- it's presented there with the salvage, only because they want to make sure that they in the end did not overcharge the customer.

But it -- but not with the concept that cost of removal was going to be the line-item ticket of that concept.

Q. So you're saying you don't disagree with the idea of include -- of salvage being a part of the definition of deprec-- what is depreciated, so long as you're not talking about a negative net salvage?

A. Well, I don't -- I think that once you get into the realm where you're -- you're going over -- if I would like just the intent of recovering the original costs and applying that over time to a group of people, that the idea was simply not to overcharge. Not -- not to go into the arena that -- that one of these components has now become significant.

I -- I -- I think that what we're trying -- what I'm trying to do, hopefully with mine, is that when I -- when I do depreciation rate, I'm going to be able to know for certain that the dollars collected are going to be for that purpose, and I -- I can very clearly clarify that that's the dollars that's coming in from the ratepayers for original cost, and it's not being co-mingled with the cost that's not a set amount to -- to start out with.

Q. Okay. You said you thought the purpose was not to overcollect. Wouldn't the purpose have been to collect the right amount of the cost of the asset whether -- and not -- not over- or undercollect?

A. I -- I agree. But I think we're getting into something here that -- it's -- it's -- it's -- again, I -- I kind of say it's similar to a maintenance.

I'm -- I'm gonna -- just like we don't -- we don't include maintenance in that depreciation. And that's still -- you know, so I want to collect that original cost. And I want to be able to collect it knowing that that is what I'm collecting, and that's the amount I'm collecting.

Q. Okay. Let's move on.

Is -- would you agree that the cost of the re-- cost of removal is a cost associated with the years that the asset provided service?

A. I -- I believe so.

Q. And during the years that the asset provides service, shouldn't it be those ratepayers, who receive service during those years, that pay for the cost of the assets?

A. I think the dilemma is that I cannot be for sure that -- only to the extent of what's currently out there at the moment for -- for incur -- for -- for costs, and that -- that presents its own dilemma is that we -- we can't seem to get from the Company costs that will actually -- we -- that we can even know to be those costs.

We -- we had to deal with this -- Mr. Rooney's

Schedule from the FERC 1's. But when we go to what's on the asset management system numbers for what's the cost of removal and what's the salvage, they don't -- they don't equate. They're not the same set of numbers.

And, in fact, as a response to one of -- of the Data Requests it says, FERC Form 1 reports cost of removal and salvage activity for the year charged to retirement work in progress. The asset system reports cost of removal and salvage activity closed plant accounts during the year.

Cost of removal and salvage recorded in retirement work in progress is not always close to the asset system in the same year costs are incurred.

Cost of removal and salvage charged initially to retirement work in progress can be reclassified to another account, such as an expense account. The reclassification of these charges will not appear in the asset system.

So we were looking to -- to try to make an allowance for what is cost removal. But even from the Company they have two sets of numbers for that cost of removal, two sets of numbers for the salvage and they don't tie up.

And to what extent do you use -- I mean, the asset management system, those are the numbers that was provided to Staff in Data Requests.

But as this clearly shows that as they filled out the -- the FERC -- FERC Form 1's for cost of removal, it says the cost of removal and salvage charged initially to retirement work in progress can be reclassified to another account, such as an expense account.

The reclassification of these charges will not appear in the asset system.

Q. So did you seek further clarification of why those numbers did not --

A. I --

Q. -- apply with what you thought they should?

A. My -- because this -- this came in and I -- I would ask that you might refer that specific question to Cary Featherstone.

Q. Okay.

A. I know that we've -- we've had the concern -- we've had concerns with other utilities. This is not the first time.

But we -- if we want to clarify which -- which group of customers and who's charging what and who's -- who's -- what -- what is the amount, we first need to get to a situation where we know what those amounts are.

Q. Well, you're not talking about knowing with certainty what those amounts will be in the future, are you? You don't expect that the Company knows that, do you?

A. Well, I guess the -- we don't know -- now, we don't know the future, but we don't know the extent to which is the correct set of cost of removal amounts and the salvage amounts.

Q. So you think you're seeing two different sets of numbers, and you're not sure why they have two -- two sets of numbers?

A. Right. I -- I think that there's -- we're not to the point yet where these numbers are as good of data as we would like to see them.

