

Exhibit No.:
Issue: *Accounting Authority Order*
Witness: *Charles R. Hyneman*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Direct Testimony*
Case No.: *GU-2005-0095*
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MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

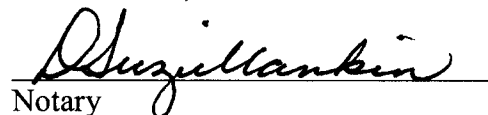
OF

CHARLES R. HYNEMAN

MISSOURI GAS ENERGY

CASE NO. GU-2005-0095

Jefferson City, Missouri
January 2005



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DIRECT TESTIMONY
OF
CHARLES R. HYNEMAN
MISSOURI GAS ENERGY
CASE NO. GU-2005-0095

Q. Please state your name and business address.

A. Charles R. Hyneman, Fletcher Daniels State Office Building, Room G8,
615 East 13th Street, Kansas City, Missouri 64106.

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

A. I am employed by the Missouri Public Service Commission (Commission) as
a Regulatory Auditor.

Q. Please describe your educational background and work experience.

A. I graduated from Indiana State University in May 1985 with a Bachelor of
Science degree in Accounting. I earned a Masters of Business Administration degree from
the University of Missouri-Columbia in December of 1988. I am a Certified Public
Accountant holding certification in the state of Missouri.

In May 1985 I was commissioned as an officer in the United States Air Force. I left
the Air Force in December 1992 and joined the Commission in April of 1993.

Q. Have you previously filed testimony before the Commission?

A. Yes. Schedule 1, attached to this testimony, lists the cases and issues on
which I have filed testimony before the Commission.

Q. What is the purpose of this testimony?

Direct Testimony of
Charles R. Hyneman

1 A. The purpose of this testimony is to provide the Staff's findings and
2 recommendations concerning Missouri Gas Energy's (MGE) request for an Accounting
3 Authority Order (AAO). MGE seeks an AAO allowing it to defer costs related to a new
4 property tax being imposed by the State of Kansas.

5 Q. Please summarize the history of this case.

6 A. On October 12, 2004, MGE, a division of Southern Union Company, filed an
7 Application before the Commission for an AAO. This case is docketed as Case
8 No. GU-2005-0095. At page 4 of its Application, MGE described the reason why it is
9 seeking an AAO in this case:

10 During its 2004 session, the Kansas Legislature passed Senate Bill 147
11 (attached hereto as Appendix A). This bill created a new property tax
12 associated with the inventories of gas held for resale and stored in
13 underground formations in the state of Kansas. The legislation was
14 made retroactive to inventories held as of January 1, 2004.

15 Based upon the December 31, 2003 level of natural gas held in storage
16 by MGE in Meade County, Kansas and other Kansas counties, MGE
17 believes that it will pay property taxes associated with this new Kansas
18 tax in the amount of \$1,262,059, in 2004. This new tax, which is
19 being applied retroactively, is an unpredictable event that could not be
20 adequately or appropriately addressed through the ratemaking process.

21 The Staff has been advised by MGE that its actual billed amount from the State of
22 Kansas is \$1,721,830, which is significantly higher than its estimate of \$1,262,059 included
23 in its Application.

24 Q. What is the Staff's findings and recommendations concerning MGE's
25 Application for an AAO in this case?

26 A. The Staff has determined that the initial imposition of a property tax by the
27 State of Kansas on MGE is an extraordinary event as defined by this Commission. This
28 event has caused MGE to incur a cost that is significant and material to its financial

1 operations. The Staff also asserts that such circumstances warrant an AAO for the actual
2 dollar amount of property taxes paid to the Kansas taxing authorities.

3 The Staff recommends that the Commission order MGE to begin to defer the actual
4 amount of property tax paid to the Kansas taxing authorities and begin to amortize, over a
5 60-month period, any amount deferred pursuant to this AAO beginning the month following
6 a final judicial resolution of the legality of the Kansas tax.

7 Q. Is the extraordinary nature of these costs related in any way to the fact that
8 these costs are in the nature of property taxes?

9 A. No. The first-time imposition of virtually any cost of any nature by an outside
10 regulatory body on a Missouri utility, if significant, would likely qualify as an extraordinary
11 event under the Commission's policy on AAOs.

12 Q. Has the Commission recently reaffirmed its position and policy on granting
13 AAOs in Missouri?

14 A. Yes. On November 10, 2004, the Commission issued its Report and Order
15 on Remand in Case No. WO-2002-273, Missouri-American Water Company. In this Order,
16 the Commission reaffirmed its longstanding policy on AAO standards of deferral.

