

Exhibit No.: 505  
Witness: Maurice Brubaker  
Type of Exhibit: Surrebuttal Testimony  
Issue: Fuel Adjustment Clause  
Sponsoring Parties: Enbridge Energy, LP  
Explorer Pipeline Company  
General Mills  
Praxair, Inc.  
Wal-Mart Stores, Inc.  
Case No.: ER-2008-0093

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of The Empire District )  
Electric Company of Joplin, Missouri )  
for Authority to File Tariffs Increasing ) **Case No. ER-2008-0093**  
Rates for Electric Service Provided to )  
Customers in the Missouri Service )  
Area of the Company )

Surrebuttal Testimony and Schedule of

**Maurice Brubaker  
on Fuel Adjustment Clause**

On Behalf of

**Enbridge Energy, LP  
Explorer Pipeline Company  
General Mills  
Praxair, Inc.  
Wal-Mart Stores, Inc.**

April 25, 2008

**BAI**

BRUBAKER & ASSOCIATES, INC.  
ST. LOUIS, MO 63141-2000

*Industrial  
Intervenor*

**Exhibit No. 505**

**Case No(s). ER-2008-0093**

**Date 5-12-08 Rptr XF**

Project 8875

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of The Empire District )  
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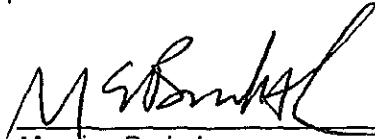
Case No. ER-2008-0093

STATE OF MISSOURI        )  
                                  )        SS  
COUNTY OF ST. LOUIS    )

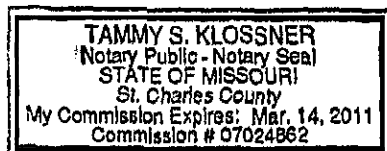
**Affidavit of Maurice Brubaker**

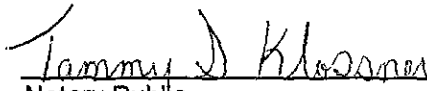
Maurice Brubaker, being first duly sworn, on his oath states:

1. My name is Maurice Brubaker. I am a consultant with Brubaker & Associates, Inc., having its principal place of business at 1215 Fern Ridge Parkway, Suite 208, St. Louis, Missouri 63141-2000. We have been retained by Enbridge Energy, LP; Explorer Pipeline Company; General Mills; Praxair, Inc. and Wal-Mart Stores, Inc. in this proceeding on their behalf.
2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony and schedule on fuel adjustment clause which was prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. ER-2008-0093.
3. I hereby swear and affirm that the testimony and schedule are true and correct and that they show the matters and things that they purport to show.

  
Maurice Brubaker

Subscribed and sworn to before me this 24<sup>th</sup> day of April, 2008.



  
Notary Public

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of The Empire District	)	
Electric Company of Joplin, Missouri	)	
for Authority to File Tariffs Increasing	)	Case No. ER-2008-0093
Rates for Electric Service Provided to	)	
Customers in the Missouri Service	)	
Area of the Company	)	

**Surrebuttal Testimony of Maurice Brubaker**

1    **Q     PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2    A     Maurice Brubaker. My business address is 1215 Fern Ridge Parkway, Suite 208,  
3           St. Louis, Missouri 63141-2000.

4    **Q     WHAT IS YOUR OCCUPATION?**

5    A     I am a consultant in the field of public utility regulation and president of Brubaker &  
6           Associates, Inc., energy, economic and regulatory consultants.

7    **Q     HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS CASE?**

8    A     Yes. I have filed three pieces of testimony prior to this filing. They are:

- 9           • Fuel Adjustment Clause / Revenue Requirement Direct Testimony, filed  
10          February 22, 2008 (Exhibit No. 500);
- 11          • Fuel Adjustment Clause / Rate Design Direct Testimony, filed March 7, 2008  
12          (Exhibit No. 502); and
- 13          • Revenue Requirement / Rate Design Rebuttal Testimony, filed April 4, 2008  
14          (Exhibit No. 503).

1    **Q     ARE YOUR QUALIFICATIONS ATTACHED TO YOUR PRIOR TESTIMONIES?**

2    A     Yes. They appear as Appendix A to the Fuel Adjustment Clause / Revenue  
3           Requirement Direct Testimony filed on February 22, 2008.

