

Exhibit No.
Issue: Overview
Witness: William L. Gipson
Type of Exhibit: Direct Testimony
Sponsoring Party: Empire District
Case No: GO-2006-0205
Date Testimony Prepared: November 2005

Before the Missouri Public Service Commission

Direct Testimony

Of

William L. Gipson

November 2005

FILED

APR 12 2006

Missouri Public
Service Commission

Exhibit No. 3
Case No(s) GO-2006-0205
Date 3/30/06 Rptr MSV

DIRECT TESTIMONY
OF
WILLIAM L. GIPSON
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. GO-2006-0205

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

2 A. William L. Gipson, 602 Joplin Street, Joplin, Missouri 64802.

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

4 A. The Empire District Electric Company ("Empire" or "Company") is my employer. I am a
5 Director and the President and Chief Executive Officer.

6 **Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND.**

7 A. I hold a Bachelor of Science Degree in Business Management Technology and an Associate
8 Degree in Computer Science from Missouri Southern State University in Joplin, Missouri.

9 **Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.**

10 A. Prior to joining Empire I worked for an international furniture manufacturing company and
11 a regional bank. I joined Empire as a Computer Programmer in 1981. I have held positions
12 in Information Services, Economic Development and Operations. My employment with
13 Empire has been continuous since 1981.

14 **Q. HAVE YOU PREVIOUSLY PRESENTED TESTIMONY BEFORE THIS OR ANY
15 OTHER REGULATORY BODY?**

16 A. Yes, I have presented testimony before the Missouri Public Service Commission ("MPSC"
17 or "Commission"), the Kansas Corporation Commission, the Oklahoma Corporation
18 Commission, and the Arkansas Public Service Commission.

19 **Q. MR. GIPSON, WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

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1 A. The purpose of my testimony is to provide an overview of the Company, the rationale
2 supporting the transaction, and the reasons the transaction will not be detrimental to the
3 public interest. In addition, I will introduce the other individuals presenting testimony in
4 support of the transaction.

5 **Q. PLEASE DESCRIBE EMPIRE.**

6 A. Empire is a Kansas corporation with its principal office and place of business at 602 Joplin
7 Street, Joplin, Missouri 64802. Empire is engaged in the business of providing electrical
8 utility services in Missouri, Kansas, Arkansas and Oklahoma; and water utility services in
9 Missouri. Our experience in the utility industry dates back to 1909 when we were
10 incorporated.

11 **Q. WILL YOU PLEASE DESCRIBE THE AREA SERVED BY EMPIRE AND GIVE A
12 BRIEF DESCRIPTION OF THE CUSTOMERS SERVED?**

13 A. Empire provides electric service in an area of approximately 10,000 square miles in the
14 southwest corner of Missouri and the adjacent corners of the states of Kansas, Oklahoma,
15 and Arkansas. Empire's operations are regulated by the utility regulatory commissions of
16 these four states as well as the Federal Energy Regulatory Commission ("FERC"). The area
17 embraces 121 incorporated communities in 20 counties in the four-state area.

18 The area economy is diversified. The service territory features small to medium
19 manufacturing operations, medical, agricultural, entertainment, tourism, and retail interests
20 all contributing to average or above-average customer growth over the last several years.

21 At the end of 2004, Empire served 133,603 residential customers, 23,536 commercial
22 customers, 363 industrial customers, 1,796 public authority customers, and four wholesale
23 customers in the four-state area in which it operates. Missouri is by far our largest operating

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1 area with 117,015 residential customers, 20,742 commercial customers, 291 industrial
2 customers, 1,447 public authority customers and 3 wholesale customers at the end of 2004.
3 Most of the communities in the four-state service area are small, with only 29 being in
4 excess of 1,500 population. Only 10 communities have a population in excess of 5,000, and
5 the largest city is Joplin, Missouri, with a population of approximately 45,500.

6 In addition to electric service, Empire also provides regulated water service to
7 approximately 4,500 customers in the Missouri communities of Aurora, Marionville, and
8 Verona.

9 **Q. PLEASE DESCRIBE THE TRANSACTION.**

10 A. Empire plans to purchase the Missouri natural gas properties ("the Business") of Aquila, Inc
11 ("Aquila"). There are approximately 48,500 customers in total, of whom 42,700 are
12 residential, 5,600 are commercial/industrial, and over 200 are transportation customers.
13 These customers reside in 44 Missouri communities served with 93 miles of transmission
14 and 1,181 miles of distribution main. Aquila has operated the system as three distinct
15 service areas. These areas are designated as MPS-Southern, MPS-Northern and L&P. The
16 L&P designation refers to the natural gas customers formerly served by St. Joe Light &
17 Power. Among the communities taking natural gas service from the Business are Sedalia,
18 Nevada and Marshall. Aquila made the decision to divest of the Business in March of 2005
19 and solicited bids from interested buyers. The bidding process used by Aquila involved the
20 submission of an initial bid by interested parties. After reviewing the initial bids for the
21 Business, Aquila notified the initial bidders if they had been selected or short-listed for
22 additional discovery, negotiations and a final bid for the property. Empire submitted an
23 initial bid on the property, was successful in making it to the second round and ultimately

