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In the Matter of the Tariffs of Aquila, Inc., d/b/a Aquila Networks - MPS and Aquila Networks - L&P Increasing Electric Rates for the Services Provided to Customers in the Aquila Networks - MPS and Aquila Networks - L&P Service Area	Case No. ER-2007-0004

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REGULATORY LAW JUDGE
JEFF DAVIS, Chairman,
CONNIE MURRAY,
STEVE GAW,
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P R O C E E D I N G S

JUDGE vOSS: All right. We'll go ahead and start with opening statements on the issue of ROE. Let me -- and we will go on the record. We are on the record in Commission Case ER-2007-0004, and we are going to begin with opening statements on the issue of ROE, beginning with Aquila.

OPENING STATEMENT

BY MR. SWEARENGEN:

MR. SWEARENGEN: Thank you, Madam Law Judge and Members of the Commission who are not here today, but hopefully are listening at home on their computers.

I am Jim Swearengen, appearing on behalf of Aquila in this case on the cost of capital issue, which is before you this morning.

I think everyone is aware that Aquila, in this case, is requesting that its Missouri Public Service and light and power operating divisions be authorized a return on common equity of 11.25 percent.

The company's witness on this topic is Dr. Sam Hadaway. I think the Commission is familiar with Dr. Hadaway. He was the Aquila rate of return witness in Aquila's last case, which was resolved back in 2006. And more recently, he testified on behalf of Kansas City Power & Light Company in its rate case, which the Commission decided back in December of 2006.

And as my good friend, Mr. Kevin Thompson, has pointed out to you earlier in this proceeding, the word that the Commission used to describe Dr. Hadaway's credentials in its report and order in the KCPL case was impeccable. So we have a witness today with impeccable credentials.

In any event, Dr. Hadaway's initial ROE recommendation which he prepared in connection with the initial filing back in June of 2006 supported a return on common equity of 11.5 percent.

However, in his rebuttal testimony, which was filed in February, he explained how he updated his initial studies through December of 2006 with a resulting 25 basis point net reduction, which takes his ROE recommendation from 11.5 to 11.25.

In summary, this 25 basis point reduction reflects the update in Aquila's construction requirements, which increased and had the effect of raising the ROE. And his update also reflects the lower capital cost environment, which now exists as compared to the time when he filed his initial testimony. And that has the effect of lowering the required return on equity.

So combining these two factors, you come up with a 25 -- with a net 25 basis point reduction in the ROE, and that gets it to 11 and a quarter.

Now, while Dr. Hadaway's recommendation may have been reduced by 25 basis points, his method of calculation -- of calculating that return has made -- has remained consistent throughout his testimony in this case and also consistent with the approach that he used in the Kansas City Power & Light case.

In this case, as in the KCPL case, Dr. Hadaway's ROE proposal is based on alternative versions of the DCF model. His recommendation is further confirmed by his risk premium analysis and his review of projected interest rates and current economic conditions.

With regard to Aquila, I think the Commission is aware that the DCF model cannot be applied directly to the company because Aquila does not currently pay dividends to its shareholders.

For this and other reasons, Dr. Hadaway applied the DCF model to a reference group consisting of 24 investment grade electric utilities. The ROE calculation that resulted from that comparison, his base ROE calculation, if you were, was 10.75 percent. And to that 10.75 percent ROE, he has added 50 basis points for Aquila's construction risk to get to his ultimate 11.25 percent recommendation.

Now, I think the evidence in this case will show that the average authorized return on equity for electric utilities in 2006 was approximately 10.36 percent. And there may be evidence introduced to show that for the first quarter of the year, for the first quarter of 2007, that that number has come down a little bit, to perhaps 10.3 percent.

But in any event, applying what we refer to as the zone of reasonableness concept that this Commission has utilized in recent cases and using these numbers as a starting point, this would indicate that an ROE zone of reasonableness in this case would be from approximately 9.3 percent to approximately 11.3 percent.

Given those facts, it's clear that the 11.25 percent recommendation that Dr. Hadaway support falls within the zone of reasonableness, although it's clearly on the high side. So some may ask why this company -- why Aquila should be awarded an ROE of 11.25 percent, which is at the high end of the zone of reasonableness and about 90 basis points above the 2006 national average.

Or stated another way, some may say why should Aquila get a return on equity, which is -- which would appear to be identical to what this Commission recently awarded the KCPL, and close to the 10.9 percent, which the Commission awarded the Empire District Electric Company back in December of 2006.

A quick response to that may be simply to turn the question around and to say, Why not? But beyond that answer, there are several other, we think, good reasons why the 11.25 percent ROE is clearly justified.

First, Dr. Hadaway's recommendation, we believe, is the most reliable proposal that you have before you in this case. By contrast, the recommendation of the Staff witness, David Parcell, which is 9 percent to 10.25 percent with a mid point of 9.625, we believe, is based on a method that is inconsistent with recent findings and conclusions of this Commission involving cost of capital and is otherwise flawed.

The 10.0 ROE recommendation of Michael Gorman, who is the witness for some of the other intervenors, may be a little closer to the mark, but we think it also is unreliable for reasons that have been spelled out in the company's testimony and will be further developed in the hearing.

Second, I think it's important to -- to note that an 11.25 percent ROE for Aquila in this case is not necessarily the same as KCPL's 11.25 percent. I say that because the Commission awarded KCPL that ROE based on a capital structure consisting of 53.69 percent equity.

And at the same time, when the Commission issued its decision in the Empire case, Empire's nine -- excuse me -- 10.9 percent return on equity was applied to a capital structure consisting of 49.74 percent equity.

By way of contrast in this case, the 2006 year end, the Aquila corporate capital structure, which the Staff and company support for purposes of setting rates in this case, consists of only 48.17 percent equity. So I think it's clear that, relatively speaking, when compared to Kansas City Power & Light Company and Empire, Aquila's capital structure can be described as equity thin.

This, of course, indicates a greater risk and would justify even a higher return on equity. Stated another way, an 11.25 percent return for KCPL is really a -- a higher award than a similar ROE for Aquila.

Third, like Kansas City Power & Light Company, Aquila is a partner in the IATAN II power plant. And, consequently, the company has significant capital needs in connection with that and other construction projects.

Dr. Hadaway has characterized that in his testimony as construction risk. And you will recall that I noted earlier, he has made a 50 basis point upward adjustment to his ROE recommendation to account for that risk. That's how he gets from the 10.75 to the 11.25.

I think this is a very critical point in his analysis, and I'm sure that the Commission will want to ask him some questions about that.

Fourth, another point I would make is that Aquila's small sized, vis-a-vis, Dr. Hadaway's proxy group indicates some greater risk and higher return on equity, although Dr. Hadaway did not make an upward adjustment to his ROE recommendation to account for this. But this is something that the Commission could consider.

And in addition, and along those lines, like the Empire District Electric Company, Aquila is heavily dependent upon natural gas in the generation of electricity and is, therefore, subject to the risk and cost of fluctuations in that fuel as well as other fuels. But, again, Dr. Hadaway did not make an upward adjustment to his proposed return on equity for that risk either.

And that is because most of the companies that make up proxy group have fuel recovery mechanisms, and his return on equity recommendation is based on the assumption that Aquila will get the fuel adjustment mechanism that it seeks in this case.

Fifth, I think the evidence in this proceeding will demonstrate that Aquila's asset sale strategy has significantly improved its balance sheet position and will provide much improved access to the capital markets to support its utility infrastructure investments.

I think it could be said that Aquila is on the way to restoring its financial integrity, which should ultimately lead to an increase in investment grade biograding.

And, finally, not withstanding the problems that the company has dealt with over the last several years, the Commission, I'm sure, is aware that the recent Commission staff management audit confirmed that no identifiable customer detriment has resulted --

MR. WOODSMALL: Your Honor, I'm going to object. He's bringing evidence into the record that no one has seen in this case.

JUDGE VOSS: I know that attorney comments don't count as evidence that can be considered by the Commission, so -- but keep that in mind, Mr. Swearengen.

MR. SWEARENGEN: Thank you. And I think in addition to that and along those same lines, the records in this proceeding will recollect that the company has experienced no what I would call formal customer complaints for quite some time, perhaps years.

So given all this, we think the 11.25 percent is clearly justified.

Let me touch briefly on another cost of capital issue that is before the Commission apparently, and that is capital structure. Although I have to confess, I am not sure what to say to you about the extent to which it really is an issue. I'll have to leave it to -- to the other parties to develop that point.

But I will tell you that Aquila, through its testimony in this case, continues to support the historical approach to determining an appropriate capital structure. And that is to say, Aquila continues to support the capital structure that results from the capital assignment process, which is 52.5 percent debt and 47.5 percent equity.

Now, this exact issue has been litigated before this Commission several times. And when I say that, I mean, the -- the issue between the assigned capital structure approach to determining capital structure as opposed to the actual corporate capital structure.

I think it was back in 1993 in a case before this Commission that the company prevailed on that issue. But since then, when litigated, the company has lost that issue. And the Commission has utilized Aquila's actual corporate capital structure for purposes of setting rates.

So as a result of that, and for purposes of a settlement of a number of issues in this case, the company has agreed with the Staff for rate-making purposes in this case to utilize Aquila's 2006 year end corporate capital structure, which consists of 51.83 percent debt and 48.17 percent equity.

Now, some of the other parties may argue for a corporate capital structure based on some other point in time or for a hypothetical capital structure based on the company's capital assignment process or something else. I'm not real sure. You're going to have to ask them about that.

Finally, on the list of issues under cost of capital was an item called cost of debt. My understanding is that's no longer contested. The cost of debt to the Aquila Networks MPS division is 6.668 percent, and the cost of debt for the L&P division is 7.8698 percent. And these figures are based on the debt which has been assigned to the -- to the divisions of 2006 year end.

That concludes my opening statement on this issue. Thank you.

THE COURT: Thank you. Staff?

MR. THOMPSON: Thank you, your Honor.

JUDGE VOSS: And since there are a few attorneys that don't regularly practice here, at least a couple, opening statements are not cited in briefs. They have no evidentiary value. Please proceed, Mr. Thompson.

BY MR. THOMPSON: Thank you, Judge, and thanks for that caution. I appreciate that.

OPENING STATEMENT

BY MR. THOMPSON:

MR. THOMPSON: Staff agrees that Dr. Hadaway's credentials are, indeed, impeccable. For that matter, so are the credentials of Mr. Parcell. So are the credentials of Mr. Foreman. Each of these three ROE expert witnesses is, indeed, an expert, a recognized expert and has every right to offer a recommendation to this Commission.

I will point out, as I have before, that there is a striking positive correlation between the recommendation each of these experts have produced and the desire of the party they represent.

Aquila, the company, would like to have a high ROE. And oddly enough, Dr. Hadaway has produced the highest recommendations.

The intervenors would like to see a low ROE, as would Staff. And oddly enough, those two experts have produced low recommendations. I don't know what that means. Maybe someone could write a dissertation on that.

This Commission uses as an analytical tool the concept of the zone of reasonableness. I have a chart here that sets out the recommendations made by these experts simply drafted against the zone of reasonableness.

And I think a striking thing that the Commission should take into account is the fact that Staff's representation and the recommendation of the intervenors are both below the average, the mid point for the year

2006, 10.36 percent, and Aquila's are above.

And Aquila's most recent recommendation, the one that is in Dr. Hadaway's rebuttal, is within but at the high end of the zone of reasonableness.

Now, if you're going to use the zone of reasonableness analysis, I think, logically, it means you start at the average. The average is 10.36. So what are the factors that would require the Commission to deviate from that average either up or down in the case of this company?

Now, in the Kansas City Power & Light case, we heard a lot of testimony about what a great company it was and how that should be reflected in its ROE. I think we're all agreed that that particular factor doesn't apply here.

Well, another factor we hear about is risk. Aquila's riskier. Well, partly, that's because of construction. It's planning to do a lot of constructing. And partly that's because it's smaller than the comparable companies. And those are both real factors.

But I suggest to you that those factors are implicitly included in these recommendations. I think most telling is the fact that if you look at the return on equity awards given over the past year for electric utilities, you will see that -- that leaving out of consideration of a -- an 11.9 percent award for a wind generation facility that this Commission's award to Kansas City Power & Light of 11.25 percent was the highest. The highest.

And now Aquila is asking for exactly the same award. And don't be confused by Mr. Swearengen's assumption that 11.25 for Kansas City Power & Light and 11.25 for Aquila are, you know, two different things. 11.25, 11.25. They look a lot the same to me.

There is no reason that you will hear that will support an award to this company that is at the very top of awards made in the nation to electric utilities. It is not the riskiest electric utility. I haven't heard that it is the smallest electric utility. And it certainly ain't the best electric utility.

I think the Commission will find the appropriate return on equity award somewhere between 10.36 and 9.36 as recommended by Staff witness Parcell and the intervenors' witness Gorman. Thank you very much.

JUDGE VOSS: Thank you. Public counsel?

OPENING STATEMENT

BY MR. MILLS:

MR. MILLS: I'm going to continue the trend of ever-shorter opening statements. I will be nowhere near as long as Mr. Swearengen and not even as long as

Mr. Thompson.

Public Counsel's witness supports the testimony of Staff witness Purcell's and intervenors' witness Gorman. As -- as Mr. Thompson pointed out, they fall in the right area of the zone of reasonableness, and I believe their testimony is credible and well-supported.

The testimony of Public Counsel witness Trippensee on the return of equity issue essentially ties return on equity to the award of a fuel adjustment clause.

If the Commission awards Aquila a fuel adjustment clause, although Public Counsel has recommended that you do not, that would have a significant impact on the riskiness and the variability of -- of Aquila, and that should be recognized through an adjustment return on equity.

Another issue that -- that I'd like to touch on that Mr. Swearengen touched on briefly is the management audit. The Commission -- the Commission Staff's report on the management audit of Aquila did not find any demonstrable monetary harm to ratepayers from a number of management mis-steps, miscalculations, misadventures. What have you.

But they also did not find that there was a great deal of attention being paid to Missouri ratepayers. And, in fact, their conclusion was the only reason

Missouri ratepayers were not harmed by all of these management adventures was through the action of the Commission Staff and the Commission itself.

That type of behavior certainly does not deserve a rewarding ROE. It should, if anything, allow Aquila an ROE that is just barely sufficient.

And the Commission should bear in mind that it's quite likely that whatever return on equity that is awarded in this case will be quickly over taken by events if, in fact, in the Commission approves the acquisition of Aquila by Great Plains Energy.

If that acquisition does get completed, Aquila will almost automatically and overnight become investment grade regardless of what the ROE awarded in this case is.

In addition, if that acquisition is approved by the Commission, Aquila and KCPL have projected enormous cost savings as a result of that acquisition so that the actual expenses of Aquila will be -- will be much, much lower following that acquisition. And so the need to provide a return to shareholders through an elevated ROE will be much lessened. Thank you.

JUDGE VOSS: Thank you. Sedalia Industrial Energy Users Association?

MR. WOODSMALL: Thank you, your Honor. I'll even be more brief.

OPENING STATEMENT

BY MR. WOODSMALL:

MR. WOODSMALL: As you consider this case, I'd ask you and the Commission to keep two words in mind, objective and subjective. In the exercise of your responsibility on this issue, there is a big difference between an objective study, which is designed through the use of widely available and acceptable data to arrive at an answer of an appropriate ROE.

Misters Gorman and Parcell have provided you such an objective study. In contrast, there's a subjective study presented in the record, that study which is based upon mere assessments designed to reach a particular result.

Mr. Hadaway has provided you such a subjective study. Rather than widely available and accepted data, Mr. Hadaway has provided you his personal belief as to stop growth rates, his projection on inflation, his projection of GEP, his projection of the equity risk premium and his opinion of the costs of no risk debt offerings.

Then when he's almost done, he subjectively increases the ROE based upon some measure of risk associated with Aquila. Subjective.

In fact, the company's requested ROE is so subjective that it made an unsupported modification to its position in its rebuttal in order to slide back within the zone of reasonableness.

The company made a 25 basis point downward adjustment in its ROE. This subjective adjustment was to avoid the hard and fast applicability of the zone of reasonableness.

In this case, SIEUA and AG Processing asks you to avoid the subjective, self-serving analysis and utilize the objective analysis proposed by Mr. Gorman. Thank you.

JUDGE VOSS: Thank you. I don't believe the Commercial Group is here on this issue. Federal Executive Agencies?

OPENING STATEMENT

BY CAPTAIN HOLLIFIELD:

CAPTAIN HOLLIFIELD: Good morning. May it please the Commission. This morning we're starting a process where we set a rate at which Aquila can realize a return on its rate base.

I don't have to tell you that this is a key point. There's big money involved. In the context of what we've discussed before, this is a crucial point at which -- at which we encourage optimal economic behavior.

In other words, as we've discussed before, it's essentially like motivating the young adult to learn how to budget and to act responsibly.

And I can't think of a better frame of reference than Mr. Thompson's chart. You've got somebody that's learning the budget. Do you bail out folks that maybe are still a little lower on the learning curve at the top end of it?

Do you keep throwing money into the account so they can keep tossing that card into the ATM machine, or do you encourage more optimal economic behavior by moderating it, by allowing for that individual to develop their own skills at managing their money?

There's a huge gulf in my analogy in the situation here. But I would respectfully submit that it's a human enterprise and that it does apply. That's just an analysis.

Even the company's witness, Dr. Hadaway, admits in his testimony that whether it be his process or any of the processes, they're not the subject of absolute precision. I wouldn't go so far as to say it's sausage making because it's not. It is a science.

But we're talking about numbers here. It's like statistics. You can weight the scale, depending on your motivation.

And as Mr. Woodsmall stated and as Mr. Thompson has stated, that is true under these circumstances. Look at the motivations that we're dealing with.

But the guidance is simple. Look at the tests that are outlined and the seminal cases at play here. There are two parts of the test, not just one. There are two parts.

Of course, formulate the return based on the company's need. But, second, look at the return with reference to what is required to similarly situated companies. It's a normative judgment here. And it's this normative judgment that is not based on geographical restraint.

We don't just look to KCPL and Empire. We look to similarly situated companies within a meaningful group. Dr. Hadaway, again, in his testimony acknowledges both parts of this test.

I urge you to pay heed to it.
It's the way that we would -- it's the way that we have to go through the process to formulate the rate of return. And it takes into account both factors, not just risk, risk, risk, risk, risk, risk, but takes into account risk, but look at it in the con -- in the overall context.

You have this range before you, an average of 10.36 percent extending 100 basis points up to 11.36 percent and down to 9.36 percent.

Before simply assigning the company exactly what they ask for first, where does the figure fall within the zone of reasonableness? Again, keep in mind what Mr. Thompson said.

Second, where does the -- where does the figure that they're asking for fall within the overall norm? And third, where does it fall -- where will it incentivized optimal economic behavior in this situation?

Does this Commission reward questionable economic practice by simply bailing out the proverbial young adult, or do we provide for steady, sustained growth that accomplishes, yes, the goals of the company under Hope & Bluefield, yet treats the ratepayers fairly. Thank you.

JUDGE VOSS: Thank you. I believe that's the last party on this issue that will make an opening statement. Is there anyone else that needed to make an opening statement? I did not think so. Aquila, you can call your first witness.

MR. SWEARENGEN: Thank you. We would call Dr. Hadaway at this time.

