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STATE OF MISSOURI  
PUBLIC SERVICE COMMISSION

TRANSCRIPT OF PROCEEDINGS

Hearing

December 12, 1997  
Jefferson City, Missouri  
Volume 7

In the matter of Missouri Public     )  
Service, a Division of UtiliCorp     )  
United, Inc., Tariff Designed to     )Case No. ER-97-394  
Increase Rates for Electric Service)  
to Customers in the Missouri     )  
Service Area of the Company.     )

and

In the Matter of the Filing of     )  
Tariff Sheets by Missouri Public     )  
Service, a Division of UtiliCorp     )Case No. ET-98-103  
United, Inc., Relating to Real-Time)  
Pricing, Flexible Rates/Special     )  
Contract, Line Extension Policy and)  
Energy Audit Program.     )

and

The Staff of the Missouri Public     )  
Service Commission,     )  
Complainant,     )  
v.     )Case No. EC-98-126  
UtiliCorp United, Inc., d/b/a     )  
Missouri Public Service,     )  
Respondent.     )

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JOSEPH A. DERQUE, III, Presiding,  
REGULATORY LAW JUDGE.  
SHEILA LUMPE, Chairperson,  
HAROLD CRUMPTON,  
M. DIANNE DRAINER,  
CONNIE MURRAY,  
COMMISSIONERS.

REPORTED BY:  
PATRICIA A. DURBIN, RMR, RPR, CCR, CSR  
ASSOCIATED COURT REPORTERS, INC.

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P R O C E E D I N G S

JUDGE DERQUE: I have three pieces of testimony for Mr. Hill. For the purposes of the record, this issue is the first issue on -- the only issue on Friday, December 12, capital structure, return on equity, cost of debt, marked E-1 through E-3, on Exhibit No. 2, the true-up reconciliation.

We have three pieces of testimony. That being the direct of Hill; that will be No. 74. The rebuttal of Hill, that will be No. 75. The surrebuttal of Mr. Hill; and that will be No. 76 and 76HC.

Is that correct, Mr. Woodsmall?

MR. WOODSMALL: It is.

JUDGE DERQUE: We're off the record.

(EXHIBIT NOS. 74, 75, 76 AND 76HC WERE MARKED FOR IDENTIFICATION.)

JUDGE DERQUE: On the record.

Mr. Woodsmall.

Let me swear in the witness.

(Witness affirmed.)

JUDGE DERQUE: Mr. Woodsmall.

MR. WOODSMALL: Thank you, your Honor.

STEPHEN G. HILL testified as follows:

DIRECT EXAMINATION BY MR. WOODSMALL:

1 Q. Would you state your name for the record,  
2 please?

3 A. My name is Stephen G. Hill.

4 Q. And by whom are you employed in this case?

5 A. By the Staff of the Public Service  
6 Commission.

7 Q. Okay. Would you give your address, please?

8 A. My business address is P. O. Box 587,  
9 4000 Benedict Road, Hurricane, West Virginia, 25526.

10 Q. And do you have what's been marked as  
11 Exhibit Nos. 74, 75 and 76 in front of you?

12 A. I do.

13 Q. Did you cause to be filed in this case  
14 Exhibit 74, direct testimony; 75, rebuttal testimony;  
15 and 76, surrebuttal testimony?

16 A. Yes, I did.

17 Q. And do you have any corrections to make to  
18 that at this time?

19 A. There is some typos in Exhibit 74.  
20 Page 9 in the quote on line 12, the range of  
21 Treasury bond yield should be 6 percent to 8 percent.

22 Q. Instead of the 8.05 percent?

23 A. That's correct.

24 Page 13, line 24, at the end of line, "that"  
25 should be changed to "than." Page 16, in the footnote  
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1 at the bottom of the page, the last percentage number  
2 in the line should be 58 percent rather than  
3 48 percent.

4 JUDGE DERQUE: Which page are you on?

5 THE WITNESS: Page 16. I'm sorry. At the  
6 very bottom of the page, footnote 4, the last line of  
7 that should read four years with approximately  
8 42 percent common and preferred stock and 58 percent  
9 long and short term debt.

10 Page 38, line 6 -- page 38, line 6 there is  
11 an upper case S and the word "is," that should not be  
12 there. It should be a small case s. That's all I  
13 have.

14 BY MR. WOODSMALL:

15 Q. And with those changes, is the information  
16 contained in Exhibits 74, 75 and 76 true and accurate  
17 to the best of your knowledge and belief?

18 A. Yes.

19 MR. WOODS: At this time I'd offer  
20 Exhibits 74, 75 and 76 into the record and tender the  
21 witness for cross-examination.

22 JUDGE DERQUE: Thank you, Mr. Woodsmall.

23 I have Exhibits 74 through 76HC offered for  
24 admission into evidence. Is there any objection?

25 Hearing none, they will be admitted.

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1 (EXHIBIT NOS. 74 THROUGH 76HC WERE RECEIVED  
2 INTO EVIDENCE.)

3 JUDGE DERQUE: Mr. Finnegan?

4 MR. FINNEGAN: I think (indicating) --

5 JUDGE DERQUE: That's okay. I'm just  
6 guessing.

7 MR. MILLS: Actually, I think you guessed  
8 right.

9 JUDGE DERQUE: Mr. Mills. I'm sorry.

10 MR. MILLS: I have no questions.

11 JUDGE DERQUE: Mr. Finnegan?

12 MR. FINNEGAN: I only have a few questions.

13 CROSS-EXAMINATION BY MR. FINNEGAN:

14 Q. Mr. Hill, I believe on page 42 of Exhibit 74  
15 you indicated that you recommended a return on equity  
16 of 10.75 percent?

17 A. That's correct.

18 Q. Which is the -- you indicated is the  
19 midpoint of the upper half of a range?

20 A. Yes.

21 Q. And that range is 10 percent to 11 percent?

22 A. That is right.

23 Q. You're making a recommendation as to 10.75,  
24 but are you saying that if the Commission were to give  
25 10 percent, that that would be a reasonable return on

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1 equity?

2 A. It's within a range of reasonable returns.

3 It wouldn't be the point estimate that I would

4 recommend.

5 Q. But it's within a reasonable range?

6 A. Yes. For the companies that Mr. Dunn

7 selected and I used in my cost of capital analysis,

8 10 percent would certainly be a reasonable allowed

9 return on equity for those companies, but because

10 we're recommending the use of UtiliCorp's consolidated

11 capital structure, which is more heavily leveraged, in

12 other words, uses more debt and less equity, the

13 company -- this company is a little bit more financial

14 risk and, therefore, deserves a higher rate of return.

15 So while 10 percent is in the range, I believe 10.75

16 is a better point estimate.

17 Q. But it would not be unreasonable for the

18 Commission to order a return of 10 percent on equity?

19 A. It wouldn't -- I wouldn't say it would be

20 unreasonable. I wouldn't recommend that they do that.

21 I would recommend that they award a return to someone

22 higher than that.

23 Q. Somewhat higher like 10.25 percent or

24 10.5 percent?

25 A. No. 10.75 percent is what I recommend.

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1           Q.     There is a difference in the dollars it  
2 produces, is there not, between 10.75 and 10.5?

3           A.     Absolutely. And the range -- the reason I  
4 give a range of 10 to 11 percent is because cost of  
5 capital is an approximation. It's not an exact  
6 science by any means.

7                     Therefore, I believe that's a representation  
8 of how accurate the process is. It certainly is no  
9 more accurate than 25 basis points. In my view,  
10 10.55 doesn't really make any sense, because the five  
11 basis points above the 10 1/2 is -- it's really lost  
12 in the process of trying to estimate that cost of  
13 capital.

14                    So in estimating, I have to come up with a  
15 range I feel that represents a reasonable estimate of  
16 what the market indicates, and then within that range,  
17 given the risk specifics of a particular company, I  
18 selected a point within that range.

19           Q.     But you said up to 25 basis points would  
20 make no difference in your recommendation. Is that  
21 what I understood you to say?

22           A.     Not exactly. What I'm saying is you can't  
23 really -- I don't think that the process is accurate  
24 enough to talk about shades of difference between  
25 10 percent and 10.25 percent with any real meaning. I



1 don't think 10.11 makes -- means anything given how  
2 accurate this process is.

3 Q. Do you know what the return was that MPS was  
4 earning during the test year?

5 A. The return on equity?

6 Q. Yes.

7 A. I don't have that number.

8 Q. You wouldn't know what it was in any prior  
9 years?

10 A. I don't have those numbers committed to  
11 memory.

12 Q. Do you know if it's more than 10.75 percent?

13 MR. SWEARENGEN: Your Honor, I'm going to  
14 object. He said he doesn't know.

15 MR. FINNEGAN: He said he doesn't have it  
16 committed to memory. I'm just asking if he knows  
17 within a range.

18 JUDGE DERQUE: Well, I'll give you about two  
19 more questions, Mr. Finnegan, on this.

20 MR. FINNEGAN: That's fine.

21 THE WITNESS: I don't know if it was more or  
22 not.

23 BY MR. FINNEGAN:

24 Q. You don't.

25 You do know that Staff is requesting a rate  
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1 decrease?

2 A. That's right.

3 Q. -- a substantial rate decrease?

4 A. Yes.

5 Q. So in your mind that would mean that it was  
6 earning more than 10.75 percent?

7 A. Well, there's more things involved than just  
8 the overall rate of return in the rate decrease.

9 Q. But rate of return basically is a fall-out,  
10 is it not, of all of the other items?

11 A. You're asking a rate-of-return witness if  
12 rate of return is a fall-out number? I would say no  
13 to that question.

14 In reality, that's the way it often works.  
15 It's the bottom line. It's what happens at the end of  
16 the day.

17 Q. Okay. Well, let me get to this.

18 If for the Company to earn -- if the Company  
19 were to earn 10.75 for the next two years and assuming  
20 that it had earned more for the prior two years, would  
21 not the average earnings for those four-year periods  
22 be greater than 10.75 percent?

23 A. That would stand to reason.

24 MR. FINNEGAN: Okay. That's all of the  
25 questions I have.

1 JUDGE DERQUE: Thank you, Mr. Finnegan.

2 Mr. Swearengen?

3 MR. SWEARENGEN: Thank you, Judge.

4 CROSS-EXAMINATION BY MR. SWEARENGEN:

5 Q. Mr. Hill, we met earlier. My name is Jim  
6 Swearengen. I'll be asking you some questions today  
7 on behalf of the Missouri Public Service operating  
8 division of UtiliCorp.

9 I note in the very first page of your direct  
10 testimony, you say you've testified on cost of capital  
11 issues in over 150 regulatory proceedings, and then  
12 you list various commissions. Did you actually take  
13 the stand in all 150 of those cases?

14 A. Very nearly. There were a couple of cases  
15 where I filed testimony where I didn't appear that  
16 were settled, but almost.

17 Q. By and large, in most of those cases, the  
18 cost of capital, capital structure, those were  
19 contested issues. Is that a fair statement?

20 A. Yes. By and large that's the case. I've  
21 testified on some other econometric sort of issues and  
22 even engineering issues at times, but by and large  
23 95 percent of those cases have been cost of capital.

24 Q. You mentioned testifying on engineering  
25 issues. Do you have an engineering background? Is

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1       that what I understand?

2           A.     Yes, I do.

3           Q.     And can you tell us what that is, please?

4           A.     Chemical engineering.

5           Q.     Okay.  And that's from Auburn University; is  
6       that right?

7           A.     That's right.

8           Q.     You also indicated that you received a  
9       master's degree in business administration?

10          A.     That's correct.

11          Q.     And was that from Tulane?

12          A.     Yes, sir.

13          Q.     And what year was that, do you recall?

14          A.     1973.

15          Q.     1973.  When did get your chemical  
16       engineering degree?

17          A.     '71.

18          Q.     In the context of earning your chemical  
19       engineering degree or your business administration  
20       degree, did you take some financial courses?

21          A.     Yes, I did.

22          Q.     Okay.  And just briefly describe what those  
23       might have been.

24          A.     Well, there were a couple of engineering  
25       economic courses in undergraduate school that related

1 to plant design issues. My concentration in graduate  
2 school was more along the lines of finance. I took a  
3 finance course every semester I was in school. I  
4 can't name the particular courses.

5 Q. That's fine.

6 Do you ever recall who the author may have  
7 been of the first textbook that you used in those  
8 finance courses?

9 A. I'm sure that we used the Van Horne text,  
10 and I think we also used the Brigham text.

11 Q. Okay. When you say the Brigham text, do you  
12 recall what the title of that may have been?

13 A. Fundamentals of Financial Management.

14 Q. Would you agree that that may be the number  
15 one finance textbook on that subject?

16 A. I don't think -- I'm aware what the market  
17 for finance textbooks is. I know it's widely cited.

18 Q. Are you familiar with Brigham and Weston's  
19 Financial Theory and Corporate Policy textbook?

20 A. I've seen it.

21 Q. Okay. And the Brigham and Weston's  
22 Managerial Finance textbook?

23 A. Yes, I've seen that also.

24 Q. How about Financial Theory and Corporate  
25 Policy by Copeland and Weston?

1           A.     I'm familiar with the names Copeland and  
2     Weston. I don't recall the title.

3           MR. SWEARENGEN: Let me have an exhibit  
4     marked at this time, if I could, please.

5           JUDGE DERQUE: That exhibit number we're  
6     going to mark for purposes of identification is  
7     Exhibit No. 77, identified as a three-page Xerox  
8     document captioned Financial Theory and Corporate  
9     Policy, Third Edition.

10          We're off the record.

11          (EXHIBIT NO. 77 WAS MARKED FOR  
12     IDENTIFICATION.)

13          JUDGE DERQUE: We're back on the record.

14          Mr. Swearengen.

15          MR. SWEARENGEN: Thank you, your Honor.

16     BY MR. SWEARENGEN:

17          Q.     Mr. Hill, I'm going to hand you what we've  
18     just marked for identification as Exhibit 77 and ask  
19     you to take a look at it. And on the third page of  
20     that document I have highlighted some information.

21          A.     I'm just looking for the publication date.  
22     I don't see it on there.

23          Q.     Are you familiar with that text at all?  
24     Have you seen that text previously?

25          A.     As I said before, I'm familiar with the  
                  776

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1 names Copeland and Weston, and I'm aware that they've  
2 authored a series of finance texts. I don't recall a  
3 particular title.

4 Q. Okay. I have highlighted in yellow ink on  
5 your copy, and perhaps underlined on the others, some  
6 language from page 621 of that text. Could you read  
7 that into the record, please?

8 A. Okay.

9 MR. WOODSMALL: Your Honor, at this point I  
10 would object. I don't believe Copeland and Weston  
11 have been established as authoritative in any way.  
12 Furthermore, any questions regarding this, Mr. Hill  
13 has said he's never seen it. I believe we're going a  
14 little far afield without establishing some type of  
15 foundation for this document, as well as the questions  
16 to be based upon this document.

17 MR. SWEARENGEN: I haven't asked him any  
18 questions about it. I'm just asking him to read that  
19 language into the record.

20 JUDGE DERQUE: Mr. Swearengen, could --

21 MR. WOODSMALL: I guess my question then  
22 would be, for what purpose is it being read into the  
23 record?

24 JUDGE DERQUE: Well, I'd prefer that you do  
25 this with your own witness, but I'm not exactly sure

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1 where you're going. I'm going to overrule the  
2 objection.

3 Go ahead, Mr. Swearengen. This is  
4 cross-examination.

5 MR. SWEARENGEN: Thank you, Judge.

6 BY MR. SWEARENGEN:

7 Q. Could you go ahead and read that into the  
8 record?

9 A. I'll just note that this is page 621 from  
10 this text, and a chapter entitled The Theory of  
11 Leasing.

12 And the underlined sentence reads: "We  
13 assume that the optimal capital structure is project  
14 specific. For example, a commercial bank with 90 to  
15 95 percent debt in its capital structure should not  
16 apply the same leverage to a wholly-owned computer  
17 division. Presumably, the computer division has its  
18 own optimal leverage, different from, paren, less than  
19 paren close, the commercial bank's."

20 Q. Now, let me ask you this question: That  
21 language you just read and the concept or concepts  
22 expressed therein, what does that mean to you?

23 A. It means to me that in a situation -- the  
24 paragraph is describing how you would value a purchase  
25 rather than a lease and an investment decision. And



1     what it says to me is that in order to figure out the  
2     present value or the future cash flows, you might use  
3     a different discount rate for one project over  
4     another.

5           Q.     Let me take a look at that just for a  
6     second, if I could.

7                     That statement that you read into the record  
8     uses the terms "optimal capital structure" and  
9     "project specific." What is your understanding, if  
10    any, of those terms?

11           A.     An optimal capital structure in theory is a  
12    capital structure that minimizes the capital cost  
13    rate. Optimal capital structure would be different  
14    for different projects, and that's why an optimal  
15    capital structure is project specific.

16           Q.     Okay. And when you say "project specific,"  
17    what is your understanding of --

18                     MR. WOODSMALL: Your Honor, again, I would  
19    object. I believe Mr. Swearengen is attempting to use  
20    this document as somehow being authoritative and  
21    asking questions to get Mr. Hill to adopt certain  
22    terms and then use that in his brief as an  
23    authoritative description of Missouri Public Service  
24    and its operations.

25                     I don't believe any foundation has been

1 established for this. The author is certainly not  
2 here. Mr. Hill has never seen this document before.  
3 They could have easily put it into surrebuttal and  
4 given him a chance to review prior to taking the stand  
5 here.

6 MR. SWEARENGEN: Judge, let me respond to  
7 that. I'm not attempting to qualify this document  
8 through this witness. I just asked him to read that  
9 language, and he can tell us what he thinks it means.  
10 And that's all I'm asking him to do, and I think  
11 that's certainly appropriate cross-examination.

