Exhibit No.:
Issues: Various Rate Base and
Cost of Service
Accounting Adjustments
Witness: Ronald A. Klote
Sponsoring Party: Aquila Networks-MPS
& L&P
Case No.: ER-

Before the Public Service Commission
of the State of Missouri

Direct Testimony

of

Ronald A. Klote

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DIRECT TESTIMONY OF RONALD A. KLOTE
ON BEHALF OF AQUILA, INC.
D/B/A AQUILA NETWORKS-MPS AND AQUILA NETWORKS-L&P
CASE NO. ER-__________

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI
DIRECT TESTIMONY OF RONALD A. KLOTE
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D/B/A AQUILA NETWORKS-MPS AND AQUILA NETWORKS-L&P
CASE NO. ER-________

Q. Please state your name and business address.

A. My name is Ronald A. Klote and my business address is 20 W. 9th Street, Kansas City, Missouri.

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

A. I am employed by Aquila, Inc. ("Aquila" or "Company"), as Director of Regulatory Accounting Services.

Q. Please describe your educational background and experience.

A. In 1992, I received a Bachelor of Science Degree in Accountancy from the University of Missouri-Columbia. I am a Certified Public Accountant holding a certificate in the State of Missouri. In 1992, I joined Arthur Andersen, LLP holding various positions of increasing responsibilities in the auditing division. I conducted and led various auditing engagements of company financial statements. In 1995, I joined Water District No. 1 of Johnson County as a Senior Accountant. This position involved extensive operational and financial analysis of water operations. In 1998, I joined Overland Consulting, Inc. as a Senior Consultant. This position involved special accounting and auditing projects in the electric, gas, telecommunications and cable industries. In 2002, I joined Aquila holding various positions within the Regulatory department.

Q. Have you previously testified before any regulatory bodies?

A. Yes. I have testified before the California Public Utilities Commission, the Public Utilities Commission of Colorado and the Missouri Public Service Commission.

EXECUTIVE SUMMARY

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to describe certain accounting adjustments made to Aquila Networks – MPS ("MPS") and Aquila Networks – L&P ("L&P") electric rate case filing.

Q. Please identify the schedules and any adjustments that you are sponsoring.

A. I am sponsoring the following cost of service (operational) adjustments and allocation issues:

CS-5 Payroll (MPS and L&P)

CS-6 Incentive (MPS and L&P)

CS-7 Affiliate Loadings (MPS and L&P)

CS-11 Benefits Summary Schedule (MPS and L&P)

CS-12 Benefits – Medical, Dental and Vision (MPS and L&P)

CS-13 Benefits – Pension (MPS and L&P)

CS-13a Benefits - ERISA Tracker Amortization (MPS and L&P)

CS-13b Benefits - Prepaid Pension Amortization (MPS and L&P)

CS-14 Benefits – Other Post Employment Benefits ("OPEB") (MPS and L&P)

CS-15 Benefits – 401K (MPS and L&P)

CS-16 Benefits – Profit Sharing Plan Contribution (MPS and L&P)

CS-17 Benefits - Long Term Incentive Plan ("LTIP") (MPS and L&P)

CS-18 Benefits – Supplemental Executive Retirement Plan ("SERP") (MPS and L&P)

CS-20 ESF / IBU Corporate Allocations (MPS and L&P)

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CS-30 Injuries and Damages (MPS and L&P)

CS-35 Bad Debt (MPS and L&P)

CS-60 Dues and Donations (MPS and L&P)

CS-65 Advertising (MPS and L&P)

CS-82 MPS Share of JEC and Iatan Expenses (MPS and L&P)

CS-83 Miscellaneous Test Year Adjustments (MPS only)

CS-85 Payroll Taxes (MPS and L&P)

CS-90 Property Taxes (MPS and L&P)

TAX-1 Current and Deferred Income Tax Calculation (MPS and L&P)

Capitalization Ratio (MPS and L&P)

In addition, I am sponsoring the following rate base adjustments:

RB-40 Accounting Authority Order ("AAO") (MPS only)

RBO-30 Accumulated Deferred Income Taxes (MPS and L&P)

RBO-31 Accumulated Deferred Income Taxes – AAO (MPS only)

RBO-100 Regulatory Asset / Liability ERISA Tracker (MPS and L&P)

WC–20 Prepayments (MPS and L&P)

WC-21 Prepayments – Pension (MPS and L&P)

WC-50 Cash Working Capital Calculation (MPS and L&P)

<u>CS-5 PAYROLL (MPS and L&P)</u>

Q. Please explain the payroll annualization adjustment.

A. The payroll annualization adjustment includes employee headcount and wage levels that are known and measurable as of June 1, 2006.

Q. Please explain how the adjustment was calculated.

A. Base salaries and wages, as of June 1, 2006, were obtained for all departments directly charging MPS and L&P and departments that are allocated to MPS and L&P. The base salaries and wages represent the annual salaries of all applicable full-time and part-time employees.

Q. Why were June 1, 2006, employee salary and wage levels selected to annualize payroll costs?

A. In order to allow for proper analysis and preparation of the payroll annualization adjustment, data was required to be selected from a period in advance of the actual rate case filing. Employee data from June 1, 2006, was the most current available at the time of my analysis.

Q. Please continue with your explanation of the payroll annualization adjustment.

A. Base salaries and wages were added to “Other Than Standard” earnings that were actually paid during the test period January 1, 2005, to December 31, 2005, resulting in total payroll before allocations.

Q. What are examples of “Other Than Standard” earnings?

A. “Other Than Standard” earnings categorize labor costs that are price extras on an employee’s standard pay. Examples include shift differential, overtime and call out pay.

Q. Please continue with your explanation.

A. The next step involved analyzing the total payroll before allocations by department to identify any direct charge-ins or charge-outs to other departments. Labor costs during the test year that were directly charged to MPS and L&P were subtracted. These costs will be added back later in the payroll model, to be explained below. Next, labor costs that were directly charged out of MPS and L&P were subtracted from total payroll before allocations. Then, costs from other departments not included in the payroll model that were directly charged to MPS and L&P were added in. These new subtotals, by department, were directly assigned to MPS and L&P where possible. When it was not possible to directly assign these costs, cost assignments were made based upon January 2006, corporate cost allocation factors. At this point, costs that had been subtracted previously for direct charges to MPS and L&P were added back in order to reflect 100% of these labor costs in the payroll model. The resulting amount is the total payroll annualization for MPS and L&P prior to the central support overhead costs savings ("EOS savings") adjustment.

Q. Please explain the EOS savings adjustment applied to total annualized payroll.

A. The EOS savings adjustment applied to total annualized payroll represents the value of the targeted headcount reduction in the central support areas. The EOS savings adjustment was computed by taking targeted headcount for certain functional areas and comparing the target amount to the June 1, 2006 actual employee headcount levels. The headcount variance was multiplied by an average functional area employee cost. Please see the testimony of Company witness Jon Empson for further discussions of the targeted headcount reductions included in the central support overhead cost savings.

Q. Please continue with your explanation of the payroll annualization calculation.

A. Per book payroll amounts recorded as of December 31, 2005 were subtracted from this annualized amount to arrive at the payroll annualization adjustment. At this point, the capitalization ratio was applied to compute the amount of payroll costs that will be capitalized or recorded to below the line accounts. This capitalization ratio is discussed later in my testimony. The payroll annualization adjustment was multiplied by the appropriate jurisdictional allocation amounts to arrive at the amounts applicable to retail and wholesale customers. The payroll annualization adjustment was then spread to Federal Energy Regulatory Commission ("FERC") accounts based on the percentage of test year per book payroll costs by FERC account to total payroll costs.

Q. What were the payroll annualization adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-6 INCENTIVE (MPS and L&P)

Q. Describe Aquila's compensation system.

A. Aquila maintains a two-factor compensation system, which consists of a fixed portion and a variable portion. The fixed portion consists of base salaries and wages. The variable portion consists of incentive pay computed based off of organizational and personal objectives. By adding together the fixed and variable components, a salary level that is comparable to market rates is obtained. Aquila's Human Resources Department conducts periodic market surveys to compare Aquila's compensation levels to market rates.

Q. Please identify the organizational objectives that govern the award of incentive payments.

A. The incentive pay plan is tied to the following organizational objectives that Aquila believes are critical to all stakeholders. They include:

- Customer service
- Reliability

- Effective use of capital
- Safety
- Reduce ongoing cost of service

Aquila's performance in each of these areas will be measured to determine what incentive compensation an employee is eligible for during the reporting period. Then, based on the employee's performance in regard to his or her personal goals, an annual incentive payment is calculated.

Q. How were the incentive pay adjustments computed?

A. The March 2006, actual incentive payout was obtained by department for applicable employees either directly assigned or allocated to MPS and L&P to calculate each individual's target percentage achievement. This actual achievement percentage was then multiplied by the increased target percentage in the new 2006 Variable Compensation Plan to determine the payout percentage. This percentage was multiplied by the base salary and wages obtained from the payroll model to compute the annualized incentive payout amount before EOS savings. This annualized incentive payout amount was then reduced by an EOS savings amount.

Q. Please explain how the EOS savings amount was calculated.

A. As discussed in Company witness Jon Empson's testimony, there is currently a targeted headcount reduction taking place. As such, the annualized incentive payout amount will be impacted by the reduced headcount. To compute the EOS savings amount associated with incentives, annualized incentive payout amounts were divided by total annualized payroll. This ratio was applied to total payroll EOS savings amounts. The resulting amount was subtracted from the annualized incentive payout amount to arrive at annualized incentives on a going forward basis.

Q. Explain how the total incentive annualization adjustment for operation and maintenance expenses was determined.

A. After the incentive annualization adjustments were spread to FERC accounts, amounts associated with the capital and non-operating expense accounts were subtracted from the totals. The resulting amounts were multiplied by the appropriate jurisdictional factors to arrive at the incentive annualization adjustment amount.

Q. What were the incentive annualization adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-7 AFFILIATE LOADINGS (MPS and L&P)

Q. Please explain Adjustment No. CS-7, Affiliate Loadings.

A. The affiliate load was established in 2001 in order to compute fully distributed costs on affiliate transactions. The loading is applied based on all internal labor charges that are direct charged from one business unit to another business unit. A system generated process applied the loading percentages and created the necessary monthly journal entries, much like the allocation process.