SAMUEL HADAWAY,

being first duly sworn to testify the truth, the whole truth, and nothing but the truth, testified as follows:

DIRECT EXAMINATION

BY MR. SWEARENGEN:

JUDGE VOSS: Please be seated. Mr. Swearengen, your witness.

MR. SWEARENGEN: Yes. Thank you.

Q (By Mr. Swearengen) Would you just state your name for the record, please?

A Samuel C. Hadaway.

Q And, Mr. Hadaway, by whom are you employed and in what capacity?

A I'm a principal in the financial consulting firm, Financo, F-i-n-a-n-c-o.

Q And where is that based?

A In Austin, Texas.

Q Thank you. Did you cause to be prepared for purposes of this proceeding certain direct, rebuttal and surrebuttal testimony in question and answer form?

A Yes.

Q And do you have copies of that testimony with you this morning?

A Yes, I do.

Q Your direct testimony has been marked as Exhibit 13. Your rebuttal testimony has been marked as Exhibit 14. And your surrebuttal testimony has been marked as Exhibit 15.

Do you have any corrections or changes that you need to make with respect to any of those testimonies this morning?

A No, I do not.

Q And if I asked you then the questions that are contained in those testimonies, would yours answers this morning be substantially the same?

A Yes.

Q And they are true and correct, to the best of your knowledge, information and belief?

A Yes.

MR. SWEARENGEN: With that, your Honor, I would offer into evidence Exhibits 13, 14 and 15 and tender Mr. Hadaway for cross-examination.

JUDGE VOSS: are there any objections to those exhibit?

MR. THOMPSON: No.

JUDGE VOSS: Then Exhibits 13, 14 and 15 are admitted.

(Exhibit Nos. 13, 14 and 15 were offered and admitted into evidence.)

JUDGE VOSS: I believe the first witness -- first on cross by counsel is the Federal Executive Agencies.

CAPTAIN HOLLIFIELD: Okay, your Honor.

CROSS-EXAMINATION

BY CAPTAIN HOLLIFIELD:

Q Good morning, Dr. Hadaway.

A Good morning.

Q I have to confess that a lot of my questions are going to come straight from your text, so we'll probably be flipping through your direct, rebuttal and surrebuttal if we could.

And I will ask you a couple of times to read into the record to make sure that I'm not misquoting you. Is that all right with you?

A That's fine. Thank you.

Q Okay. First, in your direct testimony, if you would turn to page 3, in response to the question, Please summarize your cost equity studies and state your overall rate of return recommendation.

If you would please read the sentences running between lines 6 through 11?

A Beginning with, That is to say.

Q Yes, sir.

A That is to say, the return authorized by utility by regulatory body such as this Commission -- such as the Commission should be commensurate with return on investment and other enterprises having corresponding risks.

The return should also be sufficient to ensure confidence and the financial integrity of the utility so as to maintain its credit and attract capital so that it is able to properly discharge its public duties.

Q And you understand this to be, at least generally, a distillation of the tests that we're looking at today; is that not correct?

A Yes, sir. That's my understanding.

Q The part of the sentence appears to be what I had referenced before as, you know, the part of the test that addresses the need of the utility. Is that not a correct assessment?

A It addresses the facility's financial condition I think is the way most economists think about that.

Q And what they would need to -- in the context of their financial condition in the way of a rate of return?

A I'm pausing just a little bit --

Q Okay.

A -- trying to think about the word "need" as you're using it. Certainly, the company's construction program and their need to assess and access the capital markets is part of that need, if that's what you mean.

Q That's -- it's -- that's fine. And I do take responsibility for being somewhat inartful in doing that, in phrasing that and I defer to your explanation on that.

My -- I guess what I was really curious about was the first sentence. And the first sentence appears to have, you know, kind of a breaking effect on the second part of the test. You know, if you were to read them out of order, it looks like you -- you know, look at what the company needs, and you look at the second sentence, and it says, But look at what return is being given to other similarly situated entities.

Is that not a normative effect on the second part of the test or the other part of the test?

A Some people look at the second sentence as being sort of necessary condition. If a utility is going to lose its bond rating because of too low of rate of return or other factors related to the rate-making process, then that decision by the regulator may be subject to criticism.

The first sentence is a little more general in the sense that it says a utility should be allowed a return that is commensurate with that being issued by other kinds of companies, not just utilities, but others who have those corresponding risks. So it's a little more general, I think.

Q Okay. But it does have some sort of limiting effect on that anyway, does it not? If you just had that one part of the test, you could set the rates according to you know -- I'm going to inartfully say again -- need?

A Are you talking about the second sentence or the first?

Q The second sentence?

A If you just had the second sentence, one might look at the ratios as we did in my direct testimony and say, Will this maintain a given bond rating? And that's sort of a bottom line test.

If it will not, then a Commission typically will up the rate of return to meet that need, the construction need.

Q But that first sentence says you still have to make it commensurate with other similarly situated corporations?

A As I said, that's a general statement. But then the further assessment proposed that's stated in the second sentence, maybe that's why they're stated the way they are, you know, sort of sets a floor.

So even if other companies around the world are getting 10.36 percent on average, if a given company's construction budget is much higher, as this one is, twice as high as the company is about to use, then adjustments to that average for all the other companies may be made.

Q But as you said, it generally works both ways; is that not correct?

A No. No. I didn't mean to say that. It's that the second sentence is more of a floor. It's kind of you must satisfy the financial integrity constraint, and, typically, regulatory processes will do that.

But sometimes it's necessary to adjust upward from the numbers that just the average company is getting because of higher risk of the subject matter.

Q Okay. In your rebuttal testimony, if we could turn to page 4 --

A I have that.

Q You do have that?

A Yes, sir.

Q Okay. If you would read the -- the last two sentences of that, starting with, In Missouri Gas Energy.

A I might be on the wrong page. I'm sorry. Just give me a moment.

Q It's your indented paragraph where you're citing Cases ER-2006-0314 at pages 20 through 21?

A Yes. I see that now. In Missouri Gas Energy, the Commission stated that it does not believe that its return on equity findings should in quotes, unthinkably, mirror the national average, closed quotes.

Nonetheless, the national average is an indicator of the current market in which KCPL will have to compete for necessary capital.

Q Okay. And you refer to it in the next sentence below the indented paragraph as a reasonableness check; is that not correct?

A Yes, sir.

Q If we could go to page 16 through 21 of your direct testimony in which you discuss the financial integrity -- and I'm -- I'm going to kind of go out on a limb here. It appears to me in my reading of pages 16 through 21, you're focusing on the risks posed to the company when you're outlining the financial integrity part of your testimony. Is that a fair characterization?

A I don't think that's the way I thought of this section of the testimony. I think of this as being what's in regulatory economics textbooks so where economists cite things from the law not as legal matters but just as economic matters as the basis for what to do.

Q Okay. Let's look at the first sentence on page 20 after yes. It's a response to the question, Does the electric industry utility -- electric utility industry's evolution toward competition affect financial integrity.

You referenced increased business risk from less predictable revenues must be offset by less financial risk. What --

A Yes, sir. I see that.

Q Okay. What is -- can you just go over that for me?

A Yes. The markets for utility securities have been much more volatile in the last five years in particular. And deregulation, even though it doesn't touch all states, has affected the power markets across the whole country.

The view of the electric utility industry has generally become that it is a more risky place than it was, say, prior to the year 2000. It's not an exact date, but something like five years ago.

And so that's what I'm referring to. What we see is that equity ratios on the financial risk side of most utility companies are improving, that is, companies are adding to percentage of capital to leverage their capital structures.

So to offset the operating risk, they decrease their financial risk. The average from a comparable group is a capital structure with about 48 and a half percent equity, and it's projected to go to about 49 and a half percent equity over the next three to five years.

Q Okay. In general, aside from the group of numbers that you -- or the methods that you criticize that Mr. Gorman and Parcell used, do you not criticize both of their conclusions because they are -- they inadequately address the risk that is faced by Aquila?

A They both refused to make any addition to their comparable rates, which is clearly less risky than Aquila.

Q Okay. I'm going to go back to your direct. In selecting your proxy group, you make a comment on page 4 of your direct basically starting at line 17 and running through 23.

Is it a fair characterization that you are qualifying the use or caveating the use of your proxy group because they are not, in your assessment, sufficiently representative of Aquila?

A That's not exactly the way I would think about it. I do a base rate of return on equity for the comparable group, 24 companies. I would have minimal investment grade bond rating, or that's the minimum rating that's allowed, have some other filters that we use.

But we select a very large group that I think is representative of average risk utilities in that group. Then we look at Aquila's particular construction program, and we find that it is relative to its existing net plant, twice as big as the average construction program for those comparable companies. And that's the adjustment that I made. That's the 50 basis point.

Q But the simple fact is you choose a group, and then you say, Yes, I'll use this group, but there is a caveat, and that is, they're smaller and they face different construction risks; is that not correct?

A Their -- their construction risks are smaller than Aquila's construction risks, yes.

Q Okay. I -- I read through your direct testimony, your rebuttal and your surrebuttal. And aside from your proxy group and aside from Aquila's references to KCPL and Empire, I don't see any sort of -- sort of, you know, comparison to other similarly situated utilities.

I mean, your proxy group is okay, but it doesn't represent the small size and the risk. So you -- you make an adjustment there. But there's -- there's nothing other than those two other companies in Missouri. Is -- or am I missing something?

A Well, we may not quite be on the same page. I think we do exactly what you may be saying we didn't do. We collected companies with a minimum investment grade bond rating because that's the way Aquila's rates are made, even though it does not have an investment grade bond rating, its cost of debt and cost of equity because we're using the cost of group are based on that as a criteria, if you will.

Then we also look for companies that have at least 70 percent of the revenues from regulated activities. At times, Aquila, obviously, has not had that necessarily existing characteristic. But the regulated piece of it, Missouri Public Service and Light & Power that we're setting rates for here are in that regulated business.

So we try to make the comparable group. And I do this, and Mr. Gorman and Mr. Parcell, we all do this similarly. I have a little trouble with Mr. Parcell's group only being five companies, but Mr. Gorman's is only nine.

I don't restrict my group down to small sizes because, statistically, that can be a problem. And sometimes one is questioned about some activity and one knows that. So it's not an issue. No one has criticized my group that I know of. But I think it does represent just for minimum investment grade companies the best average assessment that you can do.

Q But you're asserting that that also means that Con Edison, the Southern Company and Excel are similarly situated. I'm from the south and I know the southern company covers Alabama, Georgia, Florida and probably some other parts of the Florida that aren't covered by TDA.

And Con Edison, as best I recall, covers a good portion of the northeast. Are we asserting that they're similarly situated?

A The average of the group represents those companies that Aquila and all other similarly situated utilities we compete with in the capital markets. Con Ed is in New York City. And the only other state -- southern company that I know of is that you didn't mention is Mississippi.

The other company's group, the other 22 additional companies, are spread out all across the United States, and they represent the average risk minimum investment grade set of companies that compete for capital just like Aquila.

Q And yet they're so similarly situated that you have to do the add for construction risk; is that not correct?

A The adder for construction risk is demonstrated initially in my Schedule 1, and it's updated in my rebuttal schedule. I don't remember the number right now, but it shows that Aquila's construction relative to the existing -- to the existing net plant is twice as large as average for companies in the group.

Q Okay. In choosing your group, I want to go back to page 3. Describe how you chose the group?

A Yeah.

Q Starting with the last line on page 3, you referred to a large sample reference group selected from the Value Line investment survey. Is -- how was that group chosen and -- well, how did you choose that group?

A The Value Line part of it or the smaller --

Q Just that group. It appears to me that it's part of a larger universe of companies based on the language you use in your testimony.

A Yes, sir. The -- the Value Line follows all the major electric utility companies that are publicly traded, and there are about 61 or two of those now.

Out of that 61 or two company group, we look, No. 1, to see if they have an investment grade monitors. Some of those companies do not. Then to be used in the discounted cash flow model, companies have to be paying dividends currently.

So if a company has cut its dividends or changed it in the last two years, we include that company. Then to focus in more on the regulative piece of the business, we applied 70 percent regulated revenues as percentage of total revenues filter. Those are the three things we do.

Q Right. And I see that in your testimony. What I'm driving at is, given your testimony, you appear to have looked at a larger group of potentials and you just -- you selected your group of 20 -- you brought it down to a group of 24. And I just wanted to confirm that that was what had been done.

A Yes. We started out with, I think, 61 or two companies and ended up with 24.

Q Okay. I want to move to the discount cash flow model. I know that you reject out of hand the constant growth. And then you use the risk premium analysis to -- it's -- actually, I guess it's more than an adjunct or backup on a little bit more than a sanity check on it, it appears. But you -- you don't trust the DCF model as -- in and of itself, do you?

A No. Those are not my words, Counsel. I looked at the results for the constant growth DCF model using only analysis upgrades, and I found the results of that model not to be within a hundred basis points of the risk premium results.

Therefore, I did not include the traditional cost of growth results in my recommended range.

Q All right. Given that, the results of the DCF models, even under your analysis, including the constant growth analysis that you reject out of hand, brings the lowest ROE across the board, does it not?

A That's exactly right. And it is below the reasonable cost of equity, and it is below any rate of return on equity that's been allowed by Commissions around the country. And it's not an adequate rate of return. Therefore, I didn't include it in my range.

Q Is it not correct the Federal Energy regulatory commission refers to the use of the discounted cash flow models?

A It depends on which industry group you're talking about. They use a multi-stage model for gas pipelines, for example, which is a large part of their regulation has the GDP growth rate as part of growth rate, just like I used in my two-stage mold.

On the companies that they do just electric cases for, they have consistently, in recent cases, added on 50 to 200 basis points for other factors beyond the discounted cash flow model that they apply. So it really very much depends on which case you're talking about.

Q Yeah. But don't you, in your direct testimony on page 29, refer to the DCF model the most widely used in regulatory proceedings?

A Yes. And that is the basis for my recommendation. But it's an alternative set of the models to the basic traditional cost DCF model. Many versions of it.

Q Okay. In your rebuttal, is it not true after you've gone through and redone the numbers, you adjust basically the base rate of the ROE to 10.75 percent, and then you add -- this time, instead of 25 basis points, you add 50 basis points, you know, based on the construction risks?

A That's exactly right. We redid the numbers in

December from the models, and the results were about 50 basis points lower. So we reduced the base ROE from 11 and a quarter to 10 and three-quarters.

We reviewed the construction data. And in the initial construction data, Aquila's construction budget was about 90 percent net plant, existing net plant. The comparable group is about 60 percent.

Based on that, we recommended a 25 basis point adder. By the time we did rebuttal, we did that same analysis again. The number for Aquila is 118 percent, almost 120, and the comparable group has gone up to about 61. So it's another nearly twice as big.

Therefore, I increased the risk added by 25 basis points.

Q You're familiar with Mr. Denny Williams' rebuttal testimony, are you not?

A I have read it.

Q You've read it, since you've referenced it, obviously, you've read it. So you've, in essence, taken these numbers that Mr. Williams gave you and just plugged them into your calculations and added 50 basis points; is that not correct?

A The 118 percent that I mentioned as the updated construction percentage comes directly from Mr. Williams, yes.

Q How well do you recall Mr. Williams' testimony on that subject?
A That's the only part that I focused on.
Q So you're not surprised by the fact that Mr. Williams testimony, in fact, does say that that is an estimate, that those are projected numbers?
A They certainly are projected numbers over the next six years.
Q And it is an estimate?
A That's correct.
Q And yet you went in there and plugged it in, and that's what -- that's what we're going to submit before the Commission?
A That is what is submitted to the Commission.
Q Okay. Looking at page 3 through 5 of your rebuttal, I just wanted to confirm that you acknowledge the average return on equity is 10.36 percent and that you acknowledge basically that chart that Mr. Thompson has put up there.
And in order not to put words in your mouth, the top bar is 11.36 percent. The bottom bar is 9.36 percent.
A I think he has some slightly different numbers written there, but I'm glad you asked about that. The nine -- the 10.36, he mentioned that there was a high wind form of 11.9 percent ROE.

Q Now, we're talking -- no. Dr. Hadaway, we're talking about the chart, and we're talking about your testimony. Is it not true that you say that for the year 2006 there is an average ROE handed down of 10.36 percent plus or minus 100 basis points, and that gives you a range of 9.36 percent to 11.36 percent?

A Yes, sir. Counsel, I say that exactly. I'm not sure I see that on Mr. Thompson's chart. But it's implied by the arrows that are up there.

THE COURT: Just a second. Mr. Thompson?

MR. THOMPSON: Judge, I wonder if I might bring the chart over.

JUDGE VOSS: It might be a good idea to mark it as an exhibit what the witnesses are referring to so it will get marked for the record what we're talking about.

MR. THOMPSON: Well, I'm perfectly happy to do that. And I think that would be then Staff's Exhibit 241.

JUDGE VOSS: And it will, of course, have no independent evidentiary value. It's just to show what people are referencing, unless someone wants to object it.

CAPTAIN HOLLIFIELD: Yes, your Honor.

JUDGE VOSS: Would anyone object to have this marked as exhibit so everyone can refer to it and it's in the record for appeal?

MR. WOODSMALL: Is it an exhibit or are you accepting it into the record? If it's accepted into the record --

MR. THOMPSON: It hasn't been offered.

MR. WOODSMALL: -- then it's evidence. That's what I'm asking.

JUDGE VOSS: As an exhibit. As I say, we have no independent evidentiary value unless someone adopts it, and then objections can fly. So what is that going to be marked as, Mr. Thompson?

MR. THOMPSON: Exhibit 241. It's because I'm going to use 240 for something else.

CAPTAIN HOLLILFIELD: Okay. Are we --

MR. THOMPSON: We're still marking. That's a big marker. Thank you.

JUDGE VOSS: Are you ready to proceed?

CAPTAIN HOLLIFIELD: I am. I just wanted to make sure I wasn't speaking out of turn.

Q (By Captain Hollifield) You know, given the fact that we're looking at the -- the ROE being adjusted down to 10.75 percent and then we have this estimate that suddenly appears, it looks a lot like we're just doing everything we can to stay on the top part of the range, doesn't it?

A Nothing just appeared. It was in my direct testimony about the adjustment for the construction risk.

Certainly, in the prior cases where the Commission has looked at this, they did not look at it after the adder. So my initial estimate of 11.4 percent was clearly in the range.

My adjustment had nothing to do with staying within the range. It had to do with the fact when we redid the numbers in December, the model showed 50 basis points reduction of ROE.

Q Okay. In your rebuttal testimony, refer to both Mr. Parcell and Mr. Gorman as skewing their results. Could you define "skew" for me?

A Skewing usually means that one is tweaking the numbers or inserting assumptions in ways that cause the results to go in one direction or the other.

Q Okay. And given that use of the word -- and let's look at what we've come up with. So far, there's not much of a normative analysis in your -- your analysis.

It's -- you know, you just qualify or caveat your group, and that's the closest thing you've got. You selectively include companies in your proxy group. You toss out the limiting effect that the DCF model has because it's -- it's low, period, end of story.

And you adjust the ROE based on these estimates that come in late in the game. It's a pretty fair characterization that you're doing some skewing of your own, isn't it?

A Counsel, you completely misrepresented my testimony in your statement there. Certainly, we provided the same analysis here that we provided in several hundred cases very similar in each case.

