

1 STATE OF MISSOURI
2 PUBLIC SERVICE COMMISSION
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6 TRANSCRIPT OF PROCEEDINGS
7 Hearing
8 June 22, 2004
9 Jefferson City, Missouri
10 Volume 11
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12 In the Matter of Missouri Gas)
13 Energy's Tariffs to Implement a)
14 General Rate Increase for Natural) Case No. GR-2004-0209
15 Gas Service)
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18 MORRIS L. WOODRUFF, Presiding,
19 SENIOR REGULATORY LAW JUDGE.
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22 ROBERT M. CLAYTON,
23 JEFF DAVIS,
24 LINWARD "LIN" APPLING,
25 COMMISSIONERS.

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1 P R O C E E D I N G S

2 JUDGE WOODRUFF: Let's go on the record.

3 Welcome back for day two, GR-2004-0209. When we stopped
4 yesterday, we had Mr. Allen on the stand, but it's my
5 understanding that the parties agreed that Mr. Gillen will
6 be the first to take the stand today.

7 One matter before we take -- before we get
8 started. I noticed that Mr. Deutsch is here now for the
9 City of Joplin. Would you like to enter your appearance,
10 sir?

11 MR. DEUTSCH: Yes. Thank you, your Honor.
12 My name is Jim Deutsch, law firm of Blitz, Bardgett &
13 Deutsch, 308 East High Street, Jefferson City, Missouri
14 65101, and --

15 COMMISSIONER APPLING: I can't hear you,
16 sir.

17 JUDGE WOODRUFF: You need to use your
18 microphone. We can't hear you.

19 MR. DEUTSCH: I'm sorry. I represent the
20 City of Joplin.

21 JUDGE WOODRUFF: Thank you, Mr. Deutsch.

22 All right. Then let's bring Mr. Gillen to
23 the stand.

24 MR. HACK: Also, your Honor, we have had a
25 chance to review Exhibit 842, the reconciliation, and

1 believe it's accurate.

2 JUDGE WOODRUFF: All right. Let's take
3 care of that directly then.

4 MR. FRANSON: Then, your Honor, at this
5 time I'll offer that into evidence.

6 JUDGE WOODRUFF: 842's been offered into
7 evidence. Are there any objections to its receipt?

8 (No response.)

9 JUDGE WOODRUFF: Hearing none, it will be
10 received into evidence.

11 (EXHIBIT NO. 842 WAS RECEIVED INTO
12 EVIDENCE.)

13 JUDGE WOODRUFF: In looking at my chart
14 here, the cost of capital chart that Staff used at the
15 same time, did anyone have any objection to that? Do you
16 remember what it was?

17 MR. HACK: I do not, your Honor. What
18 number was that?

19 JUDGE WOODRUFF: That was 843.

20 MR. HACK: Could we have a chance to look
21 at that?

22 JUDGE WOODRUFF: Certainly. We've got
23 several more days to worry about it.

24 All right. Would you please raise your
25 right hand.

1 (Witness sworn.)

2 JOHN J. GILLEN testified as follows:

3 DIRECT EXAMINATION BY MR. HERSCHMANN:

4 Q. Good morning, Mr. Gillen. Can you please

5 state your name for the record?

6 A. Yes. John J. Gillen.

7 Q. Mr. Gillen, did you cause to be filed in

8 this matter rebuttal testimony that has been premarked as

9 Exhibit 4 for identification?

10 A. Yes, I have.

11 Q. Do you have a copy of that testimony in

12 front of you?

13 A. Yes, I do.

14 Q. Do you have any changes that you need to

15 make to this testimony at this time?

16 A. No, I do not.

17 Q. If I were to ask you the questions today

18 contained in that testimony, would your answers be the

19 same as are shown in Exhibit 4?

20 A. Yes, they would.

21 Q. And are those answers true and correct to

22 the best of your information, knowledge and belief?

23 A. Yes, they are.

24 MR. HERSCHMANN: I move Exhibit 4 into

25 evidence at this time and tender the witness for

1 cross-examination.

2 JUDGE WOODRUFF: Exhibit 4's been offered
3 into evidence. Are there any objections to its receipt?
4 (No response.)

5 JUDGE WOODRUFF: Hearing none, it will be
6 received into evidence.

7 (EXHIBIT NO. 4 WAS RECEIVED INTO EVIDENCE.)

8 JUDGE WOODRUFF: And for cross-examination,
9 I don't believe the City of Kansas City is here.
10 City of Joplin, any questions?

11 MR. DEUTSCH: No questions, your Honor.

12 JUDGE WOODRUFF: The Federal Agencies?

13 MR. PAULSON: No questions.

14 JUDGE WOODRUFF: Jackson County, Midwest
15 Gas, I don't believe are here today.
16 Public Counsel?

17 MR. MICHEEL: No.

18 JUDGE WOODRUFF: Staff?

19 MR. FRANSON: Yes, briefly, your Honor.
20 May it please the Commission?

21 JUDGE WOODRUFF: Certainly

22 MR. FRANSON: Thank you.

23 CROSS-EXAMINATION BY MR. FRANSON:

24 Q. Good morning, Mr. Gillen. My name is
25 Robert Franson. I'm an attorney representing the Staff of

1 the Commission. I have a few questions for you this
2 morning.

3 A. Good morning.

4 Q. Okay. Sir, I believe you only filed
5 rebuttal testimony which has been admitted into evidence
6 as Exhibit 4. Could you turn to page 3 of your rebuttal
7 specifically and look at lines 13 through 19, and then
8 could you tell me when you have had an opportunity to do
9 that.

10 A. Yes, I've done that.

11 Q. Okay. Isn't it true that therein you state
12 you prepared a capitalization statement in accordance with
13 the generally accepted accounting principles for Southern
14 Union Company, including Panhandle Eastern Pipeline
15 Company?

16 A. That is correct, yes.

17 MR. HERSCHMANN: Objection. I think it
18 says excluding.

19 THE WITNESS: Excluding Southern, yes.

20 MR. FRANSON: That is what I said.

21 THE WITNESS: That's what I heard.

22 MR. HERSCHMANN: I thought I heard
23 including.

24 BY MR. FRANSON:

25 Q. Well, just to be on the safe side, so we've

1 got a clear record, in your testimony, isn't it true you
2 prepared a capitalization statement in accordance with the
3 generally accepted accounting principles for Southern
4 Union, excluding Panhandle Eastern Pipeline Company?

5 A. That's correct, yes.

6 Q. Okay. You actually prepared two such
7 capitalization statements, did you not?

8 A. Yes, sir.

9 Q. Okay. Are those attached as schedules
10 JJG-1 and JJG-2 to your rebuttal testimony?

11 A. Yes, sir.

12 Q. Okay. Were these capitalization statements
13 that are in your schedules, JJG-1 and JJG-2, actually
14 filed with the SEC as official Southern Union financial
15 statements?

16 A. I do not believe they were, no.

17 Q. You don't know for sure, but you don't
18 think they were?

19 A. I do not believe they were.

20 Q. Why were they not filed with the SEC?

21 A. I doubt they were required to be filed with
22 the SEC.

23 Q. Were these statements created solely for
24 your rebuttal testimony in this case?

25 A. Yes, sir.

1 Q. Please turn to JJG-1 and let me know when
2 you're there, please.

3 A. I have it.

4 Q. Okay. Do you see the column labeled
5 consolidated Southern Union stand-alone?

6 A. Yes, sir.

7 Q. Okay. Can you find the amounts that appear
8 in that column in any official financial statement issued
9 by Southern Union to the investing public?

10 A. Yeah. Well, I'd have to take a look. You
11 may be able to, because as you see, in Southern Union
12 stand-alone and total consolidated there are certain
13 numbers that are the same. I would assume that total
14 consolidated, some of those would be in SEC financial
15 statements.

16 Q. But you don't know for sure that if someone
17 went looking for this column, Southern Union stand-alone,
18 whether someone in the investing public would be able to
19 find those in SEC documents filed by Southern Union?

20 A. They probably would be able to find some of
21 them, yes.

22 Q. Okay. I guess I don't think you're quite
23 understanding what I'm asking.

24 A. A good example is because I know for sure
25 the preferred stock item, \$230 million, you could find

1 that in an SEC filed statement.

2 Q. Okay. I'm not asking about the various
3 parts here. I'm asking about the whole list there, the
4 Southern Union stand-alone. That whole list, can that be
5 found in SEC documents? Not parts of it, but the whole
6 thing together, would that be found anywhere?

7 A. That exact -- those exact amounts, no,
8 probably not.

9 Q. Okay. On Schedule JJG-1, are the reclass
10 and elimination adjustments that appear on that page
11 actual adjustments that are made to Southern Union's books
12 and records for the purposes of preparing official
13 statements for the total Southern Union Company?

14 A. They are adjustments that are made within
15 the books of the company, yes.

16 Q. Okay. Could you turn to page 5 of your
17 rebuttal testimony, and specifically I'm directing your
18 attention to lines 9 through 14. Could you read that out
19 loud, please?

20 A. Line 9 which begins with the answer?

21 Q. Line 9 actually on my copy is the beginning
22 of a question, and line 14 ends with the last part of your
23 answer. Is your draft different?

24 A. Probably, yes. Could you just tell me what
25 you start with on your line?

1 Q. Did Mr. Murray attempt.
2 A. Okay. I'm sorry. That's my line 6.
3 Q. Okay.
4 A. And your -- that's fine.
5 Q. Okay. Actually --
6 A. That question through that answer you would
7 like me to read?
8 Q. Yes. Before you do that, what -- are you
9 working from a draft that is the same as what
10 Mr. Herschmann gave to the court reporter or are you
11 working from something different?
12 Let me ask you, what lines does that
13 question and answer beginning "does Mr. Murray attempt to
14 determine about Southern Union", what lines does that
15 appear at?
16 A. Line 6.
17 Q. Okay. Where does it end on your draft?
18 A. It ends on line 11.
19 Q. Okay. Thank you. Could you read that
20 question and answer?
21 A. Did Mr. Murray attempt to determine what
22 Southern Union's capital structure would be if Panhandle
23 Eastern was excluded from capital structure?
24 Q. And could you read the answer, please?
25 A. Answer: Yes, beginning on line 18, page 21

1 and ending on line 9, page 22 of his direct testimony,
2 Mr. Murray sets forth his methodology for excluding
3 Panhandle Eastern from Southern Union.

4 Q. Is it your testimony that Mr. Murray's
5 attempt to determine what the Southern Union capital
6 structure would be if Panhandle were excluded provides an
7 incorrect result?

8 A. That would be my next question and answer.

9 Q. Okay. But it is your testimony that --
10 that the -- Mr. Murray's approach gives us an incorrect
11 result; is that correct?

12 A. It's in the next question and answer.

13 Q. Okay. I'm not asking about the next
14 question and answer. I'm asking, are you testifying that
15 Mr. Murray's approach gives an incorrect result?

16 A. Well, Mr. Murray incorrectly assumes simply
17 taking Southern Union's capitalization as shown in
18 December 31, 2003 on Form 10-Q and subtracting Panhandle
19 Eastern's capitalization as shown in December 31, 2003
20 annual report off 10-K is a proper methodology for
21 calculating Southern Union's capitalization excluding
22 Panhandle Eastern.

23 Q. Okay. So my question was, you're saying
24 Mr. Murray's approach is incorrect; is that right?

25 A. I believe that's what I'm saying, yes.

1 Q. Okay. Thank you. Now, have you attempted
2 to determine what Southern Union's capital structure would
3 be if Panhandle Eastern was excluded from the Southern
4 Union consolidated capital structure?

5 A. I have not developed a capital structure,
6 but I have done a -- I have computed a Southern Union
7 stand-alone capital structure.

8 Q. Okay. Why haven't you done -- now, did you
9 say Southern Union stand-alone or --

10 A. Well, Southern Union stand-alone.

11 Q. Southern Union encompasses Panhandle
12 Eastern; isn't that correct?

13 A. Consolidated, yes, Southern Union
14 consolidated encompasses Panhandle. Southern Union
15 stand-alone does not.

16 Q. Okay. So have you done a capital structure
17 for Southern Union stand-alone?

18 A. That's JJG-1, consolidating Southern Union
19 stand-alone. That is what I computed.

20 Q. Okay. It's found in JJG-1?

21 A. Yes.

22 Q. Okay. Mr. Gillen, would you agree that the
23 money used by Southern Union to purchase Panhandle Eastern
24 either came from debt or equity sources?

25 A. It came from debt or shareholder-provided

1 funds, yes.

2 Q. And by shareholder-provided funds are we
3 talking equity?

4 A. Yes, that's equity.

5 Q. Okay. Were there any other sources for the
6 money that Southern Union used to buy Panhandle Eastern?

7 A. I don't know.

8 Q. Okay. Can you tell the Commission how much
9 debt was entered into by Southern Union to pay for any
10 part of the approximately \$612 million cash payment made
11 to acquire Panhandle?

12 A. I don't believe I have that.

13 MR. HERSCHMANN: Objection. I don't think
14 there's anything in the record to support the \$612 million
15 number. Actually, the testimony that's admitted or
16 proffered so far has a different number.

17 MR. FRANSON: Actually, your Honor, I
18 believe the question has already been answered. The
19 witness doesn't know. So I'd say that's already been
20 asked and answered.

21 JUDGE WOODRUFF: Well, do you have a source
22 for that number or where did that come from?

23 MR. FRANSON: Well, your Honor, I think I'm
24 entitled to ask questions of the witness, and if the
25 witness has a problem with the number, I think that's for

1 the witness to assert, not for Mr. Herschmann.

2 MR. HERSCHMANN: With all due respect to
3 counsel, he has to have a good faith basis for asking a
4 question, and if Mr. Oligschlaeger uses a different
5 number, if he wants to proffer the number, I'm more than
6 happy. If I'm incorrect, fine. I believe we've been
7 using a different number in the calculations.

8 JUDGE WOODRUFF: I'm going to sustain the
9 objection and strike the question and answer. Since the
10 answer was "I don't know," it's probably not going to make
11 a whole lot of difference.

12 Objection is sustained.

13 BY MR. FRANSON:

14 Q. Mr. Gillen, do you know how much of a cash
15 payment that Southern Union did make to acquire Panhandle?

16 A. Not off the top of my head, no.

17 Q. You don't have any ballpark figure?

18 A. No.

19 Q. Okay. Well, whatever the number was, do
20 you know how much debt was created by Southern Union, how
21 much was entered into by Southern Union for whatever
22 amount of cash they used to acquire Panhandle?

23 A. I don't have that off the top of my head,
24 no.

25 Q. If the Commission can determine how much

1 debt Southern Union entered into in order to pay the cash
2 necessary to acquire Panhandle, then the remainder of the
3 cash purchase price would have had to come from Southern
4 Union equity; isn't that correct?

5 A. Well, when you say it's coming from
6 Southern Union equity, what do you mean?

7 Q. Well, Southern Union has various funds
8 available to it; isn't that correct?

9 A. Right.

10 Q. Wouldn't it have had to come from Southern
11 Union funds, whatever cash they have on hand, whatever
12 sources of money that Southern Union would have available
13 to it?

14 A. It would -- I presume it would either come
15 from debt or from shareholder-provided funds of some
16 nature, yes.

17 Q. Okay. Let's look at Schedule JJG-1. Do
18 you have that in front of you?

19 A. Yes, I do.

20 Q. In the consolidating Panhandle stand-alone
21 column, you've got a line on Southern Union stand-alone
22 column. How was the amount of 646,818,137 for Panhandle
23 total common -- actually it's Panhandle stand-alone. Yes,
24 Panhandle stand-alone. How was that number, 646,818,137
25 for Panhandle total common equity -- total common

1 stockholders equity determined?

2 A. That would have come from Panhandle Eastern

3 Pipeline Form 10-K at 12/31/03.

4 Q. Okay. Is this the amount tied to the cash

5 payment made by Southern Union to acquire Panhandle?

6 A. I do not believe that is.

7 Q. And you don't know what that number is?

8 A. No, I don't.

9 Q. Now, if you could look at the amount of

10 946,501,950 in the total consolidated column, again

11 Schedule JJG-1, do you see that?

12 A. Yes, sir.

13 Q. Does that amount represent total Southern

14 Union common stockholders equity?

15 A. Yes, sir.

16 Q. Mr. Gillen, under GAAP, the generally

17 accepted accounting principles, are there accounts on

18 Southern Union's books that segregate the amount of

19 Southern Union equity associated with the ownership of

20 Panhandle?

21 A. I do not know if they separate them within

22 their books. It's possible that they'd have subaccounts

23 to separate them.

24 Q. But you don't know whether they do or not?

25 A. I don't know.

1 Q. Is it fair to say you're not -- you don't
2 generally work on Southern Union's accounts, other than
3 this case?

4 A. That's not true, no.

5 Q. Okay. So you do do some work for Southern
6 Union?

7 A. I have done work in the past. Currently
8 it's just this case.

9 Q. Okay. Thank you. Would you agree that the
10 question of how much Southern Union equity is associated
11 with the Panhandle ownership is not entirely an accounting
12 question?

13 A. You'll have to run that by me again.

14 Q. Okay. Would you agree that the question of
15 how much Southern Union equity is associated with its
16 Panhandle ownership is not entirely an accounting
17 question?

18 A. As an accountant, I would like not to agree
19 with that question.

20 Q. Okay. Let's --

21 A. Well, my answer --

22 Q. You said you would like to. Let's try your
23 answer.

24 A. My answer would be, I can give you an
25 accounting answer to that question.

1 Q. Well, let's try the accounting answer
2 first, then if you want to give a supplemental answer,
3 that will be fine.

4 A. I'm only an accounting expert.

5 Q. Okay. Let's try your accounting answer.

6 A. Okay.

7 Q. Do you remember the question?

8 A. You could determine -- no, I don't.

9 Q. Okay.

10 A. I'm sorry. I'm not trying to be difficult.

11 Q. I understand. Would you agree that the
12 question how much Southern Union equity is associated with
13 its Panhandle ownership is not entirely an accounting
14 question?

15 A. It's hard for me to agree with the
16 question. I could say that there probably are other
17 people who are not accountants who could determine a
18 Southern Union capitalization amount.

19 Q. So --

20 A. That may be determined in a way other than
21 through accounting.

22 Q. So is your answer yes, there could be other
23 aspects to this question besides accounting?

24 A. There could be other -- there could be
25 other aspects, but I'm not sure if they would be correct

1 or not under GAAP.

2 Q. Okay. Would you agree that GAAP is really
3 advisory and is not necessarily binding upon this
4 Commission in all respects?

5 MR. HERSCHMANN: Objection, calls for a
6 legal conclusion.

7 MR. FRANSON: Well, your Honor, legal
8 conclusions are done all the way through this thing, but
9 this is more -- this is their expert witness on a matter,
10 and it's really more of a policy and it really -- hold on,
11 Mr. Herschmann. It's really within this witness'
12 knowledge about GAAP. He's here as an expert witness.

13 JUDGE WOODRUFF: It sounds to me like more
14 of an accounting question than a legal question. I'm
15 going to overrule the objection.

16 MR. FRANSON: If I can be heard for a
17 moment. I think the question asks whether or not GAAP was
18 to be or has to be applied to policy making for the
19 Commission. I think the Commission is -- what the
20 Commission applies is a legal standard for the Commission
21 to determine, unless he's going to proffer him as an
22 expert on what standards this Commission uses.

23 JUDGE WOODRUFF: Your objection is noted
24 and still overruled. You can go ahead and answer the
25 question.

1 THE WITNESS: Would you mind repeating the
2 question?

3 MR. FRANSON: At this point I'm going to
4 the ask the court reporter to read it back.

5 THE REPORTER: "Question: "Would you agree
6 that GAAP is really advisory and is not necessarily
7 binding upon this Commission in all respects?"

8 BY MR. FRANSON:

9 Q. Let's break that down, first of all. Would
10 you agree that there are certain entities, whether they're
11 governmental bodies or private entities, that don't
12 necessarily, for any number of reasons, always follow
13 GAAP?

14 A. There are some entities that are not
15 required to follow GAAP, yes.

16 Q. Would you know whether this Commission is
17 one of those entities?

18 A. For their financial statements?

19 Q. No. I'm asking, would you know -- and this
20 is strictly on your knowledge -- whether this Commission
21 is obligated to follow GAAP in all respects as part of its
22 ratemaking decision process?

23 A. I would not know.

24 Q. Okay. Thank you.

25 If Southern Union had used any equity

1 funding to purchase Panhandle, would that amount of equity
2 funding be part of the \$946 million we were just
3 discussing? And that \$946 million, I believe, was from
4 Schedule JJG-1.

5 A. I have it. If they used any equity funding
6 for the purchase of Panhandle, it would be part of that?

7 Q. Yes.

8 A. I believe it would be, yes.

9 Q. Okay. Thank you.

10 If Southern Union had not purchased
11 Panhandle -- and again, this is assuming that Southern
12 Union did not purchase Panhandle -- would you expect the
13 same amount of total stockholders equity of \$946 million
14 would still appear on Southern Union's year-end 2003
15 financial statement as its total common stockholders
16 equity?

17 A. I couldn't possibly answer that.

18 Q. Have you read Mr. Dunn's surrebuttal
19 testimony?

20 A. Yes, I have. I wouldn't say I'm expert in
21 his surrebuttal, but go ahead if you have a question on
22 it.

23 Q. But you have read it?

24 A. Yes.

25 Q. Okay. Are you aware that Mr. Dunn presents

1 an estimate of the amount of common equity that should be
2 eliminated from the total Southern Union common equity
3 balance?

4 A. Yes, I am.

5 Q. Okay. As it relates to Panhandle?

6 A. Yes, sir.

7 Q. Have you had an opportunity to review
8 Mr. Dunn's calculations?

9 A. I've read his surrebuttal testimony.

10 Q. Okay. Do you agree with it?

11 A. I have not taken the numbers back to GAAP
12 financial statements, but I have no reason to disagree
13 with it.

14 Q. But you can't say for sure that you do
15 agree with it?

16 A. Well, it's not my testimony.

17 Q. I understand it's not your testimony. But
18 you don't know whether you actually agree with it because
19 you haven't done the calculations yourself; is that
20 correct?

21 A. That's correct, and I'm not supporting
22 those numbers.

23 Q. Okay. Do you know where Mr. Dunn got this
24 information?

25 A. I do not.

1 Q. You didn't give it to him?

2 A. No, sir.

3 Q. Do you know how much equity Southern Union

4 does, in fact, have in Panhandle?

5 A. I do not have that with me, no.

6 Q. But I guess my question is, I understand

7 you don't have it here with you, but do you know the

8 answer to that?

9 A. No, I don't.

10 MR. FRANSON: Thank you very much. I don't

11 believe I have any further questions, your Honor.

12 JUDGE WOODRUFF: Come up to questions from

13 the Bench, beginning with Commissioner Clayton.

14 QUESTIONS BY COMMISSIONER CLAYTON:

15 Q. Good morning.

16 A. Good morning.

17 Q. I've reviewed your testimony and I've

18 reviewed the schedules that you've supplied to us. As an

19 accountant, are you able to suggest a capital structure

20 appropriate for ratemaking purposes in your capacity as an

21 accountant?

22 A. Simply in the capacity as an accountant, I

23 probably -- well, today I would not be able to, but a

24 capital --

25 Q. Why not today? Is there --

1 A. I have not done an analysis.

2 Q. Oh, you haven't done an analysis?

3 A. No.

4 Q. Okay. Well, as an accountant, is that the

5 proper training to establish the capital structure?

6 A. I think the proper accountant with proper

7 training and experience could develop a capital structure,

8 yes.

9 Q. Do you have that proper training and

10 experience?

11 A. I would not say I've done it before. I've

12 never done it before, so I would not put myself in that

13 category.

14 Q. So the answer would be no?

15 A. That's correct.

16 Q. Okay. Schedule JJG-2, this schedule sets

17 out suggested or actual capitalization of the company as a

18 whole and also on a stand-alone basis, as well as setting

19 out the capitalization of Panhandle; is that correct?

20 A. Yes, sir, on a GAAP basis.

21 Q. Now, how does that basis differ from a

22 purely financial business?

23 A. It doesn't.

24 Q. It doesn't?

25 A. No.

1 Q. Okay. So on a purely mathematical basis,
2 could we take the figures that are listed in one of these
3 columns and determine the actual cap-- the actual capital
4 structure either on a consolidated basis or Southern Union
5 stand-alone or Panhandle stand-alone using these figures?
6 Is that an appropriate method for determining the actual
7 percentages of capital structure?

8 A. I believe my testimony was to say this
9 would be -- these schedules would be a good place to start
10 to develop that capital structure, yes.

11 Q. Well, good place to start, but I guess my
12 question is, in terms of actual -- these are the actual
13 numbers that you developed associated with the capital
14 structure of the company?

15 A. These are numbers I can't -- these are
16 numbers that came out of their financial reports at the
17 SEC.

18 Q. Okay. So if we were to -- and forgive me,
19 I'm not a financial or not a finance person. I'm not an
20 accountant in background, so a lot of these questions may
21 seem very elementary, but I need the help.

22 A. Perfectly okay.

23 Q. If I were to -- simply to say on your
24 sheet, say under the consolidated column on JJG-2, if I
25 were to add long-term debt and long-term debt due

1 currently, add those together, and then divide that number
2 by the total capitalization of the company, would that be
3 the actual long-term debt owed by the company?

4 A. That's correct, yes.

5 Q. Okay. And then notes payable would be
6 short-term debt, what's generally known as short-term debt
7 for ratemaking purposes?

8 A. I believe that's correct, yes.

9 Q. Now, the other components, I think, are a
10 little more difficult to arrive at, because I don't know
11 in terms of developing a capital structure how each of the
12 other figures are derived. For example, at this point in
13 determining the amount of preferred stock that is
14 outstanding or the amount of common stock or the premium
15 on capital stock, how are these numbers determined on an
16 accounting basis? Could you explain that to me?

17 A. Well, the first is, is it's very similar to
18 debt. I mean, there's a -- there's a number out there.

19 Q. There's a finite amount of money owed --

20 A. Right.

21 Q. -- to preferred equity holders?

22 A. Right. That's correct.

23 Q. Okay.

24 A. The equity is a combination of -- and
25 generally, equity only gets to equity in two ways; it's

1 either you sold stock in the company and got proceeds from
2 the sale of that stock, or over time you've had profits,
3 and those profits were not distributed; therefore, they
4 ended up in equity and reinvested in the company. That's
5 how you get those columns.

6 Q. Okay. Very simplistic.

7 A. That's the simplistic view. I didn't get
8 into all the other --

9 Q. Let me give you another simplistic view
10 without writing in crayon. I'm just joking.

11 A. Might be helpful.

12 Q. I know. If we were to take the total
13 capitalization of the company and you subtract out your
14 long-term debt and your short-term debt and your preferred
15 stock, that's how you determine the amount of
16 capitalization through common equity; is that correct?

17 A. That's correct.

18 Q. So under the consolidated structure -- and
19 let me ask, this is as of March 31, 2004; is that correct?

20 A. That's correct, yes.

21 Q. That would mean the total debt for the
22 consolidated company would be roughly 55 -- 55.2 percent.
23 These numbers aren't listed? I've got a calculator up
24 here, and I was doing some numbers here.

25 A. Subject to check?

1 Q. Subject to check, 12 percent equity.

2 A. I'm accustomed to lawyers taking accounting
3 positions.

4 Q. That's got to be a first.

5 So to determine the actual capitalization,
6 setting aside -- and you weren't -- I don't think you were
7 here yesterday -- the discussions regarding hypothetical
8 capital structures or necessary capital structures for a
9 utility, the actual consolidated capital structure of
10 Southern Union and including Panhandle, we could take the
11 total amount of debt and divide that by the total
12 capitalization which, subject to check, of course, is
13 55.2 percent. The preferred stock listed on line 2 of the
14 chart comes out to be 5.4 percent, and then the remainder
15 is 39.4 percent. That would be the actual capital
16 structure on a consolidated basis for the company
17 according to accounting rules, correct?

18 A. That's correct.

19 Q. And I could do the same thing under
20 Southern Union stand-alone as well, which would be the
21 company with all of Panhandle excluded, correct?

22 A. That's correct.

23 Q. In your opinion -- I don't know if this is
24 within your area of expertise -- if one wanted to exclude
25 Panhandle from the capital structure, one would have to

1 excludes the debt as well as the equity, would they not?
2 Wouldn't we have to look in this middle column at the end
3 under Southern Union stand-alone to get a market
4 capitalization excluding Panhandle Eastern?

5 A. Which column would you be looking at? I'm
6 sorry.

7 Q. I say the middle one. I mean there are
8 three -- I'm looking at the three principal columns at the
9 end on Schedule JJG-2. You've got subtotal, consolidated,
10 Southern Union stand-alone and Panhandle stand-alone. If
11 we went to exclude Panhandle, we need to exclude both the
12 debt and the equity, and the actual capitalization would
13 be in that middle column, the stand-alone column of
14 Southern Union. Do you follow me?

15 A. Yes, the middle column is Southern Union
16 stand-alone, that's correct.

17 Q. Okay. So subject to check, obviously, if
18 my calculator works, you have -- long-term debt would be
19 the two debt entries near the bottom, which would be
20 43.9 percent, short-term debt of 75.5 million. That's
21 3.2 percent. And then the preferred equity would be
22 9.8 percent.

23 I know I'm saying these numbers and you
24 have no way to verify that. But that would be the actual
25 capitalization --

1 A. Uh-huh.

2 Q. -- with Panhandle completely excluded,
3 correct?

4 A. That is -- yes, on the GAAP basis again.
5 And I don't mean to confuse you. That --

6 Q. That's easy to do, so don't worry about it.

7 A. Yeah. That's what these schedules would
8 purport to say, yes.

9 Q. Okay. Now, would these be the schedules
10 that someone in finance would use or would financial
11 schedules where -- I mean, this would be the
12 capitalization of the company that would be used on a
13 non-accounting basis or a financial basis, would they not,
14 or are there different types of capitalization schedules
15 that would be used?