Q. And, therefore, you don't think that --

A. And I -- I guess my concern is that when I -- when I looked at the -- the amount in the reserve, and given that for this Company we -- then we had two specific cases where the final wasn't allowed as -- as the Commission Order, and yet we still grew in magnitude to the level we did without any allowance for that final.

What's in there now was -- it was collected specifically for removing poles or removing a boiler tube, removing transmission lines. But not for, like, what's being inferred is -- is what's going to be that final cost of removal.

We're colle-- we were collecting for this company -- or the Company was magnitudes many, many times larger than the -- than the highest number that Mr. Rooney ever puts -- puts on his schedule for interim retirements.

Q. Now, when you say collecting, are you talking about depreciating?

A. Well, it was collected through the depreciation rate mechanism.

Q. And the chart that -- or the Exhibit 181 that Mr. England was kind enough to go through with us to make this understandable earlier, is that an example of what you would be calling collection?

Do you -- do you recall the exhibit?

A. No.

COMMISSIONER MURRAY: Does Staff counsel have a copy of that exhibit for --

BY COMMISSIONER MURRAY:

Q. And that's showing a $1,000 asset -- original cost $1,000 asset, the 10 percent return on equity and the depreciation?

A. Yeah, this is --

Q. Did you see the --

A. This is collecting only -- only original cost.

Q. No. This is collecting -- as you can see, the original cost was 1,000, but the depreciation is based on the original cost plus a $500 -- I believe it was a $500 cost of removal -- yes, that's what it was.

A. Oh, okay. So it was $1,000 plus $500.

Q. Cost of removal.

A. Oh, that was an estimation put in at the beginning, you're saying?

Q. Yes.

A. Okay. Okay. So could you ask me --

Q. Each month for 10 years $150 was depreciated?

A. Okay.

Q. And each time that happened, the rate base was reduced $150?

A. Yes.

Q. And at the end of the period, the asset was actually removed at a cost of $500?

A. Okay.

Q. Now, in that example, would you -- when you talk about they were actually collecting, are you talking about the --

A. The $50.

Q. -- cost of removal that went into those depreciation accruals each month, being a collection?

A. Yes. That $50, because otherwise you would have collected $100 each year.

Q. And the rate base would have been reduced only 100 instead of 150; is that right?

A. Right. Uh-huh.

Q. I just wanted to make sure I understood what you were calling collecting.

A. Uh-huh.

Q. On page 15 of your direct testimony you -- you make a recommendation there that the over-accrual of the book reserve for the Company's electric common assets be noted, but that no adjustment to the reserve be made at this time, because of the dynamics of depreciation estimation process.

After another depreciation study is conducted, trends in the over-accrual can be identified and appropriate steps can be proposed. The valuation of these booked reserves should be made in the future rate filings and, if appropriate, addressed if the relative magnitude changes.

And my question there is: If Staff really believes that -- that the Company has annually been charging its MPS customers over $13 million too much which is, I believe, was a statement you made --

A. That's right.
Q. -- earlier?
Why would Staff suggest that it -- it would be okay just to wait and observe future trends before making any adjustments?
A. Well, because the dollars -- when you look at the reserve -- and I -- I don't think there is anyone in this country that could go into the -- because a lot of times depreciation rates are ordered without what that net salvage is. So we can't determine what amount is in there for net salvage.
Because many times in many cases the net salvage is not identified. And when it was -- when it was done in, as Mr. England quoted "the traditional method," there is case after case where that's not identified.
We can't go in and -- and -- and know for certain what's original cost and what's -- what was for the net salvage component. So the idea here was that if I only am working with life and if I -- if I have the time between now and another depreciation study, and the only thing that's -- that is a variable is original cost or -- or my -- my average service lives, if I'm wrong -- if my estimate is not -- if my estimate is not on track, I will be able to determine if that is

what is not reflective of -- of the plant -- the lives, because that's the only variable going into it.

So at this point, because I couldn't say to this Commission, this number of dollars is from that overcollection of cost of removal; this number of dollars is from the truncation of the average service lives having compressed that; and this number of dollars is because we have better technology in the plants like better instrumentation that might save -- like save a turbine because you're starting to feel the vibrations so you -- you can get in there and do some work and -- and save -- so you don't have to actually, you know, retire the turbine. You can -- you can save it before you have a disaster.

