Exhibit No.:
Issues: True-up Audit, Company Operations, Accounting Schedules, Rate Base, Depreciation, Amortization, Property Taxes, Income Taxes
Witness: *DOYLE L. GIBBS*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Direct Testimony*
Case Nos.: *WR-2000-281 and SR-2000-282*

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

DOYLE L. GIBBS

MISSOURI-AMERICAN WATER COMPANY

CASE NOS. WR-2000-281 and SR-2000-282

Jefferson City, Missouri
March, 2000

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DIRECT TESTIMONY

OF

DOYLE L. GIBBS

MISSOURI-AMERICAN WATER COMPANY

CASE NOS. WR-2000-281 & SR-2000-282

Q. Please state your name and business address.

A. Doyle L. Gibbs, 815 Charter Commons Drive, Suite 100B, Chesterfield, Missouri 63017.

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

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

Q. Please describe your educational background.

A. I attended the University of Missouri – St. Louis, where I received a Bachelor of Science degree in Business Administration with a major in Accounting in 1976. I passed the Uniform Certified Public Accountant examination in 1988. I have been licensed as a Certified Public Accountant in the state of Missouri since February 1989.

Q. What has been the nature of your duties while in the employ of this Commission?

A. I have conducted and assisted with the audits and examinations of the books and records of utility companies operating within the state of Missouri.

Q. Have you previously testified before the Commission?

A. Yes, I have. Please refer to Schedule 1, attached to this direct testimony, for a list of cases in which I have previously filed testimony.

Q. With reference to Case Nos. WR-2000-281 and SR-2000-282, have you made an investigation of the books and records of Missouri-American Water Company (MAWC or Company)?

A. Yes, with the assistance of other members of the Commission Staff (Staff).

Q. What test year has the Staff utilized in this case?

A. The Staff has used a test year ending September 31, 1999, updated through December 31, 1999.

TRUE-UP AUDIT

Q. Is the Staff proposing a true-up audit in this case?

A. Yes. The Staff is proposing a true-up audit through April 30, 2000. The true-up audit should include all significant items related to revenue, expense, capital structure and rate base that have occurred on or prior to this date. This approach will maintain the appropriate relationship between revenues, expenses and rate base. The following items should be included in the true-up audit:

Rate Base: Plant-in-service, depreciation and amortization reserves, contributions in aid of construction (CIAC), customer advances for construction (advances), deferred OPEB assets, pension liability and deferred income taxes. Cash working capital and the income tax and interest offsets will also change to the extent these amounts are affected by other true-up items.

Income Statement: Depreciation expense as affected by plant additions, retirements, CIAC and advances, property taxes if new rates and valuations become known, revenues, postage, electricity and chemicals as affected by cost and/or customer changes, payroll and related costs as a result of changes in employee levels and wage rates and income taxes, as affected by other true-up items.

Capital Structure and Associated Embedded Costs: Changes in the Company's capital structure and associated embedded costs of the related capital items excluding return on common equity will also be reflected in the Staff's true-up audit. To be included in the true-up audit, all items must be evidenced by documentation (i.e., inspection, monthly operating reports, invoices, Company ledgers, etc.).

Q. What major events will occur after December 31, 1999 that will have a significant affect on revenue requirement?

A. The most significant event is the new investment in plant facilities scheduled to be in-service by April 30, 2000. The scheduled additions will approximately double the Company's current rate base.

Q. How will the Staff verify the items to be included in the true-up?

A. The Staff will review the potential items as documentation becomes available after April 30, 2000. The Staff's decision to perform a true-up in this case should not be viewed as a blanket acceptance of true-up audits in general for this Company or other utilities in future cases. The Staff's true-up recommendation is prompted by the Company's engagement in a significant construction program, a large portion of which the Company anticipates will be placed into service by April 30, 2000.

Q. Has the Staff included an estimate of the revenue requirement associated with the true-up?

A. Yes. An estimate of approximately $4.5 million has been reflected on Line 12 of Accounting Schedule 1 for Total Water Company. This amount represents the sum of the true-up audit estimated for each of the operating districts, as reflected on the respective districts' Revenue Requirement schedules. Because the Staff anticipates that the true-up audit will have an insignificant impact on the Brunswick and Joplin districts, no estimate for the true-up audit has been included on Accounting Schedule 1 for those districts. The true-up audit estimate included for the St. Joseph District reflects the Staff's phase-in proposal for the new treatment plant, addressed in the testimony of Staff Accounting witness Stephen M. Rackers.

