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In the Matter of Missouri-American Water Company's Tariff to Revise Water and Sewer Rate Schedules.) Case No. WR-2003-0500

KEVIN A. THOMPSON, Presiding,
DEPUTY CHIEF REGULATORY LAW JUDGE.

CONNIE MURRAY,
BRYAN FORBIS,
ROBERT M. CLAYTON, III,
COMMISSIONERS.

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P R O C E E D I N G S

JUDGE THOMPSON: Why don't we just quickly do an abbreviated version of the oral entries of appearance so I can make sure I know who's here and so our listeners and viewers know who's here. Why don't we begin with you, Ms. O'Neill?

MS. O'NEILL: Yes. Ruth O'Neill with the Office of the Public Counsel. John Coffman from my office will also be appearing.

JUDGE THOMPSON: Thank you.

MR. CONRAD: Stu Conrad, AG Processing.

MR. ENGLAND: Trip England on behalf of the company, and my partner Dean Cooper should be here later.

MR. KRUEGER: Keith Krueger for the Staff.

JUDGE THOMPSON: Thank you.

MS. VUYLSTEKE: Diana Vuylsteke for Missouri Industrial Energy Consumers.

JUDGE THOMPSON: Thank you. Okay. Do we have a report on the settlement of the rate design issues? If you'd like to defer this to later, we can do that.

MR. ENGLAND: Without a great deal of effort, I think I can give you an update.

JUDGE THOMPSON: That would be great.

MR. ENGLAND: The parties, I believe, have an agreement in principle. A draft of the agreement is being circulated. It is our hope and desire to have that filed before the lunch hour and possibly make a presentation then at 1:30 to the Commission.

JUDGE THOMPSON: That would be great. Thank you, Mr. England.

Anyone else want to weigh in on that topic?

(No response.)

JUDGE THOMPSON: Okay. Why don't we move on, then, to cash working capital? I think our first witness then would be Mr. Grubb; is that correct?

MR. ENGLAND: That's correct.

JUDGE THOMPSON: Take your seat, Mr. Grubb. I'll remind you you're still under oath. You may inquire, Mr. England.

MR. ENGLAND: Thank you.

EDWARD GRUBB, having been previously sworn, testified as follows:

DIRECT EXAMINATION BY MR. ENGLAND:

Q. Mr. Grubb, I believe you've filed direct, rebuttal and surrebuttal testimony that has been marked as Exhibits 1, 41, and 83, and I believe in your direct and rebuttal you address the issue of cash working capital; is that correct?

A. That's correct.

Q. Okay. And I think you indicated to me before you got on the witness stand that you may have an additional correction to testimony or schedule that you have not previously made?

A. Yeah, just one minor correction. It's in my rebuttal testimony, which is Exhibit 41. It's on Schedule EJG-2, page 1 of 3. At the lower left-hand corner it says plant in service 1/1/2002. It should be 1/1/2003.

JUDGE THOMPSON: Okay. What schedule was that again?

THE WITNESS: EJG-2.

JUDGE THOMPSON: Okay.

THE WITNESS: My rebuttal testimony, page 1 of 3.

JUDGE THOMPSON: Yes, sir.

THE WITNESS: On the lower left-hand corner, you see a plant in service 1/1/2002. It should be 1/1/2003.

JUDGE THOMPSON: Great. Thank you.

BY MR. ENGLAND:

Q. Is that the only correction that you're aware of?

A. Yes, sir.

MR. ENGLAND: I think then I'll tender the witness for cross-examination on the issue of cash working capital. It's my understanding that his testimony has already been received into evidence.

JUDGE THOMPSON: Let me check on that. Yes, Mr. Grubb's testimony has been received, and as I indicated we would start with questions from the Bench rather than cross-examination unless, Commissioner, you would rather defer.

COMMISSIONER MURRAY: Yes, I would rather defer. Thank you.

JUDGE THOMPSON: All right. Well, then, we will go ahead with the normal cross-examination order. Ms. Vuylsteke? I see she has stepped out.

Mr. Conrad?

MR. CONRAD: No questions, your Honor.

JUDGE THOMPSON: Mr. Finnegan?

MR. FINNEGAN: No, questions.

JUDGE THOMPSON: Ms. O'Neill?

MS. O'NEILL: No questions.

JUDGE THOMPSON: Mr. Krueger?

MR. KRUEGER: Yes, your Honor. Thank you.

CROSS-EXAMINATION BY MR. KRUEGER:

Q. Good morning, Mr. Grubb.

A. Good morning.

Q. I have just a couple questions for you. First, in regard to the cash working requirement associated with management fees?

A. Yes, sir.

Q. To whom do you pay those management fees?
A. Those are paid to American Waterworks Service Company, Incorporated.
Q. Is that an affiliate?
A. Yes, it is.
Q. You pay those fees in advance?
A. That's correct.
Q. If you didn't have this affiliate to provide these services, they would be provided in house by employees or else by consultants; is that correct?
A. The services would be provided by someone, whether it was a consultant or in house. It would have to be one of the two, yes.
Q. And in such circumstances, they wouldn't -- the fees wouldn't ordinarily be paid in advance, would they?
A. If it was a consultant, I would determine that, if it was not paid in advance, the cost of those fees would be higher because those consultants are required to fund their operation. So, for example, if the service company was not billed in advance, the service company charges would be higher, therefore --
Q. My question was just whether they would ordinarily be paid in advance?
A. I don't know that answer. It could be. It may not be.

Q. Okay. If they were -- if they were provided by employees, they would not be paid in advance, would they?
A. That's true. It would be based upon the payroll lag, and that's in our case right now, yes.
Q. So you're asking the Commission for a million dollars of working capital so you can pay an affiliate in advance?
A. The million dollars working capital is predicated upon the payment of the service company's bills in advance, and that goes in line with that service company bill being lower in cost because it is paid in advance. If it was paid in arrears, the service company bill would be higher because the service company would be incurring carrying costs of its own.
So it's just simply a tradeoff, whether you pay a higher management fee cost or pay -- or have a higher rate base because of the lag in the management fee. It's one or the other.
Q. My question was whether you're asking for including about a million dollars in cash working capital requirement so you can pay an affiliate in advance; is that correct?
A. Based upon the contract, yes.
Q. Okay. Have you read the surrebuttal testimony of Ms. McKiddy with regard to cash working capital issues?

A. Yes. Yes, I have.
Q. Specifically the excerpts from reports and orders of the Commission that appear on pages 3 and 4 of her rebuttal testimony, have you read that?
A. The reports and order that are 20 to 25, 30 years old, yes.
Q. I think that's about the age, yes. It's the ones that are shown on pages 3 and 4.
A. Yes.
Q. Would you agree that in those excerpts, the Commission stated that depreciation on deferred taxes would be excluded from the determination of cash working capital?
A. That's true.
Q. Are you aware of any decisions by this Commission in which depreciation on deferred taxes were included in the determination of cash working capital?
A. Not by this -- not by this Commission, but other Commissions have done so.
Q. My question was about this Commission.
A. This Commission, yes.
Q. Are you aware of any Missouri court decision which authorized or required depreciation and deferred income taxes to be included in the determination of cash working capital?
A. I don't think I am.

MR. KRUEGER: Okay. Thank you. That's all the questions I have, your Honor.

JUDGE THOMPSON: Questions from the Bench, Commissioner Murray?

COMMISSIONER MURRAY: Thank you.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good morning, Mr. Grubb.

A. Good morning.

Q. Regarding the issue of depreciation on deferred taxes, in your testimony, your rebuttal testimony, on page 6, you indicate there, beginning at line 6, that the investors supply cash to fund investment in the new plant such as mains, hydrants, pumping equipment, et cetera. Depreciation expense represents the recovery of those cash expenditures from customers who are receiving the service.

Can you tell me how depreciation expense represents recovery of cash expenditures?

A. Depreciation expense is a recovery of a cash expenditure. The company at one point made a $10,000 investment in a piece of equipment. Depreciation expense is built into the revenue requirement, so we recovered cash for that investment from the ratepayers through the depreciation expense.

Q. But depreciation expense is not ordinarily tied to expenditures, is it, to expenditures for current infrastructure?

A. Depreciation expense is a result of the capital expenditure. When a piece of equipment or capital expenditure is made, the company begins accruing or recording depreciation expense on its books.

Q. But the depreciation expense you're talking about here representing the recovery of cash expenditures would be depreciation expense on other infrastructure, would it not?

A. It represents all -- all infrastructure, whether it's mains, hydrants, vehicles. It's everything.

Q. But your current expenditures are not yet in --

A. The rates?

Q. -- in the depreciation that is being expensed; is that --

A. That's true. Any capital expenditure for our St. Louis district made after January 1 of 2000 -- January 1 of 2001 has not been recovered in rates yet, and anything after, I believe it was April 2000 for the old Missouri-American, any expenditure there, any depreciation expense is not being recovered in rates.

Q. And what you're asking for in terms of treatment of depreciation expense and deferred taxes relating to cash working capital is different than the treatment that the Commission has given the company in the past; is that correct?

A. That's correct. Really the issue here is, at any point in time, if you measure rate base, and that would include utility plant in service, your accumulated depreciation, your deferred taxes and all aspects of the rate base, at that point when you pick a point in time -- and that's how rates are set is a point in time; in this case it will be as of the true-up, November of 2003 -- that balance that's being reduced in rate base for the accumulated reserve and the deferred taxes, because of the lag in the collection of revenues from customers, that balance includes the accumulated depreciation and depreciation expense and deferred taxes that have not been collected from the ratepayers because of the revenue lag in the -- in the working capital calculation.

So, therefore, what our proposal is, by assigning a zero lag in the working capital calculation, you're recognizing that that accumulated reserve and that deferred tax balance has not all been collected from ratepayers at that point in time in the setting of rates.

We could have done it one of two ways. We could have incorporated it the way we did in working capital or we could have in rate base adjusted the accumulated reserve balance and the deferred tax balance in the rate base by reducing it, thus increasing the rate base to the appropriate level to reflect the fact that we have not recovered from our customers all of that balance that's on the books.

Q. And the alternate way that you could have done it, has that ever been approved by the Commission?

A. To my knowledge, I don't know if that's ever been attempted in that methodology. In my years of looking at lead lag studies and working capital, it's always been done through the working capital by assigning a zero lag to those two components.

Q. Perhaps you could help me a little bit by going over your Schedule EJG-2.

A. Okay. Schedule EJG-2 is a three-page schedule. It's a very -- I tried to, you know, focus on one asset that gets placed into service at January 1 of 2003. It's a $10,000 asset, and that rates would be set at that point in time. The asset is depreciated over a two-year life. So on the first page, page 1 of 3, you see that line, that line that's going through the graph, that would be the recording of depreciation on that asset.

On page 2 of 3 it shows that the first collection, because of the revenue lag -- and I'm going to use the St. Louis district's revenue lag of about 63 days. The first collection from our ratepayers for depreciation occurs on March 4th, and so that collection from our customers will occur all the way out to March 4th of 2005.

Q. I'm sorry. I need to ask you, why is 15,000 reflected there on page 2 as a cost of the asset?

A. Okay. That should be 10,000. I'm sorry. Okay. So on page 2 of 3 you show -- on page 1 you show the recording of depreciation expense and it's evenly, straight line over the life of asset. So at the end of 2004, you have a rate base of zero, $10,000 of investment. Recorded depreciation is 10,000, so there's no rate base -- no rate base at that point. The recording or the collection of the dollars from the ratepayers occurs on a 63-day lag. So the final collection will actually occur out in 2005.

Okay. When you go to page 3 of 3, I've combined basically the two lines cutting through the graph. The top line cutting through the graph is the recording of the depreciation. The line below that is the collection of that -- those dollars from the ratepayers. If you did a rate base at 12/31/03, which is in the middle of the graph, you'll see that the rate base on a traditional approach would have been $10,000 of the asset minus $5,000 for the accumulated depreciation that would have been recorded. So the rate base was 5,000.

Because you've only collected from your ratepayers at 12/31/03, 4,137, you really have a mismatch, so you have to in some way recognize that there's another 837 -- $863 of rate base that must be properly reflected to show that the capital invested by the company matches the rate base investment. Okay? So you need to increase rate base by the $863 to properly reflect the fact that the accumulated reserve at 12/31/03 does not reflect the fact that we collected the dollars from the ratepayers at that point.

Q.   And over time in the past, this mismatch has occurred and not been corrected, is that --

A.   By not including either an adjustment to the reserve to show that the reserve reflects not all dollars collected from ratepayers or through a working capital adjustment of putting the zero lag in the -- for those two items of depreciation in deferred taxes, there is a mismatch between rate base and capital on which the company can earn upon.

Q.   And my question is, in past rate cases that mismatch has --

A.   Has always occurred, yes.

Q.   And then in terms of the affiliate that you pay in advance, if you were taking, and I -- I haven't read it recently enough to remember what it is you're paying that affiliate for, but if you were taking whatever it is from a non-affiliate, how likely -- how likely is it that you would be paying in advance?

A. I don't know. I mean, it's probably -- I'll say you wouldn't be paying in advance, but you would be paying a higher cost for those services, because if the third party would have to be funding their expenditures because they're now providing services and not getting paid for it, so within their cost structure they would have to charge you more because they don't have the money to pay for their services before you pay for them.

Q. Do you have any empirical evidence that would substantiate that?

A. Well, I think if you just took an average monthly -- monthly amount and assuming you paid in arrears for 30 days at a time and did 15 -- a payment lag of 15 days beyond that, you can calculate an estimate of what that amount would be. But I have not ever seen any empirical study on it. A study can be done of what the impact would be.

Q. But you're making an assumption that a non-affiliate would be charging more?

A. Assuming both cost structures are exactly the same, they would have to be. They would have to. Plus the the -- the non-affiliate would have a profit factor built in, and the service company is a cost-based organization. We bill out the cost. There is no -- there is no profit built in.

COMMISSIONER MURRAY: All right. Thank you.

JUDGE THOMPSON: Commissioner Clayton?

QUESTIONS BY COMMISSIONER CLAYTON:

Q. How do we know that there's no profit built into that cost with the affiliate?

A. I believe it's in the contract that whatever the costs are of providing that service, that is what is billed out.

Q. Okay. So it's in the contract between the -- between Missouri-American and the affiliate providing the service?

A. I believe that the costs are -- I have to read through it, but historically knowing that, and one time me working for the service company, we incur costs and that's what's billed out. Nothing more above what our actual costs are are billed out.

Q. Does Staff have an opportunity to review those affiliate costs and determine or verify that they are the actual costs for the affiliate?

A. Yes.

Q. They do have the ability to do that?

A. And they've looked at numerous costs in this case.

Q. Okay. I need some help with this issue in trying to understand exactly how it works. On the cash working capital issue, not the depreciation and not the deferred taxes issue, but on the lag associated with expenses, in reading the testimony, it is not clear to me whether there is an overall dispute as to all sorts of expenses or if it just relates to management fees.

Can you explain where the dispute is with regard to the cash working capital, outside of depreciation and deferred taxes?

A. Okay. There's only basically those two disputes. One is the management fee lag, and the other is the depreciation and deferred taxes. Everything else, the company has accepted the Staff's calculation.

Q. So all other expenses with regard to cash working capital, there's an agreement we're just talking the management fees, which, I guess, includes some affiliate services; is that correct?

A. That's true.

Q. Okay.

A. Yeah, the Staff's lag is -- is a positive 42.3 days, and the company's lag is a negative --

Q. 4.13 days?

A. -- 4.13 days. Yes.

Q. Right. I got that. On this management fees portion, how much money are we talking about here between the two positions?

A. In rate base impact, it's approximately $1.04 million.

Q. And can you explain to me in terms of time on these management fees how -- what is the difference in time? I understand the plus 42.3 days is what Staff's position is and a negative 4.13, but can you explain that to me in real time?

A. I think when you say real time, I'm not sure I'm following you.

Q. Explain that to me. I don't understand it.

A. Okay. Basically, Staff's position is the service company performs services -- and we'll just do a real basic example. Month of June, service company performs services for the -- for Missouri-American, and at the end of June they bill -- they bill the company for those services. The company pays, say, on July 15th. So you have a 30-day -- what's called 30-day service period. You cut that in half. So the average service period that you have for the month of June is 15 days. Then you have about another 15 to 20 days before the bill's paid after the end of June.

Q. And this relates to management fees?

A. Management fees. That's about 40 days.

Q. Okay.

A. The company's position is, if you look at the invoice, the invoice comes down to an amount billed for the month of June, but then we subtract out what was prepaid for the previous bill. So basically what we're saying is the month of June was paid in advance or right near the beginning of the month, and then they add on what the estimated bill would be for the month of July. Okay?

Q. So in the negative 4.13 days and the plus 42.3, it's the company's position that the bill has to be paid four days earlier than when the services are provided?

A. It's an average, yes, basically.

Q. An average? Okay. And it's the Staff's position that it would generally allow for 42.3 days for those fees to be paid?

A. That's correct.

Q. Okay. Can you tell me if this Commission has ever authorized on this issue such a prepayment position?

A. For as long as I can go back the last three rate cases, the Staff and -- this is a change -- this is another change from the last case. The Staff adopted a -- I believe, a -- the 4.13 days in the last case. That was the last Missouri-American case, the 2000-281 case.

Q. So in that case, Staff agreed with approximately the average of negative 4.13 or roughly days in the last rate case?

A. In fact, that was taken from their file case in the last case, yes.
Q. Okay. In the 281 case, that was -- was that St. Louis County alone or was that the old Missouri-American case?
A. The old Missouri-American case.
Q. Okay. How did management fees work in that case? Did it work exactly the same way? Were the same service companies in existence at that time?
A. Yes.
Q. Do you recall the dollar amount in that case, considering it was pre-merger days?
A. No, I do not.
Q. All right. Would you have a guess as to an estimate?
A. Well, a lot of changes have occurred since that last case, you know. We now have the call center, and we have the shared service center functioning today that was not functioning.
Q. How are those different? How are -- I understand the call center, but the shared services, how is it different now than it was then?
A. Back then Missouri-American had their own accounting department, had their own staff accountants, had their own payroll department. You know, they had an

accounts payable procurement department.

Q. So what management fees were payable in the last rate case?

A. Management fees associated with customer billing, water quality administration, engineering, some rates and planning functions were there also.

Q. But significantly less than the number and quantity, the quantity of services that are being provided now, correct?

A. It was less back then. It's more now, yes.

Q. So there's more shared services now. What would be an example or several examples of some of the new services that are being provided through the shared services affiliate?

A. They prepare and do all payroll payments. They do all the bank reconciliations. They do what's basically the procurement-to-pay function. They issue the purchase orders to the vendors who the company is using. They pay all -- pay all invoices.

Q. And the company is much larger now than it was before, than in the last rate case?

A. When you say company, which company?

Q. Missouri-American.

A. Missouri-American? From the last 2000-281 case, that's correct.

Q. It's doubled in size?

A. Probably more than doubled.

Q. More than double. Okay. Okay. So we're talking a much larger amount of money to be authorized. I mean, it's much different now than it was back in the 281 case, would you agree?

A. When you say authorize, are you talking about the revenue requirement authorized or --

Q. The agreement by Staff in cash working capital in this lag and management fees. There are a significantly higher number of services that are being provided through management, and the company's much larger. There are more customers, more employees. There is a -- there's a vast difference between what was agreed to or what Staff's position was in the 281 case than what is going on in this case. Would you agree with that statement?

A. Yeah, in terms of the service company bill.

Q. So we're talking a million dollars in this one. We'd be talking about a significantly lower amount of money in the last case?

A. Yes, it would be lower. I just don't know what that -- what that difference would be as a result of increased costs.

Q. Okay. I started off asking you about the management or affiliate costs, the contract between

Missouri-American and the shared services center or the -- between Missouri-American and the shared services facility where the contract was based on a for-cost price, as opposed to having a cost plus type of billing mechanism?

A. That's correct.

Q. Can you explain to me how Staff is able to verify that the cost claimed by the affiliates is truly the cost on unregulated affiliates?

A. They have an opportunity to go in and request information on the costs. There's a report that has what all the costs are of each of the various functions within the service company, be it the call center, be it the shared service or the Vorhees corporate office, and those costs are some amount.

If you total all those up and compared it to what was billed to all the companies, then you would see that the numbers would agree. So there was nothing -- no add-on above the actual costs incurred by the company.

Q. Regarding depreciation and deferred taxes, I came in right in the middle of the cross-examination. Was it your testimony that the lag in depreciation and deferred taxes has been approved by the Commission in the past?

A. The prior Commission's decisions have excluded any depreciation and deferred tax in the calculation of the working capital.

Q. Okay. So if we were to approve this, would this be a first?

A. To my knowledge, yes.

Q. Okay. So this is a change from past rate cases?

A. That's correct.

Q. Okay. And what is the difference in position? I believe it's a $5 million, roughly, difference in rate base between parties?

A. Yeah, I have $5.055 million, yes.

Q. Okay. I got that. In this calculation and in your Schedule EJG-2, would it be appropriate in this analysis, since we're studying cash flows, to look at what cash is coming in from the prior period in that lag, from the prior case?

A. I'm not sure I'm following the question. Cash from the prior case?

Q. Well, we're doing a study, not on recouping the overall depreciation expense through rates. We're talking about remedying a lag at a point in time from when a rate is established with roughly 63 days passing, and we're trying to remedy that time lag on this issue; is that correct?

A. That's correct.

Q. So we're not talking about an overall

recoupement of depreciation expense. We're talking about fixing a problem with cash flows?
A. Fixing a problem with, really, rate base, stating rate base correctly for the company to earn upon.
Q. But we're dealing with cash flows, basically the lag in the money coming in, are we not?
A. That's correct.
Q. Okay. So we're dealing with a cash flow issue here?
A. That's right.
Q. When we study cash flows, shouldn't we take into consideration the amount of cash flows that the company is receiving for those 63 days on the prior set of rates in the prior case or for the prior period of time?
A. Those would have been built into the reserve. Anything collected prior, going back in time, would have been collected and reflected in the accumulated reserve as a reduction to the rate base so that the ratepayers are made whole.
Q. Well, let me give you -- maybe I'm not asking this question properly. If you look at page 3 of your Schedule EJG-2, do you have that up there?
A. Yes.
Q. This is the final compilation graph that you've got. And in -- the time period for this particular

example begins January 1, 2003 and it ends -- the plant is retired December 31, '04, but cash continues to come in all the way out to March 4th, 2005, for an extra two-month period.

My question is, in looking at the 63 days at the start, shouldn't we be taking into consideration the lag off the last case? In terms of cash, that money's going to be coming in. Shouldn't there be a reconciliation on these cash flows?

A. No, because the cash that you were collecting for that ended -- and I think I understand where you're coming from. The cash collection that ended at March 4th of 2003 was for the prior asset, and that cash collection that ended March 4th of 2003 completed the cycle for that prior asset. Now you're starting all over with a new asset, in this example.

Q. I understand, but we're just talking about cash flows. We're not talking about recouping the overall depreciation expense?

A. Well, I think the cash flows for the depreciation expense is tied to an asset which is tied to the accumulated reserve in the setting of rates along with the investment in that asset.

Q. So if we were to authorize what the company is asking here in this period of time between January 1, 2003 and March 4, 2003, the lag period at the beginning of the year from when plant in service is placed in service, theoretically the company is going to have cash flows from the prior rate case for a period of two months, and then, on March 4th, it will start to collect for cash flows for that same period of time on the new plant?

A. On the new plant and that first -- from January of '03 to March 4 of '03, that cash collection is for the previous asset that the customers were receiving the benefits for.

The whole issue is that there's a lag in the collection of any depreciation because of the revenue lag itself in the 63 days for St. Louis only, because it is shorter for the other districts, and that the reserve that is used to reduce rate base, that reserve at any point in time, because of this 63-day lag, is not properly estimated. We haven't collected all that reserve from the customers because of that lag in the revenue collection.

And that's what this third graph will show. It will show that it overlaid the first and the second, and it shows that the collection lag, collection of the depreciation comes after the recording of the depreciation expense, which creates a sort of, if you will, a mismatch in the accumulated reserve account that's being used to reduce rate base.

Q. Well, let me restate the question in this manner: Look to the end of the graph, the date of 12/31/2004, the end of the life of this particular plant in service. On -- let's assume that January 1, 2005, you start a new graph that we can't see, okay, a new plant in service, and you're going to have that same 60-day lag in the new graph that we can't see on the outside of this graph.

At that same time, you're still going to be collecting in terms of cash flows, not on recouping the overall depreciation expense, but in terms of having a steady cash flow, you're going to be receiving cash flows from this prior case, are you not?

So my question is, shouldn't there be a reconciliation of that cash flow coming in during that time? Your assumption is that there's no cash flow coming in. Well, really, there is on this issue.

A. There is, but that cash flow is relating to another asset. When you're setting rates, you're not going to have both assets in rate base. So you can't overlap the cash flow, because you can't overlap the assets, because you can't have the same two assets in service at the same time that are for the same function. One asset would go away; the other one would come on.

There is an overlap of the -- there really is an overlap of the cash flow. One will begin March 4th of

2003. The old asset, which is going, is gone, will be ending on March 3rd, 2003.

Q. But the rate that goes into effect on March 4, 2003 will be increased to make up for that supposed lag, correct?

A. On the old -- on the old asset.

Q. Well, in this example, the rate that goes into effect on March 4, 2003, will be a little higher beginning on March 4th to recoup that lag in Note No. 2, correct?