Q. Why is there a need for an affiliate loadings adjustment in this rate case filing?

A. Beginning in 2005, the affiliate loadings process was turned off. Thus, no journal entries were recorded to the books for the entire test year. The decision to turn off the loadings was made due to the large number of journal entries that were being created for amounts that were not deemed to be material. The creation of the affiliate load was to ensure that regulated business units did not subsidize non-regulated business units. As Aquila continued to exit its non-regulated businesses, the affiliate loads became smaller and smaller. As such, the decision was made to discontinue the affiliate load process in the financial accounting system, and instead to compute the amounts on an as needed basis (ie. rate cases).

Q. Please explain how the affiliate loadings adjustment was calculated.

A. During the preparation of this rate case, the affiliate loadings for test year 2005 were in the process of being computed; however, analysis was not complete at the time of the rate filing. As such, a three year average was calculated based on the affiliate entries that were posted in 2002, 2003, and 2004 to be used as a representative amount of the affiliate loadings. This amount is deemed to be conservative due to Aquila's declining non-regulated operations.

Q. What were the affiliate loading adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-11 BENEFITS SUMMARY SCHEDULE (MPS and L&P)

Q. Please explain the Benefits Summary Schedule.

A. This schedule is the accumulation of several benefits adjustments included in this rate case filing. They include the following adjustments which are explained in more detail later in my testimony:

- CS-12 Medical, Dental and Vision
- CS-13 Pension Expense
- CS-13a Pension Costs - ERISA Tracker Amortization

- CS-13b Pension Costs - Prepaid Pension Amortization
- CS-14 SFAS 106 Other Post Employment Benefits (“OPEB”)
- CS-15 401(k)
- CS-16 Profit Sharing Plan Contribution
- CS-17 Long Term Incentive Plan (“LTIP”)
- CS-18 Supplemental Executive Retirement Plan (“SERP”)

<u>CS-12 BENEFITS – MEDICAL, DENTAL AND VISION (MPS and L&P)</u>

Q. Please explain the adjustment made to the medical, dental and vision benefits.

A. The medical, dental and vision benefits adjustment is broken into two parts: self-insured coverage and premium-based coverage.

Q. Please explain the self-insured portion of medical, dental and vision benefits.

A. To calculate the self-insured portion of the claims payments, the total of actual claims paid during the test year 2005 was obtained. This total was decreased by the percentage of employee contributions calculated from the per book amounts to determine the employer portion of actual claims paid. The resulting amount was offset by EOS savings expected to be achieved. The EOS savings amount was calculated based on the percentage of the total EOS payroll savings divided by the total annualized payroll. This ratio was applied to total actual claims paid. The resulting amount was deducted from the employer portion of actual claims paid for 2005 to compute the annualized level of medical, dental and vision expense. The per book medical, dental and vision costs covering self insured claims was then subtracted from the annualized level to arrive at the adjustment amount. The capitalization ratio and appropriate jurisdictional allocators were then applied to the adjustment amount.

Q. Please explain the calculation for premium based coverage.

A. To calculate the annualized accrual for the premium based insurance, the May 2006 elections report was obtained from our outside administrator, Hewitt. The annualized accrual, net of employee contributions, was multiplied by the percentage of premium based coverage from the per book amounts to determine the annualized premium based coverage level. This amount was compared to the per book amount associated with premium based coverage. The capitalization ratio and appropriate jurisdictional allocators were applied to the resulting amount to arrive at the annualized level impacting operation and maintenance expenses.

Q. What were the medical, dental, and vision adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-13 BENEFITS – PENSION (MPS and L&P)

Q. Please explain how Adjustment No. CS-13 Pension Expense was calculated.

A. Included as part of the Stipulation and Agreement in Case No. ER-2004-0034 and continued in the Stipulation and Agreement in Case No. ER-2005-0436, Staff and Company agreed to a five-year average of actual contributions to the pension plan, either directly assigned or allocated to MPS and L&P. The pension costs for this rate case filing have been computed in a way consistent with the Stipulation and Agreements mentioned above. The five-year average included contributions made in the period from 2001 to 2005. Contributions were made in the years of 2002, 2003, and 2005. The five-year average was compared to the per book expense amount recorded during the test year. The capitalization rate was applied to the resulting amount followed by the appropriate jurisdictional factor.

Q. Does the five-year average contribution amount include a contribution made in 2005?

A. Yes. It does.

Q. Why was this contribution made?

A. Similar to the contributions in 2002 and 2003 of $35 million and $3 million respectively, Aquila contributed $8 million to the Company's pension plan in September 2005. This contribution was made to ensure that the pension plan assets exceeded the plan's accumulated benefit obligation ("ABO"). There are specific accounting rules that require writing off prepaid amounts and taking significant charges to other comprehensive income when a plan's assets fall below its ABO status. In addition, higher premiums can be charged by the Pension Benefit Guarantee Corporation ("PBGC") if the plan is under funded. Finally, if the plan is under-funded, then all plan participants are required to be notified in the event of such an occurrence. As such, the $8 million contribution in 2005 was needed to avoid these negative impacts similar to the 2002 and 2003 pension plan contributions.

Q. What were the pension expense adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-13a BENEFITS - ERISA TRACKER AMORTIZATION (MPS and L&P)

Q. Please explain what the ERISA minimum tracker amortization is.

A. As stated in the previous rate case Stipulation and Agreements in case no.'s ER-2004-0034 and ER-2005-0436 (Page 6),

> Company is authorized to reflect pension cost equal to this provision for the ERISA minimum and record the difference between the ERISA minimum and the annual provision for pension cost as a regulatory asset or liability. This regulatory asset and/or liability is intended to track the difference between the provision for the ERISA minimum contribution included in cost of service in this case, and the Company's actual ERISA minimum contributions made after the effective date of rates established in this case. This regulatory asset and/or liability will be included in rate base in the Company's next rate case and amortized over a five (5) year period.

As such, the Company has collected in rates certain amounts for pension costs during the test period. These collections are compared to actual contributions. The difference between these amounts are treated as regulatory assets or liabilities.

Q. What period of time did the Stipulation and Agreement require amounts to be amortized?

A. The Stipulation and Agreement provided for a five-year amortization.

Q. Did the company comply with the Stipulation and Agreement in this rate case filing?

A. Yes. The Company has been recording the collections as a regulatory liability. As discussed earlier, in September 2005 a contribution was made to the pension plan which off-set this liability amount for both MPS and L&P.

Q. At December 31, 2005, was the tracking mechanism described above a regulatory asset or liability?

A. For MPS, a regulatory liability existed and is reflected in rate base offset adjustment RBO-100. For L&P, a regulatory asset existed and is reflected as a rate base addition in RBO-100.

Q. How were the ERISA tracker amortization adjustments calculated?

A. For MPS, the regulatory liability balance as of December 31, 2005, offset by the contribution amount in September 2005, was obtained and amortized over five years. The capitalization rate and appropriate jurisdictional allocations were applied. This amortization was a reduction to MPS cost of service. For L&P, the regulatory liability balance as of December 31, 2005, offset by the contribution amount in September 2005, was obtained which created a regulatory asset. This amount was amortized over a five year period. The capitalization rate was applied to the annual amortization amount. This amortization increases L&P's cost of service.

Q. What were the ERISA tracker amortization adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-13b BENEFITS – PREPAID PENSION AMORTIZATION (MPS and L&P)

Q. What does the prior Case No. ER-2005-0436 provide in regards to prepaid pension amortization?

A. The Stipulation and Agreement in Case No. ER-2005-0436 provides the following at page 6-7:

> MPS rates include a $2,110,436 annual provision, prior to capitalization, for an MPS electric jurisdictional prepaid pension amortization. This amortization will be in effect for a five and one-half (5 ½) year period beginning with the effective date of rates established in Case No. ER-2004-0034. L&P rates include a $3,352,742 annual provision, prior to capitalization, for L&P electric prepaid pension amortization. This amortization will be in effect for a nine and one-quarter (9.25) year period beginning with the effective date of rates established in Case No. ER-2004-0034.

Q. Has the Company complied with the Stipulation and Agreement in Case No. ER-2005-0436?

A. Yes. The Company has complied and has included in their cost of service the annual amortization agreed too.

Q. Please explain how adjustment CS-13b Prepaid Pension Amortization has been computed for MPS and L&P.

A. The annual amortization amounts contained in the Stipulation and Agreement in Rate Case No. ER-2005-0436 were obtained and compared to per book amortization amounts. The capitalization rate was applied to the resulting amount.

Q. What were the prepaid pension amortization adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-14 BENEFITS – OTHER POST EMPLOYMENT BENEFITS (MPS and L&P)

Q. Please explain the components of the SFAS 106 Other Post-Employment Benefits adjustment.

A. The annual OPEB expense under the SFAS 106 calculation is provided by our actuary Hewitt. The calculation of post retirement benefit cost includes the following components:

- Service cost
- Interest cost
- Expected return on assets
- Prior service cost amortization
- Transition obligation amortization
- Gain / loss amortization
- Regulatory adjustment

These components are defined as follows: The employee service costs are defined as the estimated costs of benefits paid in the future, discounted to the present year. The interest cost is the increase in the projected benefit obligation due to the passage of time. The expected return on assets represents the increase in funds from interest, dividends, and realized and unrealized changes in the fair market value of the plan in the year. The prior service cost component results from amendments to the pension plan. The transition obligation is the under funded and unrecognized accumulated post-employment benefit obligation for all plan participants at the date SFAS 106 is adopted. Differences between the actuarial assumptions and actual experience, the gains/losses, are amortized over five years. Regulatory adjustment includes an adjustment to the Missouri jurisdictions for the prescribed method for recognizing actuarial gains and losses.

Q. How were the components used in calculating the OPEB adjustment?

A. The following components were added together: service cost, interest cost, amortization of transition amount, amortization of gain/loss, and amortization of prior service cost. The expected return on assets was then subtracted out of this calculation to derive the estimated OPEB expense. The direct and allocated portions of this expense were totaled to arrive at a 2006 annualized OPEB amount for MPS and L&P. The difference between the 2006 annualized OPEB amount and the amount recorded on the books as of December 31, 2005, was used to calculate the adjustment. The adjustment was then multiplied by a capitalization factor to eliminate OPEB costs that are capitalized. An appropriate jurisdictional factor was applied to the resulting amount.

Q. Has Aquila met its obligation concerning OPEB contributions as defined in the Stipulation and Agreement from Case No. ER-2005-0436?