Subsequent to the true-up audit, Staff will file True-up Accounting Schedules and testimony to present the results of its examination.

Q. When does the Staff propose to file the True-up Accounting Schedules and testimony?

A. The Staff estimates that the True-up Accounting Schedules and testimony could be filed on June 8, 2000. The Staff intends to file a True-up Audit procedural schedule with the Commission within one week of this filing.

COMPANY OPERATIONS

Q. Please describe the operations of MAWC in Missouri.

A. MAWC is comprised of seven water operating districts and one sewer operating district. The seven water operating districts are referred to by location and include the Brunswick, Mexico, Parkville (Platte County), Warrensburg, St. Charles, Joplin, and St. Joseph districts. The sewer district is referred to as the Parkville (Platte County) Sewer District.

The operating water districts in Brunswick, Mexico, Parkville, Warrensburg, and St. Charles, as well as the Parkville Sewer District, formerly known collectively as Missouri Cities Water Company (Cities), were purchased in 1993 from Cities's parent, Avatar Properties, Inc. (Avatar). The former Cities operations were merged into MAWC operations effective December 31, 1994. In addition to the operating districts, the Company has a non-operating Corporate District. Costs recorded by the Company on the books of the Corporate District are generally costs that are for the benefit of the system as a whole which can not be directly assigned to a specific operating district. The majority of customer accounting and administrative functions for all the operating districts takes place at the Corporate District, which is physically located within the St. Joseph District.

Q. What is the purpose of your direct testimony?

A. The purpose of my direct testimony is to present the Staff's position with respect to Rate Base, the allocation of Corporate District investment and expense to the operating districts, and income taxes.

ACCOUNTING SCHEDULES

Q. Please provide a general description of the Accounting Schedules.

A. This filing consists of ten sets of Accounting Schedules; one for each of the seven operating water districts, one for the operating sewer district, one for the Corporate District and a set of schedules that represents the combined water operations (Total Water). Each set of Accounting Schedules for the operating districts (water, sewer or total water) are identical in format and content, that is, a particular line item description or adjustment number in one set of Accounting Schedules will be the same in the Accounting Schedules for the other operating districts. The Accounting Schedules for the Corporate District are not for the purpose of calculating a revenue requirement for the Corporate District, but for information purposes. As such, the Corporate District schedules do not contain Accounting Schedules 1, 7, 8 or 11, which are Revenue Requirement, Depreciation, Cash Working Capital and Tax Calculation, respectively. However, the Corporate District Accounting Schedules do contain supplemental schedules that delineate the allocation of the Corporate costs to the operating districts.

Q. Please describe how the Corporate District costs were allocated to the operating districts.

A. Schedule 2, attached to my testimony, is the Corporate Allocation Factors used by the Staff to distribute the Corporate District costs to the operating districts.

Q. Please describe the allocation factors contained in Schedule 2 attached to your testimony and explain how those factors were used.

A. The basis of each factor on Schedule 2 is self-evident by the description that follows the Corporate Allocation Factor number. For example, Corporate Allocation Factor 1 is the ratio of the number of customers in one district, as of the end of the updated test year to the total number of customers in all districts. The various Corporate District cost items to which these factors were applied, are listed immediately following the calculation of the factors on Schedule 2.

Q. With respect to this case, what components of the Staff's filing are you sponsoring?

A. I am sponsoring all the Accounting Schedules, which consist of the following for each of the operating districts, including Total Water:

Accounting Schedule 1 - Revenue Requirement

Accounting Schedule 2 – Rate Base

Accounting Schedule 3 – Plant In Service

Accounting Schedule 4 – Adjustments To Plant In Service

Accounting Schedule 5 – Depreciation Reserve

Accounting Schedule 6 – Adjustments To Depreciation Reserve

Accounting Schedule 7 – Depreciation Expense

Accounting Schedule 8 – Cash Working Capital

Accounting Schedule 9 - Income Statement

Accounting Schedule 10 - Adjustments to Income Statement

Accounting Schedule 11 – Tax Calculation

The Accounting Schedules for the Corporate District, as previously stated, exclude Accounting Schedule 1, 7, 8 and 11. However, Corporate District Accounting Schedules 2, 3, 5, 9 and 10, Rate Base, Plant In Service, Depreciation Reserve, Income Statement and Adjustments To Income Statement respectively, are accompanied by supplemental accounting schedules that provide the detail of the allocation of the Corporate amounts to the operating districts.