The same analysis we provided in our direct testimony is extended to the rebuttal testimony. It's certainly not an appearance of anything. It is not lacking normative discussions, as I understand that word.

It's about a 50-page piece of testimony that describes the industry, describes the economy and describes the setting of the capital markets in which the companies have to raise capital. I'm sorry. But I entirely disagree with your interpretation.

Q And I don't expect you to agree. And I -- that's fine.

CAPTAIN HOLLIFIELD: I'm finished with my questions. Thank you.

JUDGE VOSS: All right. The next party that's here would be the Sedalia Industrial Energy Users Association.

MR. WOODSMALL: Thank you, your Honor.

CROSS-EXAMINATION

BY MR. WOODSMALL:

Q Good morning, Mr. Hadaway. How are you, sir?

A Good morning, Mr. Smallwood.
Q Woodsmall.
A Woodsmall.
Q It's a pleasure to make your acquaintance. Just for purposes of my information, I'm wondering are you familiar with Value Line's grouping of companies into regions?
A Yes, I am.
Q Okay. And can you tell me what the various regions are?
A They have an east addition, a central addition and a west addition.
Q Okay. Do you have your direct testimony there?
A Yes.
Q Will you turn to schedule SCH-1, page 2 and page 3?
JUDGE VOSS: I'm sorry, Mr. Woodsmall. I didn't hear. Which piece of testimony? Is this his direct?
MR. WOODSMALL: Direct.
JUDGE VOSS: Thank you.
A I believe I have that.
Q (By Mr. Woodsmall) And that is a listing of your 24 comparable company group; is that correct?
A Yes.
Q Can you tell me which of those 24 are in the

east region?

A I probably could if we went through them one by one, if you'd like to do that.

Q Okay. We can do that.

A Alliant is in the central area. Ameren's in the central area. American Electric Power is somewhat in both obviously.

Q Both, being what?

A Central and east. CH Energy and Central Hudson are in the east. Central Vermont is in the east. Consolidated Edison is in east. DTE is in the central. DeQuane (ph.) is in the central. Empire District is in the central. Energy East is in the east. Green Mountain Power is in the east.

Hawaii Electric is in the west. MGE is in the central. That's Madison Gas Electric. Nysource is in the central northeast utilities. It's in some of both, but they're mostly in the east group.

Instar is Walter Madison. It's in the east group. Pinnacle West is in the west group. Or I'm sorry. It's in the central group. BPL is in the east. Progress Energy is in the east. Puget's in the west. Scanna in the east. Southern is in the central, actually.

Vectron is in the central. And Excel is kind of spread, out but they're listed in the central.

Q So did you say Pinnacle West is in the central?
A Yes.
Q And they're in Arizona?
A They are.
Q Narrow definition of west, apparently.
A There are only about three or four companies in the western group. It's mostly the California Hawaii Electric and northwestern companies.
Q Okay.
A And I could be mistaken. Pinnacle, I think, has actually been in the west and in the central, but it's not a fine distinction.
Q Are you familiar with the Form 10-K that is filed by publicly traded companies?
A Yes.
Q Would you have a reason to review that document for certain companies?
A We did that to find that fourth column in this very exhibit.
Q Okay. So your answer is yes?
A My answer is yes.
Q Okay. Would you use that for other purposes?
A Usually, for the subject company, we read the 10-K just to get the background on the information for the company.

Q You wouldn't read that for any of your comparable companies other than for purposes of determining fuel adjustment clause?

A Independent. If there was an issue, we certainly would. That would be the basis for the document.

Q As one part of that 10-K document, isn't it true that a company's management is required to list the most significant risk factors which the company -- which makes the company risky?

A As a legal matter, I'm not sure what they're required to do. But companies list their significant risk factors.

MR. WOODSMALL: Okay. I'd like to mark an exhibit, your Honor.

JUDGE VOSS: You gave me two copies.

MR. WOODSMALL: Okay.

Q (By Mr. Woodsmall) Can you identify --

MR. WOODSMALL: I'm sorry. Do you have an exhibit number for this?

JUDGE VOSS: Is it 511 or 512? 511? 512?

MR. WOODSMALL: No. 511 was one that I marked yesterday, but I didn't offer.

JUDGE VOSS: Didn't offer. I was making sure I didn't -- get it on the right line. So 512.

MR. WOODSMALL: Okay. May I proceed, your Honor?

JUDGE VOSS: Yes, you may.

MR. WOODSMALL: Thank you.

Q (By Mr. Woodsmall) Can you identify Exhibit 512, please?

A Yes, sir. This is Aquila's 2006 Form 10-K.

Q And I'll represent to you that it is not complete. I mean, it's a mammoth document, so I only printed certain pages. Could you turn to what's -- at the top -- it has strange pagination, but looking at the upper right-hand corner what's marked page 21 of 166? I'm sorry. Page 25 of 166.

A Yes, sir. I have that.

Q And is that the -- you see item 1-A risk factors? Are those the risk factors that we were just recently talking about that management is required to publish?

A Again, I'm not sure what management is required to do with respect to these risk factors. But it is certainly a listing of operating risks according to the heading up there for Aquila.

MR. WOODSMALL: Okay. Your Honor, I'd ask to -- or offer Exhibit 512.

JUDGE VOSS: Are there any objections to this exhibit?

MR. THOMPSON: No objection.

JUDGE VOSS: Hearing none, it's received.

(Exhibit No. 512 was offered and admitted into evidence.)

Q (By Mr. Woodsmall) Have you had the opportunity to previously review Aquila's 10-K?

A Not this one.

Q Okay. Have you reviewed previous 10-Ks?

A Yes, sir.

Q For what purpose did you review those?

A Just to get the general background on the company.

Q Okay. Moving on, isn't it true that nuclear operations have a tendency to make an electric utility more risky?

A They certainly used to.

Q That's a yes or no question. Isn't it --

A It's not a yes or no question. Nuclear risk used to be a big concern. It is much less of a concern.

Q So are you saying, no, it doesn't make an electric utility risky or, yes, it does make it risky?

A It makes some electric utilities today very desirable as investments because it's a low cost generation source. Some people view that as a lower risk situation because they're better in the market. Certainly, the operation of a nuclear plant has risks for it, and in that sense, it does increase the risk.

Q Okay.

A And in recent years, the last years since about 2001, those companies are nuclear power plants that are operating well, have been thought of very well.

Q Would you agree that most companies 10-Ks electric utilities' 10-Ks, the presence of nuclear operations is listed as a risk factor?

A I don't know. It -- it could be.

Q Okay. Let's go through some of them. I'm handing you a document --

A Thank you.

Q Can you turn to -- can you tell me what that is?

A This appears to be the Form 10-K for Ameren for December 31st, 2006.

Q Will you turn to page 42 of that document?

A Yes. I have it.

Q And read the highlighted portion, please.

A It says, Ownership and operation of nuclear generating facility creates business, financial and waste disposal risks.

Q Thank you. Can you identify this document, please?

A This is the 2006 10-K for American Electric Power.

Q Turn to page 16.

JUDGE VOSS: Could you read into the microphone, Mr. Hadaway, just to --

Q (By Mr. Woodsmall) Read the highlighted portion.

JUDGE VOSS: Mr. Hadaway, could you read it into the microphone?

MR. WOODSMALL: Set it down.

A The base rates that certain utilities charge are currently capped or frozen.

Q (By Mr. Woodsmall) I'm sorry. That's the wrong part. The next one.

A We are exposed to nuclear generation risks.

Q Thank you. Can you identify this document, please?

A This document is DTE 10-K for 2006.

Q Turning to page 30, will you read the bottom highlighted portion?

A Operation of a nuclear facility subjects us to risk. Ownership and operating a nuclear generating plant subjects us to significant additional risks. These risks include, among others, plant security, environmental regulation and remediation, operational factors that can significantly impact the performance and cost of operating a nuclear facility while we maintain insurance for various nuclear-related risks. There can be no assurance that such insurance will be sufficient to cover our costs in the event of an accident or business interruption at that nuclear generating plant which may affect our financial performance.

Q Thank you. And rather than go through a multitude of other 10-Ks, I would ask you, looking at your Schedule SCH-1, can you tell me which of those utilities have nuclear operations?

A I haven't researched that recently, but about half of them do.

Q Can you tell me which? Ones and then I'll grant you --

A No.

Q You cannot? You can't tell me?

A Not every one.

Q Tell me which ones you know.

A Southern Company, Progress Energy, Pinnacle West. Northeast Utilities used to, but I think that Public Service in New Hampshire's plant has been sold, so they do not now. Energy East, DeQuane Light, DTE. I think the same thing about Consolidated Edison. I don't know if they still have an ownership or not. Certainly,

American Electric Power and Ameren. That's The best of my knowledge without having looked at that issue.
Q Do you know if Excel Energy has nuclear operations?
A I know the company that I'm most familiar with there is Southwestern Public Service Company, and they do not.
Q Do you know, does Excel have other --
A They own Public Service Company of Colorado, which at one time certainly did have nuclear capacity.
Q What about Northern States Power in Minnesota?
A I do not know that.
Q I'll hand you a document. Can you identify this, please?
A This is Excel Energy's 10-K for 2006.
Q And will you turn to page 35?
A Thirty-five.
Q Read the highlighted portion.
A Our subsidiary, NSP Minnesota, is subject to the risks of nuclear generation.
Q Okay. Scanna (ph.) Company is one of your comparable group; is that correct?
A Yes, sir. That's right.
Q Do you know if they have nuclear operations?
A I'm not sure.

Q I'll hand you a document. Can you identify that, please?
A That is Scanna's Form 10-K for 2006.
Q Please turn to page 29 and read the highlighted portion.
A A significant portion of SCE and GE generating capacity is derived from nuclear power, use of which exposes us to regulatory environmental and business risks. These risks could increase our costs or otherwise constrain our business, thereby, adversely affecting our results of operations cash flow and financial condition.
Q Thank you, sir. PPL is one of your comparable groups; is that correct?
A That's right.
Q Do you know if PPL has nuclear operations?
A The regulated portion of it does not now, but it did at one time.
Q The total company, it's not just your regulated of -- excuse me. It's just not the regulated portion of PPL that is your comparable company; is that correct?
A That's right.
Q Okay. Do you know if in the entirety of the PPL Corporation -- is there nuclear operations?
A I do not know.
Q I'll hand you a document. Can you identify

that, please?

A This is PPL Corporation's Form 10-K for 2006.

Q Will you turn to page 31, please, and read the highlighted portion?

A We are subject to the risks of nuclear generation, including the risk that our Susqua Hanna nuclear plant could become subject to revised security or safety requirements that would increase our capital operating expenditures associated with decommissioning our plant at the end of its licensed life.

Q Thank you. I'll hand you a document and ask you to identify it, please.

A This is Green Mountain Powers' 10-K for 2006.

Q Turn to page 5. Read the highlighted portion.

A A major source of the company's power supply is our entitlement to a share of the power generated by the 620 megawatt nuclear generating plant owned and operated by ENVY, in parentheses, the Vermont Yankee or VY plant, closed parentheses. We have a 33.6 percent equity interest in Vermont Yankee Nuclear Yankee Nuclear Power Corporation, VYNPC, which has a long-term power supply contract with ENVY that entitles us to approximately 100 megawatts to 106 megawatts of Vermont Yankee plant output through 2012.

Q Thank you. I'll show you another document. Can you identify this document, please?

A This is the Form 10-K for 2006 for Central Vermont Public Service.

Q Turning to pages 7 and 8, there's a listing of jointly owned plants. Do you see that?

A Yes.

Q Turn to page 8, please. can you tell me if there's an indication of a nuclear unit that they own?

A Yes. It indicates in the highlighted portion, Millstone Unit No. 3.

Q Okay. That's all my questions on nuclear.

JUDGE VOSS: Mr. Woodsmall, are you at a good breaking point? Assuming you have some remaining.

MR. WOODSMALL: One more question, and I will be.

Q (By Mr. Woodsmall) Can you tell me if Aquila has nuclear operations?

A Not that I'm aware of.

MR. WOODSMALL: Okay. Now I'm at a good breaking point.

JUDGE VOSS: Okay. Let's take a good break and come back at about ten after.

(Break in proceedings.)

JUDGE VOSS: We are back on the record. We're back on the record, and we'll resume with cross-examination by Sedalia Energy Users Association and AG processing, Inc.

MR. WOODSMALL: Thank you, your Honor.

Q (By Mr. Woodsmall) Moving on, sir, isn't it true that the introduction or the existence of competition in a jurisdiction tends to make an electric utility more risky?

A The part that is exposed to deregulation, yes.

Q Okay. Can you tell me which of your comparable companies are -- have some exposure to competition in their regular -- in their jurisdictions?

A I know that Ameren does. American Electric Power does. I'm not sure about Central Hudson, but I believe that New York, they do have customer choice now. Con Ed certainly does. DQE does. Or DeQuane Light does. Energy East does.

Northeast Utilities does for some of its companies, but I'm not sure about all of them. There's some choice in Arizona, but it's not deregulated. KCPL certainly does. Puget has some industrial customers that can make choices, but generally it's not deregulated. Those are the only ones that I'm sure about.

Q Do you know if DTE faces competition in its Michigan jurisdiction?

A I don't know.

Q I'll hand you a document. Can you identify this document, please?
A This is DTE's energy's 2006 10-K.
Q Will you turn to page 13? Read the highlighted portion.
A In 1998, the MPSC authorized the electric customer choice program that allowed for a limited number of customers to purchase electricity from suppliers other than their local utility.
The local utility continues to transport the electric supply to the customers' facilities, thereby retaining distribution margins.
The electric customer choice program was phased in over a three-year period with all customers having the option to choose their electric supplier in January of 2002.
Q Now turn to page 15. Read the highlighted portion.
A Detroit Edison lost 6 percent of retail sales in 2006, 12 percent in 2005 and 18 percent of such sales in 2004 as a result of customers choosing to purchase power from alternative electric suppliers.
Customers participating in the electric customer choice program consist primarily of industrial and commercial customers whose MPSC authorized full service

rates exceed their cost of service.

Customers who elect to purchase their electricity from alternative electric suppliers by participating in the electric customer choice program have an unfavorable effect on our financial performance.

Q And is Detroit Edison a company within DTE?
A Yes.
Q Do you know if Instar faces competition in Massachusetts?
A I believe it does.
Q Do you know if Excel Energy faces competition in Michigan ?
A Probably, if DTE does, it does.
Q Okay. Do you know if Excel faces the possibility of competition in Texas?
A It does not.
Q It does not?
A Not at this time.
Q Has rules or -- been written to provide for competition?
A Not -- not in the not Ercot (ph.) portion of it.
Q Okay. Do you know whether Aquila faces competition in any of its jurisdictions?
A I don't believe it does of the kind that you're describing in these documents.

Q Okay. Associated with competition in some of these states, would you agree that the utility is still subject to rate freezes?
A Many of them were for some period of time. Many of them are not now.
Q Okay. But some still face rate freezes?
A A few -- a few do.
Q Okay. Would you agree that exposures to hurricanes have a tendency to make an electric company more risky?
A Certainly, more risky. That's why they're not part of this comparable group.
Q Would it make other electric utilities more risky?
A They have been sort of the poster company for that issue because of what happened in New Orleans. But it certainly has become a discussed issue for some of the other companies.
Q Okay. And would that include Progress Energy?
A It certainly would.
Q Would that include Scanna Corp.?
A It might. Yes.
Q Would that include Southern Companies?
A Particularly, perhaps Savannah Electric and Gulf Power, two of their operating subsidiaries that are on the

various coasts would be affected.

Q Okay. Do you know if Aquila operates in any state where they face a possibility of hurricanes?

A Not -- not to my knowledge.

Q Isn't it true that exposure to affiliates with significant non-regulated operations has a tendency to make an electric company more risky?

A Now, I mentioned earlier about PP&L, and you said you wanted to focus on the total company. Are you saying does it make the regulated piece more risky than it was?

Q Does it make the total company more risky?

A Yes. The deregulated piece is certainly more risky.

Q Okay. And when you say deregulated, that also includes non-regulated. I don't want to limit deregulated to things that were once regulated and became unregulated.

A Certainly. Unregulated activities, that's why we use a 70 percent regulated revenue filter so that that doesn't dominate.

Q Okay. Can you tell me the nature of Alliance's non-regulated operations?

A No.

Q Do you know anything about their non-regulated operations?

A I do not.

Q Okay. Let me hand you a document and ask you to identify it.

A This is Alliance's 2006 10-K.

Q Turn to page 15. Can you tell me -- read the highlighted portion?

A Non-regulated generation. Other non-regulated investments includes investments in environmental engineering and site remediation, transportation, construction management services to wind farms and several other modest investments as well as a resort development in Mexico, Laguna Del Mar that Alliant Energy is divesting.

Environmental engineering and site remediation includes RTM, Inc., an environmental and engineering consulting company that serves clients nationwide in a variety of industrial market segments and specializes in consulting on solid and hazardous waste management site remediation, ground water quality monitoring, detection and air quality control.

Transportation includes a short line railway that provides freight service between Cedar Rapids and Iowa City, Large terminal and hauling services on the Mississippi River and other transfer and storage services. Construction management services for wind farms include

Wind Connect, a construction management service company that provides expertise in engineering, designing and constructing wind electrical system projects.

JUDGE VOSS: Mr. Woodsmall, I didn't hear you identify what that is.

MR. WOODMAN: I didn't identify it. He identified it as Alliant Energy's 10-K from 2006.

JUDGE VOSS: I didn't hear that. Thanks.

Q (By Mr. Woodsmall) Are you familiar with AEP's non-regulated operations?

A To some extent.

Q Tell me what you know about that.

A AEP owns companies in Texas that have been subject to the deregulation bill there, and I have worked in cases that involved those companies. So that's basically what I know about it.

Q Okay. I'll hand you a document and ask you to identify it.

A That's AEP's Form 10-K for 2006.

Q Turn to page 19, please and read the highlighted risk factor.

A Our power trading, including coal, gas, emission allowances trading and power marketing and risk management policies cannot eliminate the risk associated with these activities. And they listed weather conditions and things like that.

Q Are you familiar with DTE's non-regulated operations?

A No.

Q I'd ask you to identify this document.

A That's DTE Energy's 2006 10-K.

Q Turn to page, I believe it's 30, and read the top highlighted portion.

A Our non-utility operations may not perform to our expectations. We rely on our non-utility operations for a significant portion of our earnings.

If our current and contemplated non-utility investments do not perform at expected levels, we could experience diminished earnings potential and corresponding decline in our shareholder value.

Q And on the next page, page 31, would you read the highlighted portion?

A Our participation in energy trading markets subjects us to risks -- to risk. Excuse me. Events in the energy trading industry have increased the level of security -- I'm sorry -- scrutiny on the energy trading business and energy industry as a whole.

In certain situations, we may also be required to post collateral to support trading operations. We have established risk policies to manage the business.

Q Thank you. Are you familiar with the non-regulated operations of DeQuane (ph.) Light?

A I am not.

Q I'll hand you a document and ask you to identify it.

A This is the 10-K for 2006 for DeQuane Light Holdings and DeQuane Light Company.

Q Turn to page 8 and read the non-regulated operations there.

A DeQuane Energy Solutions, LLC (DES) is an energy facilities management company that provides energy outsourcing solutions, including operations and maintenance of synthetic fuel and energy facility.

DQE Financial Corp. is an investment and portfolio management organization focused on structure finance and alternative energy investments.

