Exhibit No.:	
Issues:	*Revenues, Purchased Gas Adjustments, Uncollectible Accounts, Medical Expenses, Rents, Income Taxes*
Witness:	*Paul R. Harrison*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Direct Testimony*
Case No.:	*GR-2004-0209*
Date Testimony Prepared:	*April 15, 2004*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

PAUL R. HARRISON

MISSOURI GAS ENERGY

CASE NO. GR-2004-0209

Jefferson City, Missouri
April 2004

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri Gas Energy's Tariffs to Implement a General Rate Increase for Natural Gas Service	)))	Case No. GR-2004-0209

AFFIDAVIT OF PAUL R. HARRISON

STATE OF MISSOURI	)	
	)	ss.
COUNTY OF COLE	)	

Paul R. Harrison, being of lawful age, on his oath states: that he has participated in the preparation of the following direct testimony in question and answer form, consisting of 21 pages to be presented in the above case; that the answers in the following direct testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Paul R. Harrison

Paul R. Harrison

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

D SUZIE MANKIN
Notary Public - Notary Seal
STATE OF MISSOURI
COLE COUNTY
MY COMMISSION EXP. JUNE 21,2004

D Suzie Mankin

TABLE OF CONTENTS

DIRECT TESTIMONY OF

PAUL R. HARRISON

MISSOURI GAS ENERGY

CASE NO. GR-2004-0209

DIRECT TESTIMONY

OF

PAUL R. HARRISON

MISSOURI GAS ENERGY

CASE NO. GR-2004-0209

Q. Please state your name and business address.

A. Paul R. Harrison, P. O. Box 360, Jefferson City, Missouri 65102.

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

A. I am a Regulatory Auditor for the Missouri Public Service Commission (PSC or Commission).

BACKGROUND OF WITNESS

Q. Please describe your educational background.

A. I graduated from Park College, Kansas City, Missouri, where I earned a Bachelor of Science degree in Accounting and Management in July of 1995. I also earned an Associate degree in Missile Maintenance Technology from the Community College of the Air Force in June 1990. In addition, I graduated from the Non-Commission Officer (NCO) Leadership School in July 1977, the NCO Academy in March 1983 and the Senior NCO Academy in February 1992. These professional military education schools trained and prepared Non-Commissioned Officers for increased levels of responsibility as Supervisors and Managers in the United State Air Force (USAF).

Q. Please describe your work background prior to working at the Commission.

A. Prior to coming to work at the Commission, I was the manager for Tool Warehouse Inc. for four and one-half years. As the manager, I supervised eight sales representatives and managed merchandise and inventory in excess of $1.5 million.

Prior to that, I was in the USAF for 23 years. During my career in the USAF, I was assigned to many different duty positions with varying levels of responsibility. I retired from active duty on May 1, 1994 as Superintendent of the 321st Strategic Missile Wing (SMW) Missile Mechanical Flight. In that capacity, I supervised 95 missile maintenance technicians and managed assets valued in excess of $50 million.

Q. Please describe your duties while employed by the PSC.

A. My duties at the Commission include performing audits of the books and records of regulated public utilities under the jurisdiction of the PSC, in conjunction with other Commission Staff (Staff) members. Acting in that capacity, I am also required to prepare testimony and serve as a Staff expert witness on cases involving the accounting issues that I am assigned.

Q. Have you previously filed testimony before this Commission?

A. Yes. Schedule 1 lists the cases in which I filed testimony, the issues that I have worked and the small informal cases that I have completed.

PURPOSE OF TESTIMONY

Q. Did you make an examination and analysis of the books and records of Missouri Gas Energy (MGE or Company) in regard to matters raised in this case?

A. Yes, in conjunction with other members of the Staff. I specifically examined information provided by the Company in response to Staff data requests, portions of the Company's general ledger, Financial and Statistical Reports, as well as workpapers supplied by MGE to support its case filing. I also examined Company Annual Reports and other information contained on the Company's Website.