16 A. Well, again --

17 Q. Does the question make sense?

18 A. Well, let me -- let me give an answer, and
19 if it's not the answer to your question, then we'll do it
20 again.

21 Q. Okay. That's fine.

22 A. For financial reporting purposes, what I
23 had historically done as a partner was, I was always
24 looking at the far left-hand-side column with a total
25 consolidated, and that's what the financial communities

1 will see. Then the company could discuss components of
2 that left-hand column about what's available or how -- you
3 know, like, what is owned by which part of the company,
4 but for the most part what you're looking at as a
5 financial investor is the left-hand side.

6 Q. Okay.

7 A. And for purposes of this proceeding, the
8 company is looking to develop Panhandle stand-alone and
9 Southern Union stand-alone.

10 Q. I understand. Now, the principal purpose
11 of your testimony is to discredit the methods used by
12 another witness; is that a fair statement? I don't mean
13 that in a rude sense, but we're all big kids around here.
14 I mean, you disagree with the methods used by another
15 witness?

16 A. I disagree with their conclusions.

17 Q. Okay. That's a nicer way to put it.
18 Lawyers always get so mean about it. Hear that fellas?

19 Now, what I'd like you to do, if possible,
20 in a general sense on this Schedule JJG -- and in the last
21 two columns you've got Southern Union stand-alone and
22 Panhandle stand-alone companies. Can you give me an idea
23 of what Witness Murray did and how his numbers compare to
24 these figures that you're using?

25 And I don't need exact figures, but can you

1 show me what he did in his removal of Panhandle from the
2 market capitalization or the consolidated capitalization?

3 A. Again, Witness Murray, as I recall, ended
4 up -- your calculations as you were determining how much
5 was equity, what percentages did you have?

6 Subject to check, of course.

7 Q. It depends. Which column are you talking
8 about?

9 A. Subject to check. Any of them.

10 Q. I think the common equity was
11 43.1 percent in Southern Union stand-alone.

12 A. That's fine. Witness Murray ended up, I
13 believe, subject to check again, somewhere around 15,
14 16 percent.

15 Q. Okay. And do you know how he came up with
16 that?

17 A. I believe what he has done is he had taken
18 all Panhandle equity out of the -- and said that --
19 everything showing up as Panhandle stand-alone equity came
20 out of Southern Union total and, therefore, what was left
21 over was for everyone else.

22 Q. Okay. So he removed the premium on capital
23 stock, and the retained earnings --

24 A. Right.

25 Q. -- is, I guess, a simplistic way to look at

1 it. So he removed the equity component and left the debt,
2 right?

3 A. Well, he removed the equity component in
4 total. I believe he also removed the debt. But when you
5 remove the -- when you take 600 --

6 Q. Witness Murray removed the debt or he left
7 it in there?

8 A. I believe he removed the debt.

9 Q. I'm not sure if that's right. I thought he
10 left it in there. Maybe we're confused. I know I'm
11 confused.

12 A. It's early.

13 MR. HERSCHMANN: Do you want me to answer
14 that?

15 COMMISSIONER CLAYTON: Go ahead, yeah.

16 MR. HERSCHMANN: I believe he removed from
17 the Panhandle side or from the Southern Union side the
18 debt associated with Panhandle, and then removed the
19 entire purchase price of Panhandle, the cash proceeds.

20 MR. FRANSON: And, Commissioner, also,
21 Staff's position is that was the right thing to do,
22 because that was the proper amount of that.

23 COMMISSIONER CLAYTON: Regardless of the
24 right thing to do, let's not let the right thing to do
25 confuse us here.

1 MR. FRANSON: Yes, sir.

2 THE WITNESS: As you can see, removing

3 these large numbers, removing 611 million or 700 million

4 out of the base of 1.2 gets you pretty small.

5 BY COMMISSIONER CLAYTON:

6 Q. Tell me why what he did was wrong, since

7 obviously the premise of my questions was incorrect. My

8 memory doesn't serve correctly. So tell me on a purely

9 accounting basis why what he did was wrong.

10 A. I believe what's taken place there is when

11 you removed that entire Panhandle stand-alone, it's only

12 there as a stand-alone company because it's still a

13 separate registrant. So they're still reporting what

14 Panhandle looked like before they were ever acquired.

15 Under GAAP, that all sorts of -- that just

16 gets -- when you buy a company, you restart the equity

17 piece. Your equity starts over. Any equity that was in

18 that company when you acquired it goes away; it goes back

19 to the people you bought it from. And now you start fresh

20 and there is a zero equity balance, except for what equity

21 you may have used to buy the company.

22 Q. Did his analysis assume that the Panhandle

23 transaction never occurred or did he treat it as occurring

24 with adjustments that you believe are inappropriate?

25 A. I'd like -- my answer to that would be I

1 believe he was doing it as if it never occurred, based on
2 numbers he used.

3 Q. Okay. If that were -- if we were to
4 determine that that is the proper way to look at the
5 capitalization of the company, wouldn't it be more
6 accurate to go back to the point in time and read the
7 books going back in time prior to the Panhandle Eastern
8 transaction, or would there be a way of actually -- I
9 guess your way here to the proper method to exclude
10 Panhandle?

11 A. Right.

12 COMMISSIONER CLAYTON: All right. Thank
13 you very much for your time.

14 JUDGE WOODRUFF: Commissioner Davis, do you
15 have any questions?

16 QUESTIONS BY COMMISSIONER DAVIS:

17 Q. Going back to the GAAP principles, what
18 would be a reason why a body wouldn't adhere to the GAAP
19 principles?

20 A. I do not know the answer to that.

21 Q. But are you aware that there are some
22 groups out there that don't adhere to GAAP principles?

23 A. Oh, there are some organizations that
24 aren't required to follow GAAP. I don't want to confuse
25 you, but a good example is the department I used to work

1 for. CPA firms don't follow GAAP. They're a partnership;
2 they're not subject to SEC rules, and they do not have to
3 follow GAAP.

4 This Commission and your budgets come from
5 a state legislative mandate. You get audited, but the
6 audit is not necessarily in accordance with GAAP. It's
7 probably in accordance with government approved financial
8 statements. So those entities don't necessarily follow
9 GAAP.

10 What we're talking about here, though, is a
11 company that is subject to SEC regulation. They must --
12 they must follow GAAP in what they file. The question
13 was, do you have to follow GAAP? Again, I'm not an
14 attorney.

15 Q. Okay. And your answer to that was? Please
16 refresh my recollection.

17 A. I thought I dodged it, but I presume you
18 can make your determination however you determine --
19 whatever determination you make, you can make. The
20 company still will have to follow GAAP. So if you choose
21 to do something that's not in accordance with GAAP, the
22 company will just have to follow that rule, that
23 determination. I don't know how else to answer that. I
24 don't mean to be confusing.

25 COMMISSIONER DAVIS: That's all right. No

1 further questions.

2 THE WITNESS: I guess I've been around
3 attorneys long enough to get confusing in my answers.

4 COMMISSIONER APPLING: Judge, I have no
5 questions of this witness.

6 JUDGE WOODRUFF: Thank you, sir. I have no
7 questions either, so we'll go back to recross. Kansas
8 City's not here.

9 City of Joplin, any questions?

10 MR. DEUTSCH: No questions, your Honor.

11 JUDGE WOODRUFF: Federal Agencies?

12 MR. PAULSON: No questions, your Honor.

13 JUDGE WOODRUFF: Jackson County and Midwest
14 Gas are not here.

15 Public Counsel?

16 MR. MICHEEL: No questions, your Honor.

17 JUDGE WOODRUFF: Staff?

18 MR. FRANSON: Briefly, your Honor.

19 RECROSS-EXAMINATION BY MR. FRANSON:

20 Q. Okay. Mr. Gillen, do you recall when
21 Commissioner Clayton asked you about whether you would
22 determine a capital structure for Southern Union excluding
23 Panhandle?

24 A. Yes.

25 Q. Okay. If you could turn to page 9 of your

1 testimony, and we'll work on the lines as soon as you get
2 there, because we may have different line numbers, whether
3 that's due to computer printing or whatever it might be.

4 A. That's fine.

5 Q. Okay. Isn't it true there, I believe, on
6 your page 8, you recommend a capital structure that is, in
7 fact, Southern Union's capital structure excluding
8 Panhandle Eastern?

9 A. Which lines are you referring to?

10 Q. Well, let me give you the question. It
11 might help. It starts on a GAAP basis, what is the
12 appropriate column from these schedules?

13 A. Okay. On a GAAP basis, I have -- it says,
14 the appropriate GAAP column would be a column in these
15 schedules titled Southern Union stand-alone.

16 Q. And which column is that and on which
17 schedule?

18 A. That would be on Schedules JJG 1 and JJG-2.

19 Q. What column?

20 A. And that would be under the far right-hand
21 side, consolidating Southern Union stand-alone.

22 Q. Okay. And the heading for that is
23 Panhandle stand-alone?

24 A. And Southern Union stand-alone, yes, sir.

25 MR. FRANSON: Okay. No further questions.

1 JUDGE WOODRUFF: Redirect?

2 MR. HERSCHMANN: Just for clarification, if

3 I could hand the witness another copy of Exhibit 4. What

4 exhibit number are we up to?

5 May I approach the witness?

6 JUDGE WOODRUFF: You may.

7 (EXHIBIT NO. 31 WAS MARKED FOR

8 IDENTIFICATION BY THE REPORTER.)

9 REDIRECT EXAMINATION BY MR. HERSCHMANN:

10 Q. Will you look at Exhibit 31, please. The

11 second page, and read to yourself the paragraph beginning

12 with "on June 11, 2003."

13 MR. HERSCHMANN: For the record, Exhibit 31

14 is Form 10-K for Panhandle Eastern Pipeline Company.

15 MR. FRANSON: Mr. Herschmann, could you

16 give a date on that? Just so it's clear on the record.

17 MR. HERSCHMANN: It's for the fiscal year

18 ended December 31st, 2003.

19 MR. FRANSON: Thank you.

20 MR. HERSCHMANN: I'd offer Exhibit 31 for

21 identification into evidence.

22 JUDGE WOODRUFF: Are there any objections

23 to its receipt?

24 MR. FRANSON: No.

25 JUDGE WOODRUFF: Hearing none, it will be

1 received into evidence.

2 (EXHIBIT NO. 31 WAS RECEIVED INTO

3 EVIDENCE.)

4 BY MR. HERSCHMANN:

5 Q. Have you had occasion to read that

6 paragraph, sir?

7 A. Yes, I have.

8 Q. Do you see in the paragraph that the

9 acquisition of Panhandle Eastern Pipeline by Southern

10 Union was acquired with a portion of the funds obtained by

11 Southern Union from the sale of its Texas operations for

12 \$437 million in cash?

13 A. Yes, sir.

14 Q. And if Southern Union's actual capital

15 structure was approximately \$940 million in June of 2003,

16 would it be appropriate to remove the \$437 million from

17 Southern Union's common equity?

18 If you don't understand that, tell me and

19 I'll try to rephrase it. Let me see if I can break it

20 down for you.

21 You see that Southern Union paid

22 \$581 million in cash to acquire Panhandle from CMS?

23 A. Yes.

24 Q. And is the \$581 million, would that be

25 exclusively Southern Union shareholder equity or would

1 cash be considered something different?

2 A. Well, you shouldn't confuse cash with
3 equity, no, if that's your question. Cash is -- cash is
4 something you have in the bank and it's tangible,
5 functionable, and you can use right away. Equity is --
6 well, that's built up in the company over time.

7 Q. So the fact that Southern Union gave to CMS
8 \$437 million in cash, does that mean that they gave them
9 \$437 million in cash and \$437 million with shareholder
10 equity?

11 A. No.

12 Q. That would be double accounting to do that,
13 right?

14 A. Yes.

15 Q. And in reviewing Mr. Murray's testimony,
16 did you realize that he actually did that, removed the
17 investment from Southern Union's total equity?

18 A. I believe that's what was happening in his
19 calculation.

20 Q. And would that cause, obviously, certain
21 amounts of Southern Union's shareholder equity to drop if
22 you took out 437 million from the proposed, say,
23 \$940 million of total equity?

24 A. Yes.

25 Q. Do you know any accounting standards that

1 would allow that to occur?

2 A. No.

3 Q. If you look at your Schedule JJG-2, and

4 look at the second column that says eliminations.

5 A. Okay.

6 Q. What does the eliminations refer to?

7 A. Basically it's amounts of Panhandle that

8 are already in the consolidated number. So you're

9 eliminating it, so you don't double account it.

10 Q. And did you make those adjustments in

11 coming to a Southern Union stand-alone capital structure?

12 A. Those adjustments would be necessary, yes.

13 MR. HERSCHMANN: If I could have a moment.

14 I'd like to approach the witness, please.

15 JUDGE WOODRUFF: You may.

16 BY MR. HERSCHMANN:

17 Q. You were asked some questions by

18 Mr. Franson dealing with Mr. Dunn's calculations, and I've

19 handed you what's been received in evidence as Exhibit 3,

20 beginning on page 9, line 6. Could you please read that

21 through page 10, line 3?

22 A. Page 9, line 6?

23 Q. Page 9, line 6. It starts with Table 1.

24 A. Through page 10, line 3?

25 Q. Line 3.

1 A. Page 9, line 6 begins with a table, which
2 is entitled pro forma capital structure Southern Union
3 company only, April 30, 2004.

4 Q. I don't need you to read it out loud; I
5 just wanted you to read it to yourself first.

6 A. Okay.

7 Q. Just read that page to yourself.

8 A. Okay. I've read it.

9 Q. And if you could look back at Exhibit 31
10 for a moment.

11 A. Exhibit 31 was which, the 10-K?

12 Q. Yes.

13 A. Okay. Got it.

14 Q. If you look at the paragraph we were
15 discussing, do you see that the 3 million shares of
16 Southern Union common stock were valued at approximately
17 \$48.9 million?

18 A. Yes.

19 Q. Looking at Mr. Dunn's calculations as to
20 how to remove Panhandle Eastern Pipeline from Southern
21 Union -- actually I'd ask you, can you tell us whether
22 that complies with GAAP?

23 A. Well, his calculations are not -- the
24 schedules I prepared, JJG-1, JJG-2, I prepared in
25 accordance with GAAP. His -- his testimony here is

1 basically going into the actual transaction itself and
2 specifically identifying monies that were raised by the
3 company to make the acquisition of Panhandle Eastern.

4 The one GAAP number in here that he could
5 go to is the \$91 million of earnings by Panhandle since it
6 was acquired. That would go back to my schedules. I
7 could find that in my schedules.

8 Q. What would the \$91 million reflect?

9 A. The \$91 million is basically earnings
10 Panhandle has had since acquisition.

11 Q. In what category would this fall?

12 A. Retained earnings.

13 Q. Is that considered equity?

14 A. Yes.

15 Q. Would it appropriately be removed from
16 Southern Union's consolidated capital structure if you
17 were trying to remove Panhandle?

18 A. Yes, it would.

19 Q. And if you're looking at Exhibit 31, the
20 10-K, would 3 million shares of Southern Union common
21 stock that was valued at \$48.9 million be considered an
22 equity investment of Panhandle?

23 A. That was -- yeah, that's specifically
24 identified by the company.

25 Q. And would that likewise be appropriate to

1 remove from Southern Union's consolidated capital
2 structure pursuant to GAAP?

3 A. Only if you're trying to specifically
4 identify what portion is Panhandle.

5 Q. And if you're trying to do that --

6 A. Yes.

7 Q. -- is that consistent with GAAP?

8 A. Then you would pull it out.

9 Q. And do you see that Mr. Dunn has actually
10 eliminated 48.9 and the \$91 million from Southern Union's
11 consolidated capital structure and made it applicable to
12 the Panhandle acquisition?

13 A. That's what he's saying in his testimony.

14 Q. And do you know how -- what other way
15 Southern Union went ahead and actually used funds to
16 acquire Panhandle?

17 A. You might be referring to his third
18 adjustment.

19 Q. And if you look at the 10-K, can you tell
20 us where the \$121,250,000 came from?

21 A. Well, it was a common stock units offering.

22 Q. And do you know whether or not -- or what
23 portion of the equity offering and the equity units
24 offering was applicable to Panhandle as either debt or
25 equity?

1 A. Well, I would only know that from reading
2 Mr. Dunn's testimony.

3 Q. Can you determine it based on looking at
4 the 10-K?

5 A. Not what portion is debt, what portion is
6 equity.

7 Q. Of the 121,250,000?

8 A. I don't think I can determine it from
9 this -- from what you handed me, no.

10 Q. Well, if Southern Union raised \$300 million
11 through a common stock offering and an equity units
12 offering that right now is debt but converts to common
13 equity in 2006, could you apportion what percentage of the
14 300 million --

15 MR. MICHEEL: I'm going to object to that
16 question. It assumes facts not in evidence.

17 JUDGE WOODRUFF: What facts are you saying
18 are not in evidence?

19 MR. MICHEEL: He said, let's assume that
20 Southern Union had a \$300 million equity offering. I
21 don't think those facts are in evidence.

22 MR. HERSCHMANN: I believe they are in
23 evidence. We already discussed it. I don't think --

24 JUDGE WOODRUFF: This is an assumption
25 about a --

1 MR. HERSCHMANN: Southern Union issued 300.
2 I mean, this is testimony that's come in. There was in
3 June of 2003 a total of \$300 million raised in common
4 stock and equity units. It's throughout the testimony
5 that the equity units convert in 2006. Mr. Dunn just
6 talked about it yesterday.

7 JUDGE WOODRUFF: I'm going to overrule the
8 objection. You can answer the question.

9 THE WITNESS: And your question again? I'm
10 sorry.

11 BY MR. HERSCHMANN:

12 Q. I'll go back and try to remember it. If
13 Southern -- well, if equity units are raised and they're
14 considered debt initially and convert to equity
15 subsequently, how is that currently maintained on the
16 books, according to GAAP, of Southern Union?

17 A. I believe it's recorded as debt.

18 Q. And if common stock was issued at the same
19 time, how would the common stock be listed?

20 A. It would be in stock and premium paid on
21 stock.

22 Q. Is that the equity?

23 A. Yes.

24 Q. And if an additional \$121 million was
25 provided for the purchase of Panhandle based on the

1 raising of the \$300 million, would it be appropriate to
2 consider part of it used as debt and part of it as equity
3 for that position, or do you know the answer to that?

4 A. I'm not sure I can answer that.

5 MR. HERSCHMANN: If I can have one moment,
6 please.

7 JUDGE WOODRUFF: You may.

8 BY MR. HERSCHMANN:

9 Q. Do you remember being asked certain
10 questions about GAAP and its applicability to this
11 Commission?

12 A. Yes, I do.

13 Q. I think there was some confusion. Were you
14 discussing as to whether or not the books of the
15 Commission had to comply with GAAP, since they're a state
16 agency that it would not have to comply with GAAP?

17 A. At one point that's the answer I gave,
18 because I presumed that that was the question.

19 Q. And maybe I can try to clarify.
20 Do you know whether or not this Commission
21 is required to comply with GAAP in issuing or rendering
22 its opinions?

23 A. I do not know for absolute certainty.

24 MR. FRANSON: Your Honor, I will object at
25 this point. The question has been answered. It was do

1 you know. That's a yes or no, and this witness has
2 answered. Anything else would be nonresponsive, and I
3 would object on that basis.

4 JUDGE WOODRUFF: I think he has answered
5 the question. Anything further would be nonresponsive.
6 Do you have another question?

7 BY MR. HERSCHMANN:

8 Q. Have you provided testimony before any
9 other commissions in relationship to the compliance with
10 GAAP?

11 MR. FRANSON: Your Honor, objection on
12 relevance. This is the Missouri Commission, not --

13 JUDGE WOODRUFF: Overruled.

14 THE WITNESS: Yes, I have.

15 BY MR. HERSCHMANN:

16 Q. And on those occasions, did the decisions
17 of the Commission comply with GAAP in relationship to the
18 companies that were appearing?

19 A. In relationship to my testimony, they did,
20 yes.

21 Q. And is the company in this case subject to
22 GAAP?

23 A. The company is absolutely subject to GAAP.

24 Q. And does GAAP reflect MGE's costs related
25 to its operation in Missouri?

1 A. Yes, it does.

2 MR. HERSCHMANN: I have no further

3 questions.

4 JUDGE WOODRUFF: Thank you. You may step

5 down.

6 THE WITNESS: Thank you.

7 MR. FRANSON: Your Honor, just a

8 housekeeping matter. Is the witness finally excused? I'm

9 sure that that will be a question that will come up.

10 JUDGE WOODRUFF: Yes, I believe he's

11 finally excused. You can go home, Mr. Gillen.

12 THE WITNESS: Thank you very much.

13 JUDGE WOODRUFF: All right. I believe,

14 then, we'll go back to Mr. Allen and pick up where we left

15 off yesterday.

16 MR. MICHEEL: And just, your Honor, so I

17 can make sure, we were on the voir dire of the witness; is

18 that correct?

19 JUDGE WOODRUFF: That is correct. Just so

20 the record is clear, when we left off yesterday afternoon,

21 MGE had made the motion to challenge the admission of this

22 witness' testimony on the grounds that he's not an expert.

23 There was extensive voir dire about that, and I promised

24 Public Counsel an opportunity to respond to that voir dire

25 to rehabilitate his witness.

1 MR. MICHEEL: First, your Honor, I'd like
2 to mark an exhibit, and that is the deposition of Travis
3 Allen. I think the whole deposition should come in. I'd
4 also like to reserve a number to get the complete video
5 deposition. I'm in the process of getting that.
6 Yesterday it was just a snippet of the deposition, so I'd
7 like to do that at least at the outset. And I believe
8 that Mr. Allen's deposition would be Exhibit 216.

9 JUDGE WOODRUFF: Yes, it would be. And
10 this is the entire transcript?

11 MR. MICHEEL: Yes, your Honor.

12 (EXHIBIT NO. 216 WAS MARKED FOR
13 IDENTIFICATION BY THE REPORTER.)

14 JUDGE WOODRUFF: And you said you wanted to
15 reserve a number for the video transcript?

16 MR. MICHEEL: Yes. That would be
17 Exhibit 217. I guess I will late file that on EFIS, your
18 Honor.

19 TRAVIS ALLEN testified as follows:

20 VOIR DIRE EXAMINATION BY MR. MICHEEL:

21 Q. Mr. Allen, do you have a copy of your
22 deposition with you?

23 A. Yes, I do.

24 Q. Has that been marked as Exhibit 216?

25 A. Yes, it has.

1 Q. And have you provided an errata sheet and a
2 signature page to that deposition?

3 A. Yes, I have.

4 MR. MICHEEL: With that, your Honor, move
5 the admission of Exhibit 216.

6 JUDGE WOODRUFF: Exhibit 216 has been
7 offered into evidence. Any objections?

8 MR. HERSCHMANN: Yes. Objection on
9 hearsay. It's an out-of-court statement offered for the
10 truth of the matter asserted therein, and further, the
11 witness is here to testify.

12 I'm not sure under what theory we're
13 offering in deposition testimony. The questions and the
14 portions that we played related directly to the rule of
15 the preliminary admissions as to whether or not this
16 witness was qualified to give the testimony. I mean,
17 counsel has the witness here. If he can lay the
18 foundation with the witness in the box that he has a
19 foundation, then that's the basis for challenging a voir
20 dire challenge, not to try to put in a deposition.

21 JUDGE WOODRUFF: Your response?

22 MR. MICHEEL: Your Honor, I think it's
23 clear under Missouri law that depositions can be used for
24 any purpose. I mean, if we want to be here all day, I'll
25 just go through all the questions and the answers in the

1 deposition. I'm trying to speed things along. And I
2 don't think it's hearsay. It was sworn testimony. I've
3 asked this witness specific -- I mean, I can ask him if
4 those were his answers and questions, if they're true and
5 correct.

6 MR. FRANSON: Your Honor, the rules in law
7 are very clear. Depositions are admissible by any party
8 for any purpose.

9 MR. HERSCHMANN: Should I address that?

10 JUDGE WOODRUFF: Yes, go ahead.

11 MR. HERSCHMANN: If counsel's right, then
12 there's no need to ever have a trial. I mean, the
13 foundation of having the witness available, the hearsay
14 rules clearly apply. This is an out-of-court statement
15 offered for the truth of the matter asserted therein. I
16 don't know if he'd give the same answers to some of this
17 or not.

18 But the basis for the objection and the
19 limited portions that were offered is foundational, and
20 that is whether this witness is qualified as an expert to
21 testify in this proceeding. If they don't qualify him or
22 try to address that issue, they're trying to offer an
23 entire deposition. That doesn't address the issue at
24 hand. He'd still have to lay a proper foundation.

25 JUDGE WOODRUFF: What is the purpose in

1 offering this entire deposition?

2 MR. MICHEEL: To give a fair and accurate
3 view of Mr. Allen's deposition yesterday. There were
4 snippets and a heavily edited videotape put into the
5 record, and this gives a clear understanding of what
6 Mr. Allen testified to in his deposition. And it also
7 gives a clear understanding of what Mr. Allen's expertise
8 is, what his backgrounds are and how he qualifies as an
9 expert in this proceeding.

10 JUDGE WOODRUFF: Your response?

11 MR. HERSCHMANN: It was cross-examination.
12 In a cross-examination under any circumstances, I can lift
13 questions that are complete questions and answers and use
14 in cross-examination. That doesn't mean that someone's
15 entire deposition comes out or else you defeat the whole
16 purpose of having a cross-examination.

17 This is how it's done; you cross-examine
18 the witness. You don't get to come up and say, let me
19 offer whatever depositions you may have given at whatever
20 point and just put them in the record. That's not how the
21 process works.

22 JUDGE WOODRUFF: Mr. Franson?

23 MR. FRANSON: Your Honor, with all due
24 respect to Mr. Herschmann, he's just plain wrong here.
25 Rule 57.07 is abundantly clear. Depositions are

1 admissible in court. This Commission is covered by its
2 rules, the civil rules of procedure. They are admissible
3 for any purpose by any party, period, end of discussion,
4 and that is what the rule says.

5 So I'm suggesting that all of this is
6 simply superfluous. All of these other depositions have
7 come in, and the reason is the rules allow it, and that's
8 what we're seeing here. And no, all trials are not going
9 to become irrelevant because generally you don't
10 necessarily depose every single person, and even if you
11 do, you still generally have something different to
12 present at trial.

13 So I'm just suggesting that all of the
14 depositions that are offered are admissible by any party
15 for any purpose. If they want to use parts of them, the
16 other parties can bring in more. If they want to use the
17 whole thing, they can.

18 JUDGE WOODRUFF: I am concerned about
19 wholesale dumping of not just this deposition but all the
20 depositions into the record without guidance from the
21 Commission on what is important about these depositions.

22 Go ahead.

23 MR. MICHEEL: And I think the importance of
24 this deposition is if -- the whole deposition read as a
25 whole demonstrates that Mr. Allen is qualified as an

1 expert to give his expert testimony here.

2 JUDGE WOODRUFF: I'm going to overrule the
3 objection and let the deposition into the record. Let's
4 go on.

5 Exhibit 216 is admitted into evidence.

6 (EXHIBIT NO. 216 WAS RECEIVED INTO
7 EVIDENCE.)

8 BY MR. MICHEEL:

9 Q. Mr. Allen, could you describe your
10 undergraduate education, what type of degree you have?

11 MR. HERSCHMANN: Just for the record, I'm
12 renewing my objection pursuant to 490.065. We didn't have
13 a ruling, that's why I'm doing it now before he --

14 JUDGE WOODRUFF: I think we're still in
15 voir dire here.

16 MR. MICHEEL: Yes, we are.

17 JUDGE WOODRUFF: Okay. And I understand
18 your objection is still there, and you made that
19 yesterday, I believe. The Commission will not rule on it
20 at this point, and it will be ruled upon at a later date
21 after evidence has been heard.

22 MR. HERSCHMANN: I just want it noted for
23 the record.

24 JUDGE WOODRUFF: I understand. That's
25 fine.

1 BY MR. MICHEEL:

2 Q. Could you tell me what you have your
3 undergraduate degree in?

4 A. I received an undergraduate degree from
5 Southern Illinois University - Edwardsville in business,
6 economics and finance with a specialization in financial
7 markets and institutions.

8 Q. And did you receive that degree with any
9 sort of honors?

10 A. Yes, I graduated magna cum laude with a GPA
11 of 3.806.

12 Q. Did you take any classes during your
13 undergraduate education that relate to determining cost of
14 capital for an entity?

15 A. Yes, I did.

16 Q. Did you take any classes during your
17 undergraduate education that relate to determining the
18 appropriate capital structure to use in financial
19 analysis?

20 MR. HERSCHMANN: Objection, leading.

21 JUDGE WOODRUFF: Overruled.

22 THE WITNESS: Yes, I took several classes
23 in my undergraduate studies regarding capital structure.
24 Specifically I can name you -- one class I took was
25 Finance 320. It's -- the course name is financial

1 management and decision-making. A --

2 MR. HERSCHMANN: I'm sorry for

3 interrupting. The witness seems to have some documents in

4 front of him that he's reading from. I don't know what

5 those are, but those documents, I believe, would clearly

6 be hearsay. At least if we could see them and know what

7 he's using, it may be beneficial.

8 JUDGE WOODRUFF: If you could show the

9 parties what you're reading from.

10 THE WITNESS: Sure. This is a copy of my

11 transcript, and this is a copy of the course descriptions

12 that I took.

13 MR. HERSCHMANN: If I could see them?

14 JUDGE WOODRUFF: Certainly.

15 MR. MICHEEL: Do we need to go off the

16 record?

17 JUDGE WOODRUFF: Do you want to go off the

18 record for a moment?

19 MR. HERSCHMANN: Yeah, just to take a look

20 at it.

21 JUDGE WOODRUFF: Let's go ahead and take a

22 break. We'll come back at 10 o'clock.

23 (A BREAK WAS TAKEN.)

24 JUDGE WOODRUFF: While we were on break,

25 Mr. Herschmann had a chance to look at those documents

1 that you wanted to look at, and he now wishes to ask some
2 voir dire questions about those documents.

