Exhibit No.:
Issues:
Witness: Steve M. Traxler
Sponsoring Party: MoPSC Staff
Type of Exhibit: Replacement Pages for Rebuttal Testimony
Case No.: EM-2000-369

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

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REPLACEMENT PAGES FOR REBUTTAL TESTIMONY

OF

STEVE M. TRAXLER

UTILICORP UNITED INC. AND EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. EM-2000-369

Jefferson City, Missouri
September 2000

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<u>Denotes Highly Confidential Information</u>

acquisition premium. The Joint Applicants and the Staff's projections are set forth below:

	UCU/Empire 000's	Staff 000's
Net Merger Savings/(Costs) Years 1-5	$ 68,662	($33,075)
Less 50% of Acquisition Premium	($102,590)	($102,590)
Net (Loss) – Years 1-5	($ 33,928)	($135,665)

My testimony will generally refer to projected merger costs and savings for years 6-10, because the projected results for these years are alleged to support the Joint Applicants' claim that the proposed UCU/Empire merger satisfies the "not detrimental to the public interest" standard in Missouri.

In summary, I will explain in my testimony that after appropriate adjustments are made to the UCU/Empire projected benefit analysis, the merger costs for years 6-10 exceed merger savings by approximately $4 million annually. This is without consideration of recovery of the merger acquisition premium. The Staff's ten-year cost/benefit analysis, Schedule SMT-2, reflects that net merger savings are significantly less than the level required to recover 50% of the merger acquisition premium plus transaction costs, as requested by the Joint Applicants.

Q. Please describe the areas addressed in your rebuttal testimony.

A. My testimony will address the following areas:

- Detrimental aspects of proposed regulatory plan
- Transition Cost Recovery – FAS 106 Curtailment Cost
- Impact of UCU's Re-engineering Project Costs

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and also reflects the Staff's projected merger costs and savings for comparison. The significant differences between Joint Applicants' and the Staff's projected merger costs and savings are reflected on Schedule SMT-2. Lines 2, 3, 4 and 5 of Schedule SMT-2 reflect the projected savings in the Transmission, Distribution, Customer Service, A&G and General Plant functions. The projected merger savings in these functional areas result from projected reductions in personnel and related payroll taxes by consolidating some of Empire's existing operations at the UCU corporate level.

The projected merger costs and savings resulting from consolidating some of Empire's current operations is summarized below as reflected on Schedule SMT-2. Lines 14, 15and 16 of Schedule SMT-2 reflect the increase in Empire's cost of service resulting from consolidating existing functions at Empire and the allocation of UCU's corporate overhead costs allocated back to Empire:

Schedule SMT-2 Line No.		**Years 6-10**	
		UCU/Empire 000's	**Staff 000's**
2	A&G/Customer Service Savings	$ 39,688	$39,688
3	Distribution Savings	$ 28,915	$28,915
4	Transmission Savings	$ 4,837	$ 4,837
5	Staff Adjustment-1999 Budgeted Positions	$ 0	($ 5,798)
7	Total Merger Savings	$ 73,440	$67,643
14	Empire Direct Costs Transferred to ESF Depts.	$ 25,405	$ 25,405
15	Empire Direct Costs Transferred to IBU Depts.	$ 14,777	$ 14,777
16	ESF & IBU Depts. **Allocated Back to Empire**	($137,253)	($170,796)
17	Empire Cost (Increase) from UCU Allocations	($ 97,071)	($130,614)
	Net Cost **(Increase)** to Empire-Lines 7 & 17	($ 23,631)	($ 62,971)
	Average Cost **(Increase)** Per Year	($ 4,726)	($ 12,594)

Q. Do the amounts summarized in your last answer indicate that both the Joint Applicants and the Staff expect a significant increase in Empire's post-merger cost

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of service due to the net impact of consolidation and allocating UCU's corporate overhead costs to Empire?

A. Yes. UCU/Empire is projecting a $23.6 million net increase to Empire's cost of service during years 6-10 after the merger closes which amounts to $4.7 million annually.

The Staff is projecting a $62.9 million net increase in Empire's cost of service, which amounts to $12.6 million annually during years 6-10 following the merger closing. Under the proposed regulatory plan, Empire's rates are not to be impacted by the merger until after the moratorium for years 1-5 expires.

Q. What assumption differences account for the approximate $39 million difference between the Staff and UCU/Empire projected cost increase from UCU's corporate overhead allocations and consolidation of existing Empire operations for years 6-10 following the merger closing?

