Exhibit No.:	
Issue:	Rate Base Revenue and Expense Cost of Capital Accounting System Depreciation Purchased Gas Adjust-ment Clause
Witness:	Kidd
Exhibit:	Direct Testimony
Sponsoring Party:	Associated Natural Gas
Case No.:	GR-97-272

ASSOCIATED NATURAL GAS
A DIVISION OF ARKANSAS WESTERN GAS COMPANY

CASE NO. GR-97-272

DIRECT TESTIMONY

OF

MARK S. KIDD
SUPERVISOR, RATE ANALYSIS
ARKANSAS WESTERN GAS COMPANY

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ASSOCIATED NATURAL GAS
DIVISION OF ARKANSAS WESTERN GAS COMPANY
CASE NO. GR-97-272
PREPARED TESTIMONY OF MARK S. KIDD

Q. Please state your name, employer, business address, and position.

A. My name is Mark S. Kidd. I am employed in the position of Supervisor, Rate Analysis in the Rates and Regulation Department of Arkansas Western Gas Company at 1083 Sain Street, Fayetteville, Arkansas 72703.

Q. Please describe your educational background and work experience.

A. I am a graduate of the University of Arkansas at Little Rock where I earned a Bachelor of Science degree in accounting (1978) and a Master of Science degree in accountancy (1985). I am a certified public accountant, licensed to practice in Arkansas since 1980. Joining Baird, Kurtz and Dobson, CPAs in 1978 as a staff accountant, I performed audit, tax, and accounting services for a wide range of clients. From 1980 to 1991 I was employed by Arkansas Power & Light Company in the Accounting Department in the positions of accountant in the General Accounting section (1980 - 1981), accounting supervisor in the Property Accounting section (1981 - 1988), and accounting supervisor in the Regulatory Accounting and Taxes section (1988 - 1991). In 1991 I left Arkansas Power & Light Company to assume my present position with Arkansas Western Gas Company. During my career I have attended various training courses, including the SGA Intermediate Ratemaking Course and the EEI Basic Tax School. Also, I represented Arkansas Power & Light Company as a member of the

EEI Depreciation Accounting Committee.

Q. What is the purpose of your testimony today?

A. On January 14, 1997, Associated Natural Gas (Associated or ANG) filed schedules with the Missouri Public Service Commission (MPSC or Commission) reflecting a $3,758,936 increase in revenues. The MPSC ordered ANG on January 28, 1997, to file its prepared direct testimony and minimum filing requirements on or before February 18, 1997 (subsequently changed to February 28, 1997). I will describe schedules contained in the following sections of ANG's filed accounting schedules: Section B - Rate Base Schedules; Section C - Income Statement Schedules; Section D - Cost of Capital Schedules; Section E - Account Codes, Standard Journal Entries, and Trial Balance; and Section F - Depreciation Information Schedules. In my testimony I will also address proposed changes to the purchased gas adjustment clause.

Q. Some of the schedules in Section C and all of the schedules in Section D present total company amounts for Arkansas Western Gas Company (Company). Please explain.

A. As a division of Arkansas Western Gas Company, it is not practical for Associated to maintain a representative capital structure. As is addressed in the testimony of Pauline Ahern and Frank Hanley, Arkansas Western Gas Company does maintain its debt and equity in proportions which are consistent with other local distribution companies. Consequently, ANG's cost of capital is determined by reference to the elements of the Company's capital structure. Schedules prepared for the Company are C-9, C-10, and all schedules in Section D.

Q. What is the test year used to calculate the rate increase proposed in Associated's tariff schedules filed on January 14, 1997?

A. Associated used the twelve month period ending July 31, 1996, as its test year and included adjustments for known and measurable changes during the succeeding twelve months ending July 31, 1997, to determine adjusted test year amounts.

Q. In the Suspension Order and Notice dated January 28, 1997, the Commission ordered ANG to include its recommendation for a proper test year in this case in its filing of testimony and exhibits. Has this been addressed?