4    **Q     WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

5    A     I will address certain positions taken by members of the Missouri Public Service  
6           Commission (MPSC or Commission) Staff in their rebuttal testimony, and certain  
7           positions taken by witnesses for Empire District Electric Company (Empire) in their  
8           rebuttal testimony.

9    **Q     PLEASE SUMMARIZE YOUR SURREBUTTAL TESTIMONY?**

10   A     My surrebuttal testimony may be summarized as follows:

- 11           1. A utility can manage many of the factors which influence the level of its fuel and  
12           purchased power costs. These include: (1) the skill of the utility in negotiating its  
13           fuel and purchased power contracts; (2) the skill of the utility in taking advantage  
14           of purchases and sales in the economy market; (3) the skill and diligence of a  
15           utility in maintaining its generation facilities and in restoring efficient units to  
16           service after unexpected outages; (4) the skill of the utility in planning its  
17           maintenance outages; (5) the skill and success of the utility in hedging  
18           transactions for its fuel supplies; and (6) the management decisions regarding the  
19           type, size and timing of facilities added to the utility's generation portfolio.
- 20           2. It is important that an FAC have incentives for the utility to appropriately manage  
21           its operations and costs.
- 22           3. Incentives in an FAC are fully consistent with the legislation which enabled the  
23           adoption of an FAC, with the Commission rules implementing the FAC structure,  
24           and with this Commission's recent decision in the Aquila case.
- 25           4. It is not necessary to track through the FAC all of the costs that are reported in  
26           fuel or purchased power accounts. Only those prudently incurred costs which are  
27           meaningful in magnitude, vary with the level of kWh generated, are volatile and/or  
28           are difficult to predict or control should be tracked through an FAC.
- 29           5. Limitations on the recovery of certain fuel and purchased power-related costs  
30           through an FAC is generally consistent with industry practice.
- 31           6. MEB Schedule 1-Surrebuttal provides an alternative FAC sharing proposal that  
32           responds to the comments of Commission Staff witness Lena Mantle concerning

1 the range of fuel cost changes from the base number over which Empire would  
2 share in deviations in cost levels.

3 **Response to Empire**

4 **Q TO WHICH EMPIRE WITNESSES ARE YOU OFFERING SURREBUTTAL?**

5 A My surrebuttal testimony responds to the "policy" testimony of Dr. Overcast, and to  
6 some of the more Empire-specific issues raised by Empire witness Scott Keith.

7 **Q DOES DR. OVERCAST SUPPORT THE INCLUSION OF A SHARING MECHANISM**  
8 **IN A FUEL ADJUSTMENT CLAUSE (FAC)?**

9 A No. Dr. Overcast does not support such a provision. In fact, in Dr. Overcast's view,  
10 each and every expense that is prudently incurred *should be guaranteed recovery*  
11 through the rate setting process. In regard to the sharing mechanism he states the  
12 following at line 17 on page 6 of his rebuttal testimony:

13 Since I believe that 100% recovery of prudently incurred fuel costs  
14 represents the correct basis for a reasonable FAC that provides a  
15 sufficient opportunity to earn a reasonable return, there is no need for  
16 designing a fuel cost system that randomly rewards or penalizes the  
17 utility based on fuel prices, weather, purchased power prices and other  
18 variables beyond the reasonable control of the utility.

19 **Q DO YOU SHARE DR. OVERCAST'S VIEW?**

20 A No. I disagree with his position.

21 **Q PLEASE ELABORATE.**

22 A First, it is important to recognize that there are many factors other than the ones  
23 mentioned by Dr. Overcast that influence the level of fuel and purchased power costs.  
24 Some of these are: (1) the skill of the utility in negotiating its fuel and purchased  
25 power contracts; (2) the skill of the utility in taking advantage of purchases and sales

1 in the economy market; (3) the skill and diligence of a utility in maintaining its  
2 generation facilities and in restoring efficient units to service after unexpected  
3 outages; (4) the skill of the utility in planning its maintenance outages; (5) the skill and  
4 success of the utility in hedging transactions for its fuel supplies; and (6) the  
5 management decisions regarding the type, size and timing of facilities added to the  
6 utility's generation portfolio. Clearly there are many factors besides those which Dr.  
7 Overcast mentions that influence the ultimate level of fuel costs incurred by a utility.  
8 To simply suggest that a sharing mechanism "...randomly rewards or penalizes..." is  
9 an incomplete and incorrect statement. Certainly, there are factors beyond the  
10 control of the utility, but there are many factors that the utility can manage. It is these  
11 factors that are targeted by the incentive considerations of my proposed fuel  
12 adjustment clause.