12 JUDGE DERQUE: Well, so far that's correct.  
13 There has been -- for purposes of administrative  
14 procedure, there has been a minimal foundation, and I  
15 will agree it's minimal foundation laid for the  
16 material that's marked Exhibit 77.

17 As this is cross-examination, I'm going to  
18 let Mr. Swearengen continue.

19 MR. SWEARENGEN: Thank you, Judge.

20 BY MR. SWEARENGEN:

21 Q. Mr. Hill, I think where we were, I was  
22 asking you your understanding of the meaning of the  
23 term "project specific."

24 A. Project specific I think is pretty self-  
25 explanatory. It means there is a specific project.

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1       They're talking about here a bank and a computer  
2       operation --  
3       Q.     Okay.  
4       A.     -- a different --  
5       Q.     Could a project be a subsidiary, let's say,  
6       of the corporation?  
7       A.     That doesn't appear to be what he's talking  
8       about in this document.  If you want to abstract those  
9       ideas to something else, then I'll agree that a  
10      project could be more than an investment in a  
11      particular instrument or a piece of equipment.  
12      Q.     Right.  I understand you said you probably  
13      hadn't seen that document before, and I'm asking you  
14      your opinion as to whether a project, you would agree,  
15      could be a subsidiary corporation?  Was that your  
16      testimony?  
17      A.     Sure.  You can define it however you like.  
18      Q.     Okay.  Well, would you define it that way?  
19      Would your definition --  
20      A.     I wouldn't define a project as a subsidiary,  
21      no.  
22      Q.     Okay.  How would you define it?  
23      A.     A project is something that you expect to  
24      invest in.  You run a corporation.  You have --  
25      somebody comes to you with an idea for an investment,

1 and you have to evaluate that investment based on the  
2 future cash flows. To me that would be a project.

3 Q. Okay. So it would be an investment or a  
4 commitment of funds or something of that sort, at  
5 least as far as you're concerned?

6 A. Yes.

7 Q. That's fair enough. Thank you.

8 Do you still have that language, that page  
9 in front of you?

10 A. Yes, I do.

11 Q. Does that paragraph go on to state that a  
12 bank or a subsidiary has different leverage in the  
13 bank than it does in the subsidiary?

14 A. It presumes that the computer division has a  
15 different leverage than the bank.

16 Q. Okay.

17 A. It doesn't say that it does. It presumes  
18 that it does.

19 Q. It presumes.

20 Now, what with respect to UtiliCorp, would  
21 you agree with me that it has -- the corporation has  
22 different subsidiary corporations?

23 A. Yes.

24 Q. Okay.

25 A. Well, it has divisions. It has different

1     operating divisions within the umbrella company  
2     UtiliCorp.

3           Q.     Okay.  And your understanding, it has  
4     different operating divisions?

5           A.     Right.

6           Q.     Okay.  And let me ask you then the first  
7     question:  Is it your understanding that UtiliCorp  
8     also has subsidiary corporations?

9           A.     Yes, that is my understanding.

10          Q.     Okay.  In addition to the divisions?

11          A.     That is right.

12          Q.     And what is your understanding of the  
13     distinction between a division and a subsidiary  
14     corporation?

15          A.     A subsidiary corporation is a separate  
16     incorporated entity.  A division is merely a  
17     description of a kind of operation.  It's different  
18     from a subsidiary corporation.  A corporation has its  
19     corporate bylaws and charter.  A division simply is --  
20     most often is an accounting definition of what type of  
21     operation.

22          Q.     And I assume you're aware that this case  
23     that we have before the Commission today is in the  
24     name of the Missouri Public Service operating division  
25     of UtiliCorp?  Is that your understanding?

1           A.     Yes.

2           Q.     Okay.  Are there any other characteristics  
3     that distinguish a subsidiary corporation from a  
4     division other than the ones that you just mentioned?  
5     I think you said separate articles of incorporation  
6     maybe.

7           A.     Generally a subsidiary -- I won't say  
8     generally, but sometimes a subsidiary will access  
9     capital markets apart from the parent holding company.  
10    That will not occur with a division, because a  
11    division doesn't exist as an entity which can issue  
12    capital.

13                 And that's the situation with Missouri  
14    Public Service.  It doesn't exist as an entity that  
15    can issue its own capital.  It doesn't issue its own  
16    capital.  As a matter of fact, outside of the confines  
17    of this building, it probably doesn't even exist.

18                 I mean, the Company in its annual reports  
19    doesn't talk about Missouri Public Service.  Missouri  
20    Public Service is divvied up in the generation and  
21    distribution in two separate divisions of UtiliCorp.

22                 So what we're dealing with here in this case  
23    is a construct that is called Missouri Public Service.

24           Q.     And what do you mean by "a construct"?

25           A.     I mean, it's a convenience of --

1 administrative convenience that the company is  
2 regulated. And in order to be regulated, the  
3 regulators have to consider all aspects of the  
4 company. So it's -- it's aggregated on that basis for  
5 this purpose. Outside of this building, outside of  
6 that purpose, it doesn't exist in that format.

7 Q. That's an interesting comment, so let me ask  
8 you this question then.

9 In your mind there really isn't any such  
10 thing as Missouri Public Service?

11 A. That's not what I said. There very  
12 definitely is, and the rates that are determined in  
13 this case are going to have a real impact on people.

14 That's not what I'm saying at all.

15 Q. Okay.

16 A. What I'm saying in the context of your  
17 question, which is the difference between a division  
18 and a subsidiary.

19 Q. Uh-huh.

20 A. A division is essentially an accounting  
21 construct within a larger company. And UtiliCorp  
22 chooses to divvy up Missouri Public Service when it  
23 talks to shareholders in its annual reports and say,  
24 Well, we've got a generation subsidiary, we have a  
25 wire subsidiary, but they don't talk about Missouri

1 Public Service. But in this context, that's what --  
2 that is what we're talking about.

3 Q. Would you agree with me that in addition the  
4 Missouri Public Service operating division, whatever  
5 it does, in fact, consist of it, is what is subject to  
6 the jurisdiction of this Commission?

7 A. Yes, I would certainly agree with that.

8 Q. Let me ask you this. I assume you read  
9 Mr. John C. Dunn's rebuttal testimony in the  
10 preparation for this case? Is that a fair statement?

11 A. Yes, I did.

12 Are you going to refer to it?

13 Q. I'm not sure.

14 A. Okay. I've got it here if I need to.

15 Q. Okay. You say you do have it?

16 A. Yes, I do.

17 Q. Why don't you turn to page 11 of that then.

18 That might be helpful.

19 A. Rebuttal?

20 Q. Yes, sir.

21 A. I'm there.

22 Q. Okay. Down there, I think, oh, lines 20 and  
23 21 at the bottom of the page, Mr. Dunn is testifying  
24 that the risk profile of the subsidiary is a carbon  
25 copy of the average risk profile of the corporation



1 and consequently the subsidiary should have its own  
2 capital structure.

3 A. Would you repeat that? I don't think that's  
4 his testimony.

5 Q. He says unless the risk profile of the  
6 subsidiary --

7 A. Oh, unless.

8 Q. -- is a carbon copy of the average risk  
9 profile of the corporation, a subsidiary should have  
10 its own capital.

11 JUDGE DERQUE: What page are you on?

12 MR. SWEARENGEN: Page 11 and 12.

13 JUDGE DERQUE: Of his rebuttal?

14 MR. SWEARENGEN: Of Mr. Dunn's rebuttal.

15 THE WITNESS: It's the very last two words  
16 on page 11.

17 JUDGE DERQUE: Oh, I see. Thank you.

18 MR. SWEARENGEN: The bottom of page 11, top  
19 of page 12. I'm sorry.

20 JUDGE DERQUE: Thank you.

21 THE WITNESS: You're asking me if that's  
22 what he said?

23 BY MR. SWEARENGEN:

24 Q. Right, you're aware that he's testified to  
25 that?

1           A.     I'm aware that's what he said, yes.

2           Q.     And are you familiar with the authors that  
3 he cites at page 12 of his rebuttal testimony?

4           A.     I'm not.

5           Q.     Okay. Do you know whether or not any of  
6 that information might have been supplied in  
7 connection with his testimony in this proceeding  
8 pertaining to that text, capital investment and  
9 capital decision?

10          A.     Am I aware if he provided a copy of what he  
11 quotes there?

12          Q.     Of any of that information relating to that  
13 text.

14          A.     I don't recall that specific text being  
15 provided.

16          Q.     Mr. Hill, I'm not going to mark this for  
17 identification, but I'm just going to hand you -- I'm  
18 going to hand you a four-page document. You can just  
19 describe what it is. Take a look at it, and then I'm  
20 going to ask you to read, if you would, please, the  
21 highlighted language on 464 and 465.

22          A.     Okay. It appears to be the front piece  
23 of -- and a couple of pages from a text entitled  
24 Capital Investments and Financial Decisions, Third  
25 Edition, by Levy and Sarnat.

1           Q.     And then what I'd like you to do is to take  
2     a look at it, and I want you to read what appears at  
3     the bottom of 464 and 465 of that, the highlighted  
4     information.

5           MR. MILLS:   Well, I'm going object to this  
6     line. I think we've gone through this before, and I'm  
7     not sure it's proper cross-examination to hand a  
8     witness a document that he's never seen before by  
9     authors he's never heard of and just have him read  
10    blindly pieces of it out of context. That seems to be  
11    the thread of Mr. Swearengen's cross-examination.

12           And I didn't object on the first one, but I  
13    think Mr. Woodsmall's objection was proper. There has  
14    been no foundation laid for this one, and there was no  
15    foundation laid for the last one.

16           JUDGE DERQUE:   Well, there was nothing  
17    improper about Mr. Woodsmall's objection.

18           In the case of marked Exhibit No. 77,  
19    certainly the record should reflect that whatever is  
20    contained in that exhibit that Mr. Hill reviewed bears  
21    on the weight it should be given.

22           And this one, there is no foundation for  
23    this, Mr. Swearengen, not at all. You're going to  
24    have to lay a little for this.

25           MR. SWEARENGEN:   I'm not going to offer the  
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1 document. I just wanted him to read that and then I  
2 was going to ask him some questions about that.

3 He can say whatever he wants to. I'm not  
4 necessarily going to ask him to agree or disagree. He  
5 can say whatever he wants to about it.

6 MR. MILLS: I think reading it is the same  
7 as offering it, whether it's -- you know, if Mr. Hill  
8 reads it or as it's reflected in the exhibit.

9 JUDGE DERQUE: The Commission would regard  
10 it on the record in reviewing the evidence as having  
11 no weight at all, Mr. Swearengen.

12 MR. SWEARENGEN: Well, I could read him this  
13 and then ask him to talk about it. I just thought it  
14 would be easier --

15 JUDGE DERQUE: You can certainly do it.

16 MR. SWEARENGEN: I thought it would be a lot  
17 easier for him just to read it and then he'd have it  
18 in front of him and I could ask him some questions  
19 about it.

20 MR. FINNEGAN: Your Honor, there is always  
21 the hearsay objection also.

22 JUDGE DERQUE: Yes, there is.

23 MR. FINNEGAN: This is testimony by somebody  
24 who is not here and can't be cross-examined. It's in  
25 writing. We don't even know who they are.

1           MR. SWEARENGEN: I'm not going to ask -- I  
2       mean, I may ask him if agrees or disagrees. He can  
3       say whatever he wants to. I have no idea.

4           JUDGE DERQUE: Mr. Swearengen, because  
5       you're the applicant, I'm going to let you proceed  
6       with this, but I'm going to note right now for the  
7       record that the weight of this is minimal at best.

8           MR. SWEARENGEN: That's fine.

9       BY MR. SWEARENGEN:

10       Q.     Would you go ahead, Mr. Hill, and read that  
11     in, please --

12       A.     Sure.

13       Q.     -- the highlighted --

14       A.     The highlighted material says as follows:

15     However, there is a distinction between the firm's  
16     cost of capital and a specific project's cost of  
17     capital. Let us elaborate.

18           The firm's cost of capital. The firm's cost  
19     of capital is a discount rate employed to discount the  
20     firm's average cash flow; hence, obtaining the value  
21     of the firm. It is also the weighted average cost of  
22     capital as we shall see below.

23           The weighted average cost of capital should  
24     be employed for project evaluation, paren, i.e.,  
25     calculating the NPV, which stands for net present

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1 value, paren close, only in cases where the risk  
2 profile of the new project is, quote, a carbon copy,  
3 unquote, of the risk profile of the firm.

4 Q. Okay. Now, let me ask you: Is that a  
5 concept that you're familiar with that you just read  
6 there?

7 A. Yes, it is a concept I'm familiar with, and  
8 fortunately in this case, the risk profile of Missouri  
9 Public Service is a carbon copy of the consolidated  
10 capital structure of UtiliCorp.

11 Q. Okay. Do you agree with this concept?

12 A. Yes.

13 Q. Okay.

14 A. I have no problem with that concept. I  
15 don't think it applies in this case.

16 Q. That's fine. Thank you.

17 Do you have Mr. Dunn's direct testimony, and  
18 you said you have his rebuttal?

19 A. Yes, I have his direct.

20 Q. Okay. Could you take a look, please, at  
21 page 37 of his direct testimony.

22 A. I have that.

23 JUDGE DERQUE: Is this Mr. Dunn's direct?

24 MR. SWEARENGEN: Mr. Dunn's direct.

25 JUDGE DERQUE: Which page?

1 MR. SWEARENGEN: Page 37.

2 JUDGE DERQUE: I'm sorry. I'm trying to

3 catch up here.

4 BY MR. SWEARENGEN:

5 Q. Mr. Hill, there's a question at the top of

6 page 37 beginning on line 1 and then an answer which

7 begins on line 3 and runs through line 9, and I take

8 it you've read that previously?

9 A. Yes.

10 Q. Are you familiar with the textbook that's

11 referred to there in line 3?

12 A. I'm not.

13 Q. You're not?

14 A. No.

15 Q. Are you familiar with any of the three names

16 of the individuals in line 3?

17 A. I've seen the name Gitman before. The

18 others, Joehnk and Pinches I've not seen.

19 MR. SWEARENGEN: At this time, your Honor,

20 could we go off the record so I could have an exhibit

21 marked, please?

22 JUDGE DERQUE: Yes, sir. If we're going to

23 go off, why don't we take about a ten-minute break.

24 (A recess was taken.)

25 JUDGE DERQUE: We're on the record.

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1 I have what I will mark as Exhibit No. 78,  
2 identified as a one-page consolidated balance sheet.

3 (EXHIBIT NO. 78 WAS MARKED FOR  
4 IDENTIFICATION.)

5 JUDGE DERQUE: We're on the record.

6 I have what I will mark for purposes of  
7 identification as Exhibit No. 79, identified as a one-  
8 page document styled note 8 and note 9, short-term and  
9 long-term debt.

10 JUDGE DERQUE: We're off the record.

11 (EXHIBIT NO. 79 WAS MARKED FOR  
12 IDENTIFICATION.)

13 JUDGE DERQUE: We're on the record.

14 Mr. Swearengen?

15 MR. SWEARENGEN: Thank you, your Honor.

16 BY MR. SWEARENGEN:

17 Q. Mr. Hill, is it your understanding that one  
18 of the issues or subjects here today is the question  
19 of how to treat the foreign debt of UtiliCorp? And go  
20 ahead and tell me what your understanding of that  
21 issue is. I just want to make sure I understand.

22 A. Yes, that's one of the issues that is  
23 presented in the Company's testimony.

24 It is an adjunct or a subpart of the issue  
25 of the overall cost of capital, which is a subissue of

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1       which capital structure you should use.

2           Q.     Right.  Thank you very much.

3                   While we were off the record -- well, let me  
4       ask you this question first.

5                   I guess in preparing yourself for this case,  
6       you did, in fact, become familiar with the  
7       consolidated capital structure of UtiliCorp.  Is that  
8       not correct?

9           A.     That's correct.

10          Q.     And in that context did you have occasion to  
11       review information which was a part of their 1996  
12       annual report?

13          A.     I did.

14          Q.     Okay.  And do you have a copy of that annual  
15       report there with you on the witness stand?

16          A.     Yes, I do.

17          Q.     And I have had marked for purposes of  
18       identification as Exhibits 78 and 79 pages 35 and 45  
19       from that annual report.  Is that your understanding?

20          A.     Yes.

21          Q.     Now, if you would just for purposes of  
22       convenience turn to Exhibit 78, which is page 35.

23                   Am I correct that that shows the  
24       consolidated balance sheets of UtiliCorp for the years  
25       1994, 1995 and 1996?

1 A. Yes.

2 Q. Now, can you look at that document and tell  
3 me for 1996 the amount of net long-term debt, please?

4 A. 1.4 billion, roughly.

5 Q. And do you find that down in the area  
6 described long-term liabilities, long-term debt net,  
7 1,470.7?

8 A. Yes.

9 Q. Is --

10 A. Those dollars are in millions. That's the  
11 left-hand column just below the middle of the page.

12 Q. Turning to the next exhibit, Exhibit 79, am  
13 I correct that that's a copy of page 45 from  
14 UtiliCorp's 1996 annual report?

15 A. Yes.

16 Q. And what does that show as the long-term  
17 debt net for UtiliCorp for 1996?

18 A. The same figure.

19 Q. Okay. Now, on that document, page 45,  
20 Exhibit 79, if you look at the detail under the third  
21 bold heading under long-term debt, am I correct that  
22 you see the terminology secured debentures of West  
23 Kootenay Power? Do you see that?

24 A. Yes.

25 Q. And can you tell us your understanding of  
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1       what that represents?

2           A.     That's the debt investment in the Western  
3       Canadian electric operations.

4           Q.     And what do you know about that debt  
5       investment?

6           A.     Um, I know that the coupon cost rate is  
7       about 9 1/2 percent, and it comprises about  
8       \$68 million of total debt capital for UtiliCorp.

