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
& L&P
Case No.: ER-2004-0034 &
HR-2004-0024
(Consolidated)

Before the Public Service Commission
of the State of Missouri

Rebuttal Testimony

of

Dennis R. Williams

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 AND AQUILA NETWORKS-L&P
CASE NOS. ER-2004-0034 AND HR-2004-0024 (CONSOLIDATED)

Q. Please state your name and business address.

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

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

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

Q. Briefly describe your education and work experience.

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

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

A. I will be addressing the maintenance adjustment and cash working capital proposed by Commission Staff ("Staff") witness Lesley Preston; treatment of Accounting Authority Orders ("AAO's) discussed in the testimonies of Staff witness Trisha Miller and Office of Public Counsel ("OPC") witness Ted Robertson; the uncollectibles (bad debt) expense adjustment proposed by Staff witness Amanda McMellen; the jurisdictional allocation proposed by Staff Witness Alan Bax; property tax and rate case expense treatment discussed in the testimony of Staff witness Trisha Miller; and the adjustment to the employer portion of health, dental and vision benefits as proposed by Staff witness Dana Eaves.

Normalized Maintenance

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

A. Staff proposes to normalize Aquila's Missouri Public Service operating division , ("MPS") maintenance expense using a 57-month historical average for production and transmission maintenance expense and a 33-month historical average for distribution maintenance expense. For Aquila's St. Joseph Light & Power operating division, ("L&P") Ms. Preston is proposing a 57-month historical average for all of non-payroll maintenance.

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

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

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

A. No.

Q. Why not?

A. The purpose of normalization is to establish an on-going level of expense for the period in which the rates set in this case will be in effect. The use of a test year to establish a "primafacie" level of operating expense is traditionally used in ratemaking. Test year costs are then normalized to adjust the test year for any abnormalities. This method has been utilized by the Staff and Aquila for the majority of the adjustments in this case and should be used to project the on-going level of expense for maintenance.

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

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

Q. What is the issue?

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

Q. Please explain.

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

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

Q. Please explain.

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

Q. How could inflation be taken into account?

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

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

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

Q. Please explain.

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

For example, the year 2001 is not a test year in this case and was not analyzed by the Staff to determine if any adjustments should be made. Initially Staff took a similar approach to normalizing production maintenance, as it had to normalizing other maintenance by using a multi-year average of expense. However, it was obvious from the production maintenance account summaries that 2001 contained a significant abnormality because one of the accounts (account 513) had a negative balance. This abnormality was brought to Staff's attention at the pre-hearing and has since been adjusted to increase its normalized non-labor production maintenance by about $670,000 for MPS. While this error stood out because of the negative number, it is reflective of the fact that if a multiple year historical average is used, all periods within that historical period need to be reviewed.

Q. Please explain.

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

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

A. Yes. The amount of audit time would increase dramatically if all expenses were adjusted for the last five years and then averaged. However, as the above example shows, the assumption cannot simply be made that selection of a historical period will level out unusual variations. Selection of a test period requires review of the entirety of that test period to determine that it reflects an appropriate ongoing level. That is one reason that I believe normalization of a single test year is the more reasonable approach.

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

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

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

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

> **Maintenance Expense Normalization - D-6**
> The Staff proposes an adjustment of approximately $1.1 million to the total non-payroll maintenance expense account. The Staff states that it found the test year maintenance expense to be abnormally high and therefore used a five-year normalized expense process to more accurately represent the ongoing level of maintenance expense. The Staff gives two reasons for its use of the five-year normalization rather than the one-year normalized method supported by UtiliCorp. - The Staff first points out that UtiliCorp has substantial discretion over the budgeting and prioritizing of maintenance projects, and this has resulted in an abnormally high test year amount as compared with previous years. Secondly, the Staff testifies that it had great difficulty obtaining information necessary to ascertain the normal amount of maintenance expense. Staff states that, to the best of its knowledge, UtiliCorp has no specific budget guidelines which specify a normal amount of maintenance expense and could provide no information as to what projects are undertaken on a recurring basis. Further, UtiliCorp did not furnish the Staff with its maintenance policies or changes for the 1994-96 time period. The Staff, therefore, used the normalization method, which is a type of averaging, to obtain its normalized expense figure...
>
> ......UtiliCorp states that the most common approach to normalizing costs is to adjust the test year for any abnormalities, as in this case the 1996 ice storm, and to use the adjusted amount to project ongoing expense. UtiliCorp points out that this method has been used by the Staff and UtiliCorp for the majority of the adjustments in this case. The UtiliCorp witness points out that the Staff failed to adjust all five years in its calculation for abnormalities.....

