

Exhibit No.:

Issues: Misc. Acctg. Issues,
Maintenance Normalization,
Cash Working Capital,
Accounting Authority Orders
(AAO),
Bad Debt,
Jurisdictional Allocations,
Property Tax,
Rate Case Expense &
Health Benefits

Witness: Dennis R. Williams

Sponsoring Party: Aquila Networks-MPS

Case No.: ER-2004-0034 &

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Before the Public Service Commission
of the State of Missouri

Rebuttal Testimony

of

Dennis R. Williams

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DENNIS R. WILLIAMS
AQUILA, INC. D/B/A AQUILA NETWORKS-MPS**

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**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI
REBUTTAL TESTIMONY OF DENNIS R. WILLIAMS
ON BEHALF OF AQUILA, INC.
D/B/A AQUILA NETWORKS-MPS
CASE NOS. ER-2004-0034**

1 Q. Please state your name and business address.

2 A. My name is Dennis R. Williams. My business address is 10700 East 350 Highway,
3 Kansas City, Missouri 64138.

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

5 A. I am employed by Aquila, Inc. (“Aquila” or “Company”) as Vice President – Electric
6 Regulatory Services for our electric network operations.

7 Q. Briefly describe your education and work experience.

8 A. I graduated in 1974 from Central Missouri State University, receiving a Bachelor of
9 Science in Business Administration degree – summa cum laude, with majors in
10 accounting and finance. After graduation, I was licensed in Missouri as a Certified
11 Public Accountant and employed as an auditor in the regulated industries division of
12 Arthur Andersen and Company. After leaving Arthur Andersen, I was employed for five
13 years with the regulatory consulting firm of Lubow McKay Stevens and Lewis. Since
14 1986 I have been employed by Aquila in various capacities.

15 Q. What is the purpose of the rebuttal testimony you now are submitting in this case before
16 the Missouri Public Service Commission(“Commission”)?

17 A. I will be addressing the maintenance adjustment and cash working capital proposed by
18 Commission Staff (“Staff”) witness Lesley Preston; treatment of Accounting Authority
19 Orders (“AAO’s) discussed in the testimonies of Staff witness Trisha Miller and Office

1 of Public Counsel (“OPC”) witness Ted Robertson; the uncollectibles (bad debt) expense
2 adjustment proposed by Staff witness Amanda McMellen; the jurisdictional allocation
3 proposed by Staff Witness Alan Bax; property tax and rate case expense treatment
4 discussed in the testimony of Staff witness Trisha Miller; and the adjustment to the
5 employer portion of health, dental and vision benefits as proposed by Staff witness Dana
6 Eaves.

7 **Normalized Maintenance**

8 Q. What issue do you have with the maintenance adjustment as proposed by Lesley Preston?

9 A. Staff proposes to normalize Aquila’s Missouri Public Service operating division ,
10 (“MPS”) maintenance expense using a 57-month historical average for production and
11 transmission maintenance expense and a 33-month historical average for distribution
12 maintenance expense

13
14
15 Q. Why did Ms. Preston select the 57-month and 33-month periods?

16 A. Her testimony does not indicate the rationale for the use of those time periods as compared
17 to some other period of time.

18 Q. Do you agree with the “Normalization” method of a historical average Ms. Preston has
19 utilized for maintenance expense for purposes of this case?

20 A. No.

21 Q. Why not?

22 A. The purpose of normalization is to establish an on-going level of expense for the period in
23 which the rates set in this case will be in effect. The use of a test year to establish a “prima-

1 facie” level of operating expense is traditionally used in ratemaking. Test year costs are
2 then normalized to adjust the test year for any abnormalities. This method has been utilized
3 by the Staff and Aquila for the majority of the adjustments in this case and should be used to
4 project the on-going level of expense for maintenance.

5 Q. A test year level of expense reflects one year of history. Why would that method be
6 preferable to looking at 57 months?

7 A. The use of history to establish the ongoing level of non-production maintenance is not at
8 issue.

9 Q. What is the issue?

10 A. I have at least three concerns with Ms. Preston’s approach in deviating from the use of test
11 year amounts.

12 Q. Please explain.

13 A. First, it introduces the question of what historical time period is most reflective of ongoing
14 costs and the opportunity for arbitrary or incorrect judgment. Is a ten-year time horizon
15 more appropriate than five years; is three years more appropriate than ten; or is 57 months
16 most representative? During its audit, Staff reviewed information on maintenance cost
17 levels for a number of years, but has left unexplained why 57 months or 33 months was
18 judgmentally selected as the appropriate ongoing level.

19 Second, the Staff’s method is extremely unreasonable in a period of rising costs. Using a
20 long-term historical average to normalize year-to-year fluctuations has the effect of ignoring
21 the impact of inflation on the Company’s costs.

