Exhibit No.:	
Issue:	*Merger Savings*
Witness:	*Mark L. Oligschlaeger*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Rebuttal Testimony*
Case No.:	*GR-2004-0072*
Date Testimony Prepared:	*February 13, 2004*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

REBUTTAL TESTIMONY

OF

MARK L. OLIGSCHLAEGER

AQUILA, INC.,

d/b/a AQUILA NETWORKS – MPS (Natural Gas)

and AQUILA NETWORKS – L&P (Natural Gas)

CASE NO. GR-2004-0072

Jefferson City, Missouri
February 2004

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P, Natural Gas General Rate Increase	)))	Case No. GR-2004-0072

AFFIDAVIT OF MARK L. OLIGSCHLAEGER

STATE OF MISSOURI	)	
	)	ss.
COUNTY OF COLE	)	

Mark L. Oligschlaeger, being of lawful age, on his oath states: that he has participated in the preparation of the following Rebuttal Testimony in question and answer form, consisting of 20 pages to be presented in the above case; that the answers in the following Rebuttal 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.

Mark L. Oligschlaeger

Mark L. Oligschlaeger

Subscribed and sworn to before me this 10th day of February 2004.

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

D Suzie Mankin

Notary

1 **REBUTTAL TESTIMONY**

2 **OF**

3 **MARK L. OLIGSCHLAEGER**

4 **AQUILA, INC.,**

5 **d/b/a AQUILA NETWORKS – MPS (Natural Gas)**

6 **and AQUILA NETWORKS - L&P (Natural Gas)**

7 **CASE NO. GR-2004-0072**

8 Q. Please state your name and business address.

9 A. Mark L. Oligschlaeger, P.O. Box 360, Suite 440, Jefferson City, MO 65102.

10 Q. Are you the same Mark L. Oligschlaeger who has previously filed direct

11 testimony in this proceeding?

12 A. Yes, I am.

13 Q. What is the purpose of your rebuttal testimony?

14 A. The purpose of this testimony is to address the direct testimony filed by

15 Aquila, Inc. (Aquila/UtiliCorp or Company) d/b/a Aquila Networks - MPS (MPS) and Aquila

16 Networks - L&P (L&P) witness Vern J. Siemek on the issue of Merger Savings.

17 Q. What other Staff witnesses are also providing rebuttal testimony on the issue or

18 merger savings?

19 A. Staff Auditing witnesses Cary G. Featherstone, Janis E. Fischer and Steve M.

20 Traxler are also providing testimony on the issue of merger savings.

21 Q. Was Mr. Siemek deposed by the Staff on the issue of merger savings?

22 A. Yes, on December 30, 2003.

1 Q. What is Aquila/UtiliCorp's proposed treatment of merger savings in this case
2 related to its merger and acquisition transaction with St. Joseph Light & Power Company in
3 2000?

4 A. As stated in the direct testimony of Mr. Siemek, Aquila/UtiliCorp proposes to
5 pass on to customers in rates in this proceeding the benefit of only one-half of the merger
6 savings it has calculated from the L&P transaction, rather than reduce its requested rate
7 increase by the full amount of these savings. Mr. Siemek provides the following reasons in
8 his direct testimony why he believes a 50/50 sharing of merger savings between
9 Aquila/UtiliCorp and its customers is appropriate:

10 1) Retaining 50% of the merger savings is equitable in lieu of not
11 reflecting the costs of the L&P acquisition in rates;

12 2) Aquila/UtiliCorp has not "realized" any of the benefits of the savings
13 generated from the L&P transaction since it was entered into; and

14 3) Allowing Aquila/UtiliCorp to retain 50% of the merger savings will
15 provide an incentive for further merger and acquisitions to take place.

16 Q. Does Aquila/UtiliCorp's proposed merger savings sharing approach apply only
17 to the Company's Missouri gas operations?

18 A. No. The Company has also made a similar proposal to share merger savings in
19 its current electric rate increase case pending before the Commission, Case No.
20 ER-2004-0034.

21 Q. Does the Company's proposal for merger savings sharing apply to both its
22 MPS and L&P divisions' gas operations?

1 A. No. Aquila/UtiliCorp is not proposing to share any of its merger savings that
2 allegedly relate to its L&P division. The merger savings sharing proposal applies only to its
3 MPS division. Staff Auditing witness Steve M. Traxler will address merger savings and costs
4 as they apply to the L&P division's gas operations in his rebuttal testimony.

5 Q. What is the Staff's position on the proposed sharing of merger savings?

6 A. As explained previously in testimony in other cases, the Staff is not opposed to
7 the sharing of merger savings through the vehicle of regulatory lag. However, the Staff is
8 opposed to Aquila/UtiliCorp's proposed method for sharing merger savings in this case for
9 the following reasons:

10 1) Aquila/UtiliCorp has had an adequate opportunity to benefit from
11 merger savings through regulatory lag since the L&P merger was entered into, and
12 special rate measures to allow the Company further opportunity to retain merger
13 savings are not necessary;

14 2) The Company's merger savings sharing proposal will have the effect of
15 taking Aquila/UtiliCorp off "cost-based rates";

16 3) Allowing sharing of merger savings in these circumstances would be
17 allowing inappropriate indirect recovery in rates of the L&P acquisition adjustment
18 and transaction costs;

19 4) The Commission should not be providing rate "incentives" for merger
20 and acquisitions, either in general or for Aquila/UtiliCorp specifically; and

21 5) Contrary to Mr. Siemek's suggestion, any merger savings associated
22 with the L&P transaction since it has been implemented have been fully realized by
23 the Company.

