Exhibit No.:
Issue: Various Rate Base and Income Statement Issues, True-up and Rate Design
Witness: W. Scott Keith
Type of Exhibit: Rebuttal Testimony
Sponsoring Party: Empire District Electric
Case No. ER-2012-0345
Date Testimony Prepared: January 2013

Before the Public Service Commission

of the State of Missouri

Rebuttal Testimony

of

W. Scott Keith

January 2013

EMPIRE
SERVICES YOU COUNT ON

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OF
W. SCOTT KEITH
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2012-0345

REBUTTAL TESTIMONY
OF
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INTRODUCTION

Q. STATE YOUR NAME AND ADDRESS PLEASE.

A. My name is W. Scott Keith and my business address is 602 South Joplin Avenue, Joplin, Missouri.

POSITION

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am presently employed by The Empire District Electric Company. ("Empire" or "the Company") as the Director of Planning and Regulatory. I have held this position since August 1, 2005.

Q. ARE YOU THE SAME W. SCOTT KEITH THAT EARLIER PREPARED AND FILED DIRECT TESTIMONY IN THIS RATE CASE BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION ("COMMISSION") ON BEHALF OF EMPIRE?

A. Yes.

PURPOSE

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My rebuttal testimony will discuss several issues related to the Empire rate base investment and statement of net operating income being proposed by the Missouri

Public Service Commission Staff ("Staff"), the Midwest Energy Users' Association ("MEUA") and the Office of the Public Counsel ("OPC") in this rate case. My rebuttal testimony will also respond to the Staff and MEUA recommendation that the Commission deny Empire's request to implement an SPP cost tracking mechanism. In addition, my rebuttal testimony will address the general rate design proposals made by the Staff, including those recommendations related to the Fuel Adjustment Clause ("FAC"). Specifically, I will address the following:

RATE BASE

- The Staff's exclusion from rate base of Empire's deferred tornado cost;
- The Staff's recommended adjustment to materials and supplies related to Empire's Edison Electric Institute ("EEI") membership dues; and
- The Staff's proposal on Iatan and Plum Point O&M tracker costs;

STATEMENT OF NET OPERATING INCOME

- The Staff adjustment to Empire's ongoing Renewable Energy Credit ("REC") revenue;
- The Staff's and OPC's adjustments to dues and donations related to Empire's membership in EEI;
- The Staff adjustment related to Empire's SPP transmission costs;
- The Staff's and MEUA's adjustments to Empire's outside service costs;
- The Staff's and OPC's adjustments to Empire's rate case costs;
- Staff's rate design proposals concerning customer charge and DSM cost recovery; and
- The Staff's and Missouri Department of Natural Resources ("MDNR") proposals

concerning revisions to Empire's Low Income Weatherization tariff.

In addition, I will describe specific items that need to be the subject of true-up.

Q. WHAT DOCUMENTS HAVE YOU REVIEWED IN THE PREPARATION OF YOUR REBUTTAL TESTIMONY?

A. I have reviewed the Staff Report Cost of Service Revenue Requirement, the Staff Rate Design and Class Cost-of-Service Report, and the following direct testimonies:

- Kimberly K. Bolin-Staff
- Michael S. Scheperle-Staff
- Stephen M. Rackers-MEUA
- Michael P. Gorman-MEUA
- Barbara A. Meisenheimer-OPC
- William Addo-OPC
- Keri Roth-OPC
- Adam Bickford-MDNR

Q. HAVE THE STAFF'S AND COMPANY'S POSITIONS ON REVENUE REQUIREMENT EVOLVED SINCE THE FILING OF THE STAFF'S DIRECT CASE?

A. Yes. Empire has updated its case through June 30, 2012, and has held discussions with Staff concerning errors in the Company's initial filing and Staff's initial filing. If those errors are corrected, several of the differences between the Company and Staff positions would be eliminated.

Q. PLEASE DESCRIBE THE ERRORS IN THE STAFF'S INITIAL FILING

THAT EMPIRE HAS DISCOVERED AT THE TIME THIS REBUTTAL TESTIMONY IS BEING FILED.

A. The following are a list of the errors and approximate revenue requirement values discovered in Empire's initial review of the Staff's direct case:

Description	Error	RR Value $000 Inc/(Decr) Staff Case
Accum. Regulatory Amortization	Jurisdictional Allocation	($.492)
Prepaid Pension Asset	Jurisdictional Allocation	($.416)
REC Revenue	Non-jurisdictional revenue included in Staff filing	$.917
SPP Transmission Revenue	Non-jurisdictional revenue included in Staff filing	$.245
Bad Debt Expense	Jurisdictional Allocation	$.398
Ice Storm Amortization	Jurisdictional Allocation	$.374
Dues & Donations	Jurisdictional Allocation	$.015
Employee Benefits	Capitalization Error	$.071
Outside Services	Jurisdictional Allocation	($.100)
Rate Case Expense	Non-jurisdictional costs included	($.547)
Insurance Expense	Capitalization Error	$.027
Advertising Expense	Jurisdictional Allocation	$.006
SLCC Non-ownership costs	Double counting of non-ownership costs	$3.027
Annualized Rate Change	Formula Error	$.097
Corp Franchise Tax	Omission of State Franchise Tax	$.465
Customer Advances	Allocation versus Direct Assign	($.094)
Customer Deposits	Allocation versus Direct Assign	($.036)
Customer Deposit Interest	Allocation versus Direct Assign	$.012

Q. DO REVENUE REQUIREMENT DIFFERENCES REMAIN BETWEEN EMPIRE AND THE STAFF AFTER THIS UPDATE AND CORRECTION PROCESS?

A. Yes, However, at the time of the preparation of my rebuttal testimony, I have not had an opportunity to review Staff's revised EMS run, so I do not know the impact of any Staff revisions for any of the above errors.

Q. IS EMPIRE OPPOSED TO THE ELIMINATION OF ICE STORM AMORTIZATION FROM THE MISSOURI RETAIL REVENUE REQUIREMENT THAT IS BEING PROPOSED BY STAFF, MEUA AND OPC?

