

Exhibit No:
Issues: Employee Benefits
Bad Debts Expense
Witness: Harold E. Mikkelsen
Type of Exhibit: Direct Testimony
Sponsoring Party: Aquila Networks – MPS
Aquila Networks – L&P
Case No:
Date Testimony to be filed: August 1, 2003

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. _____

DIRECT TESTIMONY

OF

HAROLD E. MIKKELSEN

ON BEHALF OF

**AQUILA, INC.
d/b/a
AQUILA NETWORKS – MPS
and
AQUILA NETWORKS – L&P**

**Omaha, Nebraska
August, 2003**

State of Nebraska)
) ss
County of Douglas)

AFFIDAVIT OF HAROLD E. MIKKELSEN

Harold E. Mikkelsen, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony and schedules entitled "Direct Testimony of Harold E. Mikkelsen"; that said testimony was prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge, information, and belief.

Harold E. Mikkelsen

Subscribed and sworn to before me this 15th day of July, 2003.

Richard G. Petersen
Notary Public

My Commission expires:

7/4/05

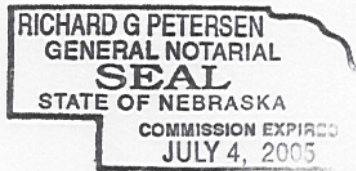


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2 **DIRECT TESTIMONY OF HAROLD E. MIKKELSEN**
3

4 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

5 A. My name is Harold E. Mikkelsen and my business address is 1815 Capitol Avenue,
6 Omaha, Nebraska.

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

8 A. I am presently employed by Aquila, Inc. ("Aquila") as a Senior Regulatory Analyst. In
9 this position, my responsibilities include the preparation and review of financial
10 exhibits and other information for regulatory filings, including rate case filings.

11 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
12 **EMPLOYMENT HISTORY.**

13 A. I attended the University of South Dakota where I received a Bachelor of Science
14 Degree in Business Administration with a major in accounting. In 1971, I began
15 working for the Peoples Natural Gas Division of Northern Natural Gas Company and
16 held various positions in the accounting, planning, and regulatory areas. In 1985,
17 Aquila, Inc.'s predecessor purchased the Peoples Natural Gas Division. Since that
18 time, I have held various positions in Aquila's planning, accounting, reporting, and
19 regulatory areas. I assumed my present position in June 1998.

20 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY REGULATORY**
21 **BODIES?**

22 A. Yes. I have testified before the Public Utilities Commission of Colorado.

23 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

1 A. The purpose of my testimony is to support and explain certain schedules and
2 adjustments to the cost of service in support of Aquila's rate case filings for its
3 Aquila Networks – MPS ("MPS") and Aquila Networks – L&P ("L&P") gas divisions.

4 **Q. PLEASE IDENTIFY THE ADJUSTMENTS THAT YOU ARE SPONSORING.**

5 A. I am sponsoring the following adjustments to cost of service:

- 6 • CS-12 Medical, Dental, and Vision Benefits (MPS and L&P)
- 7 • CS-13 Pensions (MPS and L&P)
- 8 • CS-14 Other Postretirement Benefits ("OPEB") (MPS and L&P)
- 9 • CS-15 401 (K) Adjustment (MPS and L&P)
- 10 • CS-15.5 Employee Stock Contribution Plan ("ESOP") (MPS and L&P)
- 11 • CS-35 Bad Debt Expense (MPS and L&P)

12 **COST OF SERVICE**

13 **Benefits**

14 **Q. WERE SCHEDULE HEM-1 "CS-11 BENEFITS SUMMARY SCHEDULE-MPS"**
15 **AND SCHEDULE HEM-2 "CS-11 BENEFITS SUMMARY SCHEDULE-L&P"**
16 **ATTACHED TO THIS TESTIMONY PREPARED BY YOU OR UNDER YOUR**
17 **SUPERVISION?**

18 A. Yes.

19 **Q. WHAT BENEFITS ADJUSTMENTS ARE INCLUDED IN THESE**
20 **SCHEDULES?**

21 A. These schedules include the following adjustments:

- 1 • CS-12 Medical, Dental, and Vision
- 2 • CS-13 Pensions
- 3 • CS-14 Other Postretirement Benefits (“OPEB”)
- 4 • CS-15 401 (K) Adjustment
- 5 • CS-15.5 Employee Stock Contribution Plan (“ESOP”)

6 **Q. CAN YOU PLEASE EXPLAIN THE ADJUSTMENT MADE TO THE CS-12**
7 **MEDICAL, DENTAL, AND VISION BENEFITS?**

8 A. Yes. The amount on the books at December 31, 2002 was adjusted by the known
9 health, dental, and vision coverage priced at 2003 rates.