1 Each of these points will be addressed in my and other Staff witnesses' rebuttal
2 testimony on this issue.

3 Q. What upfront costs can a utility incur in undertaking a merger and acquisition
4 transaction?

5 A. Utilities frequently pay a higher price for the assets of an acquired utility than
6 the net book value of the assets on the acquired utility's books would indicate. An
7 "acquisition adjustment" is commonly defined as the difference between the price paid for the
8 assets and the net book value of the assets acquired. Acquisition adjustments are also
9 sometimes called "merger premiums." A utility normally will also pay certain upfront
10 banking and legal fees related to the merger/acquisition attempt, called "transaction costs."
11 For financial reporting purposes, it is my understanding that utilities should combine the
12 amount of transaction costs and the amount of any payment above net book value of assets
13 acquired into one amount, and charge it to the Acquisition Adjustment account in the Federal
14 Energy Regulatory Commission Uniform System of Accounts. In this testimony, when I refer
15 to the L&P "acquisition adjustment," I will be referring to both the transaction costs related to
16 the L&P merger and the amount paid by Aquila for the L&P properties above the net book
17 value of those properties on L&P's books.

18 Q. After a utility completes a merger/acquisition transaction, how can the
19 company recover an acquisition adjustment in rates?

20 A. A utility can recover an acquisition adjustment directly through rates through
21 inclusion in rate base of the acquisition adjustment and/or an amortization to expense of the
22 acquisition adjustment, or can achieve indirect recovery of the acquisition adjustment by
23 retaining the benefits of merger savings for a period of time.

1 Q. Has the Staff ever recommended that the Commission allow direct recovery of
2 acquisition adjustments in rates?
3 A. No. The Staff is opposed to direct recovery of acquisition adjustments in rates
4 for the reasons stated in my direct testimony in this proceeding.
5 Q. Has the Commission ever allowed direct recovery of acquisition adjustments in
6 customer rates?
7 A. No.
8 Q. As an alternative to the recovery of acquisition adjustments directly in rates,
9 how can utilities retain the benefits of mergers and acquisitions for a period of time before
10 passing on those benefits to customers in rates?
11 A. Generally, there are two different ways for utilities to retain merger benefits for
12 a period of time: 1) through the phenomenon of regulatory lag; or 2) through a merger savings
13 sharing proposal such as that proposed by Aquila/UtiliCorp in this case.
14 Q. What is "regulatory lag?"
15 A. As defined in my direct testimony, regulatory lag is the passage of time
16 between when a utility's financial results change, and when that change is reflected in the
17 utility's rates.
18 Q. How does regulatory lag allow for a company such as Aquila/UtiliCorp to
19 retain merger savings for a period of time?
20 A. If this Commission approves a merger and acquisition transaction, the rates for
21 the merging utilities will not change at that point. Therefore, if a merging utility can generate
22 savings from the transaction, the utility derives a direct and immediate benefit from those
23 savings because its rates will reflect a higher cost of service than it will actually experience

1 following the merger. This situation will then persist until the utility's rates change, either as
2 a result of a rate increase application from the company in question or as a result of a
3 complaint application filed by the Staff or another party to reduce rates.

4 Q. Does regulatory lag allow for a sharing of merger savings between a utility's
5 shareholders and its customers?

6 A. Yes. Due to the existence of regulatory lag, a utility can retain 100% of the
7 benefit of any achieved merger savings until its rates change because of a regulatory
8 proceeding. After the company's rates change to reflect the lower post-merger costs, the
9 utility's customers then will receive the benefit of 100% of the achieved merger savings to
10 date. The longer a utility can avoid filing a rate proceeding, or being the subject of a rate
11 complaint, the more its shareholders can benefit from merger savings through regulatory lag.
12 Once rates are changed to reflect merger savings achieved to a point in time, any additional
13 merger savings then created by the utility over the level reflected in rates can again be
14 retained 100% for the benefit of shareholders until rates are changed.

15 Q. What is the Staff's position on the use of regulatory lag to determine how
16 much savings a utility is able to retain over time?

17 A. The Staff favors regulatory lag as a means of apportioning merger savings
18 between utility customers and shareholders. Regulatory lag provides an incentive for utilities
19 to maximize merger savings and avoid filing rate increase cases, so that a company can retain
20 merger savings for as long as possible before the savings are passed on to customers in rates.
21 Regulatory lag also allows for the utility the opportunity to indirectly recover some portion of
22 its acquisition adjustment from retention of merger savings, before such savings are passed on
23 to customers through a rate change.

