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Issues: Depreciation; Cost of Removal;
Production Plant Retirement Dates
Witness Rosella L. Schad, PE
Sponsoring Party: MoPSC Staff
Type of Exhibit: Surrebuttal Testimony
Case No.: ER-2004-0034

Date Testimony Prepared: February 13, 2004 as modified February 27, 2004

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

ROSELLA L. SCHAD, PE

AQUILA, INC.

d/b/a AQUILA NETWORKS-MPS (Electric)

CASE NO. ER-2004-0034

FILED³

MAY 10 2004

**Missouri Public
Service Commission**

*Jefferson City, Missouri
February 2004*

Exhibit No.	1103 & 1146
Case No(s)	ER-2004-0034
Date	3-1-04 Rptr JY

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of Aquila, Inc. d/b/a Aquila Networks)
L&P and Aquila Networks MPS to implement a) Case No. ER-2004-0034
general rate increase in electricity.)

AFFIDAVIT OF ROSELLA L. SCHAD, PE

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

Rosella L. Schad, PE, of lawful age, on her oath states: that she has participated in the preparation of the following surrebuttal testimony as modified on February 27, 2004, in question and answer form, consisting of 22 pages to be presented in the above case; that the answers in the following surrebuttal testimony as modified on February 27, 2004, 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.

Rosella L. Schad, PE
Rosella L. Schad, PE

Subscribed and sworn to before me this 27th day of February 2004.



Toni M. Charlton
Notary Public

TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004

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13
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15

TABLE OF CONTENTS
SURREBUTTAL TESTIMONY OF
ROSELLA L. SCHAD, PE
AQUILA, INC.
d/b/a AQUILA NETWORKS-MPS (Electric)

CASE NO. ER-2004-0034

IMPACT OF THE COMPANY’S PROPOSED DEPRECIATION RATES.....2
INCOME TREATMENT VS RATE BASE TREATMENT.....9
FINAL RETIREMENT OF LIFE SPAN PLANT17
QUANTIFICATION OF THE COMPONENTS OF THE COMPANY’S DEPRECIATION
RATES.....19
RELATIONSHIP OF DEPRECIATION TO CUSTOMER QUALITY OF SERVICE.....20

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
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22
23

SURREBUTTAL TESTIMONY
OF
ROSELLA L. SCHAD, PE
AQUILA, INC.
d/b/a AQUILA NETWORKS-MPS (Electric)

CASE NO. ER-2004-0034

Q. Please state your name and business address.

A. Rosella L. Schad, P. O. Box 360, Jefferson City, MO 65102.

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

A. I am employed by the Missouri Public Service Commission (Commission) as an Engineer in the Engineering and Management Services Department.

Q. Are you the same Rosella L. Schad who has previously filed direct and rebuttal testimonies on behalf of the Staff of the Missouri Public Service Commission in this case?

A. Yes.

Q. What is the purpose of your surrebuttal testimony?

A. I will respond to the Company's position on depreciation and cost of removal. Specifically, I will respond to the rebuttal testimonies of Ronald E. White, the Company's depreciation consultant and Company witnesses, Keith G. Stamm, H. Davis Rooney, and Susan D. Abbott.

Q. What are the issues in depreciation and cost of removal that you will address?

A. I will address:

Surrebuttal Testimony
Rosella L. Schad, PE

- 1 ▪ Impact of the Company's Proposed Depreciation Rates
- 2 ▪ Rate Base Treatment vs. Income Treatment
- 3 ▪ Final Retirement of Life Span Plant
- 4 ▪ Quantification of Company's Depreciation Rate Component Issues
- 5 ▪ Relationship of Depreciation to Customer Quality of Service

6 Q. Why are these issues that need addressing?

7 A. These issues need addressing because the Company's positions on these issues
8 increase depreciation expense and increase the Company's revenue requirement without a
9 known and measurable associated cost.

10 **IMPACT OF THE COMPANY'S PROPOSED DEPRECIATION RATES**

11 Q. Do you agree with the impact of Mr. White's presentation of the Company's
12 and Staff's proposed depreciation rates for MPS as provided in his rebuttal testimony?

13 A. No. The difference between Company's proposed depreciation rates for MPS
14 and Staff's proposed depreciation rates for MPS are attributed to three specific areas. As
15 shown in Table 1, the amount of annual depreciation expense proposed by the Company is
16 approximately \$45.5 million based on plant balances on September 30, 2003. Staff's
17 proposed depreciation expense on these same plant balances is approximately \$32 million.
18 Mr. White's depreciation rates result in \$13.5 million more annual accrual than Staff's
19 depreciation rates.

20 Q. What are the areas of differences for depreciation expense between Staff and
21 Mr. White for MPS?

22 The three specific areas of differences are depreciation expense for cost of removal
23 (cost of removal), service lives, and amortization of the accumulated depreciation reserve.

Surrebuttal Testimony
 Rosella L. Schad, PE

1 The Company's proposed annual depreciation expense for cost of removal is approximately
 2 \$7 million. The Staff has no cost of removal in depreciation rates; Staff proposes to expense
 3 cost of removal. The Company's proposed annual depreciation expense for service lives is
 4 approximately \$6.5 million more than Staff. Finally, the Company's overall proposed net
 5 reserve amortization of the accumulated depreciation reserve is approximately \$0.

6 In aggregate, the Company's proposed annual depreciation expense for MPS is
 7 approximately \$13.5 million more than Staff's, although Staff's proposes an expense amount
 8 for cost of removal of approximately \$1.5 million, as supported by Staff witness,
 9 Cary G. Feathertone in his direct testimony. The net difference between Company and Staff
 10 for depreciation and cost of removal is approximately \$12 million.