22 Q. Please explain.

1 A. As reflected on Schedule DRW-1, while non-labor maintenance costs have slight variations
2 from year to year, the ongoing trend is upward. This is for two reasons. First, inflation
3 tends to increase the cost of maintenance, even if the same level of maintenance work is
4 performed from year to year. Second, the amount of maintenance required increases in
5 direct relation to the level of plant being maintained. Total plant being maintained is an
6 obvious driver of maintenance expense. Basing the determination of an ongoing level of
7 maintenance expense on historical averages ignores both inflation and plant growth.

8 Q. How could inflation be taken into account?

9 A. There are several credible indices that could be used such as the Consumer Price Index
10 (“CPI”), the Midwest Consumer Price Index (“MCPI”), or the utility based Handy-Whitmen
11 index. Although all parties should agree that today’s cost are higher than they were in 1998,
12 the method of selecting which inflation index to use could be difficult.

13 Q. Do you have other concerns with the Staff’s approach?

14 A. Yes. Expanding a test period beyond the traditional one-year period introduces a level of
15 complexity to the normalization process than can be overcome, but which the Staff did not
16 attempt to address.

17 Q. Please explain.

18 A. In normalizing a test year, it is necessary to review the recorded transactions and adjust for
19 any significant abnormalities that make that period non-reflective of an ongoing level of
20 expense. When the test period is expanded to multiple years, each year would need to be
21 reviewed for potential abnormalities.

22 For example, the year 2001 is not a test year in this case and was not analyzed by the Staff to
23 determine if any adjustments should be made. Initially Staff took a similar approach to

1 normalizing production maintenance, as it had to normalizing other maintenance by using a
2 multi-year average of expense. However, it was obvious from the production maintenance
3 account summaries that 2001 contained a significant abnormality because one of the
4 accounts (account 513) had a negative balance. This abnormality was brought to Staff's
5 attention at the pre-hearing and has since been adjusted to increase its normalized non-labor
6 production maintenance by about \$670,000 for MPS. While this error stood out because of
7 the negative number, it is reflective of the fact that if a multiple year historical average is
8 used, all periods within that historical period need to be reviewed.

9 Q. Please explain.

10 A. By simply recognizing that one item in account 513 was abnormal and making an
11 appropriate adjustment, the Staff's method resulted in a \$670,000 change in their calculation
12 of normalized expense. When averaging such a large grouping of accounts, such as
13 maintenance expense, it is more appropriate to either adjust each year for issues that can
14 vary the average in such a large manner or use the preferred method of adjusting the test
15 year level of expense just as the Company and Staff have for most of the other adjustments
16 in this case.

17 Q. Wouldn't a review for abnormalities of five years or 57 months or some other similar period
18 of data be a tedious task?

19 A. Yes. The amount of audit time would increase dramatically if all expenses were adjusted
20 for the last five years and then averaged. However, as the above example shows, the
21 assumption cannot simply be made that selection of a historical period will level out unusual
22 variations. Selection of a test period requires review of the entirety of that test period to

1 determine that it reflects an appropriate ongoing level. That is one reason that I believe
2 normalization of a single test year is the more reasonable approach.

3 Q. Has this Commission previously ruled on the use of historical averages for maintenance?

4 A. Yes. In rate case number ER-97-394, Staff witness Tom Shaw used a five-year historical
5 average for maintenance.

6 Q. Did the Commission make a ruling on this issue in that case?

7 A. Yes. As stated in the final report and order here is a part of the findings:

8 **Maintenance Expense Normalization - D-6**

9 The Staff proposes an adjustment of approximately \$1.1 million
10 to the total non-payroll maintenance expense account. The
11 Staff states that it found the test year maintenance expense
12 to be abnormally high and therefore used a five-year
13 normalized expense process to more accurately represent the
14 ongoing level of maintenance expense. The Staff gives two
15 reasons for its use of the five-year normalization rather than
16 the one-year normalized method supported by UtiliCorp. The
17 Staff first points out that UtiliCorp has substantial
18 discretion over the budgeting and prioritizing of maintenance
19 projects, and this has resulted in an abnormally high test
20 year amount as compared with previous years. Secondly, the
21 Staff testifies that it had great difficulty obtaining
22 information necessary to ascertain the normal amount of
23 maintenance expense. Staff states that, to the best of its
24 knowledge, UtiliCorp has no specific budget guidelines which
25 specify a normal amount of maintenance expense and could
26 provide no information as to what projects are undertaken on a
27 recurring basis. Further, UtiliCorp did not furnish the Staff
28 with its maintenance policies or changes for the 1994-96 time
29 period. The Staff, therefore, used the normalization method,
30 which is a type of averaging, to obtain its normalized expense
31 figure...

32
33UtiliCorp states that the most common approach to
34 normalizing costs is to adjust the test year for any
35 abnormalities, as in this case the 1996 ice storm, and to use
36 the adjusted amount to project ongoing expense. UtiliCorp
37 points out that this method has been used by the Staff and
38 UtiliCorp for the majority of the adjustments in this case.
39 The UtiliCorp witness points out that the Staff failed to
40 adjust all five years in its calculation for abnormalities....