Specifically within the Accounting Schedules, I am sponsoring all the components of rate base, with the exception of Deferred OPEB Asset and Pension Liability, and I am sponsoring the adjustments to expense for depreciation, amortization, property tax and income tax expense included in Accounting Schedule 10, Adjustments To Income Statement.

Q. Please describe Accounting Schedule 1 for the operating districts.

A. Accounting Schedule 1, Revenue Requirement, for each of the operating districts is the Staff's calculation of the Revenue Requirement based on the rates of return sponsored by Staff witness Roberta McKiddy of the Financial Analysis Department. As previously stated, Staff's revenue requirement recommendation includes an allowance to reflect the impact of a proposed true-up audit.

Q. Please explain Accounting Schedule 2, Rate Base.

A. This schedule, for each of the operating districts, summarizes the Company's investment, net of ratepayer-supplied funds, that is used in Accounting Schedule 1 to calculate revenue requirement. For each item listed on Accounting Schedule 2, Rate Base, that is not supported by an accompanying accounting schedule, with the exception of deferred taxes, there is an amount designated "Direct Assigned" and an amount labeled "Corporate Distribution." The Direct Assigned amount reflects the cost recorded by the Company on the books of the operating district. The Corporate Distribution is the allocated portion recorded on the books of the Corporate District. The distribution of the Corporate District rate base to the operating districts is presented on Supplement To Accounting Schedule 2, which is contained in the Corporate District Accounting Schedules.

Q. Please explain Accounting Schedule 3.

A. Accounting Schedule 3, Plant-in-Service, for the operating districts lists, in column "C," MAWC's district-specific plant balances as recorded by the Company for the accounts listed in column "A" and described in column "B" as of December 31, 1999. Displayed in Column "D" are the adjusted Corporate plant balances that have been allocated to the districts. Columns "E", "H" and "G" provide the adjustment amounts, if any, the adjustment numbers, and the adjusted plant balances, respectively.

Accounting Schedule 3 for the Corporate District presents the balances, as recorded and adjusted, for the non-district specific plant in service. The adjusted amounts in column "F" have been distributed to the operating districts and reflected in column "D" of the respective district plant schedules. Supplement To Accounting Schedule 3 of the Corporate District Accounting Schedules, provides the distribution of the Corporate plant balances to the operating districts.

Q. Please explain Accounting Schedule 4.

A. Accounting Schedule 4, Adjustments to Plant-in-Service, details the individual adjustments Staff made to plant-in-service, as listed in column "E" on Accounting Schedule 3. The only adjustment Staff made to Plant-in-Service was to eliminate the balance of Account 303.99, Miscellaneous Intangible Plant recorded on the books of the Corporate District. As previously stated, the adjusted Corporate plant balances were allocated to the districts.

Q. Why did the Staff eliminate this balance from plant in service?

A. This balance represents the cost of a comprehensive planning study performed by the Company. This study is not specifically associated with individual plant items and there is no guarantee that the projects discussed in the study will be completed. Therefore, the Staff does not believe that the cost should be included in plant. However, Staff is proposing the Company recover the cost of the study by inclusion of an amortization over five years. This amortization has been included in the cost of service as a result of adjustment S-15.2 on Accounting Schedule 10, Adjustments To Income Statement.

Q. Please explain Accounting Schedules 5 and 6.

A. Accounting Schedules 5 and 6 are Depreciation Reserve and Adjustments to Depreciation Reserve, respectively. Accounting Schedule 5 presents, in total, the recorded district depreciation reserve balance at December 31, 1999 and the allocated portion of the Corporate District's depreciation reserve. The distribution of the Corporate depreciation balance is reflected on Supplement To Accounting Schedule 5 contained in the Corporate District Accounting Schedules.

As seen on Accounting Schedule 6, Adjustments To Depreciation Reserve, Staff is not currently proposing any adjustments to the reserve.

Q. Please explain Accounting Schedule 7.

A. Accounting Schedule 7, Depreciation Expense, calculates the district depreciation expense by applying the current Commission approved depreciation rates to the adjusted and allocated plant balances found on Accounting Schedule 3. The result of this calculation is compared to the test year recorded depreciation expense to determine adjustment S-14.1 on Accounting Schedule 10, Adjustments To Income Statement.

Q. Please explain Accounting Schedule 8.

A. Accounting Schedule 8 represents the calculation of the Cash Working Capital (CWC) requirement of the Company through use of a lead/lag study.

Q. What is CWC?

A. CWC represents the average amount of cash a utility must have on hand to pay the day-to-day expenses incurred to provide service to the ratepayer.

Q. Is the method which you used to calculate the CWC requirement for the Company consistent with that used in previous rate cases?