DQE Financial previously owned and operated landfill gas collection and processing systems. DQE Communications, Inc., owns, operates and maintains a high speed fiberoptic based metropolitan network and leases dark fiber from the network to commercial, industrial and academic customers.

Q Thank you. Are you familiar with the non-regulated operations of Energy East?

A No.

Q I'll hand you a document and ask you to identify it, please.

A This is the Energy East Corporation 2006 10-K.

Q Turn to page 7 under Other Bids. Will you read all the way down to the last highlighted area?

A Our other businesses include retail, energy marketing companies, non-utility generating company, a FERC regulated liquefied natural gas peaking plant, a natural gas delivery company, propane area delivery company, telecommunications assets, district heating and cooling system and an energy consulting services company.

We include their results of operations, financial condition and cash flows in our other segment. Energentix, E-n-e-r-g-e-n-t-i-x. I don't know if I said that right, Inc., and Nyseg, N-y-s-e-g, Solutions, Inc., market electricity and natural gas services throughout the state of New York.

The revenues from these two companies accounted for approximately 9 percent of Energy East's total 2006 -- revenues in 2006, 10 percent in 2005 and 9 percent in 2004. Kyuga Energy owns electric generation facilities that sell power in the NYISO and PJM interconnection wholesale markets at times of high demand.

Q And read the other one.

A Maine Com Services owns fiberoptic lines and

provides telecommunication services in Maine.
Q Thank you. Are you familiar with the non-regulated operations of Hawaiian Electric?
A I know that they own a large financial institution. But beyond that, I don't know.
Q I'll hand you a document and ask you to identify it.
A This is Hawaiian Electric Industry's Form 10-K for 2006.
Q Turn to page 10 and read the first highlighted area.
A ASB, acquired in 1988, is the third largest financial institution in the state of Hawaii based on total assets as of December 31st, 2006.
ASB has subsidiaries involved in the sale and distribution of insurance products and inactive advertising agency for ASB and its subsidiaries. Former ASB subsidiaries, ASB Realty Corporation, which had elected to be taxed as a real estate investment trust dissolved in May 2005.
Q That's fine. Thank you. Are you familiar with the non-regulated operations of Nysource.
A No.
Q I'll hand you a document and ask you to identify it, please.

A This is Nysource, Inc.'s 2006 10-K.
Q Can you turn to page 11? Read the highlighted portion.
A The other operations segment participates in inter -- energy-related services, including gas marketing, power and gas risk management and ventures focused on distribution power generation technology, including a co-generation facility, fuel sales and storage systems.
PEI operates the Liquidity Clean Energy product at BP's Whitting, Indiana refinery, which is a 2500 megawatt co-generation facility that uses natural gas to produce electricity for sale in the wholesale markets and, also, provides steam for additional use.
Additionally, the other operations segment is involved in real estate and other business.
Q Turn to page 14 , I believe it is. Read the highlighted risk factor.
A Nysource's Whitting Merchant Energy Project is operating at a loss.
Q Thank you. Are you familiar with Instar's non-regulated operations?
A No.
Q Now, I didn't highlight that one, so I'll just move on. Are you familiar -- familiar with Pinnacle West's non-regulated operations?

A No.

Q I found it. Going back to Instar, would you identify this document?

A That's Instar's Form 10-K for 2006.

Q Turn to page 13, please. Read the two highlighted portions.

A Instar's unregulated operation segment engages in businesses that include district energy operations, telecommunications and liquefied natural gas. Instar Com participated in a telecommunications venture with RCN Telecom Services, that's in Massachusetts, a subsidiary of RCN Corporation (RCP).

As part of the joint venture agreement, Instar Com had the option to exchange portions of its joint venture interests or common shares in RCN at specified periods.

Q Thank you. I believe I asked you if you were familiar with the non-regulated operations of Pinnacle West, and you said no; is that correct?

A Generally, no.

Q You say generally. Can you tell me what your familiarity is?

A They have real estate -- or they have had real estate and financial institution investments.

Q I'll hand you a document and ask you to identify it.

A This is Pinnacle West's capital corporation and Arizona Public Service Company's Form 10-K for 2006.

Q Turn to page 8. Read the highlighted portion.

A The real estate segment, 12 percent of operating revenues in 2006 consist of Sun Corp. real estate development and investment activities.

Q Turn to page 18, I believe it is.

A I'm -- I'm pausing here, Mr. Smallwood.

Q Woodsmall. Yes. Go ahead.

A The -- the whole issue here, it says right above that sentence you just had me read, the regulated electricity segment, 70 percent of operating revenues which consist of traditional regulated, retail wholesale electricity business and so forth, there are none of these companies that you have asked me about that have more than 30 percent of the revenues from these non-regulated segments.

Q I understand.

A Every one of them has 70 percent or more, and the average is about 87 percent for regulated operations.

Q I understand. Will you turn to page -- I believe it's 18.

A Okay.

Q Read the highlighted portion.

A December 31st, 2006, Suncorp. had total assets of about 607 million. Suncorp's assets consist primarily of land, with improvements to commercial buildings, golf course and substantial investments. Suncorp. continues to focus on real estate developments of master plan communities, mixed use, residential, commercial, office and industrial projects.

Suncorp. projects under development -- excuse me. Suncorp. projects under development include five master plan communities and several commercial and residential projects.

The commercial residential projects in two of the master plan communities are in Arizona. Other master plan communities are locates in St. George, Utah, Boise, Idaho, Santa Fe, New Mexico.

Q Turn to the risk factor on page 27 and read it.

A Suncorp's business and financial performance could be adversely affected by a variety of factors affecting the real estate market.

Q Thank you. Are you familiar with the non-regulated operations of PPL?

A Only that they're less than 30 percent of their 2005 operating revenues.

Q Let me ask you about that 70 percent. Did you go and make that calculation yourself, or is that based upon some screen that you use?

A I'm a partner of Brent Heidebrecht, h-e-i-d-e-b-r-e-c-h-t. I made that calculation based on the Form 10-Ks for 2005 which we had at the time we prepared both our direct testimony in June and our rebuttal testimony in December.

Q Thank you. I'll hand you a document and ask you to identify it.

A This appears to be PPL Corporation's Form 10-K for 2006.

Q Will you turn to page 14 and read the highlighted portion?

A PPL Energy Supply, LLC, an indirect wholly-owned subsidiary of PPL formed in 2000, is an energy company gauged through its subsidiaries in the generation and marketing of power, primarily in the eastern and western power markets of the U.S. and in delivery of electricity in U.K. and Latin America.

PPL Energy supplies major operating facilities for PPL Generation, PPL Energy Plus and PPL Global. PPL Energy supplies owns and controls 11,156 megawatts of electric power generation capacity and has current plans to implement capital projects at certain of its existing generating facilities in Pennsylvania and Montana that will provide 349 megawatts of additional generation capacity by 2011.

Q Thank you. There's more here. Page 16, will you read these two pages?

A PPL Synfuel Investments, LLC, a subsidiary of PPL Energy Plus, indirectly owns through its subsidiaries two production facilities that manufacture synthetic fuel from coal or coal by-products.

PPL receives federal tax credits for manufactured solid synthetic fuel products. See note 15 of the financial statements for additional information. PPL Telecom, an indirect subsidiary of PPL Energy Plus has a fiberoptic network and markets available capacity on PPL's electric fiberoptic cables in eastern and central Pennsylvania.

Q Thank you. The highlighted portion on page 18?

A PPL Global provides electricity delivery service to approximately 3.7 million company customers in the U.K. and Latin America.

Q The highlighted -- last highlighted portion on page 28 --

A We face intense competition in our energy supply business, which may adversely affect our ability to operate profitably.

Q And the two risk factors listed on page 32?

A Our international delivery business --

businesses are also subject to risk with respect to rate regulation and operational performance.

Our international delivery businesses expose us to risks related to laws in other country, taxes, economic conditions, fluctuations in foreign currency exchange rates, political and associated conditions and policies of foreign governments. These risks may reduce our results of operations from our delivery business.

Q Are you familiar with the non-regulated operations of Progress Energy?

A Only that they amounted to less than 30 percent of its operating revenues during 2005.

Q I'll hand you a document and ask you to identify it.

A This is Progress Energy's Form 10-K for 2006.

Q Turn to page 12, and please read the highlighted portion.

A Our non-regulated coal and synthetics fuel segment is involved in the production and sale of coal based solid fuel synthetic -- solid synthetic fuel as defined under the Internal Revenue code (The Code).

The operation of the synthetic fuels facilities for third parties, as well as coal terminal services, our terminal operations, support, our synthetic fuels operations, for procuring, processing coal and trans-loading and marketing of synthetic fuels.

On May 22nd, 2006, we idled our synthetics fuel facilities due to significant uncertainties surrounding synthetic fuels production.

During September and October of 2006, we resumed limited synthetic fuel production in our facilities which continued through the end of 2006. The tax credit program for production of qualifying fuels is set to expire at the end of 2007.

Q Page 17, read the highlighted portion.

A Coal and synthetic fuel operations compete with the steam and industry coal markets in the eastern United States. Factors contributing to the success of these markets include competitive cost structure and strategic locations.

There are, however, numerous competitors in each of these markets. Although no one competitor is dominant in any industry, as discussed previously, we idled our synthetic fuels facilities for a portion of 2006 due to uncertainties surrounding synthetic fuels production.

The tax credit program for production of qualifying synthetic fuels is set to expire the end of 2007.

Q Turn to page 43. Read the risk factor that's highlighted.

A Our results of operations may be federally affected if our earnings from synthetic fuels are reduced due to high -- due to the high price of oil.

Our ability to utilize tax credits may be limited. This risk is not applicable to, PEC and PEF.

Q Do you know if PEC is Progress Energy Carolina and PEF is Progress Energy Florida?

A Think that's right.

Q Okay. Turn to page 43 and read the highlighted portion.

A We are subject to risk from the operation of our non-regulated plants, including the dependence on third parties and related counter-party risks, all of which make our non-regulated generation and overall operations less profitable and more unstable. These risks are not limited to PEC and PEF.

Q And, again, PEC and PEF are the regulated operations; is that correct?

A As far as I know, that's correct.

Q Okay. Thank you.

A Done with that one?

Q Yeah. Are you familiar with the non-regulated operations of Scanna Corp.? Scanna, Scanna. I don't know.

A I think it's Scanna.

Q Okay.

A Only that they're less than 30 percent of their operations during 2005.

Q Okay. I'll hand you a document and ask you to identify it. Eventually, I'll get up there to do it. Please identify this document.

A This is the Scanna Form 10-K for 2006.

Q Turn to page 12. Read the part that's highlight, circled.

A SCI owns and operates a 500-mile fiberoptic telecommunications network and Internet network and data center facilities in South Carolina.

Through a joint venture, SCI has an interest in an additional 1,742 miles fiber in South Carolina, North Carolina and Georgia. SCI also provides tower site construction, management, retail services in South Carolina and North Carolina.

Q Thank you. I'm getting close. Are you familiar with the non-regulated operations of Southern Companies?

A I'm not any more familiar than that they don't account for more than 30 percent of their operations in 2005.

Q Just to be clear, the latest 10-K that's been filed is the 2006 10-K; is that correct?

A Most of the companies filed those in March.

Yes.

Q I'll hand you a document and ask you to identify it.

A That is the 10-K for 2006 from Southern Company.

Q Turn to page 11. Read the two highlighted portions.

A Southern LINC Wireless provides digital wireless communication services to the traditional operating companies and also markets these services to the public within the southeast.

Southern Telecom provides wholesale fiberoptic solutions, telecommunications providers in the southeast. Southern Holding is an intermediate holding subsidiary for Southern Company's investments and synthetic fuels and leverage leases and various other energy-related businesses.

Q Thank you. Are you familiar with the non-regulated operations of Excel Energy?

A Nothing beyond the fact that they have less than 30 percent of revenue coming in --

Q In 2005?

A -- in 2005.

Q I'll hand you a document and ask you to identify it.

A This is Excel Energy, Inc.'s 2006 10-K.

Q Turn to page 8, please. And read first highlighted portion.

A United Power & Land Company, which holds risk.

Q And the second highlighted portion?

A Chippewa and Flomme Bow (ph.) Improvement Company, which operates hydro reservoirs, Clear Water Investments, Inc., which owns interest, affordable housing and NSP Lands, Inc., which holds real estate.

Q And does it indicate that those are direct subsidiaries of Northern State Power in Wisconsin?

A Yes.

Q Okay. And Northern State Power Wisconsin is a subsidiary of Excel Energy?

A As far as I know. I don't know the whole chain, but that's basically true.

Q Okay. Thank you. Okay. Moving on. Can you tell me your knowledge of the non-regulated operations of Aquila?

A They certainly have evolved.

Q What are they currently?

A I do not know.

Q You don't know?

A I don't know the current status. I'm sure Mr. Williams can fill you in on that.

Q Okay. Do you know if they have currently any non-regulated operations?

A I suspect that they do, but I do not know that as a fact. Mr. Williams will have to tell you that.

Q Isn't it true that uncertainty over pending mergers have a tendency to make a company more risky?

A When issues about a merger come up, if the company has publicly traded stock to fluctuate more. And so in that sense, probably yes. If it's a favorable acquisition for shareholders, then, no, it's not. That's a risk issue.

Q Do you know if any of your comparable companies are currently in the process of closing a merger?

A We use that as one of our scans. And at the time we did the initial selection of the companies, they were not. Some of them have since back in the late spring, early summer of 2006 become involved in some merger activities.

Q Who was that?

A I'm not sure which ones. But we have changed the group over time. And to the extent it shows up in Value Line that's what they're doing, we take the company out of the group.

Q Okay. I'll hand you a document and ask you to identify it.

A This is DeQuane Light Holdings, Inc.'s Form 10-K for 2006.

Q Turn to page 6, please. Read the highlighted portion.

A On July 5th, 2006, we entered into the merger agreement with Consortium -- let me just spell this, M-a-c--y-a-r-i-e, Consortium led by M-a-c-q-u-a-r-i-e Infrastructure Partners and Diversified Utility and Energy Trusts, DUET.

Under the terms of the agreement, M-a-c-q-u-a-r-i-e Consortium will acquire all the outstanding common shares or holdings for $20 per share in cash.

Q Turn to I believe it's page 13. Thirteen. You went past it.

A Oh, sorry.

Q Read the two highlighted portions.

A There are risks if we do not complete the merger with the M-a-c-q-u-a-r-i-e Consortium, but risks are associated with the successful consummation of proposed merger with the M-a-c-q-u-a-r-i-e Consortium.

Q Can you tell me again when that merger was announced?

A In July of 2006.

Q Do you know when your surrebuttal testimony was filed in this docket? Would you accept March of 2007?

A I signed the affidavit on March 13th, so sometime after that.
Q When did you file your direct testimony in this case?
A The affidavit is dated June the 26th of 2006.
Q I'll hand you a document and ask you to identify it.
A This is Green Mountain Power Corporation's Form 10-K for 2006.
Q Turn to page 8, please. Read the highlighted portion at the bottom.
A On June 22nd, 2006, the company announced that it had entered into an agreement. It's planned merger date as of June 21st, 2006 (the merger agreement) among Northern, New England Energy Corporation, Vermont Corporation, NNEEC, North Stars, Merger Subsidiary Corporation, a Vermont corporation and wholly owned subsidiary of NNEEC (the merger sub), company -- and the company pursuant to which merger sub will be merged with and into the company (the merger).
Q Can you read down here the highlighted portion?
A A portion of the approval of the merger was filed with VPSB on August 7th, 2006, and remains pending. The VPS -- VPSB completed near this merger in January 2007 and the petition is presently under advisement by the

VPSB.

Q Thank you. Isn't it true that there is significant risks associated with an electric company having it's securities downgraded below investment grade?

A Depends on the circumstances. But usually, it is of an increased risk. That's what causes the downgrade.

Q Do you know if any of your comparable companies have been downgraded below investment grade?

A I don't know if -- one of the rating agencies may have done that. I don't believe that any of them are rated down below investment grade by both Moody's and Standard & Poors.

It's possible after we did the group in the late spring or early summer of last year, those things could have happened.

Q It wouldn't have been possible that that could have happened before you had done your analysis?

A If it was, it was not reported in public information, Value Line, CH Turner, AUS reports and documents like that that economists typically use to get their data.

Q You wouldn't want to include such a company in your comparable companies, would you?

A There's been no challenge to my comparable companies until this litany of things that you have put up here today by other witnesses in the case.

Q You wouldn't want it to affect your company?

A It would depend on the circumstances. I'm sorry.

Q Under what circumstances would you want to include a non-investment grade company in your comparable companies?

A I would not. If I knew about it and if it occurred prior to my forming the proof.

Q Okay. Handing you a document -- when did you file your direct testimony, did you say?

A I believe I told you that the affidavit was signed in June of 2006.

Q I'll hand you a document and ask you to identify it.

A This is the Form 10-K for 2006 for the Central Public Service Corporation.

Q Central Vermont? Is that --

A Yeah.

Q And they're one of your comparable companies?

A Yes.

Q Okay. Will you turn to page 14 and read the highlighted portion of what's circled there or what's in the brackets?

A Risks related to our current credit rating, which is below investment grade, June 2005, Standard & Poor's rating services (S&P) lowered our corporate credit rating to below investment grade.

We believe that restoration of our credit rating is critical to the long-term success of the company. While our credit rating remains below investment grade, the cost of capital, which is ultimately passed on to our customers, will be greater than otherwise would be.

That combined with our collateral requirements from creditors and from power purchases in sales makes restoration of our credit rating critical.

Looking ahead, as long-term power contracts with hydro Quebec and BYNPC begin to expire five to six years from now, these ratings become even more important.

Access to needed capital is also more of a concern as a non-investment grade company. That speaks to Standard & Poor's. It does not speak to Moody's.

Q Okay. Would you agree that there is increased risk to an electric utility associated with having a company that is too large?

A In some cases where a company is very dependent on usually one large commercial or industrial customer, that does sometimes get mentioned in those reports.

Q Okay. Do you know if any of your comparable companies have dependence on one single customer?

A Sure. I'm sure that some of them do, but not to the extent that it reduced their bond rating.

Q I'll hand you a document and ask you to identify it.

A This Green Mountain Power Corporation.

Q Turn to page 9. Read the highlighted portion here.

A Single customer dependence. The company's one major retail customer, IBM, accounted for 15 percent, 15.3 percent, 16.4 percent of the company's retail operating revenues in 2006, 2005, and 2004 respectively. No other retail customer accounted for more than 1 percent of the revenues during the past three years.

Q Thank you. Do you know if Aquila has any single customer that amounts to 15 percent of their revenues?

A I do not.

Q In your testimony, you discuss Aquila's small size. How did you define small?

A I looked at their total revenues and their total asset investment.

Q Okay. So you looked at revenues in plant?

A Revenues and total access.

Q Okay. Can you tell me what Aquila's revenues are?

A No.

Q Can you tell me in your comparable group which of those companies have smaller revenues?

A Well, the two Vermont companies, Central Hudson. I'm not sure about Empire District. I don't remember theirs. But there are a few companies that would be.

Q Would you agree that Madison Gas has less revenues than Aquila?

A I don't know.

Q You don't know. Would you agree -- I believe you said Green Mountain. I believe you said Empire District. Would you agree that DuQuane Light has less revenues than Aquila?