A. Well, the Notes 1, 2 and 3 actually center on the determination of proper rate base at 12/31/03, and really doesn't get into the end of the life of an asset and beginning of the life of an asset. I think the whole issue is what happens in the determination of rates set at a rate base of 12/31/03.

I mean, that's where I think I would like to center on more than the beginning of the graph or the end of the graph. If we were setting the rate base at 12/31/03, traditionally you'd have the $10,000 investment reduced by an accumulated depreciation of $5,000, and the graph shows that in -- in essence, we've only collected from our ratepayers 4,137 -- 4,137 of that depreciation expense.

Q. Theoretically, if we were to not approve this cash working capital issue, is it your testimony that the company would not recoup through depreciation its full investment in that particular plant?

A. The company would not earn upon the true regulatory rate base of it and its capital.

Q. Maybe I need to clarify. But in terms of the life of the plant, it would recoup its investment, correct?

A. Yes, that's correct.

Q. Okay. Now you're talking about a separate issue, and that's earn on rate base?

A. That's why this issue is a rate base issue only, that's correct.

Q. Right. How would this issue -- how does the issue become reconciled on the overall life of the plant and the amount of money that is recouped by the company through depreciation expense?

A. This issue would not affect that. The company's -- the depreciation rates are set. We put into rates those depreciation rates and we start recording it, you know, through that mechanism. What this simply is trying to do is to set a rate base and to recognize that you always have that lag in collecting that depreciation expense from the customers.

Q. You mentioned that -- I believe Commissioner Murray was asking you some questions, and you responded with regard to some dates and some examples regarding infrastructure replacement, and I think I wrote down the dates. You said any plant placed in service following January 1, 2001 is not included in rate base, correct? The same would be for roughly April 2000 on the old Missouri United Water.

A. That's true.

Q. I mean, is that a rough estimation?

A. Yeah.

Q. Now, they are included in rates through the ISRS right now?

A. On the infrastructure piece, that's correct.

Q. Okay. Are there parts of it that would not be included? How much non-infrastructure plant in service would there be here?

A. The rate base for the ISRS, I think, is approximately $25 million, and I think our rate base has gone up well in excess of that. I don't have the numbers, you know, right off the top of my head here, 50, 60, $70 million additional.

Q. Okay. And if we were to approve this, this would be a first that this Commission has ever done this?

A. That's correct.

COMMISSIONER CLAYTON: Okay. Thank you for your patience.

JUDGE THOMPSON: Chairman Gaw?

CHAIRMAN GAW: Thank you, Judge. I just have a few questions.

QUESTIONS BY CHAIRMAN GAW:

Q. Good morning.

A. Good morning.

Q. I'd like to focus just a bit on something that you just touched on in your testimony, and that is the affiliate transaction rule that -- I'd like to know just generally when Staff requests information about the costs that may be charged by affiliates for services performed for Missouri-American, tell me generally what information is available to them in regard to determining what those costs are and how -- and whether or not they're appropriate.

A. In my direct testimony, I filed a cost allocation manual, and attached to that cost allocation manual is a -- is an Appendix F. It's a two-page -- two-page appendix.

Q. Okay. I'm there.

A. Okay. Page 1 of 2 shows a report that is available that, in this case, it's the expenses incurred by the Belleville lab. And if you look down, those are all expenses from labor to welfare expenses, contract services, insurance, janitorial and so forth. In the process, the company can show this total cost -- and it's to be done by month or by year -- how much of these total costs are allocated to each company within the American system, and that's what gets billed.

So in looking at these costs, the Staff has an opportunity to say, well, what makes up these costs? They can actually request the transactions of the company in that respect.

Q. When they -- and when you say the transactions of the company, which company are you talking about?

A. I'm sorry. The service company.

Q. And can they -- what kind of detail can they get in that request?

A. For example, I'll just pick one out. Office -- well, office supplies and administrative supplies. The service company makes expenditures similar to what Missouri-American makes for office supplies. You know, they pay a vendor called Boise Cascade to buy their office supplies. There are vouchers that are paid and invoices and checks are issued, and that's what gets recorded as a cost for the Belleville lab, and then that cost then is allocated to Missouri-American Water Company.

Q. And the invoices and those things are available to Staff?

A. Yes.

Q. Okay. How do they get -- how does that happen? Is that something that Missouri-American already has that they deliver over on a Data Request?

A. If the Staff requested it in a Data Request, give us all transactions for this object account, for this account for the Belleville lab, the company would request that information and get a report.
Q. From the Belleville lab?
A. Yes.
Q. Okay. So if Missouri-American requests information from an affiliate, is it generally given to them?
A. If that cost is being requested in rates by the company. If there's an affiliate that incurs costs that are not being passed along to Missouri ratepayers, then we probably would not request it.
Q. Okay. So is that -- is that a determination made by Missouri-American itself about whether to make the request of the affiliate?
A. It can be. We can request some information, and we may not receive -- I don't know. It just depends upon the request and what's being requested.
Q. Is there a general policy with Missouri-American about when they will or will not make a request of an affiliate for information that's requested in a rate case by staff of Missouri-American?
A. It's not a written policy, but I think -- through the years, I think the company believes that if it's

germane to the issue, such as requested in this case, you know, we're requesting recovery of costs -- you know, from our ratepayers for costs, you know, allocated to us by an affiliate, then we would get information for those costs to support them.

Q. Has there ever been a time when a request by Missouri-American of an affiliate for information has not been honored, to your knowledge?

A. Off the top of my head, I don't recall any. I think the first one is, should we go and request it, and from there --

Q. And if I understand you correctly, that -- that is a determination made by Missouri-American about whether to make the request of the affiliate for the information?

A. That would be the first step.

Q. Is there a step after that?

A. I mean, there may be instances that I don't recall that we may have requested -- for example, one of the requests was the -- in the rate case that the company objected to was the board minutes of American Waterworks. We talked to Vorhees about that and decided that we would not get that information, because there are no costs at American Waterworks that are passed down to Missouri-American.

Q. And Vorhees, would you -- for the record, who is Vorhees?

A. Vorhees is -- I'm sorry. Vorhees is the corporate office in New Jersey.

Q. Corporate office for whom?

A. American Water.

Q. Did the corporate office -- did Missouri-American request the information be given to it from the -- from your parent, from the parent of the corporation?

A. For the board minutes?

Q. Yes.

A. I don't know if we requested it per se. I know our legal counsel, in-house legal counsel David Abernathy had the discussions. I was not part of those discussions.

CHAIRMAN GAW: I think that's all I have. Thank you.

JUDGE THOMPSON: Thank you, Chairman. Commissioner Murray?

COMMISSIONER MURRAY: Thank you.

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. I hate to belabor this issue about depreciation expenses being included in cash working capital, but I really want to understand why it is you think they should be. And you made the comment earlier, I believe, that the collection comes after the recording. Did I hear you correctly?

A. Yes. There's a lag of 63 days. We record depreciation expense, you know, as soon as the asset goes into service, and there is an implicit 63-day lag in the collection of revenues from customers.

Q. So when you talk about collection, specifically, what are you calling collection of revenues for depreciation expense?

A. In the revenue requirement is the recovery of depreciation expense, and we recover that cash from our ratepayers for that expense.

Q. And the Staff's position, as I understand it, and the position that the Commission has taken in the past regarding this issue is that, because there is no cash transaction, there's no cash outlay, that this is not appropriate to include in cash working capital; is that right?

A. I think that -- I believe that's their position, yes.

Q. And ordinarily what would be included, the company would have to -- what would be included as an expense, the company would actually have to expend some money; is that correct?

A. The Staff refers to their study as a cash working capital. I just refer to it as a working capital calculation, and in that sense, the working capital is designed to generate a rate base addition, or in some cases it can be a reduction depending on the situation of the utility and the various leads and lags in expense and revenues. But the working capital calculation can take into consideration other items than just involving cash, payments of vouchers and so forth.

What this -- what the company's proposing is to -- as shown on page 3 of 3 of my rebuttal Schedule 2, that in the setting of a rate base, the reduction in rate base for the accumulated reserve, that reduction, all those dollars in that reserve have not been fully collected from the ratepayers.

Q. Is there any authority that you have looked to that uses the methodology of working capital versus cash working capital?

A. There are a number of Commissions that basically do it the same way the company's proposed.

Q. Such as?

A. Kentucky, Tennessee, Virginia, Ohio. They have incorporated a zero lag in their working capital calculation to recognize that the reserve, accumulated reserve balance that's being deducted in rate base includes dollars that have not yet been collected from ratepayers, because of the inherent revenue lag.

COMMISSIONER MURRAY: Thank you.

JUDGE THOMPSON: Thank you, Commissioner.

QUESTIONS BY JUDGE THOMPSON:

Q. Could you tell me, Mr. Grubb, what's the total amount that the company wants in rate base for cash working capital?

A. If somebody can give me a copy of the company's --

MR. ENGLAND: Your Honor, if I may approach the witness?

THE WITNESS: -- accounting schedules.

JUDGE THOMPSON: You may approach.

MR. ENGLAND: I think this is what he's looking for.

THE WITNESS: I'm sorry.

MR. ENGLAND: And in anticipation of your next question, I'll give him Staff's accounting schedules.

JUDGE THOMPSON: Thank you.

THE WITNESS: The company's request is $7,507,000.

BY JUDGE THOMPSON:

Q. Okay. Could you repeat that?

A. $7,507,000.

Q. Okay. And do you know what Staff's figure is?
A. The number I have here in front of me is the Staff's original filing, and they've made changes to that, so I'm -- I don't have --
Q. Will Ms. McKiddy, do you believe, be able to tell me what their current number is? Is there anyone in the room that can tell me what the Staff's current position is?
MS. McKIDDY: We can get it, I'm sure.
MR. KRUEGER: We don't have it with us in the hearing room, but we can obtain it.
MR. ENGLAND: Before we go any further, if I could ask the witness, I think he was giving you our cash working capital from our filed case. It may have changed as well, so there may be changes in both.
JUDGE THOMPSON: Let me just inform you all that this is information that we expect on each issue as it's presented in the hearing room. Okay? Because, for example, Mr. Grubb has testified that the management fees issue is worth 1.04 million, correct?
THE WITNESS: That's correct.
JUDGE THOMPSON: Now, when I look at the reconciliation prepared by Staff, I see that the management fees issue is worth $114,000.
MR. ENGLAND: Your Honor, I knew that was

going to be an issue. Mr. Grubb gave you a rate base or gave, I think, Commissioner Clayton a rate base amount. Revenue requirement number is entirely different. So it's an apples-to-oranges comparison.

JUDGE THOMPSON: I appreciate you pointing that out, and what you have to do for us is explain both the apples and the oranges, so that we know what's going on here. Okay?

BY JUDGE THOMPSON:

Q. So when you say that we have a rate base difference of 1.04 million on management fees, what then is the revenue requirement effect?

A. Approximately the $114,000 that the Staff has on their schedule.

Q. Okay. And that would be the return on that 1.04 million?

A. That's correct.

JUDGE THOMPSON: Thank you. I appreciate that.

MR. ENGLAND: I'm sorry, your Honor, but I think the witness gave you a bad answer.

JUDGE THOMPSON: On redirect you'll have a chance to elicit that.

MR. ENGLAND: Okay. Thank you.

JUDGE THOMPSON: Part of the purpose of your testimony is to get into the record your position on the issues in dispute, both for the purpose of making the record for this Commission to make its decision and also for the purpose of making the record for any appeals in review that might follow that decision. And I understand and appreciate that.

But another purpose of your testimony is to inform and persuade the people sitting here who have to make that initial decision. Okay?

And so we have to stop playing hide the ball in the sense that it is difficult for those of us who are not accountants, which would include all of us, I think, up here, to go through these things and figure out what the important numbers are and how they work together. Okay? So if you would please elicit from your witnesses these basic pieces of information, okay, it will, I assure you, lead to a better order. Thank you.

So later today we will find out what the Staff position is with respect to the rate base effect of cash working capital, right? Is that correct, Mr. Krueger?

MR. KRUEGER: That depends on the questions that the Staff's witness is asked.

JUDGE THOMPSON: The question is, what is the total amount of money that Staff recommends be included in rate base for cash working capital? That's the question. I asked Mr. Grubb. He didn't know. I asked you if someone was going to be able to provide that later.

MR. KRUEGER: We will be able to provide that.

JUDGE THOMPSON: Thank you, sir.

I have no further questions, Mr. Grubb. Thank you very much.

Any other questions from the Bench?

(No response.)

JUDGE THOMPSON: Very well. We will do recross based on questions from the Bench. I think Ms. Vuylsteke is gone. Mr. Conrad's gone. Mr. Finnegan appears to be gone. Ms. O'Neill?

MS. O'NEILL: Just a couple.

RECROSS-EXAMINATION BY MS. O'NEILL:

Q. Mr. Grubb, I just wanted to clarify a couple of things about this management fee issue, because I think the other issue's probably been clarified pretty well.

You don't know what a non-affiliated service company would charge you for providing the same services; is that correct?

A. No.

Q. And you don't know whether a non-affiliated service company would give you a different price offer based on whether they were paid in advance or paid following billing and with some lag; is that correct?

A. Without knowing what their profit level is --

Q. You don't --

A. -- what their cost structure is, you would need all that information.

Q. So you don't know?

A. Without that information, I couldn't tell you.

Q. And if that was a service company that was a competitive entity, it would have some incentives to give you an offer that would be the best deal possible so they could get your contract; wouldn't that also be something that would be in the mix?

A. I don't think they could meet the service company cost level, because there is no profit in the service company. It's just costs. So no matter how competitive they were, you know, it may be difficult to meet what the service company could do it for.

Q. But their costs could be lower for various reasons; isn't that correct?

A. Total costs, including their profit?

Q. Well, you just said that there's no profit with the service company, so I'm just going to -- I want to compare cost and cost. Their costs could be lower, couldn't they?

A. I don't know.

Q. Now, you said that the Commission Staff and presumably my office could access information regarding the service company contract; is that right?

A. That's correct.

Q. Was Missouri-American required to present the service company contract to the Commission and the Staff or my office prior to entering into that agreement?

A. I don't know. That was back in 1989.

Q. Currently there's not an affiliate transaction rule in place that would require Missouri-American to bring that contract to the Commission for review before it was entered into; is that correct?

A. Not at the present time.

Q. There are some states, however, that do have affiliate transaction rules that would require that kind of review; is that correct?

A. Some do.

Q. And Illinois, for example, has that rule?

A. I believe Illinois does have one, yes.

Q. And when you were talking about information being available, I think you clarified that the information that was available for review was information that was filed in the rate case; is that right?

A. In the cost allocation manual that was in response to the last St. Louis County rate case, and from that Staff can do or OPC can do their review, and if they request it or required additional information, the Data Request process would allow for that additional information.

Q. Okay. And there's not -- and your testimony doesn't say that your company's not recovering from your customers the costs associated with these management fees, right? You're recovering those costs? The way rates are set, they're designed to recover those costs?

A. Currently?

Q. Rates are set designed to cover the costs; is that correct?

A. I'm not sure what you mean. Cover what costs?

Q. Service company costs.

A. The current rates?

Q. Yeah.

A. The current rates are set to recover the costs in the last rate case.

Q. And in this case, whatever costs are actually established as the actual cost presumably will be included in the setting of rates going forward; is that correct? It will be updated to the current levels?

A. If you include the working capital portion of that as part of the cost of the service company, then the answer would be no based upon the final Commission determination in the case.

Q. Now, again, cash working capital isn't related to -- and regarding these issues, is not related to new expenses. It just has to do with when you collect the money from your customers to pay for -- to -- as far as management fees at least, to pay those management fees; is that right? On a going-forward basis, the mismatch is that you collect from the customers later than when you send the check?

A. That's correct.

Q. But you get the money from the customers?

A. Not for the full cost of that, no, because that's what working capital is designed to do, when the Staff does their accounting schedules.

Q. You get all the money authorized in rates to pay for those expenses from your customers, correct?

A. For the actual expenditure that is made on that invoice, assuming that that's built into the rates, yes.

Q. And there's not an actual expenditure regarding depreciation expense related to this issue, correct? You're not spending out money, you're just booking money in different places?

A. Well, you make the expenditure for the investment that creates the depreciation expenses.

Q. But in this lag period we're talking about, it's not regarding a new expenditure; you're just booking it?

A. No, it's a -- depreciation is a non-cash expense. I agree to that.

Q. Deferred taxes as well?

A. That's correct.

Q. And rates will be set on a going-forward basis whether or not this component is included, so that you will, over the course of time, collect what's allowed in rates from your customers, correct?

A. In that respect, yes, but rate base is not being properly set, as I've explained earlier.

Q. You just want to get more money from your customers to cover the same period of expense so you can book the money and have it there sooner; is that fair to say?

A. No.

Q. You disagree with that?

A. I disagree with that. No. We'll collect in depreciation expense over time the full cost of assets that we placed into service, assuming we don't have any more issues such as the old St. Joe treatment plant.

Q. The rates are designed to collect the full cost?

A. The rates are designed to collect that, yes.

Q. And you're going to get that money whether you get it on January 1st or March 4th? That's the question that you want answered today?

A. The question that we need to address today is what is the rate base that's going to be set for the company to earn upon, and that rate base, as I've said before, includes a reduction for accumulated reserve that does not have all the dollars collected from the ratepayers.

Q. Except all the dollars get collected from the ratepayers, don't they?

A. Sooner or later, yes.

MS. O'NEILL: No further questions.

JUDGE THOMPSON: Mr. Krueger?

RECROSS-EXAMINATION BY MR. KRUEGER:

Q. Now, you didn't take bids for these management services, did you?

A. I did not.

Q. Essentially this was a no-bid contract, was it not?

A. I don't know that. This contract's been around. The service company contract in concept has been around since as far as I can remember.

Q. But it is a contract with an affiliate of the company?

A. Yes, it is.

Q. Now, Commissioner Clayton asked you some questions referring to the expense lag of 42 days, I believe, in connection with the management fees. Do you recall those questions?

A. Yes, I do.

Q. Now, that 42-day lag was the Staff's filed position, is that correct, in the direct case?

A. I believe that's correct.

Q. Isn't it true that the Staff's position on that is that the lag is 21 days currently?

A. I believe from the surrebuttal testimony, that's correct.

Q. Thank you. In previous Missouri-American rate cases, wasn't the management services lag part of a settlement of other issues? In other words, it wasn't an issue that was decided by the Commission; is that correct?

A. It was a settlement of an issue, but it was based upon the Staff's position. That's why we settled it.

Q. But it wasn't presented to the Commission as an issue for it to decide?

A. That's because we believe the Staff was correct in their prior cases.

Q. Commissioner Clayton asked you some questions about depreciation and cash flow. Isn't it true that with regard to the company's statement of cash flows, depreciation and deferred taxes are actually listed as sources of cash or increases in cash flow?

A. That's because they're a non-cash expense, that's correct.

Q. Thank you. Isn't the lag that you described to Commissioner Murray for depreciation expense at least in part due to the lag in recognizing plant that has been added and depreciation that has been accumulated in between cases?

A. Can you repeat that?

Q. Isn't the lag that you described to Commissioner Murray for depreciation expense at least in part due to the lag in recognizing plant that has been added and depreciation that has been accumulated in between rate cases?

A. I'm not sure how to answer that. I described the lag as being zero, and that, in setting the rates, at any point in time you have a level of in the accumulated depreciation that has not been collected from the ratepayers, and that's what I'm trying to show in the working capital requirement.

MR. KRUEGER: That's all the questions I have, your Honor.

JUDGE THOMPSON: Thank you, Mr. Krueger. Redirect, Mr. England?

MR. ENGLAND: Oh, yes.

JUDGE THOMPSON: It's almost time for a break for the reporter. Would you prefer to do that before you start or after?

MR. ENGLAND: It may help to visit with the witness. I may be able to condense this.

JUDGE THOMPSON: We'll take our break now. Why don't we come back at ten o'clock.

(A BREAK WAS TAKEN.)

JUDGE THOMPSON: Mr. England, redirect?

MR. ENGLAND: Thank you, your Honor. The first thing I need to do is apologize to my witness. He did give you a good number and not a bad number.

JUDGE THOMPSON: See, aren't you happy I stopped you?

MR. ENGLAND: Yes, I am. I need that sometimes.

REDIRECT EXAMINATION BY MR. ENGLAND:

Q. And just kind of following up on it, as a general rule of thumb for purposes of rate base dollars versus revenue requirement dollars, is there a kind of a rough percentage you can use to convert the two?

A. It depends on the overall rate of return, but it goes anywhere approximately 10 percent, in that general range.

Q. So if you have a million dollar rate base issue, it will have a very approximate revenue requirement impact of approximately $100,000; is that right?

A. Approximate, yes.

Q. Following up on some questions I believe you received from, I know, Commissioner Gaw and then Ms. O'Neill regarding allocation of costs from the affiliate, in your experience, has this been an issue in most rate cases that you've been involved in?

A. Going back to 1983, when I first started getting into rate regulation, the many commissions that I've dealt with have looked into the service company contract billing, reviewed the reasonableness of the amounts, and have always concurred that the costs are reasonable and just.

Q. Has the company, to your knowledge, always provided a copy of the affiliate contract when asked?

A. Absolutely.

Q. Has it always provided the supporting cost information when asked?

A. Absolutely.

Q. And would that include other commissions besides this Commission?

A. Yes, sir.

Q. In your experience, do you know if the others in the company have had occasion to review whether outside vendors and unaffiliated outside vendors could provide these services at a lower cost?

A. From time to time the company does evaluate certain aspects of the service company billing to determine the reasonableness of it. In fact, Mr. Baryenbruch has done studies or has reviewed studies of the service company billing to outside vendors for another affiliated company of Missouri-American and found that the service company billings were lower.

MS. O'NEILL: Your Honor, I'm going to object to this as hearsay.

JUDGE THOMPSON: Mr. England?

MR. ENGLAND: Mr. Baryenbruch will be here tomorrow and he can withstand cross-examination on that statement, your Honor.

JUDGE THOMPSON: Well, let's go ahead and ask Mr. Baryenbruch the question. Why don't you move on.

BY MR. ENGLAND:

Q. Are you aware of any evidence in this particular case where an outside vendor could provide the services that the service company provides to Missouri-American at less cost than Missouri-American incurs with its affiliate?

A. No.

Q. Now I want to ask you about lags on recovering depreciation expense to deferred taxes, for example. Is this state one that typically uses a historical test year for purposes of setting utility rates?

A. A historical test year with a terminal rate base, yes.

Q. And is it your understanding that companies -- as a result of that, that companies will not be allowed to recover depreciation expense, for example, on their depreciable assets until after those assets are placed in service?

A. That's correct.

Q. Okay. Let's take a specific example, I think, following up on some questions from Commissioner Clayton, regarding the ISRS plant. Do you recall that?

A. Yes, I do.

Q. Now, my recollection is that that plant, the ISRS plant was placed in service between January 1, 2001 and August 31st, 2003; is that right?

A. That's correct. That would be the ISRS eligible plant.

Q. Thank you.

A. Yes.

Q. Once that plant was placed in service, did the company begin accruing depreciation expense on it?

A. Yes. Immediately upon placing any of the assets into service, the depreciation expense started on those assets.

Q. And at the end of each month, was that expense then also carried over to the depreciation reserve?

A. Yes. Yes.

Q. And when you established a revenue requirement for purposes of the ISRS-eligible plant as of 8/31/2003, did you deduct from that original investment the accumulated depreciation that had occurred during that approximate two and a half year period of time?

A. Yeah. The rate base associated with the ISRS-eligible infrastructure included the original cost, deferred taxes accumulated through August 31, and then also the accumulated depreciation recorded for those assets through August 31 of 2003.

Q. Now, when is the first time ratepayers will be asked to pay depreciation and deferred taxes on that ISRS-eligible plant?

A. The effective date was December 31st of 2003.

Q. Yet those ratepayers got the benefit of a rate base reduction for depreciation expense and deferred taxes that they haven't paid yet?

A. That's correct.

Q. Thank you, sir. With respect to some questions, I think, from Ms. O'Neill regarding whether you were going to recover all of your depreciation expense or not, I believe the point you were trying to make was there's a time value of money associated with recovering that depreciation expense; is that right?

A. That's correct.

Q. And that's essentially what the cash working capital allowance is designed to recover or reflect?

A. Yes. At any point in time when you set rates, the use of a zero lag for those two items, depreciation and deferred taxes, will readjust and properly reflect the rate base to show that all those dollars in the reserve and in the deferred tax liability account have yet to be collected or have -- well, have yet to be collected from the ratepayers at that point in time when you set rates.

Q. Let me switch gears on you. In response to a question from Mr. Clayton, you indicated that the only issues with cash working capital were the management fee depreciation and deferred tax issues, if you will; is that right?

A. That's correct.

Q. We do have the different issue with Staff regarding property tax expense, do we not?

A. That's correct.

Q. And in response -- I think your response, you're the witness responsible for that?

A. I'll be here tomorrow.

Q. In your testimony, did you not make an alternative recommendation if the Commission were going to accept Staff's property tax expense for purposes of this case that would affect cash working capital?