1 Q. Has regulatory lag been the method used in this jurisdiction to apportion
2 merger savings between utility shareholders and customers?
3 A. Yes. I am not aware of any time in which the Commission has ordered use of
4 explicit merger savings proposals, such as Aquila/UtiliCorp's scheme in this case, as a means
5 to share savings between shareholders and customers.
6 Q. What treatment of merger savings did Aquila/UtiliCorp seek in its merger
7 application before the Commission for the L&P acquisition, Case No. EM-2000-292?
8 A. The Company asked for a number of special ratemaking arrangements from the
9 Commission in its application for approval of the L&P transaction. These ratemaking
10 arrangements included a five-year rate moratorium for its new L&P division, applying to both
11 the L&P electric and gas operations, so that Aquila/UtiliCorp could retain the benefit of
12 merger savings for that division for that full period of time. For its MPS division,
13 Aquila/UtiliCorp did not ask for a rate moratorium. Because the Company planned a rate
14 increase application for its MPS division for shortly after completion of the L&P merger,
15 Aquila/UtiliCorp sought another special rate arrangement that would apply to future MPS rate
16 applications; specifically that the MPS corporate allocation factors be "frozen" for a period of
17 time at pre-merger levels. Since a reduction of corporate allocation factors for
18 Aquila/UtiliCorp divisions such as MPS following a merger was held by the Company to be a
19 source of merger savings, "freezing" such corporate allocation factors would serve to preserve
20 those merger savings for retention by shareholders, even if Aquila/UtiliCorp initiated MPS
21 rate proceedings after the merger.
22 There were other features of the Company's requested post-merger treatment of L&P
23 merger savings and costs, which were referred to in entirety as the "regulatory plan."

1 Q. Did the Staff oppose Aquila/UtiliCorp's regulatory plan?

2 A. Yes.

3 Q. Did the Commission rule on the Company's proposed regulatory plan for the
4 Aquila/UtiliCorp – L&P merger in Case No. EM-2000-292, the merger application?

5 A. Yes, the Commission rejected the proposed regulatory plan, stating that the
6 Company could seek rate treatment of merger savings and costs in rate proceedings following
7 the merger.

8 Q. After the Commission issued its Order in Case No. EM-2000-292 approving
9 the L&P merger, but rejecting the regulatory plan, could Aquila/UtiliCorp have sought to
10 terminate the merger transaction if it was displeased with the terms of the Missouri
11 Commission regulatory approval?

12 A. Yes.

13 Q. Was Aquila/UtiliCorp aware at the time of the Commission's Order in the
14 merger application that regulatory lag was the traditional method used in this jurisdiction for
15 sharing of merger savings between utility customers and shareholders?

16 A. Yes. This topic was examined extensively in the testimony filed by the parties
17 in the merger proceeding in Missouri, Case No. EM-2000-292.

18 Q. Since Case No. EM-2000-292, has the Staff or any other party initiated a gas
19 rate complaint proceeding against Aquila/UtiliCorp?

20 A. No.

21 Q. Prior to the instant gas rate increase case, has Aquila/UtiliCorp filed for
22 increased gas rates for either its MPS or L&P divisions since Case No. EM-2000-292?

23 A. No.

1 Q. Did Aquila/UtiliCorp fully control the timing of the instant gas rate filing?

2 A. Yes.

3 Q. When was the L&P transaction closed?

4 A. The Aquila/UtiliCorp – L&P merger was closed on December 31, 2000.

5 Q. When was this rate proceeding filed?

6 A. Aquila/UtiliCorp filed this rate proceeding on August 1, 2003. If this rate case
7 process takes the full eleven months allowed by law, that means that the Company will be
8 able to retain all of its achieved merger savings allocable to its gas operations for
9 approximately 3.5 years after closing the merger, before prospectively passing them on to its
10 customers in rates.

11 Q. Does the Staff consider potential retention of all merger savings by the
12 Company for up to 3.5 years to be adequate retention of the savings before they are
13 prospectively passed on in rates to the benefit of Aquila/UtiliCorp customers?

14 A. Yes. Certainly, no special rate mechanism is necessary to allow Company
15 shareholders further opportunity to keep the benefit of these merger savings.

16 Q. What were Aquila/UtiliCorp's estimates of the merger savings it would be able
17 to achieve during the first three years of the L&P merger?

18 A. In the Company's merger application in Case No. EM-2000-292,
19 Aquila/UtiliCorp presented estimates of the merger savings it planned to achieve during the
20 first ten years of the merger. Based upon the testimony of Company witness Siemek in that
21 proceeding, the Company expected to achieve cumulative savings of $36.4 million by the
22 conclusion of the third year of the L&P merger.

1 A copy of one of Mr. Siemek's workpapers from Case No. EM-2000-292 showing the
2 Company's estimated merger costs and savings for the first ten years following the merger is
3 attached as Schedule 1 to this rebuttal testimony. To derive the $36.4 million cumulative
4 savings figure I reference above, add the results for line III, "Total Synergies, net of Costs to
5 Achieve," for the years 2001, 2002 and 2003.