11 **COMPARISON OF MPS ANNUAL DEPRECIATION EXPENSE (\$ MILLIONS)**

	1	2	3	4
	Annual Accrual (Ordered ER-97-394 Depreciation Rates) (\$ 12/31/01)	Annual Accrual (Ordered Depreciation Rates) (\$ 9/30/03)	Annual Accrual (Staff Proposed Depreciation Rates) (\$ 9/30/03)	Annual Accrual (Company Proposed Depreciation Rates) (\$ 9/30/03)
Dep. Exp. Service Lives	34.5	32.6	32	38.5
Dep. Exp. Net COR	14.5	0	0	7
Total Depreciation Exp.	49	32.6	32	45.5
Net COR Exp.	0	0.9	1.5	0
Total	49	33.5	33.5	45.5

Annual Difference between Company and Staff = [4] - [3] = \$12 Million

Surrebuttal Testimony
Rosella L. Schad, PE

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Q. What is the total net difference annually between the Company and Staff for the Company's total annual depreciation and annual net cost of removal?

A. The total net difference annually between the Company and Staff for the Company's total depreciation and cost of removal is \$12 million for MPS.

Q. Is Mr. White's statement in his rebuttal testimony on page 3, lines 8-10, identifying the impact of Staff's proposed depreciation rates relative to current depreciation expense levels based on September 30, 2003 plant balances?

A. No.

Q. Concerning MPS, will you provide an impact analysis of Staff's proposed annual depreciation expense for plant balances as of September 30, 2003, including Staff

Surrebuttal Testimony
Rosella L. Schad, PE

1 proposed annual net cost of removal, in comparison to currently ordered depreciation rates
2 and annual cost of removal expensed?

3 A. Yes. Staff's proposed depreciation rates generate approximately \$32 million
4 annually and annual net cost of removal is approximately \$1.5 million, for a total of
5 \$33.5 million. In comparison, current depreciation rates generate approximately
6 \$32.6 million, and together with current annual net cost of removal allowed of approximately
7 \$0.9 million, (Schedule 1) equals \$33.5 million. The impact of Staff's proposed depreciation
8 rates and cost of removal expense when compared to currently ordered depreciation rates and
9 net cost of removal is, therefore, \$0.

10 Q. Does using Mr. White's depreciation rates with cost of removal included in
11 the formula create increased levels of annual depreciation expense as plant balances grow?

12 A. Yes.

13 Q. Company witness, H. Davis Rooney's states in his rebuttal testimony, page 6,
14 lines 21-22, "This accrual level of net salvage previously recommended by Staff is about
15 40% of Staff's recommended depreciation rates in this case. I believe a \$13 million per year
16 change in cash flow and a 40 % change in depreciation is noteworthy." Do you agree with
17 Mr. Rooney with regard to the level of cash flow for cost of removal for MPS in this case?

18 A. No. As I indicated above, the level of depreciation expense for cost of
19 removal, based on the Company's depreciation rates, is approximately \$7 million.
20 Subtracting from \$7 million the net cost of removal expense, \$1.5 million, proposed by Staff
21 in this case, the reduction for net cost of removal for MPS in this case is \$5.5 million. Rather
22 than a \$13 million per year change in cash flow for cost of removal, the difference between
23 the Company and Staff is actually \$5.5 million.

Surrebuttal Testimony
Rosella L. Schad, PE

1 Q. Why is the level for cost of removal in this case not the \$13 million that
2 Mr. Rooney notes in his rebuttal testimony?

3 A. A reduction of \$13 million for cost of removal occurred in Case
4 Nos. ER-2001-672 and EC-2002-265. The net salvage rates included in the ordered
5 depreciation rates from a prior case, Case No. ER-97-394, were not included in the
6 depreciation rates in the ordered Stipulation and Agreement from Case Nos. ER-2001-672
7 and EC-2002-265. Mr. Rooney's figure is based on the earlier case, ER-97-394.

8 Q. Is there a record that explicitly states that a reduction in depreciation expense
9 occurred as a result of the last Company rate case?

10 A. Yes. On page 9 of the Company's December 31, 2002, 10-K, it is stated
11 under "Regulation": "In February 2002, we reached a negotiated settlement with the
12 Commission staff and all intervenors that resulted in a \$4.3 million annual rate reduction.
13 The rate reduction was driven primarily by a \$16.0 million reduction in depreciation which
14 reduced our cash flow but had little impact on earnings."

15 Q. Is Staff's proposal for depreciation expense and cost of removal expense in
16 this case, ER-2004-0034 based on September 30, 2003,
17 plant balances, effectively no increase or decrease from current revenues for MPS?

18 A. Yes.

19 Q. Does Mr. White's proposed depreciation rates and depreciation expense based
20 on September 30, 2003, plant balances provide for an approximately \$12 million increase
21 from current revenues for MPS?

22 A. Yes.

Surrebuttal Testimony

Rosella L. Schad, PE

1 Q. Mr. White refers to his understanding of the evolution of net salvage
2 advocated by Staff in this proceeding, pages 20-21, of his rebuttal testimony, "To my
3 knowledge, the earliest attempt by Staff to deliberately reduce depreciation expense by
4 adjusting net salvage rates was introduced with a novel formulation of a whole-life
5 depreciation rate designed to provide an allowance for net salvage equal to the average
6 realized net salvage observed over a recent band of years." Is his reference to Staff's novel
7 formulation relative to Case No. GR-98-324 accurate?