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1 signed an Asset Purchase Agreement (“APA”) with Aquila on September 21, 2005 whereby
2 Empire would acquire the assets and the related gas distribution business from Aquila. The
3 reasons behind Aquila’s decision to sell the business are discussed in the direct testimony of
4 Aquila witness Ivan Vancas. In addition, Aquila witness Thomas Fleener discusses the
5 manner in which Aquila went about the sale process and certain specific provisions
6 contained within the APA. Empire witness Ron Gatz will discuss the transaction process
7 and the integration of the Business in greater detail in his direct testimony. In addition,
8 Empire will present direct testimony from Don Schisler of Towers Perrin concerning our
9 request for specific accounting treatment related to the Aquila pension benefit costs and
10 Aquila gas employees and retirees postretirement welfare benefit costs.

11 **Q. WHAT IS EMPIRE PAYING FOR THE BUSINESS?**

12 A. This acquisition is valued at approximately \$84 million, plus adjusted working capital at the
13 time of closing. This price includes approximately 1,274 miles of transmission and
14 distribution mains, 48,500 customers as well as the associated meters, regulators, service
15 trucks and equipment necessary to operate and maintain the system

16 **Q. WHY DID EMPIRE PURSUE THIS TRANSACTION?**

17 A. We see this as an excellent opportunity to grow our utility business. The transaction fits
18 with one of our key business strategies of actively managing our weather-related risks and it
19 is clearly in our core business, a regulated utility delivering energy and energy related
20 services. It will allow us to diversify our weather risk, helping to balance our current
21 summer air conditioning peak with a natural gas winter heating peak. This is a Missouri
22 utility property that is in close proximity to our current service territory and is under the
23 jurisdiction of the MPSC by whom I believe we are respected as a solid utility operator.

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1 Finally, the Business will enable Empire to capture the benefits associated with the increase
2 in scale and scope of its operations for its shareholders and customers, both electric and gas.

3 **Q. DOES THIS TRANSACTION REQUIRE APPROVAL BY ANY OTHER STATE**
4 **REGULATORY BODIES?**

5 A. No.

6 **Q. WILL THIS TRANSACTION BE DETRIMENTAL TO THE PUBLIC INTEREST?**

7 A. No.

8 **Q. PLEASE EXPLAIN.**

9 A. The transaction will have no adverse affect on the customers of Aquila with respect to the
10 rates charged for gas service or the quality of service rendered.

11 As outlined in the application, Empire proposes to maintain the existing gas rates and
12 the related purchase gas adjustment ("PGA"). The Commission will retain jurisdiction over
13 the Business.

14 The Missouri gas customers of the Business will not see a reduction in the level of
15 service or reliability of their gas service. The day-to-day operations of the system will
16 continue to be conducted as they have in the past. We will offer jobs to all 50 plus Aquila
17 employees currently involved in field operations and welcome them to the Empire family of
18 employees. These employees will continue to operate the gas system and provide service to
19 customers. As I mentioned earlier, and as the Commission knows, Empire has a long
20 history of offering quality utility service in Missouri, and Empire and Aquila are committed
21 to a transfer of the operations that will result in as little customer disruption as possible.

22 **Q. WHAT BENEFITS WILL EMPIRE'S ACQUISITION OF THE BUSINESS BRING?**

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1 A. Empire's acquisition of the Business will bring a number of benefits to not only the gas
2 operations, but to Empire's existing electric operations. As I mentioned earlier, this
3 transaction allows Empire to mitigate some of its weather related risk, one of its key
4 business strategies. In addition, after acquisition the gas operations will have the advantage
5 of the Empire's investment grade credit rating. This should provide several benefits,
6 including greater access to capital, both permanent and operating. Empire's credit rating
7 should enable us to finance the operations at attractive rates, and in terms of operating
8 capital, Empire's financial profile should enable it to deal with various suppliers, including
9 those that supply natural gas, a key input for a gas system. I believe the Business will also
10 benefit from Empire's utility focus. Empire is focused on providing its customers with
11 reliable and cost effective utility service with a high level of customer service. I also believe
12 that Empire's economic development efforts will enable the communities on the system to
13 attract new businesses to their communities. The communities served by the Business will
14 have access to our economic development department, which will provide assistance to
15 them and their efforts to attract new business.