A. No. The amortization of Missouri jurisdictional deferred ice storm costs will be complete in December of 2012, and it should be eliminated from Empire's ongoing Missouri jurisdictional revenue requirement.

<u>FUEL ADJUSTMENT MECHANISM</u>

Q. HAVE YOU REVIEWED THE FAC POSITION TAKEN BY THE STAFF IN THIS CASE?

A. Yes. I reviewed pages 134 through 146 of the Staff Report Cost of Service as well as the accounting schedules, pages 29 through 33 of the Staff's Rate Design and Class Cost of Service Report, the Staff's proposed versions of revised FAC tariff sheets, and Staff's calculation of a new FAC base cost to determine how the various adjustments to fuel and energy costs, off-systems sales, REC revenue, fuel transportation costs and transmission costs have been handled in the Staff's proposed FAC. In addition, I reviewed the Commission's recent order in Case No. ER-2012-0166, an Ameren Missouri rate case, to see how the Commission handled the cost associated with regional transmission organizations ("RTO"). In Ameren's case this involved MISO transmission cost recovery. In addition, in the Ameren case, the Staff proposed to increase Ameren's FAC sharing from 5/95 percent to 15/85 percent.

Q. DO YOU HAVE ANY CONCERNS WITH THE FAC POSITIONS OR RECOMMENDATIONS MADE BY STAFF IN THIS CASE?

A. Yes.

Q. PLEASE DESCRIBE THEM.

A. Empire's primary concerns are related to the Staff recommended change in the existing FAC sharing mechanism of 95/5 percent to 85/15 percent and the base energy costs being proposed by the Staff. Empire is opposed to both of these recommendations. Empire's witness Todd Tarter will address Empire's concerns in these two areas.

Q. DOES EMPIRE AGREE WITH STAFF'S OBJECTIVE OF STANDARDIZING THE VARIOUS DEFINITIONS OF COSTS INCLUDED IN THE FAC SO THAT THE VARIOUS FACS USED BY MISSOURI UTILITES ARE CONSISTENT?

A. Yes. Empire agrees with the Staff's proposal to standardize the definitions and terms and operations of the FACs used by the various Missouri electric utilities. But given the time deadlines associated with rebuttal testimony and the filing date of the Staff's proposed revisions, more time may be required to fully understand the ramifications of the Staff's proposed revisions to Empire's FAC tariff wording, In general, however Empire agrees that the various FAC tariffs in use in Missouri should be consistent in terms of the costs included, how these costs are defined, and how these costs are recovered.

Q. DID THE STAFF INCLUDE TRANSMISSION COST RECOVERY AS PART OF THE PROPOSED REVISIONS TO EMPIRE'S FAC?

A. Yes. The Staff FAC tariff sheet recommendation includes transmission cost as one of the cost components in Empire's FAC. This is a new cost component for Empire's FAC, and its inclusion in Empire's FAC would make Empire's FAC consistent with the other FACs used in Missouri.

Q. WHAT IS EMPIRE'S POSITION WITH RESPECT TO THE RECOVERY OF OUTSIDE TRANSMISSION COSTS THROUGH THE FAC?

A. Empire agrees that outside transmission cost recovery should be part of the FAC. These costs represent substantial costs to Empire, are volatile, and are beyond the control of Empire's management. Empire does not agree with the Staff's position on transmission cost recovery through the FAC since it appears to be limited to the recovery of outside transmission costs associated with off-system sales, which involve a relatively low level of outside transmission expense for Empire. Empire recommends that the FAC not only be revised to recover the outside transmission costs associated with off-system sales, but also the outside transmission costs associated with sales made to Missouri retail customers.

Q. WHAT FERC ACCOUNT DOES EMPIRE USE TO RECORD OUTSIDE TRANSMISSION COSTS?

A. Empire uses FERC account 565 Transmission of Electricity by Others to record the cost of transmission services provided by other entities. At the present time, this account includes charges from Southwest Power Pool ("SPP") and Entergy, the latter which will ultimately become MISO charges when Entergy completes its move into MISO RTO.

Q. IF OUTSIDE TRANSMISSION COSTS ARE INCLUDED AS A

COMPONENT OF EMPIRE'S FAC, WOULD THAT PLACE EMPIRE'S FAC IN A POSITION SIMILAR TO THAT OF AMEREN WITH RESPECT TO TRANSMISSION COST RECOVERY?

A. Yes. This would make the Empire and Ameren FACs very similar with regard to the recovery of transmission charges from regional transmission organizations.

Q. ARE THE TRANSMISSION SERVICES ASSOCIATED WITH THE TRANSMISSION OF ELECTRICTY BY OTHERS REQUIRED TO TRANSPORT ELECTRICITY TO EMPIRE'S CUSTOMERS?

A. Yes, Empire has turned over functional control of its transmission facilities to SPP, and without SPP's services Empire would not be able to deliver electricity to its customers. These SPP transmission services essentially interconnect our power plants and purchase power resources with our customers. These SPP services also broaden Empire's access to the market in terms of its ability to sell electricity to other utilities, and enhance Empire's ability to access supplies of electricity, including renewable resources. With the start-up of SPP's next day market, the essential nature of these SPP services will become even more pronounced.

Q. DOES THE TREATMENT OF RTO TRANSMISSION COST RECOVERY REPRESENT THE MOST SIGNFICANT INCONSISTENCY BETWEEN THE VARIOUS FAC TARIFFS IN MISSOURI?

A. Yes. The inclusion of these costs in Empire's FAC will eliminate a major inconsistency between the various FAC tariffs and make Empire's FAC consistent with the FAC authorized for Ameren in Case No. ER-2012-0166.

Q. IF THE TRANSMISSION COSTS ASSOCIATED WITH THE

TRANSMISSION OF ELECTRICITY BY OTHERS ARE INCLUDED IN EMPIRE'S FAC, DOES EMPIRE NEED THE TRANSMISSION COST TRACKING MECHANISM THAT IT INITIALLY PROPOSED AS PART OF ITS RATE REQUEST?