> ….The Commission finds the weight of evidence to favor UtiliCorp on this issue and will deny the proposed $1.1 million adjustment….

Q. Has the Staff adjusted for all abnormalities in its 57 and 33-month historical averages?

A. No. The only abnormality that was adjusted was for the one in account 513 after it was brought to the Staff's attention during prehearing.

CASH WORKING CAPITAL

Q. Have you reviewed the determination of cash working capital as supported by Staff witness Lesley Preston?

A. Yes, I have.

Q. Do you have any concerns with her cash working capital determination?

A. My primary disagreement is with Ms. Preston's calculation of the revenue collection lag. Ms. Preston states that she has computed a collection lag that is considerably shorter than what would typically be computed because of her inclusion of the Company's program to sell accounts receivable.

Q. Please explain your area of disagreement.

A. Aquila has no accounts receivable sales program in place and no plans to reinstate it. The inclusion of a non-existent program in determining the Company's collection lag is not appropriate.

Q. Does Ms. Preston indicate why she has imputed the accounts receivable sales program into her calculation.

A. Yes. Ms. Preston states that the program to sell receivable to Ciesco was terminated on November 1, 2002 but she continued to compute the revenue collection as if the program was still in existence because. "The termination of the accounts receivable program is ultimately a negative result derived from problems that Aquila has faced in its non-regulated ventures."

Q. Do you agree with Ms. Preston's approach?

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

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

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

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

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

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

A. Not to my knowledge.

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

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

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

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

MPS ACCOUNTING AUTHORITY ORDERS

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

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

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

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

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

A. No I do not.

Q. Please explain.

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

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

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

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

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

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

A. No.

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

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

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

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

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

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

A. Yes. Based on the direct testimony of Staff witness Trisha Miller, Staff noted that it had included all of the deferred costs associated with the ice storm AAO. However, this was subject to change because "Aquila has been unable to provide the necessary documentation justifying the deferred costs". In addition, Ms. Miller states on pages 9 and 10 of her testimony, "the Staff requested the necessary information and documentation, as described in the above Report and Order excerpt, in Data Request Nos. 336.2 and 543. The responses to Data Request Nos. 336.2 and 543 did not include the historical analysis necessary to determine MPS' normal ongoing levels for the costs included in the deferral".

Q. How do you respond to her testimony?

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

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

Q. How did the Company answer this data request?

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

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

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

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

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

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

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

A. No. Neither of those arguments appears valid.

Q. Please explain.

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

Q. Please explain.

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

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

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

Q. What is MPS' response?

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

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

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

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

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

Q. Please explain.

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

L&P ACCOUNTING AUTHORITY ORDERS

Q. Has the Company included in rate base any unamortized AAO balances associated with its Aquila Networks – L&P ("L&P") division?

A. Yes, the Company has included the unamortized AAO balance at September 30, 2003 in rate base associated with L&P's Automated Mapping/Facility Management System ("AM/FM System").

Q. Briefly explain the AAO resulting from the AM/FM System.

A. St. Joseph Light & Power Company ("SJLP") filed an application with the Commission in January 1991 requesting the deferral and amortization of labor costs associated with the implementation of the AM/FM System, a computerized database of SJLP's transmission and distribution system. SJLP requested to amortize these labor costs over a six-year period and sought permission to include the unamortized balance of labor costs in rate base.