A. Yes. In his testimony, Ricky Gunter addresses the test year recommendation in this case.

Rate Base Schedules (Section B)

Q. Please describe Schedule B-1.

A. Schedule B-1, Derivation of ANG Division Adjusted Test Year Rate Base, sets forth the rate base amounts per the financial statements as of July 31, 1996, pro forma adjustments, and the resulting adjusted test year amounts. Schedules which provide detail support for the amounts listed on Schedule B-1 are referenced as supporting schedules. For jurisdictional allocations, these details (from Schedule B-4, B-10, and F-1) are carried to Schedules G-2 and G-2-1. Schedule G-2 also lists amounts allocated from the AWG Division (AWG) in addition to the amounts listed for the ANG Division.

Q. Please describe Schedules B-2 and B-2-1.

A. Schedule B-2, Adjustments to Test Year Rate Base - Summary, lists the effect on the elements of rate base listed on Schedule B-1 for each adjustment and in total, thus providing support for column (3) of that schedule. These adjustments are set forth in greater detail in Schedule B-2-1, Adjustments to Test Year Rate Base - Detail, which lists the following for each adjustment: (1) description of the overall adjustment, (2) rate base element(s) affected, (3) a description of the adjustment for each line, (4) references, and (5) the amount of the adjustment. I will address each adjustment in the section on rate base adjustments immediately following this section.

Q. Please describe Schedule B-4.

A. Schedule B-4, Calculation of Working Capital Assets, documents ANG's working capital requirements, which were developed by (1) utilizing a thirteen month average of certain account balances (e.g., gas storage inventory) adjusted where necessary to properly state the adjusted test year balance and (2) adding the cash working capital requirement.

Q. Please explain what the working capital assets represent.

A. Working capital assets are investments other than plant that ANG must make to serve its customers. For example, ANG must maintain materials and supplies inventories and gas in storage in order to be able to serve the demands of its customers. These types of investments are represented by thirteen month averages for the test year ending July 31, 1996. ANG also makes investments which are referred to as the cash working capital requirement. These investments arise from the provision of service in advance of payment. Specifically, ANG must make expenditures to provide service in advance of the collections it receives from its customers.

Q. Please explain how ANG determined the cash working capital requirement.

A. The calculation of the cash working capital requirement is set forth on Schedule B-4-A.

For each district, we have applied the 45 day formula to operation and maintenance expenses other than gas expense and calculated a requirement of seven days of gas expense.

Q. What is the rationale for the number of days used to determine the cash working capital requirement?

A. The 45 day formula - which was the accepted cash working capital methodology in Missouri prior to adoption of lead-lag studies - as applied to the non-gas operation and maintenance expenses is used because ANG believes that it provides a sufficient cash working capital requirement without undergoing the expense and effort of preparing a lead-lag study. For gas expense, ANG has estimated that collections for a service period are made 22 days after the end of the period and payments for gas are made approximately 15 days after the end of the period, which indicates an investment equal to seven days of gas expense.

Q. Please describe Schedule B-4-1.

A. ANG has deferred as a regulatory asset the incremental post-employment benefits other than pensions (OPEB) amounts since adoption of SFAS 106, effective January 1, 1993. Schedule B-4-1 sets forth the recoverable portion of the regulatory asset pertaining to

SFAS 106, projected as of July 31, 1997. This is consistent with cases such as EO-93-35 in which the Commission (1) authorized deferral of amounts in excess of pay-as-you-go, (2) stated its intent to allow prudently incurred OPEB costs on a pay-as-you-go basis, and (3) indicated that it is probable that capitalized OPEB costs would be recovered in rates. My testimony concerning adjustment IS-15 below discusses the amounts included in expense relative to SFAS 106.

Q. Please describe Schedule B-5.

A. Schedule B-5, Average Working Capital Asset Account Balances, lists the thirteen monthly balances of working capital assets for the test year ended July 31, 1996, as well as the average of these thirteen balances. The amounts as of July 31, 1996, and the averages of the thirteen monthly balances ending on July 31, 1996, are reflected on Schedule B-4, where the determination of the adjusted test year balances is documented.