A. No. The transmission cost tracking mechanism would no longer be needed.

Q. HAVE ANY OF THE THREE COST FACTORS CITED BY THE COMMISSION IN CONNECTION WITH THE APPROVAL OF EMPIRE'S FAC IN THE REPORT AND ORDER IN CASE NO. ER-2008-0093 CHANGED?

A. No. Fuel and energy costs still represent the single largest component of Empire's cost to serve its customers; fuel and energy costs are still beyond the control of management; and energy costs are still volatile and can cause significant swings in cash flow and income if not tracked. In addition, even with the addition of the Plum Point and Iatan 2 coal generating units, whose capacity replaced a long-term coal fired purchased power contract, Empire still has a substantial exposure to swings in the price of natural gas because many of its generating units are gas-fired. The price of natural gas is still the subject of price swings that can be driven by a variety of factors including weather, regulatory decisions, and political issues that are beyond the control of management.

Q. HOW DOES THE STAFF'S PROPOSED CHANGE IN THE FAC SHARING MECHANISM DENY EMPIRE A SUFFICIENT OPPORTUNITY TO EARN A FAIR RETURN ON EQUITY?

A. Staff's proposal to change the sharing mechanism denies Empire a sufficient opportunity to earn a fair return on equity because the additional amount of fuel and purchased power cost the Company is required to absorb under Staff's recommendation results in a dollar for dollar reduction in Empire's actual earnings.

Q. DID STAFF PROPOSE TO CHANGE THE SHARING MECHANISM IN THE RECENTLY CONCLUDED AMEREN AND GMO RATE CASES?

A. Yes, and the Commission rejected Staff's proposal in each of those cases.

Q. DOES EMPIRE GENERALLY AGREE WITH THE STAFF'S PROPOSAL TO REBASE THE EXISTING FAC?

A. Yes. However, Todd Tarter of Empire will address the specific concerns Empire has with this Staff proposed FAC base.

Q. DOES EMPIRE HAVE CONTROL OVER THE QUANTITY OF ENERGY PURCHASED OR ENERGY PRICES OR THE LEVEL OF TRANSMISSION SERVICES USED TO TRANSPORT ELECTRICITY?

A. No. The quantity of fuel and energy Empire purchases is driven by the requirements of the customers Empire serves, and the energy markets in which Empire operates set the prices for the components of fuel and energy and transportation that Empire purchases on behalf of its customers. Empire does employ a systematic approach to the timing of its fuel and energy purchases, to mitigate price volatility, and uses a competitive bidding process whenever possible to acquire fuel and energy products, but the ultimate price of the fuel and energy products it selects is set by the market, not by Empire.

Q. DOES THE STAFF'S RECOMMENDED SHARING MECHANISM HAVE ANY IMPACT ON THE ULTIMATE COST OF FUEL AND ENERGY

THAT EMPIRE MUST PURCHASE ON BEHALF OF ITS CUSTOMERS?

A. No. As I mentioned earlier, Empire's customers dictate the quantities to be produced or purchased and the fuel and energy markets set the price. The Staff's proposed sharing mechanism will have no affect on either.

Q. DO ANY OF THE OTHER REGULATORY BODIES WITH JURISDICTION OVER EMPIRE USE FUEL ADJUSTMENT MECHANISMS THAT PROHIBIT THE RECOVERY OR REFUND OF A FIXED PERCENTAGE OF PRUDENTLY INCURRED FUEL OR ENERGY COSTS?

A. No. Empire operates in four other jurisdictions - Kansas, Oklahoma, Arkansas and the Federal Energy Regulatory Commission ("FERC") - and none of these jurisdictions automatically prohibit the pass through of a fixed percentage of prudently incurred energy costs. All of these jurisdictions allow the recovery of 100 percent of prudently incurred fuel and energy costs, and as is the case in Missouri, all of these jurisdictions employ a fuel/energy review or audit process to determine whether the fuel/energy costs that passed through the various fuel adjustment mechanisms were prudently incurred. The potential for the automatic disallowance of prudently incurred fuel and energy costs as fuel and energy costs are driven higher by market forces is unique to Empire's Missouri regulatory environment.

Q. DOES THE STAFF PROPOSAL TO INCREASE THE AUTOMATIC DISALLOWANCE OF ENERGY COST INCREASES TO 15 PERCENT IN THE FAC ENHANCE THE CHANCES OF EMPIRE HAVING A

SUFFICIENT OPPORTUNITY TO EARN THE RETURN ON EQUITY AUTHORIZED BY THE COMMISSION?

A. No. The Staff proposal will have the opposite effect; it will increase the likelihood that Empire will not have an opportunity to earn the return on equity authorized by the Commission in this proceeding.

Q. DOES EMPIRE AGREE WITH THE FAC TARIFF WORDING CHANGES RECOMMENDED BY STAFF IN THIS CASE?

A. Not entirely. The Staff has proposed a new Transmission Cost factor for Empire's FAC. The Staff has defined the transmission costs to be included in the Empire tariff as the costs reflected in FERC account 565 "excluding Base Plan Funding Costs". The tariff wording in this area should be revised so that the transmission cost definition would be read as follows:

"The following costs reflected in FERC Account Number 565: transmission costs that are necessary to serve native load and transmission costs that are necessary to make off-system sales."

I have attached a marked up version of the Staff's proposed FAC tariff to this rebuttal testimony as Rebuttal Schedule WSK-1.

Q. DOES THE TRANSMISSION OF ELECTRICITY BY OTHERS RESPRESENT A SUBSTANTIAL COST FOR EMPIRE?

A. Yes, annualized transmission costs in FERC account 565 are approximately $7.7 million, and this cost is expected to increase dramatically in the next few years as the members of the SPP complete various transmission projects to enhance the capabilities of the transmission system throughout the SPP footprint. As I indicated in my direct testimony, SPP's charges for regional transmission services to Empire are expected to increase to around $12 million per year by 2014.