A. That's correct. By not allowing the company to recover the property taxes associated with the true-up plant, in essence what Staff is saying is that they will allow us to recover the actual bills, property tax bills that are paid in December of 2003, which means that we will have paid those property taxes before we collect it from the ratepayers. And in their lead lag study, they do the opposite. They're actually saying that we're collecting it from the ratepayers before we pay it.

Q. Is that another feature or result, if you will, of using a historical test year?

A. Yes, basically.

Q. Also in response to a question from Mr. Clayton, you indicated that the company is now utilizing more shared services and incurring, relatively speaking, more cost from its affiliate than it -- than it did in the prior case?

A. That's correct.

Q. Do you know if there have been cost reductions in other areas offsetting that?

A. Yes. You have cost reductions associated which would impact your working capital. Labor is reduced, and that reduces working capital. We have -- building rent has been reduced because of these initiatives, just general cash vouchers, payment of office supplies with less employees, you need less working capital for that category. Other expenses such as pensions and MoPEBs are being reduced also because of the reduction in employees.

Q. And then finally, in response to a question from Mr. Krueger, you were asked if the issue regarding management fees and the way it's handled for purposes of cash working capital was a settled issue in the last Missouri-American rate case. Do you recall that?

A. Yes, I do.

Q. Was it even a contested issue to be settled, in your opinion?

A. It was not even a contested issue.

MR. ENGLAND: Thank you, sir. I have no other questions.

JUDGE THOMPSON: Thank you, Mr. England. Thank you, Mr. Grubb. You may step down.

Ms. McKiddy?

MR. KRUEGER: Your Honor, I think we wanted to tender John Cassidy first. Although his testimony wasn't primarily in regard to cash working capital, there was one question and answer in his surrebuttal that we thought impinges upon the cash working capital.

MR. ENGLAND: If it will shorten things, we have no questions for Mr. Cassidy. All our questions are for Ms. McKiddy.

JUDGE THOMPSON: Take the stand, Mr. Cassidy. I'll remind you that you're still under oath.

THE WITNESS: Yes.

JUDGE THOMPSON: And you may inquire.

JOHN P. CASSIDY, having been previously sworn, testified as follows:

DIRECT EXAMINATION BY MR. KRUEGER:

Q. State your name for the record.

A. John P. Cassidy.

Q. And you previously filed your direct testimony, Exhibit 15, and your surrebuttal testimony, Exhibit 73, which have been admitted into the record?

A. Yes, that's correct.

Q. Do you have any corrections to any parts of that that pertain to cash working capital?

A. No, I do not.

MR. KRUEGER: Your Honor, I would tender Mr. Cassidy for cross-examination.

JUDGE THOMPSON: Thank you. I think that would be Ms. O'Neill. Well, wait. We're going to do questions from the Bench first, if that's what the Commission would like to do, and before we start, why don't you just remind us of what was your testimony that relates to cash working capital?

THE WITNESS: It is located on page 53 of my surrebuttal testimony.

JUDGE THOMPSON: What does it say?

THE WITNESS: It pertains to the fact that Missouri-American is required to prepay for goods and services from the affiliated service company. The Staff believes that's inappropriate. The Staff has found that by examining the cash vouchers of various -- a whole multitude of other vendors that are external to the American Water Company, that the company pays in arrears for those goods and services, and the Staff believes it's appropriate for Missouri-American to pay in arrears for services that are provided from the service company.

JUDGE THOMPSON: Okay. Thank you. Questions from the Bench, Commissioner Murray?

COMMISSIONER MURRAY: Thank you.

QUESTIONS BY COMMISSIONER MURRAY:

Q. And what is the total revenue requirement difference related to only that issue, if you know?

A. The difference in revenue requirement between our two positions is $114,000, approximately.

Q. And did Staff do any kind of an analysis of other service companies and what they would charge to

provide the same services?
A. No, we did not.
Q. And the analysis that you did in looking at non-affiliated Missouri-American Water's dealings with non-affiliates, explain more fully what that involved.
A. That represented examining the vouchers from a whole slew of different vendors that Missouri-American routinely does business with.
Q. Was that service related or was that product related?
A. It's -- it's related to goods and services that Missouri-American acquires or obtains from various vendors that it does day-to-day business with.
Q. What kind of services were represented?
A. I didn't conduct that study. You could ask Staff Witness Ms. McKiddy which invoices she had pulled.
Q. Okay. And the purpose for your being here this morning is just to reiterate that you disagree with the company's position on that issue; is that right?
A. Correct, that it's inappropriate for Missouri-American to be required to prepay for services from an affiliated service company.
Q. But you didn't do the study?
A. No, I did not.
Q. And there is a witness, Ms. McKiddy, who

did --

A. Who did the calculations of the cash voucher lag that Staff is proposing to apply to the management fees.

COMMISSIONER MURRAY: Thank you. That's all I have.

JUDGE THOMPSON: Thank you, Commissioner. Commissioner Clayton?

QUESTIONS BY COMMISSIONER CLAYTON:

Q. I did not bring your testimony down, and I apologize for not being more prepared. It wasn't on my cheat sheet, and so I apologize. And if I ask you a question that I should probably ask the other witness, stop me and we'll get over that.

Does Staff do an analysis of shared services to determine whether the expenses that are incurred are reasonable expenses?

A. Yes. I looked at the detail behind a lot of the service company expenses, and I'm not questioning any of those --

Q. Okay.

A. -- items.

Q. So you review the contract between Missouri-American and its affiliate or its shared services center; is that correct?

A. Yes.

Q. And you've had the ability to review that contract to determine what type of services and the cost associated with each of those services?
A. Yes.
Q. How many affiliates are there associated with these shared services?
A. The shared services represents all of the items that were in my direct testimony under the service.
Q. How many affiliates are we talking?
A. Well, it's just one affiliate combined.
Q. Okay.
A. With a multitude of services.
Q. Okay. Which affiliate is that?
A. The service -- the American Water Service Company.
Q. AWS?
A. Yes.
Q. Okay. And it provides service to all of the subsidiaries of American Waterworks throughout the country; is that correct?
A. That's correct.
Q. Did you feel the need to -- or did you believe it appropriate to determine the reasonableness of the expenses that AWS charges Missouri-American?
A. Yes, that's -- that's part of our analysis.

We look at the service companies.

Q. How do you determine that, whether it's reasonable or not?

A. We examine the detail behind -- we examine the invoices supplied to Missouri-American and the detail behind those invoices.

Q. Well, how do you determine their reasonableness in terms of the dollar amount? Do you look at possible third-party vendors?

A. I didn't do that.

Q. That's not your --

A. No.

Q. Did anyone?

A. No one from Staff did that type of analysis. The company has indicated that it's the lowest cost provider.

Q. Okay. And you believe that? I mean, you just accept it? I mean -- that sounds bad. You just accept that without doing an extra analysis?

A. Right. I accepted that. I didn't have any reason to question that at this time.

Q. Well, to determine whether to question it, wouldn't you have to do an analysis of third-party vendors? Wouldn't that be prudent on Staff's part?

A. I didn't see anything that suggested that they could have obtained the services at a lower cost.

Q. What would you need to see to indicate that they could have received the services at a lower cost?

A. I guess competitive bids.

Q. So you looked at com-- they did get competitive bids?

A. I didn't see -- I didn't ask for those competitive bids. I didn't see them, no.

Q. Okay. So if -- give me another example of information that would indicate that the expenses were reasonable.

A. Well, for example, the Belleville labs, the Staff's aware from past dealings that the company is able to -- to obtain those services at a cheaper rate than it would if it were to contract externally.

Q. And how does Staff know that?

A. Just from past cases.

Q. What information in those past cases would give Staff that information?

A. I don't know specifically.

Q. Okay. So the existence of competitive bidding would be one example of illustrating reasonable cost?

A. Yes.

Q. Doing an analysis of what third-party vendors are charging comparable businesses would be another example?

A. Yes.
Q. Can you think of any other examples?
A. I can't at this time.
Q. Okay. Well, you testified that Staff didn't look at any of that material, yet Staff has the position that these service expenses are reasonable. So I'm going to ask the question again. How did you make that determination?
A. I didn't have any reason to believe that they were unreasonable. That's all I -- the only answer I can give to that. The company --
Q. Did you do a comparison of, say, accounting rates or payroll costs associated with processing payroll?
A. No, I did not.
Q. Did you review the marketplace and make a determination of whether it was reasonable or customary with regard to these shared services whether or not the costs should be paid in advance or the expenses should be paid in advance?
A. Well, when looking -- yes, when looking at the cash vouchers and the multitude of interactions that the company has with external parties, external to Missouri-American's umbrella.
Q. Who are external parties? You mean other vendors?

A. Other vendors, outside vendors. Missouri-American pays those -- those vendors in arrears, and --

Q. But those are all different services, correct, those aren't the same services that the affiliates are -- are providing?

A. They -- yes, they represent a wide variety of goods and services.

Q. Well, for the services that are similar to these shared services, would it be customary for that type of service for the bills to be paid in advance or as they are with the shared services affiliates -- affiliate?

A. I don't believe it would be customary to pay them in advance.

Q. Tell me why that is.

A. Well, when you look at the cash vouchers, which we've used, those -- those vendors have payroll costs, those vendors have similar type costs that they have to deal with, and yet they're able to accept payment in arrears.

Q. Okay. Would it be unreasonable, in your opinion, if we were to assume that the shared services expenses are quite reasonable and are based on cost assessments, that because of that low cost of the services that they be paid in advance or simultaneously with the services, is that a fair or a reasonable part of the billing process for the company to fulfill as part of the contract?

A. If I understand your question --

Q. Is it a fair tradeoff? Is it a reasonable tradeoff to -- in exchange for getting a lower -- a low cost for these particular shared services, to pay simultaneously or early on these services, is that a fair tradeoff for the company? Is it reasonable in Staff's position?

A. No. Staff believes that the company should pay in arrears for those services. The company hasn't provided to the Staff any evidence that suggests that by paying in arrears that they would -- the service company would incur additional cost. There was -- the company provided no evidence in prehearing or in its testimony to suggest any empirical evidence that we could look at to determine if that would be the case.

Q. If what would be the case, whether it was possible to pay late?

A. Correct. I mean, if --

Q. But the contract says they're supposed to pay early, correct?

A. Right. That's what the contract says.

Q. Is that empirical evidence of agreement?

A. That's in evidence, but the Staff does not believe that's an appropriate basis to set up a --

Q. Would it be appropriate, in Staff's opinion, if you were to do a study on these expenses and they were significantly lower than what third-party vendors would be charging the company, yet to get that lower cost through the shared services that they have to pay early, would the Staff consider that reasonable?

A. I just -- I don't know if there are additional costs associated with paying late, paying late or -- I don't know that I can answer that question.

Q. Why can't you answer? I mean, is that --

A. Maybe I don't understand the question.

Q. If the shared services expenses, the bills, the invoices that are being sent by American Water Services to Missouri-American Water, if you were to have done a study and found that, say, that those expenses were 25 percent lower than what they would have been able to get on the open market through competitive bidding and through third-party vendors, would you say that 25 percent savings would warrant the provision of the contract that required paying early rather than 45 days late?

A. No. I still don't believe that would warrant early payment for those services. It's the company's -- the company is required to go out and to find the lowest cost, and just because the service company happens to be the lowest cost provider, they shouldn't be forced to have to prepay for that service.

Q. Since American Water Services is a different company and AWS said, this is the contract, we're not offering to give you 25 percent less and pay 45 days late, then the company would be forced to go to a third-party vendor, correct?

A. That's correct.

Q. Okay. So in that scenario, the 25 percent savings would not be enough savings to warrant paying early, in that example, that hypothetical example?

A. I don't know what that savings would be in terms of.

Q. 25 percent for the example.

A. Correct. I'd still say the company should pay in arrears.

Q. Okay. To answer that question in a real case, Staff would have to actually review what third-party vendors would charge for similar services, don't you think?

A. Yes.

Q. And that wasn't done here?

A. Staff didn't, correct. Staff didn't.

Q. Okay. So Staff really doesn't have any way of determining whether or not these expenses that are being charged to the shared services center are reasonable, are better than reasonable or are worse than reasonable?

A. The Staff only -- correct. The Staff only relied upon what the company indicated, that it was the lowest cost provider.

Q. So because they said so, you-all just accepted that?

A. Correct. We had no other evidence to suggest --

Q. Did you look for any other evidence?

A. No.

Q. Okay. So because of that, we have no way of knowing whether these shared service expenses are lower or higher or right on track or we have no way to evaluate that; is that a fair statement?

Let me ask you another question to move it around. Not to -- in evaluating the reasonableness of shared services expenses, would you be satisfied to just look at, say, third-party vendors or would you need to look at the books of, say, American Water Services and see what their expenses are?

A. I think you'd need to look at both American Water Service Company's books to see what the expenses are and determine if those expenses are appropriate expenses to be allocating.

Q. Are you aware of whether American Water Services pays a dividend or not to its shareholders?

A. I don't know.

Q. Did you ask for, say, the tax returns of American Water Services to determine whether or not they had a profit or not?

A. No.

Q. Did you ask for them?

A. No.

Q. Did you ask to review the books of American Water Services?

A. We did look at invoices and reports from American Water Service Company.

Q. Those were audited books? When you say the books, are you talking about outside documents or internal documents?

A. They were documents internal to the service company which provided detail of the service company billings.

COMMISSIONER CLAYTON: Okay. Thank you, Mr. Cassidy.

JUDGE THOMPSON: Chairman Gaw?

QUESTIONS BY CHAIRMAN GAW:

Q. Did Staff have information that they sought in regard to the services rendered by the affiliate that was not delivered to them?

A. No. Everything the Staff requested was supplied to the Staff.

Q. So in regard to the services and the charges for those services of the affiliate to Missouri-American Water Company, Staff did not feel there was any need to review any documents other than what you received?
A. That's correct.
CHAIRMAN GAW: I don't have any further questions.
JUDGE THOMPSON: Thank you, Chairman Gaw. Commissioner Murray?
FURTHER QUESTIONS BY COMMISSIONER MURRAY:
Q. Mr. Cassidy, is it fair to say that Staff made the assumption that everything that the company said about the services being provided by the affiliate was accurate; in other words, that the costs were reasonable and that the service company required by contract payment in advance? Did Staff accept that as true in making Staff's recommendation?
A. The company -- the company did provide some study that showed that --
Q. Yes or no. Did you accept that as true?
A. I'm not sure I understand your question.
Q. Okay. Well, what I'm getting at is, Staff is making a recommendation here that, for cash working capital, we should not include an adjustment for the fact that these services are paid in advance, correct?

A. Correct.
Q. And that is, as I understand it, Staff's position even if everything that the company says about the services that it takes from AWS is true?
A. Correct.
Q. So even if you had done an analysis that showed that, yes, the costs that are being incurred are reasonable in comparison to what it would cost to go through a non-affiliate, you still do not think that it is appropriate to allow for payment in advance?
A. Correct.
COMMISSIONER MURRAY: Thank you.
QUESTIONS BY JUDGE THOMPSON:
Q. Mr. Cassidy, I was told by an earlier witness that the company is asking the total of $7,507,000 for cash working capital. Do you know whether or not that's accurate?
A. I don't know that information.
Q. Don't know that. Okay. Do you know what is the total amount that Staff is recommending for cash working capital?
A. I don't know that either.
Q. You don't know. Do you know anyone that does know that?
A. I believe Staff Witness Roberta McKiddy should

be able to answer that.

Q. Very well.

Is it true that the service company provides functions that Missouri-American formerly performed itself?

A. Correct. Yes.

Q. And it's true that Missouri-American today includes not only the old Missouri-American, if you know what I mean by that, but also what used to be St. Louis County Water Company and what used to be the Jefferson City district of United Water - Missouri?

A. Yes, that's correct.

Q. And isn't it true that those companies also performed functions that the service company now performs? In other words, did United Water - Missouri have accountants on payroll?

A. Correct. Yes.

Q. And did they have customer service representatives on payroll?

A. Yes.

Q. And computer experts on payroll?

A. Yes.

Q. Okay. And if you were to add together the operating expenses that the old Missouri-American, plus St. Louis County Water, plus United Water - Missouri paid for those in-house functions and compare that to what they are now paying, what the current Missouri-American is now paying the service company for those functions, can you tell me whether there is a savings or not?

A. For some of those functions, there were savings, and for others there weren't. Overall, I can't tell you the total dollar impact.

Q. And would those figures, are they, as far as you know, in testimony or in the record anywhere in this case?

A. I don't believe you could discern that from figures that are in the record.

Q. If they were, would that also be some sort of gauge on the reasonableness of what Missouri-American is paying the service company for those services?

A. Yes, that would be something that would be -- that would be useful, yes.

JUDGE THOMPSON: I have no further questions. Thank you, Mr. Cassidy.

Any other questions from the Bench?

(No response.)

JUDGE THOMPSON: Very well. Cross-examination, Ms. O'Neill?

MS. O'NEILL: No questions.

JUDGE THOMPSON: Mr. England?

MR. ENGLAND: Yes, sir.

CROSS-EXAMINATION BY MR. ENGLAND:

Q. I hope to be very brief. I am advised in response to some questions from Mr. Clayton, you were referring to the service company -- or I think both of you were -- as AWS, but I'm advised that the proper acronym is AWWS?

A. Yes, American Waterworks Service Company.

Q. And apparently AWS is another affiliate but has no dealings with Missouri-American?

A. Yes.

Q. Okay. Thank you.

And again, following up on a question from Commissioner Clayton, I think he was talking about a situation where the service company was providing a good or service at a 25 percent, if you will, discount from what they could obtain it from an outside vendor. Do you recall that?

A. Yes.

Q. The only difference being that the company had to pay in advance with the affiliate, as opposed to pay in arrears with the outside vendor?

A. I recall the question.

Q. That was part of the hypothetical, I believe. Wouldn't a fair comparison or a fairer comparison be to look at the cost of the affiliate plus the cash working capital allowance cost, if you will, because of the payment in advance versus what the outside vendor would charge in arrears to determine if it's good, bad or indifferent?

A. You would have to look at the effect, the cash working capital effect as part of that.

Q. And then finally with respect to a question or two from Judge Thompson regarding the old United Water properties, you're aware of the fact that United Water was -- at least the local company was part of a holding company structure, are you not?

A. Yes.

Q. And that there were affiliate transactions, if you will, involved in that operation as well?

A. There were some.

Q. Not all of their services were provided in?

A. A small portion, yes.

Q. And I think this may get to what you were trying to say in response to one of his questions, but it's very difficult combining all these entities to make an apples-to-apples comparison between discrete account amounts from the last case, if you will, to the present case because things have changed dramatically, right?

A. The services have certainly increased now compared to what occurred back then. So there's been a lot of movement of services that were formerly done in house that are now being done at the service company. So, therefore, there's been a substantial increase in service company costs coming in the form of management fees to Missouri-American, as compared to the past case.

Q. Right. And there's also been some reductions in in-house labor costs as well, correct?

A. There have been reductions, but overall the and management fee has increased substantially four- and five-fold, compared to the last case.

Q. Okay. There have also -- also since the last case, we've had a merger of three distinct operating cultures, if you will, correct?

A. There has been a merger of three companies, yes.

Q. And, in essence, three different companies at least at one time operated in different manners with different accounting practices, different levels of affiliate transactions, et cetera, right?

A. Yes.

Q. And that makes it that much more difficult to compare or to -- to compare consolidated to -- the company three years ago versus the actual merged company today?

A. It doesn't make it difficult to compare the costs, though, that have increased five-fold from the last rate case.

Q. I believe you told Judge Thompson that you couldn't make that comparison and make a judgment one way or the other?

A. If you look at my testimony, I have a chart of management fees or service company fees that are coming from the service company that shows the increasing cost level.

Q. But I'm talking about all costs, all accounts. You haven't made that comparison and can't make that conclusion, correct?

A. I can't compare to what the costs were internally. I can only look at the service company costs that have increased.

Q. I think the answer to my question is, yes, you may have looked at it on a discrete service company basis, but you haven't looked at it on a total company basis; is that right?

A. I know what the service company costs have done. I can't tell you how it compares to what the costs were internally.

MR. ENGLAND: Okay. Thank you.

JUDGE THOMPSON: Thank you, Mr. England. Mr. Krueger?

MR. KRUEGER: No questions, your Honor.

JUDGE THOMPSON: Thank you. You may step down, Mr. Cassidy.

Now, before we -- Ms. McKiddy, I assume, is our next witness?

MR. KRUEGER: Yes, your Honor.

JUDGE THOMPSON: Okay. When I look at the amended witness list that the Staff filed in December, I don't see that Mr. Cassidy was endorsed as a witness for this issue. Are there going to be any more surprise witnesses?

MR. KRUEGER: No, your Honor.

JUDGE THOMPSON: Okay. Very well.

Step forward, Ms. McKiddy. Go ahead and spell your last name for the reporter.

MS. McKIDDY: Capital M-c, capital K-i-d, as in David, d-y.

(Witness sworn.)

JUDGE THOMPSON: You may inquire.

ROBERTA McKIDDY testified as follows:

DIRECT EXAMINATION BY MR. KRUEGER:

Q. State your name for the record, please.

A. Roberta McKiddy.

Q. Did you cause to be filed the direct testimony of Roberta McKiddy, Exhibit 20 -- premarked as Exhibit 20, and the surrebuttal testimony of Roberta McKiddy premarked as Exhibit 70?

A. Yes, I did.

Q. Do you have any corrections or changes to those pieces of testimony?
A. No, I do not.
MR. KRUEGER: Your Honor, I would offer Exhibits 20 and 70, and tender the witness for cross-examination.
JUDGE THOMPSON: Thank you, Mr. Krueger. Do I hear any objections to the receipt of Exhibit 20?
MR. ENGLAND: No, your Honor.
MS. O'NEILL: No.
JUDGE THOMPSON: Do I hear any objections to the receipt of Exhibit 70?
MR. ENGLAND: No, your Honor.
JUDGE THOMPSON: Hearing no objections, Exhibit 20 and 70 are received and made a part of the record of this proceeding.
(EXHIBIT NOS. 20 AND 70 WERE RECEIVED INTO EVIDENCE.)
Questions from the Bench, Chairman Gaw?
CHAIRMAN GAW: I'll pass right now.
JUDGE THOMPSON: Commissioner Murray?
COMMISSIONER MURRAY: Thank you.
QUESTIONS BY COMMISSIONER MURRAY:
Q. Good morning, Ms. McKiddy.
A. Good morning.

Q. In terms of the services contracts and the treatment and cash working capital of the amount that is paid in advance, when Mr. Cassidy was on the stand, I believe he was indicating that there were some studies conducted or analyses conducted by you; is that correct?

A. I looked at the invoices that they submitted in order to determine the expense lag associated with those fees.

Q. Okay. And that is all that you examined was to see whether the invoices actually contained an expense lag?

A. I also looked at any other Data Request responses that they submitted and any information related in those responses as it spoke to payment of those fees.

Q. But did you look at analyzing whether -- did you in any way analyze whether it was reasonable to incur additional costs associated with payment in advance in order to offset savings that might be occurring through use of the affiliate?

A. No, I did not.

Q. And I guess I would -- since Commissioner Clayton isn't here right now, I guess I would ask you one of the questions that he asked Mr. Cassidy, if I can remember it well enough to ask it.

Assuming that there were a 25 percent savings by using the affiliate, but that that savings could only be achieved by payment in advance, would it still be Staff's position that there should be no allowance for payment in advance?

A. I think I recalled Mr. Cassidy saying that in order to look at that 25 percent discount, you'd also have to look at how that impacts cash working capital in relation to the expense lag associated with those dollars as to whether there was any cost savings actually realized or not.

Q. Okay. In order and -- in order to do that, you would have to know what the savings were to begin with; is that right?

A. I believe you would have to know the savings.

Q. And you would also have to know the impact of the cash -- on the cash working capital?

A. Yeah. I think to look at the impact on cash working capital would actually get you to the resulting savings. I think just looking at the 25 percent discount on its own would not be sufficient.

Q. But is it accurate that Staff didn't do any of that type of analysis to, one, determine whether there was a savings or, two, to determine the impact on cash working capital if there were no savings?

A. My understanding is that we did not conduct such an analysis.

Q. So in order for Staff to arrive at the position that it was inappropriate to pay in advance, how did Staff arrive at that position?

A. Well, in my mind we arrived at that position not because there was a cost savings per se involved, but the fact that other vendors are not prepaid for services not yet rendered. And we were trying to treat the affiliate services provided just as we would consider any other suppliers providing service to the company.

Q. But was Staff aware that the company's position was that there was a significant savings realized by using the services of the affiliate through this contract that required payment in advance?

A. I'm not aware of any testimony presented by the company that spoke to savings realized by using the affiliate rather than other outside vendors.

Q. Okay. So Staff's position is based purely on the fact that there should be no payment in advance to any vendor; would that be accurate?

A. Well, there's some prepayments that are allowed, like premiums on insurance; those are normally paid in advance. Those type expenses, I think Staff does consider those appropriate prepayment type items.

Normal, every day expenses for supplies and materials, things like that that are normally paid to vendors in arrears, and I believe we consider management fees as a similar-type expense that should also be paid on that same pattern.

Q. So would that be Staff's position regardless of whether we were talking about an affiliate or a non-affiliate?

A. I believe that would be true.

Q. And then on the issue of accumulated depreciation and deferred taxes and cash working capital --

A. Yes.

Q. -- it appears that we've covered that pretty well so far with the witnesses.

Is there anything -- I guess I'll just ask you an open-ended question, since I don't have a specific question for you about it.

