

Exhibit No.:
Issue(s):
Witness:
Type of Exhibit:
Sponsoring Party:
Case Number:

Accounting Authority Order
Kimberly K. Bolin
Surrebuttal Testimony
Public Counsel
GU-2005-0095

SURREBUTTAL TESTIMONY
OF
KIMBERLY K. BOLIN

Submitted on Behalf of
The Office of the Public Counsel

MISSOURI GAS ENERGY
CASE NO. GU-2005-0095

February 15, 2005

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the matter of Missouri Gas Energy, a)
division of Southern Union Company, for
an accounting authority order concerning)
the Kansas property tax for gas in storage.)

Case No. GU-2005-0095

AFFIDAVIT OF KIMBERLY K. BOLIN

STATE OF MISSOURI)

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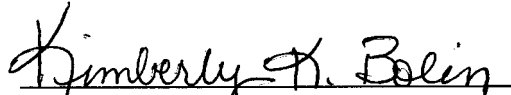
COUNTY OF COLE)

Kimberly K. Bolin, of lawful age and being first duly sworn, deposes and states:

1. My name is Kimberly K. Bolin. I am a Public Utility Accountant for the Office of the Public Counsel.

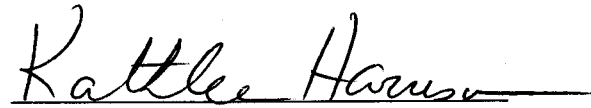
2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony consisting of pages 1 through 5.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.


Kimberly K. Bolin
Public Utility Accountant I

Subscribed and sworn to me this 15th day of February 2005.

KATHLEEN HARRISON
Notary Public - State of Missouri
County of Cole
My Commission Expires Jan. 31, 2006


Kathleen Harrison
Notary Public

My commission expires January 31, 2006.

SURREBUTTAL TESTIMONY

OF

KIMBERLY K. BOLIN

MISSOURI GAS ENERGY

CASE NO. GU-2005-0095

Q. PLEASE STATE YOUR NAME AND ADDRESS.

A. Kimberly K. Bolin, P.O. Box 2230, Jefferson City, Missouri 65102.

Q. ARE YOU THE SAME KIMBERLY K. BOLIN WHO FILED REBUTTAL TESTIMONY IN THIS CASE?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. The purpose of my surrebuttal testimony is to respond to Missouri Gas Energy (MGE or Company) witness Michael Noack's recommendation in his rebuttal testimony.

Q. DO YOU AGREE WITH THE PROPOSED LANGUAGE THAT MGE IS RECOMMENDING ON PAGE 4 OF WITNESS NOACK'S TESTIMONY?

A. No, as I stated in my rebuttal testimony, Public Counsel believes the amortization of the Accounting Authority Order (AAO) should begin effective with the final resolution of the tax. MGE's proposal would have the amortization begin June 1, 2008, if the Company does not file a general rate case by May 31, 2008.

Q. IF THE AMORTIZATION PERIOD BEGINS WHEN THE FINAL RESOLUTION OF THE TAX IS DETERMINED AND TARIFF RATES ARE NOT ADJUSTED TO REFLECT THE AMORTIZATION, WHAT IS THE EFFECT ON RATEPAYERS AND STOCKHOLDERS?

1 A. Ratepayers are entitled to pay just and reasonable rates for utility services and stockholders are
2 entitled to the opportunity to earn a reasonable return on their investment in the provision of utility
3 services. Whether these entitlements are in balance can only be determined through a determination
4 of the overall revenue requirement (overall cost-of- service). The effect of imbalances (to either the
5 ratepayers of stockholders) is commonly referred to as regulatory lag.

6 **Q. PLEASE EXPLAIN THE CONCEPT OF REGULATORY LAG.**

7 A. This concept is based on the difference in timing of a decision by management and the
8 Commission's recognition of that decision and its effect on the rate base/rate of return relationship
9 in determination of a company's revenue requirement. Prudent management decisions that reduce
10 the cost of service without changing revenues result in a change in the rate base/rate or return
11 relationship. This change increases the profitability of the firm in the short-run, and until such time
12 when the Commission reestablishes rates that properly match the new level of service cost.
13 Companies are allowed to retain cost savings, i.e., excess profits during the lag period between rate
14 cases. When faced with escalating costs (expenses or investments) which will change the rate
15 base/rate of return relationship adversely with respect to profits, regulatory lag places pressure on
16 management to minimize the change in the relationship, by filing an application for a rate increase.

17 **Q. HAS THIS COMMISSION RULED THAT IT IS NOT REASONABLE TO**
18 **PROTECT SHAREHOLDERS FROM ALL REGULATORY LAG?**

19 A. Yes. In Missouri Public Service Company, Cases Nos. EO-91-348 and EO-91-360, the
20 Commission stated:

21 Lessening the effect of regulatory lag by deferring costs is beneficial to a
22 company but not particularly beneficial to ratepayers. Companies do not
23 propose to defer profits to subsequent rate cases to lessen the effects of

regulatory lag, but insists it is a benefit to defer costs. Regulatory lag is a part of the regulatory process and can be a benefit as well as a detriment. Lessening regulatory lag by deferring costs is not a reasonable goal unless the costs are associated with an extraordinary event.