I'm saying that cannot be determined. And I know -- and this isn't an issue just in Missouri. We've run into it across the country. You -- they don't know what part of the reserve is original cost, which part is for cost removal and which part has -- if -- if you were in a remaining life situation, which -- which part might have just been an amortization.

So what I felt like here was the -- the correct thing to do was allow the time to transpire between now and another rate case -- another depreciation study.

And I could -- I -- I -- at that point, then I could say with certainty that my lives are on tar-- on target, they're -- they're appropriate for the classification and the function of the assets.

And then I would try to alleviate any -- any change there and address, as -- as I said, the overcollection and the book reserve at that time. And it would be -- it would more appropriate.

Q. How would you quantify an overcollection of the book reserve?

A. If -- if it wasn't -- if -- if I could look at it in the -- in the sense of weightwise and you -- a lot of times you do have to weight all these things.

But if -- if in five years another depreciation study is done and my theoretical relative to the accrued is of the same proportion, then I would see that the lives are -- are -- are staying in the same proportion, and nothing else is causing that.

Or -- or if my theoretical -- my accumulated is -- is starting to really vary one way, then I know that it's the lives that I'm -- I'm kind of starting to really be off on, and then I could make a recommendation at that time.

Should we at that time recommend that the monies that were -- that we now would feel like we're perhaps part of the cost of removal build-up, that could be addressed.

Q. And would it be your position that everything that's found accrued for cost of removal is an overcollection?

A. I -- I would say for this company, I think, it's -- I -- it's my view, after having reviewed as much as I have, that it probably occurred during a time span of about -- probably from the '97 case forward.

Because I think at that time we -- Staff was proposing about a 2-point-something million dollar increase in the -- in the reserve -- I mean, in the depreciation expense.

And when I went back and looked at what was the level of the accrual -- let's say at '93 -- the actual accrual wasn't anywhere near what resulted as the result after the '97 case.

So I -- I -- I really -- although I can't quantify, you know, how much would have been prior to that time -- and that's my concern. I can't really quantify that part of it going back in time.

I would say I -- I -- with certainty from the '97 case until the 2001 case that that would be representative of an overcollection of the cost of removal.

Q. That what would be representative of an overco-- overcollection?

A. The -- the level that the reserve -- the de-- the depreciation and expense was each year.

Q. Well, like, what num-- are you talking about a number, a percentage or are you just saying because it was higher or --

A. Well, the lives -- I -- I think the -- I would say that, as I noted in here, about 14-and-a-half million a year was what was being collected for the cost of removal during a time span when they were only incurring -- well, in -- in the year 1998.

According to the records we have, they spent a net cost of removal of 126,000.

Q. And that would be where you want to charge the cost of removal, based on costs that have already been incurred rather than the costs of removal of the assets that are currently in use; is that right?

A. Can you say that again?

Q. Well, in order to -- to -- to use your numbers, you have to look at removals that have already taken place, right, over a five-year period?

A. Well, the number I just mentioned, $126,000, for cost removal, that -- that is an actual net cost of removal for 1998.

Q. So that is a removal that has already occurred?

A. Right.

Q. And that is not connected with the assets that are currently in place? This has nothing to do with the cost of their removal; is that right?

A. Right.

Q. Okay. On page 13 of your rebuttal testimony at lines 6 through 8 -- 7 -- 7 and 8 -- well, actually 6 through 8 you say, in the Commission's Report and Order in Case No. ER-97-394 it was noted the Commission has also found interim costs to be sufficient for purposes of recovery.

First of all, I couldn't find that. I wondered if you could give me a page citation?

A. Oh, okay. Well, maybe -- I had it here.

Q. You set it out as a quote, so I'm assuming you took it directly from --

A. Right.

Q. -- the Report and Order.

A. Yeah.

Well, I don't seem to still have that document. Let's see. On page 23.