13 Second, I would note also that the sharing mechanism which I have proposed  
14 has a specific dollar limit on the amount of potential cost savings that could be  
15 retained by the utility, as well as a cap on the cost increase above base levels that  
16 the utility would be required to absorb. This cap on the maximum cost increase  
17 above base levels limits the impact on the utility without destroying the incentives for  
18 the utility to appropriately manage its costs.

19 Third, Dr. Overcast's assertion represents a continued effort by Empire to gain  
20 guaranteed recovery for its expense items while still allowing for the possibility of  
21 inflated returns because of uncapped revenues and reductions in the level of other  
22 costs that are recovered through base rates. Dr. Overcast's attempt to flow more  
23 expense items through the fuel adjustment clause will lower Empire's risk profile and  
24 increase the possibility that it will overearn.

1 Q DO YOU BELIEVE THAT YOUR INCENTIVE MECHANISM PROVIDES THE  
2 UTILITY WITH A REASONABLE OPPORTUNITY TO EARN A FAIR RATE OF  
3 RETURN?

4 A Yes, I do. Under my proposed mechanism, Empire can retain part of the benefits of  
5 cost reduction, and its ROE impact is limited.

6 Q DO THE COMMISSION'S FUEL ADJUSTMENT RULES PROVIDE FOR THE  
7 INCLUSION OF INCENTIVES IN FACs?

8 A Yes. The rules pertaining to the FAC are contained in 4 CSR 240 - 20.090. In the  
9 commentary accompanying the September 21, 2006 "Final Order and Rulemaking"  
10 issued by the Commission when adopting FAC rules, the Commission made the  
11 following statement in responding to issues raised by various parties:

12 The Commission finds that a clear statement that it may apportion fuel  
13 costs between base rates and a RAM is appropriate, as more fully set  
14 forth below. The Commission will not establish a fixed level of  
15 apportionment, as the inherent differences in the operation of the  
16 utilities, particularly the difference in their fuel mixes for base load  
17 generation would render a fixed amount unreasonable in some  
18 instances. The Commission believes such authority is inherently in  
19 SB179, but will add the language to clarify that it has such authority.

20 Consistent with those comments, the Commission included the following  
21 language in its 4 CSR 240 - 20.090 (11):

22 Incentive Mechanism or Performance Based Program. During a  
23 general rate proceeding in which an electric utility has proposed  
24 establishment or modification of a RAM, or in which a RAM may be  
25 allowed to continue in effect, any party may propose for the  
26 commission's consideration incentive mechanisms or performance  
27 based programs to improve the efficiency and cost effectiveness of the  
28 electric utility's fuel and purchased power procurement activities.

29 (A) The incentive mechanisms or performance based programs  
30 may or may not include some or all of the components of fuel and  
31 purchased power costs, designed to provide the electric utility  
32 with incentives to improve the efficiency and cost  
33 effectiveness of its fuel and purchased power procurement  
34 activities. [Emphasis added.]

1    **Q     SUBSEQUENT TO THE ADOPTION OF THESE RULES, HAS THE COMMISSION**  
2           **ADDRESSED THIS ISSUE FROM A POLICY PERSPECTIVE IN A UTILITY RATE**  
3           **PROCEEDING?**

4    A     Yes. In the recent Aquila Networks-MPS and Aquila Networks-L&P case, MPSC  
5           Case No. ER-2007-0004, the Commission stated as follows at page 54 of its May 17,  
6           2007 Report and Order:

7                   The Commission also finds after-the-fact prudence reviews alone are  
8                   insufficient to assure Aquila will continue to take reasonable steps to  
9                   keep its fuel and purchased power costs down, and the easiest way to  
10                  ensure a utility retains the incentive to keep fuel and purchased power  
11                  costs down is to not allow a 100% pass through of those costs.