Q. What is your primary responsibility in Case No. GR-2004-0209?

A. My primary areas of responsibility are revenues, uncollectible expense, medical expense and income taxes.

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

A. I have performed duties as a Regulatory Auditor within the Auditing Department at the Commission since January 18, 2000. In addition to acquiring general knowledge of these topics through my education, I've acquired experience in prior rate cases before the Commission as well as through formal and informal training.

Q. Please describe the formal training for your position that you have received.

A. I attended the National Association Regulatory Utilities Commissioner's (NARUC) Water Rate School in San Diego, California in May of 2000. I also attended NARUC's "On The Missouri" 2003 seminar conducted in Jefferson City, Missouri in January 2003.

Q. Please describe the informal training for your position that you have received.

A. I have successfully completed each of my assigned issues, as listed in Schedule 1, and have had the opportunity to interact with other auditors concerning these and other issues that involved the Auditing Department of the Commission.

I have attended in-house training classes, reviewed Auditing Department position papers, training manuals and technical manuals pertaining to the accounting issues in this and other cases.

I have reviewed the Commission's Report And Orders, testimony and transcripts of cases filed by this and other utilities within the jurisdiction of this Commission.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to sponsor and discuss the following Income Statement adjustments, which appear on Accounting Schedule 10, Adjustments to Income Statement and Income Tax adjustments, which are supported on Accounting Schedule 11, Income Tax:

Residential Sales:	S-1.1
Commercial and Industrial Sales:	S-2.1 and S-2.2
Gross Receipts	S-1.2, S-2.3 S-2.9 and S-2.14
Unbilled Revenues:	S-1.3
PGA Revenues:	S-1.5, S-2.5 and S-2.11
ACA Costs	S-1.6, S-2.6 and S-2.12
TOP Costs	S-1.8 and S-2.8
Uncollectible expenses:	S-36.1.
Medical Expense	S-52.4
Rents	S-55.1
Income Taxes	S- 65.1
Gross Receipts Expense	S-62.1
Kansas City earnings tax	S-68.1
Contract Demand	S-2.14 and S-2.16
Overrun/Curtailment	S-2.15 and S-2.18
Rate Code 48 Gas Costs	S-2.19

REVENUES

Q. Please give a general description of MGE's service territory in the state of Missouri.

A. MGE's service territory covers much of the western side of Missouri. The Company's customers are segregated into three different regions. Joplin (including Monett), St. Joseph, and Kansas City (including Kansas City North, Independence, Lee's Summit, and Warrensburg territories).

Each region serves four classes of customers: residential, general service (small and large), large volume and transportation customers. This testimony will address the annualization for residential and small and large general service (commercial and industrial) customer class revenues.

Q. What type of customers are in the Small General Service (SGS) and Large General Service (LGS) rate classifications?

A. Each rate class has both commercial and industrial customers. The distinction between SGS and LGS is in the volumes used by the customer, not how the gas is used.

Q. Does MGE's current tariffs specify commercial and industrial customer classes?

A. No. Unless a commercial or industrial customer qualifies for the Large Volume Service rate schedule, MGE's current tariff requires these customers to be classified as either SGS or LGS. The Staff's revenue adjustments in this case were calculated consistent with the SGS and LGS rate schedules. However, for purposes of recording these adjustments to the Income Statement within the Staff's Exhibit Manipulation System, commercial and industrial customers are combined with the SGS and LGS rate schedules consistent with MGE's accounting system.

Q. What is the basis for pricing the revenue adjustments?

A. All revenue adjustments in the Staff's cost of service were priced on the margin (the total rate excluding Purchased Gas Adjustment (PGA) gas cost rate) included in the Company's tariffs.

Q. Please provide a general discussion of the Staff's annualization of revenues, including the Staff witnesses who performed the various revenue analyses.