16 **Q. HOW WILL THE TRANSACTION BENEFIT EMPIRE'S ELECTRIC**
17 **OPERATIONS?**

18 A. The primary benefit will be associated with the increase in the scale and scope of Empire's
19 utility operations. This change will spread fixed overhead costs over a larger customer base
20 and ultimately lead to a lowering of average overhead costs for our electric customers. As I
21 mentioned earlier, the transaction will offset to some degree the weather risk associated with
22 our electric summer peak.

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1 **Q. IS THERE A PREMIUM ASSOCIATED WITH THIS TRANSACTION?**

2 A. Yes.

3 **Q. IS EMPIRE REQUESTING ANY RECOVERY OF PREMIUM AS PART OF**
4 **ACQUISITION APPROVAL?**

5 A. No. Empire is not seeking any recovery of premium in this application.

6 **Q. DOES THIS ACQUISITION HAVE ANY ADVERSE IMPACT UPON THE RECENT**
7 **IATAN 2 REGULATORY PLAN APPROVED BY THE COMMISSION IN CASE**
8 **NO. EO-2005-0263?**

9 A. No. The gas property will be held and operated in a separate, wholly owned subsidiary and
10 will have no adverse impact upon Empire's electric resource planning or its Iatan 2
11 Regulatory Plan in general. In addition, there is no need for any modification in the existing
12 electric regulatory plan due to the acquisition at this point, as the Business will produce
13 immediate cash flow upon closing

14 **Q. HOW WILL EMPIRE FINANCE THIS TRANSACTION?**

15 A. The source of financing is dependent upon the financial market conditions near the closing
16 date. For example, Empire could close the transaction using existing credit lines or a short
17 term bridge financing commitment and replace this initial financing with long term debt and
18 equity offerings when market conditions make it appropriate to do so. On the other hand, if
19 financial market conditions dictate, the transaction could be financed with permanent
20 financial instruments from the outset.

21 **Q. PLEASE DESCRIBE EMPIRE'S OVERALL FINANCIAL CONDITION.**

22 A. Empire's balance sheet is strong, with a debt to equity ratio of 52 to 48 percent at December
23 31, 2004. In addition, Empire is rated investment grade by Standard & Poor's ("S&P")

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1 BBB and Moody's Baa2. S&P, as it customarily does, has put Empire on CreditWatch-
2 negative due to the announced acquisition of the Business. S&P's overall rating for Empire
3 remained unchanged with Empire's recent shelf offering of \$400 million.

4 **Q. HOW DOES THE AQUILA GAS PROPERTY IN MISSOURI COMPARE TO THE**
5 **EXISTING EMPIRE ELECTRIC OPERATIONS IN TERMS OF INVESTMENT?**

6 A. As of September 30, 2005, Empire has over \$861 million invested net plant in its electric
7 operations. By comparison, the proposed investment in Missouri gas will be approximately
8 \$84 million. If the acquisition is approved by the Commission, the gas utility investment
9 would comprise less than 10 percent of Empire's overall investment in utility property.
10 After the acquisition, Empire would still be primarily an integrated electric utility.

11 **Q. IN GENERAL TERMS, WHAT REGULATORY APPROVALS ARE THE JOINT**
12 **APPLICANTS REQUESTING IN THE APPLICATION IN THIS CASE?**

13 A. Empire and Aquila are requesting the following approvals:

- 14 1. Authorize both Empire and Aquila to perform in accordance with the terms of APA
- 15 2. Authorize the sale, transfer and assignment of certain assets and liabilities as described
16 in the APA
- 17 3. Grant The Empire District Gas Company ("EDG") a certificate or certificates of
18 convenience and necessity authorizing EDG to provide natural gas service in the areas
19 presently served by Aquila
- 20 4. Authorize EDG to provide natural gas service in accordance with the rules,
21 regulations, rates and tariffs of Aquila, and authorize the adoption of Aquila's gas
22 tariffs by EDG.

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- 1 5. Authorize the adoption of Aquila's authorized depreciation rates on the acquired
2 property by EDG
- 3 6. Authorize the pledging of the assets of the Business by Empire in connection with the
4 financing of the transaction
- 5 7. Authorize Aquila to transfer to EDG and for EDG to acquire and record on its books
6 and records the current levels of certain assets and liabilities of Aquila related to the
7 business
- 8 8. Authorize EDG's use of the pension accounting method granted to Empire in its last
9 rate case
- 10 9. Authorize a continued use by EDG of the accounting methodology used by Aquila to
11 account for the cost associated with the Missouri gas employees and retirees
12 postretirement welfare benefit cost
- 13 10. Authorize the termination of Aquila's responsibilities as gas corporation in Missouri
14 upon the closing of the transaction
- 15 11. Authorize Aquila, Empire and EDG to enter into, execute and perform in accordance
16 with the terms of all other documents necessary to the performance of the transaction
- 17 12. Grant such other relief is necessary to complete the transaction

18 **Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY AT THIS**
19 **TIME?**

20 A. Yes, it does.