A. Yes, this method has been used by the Staff and adopted by the Commission in numerous rate cases.

Q. Please explain the components of the Staff's calculation of CWC that appear on Accounting Schedule 8, Cash Working Capital.

A. Column "A" on Accounting Schedule 8 lists various groups of expenses that the Company pays on a day-to-day basis. Column "B," Test Year Expenses, shows the Staff's annualized amounts associated with the items described in Column "A". Column "C", Revenue Lag, describes the amount of time, expressed in days, between the midpoint of the provision of service by the Company and the payment for the service by the ratepayer. Column "D", Expense Lag, describes the amount of time, expressed in days, between the receipt of and payment for goods and services (i.e., cash expenditures) used to provide service to the ratepayer. Column "E", Net Lag, is the result of the subtraction of the Expense Lag from the Revenue Lag. Column "F", Factor, expresses the CWC lag in days as a fraction of the total days in the year. This is accomplished by dividing the net lags in Column "E" by 365. Finally, Column "G", CWC Requirement, is the amount of daily cash necessary to provide service to the ratepayer. This amount is computed by multiplying the test year expenses (Column "B") by the CWC Factor (Column "F").

Q. How does a lead/lag study calculate CWC?

A. In a lead/lag study, an analysis is performed of the cash flows related to the payments received by the Company from its customers for the provision of service and disbursements made by the Company to vendors to provide that service. A lead/lag analysis compares the number of days between the payment of goods for services received from a vendor with the number of days it takes the Company to receive payment for the service the Company provided to its customers. The lead/lag study also determines whether the shareholder or the ratepayer ultimately provides CWC.

Q. How does the shareholder supply CWC?

A. When the Company spends cash to pay for an expense incurred in providing service before the ratepayer provides cash to pay for the service, then that cash must be provided by the shareholder. This cash represents a portion of the shareholder's total investment in the Company. The shareholder receives compensation for the CWC funds provided in this way by the inclusion of these funds in rate base through a return on the shareholder's investment.

Q. How does the ratepayer provide CWC?

A. The ratepayer supplies CWC when customer payments for service are received before the Company must pay for expenses incurred to provide that service. The ratepayer is compensated for the CWC provided through a corresponding reduction to rate base.

Q. How are the results from a lead/lag study interpreted?

A. A positive CWC requirement indicates that the shareholder provided the CWC in the aggregate during the year. This means that the Company must pay, on average, for the expenses incurred in providing service before cash is provided by the ratepayer.

A negative CWC requirement indicates that the ratepayer provided CWC in the aggregate during the test year. This means that the ratepayer has provided the necessary cash, on average, before the Company must pay for expenses incurred to provide that service.

Q. Has the Staff performed a lead/lag study in this case?

A. No. The Staff has adopted the lead/lag study it performed in Case No. WR-95-205, as modified in the Company's last case, WR-97-237 with one exception. The revenue lag for the Joplin district has been reduced to reflect the conversion from quarterly billing to monthly billing approved in the company's last rate case, WR-97-237. Other than the change required for the Joplin revenue lag, the Company has indicated, in response to a Staff data request, that no other changes have occurred that would have a material effect on the lags used in last rate case.

Q. Please explain the federal income tax offset, state income tax offset and interest expense offset to rate base.

A. The normalized Missouri jurisdictional expense for these components is directly tied to the computation of the revenue requirement. The computer program used by the Staff retrieves the associated expense amounts from the Income Tax schedule, Accounting Schedule 11, applies the calculated CWC factor to each component, and places the CWC requirement directly in the Rate Base schedule.

Q. Please explain Accounting Schedule 9.

A. Accounting Schedule 9 is the Income Statement for the test year ending September 30, 1999, updated through December 31, 1999. Each adjustment included on the income statement is a summary of the adjustments itemized on Accounting Schedule 10, Adjustments to Income Statement. Column "C" on the district income statements reflects the allocation of the test year recorded Corporate revenue and expense. The detail of the allocation for the Corporate test year revenue and expense can be found on Supplement To Accounting Schedule 9 in the Corporate Accounting Schedules.

Q. Please explain Accounting Schedule 10, Adjustments To Income Statement.

A. Accounting Schedule 10 itemizes the adjustments to the income statement made by the Staff. The adjustment detail on Accounting Schedule 10 is shown in two columns and has been designated "Direct" or "Corp." The Staff, when making its adjustments, has attempted to maintain the distinction of how the books and records are kept by the Company. If a revenue or expense adjustment can be directly assigned to an operating district, that adjustment would appear under the "direct" column. Adjustments that cannot be directly assigned are made in total to the Corporate District and allocated to the operating districts. The amount that appears under the "Corp." column in the district schedules is the allocated portion of the total Corporate District adjustment. Supplement To Accounting Schedule 10 in the Corporate Accounting schedules provides the detail of how the Corporate adjustment was distributed to the operating districts.