Q. ARE THERE OTHER FAC WORDING CHANGES RECOMMENDED BY STAFF THAT CONCERN EMPIRE?

A. Yes. The Staff has inserted Note A at the bottom of sheet 17i. This note discusses various items associated with the SPP Integrated Market, which is scheduled to start in 2014 and establishes meeting dates and requirements for various parties, including Empire. The first paragraph of this note should be eliminated from Empire's FAC as it is not used to develop any the cost factors in the FAC or any of the procedures used to develop the cost of energy. To the extent meetings between the various parties are needed to discuss SPP market changes they can be specified in a Commission order, rather than the FAC tariff sheet.

<u>RATE BASE ISSUES</u>

<u>TORNADO AAO COSTS</u>

Q. PLEASE DESCRIBE THE STAFF'S RATE BASE TREATMENT OF THE TORNADO COSTS DEFERRED BY EMPIRE IN ACCORDANCE WITH THE ACCOUNTING AUTHORITY GRANTED BY THE COMMISSION.

A. The Staff has eliminated the costs from Empire's rate base.

Q. DO YOU AGREE WITH THIS RECOMMENATION?

A. No. The exclusion of these costs from Empire's rate base will deny Empire a return on the investment it has made in the system to restore electric service and result in an immediate understatement of Empire's cost of service in Missouri. This is unfair and is at odds with the Commission's order originally authorizing the deferral of the tornado related costs, including additional carrying cost.

Q. OVER WHAT PERIOD OF TIME WILL EMPIRE AMORTIZE THE REMAINING DEFERRED TORNADO COSTS?

A. The deferred tornado costs will be amortized over ten years.

Q. WILL THESE COSTS BE RECOVERED AS A SPECIFIC CHARGE TO EMPIRE'S CUSTOMERS?

A. No. The tornado cost amortization will be bundled in with the other components of Empire's revenue requirement to develop Empire's overall revenue requirement. As envisioned, the level of amortization expense included in Empire's cost of service would be determined during the Company's rate cases that take place over the next ten years.

Q. THE STAFF REPORT, AT PAGE 70, INDICATES THAT THIS RATE BASE EXCLUSION REPRESENTS A WAY TO SHARE THE RISK FROM STORMS BETWEEN EMPIRE AND ITS CUSTOMERS. DO YOU AGREE?

A. No. Empire has absorbed the financial impact of the storms for almost two years. The costs deferred as a result of the storms will be spread to Empire's customers over ten years. The Staff recommendation simply understates the overall cost by denying the recovery of the cost associated with carrying the deferred storm costs for ten years. There is no risk sharing, only the denial of the cost associated with spreading the storm cost recovery over a ten-year period.

EEI DUES

Q. THE STAFF HAS MADE A SMALL REDUCTION IN EMPIRE'S

MATERIALS AND SUPPLIES BALANCE TO ELIMINATE EDISON ELECTRIC INSTUTUE ("EEI") DUES. DO YOU AGREE WITH THIS ADJUSTMENT?

A. No. The Staff has not only eliminated EEI dues from Empire's rate base, but eliminated all of Empire's EEI dues from operating costs.

Q. DO EMPIRE AND ITS CUSTOMERS BENEFIT FROM EMPIRE'S MEMBERSHIP IN EEI?

A. Yes. Empire's EEI membership provides benefits to both Empire and its customers.

Q. WHAT IS THE BASIS FOR THE STAFF'S DISALLOWANCE OF EEI DUES?

A. Staff witness Jermaine Green refers to a couple of prior Commission orders regarding EEI dues as the basis for his disallowance. The orders, which appear to refer to cases involving the Kansas City Power and Light Company, are over twenty years old. These prior orders discuss the quantification of EEI benefits between the company and ratepayers. The Staff Report at page 131 indicates that Empire has not quantified the ratepayer and shareholder benefits related to Empire's EEI membership.

Q. HAS EMPIRE'S RELATIONSHIP WITH EEI EVOLVED OVER THE LAST TWENTY YEARS?

A. Yes. Empire uses its membership in EEI to monitor critical industry issues. This relationship is very valuable considering the tremendous increase in regulatory pressures that have been building on the industry over the last twenty years, especially in the environmental area. Working with EEI and its members enables Empire to stay abreast of industry issues, and gain insight into how other utilities are approaching industry problems and issues. Empire must monitor industry issues as these issues will eventually have cost implications for Empire and its customers. Empire's EEI membership enables Empire to monitor and deal with these critical issues at a fraction of what it would cost to do on a standalone basis. This reduction in the cost of monitoring critical industry issues is a direct benefit for our customers.

Q. WHAT WAS THE ANNUAL COST OF EMPIRE'S EEI MEMBERSHIP DURING THE TEST YEAR?

A. Empire's annual dues to EEI were approximately $120,000 during the test year.

Q. DOES EEI PROVIDE EMPIRE AND ITS CUSTOMERS BENEFITS IN THE ENVIRONMENTAL AREA?

A. Yes. When new environmental rules are promulgated, EEI provides its members with a written summary of the proposed regulation. This provides a tangible cost benefit to Empire and its customers in terms of the time that would have to be spent preparing such an analysis, and the additional direct cost associated with an expansion of Empire environmental staff that would be required to monitor and track the various environmental rules and report to Empire management. Our EEI membership also provides an avenue to discuss environmental regulations through EEI environmental working groups to develop environmental compliance strategies. Empire's EEI membership is a very cost effective method of dealing with the massive increase in environmental regulations and avoid the additional environmental staff Empire would need to add if it did not maintain its EEI membership.

Q. DOES EEI HAVE OTHER COMMITTEES AND SUBCOMMITTEES THAT PROVIDE A COST EFFECITVE METHOD OF MONITORING AND COMPLYING WITH INDUSTRY ISSUES?