12                  Thus, it is abundantly clear that inclusion of incentive mechanisms in FACs  
13                  not only is consistent with Missouri rules, but is, in concept, consistent with recent  
14                  Commission findings.

15   **Q     DOES DR. OVERCAST'S POSITION SEEM TO BE AT ODDS WITH OTHER**  
16           **EMPIRE WITNESSES IN THIS REGARD?**

17   A     Yes. Empire has proposed a sharing mechanism within its proposed fuel adjustment  
18           clause in which a percentage of the costs of deviations from the base level are  
19           retained by Empire. In principle, this approach is the same approach that both Staff  
20           and I have recommended, although the specific sharing percentages and structure of  
21           the incentive mechanism are different. Nevertheless, the basic concepts are the  
22           same, and it would seem that Dr. Overcast's rebuttal is, at least in principle, equally  
23           directed to his client's position.



1    **Q    APPARENTLY IN RESPONSE TO YOUR PROPOSAL THAT CERTAIN COST**  
2           **ITEMS NOT BE PASSED THROUGH THE FAC, DR. OVERCAST STATES AT**  
3           **PAGE 3 OF HIS REBUTTAL TESTIMONY THAT WHETHER COSTS ARE FIXED**  
4           **OR VARIABLE HAS NO BEARING ON WHETHER OR NOT THESE COSTS ARE**  
5           **PRUDENT AND SHOULD BE RECOVERED. DO YOU AGREE?**

6    A    Yes. I agree that whether costs are fixed or variable, demand or commodity, they can  
7           be prudent or imprudent. Where we disagree is about his assertion that changes in  
8           prudent costs necessarily must be tracked through the FAC. The fact that a cost is  
9           prudent and is included in a account that is related to fuel has no bearing on whether  
10          it is appropriate to automatically track changes in the level of costs through the FAC.

11   **Q    WHAT ARE THE CHARACTERISTICS OF COSTS THAT SHOULD BE FLOWED**  
12          **THROUGH THE FAC?**

13   A    In addition to the requirement that the cost be prudent, costs flowed through the FAC  
14          should generally be only those that are variable with the level of kWh generated, are  
15          volatile and/or difficult to predict or control. In addition, the magnitude of the costs  
16          should be significant to the utility.

17   **Q    WHICH OF THE COSTS THAT YOU PROPOSE TO EXCLUDE FROM TRACKING**  
18          **THROUGH THE FAC DO EMPIRE WITNESSES BELIEVE SHOULD BE TRACKED**  
19          **THROUGH THE FAC?**

20   A    Empire, through Mr. Keith and/or Dr. Overcast, complains about my proposal to  
21          exclude: (1) unit train costs' (2) fuel handling costs; (3) natural gas transportation  
22          demand charges; and (4) emission allowance costs from the FAC.

1    **Q     WHY IS IT APPROPRIATE TO EXCLUDE THESE COSTS?**

2    A     Emission allowance costs should be excluded because they are  
3           environmental-related costs, and the Commission has recently adopted rules dealing  
4           with the recovery of these types of costs for a utility that has an environmental cost  
5           recovery mechanism (ECRM) in place. Empire is free to request consideration of an  
6           ECRM in a future case. This will not preclude Empire from cost recovery until then,  
7           because it has been Empire's testimony that it does not expect to incur any SO<sub>2</sub> costs  
8           for several years.

9    **Q     PLEASE ADDRESS THE OTHER COSTS.**

10   A     The other costs are basically fixed or demand-related costs, costs that are not  
11           volatile, and costs that are controllable by the utility.

12                 For example, fuel handling costs are primarily labor, and labor costs are  
13           neither volatile nor outside the control of the utility. There is no reason to distinguish  
14           labor costs associated with fuel handling from any other labor costs that are incurred.  
15           Transportation demand charges and unit train costs are fixed costs. They do not vary  
16           directly with the quantity of kWh generated, but tend to be more fixed and stable, and  
17           thus should not require pass through.

