

Exhibit No.:	ISRS
Issue:	Glenn W. Buck
Witness:	Rebuttal Testimony
Type of Exhibit:	Laclede Gas Company
Sponsoring Party:	GO-2004-0443
Case No.:	

LACLEDE GAS COMPANY

GO-2004-0443

REBUTTAL TESTIMONY

OF

GLENN W. BUCK

REBUTTAL TESTIMONY OF GLENN W. BUCK

1 Q. Please state your name and business address.

2 A. My name is Glenn W. Buck, and my business address is 720 Olive St., St. Louis,  
3 Missouri, 63101.

4 Q. What is your present position?

5 A. I am the Manager, Financial Services for Laclede Gas Company ("Laclede" or  
6 "Company").

7 Q. Please state how long you have held your position and briefly describe your  
8 responsibilities.

9 A. I was appointed to my present position in March, 1999. In this position, I am responsible  
10 for the financial aspects of rate matters generally, including financial analysis and  
11 planning. I am also responsible for the preparation of various financial forecasts and  
12 monitoring regulatory trends and developments. Additionally, in March of this year, I  
13 took on the added responsibility of directing the activities of our general accounting  
14 department, which is responsible for the timely payment of invoices due from our  
15 vendors.

16 Q. What is your educational background?

17 A. I graduated from the University of Missouri - Columbia, in 1984, with a Bachelor of  
18 Science degree in Business Administration.

19 Q. Will you briefly describe your experience with the Company prior to becoming Manager,  
20 Financial Services?

1 A. I joined Laclede in August, 1986, as a Budget Analyst in the Budget Department. I was  
2 promoted to Senior Budget Analyst in June, 1988, and transferred to the Financial  
3 Planning Department in December, 1988 as an Analyst. I was promoted to Senior  
4 Analyst in February, 1990, Assistant Manager in February, 1994, and Manager in January  
5 1996 . I acted in that capacity until being appointed to my current position.

6 Q. Have you previously filed testimony before this Commission?

7 A. Yes, I have, in Case Nos. GR-94-220, GR-96-193, GR-99-315, GR-2001-629, GT-2001-  
8 329, and GR-2002-356. Additionally, I was actively involved in the development of the  
9 Commission's rules related to the Infrastructure System Replacement Surcharge  
10 ("ISRS") for gas utilities and provided oral comment during the hearing on those rules.

11 **Summary and Purpose of Testimony**

12 Q. What is the purpose of your testimony?

13 A. The purpose of my testimony is to respond to the direct testimony and memorandum  
14 submitted by Staff witness Steven M. Rackers in regards to the Company's ISRS filing.  
15 Specifically, I will address why the Staff's recommendation to reflect certain tax  
16 deductions as an offset to the amount that the Company has requested in its ISRS filing  
17 should be rejected by the Commission.

18 Q. Please summarize the major reasons why you believe the Commission should reject  
19 Staff's proposed treatment of taxes and approve the Company's filing as submitted.

20 A. There are three main reasons why I believe the Commission should reject Staff's  
21 proposed treatment of taxes in the Company's ISRS filing:

- 22 • First, such treatment does not comport with either the plain language of the  
23 statutory provisions (Sections 393.1009, 393.1012 and 393.1015 of the Revised

1 Statutes of Missouri) that authorize the ISRS mechanism and govern how ISRS  
2 revenues are to be calculated by the Commission, or with the rules that the  
3 Commission recently adopted to implement these statutory provisions, in that it is  
4 based on a consideration of factors that are clearly outside the boundaries of those  
5 factors that are to be considered by the Commission in ISRS cases.

- 6 • Second, Staff's proposed tax treatment contradicts the Commission's own  
7 findings in Case No. WO-2004-0116 in which it determined that it was  
8 inappropriate to consider issues not specifically addressed in the ISRS Statute.
- 9 • Third, the Staff's attempt to recognize an annualized level of tax deductions in its  
10 calculation of ISRS revenues results in a classic "double dip" in that an  
11 annualized level of income tax associated with the Company's investment in  
12 ISRS projects has already been reflected in rates and flowed through to Laclede's  
13 customers. By seeking to flow through these tax effects twice, the Staff's  
14 recommended treatment is directly contrary to Staff's own prior interpretation  
15 during another ISRS case of how the ISRS mechanism was designed to work – an  
16 interpretation that flatly rejected the very kind of double recognition of expense or  
17 revenue items that Staff is now proposing. Such treatment also stands in stark  
18 contrast to the efforts made by Laclede and this Commission to prevent such a  
19 double recognition of expense or revenue items during the proceeding that was  
20 recently conducted by the Commission to establish an ISRS Rule for gas utilities.  
21 Specifically, I wrote language (and addressed the same during oral comments),  
22 Laclede proposed and, ultimately, the Commission accepted language in the

1 rulemaking designed to avoid just such an occurrence. Company witness James

2 A. Fallert will also be providing testimony in this proceeding related to this issue.

3 **Overview of ISRS Filing**

4 Q. Before addressing the reasons why you believe the Staff's proposed tax treatment should  
5 be rejected by the Commission, please provide a brief overview of Laclede's ISRS filing.