Q. Please describe Schedule B-8.

A. Schedule B-8 lists the amount of Construction Work In Progress (CWIP) as of July 31, 1996, in total and with a breakdown of the portion includable in rate base. Also listed are the expenditures for the year ended July 31, 1997, on projects expected to be completed by July 31, 1997. These amounts are included in the rate base adjustments set forth in adjustments RB-1 and RB-2.

Q. Please describe Schedule B-9.

A. Schedule B-9, Schedule of Retirement Work in Progress (RWIP), provides an analysis of the $9,780 balance of RWIP as of July 31, 1996. Of this balance, $9,656 is properly classified as RWIP, and thus includable in the balance of accumulated depreciation (adjustment RB-4).

Q. Please describe Schedule B-10.

A. Schedule B-10 sets forth the net acquisition adjustment pertaining to the acquisition of ANG by Arkansas Western Gas Company effective June 1, 1988. As of July 31, 1996, the acquisition adjustment balance was $5,716,574 and the related accumulated amortization was $2,268,617, resulting in a net acquisition adjustment of $3,447,957. Company witness Ricky Gunter discusses the acquisition adjustment in detail in his testimony.

<u>Rate Base Adjustments (Schedule B-2-1)</u>

Q. Please describe adjustment RB-1.

A. CWIP as of July 31, 1996, amounting to $352,745 is expected to be completed by July 31, 1997, and transferred to gross utility plant in service (GUPIS). The CWIP balance also includes ($806) which will transfer to other accounts. Therefore, adjustment RB-1 reduces CWIP for the $351,939 balance at July 31, 1996, and increases GUPIS by $352,745.

Q. Please describe adjustment RB-2.

A. Based on budgeted capital additions for 1996 and 1997, projected construction expenditures for the adjusted test year are $3,338,225. These expenditures less the projected CWIP balance at the end of the adjusted test year of $280,200 yield an addition to GUPIS of $3,058,025, which is the amount of adjustment RB-2.

Q. Please describe adjustment RB-3.

A. Adjustment RB-3 includes (1) an unrecorded retirement of LNG property that had occurred before the end of the test year, (2) reversal of retirements recorded in error, and (3) several transfers. Although the transfers are between accounts and districts and have a total division effect of zero, they are referenced here for audit trail purposes.

Q. Please describe adjustment RB-4.

A. This adjustment, which reduces accumulated depreciation by $9,656, is described in the discussion of Schedule B-9 above.

Q. Please describe adjustment RB-5.

A. Accumulated depreciation as of July 31, 1996, includes several items not properly includable in accumulated depreciation. Adjustment RB-5 eliminates these items, thus increasing accumulated depreciation by $10,205.

Q. Please describe adjustment RB-6.

A. As mentioned above, ANG's test year is the year ending July 31, 1996, adjusted for known and measurable events during the year ending July 31, 1997. Since ANG has adopted an adjusted test year that extends past the end of the historical test year, it has recognized that during the adjusted test year depreciation of plant in service will continue to accrue, thereby causing a reduction of rate base. The accrual, consisting of two parts, has been calculated using current depreciation rates: (1) a full year accrual on plant in service as of July 31, 1996, and (2) a half year accrual on the net additions for the year ending July 31, 1997. This second part assumes that plant activity will occur evenly throughout the adjusted test year. Use of current depreciation rates is consistent with the tariff rates applicable to customer bills during the adjusted test year because these rates are based on a cost of service using the current depreciation rates.

Q. Please describe adjustment RB-7.

A. Adjustment RB-7 adjusts working capital assets as of July 31, 1996, to the average of the thirteen monthly balances of each item or other representative balance and adds an allowance for the cash working capital requirement. This adjustment increases the $5,529,454 balance at July 31, 1996, by $1,830,092, thus producing an adjusted test year balance of $7,359,546. Working capital assets are discussed in detail in regard to Schedules B-4, B-4-A, B-4-1, and B-5.

Q. Please describe adjustment RB-8.

A. Retirements of plant in service during the adjusted test year are projected to be $594,900. Accordingly, adjustment RB-8 records reductions to GUPIS and accumulated depreciation in the amount of $594,900.