3 So you may proceed.

4 FURTHER VOIR DIRE EXAMINATION BY MR. HERSCHMANN:

5 Q. Mr. Allen, the first document that you
6 handed me was a copy of your college transcript; is that
7 correct?

8 A. I don't know if it's the first one I handed
9 you or not, but yeah, I handed you a copy of my college
10 transcript, yes.

11 Q. And was the other a course description
12 printout?

13 A. Yes.

14 Q. What year did you graduate college?

15 A. I graduated with my bachelor's degree in
16 December of 2001, and my master's degree in May of 2003.

17 Q. In the course description printouts, does
18 that include both your college and graduate school course
19 descriptions?

20 A. No, it just -- this is just a course
21 description of my undergraduate studies.

22 Q. And you graduated college in 2001, right?

23 A. Correct.

24 Q. And some of the courses that you took dated
25 back to which year? When did you first start college?

1 A. When I first went to SIUE was August of
2 1999.

3 Q. And this transcript covers all the courses
4 you took from August of 1999 'til you graduated; is that
5 correct?

6 A. That's correct.

7 Q. What is the date on the course description
8 printout that you just got off the Internet? Withdraw it.
9 I'm sorry.

10 Did you get the course description printout
11 off the Internet?

12 A. Yes, I got the course description printout
13 from the Southern Illinois University - Edwardsville
14 website.

15 Q. And what date did you get the printout?

16 A. May 26, 2004.

17 Q. And some of the courses that are referenced
18 in the course description that correspond to your
19 transcript, that's a five-year later description of the
20 course, right? You started in '99. The printout just
21 came from a couple of weeks ago, or about a month ago?

22 A. Yeah, that's correct.

23 Q. Do you know if the courses have changed in
24 five years? Withdraw that.

25 Have you gone back to take the classes

1 again since 1999?

2 A. No.

3 Q. So you don't know if the courses are the
4 same from five years ago as they are today, right?

5 A. Well, looking at the course description,
6 the titles of the courses and my understanding of what I
7 covered in those courses, I can assure you that the ones
8 that I would testify to on this printout from course
9 descriptions are the classes that I took.

10 Q. Presumably you can look at your transcript
11 and tell us what those classes were about because you
12 actually lived through it without having to refer to a
13 five-year later course description, right?

14 A. I think to have this as a reference jogs my
15 memory specifically, so I'm more comfortable doing it that
16 way.

17 Q. This is your area of expertise, right?
18 That's what you told us, right?

19 A. Yeah, this is my area of expertise.

20 Q. You need a course description to jog your
21 memory about what you took in your area of expertise? I
22 thought you told us yesterday you were more than qualified
23 to render the opinions.

24 A. There are two questions there. Which one
25 do you want me to answer first?

1 Q. Both, in any order you want.

2 A. Can you repeat?

3 Q. Sure. You told us yesterday that you were

4 more than qualified to provide the opinions in this

5 matter, right?

6 A. Correct.

7 Q. And your area of expertise you said is

8 based on your education, right?

9 A. Correct.

10 Q. Are you telling us now that you need to

11 look at a course description to describe what you learned

12 back in college?

13 A. I don't need to look at a course

14 description and tell you my knowledge, but to give you a

15 specific on exactly what was covered in a specific class,

16 it is helpful to have that.

17 Q. You don't have the foggiest idea, do you,

18 sir, as to whether or not a course description that was

19 just printed out a month ago was exactly what you learned

20 five years ago, right?

21 A. No, that's not correct.

22 Q. Do you know if the same professors are

23 teaching the same classes? Did you go back and check to

24 make sure all the professors are teaching the exact same

25 classes with the exact same books, no new editions or

1 anything in the last five years?

2 A. I know that for specific classes that I
3 tutored, that they were still using the same book after I
4 had taken the course and still being taught by the same
5 professors. A lot of courses that I took -- SIUE is not a
6 huge department, so a lot of the courses are continuously
7 taught every semester by the same instructor, yes.

8 Q. So presumably you know what those courses
9 are about, right?

10 A. Your question was whether or not --

11 Q. I have another question now. Presumably
12 you know what those courses are about, right? You just
13 told us they're same ones over and over.

14 A. I told you, yes, it's the same instructors.
15 I have a general understanding. Again, to cover the exact
16 topics of discussion, then it's helpful to have a guide.
17 It's not saying that, I mean, to ask -- I don't ask you to
18 you remember, you know, what you had for lunch three years
19 ago or, you know, what case did you try three years ago,
20 what exactly were the issues in that case?

21 Q. And I don't offer expert testimony when I
22 don't have the training either, sir.

23 A. Well, I have the training. I disagree with
24 you there.

25 Q. Tell me -- without looking at anything,

1 tell me the exact course that you took that addressed use
2 of the DCF, the CAPM and the risk premium method as it
3 related to natural gas utilities in either college or
4 graduate school.

5 A. See, that's the problem.

6 Q. I want to know if you took the course. Is
7 there a course that you took that addressed the use of the
8 DCF method, with a CAPM and risk premium as it relates to
9 utilities? And then -- I want an answer to that question,
10 and then specifically in the natural gas industry.

11 A. The answer to your question is, I took a
12 course in portfolio analysis, I took a course in security
13 analysis, as well as corporate anal-- and I think that was
14 the title of the course, corporate analysis. And the
15 answer to your question is that there is no specific
16 courses regarding finance in public utilities. You get a
17 degree in finance. You don't get a degree in finance in
18 public utilities.

19 When I have a driver's license, I have the
20 skills to go out and drive a car. I don't have a driver's
21 license that says, okay, you have the skills to drive a
22 Mustang, you don't have the skills to drive a Ford F-150.
23 It's applicable. You learn the basic fundamental skills
24 that are absolutely applicable across industries. So your
25 question is not on -- is not on target.

1 Q. Let me use your car example for a minute.
2 When you got your driver's license, you didn't think you
3 had the skills to drive professionally as an expert?
4 Could you drive in a racing setting? Did you think you
5 had those qualifications because you got your driver's
6 license?
7 A. I could have drove in a race, absolutely.
8 Q. And you think you were qualified to get in
9 the Indy 500 and drive because you had that? That's what
10 you're telling us, that's your analogy?
11 MR. MICHEEL: I'm going to object, your
12 Honor. This is beyond the scope, and now he's badgering
13 the witness at this point.
14 JUDGE WOODRUFF: I'll sustain the
15 objection.
16 THE WITNESS: Could you repeat your
17 question?
18 JUDGE WOODRUFF: The objection was
19 sustained.
20 THE WITNESS: I'm sorry.
21 JUDGE WOODRUFF: You don't have to answer
22 that question. He's going to ask you another one.
23 THE WITNESS: I'm sorry.
24 BY MR. HERSCHMANN:
25 Q. Are you telling us you don't think there

1 are any courses that deal with utility finance and the
2 application of the CAPM, the risk premium and the DCF
3 methodology for utilities?

4 A. No, that's not what I'm saying. What I'm
5 saying is that you get a degree in finance. You learn the
6 basic building blocks of the CAPM and the DCF model and
7 capital structure and capital budgeting decisions that are
8 applicable across sectors.

9 Q. Let me ask you my question, and see if you
10 can answer it. Did you take any courses that specifically
11 addressed the usage of the DCF model, CAPM and risk
12 premium as it related to utilities? It's a yes or no.

13 MR. MICHEEL: I'm going to object. It's
14 been asked three times, and he's given his answer three
15 times.

16 JUDGE WOODRUFF: It's a yes or no question,
17 if you could answer yes or no, please.

18 THE WITNESS: Could you repeat the
19 question?

20 MR. HERSCHMANN: Would you read it back,
21 please?

22 THE REPORTER: "Question: Let me ask you
23 my question, and see if you can answer it. Did you take
24 any courses that specifically addressed the usage of the
25 DCF model, CAPM and risk premium as it related to

1 utilities? It's a yes or no."

2 THE WITNESS: Is your question, was my
3 course title the use of CAPM -- if this is your question,
4 was the course title I took the use of CAPM in the DCF
5 model as it relates to or applied to a public utility
6 company, no, I didn't take that course.

7 MR. HERSCHMANN: I'd ask the witness be
8 directed to answer the question that I posed. I didn't
9 ask if it was the course title.

10 JUDGE WOODRUFF: Please answer the question
11 that was asked, if you can. Could you read back the
12 question again?

13 THE REPORTER: "Question: Let me ask you
14 my question, and see if you can answer it. Did you take
15 any courses that specifically addressed the usage of the
16 DCF model, CAPM and risk premium as it related to
17 utilities? It's a yes or no."

18 THE WITNESS: That specific question, I
19 would have to say yes, because in my studies we did talk
20 about public utility companies, but again, I didn't take a
21 course that said DCF and CAPM for a public utility.

22 JUDGE WOODRUFF: He's not asking you the
23 title. I think you've answered the question when you
24 first answered it. All right.

25 BY MR. HERSCHMANN:

1 Q. Did you go back and verify with your school
2 as to whether or not the descriptions that you printed out
3 on May 26, 2004 were the exact same course descriptions
4 that are applicable today?

5 A. That are applicable this date today?

6 Q. Yes or no, right.

7 A. No, I did not do that, but I mean, it was
8 only a month ago.

9 Q. Did you some point after May 26, 2004, up
10 until today, did you go back and contact your school to
11 ask them whether the course descriptions that are
12 contained in this document accurately reflect the courses
13 that you took beginning in 1999? That's a yes or no, did
14 you contact the school?

15 A. No, I did not.

16 MR. HERSCHMANN: I would object to the
17 witness using this exhibit in any way. I don't think
18 there's any foundation.

19 MR. MICHEEL: I don't have a problem if he
20 doesn't use that exhibit. Could you just give that to me,
21 Mr. Allen?

22 I didn't know it was going to take up 15 to
23 20 minutes.

24 JUDGE WOODRUFF: It's not been offered as
25 an exhibit, so it's not an exhibit. It's a document the

1 witness was using to refresh his memory. Since the
2 parties agree on it, I'm not going to make any other
3 ruling on it.

4 MR. MICHEEL: I don't know where we were
5 when we went down this rabbit path, so let me just start
6 again from the beginning.

7 FURTHER VOIR DIRE EXAMINATION BY MR. MICHEEL:

8 Q. Mr. Allen, did you take any classes as an
9 undergraduate that related to determining -- doing
10 analysis for a discounted cash flow method, the capital
11 asset pricing method?

12 A. Yes, I did.

13 Q. And what classes were those, sir?

14 A. Did you say as an undergraduate?

15 Q. Yes, as an undergraduate.

16 A. One course was -- the course number was
17 Finance 320; the title was financial management and
18 decision-making. And that course introduced me to the DCF
19 model, the capital asset pricing model, capital budgeting
20 decisions, as well as the valuation of securities,
21 obviously.

22 Q. And what grade did you receive in that
23 course?

24 A. I received an A.

25 MR. HERSCHMANN: If it'll help, I'll

1 stipulate that his transcript says whatever it says.

2 JUDGE WOODRUFF: The transcript's not in
3 evidence.

4 MR. MICHEEL: The transcript's not in
5 evidence, and I think I'm entitled to rehabilitate this
6 witness as I choose, your Honor.

7 JUDGE WOODRUFF: There wasn't really an
8 objection there, but I'll allow him to proceed.

9 BY MR. MICHEEL:

10 Q. Was there any other courses that you took
11 as an undergraduate that prepared you or that you looked
12 at or studied the DCF?

13 A. Where I specifically studied the DCF,
14 another course that I took was -- the course number was
15 Finance 430; the title was portfolio analysis. In that
16 course, I studied -- along with portfolio evaluation, we
17 studied various valuation -- equity valuation techniques,
18 including, again, the DCF model, as well as the CAPM
19 model, and various risk characterizations.

20 Q. And as part of your course work in that
21 course, did you do some DCF modeling?

22 A. Yes, and I received an A in that course.

23 Q. Were there any other courses in your
24 undergraduate work that dealt with DCF or determining the
25 cost of capital or any other sort of company?

1 A. In my undergraduate curriculum, we dealt
2 with it in my -- to some extent in my Finance 431 class.
3 It is a derivative securities class. That class was more
4 geared towards the use of derivative securities to hedge
5 risks, but we did talk about valuation techniques in that
6 course, yes.

7 Q. And what was your grade in that course?

8 A. I received an A.

9 Q. Did you take any undergraduate courses that
10 dealt with determination of the appropriate capital
11 structure for use as of -- for doing financial analysis?

12 A. As an undergraduate --

13 MR. HERSCHMANN: Objection, leading, vague
14 and ambiguous.

15 JUDGE WOODRUFF: Overruled. You can answer
16 the question.

17 THE WITNESS: Yeah, in my Finance 430
18 class, we talked about capital structure, as well as, I
19 believe, in my Finance 430 class, the portfolio class, but
20 mainly capital structure issues, those were more
21 advanced-type issues and those were what I covered in my
22 graduate studies.

23 BY MR. MICHEEL:

24 Q. Were there any other classes that you took
25 as an undergraduate that prepared you to conduct financial

1 analysis?

2 A. Yes, there was a lot of classes that built
3 my basic foundation of knowledge that an analyst would
4 have to have in order to perform a -- a thorough analysis.
5 One of those courses was my intermediate macroeconomic
6 theory course, and that course really -- really was a
7 course regarding markets, competition, general price and
8 quantity determinations, basic microeconomic theory course
9 type material.

10 Another course that I took was -- oh, I'm
11 sorry. And I received an A in that course.

12 Another course that I took was
13 Economics 302, which was an intermediate macroeconomic
14 theory course in which I received an A in. This course
15 introduced me or -- to basically an understanding of the
16 economic -- the overall economic environment, interest
17 rates, inflation, a basic understanding of the overall
18 macro economy.

19 Another course that I took was statistical
20 analysis for business decisions. That course is a
21 statistics course that helped me build the knowledge to
22 understand the various statistical measures that you have
23 to use as a financial analyst. Also we dealt with
24 regression analysis, ordinary least squares prediction
25 intervals.

1 Another course that I took was a GBA --
2 they call it GBA 300. And the course title is foundation
3 of business knowledge, and that course was almost like
4 a -- a discussion-type format where we discussed current
5 issues, how it related to companies, what it meant for the
6 companies. It was kind of like -- almost like a current
7 events for business knowledge-type course.

8 Q. Now, in your statistical analysis class,
9 what grade did you receive?

10 A. I received a B in that course.

11 Q. And in your Economics 302 class, what grade
12 did you receive?

13 A. I received an A in that course.

14 Q. Let's move on to your graduate school
15 education. Were there any classes that you took in your
16 graduate school education that dealt with determining the
17 cost of equity for any sort of company?

18 A. I'm sorry. There was still more I wanted
19 to get to on my undergraduate studies.

20 Q. Well, let's go to your graduate studies
21 right now.

22 A. Okay.

23 Q. Were there any classes in your graduate
24 studies that allowed you to determine the cost of capital
25 for any sort of company?

1 A. Yes. Specifically we dealt with cost of
2 capital, as well as capital structure valuation
3 techniques, including the DCF model and the capital asset
4 pricing model that I used in my analysis. I covered those
5 extensively in my graduate study of Finance 528. That
6 was -- the title of that course was security analysis and
7 modeling, and I received an A in that course.

8 Q. In that course, Finance 528, did you do any
9 modeling?

10 A. Yes, we used the DCF and the CAPM model.
11 We discussed -- we discussed it thoroughly. We discussed
12 -- it was a more in-depth class. We discussed the
13 component parts. As an undergraduate, you really just
14 looked at here are the components, how do you do this
15 calculation?

16 As a graduate student, what you did, it was
17 a more extensive and thorough analysis of individual
18 component parts, the advantages and disadvantages of them,
19 so it really allowed you to explore the models in-depthly
20 and make your own determination of what you believe was
21 the most appropriate way of performing the analysis.

22 Q. And do you know whether those models apply
23 across industry sectors?

24 A. Absolutely. I mean, with the DCF model,
25 and specifically it's more an issue of degree of

1 relativeness, but the DCF model that Gordon developed in
2 his seminal book, The Cost of Capital for a Public
3 Utility, is -- is the public utility sector is almost an
4 ideal case for the use of that model because it's a mature
5 industry.

6 Q. After your -- were there any other courses
7 other than the Finance 528 course in your graduate school
8 work that prepared you to be a financial analyst?

9 A. I would like to speak about another course
10 where we did specific DCF and CAPM. Is that okay?

11 Q. Tell me about your courses.

12 A. Yeah. Another course where I specifically
13 engaged in detailed studies regarding the DCF, CAPM,
14 capital structure, capital evaluation techniques was my
15 Finance 460 course, and the title of that course was
16 corporate financial analysis and strategy. I received an
17 A in that course.

18 Also in my graduate studies for general
19 education that prepared me to understand how everything
20 fit together in an analysis, I took a course in financial
21 innovations in engineering. I also took an advanced
22 microeconomic theory course, which again, it was -- it was
23 cost determination in markets, various market
24 applications. This course was more rigorous in the fact
25 that it dealt with the mathematics behind the theory that

1 is taught in the undergraduate level.

2 I also took an advanced -- I'm sorry. I
3 received an A in that advanced microeconomic theory
4 course. I also took an advanced macroeconomic theory
5 course, which again, it was a more thorough analysis of
6 overall economic intricate parts of the economy, as well
7 as fiscal policy, monetary policy. I received an A in
8 that course.

9 Also I took a financial strategy growth and
10 control course, which covered extensively mergers and
11 acquisitions of firms, what it does as far as to the value
12 of stock, et cetera. I received a B in that course.

13 I think that's a good synopsis of my
14 graduate education.

15 Q. And did those courses prepare you to
16 provide testimony regarding appropriate capital structure
17 and return on equity for any type of company?

18 A. Absolutely, yes. It's a foundation of
19 skills, knowledge and education that you learn in college,
20 that I learned in college specifically, that allowed me to
21 come in here and perform this analysis thoroughly. And I
22 do it for, you know, not only public utility but across
23 sectors, absolutely.

24 Q. You indicated there were other
25 undergraduate courses that you took that related. Could

1 you tell me about those?

2 A. Yes. I'm trying to remember which ones
3 they were. Okay. One course that I wanted to mention was
4 a business forecasting course that I took as an
5 undergraduate student. The course title was -- or I'm
6 sorry. The -- it was called Econ 417. Econ Finance 417
7 is how they refer to it, because it's kind of a mixture.
8 And in that course we studied various predictions or
9 various models used to make forecasts, the future.

10 Specific models that I remember are the OLS
11 regression models, also consensus forecast, which is what
12 we use, has been referred to in this course -- or I'm
13 sorry -- has been referred to in this testimony, the
14 direct testimony. I also took a course -- oh, and I
15 received an A in that course.

16 I took a course in quantitative methods for
17 economic and business analysis. That course, again, gave
18 me the mathematics that I needed to -- or supplemented my
19 mathematical understanding that I needed to perform my
20 analyses correctly.

21 And I also want to add that I took -- I got
22 an A in that Econ 400 quantitative methods course.

23 I also want to add that I took a course in
24 introduction to econometrics, and what that course was, it
25 was the use of linear regressions to make predictions and

1 correlations between variables. It's kind of a hard class
2 to describe.

3 Q. And did those courses further prepare you
4 for filing testimony regarding -- or determining cost of
5 capital for any sort of company in determining a capital
6 structure?

7 A. Absolutely. While they didn't
8 specifically -- those classes didn't specifically --
9 specifically cover the DCF model, CAPM, capital structure,
10 those are basic foundational skills and knowledge that you
11 need in order to perform an analysis thoroughly. I want
12 to add that I got an A in that econometrics course that I
13 was speaking of.

14 Q. And for your graduate school, what was your
15 overall GPA, your grade point average?

16 A. 3.7.

17 Q. What books did you read and rely on prior
18 to filing your testimony in this proceeding?

19 A. I reviewed the Principles of Corporate
20 Finance book, which was authored by Stewart Myers and
21 Richard Brealey. I read the Cost of Capital to a Public
22 Utility book, which was authored -- it's a seminal book in
23 public utility financial analysis, and that was authored
24 by Dr. Myron Gordon, who is a preeminent expert in the
25 field of public utility financial analysis and equity

1 evaluation. He's referred to as the father of the DCF
2 model, and in that book he describes various growth rate
3 methodologies that he believes to be appropriate, and one
4 of those is the methodology that I used, the sustainable
5 growth rate.

6 MR. HERSCHMANN: I'm sorry. I think the
7 question was, what books did he read to prepare his
8 testimony.

9 JUDGE WOODRUFF: He has gone beyond that
10 and is nonresponsive, if you want to ask another question.

11 BY MR. MICHEEL:

12 Q. That's fine. Are there any other books
13 that you read for preparing your testimony?

14 A. Yes. I reviewed the Fundamentals of
15 Investment, authored by Gordon Alexander and William
16 Sharp, who was one of the two guys who invented the
17 capital asset pricing model, as well as authored by
18 Jeffrey Bailey.

19 I also reviewed Investment Analysis and
20 Portfolio Management book, authored by Frank Reilly and
21 Keith Brown, as well as the Essentials of Corporate
22 Finance book, authored by Steven Ross, Randy Westerfield
23 and Bradford Jordan. Also I reviewed Cost of Capital, a
24 Practitioner's Guide, and that book was authored by David
25 Parcell.

1 Q. Did you provide this information to the
2 company in response to a Data Request well over a month
3 ago?

4 A. Yes, I did.

5 Q. Other than those books, did you review any
6 other information in preparing -- before you prepared your
7 testimony?

8 A. Yes, I did.

9 Q. And could you tell us what information you
10 reviewed?

11 MR. HERSCHMANN: I'm sorry, your Honor.
12 I'm going to object to the question. As we said, the
13 testimony, if we could have a breakdown as whether it was
14 prior to the direct, rebuttal or surrebuttal.

15 JUDGE WOODRUFF: If you could clarify.

16 MR. HERSCHMANN: If you could clarify it
17 for the first listing of the books.

18 BY MR. MICHEEL:

19 Q. Mr. Allen, did you read those books -- when
20 did you read those books that you talked about?

21 A. Prior to filing direct testimony in this
22 case, Case GR-2004-0209.

23 Q. Now, prior to filing testimony in this
24 case, is there other information that you reviewed before
25 preparing your testimony?

1 A. Yes, there is.

2 Q. And what information was that?

3 A. I reviewed the ValueLine Investment Survey.

4 I reviewed C.A. Turner Utility Reports. I reviewed Yahoo

5 Finance. I reviewed Ibbotson & Associates 2002 Yearbook,

6 as well as the Ibbotson & Associates 2003 Yearbook. I

7 also reviewed Southern Union's 2003 annual report, as well

8 as all of the company's responses to the OPC Data Request

9 2001 through 2015.

10 I also reviewed the Bluefield Waterworks

11 and Improvement Company vs. Public Service Commission

12 case, as well as FTC vs. Hope Natural Gas case. I also

13 reviewed the Kansas City vs. Kansas City Gas Company case.

14 I also reviewed a variety of previous testimonies that I

15 can give the specific numbers, if you would like.

16 Q. Why don't you do that? And you did this

17 all before -- prior to filing your direct testimony?

18 A. Yes, as I stated in my deposition, that all

19 of this was filed prior to -- I mean, was read prior to

20 filing my direct testimony. If you look -- I read the

21 direct testimony of John Tuck in Case ER-93-41. I read

22 the direct testimony of John Tuck in WR-95-205/SR-95-206.

23 I read the direct testimony of Mark Burdette in

24 Case GR-2001-292. I read the direct testimony of David

25 Murray in Case GR-2001-292.

1 I also read the direct testimony of John
2 Dunn in Case GR-2001-292, as well as the direct testimony
3 of Mark Burdette in WR-2003-0500, direct testimony of
4 David Murray in Case WR-2003-0500, the direct testimony of
5 John Dunn in Case GR-2004-0209, the direct testimony of
6 Michael Noack in Case GR-2004-0209, the direct testimony
7 of James Oglesby, Case GR-2004-0209, the direct testimony
8 of John Quain in Case GR-2004-0209, the direct testimony
9 of Carlton Ricketts in Case GR-2004-0209, the direct
10 testimony of Jay Cummings in Case GR-2004-0209, and I
11 reviewed the Data Requests that I had sent out that had
12 come back to me prior to filing direct testimony.

13 Q. With respect to the book, The Cost of
14 Capital to a Public Utility, do you know if that's an
15 authoritative book in the field?

16 A. Yes, it is.

17 Q. And do you know if there are any other
18 witnesses in this proceeding who agree with you about
19 that?

20 A. I know for a fact that the Company Witness
21 Morin agrees with that. He's stated that in his
22 deposition. As far as anybody else, I can't say for them.

23 Q. The Cost of Capital, a Practitioner's
24 Guide, do you know if any other witnesses have utilized
25 that in this proceeding?

1 MR. HERSCHMANN: Objection, calls for
2 hearsay, unless he was there when they did it.

3 MR. MICHEEL: It's attached as a schedule
4 to Mr. Dunn's testimony. That's already in the record,
5 your Honor.

6 MR. HERSCHMANN: As we addressed yesterday,
7 if it's in the record, there's no reason to re-explore it.
8 I think that was the objection yesterday when I tried to
9 read a portion of an exhibit.

10 MR. MICHEEL: That wasn't my question.

11 JUDGE WOODRUFF: The question was, do you
12 know whether or not anyone else has relied on these
13 documents -- on these books, I believe.

14 MR. MICHEEL: Yes.

15 MR. HERSCHMANN: He has no ability of
16 knowing that from firsthand knowledge.

17 JUDGE WOODRUFF: From reading the testimony
18 he could.

19 MR. HERSCHMANN: That's not firsthand
20 knowledge.

21 JUDGE WOODRUFF: I'm going to overrule the
22 objection.

23 BY MR. MICHEEL:

24 Q. Do you remember the question?

25 A. Could you repeat it, please?

1 Q. Are you aware of any other witnesses who
2 have cited David Parcell's book -- David Parcell's book,
3 The Practitioner's Guide to Cost of Capital, in their
4 testimony?

5 A. Yeah. Mr. -- Mr. John Dunn did, and I know
6 that Dr. Morin referred to it in his deposition.

7 Q. Now, you talked about the ValueLine
8 Investment Surveys, C.A. Turner Utility Reports, the
9 Ibbotson & Associates reports, The Cost of Capital to a
10 Public Utility by Myron Gordon. Are those the sources and
11 types of information relied upon by -- are those sources
12 of information something relied upon by experts in their
13 field to form an opinion?

14 A. Yes, they are. I believe ValueLine has
15 been used by every -- every witness in this case that
16 filed direct testimony, and I know that Dr. Morin referred
17 to the C.A. Turner reports in his rebuttal testimony. And
18 I believe that Yahoo Finance -- well, I can't say that,
19 but it does -- it gave -- that's where I gathered my
20 Thompson Financial data, and that's definitely data that
21 is relied upon by experts in the field.

22 Q. What about the Ibbotson & Associates
23 Yearbook, is that a document or yearbook relied upon by
24 financial analysts?

25 A. Absolutely, it is.

1 Q. You talked about the Principles of
2 Corporate Finance by a Stewart Myers. Do you know if any
3 other witnesses in this proceeding believe that Mr. Myers
4 is a -- an expert?

5 MR. HERSCHMANN: Objection again, calls for
6 belief of other witnesses.

7 JUDGE WOODRUFF: I'll sustain this one. He
8 can't know what other witnesses might think.

9 BY MR. MICHEEL:

10 Q. Were you at Mr. Morin's deposition?

11 A. Yes, I was.

12 Q. Do you know if Mr. Morin testified at his
13 deposition that he believed that Stewart Myers was an
14 expert in the field?

15 MR. HERSCHMANN: Objection.

16 JUDGE WOODRUFF: Sustained.

17 MR. MICHEEL: His deposition is already in
18 the record, your Honor.

19 JUDGE WOODRUFF: Then it's in the record.

20 MR. MICHEEL: Okay.

21 BY MR. MICHEEL:

22 Q. Is the DCF a recognized way to determine
23 the rate of return for a regulated utility?

24 A. Absolutely, it is. As I mentioned before,
25 a regulated utility almost provides a perfect situation

1 for use of the DCF model.

2 Q. And is that one of the methods that you
3 utilized to determine the cost of capital in this case?

4 A. Yes, it is.

5 Q. And is that method being utilized by
6 Witness Dunn in this case?

7 A. Yes, that method is being utilized by both
8 Witness Dunn and Witness Murray in this case.

9 Q. Is the capital asset pricing method a
10 recognized method for determining or at least checking the
11 cost of capital in a regulated utility case?

12 A. Yes, it is.

13 Q. And did you utilize that method?

14 A. Yes, I did utilize that method.

15 Q. I want to talk to you about the component
16 parts of your DCF analysis. What are the component parts
17 of a DCF analysis, the major component parts?

18 A. The major component parts of the DCF
19 analysis are the growth rate, the stock price and the
20 dividend.

21 Q. And what did you utilize to determine the
22 growth rate in your DCF model?

23 A. I primarily utilized --

24 MR. HERSCHMANN: I'm going to object. This
25 is beyond the voir dire.

1 MR. MICHEEL: I don't think it is, your
2 Honor. I mean, he has challenged this witness'
3 credibility to give testimony, and I think I'm entitled to
4 explore how he did his DCF analysis and how it's supported
5 by other experts, and it's something that's relied upon in
6 the field.

7 MR. HERSCHMANN: My objection goes to his
8 qualifications. The question is, does he have the
9 qualifications to address it, not did he do it. That's
10 not the issue here. We're challenging the qualifications
11 as foundational. That was getting into the direct
12 testimony that was in his prepared testimony.

13 JUDGE WOODRUFF: Your response?

14 MR. MICHEEL: I think it is foundational.
15 If -- I mean, if this witness did an appropriate DCF
16 analysis, it indicates that he has the knowledge,
17 training, skill and education to present expert testimony
18 to this Commission. I think it goes directly to the
19 challenge of his qualifications, your Honor.

20 JUDGE WOODRUFF: I'm going to go ahead and
21 overrule the objection. I'm going to allow you some
22 leeway, since this is a rather unusual situation for the
23 Commission.

