

Exhibit No.: 009
Issues: Policy
Witness: Robert J. Hack
Sponsoring Party: Missouri Gas Energy
Case No.: GR-2006-
Date Testimony Prepared: May 1, 2006

MISSOURI PUBLIC SERVICE COMMISSION

MISSOURI GAS ENERGY

CASE NO. GR-2006-

FILED²

FEB 07 2007

Missouri Public
Service Commission

DIRECT TESTIMONY OF

ROBERT J. HACK

Jefferson City, Missouri

May 2006

MGE Exhibit No. 9
Case No(s). GR-2006-0402
Date 1-8-07 Rptr pf

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MISSOURI PUBLIC SERVICE COMMISSION

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DIRECT TESTIMONY OF

ROBERT J. HACK

CASE NO. GR-2006-

May 2006

1 **Q. WOULD YOU PLEASE STATE YOUR NAME AND BUSINESS ADDRESS?**

2 A. My name is Robert J. Hack, and my business address is 3420 Broadway, Kansas City,
3 Missouri 64111.

4

5 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6 A. I am the Chief Operating Officer of Missouri Gas Energy ("MGE" or "Company"), a
7 division of Southern Union Company.

8

9 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.**

10 A. I graduated from Southern Methodist University with a B.A. in English Literature and
11 from the University of Kansas School of Law with a law degree.

12

13 **Q. PLEASE DESCRIBE YOUR PROFESSIONAL BACKGROUND.**

14 A. I have been in my present position since January 2006.

15

16 Prior to being named Chief Operating Officer of MGE, I served as MGE's Vice
17 President of Pricing and Regulatory Affairs beginning in October 1998. I joined the
18 Company in September of 1996 as a senior attorney.

1
2 Prior to my employment with MGE, I worked in the general counsel's office of the
3 Missouri Public Service Commission ("Commission", beginning in February of
4 1989), serving in various positions including assistant general counsel, deputy general
5 counsel and general counsel. My employment with the Commission ceased in July
6 1996.

7
8 Since 1989, therefore, my career has been focused on regulated public utilities
9 generally and, since 1996, on MGE as a regulated natural gas local distribution
10 company ("LDC").
11

12 **1. EXECUTIVE SUMMARY**

13 **Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?**

14 A. First, I will explain the fundamental business model my team continues to implement
15 at MGE, which is to be a low-cost provider of quality customer service while striving
16 to appropriately balance the interests of our primary stakeholder groups – employees,
17 customers and shareholders. In the course of this explanation I will reiterate the
18 emphasis that MGE has placed, and will seek to continue to place, on quality
19 customer service and try to bring forward specific examples of how MGE has
20 implemented this business model.

21
22 Next, I will provide an overall perspective on the ratemaking process that MGE has
23 experienced historically, in particular the fact that MGE has consistently failed to

1 achieve its Commission-authorized rate of return, as well as suggested enhancements
2 to that process. In so doing, I will address certain fundamental business challenges
3 faced by MGE and the related critical policy issues that I believe the Commission
4 itself should address in setting rates for MGE.

5
6 Finally, I will discuss the major reasons for the Company's decision to file a general
7 rate case at this time – 1) a consistent inability to achieve our Commission-authorized
8 rate of return, driven primarily by chronic and material volumetric revenue shortfalls
9 due to warm weather and declining average use per-customer; 2) the need for MGE to
10 obtain an authorized rate of return from the Commission that is competitive in the
11 industry and commensurate with the risks borne by the shareholders who invest in
12 MGE; and 3) cost of service increases attributable to other factors, including
13 additional capital deployed on MGE's system and continued exceedingly high gas
14 costs, among other things – and introduce the other MGE witnesses presenting direct
15 testimony.