A. Yes. A list of the various EEI committees was presented in the direct testimony of Jayna Long.

<u>IATAN AND PLUM POINT O&M TRACKERS</u>

Q. WHAT IS THE ISSUE INVOLVING THE IATAN AND PLUM POINT OPERATION AND MAINTENANCE COST TRACKERS?

A. The Staff has determined the level of Iatan/Plum Point deferred costs by limiting the cost deferred to specific expense accounts anticipated at the time of the implementation of the trackers (see page 110 of Staff Cost of Service Report). During the accumulation period ending June 30, 2012, the actual costs incurred involved costs and accounts that were not initially anticipated. The Staff approach to the trackers excludes these costs from Empire's authorized tracker mechanism.

Q. DO YOU AGREE WITH THE STAFF POSITON IN THIS AREA?

A. No. The Staff approach excludes specific costs from the tracking mechanism and results in an understatement of the Iatan and Plum Point deferred operating and maintenance cost balances. This exclusion will also understate the amortization of tracker costs.

Q. WAS IT POSSIBLE TO DETERMINE THE EXACT COMPONENTS OF IATAN AND PLUM POINTS COSTS ON AN ACCOUNT BY ACCOUNT

BASIS WHEN THE TRACKERS WERE ESTABLISHED AT THE END OF THE LAST RATE CASE?

A. No. A base level of Iatan/Plum Point expenses was determined using the account by account information Empire had at the time. The overall base expense levels were specified in the settlement agreement reached in the last case, but the individual accounts were not specified in the settlement agreement reached in ER-2011-0004.

Q. WHAT IS THE LEVEL OF IATAN/PLUM POINT COSTS THAT THE STAFF'S APPROACH EXCLUDES FROM THE TRACKING MECHANISM?

A. The costs excluded from the tracker under the Staff's approach are as follows:

- Plum Point-$66,976, primarily costs incurred for outside services;
- Iatan 2-$85,644, primarily for costs incurred in connection with property insurance; and
- Iatan common $18,394, primarily for costs incurred in connection with property insurance.

REC REVENUE

Q. PLEASE DESCRIBE THE ISSUE THE COMPANY HAS WITH STAFF'S ONGOING REC REVENUE.

A. REC Revenue is associated with Empire's sale of renewable energy credits derived from Empire's purchase of energy produced at the Elk River and Meridian Way wind farms. The Staff has attempted to normalize Empire's ongoing REC revenue in its determination of Empire revenue requirement. This normalized REC revenue level is also used in Staff's FAC base calculation.

Q. DOES EMPIRE AGREE WITH STAFF'S NORMALIZED REC REVENUE LEVEL?

A. No. The Staff's normalized REC level of $2.024 million is substantially higher than the REC revenue levels Empire expects to see in 2013.

Q. WHY?

A. A long-term REC sales contract that Empire had in place for a number of years expired at December 31, 2012. This long-term REC sales contract included prices that were much higher than the spot market REC prices Empire expects to see in 2013.

Q. WHAT LEVEL OF REC REVENUE DOES EMPIRE EXPECT IN 2013?

A. Using the current spot market price of RECs, Empire expects its net REC revenue to decline to $552 thousand in 2013. This represents a decline of $1.472 million from the levels forecast by Staff.

Q. DO THE CHANGES IN REC REVENUE FLOW THROUGH EMPIRE'S FAC?

A. Yes. Empire has reflected the changes in REC revenue as a component of its FAC for several years. However, given the incentive sharing mechanism built into the FAC, it is important to establish a reasonable level of REC revenues built into the FAC base to avoid penalizing Empire for the expected decline in REC revenue in 2013.

<u>SPP TRANSMISSION COSTS</u>

Q. PLEASE DESCRIBE THE ISSUE ASSOCIATED WITH STAFF'S

NORMALIZED SPP TRANSMISSION COST.

A. The Staff has established Empire's ongoing SPP costs at $4.765 million. This is substantially lower than the cost levels Empire expects to see in calendar year 2013, which are expected to be approximately $3.6 million higher than the normalized Staff levels.

Q. WHY ARE THE STAFF'S SPP TRANSMISSION COST LEVELS SO MUCH LOWER THAN THE LEVELS EMPIRE EXPECTS TO SEE IN 2013?

A. The Staff's approach to SPP transmission cost does not take into account the SPP rate increases that will occur in 2013 as the various SPP members increase their rates to recover the cost of transmission improvements.

Q. CAN EMPIRE AVOID THE EXPECTED INCREASE IN SPP TRANSMISSION FEES?

A. No. The cost and charges for these services are regulated by the FERC, and Empire is required to reimburse SPP at the FERC authorized rate. Based upon the latest forecast information we have from SPP, the SPP transmission charges are expected to increase substantially in 2013. The approach Staff has used to normalize these costs ignores what are anticipated to be substantial SPP rate increases in 2013.

<u>OUTSIDE SERVICE EXPENSES</u>

Q. PLEASE DESCRIBE THE ISSUE RELATED TO EMPIRE'S OUTSIDE SERVICE EXPENSE.

A. The issue involves using a multi-year average to establish a normalized level of outside service expenses. The Staff has used a five-year average to develop a normalized level of outside service costs (see page 129 of Staff Report) and MEUA has proposed that test year expense levels be used as the normalized level of outside service costs (see testimony of MEUA witness Rackers). Empire's filing used a three-year average of outside service expenses to establish a normalized level of costs.

Q. IS IT UNUSUAL TO USE A MULTI YEAR AVERAGE OF COSTS TO ESTABLISH A NORMALIZED LEVEL OF COSTS?

A. No. The use of multi-year averages to establish normalized cost levels is fairly common place, and its use in the area of outside service expenses is not unusual or unprecedented.

Q. IS THE APPROACH USED BY MEUA TO ESTABLISH NORMALIZED OUTSIDE SERVICE COST LEVELS ACCEPTIBLE?

A. No. The use of the test year level of outside service cost as the normalized level of costs, results in an abnormally low level of outside service expenses for Empire.