Income Statement Schedules (Section C)

Q. Please describe Schedule C-1.

A. Schedule C-1, Test Year and Pro Forma Statement of Utility Operating Income and Income Statement, lists by account the revenue and expense amounts for the test year, pro forma adjustments, and adjusted test year The adjusted test year amounts per this schedule are carried forward to Schedule G-3, where the jurisdictional allocations of both ANG and AWG amounts are set forth.

Q. Please describe Schedule C-2.

A. Schedule C-2, Adjustments to Test Year Statement of Utility Operating Income and Income Statement - Summary, sets forth each pro forma adjustment affecting revenues and expenses. On this schedule each adjustment is described and the amount of the increase or decrease is listed. The last line of each adjustment states the effect of the adjustment on net income before income taxes. Each adjustment will be addressed in the section on income statement adjustments, which immediately follows this section.

Q. Please describe Schedule C-2-1.

A. Schedule C-2-1, Adjustments to Test Year Statement of Utility Operating Income and Income Statement - Detail by Adjustment, lists the detail entries for each adjustment set forth on Schedule C-2 in order of adjustment. The amount of each entry is listed in column (4) and the effect on net income before income taxes is shown in column

(5). It is necessary to show the effect on net income before income taxes because increases to both revenues and expenses are shown as positive amounts in column (4). The effect on net income before income taxes is totaled for all adjustments on page 4.

Q. Please describe Schedule C-2-2.

A. Schedule C-2-2, Adjustments to Test Year Statement of Utility Operating Income and Income Statement - Detail by Account, lists the same detailed entries from Schedule C-2-1 in account order. Column (5) displays the total amount posted by account to Schedule C-1. Therefore, any adjustment amount from C-1 can be traced to Schedule C-2-2 to determine the adjustment(s) comprising the total. As already mentioned, Schedule C-2 describes the adjustment and provides high level effects and Schedule C-2-1 provides the supporting details of each entry by account.

Q. Please describe Schedule C-4.

A. Schedule C-4 sets forth the percentage of uncollectible accounts by operating district (Arkansas, SEMO (i.e., Southeast Missouri), Kirksville, and Butler). The uncollectible percentage is based on the net write-offs and operating revenues for the five years ending July 31, 1996. The resulting percentages by operating district are included in the revenue conversion factor calculations on Schedule C-5.

Q. Please describe Schedule C-5.

A. Schedule C-5 sets forth the revenue conversion factors by operating district based upon the applicable corporate tax rates and the percentage of uncollectible accounts as set forth on Schedule C-4. The revenue conversion factor for each Missouri district is applied on Schedule D-1-a to determine the pre-tax weighted equity cost rates.

Q. Please describe Schedule C-6.

A. Schedule C-6 sets forth the required disclosure of all test year expenditures included in operating expense in support of or for membership in, social, recreational, fraternal, religious clubs or organizations, Chambers of Commerce, and civic associations. In order to limit the issues in this case, ANG has chosen to eliminate these amounts despite its belief that such amounts represent necessary business expenses (adjustment IS-14).

Q. Please describe Schedule C-7.

A. Schedule C-7 discloses all test year advertising expenditures included in operating expense. Expense in the amount of $5,569, classified as promotional, has been eliminated (adjustment IS-16).

Q. Please describe Schedule C-8.

A. Schedule C-8 provides an analysis of account 408.1, taxes other than income taxes, for the test year and adjusted test year. The adjustments of FICA, FUTA, and SUTA are discussed in the section immediately following in the discussion of adjustment IS-1. Property taxes are addressed in the discussion of adjustment IS-4.

Q. Please describe Schedule C-9.

A. Schedule C-9, Investment Tax Credits, sets forth the test year and adjusted test year amounts for ITC amortization and accumulated deferred ITC for Arkansas Western Gas Company. This information is provided for the Company, even though the ANG Division does not carry investment tax credits on its books, since the Company's capital structure is used in the determination of ANG's weighted cost of capital (see Schedule D-1-a).