1 still in existence because. “The termination of the accounts receivable program is ultimately a
2 negative result derived from problems that Aquila has faced in its non-regulated ventures.”

3 Q. Do you agree with Ms. Preston’s approach?

4 A. No. The sales of accounts receivable is basically a short-term loan program. Ciesco, an
5 affiliate of Citibank, issued commercial paper to fund the purchased of Aquila’s current
6 accounts receivables. While it is true that Ciesco was no longer able to fund the program
7 once Aquila’s credit rating fell below investment grade, it is equally true that the typical
8 utility company does not use this approach as a source of funding. To ascribe a non-existent,
9 non-traditional funding mechanism to the determination of cash working capital for Aquila’s
10 Missouri utility operations is somewhat disingenuous. On the one hand Staff wants to insure
11 that the costs associated with Aquila’s non-utility activities are not borne by utility customer.
12 At the same time they appear to want to retain the savings that arose as a result of those non-
13 traditional activities.

14 Q. Why do you say that the sale of accounts receivable is a non-traditional source of funding for
15 utilities?

16 A. I have made inquiries with a number of electric and gas utilities operating in Missouri and in
17 other states and have found none that participate in an accounts receivable sales program.

18 Q. Specifically, what companies did you contact in Missouri.

19 A. I discussed this matter with representatives from Ameren Corp., Missouri Gas Energy,
20 LaClede Gas, and The Empire District Electric Company (“Empire”). None of these
21 companies indicated that they participate in an accounts receivable sales program.

1 Q. Has the Staff ever imputed an accounts receivable sales program into the determination of the
2 collection lag for Ameren Corporation?

3 A. Not to my knowledge.

4 Q. Has the Staff ever imputed an accounts receivable sales program into the determination of the
5 collection lag for Empire?

6 A. The Staff has never made such a proposal of which I am aware. In fact, no utility in
7 Missouri, as far as I can determine, has ever had rates set assuming an accounts receivable
8 sales program was in place when it did not exist. This fact highlights my point that because
9 Aquila has been encouraged to return to a more traditional utility operation; that because
10 Aquila has embarked upon a strategy of returning to its roots as a traditional utility; and that
11 because all parties appear to agree that customers should be insulated from Aquila's past non-
12 traditional activities, it only makes sense to set rates based upon existing, traditional
13 activities. I do not understand the application of a non-traditional, non-existent source of
14 funding.

15 Q. Is it possible that Aquila could resume its accounts receivable sales program?

16 A. While it is possible, it is unlikely in the short-term. If Aquila were ever to re-establish the
17 program, that would be the appropriate time to reflect the program in the cash working
18 capital determination – the same approach that would be appropriate for every other
19 regulated utility operating in this state.

1 **MPS ACCOUNTING AUTHORITY ORDERS**

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

3 A. An AAO is an order issued by the Commission that permits the requesting utility to defer
4 certain costs on its books (outside of a rate case) with the opportunity to subsequently
5 recover these costs through rates, as opposed to being required to expense these costs in
6 the current period. The deferral of expenses lessens the impact of regulatory lag, or the
7 time between expensing the costs and the recovery of those costs in rates.

8 Q. Please discuss the AAO's issued to MPS.

9 A. In Commission Case Nos. EO-90-114 and EO-91-358, MPS requested and was granted
10 AAO's for the Sibley Rebuild Program and Sibley Western Coal Conversion Project,
11 respectively. The Sibley Rebuild Program extended the life of the three Sibley
12 generating units by 20 years, eliminating the need to build another power plant or find
13 alternative sources of energy. The Sibley Western Coal Conversion Project allowed MPS
14 to achieve significant reductions in sulfur dioxide ("SO2") emissions at the Sibley
15 Generating Station, allowing MPS to meet environmental guidelines in accordance with
16 the Clean Air Act Amendments. In addition to the above mentioned AAO's, Aquila was
17 also granted an AAO in Commission Case No. EU-2002-1053 authorizing the deferral of
18 incremental operating expenses incurred as the result of a severe ice storm that took place
19 in January 2002.

20 Q. Do you agree with Staff witness Trisha Miller's statement on page 9 lines 9-12 of her
21 direct testimony that concludes "all the deferred costs associated with the ice storm have
22 been included in this case"?

23 A. No I do not.

1 Q. Please explain.

2 A. Ms. Miller's statement is somewhat misleading. What Ms. Miller has proposed is to only
3 allow for the amortization of the deferred costs to be included in the Company's cost of
4 service yet has disallowed the Company the ability to earn an allowed rate of return on
5 the unamortized balance related to the 2002 ice storm.

6 Q. Please describe the unamortized AAO balances that Staff has included in rate base.

7 A. Staff has included in rate base the unamortized balances at September 30, 2003 for the
8 AAO deferrals associated with the Sibley Rebuild Program and the Sibley Western Coal
9 Conversion, as authorized by the Commission in Case Nos. EO-90-114 and EO-91-358,
10 respectively.