Q. WHY IS THE TEST YEAR OUTSIDE SERVICE COST ABNORMALLY LOW?

A. In large part it is driven by the timing of the filing of Empire's Integrated Resource Plan ("IRP"). The test year ending March 31, 2012 does not include a normalized level of IRP costs. In fact, the IRP costs levels included in the test year are a negative $368 thousand. This is the direct result of an accounting adjustment made during the test year related to the cost of preparing an energy efficiency potential study in the last IRP.

Q. HOW DOES IRP PREPARATION INFLUENCE OVERALL OUTSIDE SERVICE EXPENSE LEVEL?

A. IRP preparation increases overall Outside Service expenses. The following table displays the variation in monthly outside service costs and how the preparation of the IRP increases monthly costs.

Month	Expense	Remarks
April 2009	348,395	
May 2009	119,575	
June 2009	155,510	
July 2009	213,781	
August 2009	125,749	
September 2009	478,299	IRP Preparation Cycle
October 2009	387,342	IRP Preparation Cycle
November	235,552	IRP Preparation Cycle
December 2009	594,678	IRP Preparation Cycle
January 2010	138,223	IRP Preparation Cycle
February 2010	158,767	IRP Preparation Cycle
March 2010	266,780	IRP Preparation Cycle
April 2010	285,856	IRP Preparation Cycle
May 2010	224,317	IRP Preparation Cycle
June 2010	407,291	IRP Preparation Cycle
July 2010	171,844	IRP Preparation Cycle
August 2010	366,526	IRP Preparation Cycle
September 2010	180,878	IRP Preparation Cycle
October 2010	225,265	
November 2010	131,196	
December 2010	250,361	
January 2011	64,192	
February 2011	94,180	
March 2011	274,419	
April 2011	118,568	
May 2011	33,830	
June 2011	(378,083)	Deferral of IRP Costs
July 2011	97,225	
August 2011	245,494	
September 2011	174,651	
October 2011	225,426	
November 2011	115,771	
December 2011	236,576	

January 2012	104,443	
February 2012	173,815	
March 2012	220,801	

Q. DOES THE USE OF A MULTI-YEAR AVERAGE OF OUTSIDE SERVICE EXPENSE LEVELS NORMALIZE EMPIRE'S IRP COST LEVELS?

A. Yes. Empire incurs IRP costs every three years. The use of a multi-year period of outside service costs will capture the cost of IRP compliance and normalize it. The Staff approach to outside service costs will normalize IRP costs using a five-year average and Empire's approach to outside service costs will also normalize IRP costs using a three-year average. The MEUA approach does not normalize IRP costs.

<u>OFF-SYSTEM SALES</u>

Q. PLEASE DESCRIBE THE OFF-SYSTEM SALES ISSUE.

A. The Staff and Empire have eliminated Off-system Sales ("OSS") from Empire's base revenue requirement, while MEUA has proposed that an OSS margin of $2 million be used to set Empire's overall revenue requirement. This same OSS margin would be used as part of the determination of the FAC base (Rackers page 14).

Q. DO YOU AGREE WITH THE MEUA PROPOSAL?

A. No. The level of OSS margin proposed by MEUA is not reasonable, and the historical OSS sales information that is cited by MEUA as support for its position is no longer relevant to the OSS market Empire faces currently or will face in 2013 and throughout the period rates set in this case will be in effect.

Q. ARE OSS PRICES HIGHER OR LOWER THAN THEY WERE IN THE HISTORICAL PERIOD USED BY MEUA?

A. Currently, the prices in the OSS market are substantially lower than past prices. OSS prices have declined just like natural gas prices. The MEUA forecast of $2 million does not take these price declines into account.

Q. DOES THE AVAILABILITY OF PLUM POINT AND IATAN 2 INCREASE THE LIKELIHOOD OF OFF-SYSTEM SALES MARGINS?

A. No. These units were acquired, for the most part, to replace a long-term power contract that expired, not to increase off-system sales. The largest factor driving the OSS market is the price of natural gas, and the price of natural gas is expected to remain low for several years. This means that OSS prices will remain low during the rate effective period.

<u>RATE CASE EXPENSE</u>

Q. PLEASE DESCRIBE THE ISSUE ASSOCIATED WITH RATE CASE EXPENSE.

A. The Staff has eliminated any cost recovery associated with the unamortized costs incurred in connection with Case No. ER-2011-0004, Empire's last general rate case. The ER-2011-0004 rate case costs are currently being amortized over a 48-month period. At the end of December 2012, Empire has an unamortized balance of ER-2011-0004 costs of approximately $996 thousand that will not be fully amortized until May of 2015.

Q. WHAT IS EMPIRE'S RECOMMENDATION IN THIS AREA?

A. Empire recommends that the cost of the current case be trued-up through December

31, 2012 and, if a hearing is required, that the cost of the current case include a component for the cost of the hearing. In addition, the unamortized costs associated with ER-2011-0004 should be added to the current case costs and amortized over twenty-four months along with the cost of the current case.

<u>TRUE-UP</u>

Q. HAS THE COMMISSION APPROVED THE USE OF A TRUE-UP?

A. Yes. The Commission has ordered that a true-up be concluded through December 31, 2012.

Q. WHAT ITEMS SHOULD BE ADDRESSED AS PART OF THE TRUE-UP PROCESS IN THIS CASE?

A. The following items should be included in the true-up process in this case in order to provide Commission with the most timely and relevant information available:

- All of the components of rate base, including plant in service balances and accumulated depreciation balances
- DSM investment balances
- Change in the number of customers taking service
- Fuel/Purchase Power costs associated with change in number of customers
- SPP revenue
- SPP expense
- Payroll expense
- Employee Benefits such as health care
- Rate Case expense
- Depreciation and amortization expense, including depreciation rates

- Property tax
- Income tax
- Vegetation management costs
- Various tracker balances and amortization levels
- New operating system costs, including maintenance on new systems
- Property Insurance costs
- Generation unit maintenance costs

STAFF RATE DESIGN

Q. HAVE YOU REVIEWED THE STAFF RATE DESIGN REPORT AND THE DIRECT TESTIMONY FILED BY STAFF WITNESS MICHAEL S. SCHEPERLE?

A. Yes.

Q. DOES EMPIRE ACCEPT THE STAFF'S COST OF SERVICE ALLOCATIONS IN THIS CASE?

A. Empire can accept Staff's overall cost allocation methodology and the proposed change in customer charges in this case.