6 Q. Does the $36.4 million amount of merger savings cited above apply only to the
7 Company's gas operations in Missouri?

8 A. This $36.4 million amount applies to Aquila/UtiliCorp's electric, gas and
9 steam operations in total. Mr. Siemek did not break out or allocate this amount to the electric,
10 gas and steam operations of the Company in the merger case. Most of these savings can be
11 assumed to apply to Aquila/UtiliCorp's electric operations.

12 Q. Does the Staff consider a savings amount of $36.4 million to be significant and
13 material on a total Company basis?

14 A. Yes.

15 Q. What are the Staff's overall conclusions on the equity of the Company's
16 proposal for merger savings sharing in this case?

17 A. The Staff's overall conclusion is that Aquila/UtiliCorp, by its proposal to share
18 merger savings, is attempting to convince the Commission to adopt an inappropriate approach
19 to treatment of merger savings in rates and abandon the Commission's long-standing
20 traditional approach to the treatment of merger savings in rates (regulatory lag). This is after
21 Aquila/UtiliCorp will have benefited for over three years by that traditional approach.
22 Aquila/UtiliCorp has retained any and all merger savings that have been achieved from the
23 L&P acquisition in entirety for over three years. Now, having made the decision to file a rate

1 increase application for its MPS division, the Company is requesting that the Commission
2 allow it to abandon traditional regulatory practices and to retain certain merger savings for an
3 unlimited period. This proposal is unfair and inequitable to Aquila/UtiliCorp's MPS gas
4 customers, who deserve the full reflection of Aquila's L&P merger savings in the rates they
5 will pay as a result of the instant rate proceeding. This is particularly true in the context of
6 Aquila/UtiliCorp's current request to increase gas rates for its MPS customers.

7 Q. What are "cost-based" rates?

8 A. The cost-based rate methodology means that a utility's rates are based on the
9 utility's actual costs, including operating expenses, depreciation, taxes and a return on rate
10 base. The utility's actual costs may be adjusted for various reasons before being reflected in
11 rates, but cost-based ratemaking means the utility's actual costs are the starting point of the
12 analysis. Setting rates on a hypothetical cost level, as the Company is proposing in this
13 proceeding, does not conform to cost-based ratemaking.

14 Q. How does the Company's merger savings sharing proposal violate cost-based
15 ratemaking principles?

16 A. Aquila/UtiliCorp has asked the Commission to ignore, for rate purposes, the
17 existence of 50% of certain purported merger-related savings. Acceptance of this proposal
18 would mean that the Company's MPS and L&P divisions' rates would be based upon a level
19 of expenses that are inflated above these divisions' actual cost levels.

20 Q. Has this Commission ever approved rates for utility companies that are not
21 consistent with cost-based ratemaking?

22 A. Yes, in unusual circumstances. The Commission has approved the use of
23 experimental alternative regulation sharing plans for Southwestern Bell Telephone

1 Company (SWBT) and Union Electric Company d/b/a AmerenUE (AmerenUE), which
2 allowed for a portion of any of these utilities' earnings above certain return on equity levels to
3 be paid out to customers in the form of annual credits, as opposed to being reflected in a
4 permanent rate reduction. This treatment resulted in customers potentially receiving some
5 benefit from ongoing expense reductions made by utilities, while avoiding the need for time-
6 consuming and expensive excess revenue complaint proceedings. Both the SWBT and the
7 AmerenUE experimental alternative regulation sharing plans are no longer in effect. At the
8 conclusion of both these plans, the Staff filed major excess revenues complaint cases, and
9 significant rate reductions ultimately occurred (one by a last minute settlement and one after
10 evidentiary hearings). The AmerenUE experimental alternative regulation plan proved to be
11 particularly contentious. The determination of the sharing credits for the year July 1, 1997 to
12 June 30, 1998 is on appeal to the Missouri Court of Appeals Western District.

13 A number of gas local distribution companies in Missouri have also operated under
14 sharing mechanisms in relation to their gas cost expense.

15 Q. Is Aquila/UtiliCorp's current proposal for merger savings sharing in any way
16 analogous to the sharing mechanisms previously approved for SWBT and AmerenUE?

17 A. No. Both of these utilities had a history of overearning from the Staff's
18 perspective at the time their incentive sharing mechanisms were put in place by the
19 Commission. Therefore, the effect of these incentive sharing plans was to trade off the
20 opportunity for annual rate credits for customers of these utilities in place of some amount of
21 permanent rate reductions. In contrast, Aquila/UtiliCorp is asking that the amount of
22 permanent rate increases for its customers be increased to allow it to recover a hypothetical
23 level of expenses that is greater than Aquila/UtiliCorp's actual costs of providing utility

1 service in Missouri. There is no apparent customer benefit that would be related to the
2 immediate benefits this scheme would create for Company shareholders. Aquila/UtiliCorp's
3 requested use of a hypothetical expense level to increase rates in Missouri is unprecedented.
4 It is also unfair and inequitable.