9           Q.     Do you have any understanding with respect  
10      to how the proceeds from those debentures can be  
11      utilized?

12          A.     Um, my understanding is that when funds are  
13      raised through a debt issuance or equity issuance,  
14      those funds enter the treasury, the corporate  
15      treasury, and then are disbursed as the corporation  
16      sees fit. And I haven't seen anything to the contrary  
17      in the Company's 10-Ks annual reports or the Company's  
18      testimony in this proceeding.

19          Q.     Let me ask you this question, and I'm going  
20      to read a statement and tell me if you agree or  
21      disagree.

22                 The debentures of West Kootenay Power  
23      require that, first, the lending be secured by West  
24      Kootenay assets and, second, that the money be used  
25      for West Kootenay Power purposes.

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1                   Do you agree with that, disagree or you  
2   don't know?

3           A.     Can you give me a reference on what you're  
4   reading from?

5           Q.     I'm just reading a question to you. I'm  
6   asking you whether you agree with it or not.

7           A.     I don't have an information to disagree with  
8   it or agree with it.

9           Q.     Okay. Fine.

10                  I think earlier when you were talking about  
11   differences between divisions and subsidiaries, I  
12   believe you indicated that subsidiaries do their own  
13   financing. Did you say that?

14           A.     They can. They don't always do that, but  
15   they can.

16           Q.     With respect to the secured debentures of  
17   West Kootenay Power, is it your understanding and  
18   would you agree with me that they are direct issuances  
19   of West Kootenay and Power?

20           A.     Yes. But simply because they were issued by  
21   a particular subsidiary of the Company doesn't mean  
22   that -- for example, those actual dollars are escrowed  
23   in Western Canada and have to be used in Western  
24   Canada. Those dollars can come back to the corporate  
25   treasury, and as long as the total amounts of money

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1 spent is equal to the debt issuance, the folks in  
2 Western Canada are unconcerned about the use of those  
3 funds.

4 Q. Now, what do you base that statement on?

5 A. Well, my knowledge of debt issuances and  
6 corporate finance.

7 Q. In general?

8 A. Yes.

9 Q. But not on any knowledge you may have with  
10 respect to this particular debt issuance in  
11 particular?

12 A. As I've said, I've seen nothing in the SEC  
13 documents filed by the Company, the annual reports or  
14 the evidence offered by the Company in this proceeding  
15 which would indicate otherwise.

16 Q. Further down on Exhibit 79 below where the  
17 West Kootenay Power debentures are listed, there's an  
18 item denominated -- excuse me -- an item which reads,  
19 New Zealand Denominated Credit Facility due  
20 February 28, 1998. Do you see that?

21 A. Yes, I do.

22 Q. And would you agree that technically you  
23 would call that short-term debt, that particular item?

24 A. The Company doesn't call it short-term debt.  
25 They call it long-term debt.

1 Q. What would you call it?

2 A. I believe I would call it long-term debt.

3 Q. Do you understand that that issue is  
4 denominated in New Zealand dollars?

5 A. Um, I understand that what appears on the  
6 balance sheet represents the Company's interest in  
7 that venture. And they own a 30 -- or 20 to 30  
8 percent interest in that New Zealand venture, and this  
9 is a representative portion of the debt that they own  
10 from that operation.

11 Q. Okay. Who are the other owners of that  
12 operation?

13 A. I don't know.

14 Q. But you believe there are other owners?

15 A. Well, I would assume that somebody owns the  
16 other 70 percent. I mean, the company talks about  
17 their ownership in their annual reports and they --  
18 their subsidiary. They have a wholly-owned  
19 subsidiary, which then owns the interest in the  
20 New Zealand operations, and that interest is  
21 20 percent of one company and 30 percent of another.

22 Q. In the context of your discovery in this  
23 proceeding, were you supplied a response to a data  
24 request -- were you supplied in response to a data  
25 request copies of a portion of the indenture that

1 relate to the New Zealand Credit Facility that we're  
2 talking about?

3 A. I don't believe that was -- I was supplied  
4 that in data request. Your witness in his rebuttal  
5 testimony included a couple of pages from the  
6 indentures in the Australia and New Zealand debt.

7 Q. Okay. So you have the Indenture or a  
8 portion of it that you got in some fashion? Is that a  
9 fair statement?

10 A. Well, I've seen those two pages. And as  
11 I've said in my testimony, those two pages don't tell  
12 me that the monies raised in New Zealand are required  
13 to stay in New Zealand. All they say is that the  
14 amount of money that is raised in that debt issue has  
15 got to be spent in New Zealand.

16 Q. That was going to be my question.

17 Whatever you looked at, the portion of the  
18 indenture that was supplied to you, did it require  
19 that the loan represented by that credit facility line  
20 be used in the acquisition of New Zealand properties?

21 A. What it says is that the monies raised  
22 should be invested, and it says directly or indirectly  
23 in New Zealand.

24 Q. Okay.

25 A. And my understanding, that means that the

1 Company has wide latitude about the use of those  
2 monies. As long as they borrow \$50 million and they  
3 ultimately invest \$50 million, then the lender is  
4 unconcerned. But what happens to that \$50 million  
5 is -- in my view is up to the Company.

6 Q. Now, you have a copy of Mr. Dunn's rebuttal  
7 testimony?

8 A. Yes, I do.

9 Q. If you'd turn to Schedule JCD-2, please.

10 A. Yes, I'm there.

11 Q. And I take it that you've looked at this  
12 previously?

13 A. Yes.

14 Q. And that's two pages from the indenture  
15 involving this credit facility; is that right?

16 A. Yes.

17 Q. Now, turning to the second page,  
18 paragraph 2.3, do you have that in front of you?

19 A. Yes, I do.

20 Q. Can you read that into the record, please?

21 A. Paragraph 2.3, Purpose: The entire proceeds  
22 of each drawing shall be applied by way of investments  
23 and UNZ to be applied by UNZ to finance this  
24 investments in Australasian utility companies or to  
25 repay drawings in accordance with Clause 8.1, in each



1 case in accordance with all applicable law, including  
2 all regulatory approvals and authorizations.

3 Q. Okay. In the course of your preparation for  
4 this case, Mr. Hill, did you determine whether or not  
5 UtiliCorp might have an opinion of counsel that states  
6 that if these loans proceeds amounts are used for any  
7 purposes other than as stated in the agreement, that  
8 UtiliCorp would be in violation of the agreement and  
9 that the proper remedy would be forfeit? Are you  
10 familiar with that at all?

11 A. Am I aware of counsel's opinion in that  
12 regard?

13 Q. Yes.

14 A. No, I'm not. But you said the key word  
15 there. You said "amounts." And I'm not disagreeing  
16 with you that the amounts that are borrowed are  
17 expected to be invested.

18 My point is, is that the Company gets to  
19 decide how those monies are used before they're spent.  
20 I mean, you raise \$10 million. You're not going to  
21 spend the \$10 million in the next instance. That has  
22 to go somewhere.

23 It goes to the corporate accounts, and then  
24 the corporation invests ultimately \$10 million in  
25 New Zealand, and the -- or pays down the drawings in

1       accordance with Clause 8.1, whatever.  Sure, that's my  
2       point, as long -- as long as the amounts are spent,  
3       then the company has it.

4           Q.     And I realize you're not a lawyer, and I'm  
5       not asking you a question of law, but it's your  
6       understanding that the activity that you just  
7       described, the course of conduct you just described,  
8       would be permissible under the agreement?  That's your  
9       belief?

10       A.     That's my belief, yes.

11       Q.     Okay.  Thank you.

12                 What is your understanding of the nature of  
13       the New Zealand utility that we're talking about here?

14       A.     Well, as I said, it's two separate  
15       utilities, Auckland and one other town that I can't  
16       remember.  But the Company's wholly-owned subsidiary  
17       owns a 20 percent interest in one of utilities, and I  
18       believe it's a distribution utility, but I'm not  
19       exactly sure about that.

20       Q.     Okay.

21       A.     I'd have to reread the description of it.

22       Q.     But it's clearly not a division as we've  
23       discussed earlier?  It would fall under the category  
24       of a subsidiary of some sort.  Right?

25       A.     Well --

1 Q. Or would you call it something else?

2 A. No. There is a wholly-owned subsidiary that  
3 owns -- that has the equity interest in the operation.

4 Q. Okay. Then let me ask you this question:  
5 The operations themselves then are not a wholly-owned  
6 subsidiary of UtiliCorp; is that right?

7 A. That's right.

8 Q. Okay. Thanks.

9 Now, you may have said this earlier in your  
10 answer to one of my other questions, but do you know  
11 whether or not the funds related to that transaction  
12 ever did, in fact, reach the UtiliCorp treasury? Do  
13 you know that one way or the other for a fact?

14 A. I haven't seen evidence of that, and I  
15 haven't seen evidence that that's not the case.

16 As I said, in the Company's publications to  
17 shareholders and the financial community, I see no  
18 evidence that that's not the case. And the Company's  
19 exhibits, these exhibits that we just discussed on  
20 Australia and New Zealand, the Australia prospectus,  
21 by the way, is the one that says direct or indirect  
22 investment, not the New Zealand one.

23 Those also don't indicate to me anything,  
24 except as long as the amounts spent are spent, that  
25 the money -- that UtiliCorp does not have use of that

1 money.

2 Q. But back to my original question, you don't  
3 know -- and I think you admitted, one way or the  
4 other, whether or not the funds related to that  
5 transaction ever did, in fact, reach the UtiliCorp  
6 treasury? You just don't know?

7 A. I'm haven't got hard evidence that that's  
8 the case. It's my understanding that's how the  
9 corporate treasury works. And I have not seen any  
10 evidence presented by the Company in this proceeding  
11 that that is not the case.

12 Q. Okay. So I'm trying to make sure I  
13 understand your testimony.

14 A. I answered your question.

15 Q. Are you saying the answer is, yes, you  
16 believe that it did reach the Treasury, no, it didn't,  
17 or I'll give you a third choice, you just don't know?

18 A. My belief is, my understanding of corporate  
19 finance is, is that the Company has use of those funds  
20 when the money is raised.

21 Q. That's not my question. My question is, did  
22 this money ever reach the UtiliCorp treasury?

23 A. I believe it did.

24 Q. Okay. So now you're saying that -- your  
25 testimony is that this money did reach the UtiliCorp

1 treasury?

2 A. As I answered it a moment ago, I haven't  
3 seen hard evidence, the records of the treasury, where  
4 that money entered the treasury.

5 Q. Okay. That's fine.

6 I'm going to ask you a question about your  
7 surrebuttal testimony, Mr. Hill. I know it's marked  
8 as highly confidential, but I don't think that what  
9 I'm getting into will involve that.

10 A. There's only one number in the whole thing  
11 that is confidential.

12 Q. What page is that on, by the way, so I make  
13 sure --

14 A. It is on page -- it's pretty early in the  
15 testimony, I think. Page 4.

16 Q. Okay. Thank you.

17 I'm looking at page 18 of that testimony.  
18 Down on the beginning with a sentence on line 17, you  
19 say, "Thus, the Company has provided no support for  
20 their contention that UtiliCorp financial managers,  
21 when they spend a dollar for a transmission tower in  
22 Missouri or New Zealand, how they determine what  
23 capital source provided that dollar." Is that  
24 correct?

25 A. That's correct.

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1 Q. Would you agree with me that the New Zealand  
2 business is a totally separate operation from the rest  
3 of UtiliCorp?

4 A. Well, in that it's not interconnected with  
5 anything, obviously UtiliCorp, it is a physically  
6 separate operation, but it is -- the data that appears  
7 on the balance sheet, it's obviously a very big  
8 concern of the Company. And in that sense it's not  
9 separate from the umbrella company.

10 Q. Okay. I think you testified earlier,  
11 though, that it does have owners other than UtiliCorp?

12 A. It must. Somebody has got to own the other  
13 70 percent of it.

14 Q. But you don't know who they are?

15 A. No. And that information is not published  
16 in the annual report.

17 Q. Would you agree that it has management which  
18 is independent and separate from UtiliCorp?

19 A. I think that's reasonable to assume. I  
20 would have to reread the annual report to confirm my  
21 understanding.

22 Q. But right now you wouldn't have any reason  
23 to disbelieve that?

24 A. No.

25 Q. Would you agree that it has completely

1 separate and independent funds?

2 A. It has to have some other funds besides the  
3 debt issue that appears on the balance sheet of  
4 UtiliCorp in order to operate.

5 Q. And do you have any reason to believe that  
6 its funds are in no way mingled with UtiliCorp -- or  
7 commingled with UtiliCorp?

8 A. Do I have reason to believe that the other  
9 funds besides the debt issue are not commingled? Is  
10 that the question?

11 Q. Yes. Let's talk about the other funds  
12 first. That would be fine. Yes.

13 A. That is your question?

14 Q. Yes.

15 A. I think that is a reasonable assumption.

16 Q. Okay. But with respect to the debt we  
17 talked about earlier, I think you've gone various ways  
18 on whether or not that money ever hit the treasury.

19 What would your answer be with respect to  
20 those funds being commingled with UtiliCorp?

21 A. The other funds, other than the debt issue  
22 that appears on the balance sheet?

23 Q. No. You talked about those. What about the  
24 debt issue that appears on the balance sheet?

25 A. No. It's my position that those funds are  
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1 available to UtiliCorp.

2 Q. They're available. Have they been  
3 commingled with UtiliCorp?

4 A. When monies come into the corporate  
5 treasury, those monies come in from retained earnings  
6 from debt issue equity issuances, and those funds are,  
7 in effect, commingled. And when those monies go out,  
8 which is really one of our fundamental positions in  
9 this case, it's not possible to color code those  
10 dollars and tell where those dollars came from.

11 Q. Okay. And I appreciate that. But I think  
12 earlier after going around some time, you said that  
13 you really couldn't say for sure whether or not those  
14 funds had reached the UtiliCorp treasury; is that  
15 right?

16 A. What I said is the Company hasn't offered  
17 and I haven't seen definitive evidence that those  
18 monies from New Zealand came in -- those dollars from  
19 New Zealand came into the corporate treasury. I  
20 didn't testify that I don't believe that's the case.  
21 I do believe that's the case, and that's my position.

22 Q. So your testimony now is that those funds,  
23 in fact, did reach the UtiliCorp Treasury. Is that  
24 right?

25 A. The testimony as it has always been, that --  
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1           Q.     Excuse me. I'm a little confused, because I  
2     think I think I've heard it several different ways  
3     this morning.

4           A.     I don't think so.

5           Q.     Okay. Why don't you tell us once and for  
6     all, did the funds related to that transaction ever  
7     reach the UtiliCorp Treasury?

8           A.     I believe they did.

9           Q.     Okay. And what evidence do you have that  
10    that happened?

11          A.     My evidence is, as I said before, my  
12    understanding of corporate finance and the fact that I  
13    have not seen in the Company testimony or exhibits or  
14    responses to data requests any evidence to indicate  
15    the contrary.

16                 If there is records within UtiliCorp that  
17    shows definitively that those New Zealand dollars are  
18    not allowed out of the country or did not come into  
19    the corporate treasury, it should be very simple for  
20    the Company to produce those documents. There has  
21    been no such production in this case.

22          Q.     Okay. Is it your understanding that the  
23    New Zealand electric company is similar to Aquila in  
24    the sense that its not a wholly-owned subsidiary of  
25    UtiliCorp; others have an ownership interest in it?

1 Is that what you said earlier?

2 A. I'm not sure that that's -- I'd have to  
3 check and ascertain whether or not that's the status  
4 of Aquila. That it is the status of New Zealand.

5 Q. And you don't know whether or not that's the  
6 status of Aquila?

7 A. I'd have to check.

8 Q. Back on what I think is Exhibit 79, which is  
9 page 45 from the balance sheet -- excuse me -- from  
10 the annual report, there's a line there, we were  
11 talking about the New Zealand credit facility. Right  
12 below that there's a line that talks about the  
13 Australian Denominated Credit Facility due July 20,  
14 2000?

15 A. Yes.

16 Q. And that is in what amount?

17 Does it show there on the -- I'm not trying  
18 to trick you or anything. What's your understanding  
19 of the amount of that?

20 A. For the Australian Denominated Credit  
21 Facility?

22 Q. Yes, sir.

23 A. 1996, it was 237 million.

24 Q. Have you seen portions of the Indenture of  
25 the Australian Credit Facility?

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1           A.     Yes. We referred to that in Mr. Dunn's  
2     rebuttal testimony.

3           Q.     And would you agree that the Australian  
4     business operation is not a wholly-owned subsidiary of  
5     UtiliCorp?

6           A.     Yes, I would.

7           Q.     Okay. And would you agree that the  
8     Australian operation has its own management?

9           A.     That's reasonable, yes, to believe that.

10          Q.     And would you agree that it has its own  
11     accounts that are totally separate from those of  
12     UtiliCorp?

13          A.     Let me retract that statement. I think that  
14     UtiliCorp does manage that utility operation in  
15     Australia. They get a management fee for managing  
16     that operation.

17          Q.     Okay. So your testimony now would be that  
18     the Australian operation doesn't have its own  
19     management?

20          A.     I didn't -- let me put it this way:  
21     I recall reading in the annual reports and the 10-Ks  
22     that the Company receives a management fee for  
23     managing the operations in Australia. Whether or not  
24     there are other people that also work, I don't know.

25          Q.     You don't know whether or not the company --

1 the Australian company would have its own management,  
2 you don't know one way or the other?

3 A. I don't know whether they would have  
4 additional management personnel.

5 Q. Do you know whether or not any of those  
6 funds from Australia are commingled with other  
7 UtiliCorp funds?

8 A. I think the answer would be the same,  
9 because we've gone over with New Zealand. My belief  
10 is that those funds are available to the corporate  
11 treasury. That debt appears on the balance sheet of  
12 UtiliCorp.

13 So my position would be the same.

14 Q. Now, back earlier I'd asked you a question,  
15 and in response you changed your answer to an earlier  
16 question. So let's go back to the original question.