A. Yes. Per the Stipulation and Agreement from Case No. ER-2005-0436 at page 7:

> “Aquila agree’s to make at least one payment per year equal to the current year FAS-106 calculation.”

In December 2005, Aquila funded its prior year obligations amounting to $7,017,529 reflecting the catch-up of 2003 and 2004 FAS-106 contributions and $1,975,884 for 2005. Going forward, Aquila will generally fund the FAS-106 contributions at the end of the second or third quarters.

Q. What were the OPEB adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

<u>CS-15 BENEFITS – 401K (MPS and L&P)</u>

Q. Please describe Aquila's 401(k) plan.

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

Q. Is there a portion that is matched by Aquila?

A. Yes. Aquila matches a portion of the funds invested by employees up to 6% of base salary and wages.

Q. Describe the adjustment made to cost of service for 401(k) expense on adjustment CS-15.

A. The 6% matched portion, called 401(k) Employer Share, was calculated by taking the 401(k) balance for test year end December 31, 2005, and dividing it by the per books base pay, excluding incentives, for the same period to arrive at the overall percentage of base pay matched by Aquila. This percentage was then multiplied by the annualized payroll amount as calculated in adjustment CS-5 to arrive at the annualized 401(k) cost. To calculate the 401(k) adjustment, per book 401(k) amounts were deducted from the annualized 401(k) cost. This difference was then multiplied by the capitalization rate to eliminate any costs that are capitalized from the adjustment. An appropriate jurisdictional factor was applied to the resulting amount.

Q. Why is the percentage not simply six percent of base salaries and wages?

A. Certain employees choose not to participate to the full six percent match for various reasons which has the effect of drawing down the overall percentage.

Q. What were the 401k adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-16 BENEFITS – PROFIT SHARING PLAN CONTRIBUTION (MPS and L&P)

Q. How was Adjustment No. CS-16, the Profit Sharing Plan Contribution adjustment calculated?

A. The profit sharing plan contribution allows for a contribution amount made to an employee's 401k plan at a minimum of two percent to approximately four percent. The target contribution level used by the Human Resources Department is three percent; therefore, the profit sharing plan contribution adjustment was calculated by taking an average three percent Company-wide contribution level and multiplying it by the annualized payroll amount. This amount was then compared to the per book amount recorded at test year-end December 31, 2005. The capitalization rate was applied to obtain the ESOP adjustment. An appropriate jurisdictional factor was applied to the resulting amount.

Q. What were the Profit Sharing Plan Contribution adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-17 BENEFITS – LONG TERM INCENTIVE PLAN (MPS and L&P)

Q. Please describe the purpose of a Long Term Incentive Plan ("LTIP").

A. The LTIP is the variable compensation portion of executive salaries and wages where awards are based on multi-year Company performance.

Q. Please describe the purpose of Adjustment CS-17, the LTIP adjustment.

A. The purpose of Adjustment CS-17 was to eliminate from the test year all amounts recorded to the LTIP incentive resource 1799. Thus, the Company is not asking for recovery of any LTIP-related cost in this rate case. The as recorded amount for the test year-end, December 31, 2005, was eliminated from the cost of service filing in this rate case proceeding.

Q. What were the LTIP adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-18 BENEFITS – SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN ("SERP") (MPS and L&P)

Q. Please explain Adjustment No. CS-18, SERP.

A. Please see the testimony of Company witness Philip Beyer for discussion of Adjustment CS-18 SERP.

Q. What were the SERP adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-20 ESF / IBU CORPORATE ALLOCATIONS (MPS and L&P)

Q. What do the ESF and IBU acronyms above represent in the system cost allocation process?

A. ESF represents "Enterprise Support Functions" (i.e. corporate functions). IBU represents "Intra-Business Unit" (i.e. operations support departments). These represent the two broad functions maintained by Aquila for system cost allocations. At times, the system cost allocations are referred to as the central support allocations process which has been maintained back to approximately 1995.

Q. Please describe the ESF / IBU central support function cost allocation process.

A. The central support function costs are either assigned directly or allocated to the business units using one of three methods:

- Direct Assignment of Costs: where costs are directly associated with a specific business unit they are directly charged to that business unit.
- Allocation of Costs Based on a Specific Cost Driver: this type of allocation includes allocating the net costs remaining in the pool after direct assignment and attributing them to specific business units based upon a specific cost driver. This includes developing an allocation factor that has a direct cause and effect relationship with the types of costs being allocated. An example of this would include allocating human resources costs on employee headcount.
- Allocation of Costs Based on a "General" Allocator: costs accumulated in departments that are general in nature and benefit the organization as a whole and are not necessarily reflective of a specific cost driver are allocated using a three factor formula consisting of the arithmetic average of payroll charged to expense, gross

margin, and net plant. An example of this would include allocation of the corporate accounting department.

Q. Where can an explanation of Aquila's cost allocation drivers be found?

A. Aquila's 2005 Corporate Cost Allocation Manual included with Aquila's March 2006 Annual Affiliate Filling to the Commission.

Q. Were there any changes to the allocations process during the test year?

A. No significant changes occurred during the test year. Yet, beginning January 1, 2006, the allocation drivers used to allocate costs in the methods described above were adjusted to reflect the elimination of business units that the Company has either successfully completed the sale of the utility assets, or that Company intends to complete the sale of the utility assets by year end. Please see the testimony of Company witness Jon Empson for a listing of these utility assets.

Q. Why were the allocation drivers changed January 1, 2006, when the actual sales dates were at a later date?

A. The changes were made January 1, 2006 for greater transparency and simplicity of our accounting records for both internal and external users of the financial statements.

Q. How does this change create more transparency?

A. The answer is two-fold. First, for SEC reporting purposes, the utilities held for sale have been reclassified as discontinued operations as defined under Statement of Financial Accounting Standard No. 144 (SFAS 144). The operating costs of the utility divisions held for sale reflect only the direct operating costs that are expected to be assumed by the buyer once the sales are completed. Central support costs will be provided by the buyers using their own infrastructure and, therefore, these costs are reported as part of Aquila's continuing operations. In order to maintain our records consistently with our external reporting in 2006, the discontinued operations were eliminated from the allocation process by changing the allocation percentages to reflect only the remaining business units.

Q. What is the second reason for changing the allocation percentages to reflect the utility sales as of January 1, 2006?

A. The second reason is to create more transparency in the regulated reporting and rate case preparation process. Changing the allocations once at the beginning of the year reflects an annual impact in the detail books and records supporting the cost of service for 2006. If we were to change the allocation factors with each separate utility asset closing, we would have to make four or more adjustments throughout the year. Normalizing the impact of these adjustments would likely prove to be confusing.

Q. Please compare the overall allocation percentages during the test year to the overall result of the new factors effective January 1, 2006.

A. See Schedule RAK-1.

Q. Please explain how the above changes are incorporated into Adjustment No. CS-20, ESF / IBU Corporate Allocations adjustment.

A. Very simply, the ESF / IBU Corporate Allocations adjustment consists of test year "residual" ESF and IBU allocation pool costs less central support overhead cost savings ("EOS savings") being reallocated to MPS and L&P business units based on the allocation factors in effect as of January 2006.

Q. What cost allocation methodology does Adjustment No. CS-20 use to reallocate "residual" test year allocation pool costs?

A. As described in my testimony above, the methods of assigning or allocating costs to the business units consists of the following three areas:

- Direct assignment of costs
- Allocation of costs based on a specific cost driver
- Allocation of costs based on a "general" allocator

Adjustment No. CS-20 relates to the allocation pools associated with specific cost drivers and allocation pools that are generally allocated. In essence, any "residual" cost allocated in any given month during the test year by a factor different than the allocation factor in effect at January 2006, would be adjusted in Adjustment CS-20.

Q. As previously mentioned, please explain what is meant by reallocating net "residual" allocation pool costs?

A. The term "residual" refers to the net remaining allocation pool costs that have not been included in other rate case adjustment areas in this rate filing. The majority of the "residual" pool includes charges that can be classified as non-labor in nature. The following is a listing of the types of costs that have been removed from the allocation pool since they have been adjusted individually and thus, not included in Adjustment No. CS-20. Other rate case adjustments were computed on allocated costs following the same methodology as outlined in my testimony and as utilized in Adjustment No. CS-20. The types of costs excluded from the allocation pool include:

- Payroll (CS-5), Incentives (CS-6), Employee Pension and Benefits (CS-11), Insurance (CS-21), Injuries and Damages (CS-30), Dues and Donations (CS-60), Advertising (CS-65), Postage (CS-70), Payroll Taxes (CS-85), Property Tax (CS-90), – Aquila witness Ron Klote.

- Depreciation Expense (CS-95) – Aquila witness Susan Braun.

Q. Besides adjusting the ESF and IBU total allocation pool for individual rate case adjustments, have you made other adjustments to the allocation pool costs that were allocated to MPS and L&P during the test year?

A. Yes. First and foremost, certain costs are retained in corporate business units and are not allocated out to the Network business units. As such, they are not included as part of the total allocation pool and thus not part of the cost of service in this rate case filing. In addition, the following adjustments were made to the corporate allocation pool before arriving at the net "residual" allocation pool. They include:

1. **Year-end Review**: Each year, the corporate departments, both those that allocate residual costs and those that retain costs, are audited for proper classification of major expenses. The audit examined journal transactions to determine if costs a) should have been charged to a department that does not allocate residual costs; or, b) were costs benefiting shareholders but not ratepayers. A summary of 2005 corporate costs by department and type of cost was prepared. In the Company's opinion, those costs in the amount of $180,769, should be excluded from the rate case and were, therefore, removed from the corporate cost allocation pool.
2. **Bonus:** This adjustment excludes 2005 corporate employee bonus costs of $691,004 that were allocated to MPS and L&P. MPS and L&P direct employee bonus amounts have been excluded from 2005 payroll costs in the CS-83 Miscellaneous Test Year Adjustments.

3. **Six Sigma:** One-time costs of 2005 payments to the Six Sigma Academy of $277,677 associated with the Six Sigma-based process improvement initiative at Aquila, Inc. were removed from the corporate cost allocation pool.

4. **Board of Directors**: Directors' remunerations of $73,000, for meetings other than the regularly-scheduled 2005 quarterly board meetings, and compensation of $192,709 paid to individuals who left the board of directors in 2005 were removed from the corporate cost allocation pool. Please see the testimony of Company witness Jon Empson for further discussion.