16
17 **2. MGE IS COMMITTED TO BEING A LOW-COST PROVIDER OF**
18 **QUALITY CUSTOMER SERVICE**
19

20 **Q. PLEASE EXPLAIN THE FUNDAMENTAL BUSINESS STRATEGY YOU**
21 **ARE CONTINUING TO IMPLEMENT AT MGE.**

22 **A.** Our fundamental business strategy is to be a low-cost provider of quality customer
23 service. When I began my work as MGE's Chief Operating Officer in January of

1 2006, this overall direction was already in place. Implementing this strategy requires
2 a balance of cost management and quality customer service.
3

4 **Q. WHAT GUIDING PRINCIPLES DO YOU USE IN FURTHERANCE OF**
5 **MGE'S FUNDAMENTAL BUSINESS STRATEGY OF BEING A LOW-COST**
6 **PROVIDER OF QUALITY CUSTOMER SERVICE?**

7 A. Safety is our first priority. Natural gas is safe when contained, but it is a combustible
8 commodity and can be hazardous if not contained. We take very seriously the need to
9 safeguard our customers and employees as well as the public generally. We also
10 emphasize safety throughout the business in everyday activities like driving vehicles,
11 lifting objects, and other day-to-day undertakings.
12

13 For a business to be a lasting success, its management must successfully balance the
14 interests of three key constituencies: employees, customers and shareholders. We try
15 to keep this fact in mind whenever we make decisions.
16

17 In my opinion, shareholders are not likely to be satisfied if customers are not pleased,
18 and that customers are not likely to be satisfied if employees are not satisfied.
19 Therefore, MGE places heavy emphasis on employee and customer satisfaction.
20

21 **Q. CAN YOU PROVIDE EXAMPLES OF HOW MGE HAS EMPHASIZED**
22 **EMPLOYEE SATISFACTION?**

1 A. We continue to strive for a constructive and non-adversarial working relationship
2 with our bargaining unit employees through periodic meetings to address issues of
3 mutual concern and help build a more efficient and effective company.

4
5 We also devote substantial efforts to ensuring that we communicate effectively with
6 employees. The MGE senior management team conducts "all-employee" meetings
7 two times a year throughout our service territory. We have also instituted what we
8 call our "leadership forum," during which virtually all employees with supervisory
9 responsibilities are provided with in-depth information concerning critical company
10 activities so they may provide effective responses to questions from the employees
11 who report to them.

12
13 We also conduct employee surveys, typically every twelve to eighteen months, that
14 provide us with feedback in this area.

15
16 **Q. HOW DO YOU RATE MGE'S EMPLOYEE SATISFACTION EFFORTS?**

17 A. Overall, I think we have done a good job and the employee surveys generally back
18 this up. We know, however, that the passage of time is accompanied by new
19 challenges. In order to meet these challenges successfully, we need employees who
20 understand where we are going and believe in that direction. Thus, MGE will
21 continue to emphasize employee communication and satisfaction.

22

1 Q. CAN YOU PROVIDE EXAMPLES OF HOW MGE HAS EMPHASIZED
2 CUSTOMER SATISFACTION?

3 A. MGE's customer satisfaction efforts were well under way upon my promotion in
4 January of 2006. Financial resources permitting, I intend to continue those efforts
5 during my tenure. We encourage our employees to work with the "mind of a
6 customer and the pride of an owner," and most of them are doing so. We are
7 continually striving to make it easier for our customers to do business with MGE. As
8 shown more specifically in the direct testimony of MGE witness Carlton A. Ricketts,
9 the Company has achieved and generally maintained high quality customer service
10 performance levels. Technology deployment and process improvement efforts go
11 hand in hand with appropriate staffing levels to support MGE's emphasis on customer
12 satisfaction. In fact, a newly hired class of nine customer consultants began training
13 on March 13, 2006. As explained in more detail below, MGE has achieved this high
14 quality performance in a very cost-effective fashion.

15
16 Similar to our belief that employees both desire and need effective communications,
17 MGE emphasizes effective customer communications. As the likelihood of continued
18 high gas prices became apparent early in 2005, MGE began to communicate early and
19 often about the issue with its customers.

20
21 Q. PLEASE SUMMARIZE THOSE EFFORTS.