6 A. On August 28, 2003, legislation became effective that allows gas utility companies to  
7 recover through periodic rate adjustments a return on investment and related depreciation  
8 expenses and property taxes on certain safety-related investments as well as investments  
9 in infrastructure related to public improvement projects placed in service since the update  
10 (or true-up) period of the company's last general rate proceeding. On March 1, 2004,  
11 Laclede made an ISRS filing that would raise approximately \$3.86 million on an annual  
12 basis related to such investments. On April 26, 2004, the Staff filed a memorandum and  
13 direct testimony in this proceeding. In its direct testimony, the Staff stated that with the  
14 exception of its proposed treatment of certain income tax "flow-through" items, "the  
15 Staff agrees with Laclede's calculation of ISRS revenues." (Rackers Direct, page 2, lines  
16 10-11) In fact, the Staff indicated that if the Commission accepts Laclede's calculation  
17 as the appropriate methodology for the determination of the ISRS revenues, that "based  
18 on its review, the Staff believes that Laclede's computations are correct." (Staff  
19 Memorandum, Page 3) Please note that this filing includes investments made in ISRS-  
20 eligible property for the period from August, 2002 through December, 2003, which  
21 covers plant additions made subsequent to the update / true-up period included in rates in  
22 Laclede's last rate case, Case No. GR-2002-356.

1 Q. Is it your testimony that Laclede has used the appropriate methodology for the  
2 determination of the ISRS revenues and that its computations of such revenues are  
3 correct?

4 A. Yes, to the best of my knowledge and belief, all of the information and calculations set  
5 forth in the Application filed by the Company in this case are true, correct and accurate.  
6 Such calculations have also been done in full accordance with the statutory provisions  
7 and Commission rules governing ISRS filings and therefore reflect the correct level of  
8 ISRS revenues to which the Company is entitled. As discussed below, however, Staff's  
9 proposed treatment of taxes in its own calculation of ISRS revenues does not comport  
10 with these requirements.

11 **Staff Proposed Tax Treatment Does Not**  
12 **Comport With The ISRS Statute or ISRS Rule**

13 Q. What is the ISRS surcharge designed to recover?

14 A. As noted in the Staff Memorandum, Section 393.1009 states that the ISRS  
15 mechanism is designed to provide "appropriate pre-tax revenues" defined as "the  
16 revenues necessary to produce net operating income equal to:

17 (a) The gas corporation's weighted cost of capital multiplied by the net original  
18 cost of eligible infrastructure system replacements, including recognition of  
19 accumulated deferred income taxes and accumulated depreciation associated with  
20 eligible infrastructure system replacements which are included in a currently  
21 effective ISRS; and

22 (b) Recover state, federal, and local income or excise taxes applicable to such  
23 income; and

24 (c) Recover all other ISRS costs."

25 This definition of "appropriate pre-tax revenue" is further refined by Section  
26 393.1015(4), which states in part,

1 “4. In determining the appropriate pretax revenue, the commission shall consider  
2 only (emphasis supplied) the following factors:

3  
4 (1) The current state, federal, and local income tax or excise rates;”

5 Q. How are “all other ISRS costs” defined?

6 A. According to the ISRS Rule passed by the Commission, other ISRS costs are defined as  
7 the “annual depreciation expenses, and property taxes that will be due within twelve (12)  
8 months of the ISRS filing on the total cost of eligible infrastructure system replacements  
9 less annual depreciation expense and property taxes on any related facility retirements.”

10 Q. In what way does the Staff’s proposed adjustment deviate from the statutes and the  
11 Commission’s own rules?

12 A. As discussed more fully in the testimony of Company witness James A. Fallert, the Staff  
13 has reflected in its calculation of ISRS revenues the “flow-through” tax treatment that is  
14 currently afforded to transfer of services and the book/tax capitalization differences  
15 resulting from the Internal Revenue Code (commonly referred to as Section 263A)  
16 adjustments even though both of these items are fully reflected in rates already.  
17 Specifically, the Staff has inappropriately applied this “flow-through” tax treatment as an  
18 offset to the income tax “gross-up” necessary to recover the “net operating income”  
19 provided for in the ISRS Statute and Rule.

