

Exhibit No.:
Issue: Rate Base, Income
Statement Adjustments,
Plant and Reserve
Adjustments
Witness: Leslie L. Lucas
Sponsoring Party: MoPSC Staff
Type of Exhibit: Direct Testimony
Case No.: GR-2001-292
Date Testimony Prepared: April 19, 2001

MISSOURI PUBLIC SERVICE COMMISSION
UTILITY SERVICES DIVISION

DIRECT TESTIMONY
OF
LESLIE L. LUCUS

MISSOURI GAS ENERGY,
A DIVISION OF SOUTHERN UNION COMPANY

CASE NO. GR-2001-292

Jefferson City, Missouri
April 2001

Exhibit No. 23
Date 6-25-01 Case No. GR-2001-
Reporter Hewitt

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LESLIE L. LUCUS**

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DIRECT TESTIMONY
OF
LESLIE L. LUCUS
MISSOURI GAS ENERGY
A DIVISION OF SOUTHERN UNION COMPANY
CASE NO. GR-2001-292

Q. Please state your name and business address.

A. Leslie L. Lucas, Missouri Public Service Commission, Governor Office Building, 200 Madison Street, Jefferson City Missouri 65101.

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

A. I am a Regulatory Auditor for the Missouri Public Service Commission (Commission).

Q. Please describe your educational and employment background.

A. I graduated from Lincoln University in May 1995 with a Bachelors degree in Accounting. In July 1999, I became an associate member of The Association of Certified Fraud Examiners. I commenced employment with the Commission Staff (Staff) in August 2000.

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

A. I am responsible for assisting in the audits and examinations of the books and records of utility companies operating within the state of Missouri.

Q. Have you previously filed testimony before this Commission?

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1 A. Yes, I have previously filed testimony in Case No. WR-2000-844,
2 St. Louis County Water Company.

3 Q. With reference to Case No. GR-2001-292, have you made an examination
4 of the books and records of Missouri Gas Energy (MGE or Company)?

5 A. Yes, in conjunction with other members of the Staff.

6 Q. What is the purpose of your direct testimony?

7 A. The purpose of my direct testimony is to describe the various rate base
8 components and adjustments to the Company's income statement and plant records that
9 I am sponsoring in this case.

10 Q. Please list the Accounting Schedules you are sponsoring.

11 A. I am sponsoring the following Accounting Schedules:

12 Accounting Schedule 2- Rate Base

13 Accounting Schedule 3- Total Plant in Service

14 Accounting Schedule 4- Adjustments to Total Plant

15 Accounting Schedule 5- Depreciation Expense

16 Accounting Schedule 6- Depreciation Reserve

17 Accounting Schedule 7- Adjustments to Depreciation Reserve

18 Q. Please describe Accounting Schedule 2, Rate Base.

19 A. Accounting Schedule 2 identifies the rate base components for MGE.
20 Additions to rate base include plant in service (less depreciation reserve) and other
21 investments such as working capital (materials and supplies, gas inventories and
22 prepayments). Offsets or reductions to rate base include cash working capital, deferred
23 taxes and other capital which is cost free to MGE, such as customer deposits and

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1 customer advances. I am sponsoring the Total Plant in Service, Depreciation Reserve
2 and Materials and Supplies Inventory rate base components.

3 **Rate Base**

4 Q. What Staff witnesses are sponsoring the remaining rate base components?

5 A. Staff Accounting witness Graham Vesely is sponsoring Cash Working
6 Capital (Accounting Schedule 8), Federal and State Tax Offsets and Interest Expense
7 offset. Staff witness Mike Wallis of the Procurement Analysis Department is sponsoring
8 Gas Inventory. Staff Accounting witness Charles R. Hyneman is sponsoring
9 Prepayments, Alternative Minimum Tax Credit, Customer Advances for Construction,
10 Customer Deposits, Deferred Taxes on Allocated Plant, Deferred Taxes on Direct Plant,
11 and Rate Base Offset per GM-94-40. Staff Accounting witness Mark L. Oligschlaeger is
12 sponsoring deferred income taxes related to MGE's Service Line Replacement
13 Program (SLRP) Accounting Authority Order (AAO) Nos. GO-94-234, GO-97-301 and
14 GR-98-140, as well as the Year 2000 (Y2K) AAO in Case No. GO-99-258. Staff
15 Accounting witness Janis E. Fischer is sponsoring Prepaid Pension Asset.

16 Q. Please describe how the Staff calculated the rate base component of
17 Materials and Supplies.

18 A. The Staff determined that the December 31, 2000 balance is the
19 appropriate amount to include in rate base for this component. This is the latest month in
20 the test year period in this case.

21 Q. Why was the balance at the end of the test year period of December 31,
22 2000 used for Materials and Supplies?

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1 A. The ending balance as of December 31, 2000 was used because the Staff's
2 review of the month end account balances for the past 36 months shows a downward
3 trend in the inventory levels maintained by MGE. The most current balance in this
4 account is a more representative level of investment on a going-forward basis.