22 A. Those customer communication efforts continued throughout the year in the form of:

- 1 • Specific outreach to the senior citizen community centers throughout
2 MGE's service territory with educational programs on energy
3 assistance, energy conservation and weatherization, safety education,
4 and understanding gas service;
- 5 • Specific training and educational programs for social service agencies
6 and faith-based organizations regarding energy assistance,
7 weatherization, conservation and safety education;
- 8 • Printed materials about MGE and national energy policy issues
9 provided to state and local policy makers;
- 10 • Specific information provided to municipalities about the impact on
11 franchise fees when gas prices are higher and their option to contribute
12 the resulting unanticipated revenue increases to utility fuel fund
13 efforts;
- 14 • Media campaign to promote level pay and weatherization through
15 radio/TV talk shows, local newspaper stories and radio advertising;
- 16 • Bill insert focusing on price of gas information, ABC ("Average Bill
17 Calculation") plan and conservation tips; and
- 18 • Continued match of funds to MGE fuel fund (approximately \$75,000
19 in cash and credits), Neighbors Helping Neighbors and contributed an
20 additional \$100,000 in the form of Neighbors Helping Neighbors
21 credits. (See Media Advisory attached hereto as Schedule RH-1)
22 MGE has contributed to increasing the capacity of the assistance
23 delivery system by partnering with the Mid America Assistance

1 Coalition ("MAAC") by paying the MAACLink fees for agencies that
2 provide assistance to MGE customers.
3

4 **Q. WHAT OTHER COMMUNICATION EFFORTS HAS THE COMPANY**
5 **UNDERTAKEN?**

6 A. Perhaps most important is the process MGE began in 2002 to partner with the IRS
7 and other local businesses to form the KC CASH organization. MGE is a founding
8 member of KC CASH organization (Creating Assets, Savings & Hope), a
9 metropolitan Kansas City collaborative that works to expand the capacity and
10 availability of low-income tax preparation sites and promotes access to tax credit
11 information and benefits available to income eligible clients. The ultimate goal is to
12 connect people with financial resources to improve their self sufficiency.
13

14 **Q. WHAT CAUSED MGE TO BEGIN THIS PROCESS?**

15 A. This effort began as a result of a November 6, 2002 Cold Weather Rule Roundtable
16 convened by the Commission where presenters identified the low participation rate of
17 Missouri residents applying for EITC (Earned Income Tax Credit). Based on that
18 meeting, MGE staff attended an EITC conference in Atlanta and worked to bring a
19 similar conference to Kansas City in February 2003. Soon after, KC CASH was
20 officially organized and began its mission of communicating EITC and other tax
21 credit information by establishing and staffing VITA (Volunteer Income Tax
22 Assistance) sites for low-income customers. Exit surveys of VITA site participants

1 indicate that a majority of individuals utilizing VITA sites and eligible for tax credits
2 utilize the dollars for bill payment, including utilities and groceries.

3
4 MGE is actively involved in the communities we serve to collaborate, inform, and
5 enhance customer solutions through participation with numerous community
6 organizations, including: Committee to Keep Missourians Warm ("CKMW"),
7 Professionals In Aging, LINC Aging Committee, Housing Services Coalition, Agency
8 Cluster Meetings, National Fuel Funds Network, and Chambers of Commerce.

9
10 **Q. HOW DO YOU RATE MGE'S CUSTOMER SATISFACTION EFFORTS?**

11 A. Overall, I think we have done a good job, especially when appropriate consideration
12 is given to the chronic earnings shortfalls MGE has experienced.

13
14 **Q. DO YOU HAVE ANY INFORMATION SHOWING HOW MGE'S COSTS**
15 **COMPARE TO OTHER REASONABLY COMPARABLE NATURAL GAS**
16 **LOCAL DISTRIBUTION COMPANIES IN MISSOURI?**

17 A. As shown in the direct testimony of MGE witness Michael R. Noack, MGE provides
18 service in a considerably more cost-effective fashion than other Missouri LDCs. The
19 following chart, which is based on Mr. Noack's analysis, compares MGE's operations
20 and maintenance ("O&M") costs to other reasonably comparable Missouri LDCs (i.e.,
21 larger LDCs with a meaningful proportion of their customer base that is served in
22 urban or suburban areas). In comparison to these other Missouri LDCs, MGE
23 provides service in a considerably more cost-effective fashion.