10 **Q. WHERE WERE THE 2003 RATES OBTAINED?**

11 A. The rates for 2003 were provided from the Human Resources Department of
12 Aquila. The rates are per Aquila’s contracts with its insurance service providers.

13 **Q. WHAT WAS THE METHOD USED TO ADJUST HEALTH, DENTAL, AND**
14 **VISION WITH 2003 RATES?**

15 A. The benefit elections by employee number, supplied by the Human Resources
16 Department of Aquila as of January 2003, was used to determine the existing
17 coverage election, coverage level, and corresponding dollar amount of benefits
18 coverage for each employee utilizing 2003 rates. The data was then summarized
19 by department, and multiplied by the appropriate allocation factor for each operating
20 unit of MPS and L&P. The factors used for each department were determined
21 through the corporate allocation process, which is more fully explained in the

1 testimony of Aquila witness, Bev Agut. The employer portion of health, dental, and
2 vision coverage cost was then totaled and compared to the per book level. The next
3 step was to multiply this difference by a capitalization factor to adjust figures for any
4 benefit costs that might be capitalized. The adjustment was then allocated across
5 utility class for MPS and L&P to arrive at the assignment to MPS and L&P gas
6 divisions.

7 **Q. WHAT IS THE AMOUNT OF THE ADJUSTMENT?**

8 A. The adjustment for health, dental, and vision expense is an expense decrease of
9 \$10,909 for MPS and an expense decrease of \$1,474 for L&P.

10 **Q. HOW WAS THE CS-13 EMPLOYER PENSION PLAN ADJUSTMENT**
11 **CALCULATED?**

12 A. The employer pension share was calculated using the latest available Northern Trust
13 Retirement Consulting, L.L.C. ("Northern Trust") study with fiscal 2002 data. Aquila
14 employed Northern Trust as its actuarial consultant during the test year for
15 computing pensions and SFAS 106 liabilities and expenses. (Subsequent to the
16 test year, Northern Trust was purchased by Hewitt Associates, a major human
17 resources consulting and benefits administration firm. This does not change the
18 results of the study as described in the following adjustment.) The adjustment was
19 calculated by taking the "2003 Total Allocated Net Periodic Pension Cost" per the
20 Northern Trust Study, less the amount per books at December 31, 2002. However,
21 before comparing the study amount to the per book expense, total allocated Net
22 Periodic Pension Cost was first adjusted by an amount equal to one-tenth of the

1 Pension Plan Curtailment calculations under SFAS 88 which were booked during
2 2002 as a result of Aquila's restructuring. This additional adjustment is made in
3 order to reflect amortization of the 2002 pension curtailment entry over a ten-year
4 period. The total adjustment was then multiplied by the capitalization factor to
5 exclude the capital component. For MPS and L&P, this adjustment amount was
6 then allocated by utility class to obtain the adjustments for MPS and L&P gas
7 divisions. The gas jurisdictional adjustment for pension expense is an expense
8 increase of \$119,977 for MPS and an expense increase of \$183,853 for L&P.

9 **Q. PLEASE CONTINUE BY EXPLAINING HOW OTHER POSTRETIREMENT**
10 **EMPLOYEE BENEFITS (OPEB) EXPENSES WERE CALCULATED IN COST**
11 **OF SERVICE ADJUSTMENT CS-14 UNDER SFAS 106.**

12 A. The annual OPEB expense under SFAS 106 was calculated in the same manner.
13 The adjustment was calculated by taking the "2003 Total Allocated Net Periodic
14 Postretirement Benefit Expense" per the Northern Trust Study less the amount
15 recorded on the books as of December 31, 2002. However, before comparing the
16 study amount to the per book expense, the total allocated Net Periodic
17 Postretirement Benefit Expense was first adjusted by an amount equal to one-tenth
18 of the OPEB curtailment calculations under SFAS 88 which were booked during
19 2002 as a result of Aquila's restructuring. This additional adjustment is made in
20 order to reflect amortization of the OPEB curtailment entry over a ten-year period.
21 The total adjustment was then multiplied by a capitalization factor to eliminate any
22 OPEB costs that would be capitalized.

1 **Q. AFTER THIS STEP WHAT REMAINS?**

2 A. At this stage, you are left with an OPEB expense adjustment that is allocated to a
3 utility class.

4 **Q. DID YOU ALLOCATE THIS ADJUSTMENT TO A UTILITY CLASS, AND IF SO,
5 HOW WAS IT DONE?**

6 A. Yes, I did allocate this adjustment to a utility class. For MPS and L&P, this
7 allocation was based on the split between utility classes for the per book employee
8 pension and benefit account. The resulting adjustment related to SFAS 106
9 expense was an expense decrease of \$62,445 for MPS and an expense decrease
10 of \$939 for L&P.