Q. HAS STAFF PRODUCED A REVENUE PROOF AS PART OF THE WORKPAPERS IT USED TO DEVELOP RATES IN THIS CASE?

A. Yes, but the rates proposed by the Staff do not include the revenue requirement associated with the various true-up items and therefore do not represent the final rates that Empire will need coming out of this rate case. In addition, the final revenue proof in this case should be based upon Empire's overall revenue requirement after true-up and the normalized Empire billing determinants after true-up.

DSM COST RECOVERY

Q. DOES EMPIRE OBJECT TO THE STAFF'S PROPOSAL FOR EMPIRE TO RECOVER ITS DSM COSTS USING A SEPRARTE CHARGE THAT WOULD NOT BE APPLIED TO THE CUSTOMERS OPTING OUT OF THE ENERGY EFFICIENCY PROGRAMS?

A. No. We are currently working with our billing department to see if there any impediments to the implementation of such a charge in our billing system. As of the date of this rebuttal testimony, no billing system impediments have arisen.

LOW INCOME PROGRAM

Q. PLEASE DESCRIBE THE ISSUE ASSOCIATED WITH EMPIRE'S LOW INCOME WEATHERIZATION PROGRAM.

A. The Staff and Missouri Department of Natural Resources suggest that changes be made to Empire's tariff to reflect some changes in low income standards.

Q. DOES EMPIRE AGREE WITH THE TARIFF CHANGES SUGGESTED BY STAFF AND MDNR?

A. It was unclear just exactly what tariff wording changes would need to be made to accommodate the changes being requested by Staff and MDNR. At this point, Empire agrees to work with Staff and MDNR on specific wording changes and bring them to the DSM collaborative group for discussion and consideration. In addition, Empire will be proposing a new energy efficiency portfolio in 2013. Empire believes that it may be more efficient use of time and resources to incorporate any changes in the low income weatherization tariff wording as part of the upcoming 2013 energy efficiency filing.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

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For ALL TERRITORY

FUEL & PURCHASE POWER ADJUSTMENT CLAUSE
RIDER FAC
For service on and after XX-XX-XXXX.

The two six-month accumulation periods, the two six-month recovery periods and filing dates are set forth in the following table:

Accumulation Periods	**Filing Dates**	**Recovery Periods**
September - February	By April 1	June - November
March - August	By October 1	December – May

The Company will make a Fuel Adjustment Rate ("FAR") filing by each Filing Date. The new FAR rates for which a filing is made will be applicable starting with the recovery period that begins following the Filing Date. All FAR filings shall be accompanied by detailed workpapers supporting the filing in an electronic format with all formulas intact.

DEFINITIONS

ACCUMULATION PERIOD:
The six calendar months during which the actual costs and revenues subject to this rider will be accumulated for the purpose of determining the FAR.

RECOVERY PERIOD:
The billing months during which a FAR is applied to retail customer usage on a per kilowatt-hour (kWh) basis.

BASE ENERGY COSTS AND REVENUES:
Base energy costs are ordered by the Commission in the last rate case consistent with the costs and revenues included in the calculation ~~of the Fuel~~ and Purchase Power Adjustment ("FPA").

BASE FACTOR ("BF"):
The base factor is the base energy cost divided by net generation kWh determined by the Commission in the last general rate case. BF = ~~$0.03223~~ per kWh for each accumulation period.
$0.03115

DATE OF ISSUE July 6, 2012 DATE EFFECTIVE August 5, 2012
ISSUED BY Kelly S. Walters, Vice President, Joplin, MO

FUEL & PURCHASE POWER ADJUSTMENT CLAUSE
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APPLICATION
FUEL & PURCHASE POWER ADJUSTMENT

0.95

$$FPA = \{[(FC + PP + E + TC - OSSR - REC - B) * J] * \cancel{0.85\}} + T + I + P$$

Where:

FC = Fuel Costs Incurred to Support Sales:

The following costs reflected in Federal Energy Regulatory Commission (FERC) Account Number 501: coal commodity and railroad transportation, switching and demurrage charges, applicable taxes, natural gas costs, alternative fuels (i.e. tires, bio- fuel and landfill gas), fuel additives, Btu adjustments assessed by coal suppliers, quality adjustments assessed by coal suppliers, fuel hedging costs, fuel adjustments included in commodity and transportation costs, broker commissions and fees associated with price hedges, oil costs, propane costs, combustion product disposal revenues and expenses, consumable costs related to Air Quality Control Systems (AQCS) operation, such as ammonia, lime, limestone, powder activated carbon, urea, sodium bicarbonate, and trona and settlement proceeds, insurance recoveries, subrogation recoveries for increased fuel expenses in Account 501.

The following costs reflected in FERC Account Number 547: natural gas generation costs related to commodity, oil, transportation, storage, fuel losses, hedging costs for natural gas, oil, and natural gas used to cross-hedge purchased power, fuel additives, and settlement proceeds, insurance recoveries, subrogation recoveries for increased fuel expenses, broker commissions and fees.

PP = Purchased Power costs:

The following costs or revenues reflected in FERC Account Number 555: purchased power costs, purchased power demand costs associated with purchased power contracts with a duration of one year or less, settlements, insurance recoveries, and subrogation recoveries for purchased power expenses, virtual energy charges, generating unit price adjustments, load/export charges, energy position charges, ancillary services including penalty and distribution charges, hedging costs, broker commissions, fees, and margins, SPP EIS market charges, and SPP Integrated Market charges (see note A. below)

E = Net Emission Costs:

The following costs and revenues reflected in FERC Account Numbers 509, 411.8 and 411.9 (or any other account FERC may designate for emissions expenses in the future): emission

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allowance costs offset by revenues from the sale of emission allowances including any associated hedging costs, broker commissions, fees, commodity based services, and margins.