20 Q. Is the offset recommended by the Staff related to these two items addressed in or  
21 contemplated by the ISRS Statute or Rule?

22 A. Absolutely not. As previously noted, the only items open for consideration are the  
23 “current state, federal, and local income tax or excise rates” applicable to the net  
24 operating income on ISRS-eligible property. In fact, Staff’s own Memorandum  
25 demonstrates this clearly.

1 Q. Please explain.

2 A. On page 3 of its April 26 Memorandum, the Staff repeats the language of the ISRS  
3 Statute and ISRS Rule which states that the ISRS should: “[r]ecover state, federal, and  
4 local income or excise taxes applicable to such income ...” By using the term “recover”  
5 this language clearly contemplates that there would be a positive tax amount associated  
6 with the income calculated pursuant to the preceding paragraph (a) of the Statute. This is  
7 further buttressed by another provision of the Statute, namely Section 393.1015(4)(1),  
8 which is not mentioned in Staff’s April 26 Memorandum, but is included in Staff’s May 3  
9 Memorandum Attachments. As previously noted, that Section states that in determining  
10 ISRS revenues, the *only* factor that the Commission is to consider in terms of income  
11 taxes, is the “... current state, federal, and local income tax or excise *rates*,” (emphasis  
12 supplied). When considered together, these provisions establish a very straightforward  
13 and simple methodology for determining the income tax component of an ISRS filing, i.e.  
14 that component is determined by applying the state, federal and local income tax “rates”  
15 to the income amount calculated under Section 393.1009(1)(a).

16 Q. Is there anything in this language to indicate that tax deductions associated with  
17 particular ISRS investments may also be considered by the Commission?

18 A. No, there is absolutely nothing in the language of these provisions to suggest, as the Staff  
19 has, that the Commission may go beyond this straightforward calculation and also  
20 examine issues such as the level of tax deductions associated with an ISRS investment.  
21 In fact, it indicates just the opposite by limiting the Commission to a consideration of tax  
22 *rates*. And Staff’s own Memorandum explicitly recognizes the absence of language  
23 authorizing such a consideration when it attempts to rephrase the language of the ISRS



1 Statute to accommodate Staff's proposed method for calculating taxes. As set forth at  
2 page 4 of its April 26 Memorandum, Staff states that the ISRS should "recover state,  
3 federal, and local income or excise taxes applicable to such income (including all  
4 applicable tax deductions)" (emphasis supplied). Staff may indeed believe that the  
5 computation of ISRS revenues should include a consideration of "all applicable tax  
6 deductions." However, the parenthetical language necessary to authorize such a  
7 consideration exists only on page 4 of Staff's Memorandum. It does *not* exist, however,  
8 in either the ISRS Statute or the ISRS Rule and it is difficult to imagine a clearer  
9 demonstration of that fact than the comparison which Staff provided in its Memorandum  
10 between what the ISRS Statute actually says and what it would have to say to authorize  
11 Staff's proposed method for calculating taxes. Simply put, if the legislature had wanted  
12 tax deductions to be considered and flowed-through in the calculation of ISRS revenues,  
13 it would have incorporated language to that effect into the ISRS Statute. It did not.  
14 Instead, in requiring the Commission to process these cases in 120 days, the legislature  
15 specifically limited the matters to be considered by the Commission. With respect to  
16 taxes, the Commission may consider only tax rates; it is not authorized to grapple with  
17 tax deductions.

18 Q. Are there any other reasons why you believe the flow-through of tax deductions is not  
19 contemplated by the ISRS Statute?

20 A. Yes. In those instances where the ISRS Statute wishes to have a particular revenue or  
21 expense item considered in the calculation of ISRS revenues, it uses technical terms that  
22 have been long-established and widely-recognized in the regulatory arena to describe  
23 what those items are. For example, the ISRS Statute uses such terms as "accumulated

1 deferred income taxes” and “accumulated depreciation” in describing the items that are to  
2 be considered when calculating ISRS revenues. Each of these technical terms has a very  
3 specific meaning in the ratemaking process and their inclusion in the ISRS Statute  
4 demonstrates the pains that the legislature took to describe exactly how the Commission  
5 was to calculate ISRS revenues and what items would be considered in that calculation.  
6 In much the same way, the term “flow-through” is also a technical term that has a very  
7 specific meaning in the regulatory process when it comes to calculating taxes. Indeed,  
8 the term has long been used in numerous Commission cases to describe the very kind of  
9 tax treatment that Staff is proposing in this case. The fact that this technical term, unlike  
10 the others described above, is nowhere to be found in the ISRS Statute is another fact  
11 indicating that Staff’s proposed tax treatment was not contemplated by the Statute and,  
12 indeed, is precluded by it.