17 Q. How did the Commission describe the AAOs in this order?

18 A. In this order, the Commission described an AAO as:

19 . . . an order of the Commission pursuant to Section 393.140(8)
20 authorizing an accounting treatment for a transaction or group of
21 transactions other than that prescribed by the USOA. It is an
22 accounting mechanism that has most often been used to permit deferral
23 of costs from one period to another. The immediate and primary
24 benefit of an AAO to the utility is that the deferred item is booked as a
25 regulatory asset rather than as an expense, thereby improving the
26 financial picture of the utility during the deferral period. The
27 regulatory asset is amortized over a prescribed interval and a portion is
28 recognized as an expense each month. A secondary and more remote

benefit of an AAO is that, during a subsequent rate case, the Commission may permit recovery in rates of some portion of the amount deferred. However, it is well-established that the mere granting of an AAO does not guarantee recovery of any amount of the deferral.

Q. Please describe the standards the Commission has applied in issuing Accounting Authority Orders in the past.

A. The Commission expressed its general position and standards for deferral of costs incurred outside a rate case test year in its Report and Order in Case Nos. EO-91-358 and EO-91-360, cases filed by Missouri Public Service (MPS), a division of UtiliCorp United, Inc., now Aquila, Inc. This order related to costs of rehabilitating and upgrading MPS's Sibley Generation Station, and has subsequently been referred to by the Commission as the "Sibley Order."

In the Standards For Deferral section of the Sibley Order, the Commission described certain requirements that must be met for it to allow the deferral as a regulatory asset certain costs incurred outside of a rate case test year.

These requirements (Sibley Test) are founded, in part, on the Federal Energy Regulatory Commission's (FERC) Uniform System of Accounts (USOA) description of extraordinary items in General Instruction No. 7 to the USOA for natural gas companies.

The Commission's standards of deferral state that:

1. Extraordinary events are events that occur during a period that are extraordinary, unusual and unique, and not recurring;
2. Materiality of the cost is relevant to whether the event is extraordinary, although not case dispositive;
3. The determination of whether or not a cost is extraordinary will be made on a case-by-case basis.

1 Since issuing the Sibley Order, the Commission has consistently referred to the
2 deferral requirements of the Sibley Test as the basis for its decisions on granting or rejecting
3 AAO applications. In addition, in its most recent order on AAOs in Case No. WO-2002-273,
4 the Commission reaffirmed the Sibley Test. In this order, the Commission stated:

5 In the Sibley decision, the Commission emphasized that it is the
6 extraordinary event that is the “primary focus” in any request for an
7 AAO, considered on a case-by-case basis: “The decision to defer costs
8 associated with an event turns on whether the event is in fact
9 extraordinary and nonrecurring.” The Commission emphasized that
10 “[e]xtraordinary means unusual and nonrecurring.” Also relevant, but
11 not dispositive, the Commission explained, is “whether the event has a
12 material or substantial effect on a utility’s earnings.” Another relevant
13 factor is the certainty of the event’s occurrence. “Utilities should not
14 seek deferral of speculative events since it is hard to determine
15 whether an event is extraordinary or material unless there is a high
16 probability of its occurring within the near future.

17 Q. How does FERC USOA define extraordinary costs?

18 A. The FERC describes extraordinary items in General Instruction No. 7 to the
19 USOA for natural gas companies as follows:

20 Those items related to the effects of events and transactions which
21 have occurred during the current period and which are not typical or
22 customary business activities of the company shall be considered
23 extraordinary items.

24 Accordingly, they will be events and transactions of significant effect
25 which would not be expected to recur frequently and which would not
26 be considered as recurring factors in any evaluation of the ordinary
27 operating processes of business . . .

28 To be considered as extraordinary under the above guidelines, an item
29 should be more than approximately 5 percent of income, computed
30 before extraordinary items. Commission approval must be obtained to
31 treat an item of less than 5 percent, as extraordinary. (See Accounts
32 434 and 435.)

33 Q. Why should an item or event have to be considered extraordinary before it can
34 be eligible for AAO treatment?

1 A. The ratemaking process is premised upon normality and regularity as the basis
2 for setting rates. Accounting and ratemaking rules and conventions generally reflect the
3 ongoing and normal changes to revenues, expenses and rate base that a utility will experience
4 over time. Only infrequently do extraordinary events occur which justify changes to normal
5 utility accounting and ratemaking practices and procedures.

6 Q. Please explain the reasons for the Staff's finding that the initial imposition of
7 this tax by the State of Kansas meets the Commission's standards of deferral for AAOs.