	<u>MGE</u>	<u>Laclede</u>	<u>AmerenUE</u>	<u>MoPub</u>
1998	\$116.85	\$166.35	\$167.82	\$185.21
1999	\$115.37	\$162.00	\$167.01	\$180.30
2000	\$119.81	\$164.89	\$184.86	\$212.23
2001	\$141.59	\$188.43	\$215.26	\$224.42
2002	\$117.35	\$193.29	\$274.22	\$252.15
2003	\$141.04	\$212.95	\$237.04	\$204.56
2004	\$150.58	\$216.96	\$197.07	\$214.26

Also as shown in the direct testimony of MGE witness Michael R. Noack, a comparison of annual residential bills on the basis of margin rates (the sum of the fixed monthly rate element plus volumetric delivery rates) shows that MGE is considerably lower-priced than these companies. The following chart, based on Mr. Noack's analysis, shows that MGE is the lowest price provider by a considerable margin.

<u>MGE</u>	<u>Laclede</u>	<u>AmerenUE</u>	<u>MoPub</u>
\$263.15	\$329.23	\$379.91	\$361.04

Q. AS SOMEONE WITH A GREAT DEAL OF EXPERIENCE IN THE AREA OF UTILITY REGULATION AND OPERATIONS, WOULD YOU CONSIDER IT REASONABLE TO RELY ON MR. NOACK'S ANALYSIS FOR THE PURPOSE OF COMPARING MGE'S COSTS AND PRICES TO OTHER MISSOURI COMPANIES?

A. Yes. The purpose of these cost and price comparisons is not to establish that MGE is identical to these other companies or that these other companies are identical to MGE or one another; they are clearly not identical to one another. However, I believe it is

1 reasonable to make these comparisons because they are based only on LDC
2 operations in Missouri that have at least some meaningful urban or suburban service
3 territory and are therefore subject to similar, if not always identical, economic and
4 operating conditions and regulatory requirements. Perhaps more pertinent, though,
5 increasing MGE's residential margin (i.e., non-gas cost) revenues by \$5 per month (or
6 \$60 per year, which would produce an annual revenue increase of approximately \$26
7 million) would still leave MGE's residential customers paying less than the
8 residential customers of those other Missouri companies.

9
10 **Q. MR. HACK, IS MGE COMMITTED TO ACHIEVING CUSTOMER**
11 **SERVICE PERFORMANCE LEVELS IN THE FUTURE SIMILAR TO**
12 **THOSE WHICH HAVE BEEN ACHIEVED IN THE PAST FEW YEARS?**

13 **A.** Yes, provided we have the financial resources to do so. Performance metrics such as
14 average speed of answer ("ASA") and abandoned call rate ("ACR"), which indicate
15 the quality of customer service being provided, are substantially driven by the
16 relationship between the number of customer phone calls and the number of
17 employees available to handle those calls. Call volumes seem to be sustaining at
18 historically high levels, likely due to high wholesale commodity prices that have been
19 prevailing for some time now. Contact center employee turnover is relatively high
20 compared to other parts of MGE's operation, so regular hiring in that area is typically
21 necessary just to maintain a relatively constant number of employees. We recently
22 hired nine new employees who began their training for MGE's contact center on
23 March 13, 2006, even though it was apparent at the time MGE extended these

1 employment offers in late February that margin revenues were falling short of
2 budgeted expectations by many millions of dollars. Making the decision to hire
3 contact center employees in an effort to maintain service quality metrics like ASA and
4 ACR in the face of significant revenue shortfalls is very difficult; nevertheless, MGE
5 has done so over the last several years. Over the longer term, however, choosing to
6 hire employees when earnings are consistently inadequate is not a sustainable
7 proposition.

8
9 So while we are committed to providing high quality service, we are also committed
10 to providing service at a reasonable cost to the customer. At the same time, our
11 shareholders are entitled to a reasonable opportunity to achieve the return authorized
12 by the Commission. The bottom line is that service quality must be balanced with
13 cost and earnings considerations. I firmly believe that the Commission needs to
14 demonstrate the value it places on service quality by fairly compensating MGE and by
15 providing MGE a real opportunity through the ratemaking process to realize its
16 Commission-authorized return.