A. UCU witness Siemek has assumed a 2.5% annual inflation rate in projecting the annual increase in: 1) savings, 2) costs transferred from Empire to UCU and 3) UCU corporate overhead costs allocated back to Empire after the merger. I do not consider the 2.5% inflation factor appropriate to apply to UCU's corporate overhead costs.

Q. In your opinion, should the inflation rate assumption for the UCU overhead costs allocated back to Empire after a merger also be representative of UCU's actual historical experience?

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A. Yes. UCU's current historical experience provides the best source of information for determining an appropriate growth/inflation rate for the costs subject to consolidation.

Q. Did you also prepare a historical analysis of UCU's growth rate for corporate overhead costs?

A. Yes. In response to Staff Data Request No. 594, Case No. EM-2000-292, UCU provided the Staff with total ESF and IBU Department costs for 1995-1999 and the amount that was allocated to UCU's MPS division. The results of my analysis are reflected on Schedule SMT-7 and are summarized below:

Annual % Increase in UCU ESF & IBU Dept. Costs	**Average Annual Increase**
1996-1999 - Four-Year Average	45.7%
1997-1999 – Three-Year Average	20.0%
1998-1999 – Two-Year Average	6.2%

Please note that the above percent increases are not the total for the four-year period, but represent the average annual increase in every year.

MPS' allocated share of UCU's corporate overhead costs has increased from $10.3 million in 1995 to $46.5 million in 1999. A $36.5 million annual increase in four years is significant from any point of view.

Q. Given the actual growth in UCU's corporate overhead costs allocated to MPS and the significant increase being projected by both UCU/Empire and the Staff for Empire as a result of the merger, should the calculation of an appropriate growth/inflation rate favor Empire's current ratepayers?

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A. Based on MPS's actual experience regarding allocated Overhead Costs from UCU, I believe that a 5% growth rate is the lowest growth rate that should be used. MPS actual growth rate was 3.5% in 1999 as reflected on Line 4 of Schedule SMT-7. However, based upon MPS' experience in the last three years, a rate of 20% or more could be justified.

The only year since 1995 that MPS's allocated overhead costs from UCU did not exceed 5%, by a significant amount, was 1999.

The primary purpose of analyzing the UCU/Empire projected merger costs and savings is to make a recommendation as to whether a merger with UCU is anticipated to be not detrimental to Empire's ratepayers. I believe a 5% growth rate to be the minimum assumption suitable for this objective. Referring to Schedule SMT-7, once more, the average growth rate for 1998 and 1999 of 6.2% also exceeds my 5% assumption.

~~Q. What impact did your inflation rate assumption have on the projected savings by UCU/Empire related to the consolidation of the functional expense areas identified on pages 10 and 11of this rebuttal testimony?~~

~~A. Assuming a 5% inflation rate for both merger costs and savings, from consolidation, the Staff's projected savings are higher than those of the Joint Applicants for years 6-10 by $10.7 million as reflected on lines 2, 3, 4 and 5, Column D of Schedule SMT-2.~~

Q. Referring again to Schedule SMT-2, please explain the adjustment on line 5, Staff Adjustment – 1999 Budgeted Positions.

A. This adjustment is sponsored by Staff witness Fischer and is addressed in detail in her rebuttal testimony. Witness Fischer considers the Joint Applicants'

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to Empire. The Joint Applicants reflect an increase of $23.6 million for years 6-10. The Staff's calculations result in an increase of $62.9 million based upon a more reasonable inflation rate assumption for UCU overhead costs allocated back to Empire.

Q. Given that both the Joint Applicants and the Staff are projecting an increase in Empire's cost of service as a result of consolidation and allocation of UCU's corporate overhead costs, how do UCU/Empire address this detrimental impact in their merger application?

A. UCU/Empire is proposing a regulatory plan that results in the forced subsidization of merger costs and the acquisition premiums by MPS, Empire and SJLP ratepayers. The detrimental impact of this proposed regulatory plan is addressed in this rebuttal testimony beginning on page 8 and in the rebuttal testimonies of Staff witnesses Oligschlaeger, Featherstone, Broadwater and Proctor. Additionally, the Joint Applicants are projecting savings in the joint dispatch and employee benefits conversion areas to offset the negative impact from UCU's corporate overhead allocation.

Q. In summary, will UCU/Empire's projected merger savings in the joint dispatch and benefits conversion areas offset the detrimental impact on Empire's cost of service resulting from consolidation of existing Empire functions and allocation of UCU's corporate overhead costs back to Empire?