18   **Q     WHAT WAS SAID ABOUT THESE TYPES OF COSTS IN THE AQUILA CASE**  
19           **WHICH YOU PREVIOUSLY REFERENCED?**

20   A     This is addressed at pages 42 and 43 of the Aquila case May 17, 2007 Report and  
21           Order.

22                 **i. What costs should be recoverable through the fuel adjustment**  
23                 **clause?**

24                 *Aquila originally proposed to recover through its fuel adjustment clause*  
25                 *all costs recorded in Federal Energy Regulatory Commission ("FERC")*  
26                 *Accounts 501, 509, 547, and 555. In addition to the actual costs of*

1 fuel and purchased power, these accounts also included related costs,  
2 such as unit train lease, depreciation, and maintenance costs;  
3 freeze/dust suppression costs; fuel handling costs; costs associated  
4 with fly-ash removal; gas reservation charges; and demand charges  
5 for purchased power contracts with terms in excess of one year. After  
6 considering objections of various parties, Aquila has agreed these  
7 costs will be recovered exclusively through base rates. Aquila  
8 continues to believe, however, that hedging costs and demand  
9 charges related to purchased power contracts with terms of one year  
10 or less should be recovered through the fuel adjustment clause.

11 Staff witness Cary Featherstone argues only variable fuel and  
12 purchased power costs, including variable transportation costs, should  
13 be included in a fuel adjustment clause. Specifically, Mr. Featherstone  
14 contends it is inappropriate to include demand charges for any  
15 capacity contracts, regardless of their duration, for two reasons. First,  
16 Mr. Featherstone points to the fact that demand charges are fixed  
17 costs to reserve capacity, and as such are more like plant investment  
18 cost than fuel or purchased power cost. Second, Staff opposes  
19 Aquila's use of short-term contracts to meet its growing capacity  
20 needs. Staff argues that allowing Aquila to pass on this type of cost  
21 would allow Aquila to meet its growing load requirements through  
22 short-term capacity, thus creating another disincentive for it to build  
23 generating units and placing all the risk of future fuel and purchased  
24 power cost increases on its customers. Mr. Featherstone's analysis is  
25 persuasive.

26 **Findings of Fact:** The Commission finds a reasonable fuel  
27 adjustment clause should be straightforward and simple to administer,  
28 retain some incentive for company efficiency, and be readily auditable  
29 and verifiable through expedited regulatory review. The Commission  
30 can find no probative evidence in the record to support a finding that  
31 hedging costs or demand charges related to purchased power  
32 contracts with terms of one year or less should be recovered in a  
33 different manner than purchased power contracts with longer terms.  
34 The Commission agrees with Staff, and finds that demand charges are  
35 fixed costs to reserve capacity, and as such are more like plant  
36 investment cost than fuel or purchased power cost. This is the case  
37 irrespective of the length of the purchased power contract. Further, if  
38 demand charges on short term contracts are allowed to flow through  
39 the fuel adjustment clause, Aquila would be encouraged to forgo  
40 entering long term contracts in favor of short term contracts.

41 **Conclusions of Law:** The Commission concludes it would be  
42 improper to allow Aquila to flow hedging costs or demand costs  
43 associated with any purchased power contract through its fuel  
44 adjustment clause. The Commission concludes Aquila will only be  
45 allowed to flow variable fuel and purchased power costs, including  
46 variable transportation costs, through its fuel adjustment clause.  
47 [Footnotes omitted.]

1                   It should also be noted, however, that in a Clarifying Order issued May 21,  
2                   2007, the Commission did provide that hedging costs could be passed through the  
3                   FAC.

4    **Q       DIDN'T THE AQUILA ORDER ALSO PROVIDE THAT SO<sub>2</sub> ALLOWANCE COSTS**  
5           **COULD BE INCLUDED IN THE FAC?**

6    A       Yes, it did. However, at the time of the Aquila Order, the Commission had not  
7           published any rules concerning the ECRM and that Aquila was already incurring SO<sub>2</sub>  
8           costs. Thus, the circumstances in the Aquila case are markedly different from the  
9           circumstances faced by Empire.

