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Exhibit No. 22
Issue: Amortization
Witness: Robert W. Sager
Type of Exhibit: Direct Testimony
Sponsoring Party: Empire District Electric
Case No.
Date Testimony Prepared: October 2007

Before the Public Service Commission
of the State of Missouri

Direct Testimony

of

Robert W. Sager

October 2007

Empire Exhibit No. 22
Case No(s). ER-2008-0093
Date 5-12-08 Rptr KF

DIRECT TESTIMONY
OF
ROBERT W. SAGER
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO.

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. Robert W. Sager, 602 Joplin Street, Joplin, Missouri 64801.

Q. WHO IS YOUR EMPLOYER AND WHAT POSITION DO YOU HOLD?

A. The Empire District Electric Company ("Empire" or "Company") is my employer. I hold the position of Director of Financial Services.

Q. WHAT ARE YOUR RELEVANT QUALIFICATIONS AND PREVIOUS WORK EXPERIENCES?

A. I am a licensed CPA with a bachelor of science degree in accounting from Pittsburg State University, Pittsburg, Kansas. I have been employed by Empire since October of 2006. I worked for a regional public accounting firm, BKD, for approximately ten years prior to coming to Empire. While at BKD, I was a senior manager providing auditing and consulting services to various corporations, including SEC filers.

Q. PLEASE EXPLAIN THE PURPOSE OF YOUR TESTIMONY.

A. I will discuss the regulatory plan amortization, which resulted from Commission Case No. EO-2005-0263, and the amortization calculation which has been included in this case.

Q. WHAT IS YOUR UNDERSTANDING OF THE REGULATORY PLAN AMORTIZATION?

A. I believe the intended purpose of the regulatory plan amortization provisions is to determine whether rate relief calculated under traditional methods must be supplemented in order to allow Empire to be rated at investment grade levels as provided for in the regulatory plan.

Q. HOW DOES THE AMORTIZATION WORK?

A. The amortization is an amount built into rates in addition to those costs traditionally recovered through rates. Concurrent with cost recovery, the Company records amortization expense equal to the additional amortization costs billed to customers. As a result, the increase to revenues is offset by a non-cash expense so the Company does not recognize additional net income, but does have additional cash from the amortization.

Q. IS THE AMORTIZATION CALCULATION IN THIS CASE CONSISTENT WITH EMPIRE'S REGULATORY PLAN?

A. Yes. The regulatory plan amortization was not designed as a substitute for the timely recovery of prudently incurred costs. I believe that Empire has appropriately requested rate relief under traditional methods and under the Company's filing Empire is not requesting additional amortization because the calculation indicated that additional amortization was not necessary. Attached is Schedule RWS-1 which provides that calculation.

Q. DOES THE LEVEL OF RATE RECOVERY OR AMORTIZATION PROVIDE ASSURANCE THAT EMPIRE WILL HAVE INVESTMENT GRADE CREDIT IN THE NEAR FUTURE?

A. No. While we take prudent and reasonable actions seeking to be assigned investment grade credit ratings by the agencies, we do not assign the ratings ourselves and cannot provide assurance that we will be assigned investment grade ratings. While I believe the amortization calculation is consistent with the regulatory plan, the amortization, if any, and its effect on our financial ratios by itself does not guarantee that Empire's ratings will be assigned at investment grade levels.

Q. WHY DO YOU BELIEVE THAT TO BE THE CASE?

A. Comments from S&P's Corporate Ratings Criteria 2006 guidebook (page 42) may articulate this best. It states, "The ratio medians are purely statistical, and are not intended as a guide to achieving a given rating level. They are not hurdles or prerequisites that should be achieved to attain a specific debt rating. Caution should be exercised when using the ratio medians for comparisons with specific company or industry data because of differences in method of ratio computation, importance of industry or business risk, and the impact of mergers and acquisitions." They further state, "particular caution should be used when making cross—border comparisons, because of differences in accounting principles, financial practices, and business environments." To summarize, S&P is indicating that they assess companies as a whole and meeting certain financial ratios does not guarantee a certain credit rating.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes, it does.