Is there anything that you think needs to be provided as further explanation of Staff's position on that that was not included in your testimony?

A. I don't really think there's a whole lot for me to add. The simple answer is that when looking at cash working capital from Staff's perspective, we're looking at items that require cash expenditures. And in this case, depreciation expense and the deferred income tax are two items that do not require a cash expenditure.

Q. And to your knowledge have we ever included in cash working capital any item that did not require a cash expenditure?

A. I'm not aware that this Commission has ever authorized the inclusion of any non-cash item.

COMMISSIONER MURRAY: I believe that's all I have. Thank you.

JUDGE THOMPSON: Thank you, Commissioner Murray.

Chairman Gaw?

(No response.)

QUESTIONS BY JUDGE THOMPSON:

Q. Ms. McKiddy, I was told by Mr. Grubb that the company's total cash working capital recommendation is $7,507,000 for rate base. Do you know if that figure is accurate?

A. I have no reason to believe it is not.

Q. Okay. Do you know what Staff's total cash working capital recommendation is?

A. Staff's total cash working capital as of today's date is approximately $880,000. The exact amount is $880,805.

Q. 880,805?

A. Uh-huh.

Q. And is that a change from Staff's position as originally filed?

A. Yes, it is.
Q. What was Staff's position as originally filed, if you know?
A. I believe the original filling was a negative 126,000.
Q. Okay. Just offhand, do you know what caused the change of almost a million dollars?
A. We made a correction to materials and supplies which impacted the cash vouchers account, and it shifted some dollars up the scale --
Q. Okay.
A. -- which, when we balanced, created this new number.
Q. And the revenue requirement effect of these figures is simply the rate base figure multiplied by the overall rate of return, correct?
A. That is my understanding, yes.
Q. Very well. So I believe Mr. Grubb said that the management fees issue, the difference is worth 1.04 million in terms of rate base. Is that accurate as far as you know?
A. I can tell you what dollars the Staff has in for management services in relation to CWC.
Q. What --
A. That's an amount of 742,090.

Q. Okay. And he also said that the deferred taxes and depreciation issue is worth $5.055 million rate base. Is that accurate as far as you know?

A. As far as I know, that is company's number.

Q. Okay. So these issues together make up most of what the company is requesting for cash working capital?

A. What were the two numbers again, please?

Q. Well, when I add 1.04 plus 5.055, I get 6.095. And I subtract that from 7.507 and it doesn't leave much.

A. I'd say that is a large percentage of what they're asking for.

Q. Okay. And Staff's recommended figure of over $700,000 for management fees, then, makes up most of the 880 that Staff is recommending?

A. Correct.

JUDGE THOMPSON: Very well. Any other questions from the Bench?

COMMISSIONER CLAYTON: Can I just ask a few?

JUDGE THOMPSON: Absolutely.

QUESTIONS BY COMMISSIONER CLAYTON:

Q. I'm sorry for not being down here.

A. That's okay.

Q. Thought you were going to get off the hook, didn't you? No such luck. Okay. Weren't going to answer that.

I asked some questions earlier today relating to this lag and this timing issue, and Mr. England on, I believe, his direct examination of Mr. Grubb made a reference to this cash working capital as basically being an issue of time value of money. Would you agree with that kind of characterization of this issue?

A. I don't know that I would characterize it as a time value of money. I think he's using that term in the context of earning a rate of return on what they believe they're not recovering.

In my mind, the issue is a timing difference, based on how they record things for financial purposes versus how they record things for income tax purposes or tax return purposes.

Q. Okay. In your testimony, you make several references on the depreciation and the deferred taxes issue as a non-cash expense issue and that no one actually demands payment on these; is that correct?

A. That is correct.

Q. Is that a correct characterization?

A. Yes. There is no cash expenditure.

Q. But you would agree that there is a cash outlay for those assets?

A. Yes, and that's why we include them in rate base, so that they can get recovery of those investment dollars through the rate base.

Q. Would you agree with the characterization on these issues relating to depreciation and deferred taxes that -- that this is a cash-flow-type issue?

A. I think from their perspective, yes, it is a cash flow issue, because it's basically describing regulatory lag in the recovery of those dollars.

Q. Okay. Well, do you characterize it as a cash flow issue?

A. It is a cash flow issue, but not one that should impact cash working capital, because it doesn't represent a day-to-day expense in providing utility service to the customers.

COMMISSIONER CLAYTON: I don't think I have any further questions. Thank you, Judge.

JUDGE THOMPSON: Further questions from the Bench?

(No response.)

JUDGE THOMPSON: I have one more.

FURTHER QUESTIONS BY JUDGE THOMPSON:

Q. With respect to the deferred taxes and depreciation issue, am I correct in understanding that the company's position is they're being deprived of a portion of the return on those assets?

A. Yes, that is their position.

Q. And are they, in fact, being deprived of a portion of the return on those assets?

A. I think it's just being delayed to a later time period. I don't think they're being denied that recovery.

JUDGE THOMPSON: Thank you.

COMMISSIONER CLAYTON: Can I follow up?

JUDGE THOMPSON: Absolutely.

FURTHER QUESTIONS BY COMMISSIONER CLAYTON:

Q. If they're being delayed, I guess from the answer that you just gave to the Judge, the return on that plant would come at the end of its life, rather than in the first 63 days of its life. It would come 63 days after its end of life; is that correct?

A. It would come at some point after that, yes.

Q. Okay. So it is your position that they do receive a return on that plant, it is just delayed?

A. That's my understanding of how the timing difference works, yes.

Q. So then there is a value, a time value of money question here, is there not, and it's basically 63 days worth of time; is that a fair statement?

A. Well, I think what the company's asking you to do is to make accommodation for regulatory lag, which is inherent in every case. I think to try to regulate to that and try to accommodate those timing differences would be inappropriate. Yes, maybe it does impact time value of money to some degree, but I don't know that it's appropriate to adjust cash working capital to accommodate for that.

Q. Are you aware of where -- are you aware of any case in which, in missouri, where this depreciation and deferred taxes, cash working capital issue has been approved?

A. No, I am not.

Q. Are you aware of any other states that have done it?

A. No, I am not.

Q. Have you actually researched any other states?

A. No.

Q. Enough in Missouri to worry about, right?

A. Well, regulation in each state has its own nuances. It would take a lot of research to be able to do an apples-to-apples comparison.

Q. I asked Mr. Cassidy, I believe, some questions regarding the shared services fees. Did you do any work on that?

A. No, I did not.

JUDGE THOMPSON: Okay. Thank you.

Other questions from the Bench?

(No response.)

FURTHER QUESTIONS BY JUDGE THOMPSON:

Q. You told Commissioner Clayton that you agree there is a time value of money impact, but that for some reason it's inappropriate to adjust to fix it. Could you explain that?

A. I didn't say that there -- I didn't agree that there was exactly a time value of money issue here. What there is here is a regulatory lag issue which is inherent in every rate case, and for you to adjust your cases in every instance where there's a regulatory lag issue, you kind of defeat your purposes of the ratemaking process.

Q. Okay. Regulatory lag means you don't get your money when you would like to get it?

A. Correct.

Q. But the regulatory process means delay between the day when you're entitled to get that money and the day you get that money, correct?

A. Correct.

Q. It's like putting a plant into service two months before the rate decision comes down?

A. Right.

Q. So exactly how does regulatory lag affect this issue?

A. From my perspective of cash working capital, it does not affect this issue.

Q. Well, you just told me it's a regulatory lag issue, not a time value of money issue. So I'm asking you to explain exactly how is it a regulatory lag issue?

A. It's a regulatory lag issue because the company has a timing difference between the depreciation they're recording for financial purposes and what they're actually calculating for tax return purposes. That's where the regulatory lag is.

Q. Okay. You agree that they have a right to a return on the assets dedicated to public service?

A. Yes, and that's why it's included in rate base.

Q. Okay. So exactly how is there lag in how they are receiving that return on?

A. Well, I think it's because how they're recording the depreciation expense for financial purposes is a different timing than how they're recording those expenses for tax return purposes.

Q. Okay. You've said that several times, and it's not penetrating my head. Are they paying something in taxes sooner than they're getting money back? I mean, exactly what's happening, expressed in a way that even I can understand?

A. Okay. Let's say you're accelerating depreciation at a rate faster than what you may be claiming as a depreciation methodology on your income tax pur-- or on your income tax form. You end up with less net income to be taxed when you're using that accelerated depreciation methodology, which creates less of a tax liability. That's where the deferred income tax comes in, is that difference in those methodologies of depreciation.

Q. And isn't the reward there the lower tax bill?

A. In my mind, yes.

Q. For the company?

A. Yes.

Q. Okay. So why are they seeking an additional return from the ratepayers, or is that what they're seeking?

A. Well, I think Mr. Grubb's Schedule EJG-2 was trying to imply that there was a portion of depreciation that was not being recovered and giving them that tax liability, so they were trying to make up for that difference by collecting it in cash working capital so that they could get it ahead of when their normal reporting process would have allowed them to recover that.

Q. That's exactly how I understood Mr. Grubb's testimony, was that there was a portion they were not getting. You're telling me that that's not accurate?

A. Well, they're getting it, but not in the time frame in which the company would like to get it, is how I view it. So they're trying to make up that difference in timing of getting that recovery by putting it in cash working capital so that it's recovered there. To me, it -- to allow it in cash working capital would allow them an opportunity to overrecover. They'd recover it up through the cash working capital and then they'd recover it again as they booked the depreciation.

Q. Is that a theory on which reasonable accountants might differ?

A. There's a possibility there would be a difference of opinion there.

JUDGE THOMPSON: Thank you very much. That was very helpful. Commissioner Murray?

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. I probably shouldn't delve into this any more, but you indicated that -- I believe I heard you say that the regulatory lag aspect of this issue is because of the different booking methods of depreciation for income tax purposes and regulatory purposes. Did I hear you correctly?

A. Right. The company may book their depreciation under one methodology for financial reporting purposes, but when they go to do their income tax returns, they may use a different methodology, which results in a timing difference in depreciation expense, which creates a deferred income tax.

Q. And is there an actual cash outlay for the income tax treatment?

A. Deferred income tax is a component of income tax expense, but it is -- it does not require any cash outlay.

COMMISSIONER MURRAY: Okay. I think I'll stop there. Thank you.

JUDGE THOMPSON: Other questions from the Bench?

(No response.)

JUDGE THOMPSON: I think I'm going to keep my mouth shut.

Very well. Let's go to cross-examination. Ms. O'Neill?

MS. O'NEILL: Thank you.

CROSS-EXAMINATION BY MS. O'NEILL:

Q. Good morning, Ms. McKiddy.

A. Good morning.

Q. I understand from your testimony that what we're really talking about cash working capital is cash necessary for the utility to pay its day-to-day expenses?

A. That is correct.

Q. And those are the day-to-day expenses that it incurs to provide service to its customers?

A. That is correct.

Q. And it's because it's to pay for services

incurred to provide service -- expenses -- excuse me --
needed to provide service to its customers that the
customers are expected to reimburse the company through the
rates for those cash working capital daily expenses?
A. That is correct.
Q. So expenses like depreciation expense and
deferred income taxes, which don't have to be paid, are
being collected from the customers nonetheless, because the
customers are receiving service from that plant?
A. Right. Depreciation expense and deferred
taxes are a component of cost of service and are collected
in rates.
Q. And those are separate -- those components of
rates are separate from the cash working capital that we're
talking about here; is that right?
A. Yes, that is correct. Those are adjustments
to rate base.
Q. So those things are being paid for by the
customers through the rates that are set based on other
components of the ratemaking process?
A. Correct.
Q. And the proposal the company has regarding its
proposed higher number on cash working capital would
increase the amount the customers are required to pay in
their rates; is that correct?

A. Yes, that would be correct.
Q. However, would it also be fair to say that the customer will not get any additional benefit as a result of paying these increased rates based on the company's proposal?
A. Yes, that would be correct.
MS. O'NEILL: No further questions.
JUDGE THOMPSON: Thank you, Ms. O'Neill. Mr. England?
MR. ENGLAND: Thank you, your Honor.
CROSS-EXAMINATION BY MR. ENGLAND:
Q. Good morning, Ms. McKiddy.
A. Good morning.
Q. Let me follow up on a question just asked by Ms. O'Neill. Deferred taxes and depreciation, insofar as rate base is concerned, are deductions from rate basis -- from rate base, not additions to for the ratemaking process, right?
A. I believe that is true.
Q. Okay. Thank you. And those deductions, then, are a benefit to the ratepayer, correct?
A. They would lower the rate base in which your revenue requirement is calculated, yes.
Q. That's the way in which ratepayers are compensated for the funds they pay to recover those

expenses, correct?

A. Right. That's their way of --

Q. That's a benefit to them, isn't it?

I beg your pardon?

Let me put it, they're better off because of that than if you didn't make that deduction, correct?

A. Well, it's a way for them to be compensated for money they have provided up front.

Q. And they are better off by deducting it from rate base than not deducting it from rate base, everything else constant?

A. I would call them equal in the game on that.

Q. Then --

A. If they've put it up front, then they're going to --

Q. You'd have no problem with Staff taking deferred taxes and accumulated depreciation out of the deductions to rate base and allowing us to earn on basically a full investment? Because we might be able to settle the case right now.

A. No. I'm saying the customers are providing the money up front, they should have the opportunity to earn a return if they could have invested it elsewhere.

Q. And that opportunity --

A. Now, whether that would -- you're calling it a benefit, but to me it would be a benefit if they were earning more than if they had invested their money elsewhere.

Q. My next question -- or I tried to change it. They're better off in the ratemaking process having that deduction than not having that deduction, correct?

A. It reduces the revenue requirement, so in that context, yes.

Q. Thank you.

And then in questions, I think, from the Bench -- perhaps more specifically Judge Thompson -- you were talking about this being a tax timing issue. And I believe that only affects the deferred tax element, correct? That's what the tax timing issue creates deferred taxes, correct, it doesn't create depreciation expense, it doesn't create the management fees that are also at issue here?

A. Well, the difference in booking and depreciation expense is what creates the deferred income tax.

Q. But that difference doesn't create depreciation expense; it doesn't create management fees. In other words, tax timing differences have nothing to do with whether or not you include depreciation expense or the lag in recovery of depreciation expense and lag in the recovery of the management fees, correct?

A. Could you rephrase that, please?

Q. Sure. Tax timing differences have nothing to do with the issue around the lag in the recovery of depreciation expense and the lag in the recovery of management fees, insofar as cash working capital is concerned?

A. I'm not sure I follow your question yet. Management fees does not impact the deferred income taxes, in my mind. They're -- you're trying to put them together and --

Q. No, I'm not. As a matter of fact, I'm trying to keep them separate. You've said on at least three occasions in response to the Bench that this is a tax timing issue, and I want to try to focus. First of all, I don't necessarily agree, but I want to make sure that we're really only talking about deferred taxes are a result of tax timing differences, right?

A. No. I think what I said was that -- whether to include -- that I believe the company is wanting to recover depreciation that they believe they're not recovering through cash working capital because of a difference in how it's booked for financial purposes versus tax return purposes.

Q. Isn't it more correct to say that the company is seeking to recover or reflect the lag in the receipt of depreciation expense from its customers through the cash working capital adjustments it's made?

A. Well, I believe what they're trying to recover through cash working capital is regulatory lag, which is something that we don't believe is appropriate to capture through there, specifically because these are two items that do not require cash outlays, and that is the purpose of cash working capital.

Q. I understand you don't necessarily agree with the appropriateness of it, but what we're trying to capture with the cash working capital allowance is the lag in the receipt of that money from our ratepayers, correct, not additional depreciation expense, for example?

A. You're trying -- to me, what the company is trying to recover is -- is on the investment in the asset that they do not believe they're recovering fully through their depreciation expense calculation; again, a non-cash item that doesn't require cash outlay.

Q. Are you -- you're not saying it would be appropriate for us to increase depreciation expense to this lag, are you?

A. I'm not suggesting that, no.

Q. And you're not saying we're trying to increase depreciation expense to cover this lag, right? We're trying to increase a rate base item to reflect the lag or the return on this invested money that we don't get for 63 days, correct?

A. You're trying to recover a regulatory lag dollar amount that should not be recovered in cash working capital, because it is not a day-to-day expense in the provision of utility service.

Q. I understand you don't believe it's a cash outlay, but it's -- it is a lag issue, a lag in the recovery. You like to call it regulatory lag. We call it revenue lag, but let's just call it a lag for the purposes of the question. There's a lag in the receipt of those monies?

A. As there are with other items.

Q. And if it's a cash outlay, you will accept that or acknowledge that in your cash working capital allowance?

A. Not if it's associated with regulatory lag, no.

Q. Give me an example of an actual cash outlay that's associated with regulatory lag that you've not included in your cash working capital.

A. I don't know that I could give you a specific example.

Q. Okay. Now, getting back to deferred taxes and these tax timing differences, I believe you said in questioning from the Bench that the company has the benefit, if you will, of an increased tax deduction in the early years of an asset because of accelerated depreciation, right?

A. If they use accelerated depreciation, yes.

Q. Okay. And that creates the difference between what they actually take as a tax deduction and what's used for purposes of ratemaking purposes or for purposes of their books is the deferred tax amount, correct?

A. That's what the deferred tax is based on, a portion of.

Q. Right. And in the later years of that asset, it turns around, the actual tax liability is less than it would be under straight line depreciation, correct?

A. In methodology, yes.

Q. Okay. In your direct testimony at page 11, lines 16 through 17, you say, when a utility spends cash to pay for an expense before the ratepayer provides the cash, then the shareholder must supply the necessary cash working capital, correct?

A. Yes, and that's referring to expenses necessary to provide utility service.

Q. Your criteria is it has to be a cash outlay, right?

A. Correct.

Q. Okay. So the company makes a cash outlay and then there is a lag in the receipt of that mo-- the recovery of that cash, if you will, from the ratepayer. That's shareholder-supplied funds and it creates a positive, if you will, cash working capital allowance, correct?

A. Correct.

Q. Conversely, there at the bottom of the page, beginning on line 22, you talk about ratepayers supplying cash working capital. Do you see that?

A. Yes.

Q. And say when they pay for the service provided by the utility before a utility must pay for the expense that it incurs in providing the service, correct?

A. Correct.

Q. And then I think you go on to note -- and we've had this discussion just a few minutes ago -- that the ratepayer is compensated for the funds that it provides through reduction to rate base for the associated cash working capital allowance, right?

A. Correct.

Q. And that creates what I would call a negative cash working capital allowance, right?

A. Correct.

Q. Would you agree with me that revenue lag is defined as the amount of time between the provision of service by a utility and the utility's receipt of the payment of that service from the ratepayers?

A. Yes.

Q. And I believe you've indicated in your testimony that the revenue lag differs by district, depending on the actual payment, I guess, of the bills; is that right?

A. Right, whether it was monthly billing or quarterly billing.

Q. Thank you. And I think for purposes of some discussions here today, we've been using a 63-day figure, which I believe is roughly close to what you've determined as the revenue lag in the St. Louis district; is that right?

A. Let me double check here. Hang on. Yes, in the St. Louis district, I had the rev-- total revenue lag at 62.961 days. All the other districts were about 42 days.

Q. Is that a reflection because St. Louis is primarily quarterly billed versus monthly billing in the other districts?

A. Yes.

Q. Would you agree with me that the expense lag is the amount of time between the utility's receipt of goods and services and the time when it has to pay for those goods and services?

A. It's from the midpoint of the service period to date that the expense is paid, yes.

Q. Okay. Would you agree that a utility's total capitalization on its balance sheet should equal its rate base plus other balance sheet accounts that may not be allowed for ratemaking purposes, such as construction work in progress, affiliate -- or excuse me -- acquisition adjustment, if any, deferred debits like for unamortized rate case expense, things of that nature?

A. In theory, capitalization should equal rate base, but in practice it does not always hold true.

Q. And that's because of these other amounts that I just mentioned, construction work in progress, acquisition adjustment, unamortized balances in, say, rate case expense that are not recognized in the ratemaking process, right, would not be part of the rate base?

A. That would be fair to say it would include those items.

Q. Okay. Now, as I understand it, you have not performed any kind of test or reconciliation to test your rate base -- Staff's rate base with your cash working capital allowance plus these other items that we've talked about to see if it equals total capitalization, have you?

A. I have not done such a study, no.

Q. Let's talk a little bit about depreciation, if we can. I think we've established the company has included the revenue lag associated with recovering depreciation expense from its ratepayers and its cash working capital allowance, right, or proposes to?

A. They propose to, yes.

Q. And for purposes of the St. Louis district, that's that 63 days that we talked about?

A. Yes.

Q. Okay. Staff has not, correct, has not included any amount for depreciation?

A. No, because Staff does not include non-cash items in its cash working capital.

Q. I understand. And would you agree with me, then, that when a utility places a depreciable asset in service, there is a cash outlay?

A. Yes.

Q. And that cash is supplied by the investors, correct?

A. Yes.

Q. Generally speaking?

A. Generally speaking, yes.

Q. Each month, as depreciation is taken on that depreciable asset, would you agree with me that a corresponding deduction is made to rate base to reflect accumulated depreciation?

A. Depreciation is a deduction from rate base, depreciation expense. I don't know if it's looked at on a monthly basis by Staff.

Q. I'm drawing a distinction between depreciation expense, which would hit the income statement, and accumulated depreciation, which would be balance sheet.

A. Correct.

Q. As you accrue depreciation month to month, you take that amount to the balance sheet to the accumulated depreciation reserve and increase it accordingly, correct?

A. Say that again, please.

Q. Sure. As you accrue depreciation month to month as an expense, you also, then, take it to the balance sheet account, the accumulated depreciation reserve and add it to that?

A. Correct.

Q. Would you agree with me that depreciation has oftentimes been referred to, at least in these proceedings, as a return of the investors' capital?

A. Yes, it is a return of.

Q. And a return on investors' capital would be the rate of return that you're allowed in the case, right?

A. That is correct.

Q. And I think you'd agree with me that, at least in your experience, Missouri Public Service Commission has always been a jurisdiction that uses an historical test

period, correct?
A. That is correct.
Q. In other words, plant must be in service, used and useful before the utility can earn a return on that plant, as well as a return of that plant, right?
A. That is correct.
Q. I want to ask you hopefully a simple hypothetical question, and I'd like for you, for purposes of the hypothetical, to assume a $1 million piece of plant that has been placed in service on December 31st, 2002. Okay?
A. Uh-huh.
Q. The utility files a rate case on February 1, 2003. Do you have that?
A. Uh-huh.
Q. Okay. Now, would you agree with me that, at least in Missouri, the operation of law date when rates would generally become effective from that rate filing would be approximately 11 months later or January 1 of 2004?
A. I believe so.
Q. January 1, 2004 would be the first time when the utility could begin earning a return on that plant, as well as earning a return of that plant through depreciation expense, correct?
A. Yes, it would be part of new rates.
Q. Okay. Now, let's further assume that the

annual depreciation on that plant is $60,000 a year, or $5,000 a month. All right?

A. Okay.

Q. The company will begin accruing depreciation the minute it places that plant in service on its books, will it not?

A. I believe that is correct.

Q. So in January of 2003, the first month after it's been in service, there will be a $5,000 depreciation expense, under my scenario?

A. Yes.

Q. Okay. But again, under this hypothetical and under the ratemaking that we've talked about in Missouri, recovery of this depreciation expense will not occur until January 1 of 2004, right?

A. That is correct.

Q. Now, let's assume that the test year, for purposes of this hypothetical, is the 12 months ended June 30th, 2003, mid year 2003. Okay?

A. Okay.

Q. Would you agree with me that the company will have -- this hypothetical company will have accrued six months of depreciation expense or $30,000 on this $1 million piece of plant?

A. You put it in place in December of 2002?

Q. Yes,
A. So six -- yeah. Six months ending June, you would have six months of depreciation on the books.
Q. And that would be, under my scenario, six times 5,000 or $30,000, correct?
A. Right.
Q. Okay. And for purposes of rate base, for purposes of our rate case that we filed, our rate base will actually be $970,000, which is the original investment of a million less the accumulated depreciation of $30,000?
A. If you're updating for purposes of the case through a period ending June 30, that would be correct. If you're using a test year ending December 2002, that would not be.
Q. I understand, but typically we do bring the test period forward sometime during that period of filing, do we not?
A. Typically, yes.
Q. So the dates that I've given you really are not unrealistic, given real rate case experience in this state, right?
A. No. That's similar to what we're doing in this case.
Q. Okay. Now, the ratepayers will receive compensation for the accumulated depreciation that occurred

in the first six months of 2003 in the form of a $30,000 reduction to rate base, right?

A. Well, there will be a $30,000 reduction to rate base, thus requiring a lower revenue requirement and resulting in lower rates to the customer.

Q. So the ratepayers won't pay as much as they would if the rate base were a million dollars, all other things being equal?

A. In theory, yes. As to how much that will impact the actual rate to the customer, if you're looking at only $30,000, I don't know how great of an impact that will be to the customer.

Q. You understand we're talking about one asset here?

A. Yes.

Q. So the ratepayer gets the benefit of a $30,000 reduction to rate base through accumulated depreciation that he still hasn't paid on until January 1 of 2004, right?