11 Q. Did Staff witness Miller discuss in her direct testimony the rationale Staff used to exclude
12 the unamortized AAO balance from rate base?

13 A. No. Staff provided no explanation as to why the Ice Storm AAO should be treated any
14 differently than MPS' Sibley Rebuild and Western Coal Conversion AAO by not
15 including the unamortized balance in rate base.

16 Q. Does MPS agree with Staff's exclusion of the unamortized deferred AAO balance related
17 to the Ice Storm from rate base?

18 A. No.

19 Q. What is MPS' proposed ratemaking treatment of the unamortized deferred AAO
20 balances?

21 A. For purposes of this rate proceeding, MPS has included the unamortized deferred AAO
22 balances at September 30, 2003 in rate base for the Sibley Rebuild Program, Western

1 Coal Conversion, in addition to the unamortized deferred balance of the 2002 Ice Storm
2 AAO.

3 Q. Please discuss MPS' rationale for including the unamortized deferred AAO balance of
4 the 2002 Ice Storm at September 30, 2003.

5 A. MPS expended the cash necessary to restore electric service to thousands of its
6 customers, upholding its obligation to provide safe and reliable service. This
7 unamortized AAO balance represents material and extraordinary costs that MPS has
8 already incurred and expended to repair broken lines, utility poles, electric meters, etc.
9 damaged by the ice storm in January 2002. To date, nearly two years after the effects of
10 the ice storm, the financial impact of the ice storm is not reflected in the utility rates that
11 MPS charges its electric customers. The inclusion of the unamortized AAO balance in
12 rate base is necessary to permit MPS to recover its full cost of investment in and repair of
13 the Missouri electric system. By not allowing the unamortized balance in rate base, the
14 Company is penalized from earning a reasonable return on its plant investment, and the
15 Company is not financially made whole.

16 Q. Did the Staff express dissatisfaction with the data provided regarding the determination
17 of the incremental expenses included in the costs deferred from the 2002 Ice Storm
18 AAO?

19 A. Yes. Based on the direct testimony of Staff witness Trisha Miller, Staff noted that it had
20 included all of the deferred costs associated with the ice storm AAO. However, this was
21 subject to change because "Aquila has been unable to provide the necessary
22 documentation justifying the deferred costs". In addition, Ms. Miller states on pages 9
23 and 10 of her testimony, "the Staff requested the necessary information and

1 documentation, as described in the above Report and Order excerpt, in Data Request Nos.
2 336.2 and 543. The responses to Data Request Nos. 336.2 and 543 did not include the
3 historical analysis necessary to determine MPS' normal ongoing levels for the costs
4 included in the deferral".

5 Q. How do you respond to her testimony?

6 A. Data request MPSC-0336.2, the information requested by Staff is as follows:

7 For the Ice Storm AAO please provide the following information:

8 (1) All components and their totals relating to the expenses incurred from the ice
9 storm. (2) Please provide description and amount of all items making up each
10 component requested in Item one. (3) The records supporting the incremental
11 expenses deferred. As described in the AAO Order EU-2002-1053 Item 4 these
12 records "shall include, but not be limited to, detailing of outside contractors, food
13 and lodging costs, labor and material cost, procedures and verification for expense
14 versus capitalization determinations, and determinations of incremental levels of
15 such costs versus normal on-going levels of costs." (4) As described in Item three
16 please identify the analysis and provide the analysis Company used to determine
17 incremental levels of such costs versus normal on-going levels of costs for each
18 component of costs.

19 Q. How did the Company answer this data request?

20 A. The Company interpreted the language to the request for an explanation of the procedures
21 used to determine the incremental levels of costs versus normal on-going levels. In
22 response to data request MPSC-0543, the Company provided to Staff on November 18,
23 2003 the procedures and calculations used to determine the incremental versus normal
24 on-going levels of expense. The calculations were provided in electronic format with all
25 formulas intact. In addition, Company personnel met with Ms. Miller on November 18,
26 2003 to explain in more detail the process and procedures that the Company used. Ms.
27 Miller's direct testimony suggests that Staff had to issue data requests MPSC-0544 and
28 MPSC-0564 because "the Company to date has failed to determine its normal operating
29 costs by analyzing costs incurred in prior years." However, this is simply not the case.

1 It should be noted that data request MPSC-0543 requesting “normal actual costs
2 compared to total costs used to compute the incremental costs...” was received on
3 November 14, 2003, the same day that the Company received data request MPSC-0544
4 requesting more specifically the actual costs for a 3-year period for expenses such as tree
5 trimming, overtime labor and outside contract costs. In addition to data request MPSC-
6 0544, Staff issued data request MPSC-0564 a few days later on November 18, 2003
7 requesting additional historical expenses by resource for years 2000-2003 in a specific
8 format. Company has responded to data requests MPSC-0544 and MPSC-0564 in the
9 format requested, in a timely manner within the due dates requested by Staff. More
10 specifically, data requests MPSC-0544 and MPSC-0564 were received by Staff on
11 December 4, 2003 and December 5, 2003, respectively. All of the data requests
12 mentioned in Ms. Miller’s direct testimony were answered and received by Staff prior to
13 filing its direct testimony on December 9, 2003. If additional information is still needed
14 by the Staff to further analyze the recovery of the costs requested in this case, the
15 Company will provide any additional information it may have upon request.