A. No. UCU/Empire's projected savings in the joint dispatch and benefits conversion areas are significantly overstated and, therefore, will not offset the admitted detrimental impact on Empire's cost of service resulting from functional consolidation of existing Empire operations and the allocation of UCU's corporate overhead costs to Empire. The projected savings in the joint dispatch and benefits conversion areas are

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Applicants in the area of joint dispatch savings is that the projected savings can be achieved by Empire on a "stand-alone" basis without the merger.

(5) Overstatement of savings from employee reductions as a result of the failure to recognize a normal job position vacancy rate.

Referring to Line 18 of Schedule SMT-2, the differences in projected net merger savings and merger costs (excluding the acquisition premium) are as follows:

	Years 1-10 $ 000's	**Years 6-10 $ 000's**
UCU/Empire Net Merger Savings/Costs	$176,166	$107,504
Staff Net Merger Savings/(Costs)	($ 53,083)	($ 20,006)
Difference between Staff & UCU/Empire	($229,249)	($127,510)

Q. How can you explain the monumental difference in the projected amounts reflected in your last answer?

A. There are five issues that account for such a significant difference in the ten-year projections of the Staff and UCU/Empire which are summarized below:

	Years 1-10 ($000's)	**Years 6-10 ($000's)**
UCU/Empire Net Merger Savings/Costs	$176,166	$107,504
Staff Issues:		
Proper Allocation of Joint Dispatch Savings to MPS & Empire	($192,388)	($102,977)
Staff Adjustment-1999 Budgeted Positions	($ 10,923)	($ 5,798)
Increase in Consolidation/UCU Overhead Allocations due to use of Appropriate Growth/Inflation Rate	($ 46,058)	($ 33,543)
Disallowance of Transaction Costs Assigned to Shareholders	$ 20,120	$ 14,808
~~Overstatement of Pension Benefits Conversion~~	~~($ 8,320)~~	~~($ 4,639)~~
Staff Excess of Merger Costs over Merger Savings	($ 53,083)	($ 20,006)

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Once a decision is made allowing these two companies to merge based upon projected assumptions, the merger, if consummated, it cannot be reversed in the event that the projected assumptions do not result in the expected net merger savings. The requested recovery of $93 million in merger acquisition costs in years 6-10 is a known and certain cost. The projected merger savings for years 6-10 are not known or certain.

Q. Please summarize the Staff's projected merger costs and savings for years 6-10 and how they compare to the $3 million in net merger savings projected by the Joint Applicants.

A. Line 18, Column (D) of Schedule SMT-2 reflects that merger costs are projected by the Staff to exceed savings by $20 million for the five-year period 6 through 10. Adding the 50% recovery of the acquisition adjustment results in net merger costs of $113 million for years 6-10.

The Staff's position is that the net savings from this merger will not be remotely close to being sufficient to cover merger costs and the requested 50% recovery of the merger acquisition premium.

Q. In your view, does the proposed merger between UCU and Empire make economic sense to the shareholders of UCU?

A. No. The merger savings are not sufficient to cover merger costs and the merger acquisition premium. Even if we assume that the merger generates 100% of the projected savings and the regulatory plan is approved, merger savings will not recover the costs of this merger projected for the ten-year period following the merger closing.

Q. What is the basis for the assumption in your previous answer that even if the Commission adopts the Joint Applicants' proposed regulatory plan and accepts all

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BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of the Joint Application of UtiliCorp United Inc. and The Empire District Electric Company For Authority To Merge The Empire District Electric Company With and Into UtiliCorp United Inc. and, In Connection Therewith, Certain Other Related Transactions, Filed.	)))))))	EM-2000-369

AFFIDAVIT OF STEVE M. TRAXLER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Steve M. Traxler, is, of lawful age, and on his oath states: that he has participated in the preparation of the foregoing Replacement Pages for his Rebuttal Testimony in question and answer form, consisting of 8 pages to be presented in the above case; that the answers in the foregoing Replacement Pages for his Rebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Steve M. Traxler

Steve M. Traxler

Subscribed and sworn to before me this 7th day of September 2000.