5 Q. Are other Staff witnesses addressing the matter of cost-based ratemaking?

6 A. Yes. Staff witness Featherstone is also addressing this subject matter in his
7 rebuttal testimony.

8 Q. Did Aquila/UtiliCorp pay an acquisition adjustment for the L&P properties?

9 A. Yes. I referenced in my direct testimony in this proceeding the Company's
10 response to Staff Data Request No. 381 from Case No. ER-2001-672, the Company's last
11 electric rate proceeding in Missouri, that stated that Aquila/UtiliCorp paid an acquisition
12 adjustment of approximately $108 million for the L&P properties at the time of the merger
13 closing. I have since become aware that the Company has adjusted the value of the L&P
14 acquisition adjustment since the last MPS rate proceeding, and the value of the acquisition
15 adjustment is now approximately $117 million on a total Company basis (Response to Staff
16 Data Request No. 518 in Case No. ER-2004-0034, Aquila/UtiliCorp's current electric rate
17 proceeding before the Commission).

18 Q. Is the Company seeking explicit rate recognition of the L&P acquisition
19 adjustment in this case?

20 A. No. However, if the Commission accepts Aquila/UtiliCorp's merger savings
21 proposal, the result will be indirect recovery of at least a portion of Aquila/UtiliCorp's
22 acquisition adjustment.

1 Q. Why will a proposal to share certain merger savings result in indirect recovery
2 of a portion of the Company's acquisition adjustment?
3 A. As previously discussed, the Company's merger savings sharing proposal will
4 result in rates based on a higher level of expense than that actually incurred by
5 Aquila/UtiliCorp. For financial reporting purposes, the increment of expense reflected in
6 rates higher than the Company's actual cost levels will be reflected as additional profit, and
7 will effectively result in a return of and return on a portion of the Company's acquisition
8 adjustment for the L&P properties.
9 Q. Will the amount of merger savings retained by Aquila/UtiliCorp under its
10 proposal allow the Company to fully recover the costs of the acquisition adjustment?
11 A. The Staff does not know. However, the Staff believes that acceptance of the
12 Company's merger savings sharing proposal will result in a recovery of a significant portion
13 of the acquisition adjustment.
14 Q. Please explain.
15 A. Under current financial reporting rules, Aquila/UtiliCorp is not required to
16 amortize its acquisition adjustment to expense unless its merger investment is judged to be
17 impaired in some fashion. Therefore, absent evidence of impairment, the cost of the
18 acquisition adjustment to the Company is the return on this investment.
19 In the current Aquila/UtiliCorp electric rate increase case, the Staff's recommended
20 pre-tax rate of return is 10.09%, based upon the mid-range return on equity (ROE)
21 recommendation of 9.14% made by Staff witness David F. Murray of the Financial Analysis
22 Department, with that ROE grossed up for taxes by a factor of 1.60. Applied to the
23 acquisition adjustment amount of $117 million, this results in an annual total Company

1 overall return requirement for the L&P acquisition adjustment of $11.8 million. This amount
2 should be compared to the amount of combined merger savings Aquila/UtiliCorp is proposing
3 it be allowed to retain in this case and Case No. ER-2004-0034 (the Company's current
4 electric rate proceeding) of approximately $6 million.

5 Q. Why did you use the Staff's recommended midpoint return on equity from the
6 Company's current electric proceeding of 9.14% in the above analysis, as opposed to the
7 midpoint return on equity recommended by the Staff in this gas rate proceeding of 9.22%?

8 A. For two reasons: 1) as discussed previously, most of Aquila/UtiliCorp's
9 merger savings would apply to its electric operations and not gas, and more of the acquisition
10 adjustment would be allocable to the Company's electric operations as opposed to its gas
11 operations; and 2) to be conservative, as the electric return on equity recommendation of the
12 Staff is slightly lower for Aquila/UtiliCorp's electric operations than it is for the gas
13 operations.

14 Q. Would indirect recovery of the acquisition adjustment through a merger
15 savings sharing proposal be applicable to Missouri operations only?

16 A. The Company's position is that all domestic divisions of Aquila/UtiliCorp
17 should allow sharing of L&P merger savings to account for the alleged benefits received by
18 these divisions in the reduction in post-merger corporate allocation factors applied to each
19 division. In fact, the Company requested authorization of a merger savings sharing scheme
20 related to the L&P merger from the Iowa Utilities Board (IUB) in a rate proceeding in 2002,
21 even though L&P has no Iowa operations.

22 Q. What was the IUB's response to this merger savings sharing request?

1 A. Aquila/UtiliCorp's rate application in Iowa was settled, with no reference to
2 Aquila/UtiliCorp's merger savings sharing proposal in the order from the Commission that
3 accepted the settlement.

4 Q. What is the significance of the Company's request in Iowa for L&P merger
5 savings sharing?

6 A. The significance of this request in Iowa is that Aquila/UtiliCorp is implicitly
7 admitting that its position is that indirect cost responsibility for L&P merger costs should not
8 be isolated solely to Missouri. This should be taken into account when comparing the
9 Missouri only amount of requested merger savings noted above ($6 million) with the Staff's
10 calculation of the total Company amount of return on the L&P acquisition adjustment
11 ($11.8 million).