8 A. No. I noted in my rebuttal testimony on page 14 that Staff depreciation
9 engineer, Melvin T. Love, approached these same concerns over ten years ago in the same
10 manner in Case No. ER-93-37 regarding the level of costs of removal and salvage that is
11 being accrued through depreciation rates relative to the actual amounts that are booked.
12 Staff's approach is proper ratemaking, rather than a novel formulation of the whole life
13 depreciation rate.

14 In addition, Company witness Rooney notes on page 9, lines 17-20, "In Aquila's Case
15 No. ER-90-101, Staff witness Melvin Love described in his Direct Testimony a methodology
16 to recover a five-year average level of net salvage through the depreciation rate. The
17 Commission adopted his recommendations."

18 Beginning at least 15 years ago, Staff has testified that the amount collected for net
19 cost of removal should equal the current level of net cost incurred.

20 Q. What is Staff's conclusion on the impact of the Company's Proposed
21 Depreciation Rates for MPS?

22 A. Staff's conclusion is that the impact of the Company's Proposed Depreciation
23 Rates for MPS is to charge the customers for costs that are not known and measurable, and to

Surrebuttal Testimony
Rosella L. Schad, PE

1 provide depreciation and cost of removal expense that exceed current costs by a total of
2 \$12 million.

3 While Mr. White recognizes the need to reduce the accumulated depreciation reserve
4 because past depreciation rates were too high, he is still proposing to charge customers \$5.5
5 million more annually for net cost of removal expenses than MPS is actually incurring.

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20 Q. What is Staff's recommendation for depreciation rates for the Company?

21 A. Staff's recommendation is that the Commission order Staff's proposed
22 depreciation rates, based on Staff's ASLs, as shown in Schedule 3-1 attached to my direct
23 testimony, be effective on the date of the Commission's order in this case.

1 **INCOME TREATMENT VS RATE BASE TREATMENT**

2 Q. How does Mr. Rooney's statement on page 5, lines 6-10, regarding the
3 recording of net salvage as prescribed by Commission rules limit the treatment of cost of
4 removal for ratemaking purposes?

5 A. According to 4CSR 240-20.030(4), in prescribing this system of accounts, the
6 commission does not commit itself to the approval or acceptance of any item set out in any
7 account for the purpose of fixing rates or in determining other matters before the
8 commission. The treatment of net salvage cost as an expense is possible for ratemaking
9 purposes. Thus, the Commission's rules addressing cost of removal relates to the reporting
10 of this item, not the ratemaking treatment of it.

11 Q. Can Staff provide instances when utilities received authority for exceptions to
12 the prescribed Uniform System of Accounts (USOA) accounting procedures?

13 A. Staff witness Cary G. Featherstone will address this issue in his surrebuttal
14 testimony.

15 Q. Have there been any Commission orders that directed a company to treat cost
16 of removal as an expense?

17 A. Yes. In the Stipulation & Agreement in Case Nos. ER-2001-672 and
18 EC-2002-265, the Company was directed to record "net salvage" as an expense.

19 Q. Will you present and summarize the five key points of the issue of where to
20 book cost of removal and salvage for ratemaking purposes?

21 A. Yes.

- 22 ○ Is there a requirement that the net cost of removal component must be
23 included in the depreciation rates?

Surrebuttal Testimony
Rosella L. Schad, PE

- 1 • There is not a requirement that depreciation rates include a net cost of removal
2 component.
- 3 ○ Is there a requirement that the proposed net cost of removal amount be booked
4 to the accumulated depreciation reserve?
- 5 • There is not a requirement that proposed net cost of removal or salvage be
6 booked to the accumulated depreciation reserve.
- 7 ○ Is there a requirement that the actual cost of removal and salvage amounts be
8 booked to the accumulated depreciation reserve?
- 9 • There is not a requirement that actual cost of removal and salvage amounts be
10 booked to the accumulated depreciation reserve.

11 *INCOME TREATMENT: Staff will refer to treatment of cost of removal that is*
12 *not booked to the accumulated depreciation reserve as the Income Treatment.*
13 *(See Schedule 2)*

14 The effect of this treatment will be discussed later.

- 15 ○ If neither proposed net cost of removal amount, nor actual net cost of removal
16 and salvage amounts are booked to the accumulated depreciation reserve,
17 where is each booked?
- 18 • If neither the proposed net cost of removal amount nor actual cost of removal
19 and salvage amounts are booked to the accumulated depreciation reserve:
- 20 1. When billed to the customer, the proposed net cost of removal is
21 booked as a debit to Accounts Receivable and as a credit to Revenue.
- 22 2. When the revenue is collected from customers, it is booked as a debit
23 to Cash and a credit to Accounts Receivable.

Surrebuttal Testimony
Rosella L. Schad, PE

1 3. When actual salvage is received, the actual salvage is a debit to Cash
2 and a credit to Revenue.

3 4. When actual cost of removal is incurred, it is a debit to Expense and a
4 credit to Cash.

5 *RATE BASE TREATMENT: Staff will refer to treatment of cost of removal that is*
6 *booked to the accumulated depreciation reserve as the Rate Base Treatment.*
7 *Staff's Rate Base Treatment will not, however, have net cost of removal as*
8 *component of the depreciation rate.*

9 *(See Schedule 3)*

10 The effect of this treatment will be discussed later.

11 ○ If both the proposed net cost of removal and actual net cost of removal and
12 salvage amounts are booked to the accumulated depreciation reserve, where is
13 each booked?

14 • If both the proposed net cost of removal amount and the actual net cost of
15 removal and salvage amounts are booked to the accumulated depreciation
16 reserve:

17 1 When billed to the customer, the proposed net cost of removal is
18 booked as a debit to Accounts Receivable and as a credit to Revenue.

19 2 When the revenue is collected from customers, it is booked as a debit
20 to Cash and a credit to Accounts Receivable.