5. **Norma Dunn Expense**: Aquila president and CEO Richard Green announced in May 2006, that the position of Senior Vice President-Corporate Communications held by Norma Dunn had been eliminated. This adjustment eliminated 2005 non-payroll costs of $11,284 associated with Norma Dunn that had not been eliminated in other adjustments from the corporate cost allocation pool.

6. **Customer Service GUI write-off:** In December 2005, there was a $3,352,233 write-off of a Graphical User Interface (GUI) application under development for Call Center enhancements. It was determined that the system no longer fit the Company's needs and the decision was made to abandon the project. Write-off costs of $2,773,728 not eliminated in other adjustments were removed from the corporate cost allocation pool.

7. **10750 Lease:** As a result of Aquila's utility sales, the need for fewer central corporate support personnel was recognized by the Company's decision not to renew the lease on the 10750 E. 350 Hwy building at the Raytown, Missouri campus. Lease costs of $989,490 for 2005 were removed from the corporate allocation pool.

Q. Please explain the final adjustment that was made to Adjustment No. CS-20.

A. As explained in the testimony of Company witness Jon Empson, the Company plans to have a reduction in the central support overhead costs following completion of the asset sales process that is occurring during 2006. Accordingly, the total annualized allocated corporate cost for MPS and L&P was further reduced by MPS and L&P's share of central support overhead savings. This amount was accumulated by functional area. This amount is further discussed in the testimony of Company witness Jon Empson.

Q. In summary, how was the MPS and L&P Adjustment No. CS-20 compiled.

A. Total corporate allocation pool costs were reduced by rate case adjustments and miscellaneous adjustments discussed above. The "residual" corporate allocation pool was then allocated to MPS and L&P using January 2006, allocation factors. The resulting amount was offset by the central support overhead savings amount to arrive at a total annualized "residual" corporate amount. This amount was then compared to the "residual" corporate per book amount for the test year to arrive at the adjustment amount. The appropriate jurisdictional factors were then applied.

Q. What was the amount of the MPS and L&P Adjustment No. 20, ESF / IBU Corporate Allocations, for this rate case proceeding?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-21 INSURANCE (MPS and L&P)

Q. Please explain cost of service Adjustment No. CS-21, Insurance.

A. This adjustment annualizes insurance costs based on current policy premiums, which are renewed at various times throughout the year. These premiums include the following types of coverage: property, general liability, directors and officers, workers' compensation, aviation, fiduciary liability, crime, employment practices, vehicles, finite risk, and surplus lines tax. The premiums were directly assigned to MPS and L&P based on the Company's insurance assignment methodology developed at the beginning of 2006. Additionally, cost assignments were made based upon January 2006 corporate cost allocation factors for some of the premiums, which were assigned to a corporate allocated department. The adjustment was calculated by taking the annualized direct and allocated MPS and L&P premium costs, less the per book amount at December 31, 2005. The appropriate jurisdictional factor was applied to the resulting adjustment.

Q. What were the MPS and L&P CS-21 Insurance adjustments?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-26 MAJOR MAINTENANCE EXPENSE (MPS and L&P)

Q. Please describe the two components of Adjustment No. CS-26, Major Maintenance Expense.

A. Adjustment No. CS-26 consists of (1) an increase to FERC Account 513 Maintenance of Electric plant for the increased levels of maintenance required for the South Harper peaking facility (MPS only), and (2) the adjustment for significant turbine overhauls for the following generating plants:

MPS
- Sibley #1, 2 and 3
- South Harper

- Jeffrey Energy Center ("JEC")
- Greenwood #1, 2, 3 and 4
- Ralph Green

L&P

- Lake Road Unit #1, 2, 3, 4 and 5

Q. Please describe the regular maintenance component of adjustment CS-26

A. The first component of adjustment CS-26 is for regular annual maintenance needed for the South Harper peaking facility. The South Harper peaking facility was constructed and put in service during the test year. As such, the test year does not reflect an annual level of maintenance expense for the plant. This adjustment increases the cost of service in this case to reflect an annualized level of maintenance costs for the MPS business unit only.

Q. Please describe the turbine overhaul maintenance portion of Adjustment CS-26.

A. Turbine overhaul maintenance expense is dynamic. Depending on the type of equipment being serviced, scheduled maintenance can typically follow a four to seven-year cycle. As a result, actual expense can increase considerably in years corresponding to major maintenance service. To mitigate the possibility of a large expense increase in years corresponding to a proposed rate increase, major maintenance expense is spread out over the service life of the related equipment through an accrual process. This method provides a more consistent measurement of annual maintenance expense.

Q. How was the turbine overhaul maintenance expense component of Adjustment CS-26 computed?

A. An annualized accrual level was computed for each plant covered by the turbine overhaul maintenance account. Where plant maintenance history was available, accrual amounts were computed using this history divided by the scheduled maintenance interval. For the South Harper plant, an annual accrual maintenance amount was included to begin accruing the costs of providing the periodic maintenance required. The total of the annualized accrual amounts computed were compared to amounts being accrued on the books during the test year 2005.

Q. What was the total major maintenance Adjustment for MPS?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-30 INJURIES AND DAMAGES (MPS and L&P)

Q. Please explain the costs included as injuries and damages in Adjustment No. CS-30.

A. The injuries and damages ("I&D") liability reserve FERC Account 228.2 consists of four major areas:

- General liability
- Worker's compensation
- Property damage
- Auto liability

The liability reserve houses all accrued claims expensed in FERC Account 925, I&D expense. The liability reserve is relieved when payment of I&D claims under the four categories listed above takes place.

Q. Please explain how Adjustment No. CS-30, I&D expense, was calculated for both MPS and L&P's electric operations for purposes of this rate proceeding.

MPS:

A. The Company obtained a three-year payout history from FERC Account 228.2 that shows the payout history for I&D claims. From this payout history, a three-year average was calculated on actual electric claims paid for the 12 months ended December 31, 2003, 2004, and 2005. The computed three-year average represents MPS's annualized level of I&D expense included in this rate case filing.

Q. Why was a three-year average chosen?

A. I&D claims can vary significantly from year to year. A three-year average was used to establish an appropriate on-going level of I&D expense for MPS by leveling out fluctuations in the reserve account that can exist from one year to the next depending on claims activity. This method is also consistent with the method used by the Commission Staff in MPS's last three rate proceedings, Case Nos. ER-2001-672, ER-2004-0034 and ER-2005-0436.

Q. Were there any adjustments made to actual paid claims for the test year ended December 31, 2005, that has been included in the three-year average calculation?

A. Yes. In March 2005, a journal entry was made to record insurance claims paid from May 2004 through February 2005 that had not been correctly recorded at the business unit level on a monthly basis. In the last Missouri electric rate case, Case No. ER-2005-0436, a manual adjustment had been made to include those electric paid claims that pertained to 2004 in the three-year average calculation. For purposes of this rate filing, the manual adjustment has been removed from the 2004 data in FERC Account 228.2 and the electric paid claims have been included in the 2005 data as recorded during the test year to be picked up in the three-year average calculation. This was done to avoid a double counting effect of those claims. The 2004 claims have been separately identified in the workpaper support for Adjustment No. 30.

Q. Please continue explaining how the I&D expense adjustment was completed.

A. The annualized level of I&D expense for MPS was then compared to the electric claim accruals recorded in FERC Account 925000 during the test year ended December 31, 2005. An appropriate jurisdictional factor was applied to the resulting amount.

Q. What was the amount of the MPS Adjustment No. 30, I&D expense for this rate case proceeding?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment total.

L&P:

A. L&P employed the same method as MPS for calculating the annualized level of I&D expense to include in its rate case filing. First, a three-year payout history was obtained from FERC Account 228.2 that shows the payout history for I&D. From this payout history, a three-year average was calculated on actual electric claims paid for the 12 months ended December 31, 2003, 2004, and 2005.

Q. Were there any adjustments made to actual electric paid claims for the test year ended December 31, 2005, that has been included in the three-year average calculation?

A. Yes. Similar to MPS, a journal entry was made in March 2005 to record insurance claims paid from May 2004 through February 2005, which had not been correctly recorded at the business unit level on a monthly basis. In the last Missouri electric rate case, Case No. ER-2005-0436, a manual adjustment had been made to include those electric paid claims that pertained to 2004 in the three-year average calculation. For purposes of this rate filing, the manual adjustment has been removed from the 2004 data in FERC Account 228.2 to avoid a double counting effect. The 2004 electric paid claims have been included in the 2005 data as recorded during the test year to be picked up in the three-year average calculation, which is consistent with the treatment of 2004 MPS electric paid claims.

Q. Please continue.

A. After calculating L&P's three-year average electric claim payout, an electric/steam A&G allocation percentage was applied to the three-year average to determine L&P's annualized level of I&D expense for its electric operations.

Q. Please continue explaining how the I&D expense adjustment was completed.

A. The annualized level of I&D expense for L&P's electric operations was then compared to the electric claim accruals recorded in FERC account 925000 during the test year ended December 31, 2005.

Q. What was the amount of the L&P Adjustment No. 30, I&D expense for this rate case proceeding?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment total.

CS-35 BAD DEBT (MPS and L&P)

Q. What is the purpose of the bad debt adjustment, Adjustment No.CS-35?

A. The bad debt adjustment updates MPS and L&P's electric jurisdictional test year per book bad debt expense to be in line with the rate case weather-normalized electric jurisdictional revenue levels. The first step annualizes the companies' uncollectible accounts via net write-offs to an annualized level for the test year. The annualized level of bad debt expense is calculated by multiplying the actual average net write-off rate for the last 3 years (2003-2005) by the adjusted test year level of annualized jurisdictional electric operating revenues.

Q. Why was a three-year average chosen?

A. Net write-offs will vary from year to year. A three-year average better represents an on-going level of bad debt expense for MPS and L&P by leveling out fluctuations in bad debt write-offs that can exist from one year to the next. This method is also consistent with the method used by the Commission Staff in MPS's last rate proceeding, Docket No. ER-2005-0436.

Q. Please continue.

A. The new electric jurisdictional bad debt level is compared with MPS & L&P's electric jurisdictional per books test year bad debt expense. The difference is the electric jurisdictional bad debt adjustment.

Q. What was the amount of Adjustment No. 35, bad debt expense for this rate case proceeding?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-60 DUES AND DONATIONS (MPS and L&P)

Q. Please explain Adjustment No. CS-60, Dues and Donations Expense.

A. This adjustment eliminates all dues and donations charged above-the-line to MPS and L&P's electric operations except Edison Electric Institute ("EEI") and Electric Power Research Institute ("EPRI") dues. The expenses relating to EEI and EPRI have been included in both MPS and L&P's cost of service because they provide a benefit to ratepayers.