Q. Please describe Schedule C-10.

A. Schedule C-10 is a schedule of accumulated deferred income taxes for the test year and adjusted test year for the Company. This has been prepared on a total company basis as support for Schedule D-1-a. The test year balance has been adjusted for projected increases during the adjusted test year.

Q. Please describe Schedule C-10-1.

A. Schedule C-10-1 calculates the adjustment to accumulated deferred income taxes consistent with adjustment RB-6, which records the depreciation accrual for the adjusted test year.

Q. Please describe Schedules C-11 and C-12.

A. Schedules C-11 and C-12 set forth the calculation of current and deferred income tax expense, respectively, for the test year and adjusted test year. The income tax expense amounts on these schedules are for the ANG Division before the inclusion of allocations from the AWG Division and the effect of jurisdictional allocations as set out on Schedule G-3.

Income Statement Adjustments (Schedule C-2)

Q. Please describe adjustment IS-1.

A. Adjustment IS-1 records the adjustment of payroll expense, payroll taxes, and other related costs, for known and measurable changes for the adjusted test year ended July 31, 1997. The types of changes include staffing levels, pay levels, overtime levels, step progressions, general salary increases, payroll tax base and rate changes, and changes in other payroll related costs. The adjustment comprehends the pro forma level of ANG's payroll and the allocation of payroll from Southwestern Energy Company (SWN) and the Arkansas Western Gas Division. Adjustment IS-1 increases operating expenses by $763,320.

Q. Please describe adjustment IS-2.

A. Southwestern Energy Company and AWG perform functions for the benefit of ANG that are recorded as general and administrative expenses and allocated monthly to ANG through the intercompany allocation process. The intercompany allocation process utilizes factors which remain in effect for a calendar year unless a revision is necessary. For the test year, allocations have been recorded using factors in effect for 1995 and 1996. Pro forma allocation factors have been developed based upon the 1996 factors with several revisions. Therefore, adjustment IS-2 adjusts ANG's portion of the intercompany allocation of the allocable test year expenses of SWN and AWG to the level calculated by applying pro forma allocation factors. Adjustments affecting allocable expenses of AWG or SWN, such as IS-1, have been determined by applying the change in allocable expenses to the pro forma allocation factors, recognizing that ANG's test year intercompany allocations have been adjusted to the pro forma level via this adjustment. Adjustment IS-2 increases operating expenses by $25,183.

Q. Please describe adjustment IS-3.

A. Adjustment IS-3 increases depreciation and amortization expense by $538,414 to reflect the adjusted test year level of depreciation expense, determined by application of proposed rates (Schedule F-8) to adjusted test year plant balances as set forth on Schedule F-1. My testimony will cover these schedules in a section following.

Q. Please describe adjustment IS-4.

A. Adjustment IS-4 decreases property tax expense by $20,158 to produce an expense level based on the adjusted test year balance of plant and the most recent assessment and rate of tax on assessed values available.

Q. Please describe adjustment IS-5.

A. Adjustment IS-5 eliminates $80 from revenue, records reclassification of amounts among operating expense accounts (zero net effect on operating expenses), and reclassifies amortization of the acquisition adjustment from account 4250 to account 4060 (increasing operating expenses and reducing other deductions by $279,564). As discussed in Ricky Gunter's testimony, ANG proposes to recover an appropriate return on and return of its Missouri jurisdictional investment in the net acquisition adjustment.

Q. Please describe adjustment IS-6.

A. Adjustment IS-6 increases revenues by $2,369,561 and operating expenses by $2,508,170 to adjusted test year levels that reflect adjustments for weather, customer growth, and pro forma gas expense. The testimony of Donna Campbell addresses the calculation of the adjusted test year levels. However, I address here two aspects of this adjustment. First, part of the adjustment reclassifies the $17,764 test year cost of company use gas from various operating expense accounts to gas expense. Second, the basis for the per unit rates applied to determine pro forma gas expense was determined as follows: (1) annualized gas costs were determined for each district based upon current contract terms and tariff rates; (2) allocations to firm and interruptible classifications were made in accordance with the proposed purchased gas adjustment tariff for Arkansas and the purchased gas adjustment tariff in effect for ANG's Missouri districts; and (3) the class (i.e., firm and interruptible) gas costs were divided by class Ccf sales to determine unit rates, which were then applied by Ms. Campbell to determine adjusted test year gas expense.