A. The company's new rates will not go into effect until January 1, 2004, yes.

Q. But the ratepayer gets the benefits of $30,000 of accumulated depreciation that it never paid, right?

A. Well, again, depreciation is not a cash outlay. So there was no cash involved to pay one way or the other.

Q. The investors laid out a million bucks for that plant, didn't they?

A. Well, there's a reduction to the rate base, but that rate does not hit the customer until January 2004 also.

Q. My question is, there was a cash outlay of a million bucks in December of 2002, right?

A. Correct. And that plant is included in the rate base.

Q. A year later, right?

A. Well, it's included in the rate bases for purposes of creating the new rates, for developing the new rates.

Q. It's included in rate base for purposes of recovery of depreciation, as well as recovery of return a year later, right? I thought we got this established earlier.

A. Yes. And you're confusing me. So let me think about this just a minute.

The new asset is in rate base. There is a reduction for the depreciation up to that point through the update period. It does reduce the overall cost of service to which a rate of return is applied. So, yes, there would be less money collected. Let me think. The company is recovering the asset through the rate base. They are making a return on the rate base.

Q. That's not my question. They're not getting the return until January of 2002 -- excuse me -- 2004?

A. That's when they will start earning a return, yes, based on the new rates.

Q. And that's when they'll start getting back the depreciation as well, right? Until that plant is reflected in rates, the rate -- or excuse me -- the investor does not realize a return on or a return of its investment?

A. Correct.

Q. Okay. And that would be January of 2004, under our hypothetical?

A. Correct.

Q. Okay. Now, one other question I don't think I got an answer to. There was a cash outlay of a million bucks back in December of 2002, correct?

A. Yes, there was a cash outlay.

Q. By the investor?

A. Yes.

Q. Okay. And when they finally -- the investor finally gets to realize a return on that investment in January of 2004, that investment is only $970,000 because of our mid-year test year, right?

A. On the books, that's what it is, yes.

Q. And for ratemaking purposes, that's what happens, correct?

A. In rates, that's true, but they are getting a full recovery of that asset through the depreciation expense.

Q. A year later, right?

A. Due to regulatory lag, yes.

Q. And they're not realizing a full return on their investment because it's been reduced by $30,000 for accumulated depreciation that the ratepayers never had to pay for, as of January 1, 2004?

A. In the context of rates, no, they would not be getting a recovery on that $30,000.

Q. Thank you.

Let's talk briefly about property tax, if we can, and how you've handled it for cash working capital purposes. I believe you address it at page 22, lines 9 through 11 of your direct testimony.

MR. KRUEGER: Your Honor, I don't believe that the effect of property taxes on cash working capital has been identified as an issue in this case. The statement of the issues presented mentions only the management fees, depreciation and deferred taxes. So I think it's going beyond the scope of the issues that are to be presented.

MR. ENGLAND: I think it's in your testimony. I'm required to ask -- entitled to ask about it, and it does affect the property tax issue, which you will be hearing later. And as Mr. Grubb indicated, there is an alternative cash working capital issue associated with it.

JUDGE THOMPSON: As I recall in the 281 case, we were remanded for failing to address an issue having to do with the size of mains that was never identified in the issues list. So I'm going to allow the question. The objection is overruled.

BY MR. ENGLAND:

Q. Do you have your testimony there in front of you?

A. What page again, please?

Q. 22.

A. Yes.

Q. Did I give you the right line number? I think it's 9 through 11.

A. That's my answer, yes.

Q. You've calculated an expense lag of approximate -- not approximately of 182.5 days, correct?

A. Right. That's assuming a service period of a calendar year.

Q. Now, you offset that expense lag of 182.5 days with the revenue lag of approximately 63 days to arrive at a negative cash working capital allowance for property taxes, at least in the St. Louis district, correct?

A. I believe that is true for the St. Louis district, yes.

Q. In other words, because it's a negative cash working capital allowance, and as we discussed earlier, you believe these are ratepayer supplied funds, right, on balance?

A. Are you speaking just to the St. Louis County district or --

Q. Yes.

A. Let me double check that schedule.

Q. I think it's the same for all districts, but I'll focus on St. Louis County.

A. Yes, property taxes in the St. Louis district, according to Staff's schedule, is a negative $2,297,942.

Q. And that's the net effect of the expense lag of 182.5 days versus the revenue lag of roughly 63 days?

A. Correct.

Q. Okay. In essence, what you're saying here is that the tax is precollected from the ratepayers before the company has to pay it, correct?

A. Correct.

Q. Now, let's go back to my earlier hypothetical, a utility who filed a rate case on February 1, 2003 with an operation of law date of January 1, 2004. Remember that?

A. Uh-huh.

Q. Assume further that the Commission only allows the utility to recover its last actual and known property tax expense incurred in December of 2002. Okay?

A. Uh-huh.

Q. So for purposes of the rate case, all it is allowed to recover is the tax that it incurred in 2002, not the tax or property tax it's supposed to pay in December of 2003, the month before the rates become effective, correct?

A. Well, I'm not the witness for property taxes in this case, so I don't feel qualified to answer your question. I think that would be better answered by, I believe, Mr. Doyle Gibbs.

Q. Well, it's just a hypothetical, and I'm hoping that the facts of the record will bear it out. I think they will. But under my hypothetical, isn't that true?

MR. KRUEGER: Your Honor, I object. She's still not the witness that's testifying about property taxes.

JUDGE THOMPSON: Well, as we've often ruled in these cases, if the witness knows, the witness must answer. Therefore, I'll overrule the objection. If you know, you must answer.

THE WITNESS: I do not know.

JUDGE THOMPSON: Thank you.

BY MR. ENGLAND:

Q. Do you know what property tax expense you have allowed or used for purposes of your cash working capital allowance?

A. I can tell you the dollars for each district that Staff put into the schedule, but I did not calculate those dollars.

Q. So you don't know if those dollars are based on property taxes actually paid in December of '03 or to be paid in December of '04; is that right?

A. I do not.

Q. If they were property taxes to be paid in December of '03 and rates are set in this case to become effective roughly in April, how would we be precollecting that from our ratepayers when rates go into effect in April for an expense we paid back in December of '03?

A. Could you state that again?

Q. I'm going --

A. Make sure I'm following you here.

MR. ENGLAND: Can I have that read back?

JUDGE THOMPSON: Absolutely.

THE REPORTER: "Question: If they were property taxes to be paid in December of '03 and rates are set in this case to become effective roughly in April, how would we be precollecting that from our ratepayers when rates go into effect in April for an expense we paid back in

December of '03?"

THE WITNESS: Well, if rates are going into effect in April of '04, I'm assuming that any tax or property taxes that are included in rates would be taxes that were known and measurable and paid at that point in which rates were agreed upon. Whether that would include the December 2003 taxes or not, I wouldn't know without being the witness that prepared those numbers.

BY MR. ENGLAND:

Q. My question assumes that that property tax is based on what was paid in '03.

A. So you're assuming that the test year, the update period goes through the end of December 2003?

Q. I'm just saying that for purposes of this case, the property tax expense is based on the property tax expense that was actually paid in December of '03.

A. And you were asking how we could assume those were prepaid?

Q. Right. Aren't we collecting it after the fact, Ms. McKiddy?

A. The expense lag I have in the case is after the fact, 182.5 days is after the fact.

Q. But it's a negative rate base -- or negative cash working capital, which we agreed indicates that it has been precollected or paid by the ratepayer.

Let me ask you --

A. Looking solely at that one line item, that is true. If you're looking at cash working capital in totality, it may not be that we're collecting cash working capital from the ratepayers.

Q. Let me ask you this --

A. I mean, actually in St. Louis County district, I believe, the cash working capital revenue impact is positive, not negative, which means that the shareholders are providing that.

Q. For property taxes?

A. No. For cash working capital in total.

Q. I'm just talking about the line item. I understand there are other things that balance it out, but for purposes of property taxes you've assumed that it's prepaid, right? You've got a negative 2 -- roughly $3 million cash working capital allowance?

A. Based on the information given to me to calculate the revenue requirement, yes, that is true.

Q. So the ratepayers get the benefit of a $2.3 million reduction in cash working capital, right?

A. Again, you're looking only at that one line item. When you look at all cash working capital line items, there may not be that same benefit there.

Q. I understand.

JUDGE THOMPSON: Mr. England, what is the document you're referring to?

MR. ENGLAND: I'm looking at the Staff accounting schedule. I'm not sure if I know the exhibit number.

JUDGE THOMPSON: It's Exhibit No. 25. And what tab are you in?

MR. ENGLAND: I am in the St. Louis tab, and it's Accounting Schedule 8. As a matter of fact, cash working capital is Accounting Schedule 8 in all the districts.

JUDGE THOMPSON: Thank you. And the line you were looking at?

MR. ENGLAND: Line 26.

JUDGE THOMPSON: Thank you very much. You may proceed.

MR. ENGLAND: Thank you. I forgot where I was.

JUDGE THOMPSON: You were at line 26, Schedule 8.

MR. ENGLAND: Work with me here.

THE WITNESS: I believe we were on the St. Louis County schedule.

BY MR. ENGLAND:

Q. Okay. For purposes of St. Louis County district, you have calculated a negative cash working capital allowance of roughly $2.3 million for property taxes, correct?

A. For property taxes, that is true.

Q. Which is a reduction to rate base, correct?

A. If you were looking solely at that one line item, yes, that would be a reduction.

Q. Fair enough. And what that reflects in your calculation is a precollection of those monies from the ratepayers, in other words the ratepayer supplied funds, right?

A. Yes. As it relates to the revenue lag versus the expense lag, that would be ratepayer supplied funds.

Q. Now, let me get back to my hypothetical. What if the property tax expense allowed in this case is based on December of '02? We didn't even get '03. We're really behind the gun in collecting property taxes, aren't we, Ms. McKiddy?

A. I would have to assume that if they were not allowed in the case, it was because they were not known and measurable and paid at the point when the case update period was designed.

Q. Do you know if our property tax is increasing, decreasing or bouncing around from year to year?

A. I don't know. I wasn't the witness on that issue.

Q. Okay. Let's talk about management fees, if we can for a second. Probably more than a second. I think it's been referred to as in a couple places interchangeably as management fees or service company charges; is that right?

A. I believe that's probably accurate.

Q. If we stay on your same Exhibit 25, St. Louis district's Accounting Schedule 8, it's listed as item number -- or line No. 11, management fees, I believe, although in your testimony at page 18, lines 12 through 18, you refer to it as service company charges. I just want to make sure that we -- if we start jumping back and forth, we're talking about the same thing here.

A. Yes, we are.

Q. Now, is it fair to say that when you performed your first calculation for purposes of direct testimony, you were under the assumption that these fees were paid in arrears?

A. Yes. The information I was supplied in Data Request responses from the company indicated that those fees were paid in arrears.

Q. And then I think you indicated in surrebuttal that during prehearing conference you were made aware of the fact that these charges were actually paid in advance, right?

A. I was presented a schedule during the prehearing conferences that indicated prepayment to a certain degree. In some instances they were not. It depended on the amount billed for that particular month.

Q. To a large degree they're prepaid, correct?

A. I'll just say that there were some prepayments. I don't know whether there was six months of the year or nine months of the year they were prepaid.

Q. But now in your surrebuttal testimony, if I understand it, you still stick by your calculation, except your reason for including an expense lag here is that, quote, it is inappropriate for MAWC to prepay its affiliate for services not yet rendered, end quote, right?

A. Correct. Because we believe it is an expenditure very similar to other expenditures that fall in the cash vouchers category that do not require prepayment for those services.

Q. I just want to get the sequence of events correct here. In your direct testimony, you were under the assumption that these were not paid in advance, they were paid in arrears, so you did your lead lag study and determined that there was a 290,000, at least for purposes of the direct case, cash working capital allowance associated with this, right?

A. Correct.
Q. Now, without any judgment as to whether or not it's appropriate to prepay, would you agree with me that if we, in fact, do prepay it, this calculation has to be adjusted and that cash working capital allowance increased?
A. If we agree that the company's calculation is correct and appropriate, then yes, that number would change.
Q. Okay. Again, I want to get the sequence of events. For direct testimony, you were under the assumption these were not paid in advance; is that right?
A. Based on information supplied by the company, yes, it showed that payments were not paid in advance, they were paid in arrears.
Q. Okay. Then in prehearing conference, you were made aware of the fact that some of these charges were paid in advance, correct?
A. I was presented a schedule that showed some payments were made in advance, yes.
Q. Then in surrebuttal testimony you said, well, that's okay, I'm keeping my same adjustment, but I'm going to disallow it basically because I don't think they should be prepaying these expenses, based on the testimony of Staff Witness Cassidy?
A. Well, at the time of surrebuttal we had no evidence to show that the company was required to prepay for

those services, so we chose to use the cash vouchers lag as an appropriate substitute, rather than using the original information provided by company for payment of management fees.

Q. And I think you reference Mr. Cassidy's testimony as kind of a basis for this determination that it's not appropriate to prepay these expenses, right?

A. Correct.

Q. And that was in his surrebuttal, right, that was the first time we saw that?

A. I believe that's true.

Q. I mean, it seems to me that you had already predetermined you weren't going to allow this and you've changed position in order to justify that. Is that a correct perception?

A. No. I think it's always been Staff's position that payments to affiliates should not be prepaid. I don't know that we made any special consideration to just subject Missouri-American to that way of thought.

Q. By assuming that we should be paying it in arrears and not adjusting our cash working capital allowance, we got less cash working capital allowance, right, than we otherwise would?

A. I believe that's true.

Q. And Mr. Cassidy has made other downward adjustments in our actual affiliate charges for what he considers to be inappropriate affiliate transactions, right?

A. I'm not sure what Mr. Cassidy has done.

Q. Well, assuming that he did, this is an additional penalty or disallowance, if you will, for inappropriate affiliate transactions, is that the bottom line?

A. I think the reason we have declined or not adopted the company's prepayment fees is that we've not been shown any evidence to show that it results in any benefit to the ratepayers, and also we've seen no evidence to -- to indicate that the company's required to make prepayment. So we're not sure what the -- what the cost savings or benefits of doing so really is.

Q. You've also seen no evidence that they can't get these services at a better price, have you?

A. I don't --

Q. From outside vendors?

A. I don't believe we've been given any outside bids to compare with what the affiliate company provides.

Q. So you don't know whether or not this is a good deal or not, even though they may have to prepay?

A. I personally do not know because I did not do that analysis.

Q. Getting back to my question, so we're getting penalized twice, if you will. We're getting disallowed money in the cash working capital allowance for this affiliate transaction, and then we're also losing dollars in the affiliate transaction issue adjustments?

MS. O'NEILL: Your Honor, I'm going to object to the use of the word "penalty." I don't see anything in Ms. McKiddy's testimony that suggests that any penalty should be paid. I don't think he's properly characterizing her testimony.

JUDGE THOMPSON: Objection is overruled and I will admonish the witness to please respond yes or no to the questions. Thank you.

THE WITNESS: Could you repeat your question then, please?

MR. ENGLAND: I'll try.

BY MR. ENGLAND:

Q. My question is -- and if I could come up with a better, less pejorative word as penalize, I would, but perhaps I'm a little overdefensive. In essence, we're losing money, if you will, in the rate case setting twice, once in a lower cash working capital allowance and second in a lower affiliate transaction adjustment or amount?

A. I will agree that I'm not giving the company a benefit in the cash working capital amount. As to the other adjustments, I don't know if you're being penalized twice as you characterize it. I just don't know the answer.

Q. But you know that if you were to allow us or to recognize -- excuse me in your cash working capital allowance the fact that some of these expenses are being prepaid, we would have a -- or you would have calculated a larger cash working capital allowance?

A. If I recognized the company's negative 3.31 days as the expense lag for management fees, yes, that would be true.

Q. Now, would you agree with me that it's not unusual for a utility to prepay expenses to independent, unaffiliated third-party vendors?

A. As I mentioned earlier, I believe it's appropriate to prepay for things like insurance. I don't know that services to affiliates or third parties is prepaid on a prepaid basis. I don't know that to be true.

Q. You don't know that companies pay outside witnesses, such as rate of return witnesses, a prepaid amount up front for their testimony and analysis?

A. I've not read the contracts between company and those witnesses, so I don't know what the payment arrangement is.

Q. Would you agree with me that companies often pay rent in advance?

A. I would agree that would be true, yes.

Q. It's not unusual for them to pay some types of expenses in advance; is that right?

A. Rent and insurance would be two examples, yes.

Q. Okay. Have you examined any outside vendors who provide services similar to the company to determine whether they offer discounts for prepayment or require prepayment?

A. No, I have not done that examination.

Q. Okay. Would you agree with me that if a vendor does not collect fees in advance but rather in arrears, then it will have an increased need for cash working capital itself in order to fund the additional lag in the receipt of revenues from its supplier -- or excuse me -- customer?

A. It would be fair to assume that they would need cash working capital.

Q. In response to a question from Commissioner Murray, you were talking about the cash working capital associated with management fees and something about a 25 percent discount. I'd kind of like to put this in perspective, if I can.

Counting Exhibit 25, total district, it's the -- do you have that? I'll give it to you here in a second, if I get to the right page. I think it's Accounting Schedule 8, shows the cash working capital for all of the districts combined.

MR. ENGLAND: May I approach the witness?

JUDGE THOMPSON: You may.

THE WITNESS: I think I may have that page updated.

BY MR. ENGLAND:

Q. Well, then, good, because that was going to be my next question. I'm just going to focus on the management fee line, if I can. I don't know if that's changed. In Exhibit 25, the total test year expense for management fees, line 11, is roughly $7.9 million. Is that the same in your updated case?

A. That is the amount of test year expenses. The capital revenue requirement for that line item is 742,090.

Q. That's because some days changed, right, either a lag or expense or --

A. We changed our lag from, I believe, 42 days down to 21.41 days.

Q. We still have a significant difference, though, between company and Staff, as I understand it?

A. I believe that is true.

Q. Roughly $114,000 on revenue requirement?

A. That sounds about right.

Q. Okay. And getting back again, the total test year management fee expense, that's that 7.9 million figure in column B, line 11?

A. Right. That's the number that was here, but I did not calculate that number.

Q. Okay. But you assume what's been provided to you by other Staff members rather?

A. Yes.

Q. And you assume it's correct?

A. I assume, yes.

Q. Okay. So $114,000 of an additional cash working capital allowance as it relates to the 7.9 total test year expense is, what, maybe 1.5 percent?

A. Sounds about right.

Q. Okay. A lot better than the 25 percent add on, correct?

A. Yes.

Q. Thank you.

In your surrebuttal testimony you indicate that you looked at how the company calculated cash working capital in the last St. Louis County rate case?

A. Yes.

Q. Do you recall that?

A. I looked at Steve Hanneken's schedules presented in that case.

Q. Okay. Did you also look at how Staff calculated cash working capital allowance as it pertains to service company charges or management fees, as we've discussed, in the last Missouri-American Water rate case, WR-2000-281?

A. No, I don't believe I did.

Q. Okay. You don't know whether or not Staff -- Staff's cash working capital allowance in the last Missouri-American water rate case was similar to -- at least insofar as service connection fees were concerned was similar to what the company's done in this case?

A. I don't know that.

Q. Okay.

MR. ENGLAND: Your Honor, may I approach the witness?

JUDGE THOMPSON: You may.

MR. ENGLAND: Let the record reflect that I'm handing her Staff accounting exhibit from that last case, I believe it was Exhibit 55.

JUDGE THOMPSON: Is that from the 281 case?

MR. ENGLAND: From the 281 case, yes, sir.

BY MR. ENGLAND:

Q. I think it's still Schedule 8 in each of those districts. Perhaps St. Joe, since there was no St. Louis district in that case. Pick any district.

A. I have to, because total company is showing nothing. Okay.

Q. Actually, just to clear up the record, total company says refer to each individual district, correct?
A. Yes. It says it's the sum of cash working capital for operating districts.
Q. Thank you. Take the St. Joe district for example, Schedule 8.
A. Okay.
Q. Is there a line item for management fees or service company charges as we've been talking about?
A. Yes, line 7.
Q. And what is the associated lag, please, or what are the associated lags?
A. The revenue lag is 57.01 days and the expense lag is a negative 4.13 days.
Q. Assuming I handed you a correct copy of the exhibit in that case, would you agree with me that Staff's approach in that case is roughly the same or essentially the same as the company's approach in this case?
A. My understanding is that Staff accepted company's approach in that case, but it was because there were a lot less dollars involved.
JUDGE THOMPSON: Ms. McKiddy, is that a yes or a no?
THE WITNESS: Yes.
MR. ENGLAND: Thank you, your Honor.

BY MR. ENGLAND:

Q. So is it fair to say, at least for purposes of the last case, that Staff accepted without question the fact that these charges were paid in advance and reflected them as such in the cash working capital allowance?

A. For purposes of the last case, it does appear that they did accept that approach.

MR. ENGLAND: Thank you, Ms. McKiddy.

Your Honor, do I need to have official notice taken of that accounting schedule?

JUDGE THOMPSON: Why not.

MR. ENGLAND: I would propose that I just do the cash working capital schedule, which is a one-page schedule, but if other people want other schedules from that case, I have no objection.

JUDGE THOMPSON: Why don't we do this: Why don't we reserve Exhibit No. 128 for the particular page you were inquiring about. I believe that was the Schedule 8.

THE WITNESS: Schedule 8, St. Joseph district.

JUDGE THOMPSON: St. Joseph tab. And it's WR-2000-281.

MR. ENGLAND: And we'll just make copies and distribute them after lunch.

JUDGE THOMPSON: That would be great.

MR. ENGLAND: Thank you. And with that, I have no other questions.

JUDGE THOMPSON: Thank you. It's now five minutes after the hour. We have redirect to go through, and there may be some questions from the Bench on property tax. I don't know. We will take the lunch break at this time. Why don't we return at 1:15.

Mr. Coffman?

MR. COFFMAN: Your Honor, the much-anticipated rate design settlement document has been filed through EFIS and I have a hard copy here if the Commission would like to peruse it over lunch.

JUDGE THOMPSON: That would be a wonderful thing.

MR. COFFMAN: It has been the expectation that there would be a presentation of sorts at 1:30 or thereabouts.

JUDGE THOMPSON: That would be fine.

MR. COFFMAN: Most of the other parties are anticipating that that would be the opportunity for them to come and answer any questions you had of them.

JUDGE THOMPSON: That would be great.

MR. KRUEGER: Your Honor, I would also add that the Staff intends to provide comments on that stipulation, and we hope to have that as soon as possible, by one o'clock probably, so the Commission can review those prior to the time of the presentation.

JUDGE THOMPSON: Very well. So you plan to file a written document as well, prior to 1:30?

MR. KRUEGER: That's correct, your Honor.

JUDGE THOMPSON: Why don't we then return at 1:30, rather than 1:15.

Thank you. We are adjourned.

(A BREAK WAS TAKEN.)

JUDGE THOMPSON: Mr. Coffman, do you have something to report?

MR. COFFMAN: I do. Your Honor, if it would please the Commission, I would suggest or offer myself to present --

JUDGE THOMPSON: Now you can go ahead. I wouldn't want our viewers in Germany to be unable to see what's going on. Please proceed.

MR. COFFMAN: They do have a lot riding on this case.

I was offering myself to make just a brief overview of the Stipulation & Agreement as to rate design which was filed through EFIS just earlier, and I think you-all have a copy. If anyone else needs a copy, I have a stack there on the front desk.

Then I would -- of course, we can proceed however the Commission would like. I think there are several experts or representatives of the parties that would be able to comment regarding how the stipulation affects the interest that they care the most about.

We, as the Office of the Public Counsel, initiated settlement discussions over a month ago in earnest to try to resolve this. Most folks didn't think it could be done, given the large variety and diverse nature of the interests.

It really was a difficult issue to settle because of those diverse conflicting issues, because of the multi-districts and because there is no revenue requirement settlement to apply. So that was one of the more difficult aspects of this. But just to very briefly make sure that this is understandable, I'll try to, in simple terms, explain where this settlement goes.

First of all, we have revenue neutral adjustments to most of the districts, and those correspond to Attachment 1A through 1F. They show some adjustments primarily to benefit sale for resale in each of these districts, and this was an adjustment that most of the parties saw as fair, and to a large degree corrects or revises, adjusts the rather large hit that this customer class took in many districts.

I'm sure Mr. Fischer will be glad to tell you exactly how much; I believe it's a 239 percent increase for the sale for resale customers, the water districts that buy from the St. Joseph district.

So there was some relief that everyone was willing to apply there. Primarily that comes from residential and commercial customers. You will see on these exhibits that there is a volumetric percentage change, which is the next-to-the-last column, and that's -- which is discussed in that paragraph 1. The last column on the right then shows approximately the percentage, the revenue neutral change to the class itself, which will be different.

If you look at Brunswick, for instance, there's a 3.78 percent increase to the residential class to accomplish a 5 percent reduction to sale for resale. The overall percentage change is less than that 2.5 percent increase, and that is because there will be no change in the minimum charge, the customer charge of the bill. And I could go over some of these other adjustments.

One other, I guess, typo that occurred, just a label that is missing, on the Parkville Attachment 1D. You'll note the last section of numbers down there does not have a heading. Just above it there is other public authority. The heading on that last group of numbers, the last four blocks that should apply to sale for resale, so that's just missing a heading.