Q. Please explain Accounting Schedule 11.

A. Accounting Schedule 11, Income Tax, reflects the Staff's calculation of current income taxes expense for the adjusted test year and for the recommended revenue requirements based on the recommended rates of return sponsored by Staff witness McKiddy. I will discuss the various details concerning the income tax calculation later in this testimony.

RATE BASE

Q. Please identify the specific components of rate base you are sponsoring.

A. I am sponsoring:

Plant in service

Accumulated depreciation reserve

Accumulated amortization

Case working capital including interest and tax offsets

Material and supplies

Prepayments

Contributions in aid of construction (CIAC)

Customer advances

Deferred income taxes

Pre-71 ITC

Plant in service, accumulated depreciation reserve and cash working capital have been previously discussed in my testimony.

Q. Please describe the rate base inclusion for accumulated amortization reserve for intangible plant.

A. The accumulated amortization reserve included in rate base is directly assigned to the Joplin district and is the actual recorded balance as of December 31, 1999.

Q. Please discuss materials and supplies and prepayments that are included in rate base.

A. Both materials and supplies and prepayments reflect a 13-month average for the historical test year ending September 30, 1999. The materials and supplies balances that make up the 13-month average are district specific and are therefore, directly assigned to the operating districts. Prepayments are recorded only on the books of the Corporate district necessitating the allocation of the Corporate 13-month average to the operating districts. The distribution of the Corporate rate base components, including prepayments, is shown on Supplement To Accounting Schedule 2 from the Corporate Accounting Schedules.

Q. Please discuss the reductions to rate base you are sponsoring.

A. In addition to the interest and income tax offsets previously discussed with regards to CWC, I have reduced rate base for contributions in aid of construction (CIAC), customer advances, deferred income taxes related to normalized depreciation and pre-71 ITC. Each of these items reflect the actual balance recorded on the books of the Company, whether district specific or the allocated portion of Corporate, as of December 31, 1999 except for the deferred income tax item labeled Pre-merger Missouri-Cities. This item reflects the deferred tax liability that was recorded on the books of Cities at the time it was purchased by MAWC. In the negotiated purchase, MAWC did not acquire the liability for those deferred taxes and so they were "written off" against the premium paid for the acquisition of the properties.

Q. If the Company did not acquire the deferred tax liability when Cities was purchased, was it appropriate to write-off the tax liability when recording the purchase?

A. It was appropriate from a financial reporting perspective. However, from a ratemaking perspective, those deferred taxes represented actual cash contributed by the ratepayer. Ignoring the deferred income taxes the ratepayer paid to Cities denies them the rate base reduction they deserve that is associated with the funds they provided.

Q. What adjustments to the income statement are you sponsoring?

A. The adjustments I am sponsoring are identified on Adjustments To Income Statement, Accounting Schedule 10, as follows:

Depreciation expense	S-14.1, S-14.2 and S-14.3
Amortization expense	S-15.1, S-15.2, S-15.4 and S-15.5
Property Taxes	S-16.4
Current Income Tax Expense	S-17.1
Deferred Income Tax Expense	S-18.1
ITC Amortization	S-19.1

DEPRECIATION

Q. Please identify and discuss your adjustments to depreciation expense.

A. Adjustment S-14.1, as previously discussed, adjusts depreciation expense to reflect the annualized level of depreciation based on the level of plant in service and the current approved depreciation rates in effect.

Adjustment S-14.2 reduces the depreciation expense calculated in S-14.1 for the plant in service that is supported by CIAC. This adjustment was calculated by multiplying the actual CIAC balances at December 31, 1999, by the current applicable approved depreciation rate.

Adjustment S-14.3 adjusts depreciation to reflect the test year capitalization percentage of depreciation on transportation and power-operated equipment.

AMORTIZATION

Q. Please discuss your adjustments to amortization expense.

A. The adjustments to amortization expense are identified as S-15.1, S-15.2, S-15.4 and S-15.5 on Accounting Schedule 10, Adjustments To Income Statement.

Adjustment S-15.1 eliminates the test year expense related to the amortization of a capital lease. The lease expired during the test year and the amortization expense will no longer be incurred.