24 BY MR. MICHEEL:

25 Q. Did you get a growth component for your

1 DCF?

2 A. Yes, I did.

3 Q. And what growth component -- or explain to
4 me how you determined growth and what you relied on.

5 A. The way in which I determined growth, I
6 relied on Dr. Gordon's method that he proposed in his
7 seminal book, The Cost of Capital to Public Utilities, and
8 what is called the sustainable growth rate. It's the BR
9 plus SV growth rate where B is the retention rate, R is
10 return on equity, V is the increase or decrease in value
11 as a result of a stock issuance, and S is the -- it's the
12 fraction of new stock as -- I'm sorry, it's the amount
13 of new stock as a fraction of existing stock.

14 Q. And do you know if there's any support in
15 the financial literature for use of that?

16 A. Oh, yeah, there's -- there's a ton of
17 support for that methodology. If you look on page 8-31 of
18 Mr. Parcell's Cost of Capital, a Practitioner's Guide, he
19 lists that the method was adopted by FERC, as well as he
20 lists several textbooks that support the methodology. One
21 is Reilly, R-e-i-l-l-y, 1985, Cohen, Zinbarg, Zekel 1982,
22 Sharp 1985, Howe and Rasmussen 1982, and Brealey and
23 Myers, 1984, which is one of the books that I reviewed
24 prior to -- prior to filing my direct testimony.

25 Q. You indicated that the expected dividend is

1 some component of the DCF analysis, and what did you do
2 with respect to your expected dividend?

3 A. The way in which I decided to calculate the
4 expected dividend was using what is called the semi-annual
5 form of the DCF model, and what that form is, is that you
6 take the last dividend and you analyze it, and then you
7 multiply that times 1 plus 1/2 the growth rate. I believe
8 that's more appropriate than multiplying times 1 plus the
9 entire amount of the growth rate. I believe that it does
10 a better job of capturing investor expectations.

11 Q. And you indicated about the price of this
12 stock and what did you do in regard to that?

13 A. The way in which I calculated the price of
14 stock was I took an average of the last six weeks -- for
15 each individual company in my proxy group, I took stock
16 price average for the last six weeks in an effort to try
17 to capture the current capital markets for this company,
18 as well as limit the volatility. Since these rates are
19 going to be in effect for years until -- at least several
20 years until they come in for a next rate case, it's
21 important to get the most accurate measure of the current
22 investor expectations regarding the price of that stock.

23 Q. And was your information the most current
24 information used by any of the witnesses in this case?

25 A. Yes, it was.

1 Q. Did you also calculate a capital asset
2 pricing method?

3 A. Yes, I did.

4 Q. And could you tell me what the main
5 components of that are?

6 A. The main components of the capital asset
7 pricing method is that the return is equal to a risk-free
8 rate plus beta times return on the market minus risk-free
9 rate.

10 Q. And is that an accepted way to check
11 analyses in this type of area?

12 A. Yes, it is.

13 MR. MICHEEL: With that, your Honor, I
14 would end my voir dire and suggest that the motion should
15 be overruled, that this witness clearly by edu-- let me --
16 no, let me ask this.

17 BY MR. MICHEEL:

18 Q. Mr. Allen, prior to filing your direct
19 testimony, did you have any other training other than
20 reading books and your educational background?

21 A. Yes. As discussed in my deposition, I had
22 training; specifically I had a resource in Mr. John Tuck
23 that I had -- we had a meeting and we discussed various
24 aspects of regulation and cost of capital and regulation.

25 One thing I forgot to mention in my

1 deposition was --

2 MR. HERSCHMANN: Your Honor, I'm going to
3 object to this. He just asked the question of the other
4 sources. He said Mr. Tuck and now he's trying to
5 supplement his deposition testimony.

6 JUDGE WOODRUFF: It is nonresponsive. If
7 you have a specific question --

8 BY MR. MICHEEL:

9 Q. Other than your training with Mr. Tuck, did
10 you receive any other training?

11 A. Yes. Prior to filing direct testimony,
12 I -- I -- when I was getting my deposition taken, I had
13 forgotten this and I didn't mention it, but I had a
14 conversation about general regulation regarding natural
15 gas with Mr. Micheel, as well as a conversation with
16 Mr. Russ Trippensee regarding general regulation topics.

17 And also I went to a basics -- and this was
18 after I filed direct testimony. I went to a week-long
19 conference in New Mexico, and the conference was called
20 Basics of Public Utilities, and it covered a variety of
21 topics. I mentioned this yesterday, but something I
22 forgot to mention yesterday that it covered was general
23 natural gas, the workings of natural gas, how it works,
24 main lines, just general education.

25 MR. MICHEEL: With that, your Honor, I

1 would say that this witness more than meets the statutory
2 requirements as an expert, and I would ask the Commission
3 to overrule the objection.

4 MR. HERSCHMANN: Your Honor, I would like
5 the chance very briefly to follow up on some of the
6 questions that Mr. Micheel just addressed.

7 JUDGE WOODRUFF: All right.

8 FURTHER VOIR DIRE EXAMINATION BY MR. HERSCHMANN:

9 Q. You mentioned Mr. Parcell's book; is that
10 correct?

11 A. That's correct.

12 Q. What's that book entitled, sir?

13 A. The Cost of Capital, a Practitioner's
14 Guide.

15 Q. Now, you've testified that it's your belief
16 that your training allows you to apply the DCF, the CAPM
17 and the risk premium to any industry, right?

18 A. I testified that, yes, I could apply to any
19 industry. Specifically the DCF is most appropriate to
20 this industry, so it goes to -- it goes to weight for
21 different industries.

22 Q. Let me do this: I'm going to try to ask
23 you questions. Please try to focus on the questions that
24 I ask you. If you can answer the question without adding
25 along some additional testimony, I'd appreciate it.

1 You testified in response to Mr. Micheel
2 just a moment ago that you could apply your experience
3 across the full spectrum of industries, right?

4 A. I testified that I could apply my basic
5 knowledge and skills and calculate cost of equity.

6 Q. And you didn't need any special training,
7 according to you, as related to utilities, right?

8 A. As I said, the basics of how to calculate
9 DCF and CAPM, you learn those skills and those are
10 applicable across sectors.

11 Q. And remember some discussions with
12 Mr. Micheel referring to Professors Morin's book?

13 A. I don't believe he referred to Mr. Morin's
14 book.

15 Q. Do you recall in the cross-examinations
16 yesterday of Mr. Dunn --

17 A. Oh --

18 Q. -- that that's the primary book that he
19 used?

20 A. I'm sorry. I thought you were talking
21 about what just happened, the voir dire.

22 Q. And do you recall yesterday that he
23 referred to Professor Morin's book at length?

24 A. Yes, I remember that.

25 Q. And Professor Morin's book is called

1 Regulatory Finance, Utilities Cost of Capital, right?

2 A. I honestly don't know the title of his

3 book.

4 Q. Does this help you (indicating)?

5 A. Yes, that helps me.

6 Q. All right. Is the title of the book

7 Regulatory Finance, Utilities Cost of Capital?

8 A. That is the title of the book.

9 Q. And other books that you have read since

10 you -- or prior to preparing your testimony also dealt

11 with utility cost of capital, right?

12 A. That's correct.

13 Q. And entire books have been written about

14 regulatory finance and utilities' cost of capital, right?

15 A. That's correct.

16 Q. How many books did you read prior to

17 March 15th of 2004 that dealt with specifically Regulatory

18 Finance, Utilities Cost of Capital, read the whole book?

19 A. That dealt specifically with it, and that's

20 the only topic that they covered?

21 Q. Just like Professor Morin's book, right.

22 A. I hadn't read any that covered only that

23 topic.

24 Q. And prior to this matter, when in the real

25 world, outside of being a student, did you apply the DCF

1 analysis to anything?

2 MR. MICHEEL: Your Honor, this has been
3 asked and answered. He went through all of these
4 questions in his initial voir dire. I would object on
5 that basis. We need to move this proceeding along.

6 JUDGE WOODRUFF: I'll sustain the
7 objection.

8 BY MR. HERSCHMANN:

9 Q. You mentioned Mr. Tuck just a moment ago in
10 response to questions by Mr. Micheel, right?

11 A. I'm sorry. Could you repeat that?

12 Q. Sure. You mentioned Mr. Tuck a few moments
13 ago in response to questions by Mr. Micheel?

14 A. Correct.

15 Q. And Mr. Tuck was hired by the OPC to help
16 train you, right?

17 A. I indicated that he was a resource that I
18 could go to.

19 Q. To help train you, right?

20 A. In my deposition, he was a resource that I
21 had that, you know, if I had questions regarding a topic,
22 I could discuss with him.

23 Q. Do you know whether or not he was retained
24 by the OPC to help train you to perform your duties in
25 this case?

1 A. I don't know if that's the specific title
2 that they gave him or -- you know, I don't know. They
3 didn't tell me that this is -- if you're asking me, did
4 they come to me and say, here's Mr. Tuck, he's going to
5 train you specifically, that didn't occur.

6 Q. Did he help train you?

7 A. Like I said, he was a resource that I had
8 that I could go to and ask him questions.

9 Q. Did he help train you to provide your
10 testimony?

11 A. I mean, it depends on -- the question is,
12 did he help train me? Did I have questions that I asked
13 him and that he -- he -- that I conferred with him about?
14 If that's your definition of training, then yes.

15 Q. And did Mr. Tuck have more experience than
16 you as related to the real-life application of DCF?

17 A. Yes.

18 Q. Are there things that Mr. Tuck told you he
19 disagreed with that you were going to do in this case and
20 you did it anyway?

21 A. I believe there was, yeah, one issue for
22 sure.

23 Q. What was that one issue, sir?

24 A. The one issue that Tuck said that he
25 disagreed with was the inclusion or the exclusion of

1 Missouri regulated gas companies from my proxy group, but
2 I -- looking at --

3 Q. Is that the one issue that you disagreed
4 with?

5 A. Yes, that's one issue.

6 Q. Did he tell you that he didn't understand
7 why you'd be removing them and didn't agree with your
8 circularity argument? That's a yes or no.

9 A. I don't know if that's what he said
10 specifically, but yeah, he generally didn't agree with it.

11 Q. What source did you rely upon, which
12 utility cost of capital textbook did you rely upon that
13 said Missouri companies from your expert opinion?

14 A. What I relied upon was previous
15 testimonies. It seemed that there had been a precedent
16 set that Missouri reg-- or regulated companies were not in
17 the -- should not be included in the proxy. As far as a
18 specific precedent, I'm not sure, but in reading previous
19 testimonies, that's what I saw had occurred.

20 Q. What is a precedent?

21 A. It's an established standard, would be my
22 definition. But like I said, I don't know if that's a
23 specific -- if it was actually a specific precedent. It's
24 just what I had seen in prior testimonies done.

25 Q. And who gave you those prior testimonies?

1 A. As I mentioned yesterday and in my
2 deposition, I inquired to obtain prior testimonies, and I
3 asked Mr. Russ Trippensee to obtain them for me.

4 Q. Do you believe a precedent to be a prior
5 Commission order or decision?

6 A. I already gave you my definition that I was
7 basing my assumption on.

8 Q. I understand that. This is a follow-up
9 question. Do you believe a precedent to be a prior
10 Commission order or decision?

11 A. I'm not sure. My definition was something
12 that had been performed in the past. I'd seen it
13 previously. So that's what I was basing my assumption on.

14 Q. I'm asking you -- now, this is a different
15 question. I want you to try to answer the question. In
16 your definition of a precedent, do you believe that a
17 prior decision by this Commission would be a precedent for
18 you to rely upon?

19 A. And I already answered that at the
20 beginning of my last answer. I said I'm not sure.

21 Q. So it's your understanding a precedent is
22 how the OPC has done things previously, but you don't know
23 whether or not an Order by this Commission would be
24 precedence for you to rely on?

25 MR. MICHEEL: Your Honor, that calls for a

1 legal conclusion. This witness is not a lawyer. I'm
2 going to object on that basis. He's asked and answered
3 this three times to the best of his abilities. He says he
4 doesn't know.

5 JUDGE WOODRUFF: I'll sustain the
6 objection. He did say he didn't know. This has been
7 asked and answered.

8 BY MR. HERSCHMANN:

9 Q. The reason that you decided to exclude the
10 Missouri companies, even though Mr. Tuck told you that he
11 didn't agree with it, is because that's the way the OPC
12 has done it, right?

13 A. No, that's not correct.

14 Q. Didn't you just tell us a moment ago you
15 didn't know any textbooks that say you should exclude
16 Missouri companies in applying a utility's cost of
17 capital?

18 MR. MICHEEL: I'm going to object. That's
19 been asked and answered already, your Honor.

20 JUDGE WOODRUFF: Overruled.

21 BY MR. HERSCHMANN:

22 Q. Didn't you just tell us that a few minutes
23 ago?

24 A. I told you that I had seen it in previous
25 testimony. I didn't specify that it was OPC testimony,

1 and you made that assumption.

2 Q. Was it in Mr. Murray's testimony that you
3 saw it?

4 A. I honestly don't remember. I know
5 specifically that I saw it in Mr. Burdette's testimony,
6 and as far as going back to Mr. Murray's testimony, I
7 don't believe it's in there, but I can't say for sure,
8 because I honestly don't remember if that's where I saw it
9 in there or not.

10 Q. Did you review the St. Joe Light & Power
11 Company case before submitting your testimony?

12 A. Could you be more specific?

13 Q. Sure. Did you quote out of the decision
14 from the St. Joe Light & Power case in any of your
15 testimony?

16 A. I meant specific, which case?

17 Q. I'm sorry. Case No. ER-93-41.

18 A. Yes, I did.

19 Q. Did you follow the mandate of this
20 Commission in providing your, quote, unquote, expert
21 opinion by saying that if a capital structure is outside
22 the zone of reasonableness, a hypothetical capital
23 structure must be adopted?

24 MR. MICHEEL: I'm going to object to that,
25 your Honor. First of all, it's not a mandate. That calls

1 for a legal conclusion, and Commission decisions aren't
2 precedent in a legal sense. They can change. Precedent
3 doesn't apply to that. And so that calls for a legal
4 conclusion.

5 JUDGE WOODRUFF: Overruled.

6 BY MR. HERSCHMANN:

7 Q. You can answer the question.

8 A. What was the question?

9 MR. HERSCHMANN: Could you read it back,
10 please?

11 THE REPORTER: "Question: Did you follow
12 the mandate of this Commission in providing your, quote,
13 unquote, expert opinion by saying that if a capital
14 structure is outside the zone of reasonableness, a
15 hypothetical capital structure must be adopted?"

16 THE WITNESS: Could you refer me where
17 you're talking about in my testimony?

18 BY MR. HERSCHMANN:

19 Q. Let me hand you the quote. I believe it's
20 just been copied out of your testimony.

21 MR. HERSCHMANN: Judge, may I approach?

22 JUDGE WOODRUFF: You may.

23 MR. HERSCHMANN: I apologize.

24 BY MR. HERSCHMANN:

25 Q. For reference, it's in your rebuttal

1 testimony, page 12. Question: Has the Commission ever
2 authorized the use of a hypothetical capital structure in
3 a previous rate case? Yes, it has in Case No. ER-93-41
4 re St. Joseph Light & Power Company, the Commission had
5 the following to say.

6 I think you have the quote now in front of
7 you. Directing your attention to the issue dealing with
8 the zone of reasonableness and the Commission saying that
9 the actual capital structure is entirely out of line with
10 what the Commission considers to be a reasonable range, a
11 hypothetical capital structure must be adopted. Do you
12 see that?

13 A. Yeah. Give me a second to read it myself,
14 though.

15 Q. Sure.

16 A. Okay.

17 Q. That is a quote that you put in your
18 testimony; is that correct?

19 A. That is a quote from the Report and Order,
20 correct.

21 Q. And you selected that quote and put it in
22 your testimony, right?

23 A. That is correct.

24 Q. No one compelled you to do that, right?

25 A. That is correct.

1 Q. And you told us you had a blank canvass on
2 which to prepare your testimony, right?

3 A. Yes, that was in my deposition, but it
4 wasn't in the tape that you showed.

5 Q. Okay. So you've testified that you had a
6 blank canvass, right?

7 A. In my deposition, correct.

8 Q. And you selected this quote from the
9 Commission orders and actually read the Commission order
10 before deciding that it was relevant to this proceeding,
11 right?

12 A. I selected the quote, correct.

13 Q. And you decided it was relevant to this
14 proceeding, that's why you put it in your testimony,
15 right?

16 A. That is correct.

17 Q. What do you understand the word "must" to
18 mean?

19 A. I'm trying to think of a good definition.

20 Q. Obligated?

21 A. Something that has to be done.

22 Q. Do you think that your proposed capital
23 structure for MGE of approximately 25 percent --

24 A. That's not correct.

25 Q. What is the number? And I don't mean the

1 hypothetical. Your proposed where you claim to be the
2 actual capital structure.

3 A. 26.10 percent.

4 Q. Do you think that is outside the zone of
5 reasonableness for the comparable groups of companies that
6 you used in your DCF analysis?

7 MR. MICHEEL: Your Honor, at this point
8 we're far afield from the voir dire, and I'm not certain
9 how long this is going to go on. I need to put this
10 witness up for his regular cross-examination.

11 JUDGE WOODRUFF: This does appear to be
12 moving into --

13 MR. HERSCHMANN: This goes directly to the
14 point that Mr. Micheel raised about his appropriate
15 application of the DCF analysis for which I object, and
16 he's there's not proper foundation.

17 JUDGE WOODRUFF: I'm going to allow it.

18 MR. HERSCHMANN: I'm almost done.

19 JUDGE WOODRUFF: Okay. Go ahead.

20 THE WITNESS: The zone of reasonableness
21 that I calculated for my group was -- hold on a second.
22 I've got it right here in my testimony -- approximately --
23 well, actually exactly 37.6 percent to 58.2 percent, but
24 as far as the application of the DCF model, this capital
25 structure is not a DCF model. It's not a variable on the

1 DCF model.

2 BY MR. HERSCHMANN:

3 Q. Tell me the capital structure range again.

4 I'm sorry.

5 A. 37 -- the hypothetical capital structure?

6 Q. The range that you just quoted. You said

7 37 --

8 A. That was the hypothetical capital structure

9 range.

10 Q. Okay. What was that range?

11 A. 37.6 to 58.2 percent.

12 Q. That's using your comparable companies; is

13 that right?

14 A. That was using Mr. Dunn's proxy group.

15 Q. And you relied upon those calculations in

16 providing your testimony, right? You did the calculations

17 and then relied upon it, right?

18 A. I did the calculations in my rebuttal

19 testimony, correct.

20 Q. And then you relied upon the calculations

21 in submitting the testimony, right?

22 A. In submitting the testimony? Yeah, I put

23 them in there and I submitted it.

24 Q. Now, you say the 26.1 versus the 37.6 to

25 58.2 percent is outside that range?

1 A. Yes. As I explained in my rebuttal
2 testimony, the consolidated capital structure of Southern
3 Union was outside the zone of reasonableness range, so
4 that's why I -- following the Commission's acceptance of
5 this hypothetical development, I followed the methodology
6 that was developed by Mr. Tuck in that case.

7 Q. And that's why you submitted a hypothetical
8 capital structure, right?

9 A. No. I submitted the hypothetical capital
10 structure because Mr. Dunn had -- had suggested that a
11 hypothetical capital structure would be appropriate in
12 this case. So I gave the Commission another option based
13 on a methodology that they had accepted to be the proper
14 way to develop the hypothetical capital structure.

15 Q. This was part of your blank canvass, right,
16 testimony? You decided what to put in there, right?

17 A. Absolutely.

18 Q. Now, you mentioned a moment ago that,
19 besides Mr. Tuck, Mr. Micheel was available to help train
20 you, right?

21 A. I mentioned that Mr. Micheel gave me a
22 general discussion on regulation of natural gas companies.

23 Q. Was this information you knew before you
24 met Mr. Micheel?

25 A. Before we had the conversation?

1 Q. Right.

2 A. To some degree, yeah, some of it was new
3 that I was not aware of, but specifically I'm not sure. I
4 mean, that was like two months ago. I'm not sure what was
5 new at the time and what wasn't.

6 Q. Well, what did Mr. Micheel tell you that
7 helped you prepare your testimony in this matter?

8 A. Like I said, it was just a general talk
9 regarding regulating natural gas companies, LDCs,
10 pipelines.

11 Q. Do you have all that training that
12 Mr. Micheel addressed to you during your undergraduate or
13 graduate studies?

14 A. No, there's not.

15 Q. Now, you mentioned this seminal book, Cost
16 of Capital to Public Utilities. Whose book is that?

17 A. That is a book written by Dr. Myron Gordon,
18 1974, published by Michigan State University.

19 Q. I apologize for asking this question. What
20 year were you born?

21 A. 1979.

22 Q. So safe to say you didn't read his book, at
23 least for a while after, right?

24 MR. MICHEEL: Your Honor, he's already
25 testified that he read his book prior to filing direct

1 testimony.

2 MR. HERSCHMANN: Let me address this.

3 BY MR. HERSCHMANN:

4 Q. You've said several times that Mr. Gordon's
5 book is a seminal book. Remember that testimony?

6 A. That's correct.

7 Q. When is the first time you read that book?

8 A. The first time that I sat down and actually
9 read the book was just prior -- or I'm sorry -- just after
10 being employed at the Office of the Public Counsel.

11 Q. So some point after mid March of this year
12 was the first time you read the book?

13 A. Yeah, but I had experience with --

14 Q. Would you answer my question?

15 A. I did answer your question. I said yes.

16 Q. Okay. When you get to the but part, I'm
17 going to ask you just to direct your attention to the
18 question.

19 A. Okay.

20 Q. Was this the first book that you read as
21 related specifically to the cost of capital in public
22 utilities? After you started your employment, is this the
23 first one they gave you?

24 A. They didn't give it to me. I went and
25 gathered it myself.

1 Q. Is that the first one that you read?

2 A. Yes, that's correct.

3 Q. And you read that at some point between

4 March 15 and the day you submitted your testimony, right,

5 on April 15?

6 A. Prior to submitting my direct testimony.

7 Q. What does seminal mean to you?

8 A. My definition of seminal, it's not the

9 Webster definition, I'm sure, but it would be a book that

10 is highly respected and one that kind of changed the way

11 that something is thought of and done. That is my

12 definition.

13 Q. And you were able to make the determination

14 from reading a book from 1974 that it was a seminal book

15 after you finished reading it?

16 A. I had had in numerous textbooks through

17 school that had referenced this book and had talked about

18 his methodology, and these were new editions of this book.

19 So I was aware of the book, and when I read it, it just

20 solidified my knowledge of the subject matter and I do

21 believe that it is a seminal book in the calculation of

22 cost of capital for a public utility, yes, absolutely.

23 Q. And you mentioned several times in response

24 to Mr. Micheel about what other experts would do, right,

25 or what they would rely upon? Do you remember that series

1 of questions and answers?

2 A. Yes.

3 Q. Outside of this case, okay? I want you to
4 take yourself outside of this case. How many experts have
5 you discussed in real-life situations their applications
6 of the DCF methodologies? In other words, they were
7 working on a matter and they came to discuss it with you
8 or you came to discuss it with them.

9 A. I'm sorry. Let me just try to see if I
10 understand your question correctly. How many experts did
11 I go and converse with using this, face-to-face speak
12 with?

13 Q. Before you started your employment,
14 unrelated to the --

15 A. Yeah, I understand. Yes.

16 Q. How many experts did you ever consult with
17 that said, I'm doing a DCF analysis for this company, for
18 this line of business in the real world, and I want to
19 discuss it with you?

20 A. That -- no, I've never done that.

21 Q. Did anyone ever consult with you to say,
22 listen, you finished your undergraduate and graduate
23 studies and I want to talk to you about how we apply the
24 DCF methodologies in the cost of capital to public
25 utilities?

1 A. No.

2 Q. Had anyone ever consulted with you as an
3 expert as it related to cost of capital for public
4 utilities prior to being employed by the OPC in March of
5 this year?

6 A. No.

7 Q. Now, Mr. Micheel also asked you about your
8 using the most recent financial information as related to
9 Southern Union. Do you recall that?

10 A. Yes.

11 MR. MICHEEL: Your Honor, I think that's a
12 misstatement of my question. My question was --

13 MR. HERSCHMANN: Well, I object to
14 Mr. Micheel's speech. I just got a question and answer
15 from the witness and the record is what the record is.
16 He's answered that question.

17 BY MR. HERSCHMANN:

18 Q. Mr. Allen, did you update Southern Union's
19 consolidated capital structure to reflect the changes as
20 of April 30th of this year?

21 A. Not as this year. I believe the question
22 was --

23 Q. I'm asking you -- that's the only question
24 that I asked. I asked you a question. I really want you
25 to answer the question.

1 Did you update Southern Union's
2 consolidated capital structure as of April 30th of this
3 year in submitting your testimony?

4 MR. MICHEEL: Your Honor, I'm going to
5 object to that and, again, my question to Mr. Allen was
6 not about the capital structure, your Honor. My question
7 was not about the capital structure, your Honor. My
8 question was about the stock price, not the capital
9 structure.

10 And this is completely taken out of context
11 of my question and it's not related to anything I asked
12 this witness.

13 JUDGE WOODRUFF: Your objection is going to
14 be overruled. Go ahead and ask your question.

15 BY MR. HERSCHMANN:

16 Q. Did you update your submitted testimony in
17 this case, either rebuttal or surrebuttal, to reflect
18 Southern Union's capital structure as of April 30, 2004,
19 the true-up date?

20 A. No.

21 Q. Have you had a chance to review it since
22 that time to learn that the capital structure is actually
23 changed from your 26.1 to approximately 30 percent equity?

24 A. I have not had that opportunity.

25 MR. HERSCHMANN: I renew my objection.

1 JUDGE WOODRUFF: Yes, Mr. Micheel?

2 MR. MICHEEL: I just have a couple, and my

3 couple will be a couple.

4 JUDGE WOODRUFF: This will stop at this

5 point. So go ahead, Mr. Micheel.

6 FURTHER VOIR DIRE EXAMINATION BY MR. MICHEEL:

7 Q. Mr. Allen, on page 12 of your rebuttal

8 testimony, Mr. Herschmann pointed you to a specific quote

9 from the St. Joe case, and does that case indicate that

10 when, as in the case of the actual -- does it say when, as

11 in this case, the actual capital structure is so entirely

12 out of line with what the Commission considers a

13 reasonable range?

14 A. I'm sorry. Can you direct me to a line?

15 I'm having a hard time following you.

16 Q. On line 9, the 17 starting "however."

17 A. Okay.

18 Q. When, as is the case, the actual capital

19 structure is so entirely out of line with what the

20 Commission determines is a reasonable range. Do you see

21 that?

22 A. Yes.

23 Q. And does that indicate to you that it's the

24 analyst or the Commission that makes the determination

25 about whether or not the capital structure is within a

1 reasonable range?

2 MR. HERSCHMANN: Objection, the document

3 speaks for itself.

4 JUDGE WOODRUFF: I'll sustain the

5 objection.

6 MR. MICHEEL: Your Honor, he questioned him

7 extensively about this document.

8 JUDGE WOODRUFF: We need to move on. The

9 document does speak for itself.

10 MR. MICHEEL: Nothing further.

11 JUDGE WOODRUFF: Okay. There's been an

12 objection made to Exhibits 200, 201, 202 and 215, which is

13 the errata sheet. As previously indicated, the Commission

14 will take this objection under advisement to make a ruling

15 at a later date. The exhibits will be admitted at this

16 time, subject to that objection.

17 (EXHIBIT NOS. 200, 201, 202 AND 215 WERE

18 RECEIVED INTO EVIDENCE.)

19 JUDGE WOODRUFF: And we are now ready to

20 move on to cross-examination. First for the witness,

21 first cross-examination opportunity goes to Staff.

22 CROSS-EXAMINATION BY MR. BERLIN:

23 Q. Good morning, Mr. Allen.

24 A. Good morning.

25 Q. I believe in your rebuttal testimony you

1 make a reference to the term "hypothetical capital
2 structure," and if you would, just for my understanding,
3 could you please define a hypothetical capital structure
4 for me?

5 A. Definition of the hypothetical capital
6 structure in this case is that it is a structure that is
7 representative of the general industry.

8 Q. I believe in your rebuttal testimony that
9 you use Mr. Dunn's comparable companies for the
10 hypothetical capital structure; is that right?

11 A. Yes. I utilize Mr. Dunn's proxy group for
12 the hypothetical capital structure, that's correct.

13 Q. Could you tell me your rationale for that
14 use of his proxy group?

15 A. Yeah. The rationale behind it was there's
16 two reasons. One is to eliminate that as an issue with
17 this case. I just used Mr. Dunn's group, that way save an
18 argument. And the other issue behind that is
19 statistically it adds validity to the capital structure
20 because it includes a larger sample size.

21 Q. By doing that, were you indicating any
22 problems with your original comparable companies?

23 A. No, I was not indicating a problem with
24 them. I believe that my group is comparable. It was just
25 an issue to kind of avoid that argument and get down to

1 the actual issues.

2 MR. BERLIN: Thank you. Your Honor, that

3 concludes Staff's questions.

4 JUDGE WOODRUFF: All right. Thank you.

5 City of Joplin have any questions?

6 MR. DEUTSCH: No questions, your Honor.

7 JUDGE WOODRUFF: All right. Federal

8 Agencies?

9 MR. PAULSON: No questions, your Honor.

10 JUDGE WOODRUFF: MGE?

11 MR. HERSCHMANN: May we take a two-minute

12 break first?

13 JUDGE WOODRUFF: We may.

14 MR. FRANSON: Your Honor, actually, there

15 is something that I'd like to bring up, and it's a matter

16 that the Commission has been having some concern about,

17 what you do with these depositions that have come into

18 evidence and will. I'd like to direct the Commission's

19 attention to Missouri Revised Statute, Section 536.080,

20 paren 2, in a contested case, each official of an agency

21 who renders or joins in rendering a final decision shall,

22 prior to such final decision, either hear all of the

23 evidence, read the full record, including all the evidence

24 or personally consider the portions of the record cited

25 or referred to in the arguments or brief.