Q. What was the Commission's decision in this case?

A. In Case No. EO-91-247, the Commission issued an order, which authorized SJLP to:

> "...defer and accumulate labor costs including appropriate overheads and carrying costs associated with the project, and to amortize the balance to the appropriate transmission and distribution accounts over the same six-year period used to depreciate the project's hardware and software costs. The Company is also authorized to include the unamortized balance of Account 186 in rate base for purposes of calculating revenue requirements."

Q. What is the recommendation of Mr. Robertson in regards to the AAO that L&P has included in this case before the Commission?

A. Mr. Robertson recommends that all costs associated with the AM/FM System be disallowed in the determination of L&P's current case cost of service (page 27 lines 1-2). Furthermore, Mr. Robertson recommends the remaining unamortized balance not be included in the determination of L&P's rate base (page 27 lines 8-9).

Q. What is Mr. Robertson's rationale for excluding these costs from L&P's revenue requirement calculation in this case before the Commission?

A. Based on the direct testimony of Mr. Robertson (page 27 lines 15-19), it is OPC's belief that the alleged costs were not appropriately accounted for, L&P's cost structure deficit was never adequately defined, and the six year timeframe over which the Commission authorized the amortization has long since past or will have prior to the effective law date of L&P's current case.

Q. What has been the treatment in past rate proceedings of the unamortized AAO balance of the AM/FM System?

A. In SJLP's last rate case, Case No. ER-99-247, both SJLP and Staff included the unamortized AAO balance in rate base. The accounting treatment of the AM/FM System ordered by the Commission was not disallowed from rate recovery in that prior case.

Q. What is the Company's recommendation in this case, Case No. ER-2004-0034 currently before the Commission?

A. Both Company and Staff have included the unamortized AAO balance at September 30, 2003 in rate base. This treatment is consistent with the treatment from prior rate case proceedings involving SJLP, and this case should be no exception.

BAD DEBT EXPENSE

Q. Please explain the method used by Staff witness Amanda McMellan to calculate bad debt expense for MPS and L&P's 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. Staff used the same method to calculate an annualized level of bad debt expense for L&P's electric operations; however, a 5-year and nine month ending September 30, 2003 uncollectible rate of .4476% was utilized rather than a 3-year and nine months ending September 30, 2003 uncollectible rate.

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. For L&P, Company used a 5-year average uncollectible rate of .4612% which averages the actual net write-off rates for years 1998-2002.

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

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

Jurisdictional Allocations

Q. Please explain what you mean by jurisdictional allocations.

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

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

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

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

A. No. Although Aquila used a12 CP method in developing its application, the difference in revenue requirement is minimal. For that reason, I will agree to use the 4 CP method in this case.

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

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

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

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

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

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

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

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

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

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

Q. Please summarize your position on jurisdictional allocation factors.

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

Property Taxes

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

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

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

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

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

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

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

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

Health, Dental and Vision Benefits

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

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

Q. Please explain that difference.

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

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

Q. Do you agree with Mr. Eaves contention?

A. No. The Company's self-insured portion of its benefits is based on total Aquila employees and allocated so that medical, dental and vision costs are spread over a larger group rather than just the employees based in Missouri. Aquila retains the benefit consulting firm, PriceWaterhouseCoopers ("PWC"), to actuarially estimate medical, dental and vision expenses for Aquila's employees and dependents covered by the plans. PWC uses historical actual claims plus assumptions on future medical inflation, employee turnover, likelihood of catastrophic claims, etc. PWC then assigns a cost to each coverage level in medical, dental and vision (e.g. single \$209 per month, employee plus 1 dependent \$419 per month, and employee plus two or more dependents \$628 per month). Aquila allocates the medical, dental and vision coverage cost to each state based on the actual employee enrollment in each coverage level in each state (e.g. 50 employees at \$209, 100 employees at \$419 and 200 employees at \$628). Aquila adjusts the allocated cost each 6 months based on actual enrollment in the coverage levels. Over the long term, since actual claims fluctuate from year to year, the allocation method, being actuarially based, has proven to be an accurate method of allocating cost. The allocation method is similar to the "smoothing method" to allocate pension expense. If Aquila just used actual claims for the employees in each state, the cost per employee and state could fluctuate dramatically and cost would tend to be much higher. For example, the SJLP merger agreement with Aquila requires that Aquila follow the pre-merger method for setting annual retiree medical cost. Consequently, the SJPL retiree population medical cost is calculated independently of Aquila's other retiree population. In the last three years, the SJLP pre 65 retiree medical rate has fluctuated as follows: 2002 = 8.8% decrease, 2003 = 72.7% increase and 2004 = 51.3% increase.