A. The Company's test year revenues, like its expenses, must be annualized and normalized in order to develop a cost of service that is representative of the Company's ongoing operations. In the area of revenues, the following Staff members have performed certain analyses or annualizations:

Staff Member	Area of Analysis or Adjustment
Dennis L. Patterson	Thirty-year weather normalization
James A. Gray	Normalized usage per customer through regression analysis
Kim J. Elvington	Allocation of SGS normal volumes to rate blocks through regression analysis
Anne E. Ross	Transportation, large volume service customer annualizations
Tomas M. Imhoff	Miscellaneous revenues and flex rate
Paul R. Harrison	Residential, SGS and LGS customer growth annualizations and revenue adjustments to support Staff witness Gray

The majority of the Company's revenues are affected by weather. Staff witness Patterson of the Energy Economic Analysis Department has developed normalized weather based on a 30-year analysis. Mr. Patterson's normalized weather calculations were then given to Staff witness Gray of the Energy Tariff/Rate Design Department. Mr. Gray used Mr. Patterson's 30-year normalized weather calculations to develop normal gas usage per hundred cubic feet (Ccf) by customer class and also by month for the Staff's test year.

Q. Please describe and discuss the types of adjustments the Staff developed to determine annualized revenues.

A. In general, the Staff's annualized revenues reflect the effects of the following conditions:

1. Normalized weather
2. Customers switching customer classes (rate switching)
3. Customer load changes
4. Customer growth or loss

Staffs witness Ross of the Energy Economic Analysis Department analyzed the transportation and large volume service customer classes by individual customer. Through her analysis, Ms. Ross can determine if customers have switched rate classes, come onto the system as a new customer or reduced demand on the system by a significant amount. If any of the three circumstances occurred during the test year, Ms. Ross developed an adjustment in Ccf's from the Company's records.

I am sponsoring the application of the adjustments that were developed by Mr. Gray. Mr. Gray will sponsor the methodology supporting the adjustments and I will sponsor the development of the revenue adjustments and their relationship to the Staff's cost of service calculation. Please refer to Mr. Gray's testimony for a more detailed discussion of these areas.

I have also developed the revenue adjustments to reflect customer growth. The Company's and the Staff's test year was the twelve months ending June 30, 2003. The

Staff used the customer numbers as of June 30, 2003 to annualize revenues for residential, SGS and LGS rate class. I have calculated the customer growth adjustments to reflect the increases in customers through June 30, 2003. These adjustments were again based on normal gas usage per customer as developed by Mr. Gray. A more complete discussion of the Staff's customer growth adjustments is included later in this direct testimony.

Q. Why is it appropriate to adjust revenues for normalized weather?

A. Because a principal use of natural gas is for space heating, temperature levels experienced during any 12-month period could have a significant impact on the Company's revenues. If the overall temperature were very cold during the period, the Company's revenue would be overstated in relation to normal weather. Conversely, if the overall temperature were very warm during the period, the Company's revenues would be understated in relation to normal weather. Therefore, the Staff normalized revenues for weather to eliminate the effects of above and/or below-normal temperature during the test year.

Q. What methodology did the Staff use to normalize weather?

A. Mr. Gray of the Gas Department performed the weather normalization computations. Because the Company's service territory covers much of the western side of Missouri, the Company's customers were segregated into two weather regions (Kansas City and Springfield).

Q. Please describe the Staff's adjustments relating to weather normalization.

A. Staff witness Gray developed the monthly weather normalized Ccf sales per customer for the customer classes during the Staff's test year. Generally, these classes consisted of the residential, small and large general service-heating customers. The weather normalized Ccf sales per customer were developed for each of the three regions for each customer class. In addition, Staff witness Elvington used the same time period to develop the breakdown of usage between the various rate blocks for the general service customer class.

Mr. Gray adjusted the actual monthly therm sales from the test year to reflect normalized weather. The totals were then priced on the margin to develop the Staff's weather normalized adjustments.

Q. Please explain what adjustments were made to the test year ending June 30, 2003 per book revenues.

A. The Staff made several adjustments to the starting point of Company's per book revenues. Adjustments S-1.2, S-2.3, S-2.9 and S-2.14 removes the test year gross receipt taxes from the operating revenues. Gross receipt taxes are not operating revenues for the Company. The Company acts merely as a collecting agent and remits the taxes to the appropriate taxing entities. The Staff also made adjustment S-62.1 to remove gross receipt taxes from the Taxes Other Than Income Taxes line item of the expense portion of the income statement. Gross receipt taxes are reported as both a revenue and expense item on the Company's books. Therefore, both revenue and expense adjustments are necessary to eliminate this item.