Q. What benefit does EEI provide to ratepayers?

A. EEI fosters the exchange of information on topics such as utility operations and environmental legislation. Member utilities and other interested parties rely upon EEI for authoritative analysis and critical industry data. EEI also conducts forums for member company representatives to discuss issues and strategies to advance the industry and to ensure a competitive position in a changing marketplace, resulting in significant savings for Aquila that can be passed on to both MPS and L&P customers.

Q. What are some examples of program areas and services that EEI provides to Aquila?

A. Aquila is involved in various EEI committees and general services that they provide to members. The Committees deal with specific industry issues which in many cases initiates development of various products and services, some of which are exclusive for use by members only. The following is a listing of program areas and services that provide a direct benefit to Aquila:

- Environmental
- Finance & accounting
- Infrastructure: generation, transmission and distribution

Q. Please provide some specific examples of the benefits that are recognized from the Company's involvement in the above mentioned areas.

A. With respect to environmental services, Aquila participates in the Clean Air Strategy Group, the Climate Change Group and the Environmental Executive Advisory Group. As an EEI member, Aquila representatives can meet with other members and share information and ideas related to new regulations in an effort to understand in advance new federal rules prior to promulgation. In turn, this allows for the reduction of consulting costs and reduces the overall costs of compliance, as with pollution controls, since Aquila can plan for and adapt for design changes well in advance of upcoming regulatory changes. This has proven to be a benefit with hazardous air pollutant regulations as well as air transport rules. In addition, EEI provides updates on scientific research and Environmental Protection Agency ("EPA") research such as climate change and health impacts of air pollution, which are open for discussion on pending controls and regulatory rules before various regulatory agencies. Aquila benefits from this information by hearing first-hand proposed regulatory changes to the electric industry. Aquila can gain insight on how other companies in the industry plan on implementing the changes which saves considerable consulting costs.

Q. Please continue.

A. In addition to environmental benefits, there are several benefits that Aquila realizes from membership on various transmission committee's which focus on customer reliability. EEI pulls together member utilities and facilitates focus groups allowing for the review of technology and discussions regarding utilization of assets in a cost effective manner and providing increased reliability. Aquila is currently staying abreast of several subjects for possible use in the future. One such item involves real-time monitoring of transmission lines. This involves monitoring transmission conductors to allow for dynamic loading above the standard conductor ratings. This could allow Aquila to increase its ratings on several critical transmission lines rather than rebuilding existing lines or adding new transmission lines.

Q. Have any lobbying costs associated with EEI been eliminated from this adjustment?

A. Yes. Percentages associated with lobbying activity compared to all other EEI activities were obtained from EEI and used to calculate the disallowance of lobbying expenditures for the test year ended December 31, 2005. The calculated percentage disallowance related to lobbying activity was actually applied to the 2005 EEI invoices and recorded to the general ledger during the test year to non-utility expense. The percentages are based on EEI's estimated lobbying expenditures for calendar year 2005 which were identified as lobbying and political expenditures under the Lobbying Disclosure Act of 1995.

Q. What benefit does EPRI provide to ratepayers?

A. EPRI was established in 1973 as an independent, non-profit center for electricity and environmental research. EPRI addresses critical industry issues and conducts research on behalf of its members. Through a collaborative effort, EPRI is able to bring together members, scientists, engineers and other experts in an effort to uncover solutions to challenges that face the electric power industry. EPRI's focus and solutions encompass every aspect of the electric industry, from generation, delivery and end-use, with special focus on health, safety, and the environment.

Q. What specific EPRI programs has Aquila found to be a direct benefit to the Company and ratepayers?

A. There are several programs that come to mind. The first and most significant is *The EPRI Technical Assessment Guide* ("TAG") *– Power Generation and Storage Technology Options.* Tag helps Aquila's power supply planners and decision-makers optimize capital investments in power generation and energy storage infrastructure. TAG is a widely accepted industry authoritative source of generation cost and operating data. The TAG also provides a data base and methodology for performing preliminary technical and economic evaluation of technologies. To secure similar information through other means would require extensive time at a significant cost in consultant fees and employee time. One specific example for the use of TAG is in the development of certain portions of the bi-annual IRP that Aquila files with the Commission. Other programs utilized include environmental control programs consisting of fluid spill containment systems and pollution control device development. One such example is the Mineral Oil Spill Evaluation System ("MOSES"), which was developed by EPRI in response to proposed Spill Prevention, Countermeasures, and Controls ("SPCC") regulations. This system is currently used by Aquila and is specifically designed to evaluate the probability of releases, such as oil spills reaching water. The MOSES system is most commonly used at substations and also has the capability to check various controls to see how effective they will be. In addition, Aquila is currently considering another product developed by EPRI known as the Rich Reagent Injection, which is designed to reduce nitrogen oxides.

Q. What was the amount of the MPS and L&P Adjustment No. 60, Dues and Donations Expense for this rate case?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-65 ADVERTISING (MPS and L&P)

Q. Please explain Adjustment No. CS-65, Advertising Expense.

A. This adjustment eliminates all advertising expenses recorded to above-the-line accounts for the test year ending December 31, 2005, except those expenses for informational and safety advertisements that directly benefit MPS and L&P electric customers.

Q. What do the informational and safety advertisements consist of?

A. The informational and safety advertising expenses remaining in operating expenses relate to news releases, customer bill inserts, newspaper advertisements, customer handbooks and newsletters such as the "Connected." Informational advertisements such as local community ads are placed from time to time to inform the public of Aquila's specific contact information such as phone and website address. Such ads are placed in community guides or chamber of commerce directories published annually that are distributed, for example, to new residents moving into the area. Newspaper advertisements regarding safety are generally distributed twice during the test year.

Q. Please describe the general content of the safety advertisements.

A. Safety advertisements, such as "Don't Take Chances, Call Before You Dig", inform the public of Dig-Rite programs that help residents avoid potential expense as well as serious or fatal injury.

Q. Has the Company provided additional work paper support in this rate filing that has not been provided in the past for the Advertising adjustment?

A. Yes, based on discussions with Staff during pre-hearing conferences held during the last Missouri rate case, Case No. ER-2005-0436, the Company has included with this rate filing a detailed listing of source journals for advertising expenses that were recorded to the general ledger for the twelve months ended December 31, 2005, prior to being allocated out to the various business units, specifically the MPS and L&P electric divisions. The 2005 allocation percentages were applied by department to the total invoice amounts to determine MPS and L&P's allocated electric share. This is provided in the work paper support for Adjustment No. CS-65.

Q. What was the amount of the MPS and L&P Adjustment No. 65, Advertising Expense for this rate case?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-82 MPS SHARE OF JEC AND L&P SHARE OF IATAN EXPENSES

JEC EXPENSE (MPS Only)

Q. Please explain the MPS Share of JEC Expense, Adjustment No. CS-82.

A. This adjustment begins with the MPS share of JEC operating and maintenance ("O&M") and administrative and general ("A&G") expenses, excluding JEC activity considered in other rate case adjustments. JEC activity considered in other adjustments include labor, fuel operating expense, SO2 allowances, and transmission expense. Westar operates JEC as a department within its KPL business unit. Westar reports the MPS share of JEC-related O&M and A&G activity through monthly billings. In addition, Westar bills directly to MPS costs associated with generation support, pension and benefits. Generation support costs represent billings for people who work to support JEC's daily operations, but do not charge their time directly to the JEC department within Westar's KPL business unit. Included in the generation support costs are loadings for pension and benefits.

Q. Please explain how this adjustment was calculated.

A. The adjustment normalizes test year activity for the MPS share of JEC O&M and A&G costs as well as the direct costs related to generation support, pension and benefits. Normalizing activity includes reviewing recorded transactions and adjusting for any significant abnormalities that make the test year period not representative of an on going level of expense.

Q. Were there any adjustments related to activity that would be considered abnormal during the test year ending December 31, 2005?

A. Yes. There were 2004 true-up adjustments made in March 2005, related to 2004 activity for A&G expenses, direct-billed generation support and direct-billed pension and benefits. The true-up adjustments represent corrections to accruals based on actual billings received after year-end 2004. These adjustments are considered abnormal as they relate to activity outside of the test year. Activity related to periods outside of the test year is removed to establish an on-going level of expense representative of the test year.

Q. Were there other adjustments to normalize the MPS share of JEC activity?

A. Yes. For 2006, the A&G load rate was increased from 19.28% to 22.61%. As a result, an adjustment to increase A&G expense is proposed to reflect the on-going level of A&G activity.

Q. How is the MPS share of JEC A&G expense calculated?

A. The MPS share of JEC A&G expense is calculated by multiplying total O&M expense activity related to A&G, by the A&G load rates.

Q. What was the total MPS share of JEC expense adjustment?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment total.

<u>IATAN EXPENSE (L&P Only)</u>

Q. Please briefly discuss the nature of L&P’s Share of Iatan, Adjustment No. CS-82.

A. Monthly accruals are performed related to L&P share of Iatan expenses. A year-end true-up is assessed based on review of the Iatan Summary of Transactions received from Kansas City Power & Light Company ("KCPL"). The year-end Iatan Summary of Transactions reports L&P's actual share of Iatan expenses for the year being reported. The year-end true up corrects for the over or under accrual L&P recorded throughout the year.

Q. Please explain the purpose of the L&P Share of Iatan Adjustment No. CS-82.

A. The purpose of the adjustment is to normalize the 2005 test year to reflect on going expense levels. Normalizing activity includes reviewing recorded transactions and adjusting for any significant abnormalities that make the test year period not representative of an on-going level of expense.

Q. Were there any adjustments related to activity that would be considered abnormal?

A. Yes. There were 2004 true-up adjustments made in January 2005, related to 2004 activity. In addition, there were 2005 true-up adjustments made in January 2006, related to 2005 activity. The true-up adjustments represent corrections to accruals based on actual billings received after year-end. The 2004 adjustments are considered abnormal as they relate to activity outside of the test year. Activity related to periods outside of the test year is removed to establish an on-going level of expense representative of the test year. The actual 2005 true-up adjustment recorded in 2006 was added back to 2005 test year amounts.