16 Q. What is the position of OPC witness Ted Robertson regarding MPS’ Accounting
17 Authority Orders?

18 A. The OPC recommends that the annual amortization costs of MPS’ AAO’s be included in
19 the Company’s cost of service, allowing a return of the actual expenses incurred from the
20 Sibley Rebuild Program, Western Coal Conversion project and the 2002 ice storm
21 damages. However, OPC recommends the disallowance of the unamortized deferred
22 AAO balances from the determination of MPS’ rate base (see page 12, lines 3-5 and page
23 13, lines 12-13 of witness Ted Robertson’s direct testimony).

1 Q. Please explain MPS' understanding of OPC's rationale for excluding from rate base the
2 unamortized deferred AAO balances?

3 A. Based on the direct testimony of witness Ted Robertson, (page 14, lines 14-17) OPC
4 believes that because MPS is being given a guaranteed "return of" the deferred expenses
5 related to the Sibley Rebuild, Western Coal Conversion and Ice Storm AAO's, the
6 Company should not be provided with a "return on" those same amounts. OPC also says
7 that the Commission's authorization of AAO treatment has the potential to insulate MPS
8 shareholders from risks associated with regulatory lag (page 15, lines 10-11).

9 Q. Does MPS agree with the recommended ratemaking treatment proposed by OPC
10 regarding unamortized deferred AAO balances?

11 A. No. Neither of those arguments appears valid.

12 Q. Please explain.

13 A. First the promised return of an investment is not a compelling reason for receiving no
14 return of that investment. I know of no one who would put money in a savings account
15 that paid no interest just because the savings account was guaranteed by the government.
16 Yet, Mr. Robertson suggests that because the Commission is guaranteeing return of our
17 investors' money, they should be happy earning no return on that investment. Second,
18 the AAO obviously does not insulate our shareholders from regulatory lag. Cash funds
19 were expended in January of 2002 and the Company was required to begin amortizing
20 those in February 2002. Our shareholders have already experienced two years of
21 regulatory lag, receiving no return of or on their investment during that period of time.
22 This lag will continue until rates are established in the current proceeding. Moreover,
23 MPS finds this treatment to be inconsistent with prior rulings of the Commission.

1 Q. Please explain.

2 A. The Commission ordered recovery of both the unamortized balance and related
3 amortization expense in Case Nos. ER-90-101 and ER-93-37. In the past four rate
4 proceedings involving MPS, Case Nos. ER-90-101, ER-93-37, ER-97-394 and ER-2001-
5 672, Staff has recommended the recovery of both the unamortized balance of AAO's and
6 related amortization expense. This issue was part of the total settlement agreement in
7 MPS' past two rate proceedings.

8 Q. Does Mr. Robertson make reference to any cases in his testimony where the Commission
9 has ruled against the inclusion of unamortized AAO balances in rate base?

10 A. Yes. Mr. Robertson cites one specific non-MPS rate case in his testimony where the
11 Commission has denied the inclusion in rate base of the unamortized deferred balances
12 associated with an AAO. The case that Mr. Robertson cited is Missouri Gas Energy
13 ("MGE"), Case No. GR-98-140. In that case, MGE included the unamortized balance of
14 the Safety Line Replacement Program ("SLRP") deferrals authorized by the Commission
15 that consisted of mains and service line replacement expenses incurred by MGE. Mr.
16 Robertson uses this case example as justification to disallow MPS AAO rate base
17 treatment.

18 Q. What is MPS' response?

19 A. The events or circumstances vary surrounding a utility's request for an AAO. The case
20 cited by Mr. Robertson is not a valid comparison to MPS' request for deferral of
21 expenses related to the January 2002 ice storm. In MPS' case, the costs incurred were of
22 an extraordinary nature.

1 Q. What has been the Commission's position on deferral of expenses with respect to
2 lessening the effect of regulatory lag?

3 A. As the Commission stated in MPS Case Nos. EO-91-358 and EO-91-360, "lessening
4 regulatory lag by deferring costs is not a reasonable goal unless the costs are associated
5 with an extraordinary event". As Mr. Robertson notes on page 17, lines 12-17 of his
6 direct testimony, the Commission has granted AAO accounting treatment for one-time
7 outlays of capital caused by unpredictable events outside the control of the utility. The
8 January 2002 ice storm, which was an extraordinary event that was unforeseen and
9 unpredictable in nature, should be given special consideration in regards to the
10 ratemaking treatment of the Company's rate base.