12 Q. What are the Staff's overall conclusions regarding the relationship of the
13 Company's merger savings sharing proposal to the acquisition adjustment and other merger
14 costs?

15 A. The Staff believes that Aquila/UtiliCorp's merger savings sharing proposal
16 would allow it to earn a significant indirect return on the L&P acquisition adjustment. Given
17 the past traditional practice of this Commission to deny direct recovery of acquisition
18 adjustments, the Staff believes the Commission should consider this fact in assessing the
19 Company's extraordinary proposal to share merger savings in this proceeding.

20 Q. Is the Staff's position on Aquila/UtiliCorp's merger savings sharing proposal
21 dependent solely on that proposal's impact of allowing indirect acquisition recovery?

1 A. No. The Staff would be opposed to the Company's merger savings proposal
2 even if no acquisition adjustment existed for the L&P transaction, for the additional reasons
3 stated in my and other Staff witnesses' testimony on this issue.

4 Q. At page 3 of his direct testimony, Mr. Siemek states "sharing in the savings
5 created by the merger provides an incentive for companies to create such savings for
6 customers by encouraging future mergers." Should this Commission be providing
7 "incentives" for merger and acquisition transactions?

8 A. In the Staff's opinion, no. There are two reasons for this position:
9 1) Aquila/UtiliCorp is effectively out of the merger and acquisition business at this time, so
10 there is no reason to reward Aquila/UtiliCorp to engage in an activity that it has indicated it
11 will not engage in; and 2) more generally, the Staff believes that the Commission should
12 neither encourage nor discourage merger and acquisition transactions for Missouri utility
13 companies.

14 Q. Why is the Company not involved in merger and acquisition activities at this
15 time?

16 A. Over the last 15 years or more, Aquila/UtiliCorp has been engaged in an
17 aggressive merger and acquisition program, both in the U.S. and internationally. However,
18 due to the Company's recent financial difficulties, it is the Staff's understanding that
19 Aquila/UtiliCorp has suspended any merger and acquisition activity for the time being.
20 (Deposition of Vern J. Siemek, pages 21-22). Given this, there are no merger and acquisition
21 activities on the horizon for Aquila/UtiliCorp to be "incented" to enter into.

22 Q. If the Company were still involved in merger and acquisition activities, would
23 the Staff's view on this matter change?

1 A. No. The Staff believes the Commission should neither encourage nor
2 discourage mergers and acquisitions. Companies engage in these activities primarily in
3 support of shareholder interests, and it is my understanding that the Commission is required to
4 approve such transactions unless a finding of "public detriment" is made by it. There is no
5 requirement that the Commission encourage transactions that may benefit shareholders but are
6 a detriment to ratepayers. It is the Staff's position that acquisition adjustments are a public
7 detriment.

8 In addition, even merger and acquisition transactions that may ultimately result in
9 lower cost of service and do not involve the recovery of an acquisition adjustment from
10 ratepayers can have negative impacts in other areas, such as schemes based on non-cost based
11 rate regulation. Further examples of this are, it is common for utility employee levels to
12 decline after a merger, and mergers may result in the transfer of some existing Missouri utility
13 operations to other jurisdictions. For these reasons, the Staff recommends that the
14 Commission adopt an attitude of overall neutrality toward merger and acquisition transactions
15 rather than to seek to either encourage or discourage merger and acquisition transactions.

16 Q. At pages 17-18 of his direct testimony, Mr. Siemek cites as support for the
17 merger savings sharing proposal a belief that the Company has "realized" very little or none
18 of the alleged L&P merger savings over the last three years. Is this true?

19 A. No. To the extent the Company has achieved a level of savings from the L&P
20 transaction over the last three years, Aquila/UtiliCorp has fully "realized" the savings,
21 because shareholders have been the sole beneficiaries of the savings so far. Mr. Siemek is
22 making a claim that if non-merger factors prevent an overall increase in Company earnings
23 even while merger savings occur, then the merger savings were not "realized." This is a truly

unique position. Aquila/UtiliCorp would have the Commission in effect "guarantee" a certain level of income to a utility after a merger/acquisition, or in the alternative order extraordinary ratemaking schemes for the benefit of the utility shareholders, such as merger savings sharing. Even the SWBT and AmerenUE experimental alternative regulation plans were not guarantees of certain earnings levels to SWBT and AmerenUE.

Q. What factors allegedly caused Aquila/UtiliCorp to fail to "realize" L&P merger savings?

A. On page 3 of his direct testimony, Mr. Siemek states "[c]ost increases and industry conditions unrelated to the merger have thus far prevented Aquila from realizing those benefits." More specifically, at pages 17-18 of his direct testimony, Mr. Siemek cites delays in achieving merger savings compared to the Company's original estimates of when savings could be achieved. He also states "rapid changes in personnel and cost levels precluded the significant effort and level of accuracy of costs needed to pursue rate relief" (page 17, line 21 to page 18, line 1). The Staff believes this statement is a clear reference to a belief that Aquila/UtiliCorp's financial problems in 2002 caused a decision not to file for increased rates for its Missouri divisions at that time, thus leaving the Company's earnings at a depressed level.