8 A. MGE has been operating as a Missouri natural gas company since 1994 and
9 has never had to pay such a tax to the Kansas taxing authorities. The initial imposition of
10 this tax by the State of Kansas is an event that is unusual in nature in that it is highly
11 abnormal. Taking into account the environment in which MGE operates (a natural gas
12 distribution company operating in the state of Missouri), the imposition of this tax by a state
13 without any other nexus is clearly unrelated to the ordinary and typical activities of MGE.

14 In addition to meeting the unusual in nature standard, the initial imposition of this tax
15 on MGE by definition, meets the infrequency of occurrence standard. If the courts decide for
16 the State of Kansas, MGE will incur these expenses on an annual basis and this cost will
17 become a normal recurring cost. However, if the courts decide for MGE, it is not likely that
18 MGE will incur this cost on a recurring basis in the future.

19 Finally, Kansas has billed MGE approximately \$1.7 million for this tax in 2004. This
20 cost is material to MGE's annual income. The fact that this cost is material to MGE, while
21 not dispositive to the determination of an extraordinary event, does support such a
22 determination.

SUMMARY AND CONCLUSION

Q. Please summarize the Staff's recommendation regarding MGE's request for AAO deferral treatment in this case.

A. The Staff has found that the new tax being imposed on MGE by the State of Kansas is extraordinary and material and meets the standards of deferral established by the Commission. Therefore, the Staff recommends that the Commission issue an order approving MGE's Application for an AAO in this case.

The Staff recommends that the Commission, in its order, direct MGE to begin to defer only the actual amount of property tax paid to the Kansas taxing authorities and, consistent with its policy outlined in the Sibley Order, order MGE to begin to amortize this regulatory asset, over a 60-month period, beginning the month following a final judicial resolution of the legality of the Kansas tax.

Finally, the Staff recommends that the Commission include language in its Order stating that granting this AAO does not control how the Commission will treat this deferral for ratemaking purposes. If required, all ratemaking decisions will be reserved for MGE's next rate case after final resolution of the tax.

Q. Does this conclude your direct testimony?

A. Yes, it does.

CHARLES R. HYNEMAN**CASE PARTICIPATION**

Date Filed	Issue	Case Number	Exhibit	Case Name
7/16/1993	Cash Working Capital; Other Rate Base Components	TR93181	Direct	United Telephone Company of Missouri
8/13/1993	Cash Working Capital	TR93181	Rebuttal	United Telephone Company of Missouri
8/25/1993	Cash Working Capital	TR93181	Surrebuttal	United Telephone Company of Missouri
4/11/1994	Pension Expense; Other Postretirement Benefits	ER94163	Direct	St. Joseph Light & Power Company
5/16/1994	Pension Expense; Other Postretirement Benefits	HR94177	Direct	St. Joseph Light & Power Company
4/20/1995	Pension Expense; OPEB Expense; Deferred Taxes; Income Taxes; Property Taxes	GR95160	Direct	United Cities Gas Company
5/7/1996	Merger Premium	EM96149	Rebuttal	Union Electric Company
8/9/1996	Income Tax Expense; AAO Deferrals; Acquisition Savings	GR96285	Direct	Missouri Gas Energy
9/27/1996	Income Tax Expense; AAO Deferrals; Acquisition Savings	GR96285	Rebuttal	Missouri Gas Energy
10/11/1996	Income Tax Expense; AAO Deferrals; Acquisition Savings	GR96285	Surrebuttal	Missouri Gas Energy
6/26/1997	Property Taxes; Store Expense; Material & Supplies; Deferred Tax Reserve; Cash Working Capital; Postretirement Benefits; Pensions; Income Tax Expense	GR97272	Direct	Associated Natural Gas Company Division of Arkansas Western Gas Company