17 Would you agree that the Australian  
18 operation has its own accounts?

19 A. What do you mean?

20 Q. Well, what do you understand the meaning of  
21 the term "accounts" to be?

22 A. Accounts are -- is an accounting term for a  
23 departmentalization of costs or expenses.

24 Q. And could it also be financial accounts?

25 A. Yes.

1           Q.     Okay.  And what is your understanding as to  
2     whether or not the Australian operation has any of its  
3     own accounts as you have defined them?

4           A.     I don't believe I've defined own accounts.

5           Q.     Well, you just defined the term "accounts,"  
6     didn't you?

7           A.     Well, to you in response to your question,  
8     but I thought you were talking about in my testimony.

9           Q.     No.  I'm asking, what is your definition of  
10    the terms "accounts" in response to my question?

11          A.     I think I defined it.

12          Q.     Okay.  Then based on your definition, is it  
13    your testimony that the Australian operation has any  
14    such accounts?

15          A.     Well, I would think that there are some  
16    accounting entries having to do with the Australian  
17    operation.  Obviously there are, because the debt of  
18    that operation appears on the balance sheets of the  
19    company, and there had to be an accounting entry in  
20    order for that to happen.

21          Q.     Would there be any financial accounts?

22          A.     Well, the debt would be a financial account.

23          Q.     And would you agree that those accounts are  
24    totally separate from other UtiliCorp accounts?

25          A.     No.

1           You have to define what "separate" means. I  
2 mean, there's a separate --

3           Q.     Well, you can define it.

4           A.     -- operation that is involved in entering an  
5 account, a debt or a credit for a particular, say,  
6 debt issuance. And that's a separate physical  
7 operation from entering a different kind of debt  
8 issuance. But it appears on the books of the Company,  
9 and it's not separate in that sense.

10          Q.     Would there be any, to your knowledge,  
11 separate financial accounts of the Australia  
12 operation, separate from those that UtiliCorp might  
13 otherwise have?

14          A.     I think it would be reasonable to believe  
15 that there are separate accounts, yes. I'm sure there  
16 are separate accounts within the Company.

17          Q.     Do you know whether or not UtiliCorp used  
18 any of the proceeds of the loan involving the  
19 Australian properties based on what you have seen from  
20 the indenture for any purpose other than the purposes  
21 outlined in the loan agreement?

22          A.     I don't think that the amount of monies  
23 ultimately spent by UtiliCorp in Australia are  
24 different than agreed to. I think the timing of the  
25 spending and the ability of the Company to access

1       those funds is documented in my testimony.

2           Q.     Do you know that if UtiliCorp used any of  
3       those proceeds for any purpose other than outlined in  
4       the loan agreement, that it would be in default?

5           A.     I'm not aware of that.  It's my  
6       understanding is the Indenture that we discussed in  
7       Schedule JCD-1, page 1 of 2 and 2 of 2 of Mr. Dunn's  
8       rebuttal testimony, says, with use of proceeds --

9           Q.     Excuse me just for a second, so we're clear.

10          A.     I'm answering your question.

11          Q.     I know.  I want to know what you're  
12       referring to.  That's all.

13          A.     Okay.  Mr. Dunn's rebuttal testimony.

14          Q.     Rebuttal testimony.

15          A.     Schedule JCD-1 --

16          Q.     Right.

17          A.     -- page 2 of 2?

18          Q.     Okay.  Thank you.  I appreciate that.  
19                 And you're reading from a paragraph there?

20          A.     Yes.  I'm reading from Use of Proceeds.

21          Q.     Okay.

22          A.     "The borrower shall use the net proceeds of  
23       all advances provided under this agreement for:"  In  
24       paragraph B, It says, "Subject as set out below, the  
25       acquisition, directly or indirectly, of any other

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1 similar investment in a utility or energy related  
2 corporation in Australia . . .", et cetera, et cetera.

3 So the language directly or indirectly seems  
4 to me to give the Company wide latitude.

5 Q. You know, if I knew, just as an aside  
6 here -- I mean, that was going to be my next question.  
7 It's almost like I cross-examined you 150 times  
8 previously. This is going to go on pretty fast.  
9 Thank you.

10 We talked about -- I don't know that we  
11 talked about the West Kootenay --

12 A. Yes, we did.

13 Q. -- financing issue.

14 Did we?

15 What do those three total up, West Kootenay,  
16 New Zealand and Australia? Would you agree that at  
17 least on the Exhibit 78 they would total  
18 approximately -- why don't you take a look and tell  
19 me.

20 A. Exhibit 79 really is the exhibit where you  
21 can total them up, and it's 360, \$370 million, in that  
22 neighborhood.

23 Q. Okay. And what percentage of the total debt  
24 does that constitute, roughly?

25 A. Oh, it's 370 divided by 1,400.



1 Q. What is that? I'm not real good in math.

2 A. 25 percent.

3 Q. Okay. That's fine. Thanks.

4 Now, also on that Exhibit 79, up under the  
5 category of Senior Notes, do you see one entitled  
6 Aquila Southwest Energy, 8.29 percent Series, due  
7 September 15, 2002?

8 A. Yes.

9 Q. And how much of that series is outstanding,  
10 do you know?

11 A. 75 million.

12 Q. Okay. Now, I asked you earlier about  
13 Aquila, and you said you were uncertain as to whether  
14 or not it was a wholly-owned subsidiary. Is that  
15 right?

16 A. That's right.

17 Q. So you can't answer that question one way or  
18 the other? If I said, would you agree it's not a  
19 wholly-owned subsidiary, you couldn't answer that?

20 A. I think that I -- I can't answer that  
21 definitively. If you give me a minute, I can look in  
22 the manual report and find it, but I think it's  
23 70 percent.

24 Q. Sure. Why don't you do that.

25 JUDGE DERQUE: Let's be accurate.

1 THE WITNESS: Okay. I have the information.

2 BY MR. SWEARENGEN:

3 Q. Okay. Let me just ask you a couple of  
4 questions and see if we can get at it that way.

5 Would you agree that Aquila Southwest is not  
6 a wholly-owned subsidiary of UtiliCorp?

7 A. It's not as easy an answer as I thought it  
8 was going to be.

9 At page 4 of the 1996 10-K the company lists  
10 its divisions and other investments and its ownership.  
11 For example, it lists the Oasis Pipeline Company which  
12 it recently acquired, has a 40 percent interest. It  
13 says, All other gas marketing investments it owns 100  
14 percent. I know Aquila is primarily gas marketing.

15 Q. So you don't know. Is that a fair  
16 statement?

17 A. No. What I'm saying is that it's not clear.  
18 It appears that Aquila is not 100 percent owned by  
19 UtiliCorp.

20 Q. Okay. So then the answer to my question  
21 would be, it's not a wholly-owned subsidiary of  
22 UtiliCorp?

23 A. I think that's correct.

24 Q. Okay. Good.

25 Now, let me ask you this question: Do you  
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1 have any independent knowledge of whether or not  
2 UtiliCorp had a public offering of 19 percent of the  
3 stock of that company some time ago?

4 A. Would you repeat your question?

5 Q. Do you have any knowledge as to whether or  
6 not UtiliCorp had a public offering of 19 percent of  
7 the stock of that company some time ago?

8 A. No, I'm not familiar with that.

9 Q. Okay. Do you know whether or not Aquila  
10 Southwest is publicly traded?

11 A. I do not.

12 Q. Do you know whether or not Aquila Southwest  
13 has its own lines of credit?

14 A. I know that it issued its own debt, and my  
15 understanding, that all of the short-term debt  
16 arrangements are made through UtiliCorp. If it has  
17 its own line of short-term debt credit, I'm not aware  
18 of it, and I haven't seen evidence of it in this  
19 proceeding.

20 Q. Okay. But you are aware that it has its own  
21 other types of credit facilities?

22 A. It has issued \$100 million debt issuance.  
23 The Company lists Aquila as \$1.4 billion in assets in  
24 1996. So we must assume that the rest of the assets  
25 are funded by UtiliCorp.

1 Q. And what was the nature of that financing  
2 you just described?

3 A. What was the nature of the debt?

4 A. Yes.

5 A. It was a debt issuance, a \$100 million debt  
6 issuance.

7 Q. A long-term debt?

8 A. Yes.

9 Q. Okay. Do you have any knowledge as to  
10 whether or not that debt is subject to an indenture  
11 which made Aquila Southwest responsible for protection  
12 of the funds and the proceeds of the loan?

13 A. I'm not aware of that.

14 Q. Okay. Do you have any knowledge of the role  
15 that UtiliCorp either played or did not play in the  
16 issuance of that debt?

17 A. I'm not.

18 Q. Do you have any knowledge one way or the  
19 other as to whether UtiliCorp is responsible to  
20 guarantee or otherwise responsible for that debt?

21 A. I'm not.

22 Q. Would you agree that this debt appears on  
23 this line of Exhibit 79 only because of generally  
24 accepted accounting principles?

25 A. Only because of generally accepted

1       accounting principles? I would agree with that. I'm  
2       curious about the term "only," but I would agree with  
3       what you said.

4           Q.     Thanks.

5                    If I were to add the 75 million of Aquila  
6       debt to the -- I think, what was it, 380 some million  
7       of international debt that you talked about earlier,  
8       would I get 459 million of debt?

9           A.     You certainly could.

10          Q.     Okay. And that would be debt not available  
11       to UtiliCorp, or is that the issue here?

12          A.     That's the issue here.

13          Q.     Okay.

14          A.     That's really not the issue here, actually.

15          Q.     Would you say that that debt is not  
16       available to UtiliCorp, all of that debt that I just  
17       described, the Aquila debt, plus the international  
18       debt?

19          A.     No, I wouldn't say that.

20          Q.     Would you say it is available to UtiliCorp?

21          A.     Yes.

22          Q.     Okay. And all of that debt that we just  
23       talked about would represent more than 30 percent of  
24       the debt outstanding? I think earlier you said what  
25       we totaled up is 25 percent, and when you add the

1     Aquila Southwest to that, would that get us up to  
2     around 30 percent?

3           A.     I'll accept that, sure.

4           Q.     Okay.  And if you back that debt out of the  
5     consolidated capital structure, do you know what the  
6     consolidated equity ratio of UtiliCorp would be?

7           A.     It wouldn't represent the consolidated  
8     capital structure, because you also have to back out  
9     the equity.  And if you back out the equity of those  
10    other operations, which are electric operations in  
11    which your witness said ought to be capitalized with  
12    47 percent equity, you're going to wind up a with a  
13    UtiliCorp consolidated capital structure which has an  
14    equity ratio well below 40 percent.

15          Q.     Back to my question --

16          A.     I discussed that in surrebuttal.

17          Q.     -- if you did back the debt out, though,  
18    what would the consolidated equity ratio be?

19          A.     It wouldn't be meaningful, because you can't  
20    simply eliminate the debt of a subsidiary or a  
21    division without also eliminating the equity.  If you  
22    just took the debt out, you'll get a nonsensical  
23    number.

24          Q.     I understand that.

25                 What would that nonsensical number be from  
                    824

1 your standpoint?

2 A. Well, if -- it wouldn't mean anything. It  
3 would be probably in the mid-40 percent range or  
4 something of that nature.

5 Q. Okay. Thank you.

6 MR. SWEARENGEN: Would it be appropriate to  
7 ask for a short recess?

8 I might be able to shorten this up a little.

9 JUDGE DERQUE: Certainly.

10 We'll take a recess of roughly 15 minutes.

11 Is that enough, Mr. Swearengen?

12 MR. SWEARENGEN: Thank you.

13 JUDGE DERQUE: We're off the record.

14 (A recess was taken.)

15 JUDGE DERQUE: We're back on the record.

16 Mr. Swearengen.

17 MR. SWEARENGEN: Yes. Are you ready for me  
18 to proceed, your Honor.

19 JUDGE DERQUE: Yes, sir.

20 MR. SWEARENGEN: Thank you very much.

21 BY MR. SWEARENGEN:

22 Q. Mr. Hill, I have a couple more questions to  
23 pose to you with respect to what I will call the  
24 capital structure issue, and I've got a copy of a  
25 Staff data request which I'm going to show you.

1           It's Data Request No. MPSC-148 issued in  
2       this case, Date of Request 6-12-97. I'm going to have  
3       this marked for identification.

4           MR. SWEARENGEN: I don't have copies now,  
5       but I will, of course, furnish copies, your Honor.

6           Could I have that marked at this time?

7           JUDGE DERQUE: Yes. This will be marked as  
8       Exhibit 80, identified as a one-page document, Staff  
9       Data Request No. 148.

10          We're off the record.

11          (EXHIBIT NO. 80 WAS MARKED FOR  
12       IDENTIFICATION.)

13          JUDGE DERQUE: We're back on the record.

14       BY MR. SWEARENGEN:

15           Q.     Mr. Hill, I'm handing you what has been  
16       marked for purposes of identification as Exhibit 80, a  
17       one-page document which is entitled UtiliCorp United,  
18       Inc., Case ER-97-394, Data Request MPSC-148.

19           And I'm not going to ask you to read that  
20       into the record or anything of that sort, but the  
21       first question in that data request is provide the  
22       capital structure for UtiliCorp United at December  
23       1996. Is that correct?

24           A.     Yes.

25           Q.     And then there are five other requests



1 contained in that data request. Is that not true?

2 A. That's right.

3 Q. And then is it your understanding that below  
4 those questions is the response that was provided by  
5 UtiliCorp?

6 A. That appears to be the case.

7 Q. Okay. Let me ask you this question then,  
8 Mr. Hill: In connection with the preparation of your  
9 testimony for this case, what consideration, if any,  
10 did you give to the information contained on that data  
11 request response?

12 A. Well, um, I don't recall reviewing this  
13 particular data response. I'm sure I saw it, but I  
14 don't recall the details of it.

15 Q. Okay. That's fine. Thank you.

16 MR. SWEARENGEN: That's all I have with  
17 respect to that, and I'll get the copies made, and I  
18 would offer it into evidence at this time.

19 MR. MILLS: I'd like to reserve my right to  
20 object once I've seen a copy of it.

21 MR. WOODSMALL: Yes.

22 JUDGE DERQUE: Can I see this?

23 Thank you, Mr. Swearengen.

24 Would you please withhold your offer of  
25 evidence until we've all been furnished a copy of this

1 exhibit?

2 MR. SWEARENGEN: Absolutely, I'd be happy  
3 to.

4 JUDGE DERQUE: I'm going to mark your  
5 exhibit so we will know what it is. This is No. 80.

6 When you furnish us with copies, you may  
7 offer it and we'll go from there.

8 MR. SWEARENGEN: Thanks.

9 BY MR. SWEARENGEN:

10 Q. A couple of other questions, Mr. Hill.

11 I guess it's page 23 of your direct  
12 testimony -- make sure I'm at the right place. Do you  
13 have that in front of you?

14 A. I will in a moment.

15 Q. It may be your rebuttal.

16 A. I have 23 of my direct.

17 Q. Let me check.

18 A. I don't think the rebuttal has 23 pages.

19 Q. I think what my question is, on 23, I want  
20 to make sure I understand.

21 Is that where you describe how you selected  
22 your group of companies for purposes of calculating a  
23 cost of equity?

24 A. Yes. I adopted your witness's group except  
25 for one company.

1 Q. And what company was that that you didn't --

2 A. It was IPALCO.

3 Q. Okay. Now, I know you've testified in I  
4 think you said over 150 different regulatory  
5 proceedings.

6 Have you ever received any criticism from a  
7 regulatory commission through a report and order or  
8 other decision which was critical of your work with  
9 respect to the way you've gone about selecting  
10 companies?

11 A. Yes.

12 Q. Okay. And can you tell us about that?

13 A. I'm not sure that that particular issue was  
14 dealt with. I think, however, the most negative  
15 result I've ever received was in Indiana.

16 And Indiana Commission order -- I believe it  
17 was for -- I think it was an American Waterworks  
18 Company, probably Indiana American. It was late '80s,  
19 I believe. And it was an ALJ who requested that the  
20 parties provide suggested orders, and that ALJ adopted  
21 the company's suggested order and was very negative  
22 towards me, very personally, the jargon.

23 And there have been a couple of other  
24 specific orders -- I can't recall the jurisdictions --  
25 of where they didn't accept my recommendations.

1 Q. Okay. And back to that Indiana case, can  
2 you give us a little more detail on when that was?

3 A. When it was?

4 If you like, I could supply the exact case  
5 number and that sort of thing. I think it was late  
6 '80s.

7 Q. Okay. And you think it involved the  
8 Missouri American Water Company?

9 A. Not Missouri.

10 Q. Excuse me.

11 A. Indiana.

12 Q. Indiana. Right.

13 And my question was whether or not  
14 commission had criticized your work in the past for  
15 the way you've gone about selecting companies. Was  
16 that the criticism in that order?

17 A. I think that was part of it. They  
18 criticized everything I did. So that includes the  
19 whole process. So I was pretty sure that's true.

20 Q. Any other cases in Indiana or any other  
21 jurisdictions where you appeared where your work has  
22 been criticized?

23 A. Yes. As I said, there have been other  
24 criticisms. The Maryland Commission disagreed with my  
25 dividend yield process once. Let me think.

1 I can't bring another to mind.

2 I know there's been another specific mention  
3 of a disagreement on another issue regarding cost of  
4 capital estimates.

5 Q. Have you in the past ever testified that the  
6 discounted cash flow model is inaccurate?

7 A. Is inaccurate?

8 Q. Yes.

9 A. Well, first, I have to say that --

10 Q. Well, excuse me. That would call for a yes  
11 or no answer. Have you ever testified that way?

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

13 MR. SWEARENGEN: Okay. That's all I have.

14 Thank you.

15 THE WITNESS: -- in regards to those kind --

16 MR. SWEARENGEN: Your Honor --

17 JUDGE DERQUE: I'm going to let him qualify  
18 that answer, Mr. Swearengen. We're talking about the  
19 DCF model. You don't think --

20 THE WITNESS: Right.

21 JUDGE DERQUE: Let me go over this: You  
22 don't think you have ever testified that it was  
23 inaccurate, but you were going to put a qualification  
24 in there. Let's stay within the range of the  
25 question.