Q. Please describe adjustment IS-7.

A. Adjustment IS-7 increases operating expenses by $20,227 and reduces other income by $10,904 to properly state the test year appliance program expenses. Specifically, these entries eliminate the out of period portion of charges made to recognize appliance program expenses and recognize previously unrecorded direct payroll employee benefit expense.

Q. Please describe adjustment IS-8.

A. For the test year, no allocation was made to ANG for costs pertaining to the SWN building and fixtures. Therefore, adjustment IS-8 records operating expenses in the amount of $37,006.

Q. Please describe adjustment IS-9.

A. ANG expects to incur expenses to support its rate increase applications in Arkansas and Missouri. The estimated costs for consultants, attending hearings, supplies, overnight shipping, and MPSC staff audit expense amount to $150,560. Adjustment IS-9 records a $50,187 increase in operating expenses to recognize three year amortization of these rate case expenses. I have supplied details of the rate case expense to Company witness Donna Campbell to support the jurisdictional assignments.

Q. Please describe adjustment IS-10.

A. Adjustment IS-10 records the adjustment of income tax expense as set forth on Schedules C-11 and C-12 which are discussed above.

Q. Please describe adjustment IS-11.

A. Adjustment IS-11 adjusts interest expense to the level determined by applying the weighted cost of debt per Schedule D-1-a to the ANG rate base set forth on Schedule B-1 (3.39% × $45,113,661 = $1,529,353). This amount of interest expense is reflected in the calculation of income tax expense for the adjusted test year on Schedule C-11.

Q. Please describe adjustment IS-12.

A. Effective July 1, 1996, ANG switched from card billing to envelope billing. Therefore, the test year expense does not fully reflect the cost of envelope billing, and accordingly, adjustment IS-12 increases operating expenses by $94,009.

Q. Please describe adjustment IS-13.

A. While 4 CSR 240-40.050 requires a depreciation study at least every five years, APSC Order No. 15 in Docket No. 90-004-U requires ANG to file a depreciation study every three years. Therefore, ANG anticipates incurring this cost every three years, and accordingly, adjustment IS-13 records annual expense based upon three year amortization of estimated depreciation study costs.

Q. Please describe adjustment IS-14.

A. Adjustment IS-14 records a $11,726 reduction of operating expenses pertaining to amounts in support of certain organizations (e.g., civic, social, and charitable). This adjustment was covered above in connection with Schedule C-6.

Q. Please describe adjustment IS-15.

A. Adjustment IS-15 adjusts test year expense in recognition of ANG's adoption of full accrual accounting for OPEB costs. Test year expense was recorded based on pay-as-you-go accounting. ANG proposes to adopt full accrual accounting of these costs in accordance with SFAS 106. As discussed above in connection with Schedule B-4-1, ANG has deferred incremental OPEB amounts since adoption of SFAS 106. ANG proposes to recover this regulatory asset, as projected through the end of the adjusted test year, over 20 years less the time elapsed from adoption of SFAS 106 until commencement of recovery, which is projected to be no later than December 1997. The projected amount of the regulatory asset through the end of the adjusted test year is $336,816, and the annual amortization over the recovery period is $22,330. This amount is combined with (1) the $190,400 excess of the accrual over pay-as-you-go expense and (2) the estimated $16,555 cost of external fund management, producing a total operating expense increase of $229,285.

Q. Please describe adjustment IS-16.

A. Adjustment IS-16 reduced operating expenses in the amount of $5,569. This adjustment was covered above in connection with Schedule C-7.

Q. Please describe adjustment IS-17.

A. During the test year, the AWG Division incurred expenses for relocation of general office employees while the AWG General Office Building was remodeled. These expenses were ultimately capitalized by AWG. However, some of these expenses are included in ANG's expenses for the test year as intercompany allocations. Adjustment IS-17 reduces operating expenses by $21,697 to eliminate these costs.