Schedule RWS-1

22NP

The Empire District Electric Company
Calculation of Amortization to meet Financial Ratio Targets
9/25/2007

			Total Company	Juris Alloc
1	Additional Net Balance Sheet Investment			62,224,304
2	Rate Base	Schedule D		733,148,974
3	Jurisdictional Allocation for Capital			0.83639
4	Total Capital	L1+L2		795,373,278
5	Equity	Schedule H1	** **	** **
6	Trust Preferred	Schedule H1	** **	** **
7	Long-term Debt	Schedule H1	** **	** **
8	Cost of Debt	Schedule H4		7.01%
9	Interest Expense	L7 * L8 (+$4,250,000 (TOPRs))		28,851,057
10	Electric Sales Revenue	Schedule J + Schedule D (rate increase)		375,139,158
11	Other Electric Operating Revenue	Schedule J		3,010,138
12	Operating Revenue	L10 + L11		378,149,296
13	Operating and Maintenance Expense	Schedule J		223,288,019
14	Depreciation	Schedule M		35,522,399
15	Amortization	Schedule M		11,168,836
16	Interest on Customer Deposits	Schedule J		599,219
17	Taxes Other than Income Taxes	Schedule J		12,484,292
18	Federal and State Income Taxes	Schedule J + Schedule D (rate increase)		26,463,788
19	Total Electric Operating Exp	Sum of L. 13-18		309,526,552
20	Operating Income - Electric	L12 - L19		68,622,744
21	less: Interest Expense	L9		-28,851,057
22	Depreciation	L14		35,522,399
23	Amortization	L 15		11,168,836
24	Deferred Taxes	Schedule J		2,634,852
25	Funds from Operations (FFO)	Sum of L20-24		89,097,774
26	**Additional Financial Information Needed for Calculation of Ratios**			
27	Capitalized Lease Obligations	EDE Accounts 227 + 243	-152,334	-127,411
28	Short-term Debt Balance	EDE Form 10-Q, p. 8	50,033,000	41,847,101
29	Short-term Debt Interest	EDE Accounts 417.891 + 431.400	2,366,504	1,979,320
30	Cash Interest Paid	Information Supplied by EDE	28,767,000	24,060,431
31	AFUDC Debt (capitalized interest)	EDE Form 10-Q, p. 4	3,970,000	3,320,468
32	**Adjustments Made by Rating Agencies for Off-Balance Sheet Obligations**			
33	Debt Adj for Off-Balance Sheet Obligs			
34	Operating Lease Debt Equivalent	Information Supplied by EDE/S&P	3,066,000	2,564,372
35	Purchase Power Debt Equivalent	Information Supplied by EDE	63,339,000	52,976,106
36	Total OSB Debt Adjustment	L34 + L35	66,405,000	55,540,478
37	Operating Lease Deprec Adjustment	Information Supplied by EDE/S&P	896,000	749,405
38	**Interest Adjustments for Off-Balance Sheet Obligations**			
39	Present Value of Operating Leases	L52 * 10%	306,600	256,437
40	Purchase Power Debt Equivalent	L53 * 10%	6,333,900	5,297,611
41	Total OSB Interest Adjustment	L39 + L40	6,640,500	5,554,048
42	**Ratio Calculations**			
43	Adjusted Interest Expense	L9 + L29 + L55		36,384,425
44	Adjusted Total Debt 6/30/07	L6 + L7 + L27 + L28 +L36		484,510,949
45	Adjusted Total Debt 6/30/06	Same as L65, but for prior year		399,854,960
46	Adjusted Total Capital	L4 + L27 + L28 + L36		892,633,446
47	Adj. FFO Interest Coverage	(L25 + L30 + L31 + L41)/(L9 + L31 + L41)		3.23
48	Adj. FFO as a % of Average Total Debt	(L25 + L37)/(avg. of L44 + L45)		0.2032
49	Adj. Total Debt to Total Capital	L44/L46		** **
50	**Changes Required to Meet Ratio Targets**			
51	Adj. FFO Interest Coverage Target			3.20
52	FFO Adjustment to Meet Target	(L51 - L47) * L43		-1,264,284
53	Interest Adjustment to Meet Target	L25 * (1/L51 - 1) - 1/L47 - 1)		629,716
54	Adj. FFO as a % of Average Total Debt			0.195
55	FFO Adjustment to Meet Target	(L54 - L48) * (Avg of L44 + L45)		-3,621,503
56	Debt Adjustment to Meet Target	L25 * (1/L54 - 1/L48)		18,416,906
57	Adj. Total Debt to Total Capital Target			** **
58	Debt Adjustment to Meet Target	(L57 - L49) * L46		** **
59	Total Capital Adjustment to Meet Target	L44/L57 - L46		** **
60	**Amortization and Revenue Needed to Meet Targeted Ratios**			
61	FFO Adj Needed to Meet Target Ratios	Maximum of L52, L55 or zero		-
62	Effective Income Tax Rate	Schedule G3		0.3839
63	Deferred Income Taxes	L61 * L62/(1 - L62)		0
64	Total Amortization Req for FFO Adj	L61 - L63		0

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