Adjustment S-15.2 provides for a 5-year amortization related to the comprehensive planning study previously discussed in regard to adjustments to plant in service.

Adjustments S-15.4 and S-15.5 reflect a 5-year amortization of the costs for an environmental audit and a management study, respectively.

PROPERTY TAXES

Q. How was your adjustment S-16.4 to property taxes calculated?

A. The annualized level of property taxes was determined by including in expense the actual amount paid in December of 1999. That amount was compared to the test year recorded property tax expense to determine adjustment S-16.4 in the Schedule of Adjustments.

INCOME TAXES

Q. Please explain the mechanics employed in Accounting Schedule 11 to calculate current income tax expense.

A. Net operating income (NOI), as calculated on Accounting Schedule 9, Income Statement, is the starting point of the test year income tax calculation (column B) on Accounting Schedule 11. The NOI for each rate of return (Line 1, columns C, D and E) was calculated on Accounting Schedule 1, Revenue Requirement. The applicable current and deferred income taxes are added back to NOI to determine the NOI before income taxes (NOIBT). NOIBT is then adjusted for various tax timing differences to determine the amount of taxable income. The Federal and State income taxes are calculated based on current statutory rates applied to the taxable income after allowances for applicable income tax deductions and credits. State income taxes are deductible in the determination of Federal taxable income. One-half of Federal income taxes are deductible for State taxable income.

Q. What is the justification for the additions and subtractions that were used to adjust NOIBT?

A. In general, the justification for any difference between NOIBT (as reported on the books and adjusted by the Staff) and taxable income is dictated by the Internal Revenue Code (Code). These differences are referred to as timing differences or Schedule M items. Schedule M is the Federal tax form in which the Company annually reconciles the difference between book income and taxable income. The Staff has added or subtracted the Schedule M items from NOIBT which are necessary for rate making purposes.

Q. Please discuss the depreciation adjustments to NOIBT.

A. Tax depreciation, not book depreciation, is the appropriate expense for tax purposes. Therefore, book depreciation must be added to, and tax depreciation deducted from, NOIBT to properly state taxable income. A difference exists between book and tax depreciation because the depreciable tax basis for plant is normally less than the book basis due to expenditures historically capitalized for book purposes, but expensed in the year incurred for tax purposes. In addition, the Code provides for a quicker recovery of the tax basis plant investment through the use of accelerated depreciation methods. Total tax depreciation is the sum of the two components entitled "Tax straight line depreciation" and "Excess tax depreciation," lines 15 and 16, on Accounting Schedule 11.

Q. Why is tax depreciation separated into the components tax straight line and excess?

A. Each of these components of tax depreciation has a distinct impact on total income tax expense. Straight line is the equivalent of book depreciation, restated to reflect the tax basis of the plant in service, and is provided "flow-through" rate treatment. The difference between total tax depreciation and tax straight line depreciation, identified as excess tax depreciation, is required by the Code to be "normalized."

Q. What is meant by the terms "flow-through" and "normalization?"

A. Flow-through is the tax treatment that equates the amount provided by the ratepayer for income tax expense with the amount paid to the taxing authority. Under normalization, the impact of a tax timing difference on current income tax expense is offset by the creation of a deferred income tax expense. The ratepayer provides the funds to the Company as if the tax timing difference did not exist.

Q. How were the two components of tax depreciation determined?

A. The Company provided its Fixed Asset Management System Report (FAMS), which provided the tax basis of plant and the associated tax depreciation as of the end of the test year. The tax straight line depreciation was calculated by applying the composite book depreciation rate to the tax basis of the plant.

Q. Please describe the other adjustments to NOIBT to compute taxable income on Accounting Schedule 11.

A. The additions to NOIBT include the following:

1. **Contributions in Aid of Construction (CIAC)** - For tax purposes, the Company is required to report non-extension related CIAC revenue when received from customers. For book purposes, CIAC is credited to a plant account which reduces rate base.

2. **Miscellaneous Non-deductible Expenses** - This category includes such items as travel, meals, dues, gifts and lobbying expenses which are only 50% deductible for tax purposes. An add-back to NOIBT is necessary to reflect the limit imposed by the Internal Revenue Service (IRS). The Staff amount reflects a two-year average of the adjustment included in the actual tax returns of the Company for the last two available tax years, 1997 and 1998.