Q. Please describe adjustment IS-18.

A. Adjustment IS-18 reduces operating expenses by $84,523 to properly assign expenses which were charged incorrectly during the test year.

Q. Please describe adjustment IS-19.

A. On January 1, 1993, ANG adopted the provisions of SFAS 109, which provides for adjustment of accumulated deferred income taxes (ADIT) based on outstanding timing differences applied to current tax rates. In 1993, the Federal income tax rate increased from 34% to 35%. Because ANG expected regulatory recovery of the increase in ADIT, it established a regulatory asset in the amount of $64,000, which it now proposes to recover over the 20.2 years average remaining life of the property. Therefore, adjustment IS-19 increases operating expenses by $3,168.

Q. Please describe adjustment IS-20.

A. Adjustment IS-20 reduces operating expenses by $58,342 to reflect the adjusted test year level of regulatory commission expenses.

<u>Cost of Capital Schedules (Section D)</u>

Q. Please describe Schedule D-1-a.

A. Schedule D-1-a, Summary Cost of Capital, sets forth the capital structure components, amounts, and cost rates of Arkansas Western Gas Company as of July 31, 1996, per books and adjusted. The adjusted test year weighted average cost of capital rate is 8.69%. As mentioned earlier, ANG is a division of Arkansas Western Gas Company and does not maintain its own capital structure; it is for that reason that the capital structure of Arkansas Western Gas Company is utilized to develop the cost of capital for ANG.

Q. Please describe Schedule D-2.

A. Schedule D-2, Cost of Long-Term Debt, lists the details of the Company's long-term debt to arrive at net proceeds, annual cost, and the embedded cost rate for the test year and adjusted test year.

Q. Please describe Schedule D-3.

A. Schedule D-3, Cost of Common Equity, describes in brief the development of the 11.70% required rate of return on common equity recommended by Mr. Frank J. Hanley. Mr. Hanley addresses this issue in detail in his testimony and schedules.

Account Codes, Standard Journal Entries, and Trial Balance (Section E)

Q. Would you please describe Schedule E-1?

A. Schedule E-1 lists the standard journal entries of the Arkansas Western Gas Division and the Associated Natural Gas Division.

Q. Please describe Schedule E-2.

A. Schedule E-2 discusses the accounting system in use by Southwestern Energy Company and its subsidiaries and describes the supporting schedules E-2-1 through E-2-7.

Q. Please describe Schedule E-3.

A. Schedule E-3 addresses trial balance reports for the years ended July 31, 1994, through July 31, 1996. Trial balance reporting is presented separately for balance sheet accounts and income statement accounts on Schedules E-3-1 through E-3-6. This information is presented separately for each division and for total company.

Depreciation Information Schedules (Section F)

Q. Please describe Schedule F-1.

A. Schedule F-1 lists by district and plant account the July 31, 1996, balance, pro forma adjustments, and the resulting as adjusted balance for plant in service and accumulated depreciation. Also listed are present and proposed depreciation accrual rates and the resultant annual depreciation expense. The proposed rates are covered in the discussion of Schedule F-8.

Q. Please describe Schedules F-2 and F-3.

A. Schedules F-2 and F-3 are in the same format as Schedule F-1 and provide support by adjustment for plant in service and accumulated depreciation, respectively. These adjustments are described in detail in the above section concerning rate base adjustments.

Q. Please describe Schedule F-4.

A. Schedule F-4 is in same format as Schedule F-1 and provides support for the calculation of the adjusted test year depreciation accrual, which is included on Schedule F-3 as adjustment RB-6.

Q. Please describe Schedule F-5.

A. Schedule F-5 sets forth, in the same format as Schedule F-1, support for adjustments RB-1 and RB-2, which are included on Schedule F-2.

Q. Please describe Schedule F-6.

A. Schedule F-6 sets forth, in the same format as Schedule F-1, support for adjustment RB-3 listed on Schedules F-2 and F-3. Adjustment RB-3 consists of several adjustments, each of which have been listed in separate columns on this schedule.