10   **Q       IS IT CONVENTIONAL TO EXCLUDE FIXED COSTS FROM FAC'S?**

11   A       Yes, it is. Predominantly, FACs are designed to recover changes in variable costs;  
12           that is, costs that vary on a kWh basis. In addition to the reasons I have previously  
13           mentioned, costs passed through the fuel clause are on a per kWh basis (adjusted for  
14           losses) and inclusion of demand-related costs in an FAC would burden high load  
15           factor customers because they would be required to pay a disproportionately large  
16           share of such costs. It is preferable, and more typical, to include these costs in base  
17           rates.

18   **Q       CAN YOU PROVIDE ANY EXAMPLES OF OTHER COMMISSION LIMITING THE**  
19           **RECOVERY OF CHARGES THROUGH THE FAC?**

20   A       Yes. No doubt there are many orders, rules and fuel clauses that address this  
21           subject or implement such provisions. One order that I believe is reasonably typical is  
22           the General Order of the Louisiana Public Service Commission styled in Re:

1 Development of Standards Governing the Treatment and Allocation of Fuel Costs by  
2 Electric Utility Companies, decided October 1, 1997.

3 At pages 8 and 9 of the Order, the Commission stated that the following costs  
4 would not be included in the FAC:

5 D. Excludable Costs.

- 6 • Nonfuel operation and maintenance costs such as accounting and  
7 other administrative costs.
- 8 • Procurement costs such as salaries, wages, and overheads for  
9 personnel in fuel purchasing department.
- 10 • Fuel handling and testing costs such as personnel,  
11 equipment, and other overhead costs related to coal inventory  
12 at plant site.
- 13 • Cost (net of sales revenues) of byproduct disposal such as hauling  
14 costs for bottom ash disposal.
- 15 • Property taxes including ad valorem taxes such as property taxes  
16 on railroad cars and other equipment owned or leased by utility.
- 17 • Depreciation and amortization costs (other than nuclear fuel) such  
18 as depreciation of railroad cars and other equipment owned by  
19 utility.
- 20 • Lease expense (other than nuclear fuel) such as lease expense for  
21 railroad cars and other equipment.
- 22 • Interest expense or carrying charges (other than Commission  
23 authorized return on under and over recoveries and interest on  
24 leased nuclear fuel) on capital investments and inventories such as  
25 interest due on capital investment in gas storage facility.
- 26 • Purchased power demand, capacity, or facilities charges whether  
27 explicitly identified or subsumed within an energy charge,  
28 regardless of whether affiliated or nonaffiliated parties such as  
29 purchased power demand charge based upon Mw commitment of  
30 supplier.
- 31 • Cost of and revenues from transmission for affiliated parties such  
32 as payment for transmission services under FERC open access  
33 tariff to affiliated company for pool energy purchases.
- 34 • Firm sales revenue for demands, capacity or facilities whether  
35 explicitly identified or subsumed within an energy charge,  
36 regardless of whether made to affiliated or nonaffiliated parties  
37 such as revenues received from purchaser for demand charge  
38 based upon Mw commitment from utility.

1 Q DID MR. KEITH PROVIDE ANY OTHER REASONS WHY HE DISAGREED WITH  
2 YOUR EXCLUSIONS?

3 A Yes. On page 7 of his testimony he basically raised an issue of administrative  
4 complication, complaining that having to separate these costs would be difficult.

5 Q DO YOU BELIEVE MR. KEITH'S OBJECTIONS OF ADMINISTRATIVE  
6 DIFFICULTY ARE VALID?

7 A No, I do not. I find that the points raised by Mr. Keith are extremely minor. I do not  
8 believe that the exclusions which I have proposed, which Aquila apparently is able to  
9 handle, should pose difficulties for Empire.

10 Q AT PAGES 6 THROUGH 8 OF HIS TESTIMONY, AT VARIOUS POINTS, DR.  
11 OVERCAST ARGUES THAT BECAUSE IT IS EXPECTED THAT FUEL COSTS  
12 WILL RISE IN THE NEAR TERM, THE SHARING MECHANISM IN THE FAC THAT  
13 YOU HAVE PROPOSED IS NOT SYMMETRICAL. DO YOU AGREE WITH DR.  
14 OVERCAST?

15 A No, I do not. Dr. Overcast has chosen to focus on a single element of the cost  
16 equation – namely the unit cost of fuel. He has ignored several things. First, it is not  
17 only the cost of fuel that determines the level of fuel costs. As previously mentioned,  
18 there are many other factors that determine the overall level of fuel and purchased  
19 power costs that the utility incurs. He has not addressed any of these.