Q. Are these relevant considerations to the Commission in reviewing the Company's merger savings sharing proposal?

A. Not at all. Neither the Company's failure to achieve merger savings as fast as it had projected, nor Aquila/UtiliCorp's recent financial difficulties (entirely related to its non-regulated operations), are in any way the Commission's or the Company's customers' obligation to solve. Proposing an extraordinary sharing of merger savings on account of

1 factors such as these would place an inappropriate burden on the back of the Company's
2 captive customer base.

3 Q. At page 20 of his direct testimony, Company witness Siemek sponsors a
4 proposal to devote half of the L&P merger savings to be retained by Aquila/UtiliCorp under
5 its merger savings sharing proposal to a low-income customer assistance program. Does the
6 Staff have a position on this proposal?

7 A. Yes. While the Staff encourages utilities to consider the needs of low-income
8 customers in their policies and donation practices, the Staff cannot support a proposal to
9 increase general customer rates by imputing hypothetical expenses into cost of service,
10 regardless of claimed benefits to low-income customers.

11 Q. Mr. Siemek appears to portray the Company's merger savings sharing proposal
12 as actually benefiting customers on a 75/25 basis, taking into account the half of
13 Aquila/UtiliCorp's share of merger savings that will be devoted to low-income customer
14 programs. Is this view accurate?

15 A. No. If the Company's merger savings sharing proposal were adopted, any
16 additional monies devoted by Aquila/UtiliCorp to low-income customer resources would
17 logically have an impact of reducing the Company's bad debt expense. If this occurs, and the
18 Company's actual bad debt expense is then lower than the rate allowance for that item, the
19 Company's earnings levels will increase (all other factors held equal).

20 Q. Does this conclude your rebuttal testimony on merger savings sharing?

21 A. Yes, it does.

Summary of Synergy Benefits, net of Costs to Achieve

UtiliCorp/Saint Joseph Light and Power

(Dollars in Current 000's)