21 3 The proposed net cost of removal is booked as a debit to Expense and
22 as a credit to the Accumulated Depreciation Reserve.

Surrebuttal Testimony
Rosella L. Schad, PE

1 4 When actual salvage is received, the actual salvage is a debit to Cash
2 and a credit to Accumulated Depreciation Reserve.

3 5. When the actual cost of removal is incurred, it is booked as a debit to
4 Accumulated Depreciation Reserve and a credit to Cash.

5 Q. Mr. Rooney's statement on page 5, lines 25-27, of his rebuttal testimony
6 addresses Company's position on net salvage in the depreciation rate, "Account 108 is a
7 normal component of rate base. Additionally, as a component of accumulated depreciation
8 under Missouri regulations, it is appropriate to include net salvage in the depreciation rate."
9 Does Staff believe Missouri regulations require net salvage to be included in the depreciation
10 rate?

11 A. No.

12 Q. What is cost of service treatment, referred to by Mr. Rooney on page 8, line
13 16 of his rebuttal testimony?

14 A. Cost of service treatment refers to the currently ordered accounting for cost of
15 removal expense. Staff is using the term, Income Treatment.

16 Q. For cost of removal built into the revenue requirement as an expense and not
17 as a component of depreciation rates, can you demonstrate a comparison of Rate Base
18 Treatment and Income Treatment for actual cost of removal incurred?

19 A. Yes. I will demonstrate this comparison, for illustration only, on Schedule 2 and
20 Schedule 3, for Income Treatment and Rate Base Treatment, respectively, for the following
21 three levels of annual actual cost of removal incurred. Both the Income Treatment and the
22 Rate Base Treatment is demonstrated with the annual net cost of removal as an expense built

Surrebuttal Testimony
Rosella L. Schad, PE

1 into the revenue requirement, i.e, the net cost of removal component is not included in the
2 depreciation rates.

3 1. Net cost of removal built into electric rates, as an expense, is equal to the actual
4 cost of removal incurred;

5 2. Net cost of removal built into electric rates, as an expense, is greater than actual
6 cost of removal incurred;

7 3. Net cost of removal built into electric rates, as an expense, is less than the actual
8 cost of removal incurred;

9 Q. Why is it important for Staff to make this comparison between the Income
10 Treatment and Rate Base Treatment?

11 A. Staff needs to make this comparison between the Income Treatment and the
12 Rate Base Treatment in order to demonstrate its method for expensing cost of removal and
13 the Company's request to utilize Rate Base Treatment.

14 The Rate Base Treatment has the impact, if the Commission desires such resolution,
15 of being a tracking mechanism for the difference between actual net cost of removal incurred
16 and the ordered level of cost of removal that the Company will collect. This would allow the
17 Company to bring any under-recovery or over-recovery from current levels included in this
18 rate case forward to the next rate filing. Using Rate Base Treatment does not require a
19 component for cost of removal be built into depreciation rates, as the Company is requesting.
20 However, regardless of whether Income Treatment or Rate Base Treatment is used, it is
21 important that amounts ordered for net cost of removal should not exceed the level the
22 Company is currently incurring.

Surrebuttal Testimony
Rosella L. Schad, PE

1 Q. Mr. Rooney's rebuttal testimony, beginning on page 12, discusses his
2 conclusion that an on-going disallowance results from Staff's method. Did he ever address
3 the on-going, and several-times-larger, over-collection that results from the Company's
4 method?

5 A. No. I have prepared Schedule 4 to analyze the results of the Company's
6 position. This schedule, for illustration only, is to demonstrate the overcharging of customers
7 for cost of removal.

8 Q. Mr. Rooney states on line 4 of page 12 that "Staff's estimation method will
9 not equal actual costs incurred over time?" For the retrospective analysis performed by Mr.
10 Rooney in Corrected Schedules HDR-1 and HDR-2, does he rely on actual cost of removal
11 amounts provided to Staff?

12 A. No. The Company provided Staff actual cost of removal and salvage amounts
13 for the period 1997 to 2002 in response to Data Request Nos. 276 and 276.1. In addition,
14 Staff had previous amounts for cost of removal and salvage back to 1993 from Aquila's last
15 case, Case No. ER-2001-672. The amounts provided by the Company in data request
16 responses do not equal the amounts identified by Mr. Rooney in his Corrected
17 Schedules HDR-1 and HDR-2.

18 Q. Have you performed a comparison, for illustration purposes, of Staff's
19 proposed expensing of net cost of removal using five-year averages to MPS's collection of
20 revenue for the net cost of removal for years 1998-2002, utilizing the approximate amount of
21 net cost of removal collected in 1998 based on the net cost of removal component of the
22 ordered depreciation rates from Case No. ER-97-394?

Surrebuttal Testimony
Rosella L. Schad, PE

1 A. Yes. This comparison, as shown on Schedule 4, starts in 1998. I used the
2 approximate amount of net cost of removal collected in 1998, \$11.5 million, as a result of the
3 net cost of removal component of depreciation rates ordered in Case No. ER-97-394.
4 Utilizing Staff's method retrospectively, a \$1.7 million under-recovery exists at the
5 conclusion of 2002. Startling, though, is the outcome of the Company's position. For the
6 four years MPS' depreciation rates were in effect, \$46 million was, at a minimum, collected
7 from customers in their electric rates. Following Case No. ER-2001-672, an additional
8 approximate \$0.9 million net cost of removal was collected annually from customers, for a
9 total of \$46.9 million over the five-year period. During the same time period, MPS incurred
10 \$7.4 million net cost of removal. The \$1.7 million under-recovery resulting from Staff's
11 method pales compared to the MPS' \$39.5 excess collection.