5 Q. Please explain the Accounting Schedules for Plant in Service,
6 Depreciation Reserve and Depreciation Expense.

7 A. Accounting Schedule 3, Total Plant in Service, lists in Column B MGE's
8 per book plant balances by FERC Uniform System of Accounts (FERC account) at the
9 end of the December 31, 2000 test year, corporate allocated Plant and MGE's projected
10 increases in Plant through June 30, 2001. June 30, 2001 is the end of the Staff's
11 recommended true-up period in this case. The Staff's Plant adjustments (detailed in
12 Accounting Schedule 4, Adjustments to Total Plant) are listed in Columns C and E and
13 the Staff's recommended plant balances adjusted for known and measurable changes
14 through the end of the test year are shown in Column F. Accounting Schedule 4,
15 Adjustments to Total Plant, provides a brief description of the individual adjustments
16 listed in Column E of Accounting Schedule 3.

17 Accounting Schedule 5, Depreciation Expense, lists in Column B the
18 adjusted plant in service balances from Accounting Schedule 3, Column F. Column C
19 lists the current Commission approved and/or Staff proposed depreciation rates
20 (see testimony of Staff witness Paul Adam), which are applied to each FERC account.
21 The rates in Column C are then applied to the plant balances in Column B to determine
22 the annualized level of depreciation expense that appears in Column D. The total
23 depreciation expense is taken to Accounting Schedule 9, Income Statement.

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Accounts 301 Leasehold Improvements, and 303 Miscellaneous Intangible Plant, have a zero depreciation rate because these accounts are being amortized to Account 404, Amortization Expense.

Accounting Schedule 6, Depreciation Reserve, lists in Column B, MGE's per book depreciation reserve balances by FERC account as of December 31, 2000. Also included in the depreciation reserve for corporate allocated Plant and the estimated increase in reserve through June 30, 2001. The Staff's Reserve adjustments (listed in Accounting Schedule 7, Adjustments to Depreciation Reserve) are listed in Columns C and/or E and the Staff's adjusted balances through December 31, 2000 are shown in Column F. Accounting Schedule 7 provides a brief description of the individual adjustments listed in Column E of Schedule 6.

Income Statement Adjustments

Q. What Income Statement adjustments are you sponsoring?

A. I am sponsoring the following adjustments that are incorporated in Accounting Schedule 9, Income Statement. These adjustments are individually listed on Accounting Schedule 10, Adjustments to Income Statement: S-41.1, S-45.4, S-52.3, S-56.1, S-57.1 and S-57.3

Q. Please explain adjustments S-41.1, S-45.4 and S-52.3 listed on Accounting Schedule 10, Income Statement.

A. These adjustments remove certain advertising costs from MGE's cost of service.

Q. Please describe the past treatment of advertising expenses by the Commission.

1 A. As part of Re: Kansas City Power and Light Company, 28 Mo.P.S.C.
2 (N.S.) 228 (1986) (KCPL), the Commission adopted an approach that classifies
3 advertisements into five categories and provides separate rate treatment for each
4 category. The five categories of advertisements adopted by the Commission for purposes
5 of this approach are:

- 6 1. General-informational advertising that is useful in the provision of
7 adequate service;
- 8 2. Safety-advertising which conveys the ways to use the Company's
9 service safely and to avoid accidents;
- 10 3. Promotional-advertising used to encourage or to promote the use of the
11 particular commodity the utility is selling;
- 12 4. Institutional-advertising used to improve the Company's public image;
13 and,
- 14 5. Political-advertising which is associated with political issues.

15 The Commission adopted these categories of advertisements because it
16 believed that a utility's revenue requirement should include the reasonable and necessary
17 cost of general and safety ads, should disallow the cost of institutional or political ads and
18 should include the cost of promotional ads only to the extent that the utility can provided
19 cost justification for the ad (KCPL, pp. 269-271).

20 Q. What standard did the Staff apply to evaluate the Company's advertising
21 expense in this Case?

22 A. The Staff applied the standards as initially established in KCPL, and
23 utilized in subsequent cases, to determine the test year level of advertising expense for
24 the general, safety, institutional, promotional and political categories of advertising. The
25 Staff is proposing to disallow advertisements that are found to be institutional,

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1 promotional, unrelated to the gas industry or which ask for charitable dues and donations.
2 The Staff allowed all general and safety-related advertisements to the extent that they
3 were related to the gas industry and beneficial to Missouri ratepayers.

4 Q. How did Staff apply the KCPL standard to the examination of advertising
5 expense in this case?

6 A. Staff categorized all of the Company's advertisements using the KCPL
7 standard. The process began by reviewing the ads that the Company supplied, accounts
8 payable vouchers, billing company's invoices and explanations given by MGE for the
9 advertisements to determine which of the following "primary messages" the Company
10 designed the advertisement to communicate:

- 11 1. the promotion of a service or product (Promotional);
- 12 2. the dissemination of information necessary to obtain safe and
- 13 adequate gas service (General and Safety);
- 14 3. the promotion of the Company image (Institutional); or
- 15 4. the endorsement of a political candidate or any political message
- 16 (Political).