A I would be surprised if that's so, but it may be. That's not one of the screens we used.

Q I believe you said Central Vermont and CH -- Central Hudson; is that correct?

A Right.

Q Okay. So Central Hudson and Central Vermont, DuQuane Light, Empire District, Green Mountain and MGE. You also said that you looked at plant size or the amount of plant -- net assets on -- I don't want to put words in your mouth. What did you say you looked at to determine that Aquila was smaller?

A In Value Line, I list the revenues of the companies and total assets of the companies. And so those are the things I looked at.

Q Total assets. Can you tell me what Aquila's total assets are?

A No.

Q Can you tell me of your comparable group who has that total assets?

A Probably the same companies that you read before.

Q So you would agree that Central Hudson --

A Mr. Smallwood, I don't know that -- that's not a filter that we use. I think it's irrelevant in the sense that we used a large group, and we tried to make it representative of the average electric utility industry. Specifics like that simply don't come into the process.

Q Okay. When you looked at construction risk in this case, isn't it true that you looked at the budgeted investment for the next six years and divided that by net plant?

A That's correct.

Q Okay. Can you tell me what net plant is?

A It's a little over a billion dollars.

Q Can you tell me how net plant is defined, how it's calculated?

A For most utility companies, it's the cost of the plant minus depreciation. But sometimes there are adjustments for regulatory factors and things like that.

Q Would you agree that, absent any additional investment, net plant will tend to decrease over time as a result of depreciation?

A That's the definition. Yes.

Q Okay. Therefore, if there were no additional investment over time, construction risks would tend to increase when you have additional investment? Your denominator is getting smaller?

A It's the same for every company, though.

Q Okay.

A It's -- it's no different from the companies in the comparable group. The same things happen for them as well.

Q If Aquila has not been investing in the company, their construction risks will be larger because net plant is smaller; is that true?

A We'd have to think about that and look at all the surroundings. That's a possible effect, but there might be many other things, too.

Q You told me that you measured construction risk by the budgeted investment divided by plant?

A Yes. That's because that's what the rating agencies do.

Q Okay. Absent any additional investment by Aquila over time, that construction risk will go up because of depreciation?

A I think you're setting up sort of a totalogy, if you will, this, this, that. But it happens to all companies. Depreciation is the same process for the comparable company group as it is for Aquila.

If you're saying that Aquila over the last several years has had financial difficulties and, therefore, their plant investment has been less, possibly.

But what the rating agencies looked at is how big the investment program is relative to existing net plant. Now, I've never seen them mention the factor that you are describing.

Q Okay. Did you look at Aquila's investment in its Missouri properties over the last five years?

A No, I didn't. I did just what the rating agencies do.

Q Okay. Are you familiar with Staff's expressed concerns regarding Aquila' planning process?

A No.

Q Are you familiar with Staff's concerns that Aquila has not invested in plant and instead entered into purchase power agreements?

A I have not been involved in those issues.

Q Can you tell me how long Aquila has been rated below investment grade?
A I looked at that last night, but I don't remember which year it changed.
Q Do you have any idea --
A 2002, I'll say.
Q Okay.
A But I don't know if that's a fact or not.
MR. THOMPSON: I'm going to object, your Honor. He said he didn't know.
MR. WOODSMALL: I'm moving on. But thank you for protecting the witness.
MR. THOMPSON: That's quite all right.
Q (By Mr. Woodsmall) During this time, is it your understanding that Aquila has had a large debt load?
A It -- it's certainly had a large debt percentage of capital during that time.
Q Okay. In fact, isn't it true that recently Aquila has sold several utility operations in an effort to reduce its debt?
A Yes.
Q Just about done. Can you tell me what capital structure you're recommending in this case?
A Forty-seven and a half percent equity, 52 and a half percent debt. But it's my understanding just from

what I was told and heard in the opening statements this morning, there is agreement, at least among some of the parties, to use the actual capital structure, which contains 48 and change percent equity.

Q Can you tell me how you reach the 47.5 equity ratio?

A Yes. I was given that number as part of the company's capital assignment process. I reviewed it. I talked to people who did it. I understood what they did.

I compared that then to the comparable companies' structures, found it to have less equity slightly, but about the same and cited those things in my testimony.

Q Can you tell me when this capital assignment study was done by the company?

A I don't know when it was last updated, but it's been going on since the 1980s.

Q Can you tell me if -- do you know if it's been updated since you initially filed your testimony?

A I do not know.

Q Okay.

A Mr. Williams would know about that.

MR. WOODSMALL: Okay. No further questions. Thank you.

JUDGE VOSS: Who is up next?

MR. THOMPSON: That would be Staff, your Honor.
JUDGE VOSS: Yes. It would be Staff. As I said before, if every single party didn't have a separate independent list of cross --

CROSS-EXAMINATION

BY MR. THOMPSON:
Q Good morning, Dr. Hadaway.
A Good morning, Mr. Thompson.
MR. THOMPSON: May I approach, your Honor? I'd like to get my chart back.
JUDGE VOSS: Yes, you may.
MR. THOMPSON: Thank you.
Q (By Mr. Thompson) Thank you, sir. Have you had an opportunity, Dr. Hadaway, to examine this chart that's been marked as Exhibit 241?
A Well, I've -- I was looking at it until -- earlier in the day.
Q And would you agree with me that the recommendation that you sponsored in your direct testimony was 11.5?
A The total recommendation was. But the base ROE, which is what the Commission has used in its comparison for this test of reasonableness in the past was -- was within the range of reasonableness at 11 and a quarter.
Q So the total recommendation was 11.5. And would

you agree that that's represented by this diamond-shaped mark here on this graph?

A I think that's a fair representation, yes.

Q And would you agree that your revised recommendation sponsored in your rebuttal testimony was 11.25?

A That's the total, including the risk adjustment, yes.

Q And would you agree that that total recommendation is represented by this diamond-shaped mark here on this graph?

A It is.

Q And have you read the testimony offered by Mr. Gorman on behalf of certain intervenors?

A Yes, I have.

Q And would you agree that his recommendation was 10.0 ?

A Yes, it is.

Q And would you agree that that's represented by this diamond-shaped mark here?

A Yes.

Q And have you read the testimony of Staff witness, Mr. Parcell?

A I have.

Q And would you agree that his representation was a range from 9.0 to 10.0 to 10.25?

A That's right.

Q With a mid point at 9.625?

A Yes, sir.

Q And would you agree that that range and that midpoint are represented by this graphic here?

A Yes.

Q And you're familiar, you've indicated, with the Commission's analytical tool referred to as a zone of reasonableness; isn't that correct?

A Yes.

Q And you understand, do you not, that that zone is 100 basis points on either side of the average of recently awarded return on equity in the industry under consideration?

A That's right.

MR. THOMPSON: And I'd like to get an exhibit marked, and this would be Exhibit 240. I told you I had saved that number for something. And this, your Honor, is identified as the Regulatory Focus, January 30th, 2007, published by Regulatory Research Associates. And I have copies for the Bench.

JUDGE VOSS: Okay. I'll mark all of them for the commissioners who aren't here.

MR. THOMPSON: Okay. I think that's enough.

Here's one for you, sir.

MR. HADAWAY: Thank you.

MR. THOMPSON: Are you ready, Ms. Reporter?

THE COURT REPORTER: Yes.

Q (By Mr. Thompson) Do you recognize that document that has been marked as Staff's Exhibit 240?

A Yes, I do.

Q And would you agree with me that that document is a publication that sets out the returns on equity that have been awarded over a particular period of time, in particular, industries by state regulatory bodies?

A Yes. The rates of return for gas, electric and to the extent there are any telephone companies.

Q Okay. Would you agree with me, turning to page 3, that the average for year 2006 is 10.36?

A Yes, it is.

Q And that average is represented on this chart marked as Exhibit 241 by this somewhat livid purple line here; is that correct?

A That's right.

MR. THOMPSON: I hate to disagree with you, your Honor, but I would suggest that an opening statement can be substantive evidence when it includes an admission against interest.

And I would draw your attention to the admission against interest made by Mr. Swearengen when he stated that the return on equity average for the first quarter of 2007 is 10.3.

Q (By Mr. Thompson) Did you hear that testimony or that opening by Mr. Swearengen, sir?

A I did.

Q Now, 10.3 is not represented on this chart, is it, so far as you can see?

A No.

Q But that would be slightly lower at either end than the zone of reasonableness that is indicated here, is it not?

A Well, under the Commission's procedures, you would probably take off the first quarter of 2006 and add 10.3. I don't think you would just look at it as one point.

Q Okay. But -- but if you were just going with that, it would be somewhat lower than what's represented here; isn't that correct?

A That's right.

Q Okay. So would you agree with me that this chart is an accurate representation of the values that it purports to portray graphically?

A Mr. Thompson, I tried to say to counsel for Air Force earlier, over half the companies in that 10.36

average are distribution and transmission and distribution only companies. They are not integrated companies.

So this comparison, while it was used by the Commission, is -- you know, I think it's a factual representation of the totals here. It does not tell the details which are included in your Exhibit 240.

If you look beside the companies, T&D and DI, those footnotes mean that these are distribution only and transmission and distribution only companies which are typically thought of as being slightly lower risk than the integrated companies.

So while it's factual, I think that information is important in terms of perspective for your chart.

Q Thank you for that gloss. And with that in mind, do you agree that this factually is accurate representing the items it purports to represent?

A Yes, sir, I believe it does.

MR. THOMPSON: And with that, I will move the admission of Exhibit 241.

JUDGE VOSS: Are there any objections to the admission of this exhibit?

MR. WOODRUFF: Did he say 241 or --

JUDGE VOSS: 241.

MR. THOMPSON: This is 241.

MR. WOODSMALL: Okay. I'm sorry.

MR. THOMPSON: And the RRA report is 240.

JUDGE VOSS: I'll note, in the copy I had, it had Exhibit 519, probably from another case at the bottom, so you might want to mark that out.

MR. THOMPSON: That was -- that was from the recent Ameren case. We're saving the taxpayers' money by reusing exhibits as much as possible. Any objection?

JUDGE VOSS: Hearing none, Exhibit 241 is admitted into evidence.

(Exhibit No. 241 was offered and admitted into evidence.)

MR. THOMPSON: Thank you, your Honor. And I would also at this time move the admission of Exhibit 240, which is the Regulatory Research Associates report for January 30th, 2007.

JUDGE VOSS: Are there any objections to that exhibit? Hearing none, it is admitted.

(Exhibit No. 240 was offered and admitted into evidence.)

Q (By Mr. Thompson) Now, Dr. Hadaway, you were paid to do your research and prepare your analysis and to appear for testimony today; isn't that correct?

A Yes, sir.

Q Do you happen to recall how much you've been paid?

A I do not know.

Q Okay.

A I have a record on the units.

Q Do you know if those invoices have been provided to Staff?

A Typically, they are. I don't know if they have been yet or not. But it tells on there exactly what I am paid. Or what my company is paid, not what I'm paid.

Q Yes, sir. Now, the -- the Captain, who represented Federal Executive Agencies, I don't recall if it was during his opening or during questioning, stated that what you do is a science. Do you recall that characterization?

A I'm not sure if I do or not.

Q Would you accept that he did make that characterization for purposes of going forward with this question?

A Certainly.

Q In fact, it's not a science at all, is it? It's an art. Wouldn't you agree with me that it is an art rather than a science?

A It's a combination of the two.

Q I would refer you to your testimony on page 22 of your direct in which you stated, and I don't have the line number, quote, estimating the cost of equity is fundamentally a matter of informed judgment, closed quote. Do you agree that you made that statement?

A I did. But that's following many, many pages explaining the science part of it, the equations and the things we would use to do the mathematical calculations.

Q Well, let me ask you this: In a science, would you agree with me that anyone who is able to read could take a laboratory report and use the apparatus described in that report and follow the steps described in that report and replicate the experiment there in recorded?

A Mr. Thompson, I kind of remember in chemistry almost failing a course by not being able to do just that. But I see what you're saying. And I certainly don't disagree if we followed all the instructions exactly right and the model was not too complicated, we might replicate the results.

Q And do you think that I, a mere attorney, who is -- is --

MR. WOODSMALL: I object.

Q (By Mr. Thompson) -- unable, I'll admit, unable to add or subtract accurately, do you think I could take the formula for the DCF model, the formula for the risk premium model, the formula for the capital assets pricing model and apply those to numbers that I might find in Value Line reports and produce a return on equity recommendation for this or any company that anyone should pay attention to at all?

A Well, that's -- that's the half and half of the question that you asked me. Just as in a chemistry class, if the instructor tells us how to do the models and how to put the input in correctly, then you would have an estimate of the cost of equity if the inputs that were given to you by someone were correct.

Mechanically, the CAP-M is not difficult to use. The DCF model, even in its various form, is fairly simple compared to a lot of equations. And the risk premium is very, very easy.

Q But isn't it a matter of expertise to select the inputs that go into those equations and result in estimations?

A Yes.

Q Now, in your testimony, you describe a traditional constant growth, discounted cash flow model analysis that you, in fact, discarded; isn't that correct?

A Yes, sir.

Q And you report that the results of that analytical exercise were a range of 10.0 to 10.1; isn't that correct?

A I believe that's right.

MR. THOMPSON: That's all the questions that I have. Thank you, Doctor.

JUDGE VOSS: Public Counsel is next. Public Counsel?

MR. MILLS: Thank you.

THE COURT REPORTER: I need to change paper real quick.

MR. MILLS: Good morning, Dr. Hadaway.

DR. HADAWAY: Good morning.

JUDGE VOSS: Just a second, Mr. Mills.

(Break in proceedings.)

JUDGE VOSS: You can begin whenever you're ready, Mr. Mills.

CROSS-EXAMINATION

BY MR. MILLS:

Q Dr. Hadaway, my name is Lewis Mills. I represent the Public Counsel in this proceeding. Is it your testimony that lower interest rates have occurred since you filed your direct testimony in this case?

A Yes.

Q Okay. Is it also your testimony that this decrease in interest rates has caused the cost of equity capital to decline?

A The models indicate that, yes.

Q Do you have any reason to dispute the models?

A No. That's why I reduced my recommendation by

50 basis points for the base.

Q So you agreed with those models and made a reduction in your rebuttal testimony?

A I did.

Q Okay. Is it also your testimony that forecasts of future interest rates are lower than when you filed your direct testimony?

A They are a little bit lower. Yes.

Q When was the analysis that's included in your correct testimony completed?

A Probably about the first of June of 2006.

Q And that analysis would have included both current and forecasted interest rates, would it not?

A It did. Yes.

Q Okay. And have both current and forecasted interest rates declined since that time?

A They have declined a little bit more on the actual interest rates. The BBB rate was about 6.6 percent when we were preparing the testimony in June. And it's now 6.25 percent this last week. The forecast was for a 5.4 percent Treasury bond rate one year out. At that time, that was for the middle of 2007.

The forecast now for one year out is 5.3 three percent. So the forecast has come down some, but not as much as the actual rates.

Q Okay. Are you familiar with the -- the concept of circular reasoning?
A I've heard the term used.
Q Okay. What does it mean to you?
A I suppose it means that if you make a given assumption, then other things follow from that automatically.
Q Okay. And is it your understanding that a result reached from circular reasoning would not be a valid result?
A It depends on what it's used for.
Q Did you do a company-specific DCF for Aquila?
A No.
Q Why not?
A The company doesn't have the financial data required to do that. And, certainly, the utility operating companies are not publicly traded, so they couldn't be done that way at all.
Q Okay. Did you include Aquila in your comparable group?
A No.
Q And why not?
A Because it does not meet the minimum investment grade dividend payment grade requirements of the field.
Q Typically, when you do DCF analysis for other

companies, do you include the target company in your comparable group?

A We do not.

Q And why is that?

A Just because it creates a focus on that company that is not typically statistically valid. A one-company sample is not very useful. Even where conditions such as AEP, for whom we do rate of return work, even when companies like that would fit the criteria otherwise, we do not include them in the group.

Q And is that partly because that would lead to circular reasoning?

A No. It just leads to focus particularly in proceedings like this on that one observation, which, in my experience, is not as statistically valid an approach as looking at a broad roof. But we didn't.

Q But would it not also lead to circular reasoning by including the target in the comparable group?

A In some Commissions, they require a look at that one individual company. And in earlier times when utilities were more homogenous than they are now, a lot of Commissions just looked at the -- the one company.

They didn't consider it to be circular at all. They were looking at the risk of, you know, the subject company.

Q Okay. Now, would you agree that the case we're currently involved in is a general rate proceeding?
A If that's a legal question, I don't know. But I understand that's what we're doing.
Q The object is to set rates for Aquila based on all relevant factors; isn't that correct?
A Again, I'm hesitant to tell you what the purpose of this is. We're here for a rate case, and I'm here to testify about the cost of capital.
Q All right. Do you still have a copy of Exhibit 240 in front of you, the Regulatory Focus from January of 2007?
A Yes, sir, I do.
Q Is that the source of the information that you included in the table found in your rebuttal testimony on page 4, lines 18 through 27?
A Yes, it is. I'm sorry. I see now that the date that I have there is one day off in my testimony. So that -- but there's only one RRA publication during that time period, so that's --
MR. MILLS: Your Honor, I'd like to have an exhibit marked.
JUDGE VOSS: Okay.
MR. MILLS: 409; is that correct?
JUDGE VOSS: That's what I have as your next

exhibit. What would you like to title that exhibit?

MR. MILLS: This is a synopsis of the -- the rates of return for the electric utilities contained in Exhibit 240.

Q (By Mr. Mills) Dr. Hadaway, can I get you to confirm that that Exhibit 409 reflects the numbers that are -- the rate of return numbers that are reflected on pages 6 and 7 of Exhibit 240?

A It -- it does, but it's not complete because it doesn't have those footnotes that I mentioned earlier that tells you that 13 of these are T&D companies.

Q Right. But in terms of the -- just to show the date of the award, the name of the company and the ROE awarded, that's an accurate exhibit?

A Yes. I checked them quickly, but I believe you're right.

MR. MILLS: Okay. With that, I'll like to offer Exhibit 409.

JUDGE VOSS: Are there any objections to this exhibit?

MR. THOMPSON: None.

JUDGE VOSS: Hearing none, it is admitted.

(Exhibit No. 409 was offered and admitted into evidence.)

MR. MILLS: Your Honor, I'd like to get another exhibit marked.

JUDGE VOSS: This is 410?

MR. MILLS: Yes.

MR. THOMPSON: Thank you.

JUDGE VOSS: What did you want to title this exhibit, Mr. Mills?

MR. MILLS: Gosh, I didn't realize I get to title it. I would call this Commission authorized returns for 2006, excluding Missouri cases and Iowa incentive case.

Q (By Mr. Mills) Dr. Hadaway, do you have a calculator there with you?

A I do.

Q Okay. It may come in handy. If you'll notice, Exhibit 410 has got three fewer utilities on it than Exhibit 409; is that correct?

A Yes.

Q And I'll -- I'll give you a hint, but you can confirm this. It excludes two Missouri cases and one particular Iowa case; is that correct?

A Yes, it does.

Q Okay. And you can either calculate this yourself or -- or rely on my representation. But if you exclude those three returns, the average drops from 10.36 to 10.22, and the median drops from 10.25 to 10.20. Would you like to calculate that?