13 Q. On page 3, Lines 10 – 16 of his direct testimony, Mr. Rackers appears to imply that the  
14 flow-through treatment of transfer of services and 263A adjustments are analogous to the  
15 deductibility of interest expense. Are these items in any way similar to interest expense  
16 in the context of an ISRS filing?

17 A. No. Unlike the service transfers and 263A adjustments, the statute specifically  
18 contemplates the income taxes related to the weighted cost of capital, of which interest  
19 expense is a component, when it referred to the “taxes applicable to such income” where  
20 income was defined as the “corporation’s weighted cost of capital multiplied by the net  
21 original cost of eligible infrastructure system replacements”. The calculation of the cost  
22 of debt is specifically described in 393.1015(4), which details the items that the  
23 Commission shall consider in determining the ISRS surcharge. The revenue requirement

1 needed to produce the targeted rate of return is increased by the income taxes that will be  
2 paid on that revenue in order to produce the targeted return after tax. It is necessary to  
3 include the interest deduction in order to recognize that component of rate of return is tax  
4 deductible. The statute clearly includes taxes related to recovery of income, and excludes  
5 consideration of other income tax items. Nowhere, however, in this section of the ISRS  
6 statute, or for that matter, the Commission's ISRS Rule, are transfer of services, 263A  
7 adjustments, or even the concept of "flow-through" tax treatment mentioned.

8 **Staff's Proposed Tax Treatment Is Inconsistent**  
9 **With The Commission's Past ISRS Determinations**  
10

11 Q. Is the Staff's proposed tax treatment consistent with how the Commission has applied the  
12 ISRS Statute in prior cases?

13 A. No. A similar issue involving what the Commission may and may not consider under the  
14 language of the ISRS statute came up in the Missouri-American Water Company  
15 ("MAWC") ISRS case (Case No. WO-2004-0116). In that proceeding, MAWC included  
16 an adjustment to the accumulated depreciation component of its ISRS filing to recognize  
17 the net cost of removing the old plant that was replaced with ISRS plant. Other parties  
18 opposed inclusion of this adjustment.

19 Q. How did the Commission find in that proceeding?

20 A. The Commission rejected MAWC's adjustment. In rejecting the adjustment, the  
21 Commission stated that it, "... agrees that net cost of removal of the non-ISRS plant  
22 should not be included in the ISRS calculations. The statute *narrowly* prescribes the  
23 factors that the Commission may consider when calculating the ISRS". (emphasis  
24 supplied) The Commission further rejected a proposed adjustment related to property  
25 taxes for property added after January 1, 2003, stating that "*A plain reading of the*

1        *statute* (emphasis supplied) indicates that ISRS costs include property taxes that will be  
2        due within twelve months of the ISRS filing. Property taxes on plant added after January  
3        1, 2003 are not due until more than twelve months after the ISRS filing”. Similarly, a  
4        plain and narrow reading of the statute in this case indicates that, like the net cost of  
5        removal and property tax items rejected by the Commission in MAWC’s case, the flow-  
6        through tax treatment that Staff has proposed in this case for service transfers and 263A  
7        adjustments must be rejected because such treatment is not a factor that the Commission  
8        may consider under the ISRS Statute.

9                                    **Staff’s Adjustments Amount to a “Double-Dip”**

10    Q.     Are the language of the ISRS Statute and Rule, and the Commission’s decision in the  
11            MAWC case, the only reasons why the Company believes that the Staff’s proposed tax  
12            treatment is inappropriate?

13    A.     No. This issue must, of course, be decided based on what the ISRS Statute says, no  
14            matter what a party’s individual views of the Statute may be. That said, however, it is  
15            important for the Commission to recognize that Staff’s proposed tax treatment is also  
16            fundamentally unfair in that it seeks to double count the tax deduction effects associated  
17            with ISRS projects. As discussed more fully by Laclede witness James Fallert, an  
18            annualized level of current tax deductions associated with the Company’s investments in  
19            ISRS projects is already reflected in the Company’s rates and reflecting such a level  
20            again, as Staff has proposed to do, amounts to a classic “double dip”.

21    Q.     Does Laclede find Staff’s attempt to double count these tax effects particularly  
22            objectionable?