D Suzie Mankin

D SUZIE MANKIN
NOTARY PUBLIC STATE OF MISSOURI
COLE COUNTY
MY COMMISSION EXP. JUNE 21,2004

Utilicorp / Empire Electric Company
Summary of Synergy Benefits, net of Costs to Achieve

UCU / Empire Projected Merger Cost / Benefit Analysis

	UCU / Empire Projected Merger Cost / Benefit Analysis	UCU/Empire Total All 10 Years 000's (A)	Staff Total All 10 Years 000's (B)	UCU/Empire Total Years 6 - 10 000's (C)	Staff Total Years 6 - 10 000's (D)
	Operating Costs - Current Dollars				
1	Dispatch / Generation Savings	$ 197,885	$ 5,496	$ 108,238	$ 5,261
2	General & Administrative / Customer Accounts Savings	$ 74,766	$ 74,767	$ 39,688	$ 39,688
3	Distribution Savings	$ 52,319	$ 52,318	$ 28,915	$ 28,916
4	Transmission Savings	$ 8,572	$ 8,570	$ 4,837	$ 4,836
5	Staff Adjustment - 1999 Budgeted Positions	$ -	$ (10,923)	$ -	$ (5,798)
6	Conversion to Utilicorp Benefits	$ 50,030	$ 50,030	$ 28,450	$ 28,450
7	Total O & M Savings	$ 383,572	$ 180,259	$ 210,128	$ 101,354
	Capital Savings (Costs)				
8	Depreciation - Interconnect / SCADA / T&D	$ (408)	$ (408)	$ 978	$ 978
9	Amortization of Transaction / Transition Costs	$ (29,618)	$ (9,498)	$ (14,808)	$ -
10	Return on Interconnect SCADA / T&D	$ 5,487	$ 5,487	$ 8,277	$ 8,277
11	Return on Trnasaction / Transition Costs	$ -	$ -	$ -	$ -
12	Total Capital Savings (Costs)	$ (24,539)	$ (4,419)	$ (5,553)	$ 9,255
13	**Total Synergies, net of Costs to Achieve**	$ 359,033	$ 175,840	$ 204,575	$ 110,609
	Net Enterprise Support Functions Allocated to Empire				
14	Empire Direct Costs transferred to ESF Departments	$ 47,859	$ 47,859	$ 25,405	$ 25,405
15	Empire Direct Costs transferred to IBU Departments	$ 27,838	$ 27,837	$ 14,777	$ 14,777
16	ESF and IBU Departments **Allocated Back to Empire**	$ (258,564)	$ (304,619)	$ (137,253)	$ (170,796)
17	Net UCU Corpoarate Overhead Depts. Allocated to Empire	$ (182,867)	$ (228,923)	$ (97,071)	$ (130,614)
18	**Total Synergies, net of Costs to Achieve and Allocated Costs**	$ 176,166	$ (53,083)	$ 107,504	$ (20,006)
	Premium Costs				
19	Return on Premiun	$ (274,034)	$ -	$ (127,088)	$ -
20	Amortization of Premium	$ (69,880)	$ -	$ (34,940)	$ -
21	Reflect non-tax deductibility of Premium	$ (46,586)	$ -	$ (23,293)	$ -
22	Total Premium Cost	$ (390,500)	$ -	$ (185,321)	$ -
23	**SJLP Share of Premium Costs - 50 %**	$ (195,250)	$ -	$ (92,661)	$ -
24	**Synergies, net of 50 % of Premium**	$ (19,084)	$ (53,083)	$ 14,844	$ (20,006)
25	**Average per Year**	$ (1,908)	$ (5,308)	$ 2,969	$ (4,001)

26	Inflation Rate - UCU ESF / IBU Dept. Costs	5.0%
27	Inflation Rate - Empire Costs Transferred to UCU and Savings	2.5%

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Utilicorp / Empire Electric Merger
Case No. EM 2000-369

Analysis of UCU Corporate Overhead Costs - allocated to MPS

Line No.	UCU Corporate Overhead Costs - allocated to MPS	1995	1996	1997	1998	1999
1	ESF Department Costs allocated to MPS	$ 9,304,100	$ 25,407,000	$ 31,560,797	$ 30,501,487	$ 34,368,908
2	IBU Department Costs allocated to MPS	$ 1,010,882	$ 1,428,779	$ 9,696,027	$ 14,403,754	$ 12,105,621
3	Total Costs UCU Overhead Costs allocated to MPS	$ 10,314,982	$ 26,835,779	$ 41,256,824	$ 44,905,241	$ 46,474,529
4	**Percent Increase per Year**		**160.2%**	**53.7%**	**8.8%**	**3.5%**
5	Average Increase - 1996 - 1999			4 yr. Average	1996 - 1999	45.7%
6	Average Increase - 1997 - 1999			3 yr. Average	1997 - 1999	20.0%
7	Average Increase - 1998 - 1999			2 yr. Average	1998 - 1999	6.2%

Source: Data Request 594, EM 2000-292