Q. What was the total adjustment for L&P Share of Iatan?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment total.

CS-83 MISCELLANEOUS TEST YEAR ADJUSTMENTS (MPS Only)

Q. Please explain Adjustment No. CS-83, Miscellaneous Test Year Adjustments.

A. Adjustment No. CS-83 includes miscellaneous adjustments to eliminate certain transactions recorded during the test year from the cost of service filing in this rate case. The first miscellaneous adjustment includes the elimination of amounts that were written off during the test year for disallowances of South Harper legal and storage costs as determined in the settlement of Case No. ER-2005-0436. The second adjustment includes the elimination of certain bonus transactions that were recorded to the bonus resource 1003. These amounts were eliminated from the cost of service filing. An appropriate jurisdictional factor was applied to both adjustment amounts.

Q. What was the amount of Adjustment No. CS-83, Miscellaneous Test Year Adjustments for MPS?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment total.

CS-85 PAYROLL TAXES (MPS and L&P)

Q. What types of payroll taxes are included in the payroll tax adjustment, Adjustment No. CS-85?

A. The payroll tax adjustment includes Social Security Tax (“FICA”) and Medicare taxes.

Q. How was the payroll tax adjustment calculated?

FICA

A. During 2006, the first $94,200 of an employee’s compensation will be taxed at the FICA tax rate of 6.2%. Therefore, FICA payroll tax ratios had to be computed and applied to the total annualized payroll. The FICA ratios were computed by using the salary and wage database as of June 1, 2006. All salary and wage costs up to a limit of $94,200 were totaled and divided by the total salary and wage costs to obtain the FICA payroll tax ratios. The ratios computed were applied to the annualized payroll amounts to compute an annualized FICA tax amount. The FICA tax adjustments are the differences between the annualized FICA taxes and the per book test year FICA taxes. The capitalization rate was then applied to the adjustment total to eliminate that portion of the FICA tax adjustment that pertains to non-operating expenses. In addition, the appropriate jurisdictional factors were applied to the resulting adjustment.

MEDICARE

A. Unlike the FICA tax rate, the Medicare tax rate of 1.45% does not contain a payroll dollar ceiling. Therefore, the 1.45% was directly applied to total annualized payroll. The result was compared to the Medicare tax per book amount for the 12 months ending December 31, 2005. The difference between the annualized level of Medicare tax and the per book Medicare tax represents the adjustment to Medicare taxes. The capitalization ratio is applied to the adjustment amount to exclude the payroll taxes that are capitalized. Finally, the appropriate jurisdictional amounts are applied to the result.

Q. What were the Payroll Tax adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

CS-90 PROPERTY TAXES (MPS and L&P)

Q. Please describe Adjustment No. CS-90, Property Taxes.

A. This adjustment annualizes property tax expense for the test year ending December 31, 2005.

Q. Please explain the methodology used for annualizing property tax expense.

A. A ratio was developed based on property taxes paid in 2005 as a percentage of gross plant. For purposes of developing the ratio, gross plant is defined as direct plant-in-service, common plant-in-service, fuel stock, fuel stock expense undistributed, plant materials & supplies, stores expense undistributed, and gas stores underground – current. Balances for gross plant were obtained from the 2004 FERC Form 1, as property taxes paid in 2005 were based on the assessed values of 2004 plant assets. The resulting percentage from the above ratio was applied to the test year-end annualized level of direct and allocated plant-in-service, materials & supplies, and fuel stock. The result represents the annualized level of property tax expense. The annualized level of property tax expense was then compared to the amount of property tax expense recorded on the books for the test year 2005. The appropriate jurisdictional factor was applied to the result.

Q. What was the total property tax expense adjustment for both MPS and L&P?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the adjustment totals.

<u>TAX-1 CURRENT AND DEFERRED INCOME TAX CALCULATION (MPS and L&P)</u>

Q. Please explain the current income tax expense adjustments calculated in Schedule 8 of MPS and L&P's revenue requirement models.

A. Certain adjustments are made to net income to compute the current provision for income tax expense. These adjustments begin by taking adjusted net income and applying various adjustments which are either added to or subtracted from net income to obtain net taxable income for ratemaking. The adjustments are the result of various book versus tax timing differences and their implementation under separate tax methods: flow-through versus normalization. The resulting net taxable income for ratemaking is then multiplied by the appropriate federal and state tax rates to obtain the current provision for income taxes. A federal tax rate of 35 percent and a state income tax rate of 6.25percent were used in this calculation. The difference between the calculated current income tax provision and the per book income tax provision is the current income tax provision adjustment.

Q. Please describe the adjustments to net income before taxes.

A. The following are adjustments made to net income before taxes:

- Book depreciation (including transportation depreciation) expense is added to net income. This amount is added back to net income to avoid deducting depreciation amounts twice for income tax purposes. Tax straight-line depreciation replaces book depreciation as a deduction from income for the income tax calculation.
- Schedule M timing differences, including meals and entertainment, contributions in aid of construction and advances for construction recorded for the 2004 tax year, which was filed in 2005, have been added back to income. This amount has historically been included as an add back in determining the current income tax provision. The timing differences associated with contributions in aid of construction

and advances for construction are normalized with deferred income taxes computed as discussed below.

- Interest expense is subtracted from net income before taxes. It is calculated by multiplying net rate base by the weighted average cost of debt proposed in this proceeding. This interest synchronization technique ensures the interest deduction in the income tax expense calculation equals the interest expense provided in rates.
- Tax depreciation is subtracted from net income. It is divided into two components: (1) tax straight-line depreciation and (2) tax depreciation in excess of tax straight-line depreciation. Tax straight-line depreciation represents book depreciation expense restated to reflect the tax basis of plant in service. No deferred taxes are provided for tax straight-line depreciation; thus it can be considered a flow through item. Tax depreciation in excess of tax straight-line depreciation is simply the difference between the tax straight-line depreciation calculation and the total tax depreciation deduction. The excess tax depreciation is normalized in this filing, thus the appropriate deferred income tax amounts are provided for in the income tax provision calculation.
- IRC Section 199 deduction for domestic production activities. This calculated deduction is subtracted from net income. For further discussion, please see the testimony of Company witness Jeffrey Stamm.

Q. Please explain how the tax straight-line depreciation amount was computed in this rate case filing for both MPS and L&P.

A. As stated in Appendix E of the Unanimous Stipulation and Agreement in Case Nos. ER-2004-0034 and HR-2004-0024, Aquila agreed to complete a formal tax study to develop the best methodology for computing regulated income tax expense. The study was agreed to again in the Nonunanimous Stipulation and Agreement in Case No. ER-2005-0436. In particular, the study is to develop a mutually agreeable basis for computing a tax deduction associated with depreciation expense for ratemaking purposes. As such, Aquila has agreed to the following:

> The Staff method used to calculate the tax deduction for book depreciation in the calculation of regulated income tax expense in this case will continue to be used in future rate cases until this study is completed or another method is mutually agreed upon.

At the time of this filing, the tax study was not complete. As such, the method proposed by Staff in Case No. ER-2004-0034 has been used to compute the tax straight-line depreciation amount for this rate case filing. For more discussion on the calculation of tax straight-line depreciation, please see the testimony of Company witness Jeffrey Stamm.

Q. Please describe the deferred income tax adjustment.

A. The deferred income tax adjustment is broken down into the following three components:

1. Schedule M timing differences: contributions in aid of construction and advances for construction. These add backs to income are tax affected and normalized consistent with Staff's calculation in the prior rate case filing.
2. The second component of deferred tax expense represents the tax affected timing difference between tax straight-line depreciation expense and tax depreciation expense. This is consistent with the normalization calculation in the previous rate case filing.

3. The third component includes an amortization of excess deferred income taxes resulting from the 1986 Tax Reform Act, which created excess deferred tax amounts associated with depreciation timing differences. As such, a manual amortization has been created to amortize excess deferred taxes created from the change in tax rates back to customers.

The combination of the above three components make up the amounts recorded as deferred income tax expense.

Q. What was the amount of the MPS and L&P current and deferred income tax expense adjustment for this rate case proceeding?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-4 for the MPS and L&P current and deferred income tax expense adjustment amounts.

CAPITALIZATION RATIO (MPS and L&P)

Q. What is the capitalization ratio?

A. The capitalization ratio represents the portion of cost that is not operational or maintenance in nature. Among those items not considered operational are all capital and balance sheet accounts and other income/deduction "below-the-line" accounts. Since a portion of these labor dollars are capitalized, the adjustment is decreased by a factor of one minus the capitalization rate to arrive at only the portion of benefits that should be expensed in the test year.

RB-40 ACCOUNTING AUTHORITY ORDER (AAO) (MPS Only)

Q. What is the purpose of your discussion of accounting authority orders ("AAO")?

A. The purpose is to explain the necessity of rate case recovery of costs deferred by the AAO's issued to MPS by the Commission in Case Nos. EO-90-114 and EO-91-358, in connection with MPS's Sibley Rebuild Program and the Sibley Western Coal Conversion Project.

Q. What is an AAO and what is its purpose?

A. An AAO is an order issued by the Commission that permits the requesting utility to defer certain costs on its books (outside of a rate case) with the opportunity to subsequently recover these costs through rates as opposed to being required to expense these costs in the period incurred. This treatment spreads the effect of an event over a period of time, thereby reducing the impact on customers, and can lessen the effect of regulatory lag, or the time between incurring costs and the recovery of those costs in rates.

Q. Please discuss the AAO's issued to MPS which are the subject of your testimony.

A. In Case Nos. EO-90-114 and EO-91-358, MPS requested and was granted AAO's for the previously mentioned Sibley Rebuild Program and Sibley Western Coal Conversion Project.

Q. Please discuss these projects.

A. Both projects were and are critical to MPS's ability to continue to provide reliable electric service to its customers at a reasonable cost. Briefly, the Sibley Rebuild Program extended the life of its three generating units by twenty years. Without this rebuild program, MPS would have had to find alternative sources of energy before Sibley Units 1 and 2 were retired from use in 1990 and Sibley Unit 3 by the mid-1990's. The Sibley Western Coal Conversion Project allowed MPS to achieve significant reductions in sulfur dioxide ("SO2") emissions at the Sibley Generating Station. This project allowed MPS to stay in compliance with the Clean Air Act amendments and to protect the environment.

Q. What costs are being deferred by MPS in rate base Adjustment No. RB-40?

A. MPS's AAO addition to rate base includes deferred depreciation and carrying costs (interest) associated with the plant-in-service resulting from the previously discussed Sibley projects at December 31, 2005. A jurisdictional factor was applied to each AAO to ensure only the portion affecting MPS's electric jurisdictional operations was included in rate base.