Staff adjustment S-1.3 eliminates unbilled revenues from the test year. The unbilled revenue adjustment is made to reflect the Company's revenues on a billed basis for the test year. In the Staff's test year, there are gas sales to customers relating to either usage periods outside the test year, or gas usage that has not yet been recognized on the bills; this can occur at both the beginning and end of the test year. To recognize this usage, utilities generally book an unbilled adjustment to revenues. The purpose of the adjustment is to reflect an estimate of what the actual revenues are for that month. For purposes of a rate case, the adjustment for unbilled revenues must be eliminated from the Company's books, in order to reflect revenues during the test year on a billed basis.

Q. Please explain adjustments S-1.1, S-2.1 and S-2.2 and how the Staff annualized gas-operating revenues for the residential, SGS and LGS class customers.

A. Adjustment S-1.1 applies to the annualization of residential customer revenues, which contains two components, the base charge and the commodity charge. The base charge is the minimum monthly charge that MGE assesses to a customer for supplying the gas service. The monthly base charge revenue is calculated by multiplying the base charge by the Staff's monthly level of customers. The Staff's annualized base charge revenue is the sum of the twelve monthly base charge revenues. The commodity charge is the rate MGE charges a customer for each Ccf of gas usage. Residential and LGS customers have only one commodity charge rate block, while SGS customers have two commodity charge rate blocks. For SGS customers, block one represents usage of 0 through 600 Ccf and block two represents usage over 600 Ccf by month. Please refer to the testimony of Staff witness Elvington for a discussion of this area and the assignment of Ccf usage between blocks.

To annualize the residential commodity charge revenues, the monthly level of annualized customers were multiplied by the Staff's normal usage per customer, based on normal weather, to derive monthly usages. Please refer to Staff witness Gray's direct testimony for the development of normal usage per customer based on normal weather. The residential normal monthly usages were then multiplied by the commodity charge to determine the monthly commodity charge revenues. For SGS customers, the Staff allocated the normal monthly usages to each of the Company's rate blocks and then multiplied the blocked usage by the appropriate block commodity charge. The sum of each rate block for each of the twelve months was the Staff's annualized commodity revenue. The total annualized revenue for the SGS and LGS rate class was calculated by adding the annualized base charge revenues to the annualized commodity charge revenue adjustments S-2.1 and S-2.2.

Q. Why is it necessary to distribute the customers through a 12-month period?

A. As can be seen from Schedules 2 through 4 of my direct testimony, customer levels fluctuate during any calendar year. Generally, customer levels are higher in the winter months and decrease during the summer months. Likewise, normal usage per customer is greater in the winter months than in the summer months. Distributing customers through the 12-month period enables the Staff to more accurately annualize revenues to reflect seasonal impact on usage.

Q. Did the Staff use this methodology for growth annualization in all three regions of the Company?

A. Yes, the Staff used the same methodology. Overall, the Company has been experiencing steady growth in customers up through the test year, except for the St. Joseph district. The number of customers at any given point in time, except for the ending months of 2001 and 2003, has been higher than the same period in the preceding year since 1997. Schedule 2, Schedule 3 and Schedule 4 attached shows MGE's total residential, small and large general service customer growth trend since July of 1997. However, the Staff would note that the loss in customer numbers in July 2003 was more than twice the loss in any other month from 1997 to 2003. These schedules show that all three of the rate classes lost a total of 7,748 customers during the last six months of the calendar year 2003.

Q. Could MGE explain the declining customer numbers?

A. No. There are a number of possible reasons for the apparent loss of customers from MGE's system, including faulty data. Since the Company has not been able to explain and verify the loss, the Staff is using the test year customer numbers to annualize the revenue for all three classes of customers. Without further information from the Company on its apparent losses, the Staff has chosen not to reflect the change in customer numbers for the test year update period in this case.