A I'll be happy to do that if you want me to, but it certainly appears be to correct. If you take out the three highest ones, integrated utility companies, and leave all the T&D companies in there, you're going to get a lower result.

Q That really wasn't my question, but thank you for offering that remark. Have you confirmed that those numbers are correct?

A I have not. Would you like me to do it? I'll be glad to.

Q Yes. Yes, please.

A I get a slightly different answer, but I'm doing it probably with some rounding. You may have done this in the computer. But they're certainly very close, within rounding.

Q Within acceptable rounding?

A I think so.

Q Okay. Now, if I can get you to turn back to Exhibit 240, which is the Regulatory Focus exhibit, for the electric utility decisions that are cited on page 5 through 7, can you verify that only one of the utilities for whom a return on equity percentage is listed does not have an amount listed under the column Amount in Millions of Dollars?

A It will take a few minutes to -- if you wanted to point me to where that is, I'll be happy to look.
Q I'm looking specifically on page 6 in the middle of the -- the first quarter of 2006, the Mid-American Energy case in Iowa.
A Yes. I see that.
Q That does not have a -- millions of dollars nor an entry for test year and rate base nor an entry for common equity as capital structure?
A It does not.
Q Nor overall rate of return?
A No, it does not.
Q Okay. And that has an 11.90 ROE listed; is that correct?
A Yes. Correct.
Q With a footnote. Can you turn to the footnote section and tell me what Note 4 says?
A Footnote 4 is on the last page, page 10, of the exhibit. And it says ROE applies only to a proposed 545 megawatt wind generation project.
Q Okay. And what was your understanding of what that means?
A It means that the company has applied to build this project and that Commission in Iowa stated that they with give them 11.9 percent ROE.

Q And so the calculation of that ROE is a different exercise than what we're doing here in this case; is that correct?

A I was not involved in the case. I've actually talked to Mid-American people about it, but I don't know how it was calculated.

Q Okay. But judging from the lack of other information on page 6, it appears as though that was done outside of the context of a general rate case?

A It was done in a special proceeding like the FERC has done to encourage transmission investment. The Iowa Commission was willing to establish an ROE and track the ROE to encourage investment in those projects.

Q Okay. Thank you.

A The rate case would come later, I assume.

Q And turning back to Exhibit 410, in comparing 410 to 409, that Iowa decision is one of the three that was omitted; that is correct?

A Yes.

MR. MILLS: Okay. Your Honor, I would like to offer Exhibit 410.

JUDGE VOSS: Are there any objections to the admission of 410? Hearing none, it will be admitted.

(Exhibit No. 410 was offered and admitted into evidence.)

Q (By Mr. Mills) Now, turning to Exhibit 409, what Commission authorized the highest rate of return in 2006?

A The Iowa Commission.

Q Okay. After the Iowa case, which the next highest?

A Missouri Commission.

Q Okay. What is the third highest?

A Wisconsin, the first entry there, Northern States Power.

MR. MILLS: Okay. Your Honor, I'd like to have another exhibit marked.

JUDGE VOSS: Thank you. 411. Mr. Mills, if you have enough, I think I'm one short. I can make a copy.

MR. MILLS: I have plenty.

JUDGE VOSS: Thank you.

MR. MILLS: You're welcome.

Q (By Mr. Mills) Mr. Hadaway, what I've just handed you is a portion of the transcript from a recent Commission proceeding, Case No. ER-2007-0002 in which a return on equity witness sponsored by the Commission Staff was talking about -- primarily about returns awarded in Wisconsin.

MR. MILLS: And, your Honor, I'd like the Commission to take official notice of Mr. Hills' testimony in that case relating to the Wisconsin Commission.

JUDGE VOSS: Mr. Who?

MR. MILLS: Yes. Staff witness Steve Hill in the UE case.

JUDGE VOSS: You're wanting his filed testimony or the --

MR. MILLS: No. His testimony on the stand that's represented by this section of the transcript, questions by Commissioner Clayton and responses by Mr. Hill. And that's what's represented by Exhibit 411.

JUDGE VOSS: Are there any objections? That's fine.

MR. MILLS: Do you want to admit that as an Exhibit number, just so it's --

JUDGE VOSS: I think it will make it more convenient.

MR. MILLS: Okay. That's fine.

JUDGE VOSS: Would anyone have any objection to having this exhibit admitted? It's admitted.

(Exhibit No. 411 was offered and admitted into evidence.)

MR. MILLS: Your Honor, I'm going to show the witness another document. I don't believe I have to have this exhibit. It just has some calculations that may be helpful. I'll pass it out. I don't think it needs to be marked.

JUDGE VOSS: Okay.

A Thank you.

Q (By Mr. Mills) This is really the same as 410. It just has the quarterly calculations on it.

A Okay.

JUDGE VOSS: Mr. Mills, do you think your questions will make it clear what you're talking about for the Commissioners that aren't here if you don't mark this?

MR. MILLS: Well, why don't we go ahead and mark it? It certainly won't hurt.

JUDGE VOSS: Okay.

Q (By Mr. Mills) Dr. Hadaway, what I've been -- what I've just handed you and has been marked as Exhibit 412 is a document very similar to Exhibit 410, except that it has another column which shows the average by quarter of the -- the companies that are included on this exhibit.

And I'm going to ask you some questions that have to do with those quarterly averages, so if you want to -- if you want to confirm that those are accurately calculated for the purpose of asking my -- answering my questions, you may want to go ahead and --

A I don't feel that I need to do that. I'm happy to try to answer your question.

Q Okay. Okay. Now, when were the - the two

Missouri Commission decisions issued, the 11.25 and the 11.0?

A I'm sorry. I may be confused there. Did you say 11.0?

Q I did, but I misspoke. I meant 11.25 and 10.90?

A Okay. I see those. They were both in December of 2006.

Q Okay.

A Although there is a typo on this exhibit that says 2007.

Q You're absolutely right. There is a typo there.

A It's just a typo. It's not a substantive --.

Q Okay. All right. Now, with those two Missouri return on equities, is one 50 basis points higher than any other return on equity authorized during the fourth quarter of 2006?

A I mean, the numbers are what they are. It -- are you asking me if it's -- how much more --

Q Is the 11.25 50 basis points higher than -- than -- other than the Missouri one than the next highest number?

A Well, it is. But, again, you're comparing to a bunch of T&D cases. They're not integrated utilities.

Q That wasn't my question.

A Well, I understand. But it's not a direct comparison. It's not a fair comparison.

Q You've made that point clear. I'm just asking about the numbers. And is the lower one 15 basis points higher than any others?

A Yes.

Q Okay. Now, with respect to the averages, is the -- is the highest Missouri decision 104 basis points higher than the average return authorized during the fourth quarter of 2006?

A I may be doing this backwards. It looks like it's nine basis points.

Q Higher -- the hundred --

A The 109 basis points.

Q The 109. Okay. And how about the --

A I'm sorry. I think maybe we're both doing this wrong. Let me just do -- do the calculation, please. Yes. I think that's right.

Q Okay. And is the other one 69 basis points higher?

A Yes. That's the one I was working on. I'm sorry. That's right.

Q Okay. Now, is your revised recommendation in this case of 11.25 percent, then, also 104 basis points higher than the fourth quarter reported ROEs that the

Missouri cases are excluded?

A The total request by the company including the risk data is, but the 10.75 base, which is what the Commission used in the KCPL case is not.

Q What did the Commission award in the KCPL case?

A 11.25.

Q What do customers pay rates based on?

A 11.25, I assume, if I understand the question.

Q And if your recommendation is approved in this case, will customers pay rates based on an 11.25 return?

A Counsel, my point is that you are making a comparison that's not consistent with the Commission's --

MR. MILLS: Your Honor, can I get the witness to answer my questions instead of what he wants to answer?

JUDGE VOSS: Please answer the questions. I'm sure Mr. Swearengen is more than capable of helping you clarify your answers on redirect.

MR. HADAWAY: Yes, your Honor.

JUDGE VOSS: Okay.

Q (By Mr. Mills) My question was, if the Commission authorizes an 11.25 percent rate of return in this case, is that what the rates will be based on?

A As far as I know.

MR. MILLS: Okay. Your Honor, I'd like to have another exhibit marked.

JUDGE VOSS: Did you want to offer 410 -- or 412?

MR. MILLS: Sure. I would like to offer Exhibit 412.

JUDGE VOSS: Does anyone have an objection to 412? Hearing none, it's admitted.

(Exhibit No. 412 was offered and admitted into evidence.)

JUDGE VOSS: Mr. Mills, with regard to Exhibit 409 and following, were they all for January of 2006, or is the 2007 on these other sheets source reference accurate?

MR. MILLS: They should all be 2006. There is one sheet that has an inaccurately typed in '07. And I believe that is line 24 on Exhibit 409. And as Dr. Hadaway pointed out, that one should also be '06.

JUDGE VOSS: Thank you.

MR. MILLS: You're welcome.

Q (By Mr. Mills) Now, Dr. Hadaway, with respect to Exhibit 413, which I have just handed you, do you understand that that is an exercise similar to the one that we went through on Exhibit 410 in that it removes the two Missouri cases, that one Iowa case that we talked about and the Wisconsin return?

A It says it includes the Wisconsin -- excludes

Wisconsin due to their past policy --

Q Yes.

A -- is what it says.

Q So that brings the total number of companies shown on this -- the total number of decisions shown on -- on this sheet down to 21 and drops the average to 10.18 and the median to 10.20 --

A That's correct.

Q -- is that correct?

MR. MILLS: Okay. Your Honor, I'd like to offer Exhibit 413.

JUDGE VOSS: Are there any objections to this exhibit? Hearing none, it is admitted.

(Exhibit No. 413 was offered and admitted.).

Q (By Mr. Mills) Okay. Dr. Hadaway, I'm going to switch gears just a little bit here and talk about a fuel adjustment clause for a moment.

In general terms, all else being equal, will a fuel adjustment clause stabilize the revenues of Aquila?

A All else being equal, it should.

Q Okay. And does stabilization of revenues result in less earnings volatility?

A Typically, it does.

Q Okay. Would you expect that it would for Aquila if a fuel adjustment clause is awarded in this case?

A Everything else being equal, yes.

Q Okay. And does a reduction in earnings volatility result in a decrease in business risk, again, all else being equal?

A It does. And that's why I didn't have any adder for that fact under this case.

MR. MILLS: Your Honor, I'd like to have the gratuitous comment added to the end of that question stricken.

JUDGE VOSS: I was passing exhibits. I didn't hear it.

MR. MILLS: Can we have it read back, please?

JUDGE VOSS: It would help if you start with the question.

(The previous question and answer were read back.)

MR. MILLS: And the answer is yes, it does. And the why I didn't do something different in this case is simply gratuitous and non-responsive, and I'd ask that it be stricken.

MR. SWEARENGEN: You can go ahead and strike it, I'll ask him that later on.

JUDGE VOSS: I was going to say -- okay. Please strike that from the record.

MR. MILLS: Thank you. Now, I'd like to talk about the CAP-M for a few minutes. In your rebuttal testimony, on page 8, lines 22, 23 and page 9, lines 15 to 17, is it -- is it an accurate reading of your testimony there that you -- that you discount the value of the CAP-M for regulatory proceedings?

A Yes, I do. Most regulators do that as well.

Q So is it your testimony in this case that you believe the CAP-M provides limited value to the Commission in setting rates?

A Some commissions look at CAP-M. Some don't. Most do not. I do not typically.

Q So in your expert opinion, in this case, does it provide good value or little value to the Commission?

A It depends on the Commission's choices. It's a received model that some witness use. I wrote my doctoral dissertation on the capital asset pricing model. And because of the number of inputs and requirements that that model has, it results in a wide range of cost of capital estimates.

For that reason, equally credible people offering equally reasonable assumptions can get very, very widely different answers. And most Commissions don't use that model because of that.

Q And my question didn't have anything to do with most Commissions. My question was, would you, in your expert opinion, advise this Commission to rely on the CAP-M or not rely on it?

A I wouldn't advise them one way or the other. I'm stating personally, I don't use it.

Q And why is that?

A Because of what I just said.

MR. MILLS: Okay. Your Honor, I'd like to have another exhibit marked.

JUDGE VOSS: How much more do you think you have, Mr. Mills? Significant or --

MR. MILLS: I am well over halfway through.

JUDGE VOSS: Because it's noon. We might take a break. Are you at a decent breaking point with that exhibit?

MR. MILLS: Sure.

MR. THOMPSON: You know, I have a medical condition, your Honor.

JUDGE VOSS: You have a medical condition?

MR. MILLS: It's called hunger, and it's chronic. Yes. I can -- I'm certainly happy to break here if you'd like.

JUDGE VOSS: If it's a good point -- yeah. I just think -- that way people can get their blood sugar back up.

Okay. We are off the record. We will come back at 1:00.

(Lunch recess.)

JUDGE VOSS: All right. We are back on the record resuming cross-examination by Office of Public Counsel.

Q (By Mr. Mills) Dr. Hadaway, before we broke for lunch, we were talking about CAP-M.

MR. MILLS: And I'd like to get an exhibit marked, please. This is 414.

JUDGE VOSS: Uh-huh. I do like exhibit titles, if you have them.

MR. MILLS: This is an excerpt of the direct testimony of Dr. Hadaway in Case No. E-2006 -0314.

JUDGE VOSS: I understand Commissioner Gaw will be joining us, but he was in a meeting and hasn't even had food yet.

Q (By Mr. Mills) Dr. Hadaway, do you recognize the document that's marked as 414 that I just handed you as a section of your testimony from the KCPL rate case, ER-2006-0314?

A Yes, I do.

Q Can you tell me the source of the information that's shown on the table of -- at the top of page 28 of your direct testimony in that case?

A The top five rows come from Regulatory Research

Associates, similar to the document we were looking at this morning but from an earlier time.

Q Okay.

A And the utility cost of debt comes from what's called Emergent or Moody's record. It has Moody's utility bond rate indexes in it.

Q Okay. And is that the -- the same source of information that you use in Table 1 on page 4 of your rebuttal testimony in this case?

A Yes, it is. And, again, the date on that table should be January 30th, not the 31st. I noticed that a while ago when we were looking at the others, just so there's no confusion. It's just one RRA document, and it's January 30th.

Q Okay. Now, turning to Exhibit 414, which is your -- your KCPL testimony, is it accurate to characterize those averages as having a downward trend since 2001 with a slight uptake in 2002?

A They're a little lower on the -- on the most recent one, yes.

Q So except for the uptake in 2002, it's gone down steadily since 2001; is that correct?

A Well, it's gone down the last three or four years now, yes.

Q Okay. And so far in 2007, it's lower yet again;

is that correct?

A   Yes. Just one observation for the first quarter.

Q   Right.

A   But that observation is 10.3 percent as opposed to 10.36.

Q   Okay. And those two tables show the quarterly averages for each year; is that correct?

A   That's right.

Q   Is it correct that the average return for -- that no quarter since the last quarter of 2003 has exceeded 11 percent?

A   I believe the 11 percent in the first quarter of 2004 is the last 11 percent average, yes.

Q   Okay. But it's never exceeded that 11 percent since 2003?

A   Not that I'm aware of. No.

Q   Okay. Let me -- let me ask you about that qualifier. What do you mean by not that you're aware of? Are there some other RRA numbers that --

A   Oh, I'm sorry. That's just a matter of speaking. I don't think there are any other numbers.

Q   Okay.

A   You've just given me little pieces of things here.

Q Okay.
A I think your statement was exactly right.
Q Okay. Thank you. Now, in general, are rate of return recommendations based on data from periods prior to the implemation -- implementation of rates?
A Usually, the record is made before the order is done, yes.
Q And the date is based on periods before that?
A Right.
Q Okay. So is it accurate to state that authorized returns could be characterized as lagging behind the market return?
A Some people argue that. But some Commissions literally look in the paper when they're getting ready to do their -- their final order. I mean, I -- I've had that in a recent case where a Commissioner asked me questions from that day's newspaper.
So there can be some lag. I don't disagree with that. But it's not always profit.
Q Now, your original recommendation was 11.50 percent; is that correct?
A It was the base rate of return of 11.25 percent for the comparable group plus 25 basis points, which made the total 11.5.
Q Okay. Now, is it accurate that either that

original recommendation of 11.5 percent or the revised recommendation of 11.25 percent is higher than the annual average of authorized return on equity by utility Commissions at any quarter in this century?

A If you mean since 2000 --

Q Yes.

A -- no. I don't -- I don't think that's right.

Q Okay. Which -- which quarters have been above 11.25?

A Well, if you look at 2001 in whatever number this exhibit is of my testimony, 414, there are two quarters there that are above 11.25.

Q After 2001? Or 2003?

A Yes. In 2003, the fourth quarter was 11.47, so there are a number of observations above 11 and a quarter in this century.

Q Any as high as 11.5 since 2002?

A Since 2002, no.

Q Now, is Aquila considered investment grade by rating agencies now?

A No.

Q Okay. Do you know how long they have been below investment grade?

A Well, I was asked this earlier, and said I thought it was since 2002. But I answered that I didn't really know.

Q Okay. Is Aquila a partner in the IATAN II construction project?

A Yes.

Q Will that project represent a significant capital investment by Aquila over the next few years?

A Yes. It certainly will.

Q Okay. Do you know, are there two other Missouri utilities, KCPL and Empire District, that are also partners in that project?

A I know KCPL is. I don't know about Empire.

Q Okay. And from your involvement in the recent KCPL rate case, are you aware that KCPL has what was referred to in that case and what has been referred to generally as a regulatory plan?

A Yes.

Q Okay. Is that regulatory plan premised on providing KCPL the opportunity to maintain investment grade status?

A I was not involved when they did all the particulars of it, but I learned about it in the last case. And what it states is that they will attempt to get Standard & Poor's financial metrics or ratios in the upper two-thirds of BBB ratings which implies metrics consistent with BBB.

Q Okay. And is it your understanding that is because, generally speaking, the cost of capital is lower for companies that are investment grade?
A Yes.
Q Okay. Now, under the KCPL regulatory plan, are ratepayers given credit in the rate-making process for providing the necessary cash flows?
A They will be when -- you know, the plant is completed, it will have a lower value --
Q Right. Okay.
A -- based on any amortization that they do prior to operation.
Q Okay. Does Aquila have a regulatory plan?
A Not that I know of.
Q Okay. Now, is it your understanding that Aquila's non-regulated activities are the reason underlying Aquila's current status as below investment grade?
A I really haven't analyzed that. Certainly, there was a lot of discussion in the press about Aquila and its problems with non-regulated activities.
But I don't know and I haven't read all the rating reports from back in the earlier days to -- to know exactly what the causes were.
Q Okay. For Aquila ratepayers, will they receive

any credit or recognition in any future rate proceeding for providing profits to Aquila?

A Only if you put construction work in progress into rate base and provide a profit on that. To my knowledge, that would be the only way. And I don't think you can do that in this state.

Q Okay. Now, if I can get you to turn to Schedule 17 to your rebuttal testimony?

A Yes. I have that.

Q Let me catch up. Now, is this an update of an earlier schedule?

A Yes, sir.

Q And what exactly did you do to update it?

A I asked the company to provide me with the additional construction forecast that they now had at the end of 2006 as compared to where we were back in the spring in -- early summer of 2006.

Q So, basically, you moved Aquila's net plant up a year based on more recent data?