11 **Q. PLEASE DESCRIBE AQUILA'S 401(K) PLAN.**

12 A. Aquila provides its employees with an optional benefit known as the 401(k) plan. The
13 plan is administered by J.P. Morgan / American Century Retirement Plan Services.
14 The 401(k) plan is a retirement savings program that allows employees to invest a
15 percentage of their salary for retirement.

16 **Q. IS THERE A PORTION THAT IS MATCHED BY AQUILA?**

17 A. Yes. Aquila matches a portion of the funds invested by employees up to six percent
18 (6%) of base salary and wages.

19 **Q. PLEASE DESCRIBE THE ADJUSTMENT MADE TO COST OF SERVICE ON
20 ADJUSTMENT CS-15 401(K) EXPENSE.**

1 A. The 6% matched portion, called 401(k) Employer Share, was calculated by taking
2 the 401(k) balance for test year end December 31, 2002 and dividing it by the per
3 books base pay, excluding incentives, for the same period to arrive at a percentage
4 of base pay being matched by Aquila. This ratio was then multiplied by the
5 annualized net base pay as calculated on adjustment CS-5 to come up with an
6 annualized 401(k) amount.

7 **Q. WHY IS THE PERCENTAGE NOT SIMPLY 6% OF BASE SALARIES AND**
8 **WAGES?**

9 A. Certain employees choose not to participate to the full 6% match for various
10 reasons. This has the effect of drawing the percentage slightly lower.

11 **Q. WHAT IS THE ADJUSTMENT FOR MPS AND L&P?**

12 A. The adjustment for 401(k) expense is an increase of \$1,871 for MPS and a
13 decrease of \$1,386 for L&P.

14 **Q. HOW WAS CS-15.5, THE ESOP PORTION OF THE ADJUSTMENT**
15 **CALCULATED?**

16 A. The ESOP portion was calculated in the same manner. The ESOP amount per
17 books for the test year-end, December 31, 2002 was divided by the base salaries
18 and wages per books for the same time period. This ratio was then multiplied by
19 the 2003 annualized base salaries and wages as calculated in CS-5 to arrive at the
20 adjusted ESOP level in total for 2003. Next, a capitalization ratio was applied, and

1 then the adjustment was allocated to utility class on the same basis as discussed
2 above in the 401(k) adjustment.

3 **Q. WHAT IS THE AMOUNT OF THE ESOP FOR MPS AND L&P?**

4 A. The adjustment for ESOP expense is an increase of \$1,012 for MPS and a
5 decrease of \$496 for L&P.

6 **Q. ARE ANY OTHER AQUILA BENEFITS, AS ADJUSTED, INCLUDED IN COST**
7 **OF SERVICE ADJUSTMENT NUMBER 11 – BENEFITS SUMMARY**
8 **SCHEDULE?**

9 A. No. Only the benefits determined and listed above are included in Cost of Service
10 Adjustment Number 11 – Benefits Summary Schedule.

11 **BAD DEBT EXPENSE**

12 **Q. WHAT IS THE PURPOSE OF THE BAD DEBT ADJUSTMENT IN CS-35?**

13 A. The bad debt adjustment updates MPS and L&P gas jurisdictional per book bad
14 debt expense to be in line with MPS and L&P new weather normalized gas
15 jurisdictional revenue levels. The first step calculates an adjusted level of bad debt
16 expense for the test year ending December 31, 2002 by multiplying weather
17 normalized gas jurisdictional revenues for the same period times a bad debt
18 expense rate of 1.738591 percent for MPS and 1.012585 percent for L&P. The
19 bad debt expense rate was determined by calculating a percentage based on a
20 three-year average of actual bad debt write-offs to revenues for the last three years
21 (2000-2002).

1 **Q. WHY IS A THREE-YEAR AVERAGE USED?**

2 A. Bad debt levels can vary significantly from year to year. Therefore, using data from
3 only one year may serve to over or under state ongoing bad debt levels. Using this
4 rate provides a more accurate representation of the current bad debt trend and
5 reflects a representative level of expense in the test year by using an average of
6 several years' history of actual bad debt write-offs to revenues in determination of
7 the rate. The three-year average rate used was the most current data available at
8 the time this adjustment was prepared.

9 **Q. PLEASE CONTINUE**

10 A. Next, the new gas jurisdictional bad debt level is compared to MPS and L&P gas
11 jurisdictional per books bad debt expense. The difference is the MPS and L&P
12 jurisdictional bad debt adjustment. The adjustment for bad debt expense is an
13 expense decrease of \$356,854 for MPS and an expense decrease of \$5,581 for
14 L&P.

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

16 A. Yes.