The Staff recommends that the Company perform a geographical study by area of its rate classes to determine the accuracy of its customer counts and to also identify what is causing the loss of customers.

In response to Staff Data Request No. 60.1, concerning MGE's customer losses from July 2003 on, the Company responded by stating:

> "it is correct that for each of the months of July 2003 through December 2003, the number of residential regular bills in Kansas City is lower than the corresponding month in the prior year. The Company would note that a similar result occurred in the six months of June through November 2001 as compared to the corresponding months in 2000. The Company would also note that for the first half of the period considered (1997 through 2000) each of the 36 month-to-corresponding-month comparisons showed increasing customer counts, while one-third of such comparisons in the second half of the period (2000 through 2003) showed declining customer counts. In recent years, the growth in Kansas City residential customers has certainly reversed the pattern that was observed several years ago. The Company notes that the bill data for both the original test year ended June 30, 2003 and the updated test year ended December 31, 2003 was obtained from CSS downloads of information used to generate customer bills".

The Staff believes that the Company should have already performed some type of study or analysis to verify the customer loss, and determine the reason or reasons it is occurring.

Q. Does the Staff have any plans to monitor the number of customers after December 31, 2003?

A. Yes. It is the Staff's intention to continue to monitor the number of customers billed after the update period (December 31, 2003) to verify the accuracy of Staff's calculation. The Staff has reviewed the number of customers billed in January and February of 2004 and they still show losses (in comparison to same months in 2003).

Q. What is the Staff's plan if additional information is received from MGE concerning the reasons for its recent decline in customer numbers?

A. If appropriate, the Staff will revisit the calculation.

Q. Please explain how the Staff annualized SGS and LGS revenues.

A. Small and large general service customers have two commodity charges covering different periods (November through March and April through October) of the year. In addition, small general service customers have two usage rate blocks as discussed earlier in my testimony.

To annualize the commodity charge revenues, the monthly level of customers by customer class was multiplied by the Staff's normal usage per customer, based on normal weather. The large general service normal monthly usages were then multiplied by the seasonal commodity charge to determine the monthly commodity charge revenues. For small general service customers, the Staff allocated normal monthly usages to the Company's rate blocks.

Q. Please describe the phenomenon of customers switching customer classes or rate switching.

A. Customers switching customer classes, or rate switching, can occur for several reasons. The nature of a customer's operations may have changed and another customer class is now more appropriate. The customer may find it to be economical to switch to another customer class. Finally, the customer may decide to procure its own gas, which would also make a rate switch necessary. Please refer to Staff witness Ross for further discussion of this area.

PURCHASED GAS ADJUSTMENTS

Q. Please explain what adjustments were made to test year ending December 31, 2003 per book revenues for purchased gas.

A. Adjustments S-1.5, S-2.5 and S-2.11 are line item adjustments to adjust revenues to reflect MGE's test year per book expense for gas purchases. Gas purchase expenses are estimated and assessed to ratepayers through MGE's PGA Clause. The PGA Clause provides MGE an estimating methodology for recovering purchased gas expense, which is subsequently trued-up through the Actual Cost Adjustment (ACA) mechanism. Therefore, purchased gas expense and revenues generally are netted to equal zero for purposes of rate cases. Adjustments S-1.5 and S-2.5 and S-2.11 eliminate PGA revenues for the test year from the appropriate revenue accounts, and adjustment S-10.1. eliminates the purchased gas expense portion from the books.

Q. Please explain adjustments S-1.8 and S-2.8.

A. Adjustments S-1.8 and S-2.8 remove the take-or-pay portion of the PGA revenues.

Q. Please explain adjustments S-1.6, S-2.6 and S-2.12.

A. Adjustments S-1.6, S-2.6 and S-2.12 adjust the PGA revenue for the ACA true-up mechanism.

Q. Please explain adjustment S-2.14 and S-2.16.

A. Adjustments S-2-14 and S-2.16 are line item adjustments to adjust revenues to reflect MGE's test year per book expense by removing the contract demand costs.