The remaining subtractions from NOIBT include:

1. **Interest expense** - Interest is a below-the-line expense on the income statement of MAWC and is not reflected on the Staff's Income Statement, Accounting Schedule 9. However, interest expense is a deduction for tax purposes. Interest expense was calculated by multiplying rate base by the Staff's calculated weighted cost of debt which is sponsored by Staff witness McKiddy. This method of determining interest expense is known as interest synchronization because the interest used in the calculation of income tax expense is matched with the interest expense the ratepayers are required to provide to the Company in rates. Interest synchronization has been consistently used by the Staff and adopted by the Commission in past orders.

2. **Cost of Removal** - These costs are included in depreciation expense over the life of the depreciable property on the books but are deductible on the tax return in the year incurred. The Staff amount, similar to miscellaneous non-deductible expense, reflects an average of the tax timing adjustment included in the actual tax returns of the Company for the last two available tax years.

Q. Regarding the adjustments to arrive at taxable income, you indicated that the excess tax depreciation was normalized. What treatment is being proposed by the Staff for the other additions or subtractions made to NOIBT?

A. It is the general policy of the Staff to provide flow-through treatment for all tax timing differences that are not required to be normalized by the Code.

Q. How was the income tax adjustment you are sponsoring for current income tax expense quantified?

A. The adjustment to current income tax expense, adjustment S-17.1, was determined by subtracting the test year recorded income tax expense from the current income tax calculated on Accounting Schedule 11.

Q. Please describe adjustment S-18.1.

A. Adjustment S-18.1 adjusts deferred income tax expense to reflect the normalization of the timing difference related excess depreciation, as discussed above with regard to adjustments made to determine the level of taxable income.

Q. Please describe adjustment S-19.1 to amortize ITC.

A. The Staff has made no adjustment to the test year recorded level of ITC amortization

Q. Does this conclude your pre-filed direct testimony?

A. Yes. It does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri-American Water Company's Tariff Sheets designed to implement general rate increases for water and sewer service provided to customers in the Missouri area of the company.	)))))	Case No. WR-2000-281
In the Matter of Missouri-American Water Company for a general sewer rate increase	))	Case No. SR-2000-282

AFFIDAVIT OF DOYLE L. GIBBS

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Doyle L. Gibbs, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 63 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Doyle L. Gibbs

Doyle L. Gibbs

Subscribed and sworn to before me this 31st day of March, 2000.

Toni M. Willmeno

Toni M. Willmeno
Notary Public, State of Missouri
County of Callaway
My Commission Expires June 24, 2000

TONI M. WILLMENO
NOTARY SEAL
NOTARY PUBLIC
STATE OF MISSOURI

RATE CASE PROCEEDINGS
DOYLE L. GIBBS

Company	Case Number
Arkansas Power & Light Company	ER-85-20
Arkansas Power & Light Company	ER-85-265
Associated Natural Gas Company	GR-79-126
Atmos Energy Corporation/United Cities Gas Company	GM-97-70
Capital City Water Company	WR-82-117
Citizens Electric Cooperative	ER-79-102
Citizens Electric Cooperative	ER-81-79
Empire District Electric Company	ER-95-279
Laclede Gas Company	GR-77-33
Laclede Gas Company	GR-78-148
Laclede Gas Company	GR-80-210
Laclede Gas Company	GR-81-245
Laclede Gas Company	GR-82-200
Laclede Gas Company	GR-96-193
Laclede Gas Company	GR-98-374
Laclede Gas Company	GR-99-315
Lake St. Louis Sewer Company	SR-80-189
Missouri-American Water Company	WR-89-265
Missouri-American Water Company	WM-93-255
Missouri-American Water Company	WR-93-212
Missouri-American Water Company	WR-97-237
Missouri-American Water Company	SR-97-238
Missouri-American Water Company	WO-98-204
Missouri Cities Water Company	WR-78-107
Missouri Cities Water Company	SR-78-108
Missouri Cities Water Company	WR-83-14
Missouri Cities Water Company	SR-83-15
Missouri Cities Water Company	WR-85-157
Missouri Cities Water Company	SR-85-158
Missouri Cities Water Company	WR-86-111
Missouri Cities Water Company	SR-86-112
Missouri Cities Water Company	WR-89-178
Missouri Cities Water Company	SR-89-179
St. Joseph Water Company	WR-77-226
St. Louis County Water Company	WR-78-276
St. Louis County Water Company	WR-83-264
St. Louis County Water Company	WR-87-2
St. Louis County Water Company	WR-88-5
St. Louis County Water Company	WR-94-166