Maintaining the financial integrity of a utility is also a reasonable goal. The deferral of costs to maintain current financial integrity though is of questionable benefit. If a utility's financial integrity is threatened by high costs so that its ability to provide service is threatened, then it should seek interim rate relief. If maintaining financial integrity means sustaining a specific return on equity, this is not the purpose of regulation. It is not reasonable to defer costs to insulate shareholders from any risks.

Q. ON PAGE 4 OF WITNESS NOACK'S REBUTTAL TESTIMONY HE EFFECTIVELY STATES THAT THE PURPOSE OF COMPANY'S REQUEST IS, "TO PROTECT ITSELF FROM SIGNIFICANT UNRECOVERED COSTS..." WILL THE PROPERTY TAX ON GAS STORED IN KANSAS BE UNRECOVERED AS WITNESS NOACK ASSERTS?

A. No. Under rate of return regulation the Company is given an opportunity to earn a fair and reasonable return, the Company is not guaranteed any specific level after consideration of all revenues and costs. If consideration of all revenues and costs result in a positive rate or return, all costs are being paid for by current revenues. The only question remaining is whether or not the resulting earnings are determined to be adequate. Thus if the Company incurs an expense and still earns a positive return on equity, that expense is not unrecovered as witness Noack asserts.

Rate of return regulation looks at all relevant factors associated with the provision of service. The valuation of these factors is quantified on the income statement and balance sheets. Rate of return regulation has the Commission, like investors in non-utility industries, review the overall result of the operations, i.e. the return on equity. Rate of return regulation does not track individual costs or revenue flows and adjust rates according to specific changes in these amounts. The practical effect

1 of this request for an AAO is to set up a tracking mechanism for a normal on-going expense, and
2 thus effectively guarantee a portion of earnings because absent the AAO, earnings would be lower
3 all things else being equal.

4 **Q. ARE ALL THINGS ELSE EQUAL IN THE UTILITY OPERATIONS?**

5 A. No. Utilities are dynamic industries and changes are always occurring. Numerous factors put
6 pressure on earnings to rise such as increases in the depreciation reserve, increasing number of
7 customers, or increasing deferred taxes. Conversely other factors put downward pressure on
8 earnings. To isolate a possible change in one normal on-going expense and the resulting impact on
9 earnings is not appropriate. This tracking mechanism results in single-issue ratemaking.

10 **Q. HAS THE COMPANY STATED IT WILL NOT EARN A RETURN IF THE**
11 **COMPANY HAS TO PAY THE PROPERTY TAX ON GAS STORED IN KANSAS?**

12 A. No.

13 **Q. DOES PUBLIC COUNSEL BELIEVE THE COMPANY TIME LIMITATION OF**
14 **MAY 31, 2008 AS REASONABLE?**

15 A. No. If the Company is able to wait until May 31, 2008 to seek recovery of these deferrals that
16 should demonstrate that the magnitude of the deferrals is not extraordinary nor is the recovery of
17 the deferral necessary to earn a reasonable return on its investment.

18 **Q. UNDER THE COMPANY'S PROPOSAL HOW MANY YEARS OF PROPERTY TAXES**
19 **ON THE GAS STORED COULD BE ACCUMULATED IN THE AAO?**

20 A. Under the Company's proposal, the Company could accumulate up to five years worth of property
21 taxes on gas stored. Property taxes are a normal, recurring expense that fluctuates from year to year

1 and are included in the Company's cost of service. The Company's proposal will allow the
2 recovery of more than one year of property tax expense to be included in the Company's future
3 rates.

4 **Q. HAS THE COMMISSION DETERMINED THAT A TIME LIMITATION FOR**
5 **SEEKING RATE RECOVERY OF A DEFERRAL GRANTED BY AN ACCOUNTING**
6 **AUTHORITY ORDER IS APPROPRIATE?**

7 A Yes, it has. In Missouri Public Service Company, Case No. EO-91-358 and EO-91-360, the
8 Commission stated:

9 The Commission finds that a time limitation on deferrals is reasonable
10 since deferrals cannot be allowed to continue indefinitely. The
11 Commission finds that a rate case must be filed within a reasonable time
12 after the deferral period for recovery of the deferral to be considered. For
13 purposes of this case the Commission finds that twelve months is a
14 reasonable period. This limitation accomplishes two goals. First, it
15 prevents the continued accumulation of deferred costs so that total
16 disallowance would not affect the financial integrity of the company of the
17 Commission's ability to make the disallowance; and secondly, it ensures
18 the Commission a review of those costs within a reasonable time. If the
19 costs are truly extraordinary, recovery in rates should not be delayed
20 indefinitely. A utility should not be allowed to save deferrals to offset
21 against excess earnings in some future period.

22 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

23 A. Yes.