11 Q. Do you agree with Mr. Robertson's conclusion on page 19 lines 1-11 of his direct
12 testimony where he states "The purpose of the accounting variance is to protect MPS
13 from adverse financial impact, caused by regulatory lag, by providing it with a vehicle
14 that allows it the opportunity to capture and recover costs it normally would not have had
15 the opportunity to recover. The accounting variance should not be used to place the
16 Company in a better position than it would have been if plant investment and rate
17 synchronization been achieved. Just as it would be unfair to deny MPS recovery of its
18 reasonable and prudent investment due to regulatory delays which the Company could
19 not control, it would be unfair if MPS were allowed to reap a windfall, at the ratepayers
20 expense, due to a regulatory delay that ratepayers could not control"?

21 A. No I do not. The Company is not asking for any treatment that would result in a
22 "windfall" to the Company as Mr. Robertson portends. In fact, Mr. Robertson is
23 proposing exactly what he states would be unfair.

1 Q. Please explain.

2 A. First, MPS is not protected from adverse financial impact caused by regulatory lag
3 because the actual Order required MPS to begin the ice storm amortization in February
4 2002 before MPS had the ability to begin recovery in rates; therefore, the unamortized
5 AAO balance proposed by the Company to be included in rate base has been reduced by
6 20 months of amortization. Second, MPS would be denied its ability to recover its
7 reasonable and prudent investment due to regulatory delays that were outside the control
8 of the Company. The Company could not control the natural forces that led to the ice
9 storm as well as the costs that resulted from it to restore service to the ratepayer in the
10 most prudent and expeditious manner possible.

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BAD DEBT EXPENSE

Q. Please explain the method used by Staff witness Amanda McMellan to calculate bad debt expense for MPS electric operations.

A. For MPS' electric operations, Staff witness Amanda McMellan used an average uncollectible rate of .6587% that was calculated by multiplying the actual net write-off rates for the 3 years and nine months ending September 30, 2003. The average uncollectible rate was then multiplied by Staff's adjusted annualized level of MPS electric revenues to come up with an annualized level of bad debt expense.

Q. How does Staff's method differ from the method used by the Company?

A. The method used by Company and Staff is the same with one exception. Company used a 3-year average uncollectible rate of .8022% for MPS' electric operations which averages the actual net write-off rates for years 2000-2002.

1 Q. Why does the Company believe that a 3-year and 5-year average uncollectible rate for
2 MPS is more appropriate than the average uncollectible rate for MPS and L&P
3 calculated by Staff?

4 A. By including only the first 9 months in 2003 in the average uncollectible rate calculation,
5 Staff has arbitrarily excluded the Company's net write-offs recorded during the fourth
6 quarter of 2003. Historically, in the past two years, fourth quarter net write-offs have
7 been higher than the first three quarters. The exclusion of fourth quarter write-offs
8 results in an understatement of the total net write-offs for 2003 by approximately 50
9 percent for MPS. As such, it is not reasonable to disregard fourth quarter
10 net write-offs because this will significantly skew the average uncollectible rate.

11 **Jurisdictional Allocations**

12 Q. Please explain what you mean by jurisdictional allocations.

13 A. MPS has seven wholesale customers that are subject to Federal Energy Regulatory
14 Commission ("FERC") jurisdiction, meaning that rates are set by FERC not the
15 Commission. Since the Commission does not set rates for these customers, the cost of
16 service for these customers has to be eliminated from this case. Eliminating their cost of
17 service is completed by allocating a portion of total cost of service to the wholesale
18 customers. The method for allocating cost was addressed by Staff witness Alan Bax and
19 Company Witness Beverlee Agut in their direct testimonies.

20 Q. What are the key differences in methods used by Staff and Company?

21 A. Staff used a four coincident peak (4 CP) method for its demand allocator. This is
22 explained in detail on page 6 of Mr. Bax's direct testimony. The Company used a twelve
23 coincident peak (12 CP) method of its demand allocator.

1 Q. Are you addressing the reasons why Aquila believes 12 CP is the appropriate method to
2 allocate demand costs?

3 A. No. Although Aquila used a 12 CP method in developing its application, the difference in
4 revenue requirement is minimal. For that reason, I will agree to use the 4 CP method in
5 this case.

6 Q. What item then causes the primary difference in the allocations between Staff and the
7 Company?

8 A. The loss of the City of Odessa as a wholesale customer is the key difference. Staff has
9 included Odessa in calculating the demand factor. The Company has excluded Odessa.

10 Q. Why did Aquila exclude Odessa in calculating its demand allocation?

11 A. Odessa notified Aquila in March of 2003 that it was executing a clause in its contract to
12 discontinue service and it will no longer be a customer of Aquila beginning April 1,
13 2004. This information was known and measurable before September 30, 2003, and the
14 event takes place prior to the time the new rates established in this case will be placed
15 into effect. Odessa is the largest wholesale customer on the MPS system and causes a
16 significant reduction in the demand allocation.

17 Q. Does Odessa leaving the MPS system affect any other jurisdictional allocation factors?

18 A. Yes. It impacts all the jurisdictional allocation factors that include energy, payroll and
19 plant allocations.

20 Q. In comparison to Staff's approach, what is the revenue requirement impact of excluding
21 Odessa from the demand allocator determination?