1 A. Yes, because during the formulation of the ISRS Rule, Staff expressed concern that the  
2 Rule should avoid “double-recovery” of certain expenses related to ISRS-eligible plant.  
3 Specifically, the Staff was concerned that the ISRS would allow for recovery of  
4 depreciation and property taxes on new ISRS-eligible plant while current rates already  
5 included an allowance for these expense items in the form of recognized depreciation  
6 expense and property taxes on the property items that were being retired. Under such  
7 circumstances, there was a potential for “double-recovery” of depreciation expense and  
8 property taxes on both the retired and replacement plant.

9 Q. How did Laclede react to this concern?

10 A. Laclede recognized it and agreed that the Statute was not intended to result in a double-  
11 recovery of costs and so we took the lead in attempting to develop a solution to Staff’s  
12 concern.

13 Q. What did Laclede propose to address Staff’s concern?

14 A. As stated earlier in testimony, I wrote, Laclede proposed, and, ultimately, the  
15 Commission adopted language that would avoid just such an occurrence. Specifically  
16 Laclede proposed, and other utilities agreed to support, the following addition to the  
17 definition of other “ISRS costs” included in the Commission’s Proposed Rule: “ISRS  
18 cost – annual depreciation expenses, and property taxes that will be due within twelve  
19 (12) months of the ISRS filing on the total cost of eligible infrastructure system  
20 replacements *less annual depreciation expenses and property taxes on any related facility*  
21 *retirements*” (Laclede language in italics). By specifying that the total cost of  
22 infrastructure replacements would be reduced by the depreciation expenses and property

1 taxes associated with the plant that was being replaced, this language specifically  
2 prevented a “double-recovery” of these expense items.

3 Q. Would the Staff’s proposed adjustments amount to “double-recognition” of the tax  
4 benefits related to service transfers and 263A adjustments?

5 A. Yes. As Company witness Fallert clearly demonstrates, our customers are already  
6 enjoying the tax benefits related to these two items through an annual flow-through  
7 allowance that was embedded in current rates. To “flow-through” these benefits again  
8 through an ISRS filing amounts to a “double-recognition” of this annual allowance. It is  
9 important to note that these benefits are not cumulative. In other words, the annual tax  
10 savings do not continually grow as more investments are made year-after-year.

11 Q. Has the Staff previously recognized that it is contrary to the ISRS Statute as well as good  
12 regulatory policy to permit a double recognition of an item that is already embedded in  
13 rates?

14 A. Yes. In its Brief in the MAWC case discussed above, the Staff raised this very point in  
15 arguing why the Commission should not permit MAWC to recover its net cost of removal  
16 in its ISRS filing. Specifically, the Staff stated in its Brief that such inclusion was  
17 inappropriate because there was already an allowance for removal costs embedded in  
18 MAWC’s rates, and recognition of such costs in the utility’s ISRS filing would therefore  
19 result in a double-recovery. In addition to arguing that such a result was by its very  
20 nature inappropriate, the Staff also contended that such a double-recovery was never  
21 contemplated or sanctioned by the ISRS Statute. The very same considerations are  
22 equally applicable to what Staff has attempted to do in this case with its proposed tax  
23 treatment. For the very reasons that the Staff was right in opposing a double recovery of

1 removal costs in MAWC, it is wrong for seeking a double recognition of these tax  
2 benefits in this case. The Commission can and should be consistent, however, by  
3 rejecting Staff's proposed tax treatment in this case just as it rejected MAWC's treatment  
4 of cost of removal in that case.

5 Q. Does this complete your testimony?

6 A. Yes, it does.

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**


In the matter of the verified application	)	
and petition of Laclede Gas Company for	)	<b><u>Case No. GO-2004-0443</u></b>
establishment of an infrastructure	)	Tariff No. YG-2004-1028
system replacement surcharge	)	

A F F I D A V I T

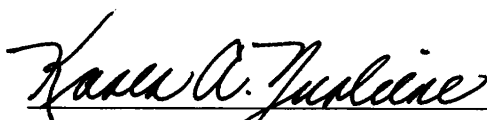
STATE OF MISSOURI   )  
                                          )   SS.  
CITY OF ST. LOUIS    )

Glenn W. Buck, of lawful age, being first duly sworn, deposes and states:

1.       My name is Glenn W. Buck. My business address is 720 Olive Street, St. Louis, Missouri 63101; and I am Manager, Financial Services, for Laclede Gas Company.
2.       Attached hereto and made a part hereof for all purposes is my rebuttal testimony.
3.       I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.

  
\_\_\_\_\_  
Glenn W. Buck

Subscribed and sworn to before me this 20th day of May, 2004.

  
\_\_\_\_\_  
KAREN A. ZURLIENE  
NOTARY PUBLIC - NOTARY SEAL  
STATE OF MISSOURI, CITY OF ST. LOUIS  
MY COMMISSION EXPIRES FEBRUARY 18, 2008