1           THE WITNESS: But all equity cost estimation  
2 models are inaccurate. I think that the DCF is the  
3 least inaccurate or the most accurate of the bunch.

4           JUDGE DERQUE: Thank you.

5           MR. SWEARENGEN: That's all I have. Thanks.

6           JUDGE DERQUE: Thanks, Mr. Swearengen.

7           Chair Lumpe?

8           CHAIR LUMPE: Just one question, Mr. Hill.

9           QUESTIONS BY CHAIR LUMPE:

10          Q. The issue here of the consolidated capital  
11 structure versus an assigned capital structure --

12          A. Yes.

13          Q. -- has this been an issue in previous  
14 UtiliCorp MoPub cases?

15          A. Yes, it has.

16          Q. And what was the agreed position in those  
17 cases?

18          A. Um, it's gone both ways.

19                 In the 1990 case the Commission upheld the  
20 use of a consolidated capital structure. And in the  
21 1993 case it's kind of an unusual case, because it was  
22 a partially settled case. And in that case -- it's my  
23 understanding the Staff didn't brief the case, and  
24 they didn't address the issue of capital structure  
25 because they had settled with the Company on a final

1 number.

2 Because of the fact that it wasn't a  
3 completely settled case, the Commission wrote a  
4 complete order in which they adopted the Company's  
5 assigned capital structure.

6 But it's also my understanding that this  
7 Commission has taken the position at the Federal level  
8 that a consolidated capital structure is a preferred  
9 way to go.

10 So the Commission has been on both sides of  
11 the issue, and this will be the definitive case in  
12 that regard.

13 CHAIR LUMPE: Thank you very much.

14 JUDGE DERQUE: Commissioner Murray?

15 COMMISSIONER MURRAY: Thank you. I have  
16 just a couple of questions.

17 QUESTIONS BY COMMISSIONER MURRAY:

18 Q. And I apologize because we've probably gone  
19 over this some of the times that I've been out of the  
20 hearing room.

21 The reason that Aquila debt was included,  
22 can you go over that briefly?

23 A. Yes.

24 If I can expand your question to include all  
25 of the debt that was referred to, the Aquila debt, as

1 well as the foreign debt.

2 Q. Okay.

3 A. As I said to Mr. Swearingen, the issue of  
4 foreign debt is really -- is really not the focus  
5 here. The company wants it to be, but that's not  
6 really the focus.

7 What we're trying to do is estimate the  
8 overall cost of capital -- appropriate overall cost of  
9 capital for this company. And we look -- because  
10 Missouri Public Service doesn't issue its own debt, it  
11 doesn't issue its own equity. All of the capital is  
12 supplied by UtiliCorp. Therefore, we have to look to  
13 UtiliCorp capital structure in order to determine  
14 those cost rates.

15 We look at the market for equity cost rates,  
16 we look at similar companies and get equity cost  
17 rates, but for indebted cost rates, debt cost rates,  
18 we have to look to the parent company.

19 Now, the parent company includes in its  
20 system of accounts all of that debt, the Aquila debt,  
21 the debt from New Zealand, the debt from Canada and  
22 the debt from Australia.

23 Those monies are in the accounts of  
24 UtiliCorp. Those monies comprise the pool of funds  
25 that UtiliCorp has to invest in its operations. And

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1 using those monies, all of those monies, we can assess  
2 what the embedded cost of debt for UtiliCorp is. And  
3 that provides us the best estimate in my view of an  
4 embedded debt cost to use for regulatory purposes in  
5 this case.

6 And that's a different position than the  
7 Company's, which wants to use an assigned capital  
8 structure. But they want to use debt costs that are  
9 related to UtiliCorp, and there's a definite mismatch  
10 with that, because their assigned capital cost is not  
11 related to the UtiliCorp. It's different.

12 So the reason that I include the Aquila  
13 debt, as well as the foreign debt, is because those  
14 are all monies that appear on the books of account of  
15 UtiliCorp. And the best way to estimate the embedded  
16 cost of debt of the funds available to Missouri Public  
17 Service is to look at the consolidated capital  
18 structure of UtiliCorp.

19 COMMISSIONER MURRAY: Thank you.

20 JUDGE DERQUE: Chair Lumpe, do you have  
21 anything else?

22 CHAIR LUMPE: No.

23 JUDGE DERQUE: Okay. Recross based on  
24 Commission questions?

25 Mr. Mills?

1 MR. MILLS: Just one.

2 RECROSS-EXAMINATION BY MR. MILLS:

3 Q. In response to a question by Chair Lumpe,  
4 you referred to the '93 Missouri Public Service case.

5 A. Yes.

6 Q. Is that correct?

7 Are you aware that that case is still on  
8 appeal in circuit court?

9 A. I found out yesterday that it's still on  
10 appeal. So it's -- I guess it's not been finally  
11 decided.

12 MR. MILLS: That's all I have. Thanks.

13 JUDGE DERQUE: Mr. Finnegan?

14 MR. FINNEGAN: I have no questions.

15 JUDGE DERQUE: Mr. Swearengen

16 MR. SWEARENGEN: Thank you, your Honor.

17 RECROSS-EXAMINATION BY MR. SWEARENGEN:

18 Q. One more follow-up with respect to that 1993  
19 UtiliCorp rate case in which the Commission found that  
20 the divisional capital structure of MPS was the  
21 appropriate capital structure.

22 You are aware, are you not, that the Office  
23 of Public Counsel represented by Mr. Mills here did,  
24 in fact, litigate that case and that issue before the  
25 Public Service Commission?

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1           A.     That's my understanding.

2                     MR. SWEARENGEN:   Okay.   Thanks.   That's all  
3   I have.

4                     JUDGE DERQUE:   Redirect, Mr. Woodsmall?

5                     MR. WOODSMALL:   Yes.

6   REDIRECT EXAMINATION BY MR. WOODSMALL:

7           Q.     Let's work backwards a little bit.

8                     You were asked some questions regarding  
9   whether your work has ever been criticized in other  
10   jurisdictions.   Do you recall those questions?

11          A.     Yes.

12          Q.     In order to paint a complete picture, have  
13   your recommendations ever been accepted or praised by  
14   a commission?

15          A.     Yes.   More often than not the Commission  
16   will -- in the order will present the testimony of the  
17   parties and then say, Given that we think this.   And  
18   that's more often the case, and really they don't talk  
19   about the individual -- the merits or demerits of the  
20   individual witnesses, but there have been case where,  
21   as I said to Mr. Swearengen, the commission have been  
22   pleased with my work, but there have also been cases  
23   where they have been, specifically in the states of  
24   Arizona and Washington and Vermont, those commissions  
25   all singled out my analysis as the most reliable and

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1       relied on.

2           Q.     And you would say that those instances far  
3       outweigh the number of instances in which the  
4       commission has been critical?

5           A.     I believe that my testimony has been well  
6       received.

7           Q.     You were asked several questions regarding  
8       the international debt issuances of UtiliCorp and its  
9       international operations. Do you recall those  
10      questions?

11          A.     Yes.

12          Q.     If there was evidence that, for instance,  
13      New Zealand or the Australian dollars received from  
14      these debt issuances didn't enter the UtiliCorp  
15      treasury, would you have expected to see that somehow  
16      presented in testimony?

17          A.     Yes.

18                 As I said to Mr. Swearengen, one of the  
19      reasons for my belief that the Company follows  
20      standard corporate practice, which is to -- when they  
21      issue debt, that money is collected, say \$100 million,  
22      that money comes into the corporate treasury and then  
23      is used for general corporate purposes. You can't  
24      trace those dollars.

25                 If some other situation existed, if the

1 UtiliCorp board was all going to be arrested if that  
2 money left Australia or they had proof that those  
3 monies never came into the treasury, it would be --  
4 seem to me a simple matter to have their witness  
5 present such proof in his rebuttal or surrebuttal  
6 testimony. And we've already discussed what he has  
7 presented, and I don't believe that that is evidence  
8 of their position.

9 Q. And they had opportunity, that is, you  
10 didn't bring up this point in surrebuttal so they were  
11 foreclosed from that opportunity?

12 A. Yes. This was an issue from the get-go.

13 Q. Okay. Can you tell me, you were asked  
14 questions about backing out the international and  
15 Aquila debt in calculating the consolidated capital  
16 structure after backing out that debt. Can you tell  
17 me why it's not appropriate to back out just the debt?

18 A. Well, because you don't finance a company  
19 with just debt. I mean, the Aquila debt we're talking  
20 about is \$100 million, or was originally. Now it's  
21 down to 75.

22 And they list \$1.4 billion of assets for  
23 Aquila. Obviously that's not -- the Company is not  
24 capitalized with \$75 million of debt.

25 And the same is true for the utility

1 operations in Canada and Australia and New Zealand.

2 So if you're going to back out a piece of  
3 the capital, then you need to back out the other parts  
4 of the capital also. And if you do that, what you  
5 find is the resulting consolidated capital structure  
6 is -- would have an equity ratio below the roughly  
7 40 percent that we recommend.

8 So if you followed the Company's advice and  
9 got rid of that debt, the proper way to treat it is  
10 getting rid of the equity also. And if you did that,  
11 you would have a more leveraged capital structure than  
12 the Staff recommends.

13 So that indicates that our recommendation --  
14 capital structure recommendation is conservative in  
15 the company's behalf.

16 Q. Can you tell me whether a rating agency  
17 would consider all debt, including the international  
18 and Aquila debt, when assigning bond ratings?

19 A. Certainly. It appears on the Company's  
20 books of account. It's recorded that way because of  
21 GAAP, and those -- those debt costs are very real.

22 They impact the financial risk of the  
23 Company, and they're considered in assigning bond  
24 ratings. The bond ratings then impact the cost rate  
25 at which a company is able to borrow and the cost of

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1 capital to -- ultimately to Missouri Public Service.

2 Q. So the cost of debt that you calculated in  
3 this case was based upon a market which considered all  
4 UtiliCorp debt including international and Aquila?

5 A. Yes. And the cost of debt that I  
6 calculated, by the way, is very similar to the overall  
7 cost of debt that the Company reports in its  
8 statistical supplement that it publishes with its  
9 annual report.

10 Q. Do you still have Exhibit 77 before you? It  
11 was entitled Financial Theory and Corporate Policy by  
12 Copeland and Weston.

13 A. Yes, I do.

14 Q. And I know you were asked to read just a  
15 portion of this, and you haven't read the rest of the  
16 main -- the document, if you will, but just from the  
17 portion that you have read, can you tell me why the  
18 concept expressed there does not apply to the case in  
19 hand?

20 A. Well, the concept does and doesn't apply to  
21 the case at hand.

22 It doesn't apply in the way that the Company  
23 would like for it to. In theory, though, I have no  
24 problem with the concept. And to refresh your memory,  
25 here is what we're talking about.

1           This concept is that you capitalize  
2     operations of different risks differently. If you  
3     have a very risky operation, you're not going to  
4     capitalize it with a lot of debt, because if it goes  
5     in the tank, then you're stuck with the debt payments  
6     and you can default and the debtholders can shut you  
7     down.

8           So a risky operation, you're going to  
9     capitalize on more equity and less debt. And vice  
10    versa, a very stable operation, you're going to  
11    stabilize with more debt and less equity.

12          That's basically what this is saying, and I  
13    certainly have no problem with that. And different  
14    operations will have different requirements. And  
15    there was a term brought up in this quote, as well as  
16    of the testimony of Mr. Dunn, the carbon copy issue.

17          Well, here's why this theory works in favor  
18    of the Staff and not in favor of the Company. When I  
19    reviewed the capital structures existing today in the  
20    market for a triple B-rated electric utilities, that  
21    average capital structure was virtually identical, a  
22    carbon copy, if you will, if I can borrow that phrase,  
23    of UtiliCorp's consolidated capital structure.

24          So that tells me that the capital structure  
25    for UtiliCorp, the consolidated capital structure, is



1 the appropriate capital structure to use for setting  
2 rates for Missouri Public Service, because UtiliCorp  
3 is a triple B-rated company. It is triple B rated  
4 because it has a capital structure consisting of about  
5 40 percent equity and 60 percent fixed income capital.

6 And so that determines the cost rate of the  
7 debt capital available to Missouri Public Service.  
8 Therefore, we look to that capital structure to set  
9 rates for Missouri Public Service.

10 Because this theory that they brought up in  
11 Exhibit 77 supports the Staff's position because the  
12 risk of a triple B-rated electric results in a capital  
13 structure in the marketplace which is a carbon copy of  
14 UtiliCorp's consolidated capital structure.

15 MR. WOODSMALL: I have no further questions.

16 JUDGE DERQUE: Thank you, Mr. Woodsmall.

17 Thank you, Mr. Hill.

18 THE WITNESS: Thank you.

19 (Witness excused.)

20 JUDGE DERQUE: I note that Exhibits 77  
21 through 80 have not been offered, Mr. Swearingen.

22 MR. SWEARENGEN: Yes. I was going to offer  
23 them.

24 JUDGE DERQUE: I was just stating that. I'm  
25 obviously not going to force you to offer them.

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1                   MR. WOODSMALL: Staff has no objections to  
2 any of the four.

3                   MR. SWEARENGEN: Are we on the record, your  
4 Honor? I can do that now.

5                   JUDGE DERQUE: Yes. It's strictly up to  
6 you.

7                   MR. SWEARENGEN: Okay. At this time I would  
8 offer into evidence Exhibits 77, 78 and 79.

9                   JUDGE DERQUE: Any objection to the evidence  
10 of Exhibits 77, 78 or 79?

11                  MR. WOODSMALL: No objections to those  
12 three.

13                  JUDGE DERQUE: Hearing no objection, they  
14 will be admitted.

15                  (EXHIBIT NOS. 77 THROUGH 79 WERE RECEIVED  
16 INTO EVIDENCE.)

17                  MR. SWEARENGEN: Now, your Honor, with  
18 respect to Exhibit 80, it was my understanding that  
19 the bench did not want me to offer that until the  
20 other parties had an opportunity to review that data  
21 request response.

22                  JUDGE DERQUE: Until we all are furnished  
23 copies.

24                  MR. SWEARENGEN: Right.

25                  JUDGE DERQUE: And have an opportunity to  
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1       see it.

2               MR. WOODSMALL:  And I'll make those at the  
3       next break.

4               MR. SWEARENGEN:  Thank you, Judge.

5               JUDGE DERQUE:  Mr. Mills.

6               MR. MILLS:  Yes.  At this time I'd like to  
7       call Mark Burdette to the stand, please.

8               JUDGE DERQUE:  I have three pieces of  
9       testimony for Mr. Burdette.  None of them are  
10       confidential.  Is that correct?

11              MR. MILLS:  That is correct.

12              JUDGE DERQUE:  Okay.  The direct will be 81,  
13       the rebuttal will be 82 and surrebuttal will be 83.

14              And we're off the record.

15              (EXHIBIT NOS. 81 THROUGH 83 WERE MARKED FOR  
16       IDENTIFICATION.)

17              JUDGE DERQUE:  We're on the record.

18              (Witness affirmed.)

19              JUDGE DERQUE:  Mr. Mills.

20              MR. MILLS:  Thank you, sir.

21       MARK BURDETTE testified as follows:

22       DIRECT EXAMINATION BY MR. MILLS:

23              Q.     Can you state your name for the record?

24              A.     Mark Burdette.

25              Q.     And by whom are you employed and in what  
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1 capacity?

2 A. Missouri Office of the Public Counsel as a  
3 public utility financial analyst.

4 Q. Have you prepared and caused to be filed in  
5 this case testimony which has been marked as  
6 Exhibits 81, 82 and 83, consisting of your direct,  
7 rebuttal and surrebuttal testimony?

8 A. Yes.

9 Q. If I were to -- first of all, do you have  
10 any corrections or additions you wish to make to that  
11 testimony?

12 A. There was some errors to some schedules, but  
13 I believe we filed -- in my rebuttal I corrected the  
14 errors in the direct. So I do not believe there are  
15 any further errors.

16 Q. If I were to -- are those answers true and  
17 correct to the best of your knowledge and belief?

18 A. Yes.

19 Q. If I were to ask you the same questions that  
20 are contained in that testimony here today, would your  
21 answers be the same?

22 A. Yes.

23 MR. MILLS: With that I will offer  
24 Exhibits 81, 82 and 83 and tender the witness for  
25 cross-examination.

1 JUDGE DERQUE: Thank you, Mr. Mills.  
2 Is there any objection to the admission into  
3 evidence of Exhibits 81, 82 or 83?  
4 MR. SWEARENGEN: No objection.  
5 JUDGE DERQUE: Hearing no objection, they  
6 will be admitted.  
7 (EXHIBIT NOS. 81 THROUGH 83 WERE RECEIVED  
8 INTO EVIDENCE.)  
9 JUDGE DERQUE: Mr. Woodsmall?  
10 MR. WOODSMALL: No questions. Thank you.  
11 JUDGE DERQUE: Mr. Finnegan?  
12 MR. FINNEGAN: Yes, I have a few questions.  
13 MR. SWEARENGEN: Your Honor, now,  
14 Mr. Finnegan, of course, has adopted the position of  
15 the Office of Public Counsel on this issue. I don't  
16 know that he ought to be entitled to cross-examine.  
17 JUDGE DERQUE: Mr. Swearengen, he's on the  
18 hearing memorandum as being a cross-examining party.  
19 MR. SWEARENGEN: That's right, but he's  
20 friendly to this position. I don't want any friendly  
21 cross-examination on the record.  
22 MR. WOODSMALL: I believe we should hear the  
23 question before.  
24 JUDGE DERQUE: Yeah, I was going to say, if  
25 there is, you may object.