Q. What has been the treatment of the unamortized balance of the Sibley-related AAO's and amortization expense in past rate proceedings involving MPS?

A. In Case Nos. ER-90-101 and ER-93-37, MPS has been allowed the recovery of both the unamortized balance of AAO's and the related amortization expense related to the Sibley AAO's.

Q. What are the AAO components that have been included in MPS's rate base?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-2 for the AAO balances that has been included in rate base for this rate filing.

RBO-30 ACCUMULATED DEFERRED INCOME TAXES (MPS and L&P)

Q. Please describe the accumulated deferred income tax offset to rate base.

A. The accumulated deferred income tax offset to rate base includes the accumulation of tax effected timing differences between the general ledger and tax accounting records. These items are known as Schedule M's in the Company's annual tax return. The majority of timing differences included in this filing are from general ledger accounts that include timing differences associated with plant activity. They include both MPS and L&P directly assigned timing differences, as well as, corporate timing differences which are common to all Aquila jurisdictions.

Q. What time period was used for accumulated deferred income taxes?

A. Accumulated deferred income taxes are based on actual and estimated timing differences through December 31, 2005.

Q. Please explain how the accumulated deferred income tax amount was computed.

A. The accumulated deferred income tax amount includes the following components:

- Accumulated deferred income taxes include timing differences recorded in MPS and L&P FERC Accounts 190, 282 and 283. Balances in FERC Accounts 190, 282 and 283 at December 31, 2005, include timing differences based on the actual tax return filings through December 31, 2004 and estimates for the period ending December 31, 2005.
- Accumulated deferred income taxes include MPS and L&P allocable share of applicable balances recorded in corporate FERC Accounts 190, 282 and 283. As described above, corporate FERC Accounts 190, 282 and 283 at December 31, 2005, includes timing differences based on actual tax return filings through December 31, 2004 and estimates for the period ending December 31, 2005.

Q. Please describe the adjustments made to the Schedule M timing differences described above?

A. The adjustments made to the Schedule M timing differences include the following:

- For tax preparation purposes, the transaction activity creating differences between book and tax records residing on the previous UED business unit (now NETCO) were included entirely with the Schedule M timing differences recorded on the MPS (now MPMOE) business unit. As such, the UED adjustment column removes these balances from MPMOE's Schedule M timing differences and allocates only MPMOE's appropriate share of these timing differences.

- Based on the Unanimous Stipulation and Agreement in Case Nos. ER-2004-0034 and HR-2004-0024, all parties agreed to establishing a prepaid pension amount and amortizing this prepaid amount over five and one-half and nine and one-quarter year periods for MPS and L&P, respectively. In order to compute the tax versus book timing difference associated with the pension Schedule M, the prepaid pension amount granted in Case No. ER-2004-0034 was amortized through December 31, 2005. The applicable tax rate of 38.39 percent was then applied to the unamortized balance to compute the deferred taxes associated with the pension Schedule M.

Q. What is the total electric accumulated deferred income tax rate base offset for MPS & L&P?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-2 for the MPS & L&P accumulated deferred income tax rate base offset amounts.

RBO-31 ACCUMULATED DEFERRED INCOME TAXES – AAO (MPS Only)

Q. Please explain Adjustment No. RBO-31, Deferred Taxes - AAO's.

A. Adjustment No. RBO-31 calculates deferred taxes on the unamortized deferred AAO balances at December 31, 2005, for the 1990 and 1992 Sibley Rebuild and Western Coal Conversion Projects. Please see the testimony above on Adjustment No. RB-40 for a description of the 1990 and 1992 Sibley Rebuild and Western Coal Conversion Projects.

Q. Please explain the calculation of deferred taxes on the 1990 and 1992 AAO's.

A. Total unamortized deferred AAO balances were obtained. The depreciation component of the deferred AAO balances was subtracted out of the unamortized deferred balances as no deferred taxes are provided for these amounts. The income tax rate of 38.39% was applied to the resulting amount to obtain the associated accumulated deferred taxes which are used to offset the AAO rate base component. The appropriate jurisdictional factors were then applied.

Q. What is the total AAO accumulated deferred income tax rate base offset for MPS?

A. Please refer to the testimony of Company witness Susan Braun, Schedule SKB-2 for the MPS AAO accumulated deferred income tax rate base offset amount.

RBO-100 REGULATORY ASSET / LIABILITY ERISA TRACKER (MPS and L&P)

Q. Please explain what the Stipulation and Agreement in Rate Case Nos. ER-2004-0034 and ER-2005-0436 states concerning the Regulatory Asset/Liability ERISA Tracker.

A. As stated in the Stipulation and Agreement in Case Nos. ER-2004-0034 and ER-2005-0436 (page 6-7),

> Company is authorized to reflect pension cost equal to this provision and record the difference between the ERISA minimum and the annual provision for pension cost as a regulatory asset or liability. This regulatory asset and/or liability is intended to track the difference between the provision for the ERISA minimum contribution included in cost of service in this case, and the Company's actual ERISA minimum contributions made after the effective date of rates established in this case. This regulatory asset and/or liability will be included in rate base in the Company's next rate case and amortized over a five year period.

As such, the Company has collected in rates certain amounts for pension expenditures. These collections are compared to actual contributions. The difference between these amounts are treated as regulatory assets or liabilities.

Q. Did the Company comply with the Stipulation and Agreement in this rate case filing?

A. Yes. The Company has been recording the pension cost collections as a regulatory liability. As discussed earlier, in September 2005, a contribution was made to the pension plan which off-set this liability amount for both MPS and L&P.

Q. At December 31, 2005, was the tracking mechanism described above a regulatory asset or liability?

A. For MPS, a regulatory liability existed and is reflected in rate base offset adjustment RBO-100. For L&P, a regulatory asset existed and is reflected as a rate base add in RBO-100.

Q. What were the Regulatory Asset / Liability ERISA Tracker rate base components for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-2 for the rate base totals.

WC–20 PREPAYMENTS (MPS and L&P)

Q. What was the method used to calculate Prepayments – Other Than Pensions, Adjustment No. WC-20?

A. Prepayments have been included in rate base using a thirteen-month average. Prepayments are a normal working capital rate base allowance as they represent an investment of funds, (i.e., cash outlay), made in advance of the future service period to which they apply. For example, prepaid items such as prepaid insurance and prepaid software licenses have been included in this calculation. The month-end balances were averaged for the months of December 2004 through December 2005. For both MPS and L&P, the calculation includes

MPS and L&P direct prepayments as well as the MPS and L&P allocated share of common enterprise support function prepayments.

Q. Please explain why a thirteen-month average calculation was used.

A. The computation of a thirteen-month average serves as a better measure of investment rather than the use of any one single month. Due to monthly fluctuations in the prepaid balance, no single month is representative.

Q. What were the prepayment adjustments for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-2 for the adjustment totals.

WC-21 PREPAYMENTS – PENSION (MPS and L&P)

Q. What does Case No. ER-2005-0436 provide in regards to prepaid pension amounts.

A. The Stipulation and Agreement in Case No. ER-2005-0436 provides the following at pages 6-7:

> MPS rates include a $2,110,436 annual provision, prior to capitalization, for an MPS electric jurisdictional prepaid pension amortization. This amortization will be in effect for a five and one-half (5 ½) year period beginning with the effective date of rates established in Case No. ER-2004-0034. L&P rates include a $3,352,742 annual provision, prior to capitalization, for L&P electric prepaid pension amortization. This amortization will be in effect for a nine and one-quarter (9.25) year period beginning with the effective date of rates established in Case No. ER-2004-0034.

Q. Has the Company included a prepaid pension amount in rate base consistent with the amount in the Stipulation and Agreement in Case No. ER-2005-0436?

A. Yes. The Company has included rate base adds for the unamortized portion of prepaid pension amounts at the end of the test year December 31, 2005.

Q. What were the prepaid pension components of rate base for MPS and L&P?

A. Please see the testimony of Company witness Susan Braun, Schedule SKB-2 for the rate base totals.

WC-50 CASH WORKING CAPITAL CALCULATION (MPS and L&P)

Q. What is cash working capital?

A. Cash working capital ("CWC") is the amount of cash necessary for MPS and L&P to pay the day-to-day expenses incurred to provide electric service to their customers.

Q. Is the method used in the current rate case to calculate MPS and L&P's CWC requirements the same method that has been used in previous cases?

A. Yes. The method has been proposed by the Commission Staff in numerous rate proceedings including Case Nos. ER-99-0247, ER-2001-0672, ER-2004-0034 and ER-2005-0436.

Q. Please explain this method.

A. A lead/lag study determines the amount of cash that is necessary on a day-to-day basis to provide energy services to customers. A lead/lag study analyzes the cash flows related to the payments received from its customers for the provision of electric service and the disbursements made by MPS and L&P to its suppliers and vendors of goods and services necessary to provide the energy services. A lead/lag study determines the number of days MPS and L&P has to make payments after receiving goods or services from a vendor and is compared with the number of days it takes to receive payment for the energy services provided to its customers.

Q. What are the sources of CWC?

A. Ultimately, shareholders and ratepayers provide all sources of cash working capital.

Q. How do shareholders supply CWC?

A. When MPS and L&P expend funds to pay for an expense before the ratepayers provide the cash through rates, the shareholders are the source of the funds. This cash represents a portion of the shareholders' total investment in MPS and L&P. The shareholders are compensated for the CWC funds they provided by the inclusion of these funds in rate base. By including these funds in rate base, the shareholders earn a return on the funds they have invested.

Q. How do ratepayers provide CWC?

A. Ratepayers supply CWC when they pay for energy services received before MPS and L&P pay expenses incurred to provide that service. Ratepayers are compensated for the CWC that they provide by reducing rate base by the amount of CWC the ratepayers provide.

Q. How is the amount of CWC provided by both the ratepayers and shareholders generally determined?

A. A lead/lag study is performed.

Q. How are lead/lag study results interpreted?

A. A positive CWC requirement indicates that, in the aggregate, the shareholders provided the CWC for the test year. This means that, on average, the Company paid the expenses incurred to provide the energy service to the ratepayers before the ratepayers paid the Company for the provision of utility service. A negative requirement indicates that, in aggregate, the ratepayers provided the CWC during the test year. This means that, on average, the ratepayers paid for their electric service before the utility paid the expense incurred to provide those services.