Q. Please explain adjustment S-2.15 and S-2.18.

A. Adjustments S-2.15 and S-2.18 are line item adjustments to adjust revenues to reflect MGE's test year per book expense by removing the overrun/curtailment costs.

Q. Please explain adjustments S-2.19.

A. Adjustment S-2.19 adds the Succession Rate Code 48 gas costs to commercial small general service gas sales.

UNCOLLECTIBLE ACCOUNTS

Q. Please explain adjustment S-36.1.

A. Adjustment S-36.1 adjusts the test year per book balance in the uncollectible account to the actual bad debt write-offs average for the last five years ending December 31, 2003.

Q. Why does the Staff propose a five-year normalization adjustment in this case?

A. MGE's level of bad debt write-offs over the last five years has been volatile. By using a five-year average normalization method, abnormal levels of bad debt write-offs are appropriately levelized for rate purposes.

MEDICAL EXPENSES

Q. Please describe adjustments S-52.4.

A. Adjustments S-52.4 adjust the test year medical costs of MGE based upon the actual medical claims paid for the twelve months ended December 31, 2003, the end of the test year update period of this case. The analysis of these expenses included total employee contributions and total claims paid in each account for the calendar years 1999 through 2003. Medical costs through the test year update period were used since the actual paid claims show a continuous increase over the last several years.

RENTS

Q. Please describe adjustment S-55.1

A. Adjustment S-55.1 offsets the MGE Broadway parking lot lease expense for rent received from Broadway Ford.

INCOME TAXES

Q. Please explain adjustments S-65.1.

A. Adjustment S-65.1 adjusts current income tax expense from the level included in the Company's books and records to the annualized amount calculated on Accounting Schedule 11, Income Tax.

Q. Please describe Accounting Schedule 11, Income Tax.

A. Accounting Schedule 11 reflects the Staff's calculation of current and deferred income taxes based on the Company's adjusted operating results for its gas operations.

Q. Is the Staff including an amount for deferred income tax expense in its case?

A. No.

Q. Please describe how the current income tax component of the total income tax expense is calculated on Accounting Schedule 11, Income Tax.

A. The Current Income Tax component (Line 28) is calculated by taking the Net Operating Income Before Taxes (NOIBT) amount from Accounting Schedule 9, Income Statement, and adjusting for additions to and deductions from NOIBT that appear on Accounting Schedule 11, lines 2 through 7. This amount (Net Taxable Income) is then multiplied by the appropriate federal and state income tax rates, giving consideration to the fact that federal income taxes are deductible for state income tax purposes, and state income taxes are deductible for federal income tax purposes.

Q. Please explain why Interest Expense, line 5 of Accounting Schedule 11, is subtracted from NOIBT to arrive at Net Taxable Income and how it was calculated.

A. Interest expense is recorded below-the-line on MGE's income statement and is not reflected in the Staff's calculation of Net Operating Income on Accounting Schedule 9. When an item is booked below-the-line, it is not included in the calculation of net operating income. An item booked below-the-line is generally included in "other operating revenues and expenses." Since the Staff's revenue requirement is based on the amount of net operating income, an item booked below-the-line will have no impact on the revenue requirement. If a cost is booked below-the-line and is not recovered elsewhere, it will be borne by the shareholders and not the ratepayers.

For ratemaking purposes, the Company recovers interest expense through the weighted cost of debt portion of the overall rate of return on rate base. However, interest expense is a deduction for tax purposes and must be reflected in the calculation of income tax expense. The tax deduction for interest expense was calculated by multiplying the Rate Base amount on Accounting Schedule 2 by the Staff's calculated weighted cost of debt, which is sponsored by Staff witness David Murray of the Financial Analysis Department. This method is known as “interest synchronization” because the interest expense used in the calculation of income tax expense is matched (synchronized) with the interest expense the ratepayers are required to provide the Company in rates (rate base multiplied by the weighted cost of debt). Interest synchronization has been consistently used by the Staff and adopted by the Commission in numerous past orders.