20 In addition, he has taken a short-term view in assuming that the direction of  
21 fuel cost changes is continuously upward. This has not been the case in the past,  
22 and it likely will not be the case in the future. In the recent past, we have seen both  
23 increases and decreases in the level of both coal and natural gas costs. Thus, it is

1 entirely possible that during the course of the existence of the FAC there will be some  
2 decrease in fuel costs.

3 Furthermore, my proposed *sharing mechanism* allows the utility to retain the  
4 benefits of decreases in the average cost of fuel and purchased power, as well as  
5 requires it to participate in absorbing costs associated with increases in the cost of  
6 fuel and purchased power, the clause which I have proposed is symmetrical.

7 Finally, to the extent that Dr. Overcast's criticism that my proposal is  
8 asymmetrical, that criticism is equally applicable to the fuel adjustment clause  
9 proposal advanced by Empire.

10 **Response to Commission Staff**

11 **Q HAVE YOU REVIEWED THE REBUTTAL TESTIMONY OF STAFF WITNESS LENA**  
12 **MANTLE WITH RESPECT TO YOUR FAC TESTIMONY?**

13 **A Yes.**

14 **Q AT PAGE 8 OF HER TESTIMONY, LINE 8, SHE INDICATES THAT UNDER YOUR**  
15 **PROPOSAL AFTER COSTS WOULD INCREASE MORE THAN 11%, EMPIRE**  
16 **RECOVERS "...ALL COSTS FROM THE RATEPAYERS." IS THIS AN**  
17 **ACCURATE STATEMENT?**

18 **A** I believe I understand what Ms. Mantle is saying. However, to be clear, I think a more  
19 precise statement would be that Empire recovers "...all additional costs from the  
20 ratepayers, above that level." In other words, Empire cannot go back and recapture  
21 all cost increases. It must absorb the \$3 million of increases up to that point.

1    **Q     MS. MANTLE GOES ON TO SAY THAT ABOVE THAT LEVEL OR CAP THAT**  
2           **EMPIRE HAS NO INCENTIVE TO MANAGE ITS COSTS SINCE ALL ADDITIONAL**  
3           **COSTS WOULD BE PASSED ON TO THE RATEPAYERS. DO YOU AGREE?**

4    A     I understand Ms. Mantle's point. In my proposed FAC with the cap on the absorption  
5           of costs, and the other features, she is correct that there is no additional incentive  
6           once the cap is hit.

7    **Q     HAVE YOU PREPARED AN ALTERNATIVE SHARING STRUCTURE THAT**  
8           **ADDRESSES MS. MANTLE'S CONCERNS?**

9    A     Yes. MEB Schedule 1-Surrebuttal provides an alternative form of sharing mechanism  
10          which is designed to provide an incentive to Empire over a wider range of fuel cost  
11          deviations from the base. This alternative sharing mechanism maintains the same \$3  
12          million cap on absorptions by Empire of increases in cost, and retention by Empire of  
13          the benefit of decreases in costs. It differs in that I have eliminated the dead band  
14          which previously required Empire to absorb the first  $\pm$  \$1.2 million deviation from the  
15          base. By taking those dead band dollars and spreading them out over a broader  
16          range of cost changes, an incentive to control costs can be maintained over a much  
17          broader range.

18   **Q     PLEASE ELABORATE ON THIS ALTERNATIVE.**

19   A     As shown on MEB Schedule 1-Surrebuttal, there are two sharing bands. For the first  
20          \$20 million of deviations in fuel costs from the base (representing about a 16%  
21          deviation in fuel costs from the base) the stockholder retention percentage is 5% –  
22          the same as proposed by Empire. However, beyond the initial \$20 million deviation,  
23          additional deviations are shared 90% to customers and 10% to stockholders. The \$3  
24          million retention cap is hit at  $\pm$  \$40 million (31% from the base), rather than at  $\pm$  \$13.2



1 million (11%) from the base in the proposal contained in my March 7, 2008 direct  
2 testimony.