12 Q. Have you performed a comparison, for illustration purposes, of Staff's
13 proposed expensing of net cost of removal using five-year averages to MPS' Company's
14 proposed cost of removal in depreciation, projecting out to year 2007?

15 A. Yes. This comparison is also shown on Schedule 4. Starting out with
16 \$0.9 million for net cost of removal for 2003, followed by Staff's proposed \$1.5 million
17 annually for four years results in \$6.9 million collected in rates. In comparison, the
18 Company's proposed \$7 million annually for four years, will result in an additional
19 \$28.9 million collected in rates. Even if an average \$1.8 million spent annually for actual net
20 cost of removal, the total amount spent over the five years would be \$9 million .

21 Using the \$9 million as a benchmark for the amount spent for five years 2003 to
22 2007, and \$28.9 million collected in customer rates, yields a \$19.9 million over-collection to
23 the Company for those five years. Combining the years 1998 to 2002 and 2003 to 2007 the

Surrebuttal Testimony
Rosella L. Schad, PE

1 Company collects \$59.4 million more than they actually spent for net cost of removal over
2 the ten-year period. On an annual basis, this is approximately \$6 million dollars per year.
3 These two examples illustrate the size of the over-collection mechanism proposed by the
4 Company.

5 Q. Is it the Company's position that the ratepayer is protected under their scheme
6 of over-collection for cost of removal?

7 A. Yes. Mr. Rooney asserts on page 3, lines 9-16, "If the amount collected from
8 the customer is greater than the amount spent by the Company, rate base is reduced. This
9 rate base reduction is carried forward to future rate cases, reducing the revenue requirement
10 until lower depreciation rates are established. The ratepayers receive the Company's cost of
11 capital as return on any collected money through the reduction of the Company's rate base
12 until they receive return of their money through lower depreciation rates."

13 Q. Is Mr. Rooney's method of protection the Rate Base Treatment?

14 A. Yes. However, even under Rate Base Treatment, the amount of net cost of
15 removal collected should be of the same magnitude as the actual net cost of removal
16 incurred. The amount of net cost of removal collected should not be several magnitudes
17 larger than the actual amount of net cost of removal incurred.

18 Q. Will customers realize the benefits of rate base reduction each year there are
19 overcollections?

20 A. No. Customers will realize benefits of rate base reductions only after the
21 Company's next rate case.

22 Q. In the current case the Company is proposing to collect from MPS ratepayers
23 approximately \$5.5 million more annually than what the Company is currently incurring for

Surrebuttal Testimony
Rosella L. Schad, PE

1 net cost of removal. Is it Staff's view that the ratepayer is protected under the Company's
2 scheme of over-collection for cost of removal?

3 A. No. It is Staff's view that the ratepayer is protected when rates are established
4 on known and measurable costs. Clearly, based on actual expenditures made for cost of
5 removal and receipts for salvage, the amounts the Company is requesting in this case and has
6 collected in the past has resulted in a substantial over-payment for this item.

7 Q. What is Staff's conclusion regarding Income Treatment vs. Rate Base
8 Treatment as an avenue for collecting net cost of removal on a current basis?

9 A. Staff's conclusion is that either Income or Rate Base Treatment can be used to
10 collect net cost of removal on a current basis; however, it is not necessary to build a
11 component of net cost of removal into depreciation rates in order to collect for net cost of
12 removal from the ratepayers.

13 Q. What is Staff's recommendation regarding the collection of net cost of
14 removal for the Company?

15 A. It is Staff's recommendation that the Commission order collection of annual
16 net cost of removal equal to the average of the last five years, 1998 to 2002, in customer rates
17 for the Company, as identified in Staff witness Cary Featherstone's direct testimony.

18 **FINAL RETIREMENT OF LIFE SPAN PLANT**

19 Q. The Company's witness on Policy, Keith G. Stamm, in his rebuttal testimony
20 page 15, lines 19-20, notes that the current approach to cost of removal recovery is unfair to
21 our customers, a matter of intergenerational inequity. Did he ever address the on-going,
22 substantial over-collection that results from the Company's method, the real matter of
23 intergeneration inequity?

Surrebuttal Testimony
Rosella L. Schad, PE

1 A. No. The fact that current customers are being asked to pay in rates millions of
2 dollars annually for costs the Company is not incurring, and may never incur, is never
3 presented as a genuine concern. Instead, the Company clothes these monies as necessary to
4 keep the Company from feeling the financial chills of retirement and dismantling of a
5 generation plant.

6 Q. Has the Commission previously addressed final costs of removal of fossil-
7 fueled plants?

8 A. Yes. I noted, on page 6 of my rebuttal testimony, the Company has taken a
9 position in this case that conflicts with the prior Commission orders on this issue.

10 Q. On page 17, lines 2-11, Mr. Rooney references Case No. WR-2000-281 and
11 Staff's position on final retirements and associated cost of removal. Did that case address a
12 specific life span facility, and if so, was the facility dismantled and did reclamation of the site
13 occur?

14 A. Case No. WR-2000-281 was a rate filing of Missouri American Water
15 Company. In question was the life span facility, a water treatment plant that was ultimately
16 retired. However, the Company sold the facility and some of the site without removing the
17 plant. The facility was never fully dismantled and reclamation of the site did not occur. This
18 is exactly the reason that Staff maintains that only known and measurable costs should be
19 included in customer rates today.

20 Q. Mr. White introduces his concern, on page 15 of his rebuttal testimony, with
21 Staff abandoning life-span treatment for production plant. Does he also note that Company's
22 previous estimates of retirement dates of production plants did not occur?