1 Judge, the suggestion is, based from the
2 statutes, that the Commissioners and yourself would be
3 reviewing parts that you want to review or parts pointed
4 out by the parties in the Briefs, not necessarily reading
5 the entire thing.

6 JUDGE WOODRUFF: Thank you for that
7 clarification, and I was aware of that statute. You can
8 be sure the Commissioners are very aware of it as well.

9 What I am concerned about and what I have
10 expressed before is I don't want to have a whole lot of
11 documents dumped into the record without some
12 clarification to the Commission about what is important in
13 those depositions. So if the whole deposition has to come
14 in for some reason, we would expect at least in the
15 briefing that the parties would point out that this
16 portion of the deposition is what is important. And I'm
17 not -- by saying that, I'm not making any rulings on any
18 future offerings of depositions.

19 That is the concern of the Commissioners,
20 that they not be expec-- that we don't just dump a whole
21 bunch of stuff into the record that they would be expected
22 to read and digest everything.

23 All right. Let's go ahead and take a break
24 until 11:30.

25 (A BREAK WAS TAKEN.)

1 JUDGE WOODRUFF: We're back on, and we're
2 about to begin the cross-examination of Mr. Allen by MGE.
3 MR. HERSCHMANN: Thank you.
4 JUDGE WOODRUFF: And I will tell the
5 parties that we'll plan on breaking at approximately
6 12 o'clock probably 'til about 1:30 today.
7 CROSS-EXAMINATION BY MR. HERSCHMANN:
8 Q. Mr. Allen, let me begin by following up on
9 questions from Mr. Berlin. Did you attempt to calculate a
10 hypothetical capital structure for the comparable groups
11 using your comparable companies?
12 A. No, I did not. I used Mr. Dunn's.
13 Q. When you selected your comparable
14 companies, did you think they were more comparable to MGE
15 than the companies selected by Mr. Dunn?
16 A. Yes, I did.
17 Q. Are you capable of doing the calculations
18 for your comparable companies compared to the ones you did
19 for Mr. Dunn's?
20 A. I'm sorry. I don't understand your
21 question. In what regards?
22 Q. Can you do it? Can you do the actual
23 calculations just using your comparable companies and not
24 Mr. Dunn's comparable companies?
25 A. I understand that. What calculation are

1 you referring to?

2 Q. To determine the hypothetical capital
3 structures for your comparable group.

4 A. Yes.

5 Q. Did you ever look at the different --
6 withdrawn.

7 Did you ever consider doing a hypothetical
8 capital structure using your comparable group?

9 A. I considered it, but I only performed it on
10 Mr. Dunn's group. I didn't perform it on my group, no.

11 Q. Do you know whether or not, if you
12 performed it on your group, the hypothetical capital
13 structure for your group would have provided for more
14 equity?

15 A. I do not know that.

16 Q. How long would it take you to do the
17 calculations?

18 A. I would have to calculate the average
19 equity ratios, and then I'd have to calculate the mean,
20 and then I'd have to calculate standard deviation and the
21 pro rata adjustment. If I had to do it by hand, it would
22 take a little bit of time.

23 Q. If you had a calculator?

24 A. Still take a little bit of time.

25 Q. What does a little bit of time mean?

1 A. For each company I'd have to do that. It
2 would probably take, if I had to do it by hand, a good
3 hour.

4 Q. When you say by hand, do you mean --

5 A. With a calculator.

6 Q. -- with a calculator?

7 A. Yes.

8 MR. MICHEEL: I'm going to just do a
9 preemptory objection here. To the extent Mr. Herschmann
10 is going to ask my witness to do the calculation, I would
11 object to that. He's already testified that he hasn't
12 done the calculation, your Honor. So if that's the road
13 we're going down, I'm just going to get the objection out
14 there.

15 JUDGE WOODRUFF: Sounds like a preemptory
16 objection. Is that where you're headed?

17 MR. HERSCHMANN: I may ask him to do it
18 during lunch. There's \$19 million on the table.

19 JUDGE WOODRUFF: When you ask him, I'll
20 rule on the objection.

21 BY MR. HERSCHMANN:

22 Q. Did you make any determinations to check
23 what was the authorized return on equity for any of the
24 comparable companies that you were using?

25 A. I have checked that.

1 Q. And what were those authorized returns?
2 A. I don't have that with me, so I don't know
3 off the top of my head.
4 Q. Did you read Professor Morin's testimony?
5 A. I read Mr. Morin's rebuttal testimony.
6 Q. Did you know what the RRA was before you
7 started working at the OPC?
8 A. Yes.
9 Q. Had you ever looked at the RRA prior to
10 working at the OPC?
11 A. I had seen it before.
12 Q. And did you review the information that's
13 cited in Mr. Morin's testimony as to whether or not the
14 actual referenced authorized rates of return that he
15 describes were accurate?
16 A. I didn't check it for Dr. Morin's
17 testimony. I checked -- I double checked Mr. Dunn's
18 testimony to the RRA report that he provided us in a Data
19 Request.
20 Q. What was the reason that you didn't check
21 Dr. Morin's calculation or information?
22 A. Because Dr. Morin didn't reference me in
23 his rebuttal testimony, so I -- I had limited resources
24 and time, so I spent my time working on Mr. Dunn's
25 testimony and Mr. Murray's testimony.

1 Q. Did Dr. Morin address you during his
2 deposition testimony?

3 A. Yes.

4 Q. Did anyone tell you you should not look at
5 any other Commission's orders regarding what they had said
6 was the authorized return on equity?

7 A. No.

8 Q. Do you think it's relevant to what other
9 commissions are doing for comparable companies to MGE in
10 authorizing the return on equity?

11 A. I think that the cost of capital is
12 relevant, but the cost of capital is a completely
13 different thing than the authorized rate of return.

14 Q. For the cost of capital, did you review it?

15 A. No, I did not. I don't know of a source
16 where you can actually go and -- strike that. No, I did
17 not review it.

18 Q. Do you think it's relevant in making your
19 recommendations that this Commission have some
20 relationship to what your comparable companies are being
21 allowed the opportunity to earn?

22 A. I think the most important thing, as far as
23 relevance, is what the results show based on the analysis
24 that I did for this company right now, not the authorized
25 rate of return that is published by other -- other

1 commissions. That's not the important thing that the
2 Commission should look at, no.

3 Q. I don't think I asked you if it was the
4 important thing.

5 MR. HERSCHMANN: Could you read back the
6 question, please?

7 THE REPORTER: "Question: Do you think
8 it's relevant in making your recommendations that this
9 Commission have some relationship to what your comparable
10 companies are being allowed the opportunity to earn?"

11 THE WITNESS: If I am forced to answer that
12 with a yes or no question, then I would have to say no,
13 because of the reason I said before.

14 BY MR. HERSCHMANN:

15 Q. Do you agree there's a limited amount
16 of capital that's to be invested in competing industries
17 and competing companies?

18 A. A limited amount, is that your question?

19 Q. Yeah.

20 A. I think the amount of capital theoretically
21 is not limited, no.

22 Q. You don't think that there's a limited
23 amount of capital that companies have to go out into the
24 marketplace and try to raise, competing companies?

25 A. Your question was whether or not I thought

1 that there is a limited amount of capital. And
2 theoretically, no, I don't, because theoretically there
3 is -- there is an endless amount of investors. I guess
4 not endless. I guess it would be the population. So if
5 that's -- if that's your question, yes.

6 Q. Theoretically you're saying that the
7 government can print more money and it can just be a
8 wealth of funds available that the government can decide
9 to invest in different companies and people can just go do
10 that, right? Is that --

11 A. That's not what I'm saying. I'm saying
12 theoretically the limit is the total amount of the
13 population. Now, realistically, yes, there is a limit.

14 Q. I want to deal with not the theoretical,
15 not the schooling type of stuff but in the practical world
16 type of issues. You know that when a company goes to
17 market to sell an instrument, they put a limit on how much
18 they're trying to sell and see if it gets oversubscribed
19 or undersubscribed. Are you aware of that?

20 A. Absolutely, but that wasn't the premise of
21 your question before. Yes, that is correct.

22 Q. And do you understand -- did you read
23 Bluefield and Hope, those Supreme Court decisions?

24 A. I did read those cases. I'm not a lawyer,
25 as far as basically the legal aspects, the technical

1 aspects of it, but I do understand -- I did read it to get
2 a grasp of the issues that they brought up, as far as
3 determining a fair rate of return.

4 Q. You know that they talk about competing
5 risks -- well, withdrawn.

6 Do you believe companies compete for
7 capital that's in the marketplace when they try to sell
8 financial instruments?

9 A. Yes, they do.

10 Q. In your opinion, does Southern Union
11 compete for access to capital?

12 A. Yes, they do.

13 Q. With whom do you believe they compete?

14 A. They compete with -- well, an investor will
15 look at all his options, based on risk and corresponding
16 return. So they compete with companies that have the same
17 risk return relationship.

18 Q. Do you think they compete with other
19 utilities if an institutional investor wants to maintain,
20 as part of his portfolio, investments in utilities?

21 A. Yes, they do.

22 Q. Agreeing that that's the premise for which
23 the competition exists, do you think it's relevant to
24 whether or not your comparable companies are getting a
25 greater return on equity than what you're recommending

1 occurs in this case?

2 A. I'm sorry. Could you repeat that question?

3 MR. HERSCHMANN: Could you read it back,
4 please?

5 THE REPORTER: "Question: Agreeing that
6 that's the premise for which the competition exists, do
7 you think it's relevant to whether or not your comparable
8 companies are getting a greater return on equity than what
9 you're recommending occurs in this case?"

10 THE WITNESS: I think what is relevant is
11 the market derived cost of capital, not the authorized
12 rate of return.

13 BY MR. HERSCHMANN:

14 Q. You think authorized rate of return is
15 irrelevant then?

16 A. I think the most relevant factor here is
17 the cost of capital.

18 Q. I'm not asking you what most relevant is.

19 MR. HERSCHMANN: Could you repeat the
20 question?

21 THE REPORTER: "Question: You think
22 authorized rate of return is irrelevant then?"

23 THE WITNESS: You had asked me a question
24 before regarding RRA and authorized rates of return. I
25 direct you to my answer there, when I said if I'm forced

1 to say yes or no, then I'd have to say no, because I
2 believe the most important thing is the actual
3 market-derived cost of capital, not the authorized.

4 BY MR. HERSCHMANN:

5 Q. So based on your last statement, if this
6 Commission authorized rate of return of 12 percent, that
7 should have no impact on MGE, right?

8 A. No. That's going to have an impact. What
9 they authorize is going to have an impact upon MGE, yes.

10 Q. You think it will be more attractive to
11 investors if the authorized rate of return is higher
12 rather than lower?

13 A. Investors are going to select companies
14 that offer the best risk and return relationships, so yes.
15 And with respect to whether or not a risk -- one company
16 that has comparable risk is earning a higher rate of
17 return, they're going to be attracted to that company,
18 correct. Yes.

19 Q. That being said, for your comparable
20 groups, are their authorized rate of returns higher than
21 what you're recommending in this case?

22 A. As I stated, I don't have that list with
23 me. Based on -- based on the testimony of Mr. Dunn with
24 the RRA that he had in his -- I believe it was his direct
25 testimony -- correct me if I'm wrong; it might have been

1 his rebuttal -- the authorized rate of return was
2 somewhere in the 11 percent range, I believe, and I'm
3 recommending 9.1-- 9.01 to 9.34 range.

4 Q. If you were an investor, which companies
5 would you prefer to invest in, ones with the 11 percent
6 authorized rate of return or the ones with the 9 percent
7 authorized rate of return, all things being equal?

8 A. If everything is equal, and that's a big
9 statement, if everything is equal, then an investor is
10 going to want to invest in a company that's offering
11 higher rate of return.

12 Q. How about if all the other competitors are
13 getting 11 percent average authorized rate of return and
14 MGE was getting a 9 percent authorized rate of return, do
15 you think that that would hinder MGE's opportunities to go
16 out and raise capital in the markets?

17 A. You know, it depends on the risk
18 characterizations. The RRA report showed various
19 companies. Specifically I can't remember if it
20 encompassed my entire group, but I'm sure it didn't. So
21 it really depends on the risk characterization. It's a
22 risk return tradeoff. It's not as simple as you make it
23 sound.

24 MR. HERSCHMANN: Could you read back the
25 question again?

1 THE REPORTER: "Question: How about if all
2 the other competitors are getting 11 percent average
3 authorized rate of return and MGE was getting a 9 percent
4 authorized rate of return, do you think that that would
5 hinder MGE's opportunities to go out and raise capital in
6 the markets?"

7 THE WITNESS: I can't answer that with a
8 yes or no.

9 BY MR. HERSCHMANN:

10 Q. You say riskier companies. Do you believe
11 a company that is more highly leveraged is riskier?

12 A. Theoretically, if everything else is equal
13 between two companies, Company A and Company B, if
14 Company A has more leverage than Company B, yes,
15 Company A is riskier. But just because a company has a
16 higher leverage ratio does not in any way mean that they
17 are overall riskier than another company. That is a
18 misconception.

19 Q. I didn't ask that question.

20 MR. HERSCHMANN: Move to strike the last
21 part of his answer as not responsive.

22 MR. MICHEEL: I think he's entitled to
23 explain his answer, your Honor.

24 JUDGE WOODRUFF: It was nonresponsive. The
25 motion to strike is granted, and the last portion of the

1 answer is stricken.

2 BY MR. HERSCHMANN:

3 Q. Do you believe that investors that invest
4 in riskier companies are expecting a higher return?

5 A. Vis-a-vis a company with less risk?

6 Q. That's correct.

7 A. Correct.

8 Q. In your analysis, did you believe or state
9 that MGE is riskier because of its capital structure than
10 your comparable group?

11 A. Could you direct me to my testimony to
12 where you're speaking of?

13 Q. I'll just ask it directly. Do you agree
14 that in your analysis, MGE is riskier than the comparable
15 groups that you identified in your testimony?

16 A. To a degree, I do have to agree that
17 Southern Union is riskier.

18 Q. And you just told us that investors who
19 invest in riskier companies expect greater returns, right?

20 A. That is correct.

21 Q. And if the authorized rate of return for
22 your comparable group is approximately 11 percent, and you
23 just told us MGE is riskier, doesn't logic dictate that
24 the authorized rate of return should be higher for the
25 more risky company in your analysis?

1 A. I'm assuming you're using that 11 percent
2 as a hypothetical number --

3 Q. Correct.

4 A. -- correct?

5 Could I hear the question again?

6 MR. HERSCHMANN: Read it back, please.

7 THE REPORTER: "Question: And if the
8 authorized rate of return for your comparable group is
9 approximately 11 percent, and you just told us MGE is
10 riskier, doesn't logic dictate that the authorized rate of
11 return should be higher for the more risky company in your
12 analysis?"

13 THE WITNESS: Financial theory would say
14 that a riskier company would require a higher return, but
15 there are other things you have to consider in this case.

16 BY MR. HERSCHMANN:

17 Q. Based on the financial theory that you just
18 mentioned, shouldn't the recommendation for MGE be above
19 the comparable companies?

20 A. Based solely on financial theory, to a
21 degree, yes, my group is -- Southern Union is a bit -- to
22 a degree riskier than my comparable group.

23 Q. Now, have you ever consulted with any
24 management of any companies, publicly traded utilities?

25 A. No.

1 Q. Have you ever consult with any managements
2 of any publicly traded companies at all?

3 A. No, I haven't.

4 Q. And is it true that every company has a
5 different capital structure and leverage?

6 A. Yeah, every company has a different
7 structure, except for -- I mean, if you're doing a broad
8 generalization, except for by chance, then there could be
9 two companies that have the same capital structure. And
10 each company's optimal capital structure is different and
11 it's determined by management.

12 Q. And those are management decisions as to
13 whether or not they want to maintain certain equity, if
14 they can raise it, or certain debt, and how they actually
15 manage the company, right?

16 A. That is correct.

17 Q. Do you know what Southern Union's capital
18 structure was before it acquired Panhandle?

19 A. I can give an approximation on -- based on
20 the 2001 rate case, but off the top of my head, no, I
21 can't give you an answer to that question right now.

22 Q. Well, do you know what -- prior to the sale
23 of the Texas operations, do you know what the capital
24 structure was then?

25 A. Same answer as far as off the top of my

1 head. I don't know it off the top of my head.

2 Q. Did you have occasion to read the

3 Stipulation & Agreement and the subsequent Order in

4 relationship to Southern Union's acquiring Panhandle?

5 A. Yes, I did.

6 Q. Did you read the conditions that were

7 imposed?

8 A. Yes, I did.

9 Q. Do you recall that you cite in your

10 testimony, your surrebuttal testimony that Southern

11 Union's acquisition of Panhandle placed increased risk on

12 Missouri ratepayers?

13 A. Could you direct me to that page?

14 Q. Try page 8.

15 A. Did you say rebuttal or surrebuttal?

16 Q. I believe it's surrebuttal, page 8.

17 A. Okay. I've read it. Could you repeat your

18 question, please?

19 Q. I think the question was, did you state

20 that Southern Union's acquisition of Panhandle put MGE

21 ratepayers at increased risk?

22 A. That's not what I said specifically. I'm

23 assuming you're referring to the question that starts at

24 line 13 on page 8.

25 Q. Yes.

1 A. I said -- the question was, why is it
2 inappropriate to exclude PEPL or Panhandle debt from the
3 capital structure. My answer was the reason it is
4 inappropriate to exclude PEPL debt from the capital
5 structure is because ratepayers and shareholders share in
6 the risk of the Panhandle acquisition, but
7 disproportionately in the potential benefits. That is --
8 Q. I'm sorry. If you're just going to read
9 your answer, it's in the record.
10 A. Yeah.
11 Q. I'm not concerned with that.
12 A. Okay.
13 Q. Did the OPC request that the MGE ratepayers
14 be insulated from Southern Union's acquisition of
15 Panhandle?
16 A. Specifically, the stipulation on page 9,
17 part E says that Southern Union will not recommend an
18 increase or claim Staff should make an adjustment to
19 increase the cost of capital for MGE as a result of the
20 transaction. Any increases in the cost of capital --
21 Q. I'm sorry. I didn't ask you to read from
22 it. I asked --
23 MR. HERSCHMANN: Can you read back the
24 question, please?
25 THE REPORTER: "Question: Did the OPC

1 request that the MGE ratepayers be insulated from Southern
2 Union's acquisition of Panhandle?"

3 BY MR. HERSCHMANN:

4 Q. That's a yes or no.

5 A. Yes.

6 Q. Can you turn to page 5 of the Stipulation &
7 Agreement; under point 2, can you read the heading into
8 the record?

9 A. It reads, insulation of Southern Union's
10 MGE operating division from Panhandle business.

11 Q. Does it then say, to insulate MGE from the
12 transaction, which is a defined term, Southern Union
13 agrees that . . . Do you see that?

14 A. Yes.

15 Q. And do you see what Southern Union agreed
16 to do to insulate MGE ratepayers from the acquisition of
17 Panhandle?

18 A. Where specifically are you referring to in
19 the Stipulation & Agreement?

20 Q. You know, why don't you read into the
21 record starting at Southern Union/Panhandle Corporation
22 and successor entities?

23 A. Southern Union/Panhandle Corporation,
24 parenthesis, quotation SUPC, quotation, parentheses, that
25 successor entities or any direct or indirect subsidiary of

1 Southern Union that acquires or owns any equity interest
2 in Panhandle will be owned and operated as separate
3 subsidiary -- or as a separate subsidiary of Southern
4 Union. Southern Union and MGE will not directly or
5 indirectly allow any Panhandle debt to be recoured to
6 them, pledge Southern Union or MGE equity as collateral or
7 security for the debt of any Panhandle entity, give,
8 transfer, invest, contribute or loan to any Panhandle
9 entity any equities or cash without Commission approval.

10 Southern Union will not transfer the SUPC
11 and successor entities or any subsidiary thereof directly
12 or indirectly assets necessary and useful in providing
13 service to MGE's Missouri customers without Commission
14 approval. Southern Union will not enter directly or
15 indirectly into any make-well agreements or guarantees or
16 guarantee the notes, debt obligations or other securities
17 of any Panhandle entity without Commission approval.

18 Southern Union will not adopt, indemnify,
19 guarantee or assume responsibility for payment of either
20 directly or indirectly any of the current or future
21 liabilities of any Panhandle entity without Commission
22 approval. Southern Union will exercise its best efforts
23 to insulate MGE from any adverse consequences from its
24 other operations or the activities of any of its
25 affiliates.

1 Southern Union will submit reports
2 certifying its compliance with this paragraph 2 on a
3 quarterly basis to Staff, Public Counsel, and other
4 interested parties that are subject to a Commission
5 Protective Order until the Commission determines that MGE
6 is insulated from Southern Union's other operations and
7 the activities of any of its affiliates or that the
8 requirement is no longer needed.

9 Do you want me to continue?

10 Q. In a moment. Do you have any evidence to
11 demonstrate that Southern Union has violated any of the
12 provisions that you just read into the record?

13 A. I do not.

14 JUDGE WOODRUFF: Before you ask your next
15 question, it's 12 o'clock, so it's time to break for
16 lunch.

17 MR. HERSCHMANN: Could I just ask one to
18 address the point that Mr. Micheel raised?

19 JUDGE WOODRUFF: All right. One more.

20 BY MR. HERSCHMANN:

21 Q. If you used your computer over lunch with
22 the data you've already inputted for the comparable
23 companies, would you be able to do a calculation on
24 hypothetical capital structure for your comparable group?

25 MR. MICHEEL: Your Honor, I'm going to

1 object to that. They had every opportunity to do that
2 calculation if they wanted to do it, and I'm not going to
3 submit my witness for doing calculations that the company
4 had every ability to do in their surrebuttal testimony and
5 for whatever reason chose not to do. So I'm going to
6 object. I think it's an improper request and improper
7 cross-examination.

8 JUDGE WOODRUFF: At the moment he's only
9 asked him if he could, and I'm going to let him answer
10 that question first. Can you?

11 THE WITNESS: Yes, I could.

12 BY MR. HERSCHMANN:

13 Q. How long would it take you, presuming you
14 have the financial information already in your system?

15 A. If I had the information on my computer,
16 probably 15 minutes.

17 MR. HERSCHMANN: In light of that answer,
18 I'd ask that, with \$19 million on the line, that this
19 witness do it during the recess.

20 MR. MICHEEL: Your Honor, the same
21 objection. They had every opportunity to do that
22 calculation in their surrebuttal testimony. I think it's
23 highly inappropriate to ask my witness to be doing
24 calculations the company could have done.

25 JUDGE WOODRUFF: Could the company have

1 done these calculations?

2 MR. HERSCHMANN: I'm sure we could have. I

3 can ask the witness sitting on the witness stand to do it,

4 but it -- and there's nothing wrong with that in cross,

5 and we've done the calculations, and if you want me to

6 take the time to do it that way, I can. It's 15 minutes,

7 with all due respect. Your Honor, with your permission,

8 let's take an extra 15 minutes for lunch. With \$19

9 million on the table, we should come up with his answer.

10 JUDGE WOODRUFF: I believe that that is

11 information that the Commissioners are going to want

12 anyway. I'll direct you to go ahead and do that. We will

13 take until 1:30 for lunch.

14 With that, we are adjourned until 1:30.

15 (A BREAK WAS TAKEN.)

16 JUDGE WOODRUFF: When we left off, we were

17 in the midst of cross-examination of Mr. Allen by MGE.

18 You may proceed, sir.

19 BY MR. HERSCHMANN:

20 Q. Mr. Allen, did you have the chance to run

21 those calculations during the lunch break?

22 A. Yes.

23 Q. Have you created any documents that we can

24 view?

25 A. Yes.

1 MR. HERSCHMANN: Can I approach the
2 witness, please, and get a copy?
3 (EXHIBIT NO. 32 WAS MARKED FOR
4 IDENTIFICATION BY THE REPORTER.)
5 MR. HERSCHMANN: May I approach?
6 JUDGE WOODRUFF: Yes, you may.
7 BY MR. HERSCHMANN:
8 Q. Do you have Exhibit 32 for identification
9 in front of you?
10 A. This is just marked 32, correct?
11 Q. Yes. I'm sorry. Can you tell us what is
12 contained in Exhibit 32?
13 A. This is a hypothetical capital structure
14 that is consistent with the methodology that I used in my
15 rebuttal testimony, but is done only on the companies that
16 I used in my direct testimony analysis.
17 Q. And dealing with the common equity ratio,
18 what is that percentage?
19 A. On Exhibit 32, it shows that common equity
20 ratio is 37.47 percent.
21 Q. And the preferred equity ratio?
22 A. Preferred equity ratio on Exhibit 32 is
23 5.74 percent.
24 Q. And what is the long-term debt?
25 A. The long-term debt on Exhibit 32 is

1 49.78 percent.

2 Q. And the short-term debt, is that the
3 short-term debt average of the comparable groups that you
4 have, or is that the short-term debt that you've
5 attributed to MGE -- or Southern Union? I'm sorry.

6 A. That is the short-term debt that I showed
7 on schedule -- revised Schedule TA-1 in my rebuttal
8 testimony.

9 Q. What I'm asking is, is that the short-term
10 debt average of the comparable companies that you've
11 listed or is that actually Southern Union's short-term
12 debt?

13 A. That is Southern Union's.

14 Q. And if you remove Southern Union's --
15 withdrawn.

16 Do you know that Southern Union currently
17 has no short-term debt?

18 A. I am aware as of April 30th they have no
19 short-term debt.

20 Q. If you would remove the short-term debt
21 from your calculations on Exhibit 32, what would the
22 numbers be?

23 A. Just a second. Okay.

24 Q. What is the answer on that, sir?

25 A. If you remove the short-term debt from

1 Exhibit 32, what you would have would be a common equity
2 ratio of 40.30 percent, a preferred equity ratio of
3 5.74 percent, and a long-term debt ratio of 53.96 percent.
4 That's if you do it consistent with the methodology that I
5 used to develop the hypothetical capital structure.

6 Q. Can you rate those three numbers on
7 Exhibit 32, please, with the notation that it would result
8 in the removing of the short-term debt?

9 A. Yes.

10 Q. Have you done that?

11 A. I'm working on it.

12 Okay.

13 MR. HERSCHMANN: At this time, I'd offer
14 Exhibit 32 for identification into evidence.

15 JUDGE WOODRUFF: All right. Exhibit 32 has
16 been offered into evidence. Are there any objections to
17 its receipt?

18 (No response.)

19 JUDGE WOODRUFF: Hearing none, it will be
20 received into evidence.

21 (EXHIBIT NO. 32 WAS RECEIVED INTO
22 EVIDENCE.)

23 BY MR. HERSCHMANN:

24 Q. Now, the calculations that you've done in
25 this Exhibit 32, do they reflect an actual higher equity

1 ratio for the comparable group of companies than the
2 calculation that you had submitted in your prior prepared
3 testimony?

4 A. I'm assuming you're referring to whether or
5 not these calculations are higher than the hypothetical in
6 my rebuttal testimony?

7 Q. That's correct.

8 A. Common equity, is that what you asked?

9 Q. Yes.

10 A. Yes.

11 Q. And if you were going to -- withdrawn.

12 When you selected your comparable companies
13 to submit in your testimony, you believe those were the
14 companies that were most comparable to MGE; is that
15 correct?

16 A. Based on my analysis, I believe that to be
17 a comparable proxy group.

18 Q. Have you had occasion to think over the
19 lunch break as to whether or not you are aware of any
20 textbooks that would support your determination not to
21 include Missouri-regulated companies in your comparable
22 group?

23 A. I have not.

24 Q. So currently you're not aware of any source
25 other than the OPC policy of not including

1 Missouri-regulated companies in your comparable group,
2 right?

3 A. I never referred to it as an OPC policy.

4 Q. Did somebody tell you -- withdrawn.
5 Who told you you shouldn't include Missouri
6 regulated companies in your comparable group?

7 A. Nobody told me that.

8 Q. How did you come to the conclusion not to
9 include them?

10 A. As I mentioned to you earlier, after
11 reading prior testimonies.

12 Q. Did you seek to verify in any source
13 whether or not those prior testimonies had any support in
14 utility regulatory industry -- I'm sorry --
15 utility-regulated industry?

16 A. I don't understand your question.

17 Q. You read the testimony of Mr. Burdette,
18 right?

19 A. Correct.

20 Q. In Mr. Burdette's testimony, he said they
21 were not going to include Missouri companies, right?

22 A. Yes, I saw that in his previous testimony
23 filings.

24 Q. In response to questions by Mr. Micheel,
25 you referenced a bunch of books that you've read recently,

1 right?

2 A. Correct.

3 Q. Did any of those books that you referenced

4 cite to the proposition that this Commission should

5 exclude companies that they regulate in determining a fair

6 rate of return or return on equity for a comparable group?

7 MR. MICHEEL: I'm going to object, your

8 Honor. That's been asked and answered.

9 JUDGE WOODRUFF: Overruled.

10 THE WITNESS: Could you repeat the

11 question?

12 MR. HERSCHMANN: Could you read it back?

13 THE REPORTER: "Question: Did any of those

14 books that you referenced cite to the proposition that

15 this Commission should exclude companies that they

16 regulate in determining a fair rate of return or return on

17 equity for a comparable group?"

18 THE WITNESS: No.

19 BY MR. HERSCHMANN:

20 Q. Have you heard of FERC?

21 A. Yes.

22 Q. What do you understand FERC to be?

23 A. FERC is the Federal Energy Regulatory

24 Committee.

25 Q. Do you know what FERC regulates?

1 A. FERC regulates gas distribution pipelines.

2 Q. Do you know if FERC as a policy considers

3 its other decisions in regulating various interstate

4 pipelines that it oversees?

5 A. I don't know.

6 Q. Do any of the textbooks that you reviewed,

7 do you see any citation that says FERC doesn't consider

8 the other companies that it regulates or review the other

9 companies' decisions in reaching its conclusions?