1 MR. SWEARENGEN: Thanks.

2 JUDGE DERQUE: I understand that, and that's  
3 fine for pointing it out. If there is any friendly  
4 cross, you may object to it.

5 MR. FINNEGAN: I'm just trying to get some  
6 clarification myself, your Honor.

7 JUDGE DERQUE: That's fine. You go right  
8 ahead.

9 CROSS-EXAMINATION BY MR. FINNEGAN:

10 Q. Mr. Burdette, on page 24 of Exhibit 81, your  
11 direct testimony, are you on that page?

12 A. Yes.

13 Q. Okay. You're recommending a 10.7 percent  
14 return?

15 A. Correct.

16 Q. I believe you state that this should be no  
17 more than 10.7 percent?

18 A. Yes.

19 Q. Does that mean a lesser figure would not be  
20 unreasonable?

21 MR. SWEARENGEN: Objection, your Honor.  
22 That's friendly cross-examination. That's just what I  
23 was concerned about.

24 JUDGE DERQUE: Sustained.

25 BY MR. FINNEGAN:

1           Q.     All right.  Mr. Burdette, on page 24 you  
2     make a statement, "The high (average) cost of equity  
3     calculated for the industry group was 9.57%."

4                     What is the purpose of saying -- putting  
5     that in there?

6           A.     The purpose of that would be to show that  
7     10.7 percent, my recommendation is above one of the  
8     calculations for the industry group, to point out that  
9     I am not recommending a number for -- from the  
10    perspective of the Company, I'm not making a  
11    recommendation that's too low.

12          Q.     Okay.  And in other words, you're  
13    recommending something over and above the industry  
14    group?

15                   MR. SWEARENGEN:  I'm going to object,  
16    your Honor.  His testimony speaks for itself.  
17    Mr. Finnegan's client has adopted the position of the  
18    Public Counsel.  I don't think he needs to clarify  
19    anything.

20                   JUDGE DERQUE:  Sustained.

21                   Mr. Finnegan, as you may have ascertained,  
22    I'm not going to give you too much leeway.

23                   MR. FINNEGAN:  I understand.

24                   JUDGE DERQUE:  Please be careful.

25    BY MR. FINNEGAN:

1           Q.     By giving the Company more than the industry  
2 group, are you rewarding the Company?

3           MR. SWEARENGEN:   Same objection.

4           JUDGE DERQUE:   No.   I think that's a fair  
5 question.   It's overruled.

6           You may go ahead and answer, Mr. Burdette.

7           THE WITNESS:   No, I don't think I'm  
8 rewarding the Company.   I believe I made a reasonable  
9 and appropriate recommendation based on my analysis.

10          BY MR. FINNEGAN:

11          Q.     If the Commission were to adopt 9.57  
12 percent, that would not be unreasonable?

13          MR. SWEARENGEN:   Objection.   That is clearly  
14 self-serving, and he's adopted the position of the  
15 Public Counsel in this case.

16          MR. MILLS:   Well, at least in this  
17 particular question, if I may be allowed to respond, I  
18 think he's trying to -- although he adopted the  
19 position of the Public Counsel, it is not the position  
20 of the Public Counsel that is recommending  
21 9.57 percent.   And I think this really goes outside of  
22 Public Counsel's position.

23          He's trying to explore how Public Counsel's  
24 position as filed relates to some other numbers in his  
25 testimony.   It may be adverse to the Company's

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1 interest. It does not necessarily mean that it's  
2 friendly to our position.

3 JUDGE DERQUE: Mr. Woodsmall?

4 MR. WOODSMALL: I agree wholeheartedly with  
5 what Mr. Mills just said.

6 MR. SWEARENGEN: Of course, Mr. Finnegan has  
7 adopted the Public Counsel's position, which is  
8 explained in the testimony and the hearing memorandum.

9 MR. FINNEGAN: I believe it says I support  
10 the Public Counsel's position.

11 MR. WOODSMALL: And this question, I  
12 believe, could be used to establish an ROE below what  
13 Public Counsel is testifying to.

14 So I believe to the extent that he's  
15 attempting to establish a position adverse to Public  
16 Counsel or below that, he should be allowed to use any  
17 witness presented in this case for that purpose.

18 MR. SWEARENGEN: I disagree with that.

19 JUDGE DERQUE: That's not his -- that's not  
20 his position. That's not the stated position of  
21 Jackson County.

22 MR. FINNEGAN: In opening statement, if you  
23 recall, I indicated that we adopted Public Counsel's  
24 position because it was the lowest. And if there is  
25 lower position available, we would support that too.

1 MR. SWEARENGEN: And I appreciate that.

2 MR. FINNEGAN: I don't think this Company  
3 should be rewarded for anything.

4 JUDGE DERQUE: Well --

5 MR. SWEARENGEN: But when they adopt the  
6 position, that's the position, and I don't think then  
7 he ought to make -- try to change it to something  
8 else.

9 MR. FINNEGAN: The word was not adopted. I  
10 said support.

11 MR. SWEARENGEN: Well, you just said  
12 adopted.

13 JUDGE DERQUE: I think I said adopted.

14 MR. SWEARENGEN: He did too.

15 JUDGE DERQUE: Mr. Finnegan, I'm going to  
16 sustain the objection and tell you why. Basically in  
17 fundamental fairness to UtiliCorp, I'm going to  
18 sustain the position.

19 I'm not trying to -- I'm not trying to in  
20 any way limit Jackson County's due process right here,  
21 but I'm afraid we're going to very shortly get into a  
22 situation where not only do we have friendly cross but  
23 we also have self-serving answers, and I would like to  
24 avoid that.

25 MR. FINNEGAN: In light of that, I can

1       preserve this for a brief. I believe everything is in  
2       the testimony.

3               JUDGE DERQUE: Certainly. Like I said, I  
4       don't want to restrict your right to continue.

5               MR. FINNEGAN: That's fine. I can stop  
6       right there.

7               JUDGE DERQUE: Okay. Thank you.

8               Mr. Woodsmall?

9               MR. WOODSMALL: No questions. Thank you.

10              JUDGE DERQUE: Mr. Swearengen?

11              MR. SWEARENGEN: I have no questions, your  
12      Honor. Thank you.

13              JUDGE DERQUE: Chair Lumpe?

14              CHAIR LUMPE: I don't have any questions.

15              JUDGE DERQUE: And Commissioner Murray?

16              COMMISSIONER MURRAY: I don't believe I do  
17      either.

18              JUDGE DERQUE: Redirect, Mr. Mills?

19              MR. MILLS: I don't believe so. Thank you.

20              JUDGE DERQUE: Thank you, Mr. Burdette.

21              (Witness excused.)

22              MR. WOODSMALL: Your Honor, could I take two  
23      minutes and get the schedules out of my office. I  
24      thought we'd have another recess in there.

25              JUDGE DERQUE: We're off the record.

1 (A recess was taken.)  
2 JUDGE DERQUE: Back on the record.  
3 Three pieces of testimony for Mr. Dunn. Is  
4 that correct?  
5 MR. SWEARENGEN: Yes, direct, rebuttal and  
6 surrebuttal.  
7 JUDGE DERQUE: And none of those are  
8 confidential?  
9 MR. SWEARENGEN: I believe that's right.  
10 JUDGE DERQUE: The direct will be 84, the  
11 rebuttal will be 85, surrebuttal will be 86.  
12 (EXHIBIT NOS. 84 THROUGH 86 WERE MARKED FOR  
13 IDENTIFICATION.)  
14 (Witness sworn.)  
15 JUDGE DERQUE: Thank you, sir. Please have  
16 a seat.  
17 Mr. Swearengen.  
18 JOHN C. DUNN testified as follows:  
19 DIRECT EXAMINATION BY MR. SWEARENGEN:  
20 Q. Would you state your name for the record,  
21 please?  
22 A. It's John C. Dunn, D-u-n-n.  
23 Q. Mr. Dunn, by whom are you employed?  
24 A. I'm employed by John C. Dunn and Company.  
25 Q. And did you cause to be prepared for  
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1 purposes of this case three pieces of testimony in  
2 question and answer form?

3 A. Yes, sir, I did.

4 Q. And you understand your rebuttal  
5 testimony -- excuse me -- your direct testimony has  
6 been marked as Exhibit 84, your rebuttal testimony  
7 is Exhibit 85 and your surrebuttal testimony is  
8 Exhibit 86; is that correct?

9 A. That's correct.

10 Q. And all three pieces of that testimony  
11 concern the capital structure rate-of-return issues;  
12 is that correct?

13 A. Yes, sir, that's correct.

14 Q. Mr. Dunn, with respect to Exhibit 84, your  
15 direct testimony, are there any changes that you need  
16 to make in that document?

17 A. Yes, sir, I have some typographical changes.

18 Q. Could you tell us what they are by page and  
19 line number, please?

20 A. The first appears on page 17, line number  
21 12. The fifth word in the line is for, f-o-r. It  
22 should be o-r.

23 The next change appears on page 26, line 2.  
24 The last word in the line says historically, and the  
25 l-y should be knocked off of that word so that it

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1       should just be historical.

2                   And then the next line has extrapolation.

3       The first word should be extrapolated, e-d.

4           Q.     Any other changes in your direct testimony?

5           A.     Page 36, line 6, the fifth word in the line  
6       acquired should be deleted. Those are all of the  
7       changes I have to the direct, but I do have some  
8       changes to the rebuttal.

9           Q.     Would you tell us the changes to the  
10       rebuttal testimony, Exhibit 85, please?

11          A.     Page 8, this change extends over lines 14  
12       and 15. The last word of the line on 14 is the word  
13       "does." That should be deleted, and the balance of  
14       that sentence on line 15 should be deleted and the  
15       words adjusts UtiliCorp total company short-term debt  
16       by the amount of MPS construction work in progress.  
17       And I'll read that more slowly.

18                   MR. FINNEGAN: That's a typographical?

19                   THE WITNESS: It was actually a correction  
20       of something that was brought my attention in the  
21       surrebuttal of the OPC.

22       BY MR. SWEARENGEN:

23           Q.     Would you give us those words again, please?

24           A.     Adjusts UtiliCorp total company short-term  
25       debt by the amount of MPS CWIP.

1           Q.     And then what happens to the words on  
2     line 16 on that page? Do they stay or do they come  
3     out?

4           A.     The balance of that line should be fine.

5           Q.     Okay.

6           A.     And I have a companion change on page 41 of  
7     the rebuttal, line 8, the third and second words from  
8     the end of the line, "did not" should be deleted and  
9     replaced with the words "did so incorrectly."

10          Q.     Any other changes on your rebuttal  
11     testimony?

12          A.     No, sir. I have one change on the  
13     surrebuttal.

14          Q.     Tell us what it is, please.

15          A.     On page 12 of the surrebuttal, the end of  
16     line 10, the words "to reduce those costs" should be  
17     inserted.

18          Q.     To reduce those costs.

19                     Period?

20          A.     Period.

21                     So the sentence should read, I believe that  
22     any revenues which the Commission finds to be excess  
23     should be used to reduce those costs.

24          Q.     Mr. Dunn, if I ask you the questions which  
25     are contained in your three pieces of testimony,

1 Exhibits 84, 85 and 86, would your answers today be as  
2 contained in that testimony and as you have corrected  
3 them today?

4 A. Yes, sir, they would.

5 MR. SWEARENGEN: At this time, your Honor, I  
6 would offer into evidence Exhibits 84, 85 and 86 and  
7 tender the witness.

8 And excuse me, your Honor. Mr. Woodsmall  
9 was kind enough to make necessary copies of  
10 Exhibit 80, and if it's possible, I would offer that  
11 at this time as well.

12 JUDGE DERQUE: You are also offering  
13 Exhibit 80, Mr. Swearengen?

14 MR. SWEARENGEN: Yes, I would offer  
15 Exhibit 80.

16 JUDGE DERQUE: I have Exhibits 80 styled DR  
17 No. 148, and the testimony of Mr. Dunn, Exhibits 84,  
18 85 and 86 offered for admission into evidence.

19 Are there any objections?

20 MR. WOODSMALL: No objections.

21 MR. MILLS: I have no objections to 84, 85  
22 and 86. I really haven't had a chance to look at 80.

23 JUDGE DERQUE: 84, 85 and 86 will be  
24 admitted.

25 (EXHIBIT NOS. 84 THROUGH 86 WERE RECEIVED  
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1 INTO EVIDENCE.)

2 MR. SWEARENGEN: Thank you.

3 MR. MILLS: I don't believe I have any  
4 objection. Although I would note for the record that  
5 it doesn't appear on the copy of the data request that  
6 I have who exactly asked the data request, and  
7 normally it would do so.

8 JUDGE DERQUE: The Staff.

9 MR. MILLS: Correct. But usually on the  
10 data request the form that is submitted has the name  
11 of the person asking it. I don't see that here.

12 JUDGE DERQUE: This one doesn't have it.

13 Mr. Woodsmall, you may enlighten Mr. Mills  
14 if you happen to know.

15 MR. MILLS: I do. It was Staff witness  
16 Traxler.

17 JUDGE DERQUE: Okay. Thank you. Exhibit  
18 No. 80 will be admitted.

19 (EXHIBIT NO. 80 WAS RECEIVED INTO EVIDENCE.)

20 JUDGE DERQUE: Mr. Finnegan?

21 MR. FINNEGAN: I believe I'm third on the  
22 list here of MPS witnesses.

23 JUDGE DERQUE: Pardon me?

24 MR. FINNEGAN: I think I'm supposed to be  
25 the third questioner.

1 JUDGE DERQUE: Yeah, you are.  
2 MR. FINNEGAN: I'm reading a memo here.  
3 JUDGE DERQUE: Am I mistaken? The MoPub  
4 witness cross-examination --  
5 MR. FINNEGAN: Oh, I'm sorry.  
6 JUDGE DERQUE: -- Sedalia Industrial, that's  
7 Mr. Brownlee and he's not here.  
8 MR. FINNEGAN: I am first.  
9 JUDGE DERQUE: The IBEW, and that's Keevil,  
10 and he's not here.  
11 MR. FINNEGAN: I can do that.  
12 I'm sorry. I thought I was in the MGE case.  
13 CROSS-EXAMINATION BY MR. FINNEGAN:  
14 Q. Mr. Dunn.  
15 A. Mr. Finnegan.  
16 Q. How long ago was it when you left the Public  
17 Service Commission?  
18 A. It's been almost 25 years. About six months  
19 after you left.  
20 Q. Do you remember that time in Kansas City  
21 at the Sneaky Pizza --  
22 A. All right.  
23 Q. I withdraw that.  
24 I have a couple of questions, Mr. Dunn.  
25 On page -- and even though we're friends,

1 this is not going to be friendly cross.

2 On page 56 of your testimony.

3 JUDGE DERQUE: Is this the direct?

4 BY MR. FINNEGAN:

5 Q. Your direct. I'm sorry. Exhibit 84.

6 A. Yes, sir, I have that.

7 Q. Okay. On line 2, would you please read the  
8 first two sentences there?

9 A. "The comparative group cost of common equity  
10 is 12.0 percent. As a practical matter, the return  
11 components in the cost of service should not be lower  
12 than this amount."

13 MR. FINNEGAN: Okay. That's all of the  
14 questions I have. Thank you.

15 JUDGE DERQUE: Thank you, Mr. Finnegan.

16 Let's see. Mr. Mills?

17 MR. MILLS: Yes. I think I have just one  
18 question.

19 CROSS-EXAMINATION BY MR. MILLS:

20 Q. Mr. Dunn, if I could have you turn to page  
21 32 of your direct testimony.

22 A. I have page 32, sir.

23 Q. In your example there, does either A or B  
24 issue either stock or debt?

25 A. They could or could not. It's irrelevant.

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1 MR. MILLS: That's the only question I had.  
2 Thank you.

3 JUDGE DERQUE: Thank you, Mr. Mills.

4 Mr. Woodsmall?

5 MR. WOODSMALL: Yes. I just need to mark  
6 two exhibits.

7 JUDGE DERQUE: This will be Exhibit No. 87,  
8 the direct testimony of John C. Dunn in ER-93-37. And  
9 Exhibit No. 88, the direct testimony of Mr. John C.  
10 Dunn in Case No. ER-90-101.

11 We are off the record.

12 (EXHIBITS NOS. 87 AND 88 WERE MARKED FOR  
13 IDENTIFICATION.)

14 JUDGE DERQUE: We're back on the record.

15 Mr. Woodsmall?

16 CROSS-EXAMINATION BY MR. WOODSMALL:

17 Q. Mr. Dunn, do you have what's been marked as  
18 Exhibit 87?

19 A. Yes, sir, I do. That's the direct testimony  
20 in 93-37?

21 A. And was that prepared under your supervision  
22 or by you?

23 A. I assume this is an accurate copy of my  
24 testimony, yes.

25 Q. Okay. And that was filed in Case  
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1 No. ER-93-37; is that correct?

2 A. I believe so.

3 Q. Similarly, do you have what's been marked as  
4 Exhibit 88?

5 A. I do.

6 Q. And can you tell me what that document is?

7 A. That is a copy or what I accept to be a copy  
8 of my direct testimony in Case No. 90-101 concerning  
9 Missouri Public Service.

10 Q. And that document was prepared by you or  
11 under your supervision?

12 A. Yes, it was.

13 MR. WOODSMALL: At this time I'd offer  
14 Exhibits 87 and 88 into evidence.

15 JUDGE DERQUE: Is there any objection?

16 MR. SWEARENGEN: No objection.

17 JUDGE DERQUE: Seeing none, they will be  
18 admitted.

19 (EXHIBIT NOS. 87 AND 88 WERE RECEIVED INTO  
20 EVIDENCE.)