A Well, we took, obviously, 2006 off, and we added 2012 and that's based on the six-year forecast. It's really a five-year forecast because 2007 is kind of what's going on right now. But that's the thing that Mr. Williams has in his testimony and can explain the details of.

Q Okay. So the last line above the source shows that you're looking at Aquila's net plant from 2007 to 2012?

A That's right.

Q Okay. Did you update the capital expenditures for the companies you're comparing it to?

A Yes.

Q This shows 2006 through 2011.

A That's all Value Line had. You know, in December when we were doing this, Value Line didn't have its additional forecast on there.

Q So that the numbers you're looking at for Aquila are a year more recent than all the numbers you're comparing them to?

A They're not exactly. They're based on a year later period, but they're still based on the same number of years. And for the other companies, Value Line does update those.

If you look back at the original rate testimony schedule like this, you'll see that they are different for the comparable companies as well.

Q And the way you've laid this out, Aquila net plant goes up between 2005 and 2006; is that correct?

A Oh, yes uh-huh. That is correct.

Q But yet you're comparing that to 2005 net plant for all the other companies?

A Again, that's because that's the base of what's in the Value Line data.

Q Right. And I'm not really trying to get to why you're doing that. Mr. Swearengen can ask you that. I'm trying to get at what you did.

A That's exactly what we did.

Q Okay. And it's at least possible, if not likely, that many of those utilities will have greater net plant in 2006 than they did in 2005 just as Aquila does; is that not true?

A Well, I think if I just let that one lay and say yes or no, we'd get a misinterpretation. Because when the Value Line dates put 2006 in there, they will put the 2012 numbers in for those companies as well. They do that consistently.

So you can say if we compared 2012 to 2005 and what your implication would be would be correct. But that's not the way Value Line's going to do it, and that's not the way we do it.

Q Now, what you did was you looked at a period of Aquila that's more very recent than the period for all the other companies; is that correct?

A That is correct --

Q That's --

A -- because --

MR. MILLS: That's all the questions I have. Thank you.

JUDGE VOSS: Okay. I'm trying to find out --

MR. MILLS: Your Honor, did I offer Exhibit 414?

JUDGE VOSS: I don't believe so.

MR. THOMPSON: No.

MR. MILLS: I would like to offer 414 at this time.

JUDGE VOSS: Are there any objections to 414? Hearing none, it is admitted.

(Exhibit No. 414 was offered and admitted into evidence.)

JUDGE VOSS: In furtherance of proceeding as rapidly as possible, I'm going to go ahead and start redirect with the understanding that if Commissioner Gaw comes down and joins us, it may lead to more because I don't have any independent questions for the witness. Does that sound okay to everyone?

MR. SWEARENGEN: Fine.

JUDGE VOSS: And, Mr. Swearengen, we will proceed with some redirect.

MR. SWEARENGEN: Thank you.

REDIRECT EXAMINATION

BY MR. SWEARENGEN:

Q Dr. Hadaway, let's just stay on that Schedule 17 for a minute that Mr. Mills was asking you about, Schedule 17 to your rebuttal testimony. And he was asking you some questions about the -- the time periods that you were looking at comparing Aquila and the other companies.

And why did you look at a more recent time period for Aquila if that is, in fact, what you did?

A Those are the most recent forecast data that are available. My concern was that he was saying that 2005 for the other companies was somehow smaller based on the comparison of Aquila to itself from 2005 to 2006.

Certainly, that's the case. But it goes in the other direction. If you take the 2005 net plant for those comparable companies and add this updated data even through 2011, the Value Line has it higher. That makes ratio higher.

And in the rebuttal testimony, it is higher than it was in the direct testimony. So, in fact, what he was asking me about, what I was trying to explain was that, if anything, this is kind of an over-statement of the percentage for the comparable companies, if anything.

Q So then if I -- if I asked you does the exhibit somehow distort the result you're attempting to show, what would your answer be?

A No, it does not.

Q In turning back, kind of looking backwards here, if we can, to Exhibit 414, which is some direct testimony that you -- a portion of some direct testimony that you presented in the KCPL case last year -- do you have that in front of you?

A Yes, sir.

Q Up at the top of page 28 where those numbers are laid out for 2001 through 2005 by quarter, am I correct to understand that those are -- are averages for the returns that would have been awarded in each of those quarters?

A Yes, sir. That's right.

Q Now, let's take 2003, for example. I think maybe that's the most recent -- the first quarter of 2003 would be the most recent quarter on that document where the average return would have been above 11 and a quarter? Is that a correct statement?

A Yes, sir. That's right.

Q And for the average -- the average shown there is 11.47 percent; is that correct?

A Yes.

Q And for that average to be 11.47, there would have had to have been some awards above that amount and some below that amount; is that true?

A Yes.

Q Okay. This morning, I believe it was Mr. Mills

that -- well, excuse me. I think it was General Counsel that put in front of you what was marked as Exhibit No. 240, the Regulatory Research Associate Regulatory Focus dated January 30, 2007?
A Yes, sir.
Q Do you still have that in front of you?
A I do.
Q And for purposes of what we're talking about in this proceeding, I take it we should just focus on the -- the information pertaining to electric utilities?
A That's all that I have used in this case. Since this is an electric utility case, that's what most people would do.
Q And over on I guess it's page 7 of that document where the -- at the bottom where the full year 2006 averages are -- are shown in the second column under ROE, it says 2.36; is that correct?
A Yes, sir.
Q And is it your understanding that that's the source of this -- this number that we've been using and our discussions today about the 2006 average --
A Yes.
Q -- electric return? Okay. Now, as a follow-up to that, I think Mr. Mills took information from this exhibit and put together a series of exhibits, 409, 410,

412 and I think 413 and made various adjustments as set out in those documents. Do you recall that?

A Yes, he did.

Q Is there -- when looking at -- at Exhibit 414, 410, 412 and 413 and comparing them back to Exhibit 240, is there some common thread or common denominator that is present or missing with regard to those exhibits?

A What I tried to say then was that these exhibits don't have the footnotes, so it's impossible for one just looking at them to see that -- I said 13 cases. There were 13 cases cited during 2006, but only 11 of them were T&D cases that had ROE.

So I misspoke a little bit earlier. But 11 of these cases of the 25 with regard to distribution and transmission and distribution only -- pardon me. The -- the thing about that is that if you look on Exhibit -- Staff 240 and you go off to page 6, that's where 2006 starts.

And then the far right-hand column, that's where the footnotes are. Any of those companies that say DI means distribution only. And any of them that say TD mean transmission and distribution only.

That's where there are 11 of the companies with ROEs that are either distribution or transmission and distribution.

And if you look at those companies' ROEs, they are by far the lowest numbers in this document starting in January of -- the 27th of 2006, you see United Illuminating in Connecticut, 9.75.

If you go down to June 6th, 2006, you see Del Marva at 10.0. If you go to Maine Public Service, July -- on July 6, you see 10.2. If you go to Common Wealth Edison, July 28th, you see 10.05.

If you go -- and this is where I made a mistake. Some of them don't specify the ROE, and I counted them previously. The center point is in there with a T&D, but it doesn't have an ROE. So now I'm correcting that.

So you go on down, October 6, you find Intel Energy Systems. They're a little distribution company in New Hampshire, distribution only, 9.67.

If you look at the next page, your three Illinois Commission decisions, November 21st, they're 10.12 and 10.08 and 10.08.

Q Okay.

A If you go on down, you see a couple more cases that don't have the ROEs that are distribution cases. But the point is, in these exhibits that Public Counsel used, he's taken out three and more cases for various reasons.

All of those are integrated electric cases. One about the wind power exhibit, I certainly agree is an unusual case. But he didn't take out any T&D cases that were consistently much lower than the national average.

Had he taken those out, the national average would have been significantly higher than 10.36. So I was not able to say that before, but I think that's the fair picture of what this exhibit should show.

Q Is Aquila a distribution company only?

A No. It's an integrated electric company.

Q Is it a transmission and distribution company?

A No. It has -- it does those functions, but it also certainly has generation, so it is a full integrated electric utility.

Q Mr. Thompson had asked you some questions about whether what you do is an art or a science and in the process of those questions asked you about a DCF calculation that you performed in connection with this case where the result, I think you said, was 10 percent, 10.1 percent ROE. Do you recall that question?

A Yes, I do.

Q And I think you said that you did not use the results of that particular DCF model in this case; is that true?

A That's correct, sir.

Q And why did you use those results?

A If we look in my direct testimony, it's what's called Schedule SCH-11. I provide various risk premium test reasons in that exhibit. And I show the traditional constant growth number up there 10.00 to 10.1. If you compare that to any of these risk premium data, the result is more than a hundred basis points lower. And I excluded the cost of growth, traditional growth rates, for that reason.

When we did the same thing in the rebuttal testimony for the update, just like the other models, the constant growth model has gone down about 50 basis points. It's now showing only about 9.4.

The risk premium has also gone down about 10.75. So, again, the constant growth DCF model with traditional growth rates included in it produces an ROE that, to my way of thinking, is below the reasonable range relative to my risk premium analysis. And that's why, basically.

Q Several times this morning in response to questions, you said that -- you used the word screen in describing your process of selection of proxy companies, comparable companies. Do you recall that?

A Yes, sir.

Q And what do you -- what do you mean by the use of that word "screen?" What did you mean?

A We take all the companies that are published in the three editions of Value Line that cover electric utilities. There's 61 or two of those, you know.

We then checked their bond ratings. And if either Moody's or Standard & Poors has them as an investment grade graded company, they have passed the initial screen. So bond rating test is first.

In Central Vermont, for example, it does not have investment grade rating by Standard & Poors, but did have one by Moody's. So that's why it was included.

We then look at the percentage of revenues derived from regulated services, either electric utility sales or gas-related sales, totally regulated, and we divide that by total revenues.

And if that number is not at least 70 percent, in other words, if all those other kinds of activities are more than 30 percent and we exclude the company, the average for the group is over 80 percent regulated revenues, eight 87 in one group and 84, something like that in the other.

And so we screen the companies by applying those tests to see if they represent what we're trying to represent.

Q Okay. Now, at one point you said that size was not a screen that we used. What do you mean by that?

A Size is an issue that some Commissions, including this Commission, have sometimes looked at to see if they need to adjust the ROE upward for a small company. This Commission has done that. I did not do that. Aquila is certainly smaller than Southern Company.

I think we went through a series of questions that maybe there were about six out of the 24 that may be smaller than Aquila. And that means the others are larger.

So we don't use that because we don't try to narrow the group down since all the companies, given a certainly bond rating, competed for capital in the same competitive markets. We don't use size as a screen.

Q Did you say that Value Line was -- Value Line's investment survey was the source of the information that you used for determining your group of comparable companies?

A That, and -- and, obviously, the bond ratings come from the rating agencies. We use the publication from -- it's actually AUS Services or something now. But it's usually called the C.A. Turner report, the same one that the other witnesses in this cased used.

And we collect up all the data. Value Line is the basic source of the data.

Q How -- how does Value Line characterize nuclear ownership regeneration in terms of risk?

A It's what I tried to say this morning. Nuclear risk is not viewed as a serious question. Many companies now requesting extensions of their licenses, they're requesting new nuclear plant construction licenses.

Over the past at last four years since gas prices have become so volatile and energy prices in general, nuclear power plants have been looked at as a stabilizing feature for most of the companies as compared -- nuclear operations has always been considered more risky, and, certainly, nuclear construction just because of the size and the time lag. But that's sort of a stale comparison today. It's just not the way the financial markets look at things.

Q I think early this morning it was Captain Hollifield that asked you whether -- and I think he said that -- that made the comment that perhaps you do not trust the DCF model. He suggested that. Do you recall that?

A Yes, I recall it.

Q And what is your response to that?

A I think it was in conjunction with one of the questions you asked me a few minutes ago about why we didn't use the traditional cost of growth model. It doesn't have anything to do with trusting or distrusting the model. It has to do with testing its results, again, to check the reasonableness.

So I use two other versions of the DCF model, so-called multi-stage model, and, also, a constant growth version. But one uses a much longer term growth rate than the other witnesses.

Q Let me ask you just a couple of other questions. I think it was Mr. Woodsmall that had an exhibit that was a portion of the company's 10-K. Do you recall that?

A Yes.

Q Do you have a copy of that in front of you, an exhibit? I think it was Exhibit 512.

A Yes. I have that.

Q And if you would turn, please, to page 25 on 166. It's shown in the upper right-hand corner. Do you have that?

A Yes, sir, I do.

Q And at the top of that page, is it -- are the words "risk factors" on your copy?

A Yes, sir.

Q And below that, Operating Risks?

A Yes, sir.

Q Can you read into the record, please, the paragraph that begins with the words, If we cannot complete?

A If we cannot complete this asset sale or if we are not able to retire a principal amount of debt sufficient to reduce our interest expense to a level that can be satisfied by the cash flow generated by our remaining utility operations, we will continue to have a cash flow shortfall. We may also need to explore alternatives with respect to financing the significant capital expenditures anticipated in connection with environmental upgrades and compliance as well as capital expenditures generally required to continue to provide safe, reliable service to our remaining utility customers.

Q Thank you. And then over the lunch hour break, were you able to take a look at the complete copy of Aquila's Form 10-K dated December 31, 2006?

A I looked through it, and I did find additional information in it.

MR. SWEARENGEN: Could I have an exhibit marked, please?

JUDGE VOSS: Yes. Let's see. What are you guys up to?

MR. SWEARENGEN: I have no idea what the number should be.

JUDGE VOSS: I will try to check that for you. Let's see. I have 38.

MR. SWEARENGEN: 38. Okay. Thank you.

MR. THOMPSON: Have you got one for me?

MR. >SWEARENGEN: I do.

MR. THOMPSON: Thank you.

MR. SWEARENGEN: Are we ready?

JUDGE VOSS: Yes. And this is the 10-K that -- Aquila's 10-K additional page?

MR. SWEARENGEN: Yes.

Q (By Mr. Swearengen) Dr. Hadaway, do you have in front of you what has been marked for purposes of identification as Exhibit 38, a one-page document, which I will represent to you is page 33 from Aquila's Form 10-K filed with the FCC for the year ending December 31, 2006? Do you -- do you recall talking a look at -- at this page over the lunch break?

A Yes, I did.

Q And where on that document are the construction expenditures for the company discussed? Can you tell us?

A There's a table that demonstrates up above that the company's construction requirements through 2009 are well over a billion dollars. If we look at just the electric part, it's 284 million in 2007, and it goes to 400 million in 2008, 362 million in 2009.

MR. SWEARENGEN: Thank you. I would offer into evidence Exhibit 38.

JUDGE VOSS: Are there any objections to that exhibit? Hearing none, it will be admitted.

(Exhibit No. 38 was offered and admitted into evidence.)

MR. SWEARENGEN: That's all I have. Thank you.

JUDGE VOSS: Now we'll going back to questions from the Bench. Commissioner Gaw, did you have any questions for this witness?

COMMISSIONER GAW: Maybe just -- just a few.

CROSS-EXAMINATION

BY COMMISSIONER GAW:

Q There -- you were referencing earlier a distinction between vertically integrated utilities and -- and distribution companies and transmission companies, maybe. I can't remember if you included transmission companies or not.

A I included transmission and distribution. They're listed in RRA as the ones with the T&D beside them. And DI is just distribution only.

Q Okay. And can you give me an example of a distribution company?

A Yes. The three Ameren subsidiaries that operate in Illinois are distribution only companies.

Q The -- can you name them for me?

A They're -- they're listed on the exhibit that we were looking at just a moment ago on page 6 or 7. If we look on page 7 of Exhibit --

JUDGE VOSS: Is that 512?

A Staff Exhibit 240. I'm sorry. I got it backwards. Staff Exhibit 240, page 7.

Q (By Commissioner Gaw) Do you want to tell me who they are since I'm trying to filter through who --

A Yes, sir. November 21st, there near the top of that page, you see Central Illinois Light, Central Illinois Public Service and Illinois Power. Those three are distribution only companies. Or I'm sorry. They're T&D companies.

Q Transmission and distribution?

A Yes.

Q Okay. And how are their rates set?

A The Illinois Commerce Commission has rate proceedings and sets the rates just for that function.

Q Okay. Do you know whether or not those -- those companies are load serving entities or whether -- excuse me. Are they load serving entities or not?

A Do you mean in the sense of providing generation?

Q Yeah. You know -- you've heard the term load serving entity before, haven't you?

A Well, I'm not sure if I'm familiar with how you use it here.

Q Okay. In regard to -- in regard to the provision of service in Illinois, who pays -- what -- who pays the entities that are listed here as Central Illinois Light, Central Illinois Public Service and Illinois Power for the -- for the service they provide?

A If it's like most states -- and, Commissioner Gaw, I am -- I'm just speaking from things that I do know about in some other states. Typically, the so-called retail electric providers pay the T&D wires companies.

But the wire -- the reps collect the money and then pay it over to them. In Illinois, I don't know if they really have any -- very many people that are participating as alternative providers.

Q Are you familiar with the status of the Illinois retail market place?

A I have, like everyone, read quite a bit about the concerns they have about their power auction -- auctions to obtain the -- I think it would have been the load serving part of what you were asking me about.

Q Okay. And do you know -- but do you know the particulars of how the -- I believe you said retail electric providers, how they fit in with these transmission and distribution companies?

A Again, speaking from the actual experience that I have not in Illinois, but the T&D companies are just pure wires delivery businesses in most of the regulated states. And how they interface with the reps may very well depend on whether that market is developed.

In Texas where I'm most familiar with the operations, there are many reps, and the reps pay the wires companies.

Q Yes. Okay. But in Illinois, are you familiar with how they inter-relate and how those things --

A I'm not sure that their market has really been forthcoming.

Q Do you know when their market opened --

A I did the --

Q -- generally?

A I did the Comet case, and I think it may have been 2002. But, again, I don't have those facts at my fingertips.

Q You don't know, then, whether or not the -- the actual auctions of that took place, when they would have taken place, the --

A The actual auctions occurred about a year ago.

Q In fact, toward the end of last year? Would that be correct?

A Yes, sir.

Q Now, would these entities that you -- that you mentioned, Central Illinois Light, Central Illinois Public Service and Illinois Power, would they be impacted by the regulatory environment in Illinois?

A Certainly.
Q In what way?
A There has been concern because of the controversy about the power auctions and whether or not the much higher prices that were involved now that the price freezes have gone off on in that state, how -- how to translate those additional costs to the customers.
Q And when you say customers, what -- who do you mean as customers?
A The retail customers, like a residential customer or commercial customer.
Q All right. Now, I'm trying to make sure I'm following you here, so I apologize for -- for some of these questions. They may be -- they may seem very simplistic.
But when you're -- when you're dealing with the -- the distribution and transmission companies, why would that regulatory environment matter?
A The rate of return that's established is applied to those entities' investment in transition and distribution, and it includes consideration for their operating expenses, their O&M expenses and that sort of thing. So it's a standard rate case, from my experience.
Q Yes. I -- okay. I understand what you're -- what you're answering. I was asking a slightly different

-- for a slightly different response, and that is in regard to the amount that they received, the -- the payment that they receive, if it's like you believe it to be, as you described in Texas, they get paid by the retail electric providers that are using their system, correct?

A If -- if they have ones external to themselves. Many of the companies simply haven't had that developed in Illinois, from my understanding.

Q What do you mean? That they hadn't had it developed, what does that mean?

A There just aren't a bunch of retail electric providers that aren't incumbent utilities.