17
18 **Q. CAN YOU PROVIDE EXAMPLES OF HOW MGE HAS EMPHASIZED**
19 **SHAREHOLDER SATISFACTION?**

20 **A.** In addition to the significant efforts toward cost control that we devote every single
21 day (as evidenced by the cost comparisons to peer companies in Missouri discussed
22 earlier), the filing of this rate case is another example of the emphasis MGE places on
23 shareholder satisfaction. It troubles me that MGE finds it necessary to make this rate

1 increase filing so soon after MGE's most recent rate order took effect in October of
2 2004. The filing of a general rate case, while necessary and a part of doing business
3 as a regulated public utility, is not something we take lightly. It is an expensive and
4 time consuming process that diverts substantial management attention away from the
5 Company's primary mission, which is to provide safe and reliable gas service to its
6 customers. Nevertheless, without revenues sufficient to generate a return that is
7 competitive in the marketplace, the Company will be in no position to provide the
8 quality of service our customers expect and deserve. Therefore, MGE has decided to
9 file this rate case.

10

11 **Q. HOW DO YOU RATE MGE'S SHAREHOLDER SATISFACTION EFFORTS?**

12 A. Overall, I think we have a considerable amount of work left to do. I cannot
13 characterize our efforts as successful in this area primarily because, as shown in the
14 direct testimony of MGE witness Michael R. Noack, MGE has consistently failed to
15 achieve its Commission-authorized rate of return.

16

17 **3. RATEMAKING PRACTICE, POLICY AND IMPACTS**

18 **Q. WHAT IS YOUR UNDERSTANDING OF THE OVERALL OBJECTIVE OF**
19 **THE RATEMAKING PROCESS AND THE ROLE AND RESPONSIBILITY**
20 **OF THE COMMISSION?**

21 A. My understanding is that rates should be set so as to provide the utility with a
22 reasonable opportunity to achieve its authorized return. The authorized return itself
23 must be sufficient to compensate shareholders for the risk they bear while enabling

1 the attraction of capital on reasonable terms in the competitive marketplace. The
2 Commission's responsibility is to balance the multitude of sometimes conflicting
3 interests that arise through this process (e.g., enhanced service levels vs. lower rates;
4 small customer interests vs. large customer interests; customer interests vs.
5 shareholder interests; etc.) and set rates that are just and reasonable. Unfortunately,
6 the interests of the Company's shareholders have not been adequately addressed
7 through the rate setting process as evidenced by the fact that MGE has consistently
8 failed to achieve its Commission-authorized rate of return.

9
10 **Q. CAN YOU EXPLAIN WHY MGE HAS CONSISTENTLY FAILED TO**
11 **ACHIEVE ITS COMMISSION-AUTHORIZED RETURN?**

12 **A.** First, although unanticipated expenditures which impair achieved returns do crop up
13 from time to time, the incidence of such events is relatively infrequent in MGE's
14 history. Overall, I believe MGE has effectively managed its operating and
15 maintenance ("O&M") expenses while at the same time delivering high quality
16 service to our customers. Effective management of O&M expenses serves the dual
17 interests of customers (through rates lower than they would otherwise experience) and
18 shareholders (through reduced earnings erosion).

19
20 In a nutshell, MGE has consistently failed to achieve its authorized return primarily
21 because of the way in which its rates have been set in the past. The regulatory process
22 has resulted in rates for MGE based on assumptions that have not reasonably reflected
23 the reality of MGE's operations. In particular, rate design decisions have largely

1 relied on volumetric rate elements for cost recovery, making the Company's revenues
2 and earnings dependent on cold weather, even though the vast majority of MGE's cost
3 structure does not vary with changes in volumes or weather. Compounding this
4 increased dependence on cold weather is the fact that the actual per-customer usage
5 experienced on MGE's system rarely, if ever, reaches the per-customer usage
6 employed in the regulatory process of setting MGE's rate levels. Finally, as shown in
7 the direct testimony of MGE witness Michael R. Noack, MGE's actual bad debt
8 expense has exceeded its rate case allowance by approximately \$1 million annually,
9 on average over the past ten years. Ever-increasing bad debt expense and continually
10 declining per-customer usage are factors which have also been exacerbated by the
11 extraordinarily high natural gas commodity prices that have been prevailing for some
12 time now. It is becoming increasingly apparent that high natural gas prices also
13 contribute significantly to higher call volumes being experienced by MGE's customer
14 contact center, straining the resources required in this area as well.