21 MR. WOODSMALL: I have no further questions,  
22 your Honor.

23 JUDGE DERQUE: Questions for Mr. Dunn.  
24 Chair Lumpe.

25 CHAIR LUMPE: I guess I'm sort of wondering  
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1 if I should have questions for you.

2 QUESTIONS BY CHAIR LUMPE:

3 Q. Mr. Dunn on page 5 of your direct you talk  
4 about reregulation in the coming new environment.  
5 What do you mean by that?

6 A. Historically this Commission from the time  
7 that I worked here until very recently has been  
8 involved in costs of service regulation, where the  
9 Commission set the rates and fairly well controlled  
10 all of the activities of the utilities under their  
11 jurisdiction.

12 And I believe what's happening now is,  
13 similar to what has happened in the natural gas  
14 industry and what is in the process of happening in  
15 the telephone communication industry, the Commission  
16 is developing a process where it's going to inject an  
17 element of competition into that traditional cost of  
18 service regulation, so that there will be both  
19 competition and regulation.

20 So rather than to refer to it as  
21 deregulation, which I don't believe it is, I think  
22 it's a reregulation, a new kind of regulation, where  
23 the Commission simply adds to its bag of tools, if you  
24 will, to regulate utilities, competition.

25 Q. So it's more a different kind of

1 regulation -- when I read that it was a regulation  
2 competition, reregulation, that's not what you were  
3 referring to? You were referring to a different kind  
4 of regulation in a competitive environment? Am I  
5 correct?

6 A. You're correct. There will be continued  
7 regulation, but there will be competition alongside  
8 that regulation.

9 Q. In your surrebuttal testimony, around  
10 pages 11 and so, you talk about actions that perhaps  
11 the Commission should be taking for this. Are you not  
12 aware of the preparations that the Commission is  
13 taking?

14 A. Oh, I am aware that the Missouri Commission  
15 has under study and it has taken actions to promote  
16 the cause of competition. I think that --

17 Q. Do you not feel they're adequate?

18 A. I'm not questioning the adequacy. Somebody  
19 has to make the first step, and it was my impression  
20 that this case -- and my belief that this case is sort  
21 of a first step, where the Commission is going to be  
22 exposed to a number of opportunities to make decisions  
23 about regulation.

24 And then in addition to that, I think the  
25 Commission is offered the opportunity in this case

1 to -- to prepare this particular company for  
2 competition in much the same way it will have to  
3 prepare all of the other companies under its  
4 jurisdiction.

5 Q. And you don't think that perhaps it's  
6 premature to take those steps in this case before we  
7 have finished the -- have the recommendation from the  
8 task force and see the legislation, that we should  
9 take action before that happens?

10 A. For the limited purposes that I've  
11 suggested, and specifically what I've suggested is  
12 that there's some regulatory overhang here, some  
13 things on the books of the Company that need to be  
14 amortized.

15 I don't think those things are subject to  
16 dispute, and I think the Commission can get on with  
17 taking care of some of those things now. And anything  
18 that the Commission does in this particular case in  
19 that area I don't think could possibly be in conflict  
20 with the idea -- or the ideas that are ultimately put  
21 forth by the task force or the Commission in some  
22 subsequent hearing or some legislative mandate.

23 Q. And it's your belief then that the various  
24 things the Company is recommending here will  
25 ultimately be part of the recommendation of the task



1 force?

2 A. I believe that -- I can't speak for the task  
3 force obviously, but I believe that anything that the  
4 task force or legislation does in terms of a decision  
5 on transition costs or stranded costs wouldn't be in  
6 conflict with the actions that I think that the  
7 Commission can take here to begin to prepare the  
8 company for re-- for competition.

9 Q. I just wondered, because I know one of the  
10 other witnesses from the Company, there was suggested  
11 legislation, and I just wondered whether you felt we  
12 should act what I would consider perhaps to be  
13 prematurely in advance of legislation, in advance of  
14 the task force recommendations, that we are taking a  
15 deliberate look, and it might be your position that we  
16 weren't looking fast enough.

17 A. Could I clarify?

18 If I gave you the impression that I don't  
19 think you're working fast enough, I think you're  
20 working on the problem, but I don't think that the new  
21 scheme or paradigm or whatever you end up calling it  
22 has to come forth fully implemented and ready to go.  
23 It can be done stepwise.

24 And a step can be taken here and a step can  
25 be taken in some other company's ultimate case. And

1 with care all of those steps will blend into what the  
2 Commission ultimately decides to do.

3 Q. Mr. Dunn, some of the testimony had pointed  
4 out that you had taken a different position here from  
5 that in another case in the consolidated structure  
6 versus assigned structure. Could you sort of explain  
7 why you now take a different position?

8 A. Well, the positions were not different.  
9 They're theoretically consistent. But in that  
10 particular case, I did recommend a consolidated  
11 capital structure, and in this case I'm recommending a  
12 division capital structure, which is the same as a  
13 subsidiary capital structure.

14 The other case involved Missouri American  
15 Water Company, and Missouri American Water Company is  
16 a company which is comprised of numerous State water  
17 utilities. It's a very, very homogeneous company with  
18 maybe 20 subsidiaries, all of which are pretty much  
19 the same, and the Company as a whole is pretty much  
20 the same as all of the subsidiaries, only much larger.

21 And in that particular case we do have what  
22 is called the carbon copy. And in that particular  
23 case my recommendation was, since there was no study  
24 to indicate that Missouri should have a higher equity  
25 ratio and since there was no study allocating the

1 capital for all of the Company, that they should use  
2 the consolidated capital structure, which was not  
3 hugely different than what I was recommending or what  
4 they wanted.

5 That they should use the consolidated  
6 capital structure and do a study and come back to the  
7 Commission and say, Here is why we want to do this  
8 this way. And the Commission can make a decision.

9 Now, in this particular case you have  
10 UtiliCorp, which I believe to be -- well, it's a  
11 classic complex company. It has international  
12 operations, some of which are in strictly the utility  
13 business, most of which are in pure investments and  
14 joint ventures. It has the traditional natural gas  
15 distribution, electric generation and distribution  
16 utility business, which is the second big segment of  
17 the Company, and then it has Aquila, which is the  
18 third big segment of the Company.

19 It's complex in the sense that Aquila is a  
20 separate company, publicly traded, totally separate  
21 from UtiliCorp. And to correct something that was  
22 said earlier today, not all of its equity appears on  
23 UtiliCorp's books. Its accounts are not commingled.  
24 Funds that belong to Aquila are never permitted into  
25 UtiliCorp. The same is true of the international

1 operations.

2           So UtiliCorp is a complex company. Each of  
3 these groups of businesses are different one from the  
4 other, and each of them should have a different kind  
5 of capital structure.

6           Q. In that case, using the consolidated  
7 structure, I think your testimony saved customers  
8 substantial dollars. Why wouldn't that happen here  
9 and why wouldn't that be a good thing?

10          A. In the Missouri American case?

11          Q. Right.

12          A. In the Missouri American case, I believe  
13 that there was genuine phantom equity in that case.  
14 What was going on there was that the Company came in  
15 and said, Well, our consolidated structure has  
16 36 percent equity in it, but we want to be regulated  
17 on the basis of 40 percent equity or 38 or something  
18 like that. No reason for -- no explanation, just  
19 other companies sort of like this, we'd like the same  
20 thing.

21           UtiliCorp has done careful, careful analysis  
22 to determine how each of its subsidiaries should be  
23 regulated, how each of its divisions should be  
24 regulated and how each of them should be capitalized.  
25 And it's put together a capital structure system that

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1 began back in 1986, 1985, and through that -- or since  
2 that period of time it's been continuously  
3 implemented, and it's been applied, reviewed by seven,  
4 ten other commissions. It's been accepted by its  
5 auditors, by the commissions, by large groups of  
6 people, financial analysts. And as a consequence, I  
7 think it's right. I think it's a matter of right and  
8 wrong.

9 Q. You're telling me that over the years  
10 through various decisions, the assigned capital  
11 structure has been used, you said a number of  
12 commissions going back, et cetera, et cetera, that  
13 it's always been the assigned?

14 A. Always been the assigned, since 1986, I  
15 believe. 1985, '86. In the process of  
16 implementation, the Company went back and did a  
17 simulated year to make sure that they could do it, and  
18 then they implemented their programs to make it happen  
19 to the learning programs and the computer programs.

20 And I believe all of that occurred in the  
21 1986 time frame. And ever since that time it's been  
22 continuously applied, and I think the first commission  
23 that reviewed it was probably Kansas, perhaps  
24 Michigan, but since that time it's been reviewed by  
25 Kansas, Michigan, West Virginia, Nebraska, Iowa,

1 Minnesota.

2 Q. So your response is in terms of other  
3 commissions, not necessarily the Missouri Public --

4 A. The Missouri Commission has also reviewed it  
5 in the last case and accepted it.

6 Q. But not the case before?

7 A. That's right. There is a little history to  
8 that.

9 Q. I thought you were talking about the  
10 Missouri Commission going back to the '80s, and I  
11 thought --

12 A. I'm sorry.

13 Q. I thought I heard it in the '90s --

14 A. No, no. I'm sorry. The Missouri Commission  
15 has -- its position has evolved to the current stand-  
16 alone capital structure.

17 Q. All right. You talked about the commingling  
18 of foreign debt and said that it was not commingled?

19 A. That's correct.

20 Q. Did you present evidence to anyone at Staff,  
21 in your testimony evidence, of that noncommingling?

22 A. It's in my testimony, it's in the hearing  
23 memorandum.

24 Q. Would you cite for me where in your  
25 testimony so I might look that up?

1           A.     Yes, ma'am.

2                     Page 5 of the rebuttal testimony is a bullet  
3 point which refers to a group of the other testimony  
4 that shows up subsequent to this in the rebuttal  
5 testimony, and it states that using the consolidated  
6 capital structure, implies that the capital in that  
7 structure is available to finance the Missouri rate  
8 base.

9                     This is an incorrect assumption, since a  
10 significant part of the long-term debt is  
11 international, and the money cannot leave the country  
12 of origin. And part of the long-term debt is issued  
13 by other UtiliCorp subsidiaries and is legally  
14 required to be used inside of those publicly traded  
15 entities and not in Missouri.

16           Q.     And you have evidence that it may not leave  
17 the country of origin?

18           A.     Yes, ma'am.

19           Q.     Have you submitted that anywhere, that  
20 evidence?

21           A.     We have submitted the -- again, with respect  
22 to the rebuttal testimony, the attachments to that  
23 rebuttal testimony which were read to you as a part of  
24 earlier cross-examination, show the purpose of the  
25 proceeds on the Australia debt and the purpose of the

1 proceeds on the New Zealand debt.

2 The problem of proving a negative is sort of  
3 an odd thing, but the way these international  
4 financings are handled UtiliCorp never saw the money.

5 It's sort of like financing your house.  
6 When I bought my house, I didn't -- nobody handed me a  
7 check for the loan. They took -- I signed up for the  
8 loan, they wrote a check and they gave it to somebody  
9 else. They never gave it to me.

10 And that's exactly what happened in  
11 connection with the Australian and New Zealand  
12 properties. In both of those instances the money was  
13 never, ever given to UtiliCorp. The money was  
14 transferred directly to a third party.

15 In the case of the properties in Canada, the  
16 British Columbia Electric Utility, those financings  
17 take place inside of that company. And Canada, like  
18 all of these other countries, protects its own  
19 capital. It doesn't permit Americans or foreign  
20 nationals or foreign corporations to borrow money in  
21 Canada and move it to America for American purposes.  
22 They just don't let that money out of the country.

23 And then Aquila is a slightly different kind  
24 of thing. Aquila is a freestanding publicly traded  
25 company, and it has obliged all of its officers, its



1 board, everybody else, has fiduciary duties to keep  
2 that money inside that company. Now, those checks  
3 never get anywhere near UtiliCorp. They go straight  
4 to Aquila and that's it.

5 Q. So you're saying it's not in your treasury;  
6 it doesn't come to you?

7 A. It's never been in the treasury, and I  
8 believe that perhaps the very best evidence would be  
9 to ask somebody in an accounting clerk position at  
10 UtiliCorp if they've ever recorded such a matter.

11 But as a legal matter, I think these  
12 documents all demonstrate that this money, if you know  
13 the history of what is going on here, never, ever  
14 reaches UtiliCorp's treasury.

15 Q. I have about two more here.

16 Are you -- in the new environment that we're  
17 talking about again, are you aware of any research  
18 that would show a move away from utility stock  
19 purchases that people would in the new environment not  
20 look at utility stocks anymore? Do you have any  
21 research showing that?

22 A. There is some research that -- and I don't  
23 know if you're elevated to the level of research.  
24 There is some pronouncement by Moody's and Standard  
25 and Poors which indicate generally that they believe

1       that as the industry becomes more competitive, it will  
2       become more bipolar, that there will be winners and  
3       losers and that there will be a group of companies  
4       that will not survive.

5           Q.     And does that relate to your 12 percent rate  
6       of return, that you feel that that's essential because  
7       of that volatility?

8           A.     I believe that combined -- now, the 12  
9       percent is combined with a couple of things. It's  
10      combined with the Company's willingness to enter into  
11      some sort of refund arrangement, where they have a  
12      performance-based rate. And I think under those  
13      circumstances there's no risk to the consumer.

14                 The Commission sets that rate and permits  
15      the Company to exercise the maximum efficiency it can  
16      as some sort of a sharing arrangement. Something like  
17      the UE sharing arrangements.

18           Q.     The last one, in your surrebuttal, I think  
19      it was on the page where you made a correction or so,  
20      you talked about if there -- you talked about excess  
21      revenues, that they should be used if there are those,  
22      I'm assuming you're saying, because I assume you're  
23      saying there aren't excess revenues. Is that correct?

24                 But should there be excess revenues, should  
25      we admit to that, it should be used then to reduce

1 transitional stranded cost. Is that what you were  
2 talking about?

3 A. Yes, ma'am. It's just that simple. It  
4 seems like to me that it's sort of an exercise in  
5 futility to reduce rates and then increase rates,  
6 really run the risk that once competition arrives,  
7 that the Company won't be ready.

8 I think competition holds such a huge  
9 promise for customers that we should get the incumbent  
10 utilities ready to compete, so they'll be vigorous  
11 competitors and produce the lowest possible prices.

12 Q. There are some suggestions that if you-- I  
13 think it's securitize, or whatever the word they use,  
14 on transitional costs, that that would lower rates to  
15 the consumer. Now, I don't understand how that would  
16 happen.

17 But you would suggest that this would be a  
18 preferable way to some other way of dealing with  
19 stranded cost in zero excess revenues?

20 A. Well, I think that you have the opportunity  
21 today to deal with it here in this particular company.  
22 Securitizing them does not get rid of them. It simply  
23 stretches them out again and makes them some sort of  
24 an obligation of the future.

25 Q. I never understood how that lowers the cost

1 to the consumer?

2 A. I'm not sure that it does.

3 Q. I keep reading that it says it does and

4 I'm --

5 A. I'm not sure that it does. I think over the  
6 long run there are very few things that can be done to  
7 absolutely lower the cost, other than I believe  
8 competition will lower costs to consumers. I think it  
9 will do it very quickly.

10 CHAIR LUMPE: Thank you.

11 JUDGE DERQUE: Commissioner Murray?

12 COMMISSIONER MURRAY: Thank you.

13 QUESTIONS BY COMMISSIONER MURRAY:

14 Q. Good morning.

15 A. Good morning.

16 Q. I'd like to refer you to page 11 of your  
17 rebuttal testimony, starting at line 19.

18 A. I'm sorry. I just haven't got that yet.

19 Yes, ma'am, I have that.

20 Q. You refer to there being more than

21 150 business entities represented by UtiliCorp?

22 A. Yes, ma'am.

23 Q. And that each has a different risk profile  
24 and different return requirements.

25 Are you saying that the Company traces the  
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1 flow of debt and equity throughout the 150 different  
2 business entities?

3 A. It treats most of those businesses sort of  
4 as a group. For very small start-up business, for  
5 example, it has a number of small start-up businesses.

6 And it says in the case of those companies  
7 that are small start-up, if they would be financed  
8 100 percent equity. If somebody else was starting  
9 them, we'll finance them 100 percent equity.

10 But for each of those entities, to the  
11 extent that they actually get up and get started and  
12 get capital, they do have their own capital structure.  
13 And then --

14 Q. And you can trace the funds within each one  
15 of these 150 entities?

16 A. That's correct. The tracing thing is sort  
17 of a red herring. There is no tracing. There's only  
18 a couple of things that come into UtiliCorp's  
19 treasury.

20 They have capital transactions where they  
21 get debt and they have capital transactions where they  
22 get equity and they have revenue. Well, they know how  
23 much revenue they have coming in and they know how  
24 much debt and they know how much equity. They take  
25 the debt and they say we're going to put this debt

1 here and we're going to put some debt here. I mean,  
2 it's not a huge complex problem.

3 Q. So it is an allocation that the Company  
4 makes by choice?

5 A. That's correct, based on their studies.

6 Q. And so on page 12 where you say at line 6,  
7 It's management's job to select the capital structures  
8 for business activities under their direction and  
9 control, you are saying that management determines  
10 how to allocate debt and equity among all of its  
11 150 entities?

12 A. That's correct, based on the studies that  
13 they had done and the studies that they do.

14 Q. But not based upon any actual flow of money  
15 to or from any one of those entities?

16 A. Well, for some very big entities. All of  
17 the international operations, Aquila and British  
18 Columbia, those entities are based on their own  
19 transactions.

20 Q. Okay. How do you trace the funds that are  
21 derived from foreign debt?

22 A. The house example I think is a fairly good  
23 one, because it's really what happens. When you  
24 bought your house -- or when I bought my house anyway,  
25 I financed it. I never got my hands on that money. I

1 never could do it.