Q. And I've got the bound volume, so --

A. Hopefully I --
Q. -- can you tell me what --
A. It was -- it was under a section called terminal net salvage.
Q. And -- okay. I see it now. I -- I was in that section. I just think I had my tab over it was why I didn't see it.
A. Oh, okay.
Q. What does that mean, do you know?
A. Well, I -- what I think it meant was that what the Commission did not want to do was -- was to have in the depreciation any component for the -- a final dismantling and -- and brown fill reclamation of a -- like a power plant.
I think that they did find that if you was going to have ongoing replacement of boiler tubes and poles and transmission -- I mean -- well, transmission line and components of that nature, that they found it -- that those interim costs are recoverable in -- in the -- in the rates.
Q. Okay. In your next statement after that quote in your testimony on page 13 is that the level of interim costs that should be recovered needs to reflect the current level of removal costs that the Company is incurring.

You didn't get that anywhere out of that Report and Order, did you?
A. I think that's my statement.
Q. All right. That doesn't follow from that -- from the reasoning in the Report and Order, does it?
A. Well, at the end of that section it wou-- it -- it went on to say the Commission finds that these terminal net salvage costs are speculative and not known and measurable and, therefore, may not be included in current rates.
Q. That was terminal?
A. It is.
Q. This is -- your statement is about interim costs.
A. Right. I -- I think, if I understood it, and -- and tracking back to the '93 and '90 there had been a consistency, at least in those cases, and if you would -- then I'm saying I am fur-- one case further.
In those first two cases that I spoke about, the Commission, if I understood it right, Melvin Love had recommended that the depreciation rate include a component for recovery of the interim costs, and at a -- at a current level basis.
And I saw in this -- so after a '90 case and after a '93 case, I didn't see anywhere in here that

that had been a diversion from that kind of a concept.
And then in conjunction with the clause that costs that become speculative are not known and measurable are not allowed, those two thoughts in conjunction then reflect that statement I -- I have there.
Q. Okay. And you -- on page 14 of your rebuttal you answer a question -- the question reads, has the Commission ordered depreciation rates that did not include a component for interim costs of remov-- removal; that is, a net salvage percentage, and your answer is, yes, and then you cite two cases.
Were those the only two that you know of?
A. To the extent that I could expand on that, I feel that the -- the stipulation and agreement that we just had in the 622 case -- and I know that this is always a situation where those -- those are usually black-box settlements.
But in that 622 case there was specific language in there that the depreciation rates that Staff had proposed were to be utilize and that the cost of removal was to be expensed.
So to the extent that I feel that that one --
Q. Do you understand why we don't use stipulation and agreements to indication any kind of Commission

policy?
A. I do. Although on that one, there was a statement specifically setting that out.
Q. But stipulations and agreements set out lots -- lots of various things that the parties have given --
A. As far as policies, I agree.
Q. Yes. And we don't know why an agreement was made to do certain things.
A. Oh, okay. I'll agree -- I'll agree with that, yes.
Q. Okay. In that case you were ref-- referring to, what -- what company was that?
A. That's this company.
Q. Okay. And that was -- what was the number?
A. 2001-622.
Q. Okay. And the two that you cited here were not stipulations and agreements; is that right?
A. That's correct.
Q. Okay. And --
A. And I -- and if I -- you know, I hope I didn't say that that was policy in that statement. I'm just saying that --
Q. I wouldn't have asked you if you said that.
A. Okay.

Q. I just asked you if you had any other cases that --

A. Oh, okay.

Q. You did say the methodology was incorporated. And I think you're saying the Commission ordered depreciation rates that did not include component for interim costs of removal not by stipulation and agreement, but by Commission Order?

A. Right.

COMMISSIONER MURRAY: I thought I had some other questions, but I -- I may -- that may be the end of it if I could just look through here one more time.

THE WITNESS: Okay.

COMMISSIONER MURRAY: That must be it.

Thank you.

THE WITNESS: Okay.

JUDGE JONES: Okay. Will there be recross?

MR. ENGLAND: One quick one, Your Honor.

RECROSS-EXAMINATION BY MR. ENGLAND:

Q. Ms. Schad, I think that Stipulation/Agreement you were referring to was in Case ER-2001-672?

A. I'm sorry if I misspoke that number. I think I said 622.

Q. That's -- I -- I thought I heard -- I heard something else.

And the other thing just to add to it, it also provided that the parties were free to contest the treatment of future net salvage costs in the next case in which Missouri Public Service's rates are at issue, right?

A. That is correct.

MR. ENGLAND: Okay. Thanks. No further questions.

JUDGE JONES: Thank you. Now we'll have redirect from the Staff.