10 A. I'm not sure I understand your question.

11 Could you --

12 Q. Did you read any textbooks that would

13 reflect that FERC, in overseeing interstate pipelines,

14 would set a policy of not reviewing or looking at its own

15 decisions because it oversees those pipelines?

16 A. I'm not familiar with that.

17 Q. Were you able to convince Mr. Tuck that it

18 was appropriate to exclude Missouri-regulated companies?

19 A. I didn't try to convince him. It's

20 ultimately my decision.

21 Q. Did he tell you that he disagreed with your

22 decision?

23 A. Yes.

24 Q. How many more years of experience did

25 Mr. Tuck have in this industry than you?

1 A. I don't know specifically.

2 Q. Have you had occasion to review

3 Professor Morin's testimony in this matter? Did you

4 review his prepared testimony previously?

5 A. I reviewed his rebuttal testimony briefly

6 shortly after it was filed.

7 Q. Did you have occasion to look at his CV?

8 A. His what?

9 Q. His resume.

10 A. Oh. No, I don't recall looking at it.

11 Q. Do you have his testimony in front of you?

12 A. Yes, I have it.

13 Q. Can you turn to his resume attached as an

14 exhibit?

15 A. Which page is that?

16 Q. It's Schedule RAM-1, pages 1 through 19.

17 A. Okay.

18 Q. Will you take a quick moment just to flip

19 through it?

20 A. Okay.

21 Q. Does he seem to have an extensive

22 experience in cost of capital in regulated utilities?

23 A. Yes.

24 Q. You see that he's written several books and

25 published articles and given courses related to cost of

1 capital for regulated utilities?

2 A. I saw the books and articles. Courses,
3 could you direct me to a page, please?

4 Q. I believe it may be in the actual text of
5 his testimony, but let me ask you this: Do you think that
6 Professor Morin has more experience than you in
7 relationship to cost of capital and the issues in this
8 matter?

9 A. Yes.

10 Q. When you were submitting your job
11 application to the banks that you mentioned, did you claim
12 to be an expert in anything on your resume?

13 A. No.

14 Q. Do you think given the choice that this
15 Commission will have between listening to your opinions
16 and your experience compared to those of Professor Morin,
17 given the choice, should they listen to you more heavily
18 and your opinion or Professor Morin?

19 A. In my opinion?

20 Q. Yes.

21 A. They should listen to me more carefully.

22 Q. What's the basis of that opinion?

23 A. Because I've created a fair rate of return
24 recommendation that will result in just and reasonable
25 rates.

1 Q. And yet this is the first time you've ever
2 done this in the real world, right?

3 A. That is correct.

4 Q. What have you done to analyze
5 Pennsylvania Enterpri-- I'm sorry -- Panhandle's business
6 plan?

7 A. I have not looked at Panhandle's business
8 plan.

9 Q. Have you reviewed any of Southern
10 Union's -- conducted any analysis of Southern Union's
11 business plans?

12 A. No.

13 Q. How did you quantify what you claim to be
14 the purported risk to MGE ratepayers in light of the
15 Stipulation & Agreement related to the acquisition of
16 Panhandle?

17 A. I'm sorry. Could you be more specific with
18 that question?

19 MR. HERSCHMANN: I'm not sure I can. Can
20 you read it back?

21 THE REPORTER: "Question: How did you
22 quantify what you claim to be the purported risk to MGE
23 ratepayers in light of the Stipulation & Agreement related
24 to the acquisition of Panhandle?"

25 THE WITNESS: Are you referring to a

1 specific page in my testimony?

2 BY MR. HERSCHMANN:

3 Q. No. I'm asking you a question.

4 A. The question is, how did I quantify the

5 risk related to the Stipulation & Agreement, the

6 acquisition of Panhandle?

7 Q. Right. You said there's an increased risk?

8 A. Yes.

9 Q. How did you quantify that dollar value that

10 you say -- let me take a step back.

11 Do you have any reason to believe that

12 Panhandle or Southern Union will go bankrupt?

13 A. I -- I can't make that determination.

14 Q. Well, do you have any reason to believe

15 it's going to happen?

16 A. I don't have any reason to believe that

17 it's going to happen, but I equally don't have any reason

18 to believe it's not going to happen. It could happen.

19 Q. I'll give you this. I think any company

20 may be able to go bankrupt.

21 A. Exactly.

22 Q. I want to come out of the theoretical stuff

23 and come to the practical environment now. Do you have

24 any evidence, any reason to believe, in reviewing

25 anything, that you believe that it's likely to happen or

1 it's possible it's going to happen within the next five
2 years that Southern Union or Panhandle will go bankrupt?

3 A. I have not reviewed extensively to say for
4 sure that, yes, they could go bankrupt, but it is a
5 theoretical possibility, absolutely.

6 Q. I really want to come out of the
7 theoretical, because you're making a recommendation in
8 this case. I want you to tell us if you're aware in your
9 financial analysis to say, you know what, I've looked at
10 Southern Union now and I've looked at their business plan
11 and their finances and their equity offerings, their debt
12 offerings and their total plan, and I have reason to
13 believe they're on the verge of bankruptcy. Do you have
14 any reason to believe that?

15 A. I cannot make that determination right now.
16 Did anybody have any reason to think that Enron was going
17 to go bankrupt before they went bankrupt?

18 Q. Absolutely, sir. The people that were
19 involved in the corruption, they had every reason to
20 believe that.

21 A. But did the industry?

22 Q. Are you equating MGE to Enron?

23 A. I'm equating the possibilities. There's a
24 possibility.

25 Q. Let's focus on probability.

1 A. I'm thinking I have to look at all angles.

2 Q. One of the angles that you're factoring in

3 in the recommendations that you give in this case is the

4 potential that Panhandle is going to go bankrupt and,

5 therefore, it's going to impact Southern Union as a whole

6 and, therefore, it may have some impact of the ratepayers

7 in Missouri, right, sir?

8 A. The issue is this --

9 Q. Can you answer that question?

10 A. Could you state it again? I'm sorry.

11 MR. HERSCHMANN: Could you read it back,

12 please?

13 THE REPORTER: "Question: One of the

14 angles that you're factoring in in the recommendations

15 that you give in this case is the potential that Panhandle

16 is going to go bankrupt and, therefore, it's going to

17 impact Southern Union as a whole and, therefore, it may

18 have some impact of the ratepayers in Missouri, right,

19 sir?"

20 THE WITNESS: I cannot say that Panhandle's

21 going to go bankrupt, if that answers your question.

22 BY MR. HERSCHMANN:

23 Q. You have no reason to believe that

24 Panhandle's having any financial problems, right?

25 A. I cannot say that they are.

1 Q. So do you have any -- okay. I'm sorry.
2 And do you have any reason to believe that
3 Southern Union's having any financial problems now?
4 A. I cannot say that they are.
5 Q. Do you have any reason to believe that
6 currently, sitting here today, the MGE ratepayers are at
7 risk that Panhandle is going to go bankrupt and,
8 therefore, in violation of the Stipulation & Agreement and
9 Order from this Commission, it's going to impact the MGE
10 ratepayers? Do you have any basis for that belief?
11 A. The issue of impacting MGE ratepayers, it
12 has already impacted MGE ratepayers, and it's not limited
13 to that they're going to go bankrupt.
14 Q. Let's focus first on the bankruptcy issue.
15 A. Okay.
16 Q. Could you answer the question I asked as
17 relates to bankruptcy?
18 THE WITNESS: Could you read it back?
19 THE REPORTER: "Question: Do you have any
20 reason to believe that currently, sitting here today, the
21 MGE ratepayers are at risk that Panhandle is going to go
22 bankrupt and, therefore, in violation of the Stipulation &
23 Agreement and Order from this Commission, it's going to
24 impact the MGE ratepayers? Do you have any basis for that
25 belief?"

1 THE WITNESS: I cannot say that they're
2 going to go bankrupt.

3 BY MR. HERSCHMANN:

4 Q. A potential detriment to the MGE ratepayers
5 that may relate to a potential bankruptcy of Panhandle,
6 you have no basis for that statement, right, or that
7 belief?

8 A. If you limit it to that, yes.

9 Q. Now, can you take out the Stipulation &
10 Agreement again, and we were covering the section dealing
11 with insulation of Southern Union's MGE operation from
12 Panhandle business on page 5, and we got to page 6. Can
13 you look at that for a moment?

14 A. I have to find it. What page?

15 Q. Page 6, please.

16 A. Okay.

17 Q. You see the section that says, conditions
18 to further insulate Southern Union's Missouri customers
19 from any possible adverse consequences associated with the
20 transaction. Do you see that?

21 A. Yes.

22 Q. Do you have any reason -- withdrawn.
23 Do you claim that MGE has violated this
24 agreement in any way?

25 A. Are you speaking specifically to point

1 No. 3?

2 Q. The insulation section that we're

3 discussing, yes.

4 A. Point No. 3?

5 Q. Points 2 and 3.

6 A. Okay.

7 Q. Let me see if I can expedite that. Can you

8 turn just to page 24 for a moment?

9 A. Sure.

10 Q. And can you tell us who signed this

11 Stipulation & Agreement on behalf of the Staff?

12 A. Looks like Robert Franson.

13 Q. And who signed it on behalf of OPC?

14 A. Douglas Micheel.

15 Q. Are you aware of whether or not Mr. Franson

16 or Mr. Micheel have made any claims, whether verbally or

17 in writing, that there's a violation of the Stipulation &

18 Agreement and Order?

19 A. I'm not aware of that.

20 Q. Now, you understand that your counsel

21 sitting here today is a signatory to this agreement,

22 right?

23 A. That's correct.

24 Q. You understand that a Stipulation &

25 Agreement means the parties have stipulated and agreed to

1 something?

2 A. That's correct.

3 Q. There are conditions here with which your

4 counsel agreed would insulate Southern Union's Missouri

5 customers from any possible adverse consequences

6 associated with the Panhandle transaction, right?

7 A. I believe that's what the premise of the

8 Stipulation & Agreement is, yes.

9 Q. And are you saying Mr. Micheel didn't

10 negotiate the terms correctly or he didn't protect

11 Missouri ratepayers correctly when he signed the

12 Stipulation & Agreement?

13 A. I'm saying that that was the premise of the

14 Stipulation & Agreement.

15 Q. Do you have any reason to believe that it

16 didn't do what it was set out to do?

17 A. I don't have any documents that say that

18 they violated the Stipulation & Agreement.

19 Q. That isn't my question.

20 MR. HERSCHMANN: Could you read it back,

21 please?

22 THE REPORTER: "Question: Do you have any

23 reason to believe that it didn't do what it was set out to

24 do?"

25 THE WITNESS: You're referring to the

1 Stipulation & Agreement, the Stipulation & Agreement did
2 not do what it set out to do?

3 BY MR. HERSCHMANN:

4 Q. Right.

5 A. Like I said, I don't have any documents
6 that support -- that say that it is not sufficiently
7 insulated. And I'm not -- I don't see any documents
8 that -- I have not had any documents come across my desk
9 that say that there is a violation, so that's my
10 understanding.

11 Q. I'm not asking you about documents. I'm
12 asking you about your beliefs.

13 Do you have any reason to believe that the
14 Stipulation & Agreement that discusses insulation of the
15 Missouri ratepayers from the transaction, and then further
16 conditions to insulate them, did not accomplish what it
17 was set out to do in this agreement?

18 A. I think there's certainly an issue in this
19 case that I've laid out in my, I believe my rebuttal
20 testimony regarding the floatation costs that would
21 absolutely violate -- MGE's asking for a floatation cost
22 adjustment, and it's my opinion that this would absolutely
23 violate this Stipulation & Agreement, yes.

24 MR. HERSCHMANN: Move to strike as
25 nonresponsive. That wasn't my question.

1 JUDGE WOODRUFF: I'm going to overrule it.
2 You can go back again if you want to.
3 BY MR. HERSCHMANN:
4 Q. This agreement was designed to do
5 something, right?
6 A. That's correct.
7 Q. And your counsel, who you told us helped
8 train you to get ready for your testimony in this case, is
9 a signatory to the agreement, right?
10 A. That's correct.
11 Q. Mr. Franson, sitting here, who's
12 representing Staff in the case, was also a signatory to
13 the agreement, right?
14 A. That's correct.
15 Q. And the conditions here were designed to
16 protect the Missouri ratepayers from the Panhandle
17 acquisition, right?
18 A. That is correct.
19 Q. Do you have any reason to believe that when
20 the agreement was signed and approved by this Commission,
21 it didn't do what it was set out to do?
22 A. I have reason to believe that there is a
23 risk increase to Missouri ratepayers as a result of that
24 capital that will they have influxed into Panhandle,
25 absolutely.

1 Q. So you think the Stipulation & Agreement,
2 in your one month of experience at the OPC, didn't do what
3 it was set out to do based on the multiple years of
4 experience by Mr. Micheel and Mr. Franson in negotiating
5 it, right?

6 A. I believe they tried to insulate Missouri
7 ratepayers to the best of their ability.

8 Q. And you don't think they accomplished it
9 based on your testimony in this case, right?

10 A. I believe -- I believe there's a risk.

11 Q. And it's a risk they weren't able to
12 address in the Stipulation & Agreement that you can talk
13 about based on your couple of months of experience here?

14 A. I'm sorry. Can you repeat that?

15 Q. You don't think they were able to adjust
16 the years based on all the years of experience that they
17 have at OPC and the Commission in the Stipulation &
18 Agreement, and that based on your limited experience here,
19 you can make an assessment that there's still risk that
20 they couldn't handle?

21 A. I'm saying that they did it to the best of
22 their ability, but to capture all of the risk, I'm not
23 sure that this did that.

24 Q. And you know better already, being here a
25 few months, than they do based on their multiple years of

1 experience, right?

2 A. Well, I'm an expert in finance and they are
3 not.

4 Q. Didn't you tell us a moment ago that
5 Mr. Micheel here helped train you?

6 A. I told you that Mr. Micheel helped me --
7 gave me a basic talk regarding the structure of the
8 natural gas industry. That's what I told you.

9 Q. You think Mr. Micheel has any expertise
10 based on all of his years of being involved in all the
11 cases that he mentioned in the opening statement, maybe
12 even more experience than you do in the practical world on
13 these issues?

14 A. I'm not sure I understand the question
15 there. Does he have more experience litigating cases than
16 me? Absolutely. But does he have the expertise in
17 financial training that I have? No, he doesn't.

18 Q. Does he have more experience than you do in
19 cost of capital for regulated utilities?

20 A. In litigating cases?

21 Q. No. Overall, sir. You never dealt with
22 the cost of capital in a regulated utility before you got
23 to the OPC, right?

24 A. That's correct.

25 Q. How many CAPM models did you run?

1 A. Three.

2 Q. And what were the differences -- withdrawn.

3 How many ways can you run a CAPM analysis?

4 A. What do you mean?

5 Q. Are there different ways to run -- is there

6 different formulas or is there one formula?

7 A. The basic formula is the one that I laid

8 out in my testimony. There's different inputs. I mean,

9 presumably there could be an infinite number of inputs

10 that you could use. Theoretically, there is.

11 Q. When you ran the CAPM analysis, you ran the

12 one that you thought was most applicable to this case; is

13 that right?

14 A. That's correct.

15 Q. And of the three that you did run, which

16 one did you run first?

17 A. The three that I ran, I ran the one that I

18 used first because that's -- that was my -- my preference,

19 the inputs that I used, those were the ones that I

20 believed to be most appropriate.

21 Q. And when did you come to that conclusion?

22 A. Through my education process.

23 Q. I'm sorry. When after you ran the first

24 one did you come to the conclusion it was the right

25 answer?

1 A. I don't think you understood my answer.
2 What I'm saying is that the question is not how you run
3 the CAPM. The question primarily is the inputs. And
4 through my education and my years experience with it, the
5 inputs that I used, those are the ones that I preferred to
6 use in the CAPM analysis. And that's the best answer I
7 can give to that.

8 Q. I don't think you understood my question.
9 You told us you ran three CAPM analyses, right?

10 A. That's correct.

11 Q. And you told us that the one you decided to
12 submit and discuss in your written testimony, not in the
13 schedules, was the first one that you ran, right?

14 A. That's correct. It was the -- the one that
15 I submitted in my testimony was the first one I ran.

16 Q. And that was the one -- when you finished
17 running it, were you really comfortable with it?

18 A. Yes.

19 Q. You thought it was accurate, right?

20 A. Yes.

21 Q. You didn't need to check it over again, did
22 you?

23 A. I ran the other two because I knew that
24 there would be controversy over the risk-free rate that I
25 chose.

1 Q. Why did you know there would be controversy
2 over it?

3 A. Because that is the one variable that there
4 is a lot of controversy over, regardless of any CAPM
5 analysis.

6 Q. And did you run it to check your first
7 numbers to see how reasonable they were?

8 A. No.

9 Q. When you ran the second one, was that
10 higher or lower than the one you're recommending to this
11 Commission?

12 A. Do you have a page number?

13 Q. I'm talking about your schedules. Do you
14 know which ones they are?

15 A. I'm not sure where it is. The second one I
16 ran was -- was run using the 10-year T note, and it was
17 higher.

18 Q. And what about the third one that you ran?

19 A. I ran that one using the 30-year T note,
20 and it was higher.

21 Q. Did you run the CAPM as a check on your DCF
22 calculations?

23 A. That's correct.

24 Q. When it came out with -- well, what was
25 your total DCF calculation range?

1 A. The entire range before I threw out the
2 low?

3 Q. Right.

4 A. 8.04, 9.01, 9.34.

5 Q. And when you ran your CAPM to check it, did
6 you notice a difference between the 9.34 number and the
7 10.27 number that you got?

8 A. Yes. I noticed there was a difference
9 between those two numbers.

10 Q. And you decided to ignore the 10.05 and the
11 10.27 numbers that you got, right?

12 A. That's not correct.

13 Q. You didn't use them, did you?

14 A. I did not use them, but I told you
15 beforehand that I determined what I was going to use
16 before I even ran the calculations. So what the numbers
17 turned out to be, that's what they turned out to be. I
18 didn't manipulate the data.

19 Q. There was no reason to even do that
20 calculation, then, right?

21 A. There was a reason to do the calculation,
22 as I said, because I knew that there would be controversy
23 regarding my use of the 3-month T bill. So I ran the
24 other models just for completeness.

25 Q. And then ignored them after you ran them,

1 right? You didn't adjust anything for them?

2 A. I didn't use them.

3 Q. You ignored them, right?

4 A. I didn't use them.

5 Q. You went through the effort of running the

6 calculations, right? Did you go through that effort?

7 MR. MICHEEL: I'm going to object. That's

8 been asked and answered now at least three or four times,

9 your Honor.

10 JUDGE WOODRUFF: I'll sustain the

11 objection.

12 BY MR. HERSCHMANN:

13 Q. You picked the lower CAPM number because it

14 was convenient for you and it worked within the results

15 that you wanted, right?

16 A. Absolutely not. I've already answered the

17 question that I picked the inputs that I was going to use,

18 and regardless what it turned out to be, that's what it

19 was going to be.

20 MR. HERSCHMANN: Would you read back the

21 answer for a moment, please?

22 THE REPORTER: "Answer: Absolutely not.

23 I've already answered the question that I picked the

24 inputs that I was going to use, and regardless what it

25 turned out to be, that's what it was going to be."

1 BY MR. HERSCHMANN:

2 Q. Once you picked those inputs, you weren't

3 going to make any changes regardless of the results,

4 right?

5 A. I was not going to manipulate the data.

6 The most important thing is picking the inputs and being

7 comfortable with the inputs you use in the model. Now, if

8 the results were -- if the results of my CAPM turned out

9 to be 10.5 with the CAPM model that I chose to use, which

10 as I've indicated was selected before the results even

11 came out, then yes, I would have noted that there was a

12 problem with my DCF analysis. But it didn't. The CAPM

13 that I'd already chose to use was right in the middle of

14 the range. So it completely, it absolutely supported my

15 analysis.

16 Q. What did Professor Morin say about your two

17 calculations, sir?

18 A. Professor Morin did not speak to my two

19 calculations.

20 Q. Do you remember listening to his

21 deposition?

22 A. Yes.

23 Q. Do you have his deposition in front of you?

24 A. Yes.

25 Q. Can you turn to page 105?

1 A. Okay.

2 Q. Do you see the question asked by

3 Mr. Micheel beginning -- he says, let me say that you have

4 a DCF analysis and you come up with a DCF range of

5 9.01 percent to 9.3 percent. Can you make that

6 assumption? Answer: Yes.

7 Let's say that you do a capital asset

8 pricing methodology analysis and you come up with a result

9 of 9.17. Can you make that assumption? Answer: Yes.

10 What does that tell you? Answer: That

11 tells you that something is wrong.

12 I'm sorry. Let me say that again. I'm

13 sorry.

14 That tells you that something's wrong,

15 because I can't visualize a rate of return of 9 percent

16 when the long-term Treasury bonds are expected to be

17 6 percent.

18 Question: Well, that wasn't my question

19 about whether or not. My question was, what does that

20 tell you about the reliability of the DCF method and the

21 CAPM method? Answer: It tells you that those two are

22 consistent with one another, but it doesn't tell you that

23 that's -- that that's the cost of equity. It's not

24 implemented properly.

25 Question: What does it mean if they're

1 consistent with one another from a statistical standpoint?

2 Answer: Roughly within the same range, maybe within

3 50 basis points of one another.

4 Question: And if you had that example that

5 I just gave you, a DCF range of 9.01 to 9.3 percent and a

6 CAPM result of 9.17 percent, wouldn't that indicate that

7 your CAPM and your DCF were compatible? Answer: It would

8 probably indicate to me that they're both wrong.

9 Do you see that?

10 A. Yes.

11 Q. That testimony was based on your

12 calculations, right?

13 A. It was a hypothetical.

14 Q. Based on your numbers, though, right, sir?

15 A. I can't disagree with that, but it

16 wasn't -- he didn't specifically say my numbers.

17 Q. Didn't say your name, but these are the

18 numbers that you used in your submission in this case,

19 right?

20 A. Correct.

21 Q. And you actually ran a CAPM -- two CAPM

22 calculations that came out higher than your DCF analysis,

23 and then decided not to use them, right?

24 A. No, that's not correct.

25 Q. Didn't you tell us a moment ago you didn't

1 use them? When I asked you if you ignored them, you said,
2 I didn't use them?

3 A. I did not use them.

4 Q. So you ran the other two CAPM analyses to
5 check the DCF and then did not use it, right?

6 MR. MICHEEL: Your Honor, that's been asked
7 and answered now about four times. I'm going to object
8 yet again.

9 JUDGE WOODRUFF: The last time he got a
10 different answer. I'm going to overrule the objection.
11 You can inquire.

12 MR. HERSCHMANN: Would you read back the
13 question.

14 THE REPORTER: "Question: So you ran the
15 other two CAPM analyses to check the DCF and then did not
16 use it, right?"

17 THE WITNESS: I ran the other two CAPM
18 analyses to check my DCF, and then I did not use it. That
19 was the question?

20 BY MR. HERSCHMANN:

21 Q. Yes.

22 A. I ran all three. I did not use the last
23 two. I don't know if I'd misspoken before, but that's my
24 answer.

25 Q. Do you recall saying that you believe

1 short-term debt should be excluded from a rate of return
2 analysis only if it is less than 2 percent of the capital
3 structure after construction work in progress is
4 subtracted?

5 A. Yes.

6 Q. Where did you get the 2 percent number from
7 or less than 2 percent?

8 A. Through my education. It's common that
9 it's between 2 and 3 percent.

10 Q. What textbook do you have as a source
11 dealing with utilities cost of capital for that statement?

12 A. I don't have any textbook source.

13 Q. What's the basis then -- or withdrawn.
14 Did you read a case that said that you
15 should use the less than 2 percent number?

16 A. I believe that it was in Mr. Burdette's
17 testimony, and along with my education of the basic --
18 generally the basic level is somewhere between 2 and 3
19 percent. He had used 2 percent. So I considered that
20 adequate, and I adopted that.

21 Q. What source did you use to check
22 Mr. Burdette's 2 percent number, whether it be some
23 Internet source, a textbook, a peer review article, any of
24 the books that you read; where did you check that number
25 to make sure that it complied with accepted methodologies?

1 A. That is -- again, it's almost like a -- I
2 don't know. I can't give you a specific source.

3 Q. That's because you didn't check it
4 anywhere, right?

5 A. It's not a -- I didn't consider it to be an
6 issue because it's a well known -- I mean, through my
7 education, that is what we -- that's what I was taught.
8 And after seeing Mr. Burdette's testimony, I had no reason
9 to disbelieve that.

10 Q. What does Mr. Burdette do now?

11 A. I don't know.

12 Q. What did he do before he came to the OPC?

13 A. I don't know.

14 Q. What is his educational background?

15 A. You know, I read it in his direct
16 testimony, but I can't recall exactly what his educational
17 background is. I think he had an MBA, with a
18 specialization in finance, but I can't be sure of that.

19 Q. Did you discuss this percent number with
20 anybody prior to putting it into your testimony?

21 A. I think it came up in conversation with
22 Mr. Tuck, but I can't be sure of that.

23 Q. What would the results have been if you
24 didn't use this 2 percent number or less than 2 percent?

25 A. I'm not sure. I didn't check that.

1 Q. What was the reason you didn't check it,
2 sir?

3 A. Because I was comfortable with the
4 standards that I set.

5 Q. Did you ask Mr. Tuck, did he have a source
6 for the less than 2 percent?

7 A. I don't believe.

8 Q. Did you ask Mr. Micheel if he had a source
9 for the less than 2 percent?

10 A. I don't believe I talked to Mr. Micheel
11 about it.

12 Q. Did you go on the Internet to find a source
13 for the less than 2 percent?

14 A. No.

15 Q. You mentioned the issue of floatation
16 costs; is that correct?

17 A. That is correct.

18 Q. Why do you believe -- withdrawn.
19 Was all of the proceeds from the equity --
20 common equity offering and equity units offering used to
21 acquire Panhandle?

22 A. I'm sorry. Which equity offering are you
23 referring to?

24 Q. Let me take a step back. You object to any
25 request dealing with floatation cost; is that correct?

1 A. I'm sorry. What did you say?

2 Q. You object to the request that floatation

3 costs be included in this proceeding, right?

4 A. Yes.

5 Q. What floatation costs are you objecting to?

6 A. Mr. Dunn, in his direct testimony, has

7 testified that he believes that the floatation costs

8 should be added to the rate of return because of the fact

9 that he believes that Southern Union will be issuing stock

10 in the future.

11 Q. Do you know for what reason Southern Union

12 will be issuing stock in the future?

13 A. Yes.

14 Q. Have you read somewhere what the intent is

15 for the offerings?

16 A. Southern Union is under -- has made --

17 Q. My question is, have you read something?

18 MR. HERSCHMANN: Can you read back the

19 question, please?

20 THE REPORTER: "Question: Have you read

21 somewhere what the intent is for the offerings?"

22 THE WITNESS: My understanding is that it

23 is to shore up their balance sheet.

24 BY MR. HERSCHMANN:

25 Q. Did you read that somewhere, sir?

1 A. I believe through -- I read it on a
2 Standard & Poor's website.

3 Q. When did you read it on the Standard &
4 Poor's website that Southern Union's planned equity
5 offering was going to be to shore up their balance sheet?

6 A. I don't know the specific date.

7 Q. Do you know what Southern Union -- well,
8 withdrawn.

9 You told us earlier you didn't know what
10 Southern Union's balance sheet was like before it acquired
11 Panhandle, right?

12 A. I told you I couldn't give you a specific
13 number.

14 Q. Was it comparable to what it was like
15 before Panhandle as after Panhandle; do you know that?

16 A. I can't tell you off the top of my head.

17 Q. If they were similar to each other, do you
18 have any reason to believe that an equity offering would
19 have been related to Panhandle as of today versus an
20 overall corporate strategy?

21 A. Could you repeat that?

22 Q. Do you have any understanding based on
23 anything that you've read as to what would be the explicit
24 purpose for any equity offerings at this time?

25 A. Yes, based on anything I've read, I do have

1 an understanding of what the equity offering would be.

2 Q. And you think that's to improve Southern
3 Union's balance sheet, right?

4 A. Correct.

5 Q. And if Southern Union's balance sheet was
6 similar to -- it is -- the way it is now before the
7 Panhandle acquisition as it is after the Panhandle
8 acquisition, you still believe that the equity offering is
9 a -- would have a negative impact on MGE ratepayers?

10 Do you want me to rephrase that?

11 A. Yeah, that was a pretty loaded question.

12 Q. Yeah. It was a good one. Doug appreciated
13 that.

14 I want to focus on floatation costs. Okay.

15 It's your belief that the request for floatation costs is
16 inappropriate because it relates to an equity offering,
17 and the equity offering is solely because of the Panhandle
18 related acquisition, right?

19 A. Yes, I believe that the Panhandle
20 acquisition substantially leveraged their capital
21 structure.

22 Q. Okay. And if the Panhandle acquisition did
23 not substantially leverage Southern Union's capital
24 structure, do you still have a further objection or claim
25 that the floatation costs would violate the Panhandle

1 agreement?

2 A. When you look at -- when we're talking
3 about the consolidated capital structure, it absolutely
4 did. I mean, you add \$1.2 billion of debt to a -- at that
5 time a \$2 billion capital structure.

6 Q. That's your answer?

7 A. That's it.

8 Q. So if it turns out that you're wrong about
9 that it didn't substantially change Southern Union's
10 balance sheet, you don't have any objection to a
11 floatation cost adjustment, right?

12 A. I would have to look at it and see if I
13 thought I was wrong.

14 Q. Presume for a moment that it didn't.

15 A. I can't make that presumption.

16 Q. You can't think outside the box?

17 A. No.

18 Q. Other than the floatation costs question,
19 do you think there's any other violations in the
20 Stipulation and Order?

21 A. As I mentioned before, I have not seen
22 anything come across my desk.

23 Q. Now, have you had occasion -- withdrawn.
24 You agree that equity investors can only
25 buy stock in Southern Union, they can't buy it in MGE,

1 right?

2 A. If you buy stock in Southern Union, you're

3 buying stock in the entire company, including Panhandle

4 and MGE.