3 While other structures could be devised, I believe this structure addresses Ms.  
4 Mantle's concern, while still maintaining a cap on Empire's financial exposure.

5 **Q DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

6 **A** Yes, it does.

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# The Empire District Electric Company

## Alternative Sharing Structure

(\$ Millions)

Change in Net Cost Level from Base *	Amount in Band	Sharing Percent		Maximum Sharing Dollars in Band		Cumulative Sharing Dollars		Cumulative Impact on Return on Equity
		Customer	Stock- holder	Customer	Stock- holder	Customer	Stock- holder	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
> \$40.0 }		100%	0%	All	None	\$37.0 + <sup>1</sup>	\$3.0	50 Basis Points
\$40.0 }	\$10.0	90%	10%	\$9.0	\$1.0	\$37.0	\$3.0	50 Basis Points
\$30.0 }	\$10.0	90%	10%	\$9.0	\$1.0	\$28.0	\$2.0	33 Basis Points
\$20.0 }	\$20.0	95%	5%	\$19.0	\$1.0	\$19.0	\$1.0	17 Basis Points
B A S E }	(\$20.0)	95%	5%	(\$19.0)	(\$1.0)	(\$19.0)	(\$1.0)	17 Basis Points
(\$20.0) }	(\$10.0)	90%	10%	(\$9.0)	(\$1.0)	(\$28.0)	(\$2.0)	33 Basis Points
(\$30.0) }	(\$10.0)	90%	10%	(\$9.0)	(\$1.0)	(\$37.0)	(\$3.0)	50 Basis Points
(\$40.0) }		100%	0%	All	None	(\$37.0) + <sup>2</sup>	(\$3.0)	50 Basis Points

### Notes:

<sup>1</sup> Customers are responsible for \$37.0 million plus any additional costs above \$40.0 million.

<sup>2</sup> Customers receive \$37.0 million plus any additional savings above \$40.0 million.

\*Fuel and purchased power costs minus off-system sales revenue

## The Empire District Electric Company

### Impact on Company Return on Equity From Change in Recovery of Total Fuel Costs (Based on Alternative Sharing Structure)

Line	Description	Company Requested Missouri Jurisdictional (1)	Scenario #1 (2)	Scenario #2 (3)	Scenario #3 (4)
1	Total Missouri-Retail Fuel & PP <sup>1</sup>		\$ 142,191,310	\$ 142,191,310	\$ 142,191,310
2	Less: Purchased Power Demand <sup>1</sup>		\$ 13,384,576	\$ 13,384,576	\$ 13,384,576
3	Cost of Energy Requested (L1 - L2)		\$ 128,806,734	\$ 128,806,734	\$ 128,806,734
4	Amount Change in Fuel & PP <sup>2</sup>		\$ 20,000,000	\$ 30,000,000	\$ 40,000,000
5	Company Cumulative Responsibility <sup>2</sup>		\$ 1,000,000	\$ 2,000,000	\$ 3,000,000
6	Income Tax Gross Up Factor <sup>3</sup>		1.62308	1.62308	1.62308
7	Change in Company's Operating Income (L5 / L6)		\$ 616,113	\$ 1,232,225	\$ 1,848,338
8	Operating Income After Fuel & PP Impact (\$68,622,744 less adjustment in L7)	\$ 68,622,744 <sup>4</sup>	\$ 68,006,631	\$ 67,390,519	\$ 66,774,406
9	Jurisdictional Rate Base	\$ 733,148,974 <sup>4</sup>	\$ 733,148,974	\$ 733,148,974	\$ 733,148,974
10	Rate of Return (L8 / L9)	9.36% <sup>4</sup>	9.28%	9.19%	9.11%
11	Calculated Return on Equity	11.60% <sup>5</sup>	11.43%	11.27%	11.10%
12	Basis Point Reduction		17	33	50

Source:

<sup>1</sup> Schedule WSK-2

<sup>2</sup> MEB Schedule 2, Page 1 of 2

<sup>3</sup> Direct Testimony of W. Scott Keith, Section G, Schedule 3, Page 1 of 3

<sup>4</sup> Direct Testimony of W. Scott Keith, Section D, Schedule 1

<sup>5</sup> Direct Testimony of W. Scott Keith, Section H, Schedule 1 (Confidential)