15
16 **Q. PLEASE ELABORATE ON YOUR POINT ABOUT RATE DESIGN.**

17 A. Since MGE began operations in 1994, the majority of the revenue increases approved
18 by the Commission for MGE have been placed on volumetric rate components.
19 Because volumetric rates are subject to variation in relation to weather, the percentage
20 of MGE's revenues dependent on weather has increased over time.

21
22 **Q. PLEASE ELABORATE ON YOUR POINT ABOUT PER-CUSTOMER**
23 **USAGE.**

1 A. As shown in the direct testimony of MGE witness Russell A. Feingold, the per-
2 customer usage assumed through the rate setting process has consistently and
3 materially declined over the years, but has still routinely exceeded the usage per-
4 customer actually experienced on MGE's system. The following chart, based on Mr.
5 Feingold's analysis, compares actual usage per customer to the usage per customer
6 (residential) over the last seven years assumed through the rate setting process to
7 calculate MGE's rates:

	<u>Actual Usage per-Customer</u>	<u>Rate Case Usage per-Customer</u>
8		
9	FY99 882 Ccf	1,035 Ccf
10	FY00 812Ccf	1,035 Ccf
11	FY01 1011 Ccf	1,035 Ccf
12	FY02 806 Ccf	965 Ccf
13	FY03 911 Ccf	965 Ccf
14	FY04 841 Ccf	965 Ccf
15	CY05* 798 Ccf	903 Ccf
16	CY06# 358 Ccf	493 Ccf

17 *MGE's fiscal year end changed from June 30 to December 31 in 2005.

18 #Through March of 2006 per Schedule H-21 of MGE witness Noack's direct
19 testimony.
20
21

22 Because actual usage per-customer has not—even in the so-called cold years of FY01
23 and FY03—reached the rate case usage per-customer, MGE has not been able to
24 achieve its authorized rate of return. This volumetric revenue shortfall – which is the
25 product of differences between actual weather and “normal” weather assumed through
26 the rate setting process as well as consistently declining customer usage independent
27 of weather impacts – is the primary reason MGE finds it necessary to file this rate
28 case so soon after the implementation of its last rate order in October 2004. Absent a
29 meaningful solution in this rate case to the material and chronic problem of variable

1 and declining usage per customer, it is a virtual certainty that MGE will be required to
2 file another rate case quickly on the heels of the conclusion of this one.

3
4 **Q. PLEASE ELABORATE ON YOUR POINT ABOUT BAD DEBT EXPENSE.**

5 A. As shown in the direct testimony of Mr. Noack, bad debt expense varies considerably
6 from year to year. The following chart, which is based on Mr. Noack's analysis,
7 shows the relationship between actual bad debt experienced by the Company and the
8 bad debt allowance included in rates for the past ten years:

	<u>Actual Bad Debt</u>	<u>Bad Debt Allowance in Rates</u>
9 FY96	\$3,906,455	\$3,409,662
10 FY97	9,442,692	3,409,662
11 FY98	4,469,856	3,409,662
12 FY99	2,584,998	4,325,000
13 FY00	1,696,606	4,325,000
14 FY01	12,653,781	4,325,000
15 FY02	3,211,390	4,323,292
16 FY03	6,602,056	4,323,292
17 FY04	8,537,318	4,323,292
18 CY05*	7,108,777	7,042,000

19
20 * MGE's fiscal year end changed from June 30 to December 31 in 2005.
21
22

23 The foregoing shows that actual bad debt expense varies dramatically from year to
24 year, so much so that it is difficult—if not impossible—to identify a “normal” level of
25 bad debt expense. On average—over that ten-year period—MGE's actual bad debt
26 expense exceeded its bad debt allowance in rates by more than \$1.6 million per year.
27 This has also directly contributed to MGE's inability to achieve its authorized rate of
28 return.
29

1 **4. THE MAJOR REASONS FOR MGE'S RATE CASE FILING**

2 **Q. WHY HAS THE COMPANY DECIDED TO FILE A GENERAL RATE CASE**
3 **AT THIS TIME?**

4 **A. The Company has made the difficult, but necessary, decision to file a general rate case**
5 **at this time for the following principal reasons:**