1 A. Depending on the final outcome of the cost of service and rate base to be determined in
2 this case, properly reflecting Odessa's termination as a customer shifts approximately
3 \$1.5 million from wholesale rates.

4 Q. What would be the result that if the Commission accepts the Staff's approach of treating
5 Odessa as a customer even though it will have left the system by the time rates are in
6 effect?

7 A. MPS would be prohibited from recovering these costs after April 1, 2004 because the
8 revenue from Odessa would be gone.

9 Q. Please summarize your position on jurisdictional allocation factors.

10 A. I agree to use the Staff's method, 4 CP, instead of Aquila's 12 CP method to determine
11 the demand allocator. I believe the City of Odessa should be excluded in calculating all
12 of the jurisdictional allocation factors.

13 **Property Taxes**

14 Q. Please explain your understanding of Staff witness Trisha Miller's adjustment to
15 annualize property tax expense.

16 A. After examining property tax payments made in 2000, 2001 and 2002, Ms. Miller
17 computed a ratio of property tax payments to levels of property. This ratio was applied to
18 the net plant in service, fuel stock and material and supplies balances at December 31,
19 2002 - the end of the test year. The resulting amount was the annualized level of property
20 tax expense used by Staff in their cost of service calculation.

21 Q. How does this calculation of property tax expense compare to Aquila's calculation of
22 property tax expense?

1 A. Aquila developed a ratio of actual property tax payments in 2002 to plant in service as of
2 December 31, 2001. This ratio was applied to plant in service, fuel stock and materials
3 and supply as of September 30, 2003.

4 Q. Why did Aquila select September 30, 2003 plant in service balance?

5 A. September 30, 2003 represents the update period in this rate case proceeding in which all
6 known and measurable amounts are included in Aquila's cost of service filing. This
7 includes plant placed in service before the end of the update period. The balance at
8 September 30, 2003 represents the plant balances on which property taxes will be
9 assessed and paid on a going forward basis.

10 Q. Does Aquila believe that the plant in service balance as of September 30, 2003 should be
11 used to annualize property tax expense amounts?

12 A. Yes. Using Staff's calculation methodology, Aquila is being denied recovery of property
13 tax expense amounts associated with property that was placed in service during the
14 known and measurable time frame.

15 **Health, Dental and Vision Benefits**

16 Q. What issues do you have with Staff's determination of the ongoing level of the
17 employer's share of health, dental and vision benefits for MPS ?

18 A. The employer's share of health, dental and vision benefit annualization method employed
19 by Staff witness Dana Eaves was identical to Aquila's employer's share of health, dental
20 and vision benefit annualization method with one exception.

21 Q. Please explain that difference.

22 A. Staff witness Eaves made an adjustment to the accrual of the Company's self-insured
23 portion of health, dental and vision for MPS to reflect actual claims paid. Mr.

1 Eaves states that his adjustment corrects the historical over-accrual on the Company's
2 books for the self-insured portion of health, dental and vision, which has been higher than
3 actual costs.

4 Q. Do you agree with Mr. Eaves contention?

5 A. No. The Company's self-insured portion of its benefits is based on total Aquila
6 employees and allocated so that medical, dental and vision costs are spread over a larger
7 group rather than just the employees based in Missouri. Aquila retains the benefit
8 consulting firm, PriceWaterhouseCoopers ("PWC"), to actuarially estimate medical,
9 dental and vision expenses for Aquila's employees and dependents covered by the plans.
10 PWC uses historical actual claims plus assumptions on future medical inflation,
11 employee turnover, likelihood of catastrophic claims, etc. PWC then assigns a cost to
12 each coverage level in medical, dental and vision (e.g. single \$209 per month, employee
13 plus 1 dependent \$419 per month, and employee plus two or more dependents \$628 per
14 month). Aquila allocates the medical, dental and vision coverage cost to each state based
15 on the actual employee enrollment in each coverage level in each state (e.g. 50 employees
16 at \$209, 100 employees at \$419 and 200 employees at \$628). Aquila adjusts the
17 allocated cost each 6 months based on actual enrollment in the coverage levels. Over the
18 long term, since actual claims fluctuate from year to year, the allocation method, being
19 actuarially based, has proven to be an accurate method of allocating cost. The allocation
20 method is similar to the "smoothing method" to allocate pension expense. If Aquila just
21 used actual claims for the employees in each state, the cost per employee and state could
22 fluctuate dramatically and cost would tend to be much higher. For example, the SJLP
23 merger agreement with Aquila requires that Aquila follow the pre-merger method for

1 setting annual retiree medical cost. Consequently, the SJPL retiree population medical
2 cost is calculated independently of Aquila's other retiree population. In the last three
3 years, the SJLP pre 65 retiree medical rate has fluctuated as follows: 2002 = 8.8%
4 decrease, 2003 = 72.7% increase and 2004 = 51.3% increase.