Surrebuttal Testimony
Rosella L. Schad, PE

1 A. No. Mr. White never acknowledges that the Company's proposed previous
2 retirement dates did not occur. I discussed production plant retirement dates on pages 15-18
3 of my rebuttal testimony. Contrary to Mr. White's position, Staff's determination of ASL's
4 for production plant more appropriately recovers original cost over the used and useful life of
5 the generating facility.

6 Q. What is Staff's recommendation regarding final retirement of life span plant?

7 A. Staff's recommendation is that projecting final retirement of life span plant
8 and associated retirement costs is more appropriate at the time the Company's management
9 makes a commitment to retire a facility and should be disallowed in the current case.

10 **QUANTIFICATION OF THE COMPONENTS OF THE COMPANY'S**
11 **DEPRECIATION RATES**

12 Q. Is it feasible to take Mr. White's depreciation rates and ascertain how much of
13 the rate reflects individual component issues: future estimated cost of removal for life span
14 plant, future estimated interim cost of removal for life span plant and final retirement of mass
15 property plant, truncation of the Average Service Live (ASL) curve for date certain
16 retirements of life span plant, and use of the vintage group procedure and remaining life
17 technique to develop ASLs?

18 A. No. The component issues are of such an interrelated nature for each account,
19 that the quantification of each individual component issue cannot be framed alone.

20 Q. Mr. White provides Table 8 on page 14 of his direct testimony that displays
21 "Company vs. Staff Production Plant Statistics." A Remaining Life column is presented
22 under "Staff," and Mr. White notes on lines 14-16 that, "Table 8 provides a comparison of
23 composite average and remaining lives requested by Aquila using the vintage-group

Surrebuttal Testimony
Rosella L. Schad, PE

1 procedure with those advocated by Staff using the broad-group procedure.” Did Staff
2 advocate remaining lives as this comparison infers?

3 A. No. This is a misrepresentation of Staff’s position.
4
5
6
7

8 Q. What is Staff’s recommendation on the Company’s proposed depreciation
9 rates?

10 A. Staff’s recommendation is that the Company’s proposed depreciation rates are
11 not reflective of the Company’s known and measurable costs and should not be ordered.

12 **RELATIONSHIP OF DEPRECIATION TO CUSTOMER QUALITY OF SERVICE**

13 Q. Company witness Susan D. Abbott indicates a relationship between
14 depreciation and customer quality of service on page 20 of her rebuttal testimony,

15 A more direct and immediate impact on ratepayers is the quality of the
16 service they receive. The entire electric industry has an aging
17 infrastructure, and MPS are no exceptions. If service is to
18 be kept at a reasonable level, depreciation allowed in rates must be
19 relative to needed capital expenditures to maintain the system. Cutting
20 depreciation rates so as to keep rates down does a disservice to
21 customers who have become used to high quality electric service. It is
22 only reasonable, then, that utilities be allowed depreciation rates that
23 will allow them to maintain their systems in good working order.

24 Do you agree with Ms. Abbott’s statements regarding depreciation rates and customer quality
25 of service?

26 A. No. Staff does not believe that depreciation rates should be determined based
27 on a designated level of needed cash flow. Depreciation analysts do not establish a

Surrebuttal Testimony
Rosella L. Schad, PE

1 relationship of depreciation to customer quality of service issues. There are no safeguards at
2 Aquila that additional funds generated from this case will be used for regulated services, let
3 alone to maintain or increase customer service.

4 Q. Do you agree with Mr. Stamm's declaration of Staff's motives on page 17,
5 lines 1-2 of his rebuttal testimony, "Still, the Staff has attempted to offset these legitimate
6 increases through introduction of unreasonable and unwarranted measures."?

7 A. No. Staff strives to determine the appropriate level of revenue that should be
8 collected from customers in rates based on the Company's known and measurable costs.
9 There are no underlying functions in depreciation that relate to customer quality of service.

10 Q. What is Staff's conclusion regarding a relationship of depreciation to
11 customer quality of service?

12 A. Staff's conclusion is there is no relationship connecting depreciation and
13 customer quality of service.

14 Q. In summary, please provide Staff's conclusions.

15 A. Staff's conclusions are:

- 16 1) The impact of the Company's Proposed Depreciation Rates is to
17 charge the customers for costs that are not known and measurable,
18 and that will allow the Company to collect annually more revenues
19 than the related costs incurred each year.
- 20 2) The Company use of either the Income or Rate Base Treatment
21 does not require that a net cost of removal component be built into
22 depreciation rates.

Surrebuttal Testimony
Rosella L. Schad, PE

1 3) Projecting final retirement of life span plant and associated costs to
2 remove these assets is more appropriate at the time the Company's
3 management makes a commitment to retire a facility and should be
4 disallowed in the current case.

5 4) Component issues of the Company's proposed depreciation rates
6 cannot be individually quantified.

7 5) Customer quality of service is not a function of depreciation.

8 6) The Company's position on these issues increases depreciation
9 expense and increases the Company's revenue requirement without
10 associated known and measurable costs.

11 Q. Please provide Staff's recommendation regarding depreciation rates and net
12 cost of removal.

13 A. Staff's recommendation is that, because the Company's depreciation rates are
14 not based on known and measurable costs, the Commission order Staff's proposed
15 depreciation rates and net cost of removal amounts.