After these adjustments to revenue -- we call these revenue neutral adjustments -- are made -- and by the way, they are not made to the rates in the Jefferson City district, the St. Charles district or the St. Louis County district. It was not -- there was not such disparity that anyone thought that there needed to be these type of adjustments there. I will note that later on in the process there is a very minor adjustment to the Jefferson City rates, and I'll get to that later.

The main operative paragraph in this stipulation is the paragraph 2, which is called the revenue requirement adjustment. That tells you how any revenue deficiency or revenue requirement excess would be applied in this case.

Essentially any rate increase or rate decrease would be applied to each customer class or revenue classification equally, and then within that class, after that percentage increase or decrease is determined, would then be applied to the volumetric components, the meter charge, the customer charge. In other words, the flat rate portion of your bill would remain the same. And if there was, say, a 5 percent change, that whatever percent would be needed to each of the volumetric components equally would be made so that the entire class received a 5 percent change. Hope that's clear.

There is one interdistrict revenue

contribution that I hadn't mentioned, and that is essentially from the rate, customers of St. Louis County to the Brunswick district. And there's been much talk over many years about the interdistrict issues, subsidies, contributions between districts. My office favors the district-specific method that the Commission had adopted in the last case, except in situations of very dramatic rate shock and that some contribution seems reasonable to mitigate what would otherwise be dramatic increases.

The one district that would, under most cost of service studies performed in this case, receive a rather large impact -- and that would be the Brunswick district. I believe most studies showed them receiving more than a 100 percent increase as a result of this case. To mitigate that, the parties were all in agreement that Rate A customers of St. Louis could contribute without barely noticing $213,000 contribution, which, depending on how some other issues play out, would be a more manageable increase, 15 percent or so to the entire Brunswick district as far as an increase.

The impact, I believe, to the Rate A customers in St. Louis, which were essentially the residential and small commercial customers, the revenue neutral impact for them would be somewhere in the range of .2 percent. That would be rather small and appeared to be overall fair in this case.

Apart from that, the parties are in agreement that there shall be no other interdistrict revenue contributions, and that was important to several parties.

Paragraph 4 talks about public fire hydrant charges. It's my understanding that only the St. Louis County district has a separate, broken-out charge for public fire hydrants. Essentially the status quo will be maintained. That's a charge that will stay in St. Louis County. No other charges would be created as the company had proposed.

Paragraphs 5 and 6 call for studies and information to be collected to allow potentially some exploration of customer class definitions, perhaps in the next rate case. And then bill consolidation will be studied in a rather limited way, and that would be consolidation of bills for one customer that has contiguous properties. And the evaluation will include what impact that would have on other customer classes, but it's something that is important to some attorneys here and some clients. They would like to look at that.

No. 7 is interruptible rate, and this is something that was opposed by Staff and something that we had some concern about in my office. The rates, terms and conditions of the tariff that would apply to this interruptible rate in the Joplin district were extensively negotiated between Empire District Electric, which would be the customer, between the water company and my office and the representatives of the City of Joplin.

And it's our belief that this is a fair settlement that is narrowly tailored only to the Joplin district, where there is some concern about future water supply, and where we have a customer there that apparently does have storage and supply to cover an interruption and is willing to enter into the terms that you see here, a 15-year term and minimum taker pay provision of half a million dollars.

The elimination of the minimum usage amount, paragraph 8 refers to the Jefferson City district. It is my understanding that only the Jefferson City district has what's called included usage in the minimum charge. The meter charge includes 100 cubic feet a month of water. And I talked to customers before that have a problem with that. They often complain that they have to pay for water even before they use it. Another way you can look at it is that you get 100 cubic feet free, but it's inconsistent with the other districts.

I think everyone that addressed this issue supported eliminating it and adjusting the rates accordingly. What this would do would be take out the minimum usage, the meter charge and just a fixed charge and don't include the water, and then adju-- the next volumetric block is adjusted to make up that difference. So it's the expectation that there would be hardly any noticeable change in anyone's bill as a result of this change.

Connection fees for new service, that was a company proposal no one opposed. The rest of it is the typical boilerplate that lets you know that no one here is in agreement to any of this as a matter of principle whatsoever. It is reached only for the purpose of settlement, and that was no small feat.

Hope that covers everything generally enough. I know we have limited time, so I'll just sit down, unless there's some questions of me.

JUDGE THOMPSON: Thank you, Mr. Coffman. Questions from the Bench, Chairman Gaw?

CHAIRMAN GAW: Are you going to do this for each representative that signed off on this, have a presentation?

JUDGE THOMPSON: I wasn't planning to.

CHAIRMAN GAW: Are you just going to open it up for questions?

JUDGE THOMPSON: I was just going to open it up for questions.

CHAIRMAN GAW: I just wanted to make sure. I didn't want to be redundant. Thank you.

Let me ask, who's here for Joplin?

MR. ELLINGER: Marc Ellinger.

CHAIRMAN GAW: Mr. Ellinger, if you would come up for just a minute.

MR. ELLINGER: Sure.

CHAIRMAN GAW: Give me your impression of this from Joplin's standpoint.

MR. ELLINGER: Joplin's very actively involved in this because of the interdistrict revenue contribution issue, which has really been the crucial issue for Joplin. We think that the stipulation, especially with respect to language relating to the contribution of Brunswick and the affiliated paragraph No. 3 is very fair to the consumers of Joplin.

It's been presented to the council members down there, and they all believe it's very fair. And as a result, the City signed off -- authorized me to sign off on it, and we think that it's a good stipulation for our consumers.

CHAIRMAN GAW: Obviously you've signed off on this concept in dealing with Empire getting an interruptible rate. Were you supportive of that concept to begin with or was that a compromise for you?

MR. ELLINGER: We had concerns about it

initially. We worked through a number of drafts on the tariff sheet. Also worked with the Office of the Public Counsel on that issue and talked it over extensively with the City. And I think we're comfortable with what the tariff sheet came up to in the end.

CHAIRMAN GAW: Okay.

MR. ELLINGER: For a one-time purpose. It is really only for this particular situation. If some other customer were to try to have a similar interruptible rate convert, then that would be addressed in a separate rate case.

CHAIRMAN GAW: Does this -- do you believe that this does anything in regard to -- did you get any impression in regard to this having any impact on future plant build for Joplin?

MR. ELLINGER: The overall stipulation or the tariff?

CHAIRMAN GAW: In particular the -- the Empire -- the Empire portion of this. Is there some understanding or any belief that that had anything to do with the necessity of new construction?

MR. ELLINGER: No. There was no discussion with respect to the City of Joplin being involved as to whether this implied that there should be a new plant or new construction or, conversely, if by having the interruptible rate would alleviate the need for any new construction.

CHAIRMAN GAW: That's all I have. Does anybody want to ask questions of this attorney while we're on it?

MR. ELLINGER: Thank you.

CHAIRMAN GAW: Thank you very much.

JUDGE THOMPSON: Thank you, Mr. Ellinger.

CHAIRMAN GAW: Who's representing Brunswick? Does Brunswick have counsel? Where is Brunswick's counsel?

MR. COFFMAN: Me, I guess.

CHAIRMAN GAW: You know, this says something. I'm not sure what it says.

MR. COFFMAN: It was kind of a joke that Brunswick does fairly well without representation.

CHAIRMAN GAW: That's where I was going,

MR. COFFMAN: I guess I'm probably the only one here that would purport to represent customers in Brunswick.

CHAIRMAN GAW: I would claim that, I think. Anyway, give me an idea. I know we don't have -- obviously we don't have the rest of the case, so how does this -- again you've got -- you've got the percentages in here in regard to the increases. Do you know what that means to an average customer if -- assuming there was no change in everything else, which obviously is --

MR. COFFMAN: You need to look at the -- well, it's hard to know without a revenue requirement.

CHAIRMAN GAW: It really is. But you make an assumption it's consistent, though?

MR. COFFMAN: I believe even with the Staff's recommended revenue requirement reduction, there's still a very significant increase in Brunswick. And although it may be somewhat different than this percentage, it was -- the number that is the 213,000 was -- was developed with a target of essentially 15 percent that we thought would be a nice cap, as far as 15 percent increase in the district. It may wind up more or less than that. I don't know.

CHAIRMAN GAW: But did anybody -- again, I know there's no revenue issue resolved here, but did anyone run a number on an average customer impact if revenue remained consistent with what it is today?

MR. COFFMAN: For the Brunswick district?

CHAIRMAN GAW: For an average customer. I don't know that I expected you to. I'm just asking if someone did that.

MR. COFFMAN: I didn't do that.

CHAIRMAN GAW: All right.

MR. COFFMAN: I might point out --

CHAIRMAN GAW: You're the only one that probably would have, I think.

MR. COFFMAN: One other caveat that I didn't mention earlier: There are certain billing determinants, revenue numbers and customer numbers that are used in developing these sheets, and those numbers may be subject to some change based on the true-up, and so there is still some slight change that could occur as a result of numbers being trued up, customer numbers, revenue numbers being adjusted. I just wanted to bring up that, make sure you were aware of that.

CHAIRMAN GAW: All right. Thank you.

Who was pushing the issue of getting rid of the Jefferson City charge on the -- where there's a certain amount of water that you get for no additional payment? Who pushed that being changed from what it is today?

MR. COFFMAN: I believe it was recommended by Staff, Public Counsel and the company.

CHAIRMAN GAW: Everybody, the Staff, Public Counsel and the company, all three of you thought that should be the case? Is that generally the principle that you-all go by on these cases? I realize it's in the whole scheme of things might not seem large, but I can see that being an issue that people want to talk about.

MR. COFFMAN: It's not been a litigated issue that I can recall, but I have heard customers complain about it and ask questions about it because they don't understand it.

CHAIRMAN GAW: Yeah. I think customers -- that you may hear customers complain about the changes, too.

MR. COFFMAN: It would be my expectation it really wouldn't be noticeable.

CHAIRMAN GAW: Tell me how you think it won't be noticed and that maybe will help me understand it better.

MR. COFFMAN: Because where now Jefferson City customers receive 100 cubic feet free and they won't now, the next block rate will be adjusted in such a way that -- downward to the point that you would receive the same billed amount each month for the same usage.

CHAIRMAN GAW: That's assuming --

MR. COFFMAN: Unless you don't use it. I mean, the only one --

CHAIRMAN GAW: If you don't use very much water, then you'll get an increase out of this change?

MR. COFFMAN: If you're gone this month on holiday and you use no water, then you might notice a slight change, but this isn't a lot of water. We were trying to figure out how much. It's about two baths a week.

MR. CONRAD: Speak for yourself.

CHAIRMAN GAW: I'm not going down that road. Okay.

MR. COFFMAN: If you want a more expert

opinion, we do have rate design experts who can testify.

CHAIRMAN GAW: I think you've explained it just fine. Is it correct -- and maybe you can answer this. Is it correct that the blocks are staying basically the same as they are currently in all of the districts?

MR. COFFMAN: There's one exception to that.

CHAIRMAN GAW: Okay. Go ahead.

MR. COFFMAN: Mr. Finnegan representing the Platte County, Parkville district might.

MR. FINNEGAN: Do you want me to start on that?

CHAIRMAN GAW: Wherever you'd like.

MR. FINNEGAN: As far as Riverside is concerned, I not only represent Riverside -- that's who I've intervened for -- but I've since that time been supported by the City of Parkville, and also by Lake Lacomis and Public Water Supply District No. 6, which are resellers of water. Parkville and Riverside both get their water directly from the company. We also have some other users that have contributed.

The whole idea was to get back to where we were before the last rate case with -- as far as the rate design. So, and what we've gotten here is a single rate -- four-block rate for all customers, and although there seems to be a rather large increase for the industrial class, if you look at the class, for one thing the total revenues is $12,000 now, going to 18,000.

CHAIRMAN GAW: Tell me where you are. Okay. I'm with you now.

MR. FINNEGAN: Attachment 1D.

CHAIRMAN GAW: Thank you, for purposes of the record.

MR. FINNEGAN: Attachment 1D. It's a very small industrial class. They don't even get into the third block, much less the fourth block, and if you look at -- I have a little chart here I'll pass out that will show what the increases were the last case, if I may.

JUDGE THOMPSON: You may.

MR. FINNEGAN: Basically it shows that there was about a 67 percent increase overall for the district, and among the customer classes, the residential class received less, the commercial class received less, the industrial class only received about a 25 percent increase instead of 67. The other public authorities received more than the average and the OWU, which is sales for resale customers, other water utilities, received a substantial, like, a 170 or 165 percent increase.

What this does here is what we wanted to have done, and it's to equalize the rate, get it back to this line to start with, and then the increases will go on a percentage basis, a volumetric percentage basis within the blocks.

CHAIRMAN GAW: Who was -- whose clients are those that got that 40 percent --

MR. FINNEGAN: The other water users?

CHAIRMAN GAW: No. The industrials.

MR. FINNEGAN: That's in the Riverside district.

CHAIRMAN GAW: Okay. So you've got them, too?

MR. FINNEGAN: Yes.

CHAIRMAN GAW: All right. That's all I have on that, I think.

MR. FINNEGAN: Okay. Thank you.

CHAIRMAN GAW: Thank you.

JUDGE THOMPSON: Thank you, Mr. Finnegan.

CHAIRMAN GAW: I may be done, Judge. Just a second. I am done, unless you want me to inquire of Staff at this point, or I'll wait. Whatever you want to do.

JUDGE THOMPSON: Commissioner Murray, you would be next up. Would you prefer that Chairman Gaw inquire of Staff or would you like to ask?

COMMISSIONER MURRAY: That would be fine. I don't have very many questions.

CHAIRMAN GAW: Okay. I guess all I want to do is just get feedback from Staff at this point, and obviously you-all are not signing off on this. And I briefly had a chance to review the comments. I'm just trying to see if there's anything that you-all want to add to this issue of trying to get to a better understanding of why Staff is choosing not to sign. I understand you're not objecting. I'm just trying to get a better understanding about why Staff has chosen not to sign the stipulation.

MR. JOHANSEN: Do I need to come up?

JUDGE THOMPSON: Yeah, why don't you come on up to the witness stand, Mr. Johansen. Spell your name for the reporter.

MR. JOHANSEN: J-o-h-a-n-s-e-n, Dale Johansen.

(Witness sworn.)

JUDGE THOMPSON: Take your seat. You may inquire, Mr. Chairman.

CHAIRMAN GAW: Thank you.

DALE JOHANSEN testified as follows:

QUESTIONS BY CHAIRMAN GAW:

Q. Mr. Johansen, I think you probably heard my general question. You want to respond to why Staff has chosen not to sign off on this agreement? And I know that you have provided written comments to that effect through counsel, but I'd like to hear whether -- I'd like to hear that in your own words in general.

A. Certainly. First of all, I would advise you that I worked very closely with Mr. Krueger on developing the comments that we did file. So most of the -- most of the things that I would normally say in response to that are covered by the written comments.

I do think, though, that from the standpoint of why we are -- chose not to sign on to the agreement, the basic reason for that is -- has to do with the fact that a lot of the concerns or issues, if you will, that we raised in our testimony in this case were not actually addressed by the compromise that was reached. That's the main reason why we did not feel it was appropriate for us to sign on to the agreement.

Now, on the other hand, as we state in the comments, this is a -- what we believe to be a reasonable compromise among the parties that did sign the stipulation.

And I think most importantly in that regard is the fact, as Mr. Coffman mentioned earlier and as we mention in our written comments, that the parties that signed the stipulation are a very diverse group of customers-based intervenors, as well as the company and the Office of the Public Counsel. And basically that's the main reason that we're not opposing the stipulation, even though the compromise does not address what we believe to be some rate design issues that need to be addressed.

Q. Okay. Do you want to -- do you want to spell out what those are?

A. The -- one of the main issues that we raised in the rate design testimony that was filed in the case by the Staff was movement away from rate blocks for the customer classes to a single block rate for each class, similar to what is currently in place in the St. Louis County district, the former St. Louis County Water Company. We felt it was reasonable to move all of the districts to that type of rate design.

The compromise that was reached among the parties retains the block design for the districts. It was established in the last Missouri-American rate case. And again, while we think there was a change there that was justified, because the proposal utilizes the block rates that were established in the last case, which in great part were established based on the cost of service study that the Staff provided in that case, we don't have too great a concern over the fact that those block rates are remaining at this point.

Q. Okay. Anything else other than the block rates?

A. There are some other issues regarding allocation factors between the classes and within the classes where there were difference among the parties, but I really think that probably the main issue between our proposal and the compromise here has to do with the retention of the block rates in the compromise versus going to the single blocks.

CHAIRMAN GAW: That's all I have.

JUDGE THOMPSON: Thank you, Mr. Chairman.

Does anyone else have questions for Mr. Johansen before I allow him to step down? Commissioner Murray?

COMMISSIONER MURRAY: I can address this with him first, I guess.

QUESTIONS BY COMMISSIONER MURRAY:

Q. I just had a question about whether the allocation issues just -- they just went away here, we didn't address them; is that right?

A. The -- from the standpoint of the allocation issues between the customer classes within the districts that existed between the Staff's study and the other studies that were presented, those, in essence, did just go away, because the compromise does not address that. And again, we felt that those were important but that they were not so important as to oppose this.

Q. All right. And is it your understanding that the adjustments that are being made return the customer classification percentages back pretty close to what they were before the last rate case?

A. Well, no. Basically from the standpoint of the rates themselves, the interclass shifts that are being made as a result of this compromise do not go anywhere close back that far; for example, the rates that existed before the last case.
Q. Well, I understand that.
A. Right.
Q. I'm just talking about the allocations between the classes.
A. I don't believe -- my understanding of the revenue shifts that are being -- that would be implemented under -- under this proposal is that the class allocations were not specifically used to determine what those shifts should be. It was looked at more from the standpoint of total revenues between the classes, and then the resulting percentages are simply a result of those revenue shifts.
COMMISSIONER MURRAY: All right. That's all I have for this witness. Thank you.
JUDGE THOMPSON: Thank you, Commissioner. Commissioner Clayton?
(No response.)
JUDGE THOMPSON: You may step down, Mr. Johansen.
Do you have other questions, Commissioner Murray?

COMMISSIONER MURRAY: I don't believe I do. Thank you, Judge.

JUDGE THOMPSON: Commissioner Clayton?

COMMISSIONER CLAYTON: May I address Mr. Coffman?

JUDGE THOMPSON: Whoever.

COMMISSIONER CLAYTON: Mr. Coffman, just generally speaking, in terms of residential customers, can you tell me who -- which residential customers throughout the different districts did the best in this Stipulation & Agreement?

MR. COFFMAN: I guess it would depend on how -- what you were comparing it to, if you were assuming that -- if you're assuming that the company's proposed rate design would have prevailed or if you were assuming that the Staff of the Commission's proposed rate design.

COMMISSIONER CLAYTON: I'm looking at it just from current rates, if you just take it from what current rates are.

MR. COFFMAN: Well, comparing it to the status quo, it would be a combination of the percentages you see on the revenue neutral adjustments, as well as a consideration of whether there is an overall revenue requirement increase or decrease as a result of this case. Meter charges, customer charges, what have you would remain the same, so if --

COMMISSIONER CLAYTON: You're giving me an answer that's far more complicated than what I'm looking for. In terms of status quo in existing rates right now, did any residential customer see a rate decrease?

MR. COFFMAN: Simply as a result of this stipulation, no, but there are districts where there would be essentially no change.

COMMISSIONER CLAYTON: Okay. Then they would be the ones that probably did the best here with no change, correct? Which neighborhoods would those be?

MR. COFFMAN: St. Charles, St. Louis County and Jefferson City would essentially see almost no change, assuming there was no revenue requirement change. The way that we evaluated the settlement was based upon the cost of service studies performed by the Staff and by the company, and looked at if those rate designs had prevailed, where residential and commercial customers would be.

We believe that the vast majority of residential and commercial customers fare better with this settlement than with either of those filed positions.

COMMISSIONER CLAYTON: Okay. Did Brunswick -- and I know this is going to sound bad, did they do the worst? But I know they're being subsidized. But is the 15 percent that you mentioned earlier, is that the --

MR. COFFMAN: On that point, I think that a more professional and precise answer could be made by my witness, Ms. Meisenheimer, and I think she would love an opportunity to elaborate on that.

JUDGE THOMPSON: Ms. Meisenheimer, take the stand, please. Go ahead and spell your last name for the reporter.

MS. MEISENHEIMER: M-e-i-s-e-n-h-e-i-m-e-r.

(Witness sworn.)

JUDGE THOMPSON: Take your seat. You may inquire.

BARBARA A. MEISENHEIMER testified as follows:

QUESTIONS BY COMMISSIONER CLAYTON:

Q. Perhaps I should start from where I did before. I'm just trying to get an idea of differences among various residential customers in the rate design between the status -- between current rates as they are now set with -- under the design in this Stipulation & Agreement, who has the most change or where is the most change and who has the most benefit, who got the least benefit, or perhaps would have the largest increase? So if you could just give me an idea of that.

A. In terms of current rates, the settlement, in my opinion, based on my evaluation, you have three cost studies before you. Brunswick comes out roughly about, I think it's 7 -- $779 different on a revenue neutral basis, $779 higher on a revenue neutral basis because the settlement proposal includes maintaining support of $213,000 even, instead of a number which the company had included in their cost study to maintain support of $213,779.

The Staff cost study acknowledged that Brunswick was far below its cost. The numbers vary somewhat. So did our cost study. So basically, I think the net impact on Brunswick is about $779 on a revenue neutral basis. That is, if you order, you know, a particular revenue requirement that would keep them at the same place, they've lost relative support of $779.

With respect to Mexico, the way that I view Mexico -- and this is, you know, my opinion only -- Mexico, I believe, does get a small increase under our proposal -- the one thing I didn't bring with me -- that we're supporting in the stipulation. The net bill impact on a revenue neutral basis, that is before you decide whether there's a revenue requirement increase or decrease, is about 2.5 percent on residential customers --

Q. In Mexico is where we're talking now?

A. Yes.

Q. Okay.

A. Compared to -- from Public Counsel's perspective, compared to what those customers could have faced, we view -- or I view that the Mexico customers got a deal in this because of the increases proposed by the other parties. So I think they ended up better off than they might have under a contested process. Did you want me to continue?

Q. Sure.

A. The districts where the parties agreed to an equal percent increase or decrease, there is no net impact on the customers compared to where they are today. So that would include St. Louis, St. Charles, Jefferson City, with the exception of the adjustment to eliminate the minimum usage, and I believe that was -- that was -- or those were the three districts where we just agreed to an equal percent increase or decrease based on your decision about revenue requirement.

There are -- the St. Joseph district, obviously a problem child, lots of different interests to balance in that one. The way I guess I view how customers came out is better off than they might have. I can't say that they are not paying, that they won't be paying more on a revenue neutral basis than they are today in what we agreed to settle for, compared to where they could be, depending on the decision about revenue requirement and how you view issues of fairness between districts or customers within a district, the existing rates and the rate impacts that have occurred recently.

I think we came out for residential customers and commercial customers. In fact, I think it's about as well as any of the parties probably could have come out. That's my own opinion.

Q. Can you tell me the philosophy of OPC in terms of how it balances the needs of various consumers in such a very diverse set of customers?

A. This was difficult. And I can't speak for Mr. Coffman, because ultimately it's his decision. To the extent I had input into making those decision, we did look at the impact on customers in each district, looked at specifically what had happened in previous cases in those districts, and weighed what we believed potentially to be our risk of ending up with a worse outcome than we could negotiate.

Q. Is it the position of your office to follow the interests of simply residential customers or do you also follow the interests of industrial or commercial or water resale? Do you look at all of them or is it purely residential customers?

A. We look at all of them.

Q. You look at all of them.

A. We look at all of them. Now, certainly in some instances --

Q. Well, let me make sure I understand. I know you look at all of them, but is your interest in protecting -- are you saying protecting all of those customers or you're just examining all of them relative to each other?

A. I believe that we look to all of them to ensure we're not going to do something that would be excessively harmful to any. Certainly where no -- where a particular customer class would have no other representation, we're going to watch out for their interests more, I guess, because there are other parties that have -- that have an interest.

Q. So it could vary on the case by the amount of representation that's involved in the case?

MR. COFFMAN: Commissioner Clayton, I mean, I can attempt to answer your question.

COMMISSIONER CLAYTON: Well, I'm looking here out at the Cole County Bar Association, and I was just wondering if your role varies in -- with regard to whose interests that you protect or that you watch out for?

MR. COFFMAN: It's my understanding of my statutory charge that I'm to represent all of the customers with a particular focus on customers that would otherwise not be represented. Traditionally for the Office of the Public Counsel, that has been residential and small business customers, to some degree, when it comes to rate design are more equal than others in our representation. We pay particular attention to those.

But our focus in this case particularly was to try to reach a result that was fair overall, that tried to avoid any dramatic rate shock to any particular customer class.

The only revenue neutral increase here that's even double digit is with respect to the small class of industrial customers in Parkville, and there we had rates that were the lowest overall, to which there was some representation already in the case, and they had gotten a very good deal in the last case. So we have those customers actually asking for this particular --

COMMISSIONER CLAYTON: Did they have the same counsel in the last case?