RATE CASE PROCEEDINGS
DOYLE L. GIBBS

Company	Case Number
Southwestern Bell Telephone Company	TR-79-213
Southwestern Bell Telephone Company	TR-80-256
Southwestern Bell Telephone Company	TR-86-84
Union Electric Company	ER-77-154
Union Electric Company	ER-80-17
Union Electric Company	ER-81-180
Union Electric Company	HR-81-259
Union Electric Company	ER-82-52
Union Electric Company	ER-83-163
Union Electric Company	ER-84-168

Missouri-American Water Company
WR-2000-281 & SR-2000-282

Corporate Allocation Factors

1 **Customers - TYE as Updated:**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
486	4,977	4,465	101	5,997	25,971	22,058	31,068	95,123
0.51%	5.23%	4.69%	0.11%	6.30%	27.30%	23.19%	32.66%	100%

Applicability:
- Other Revenues
- Source of Supply - All accounts
- Pumping - All accounts
- Customer Accounting: Account 903.2, Contract & Order Labor
  Account 907, Service & Information

2 **Number of Bills - TYE as Updated:**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
5,832	59,724	53,580	1,212	71,964	311,652	264,696	128,080	896,740
0.65%	6.66%	5.97%	0.14%	8.03%	34.75%	29.52%	14.28%	100%

Applicability:
- Customer Accounting: Account 902, Meter Reading
  Account 903.3, Collecting Expense
  Account 903.5, Billing & Accounting Expense
  Account 903.6, Billing & Accounting Labor

3 **Corporate Customer Accounting Composite**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
2,281	23,361	20,957	474	28,148	121,901	103,534	81,223	381,880
0.60%	6.12%	5.49%	0.12%	7.37%	31.92%	27.11%	21.27%	100%

Applicability:
- Customer Accounting: Account 901, Supervision
  Account 905, Miscellaneous

4 **Length of Mains (feet)**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
68,761	455,615	417,192		474,688	2,310,890	1,793,509	3,160,432	8,681,087
0.79%	5.25%	4.81%	0.00%	5.47%	26.62%	20.66%	36.41%	100%

Applicability:
- All Transmission & Distribution Expense

5 **Labor Composite**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
73,736	246,493	197,436	4,497	165,618	555,971	902,779	1,328,715	3,475,246
2.12%	7.09%	5.68%	0.13%	4.77%	16.00%	25.98%	38.23%	100%

Applicability:
- All A&G expenses
- General Plant
- Accumulated Depreciation Reserve on General Plant
- Accumulated Amortization Reserve
- Miscellaneous Non-deductible Expenses

Missouri-American Water Company
WR-2000-281 & SR-2000-282

Corporate Allocation Factors

6 **Revenue**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
111,555	1,560,655	1,549,068		1,856,992	8,023,197	7,484,377	10,009,529	30,595,373
0.36%	5.10%	5.06%	0.00%	6.07%	26.22%	24.46%	32.72%	100%

Applicability:
PSC Assessment for Water Operations

7 **Taxable Income**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
(230,483)	(256,638)	(334,332)	(13,028)	394,051	1,676,069	1,817,185	2,999,512	6,052,337
-3.81%	-4.24%	-5.52%	-0.22%	6.51%	27.69%	30.02%	49.56%	100%

Applicability:
Per Book Current Income Tax Expense

8 **Annualized Deferred Income Tax Expense**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
10,374	111,751	79,941	1,647	89,142	344,883	212,533	126,481	976,752
1.06%	11.44%	8.18%	0.17%	9.13%	35.31%	21.76%	12.95%	100%

Applicability:
Per Book Deferred Income Tax Expense

9 **Net Book to Tax Depreciation Reserve Difference**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
162,969	1,545,863	1,187,707	45,664	1,238,181	5,175,508	9,090,675	12,552,172	30,998,737
0.53%	4.99%	3.83%	0.15%	3.99%	16.70%	29.33%	40.49%	100%

Applicability:
Deferred Income Tax Balances

10 **Net Plant**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
1,048,723	7,050,293	9,143,057	61,911	8,056,757	41,761,514	25,075,942	24,440,756	116,638,952
0.90%	6.04%	7.84%	0.05%	6.91%	35.80%	21.50%	20.95%	100%

Applicability:
State Franchise Tax

11 **Direct Assigned Net CIAC**

B'wick	Mexico	P'ville W	P'ville S	W'burg	St.Chas	Joplin	St. Joe	Total
167,247	852,232	1,896,113	0	1,867,494	13,776,036	3,241,297	2,211,921	24,012,340
0.70%	3.55%	7.90%	0.00%	7.78%	57.37%	13.50%	9.21%	100%

Applicability:
Accumulated Depreciation on CIAC