5 **Rate Case Expenses**

6 Q. Do you have any comments regarding the Staff's adjustment to reflect rate case
7 expenses?

8 A. Yes. I generally agree with Staff witness Trisha Miller's testimony regarding rate case
9 expenses. Ms. Miller has proposed a three year amortization period of rate case expenses
10 and has suggested that because some rate case costs are directly associated with the
11 length of the case that it will be necessary to work with the Company to establish an
12 ongoing level of rate case expense. At this point, however, Staff's accounting schedules
13 reflect only those minimal incremental rate case expenses that had been reflected in our
14 accounting records at the time the Staff filed its direct testimony in early December.
15 Most of the Company's rate case expenses will be incurred as a result of pre-hearings and
16 hearings involving outside legal counsel, and expert testimony preparation from outside
17 witnesses. Currently, estimated rate cases expenses as reflected by the Company's filing
18 are more reflective of the actual costs that will ultimately be incurred than are those
19 reflected in Staff's accounting schedules.

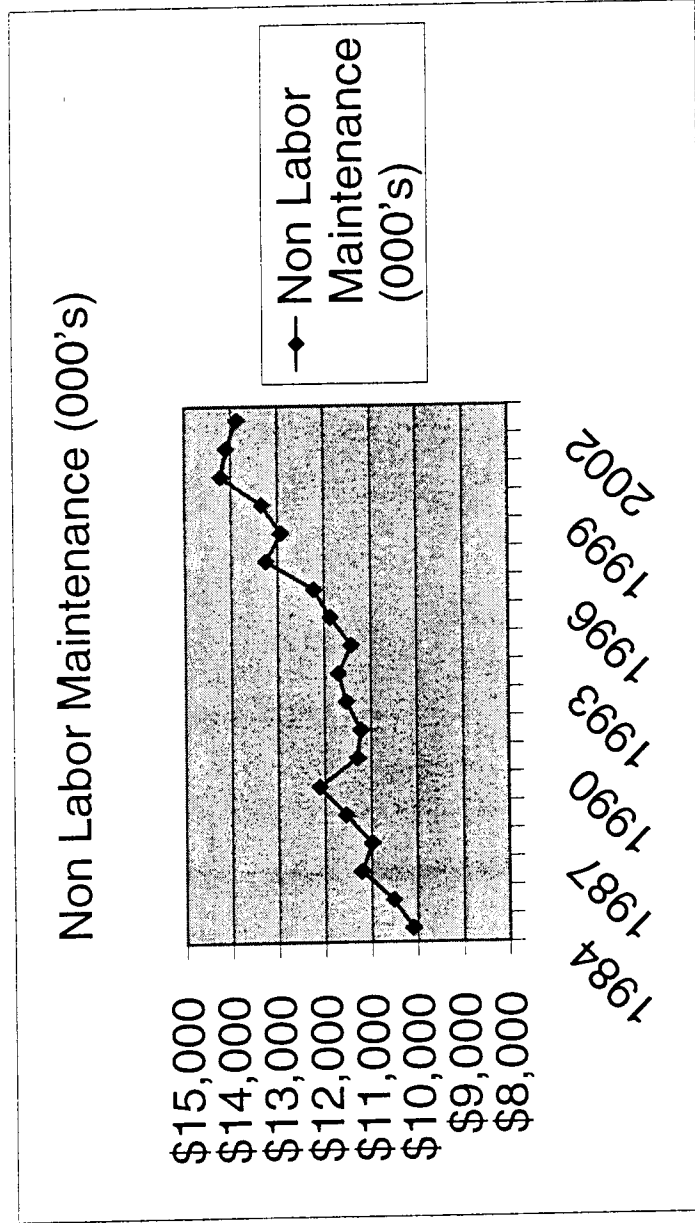
20 Q. Does this conclude your rebuttal testimony?

21 A. Yes.

Missouri Public Service Non-Labor Electric Maintenance

Rolling
5 year average

Year	Non Labor Maintenance (000's)
1984	\$ 10,104
1985	\$ 10,525
1986	\$ 11,216
1987	\$ 10,993
1988	\$ 11,545
1989	\$ 12,117
1990	\$ 11,296
1991	\$ 11,220
1992	\$ 11,530
1993	\$ 11,695
1994	\$ 11,422
1995	\$ 11,861
1996	\$ 12,227
1997	\$ 13,243
1998	\$ 12,923
1999	\$ 13,333
2000	\$ 14,225
2001	\$ 14,108
2002	\$ 13,874



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 [REDACTED]

Case No. ER-2004-0034

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

[REDACTED]

County of Jackson)
State of Missouri)

ss

AFFIDAVIT OF DENNIS R. WILLIAMS

Dennis R. Williams, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony of Dennis R. Williams;" 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.

Dennis R. Williams
Dennis R. Williams

Subscribed and sworn to before me this 26th day of January, 2004.

Terry D. Lutes
Notary Public
Terry D. Lutes

My Commission expires:
8-20-2004