Q. Are you sponsoring any items in the Staff’s Rate Base, as depicted within Accounting Schedule 2?

A. Yes. I am sponsoring the line items Deferred Income Taxes-Direct Plant; Deferred Income Taxes-Allocated Plant; Deferred Income Taxes, GO-94-234; Deferred Income Taxes, GO-97-301; Deferred Income Taxes SLRP, GR-98-140; Deferred Income Taxes GR-2001-292; and Deferred Income Taxes, Year 2000 AAO.

The first two items represent the portion of MGE's December 31, 2003 balance of the accumulated deferred income tax reserve related to prior depreciation tax timing differences that is appropriate to include for ratemaking purposes in this proceeding. The last five-rate base items relate to deferred taxes associated with past Accounting Authority Order deferrals authorized by the PSC. Three of these items relate to Service Line Replacement Program deferrals, with the last deferral item relating to Year 2000 (Y2K) costs.

Q. Please explain why accumulated deferred income taxes are an offset to rate base.

A. MGE's deferred tax reserve represents, in effect, a prepayment of income taxes by MGE's customers. As an example, because MGE is allowed to deduct depreciation expense on an accelerated basis for income tax purposes, depreciation expense used for income taxes is considerably higher than depreciation expense used for ratemaking cost of service purposes. This results in what is referred to as book-tax timing difference and creates a deferral of income taxes to the future. The net credit balance in the deferred tax reserve represents a source of cost-free funds to MGE. Therefore, the rate base is reduced by the deferred tax reserve balance to avoid having customers pay a return on funds that are cost free to the Company. The most significant book-tax timing difference is caused by the differences between accelerated tax depreciation and book depreciation. Generally, deferred income taxes associated with all book-tax timing differences which are created through the ratemaking process should be reflected in rate base.

Q. Please explain why deferred taxes associated with the SLRP and Y2K programs are included within Accounting Schedule 2.

A. The SLRP deferred tax line I am sponsoring relates to the fact that the Company was previously and is currently allowed to currently deduct SLRP expenses for income tax purposes that are being deferred for financial reporting purposes. The Y2K deferred tax line I am sponsoring relates to the fact that MGE was previously allowed to currently deduct Y2K related costs for income tax purposes that were deferred for financial reporting purposes. Both of these situations gave rise to tax timing differences. Normalization of these tax-timing differences means the MGE's customers are required to pay the income taxes to taxing authorities. Recognizing a rate base deduction for SLRP and Y2K deferred taxes gives customers appropriate credit for providing funds to the utility to use for corporate purposes for a period of time before payment to taxing authority.

Q. Please explain adjustment S-68.1 and identify why the Staff is proposing the Kansas City earnings tax be calculated as an operating expense instead of reflecting it in the effective tax rate for Income Taxes.

A. Adjustment S-68.1 for The Kansas City earnings tax apportionment calculation is derived from Southern Union Company's annual gross receipts, instead of MGE's stand-alone earnings. (Southern Union is MGE's parent Company.) In response to Staff Data Request No. 16.1, the amount of the Kansas City earnings tax varied dependant upon the fluctuation of the gross receipts earned by Southern Union. The Staff believes this tax should be normalized by using a five-year average of payments to Kansas City.

Q. Please explain the rate base component Alternative Minimum Tax Credit (AMT Credit).

A. The AMT Credit is directly related to, and in fact, is an offset to deferred income taxes. As a result of certain Internal Revenue Service (IRS) regulations, over the past several years Southern Union has been what is referred to as an "AMT taxpayer." IRS regulations reduce or eliminate certain corporate tax benefits used to reduce taxable income if a company's regular income tax falls below a certain threshold. One of the major tax benefits reduced is accelerated tax depreciation. While the deferred tax reserve is set up to reflect the full income tax effect of book-tax depreciation timing differences, the tax effect of the amount of accelerated tax depreciation which is not allowed to be deducted on the current year's tax return is recorded as an AMT tax credit. The AMT credit is a reduction in accumulated deferred income taxes and has the effect of increasing MGE's rate base.