5 Q. And you can't buy MGE individually, right?

6 A. That's correct.

7 Q. Are you aware of whether any commissions

8 have ever used a hypothetical capital structure for

9 ratemaking purposes?

10 A. Yes, this Commission has done it.

11 Q. That's for a division of the company,

12 right?

13 A. I'm sorry.

14 Q. That's in relationship to a division of a

15 company, right?

16 A. Are you referring to the St. Joe case?

17 Q. Yes.

18 A. I'm not sure if St. Joe's was a division or

19 not.

20 Q. Did you ever look at any cases or in the

21 textbooks that you read that commissions actually use a

22 hypothetical capital structure for the divisions that they

23 oversee in their jurisdiction?

24 A. I have not seen any textbooks.

25 Q. Did you review any decisions that would

1 have reflected the fact that commissions look at the
2 divisions that they oversee when they set rates for that
3 division based on a typical capital structure?

4 A. I'm sorry. Could you repeat that?

5 Q. Sure. Did you review any decisions for any
6 jurisdictions in the whole country that would have
7 informed you of the fact that commissions, when they're
8 setting rates for the divisions of the company that they
9 oversee, look at the hypothetical capital structure for
10 that division?

11 A. I have not seen anything. The case that I
12 looked at was applicable to this Commission and what
13 they've said in the past. That was based on my
14 hypothetical capital structure.

15 Q. Would it surprise you that the
16 jurisdictions that oversee divisions of the company
17 actually focus on the division of the -- that company?
18 Withdraw that.

19 Would it surprise you that if commissions
20 were setting rates for divisions of a company, they would
21 look at the hypothetical capital structure for that
22 division?

23 A. Would it surprise me? When you're in the
24 land of hypothetical, no, it wouldn't.

25 Q. Did you have occasion to read Mr. David

1 Murray's testimony in this case?

2 A. Yes.

3 Q. And did you agree with everything that was
4 contained in his testimony?

5 A. Are you speaking to his direct testimony?

6 Q. All his prepared testimony and his
7 deposition.

8 A. I didn't agree with everything in there.

9 Q. There were actually many things that you
10 didn't agree with; is that correct?

11 A. Yes. As stated in my deposition, there was
12 a lot of things in his testimony, his methodology that I
13 didn't agree with, but his end result, I can't honestly
14 disagree with that.

15 Q. Let's talk about his methodologies for a
16 moment. There are many things in his methodologies that
17 you think he did incorrectly, right?

18 A. Yes. I stated that in my deposition.

19 Q. And prior to submitting your surrebuttal
20 testimony and your rebuttal testimony, with whom did you
21 speak at the OPC?

22 A. Oh, I don't know. Casually I probably
23 spoke to everybody. I'm a pretty friendly guy.

24 Q. Try to keep it focused in to this case.

25 A. Can you be more specific? I'm sorry. That

1 was inappropriate. I apologize.

2 Q. That's okay. It's been a long day.

3 As far as matters related to the submission

4 of your testimony and your deposition, with whom did you

5 speak?

6 A. Specifically, I probably -- I think I spoke

7 with Mr. Micheel and Mr. Trippensee. It's kind of hard

8 for me to remember who exactly I spoke with and about

9 what.

10 Q. Did you speak to Mr. Allen about his

11 testimony?

12 A. I am Mr. Allen.

13 Q. I'm sorry. Did you speak to Mr. Murray

14 about his testimony?

15 A. After filing or before?

16 Q. Both.

17 A. Not before.

18 Q. After the filing of the testimony?

19 A. Yes, but I was -- nothing that I remember.

20 I was -- I didn't speak any specifics because I was aware

21 that I would probably be deposed. So I tried to not speak

22 about the specifics of an analysis or the case.

23 Q. Did you speak to anyone else at the Staff?

24 A. No.

25 Q. When you prepared your surrebuttal

1 testimony in this case -- I'm sorry -- your rebuttal
2 testimony, you listed two matters for which you disagreed
3 with Mr. Murray; is that correct?

4 A. That's correct.

5 Q. What were those two matters?

6 A. Embedded cost of -- his calculation of the
7 embedded cost of long-term debt, and the way in which he
8 calculated the level of short-term debt.

9 Q. And you included those two things in the
10 testimony; is that correct?

11 A. That's correct.

12 Q. And were there other things that you
13 disagreed with that you decided not to put in your
14 rebuttal testimony?

15 A. Yes. I have limited resources and limited
16 time, so I focused on the bigger issues, and I thought
17 that was -- the bigger issue was Mr. Dunn's analysis.

18 Q. Let me ask this question: Did you have
19 other criticisms or disagreements with how Mr. Murray was
20 trying to run his methodologies for this case?

21 MR. MICHEEL: I'm going to object, your
22 Honor. It's been asked and answered. He's asked that two
23 or three times, and this witness has said yes.

24 JUDGE WOODRUFF: I'll sustain the
25 objection. I think he has answered that question. You

1 can move on.

2 BY MR. HERSCHMANN:

3 Q. You had criticisms of Mr. Murray -- do you
4 need to take a break?

5 A. No. I'm all right. It was just ice.
6 What was the question?

7 Q. Did you have these disagreements that you
8 listed in your deposition testimony about Mr. Murray's
9 calculations at the time you submitted your rebuttal
10 testimony?

11 A. Yes.

12 Q. So you disagreed after reviewing
13 Mr. Murray's submission of his testimony with how he
14 calculated his long-term debt cost, right?

15 A. Correct.

16 Q. How he calculated his short-term debt,
17 right?

18 A. The level of short-term debt, correct.

19 Q. You disagreed with his use of negative
20 growth rates, right?

21 A. I'm assuming you're referring to my
22 deposition. If you could refer me to a page, that way I
23 would know what you're speaking of.

24 Q. I don't have it down as pages. I just have
25 it written down.

1 A. Just a second then. I'll find it.

2 Q. According to my notes, it's going to be in
3 the 70-pages range. I'm told if you look starting at
4 page 72 you can tell. If you can answer it without
5 looking at your deposition, that may be a little quicker,
6 and if we miss something, just tell me. Did you disagree
7 with how Mr. Murray -- or Mr. Murray's use of negative
8 growth rates?

9 A. Yes.

10 Q. You disagree with how Mr. Murray used data
11 only through 2002?

12 A. Yes.

13 Q. You disagree with how Mr. Murray used
14 historic market premium in his CAPM?

15 A. Yes.

16 Q. Moving to the sixth disagreement, did you
17 disagree with Mr. Murray's calculation of growth rate?

18 A. Yes.

19 Q. Did you disagree with how Mr. Murray picked
20 his comparable company selection criteria 90 percent
21 income from natural gas distribution?

22 A. Yes. My filter was 60 percent.

23 Q. There are a lot of inputs that go into the
24 DCF calculation that you think Mr. Murray did wrong,
25 right?

1 A. Specifically, I think they pertain to the
2 growth rate, the ones that you've listed, DCF.

3 Q. And you actually think that Mr. Murray's
4 work was done in a mechanistic form, right?

5 A. Yes, I believe it was not subjective
6 enough.

7 Q. And did you discuss your opinion of
8 Mr. Murray's testimony with Mr. Tuck?

9 A. I don't remember having a specific
10 conversation where we sat down and talked specifically
11 about that. It may have come up. I honestly don't
12 recall.

13 Q. And did Mr. Tuck say that you were right,
14 Mr. Murray was inaccurate in the inputs that he used?

15 A. I don't recall that.

16 Q. Did he disagree with you about your opinion
17 of Mr. Murray?

18 A. I honestly don't recall. I know Mr. Tuck
19 was in agreement with my analysis. So, I mean, I don't
20 want to put words in his mouth.

21 Q. And did you use the annual DCF model -- I'm
22 sorry. You used the semi-annual DCF model and you
23 disagree with Mr. Murray's use of the annual DCF model,
24 right?

25 A. That's correct. I believe my -- the

1 semi-annual is a better use of a model.

2 Q. And you disagree with how Mr. Murray tried
3 to calculate the growth rate, right?

4 A. That's correct.

5 Q. You actually disagree with how he performed
6 the CAPM analysis, and that he used the dividend growth
7 rates and you decided not to, right?

8 A. Not the CAPM.

9 Q. I'm sorry?

10 A. Not CAPM.

11 Q. I'm sorry?

12 A. Dividends have no part in CAPM.

13 Q. I apologize. Did you perform the CAPM
14 differently than Mr. Murray?

15 A. Yes.

16 Q. And you don't think he did that correctly
17 either, right?

18 A. He criticized me for using the current
19 risk-free rate. What he did was used historical market
20 risk premium, and I believe that doesn't do as good a job
21 of capturing current investor expectations.

22 Q. And you think he did it incorrectly, then,
23 right?

24 A. I -- it's hard to say. It's a subjective
25 thing, but I would not have done it that way.

1 Q. And did you disagree with his use of
2 dividend growth rates?

3 A. In this specific case, yes.

4 Q. How many investors of utilities have you
5 spoken with?

6 A. I haven't spoken to any. Well, I spoke to
7 Mr. Dunn.

8 Q. Fair enough. Are you going to rely on
9 Mr. Dunn's recommendations of matters in this case?

10 A. No.

11 Q. This will be a lot quicker if you will.
12 How many institutional investors did you
13 speak to in your career?

14 A. I've spoke with Mr. Tuck, but that's the
15 extent of it.

16 Q. Other than Mr. Tuck -- let's separate this
17 case for a minute. Have you ever spoken to any
18 institutional investors as to what they are looking for in
19 returns on equity?

20 A. No, I have not.

21 Q. Did you ever consult or ask to be put in
22 contact with anyone at S&P or Moody's to talk about what
23 their views were on return on equity or ROR?

24 A. Not specifically for ROR and return on
25 equity.

1 Q. Have you ever read any criticisms of the
2 ratemaking process in Missouri by any of the analysts from
3 either S&P or Moody's?

4 A. No.

5 Q. Have you ever heard of any criticism about
6 the process of ratemaking in Missouri compared to other
7 jurisdictions?

8 A. Yes.

9 Q. What were the criticisms that you heard?

10 A. The criticisms are limited to Mr. Dunn's
11 direct testimony.

12 Q. You ever go on the Internet to see if you
13 can find the criticisms that exist on ratemaking for
14 Missouri compared to other jurisdictions?

15 A. No.

16 MR. HERSCHMANN: I'll pass the witness.

17 JUDGE WOODRUFF: All right. Thank you.

18 We'll come up then for questions from the Bench.

19 Commissioner Clayton?

20 QUESTIONS BY COMMISSIONER CLAYTON:

21 Q. Where to begin. Where to end. I'd like to
22 start off by looking at an exhibit that we looked at
23 earlier today. Do you have a copy of John J. Gillen's
24 rebuttal testimony, Schedule JJG-2?

25 A. No, I do not.

1 JUDGE WOODRUFF: If counsel could provide
2 that for him?

3 MR. MICHEEL: I figured you were going to
4 ask me that. If you bear with me, I do have it. JJG-2?

5 COMMISSIONER CLAYTON: It's the one that we
6 were working on this morning.

7 MR. MICHEEL: Okay. There it is.

8 BY COMMISSIONER CLAYTON:

9 Q. Have you seen that document before?

10 A. I read his testimony briefly, but I have
11 not studied this document, no.

12 Q. What I'd like you to do is -- well, were
13 you in the -- were you in the hearing room when Mr. Gillen
14 was on the stand this morning before we went upstairs to
15 agenda and talked about subjects that were completely off
16 this subject matter for five hours?

17 A. Yes, I was in the room.

18 Q. Okay. I'd like you to take a moment and
19 look at that document. It has three columns of interest;
20 the subtotal of the consolidated capital structure -- or
21 excuse me -- the consolidated capitalization of Southern
22 Union Company has a -- it has the Southern Union
23 stand-alone capitalization, as well as the Panhandle
24 stand-alone structure.

25 A. Okay.

1 Q. And what I'd like for you to tell me is, in
2 light of the simplistic by basically dividing the debt
3 entries here by the total capitalization, we come up with
4 the ratios for each of -- for debt, for preferred stock
5 and then the common equity. Could you explain to me how
6 your analysis computes with these three columns at the end
7 of Schedule JJG-2?

8 Do you understand my question?

9 A. You want to know how my analysis or my
10 capital structure computes with these two?

11 Q. Yes.

12 A. Okay.

13 Q. How would your column fit into this, in
14 terms of the capital structure of MGE that should be used
15 for ratemaking purposes?

16 A. The capital structure, Commissioner, that I
17 have recommended in my direct testimony -- I'm sorry. I
18 updated it in my rebuttal testimony.

19 Q. Whichever testimony.

20 A. Yeah. I updated it in my rebuttal
21 testimony. The capital structure is based on
22 December 31st, 2003 numbers, and it is the consolidated
23 capital structure. So it would be representative of the
24 far-left column in Mr. Gillen's table here. I'm not sure
25 if he has the exact numbers. But I -- I calculated this

1 based off of a Data Request that I sent to the company,
2 and so I'm not sure that answers your question or not.

3 Q. Well, I think that it does, but the numbers
4 on this, if you actually run the percentages, the ratios,
5 the debt that's down at the bottom, amounts of both short-
6 and long-term amounts of about 55 percent preferred equity
7 is roughly 9.8 percent, leaving common equity of 43.1,
8 your proposed consolidated capital structure is
9 26.1 percent for common equity, 6.17 percent for
10 preferred, and then another roughly 67, 68 percent for
11 debt.

12 A. Okay.

13 Q. So what I want to know is how your column
14 of consolidation would compare to that and how those
15 percentages come out. I'm not asking for specific numbers
16 on each line, but I'm asking, generally speaking, what
17 would yours look like? That consolidated section, that
18 first column removes the Panhandle equity under
19 eliminations, that was discussed earlier, and it also
20 removes the retained earnings.

21 A. Uh-huh.

22 Q. So what other -- what other changes have to
23 occur to this to make it reflect your capital structure?

24 A. The date of Mr. Gillen's calculation was
25 March 31st, 2004, whereas I calculated mine on December.

1 Q. So there's a three-month difference?

2 A. Yeah.

3 Q. Was that due to an increase or a reduction

4 in debt? Obviously there would have to be an increase in

5 debt somewhere?

6 A. Yeah. It looks as though -- I mean, if you

7 give me a second to study this.

8 Q. We've got the next two weeks.

9 A. Yeah, it looks as though -- I mean, I don't

10 have the specific table here that I used to calculate --

11 Q. I understand.

12 A. -- my numbers, so to try --

13 Q. I want a general guidance of how the

14 numbers changed. Obviously --

15 A. The debt -- it looks like the debt has

16 increased by apparently roughly \$100 million, if I'm

17 reading this table correctly. Stockholders equity they

18 have at approximately \$1.2 billion that I'm assuming --

19 I'm not sure how I can get -- I would have to look at my

20 sheet.

21 Q. Do you have that sheet close by?

22 A. I have it up in my office.

23 MR. MICHEEL: We will be happy to -- we've

24 already calculated some other things, your Honor, so if

25 you want to take a five-minute break . . .

1 COMMISSIONER CLAYTON: I don't know if
2 that's necessary.

3 MR. MICHEEL: Okay.

4 BY COMMISSIONER CLAYTON:

5 Q. Is basically the difference in actual
6 consolidated capital structure the difference just based
7 on changes in numbers over time, or is there an actual
8 difference in computation of how this structure should be
9 set up?

10 A. If you look also, Commissioner,
11 Mr. Gillen's capital structure does not include any
12 short-term debt.

13 Q. Well, it actually does, I think.

14 A. I don't --

15 Q. We think that's notes payable, which is the
16 last line.

17 A. I may be mistaken.

18 Q. So am I comparing apples to oranges here?

19 A. I think so.

20 Q. Are you aware of anything that -- anything
21 significant that happened between December 31 and March 31
22 which would modify the actual capital structure?

23 A. I know they had a shelf registration of
24 equity, but I don't believe they have issued any equity
25 since then, and I'm not aware of any excessive amounts of

1 debt they've taken on. Short-term debt, they've cleared
2 out that balance. That's what I'm aware of as of right
3 now.

4 Q. So other than the short-term debt, you're
5 not aware of any other changes?

6 A. Not that I'm aware of.

7 Q. I want to know how we get from in this
8 actual consolidated structure from your 26 percent to in
9 this chart roughly 43 percent in common equity? What
10 would be the answer?

11 If I'm not asking a fair question, maybe
12 someone could object or something, but since you are the
13 finance person, I need you to explain that to me.

14 A. I'm not sure I can answer that without
15 looking at my calculation and trying to compare it to
16 this. I haven't studied this -- this chart.

17 Q. Okay. Your initial proposed consolidated
18 capital structure is very similar to Staff's. Is the
19 methodology the same or is it not in your --

20 A. Our capital structures?

21 Q. In your consolidated.

22 A. I believe the difference between Staff --
23 the primary difference between Staff and I, it is pretty
24 similar, but there was a difference in the way in which we
25 calculated our level of short-term debt. Staff

1 essentially took, like, a snapshot, and what I did was I
2 took a -- a look at it over an entire year's process,
3 because I believe that gives a better calculation of how
4 this company uses short-term debt over -- on a consistent
5 basis.

6 Q. Okay. Well, that's small potatoes. That's
7 just a small difference?

8 A. Yes. Yes.

9 Q. Explain to me how you calculated your
10 proposed hypothetical capital structure.

11 A. Okay. Do you have Exhibit 32 in front of
12 you, sir, or do you have a copy of my rebuttal testimony
13 in front of you? That will be easier.

14 Q. I've got all of it up here, but like you, I
15 don't know if I can find it right away. It may be up in
16 my office. Can I run up and get it?

17 A. Sure. You know what, you're not on the hot
18 seat, so why not?

19 Q. Well, I will at some point. I've got
20 Exhibit 32, though.

21 A. Okay. Exhibit 32 is what the company asked
22 me to do over lunch. This is not my recommended
23 hypothetical capital structure, but it will serve as a
24 basis for how I calculated my hypothetical capital
25 structure.

1 Q. Okay.

2 A. What I did, sir, was you see the common
3 equity ratio on the top part of this page, this Exhibit 32
4 titled common equity ratio?

5 Q. Maybe I'm not looking at Exhibit 32.
6 Common equity, it doesn't say ratio?

7 A. I'm sorry. Common equity. Yeah, it is a
8 ratio. I'm sorry. I had collected this for each company
9 in -- in my recommended hypothetical capital structure, I
10 have collected these percentages for the last five years
11 for each company in Mr. Dunn's group, or his comparable
12 group.

13 The reason I did it for Mr. Dunn's group
14 was because, when you're in -- thinking of a hypothetical
15 capital structure, what you want to do is you want to get
16 as broad a picture as you can, because you're trying to
17 get an indication as what does a typical LDC's capital
18 structure look like. So in order to do that, what I did
19 was I calculated what I called in my rebuttal testimony a
20 zone of reasonableness.

21 So if you follow along with me, each
22 company has an average. I've averaged their capital
23 structure, their equity ratio for the last five years, and
24 that's shown below; in this example it's 49.75. Then I
25 took the standard deviation of that group of averages, and

1 I added a standard deviation and I subtracted the standard
2 deviation from my -- from my mean equity ratio. So in
3 this example it was 49.75.

4 I would have added the 9.45 and subtracted
5 the 9.45 from it, and that gives you what I called a zone
6 of reasonableness. It gives you one standard deviation
7 away from the mean and not -- and what that definition of
8 one standard deviation from the mean is, it's going to
9 include all -- about 68 percent of all -- of all
10 observations, excluding the outliers.

11 So once I calculated the range, I
12 attributed the low end of my recommended range to Southern
13 Union, because it's my opinion that the most -- the
14 capital structure that should be adopted in this
15 proceeding is a consolidated capital structure. And my
16 calculation, the consolidated capital structure as of
17 December 31st, 2003 was 26.1 percent, so there was no need
18 to -- to bring Southern Union any farther up into the zone
19 of reasonableness. I brought them up to the zone of
20 reasonableness, which was the bottom end of that range.

21 The next step that I did was I -- in this
22 example, it was 37.47. What I did was I took the
23 preferred equity ratio that I calculated on revised
24 Schedule TA-1, which was, in this example, 5.74 percent,
25 and whatever was left, so when you add 37.46 to 5.74 you

1 get 43.21. I believe I just -- I misled you in my haste
2 to explain this, and I'm going to try to backtrack to --
3 to correct my mistake.

4 The zone of reasonableness in this case
5 right here is if you subtract the 9.45 from the 49.75, the
6 bottom of the zone of reasonableness is 40.3 percent.
7 Correct. So that was my beginning equity ratio in my
8 development of my hypothetical capital structure.

9 To that 40.3, in this example, I added
10 back the 5.74, and that left me with approximately --
11 53.96 percent of the capital structure was unassigned. So
12 the next step in this calculation was I assigned all that
13 53.96 to long-term debt. So now we have -- at this stage
14 of the calculation, we have a common equity ratio of
15 40.3 percent, a preferred of 5.74 percent and a long-term
16 debt of 40 -- I'm sorry -- 53.96 percent.

17 Now, I also had to add back in the
18 short-term debt balance of Southern Union, which was
19 7.01 percent. So the way in which I did this was I said,
20 okay, let's say the entire amount of the capital structure
21 they have is actually \$1 in capital. So let's take \$7.01
22 away from that. So we have a short-term debt balance of
23 7.01 percent, and we had \$92.99 to distribute between
24 common equity, long-term debt and preferred stock.

25 What I did to calculate the numbers in this

1 example is you take 40.3 percent times \$92.99 and you get
2 37.47 percent. To get the preferred equity ratio, you
3 take 5.74 percent times the 92 -- the 92 -- the 92.99; you
4 get the 5.74. And then you multiply the long-term debt
5 that we had left, which was 53.96 times the 93.99 and you
6 get the 49.78 percent, and that's the way in which I
7 calculated it.

8 Q. Could you repeat that?

9 A. Sure.

10 Q. I'm just kidding.

11 A. No, I will.

12 Q. Don't. Don't repeat it. Don't repeat it.

13 A. Because it's an important step and I can
14 absolutely explain it again.

15 Q. On this hypothetical structure, you're
16 advocating that we should be using the actual consolidated
17 capital structure, correct?

18 A. I am advocating that. Mr. Dunn has
19 suggested that a hypothetical was appropriate. So what I
20 did was I provided the Commission with an appropriate
21 hypothetical.

22 Q. Okay. So you're giving us a second
23 alternative, but you're sticking to your guns on the first
24 consolidated capital structure, correct?

25 A. Correct.

1 Q. Okay. Now, in your opinion, are there --
2 is there ever an occasion where one should use a
3 hypothetical capital structure and not use an actual
4 consolidated or an actual capital structure? When should
5 you deviate from the actual numbers?

6 A. Honestly, sir, it is the Commission's
7 decision based on the ruling in '93. And their Order,
8 their ruling was that they believe that in a situation
9 where the consolidated capital structure is so out of line
10 with the rest of the industry, that's when you should use
11 a hypothetical.

12 Q. My question was, in your opinion, when
13 should a commission or an entity deviate from an actual
14 structure?

15 A. I believe that in the situation where the
16 capital -- I have to agree with the Commission decision
17 that whenever it's so out of line with the rest of the
18 industry, that it would be appropriate to use
19 hypothetical.

20 Q. Okay. So you would agree that if the
21 actual capital structure is so out of line from the
22 industry norms, that there should be a deviation to
23 some -- at that point you could deviate to the
24 hypothetical capital structure, correct?

25 A. I would say that's reasonable.

1 Q. Okay. Now, explain to me why an equity
2 level of only 26 percent on your proposal -- explain to me
3 why that -- or how that is not out of line with the other
4 comparables that are listed on Exhibit 32.

5 A. It is out of line, but in making my
6 recommendation, I had to weigh other factors, and the
7 factor that kept coming back was this is as a result of
8 management's decision to -- to strive for their aggressive
9 growth.

10 Q. So is this -- should the Commission look at
11 this as punishment?

12 A. No, not as punishment. If you -- if you
13 recommend, for example, when I was making my direct
14 testimony recommendation, if you recommend Mr. Dunn's
15 quasi-hypothetical capital structure that he produced,
16 you're, in essence, increasing the rate for Missouri
17 ratepayers.

18 Like I was trying to explain before, when
19 Southern Union invested this \$600 million worth of capital
20 in Panhandle, whether or not that -- that Panhandle
21 acquisition is profitable or not, there is a risk being
22 borne by the Missouri ratepayers, and that risk is the
23 possibility that that capital could be gone, that
24 something could happen to Panhandle and that capital would
25 be gone.

1 So that's money that could have been used
2 to pay down debt or to replace infrastructure that would
3 have benefited ratepayers. But if this Panhandle
4 transaction turns out to be a great success for Southern
5 Union, the benefits, the primary benefits don't go to
6 ratepayers; they go to shareholders through an equity --
7 through an increase in equity price.

8 Q. How low would the equity ratio have to be
9 before you said, well, that's too low and it's out of line
10 and it's not going to -- it's not going to allow the
11 company to obtain capital at a reasonable cost?

12 A. I think that it is -- it's not so simple as
13 saying a specific number. It is based on the specifics of
14 a case. I wholly believe, though, that this hypothetical
15 capital structure would produce just and reasonable rates,
16 or else I would not have recommended it or proposed it in
17 my rebuttal testimony. But I still think I just kept
18 coming back to the conclusion that this is management's
19 aggressive growth strategy that has produced this capital
20 structure.

21 This is the capital structure that, when an
22 investor goes -- an equity investor wants to invest in
23 Southern Union, this is the capital structure that they
24 are looking at. It's not the contrived capital structure
25 that Mr. Dunn has proposed, and it's not the hypothetical

1 capital structure.

2 Q. What's the difference between his
3 contrived, closed quote, capital structure and your,
4 quote -- what did you call it?

5 A. Hypothetical.

6 Q. Not contrived? No. It's hypothetical for
7 you?

8 A. Yes.

9 Q. But it's contrived for Mr. Dunn?

10 A. Yes, and I -- I probably shouldn't have
11 used that the word, and I apologize. It was
12 inappropriate.

13 Q. Well, basically aren't they both contrived
14 in some sense? I mean, basically they're both
15 hypothetical structures.

16 A. But the difference, sir, is this: The
17 difference is that Mr. Dunn, in his direct testimony, he
18 does not take out any of the equity. He simply took out
19 the debt of Panhandle, and then he tries to explain it
20 later in his rebuttal whenever -- whenever -- well, I
21 don't want to put words in his mouth, but he tries to
22 explain it later.

23 But in his direct testimony, his initial
24 filing, he simply said that he eliminated Panhandle, but
25 the only thing he did was take out the approximately

1 \$1.2 billion worth of Panhandle debt. That is why his
2 ratios are so high.

3 Q. I'm going to come back to that, what you
4 just said. Before I do that, though, were you in the room
5 when we were able to question Mr. Dunn yesterday?

6 A. Yes, I was.

7 Q. We were going through the Moody's report
8 and it stated that Southern Union was highly leveraged. I
9 think it was -- the language in the Moody's report said
10 that it was highly leveraged even before the Panhandle
11 Eastern acquisition. And I asked him what the common
12 equity ratio was prior to the Panhandle acquisition. He
13 said, oh, it was roughly 25, 26, 27 percent, very similar
14 to the way it is now.

15 If we were to assume that the transaction
16 ever occurred and that was the actual consolidated -- the
17 consolidated capital structure, then would you still argue
18 that they should be held to that low equity ratio when
19 there basically is no action that would have caused that?

20 A. I understand you're basing this on an
21 assumption, but I simply have a hard time believing that
22 the addition of the \$1.2 billion worth of debt did not
23 contribute to this capital structure ratio. As
24 Mr. Herschmann asked me earlier to -- what the capital
25 structure was before, I answered I don't know. I don't

1 know that offhand, prior to the Panhandle acquisition.

2 Q. Okay. Schedule JJG-2 -- and I'll try to

3 wrap this up and give the other Commissioners an

4 opportunity. I hate to be a time bandit.

5 On Schedule JJG-2 --

6 A. Yes.

7 Q. -- on the Southern Union stand-alone

8 numbers that are there listed in the column second from

9 the right.

10 A. Okay.

11 Q. Would you agree that the Panhandle debt has

12 been removed from that capital structure? Would that be

13 an appropriate method of removing the Panhandle Eastern

14 transaction?

15 A. Honestly, Mr. Clayton --

16 Q. No.

17 A. No. Honestly. I'm sorry. This is an

18 accounting GAAP issue for reporting.

19 Q. So is this an inappropriate schedule to be

20 comparing?

21 A. I believe it is. This is -- this is an

22 accounting issue.

23 Q. Okay. Okay. All right. Now, I want to

24 talk just very briefly about how long have you been with

25 the Office of the Public Counsel?

1 A. I have been here -- I believe I started the
2 second week of March.

3 Q. And I know this is -- you-all have gone
4 through this when we weren't in the room. What was
5 your -- what was your undergraduate education?

6 A. My degrees?

7 Q. Yes.

8 A. My degrees, as an undergraduate I graduated
9 with a degree in economics and finance with a
10 specialization in financial markets and institutions;
11 graduated magna cum laude.

12 Q. From?

13 A. From Southern Illinois University -
14 Edwardsville.

15 And my graduate studies, I graduated with a
16 master's degree in economics and finance with a
17 specialization in finance from Southern Illinois
18 University - Edwardsville.

19 Q. Okay. So you've got the undergraduate
20 finance and economics background, as well as a master's?

21 A. Correct.

22 Q. But this is your first finance-related job?

23 A. That's correct.

24 Q. Okay. Have you ever done any type of work
25 like this outside of an academic environment?

1 A. No.

2 Q. Tell me, if there are any, what books, what
3 texts, what mentors in finance you have looked to --

4 A. Okay.

5 Q. -- for your post-education education.

6 A. Prior to -- things I looked at prior to
7 filing direct testimony, sir?

8 Q. Yes.

9 A. I looked at the ValueLine Investment
10 Survey. I looked at C.A. Turner Utility Reports, Yahoo
11 Finance, the Ibbotson & Associates 2002 and 2003 Yearbook.
12 I also looked at the Principles of Corporate Finance
13 textbook.