Q. Was there a lead/lag study prepared for MPS and L&P for this rate case proceeding?

A. No. Prior to filing the last Missouri rate case, Case No. ER-2005-0436, a thorough lead / lag study was completed using 2004 data. For the most part, the computed lead / lag days from the 2004 study were used for this rate filing with the exception of the following items which have been updated with 2005 data: revenue lag, purchased power, sibley coal and freight, lake road coal and freight, ad valorem taxes and city franchise taxes.

Q. What was the result of the lead / lag study?

A. The results of the lead / lag demonstrates that, in the aggregate, ratepayers have supplied funds to the utility to pay for expenses prior to the utility paying for the same expenses. As such, a rate base offset amount will be included in this rate case filing.

Q. Where can the calculation of the CWC calculation be found?

A. Please see Schedules RAK - 2 & RAK – 3 attached to my testimony which details the calculation of the CWC rate base offset for MPS and L&P, respectively. Included within the calculation are the computed lead / lag days which were updated for the 2005 test year.

Q. Please explain the components of the calculation of CWC that appears on Schedules RAK- 2 & RAK - 3.

A. The components of the calculation are as follows:

1) Column A (Account Description) lists the types of significant cash expenditures that MPS and L&P pay on a day-to-day basis.
2) Column B (Test Year Expense) provides the amount of annualized expense included in the cost of service. It shows the dollars associated with the items listed in column A on an adjusted Missouri jurisdictional basis.
3) Column C (Revenue Lag) indicates the number of days between the midpoint of the provision of service by MPS and L&P and the payment for the service by the ratepayer.

4) Column D (Expense Lead) indicates the number of days between the receipt of and the payment for the goods and services (i.e. cash expenditures) used to provide service to the ratepayers.

5) Column E (Net Lag) results from the subtraction of the Expense Lead (column D) from the Revenue Lag (column C).

6) Column F (Factor) expresses the CWC lag in days as a fraction of the total days in the test year. This is accomplished by dividing the Net Lags in column E by 365 days.

7) Column G (CWC Requirement) reflects the average amount of cash necessary to provide service to the ratepayer. This is computed by multiplying the Test Year Expenses (column B) by the CWC Factor (column F).

Q. Does this conclude your direct testimony?

A. Yes.

Change in Expense Allocations from Test Year to 2006

Line No.	State/Utility	Test Year Allocations	Allocations Eff. 1/1/06
1	Michigan Gas	7.83%	0%
2	Minnesota/South Dakota Gas	14.30%	0%
3	Nebraska Gas	11.36%	16.94%
4	Iowa Gas	9.15%	13.65%
5	Missouri Gas	2.75%	0%
6	Kansas/TX/OK Gas	7.23%	10.78%
7	Colorado Gas	3.72%	5.54%
8	MPS Electric	20.43%	30.46%
9	L&P Electric	6.87%	10.25%
10	Kansas Electric	7.44%	0%
11	Colorado Electric	6.20%	9.24%
12	All Other Non-Utility	2.72%	3.14%

Aquila Networks - MPS
Cash Working Capital - Schedule 6
TYE 12/31/05; Update (K&M) 6/30/06; True-up (TBD)

Line #	Account Description (A)	W/P Ref	(Elec-Juris) Test Year Expenses (B)	Revenue Lag (C)	Expense Lead (D)	Net (Lead)/Lag (C) - (D) (E)	Factor (Col E/365) (F)	CWC Req (B) X (F) (G)
	Operations & Maintenance Expense							
1	Cash Vouchers	diff	77,623,714	39.1335	45.6250	(6.4915)	(0.01778)	(1,380,532)
2	Federal Income Tax Withheld		3,492,455	39.1335	12.4259	26.7076	0.07317	255,548
3	State Income Tax Withheld		1,039,425	39.1335	12.4259	26.7076	0.07317	76,056
4	FICA Taxes Withheld - Employee	CS-85	1,975,867	39.1335	12.4259	26.7076	0.07317	144,577
5	Net Payroll	CS-5	25,846,504	39.1335	13.9259	25.2076	0.06906	1,785,009
6	Accrued Vacation		684,670	39.1335	365.0000	(325.8665)	(0.89278)	(611,263)
7	Purchased Gas & Oil	FPP-10	9,101,107	39.1335	39.5900	(0.4565)	(0.00125)	(11,383)
8	Injuries & Damages	CS-30	974,228	39.1335	113.8092	(74.6757)	(0.20459)	(199,318)
9	Purchased Power	Sch 7, AC 555	166,761,941	39.1335	35.8146	3.3189	0.00909	1,516,346
10	Sibley - Coal & Freight	FPP-10	45,969,904	39.1335	19.5916	19.5419	0.05354	2,461,203
11	Jeffrey - Coal	FPP-10	15,426,096	39.1335	29.8000	9.3335	0.02557	394,464
12	Jeffrey - Operations	CS-82	4,579,581	39.1335	29.8000	9.3335	0.02557	117,106
	Total Operation & Maintenance Expense		353,475,492					4,547,814
13	Interest Expense	Sch 8	30,012,248	39.1335	92.0000	(52.8665)	(0.14484)	(4,346,966)
	Taxes other than Income Taxes							
14	Ad Valorem/Property Taxes	Sch 7, AC 408.1	9,651,289	39.1335	188.9490	(149.8155)	(0.41045)	(3,961,405)
15	FICA Taxes - Employer's	CS-85	1,975,867	39.1335	12.4259	26.7076	0.07317	144,577
16	Unemployment Taxes (FUTA & SUTA)	CS-85	154,092	39.1335	76.3750	(37.2415)	(0.10203)	(15,722)
17	Corporate Franchise Taxes		276,305	39.1335	(76.0000)	115.1335	0.31543	87,156
18	City Franchise Taxes		20,747,597	39.1335	98.1913	(59.0578)	(0.16180)	(3,357,007)
19	Sales Taxes	ST-1	10,599,991	39.1335	35.2000	3.9335	0.01078	114,233
	Total Taxes other than Income Taxes		43,405,141					(6,988,167)
20	Current Income Taxes-Federal	Sch 8	(6,455,232)	39.1335	38.5000	0.6335	0.00174	(11,204)
21	Current Income Taxes-State	Sch 8	(1,152,720)	39.1335	38.5000	0.6335	0.00174	(2,001)
	Total Cash Working Capital Requirement		419,284,929					(6,800,524)

Aquila Networks - L&P (Electric)
Cash Working Capital - Schedule 6
TYE 12/31/05; Update (K&M) 6/30/06; True-up (TBD)

Line #	Account Description (A)	W/P Ref	(Elec-Juris) Test Year Expenses (B)	Revenue Lag (C)	Expense Lead (D)	Net (Lead)/Lag (C) - (D) (E)	Factor (Col E/365) (F)	CWC Req (B) X (F) (G)
	Operations & Maintenance Expense							
1	Cash Vouchers	diff	24,286,676	39.1335	45.6250	(6.4915)	(0.01778)	(431,937)
2	Federal Income Tax Withheld		1,239,127	39.1335	12.4259	26.7076	0.07317	90,669
3	State Income Tax Withheld		361,810	39.1335	12.4259	26.7076	0.07317	26,474
4	FICA Taxes Withheld - Employee	CS-85	703,376	39.1335	12.4259	26.7076	0.07317	51,467
5	Net Payroll	CS-5	9,999,724	39.1335	13.9259	25.2076	0.06906	690,600
6	Accrued Vacation		220,312	39.1335	365.0000	(325.8665)	(0.89278)	(196,691)
7	Purchased Gas and Oil	FPP-10	659,730	39.1335	39.5900	(0.4565)	(0.00125)	(825)
8	Injuries and Damages	CS-30	228,075	39.1335	237.7933	(198.6598)	(0.54427)	(124,135)
9	Purchased Power	Sch 7, AC 555	33,342,704	39.1335	35.8146	3.3189	0.00909	303,181
10	Lake Road - Coal & Freight	FPP-10	11,127,592	39.1335	19.5916	19.5419	0.05354	595,765
11	Iatan - Coal	FPP-10	5,996,768	39.1335	31.6000	7.5335	0.02064	123,772
12	Iatan - Operations	CS-82	6,266,824	39.1335	33.0000	6.1335	0.01680	105,308
	Total Operation & Maintenance Expense		94,432,718					1,233,648
13	**Interest Expense**	Sch 8	7,699,222	39.1335	92.0000	(52.8665)	(0.14484)	(1,115,153)
	Taxes other than Income Taxes							
14	Ad Valorem/Property Taxes	Sch 7, AC 408.1	3,228,771	39.1335	182.0281	(142.8946)	(0.39149)	(1,264,038)
15	FICA Taxes - Employer's	CS-85	703,376	39.1335	12.4259	26.7076	0.07317	51,467
16	Unemployment Taxes (FUTA & SUTA)	CS-85	66,806	39.1335	76.3750	(37.2415)	(0.10203)	(6,816)
17	Corporate Franchise Taxes		122,504	39.1335	(76.0000)	115.1335	0.31543	38,642
18	City Franchise Taxes		3,233,542	39.1335	40.2083	(1.0748)	(0.00294)	(9,522)
19	Sales Taxes	ST-1	2,274,412	39.1335	35.2000	3.9335	0.01078	24,511
	Total Taxes other than Income Taxes		9,629,411					(1,165,756)
20	Current Income Taxes-Federal	Sch 8	(2,014,719)	39.1335	38.5000	0.6335	0.00174	(3,497)
21	Current Income Taxes-State	Sch 8	(359,771)	39.1335	38.5000	0.6335	0.00174	(624)
	Total Cash Working Capital Requirement		109,386,861					(1,051,383)

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Aquila, Inc. d/b/a Aquila Networks-MPS and Aquila Networks-L&P, for authority to file tariffs increasing electric rates for the service provided to customers in the Aquila Networks-MPS and Aquila Networks-L&P area	))))))	Case No. ER-_________

County of Jackson)
) ss
State of Missouri)

AFFIDAVIT OF RONALD A. KLOTE

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

Ronald A Klote

Ronald A. Klote

Subscribed and sworn to before me this 3rd day of July, 2006.

Terry D Lutes

Notary Public
Terry D. Lutes

My Commission expires:

8-20-2008

Notary Public
Notary Seal
State of Missouri

TERRY D. LUTES
Jackson County
My Commission Expires
August 20, 2008