Q. Please describe Schedule F-7.

A. Schedule F-7 lists the balances and activities pertaining to test year plant in service in the same detail as Schedule F-1.

Q. Please describe Schedule F-8.

A. Schedule F-8 addresses the depreciation study as of December 31, 1993, as discussed above in the description of Schedule F-1. As noted on Schedule F-8, the study was filed on July 1, 1994, and ANG is requesting approval of new rates based upon the study. However, revised Exhibits I, IIA, IIB, and IIC, replacing the exhibits originally filed, are included with Schedule F-8. It is the proposed rates referred to in the revised exhibits that ANG proposes to make effective.

<u>Purchased Gas Adjustment Clause</u>

Q. Included in Associated's January 14, 1997, filing were revised tariff sheets pertaining to its purchased gas adjustment (PGA) clause. Please describe the proposed changes to the PGA clause.

A. In the existing clause a reference is made to the volume of gas transported over ANG Northwest Arkansas transportation facilities to Ark-La for redelivery to the ANG service areas. (ANG Northwest Arkansas transportation facilities are actually the facilities of the AWG Division that have been allocated to the ANG Division.) The connection with NOARK Pipeline System is presently being utilized, but regardless of which pipeline is used, the same Northwest Arkansas facilities of ANG are utilized to deliver gas. Consequently, reference to a particular pipeline is inappropriate and thus the reference to Ark-La has been deleted (see Sheet Nos. 16 and 16O).

Q. Please discuss the charges for volumes transported over the ANG Northwest Arkansas facilities - both volumes transported for re-delivery to ANG sales customers and volumes transported for re-delivery to ANG transportation customers.

A. The rate applicable to volumes transported over the ANG Northwest Arkansas facilities for re-delivery to the ANG service area for sales purposes has been changed from $0.183 per Mcf to $0.35105 per Mcf. For any transportation of gas over the ANG Northwest Arkansas facilities for re-delivery to SEMO transportation customers there is a proposed $0.16414 per Mcf credit to SEMO district sales customers since the cost of the facilities is being fully recovered from sales customers by application of the $0.35105 rate per Mcf (see Sheet No. 16P). Therefore, application of these provisions of the clause will result in the following impact on sales customers of the SEMO District: (1) additional gas costs for sales volumes transported over ANG Northwest Arkansas facilities and (2) a reduction of gas costs if SEMO District transportation customers utilize the ANG Northwest Arkansas facilities. Witness Donna Campbell discusses the development of these rates in her testimony.

Q. What other changes have been made to this clause?

A. The billing determinants for SEECO purchases and the ANG Northwest Arkansas facilities charge have been revised to reflect the level utilized in this case (see Sheet Nos. 16E, 16F, 16G, and 16H). On Sheet No. 16G the billing determinant for MRT Energy Marketing agency fees has been eliminated since agency fees will be recovered through margin costs in accordance with Staff's preference. On Sheet Nos. 16J and 16N some out of date references to pipelines serving the interconnected portion of ANG territory have been eliminated from the jurisdictional allocation provisions applicable to take-or-pay and transition cost recovery factors. Similarly, the references to SEMO service areas have been updated on Sheet 16P. Finally, on Sheet 16R the interest rate applicable to refunds has been reduced from an unreasonably high level of nine percent to five and one-half percent.

Q. Why does ANG propose five and one-half percent?

A. We believe that the nine percent rate applicable to ANG's Missouri customers is too high. We are aware that a five and one-half percent rate was applicable to customers of regulated utilities in Arkansas for 1996, including ANG's Arkansas customers (APSC Docket No. 95-592-U, Order No. 3). We are also aware that the Arkansas Staff follows a procedure which evaluates current conditions to set the rate of interest applicable to deposit interest. Therefore, we have proposed that the rate of interest applicable to customer deposits for the Missouri jurisdiction be established at five and one-half percent.

Q. Has the base cost of gas per Ccf been modified?

A. No. The base cost of gas per Ccf set forth in the PGA clause and on the tariff sheets for sales service is unchanged.

Q. Does this conclude your direct testimony?

A. Yes.