TC = Transmission Costs:

X

The following costs reflected in FERC Account Number 565 ~~(excluding Base Plan Funding costs)~~: transmission costs that are necessary to receive purchased power to serve native load and transmission costs that are necessary to make off-system sales.

OSSR = Revenue from Off-System Sales:

A. The following revenues or costs reflected in FERC Account Number 447: all revenues from off-system sales but excluding revenues from full and partial requirements sales to Missouri municipalities that are associated with Empire, hedging costs, SPP EIS market charges, and SPP Integrated Market revenues (see note A. below)

REC = Renewable energy credit revenue:

Revenues reflected in FERC account 509 from the sale of Renewable Energy Credits that are not needed to meet the Renewable Energy Standard.

Hedging Costs = Hedging costs are defined as realized losses and costs (including broker commission fees and margins) minus realized gains associated with mitigating volatility in the Company's cost of fuel, fuel additives, fuel transportation, emission allowances, transmission and purchased power costs, including but not limited to, the Company's use of derivatives whether over-the counter or exchange traded including, without limitation, futures or forward contracts, puts, calls, caps, floors, collars, and swaps.

X

Note A. ~~In anticipation of the implementation of the SPP Integrated Market, the Company and the Missouri Public Service Commission Staff (Staff) will meet quarterly to discuss and review the charge types proposed by SPP and the new market. The Company will provide a listing of charge types and definitions to discuss. Staff and other interested intervenors will provide feedback relating to those costs included in the Fuel Adjustment Clause. Documentation of the quarterly meetings will be filed with the most closely following monthly Section 5 report to be filed with the Commission.~~

Should FERC require any item covered by factors FC, PP, E or OSSR to be recorded in an account different than the FERC accounts listed in such factors, such items shall nevertheless

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be included in factor FC, PP, E or OSSR. In the month that the Company begins to record items in a different account, the Company will file with the Commission the previous account number, the new account number and what costs or revenues that flow through this Rider FAC are to be recorded in the account.

X

B = Net base energy cost is calculated as follows:

$B = (S_{AP}$ * ~~$0.03223)~~
$0.03115

S_{AP} = Actual net system input at the generation level for the accumulation period.

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$$J = \frac{\text{Missouri retail kWh sales}}{\text{Total system kWh sales}}$$

Where Total system kWh sales includes sales to Missouri municipalities that are associated with Empire and excludes off-system sales.

T = True-up of over/under recovery of FAC balance from prior recovery period as included in the deferred energy cost balancing account. Adjustments by Commission order pursuant to any prudence review shall also be placed in the FPA for collection unless a separate refund is ordered by the Commission.

I = Interest applicable to (i) the difference between Total energy cost (FC + PP + E + TC – OSSR – REC) and Net base energy cost ("B") multiplied by the Missouri energy ratio ("J") for all kWh of energy supplied during an AP until those costs have been recovered; (ii) refunds due to prudence reviews ("P"), if any; and (iii) all under- or over-recovery balances created through operation of this FAC, as determined in the true-up filings ("T") provided for herein. Interest shall be calculated monthly at a rate equal to the weighted average interest paid on the Company's short-term debt, applied to the month-end balance of items (i) through (iii) in the preceding sentence.

P = Prudence disallowance amount, if any, as defined below.

FUEL ADJUSTMENT RATE

The FAR is the result of dividing the FPA by estimated recovery period S_{RP} kWh, rounded to the nearest $0.00000. The FAR shall be adjusted to reflect the differences in line losses that occur at primary and above voltage and secondary voltage by multiplying the average cost at the generator by 1.0502 and 1.0686, respectively. Any FAR authorized by the Commission shall be billed based upon customers' energy usage on and after the authorized effective date of the FAR. The formula for the FPA is displayed below.

$$FAR = \frac{FPA}{S_{RP}}$$

Where:

S_{RP} = Forecasted Missouri NSI kWh for the recovery period.

$$= \text{Forecasted total system NSI} * \frac{\text{Forecasted Missouri retail kWh sales}}{\text{Forecasted total system kWh sales}}$$

Where Forecasted total system NSI kWh sales includes sales to Missouri municipalities that are associated with Empire and excludes off-system sales.

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PRUDENCE REVIEW

Prudence reviews of the costs subject to this FAC shall occur no less frequently than every eighteen months, and any such costs which are determined by the Commission to have been imprudently incurred or incurred in violation of the terms of this rider shall be returned to customers. Adjustments by Commission order, if any, pursuant to any prudence review shall be included in the FAR calculation in P above unless a separate refund is ordered by the Commission. Interest on the prudence adjustment will be included in I above.

TRUE-UP OF FPA

In conjunction with an adjustment to its FAR, the Company will make a true-up filing with an adjustment to its FAC on the first Filing Date that occurs after completion of each recovery period. The true-up adjustment shall be the difference between the revenues billed and the revenues authorized for collection during the true-up recovery period, i.e. the true-up adjustment. Any true-up adjustments or refunds shall be reflected in item T above and shall include interest calculated as provided for in item I above.

AFFIDAVIT OF W. SCOTT KEITH

STATE OF MISSOURI)
) ss
COUNTY OF JASPER)

On the __14th__ day of January 2013, before me appeared W. Scott Keith, to me personally known, who, being by me first duly sworn, states that he is the Director of Planning and Regulatory of The Empire District Electric Company and acknowledges that he has read the above and foregoing document and believes that the statements therein are true and correct to the best of his information, knowledge and belief.

W. Scott Keith
W. Scott Keith

Subscribed and sworn to before me this __14th__ day of January, 2013.

ANGELA M. CLOVEN
Notary Public - Notary Seal
State of Missouri
Commissioned for Jasper County
My Commission Expires: November 01, 2015
Commission Number: 11262659

Angela M. Cloven
Notary Public

My commission expires: 11/01/15.