REDIRECT EXAMINATION BY MR. SCHWARZ:

Q. At -- at some stage you were asked a question that you don't know what cost of removal will be next year; is that --

A. That's correct.

Q. Does the Company know what the cost of removal will be next year?

A. No. I -- I -- I guess I would like to rephrase that. I don't know if they know, but I would assume they don't.

Q. Now, there was some discussion about whether for lifespan plant paying with -- collecting the cost of removal after the plant has been retired, and those costs are actually known, but violate the intergenerational equity.

Do you recall those lines of questions?

A. Yes.

Q. Isn't it true that the customers who would be paying those costs at that time won't be paying for the cost of removal of the plant that's serving them?

A. I would assume that to be the case.

Q. So there's some balance there, isn't there?

A. Yes.

Q. You were also asked -- well, let me ask you this: Expensing rather than providing rate-base treatment of cost of the removal would provide an incentive for the Company to keep the costs of removal down, wouldn't it?

A. It would, as well as any kind of planning arrangement for -- for a rate-case scenario.

Q. Uh-huh.

And the use of tracker mechanisms were concerned, would it be possible to simply use trackers for all of the Company's expenses and have all rates be interim subject to refund?

A. Certainly.

Q. But not very practical?

A. It -- it may be practical for items that are of large magnitude and -- and quite variable; however, cost of removal is certainly not in that situation at this time.

Q. Do you still have Exhibit No. 181 in front of you?

A. Oh.

Q. It's Mr. England's --

A. Yes. Okay.

Q. Do you have it -- do you have that?

A. Yes.

Q. Now, under the column 10 percent return -- are you with me?

A. Yes.

Q. In Year 2 -- and let's say the Company doesn't have another rate case until the end of Year 6 -- so in Year 2 what would they be collecting in rates for the return on that rate base?

A. $85.

Q. If they -- if they haven't reduced rates, won't they still be collecting the $100 that was set in rates?

A. Yes.

Q. And in Year 3, what will they be collecting in rates?

A. $100.

Q. And in Year 4?

A. Same.

Q. Same.
So -- and when rates are rebased in Year 6, they would be rebased to $25. But in the subsequent years, they would continue to collect the $25 in rates, would they not?
A. Yes.
Q. Let's assume for some reason that rates are reset in Year 6, and for one reason or another the plant is retired. Rates aren't reset until Year 12.
Will the -- what will the Company collect in depreciation in Year 7?
A. Can you repeat that again, Mr. Schwarz?
Q. Assume that rates are reset in Year 6.
A. Okay.
Q. Okay. The -- for depreciation purposes, the depreciation expense on that property will remain $150, won't it?
A. Yes.
Q. And if for one reason or another, an accident, the plant is -- is retired in Year 8, they will continue to collect that $150 in rates until the rates are reset, won't they?
A. Yes.
Q. Is it unreasonable to expect an electric utility to invest in an electric utility plant?

A. No.
Q. Do you have a copy of Mr. White's testimony and schedules?
A. Yes.
Q. Were you here -- let me ask you this: When I asked him about his ob-- objectives of depreciation being -- having something to do with the present value of future net revenue or cash in-flows attributable to the use of that asset alone.
Do you --
A. Yes.
Q. -- recall that?
Is -- is that a definition that's commonly used in the -- or traditionally used in the utility arena?
A. I don't believe so.
Q. You didn't -- you didn't do a net present value of the revenue streams attributable to individual pieces of utility property?
A. The -- the revenues that those created as a result of those having been in service?
Q. Yes.
A. No.
Q. Are you aware of anyone who does that?
A. I would say that in an academia world it

probably does get done on a frequent basis.

Q. But not in the world of utility regulation?

A. No.

MR. SCHWARZ: I think that's all I have. Thank you.

JUDGE JONES: Ms. Schad, you may step down.

THE WITNESS: Okay.

(Witness excused.)

JUDGE JONES: Will Staff call its next witness.

MR. SCHWARZ: Cary Featherstone.

JUDGE JONES: And, Mr. Featherstone, you still remain under oath.

MR. SCHWARZ: And his testimony has been identified and offered, so I just need to tender him for cross-examination on this issue --

JUDGE JONES: I believe that's true.