MR. COFFMAN: I believe they did. I believe they did. So, yes. I hope that answers your question. I mean, we were hoping to avoid the type of result that was received in 2000, which was a result that overall applied rate shock dramatically to certain classes, particularly in the St. Joseph area. And there were some things that most parties thought could be adjusted or corrected and we tried to move in that direction.

There's nothing in this Stipulation &

Agreement that, I believe, is contrary to the direction generally that the cost studies are pointing to. There are some, you know, compromises obviously made, but I think it's overall a fair deal.

COMMISSIONER CLAYTON: Well, posing just the straight-ahead question is this: Are you satisfied as the Public Counsel that all of the residential customers are treated fairly and equitably or in an equitable manner in this Stipulation & Agreement?

MR. COFFMAN: Yes, I am.

COMMISSIONER CLAYTON: And may I ask the same question to Ms. Meisenheimer?

THE WITNESS: Yes.

COMMISSIONER CLAYTON: Okay. Thank you.

QUESTIONS BY CHAIRMAN GAW:

Q. I'd just like to briefly follow up. Public -- what was Public Counsel's original position in regard to the elimination of the blocks, the rate blocks?

A. We recommended maintaining the blocks and making adjustments to those blocks because of the issue of we're very supportive of a balanced movement toward the goal. And so we were very concerned about some of the proposals and saw a great deal of risk in making big changes to the blocks themselves and applying changes to blocks that would create large individual customer impacts within a class.

So the outcome of this settlement in all the districts, I believe, except for Parkville, was an equal percent increase on and -- I'm sorry -- and St. Joe, there are some changes within the blocks. But I think as a general rule, the focus is to change rates in a balanced manner on all the blocks so that you minimize customer impacts, and that was a very important component that -- that we view as a benefit within the settlement.

Q. Okay. If you started out with no history at all in the past on this case, philosophically do you-all support the concept of having multiple rate blocks in general as a philosophy, instead of having one rate block? I'm just trying to see what this issue is from a policy standpoint regarding the rate blocks from Public Counsel's standpoint.

A. I can answer it from an economic perspective.

Q. Whatever. However you two want to handle it between you.

MR. COFFMAN: Go ahead.

THE WITNESS: From an economic perspective, there are generally benefits in designing declining block rates where you're not near capacity of a plant --

BY COMMISSIONER GAW:

Q. Okay.

A. -- and where there are cost savings being achieved. So as a general rule, declining block rates more reasonably reflect cost savings, if they're present.

Q. Okay.

A. And in this case with utility services, as a general rule, there is an acknowledgement of some kind of cost savings with large volume production. There are a couple of instances where -- where increasing block rates might be appropriate. That is, as you near capacity of a plant, unless you can make some type of other arrangement.

Also, if you wanted to put special emphasis on conservation, you might redesign rates so that they increase, where there's a shortage of a natural resource. In Missouri we're fortunate; that doesn't seem to be as much a problem for us as other states.

The manual, the water manual has a couple of different block designs in them, and to be fair, I want to say that a constant block rate is also in there as one of them. But from an economic perspective, unless the costs -- the unit costs are flat, I think that there are economic reasons that are supported both by pure cost efficiency considerations and by public policy aspects within economics of designing your rate blocks so that they're not flat.

CHAIRMAN GAW: Okay. And, Public Counsel, are you in complete agreement with your witness' testimony?

MR. COFFMAN: Yes, I am. I thought it was a very good answer.

CHAIRMAN GAW: All right.

BY CHAIRMAN GAW:

Q. And forgive me. I know that this has already been discussed. I'm trying to understand that 15 percent on Brunswick that you mentioned earlier. Can you help me understand where that number comes from, if I heard it right?

A. Our original proposal was that Brunswick would receive something like a 15 percent increase, and then the rest that was necessary for Brunswick to reach its revenue requirements should be supplied from somewhere else, if there were other districts getting large decreases, which is what we had anticipated happening from our cost studies in this case.

Q. Okay.

A. Now, I'm not absolutely sure that it actually works out to be a 15 percent, and Mr. Coffman might have been referring to the way the $779 ultimately spread. We didn't -- I didn't calculate that out. We came to an agreement with respect to a specific support number and that was the $213,000. Whatever is left will be spread in an equal percent, with the exception of I think we made the adjustment in Brunswick with the 5 percent for sale for resale, because their rates are very high relative to the other rates within the Brunswick district.

And I believe you were at the public hearing and listened to some of the concerns of those public water supply district customers.

Q. Right. So the issue -- the percentages, though, that I have here on your charge, when I'm looking at those percentages and I go down through there, are those of any meaning if revenues stayed constant with what it is today?

A. Yes, in my opinion, they are. The volumetric percent change, which is the next to the last column, a lot of it depends on how do you want to present information about how rates are going to change. Since there aren't going to be any changes in the customer charge, one way to represent a rate change is to say how much does -- do the rates that are going to change change, and that's what that shows you.

So the volumetric rates, based on this revenue neutral agreement, before you decide whether there's a revenue requirement change, would go up by 3.78. If instead you said, well, how does that really affect the customer's total bill, then that is more characteristic of what's shown in the last column.

Q. Of course, all that is -- I mean, this is --

this is really only a piece of the big picture and we have to see the rest of the case resolved before we know what we're really talking about on numbers by customers?

A. Yes.

Q. I recall -- I recall that there was a long discussion in Joplin by one individual who was very concerned about fire district charges or fire hydrant charges, and since there seems to be no particular charge in this stipulation, does that mean that that gentleman will be satisfied? Does anyone know the answer to that who was in Joplin?

MR. ELLINGER: Commissioner, I can honestly say I have no idea what the answer to that is.

CHAIRMAN GAW: He was very interested in it, and he took a lot of time in making a presentation, and I'm just curious.

MR. ENGLAND: Your Honor, I recall the witness. I was there.

CHAIRMAN GAW: Yes, you were. And you asked him a question, I believe.

MR. ENGLAND: Your memory is now even better than mine. But for the life of me, we have two issues, I can't -- we have two issues. You've got public fire and then you've got private fire, and my recollection this fellow was talking about public fire. In the current tariff in Joplin, public fire is not recovered, if you will, explicitly through a separate charge as it is in St. Louis. So that means, to my way of thinking, nothing's going to change as far as public fire is concerned in Joplin, and if that witness was unhappy with the status quo, he's going to be equally unhappy with the stipulation.

CHAIRMAN GAW: And I cannot recall. I'll have to go back and look at the record and see whether he was complaining about the current status or what was being proposed.

MR. ENGLAND: Actually, I think he was getting -- I don't want to characterize him as supporting the company, but I think his position was there was a certain class that should bear proportionately more of the cost of public fire than others. Beyond that, I honestly can't remember.

CHAIRMAN GAW: Yeah. Okay. I just wanted to ask. I know it's not the biggest part of this case. That's all I have, Judge. Thank you.

JUDGE THOMPSON: Thank you, Chairman. Further questions from the Bench?

(No response.)

JUDGE THOMPSON: I have some questions but they're procedural in nature. I think the parties are going to need to know quickly -- thank you for your testimony, Ms. Meisenheimer.

The parties are going to need to know quickly whether or not the Commission is going to accept this Stipulation & Agreement or whether you're going to have to try this matter. And stipulations and agreements typically go to an agenda session to be voted out. So I think what we would need to do, then, is to take this to agenda as soon as that can be accomplished, and given the 24-hour notice requirements of the Sunshine Law, there's none tomorrow anyway, so the soonest agenda, then, would be Tuesday.

So what I would propose to do would be to take this agenda for a vote, take this agreement -- pardon me -- to agenda for a vote on Tuesday.

Now, the stipulation, I noticed, does not include the standard boilerplate language waiving appeal rights as to the issues resolved by the Stipulation & Agreement. Is that an oversight or is that on purpose or what does that mean? Mr. Fischer?

MR. FISCHER: I'm sorry. John could probably answer that better. I was just going to -- before I lost all the Commissioners, I was hoping to make a brief statement.

JUDGE THOMPSON: I'm sorry. Well, they'll be back.

MR. COFFMAN: I'll just address that. As to these particular parties who are signatories, I would doubt that an appeal would be proper if this was actually and properly adopted as intended.

JUDGE THOMPSON: I just want to understand, if you don't like revenue requirement and you appeal that, are you going to take this with it?

MR. COFFMAN: That would not be my intent, unless there -- I mean, there are interplays between issues, and I know that.

JUDGE THOMPSON: Sure. I'm just trying to understand that feature of it.

MR. COFFMAN: I would point out, if you are considering a swift agenda session to discuss this, that the rule does require with nonunanimous stipulations seven days for any nonsignatory to raise an objection or state that they would like a hearing on some issues.

It's my understanding that every party represented here is a signatory other than the Utility Workers Union of America Local 335 and the Staff of the Commission, both of which have represented to me that they waive their right to request a hearing, and you have Staff here today putting that on the record.

The attorney for the Local 335 is Jan Bond. She is currently in the hospital. It's, as I understand, not a serious matter, but if the Commission was wanting to get something in writing from her, she said that it might be possible for her to put that together.

So the Commission could either wait, I imagine, the seven days, whereupon if nothing was filed this would automatically be considered a unanimous stipulation, or make some effort or instruct somebody to contact Jan Bond and see if they wouldn't submit a pleading or letter.

JUDGE THOMPSON: You're quite right, Mr. Coffman, the rule does require seven days. So we will wait the interval required by rule and see where we stand at the end of that interval. And I appreciate you pointing that out. That certainly takes care of the questions I had. Mr. England?

MR. ENGLAND: Your Honor, I'd like to address the lack of the appeal provision. I think it's problematic when you have a Stipulation & Agreement to something less than all of the issues in the case, and the ultimate rate design as the stipulation contemplates will also be dependent on what the Commission does on revenue requirement, which, you know, we don't have a settlement on. So I think that's another reason why it's probably not appropriate to have a nonappeal clause in there.

JUDGE THOMPSON: Okay. Very good. Anyone have anything else on the rate design?

Mr. Fischer, you wanted to make a statement?

MR. FISCHER: Just for a moment, your Honor. For the record, I'm Jim Fischer. We represent the water districts in the St. Joseph area.

And before the Commissioners left and before we ended this presentation, I just wanted to go on the record and thank the Office of the Public Counsel, particularly John Coffman, Barb Meisenheimer and Jim Busch, for their leadership role in getting all these diverse ratepayer interests together. It was a very difficult task, as you can imagine, and I have truly appreciate their efforts.

Now, my clients happen to be the water wholesalers in the St. Joseph area, and if you will look on Attachment 1E, our rates under this stipulation will go down approximately 14.5 percent, which appears to be a good result from our standpoint.

However, you also have to keep in mind, and we're very pleased and support this stipulation totally, but in the last case, the rates for these same customers went up 239 percent, which was certainly an unprecedented and -- amount in my tenure.

And in answer to another question from Commissioner Clayton on how does this impact the residential customers in the state, I would just respectfully point out that the water districts represent the rural residential customers. Their customer base is almost 100 percent residential in nature, and as result of the fact these are not-for-profit political subdivisions, they pass along any rate increase they get from Missouri-American directly to their residential customers.

As an example, today under the current rates, the residential customer in the City of St. Joseph pays for a typical 6,000 gallons per month just under $25 per month. However, if you step across the line into the water districts that we represent, because we had to pass along that rate increase from the last case, the typical residential customer using that same 6,000 gallons pays between $49 and $51, depending on which of the three districts you go to.

So we will be able to hopefully adjust the water districts' rates somewhat, but now our rates will only be 225 percent higher than they were in 1997.

So with that, again, I want to thank the Office of the Public Counsel and all of the parties for being willing to address this situation, and we certainly see this as a step in the right direction. Any questions?

Thank you.

JUDGE THOMPSON: Thank you, Mr. Fischer. Okay. Why don't we take a five-minute recess? I'm sorry. Mr. Zobrist?

MR. ZOBRIST: Carl Zobrist. I represent the St. Joseph Water Rate Coalition. I just wanted to echo what Jim Fischer had to say about the work that Public Counsel did and to reemphasize to the Commission that this is a product of not just yesterday and the day before, but a lot of other days, to the extent, perhaps, things seem a little bit curious. I can tell you we talked about a lot more curious things, and this was the best that we could do for everyone involved.

And I would say that specifically for myself because, representing the coalition, I've got clients who are in the customer in the commercial area or in the other public authority areas, as well as the industrial area, and you'll see some even different percentages when you go along now.

And we thoroughly thrashed that out with members of our particularly commercial class, because, for example, at the last rate case -- and I appreciate what the Chairman had to say, but you can't look at this case without looking at history, at least the previous rate case, and that was where there was rate shock in the St. Joseph district, but among the people who got hit, the residential ratepayers were relatively hit among the least and so that's why that 7.7 percent appears to be reasonable to us.

The commercial class was hit sort of the next hardest, but that's why their increase is, then, the next lowest. Mr. Fischer's clients were hit the hardest, and then it was the industrial group, with an increase of about 170 percent. And having talked with people in the City of St. Joseph, Buchanan County, the school district, the county -- pardon me -- the college there, Missouri Western, as well as a wide variety of industrial users and commercial users, we really do think this is a good compromise and really would offer this for your serious consideration and acceptance. Thank you.

JUDGE THOMPSON: Thank you, Mr. Zobrist. Thank you very much.

Who else? Mr. Conrad?

MR. CONRAD: Very quick, I do have one -- one additional point that I think dramatizes the points that have been made earlier. By your leave, we have a chart that shows what the 1997 rates that were approved in the 2000 proceeding -- by your leave.

JUDGE THOMPSON: Yes, please.

MR. CONRAD: To just quickly explain -- since I've got this guy, I'll use it -- the horizontal line is approximately drawn at about 78 or 79 percent. That was the percentage increase for the entire district in St. Joe as an aggregate in the last case, basically resulting from the huge plant addition of something like $70 or $72 million of rate base. However, the bars show how that was spread.

A few moments ago, Mr. Fischer told you about his clients, the other water utilities, mentioned -- Mr. Zobrist mentioned the industrials. The residentials got the lowest hit. What this package does, it does not, quote, fix it, because I don't know that everybody would ever be able to agree on what fixing it means, but it makes some progress toward adjusting all of those bars.

This one comes down a bit. This one comes down a bit (indicating). OPA is basically left where they are in the St. Joseph district. The commercials come up a very small amount, and the residential come up a small amount. So we're bringing that together, back more to where there is an equivalent burden. And I think that amplifies Mr. Zobrist's comment to Chairman Gaw about the idea it would be very difficult to look at this case in isolation.

And to that point, let me lift up one final thing. It pertains to appeals. The last case was appealed and was remanded and still sits at this Commission. There is -- some of you have talked about existing rates. There is no finally approved rate coming out of the 2000 case. The last lawful final appealable rate for this company with respect to St. Joseph is the 1997 rates.

Any questions?

JUDGE THOMPSON: Thank you, Mr. Conrad.

Anyone else?

MR. ENGLAND: Well, at the risk of engaging Mr. Conrad in a debate, I just would note that the company does not agree with his legal opinion.

JUDGE THOMPSON: I won't say I'm startled by that.

Ms. McKiddy -- Mr. Krueger, I believe you were going to redirect.

MR. STEWART: Judge, before you start?

JUDGE THOMPSON: Yes, sir?

MR. STEWART: Many of us who were signatories to the stipulation had prefiled testimony that was marked and submitted to the court reporter, but a lot of us won't be here for the --

JUDGE THOMPSON: We'll go through the list, and anything that hasn't been offered we will ask if there are any objections to its receipt at the end of the hearing. Okay?

MR. STEWART: I was going to say, if necessary on the record, I would go ahead and offer the two pieces of testimony for me.

JUDGE THOMPSON: That's what Mr. Conrad was doing, and if I had it easily set out --

MR. STEWART: I will make this very quickly. I would offer Exhibit 30, which is Kalbarczyck direct and

Exhibit 84, which is Kalbarczyck surrebuttal.

JUDGE THOMPSON: All right. Do I hear any objections to receipt of Exhibit 30 and 84?

MR. ENGLAND: None here, your Honor.

JUDGE THOMPSON: Hearing no objections, those exhibits are received and made a part of the record of this proceeding.

(EXHIBIT NOS. 30 AND 84 WERE RECEIVED INTO EVIDENCE.)

JUDGE THOMPSON: Do you want to run through yours?

MR. CONRAD: Sure. I have one to run through. It's Exhibit 60, the rebuttal testimony of Donald Johnstone; it is offered on behalf of Ag Processing, Inc., and also the City of Riverside.

JUDGE THOMPSON: Any objections to the receipt of Exhibit 60?

MS. O'NEILL: No.

MR. ENGLAND: No objections.

JUDGE THOMPSON: Hearing none, Exhibit 60 is received and made a part of the record of this proceeding.

(EXHIBIT NO. 60 WAS RECEIVED INTO EVIDENCE.)

MS. O'NEILL: Your Honor, do you want to just receive testimony from Public Counsel's rate design witnesses also at this time?

JUDGE THOMPSON: Sure.

MS. O'NEILL: In that case, I would offer Exhibit 34, the direct testimony of Barbara Meisenheimer; Exhibit 55, rebuttal testimony of Meisenheimer; Exhibit 64, surrebuttal testimony of Barbara Meisenheimer; Exhibit 32, the direct testimony of James Busch; Exhibit 54, the rebuttal testimony of James Busch; and Exhibit 63, the surrebuttal testimony of James Busch.

JUDGE THOMPSON: Okay. Do I hear any objections to the receipt of Exhibits 32, 34, 54, 55, 63 or 64?

MR. ENGLAND: No, your Honor.

JUDGE THOMPSON: Hearing none, those exhibits are received and made a part of the record of this proceeding.

(EXHIBIT NOS. 32, 34, 54, 55, 63, AND 64 WERE RECEIVED INTO EVIDENCE.)

MR. KRUEGER: And as long as we're at it, I guess we might as well offer Mr. Hubbs' testimony, if I can find the exhibit numbers. Exhibit 33, Hubbs direct, Exhibit 36, Hubbs rebuttal, and Exhibit 74, Hubbs surrebuttal.

JUDGE THOMPSON: Do I hear any objection to the receipts of Exhibits 33, 36, 74?

MR. ENGLAND: No.

JUDGE THOMPSON: Hearing no objections, those three exhibits are received and made a part of the record of this proceeding.

(EXHIBIT NOS. 33, 36 AND 74 WERE RECEIVED INTO EVIDENCE.).

MR. ENGLAND: As long as we're at it, may I offer the three exhibits sponsored by our rate design witness, Paul Herbert. I believe they are Exhibit 9, his direct; Exhibit 48, his rebuttal; and Exhibit 82, his surrebuttal.

JUDGE THOMPSON: Do I hear any objection to receipt of Exhibits 9, 48 or 82?

MS. O'NEILL: None.

JUDGE THOMPSON: Hearing no objections, Exhibits 9, 48 and 82 are received and made a part of the record of this proceeding.

(EXHIBIT NOS. 9, 48 AND 82 WERE RECEIVED INTO EVIDENCE.)

JUDGE THOMPSON: Is that it?

Mr. Krueger, you may inquire.

MR. KRUEGER: Thank you, your Honor.

ROBERTA McKIDDY testified as follows:

REDIRECT EXAMINATION BY MR. KRUEGER:

Q. Good afternoon, Ms. McKiddy.

A. Good afternoon.

Q. Mr. England asked you some questions this morning about the benefit to the ratepayer of subtracting accumulated depreciation from -- that was not collected from ratepayers. Do you remember those questions?
A. That is correct.
Q. After new rates go into effect, does the depreciation expense continue to accumulate?
A. Yes, it does.
Q. What effect does this have on rate base?
A. It reduces rate base, but it has no impact on rates until the next rate case is filed.
Q. Okay. So does that produce what Mr. England might refer to as a benefit to the shareholders?
A. Yes, that would be a benefit to the shareholders.
Q. Is that a form of regulatory lag that benefits the shareholder?
A. Yes, it is.
Q. Now, am I correct to understand that in calculating cash working capital, the property tax expense lag represents the time between the midpoint of the time when the service is provided to the date of payment?
A. Yes, from the midpoint of the service period to the time, date it's paid.
Q. Does this lag reflect the time when expenses

are included or recovered in rates?
A. No, it does not.
Q. Is it intended to reflect that?
A. No, that is not the purpose of cash working capital studies.
Q. Have you examined the service company contracts between the company and AWWS that we've been talking about?
A. I have not.
Q. In the hypothetical that Mr. England described where the plant was placed in service as of December 31, 2002, do you remember his questions to you about that?
A. Yes, I believe I do.
Q. In a situation like that, who decides when the rate case will be filed?
A. The company decides that.
Q. If the plant goes in service, if a plant that's completed and placed in service on December 31, 2002, and depreciation accrues before new rates go into effect and before the company recovers the depreciation from its customers, is that what's called regulatory lag?
A. Make sure I understand here. The example that Mr. England gave this morning was when a million dollars asset goes into place at the period where rates are determined, there was a $30,000 depreciation expense

deducted, so only $970,000 was actually considered for rates. And your question again was relating to that?

Q. Yes. Is that a result of regulatory lag that that is not reflected in rates until some depreciation has accrued, has accumulated?

A. Yes, that would be true.

Q. Is cash working capital included in rate base in order to lessen the effects of regulatory lag?

A. Yes.

Q. Do you know if property taxes are included in the determination of revenue requirement?

A. I do not.

Q. Okay. Do you know of any non-cash item that has ever been included in cash working capital in the determination of cash working capital by this Commission?

A. No, I do not.

Q. Is depreciation a non-cash item?

A. Yes, it is.

Q. Is deferred taxes a non-cash item?

A. Yes, it is.

Q. Have you seen any evidence in this case that shows that the management fees charged by AWWS are 25 percent less than what the company would have to pay to another vendor?

A. I have not seen any evidence of that.

Q. Is there any reason at all to believe that the fees charged are less than any amount than they would be if provided by another vendor?

A. I have seen no evidence that would imply that.

Q. I'm not sure I understood your answer to a question that I asked a little bit earlier. Is cash working capital included in rate base for the purpose of lessening the effects of regulatory lag?

MR. ENGLAND: Objection, asked and answered.

JUDGE THOMPSON: Would you read that back.

THE REPORTER: "Question: I'm not sure I understood your answer to a question that I asked a little bit earlier. Is cash working capital included in rate base for the purpose of lessening the effects of regulatory lag?"

MR. ENGLAND: And her answer was yes. I thought that was pretty clear.

JUDGE THOMPSON: One of the clearest answers I've heard in this case so far. I'll sustain the objection.

MR. KRUEGER: I have no other questions, your Honor.

JUDGE THOMPSON: Thank you, Mr. Krueger.

Ms. McKiddy, you may step down.

Transportation expenses, did we have Mr. Lehman here?

MR. COOPER: Yes.

JUDGE THOMPSON: I assume we'll hear from Mr. Lehman next?

MR. COOPER: I think -- either way we do that, your Honor, but I think there was some discussion that Staff wanted to perhaps do employee expenses next. But setting both those aside for a second, it's my understanding --

JUDGE THOMPSON: Step up to the podium.

MR. COOPER: I'm sorry. Need to be near a microphone.

JUDGE THOMPSON: Absolutely.

MR. COOPER: And I haven't directly spoken to Ms. O'Neill about this, but it's my understanding she's been included in this. But I think Staff, the company and perhaps OPC have -- well, why don't we go ahead and take that break. Let me finish locking this down with Ms. O'Neill.

JUDGE THOMPSON: Ten minutes.

(A BREAK WAS TAKEN.)

(EXHIBIT NO. 128 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

JUDGE THOMPSON: Mr. Lehman, come on up and take the stand, sir. Could you spell your last name for the reporter, please.

MR. LEHMAN: My last name is Lehman, L-e-h-m-a-n.

(Witness sworn.)

JUDGE THOMPSON: You may inquire, Mr. Cooper.

DOUGLAS LEHMAN testified as follows:

DIRECT EXAMINATION BY MR. COOPER:

Q. Mr. Lehman, are you sponsoring or did you prepare for purposes of this case rebuttal testimony and is your rebuttal testimony in question and answer form?

A. Yes, Mr. Cooper, I did.

Q. Is it your understanding that those exhibits have been marked as Exhibit 43 and Exhibit 77 for identification?

A. I'm not sure of the numbers, but I know they've been marked for identification.

Q. Work with me. They're 43 and 77?

A. Yes.

Q. It's my understanding you have a correction that needs to be made to Exhibit 43; is that correct?

A. That is correct. On page 8 of my rebuttal testimony, at the bottom of the page, the very last line, line No. 25, the year 2001 is incorrect. It should be 1999.

Q. Do you have any other corrections that need to be made?

A. That is the only one of which I'm aware at this point.

Q. Now, based upon your surrebuttal testimony, it's also my understanding that you have adopted the testimony -- the direct testimony of Mr. Robert B. Maul and intend to stand cross-examination on that testimony as well; is that correct?

A. Yes, that is correct.

MR. COOPER: Your Honor, at this time I would offer into evidence Exhibits 43 and 77, which are the rebuttal testimony and surrebuttal testimony filed by Mr. Lehman. I would also offer Exhibit 7, which is the direct testimony of Mr. Robert B. Maul.

JUDGE THOMPSON: Okay. Do I hear any objections to the receipt of Exhibit 7, 43 or 77?

MR. BATES: No objection.

