

TAX STUDY

All Parties agree that Aquila first implemented Staff's method for calculating straight-line tax depreciation with the effective date of Case No. ER-97-394. MPS will continue for purposes of this Stipulation and Agreement to calculate straight-line tax depreciation in accordance with Staff's method.

Aquila agrees to undertake a study to develop the level of detail needed to assess the best methodology to determine the regulated income tax expense of its MPS operations for Missouri ratemaking purposes. A specific outcome of the study is to create a mutually agreeable basis for the determination of the future adjustment to the amount of regulated book depreciation expense included in a cost of service study that should be used as a tax deduction for ratemaking purposes.

Aquila proposes that the study be conducted in at least two stages. The study will use plant balances as of December 31, 2002 for study purposes. Progress on the first phase of the study will be reviewed with Staff no later than September 30, 2004. This date does not preclude the Company from reviewing with Staff its progress or seeking Staff's input on the study at earlier dates. The purpose of the preliminary study is to address several of the major items, provide a preliminary view of the results, assess the time and resources required, and allow both the Staff and the Company to identify additional items that may require assessment in the next stage. In the initial phase of the study, the Company will:

- Quantify the basis differences deducted by year.
- Quantify the allowance for funds used during construction ("AFUDC") equity capitalized for book by year.

- Determine the ratio of original book plant in service to current book plant in service by year.
- Identify book depreciation rates by year.
- Quantify remaining undepreciated tax basis.
- Quantify remaining undepreciated book basis.
- Calculate the “gross up” of accumulated deferred taxes by dividing by the appropriate tax rates.
- Calculate required vs. recorded accumulated deferred income taxes.
- Prepare, with input from Staff, a prioritized list of issues unresolved by the preliminary study.
- Prepare a timetable for delivery of the next stage.

The study will incorporate the following outline for Phase 1 in order to identify the items that will be addressed to arrive at study’s desired outcome.

1) The difference between the book and tax basis of the property by year the property was first placed in service.

a) The individual items that make up that difference.

i) The individual items that are permanent differences between tax and book basis of property.

ii.) The individual items that are differences between tax and book basis of property that are recognized in different periods.

a.) The differences that result in the book basis being greater than the tax basis.

b.) The differences that result in the tax basis being greater than the book basis.

b) For the 1.(a)ii. items that have at one time had their tax consequences treated under the flow-through method for determining the amount of regulated income tax expense to be used to establish rates.

i.) The time period that each item was treated using flow-through method.

ii.) The amount for each item that was flow-through to consumers by relevant tax rate.

2) The difference in methods used to determine the amount of book depreciation expense versus the method used to determine the amount of straight-line tax depreciation used to calculate regulated income tax expense.

A) Book rate versus Guideline Line rate.

B) Open ended accounting versus close-end accounting.

C) Recording of Retirements

D) Other Differences

E) 2A. through 2D. for method differences that have at one time been used to calculate regulated depreciation expense differently than the straight-line tax depreciation amount used to determine the amount of regulated income tax expense for the establishment of rates.

i) The time period that each type method difference was used for book and straight-line tax purposes.

- ii) The amount of the difference that was used to establish rates to consumers by relevant tax rate.
- 3) Identify sources of data relevant to Phase 1 of the study.
 - A) Property records system.
 - B) Income tax system.
 - C) Schedule M per Annual Tax returns.
 - D) Workpapers identified from any regulatory proceedings.
 - E) Straight-line tax schedules.
 - F) Other.

Staff and Company acknowledge that in a study of this type, limitations in the available records may exist. In the event such limitations exist, Staff and Company will work together to suggest reasonable and mutually acceptable solutions. The Staff method used to calculate the tax deduction for book depreciation in the calculation of regulated income tax expense in this case will continue to be used in future rate cases until this study is completed or another method is mutually agreed upon.

Staff agrees to join Aquila in letter requesting a private letter ruling from the IRS that the method that Aquila has been using for computing straight-line tax depreciation does not violate the normalization requirements of the IRS code – the language in the letter to the IRS must be approved by the Staff prior to the letter being submitted to the IRS.