	2001	2002	2003	2004	2005	First Five Full Years Total	Average Years 1-5	2006	2007	2008	2009	2010	Years 6-10 Totals	Average Years 6-10	Ten Full Years Totals	Ten Full Years Average
I Operating Costs Current Dollars																
1 Dispatching/Generation Savings See I.1	$ 3,820	$ 4,358	$ 5,196	$ 6,021	$ 6,687	$ 26,082	$ 5,216	$ 7,817	$ 6,502	$ 7,274	$ 6,557	$ 5,733	$ 33,883	$ 6,777	$ 59,965	$ 5,997
2 General & Administrative Savings See I.2	$ 5,193	$ 5,599	$ 5,739	$ 5,882	$ 6,029	$ 28,442	$ 5,688	$ 6,180	$ 6,334	$ 6,493	$ 6,655	$ 6,822	$ 32,484	$ 6,497	$ 60,926	$ 6,093
3 Distribution Savings	$ 1,385	$ 1,821	$ 1,965	$ 2,014	$ 2,064	$ 9,249	$ 1,850	$ 2,116	$ 2,169	$ 2,223	$ 2,279	$ 2,336	$ 11,122	$ 2,224	$ 20,370	$ 2,037
4 Transmission Savings	$ 315	$ 548	$ 562	$ 576	$ 590	$ 2,591	$ 518	$ 605	$ 620	$ 636	$ 652	$ 668	$ 3,180	$ 636	$ 5,772	$ 577
5 Conversion to UtiliCorp Benefits See I.5	$ 1,996	$ 3,022	$ 2,976	$ 3,401	$ 3,626	$ 15,021	$ 3,004	$ 3,876	$ 4,152	$ 4,454	$ 4,728	$ 5,003	$ 22,213	$ 4,443	$ 37,234	$ 3,723
6 Total O&M	$ 12,709	$ 15,348	$ 16,437	$ 17,894	$ 18,997	$ 81,385	$ 16,277	$ 20,594	$ 19,777	$ 21,079	$ 20,870	$ 20,561	$ 102,882	$ 20,576	$ 184,267	$ 18,427
II Capital Savings (Costs):																
1 Depr - Interconnect/SCADA/T&D See II 1	$ (285)	$ (330)	$ (324)	$ (318)	$ (313)	$ (1,570)	$ (314)	$ (307)	$ (302)	$ (296)	$ (290)	$ (330)	$ (1,525)	$ (305)	$ (3,095)	$ (310)
2 Amort of Transaction/Transition Costs	$ (1,509)	$ (1,509)	$ (1,509)	$ (1,509)	$ (1,509)	$ (7,545)	$ (1,509)	$ (1,509)	$ (1,509)	$ (1,509)	$ (1,509)	$ (1,501)	$ (7,537)	$ (1,507)	$ (15,082)	$ (1,508)
3 Return on Interconnect SCADA /T&D	$ (896)	$ (897)	$ (841)	$ (786)	$ (731)	$ (4,152)	$ (830)	$ (677)	$ (624)	$ (571)	$ (519)	$ (463)	$ (2,854)	$ (571)	$ (7,006)	$ (701)
4 Return on Transaction/Transition Costs	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
5 Total Capital Savings (Costs)	$ (2,690)	$ (2,736)	$ (2,674)	$ (2,613)	$ (2,553)	$ (13,267)	$ (2,653)	$ (2,493)	$ (2,435)	$ (2,376)	$ (2,318)	$ (2,294)	$ (11,916)	$ (2,383)	$ (25,183)	$ (2,518)
															$ -	$ -
III Total Synergies, net of Cost to Achieve	$ 10,019	$ 12,612	$ 13,763	$ 15,281	$ 16,443	$ 68,118	$ 13,624	$ 18,101	$ 17,342	$ 18,703	$ 18,552	$ 18,267	$ 90,966	$ 18,193	$ 159,084	$ 15,908
IV Enterprise Support Functions Allocated (In) Current Dollars																
1 SJLP Direct Costs transferred to ESF See I.2	$ 2,292	$ 2,350	$ 2,409	$ 2,469	$ 2,530	$ 12,050	$ 2,410	$ 2,594	$ 2,659	$ 2,725	$ 2,793	$ 2,863	$ 13,633	$ 2,727	$ 25,683	$ 2,568
2 SJLP Direct Costs transferred to IBU	$ 922	$ 1,212	$ 1,308	$ 1,341	$ 1,374	$ 6,157	$ 1,231	$ 1,409	$ 1,444	$ 1,480	$ 1,517	$ 1,555	$ 7,404	$ 1,481	$ 13,561	$ 1,356
3 Support Functions Allocated (In)	$ (12,375)	$ (12,685)	$ (13,002)	$ (13,327)	$ (13,660)	$ (65,049)	$ (13,010)	$ (14,002)	$ (14,352)	$ (14,710)	$ (15,078)	$ (15,455)	$ (73,597)	$ (14,719)	$(138,645)	$(13,865)
4 Net Allocations (costs) savings to SJLP	$ (9,161)	$ (9,123)	$ (9,265)	$ (9,517)	$ (9,755)	$ (46,842)	$ (9,368)	$ (9,999)	$ (10,249)	$ (10,505)	$ (10,768)	$ (11,037)	$ (52,559)	$ (10,512)	$ (99,401)	$ (9,940)
V Total Synergies, net of Costs to Achieve and Allocated Costs	$ 858	$ 3,489	$ 4,478	$ 5,764	$ 6,688		$ 4,255	$ 8,101	$ 7,093	$ 8,198	$ 7,784	$ 7,230		$ 7,681		
VI Premium Costs																
1 Return on Premium See IV:1	$ (10,203)	$ (9,941)	$ (9,680)	$ (9,418)	$ (9,156)	$ (48,399)	$ (9,680)	$ (8,895)	$ (8,633)	$ (8,371)	$ (8,110)	$ (7,848)	$ (41,857)	$ (8,371)	$ (90,256)	$ (9,026)
2 Amortization of premium	$ (2,302)	$ (2,302)	$ (2,302)	$ (2,302)	$ (2,302)	$ (11,510)	$ (2,302)	$ (2,302)	$ (2,302)	$ (2,302)	$ (2,302)	$ (2,302)	$ (11,510)	$ (2,302)	$ (23,020)	$ (2,302)
3 Reflect non-tax deductibility of premium	$ (1,535)	$ (1,535)	$ (1,535)	$ (1,535)	$ (1,535)	$ (7,673)	$ (1,535)	$ (1,535)	$ (1,535)	$ (1,535)	$ (1,535)	$ (1,535)	$ (7,673)	$ (1,535)	$ (15,347)	$ (1,535)
4 Total Premium cost	$ (14,040)	$ (13,778)	$ (13,516)	$ (13,255)	$ (12,993)	$ (67,582)	$ (13,516)	$ (12,731)	$ (12,470)	$ (12,208)	$ (11,946)	$ (11,685)	$ (61,041)	$ (12,208)	$(128,623)	$(12,862)
VII SJLP share of premium costs	$ (7,020)	$ (6,889)	$ (6,758)	$ (6,627)	$ (6,497)		$ (6,758)	$ (6,366)	$ (6,235)	$ (6,104)	$ (5,973)	$ (5,842)	@50%	$ (6,104)		
VIII Synergies, net of 50% of premium (Line V less VII)	$ (6,162)	$ (3,400)	$ (2,280)	$ (864)	$ 192		$ (2,503)	$ 1,736	$ 858	$ 2,094	$ 1,811	$ 1,388		$ 1,577		

See Appendix VJS-A for details of calculations.

Shared synergies Master 1011 NHome Inflated.xls

Prepared October 12, 1999

VJS-1
ANNUAL DETAIL

Schedule 1