14 Q. By whom?

15 A. It was authored by Stewart Myers and
16 Richard Brealey. Cost of Capital to a Public Utility, I
17 read that textbook authored by Myron Gordon, who is the
18 father of the DCF model. Also I looked at the Regulation
19 of Public Utilities, which was authored by Charles
20 Phillips.

21 Q. Is that one this right here (indicating)?

22 A. Mine's not red. Might be a different
23 edition.

24 Q. I got it. Go ahead.

25 A. The Fundamentals of Investment book was

1 written by William Gordon -- I'm sorry -- Gordon Alexander
2 and William Sharp and Jeffrey Bailey. I also looked at
3 the Investment Analysis and Portfolio Management book,
4 which was authored by Frank Reilly and Keith Brown.
5 Essentials of Corporate Finance textbook, which was
6 authored by Steven Ross, Wendell Westerfield and Bradford
7 Jordan. Also I looked at Cost of Capital, a
8 Practitioner's Guide, authored by David Parcells, or David
9 Parcell. I'm sorry.

10 I looked at Southern Union's 2003 annual
11 report. I looked at all the Data Request responses that
12 Southern Union had provided.

13 Q. Okay. I was looking more of academic.

14 A. Okay. I'm sorry.

15 Q. You did all that in three months?

16 A. A lot of those textbooks were textbooks I
17 used in my course work, and I reviewed them, yes.

18 Q. Okay. Okay.

19 A. Yes, I was working quite a bit.

20 COMMISSIONER CLAYTON: Thank you.

21 JUDGE WOODRUFF: Commissioner Davis?

22 COMMISSIONER DAVIS: No questions at this
23 time.

24 JUDGE WOODRUFF: Commissioner Appling?

25 QUESTIONS BY COMMISSIONER APPLING:

1 Q. Mr. Allen, I'm a country boy and I can't
2 wait to get out of here to get to the gym tonight.

3 A. We have something in common.

4 Q. I know. It's a little frustrating right
5 now.

6 But anyway, knowing what you know about
7 this case today and the information and the knowledge that
8 you had before you submitted your data on this case, is
9 there anything that you would do different, and if yes,
10 what would it be?

11 A. With this specific case? I think I would
12 probably exclude -- not exclude the Missouri-regulated
13 utilities, but as far as the overall impact on my
14 analysis, it really doesn't have a meaningful impact.
15 That's the only thing right now that I can think of that I
16 would change.

17 JUDGE APPLING: Thank you, sir. No further
18 questions.

19 JUDGE WOODRUFF: All right. I don't have
20 any questions.

21 Time for a break. Let's come back at 3:20
22 with redirect -- or excuse me -- recross.

23 (A BREAK WAS TAKEN.)

24 JUDGE WOODRUFF: Okay. We're back on the
25 Internet, and we're back on the record. When we finished,

1 we had just had questions from the Bench for Travis Allen,
2 so we'll begin with recross, beginning with Staff.

3 MR. BERLIN: No questions.

4 JUDGE WOODRUFF: Kansas City's not here.
5 Joplin's not here.

6 Federal Agencies?

7 MR. PAULSON: No questions.

8 JUDGE WOODRUFF: MGE?

9 RECROSS-EXAMINATION BY MR. HERSCHMANN:

10 Q. I'm just going to follow up on some of
11 Commissioner Clayton's and Appling's questions, which I
12 think were probably better than mine.

13 You responded to Commissioner Clayton that
14 when you were looking at a hypothetical capital structure,
15 you looked at a broad range of LDC businesses; is that
16 correct?

17 A. I looked at -- I wanted to get a broader
18 view, so I looked at either mine or Mr. Dunn's, and the
19 broader view, the broader range was Mr. Dunn's, so I used
20 his group.

21 Q. Wouldn't it be more appropriate to look at
22 the broad range of companies that you believe were
23 comparable to MGE?

24 A. Not when you're dealing with a hypothetical
25 capital structure. It's completely -- the idea is to get

1 a broader view. So Mr. Dunn's proxy group had
2 15 companies, mine had 8. So I chose his.

3 Q. And the calculations that you did in hand
4 on Exhibit 32, those are the ones that will reflect your
5 comparable group exclusive of short-term debt, right?

6 A. When Commissioner Clayton was asking me to
7 work on this, I wrote some more on this, but yes, the
8 original stuff that I wrote, correct.

9 Q. Just so the record is clear, on the exhibit
10 do you have down as common equity 40.30 percent, preferred
11 equity 5.74 percent and long-term debt at 53.96 percent,
12 and that would be excluding short-term debt, right?

13 A. That is correct. That is my hypothetical
14 capital structure with my proxy group, excluding
15 short-term debt.

16 MR. HERSCHMANN: Can I approach the witness
17 for a minute?

18 JUDGE WOODRUFF: You may.

19 BY MR. HERSCHMANN:

20 Q. So the record is clear, can you circle
21 those numbers in red so we have clear indication on the
22 exhibit.

23 A. Yes.

24 MR. HERSCHMANN: The court reporter just
25 informed me that the exhibit that he's actually been

1 writing on is his copy, if we can mark that as Exhibit 32A
2 and move that into evidence as well.

3 JUDGE WOODRUFF: What would be the purpose
4 of that?

5 MR. HERSCHMANN: It has the calculations
6 that he did.

7 JUDGE WOODRUFF: I thought you did those on
8 the original exhibit.

9 THE WITNESS: I thought we put that on the
10 record, but I'm not sure.

11 MR. HERSCHMANN: I was just informed by the
12 court reporter that it's not on the original, it's on the
13 copy of the exhibit.

14 JUDGE WOODRUFF: I'll ask the court
15 reporter, is that correct?

16 THE REPORTER: Yes.

17 JUDGE WOODRUFF: Does the counsel want to
18 see your -- I don't want to put anything into the record
19 that we thought was private notes. Was there anything on
20 there that you need to let your counsel look at?

21 THE WITNESS: I don't really think it's
22 legible or understandable, so --

23 MR. HERSCHMANN: Could we give the witness
24 the original 32, and if you can just write those numbers
25 again?

1 MR. MICHEEL: Your Honor, I think we've
2 already established that I'm not an expert in that anyway.

3 JUDGE WOODRUFF: All right. We'll give him
4 the original 32A, and he can write on it, original 32.

5 MR. HERSCHMANN: If you can just write that
6 down in red, please.

7 THE WITNESS: Sure.

8 Okay.

9 BY MR. HERSCHMANN:

10 Q. Now, in response to a question by
11 Commissioner Clayton, you said that you had to back in the
12 short-term debt. Do you remember responding to a question
13 when you did the calculations, you had to back into
14 short-term debt as it related to Exhibit 32?

15 A. That's correct.

16 Q. What -- well, withdrawn.

17 There is no requirement that you put back
18 in the short-term debt, because currently Southern Union
19 has no short-term debt, right?

20 A. Currently they have no short-term debt.

21 Q. There's no obligation to include it, you
22 just decided to include it back into your calculations,
23 right?

24 A. I decided based on the history of Southern
25 Union's level of short-term debt to put it back into the

1 calculation, correct.

2 Q. Do you know what Southern Union's future
3 plans are in relationship to short-term debt?

4 A. The company has sent -- responded to Data
5 Requests that I had sent out. As far as their plans --
6 let me see. I think I have it right here. Do you want me
7 to get it?

8 Q. Sure. Please.

9 A. I don't have those specific Data Request
10 responses with me.

11 Q. Do you recall whether the company was going
12 to maintain the level of short-term debt that you
13 attributed to it going forward or whether there was going
14 to be a reduction or elimination?

15 A. I can't say right now, because I recall
16 reading it, but I don't recall exactly what it said. And
17 I would prefer to have it in front of me.

18 Q. Let me just ask you, if it turns out that
19 the intention of the company response to the Data Request
20 reflects that there'll be either a reduction or
21 elimination in short-term debt, would that then change
22 what you said was the requirement that you put back in the
23 short-term debt in your calculations?

24 A. If the company is willing to testify under
25 oath that they do not plan to have short-term debt in

1 excess of 2 percent after construction work in progress is
2 taken out of 2 percent of their capital structure, the OPC
3 is willing to consider taking it out of the capital
4 structure, yes.

5 Q. What happens if it's 3 percent? I just
6 want to know, is that negative --

7 A. That would be -- you'd have to speak to my
8 attorney for that.

9 Q. Okay. And when you talked about outside
10 the zone of reasonableness in response to Commissioner
11 Clayton's questions, whether or not a company falls
12 outside the zone -- withdrawn.

13 The capital structure is determined by the
14 management of the company, right?

15 A. That is correct.

16 Q. And whether or not a company falls outside
17 the zone of reasonableness in your definition, that's
18 because of management decisions, right?

19 A. That is correct. They determine the
20 capital structure.

21 Q. And when the Supreme Court standards talked
22 about comparable companies and comparable risks, it is
23 your requirement under that standard to figure out what
24 are comparable companies and what are the comparable
25 risks, right?

1 A. Are you speaking of Hope and Bluefield?
2 Q. Yes.
3 A. Specifically -- just a second.
4 Q. Let me see -- I'll make it really simple.
5 In your response to Commissioner Clayton's questions, you
6 felt that those were truthful answers that complied with
7 the Supreme Court standards, right?
8 A. I don't mean to be difficult, but which
9 answer?
10 Q. Dealing with the zones of reasonableness.
11 A. Yes.
12 MR. HERSCHMANN: I have no further
13 questions.
14 JUDGE WOODRUFF: Thank you. Then redirect?
15 REDIRECT EXAMINATION BY MR. MICHEEL:
16 Q. Mr. Allen, do you recall that
17 Mr. Herschmann asked you some questions about the
18 Regulatory Research Associates?
19 A. Yes.
20 Q. And do you recall that you were forced to
21 answer that question in a yes or no basis?
22 A. Yes.
23 Q. And you indicated it was very hard for you
24 to answer yes or no?
25 A. Yes.

1 Q. Was there something that you wanted to add
2 to that response?

3 A. Yes, there was. While I think that that is
4 certainly something that the Commissioners -- what we were
5 talking about was the authorized returns that are reported
6 in a Regulatory Research Association publication. While I
7 believe that, you know, the Commission, that is something
8 they can certainly look at, that is not something that I
9 believe they should put a lot of weight to, because
10 there's an -- entirely a difference between the authorized
11 rate of return and the actual cost of capital.

12 There is a lot of reasons why the
13 authorized rate of return could be higher than the actual
14 cost of capital. One example in this case is MGE's asking
15 for a 25 percent boost for management efficiency. Now, so
16 that would -- that has nothing to do with the cost of
17 capital. So there are reasons why the authorized rate of
18 return is higher than the actual cost of capital, and that
19 should be taken into consideration.

20 MR. HERSCHMANN: I'm sorry. I'm just going
21 to object. I think maybe the witness misspoke. I think
22 he said 25 percent. I think he meant 25 basis points.

23 THE WITNESS: Yes. I'm sorry. I meant 25
24 basis points.

25 MR. MICHEEL: Thank you. I was going to

1 make that correction, too.

2 BY MR. MICHEEL:

3 Q. Do you recall Mr. Herschmann's questions
4 regarding whether a highly -- or a company that has higher
5 leverage than another company is more risky than another
6 company?

7 A. Yes.

8 Q. And again, do you recall you were forced to
9 answer that question with a yes or no?

10 A. Yes.

11 Q. And do you recall indicating that -- that a
12 highly leveraged company is riskier, everything else being
13 equal, and then you wanted to add something?

14 A. Correct.

15 Q. Would you please explain what you meant by
16 everything else equal?

17 A. In order to -- if you're specifically
18 looking at -- or let me start over.

19 If you want to think financial theory, what
20 you're going to read in the textbooks, every basic
21 fundamental textbook is going to say that if a company is
22 more highly leveraged, they are riskier than a less
23 leveraged company, all else equal.

24 And that's a very important phrase that you
25 have to keep in mind when reading these testimonies, all

1 else equal. A company can have a higher leverage ratio,
2 say Company A can have a higher ratio than Company B, but
3 that does not mean that Company A is riskier than
4 Company B.

5 The overall risk is the most important
6 thing to look at. That's what investors look at when they
7 invest. So to make a characterization that, just based on
8 the financial leverage that one company is riskier than
9 the other, that's incorrect.

10 Q. Do you recall questions from Mr. Herschmann
11 regarding the fact that if a company has higher leverage
12 than the average return 11 percent for the average
13 companies, that logic would dictate that a more risky
14 company should have a higher return on equity? Do you
15 recall those questions?

16 A. I'm sorry. Could you repeat that,
17 question?

18 Q. Do you recall Mr. Herschmann's questions
19 regarding that the RRI number is 11 percent return on
20 equity, and that doesn't logic dictate that the ROE should
21 be higher for a company that is more risky?

22 A. Yes.

23 Q. And I think you said there are other things
24 to consider?

25 A. Yes.

1 Q. And my question -- you weren't allowed to
2 answer that. My question is, what other things are there
3 that should be considered by this Commission?

4 A. The other things that should be considered
5 are what I have talked about before, and the most
6 important thing that I want to point out is that
7 Southern Union's investment into Panhandle, they invested
8 \$600 million worth of capital into Panhandle.

9 Now, whether or not Panhandle has problems
10 in -- cash flow problems or not, that \$600 million, that
11 does increase the risk to ratepayers. That's \$600 million
12 that could, as I said before, have been invested in the
13 infrastructure, been used to pay down debt, things that
14 are beneficial to ratepayers.

15 But the thing is by doing that, they
16 increase the risk to both shareholders and ratepayers, but
17 the primary beneficiaries of this Panhandle transaction
18 turns out to be a great success and a real profitable
19 entity to them, it goes to shareholders through a higher
20 equity price.

21 Now, if we adopt Mr. Dunn's capital
22 structure and his recommendation, not only are you saying
23 you're allowing MGE to increase the risk to Missouri
24 ratepayers without allowing them to share in the potential
25 benefits, but you're also increasing their rates on top of

1 that. To me that's just absolutely inappropriate and,
2 consequently, I just do not believe that Mr. Dunn's
3 analysis should be adopted by this Commission.

4 Q. You had some questions from Mr. Herschmann
5 regarding short-term debt and the appropriate levels, and
6 Mr. Herschmann asked you if there were any textbook
7 sources. Do you recall those questions?

8 A. Yes.

9 Q. Do you have any practitioner guide sources
10 that support your use of short-term debt?

11 A. Yes, I do.

12 Q. And what would that be?

13 A. That is the Cost of Capital, Practitioner's
14 Guide, written by David Parcell. And in this book he says
15 that two of the most common criteria used to determine
16 whether or not short-term debt should be included into the
17 capital structure is, one, what's the overall level
18 compared -- comparative to the capital structure? Two,
19 what has -- has this level of short-term debt been
20 consistent?

21 And in the case of Southern Union, my
22 opinion is that the overall level is significant. It's
23 78.01 percent, and it has been consistent. It has been
24 high, higher than construction work progress for the
25 last -- over the last year.

1 Q. And so does that lend support to your
2 belief?

3 A. Yes, I believe it does.

4 Q. You had some questions from Mr. Herschmann
5 regarding floatation costs and whether or not you've seen
6 from -- I think you responded that you saw something from
7 S&P that indicated that due to the leverage caused by the
8 Panhandle acquisition, that Southern Union Company was
9 going to be issuing equity. Do you recall those
10 questions?

11 A. Yes, I do.

12 Q. And do you have a copy of Mr. Dunn's
13 testimony with you, his rebuttal testimony?

14 A. Yes.

15 Q. Could you get it out and turn to page 14?

16 A. Okay.

17 Q. And I'm looking at the answer there
18 starting on line 4. Is that a statement in Mr. Dunn's
19 testimony from Standard & Poor's regarding Southern Union
20 Company's need to issue equity?

21 MR. HERSCHMANN: I'm sorry. Tell me where
22 you are again.

23 MR. MICHEEL: Page 14, the answer beginning
24 on line 4 of Mr. Dunn's rebuttal testimony, which is in
25 evidence as Exhibit 2.

1 THE WITNESS: To answer your question, yes,
2 it is.
3 BY MR. MICHEEL:
4 Q. And does that indicate that Southern Union
5 Company's going to be issuing equity?
6 A. Yes.
7 Q. As a result of its high leverage?
8 A. What it indicates to me is that as a result
9 of --
10 MR. HERSCHMANN: I'm going to object. The
11 document's in evidence. He's now interpreting what the
12 actual testimony says. He's looking at the testimony and
13 now we're going to interpret what it says.
14 MR. MICHEEL: It quotes the S&P. It has
15 the S&P quote in quotes, and Mr. Allen's response to
16 Mr. Herschmann was I read something from Standard & Poor's
17 that says that. And I'm trying to say, is this the item
18 that you've read from Standard & Poor's that says that.
19 And it's in quotes in Mr. Dunn's testimony.
20 JUDGE WOODRUFF: I think the question has
21 already been answered that this was the source of his
22 knowledge; is that fair to say? The objection is to his
23 interpreting of what that document means, and the document
24 is already in evidence.
25 THE WITNESS: There --

1 JUDGE WOODRUFF: I'm going to go ahead and
2 sustain the objection.
3 BY MR. MICHEEL:
4 Q. Have you seen any other documents through
5 discovery that indicate that?
6 A. Yes, I have.
7 Q. And what documents are those?
8 A. A Credit Lyonnais report.
9 Q. And what does that report indicate?
10 A. It indicates that Southern Union has an
11 extremely high leveraged capital structure, and that they
12 will have to -- they plan on issuing equity in order to --
13 to balance or draw down the debt percentage in their
14 capital structure, because it also indicates that they
15 have made several public statements that they're going to
16 do this.
17 MR. HERSCHMANN: I'm sorry. I didn't hear
18 the source.
19 THE WITNESS: Credit Lyonnais.
20 MR. MICHEEL: Credit Lyonnais.
21 MR. HERSCHMANN: I don't think Credit
22 Lyonnais was one of the major banking firms.
23 THE WITNESS: I'm sorry?
24 MR. MICHEEL: Is there an objection or --
25 MR. HERSCHMANN: I don't understand the

1 source.

2 BY MR. MICHEEL:

3 Q. Did you know that Credit Lyonnais is an
4 investment bank?

5 A. Yes.

6 Q. And that's a source that you got from
7 discovery from Southern Union?

8 A. Yes.

9 MR. MICHEEL: I have no further questions.

10 JUDGE WOODRUFF: All right. Thank you.
11 You may step down.

12 THE WITNESS: Those are the best words I've
13 heard all day.

14 (Witness excused.)

15 JUDGE WOODRUFF: I believe the next name on
16 the list then is Barbara Meisenheimer.

17 MR. MICHEEL: We would call Barbara
18 Meisenheimer. And, your Honor, with respect to
19 Ms. Meisenheimer, she has filed testimony on a large
20 number of issues. With respect to the rate of return, her
21 testimony is only in her rebuttal testimony at pages 2
22 through 9, so I don't know how you want to do this. I
23 don't know how you want to do schedules; I don't know how
24 you want to deal with admitting all of her testimony. She
25 has revenue requirement testimony, rate design testimony.

1 That's my question.

2 JUDGE WOODRUFF: Sure. Why don't you go
3 ahead and offer the document. At this point, I will defer
4 ruling on it until her testimony is complete later on in
5 the week.

6 MR. MICHEEL: So you want me to offer all
7 of her testimonies?

8 JUDGE WOODRUFF: Offer what she's going to
9 be cross-examined about for this one.

10 MR. MICHEEL: Okay. Just her rebuttal.
11 Okay.

12 MR. FRANSON: Your Honor, just before
13 Ms. Meisenheimer gets up, what is the plan? First of all,
14 I think the next name on the list is Mr. Murray; is that
15 correct?

16 JUDGE WOODRUFF: It's Mr. Tuck.

17 MR. FRANSON: Tomorrow morning at 8:30?

18 JUDGE WOODRUFF: Tomorrow morning at 8:30.

19 MR. FRANSON: My question is, are we going
20 to finish today after Ms. Meisenheimer's testimony?

21 JUDGE WOODRUFF: That is my intent, yes.

22 (Witness sworn.)

23 JUDGE WOODRUFF: Thank you. You may be
24 seated. You may inquire.

25 BARBARA MEISENHEIMER testified as follows:

1 DIRECT EXAMINATION BY MR. MICHEEL:

2 Q. Would you state your name.

3 A. My name is Barbara Meisenheimer.

4 Q. And how are you employed, Ms. Meisenheimer?

5 A. I'm a chief utility economist with the

6 Office of the Public Counsel.

7 Q. And have you caused to be filed in this

8 case your rebuttal testimony that's been marked for

9 purposes of identification as Exhibit 209?

10 A. Yes, I have.

11 Q. And is the issue relating to the cost of

12 capital contained in your rebuttal testimony roughly at

13 pages 2 through 9 with certain schedules, 2 through 10

14 with certain schedules. Excuse me.

15 A. I get 2 through 9 with two schedules and

16 the schedules are Schedule 1 and Schedule 2.

17 Q. And do you have any corrections that you

18 would like to make to that portion of your testimony or to

19 those schedules?

20 A. Yes, I do. I have two corrections to

21 Schedule No. 1.

22 Q. And what are those?

23 A. About three-quarters of the way down the

24 page on the left side, where I am providing descriptions

25 and names, there is a line which reads, the standard

1 deviation a non-scaled measure of disbursement about the
2 mean. I'd like to change that to "dispersion."
3 Q. Could you spell dispersion?
4 A. D-i-s-p-e-r-s-i-o-n.
5 And in the next subsection where it begins,
6 Mr. Dunn calculates coefficient of variation, in the one,
7 two, three, fourth line, there is a misspelling of
8 dispersion that I would like to correct for.
9 Q. And that's just changing the U and the I?
10 A. The E.
11 Q. Or the E. I'm sorry. Are there any other
12 corrections?
13 A. No, sir.
14 Q. With that, if I asked you the questions
15 regarding this issue and on those schedules today, would
16 your answers be the same or similar?
17 A. Yes, they would.
18 MR. MICHEEL: I would move the admission,
19 your Honor, of that portion of the testimony and tender
20 Ms. Meisenheimer for cross.
21 JUDGE WOODRUFF: All right. You've offered
22 a portion of the testimony. I'm not going to rule on it
23 until all her testimony can be offered, so we'll go ahead
24 and tender her for cross, then.
25 And for cross-examination, we can begin

1 with Staff.

2 MR. BERLIN: Your Honor, Staff has no
3 questions.

4 JUDGE WOODRUFF: Kansas City's not here and
5 Joplin's not here.

6 Federal Agencies?

7 MR. PAULSON: No questions, sir.

8 JUDGE WOODRUFF: Jackson County and Midwest
9 Gas are not here.

10 MGE?

11 MR. HERSCHMANN: I have no questions.

12 JUDGE WOODRUFF: Then we'll come up for
13 questions from the Bench. Commissioner Clayton, do you
14 have any questions?

15 QUESTIONS BY COMMISSIONER CLAYTON:

16 Q. Ms. Meisenheimer, would you just give us on
17 this issue -- your testimony on this issue basically
18 relates to some statistical analysis associated with -- is
19 it risk? Would you just summarize your testimony for us?

20 A. The testimony I've provided in this section
21 of the case is very limited. It is specifically to
22 address a statistical analysis that Mr. John Dunn claimed
23 supported some kind of adder to the rate of return to
24 reflect that MGE is riskier than the group of companies
25 that he selected for his comparable group.

1 And specifically I'm here to talk about why
2 the statistical analysis that he developed is not
3 appropriate for use? If you wanted me to go into a brief
4 description, I would, or I can wait for another question.

5 Q. No. That's all right. Why don't you go
6 ahead and describe it for us. You came all the way up
7 here. Just give us a general overview of your critical
8 analysis of Mr. Dunn's use of statistics.

9 A. I think that I can sum it up pretty quickly
10 if I can direct you to Schedule 2 of my testimony.

11 Q. Rebuttal or surrebuttal?

12 A. Only in my rebuttal is the place where I
13 address Mr. Dunn's testimony.

14 Q. Go ahead.

15 A. The various groups of lines that are in
16 horizontal lines, okay, those represent five years of data
17 regarding the return for the various companies in the
18 sample group that he selects. The thing that I would have
19 you observe about that data, No. 1, is if you look at
20 those five data points for each company, you might get a
21 feel for how much variation is there. In other words,
22 what is the -- the horizontal distance within which those
23 points vary.

24 So I tried to show that to you down here
25 with this arrow, and also with this one (indicating),

1 because I wanted to be fair about it. No. 1, I wanted to
2 show you when there -- where there's a lot of variation
3 and one where there's less variation. So that's their
4 mo-- that's their -- where those points fall out, you
5 could consider where would the mean be of those five
6 sample points, and how much does each of those sample
7 points vary?

8 That is, in some manner you can think of
9 that as the potential risk that they're not going to get
10 the mean value. Instead they're going to get, you know,
11 something around the mean of those values, something
12 besides the mean. That, in a sense, is measured risk.
13 Okay. So what I tried to do is show you how Mr. Dunn's
14 calculation homog-- calculations homogenize the data from
15 all these companies into something that I would call --
16 honestly I would call it misleading, in terms of the
17 results.

18 And if you will look right up at the top, I
19 have a little bracket that says "Mr. Dunn's calculated" --
20 oh -- "calculation averages away the normal variation
21 exhibited by companies." These -- that little group of
22 points is what he derives from his method of averaging all
23 of these, which are much more dispersed.

24 So in other words, if you say that the
25 difference between the mean of a group and how much the

1 various points could get away from that mean, here they
2 can't get away from it hardly at all. They're packed up
3 really tight together. So that's going to indicate that
4 this group, the way he derived it through the mathematical
5 calculations of averaging, ends up averaging away the real
6 variation that you can see actually occurs between all the
7 companies in the sample group.

8 My job isn't -- I'm not here to tell you
9 what is the right sample group to pick. That's why we
10 brought you Mr. Allen's testimony. That's why we'll bring
11 you Mr. Tuck's testimony. I'm here for a very limited
12 purpose, and that is only to tell you that the statistical
13 analysis that he claims justifies a higher rate of return,
14 it does not make sense to me.

15 And I show you in another schedule, another
16 way to get to the same conclusion, and that is, I show you
17 how it -- how he did his calculations. Okay. He didn't
18 look at the individual companies and say, how good is this
19 company -- how good is MGE or how is MGE doing compared to
20 each of the particular other companies?

21 Instead, he takes the data, averages it
22 within the year, which in my opinion I don't find any
23 meaningful reason to do that from a statistical
24 perspective, then uses the averaged amounts to come up
25 with a measure of variation to compare to MGE. So he's

1 comparing apples to oranges, in my opinion.

2 COMMISSIONER CLAYTON: Thank you.

3 JUDGE WOODRUFF: Commissioner Appling?

4 COMMISSIONER APPLING: I didn't do well

5 when I took my statistics class, so I'm going to pass on

6 any questions. You'll probably confuse me more than I am

7 already. No questions.

8 THE WITNESS: Welcome, Commissioner.

9 COMMISSIONER APPLING: Thank you.

10 JUDGE WOODRUFF: Recross beginning with

11 Staff.

12 MR. BERLIN: Staff has no recross

13 questions, your Honor.

14 JUDGE WOODRUFF: Okay. KC and Joplin

15 aren't here.

16 Federal Agencies?

17 MR. PAULSON: No questions.

18 JUDGE WOODRUFF: MGE?

19 RECROSS-EXAMINATION BY MR. HERSCHMANN:

20 Q. I really thought I was getting out of here

21 without a question. Just to follow up on Commissioner

22 Clayton's question, you're not claiming that Mr. Allen's

23 testimony regarding Southern Union being outside the zone

24 of reasonableness is false, are you?

25 A. I don't think that I'm familiar enough with

1 that section of the testimony to comment. I'm here for a
2 very limited purpose to look at the impact of historic
3 returns over a five-year period as one little component of
4 all of the issues that Mr. Allen testified. So I don't
5 think I can answer that.

6 Q. You're not in any way addressing his expert
7 opinion as it were dealing with zone of reasonableness,
8 right?

9 A. I'm -- I'm not sure that I'm familiar
10 enough with what all is encompassed in his zone of
11 reasonableness to comment on whether what I say touches on
12 that or not.

13 Q. In your prepared testimony, you weren't
14 addressing anything as related to Mr. Allen's analysis and
15 calculations of zone of reasonableness, right?

16 A. I didn't review Mr. Allen's calculations on
17 reasonableness.

18 MR. HERSCHMANN: I have nothing further.

19 JUDGE WOODRUFF: Redirect?

20 REDIRECT EXAMINATION BY MR. MICHEEL:

21 Q. I just have a couple, because I want to
22 clear this up. The analysis that you did,
23 Ms. Meisenheimer, it does not relate to the capital
24 structure issue; it relates to the return on equity issue.
25 Is that your understanding?

1 A. That's correct.

2 Q. And so this is about an adjustment that

3 Mr. Dunn proposes, because he claims that MGE is

4 statistically more risky than his comparable companies; is

5 that your understanding?

6 MR. HERSCHMANN: Objection, leading.

7 JUDGE WOODRUFF: It is leading, but I'm

8 going to allow it anyway. Overruled.

9 THE WITNESS: That is my understanding.

10 BY MR. MICHEEL:

11 Q. And it has nothing to do with capital

12 structure; it's all about the return on equity?

13 A. My testimony is about the return on equity

14 and one limited portion of it.

15 MR. MICHEEL: That's all I have, your

16 Honor.

17 JUDGE WOODRUFF: Thank you.

18 Ms. Meisenheimer, you can step down.

19 (Witness excused.)

20 JUDGE WOODRUFF: With that, then, I believe

21 that's all the testimony we'll hear today. We'll start

22 tomorrow morning with Mr. Tuck.

23 Anything else anyone wants to bring up

24 while we're still on the record?

25 (No response.)

1 JUDGE WOODRUFF: All right. Have a good
2 evening.

3 WHEREUPON, the hearing of this case was
4 recessed until June 23, 2004.

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