Q. Please explain why the Staff is proposing to eliminate the Alternative Minimum Tax (AMT) credit from the accumulated deferred income tax calculation?

A. The Staff is analyzing the way that MGE calculates its AMT portion of tax consolidated with Southern Union instead of as a stand-alone Company. The Staff submitted Data Request No. 277, on March 31, 2004, requesting that MGE provide the Staff with a calculation of what MGE's AMT credit would be calculated on a MGE stand alone basis (e.g. MGE depreciation, taxable income, etc.), with all supporting workpapers. The Staff believes that Missouri ratepayers should not be responsible for payment of AMT unless that tax liability is directly associated with the financial results of Southern Union's MGE division. Once the Staff receives a response to this data request, a determination will be made whether to include or exclude the AMT credit in rate base.

Q. Does this conclude your direct testimony?

A. Yes, it does.

CASE PROCEEDING/PARTICIPATION

PAUL R. HARRISON

COMPANY	CASE NO.	TESTIMONY/ISSUES
Union Electric Company d/b/a AmerenUE	GR-2003-0517	**October 2003** Direct – Corporate Allocations; UEC Missouri Gas Allocations; CILCORP Allocations; Rent Expense; Maintenance of General Plant Expense; Lease Agreements and Employee Relocation Expense
Union Electric Company d/b/a AmerenUE	EC-2002-1	**June 2002** Surrebutal - Coal Inventory; Venice Power Plant Fire; Tree Trimming Expense and Automated Meter Reading Service
Laclede Gas Company (Gas)	GR-2002-356	**June 2002** Direct - Payroll; Payroll Taxes; 401k Pension Plan; Health Care Expenses; Pension Plan Trustee Fees and Clearing Account
Union Electric Company d/b/a AmerenUE (2nd period, 3rd EARP)	EC-2002-1025	**April 2002** Direct - Revenue Requirement Run; Plant in Service; Depreciation Reserve; Other Rate Base items; Venice Power Plant Fire and Coal Inventory
Union Electric Company d/b/a AmerenUE	EC-2002-1	**March 2002** Direct - Materials and Supplies; Prepayments; Fuel Inventory; Customer Advances for Construction; Customer Deposits; Plant in Service; Depreciation Reserve; Venice Power Plant Fire Expenditures; Tree-Trimming Expense; Automated Meter Reading Expense; Customer Deposit Interest Expense; Year 2000 Computer Modification Expense; Regulatory Advisor's Consulting Fees and Property Taxes

COMPANY	CASE NO.	TESTIMONY/ISSUES
Union Electric Company d/b/a AmerenUE	EC-2002-1	**July 2001** Direct - Materials and Supplies; Prepayments; Fuel Inventory; Customer Advances for Construction; Customer Deposits; Plant in Service; Depreciation Reserve; Power Plant Maintenance Expense; Tree-Trimming Expense; Automated Meter Reading Expense; Customer Deposit Interest Expense; Year 2000 Computer Modification Expense; Computer Software Expense; Year 2000 Computer Modification Expense; Regulatory Advisor's Consulting Fees and Board of Directors Advisor's Fees
Union Electric Company d/b/a AmerenUE (2nd period, 2nd EARP)	EM-96-149	**March 2001** Direct - Coal Inventory
Union Electric Company d/b/a AmerenUE (Gas)	GR-2000-512	**August 2000** Direct - Cash Working Capital; Advertising Expense; Missouri PSC Assessment; Dues and Donations; Automated Meter Reading Expenses; Computer System Software Expenses (CSS); Computer System Software Expenses (Y2K); Computer System Software Expenses (EMPRV); Generation Strategy Project Expenses; Regulatory Advisor's Consulting fees and Board of Directors Advisor's fees
SUMMARY OF SMALL RATE CASE PARTICIPATION		
Roark Water and Sewer	QW-2002-0005 QS-2003-0006	**August 2003** Lead Auditor
Mill Creek Sewer	2002-00682	**January 2003** Lead Auditor