MR. SCHWARZ: -- which I do.

JUDGE JONES: Does Aquila have cross for Mr. Featherstone?

MR. ENGLAND: No, we don't, Your Honor.

JUDGE JONES: Will there be questions from the Bench for Mr. Featherstone?

COMMISSIONER MURRAY: Just a few. Thank you. And I will try to keep it to a few. I know the hour is late.

CARY G. FEATHERSTONE, having been previously sworn, testified as follows:

QUESTIONS BY COMMISSIONER MURRAY:

Q. But I would like you to go to page 10 of your direct testimony. And --

A. Yes, ma'am.

Q. Actually on page 9 -- the bottom of page 9 there is a question posed there, have cost of removal and salvage value been treated in this way in prior Aquila rate cases, and your answer is, yes.

And I -- I think it's interesting that the reader has to be rather alert to -- to pick up on the fact that you're talking about primarily Staff's position in other rate cases.

But you do make the statement that it was a method that Staff used in the last Aquila rate case, which was a stipulation and agreement, correct?

A. It -- it was. The -- the language specifically spelled out --

Q. I understand that.

A. It identified -- I think you visited with --

Q. Yes.

A. -- with Ms. Schad. It did spell out how depreciation was going to be calculated.

Q. And that was based on the stipulation and agreement, then?

A. It was.

Q. And this was Staff's method that you're speaking of, which is --

A. Yes.

Q. And -- and then the next question was, has Staff treated cost of removal and salvage amounts in other rate cases consistent with the way that they've been treated in this case, and your answer, again, is yes.

And you cite several cases.

A. Yes.

Q. And you say the cases that cost of removal has been treated as an expense item netted against any salvage amounts are -- and, once again, I think you're talking about in Staff's recommendations; is that right?

A. Yes. My testimony is only addressing how Staff viewed this issue and how it filed testimony with -- with regard to this issue in these cases.

Q. Okay. And were any of those cases that you listed -- did they result in stipulation and agreements?

A. Pardon me. Many of them were

stipulation/agreements. Probably be easier to talk about the ones that were not.

Q. Okay. Which ones were not?

A. The St. Louis County Water case, Case No. WR-2000-844 was an ordered case.

Q. Okay.

A. And that was -- the methodology was rejected by the Commission. The Empire District Electric Company case, Case No. ER-2001-299 -- that case was ordered, and I believe that case -- the Commission adopted the position.

There is one other case that's not on this list. It was what I filed in the gas case, and it was an ordered case that adopted Staff methodology. And that was a Northeast Missouri Rural Telephone case, Case No. TR-2001-344.

Q. When you're talking about a -- a rural telephone case, you're talking about a -- an insignificant effect on revenue requirement, are you not, for this issue?

A. I don't know.

Q. Okay.

A. I -- I guess I would say that someone felt it was significant in -- in -- in that they brought it before the Commission as a dispute to be resolved.

Q. Give me the cite on that again, if you would. I didn't get that full cite.

A. I'm sorry. It's Northeast Missouri Rural Telephone.

Q. Uh-huh.

A. Case No. TR-2001-344.

Q. 344.

And that specific issue was contested?

A. Yes, ma'am.

COMMISSIONER MURRAY: Well, I hate to disappoint you, but I don't think I have any more questions.

Thank you.

JUDGE JONES: Will there be redirect based on the questions from the Bench?

MR. ENGLAND: I'm sorry? Is that a --

JUDGE JONES: No. Recross -- I'm sorry -- based on questions from the Bench?

MR. ENGLAND: I -- I was triggered by Commissioner Murray's questioning.

RECROSS-EXAMINATION BY MR. ENGLAND:

Q. Good evening, Mr. Featherstone.

A. Good evening.

Q. You list on the -- on page 10 all of these cases where Staff has expensed cost of removal. And the very first one caught my attention, AmerenUE gas case, GR-2000-512.

When I inquired of Ms. Schad about her experience, I thought she indicated to me that that was a case where they followed the traditional -- excuse me -- that the Staff followed the traditional approach.

You, however, indicate that it's the expensing approach. Can you help me on that?

A. Can I have one second?

Q. Sure.

A. I can't -- I'm sorry. I don't have that Order. That's something that we could provide you.

Q. Well, it -- I mean, I just -- it occurred to me as I was loo-- when I saw that number there, because that -- and I had written it down when I was asking her the question.