16 Q. Does this conclude your surrebuttal testimony?

17 A. Yes, it does.

UtiliCorp United dba Missouri Public Service
Case: ER-01-572
12 Months Ended December 31, 2000

Income Statement

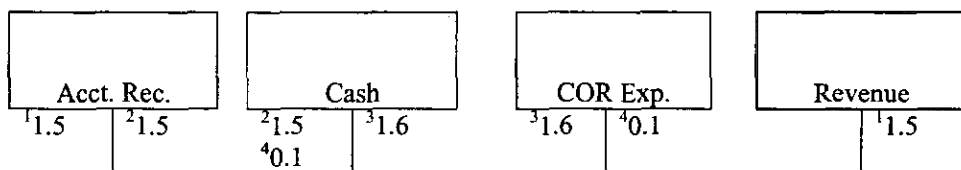
Line No	Acct Description	Total Company	Total Co Adjustment	Alloc Factor	Jurisdictional Adjustment	Adjusted Jurisdictional
(A)	(B)	(C)	(D)	(E)	(F)	
78	913.000 Sales Advertising Expense	444,740	(417,658)	86.9190	0 S-77	23,539
79	916.000 Misc Sales Expense	447,606	(29,046)	86.9190	0 S-78	363,808
80	920.000 Admin & General Salaries	11,885,764	(298,288)	85.6280	0 S-79	9,922,124
81	921.000 Office Supplies & Exp	9,760,630	(2,487,317)	85.6280	0 S-80	6,227,992
82	922.000 Admin Expense Transfer Credit	(1,712,829)	45,685	85.6280	0 S-81	(1,426,686)
83	923.000 Outside Services Employed	4,787,326	(910,907)	86.1400	(39,157) S-82	3,299,990
84	924.000 Property Insurance	575,768	163,005	91.0230	0 S-83	672,453
85	925.000 Injuries and Damages	1,977,809	(4)	71.4000	(672,986) S-84	739,157
86	926.000 Employee Pensions & Benefits	6,328,895	(1,632,015)	89.4570	0 S-85	4,201,688
87	927.000 Franchise Requirements	0	0	85.6280	0	0
88	928.000 Regulatory Commission Expense	1,034,107	(175,397)	86.9470	94,695 S-86	841,319
89	929.000 Duplicate Charges-Credit	(72,539)	0	85.6280	0 S-87	(63,114)
90	930.100 General Advertising Exp	25,919	(19,034)	85.6280	0 S-88	5,685
91	930.200 Misc General Expense	990,804	(1,155,641)	85.6280	0 S-89	(140,147)
92	931.000 Admin & General Expense	1,103,469	(262,188)	85.6280	0 S-90	720,778
93	935.000 Admin & General Maint Exp	548,111	(78,802)	83.3360	0 S-91	439,260
94	Total	\$ 211,934,468	\$ (29,525,932)		\$ (1,037,240)	\$ 179,144,595
Depreciation Expense						
95	403.000 Depreciation Expense	\$ 47,691,112	\$ 0	98.2450	\$ (16,236,356) S-92	\$ 30,617,779
96	404.405 Amortization Exp. Plant	204,726	(25,438)	85.5900	0 S-93	158,240
97	Cost of Removal/Salvage	0	892,289	98.2450	0 S-12	878,629
98	Total	\$ 47,895,841	\$ 866,851		\$ (16,236,356)	\$ 31,549,654
Other Operating Expenses						
99	408.100 Taxes Other Than Income Taxes	\$ 19,451,317	\$ (3,873,499)	90.3410	\$ 487,377 S-94	\$ 14,560,534
100	Total	\$ 19,451,317	\$ (3,873,499)		\$ 487,377	\$ 14,560,534
101	Total Operating Expenses	\$ 275,251,626	\$ (32,532,550)		\$ (16,786,219)	\$ 215,354,793
102	Net Income Before Taxes	\$ 43,628,991	\$ 37,250,601		\$ 16,786,219	\$ 101,478,330

For each type of treatment, the analysis considers three dynamics for the level of actual net cost of removal relative to the level of net cost of removal built into a company's revenue requirement. The dollars (in millions) shown below are for presentation purposes only.

INCOME METHOD

- The first dynamic is for the actual net cost equaling the net cost in the revenue requirement; and
- The first dynamic results in no effect to income or to rate base.

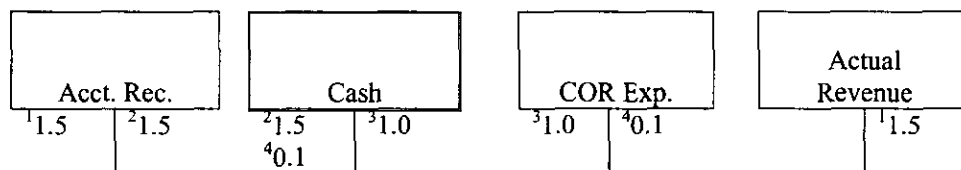
Net COR Built Into Electric Rates as an Expense = Actual Net COR Incurred



Rate Base: \$0 No Effect
Income: \$0 No Effect on Earnings

- The second dynamic is for the net cost in the revenue requirement exceeding the actual net cost; and
- The second dynamic results in increased earnings to income and no effect on rate base.

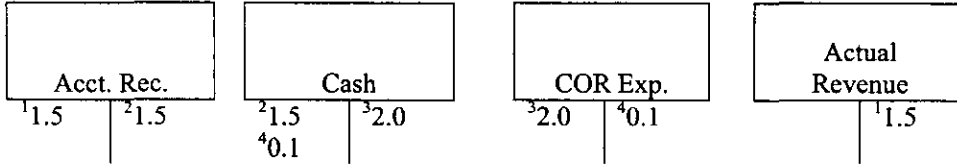
Net COR Built Into Electric Rates as an Expense > Actual Net COR Incurred



Rate Base: \$0 No Effect
Income: \$0.6 ↑ in Earnings

- The third dynamic is for the actual net cost exceeding the net cost in the revenue requirement; and
- The third dynamic results in decreased earnings to income and no effect on rate base.