Date Filed	Issue	Case Number	Exhibit	Case Name
8/7/1997	FAS 106 and FAS 109 Regulatory Assets	GR97272	Rebuttal	Associated Natural Gas Company Division of Arkansas Western Gas Company
11/21/1997	OPEB's; Pensions	ER97394	Surrebuttal	UtiliCorp United Inc. d/b/a Missouri Public Service
3/13/1998	Miscellaneous Adjustments; Plant; Reserve; SLRP; AMR; Income and Property Taxes;	GR98140	Direct	Missouri Gas Energy, A Division of Southern Union Company
4/23/1998	Service Line Replacement Program; Accounting Authority Order	GR98140	Rebuttal	Missouri Gas Energy, A Division of Southern Union Company
5/15/1998	SLRP AAOs; Automated Meter Reading (AMR)	GR98140	Surrebuttal	Missouri Gas Energy, A Division of Southern Union Company
7/10/1998	SLRP AAOs; Reserve; Deferred Taxes; Plant	GR98140	True-Up	Missouri Gas Energy, A Division of Southern Union Company
4/26/1999	Merger Premium; Merger Accounting	EM97515	Rebuttal	Western Resources Inc. and Kansas City Power and Light Company
9/2/1999	Accounting Authority Order	GO99258	Rebuttal	Missouri Gas Energy
3/1/2000	Acquisition Detriments	GM2000312	Rebuttal	Atmos Energy Company and Associated Natural Gas Company
5/2/2000	Deferred Taxes; Acquisition Adjustment; Merger Benefits; Merger Premium; Merger Accounting; Pooling of Interests	EM2000292	Rebuttal	UtiliCorp United Inc. / St. Joseph Light and Power

Date Filed	Issue	Case Number	Exhibit	Case Name
6/21/2000	Merger Accounting Acquisition	EM2000369	Rebuttal	UtiliCorp United Inc. / Empire District Electric Company
11/30/2000	Revenue Requirements	TT2001119	Rebuttal	Holway Telephone Company
4/19/2001	Revenue Requirement; Corporate Allocations; Income Taxes; Miscellaneous Rate Base Components; Miscellaneous Income Statement Adjustments	GR2001292	Direct	Missouri Gas Energy, A Division of Southern Union Company
12/6/2001	Corporate Allocations	ER2001672	Direct	UtiliCorp United Inc. d/b/a Missouri Public Service
12/6/2001	Corporate Allocations	EC2002265	Direct	UtiliCorp United Inc. d/b/a Missouri Public Service
1/8/2002	Acquisition Adjustment	EC2002265	Rebuttal	UtiliCorp United Inc. d/b/a Missouri Public Service
1/8/2002	Acquisition Adjustment	ER2001672	Rebuttal	UtiliCorp United Inc. d/b/a Missouri Public Service
1/22/2002	Acquisition Adjustment	ER2001265	Surrebuttal	UtiliCorp United Inc. d/b/a Missouri Public Service
1/22/2002	Acquisition Adjustment; Corporate Allocations;	EC2001265	Surrebuttal	UtiliCorp United Inc. d/b/a Missouri Public Service
4/17/2002	Accounting Authority Order	GO2002175	Rebuttal	Utilicorp United Inc. d/b/a Missouri Public Service & St. Joseph Light & Power

Date Filed	Issue	Case Number	Exhibit	Case Name
8/16/2002	Prepaid Pension Asset; FAS 87 Volatility; Historical Ratemaking Treatments-Pensions & OPEB Costs; Pension Expense-FAS 87 & OPEB Expense-FAS 106; Bad Debt Expense; Sale of Emission Credits; Revenues	ER2002424	Direct	The Empire District Electric Company
3/17/2003	Acquisition Detriment	GM20030238	Rebuttal	Southern Union Co. d/b/a Missouri Gas Energy
12/9/2003	Current Corporate Structure; Aquila's Financial Problems; Aquila's Organizational Structure in 2001; Corporate History; Corporate Plant and Reserve Allocations; Corporate Allocation Adjustments	HR20040024	Direct	Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P
12/9/2003	Corporate Plant and Reserve Allocations; Corporate Allocation Adjustments; Aquila's Financial Problems; Aquila's Organizational Structure in 2001; Corporate History; Current Corporate Structure	ER20040034	Direct	Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P
1/6/2004	Corporate Allocation Adjustments; Reserve Allocations; Corporate Plant	GR20040072	Direct	Aquila, Inc.
2/13/2004	Severance Adjustment; Supplemental Executive Retirement Plan; Corporate Cost Allocations	HR20040024	Surrebuttal	Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P
2/13/2004	Severance Adjustment; Corporate Cost Allocations; Supplemental Executive Retirement Plan	ER20040034	Surrebuttal	Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P

Date Filed	Issue	Case Number	Exhibit	Case Name
4/15/2004	Pensions and OPEBs; True-Up Audit; Cost of Removal; Prepaid Pensions; Lobbying Activities; Corporate Costs; Miscellaneous Adjustments	GR20040209	Direct	Missouri Gas Energy
6/14/2004	Alternative Minimum Tax; Stipulation Compliance; NYC Office; Executive Compensation; Corporate Incentive Compensation; True-up Audit; Pension Expense; Cost of Removal; Lobbying	GR20040209	Surrebuttal	Missouri Gas Energy