Rate Case Expenses

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

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

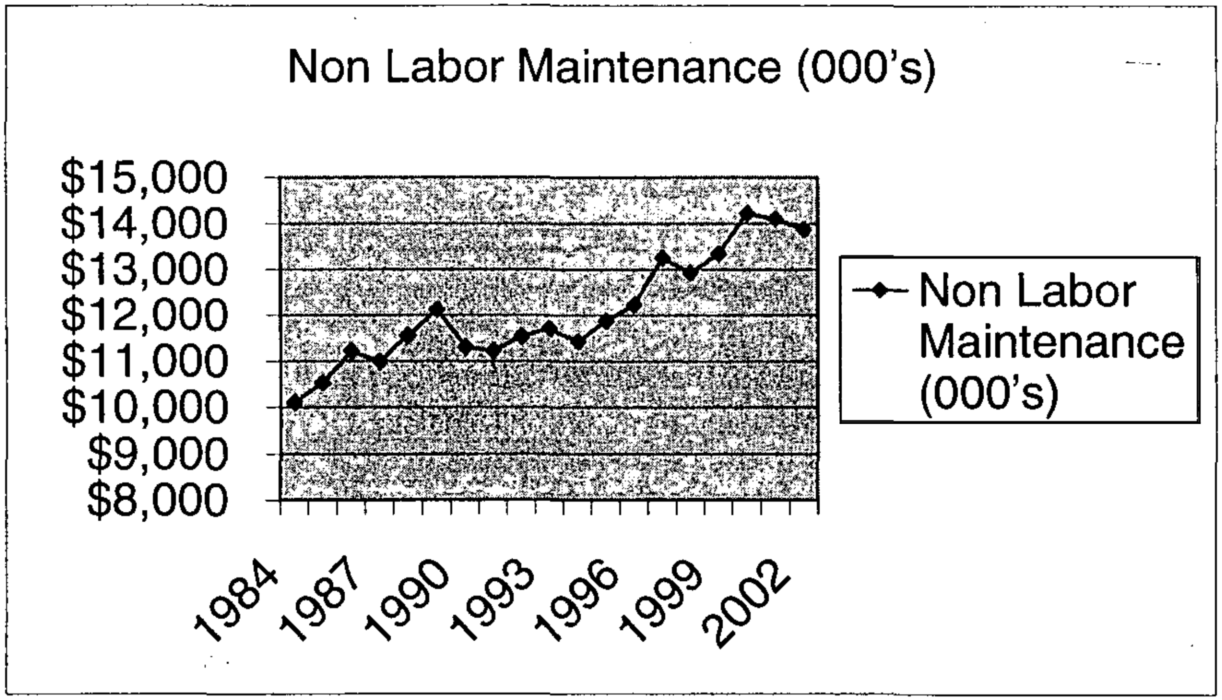
Q. Does this conclude your rebuttal testimony?

A. Yes.

Missouri Public Service
Non-Labor Electric Maintenance

Rolling
5 year average

		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



Schedule DRW-1

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 and Aquila Networks-L&P area	)	Case No. ER-2004-0034
In the matter of Aquila, Inc. d/b/a Aquila Networks-L&P, for authority to file tariffs Increasing steam rates for the service provided To customers in the Aquila Networks-L&P area	)	Case No. HR-2004-0024

County of Jackson)
) ss
State of Missouri)

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

TERRY D. LUTES
Jackson County
My Commission Expires
August 20, 2004