Q Okay. If it is an incumbent utility that is providing service through these transmission and distribution companies, are they the same company that's providing that power, or could -- is it probably an affiliate of that -- of that T&D?

A The -- the one that I know about is -- is Commonwealth Edison because that's the case I worked in up there last year.

Q Okay.

A And they do have -- excuse me. They do have a generation affiliate that had a power contract. That same affiliate also bid in the auction, and I don't know what the ultimate results of the auction -- how that all turned out.

Q Okay.

A But once the rate freeze went off, whatever the results of the auction produced were going to be much higher prices for the consumers in the state.

Q And I guess, again, that would probably be the case in -- with -- with any utility operating, for instance, the Ameren utilities that you mentioned here, it would -- it would not surprise you if the -- a majority or -- or -- of the power being sold over the transmission and distribution companies' facilities would be supplied by an affiliate of those T&D companies?

A It -- it was prior to the auction, certainly. But after the auction, it just depended on the results of the auctions, and I don't know from these companies.

Q It wouldn't have surprised you if that had been the result, though, correct?

A It was the result for Commonwealth Edison, at least on these questions.

Q Okay. Now, why would a transmission and distribution company be impacted by the instability -- the uncertainty of the implementation of the retail market? Because I think you described that a little earlier. Why would they be impacted by that environment?

A I may not have fully appreciated your question.

I was thinking of how their rates were set and how they were impacted by the regulatory environment, the level of return and that sort of thing.

Q Yes.

A With respect to price of power, other than conservation where companies are asking for a decoupling method and things like that, the volatility of the whole power market simply make the whole industry appear to be more risky. And it is.

Q Okay. So in the event that -- for one thing, unless they just set their prices to the be -- I keep wanting to say load serving entity, I'm sorry, that's the term I'm used to -- to the retail electric providers. Unless it's all just done at a set price regardless of volume, then the volumetric differences will have an impact on their revenue stream of the T&D?

A For some companies, rate designs have been changed to straight fixed variable kinds of things and whatnot like that. But for most companies, they have not.

Q Okay.

A Other than -- other than the recovery and the customer charge and some decoupling activities, they have not.

Q Okay. So in -- so in that event, that would be one degree of uncertainty that asks for the T&D companies in a retail choice environment?

A Yes.

Q And then would it also have some potential impact on the company's risk as a T&D company if the affiliates -- the affiliate generating company might be impacted by the advent of the retail market?

A I'm --

Q In other words -- in other words, when credit rating agencies are setting some of their ratings, is it not the case that they will, under most circumstances, examine beyond the limits of the T&D company itself, and an affiliate generating company might bleed off into the setting of the -- of the rates -- or of the credit rating agency? Sorry about that.

A If -- if they're all still part of the same company, I -- I suppose that would be the case.

Q And when you say same company, do you mean that they have to be under the same corporation or if they're -- as long as they're still affiliates of one another? That would be the question.

A If -- if a generating affiliate of a company had some disastrous result occurring, it would depend on what some people rate fencing and whether or not you treat it as if it were a separate issue somehow. I don't know that splitting up companies -- that has been an issue. It could have been. Mostly, that obviously occurs in mergers and acquisitions, things like that.

Q Yes. So there are additional risks in that environment for a T&D company that might not necessarily be present in a vertically integrated state, correct?

A Well, I don't know if I can agree with that because it -- I think what you're suggesting is that if they are still affiliates, they're all part of one company --

Q Yes.

A -- and they haven't actually divested of the T&D operations and integration into separate companies, that makes them look more like an integrated utility --

Q Yes.

A -- in terms of parent company overall.

Q Yes.

A And, again, I don't know mean to be prevential, but in the state of Texas, most of the companies there, there two of the major ones, literally sold their generation. They divided up into different companies. They separate T&D wires companies center point and does not have even a retail electric provider, for example.

Reliant does, and Reliant has the generation. But they divided up into separate companies, so it's an issue there.

To the extent that Commonwealth Edison does have generation that is part of the same Exalon public company and the wires company is also a part of that, then they are a bit more like an integrated company would be.

Q Okay. So would it not be the case that if -- if affiliates were still providing generation into the market in a retail choice state, affiliates of a T&D company, and the state were moving into a new environment regarding the -- regarding retail choice from -- from a transitionary period in -- in -- where there were rate freezes and other things going on that, in fact, there -- there may be some additional risks to that T&D company that would be -- well, let's say, risks that would be equal to or in some cases greater than what might exist in a vertically integrated state that was not moving toward retail choice?

A If we put that last part on where the whole company is -- is a fully regulated environment, you -- you might touch on that -- that same issue.

Those companies, though, that we're talking about in Illinois, if they get their power supply from an auction where it's not necessarily an affiliate provider, then the matter of the deregulated piece being more risky is certainly true.

But whether that really is going to spill over, there's a way for it to spill over again. In the companies that's I'm most familiar with, it cannot in Texas.

Q Do you know whether or not there has been a recent downgrade of the Ameren utilities in Illinois as a result of the regulatory -- regulatory changes and questions that are arising in regard to what may happen to the retail choice markets going forward?

A Yes.

Q Tell me what you -- what that downgrade was, if you know.

A I -- I don't know the details. I just saw that it happened.

Q Okay. So, in fact, are you familiar with whether or not that particular downgrade potentially or did impact the entirety of the Ameren affiliates?

A It -- at least Standard & Poor's is very forthcoming in talking about their corporate groupings and ratings being related to parents and affiliates.

Q Okay.

A The other rating agencies don't say as much about it. But they have certain things -- if they change an owner's rating will have the impact if there's anything changed down in the subsidiary's operations or not.

Generally, though, my statement is about T&D companies being less risky follow directly from what the rating agencies have said. I've testified in many of these cases. And, obviously, companies don't like having the lowest rate of return possible. Like the companies in the New England states have gotten 9 and a half, something like that, and they argue that some of the very things that you're talking about exist.

And I'm familiar with what you're saying. But the rating agencies say the T&D companies are going to be typically given business positions, Standard & Poor's says of there whereas an integrated company is likely to be a five.

So while these things you're asking me about or speaking about are certainly possibility, they are not way things are generally reviewed.

Q Well, in -- in general, are most T&D companies set up like they are in Texas?

A Many of them sort of are. They don't have -- most places don't have the complete separation and, certainly, for example, TSU did not sell off its various assets. It formed three different parts to the company, a retail electric provider and wires company and power generation, which is a merchant function now. But it's still all part of the same holding company.

Q All right. And I believe you've already testified that when the spin-off doesn't do go outside of an affiliate that they -- that they still resemble more of the nature of a vertically integrated company?

A At the parent level, certainly, they do.

Q All right. And have you done an analysis of these T&D companies that are included in lists that have been discussed earlier here today to differentiate between those T&D companies that are completely separate and apart from affiliates that -- that are self-generation or not?

A We -- we have actually tried to do that. But -- but because most of them are part of a larger entity like you're suggesting, there's just not statistically a large sample. Center Point would be a good example.

Q Of -- of which?

A Of just a pure T&D operation.

Q Okay.

A Part of the old Reliant Energy Company. But Exalon, obviously, is a big company, and that's the publicly traded entity for Commonwealth Edison.

Ameren is the publicly traded entity for the other three Illinois companies up there. So there's not a publicly traded sample that you can use to see if there's a different in the rate of return.

But, certainly, the results of the rate cases indicate that there -- the results have shown that the returns that are allowed have been lower.

Q Of what -- of which companies?
A The T&D companies. They're much lower.
Q Of all T&D companies or just of the companies that are separated?
A Oh, I'm sorry. A little earlier, we went through staff Exhibit 240 on pages 6 and 7. They have footnotes that show the rate case results for the distribution only and T&D companies.
And if you look at those, they are the ones that are 9.55, 9.75, 10.0. The integrated electric companies' numbers are higher than those. There aren't any integrated electric companies that got rates of return as low as 9.55 or even 9.75.
Q Do you know what the rationale was for setting those rates in each one of those cases?
A Not in each one. But I was the witness for the Commonwealth Edison. I was the witness for Utilicorp in New Hampshire. You know, I've testified in a number of cases in Texas. So, you know, I've seen the issues. I just -- yeah. I can't for all of the cases, but I can speak for those.
Q And you've already stated that in Texas, most of the T&D companies are separated from any generation companies?
A Well, of the three major companies --

Q Other than IATAN II?
A Yes. Of the three major companies, two are and one's not.
Q Two are separated and one is not separated?
A Yes.
Q And in a retail choice environment, the generating company itself, would you say that it is subject to more or less risk than a vertically integrated company in a non-retail choice state?
A Merchant generator?
Q Merchant or -- just any -- any of the companies that are -- that are providing load service as retail electric providers. I see -- I see a merchant generator at as something different maybe than you do, so I'm being careful now with my terms.
A Certainly, the deregulated generation function is more regulated, is more risky than the regulated T&D function.
Q All right. Have you ever done any -- I don't suppose there would have been a reason for you to have done some sort of an analysis about the incremental difference in that risk?
A The -- the way we did that was to take a look at oil and gas delivery companies, high fixed cost companies, forest and paper would products companies. The rating

agencies have done an analysis like this comparing maybe what merchant generators are going to look like. Then we prepared the integrated electric company data before deregulation and gas distribution only companies.

Q Yes.

A And we found that gas distribution companies and regulated electric companies didn't have significant variability in their cash flows. But, certainly, relative to the deregulated and forest and paper products, energy products and those kinds of things that the regulated entities were certainly less risky. That's the analysis we've done, and I've presented that in several cases.

COMMISSIONER GAW: Okay. I think that's all I have, sir. Thank you.

MR. HADAWAY: Thank you.

JUDGE VOSS: Is there any redirect based on questions from the Bench?

MR. WOODSMALL: Recross first?

JUDGE VOSS: I meant recross.

MR. WOODSMALL: I have one.

CAPTAIN HOLLIFIELD: I've got one.

JUDGE VOSS: Did you have any, Captain?

CAPTAIN HOLLIFIELD: In the -- give me the order. I forgot.

JUDGE VOSS: Well, on the official list, it would be you, then Sedalia Industrial Energy Users.

RECROSS EXAMINATION

BY CAPTAIN HOLLIFIELD:

Q Dr. Hadaway, I just wanted you to -- back here. I just wanted you to repeat the -- what you had said about my characterization of your treatment of the DCF model, please.

MR. SWEARENGEN: Your Honor, I'm going to object to that. I think that's something that Commissioner Gaw brought up, and I think these cross-examination questions should be limited to questions that were based on his questions.

CAPTAIN HOLLIFIELD: My apologies. I --

JUDGE VOSS: It is confusing when we break in the middle, but these are just based on the questions that Commissioner Gaw asked.

CAPTAIN HOLLIFIELD: Thank you.

JUDGE VOSS: Mr. Woodsmall?

MR. WOODSMALL: Thank you.

RECROSS EXAMINATION

BY MR. WOODSMALL:

Q You mentioned that you had testified in the Illinois cases; isn't that correct?

A In the Commonwealth Edison case.

Q Okay. Can you tell me what ROE the Commission authorized there?

A I believe it was 10.05.

Q And what was your recommendation in that case?

A I think 11 percent.

MR. WOODSMALL: Thank you.

JUDGE VOSS: Is that the only -- end of your questions, Mr. Woodsmall?

MR. WOODSMALL: Yes. Thank you.

JUDGE VOSS: Staff, do you have any --

MR. THOMPSON: I have one.

RECROSS EXAMINATION

BY MR. THOMPSON:

Q With respect to the companies set out in Exhibit 240 --

A Yes, I have that.

Q -- those ROEs are reported for the year 2006. Are you -- can you tell me any case in which the Commission excluded T&D companies in calculating the -- the average?

A Other than the exhibits I saw today, I haven't seen anybody exclude any of the companies, and I have not.

MR. THOMPSON: Thank you very much. No further questions.

JUDGE VOSS: Public Counsel?

MR. MILLS: No questions. Thank you.

JUDGE VOSS: Any redirect based on --
MR. SWEARENGEN: I have just one.
JUDGE VOSS: Okay.

REDIRECT EXAMINATION

BY MR. SWEARENGEN:

Q Dr. Hadaway, Commissioner Gaw had asked you some questions about the T&D companies in Illinois just generally and discussed with you some risks that those companies might be experiencing. Do you recall that?
A Yes, I do.
Q Would it be your understanding that in setting the authorized rate of return for those T&D companies, the regulators would take into account those risks?
A The company asked them to take those into account. I'm not sure in Illinois if they did or not.
Q Okay. What about in any other jurisdiction?
A In Texas -- I'm sorry to sound -- it's just where I've done most of my work, and it's what I know mostly about. The Commission adjusted the capital structure downward and adjusted the ROE upward to the same -- approximately the same level as the average return.
Q And they did that why?
A Based on staff recommendation, they adjusted the Staff recommendation up 50 basis points to avoid having to do double counting of capital structure and ROE.

MR. SWEARENGEN: Thank you. That's all I have.

JUDGE VOSS: Seeing no further questions, I believe, Mr. Hadaway, you're excused.

MR. HADAWAY: Thank you, your Honor.

JUDGE VOSS: And I guess we are ready for Mr. Trippensee.

RUSSELL TRIPPENSEE,

being first duly sworn to testify the truth, the whole truth, and nothing but the truth, testified as follows:

DIRECT EXAMINATION

BY MR. MILLS:

JUDGE VOSS: I'm sorry. Please proceed, Mr. Mills.

Q (By Mr. Mills) Mr. Trippensee, are you the same Russell Trippensee who has prepared and caused to be filed direct testimony which has been marked as Exhibit 111 -- I'm sorry -- as Exhibit 403 and rebuttal testimony, which has been marked as Exhibit 404?

A Yes, I am.

Q And if I were to ask you the same questions that are contained therein here today, would your answers be the same?

A Yes, they would.

Q Do you have any corrections to make to those testimonies?

A Not to my knowledge.
Q And are the answers therein true and correct to the best of your knowledge?
A Yes, they are.
MR. MILLS: Your Honor, with that, I will offer Exhibits 403 and 404 and tender the witness for cross-examination.
JUDGE VOSS: Are there any objections to the admission of those exhibits? I know they do cover more than just this issue.
MR. SWEARENGEN: That -- that would be my only concern, that -- that they do cover more than the issue we're dealing with today. So if you could reserve ruling until he's testified on all of those, I think that would be appropriate.
JUDGE VOSS: Would that be all right with you, Mr. Mills?
MR. MILLS: Fine with -- fine with me.
JUDGE VOSS: Let's see. Public Counsel's witnesses. Federal Executive Agencies, do you have any questions for Mr. Trippensee?
CAPTAIN HOLLIFIELD: No questions, your Honor.
JUDGE VOSS: Sedalia Industrial Energy Users?
MR. WOODSMALL: No, thank you, your Honor.
JUDGE VOSS: Staff?

MR. THOMPSON: No questions.

MR. SWEARENGEN: Well, if somebody doesn't ask him, he's going to be upset because I know he missed a golf day this afternoon, so --

MR. TRIPPENSEE: Too cold for that, Mr. Swearengen.

CROSS-EXAMINATION

BY MR. SWEARENGEN:

Q Let me just ask you a couple of questions. I'm just looking at your direct testimony, Mr. Trippensee, which is the -- that deals with rate of return; is that correct?

A That is correct.

Q Okay. And I think you have another piece of rebuttal perhaps. Does that deal with rate of return, your rebuttal?

A Only to the extent it discusses the fuel adjustment clause, which is the purpose of the testimony on rate of return. But it's just more a description, not a direct relationship.

Q Okay. On -- and I'm looking at page 3 of your direct where you have some testimony under the heading Fuel Adjustment Clause Risk Reduction.

A That is correct.

Q And that's the testimony that you have this

afternoon that's pertinent to this issue; is that right?
A Yes, sir, it is. If -- if a fuel adjustment clause is adopted in this case.
Q Right.
A Absent a fuel adjustment clause adoption, the balance of this testimony would not be necessary.
Q I understand. And were you here today and heard Mr. Hadaway testify that -- that his rate of return recommendation is based on the assumption that the company will receive a fuel adjustment clause?
A Yes, I was.
Q And -- and you heard him say that or you understand that to be his testimony?
A Yes, I do.
Q And is it also your understanding that the company has not made any kind of upward adjustment to its proposed rate of return to account for fuel risk because of its anticipation that it will receive a fuel adjustment clause?
A That is the company's position. Yes.
Q I think maybe -- have you testified on rate of return previously?
A Yes.
Q In what cases?
A Missouri Gas Energy.

Q Is that the case where we objected to your testimony and the Commission said that you'd been around the business for 30 years so you could -- you could talk about that? Is that -- is that the right one?

A They may have made something to that effect.

Q Okay.

A Missouri Gas Energy. Atmos Energy recently. I believe in the Atmos case someone pointed out a case, telephone case from the mid '80s where I had some rate of return testimony.

Q Okay. You're familiar with the discounted cash flow model, DCF model?

A Yes, I am.

Q Okay. Would you agree with me that the -- the discounted cash flow model is predicated on the concept that a stock's price represents the present cash value of all future cash flows expected from the stock?

A That's my general understanding. Yes.

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

JUDGE VOSS: Commissioner Gaw, do you have any question for this witness?

COMMISSIONER GAW: No, thank you.

MR. TRIPPENSEE: Thank you.

JUDGE VOSS: Is there any redirect based on questions?

MR. MILLS: I have no redirect. Thank you.

JUDGE VOSS: Well, then, Mr. Trippensee. You are going to have a good Friday. You're excused.

I have a couple things quickly. Mr. Mills, you were not here yesterday. Mr. Dandino was here actually --

MR. MILLS: The day before.

JUDGE VOSS: -- Monday, and you had said that you thought that the additional issues you wanted to amend before would be resolved with the stipulation. Are you withdrawing your motion then to amend the issue list?

MR. MILLS: Assuming that Commission is going to adopt the stipulation and agreement. If not, then there's going to be a whole lot of issues that are in play, and that would be one of them. So I -- I think --

JUDGE VOSS: Reserve --

MR. MILLS: I think I would like to continue to reserve that -- the right to -- but I --

JUDGE VOSS: Okay.

MR. MILLS: In all likelihood, we're going to withdraw that. It's just not quite to the point where we know for sure that it's moot, so --

JUDGE VOSS: Good point.

MR. THOMPSON: I just --

JUDGE VOSS: Are there any additional issues that we need address before we go off the record?

MR. WOODSMALL: What time are we starting Monday?

JUDGE VOSS: 8:30. One thing I will note is I'm still waiting for feedback from a couple Commissioners, but I'm setting up two different times for the stipulation presentation because I have to reserve a phone bank or a Meet Me call so that parties can call in.

So it will either be at -- unless there's a change in the Commission, the notice will come out. I'm hoping for it to either be at 9:00 on Wednesday, presuming we get fuel adjustment clause and all the issues on Tuesday as the original schedule said we would.

In the more likely event that the fuel adjustment clause takes two days, we will do the stipulation presentation on Thursday at nine. And there will be a single phone number reserved for both of those times, and I'll let the parties know no later than 8:00 on Tuesday night by e-mail from that mass e-mail list which of the two dates. All right?

MR. THOMPSON: Thank you, Judge.

JUDGE VOSS: Okay. Thank you. We are off the record.

I N D E X

E X H I B I T S