So, yeah, if you could just kind of clarify that with after-the-fact representation, that would be fine. I mean, it's one or the other, right?

A. Yes.

Q. It -- it was either expensed or -- or accrued as part of the rate?

A. Yes.

Q. Okay.

A. The information that I had -- and right now I don't have it with me -- pardon me -- that I relied on was the -- the Staff's methodology -- current methodology.

MR. ENGLAND: Okay. Your Honor, could I --

THE WITNESS: We can --

MR. ENGLAND: -- request that maybe that be clarified later? I don't need further examination or anything like that. A statement one way or the other would be sufficient.

JUDGE JONES: Yes, I suppose you can step down, but --

COMMISSIONER MURRAY: Can I --

JUDGE JONES: -- not be excu-- oh --

COMMISSIONER MURRAY: -- just ask one more question?

JUDGE JONES: -- Commissioner Murray.

COMMISSIONER MURRAY: I -- I'm sorry.

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. Something you just said, I have to ask you this: You said Staff's current methodology. When -- when did that become Staff's methodology?

A. Well, I don't know the exact date. It's been several years. I think probably most of this decade, if not all. I -- I think probably around 2000, maybe 1999.

COMMISSIONER MURRAY: Thank you.

THE WITNESS: Uh-huh.

JUDGE JONES: I -- is it necessary for -- may he be excused after this?

MR. ENGLAND: Oh, yeah, I -- the rep-- a statement from counsel would be sufficient just for purposes of the record --

JUDGE JONES: Okay.

MR. ENGLAND: -- whenever.

THE WITNESS: I will be here tomorrow.

MR. SCHWARZ: Well, you know, I --

MR. ENGLAND: I want him to do it right now, Your Honor.

MR. SCHWARZ: I -- I would like -- I would like to be able to do that through whatever counsel actually happens to be in the hearing room --

JUDGE JONES: That'll be --

MR. SCHWARZ: -- as opposed to myself. We could certainly arrange --

JUDGE JONES: That'll be fine.

MR. ENGLAND: That's fine.

Thank you, Your Honor.

Thank you, Mr. Featherstone. You may step down.

THE WITNESS: Thank you.

(Witness excused.)

JUDGE JONES: With that, we will conclude the hearing, and we are adjourned. And we will continue tomorrow at 8:30 in the morning.

WHEREUPON, the hearing of this case was adjourned until 8:30 a.m., Friday, March 5, 2004.

I N D E X

DEPRECIATION/COST OF REMOVAL

E X H I B I T S   I N D E X

	MARKED	RECEIVED
Exhibit No. 38 Direct Testimony of H. Davis Rooney	*	1380
Exhibit No. 39 Rebuttal Testimony of H. Davis Rooney	*	1380
Exhibit No. 40 Surrebuttal Testimony of H. Davis Rooney	*	1380
Exhibit No. 101 Direct Testimony of Rosella L. Schad	*	1421
Exhibit No. 102 Rebuttal Testimony of Rosella L. Schad	*	1421
Exhibit No. 103 Surrebuttal Testimony of Rosella L. Schad	*	1421
Exhibit No. 146 Corrected Schedule 4	*	1421
Exhibit No. 176 Updated Valuation of Aries Unit Capacity PS Share of Cass County Lease Costs	1368	
Exhibit No. 180 Retrospective Analysis of Staff's Method New Rates Each Year	1376	1380
Exhibit No. 181 Handwritten schedule	1417	1418
Exhibit No. 1038 Revised Direct Testimony of H. Davis Rooney	*	1380

E X H I B I T S I N D E X (CONTINUED)

	MARKED	RECEIVED
Exhibit No. 1039 Revised Rebuttal Testimony of H. Davis Rooney	*	1380
Exhibit No. 1040 Revised Surrebuttal Testimony of H. Davis Rooney	*	1380
Exhibit No. 1101 Revised Direct Testimony of Rosella L. Schad	*	1421
Exhibit No. 1102 Revised Rebuttal Testimony of Rosella L. Schad	*	1421
Exhibit No. 1103 Revised Surrebuttal Testimony of Rosella L. Schad	*	1421

* Exhibits marked prior to proceedings.