Net COR Built Into Electric Rates as an Expense < Actual Net COR Incurred



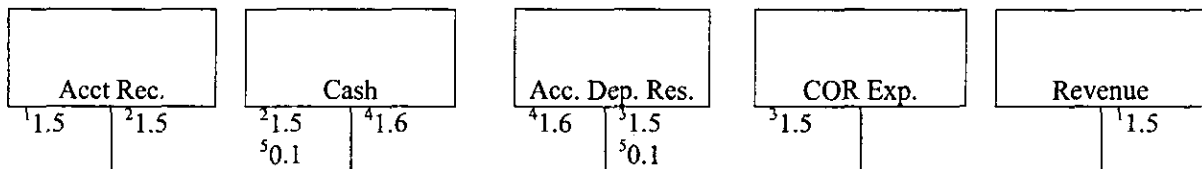
Rate Base: \$0 No Effect
 Income: \$0.4 ↓ in Earnings

For each type of treatment, the analysis considers three dynamics for the level of actual net cost of removal relative to the level of net cost of removal built into a company's revenue requirement. The dollars (in millions) shown below are for presentation purposes only.

RATE BASE METHOD

- The first dynamic is for the actual net cost equaling the net cost in the revenue requirement; and
- The first dynamic results in no effect to rate base or income.

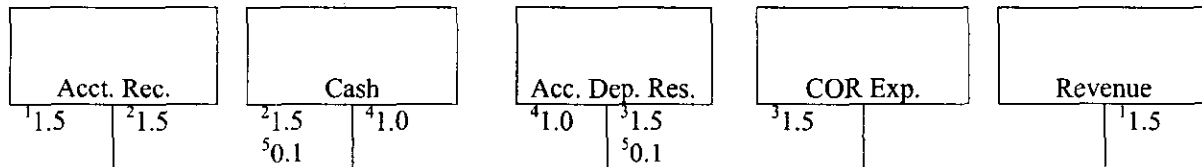
Net COR Built Into Electric Rates = Actual Net COR Incurred



Rate Base: \$0 No Effect
 Net Income: \$0 No Effect on Earnings

- The second dynamic is for the net cost in the revenue requirement exceeding the actual net cost; and
- The second dynamic results in a decrease to rate base and no effect on income.

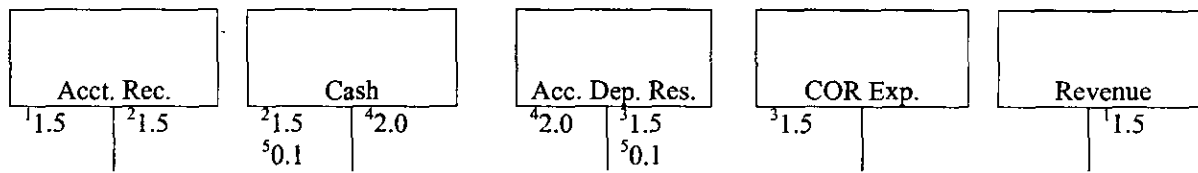
Net COR Built Into Electric Rates > Actual Net COR Incurred



Rate Base: \$0.6 ↓ to rate base
 Net Income: \$0 No Effect on Earnings

- The third dynamic is for the actual net cost exceeding the net cost in the revenue requirement; and
- The third dynamic results in an increase to rate base and no effect on income.

Net COR Built Into Electric Rates < Actual Net COR Incurred



Rate Base: \$0.4 ↑ to rate base
 Net Income: \$0 No Effect on Earnings

STAFF MODIFICATION TO SCHEDULE HDR-1, RETROSPECTIVE ANALYSIS OF STAFF'S METHOD						
YEAR	COST OF REMOVAL	SALVAGE	NET COST OF REMOVAL	RATE RECOVERY 5-YEAR AVERAGE	(UNDER)/OVER RECOVERY OF STAFF'S METHOD	COLLECTED NET COST OF REMOVAL
1993	(2,545,103)	410,730	(2,134,374)			
1994	(140,472)	373,010	(232,538)			
1995	(2,998,889)	438,002	(2,560,887)			
1996	(1,399,148)	339,912	(1,059,236)			
1997	(452,875)	190,589	(262,285)			
1998	(303,736)	177,357	(126,379)	(1,249,864)	1,123,485	(11,500,000)
1999	(1,916,892)	90,577	(1,826,315)	(848,265)	(978,050)	(11,500,000)
2000	(3,811,253)	854,021	(2,957,232)	(1,167,020)	(1,790,212)	(11,500,000)
2001	(1,439,615)	717,872	(721,743)	(1,246,289)	524,546	(11,500,000)
2002	(2,479,058)	708,507	(1,770,550)	(1,178,791)	(591,759)	(900,000)
SUM OF YEARS 1998-2002			(7,402,219)	(5,690,230)	(1,711,990)	(46,900,000)
FIVE YEAR AVG.-1998-2002				(1,480,444)		
2003			(1,800,000)	(1,500,000)	(300,000)	(900,000)
2004			(1,800,000)	(1,500,000)	(300,000)	(7,000,000)
2005			(1,800,000)	(1,500,000)	(300,000)	(7,000,000)
2006			(1,800,000)	(1,500,000)	(300,000)	(7,000,000)
2007			(1,800,000)	(1,500,000)	(300,000)	(7,000,000)
SUM OF YEARS 2003-2007			(9,000,000)	(7,500,000)	(1,500,000)	(28,900,000)
SUM OF YEARS 1998-2007			(16,402,219)			(\$75,800,000)
COR 1998-2007						(\$16,402,219)
UNDER/OVER-RECOVERY						(\$59,397,781)