17 Once the primary message was determined, the advertisement was
18 classified accordingly.

19 The Staff requested that the Company supply the cost of all
20 advertisements on a per-advertisement basis. Based on its categorization, the Staff
21 removed the expenses associated with advertisements that were classified as institutional
22 or promotional, as well as general advertisements unrelated to the gas industry or
23 Missouri ratepayers.

24 Q. What media does the Company utilize to place their advertisements?

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1 A. The Company mainly uses the following media to place their
2 advertisements:

- 3 1. Radio
- 4 2. Print (Newspaper)
- 5 3. Other Print

6 Q. Please describe the promotional advertisements which the Staff removed
7 from MGE's cost of service.

8 A. Staff removed the following advertisements as promotional in nature:

9 Corporate Challenge t-shirts, MGE yellow logo lollipops-Corporate
10 Challenge, Corporate Challenge youth t-shirts, MGE advertisement in Barton Chamber of
11 Commerce Map, Smart Choice advertisements, booth rental at ASHRAE education day,
12 ad in Home Builders Association Magazine, MGE ad in Greater Kansas City Chamber of
13 Commerce Directory, MGE Logo Towels- Home Builders Association Golf Tournament.

14 Q. What types of institutional advertising did the Staff remove?

15 A. The Staff removed MGE radio holiday greetings and a
16 "Philanthropic Profile" in Ingram's magazine.

17 Q. Please explain adjustment S-57.3.

18 A. This adjustment amortizes the debit depreciation reserve balance in
19 Account 395, laboratory equipment, over five years. MGE has retired all laboratory
20 equipment plant in service, but maintains a debit reserve balance on its books. This
21 adjustment allows MGE to remove this reserve balance from its books and recover the
22 under accrual associated with this account.

23 Q. Please describe adjustment S-56.1 and S-57.1.

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1 A. Adjustment S-56.1 annualizes depreciation expense based on 1) MGE
2 plant in service at December 31, 2000, 2) corporate allocated plant, and, 3) MGE's
3 projected increase in plant through June 30, 2001. Adjustment S-57.1 annualizes the
4 amortization expense related to Account 303 Miscellaneous Intangible Plant, and
5 Accounts 375.2 and 390.2, Leasehold Improvements.

6 **Plant and Reserve Adjustments**

7 Q. What Plant adjustments are you sponsoring?

8 A. I am sponsoring the following Plant adjustments incorporated into
9 Accounting Schedule 3, Total Plant in Service. These adjustments listed on Accounting
10 Schedule 4, Adjustments to Total Plant, are: P-6, P-8, P-9, P-10, P-11.1, P-11.2, P-12,
11 P-13, P-14, P-15, P-18.1, P-18.2, P-19, P-20.1, P-20.2, P-23, P-27, P-28, P-46, P-47
12 and P-48.

13 Q. What Reserve adjustments are you sponsoring?

14 A. I am sponsoring Reserve adjustments R-11, R-24 and R-40.

15 Q. Please explain Plant adjustments P-6, P-8, P-9, P-10, P-11.2, P-12, P-13,
16 P-14, P-15, P-18.1, P-19, P-20.1, P-23, P-27 and P-28.

17 A. These adjustments recognize plant that was in service at December 31,
18 2000, but not yet properly classified to specific plant accounts.

19 Q. Please explain Plant adjustments P-46, P-47 and P-48.

20 A. These adjustments reflect the additions of MGE's projected increase in
21 Plant in Service from December 31, 2000 through June 30, 2001.

22 Q. Please explain Plant adjustment P-18.2.

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1 A. This adjustment capitalizes the cost of installing a sink and water heater at
2 an MGE facility. The Staff believes MGE incorrectly charged this cost to expense, as this
3 cost should provide benefits over several years.

4 Q. Please explain adjustment P-20.2.

5 A. This adjustment capitalizes the cost to refinish office furniture. The Staff
6 believes this cost increases the service life of the furniture and therefore should be
7 capitalized instead of expensed.

8 Q. Please explain Plant adjustment P-11 and Reserve adjustment R.11.

9 A. These adjustments reflect the retirement of inactive meters from MGE's
10 Account 380, Services.

11 Q. Please explain Reserve adjustment R-24.

12 A. This adjustment removes the debit reserve balance in Account 395,
13 Laboratory Equipment. The Staff is proposing that MGE be allowed to recover this
14 amount through a five-year income statement amortization.

15 Q. Please explain Reserve adjustment R-40.

16 A. This adjustment increases MGE's depreciation reserve by one-half of the
17 Staff's annualized level of depreciation to estimate the reserve at June 30, 2001.

18 Q. Does this conclude your direct testimony?

19 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In The Matter of Missouri Gas Energy's Tariff)
Filing For General Rate Increase) Case No. GR-2001-292

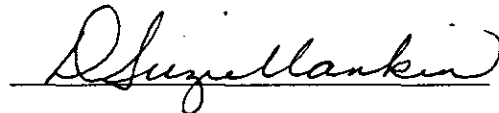
AFFIDAVIT OF LESLIE L. LUCUS

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Leslie L. Lucas, being of lawful age, on her oath states: that she has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 10 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.


Leslie L. Lucas

Subscribed and sworn to before me this 18th day of April 2001.



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