2 Q. I heard you -- excuse me. I heard your  
3 explanation to Chairman Lumpe. But how do you -- I  
4 don't believe that answered the question as to how you  
5 actually traced that money, how you show it or what  
6 documents you've used to show it.

7 A. In the case of the Australian operation, for  
8 example, that's a large electric utility. It's a  
9 billion dollar company.

10 UtiliCorp owns less than half of that  
11 company. That company has its own capital structure,  
12 it has its own long-term debt, short-term debt, it has  
13 its own management. It has everything. It's a  
14 freestanding entity over there.

15 Q. Which company are you talking about?

16 A. I'm talking about Australia.

17 The same applies to New Zealand and the same  
18 applies to Canada. But Australia sits there. That  
19 money that was borrowed by UtiliCorp, combined with  
20 some equity which UtiliCorp supplied, was used to  
21 purchase stock from an electric authority in  
22 Australia.

23 I mean, it was a privatization. The  
24 government owned the company first, and UtiliCorp and  
25 another major investor purchased it from the

1 government. And the money that UtiliCorp borrowed  
2 went from the lender to the government in Australia.  
3 It never got into UtiliCorp's hands.

4 Q. And there's a separate set of books that  
5 shows that?

6 A. There is a totally separate company, with  
7 separate employees, a separate president, separate  
8 management, separate everything.

9 UtiliCorp is a manager of that particular  
10 company, and in its management capacity it doesn't  
11 decide how to extend the line, and it doesn't do  
12 anything that are actually sort of on the ground kind  
13 of work, day to day running the company. It gives the  
14 company advice on how to be more efficient and how to  
15 streamline their operation and use some American  
16 techniques and management tools to run a better  
17 company.

18 Aquila is another example which I'm quite  
19 familiar with. Aquila has an operation in San  
20 Antonio, Texas, which could be divorced and separated  
21 from UtiliCorp tomorrow morning.

22 Q. Okay. And I want to be clear that I  
23 understand your position here.

24 Your position is that the debt portion for  
25 those separate entities should be not included in the



1 capital structure in calculating Missouri Public  
2 Service capital structure?

3 A. Not precisely.

4 Q. Okay. Would you explain?

5 A. The reason that all of this issue about the  
6 international debt comes up in the first place is  
7 because somebody is suggesting to use the consolidated  
8 capital structure. We have, like, 15 criticisms of  
9 why you can't use the consolidated capital structure,  
10 why it's wrong.

11 One of those criticisms is that this money  
12 is just not available. There is allocated equity in  
13 UtiliCorp to its international operations. It's not  
14 here, but it's allocated over to the international  
15 operations. And there's allocated equity or equity of  
16 their own in the international operations.

17 The same is true of Aquila. There is --  
18 Aquila has a capital structure just exactly like  
19 Missouri Public Service. Aquila's capital structure  
20 is, I think, 40 percent or 45 percent, 50 percent  
21 equity. Aquila pays dividends to UtiliCorp at the  
22 same time they pay a dividend to their public  
23 shareholders. And Aquila treats UtiliCorp just like  
24 it treats any public shareholder that would go out and  
25 a buy 100 shares of that stock. So there's no way

1       that this debt gets commingled.

2               Now, that's the only reason we brought it up  
3       in the first place. How all of this happened in the  
4       first place is that UtiliCorp has a pool of capital.  
5       And they say, this piece goes to this subsidiary, this  
6       piece goes to this division. There is a piece in that  
7       allocation process that is assigned to Australia.  
8       There's a piece that's assigned to Aquila. There is a  
9       piece that is assigned to Canada.

10              All of that has been done and it was  
11       supplied to the Staff. It's been done three times  
12       actually. It was done in '86. It was reviewed in  
13       1992 or so, and then it was done again in its entirety  
14       in 1996. And these are big, comprehensive studies of  
15       all of the capital of UtiliCorp.

16              Q.     And the equity portions of those entities is  
17       the company attempting to assign those equity portions  
18       of those entities to the calculation for Missouri  
19       Public Service?

20              A.     No, ma'am.

21              Say UtiliCorp had \$100 worth of equity, for  
22       sake of an example, and they assigned \$40 to Missouri  
23       Public Service, and say they assign \$10 to Peoples,  
24       \$20 to international companies and \$10 to Aquila, I  
25       mean, that's an assignment to each of the pieces. You

1 add it all up and you have UtiliCorp's total equity.

2 The contrary position here is, don't do  
3 that, just add up all of the equity and call it  
4 UtiliCorp's Missouri Public Service. And we're saying  
5 that that's, you know, not the right way to do it.

6 But we're not using the same equity two  
7 places, and we're not changing the equity from year to  
8 year. You can go back through the annual reports that  
9 have been filed, the surveillance reports that have  
10 been filed with this Commission and the same equity  
11 and the same debt has been in Missouri Public Service  
12 all of those years.

13 The same is true of Aquila. When Aquila did  
14 its public offering, its debt and equity is the same  
15 debt and equity that was assigned from this capital  
16 structure system to Aquila just prior to the debt and  
17 equity. It had been -- nothing changed.

18 So we're not trying to get double duty out  
19 of these dollars. That's the alternative.

20 The alternative is to try and have a  
21 different capital structure every time you come and  
22 get the most beneficial result. But that's been the  
23 sole -- you know, it's just one of many reasons why I  
24 believe they're wrong.

25 Q. Okay. You've made reference in your  
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1 testimony to the changing environment --

2 A. Yes, ma'am.

3 Q. -- in electric utilities and the need to  
4 change the regulatory structure for regulated  
5 companies as a result of that changing environment.

6 Doesn't the changing environment behoove the  
7 commissions to be more careful that entities that own  
8 both regulated -- or companies that own both regulated  
9 and deregulated or reregulated entities do not shift  
10 debt and equity improperly between those?

11 A. Oh, I think it does. But I think once  
12 you're fairly, fully implemented it won't make much  
13 difference. I don't think we'll be doing this kind of  
14 thing five or ten years from now.

15 But in the meantime, you're right, you need  
16 to get this all nailed down on paper and not be  
17 shifting around. And that's I think one of the high  
18 points of this particular approach. UtiliCorp  
19 committed to do this back in 1986, and it hasn't been  
20 shifted around. It's been basically the same since  
21 1986. It's 11, 12 years now.

22 The alternative, which I believe was what  
23 was going on in Missouri American Water, is to move it  
24 around. I don't have a study, I don't do this, I  
25 don't do that, but it just sort of feels like we ought

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1 to be here today.

2 Q. Okay. Forgive me if I'm confused about your  
3 Company's position, but I have heard arguments or read  
4 arguments in the testimony that because of the  
5 changing environment there is more risk created, and  
6 that it's my understanding that you are saying that  
7 the shareholders of Missouri Public -- I mean the  
8 ratepayers of Missouri Public Service should also  
9 share in that increased risk and it should not just be  
10 on the shareholders. Is that correct?

11 A. That's sort of reasonable to say it that  
12 way. There is more risk, which I think entitles the  
13 Company to more return, but I don't think it's going  
14 to cost the customer any more money.

15 And I -- please stop me if you think I'm  
16 going afield here, but it seems like to me that we've  
17 been rolling along now for 25 or 50 years regulating  
18 utilities sort of the same way; and we found out when  
19 we deregulated the gas industry, the prices went down.  
20 And there are two or three things that have happened  
21 to utilities, I believe, as a consequence of  
22 regulation which has made them less than totally  
23 efficient. And I think that competition will make  
24 utilities as efficient as they can be. It will make  
25 them better companies.

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1           Now, that doesn't mean that you're not going  
2   to have to continue to regulate them, and it will just  
3   be a different kind of thing. I don't think I'll be  
4   arguing about accounting adjustments and all of that  
5   kind of detail. I don't think you'll have to cope  
6   with that detail anymore. I think you'll have to make  
7   sure that the competitive environment is good and that  
8   the playing field is level and that there's a proper  
9   number of companies competing with each other.

10        Q.    I can see how that argument would hold true  
11   if all of the companies were in an equal situation in  
12   terms of being competitive, but are we not still in an  
13   environment in which we have some entities that are  
14   still in the regulated environment and others are free  
15   to compete, and those different types of entities  
16   exist within UtiliCorp?

17        A.    UtiliCorp doesn't have an entity, I don't  
18   believe, that competes with Missouri Public Service.

19           Now, I think they want to.

20        Q.    I'm not talking about competing with  
21   Missouri Public Service. I'm talking about being able  
22   to compete in the industry.

23        A.    Oh, they do. And maybe I've misunderstood  
24   what -- you know, I might have been answering the  
25   wrong question here.

1           Aquila is more risky in certain respects to  
2   Missouri Public Service, and it's entitled to a  
3   different return level than Missouri Public Service.

4           And I don't think that MoPub customers  
5   should pay any of that. I mean, we ought to have  
6   Aquila over here in a box and we ought to have MoPub  
7   here in a box and International over there in a box  
8   and each of them ought to get their own return and  
9   each of them ought to have their own level of costs.

10          If anything, one of the major, I believe,  
11   benefits of the capital structure study is that it  
12   assigns the capital costs to the individual pieces, so  
13   that the more-risk entities in it are not being  
14   subsidized by the regulated less risky entities.

15          I'm only saying that generally, because I  
16   think some regulated entities are getting more risky  
17   or as risky as the nonregulated. But that's sort of a  
18   detail.

19          You're talking about the grand scheme of  
20   moving costs around and causing customers to pay costs  
21   that they shouldn't. And I think this is one -- the  
22   capital structure system is one thing that keeps that  
23   from happening.

24          COMMISSIONER MURRAY: Thank you.

25          JUDGE DERQUE: Recross based on Commission  
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1 questions?

2 Mr. Finnegan?

3 MR. FINNEGAN: No questions.

4 JUDGE DERQUE: Mr. Mills?

5 MR. MILLS: I don't believe so. Thank you.

6 JUDGE DERQUE: And the Staff?

7 MR. WOODSMALL: No questions.

8 JUDGE DERQUE: Redirect, Mr. Swearengen?

9 MR. SWEARENGEN: Just a couple, your Honor,  
10 if I may.

11 JUDGE DERQUE: Why don't we pause just a  
12 second.

13 Go ahead, Mr. Swearengen.

14 REDIRECT EXAMINATION BY MR. SWEARENGEN:

15 Q. Mr. Dunn, on that last point you were  
16 making, is it your testimony -- or you indicated that  
17 the company, that UtiliCorp ought to be in these  
18 different boxes and each ought to have its own capital  
19 structure and its own return. And you also said that  
20 some of the business undertakings and enterprises of  
21 UtiliCorp are riskier than the Missouri Public Service  
22 operations. Is that what you said?

23 A. Yes, sir.

24 Q. Now, what was the point that you were trying  
25 to make with respect to how the Missouri divisional



1 capital structure that the company is proposing in  
2 this case would serve to protect Missouri customers  
3 from the potential higher risks of the other business  
4 undertakings?

5 A. There's at least two ways. One is that  
6 UtiliCorp acquires a lot of large companies or has in  
7 the past acquired a large of large companies. Those  
8 acquisitions cause the equity ratio to go up and down.

9 When a division equity ratio and capital  
10 structure is established and locked in, as it has  
11 been in this case and as it has been for the last  
12 10 years, there's not extraneous movement in the  
13 capital structure as a result of the other things that  
14 are going on in the UtiliCorp.

15 So that insulates the electric utility from  
16 all of the other activities in the Company. That's a  
17 benefits. And it protects the customer from the cost.

18 And then I think separate from that, the  
19 risks that other entities may have simply just don't  
20 flow into UtiliCorp, because we've structured an  
21 analysis based upon comparable electric utilities.

22 I think all three of the analysts here have  
23 used the same -- sort of the same group of companies  
24 to establish a return. So we're not finding a return  
25 based on any entity that might be more or less risky.

1 We're not looking at UtiliCorp. We're looking at  
2 electric utilities that are sort of like MoPub.

3 Q. Thank you.

4 I think it was in response to a question  
5 from Commissioner Murray, I believe. You said that we  
6 won't be doing this kind of thing five to ten years  
7 from now. What did you mean by that?

8 A. Well, what I see happening in this -- and it  
9 doesn't -- obviously it's just one person's opinion,  
10 but it seems like to me that there will be a healthy  
11 dose of competition injected into the retail electric  
12 operation.

13 Now there's going to be regulated pieces in  
14 there. The distribution properties might be  
15 regulated. There's a number of things that will be  
16 regulated.

17 But, oh, I don't know if this case has a  
18 redispatch of power plants in it or a big  
19 determination of whether or not there should be  
20 maintenance on Sibley or no maintenance on Sibley,  
21 those kinds of issues that consume so much time, and  
22 where the Commission is bogged down, I think, in a lot  
23 of detail of accounting data and things like that, I  
24 don't think that will happen in the future.

25 In the future the Commission will be worried

1 about and concerned with the levelness of the playing  
2 field. Have I got a good strong, incumbent company  
3 out there forcing the price down? Have I got -- am I  
4 permitting that company to compete as vigorously as it  
5 can?

6 Those are the kinds of things I think the  
7 Commission will be more concerned about, trying to  
8 maximize the benefits that come out of Commission --  
9 out of competition.

10 Q. I think it was Mr. Mills that asked you and  
11 you referred to page 32 of your direct testimony about  
12 some subsidiaries that are shown under Column A and  
13 Column B, and I'm not sure exactly what his question  
14 was, but I think it was along the lines of, can the  
15 subsidiaries or can they not issue stock? Do you  
16 recall that question?

17 A. Yes, I do.

18 Q. And I think you said it was irrelevant?

19 A. Yes.

20 Q. Was that your answer?

21 A. That was my answer.

22 Q. And why is that irrelevant?

23 A. I don't think the fact that a company issues  
24 debt on its own has anything to do with the proper  
25 financing in the company if it's a wholly-owned

1 subsidiary. Just because the company issues some  
2 debts doesn't change the rules. The rules for this  
3 kind of work -- and, you know, for something that has  
4 an absolute right or wrong, there's a lot of  
5 discussion about this capital structure issue, but the  
6 bottom line is that the way you go about doing capital  
7 structures, if you're going to be involved in applying  
8 mainstream finance theory, is that you develop a  
9 capital structure for each of your projects or  
10 activities and a project can be everything from a  
11 subsidiary to buying a computer. And you developed a  
12 capital structure for each of those pieces and you  
13 total it up and that's what you are. That's your  
14 consolidated structure.

15           It doesn't make any difference whether those  
16 pieces are publicly traded, partially publicly traded,  
17 issued their own debt. That's an old throwback to the  
18 concept of who owns the capital determines the cost.

19           And the cost of capital is a function of the  
20 risk and where it's invested. It's not a function of  
21 who owns it.

22           Q. I think you were answering about the  
23 issuance of debt, and my notes indicate that Mr. Mills  
24 asked you about whether or not those subsidiaries  
25 issued stock, and your response was, irrelevant.

1                   Would your answer be the same for stock as  
2     you've just explained for the issuance of debt?

3           A.       It certainly would. And Aquila is a good  
4       example that parallels it. Aquila has stock that is  
5       owned by UtiliCorp, and it has stock that's owned by  
6       the public.

7                   Both of those owners deserve the same return  
8       on that equity. It doesn't make any difference that  
9       one is UtiliCorp and one is a group of individuals.

10 Q. One last question, Mr. Dunn. I think in  
11 response to Chair Lumpe, you made a couple of  
12 comments. You said at one point there are some things  
13 that need to be amortized, and you didn't go ahead and  
14 explain what you meant by that, and then you also said  
15 there were actions which this Commission could take  
16 now in this case that in your opinion would not be in  
17 conflict with what the joint task force might  
18 recommend or not recommend.

19                   What did you mean by those two statements?

20           A.     UtiliCorp or Missouri Public Service, almost  
21     every regulated entity in the United States, has  
22     regulatory assets. And Missouri Public Service has  
23     some regulatory assets that were created by action of  
24     the Missouri Commission.

25                    Those regulatory assets are appropriate  
895

1 under the fully regulated scheme that we're in today,  
2 and those regulated assets will not generate revenue  
3 and will not work, not be valuable under a partially  
4 competitive scheme.

5 Now, between here and there, between full  
6 regulation and competition, something has to be done  
7 with those assets. And I think what I have suggested  
8 is that if, in fact, there is a rate reduction that  
9 comes out of this proceeding, that that rate reduction  
10 be used at least in part or substantially or to some  
11 degree to reduce those regulated assets or regulatory  
12 assets, so that UtiliCorp and Missouri Public Service  
13 don't go into the next era with an overburden which  
14 keeps them from becoming a vigorous competitor.  
15 Because that I think that will stop the benefits of  
16 competition from flowing.

17 Q. And why is that?

18 A. I think what is going to happen in the  
19 future is that you're going to have the incumbent  
20 electric utility, and that will be a company like  
21 Missouri Public Service or Union Electric or one of  
22 the other companies, Empire, St. Joe, those will be  
23 the incumbent electric utilities in their service  
24 areas.

25 As competition comes in, new companies will

1       come into those markets, and presumably they'll be  
2       capable of charging lower prices than the incumbent  
3       utility. Well, they'll only charge enough lower price  
4       to get enough business. They won't necessarily charge  
5       the lowest price they can get. If the incumbent  
6       utility is handicapped, they won't be able to lower  
7       their price further.

8               And if they don't have adequate financial  
9       strengths, they won't be able to become a vigorous  
10      competitor and lower their price to compete on a price  
11      basis with these new companies. And so we'll end up  
12      sort of settling, if you will, on an equilibrium,  
13      where the price is not as low as it could be.

14             MR. SWEARENGEN: Thank you very much.  
15      That's all I have.

16             JUDGE DERQUE: Thank you, Mr. Swearengen.

17             Thank you, Mr. Dunn.

18             Well, let's go off the record.

19             WHEREUPON, the hearing of this case was  
20      adjourned until 8 a.m. Monday, December 15, 1997.

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