- 6 1. MGE's continued inability to achieve the Commission-authorized
7 return on investment;
- 8 2. MGE's continued need to obtain an authorized return level sufficient
9 to compensate the Company's shareholders for the investment risks
10 they bear while enabling MGE to attract capital on reasonable terms in
11 the competitive financial marketplace (MGE's current authorized
12 return, which is based on a 10.5% return on equity ("ROE") and a
13 capital structure comprised of 29.99% common equity, fails this test.
14 This is because 10.5% ROE is below the norm and a common equity
15 ratio of 29.99% is so far lower than the industry norm, as can be seen
16 by examining Schedule FJH-17 of MGE witness Hanley's direct
17 testimony, that that the combination of the two results in an overall
18 rate of return that is lower than any other authorized return we are
19 aware of in the country.);
- 20 3. MGE's continued need for a ratemaking solution to remedy material
21 and chronic volumetric revenue shortfalls associated with declining
22 customer usage and actual weather being warmer than the "normal"
23 weather assumed through the rate setting process.

1 Although other factors, such as higher than expected bad debt levels, justification for
2 higher authorized depreciation rates, and the need to have a ratemaking mechanism
3 that addresses unpredictable but potentially significant environmental remediation
4 expenditures, have contributed to MGE's insufficient earnings situation, the foregoing
5 represent the driving factors of this rate case filing.

6
7 **Q. PLEASE INTRODUCE THE OTHER WITNESSES PRESENTING DIRECT**
8 **TESTIMONY ON MGE'S BEHALF IN THIS RATE CASE FILING.**

9 A. The other witnesses providing direct testimony, and the subject matter of that
10 testimony, are as follows:

- 11 • Michael Adams – cash working capital, lead/lag study;
- 12 • Ronald J. Amen – class cost-of-service;
- 13 • Russell A Feingold – measure of “normal” weather; revenue adjustments;
- 14 rate design and ratemaking proposals;
- 15 • Frank Hanley – cost of capital;
- 16 • Michael R. Noack – other revenue requirement items, including
- 17 • Carlton A. Ricketts – customer service; and
- 18 • Thomas J. Sullivan – depreciation expense and capital recovery schedule.

19
20 **Q. DO YOU HAVE ANY RECOMMENDATIONS FOR THE COMMISSION?**

21 A. Yes. The Commission should re-examine the way in which it sets rates for MGE.
22 Simply taking a “business as usual” approach will not work because an examination
23 of past results establishes that MGE has not been afforded a reasonable opportunity to

1 achieve its authorized return. In particular, the Commission needs to substantially
2 moderate or eliminate the revenue shortfalls MGE experiences related to weather and
3 declining customer usage by reducing the proportion of MGE's revenue stream that
4 varies on the basis of customer usage. The Company's various ratemaking proposals
5 presented and explained by Mr. Feingold directly address this chronic deficiency. In
6 addition, the Commission should also take a close look at the usage per customer
7 (e.g., billing determinants) and bad debt levels proposed for MGE's rates to ensure
8 that such usage and bad debt levels actually have some reasonable likelihood of being
9 achieved. If a meaningful solution to these issues is not implemented as a result of
10 this rate case, then the unfortunate fact is that the Company's only will be to file
11 another general rate proceeding close on the heels of this one. I do not believe such a
12 result to be in the best interest of any of MGE's primary stakeholder groups
13 (customers, employees or shareholders).

14
15 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

16 **A.** Yes, at this time.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy's
Tariff Sheets Designed to Increase Rates
for Gas Service in the Company's Missouri
Service Area.

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)
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Case No. GR-2006-____

AFFIDAVIT OF ROBERT J. HACK

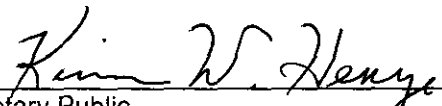
STATE OF MISSOURI)
)
COUNTY OF JACKSON) ss.

Robert J. Hack, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Direct Testimony in question and answer form, to be presented in the above case; that the answers in the foregoing Direct Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.



ROBERT J. HACK

Subscribed and sworn to before me this 1st day of MAY 2006.



Notary Public

My Commission Expires: Feb. 3, 2007

Kim W. Henzi
Notary Public - Notary Seal
State of Missouri
Jackson County
My Commission Expires Feb. 3, 2007