JUDGE THOMPSON: Hearing no objections, those exhibits are received and made a part of the record of this proceeding.

(EXHIBIT NOS. 7, 43 AND 77 WERE RECEIVED INTO EVIDENCE.)

JUDGE THOMPSON: We will start with questions from the Bench. Commissioner Murray?

COMMISSIONER MURRAY: Thank you, Judge.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good afternoon.

A. Good afternoon, Commissioner.

Q. When I was reading your testimony, I just questioned why did you use a three-year average for transportation expense and a five-year average for employee expenses and then a four-year average for relocation expenses? Why were the different number of years used?

A. That's a very good question. The difference is essentially due to the availability of data. For example, the reason we used a four-year and not a five-year average in the area of relocation expense was because there really wasn't data available for 1998 for relocation. It was in three prior entities and done by -- and held by a consultant and simply wasn't available. So we used what was available, which was a four-year average in that case. In transportation, we only had two good years beyond the test year of history, and we used those three years.

Q. Any reason in particular that you did not have records for the years beyond that?

A. The primary reason there was that in that period of time farther back, 1999 to '98, the current entity was three separate entities with separate accounting systems, separate account structure and separate data storage.

Q. And Staff's position, as I understand it, is that, at least for transportation expense, and I may be mixed up as to which ones, but I believe that Staff's position is for transportation expense to take the most recent year's data; is that right?

A. Yes. As a matter of fact, Ms. Hanneken and I spoke just a few minutes ago and we hopefully clarified our differences. The Staff position, as I understand it, is that it is test year or 1,014,000.

Q. And your position as to why we should look at an average versus just the test year, would you explain that?

A. Our position advocating the average is because the expense category fluctuates and can fluctuate significantly. For example, in 2003 the O&M expense for transportation ended up at 1.66 million, substantially above test year. And because the expense category does fluctuate, we would argue for a longer time frame of averaging.

Q. And how has transportation expense been treated in the past?

A. I attempted to do some research in that, but it was essentially a small enough issue that it was below the radar screen of the final order and report, so I'm not certain.

Q. How about employee expenses?

A. Employee expenses, it's my understanding that a three-year average has been somewhat common in the past.

Q. Three-year?

A. Yes.

Q. And you're suggesting five-year?

A. Right. We're suggesting five-year because we have five years of good data available, and in the situation where the data's available, we believe it makes sense to look at a longer-term average.

Q. What if you had ten years available?

A. I suppose an argument could be made for that. It might be a little burdensome, but you could probably make an argument for that. There's some entity issues as you go back in time.

Q. And for employee expenses, is the Staff also recommending just the test year data?

A. I believe the Staff's position is the test year amount, which is 297,408 versus our average. And I'll have to look that up. The five-year average is 472,791.

Q. And do you know what Staff is recommending?

A. I believe they're recommending test year.

Q. And again, I guess your position would be the same as -- the reason for averaging there as it would be for averaging transportation expense?

A. That's correct. It's an expense category that fluctuates, sometimes significantly, and for all stakeholders involved, it makes sense to look at it on a longer-term basis.

Q. Is Staff taking the position that the trend has been down in both of these or one or the other of these categories?

A. Commissioner, I believe that they are taking the position that there is a secular decline or a long-term decline in employee expenses. I would argue against that. If you look at the numbers 1998 through 2001, they're essentially flat line, when you look at perhaps a post 9/11 effect. They were down in 2002 because of some budgetary restrictions.

Q. Excuse me. Which chart are you looking at?

MR. COOPER: He's looking at a chart that's not in his testimony.

THE WITNESS: It's an exhibit that we had intended to enter into testimony.

BY COMMISSIONER MURRAY:

Q. But you've not?

A. But we have not yet done so.

Q. Would you like to do that?

MR. COOPER: Your Honor, may we mark an exhibit?

JUDGE THOMPSON: We may. This will be Exhibit 129. How do we describe this?

MR. COOPER: Why don't we describe this as employee expenses 1998 to 2003.

JUDGE THOMPSON: Very well.

(EXHIBIT NO. 129 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY COMMISSIONER MURRAY:

Q. Mr. Lehman, you were telling me about the difference in the years on this Exhibit 129; is that correct?

A. Yes. Going back to the notion of is there a secular or long-term decline in this category, my argument is that if you look at the years 1998 through 2001 and attempt to factor out a 9/11 effect, that they're essentially flat over that four-year period. The expense is down significantly in 2002, due to some budgetary restrictions, and then it's popped back up again in the year 2003. So given that kind of fluctuation, especially in the last couple of years, we're arguing for a longer-term five-year average.

Q. Taking the current test year or three-year average would give you the worst results of the last five years, would it not?

A. I would -- I would believe so, yes, Commissioner.

Q. On transportation expenses, are they showing any kind of a trend?

A. The trend in transportation is, I guess, probably not a trend at all. If you look at the O&M

transportation numbers, 2000 is 1.766 million.

Q. Where can I look at that?

A. Schedule DML-3 attached to my rebuttal testimony.

Q. Somehow I'm disorganized at the moment. Just a second. Say that again, schedule?

A. It's page 13 or Schedule DML-3 on my rebuttal testimony.

Q. All right.

A. And I'm focusing only on the top line there that says O&M transportation. And we're seeing 1.766 million in 2000, 1.578 million in 2001, and then in 2002, 1.145, although in discussions with Staff, that number is a number that we would argue a bit.

Q. As not being correct?

A. There was an issue that occurred in 2002 that is one of the bones of contention here, and that is the liquidation of the transportation reserve that was put in place in 1995. That particular issue has an amount attached to it of 130,758. That reserve was liquidated in the year 2002, and we believe to get a true number for O&M transportation in that year, that you have to add it back to the book number, because it's an anomalous credit that's in there. So Staff's position would be $130,000 less than our 1.145 in that year.

In this current year, the number is 1.616 million. I mean 2003 when I say current year.

Q. 1.616 million?

A. That's correct.

Q. And is Staff's position the 2002 test year number that is shown here, the 1,145,575?

A. No. Actually Staff's position would be that number less the transportation reserve number of 130, I believe.

COMMISSIONER MURRAY: I think that's all I have. Thank you.

JUDGE THOMPSON: Thank you, Commissioner Murray.

Chairman Gaw?

CHAIRMAN GAW: I'll pass. That's fine.

JUDGE THOMPSON: Commissioner Clayton?

QUESTIONS BY COMMISSIONER CLAYTON:

Q. Just to clarify on a couple of things, I guess to start somewhere, start with employee expense and the exhibit that you just handed out, 129. Just as a little background, there are four accounts listed on this exhibit. Can you tell me just very briefly what each account is?

A. Yes. The first account on the list is 575340, and that is employee expense miscellaneous. It's kind of a catchall for everything in that general category. The second line, 575342, is employee expense for conference and registration fees.

Q. A critical component, I understand.

A. Account 575350 is employee expenses for meal and travel that are tax deductible, and then the companion account 575351 is for employee expenses for meals and travel that are nondeductible from a tax standpoint. So those are the four object accounts that we have included in the employee expense definition.

Q. What would be an example of a nondeductible meal and travel expense?

A. Most everything in those accounts is split 50/50 based on tax deducibility and nondeductibility. And I, at the moment, can't think of an example of a nondeductible item on its own; only the 50 percent portion.

Q. So 50/50 is between account 350 and account 351?

A. That's correct.

Q. Now, at the bottom of this it says that the meals were split between 340 and 351?

A. That was an accounting issue historically.

Q. Okay.

A. That wasn't a tax issue.

Q. Do you have any idea why there was no meal and travel in 350 for '98, 2000 and 2001?

A. That goes back to that same footnote, and those amounts were combined in 575340, the first line.

Q. So you didn't use that account for those?

A. Right. It would be impossible to go past -- to go back and recast those.

Q. Okay. I reviewed your testimony, but I couldn't get from it a characterization of the five -- in the five years how the expense amount came about. And when I say that, I'm trying get an idea of -- in determining a trend, whether there's been more or less travel or more or less employee expense as time passes. Do you know what level of travel and miscellaneous expense or why there was a decline over those years?

A. It would be my opinion that if you kind of bump up 2001 for the 9/11 effect, basically everything came to a screeching halt on that day for the entire fall. If you increase that number somewhat for that effect, from '98 through 2001, you've essentially got a flat line, you know, minor variations, say around the $525,000 range. It's really in 2002 where there were budgetary restrictions that the number came down so far.

Q. Is it your testimony that the five-year average, the $472,000 figure is a -- is an accurate depiction of what the company will incur in terms of employee expenses in future years?

A. Yes, Commissioner. Given that this expense fluctuates, and sometimes for reasons that are not entirely within the company's control, it's better to use a longer-term viewpoint on this.

Q. That figure is even -- that figure's even higher than the 2003 expenses, correct?

A. That's correct.

Q. Okay. Other than employee expense and transportation expense, can you give me other examples, to the best of your knowledge, where we do averaging over an extended period of time on other issues in this case?

A. There is another example, and it's a companion expense to employee expense, and that's relocation expense. In that particular case we're using a four-year average because that is a category that fluctuates significantly from year to year.

Q. Okay. Any others?

A. Not that I've had direct experience with.

Q. Okay. To be consistent, shouldn't we use averaging in most all issues involving expenses?

A. I think there's probably a case to be made for reasons where there are fluctuations. If something is consistent, there probably would be no point in it.

Q. Well, what would you consider a significant enough fluctuation, what percentage of the overall expense or what amount of money?

A. That would be an arbitrary call on my part. I just wouldn't really have a good guess.

Q. Well, then, how did you decide arbitrarily to use a five-year average, then? I mean, that's what you're here for, right?

A. Yeah.

Q. To give us an opinion?

A. It was my opinion that a five-year average would be a good step toward balancing the interests of all stakeholders involved. It would be a long enough period of time so that either side in the case would not be able to influence it significantly either way, and represents a good compromise, if you will, on that philosophy.

Q. A compromise between?

A. Between test year and -- and a longer-term average.

Q. A longer term than five years?

A. Than five years, yeah.

Q. Well, if you go back prior to five years, then, would that average be even higher?

A. I really wouldn't have any idea. You get into a situation where you've got multiple historical entities and maybe not adequate accounting records.

Q. Well, then, how was your figure a compromise?

You mentioned compromise between Staff and --
A. Between trying to go farther back in time, if possible, and test year.
Q. Okay. How do you reconcile the figures for pre-merger employee expenses, pre-St. Louis County and Missouri United Water, prior to, I guess, year 2000 or prior to year 2001?
A. The employee expense category happens to be one category where those records are the same for almost any business, and they're easily accessible from the prior three entities.
Q. Okay. So --
A. So we had no trouble building a five-year history.
Q. Okay. So the '98 figure of 526,000 would be those accounts from each of the three entities, the traditional Missouri-American, St. Louis County and the Missouri United?
A. That's correct.
Q. Okay. Okay. So is it your testimony that with that consolidation, that there is an overall reduction to employee expenses? I mean, a three-year average, that's more or less what you're saying?
A. No, Commissioner, that's not -- that's not my testimony. The consolidation doesn't necessarily mean a

reduction in this category.

Q. Okay. There are no economies of scale to be benefited from here?

A. This is not necessarily a category that would lend itself to economies of scale. It's much more driven by outside entities; for example, EPA regulation, new standards where people have to be plant operators and such, have to be trained.

Q. I want to make sure when you answered this that I understood your answer. Were you able to give me an example of a nondeductible meal and travel expense?

A. Other than the 50/50 breakdown, no, Commissioner, I was not.

Q. I know that there was a 50 percent or 50/50 break between varying accounts, but is there any other significance to that? Is that a tax implication or --

A. I'm the last person, I think, probably who should be testifying on taxes, but it's my understanding of this simple issue that the travel and meal expenses are broken down 50/50 in the tax code; 50 percent deductible, 50 percent nondeductible.

Q. Can you give me an idea of what the transportation expense actually involves, what it includes?

A. There's probably three primary elements to the transportation expense, which in a broad sense is simply the care and feeding of the fleet. One, you've got vehicle fuel; two, you've got vehicle maintenance and parts; and three, vehicle repair.

Q. So which of those amounts were most volatile?

A. I would say vehicle repair would be the most volatile. It depends on what breaks and what gets damaged from year to year.

Q. You testified that you had no records for transportation expense going back more than three years?

A. I've not reviewed any transportation records prior to the year 2000.

Q. So why is that?

A. I think the issue is primarily the entity issue. Going back in time, you've got three different entities at that point in time, 1999 and prior, with different accounting systems, different account structures, different records availability.

Q. So it is your opinion that the three-year average is roughly 1.3 -- $1.327 million?

A. I should clarify that. In meeting with Staff just before this testimony, we did establish and clarify our differences as Staff being at 1.014 million, their case, and our case, the three-year averaging at 1.453 million. So there should be a little bit of change there.

Q. So yours actually went up from your prepared testimony? I may have written it down wrong, but I had 1,327,482 as the company's position for a three-year average.

A.   Right. We've clarified that at 1.453 million.

Q.   So after conversations with Staff, your position improved?

A.   Our difference actually widened.

Q.   Indeed it did. So much for settlement talks, right? Okay. Can you explain to me the heavy-duty maintenance reserve issue?

A.   That was a reserve, as I understand it, that was put in place in 1995, and on an hourly basis of use for heavy equipment, amounts were accrued into a maintenance reserve, so that when a large expensive piece of equipment had some kind of a problem or failure, that there was money available to deal with that. That maintenance reserve was liquidated in 2002 in full. That amount was 130,758.

Q.   Was it like a rainy day fund for heavy vehicles, is that what it is, or is this just an accounting ledger, is this like a bank account, is it a savings account? I'm trying to get a handle on it.

A.   It was a reserve that was accrued to help deal with large-scale repair costs that wouldn't have been budgeted for.

Q.   So it was money set aside -- I mean, it would be money set aside for future use by the company; is that a fair way to --

A. That's one way to characterize it.

Q. And Staff says that that should be used -- one third of that should be used to offset?

A. Right. Staff is arguing, as I understand it, for a three-year amortization of that credit.

Q. And you-all believe that there should -- what is the company's position?

A. Our position is that, because of the existence of the $130,000 credit in the test year, that it should be added back to have a true measure of test year activity.

Q. So, at what point would the ratepayers receive a credit for that reserve, or would they ever, in your opinion?

A. I don't know.

COMMISSIONER CLAYTON: Thank you.

JUDGE THOMPSON: Commissioner Murray?

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. Mr. Lehman, which five years did you use in your employee expenses average?

A. In of the average, we used 1998 through 2002 for a five-year average. We included the year 2003 only for informational purposes.

Q. Okay. Did you include the year 2002?

A. That's correct.

COMMISSIONER MURRAY: Thank you. That's all.

JUDGE THOMPSON: Thank you, Commissioner. Chairman Gaw?

CHAIRMAN GAW: I don't have any questions.

JUDGE THOMPSON: My first question, actually, perhaps is for counsel, which is when we made the new list of issues, we seemed to have neglected certain issues that this witness has provided some testimony on. I'm referring to dues and donations and advertising expense. Are those going to settle or are we going to try them or --

MR. SNODGRASS: Judge, from the Staff's perspective -- this is Mr. Snodgrass for the record -- we have talked to the company about settling dues and donations, lobbying and advertising, and that's still in progress.

JUDGE THOMPSON: So that's ongoing?

MR. SNODGRASS: That's an ongoing situation.

JUDGE THOMPSON: That's all I needed to know. Thank you

QUESTIONS BY JUDGE THOMPSON:

Q. Mr. Lehman, I mean, I want to make sure I understand. This is a revenue requirement issue, right?

A. That's correct.

Q. So the Staff's position with respect to transportation is 1,327,482?

A. No. Unfortunately, it is 1.453 million at this point.

Q. So 1.453 million and change, or is that 000? I hate to be nitpicky, but I wouldn't want to see you get less than your necessary operating expenses.

A. Judge, I don't have that exhibit available, but I believe Ms. Hanneken has that.

Q. All right. So someone will be able to provide that to me eventually. And as far as you know, Staff's position is 1,101,989, or has that changed?

A. Unfortunately, that has also -- as I understand Staff's position, it is 1.014 million.

Q. And that's, again, changes since things were filed originally?

A. Correct, based on our discussions prior to this testimony.

Q. And if I were to ask you about employee expenses and your position and that of Staff, I would hear that those were also changed?

A. No. Those -- on the list of issues, the revenue requirement value of 199,949 is correct.

Q. So you're talking about the reconciliation?

A. Yes.

Q. All right. So does that mean the company's position is 472,791?

A. That's correct.

Q. And that Staff's is 297,408?

A. I believe so.

JUDGE THOMPSON: Great. Thank you very much. I have no other questions for you. Further questions from the Bench?

(No response.)

JUDGE THOMPSON: Very well. Cross-examination, Ms. O'Neill?

MS. O'NEILL: No questions.

JUDGE THOMPSON: Mr. Bates?

MR. BATES: Thank you, your Honor.

CROSS-EXAMINATION BY MR. BATES:

Q. Good afternoon, Mr. Lehman.

A. Good afternoon, Mr. Bates.

Q. I just have a few questions for you.

Do I understand that regarding employee expense, you claim that new accounting standards, new water treatment standards and new environmental regulations and changes in procurement, new software, new software updates required in most cases additional employee training, is that your position?

A. All of those things can generate additional employee training and travel requirements, yes.

Q. Given that, since 1999, the overall level of employee expense has dropped; is that true?
A. If you look -- if you look at the raw numbers, that is true.
Q. So are you saying that there have been no changes in any of those factors?
A. There have been many changes in those factors.
Q. That being the case, why has the overall level of employee expense dropped since 1999?
A. Primarily for the two reasons that -- that I've mentioned earlier. In 2001 there was what I'm calling a 9/11 effect in the latter part of the year, and in 2002 there were -- even though it was prior to my employment, there were active budgetary restrictions on travel.
Q. I think you also stated that the company believed that longer-term average of five years provides a more appropriate amount to include in rates; is that correct?
A. That is correct.
Q. Did the company respond in -- to Staff Data Request 435 that it was inappropriate to use an average of five years?
A. I don't know.
Q. Did you prepare that Data Request?
A. I would have to research that.

MR. BATES: May I approach the witness?
JUDGE THOMPSON: You may.
BY MR. BATES:
Q. Mr. Lehman, would you identify that for the Commission, please?
A. What I've got, it's a copy of Data Request 435 dated October 27th, '03.
Q. And first of all, did you prepare that?
A. No. I believe Mr. Grubb prepared that.
Q. Okay. But can you read what the Staff response was?
A. The company response is as follows: The company did not use a five-year average because the St. Louis district was not a part of the American system in 1998. St. Louis County rarely relocated employees; therefore, using 1998 is not appropriate.
Q. Okay. Is that still the company's position, as far as you know?
A. In terms of relocation expense, that is -- that is appropriate, because we did not use 1998 because we felt we did not have good data.
Q. Okay. I think you've also stated that the company does not have five years of good data in the area. Is that what you're talking about by that?
A. In the area of relocation expense, that's

correct.

Q. Oh, in the re-- that's right. Thank you.

Did you provide this data response to Staff Data Request No. 277?

A. I can't recall what that specifically was.

Q. Excuse me just a second. I apologize. It's Data Request 271.

A. I can't recall the Data Request 271 specifically.

MR. BATES: May I approach the witness?

JUDGE THOMPSON: You may.

BY MR. BATES:

Q. Mr. Lehman, I'm going to ask you to identify what I've just handed you.

A. Okay. What you've given me is a copy of Data Request 271 dated August 6th, 2003.

Q. Did you prepare that?

A. That -- this Data Request is signed by me, yes. That's correct.

Q. Okay. And what was the question on Data Request 271?

A. The request is, please provide a detailed explanation for the decline in employee expenses in 2002, as compared to 1999 through 2001. Provide all documentation calculations. Also please provide all justification for the increase proposed in 2003.

Q. And would you read what your answer was, please?

A. It's a two-paragraph answer. The first paragraph is, during 2002 the company experienced a significant cost increase in pension expense. In an attempt to mitigate the impact, the company curtailed expenses in the employee expense category by 128,000. The pension expense increased from 228,000 in 2001 to 1.278 million in 2002.

Second paragraph, the company's proposal to increase the test year level of employee expenses is based on moving back to the level of employee expenses that was incurred prior to the year 2002, based on employee average.

Q. Okay. So would you agree with me that the company did provide the data, five years of good data in this area on relocation expense?

A. No. The relocation, we provided four years of good data.

Q. Okay. In response to that Data Request, do you see any qualification to indicate that the response was incomplete or inaccurate or otherwise in any way wrong?

A. No, sir.

Q. Okay. Has the company, to your knowledge, provided Staff with an update of this Data Request?

A. We provided a number of true-up updates, especially in recent days, and I'm not certain whether this is one of them.

Q. Okay. What, in your opinion, would be the effect of using this data in a five-year average of relocation expense?

A. Again, we're proposing only a four-year average in relocation. And the reason we're doing so is because it fluctuates so much from year to year, that we think it's appropriate to use a longer-term viewpoint.

Q. Okay. But what do you believe the effect of using the data on a five-year average would be, whether or not you feel it's appropriate?

A. Since we do not have good data for 1998, the effect would be to put a zero in that year and, of course, lower the average.

Q. You don't think it's possible to get any sort of reliable data from 1998?

A. What I was told was that the records are in the hands of a consultant and we didn't have them in our possession.

Q. Do you recall who told you that?

A. Someone in our operation. I can't recall specifically.

Q. So let me ask you this: Does the company currently believe that an amount in excess of $470,000 is appropriate going forward?

A. That's correct. In our case is a number of 472,000 in employee expenses.

Q. Okay. And you mentioned something about post-9/11 expenses earlier; is that correct?

A. That's correct.

Q. Has there been an analysis supplied to the Staff or by you personally that supports all effect -- excuse me -- that supports some 9/11 effect on employee expense?

A. We have not done a study.

Q. Okay. Has there been any particular reason you haven't done that study?

A. No particular reason. I believe the data would show that to be the case, but I've not done the study.

MR. BATES: All right. Thank you very much.

JUDGE THOMPSON: Thank you, Mr. Bates. Redirect, Mr. Cooper?

MR. COOPER: No questions, your Honor.

JUDGE THOMPSON: Thank you. You may step down, Mr. Lehman.

Our next witness, I believe, would be Ms. Hanneken; is that right? Is she here?

MR. SNODGRASS: Your Honor, we do have a

couple of questions on the transportation expense issue. That was my issue in this case and was kind of taken up on the stand by Mr. Lehman.

JUDGE THOMPSON: Didn't we just complete cross-examination by Staff for Mr. Bates?

MR. SNODGRASS: No. He was dealing with the employee expenses.

JUDGE THOMPSON: I see. I apologize.

CROSS-EXAMINATION BY MR. SNODGRASS:

Q. Good afternoon, Mr. Lehman.

A. Good afternoon, Mr. Snodgrass.

Q. So, briefly just referring to some questions from Commissioner Murray, directing your memory back to those, hasn't the Staff added something into its number 2/3 of the liquidation of the heavy-duty maintenance reserve?

A. Right. That's correct. Staff adjustment S-14.11 added back 87,172 of that reserve.

Q. And hasn't the company agreed with the Staff's adjustment for this item?

A. No. Actually, our position is that the entire reserve should be added back.

MR. COOPER: Everybody's looking my way. I need to -- actually, could we go off the record for about five minutes, your Honor? Let me talk to Mr. Snodgrass and I think we can maybe remove something from -- as an issue in this case.

JUDGE THOMPSON: Don't let me interfere with that. Are we going to be going back on the record today?

MR. SNODGRASS: Yes, sir.

JUDGE THOMPSON: Have at it.

(AN OFF-THE-RECORD DISCUSSION WAS HELD.)

JUDGE THOMPSON: Did we resolve anything?

MR. SNODGRASS: I believe so, your Honor.

MR. COOPER: I want to confirm, I guess, I believe consistent with Mr. Snodgrass' understanding, we have no issue with that piece of transportation expense, the maintenance reserve piece of that and how it has been treated by the Staff.

JUDGE THOMPSON: Very well.

MR. SNODGRASS: I believe our next witness would be Jeremy Hagemeyer.

JUDGE THOMPSON: I believe Mr. Cooper gets a chance to do some redirect on your --

MR. COOPER: I have no redirect for Mr. Lehman. We can move on to Mr. Hagemeyer.

JUDGE THOMPSON: We're going to move on to Hagemeyer tomorrow. So we're going to be in recess until tomorrow morning at 8:30.

WHEREUPON, the hearing of this case was recessed until January 8, 2004.

I N D E X

MISSOURI-AMERICAN'S EVIDENCE

STAFF'S EVIDENCE

(Transportation Expenses/Employee Expenses)

MISSOURI-AMERICAN WATER'S EVIDENCE

EXHIBITS INDEX

EXHIBIT NO. 70
    Surrebuttal Testimony of Roberta McKiddy * 2097

EXHIBIT NO. 74
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EXHIBIT NO. 77
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EXHIBIT NO. 82
    Surrebuttal Testimony of Paul Herbert * 2204

EXHIBIT NO. 84
    Kalbarczyck Surrebuttal * 2202

EXHIBIT NO. 128
    Schedule 8 - St Joseph district 2209

EXHIBIT NO. 129
    Employee Expenses 1998 to 2003 2215

*Premarked exhibit.