

Exhibit No.

Issue: Fuel Adjustment, Bad Debt Expense,
DSM and Vegetation Management Costs

Witness: W. Scott Keith

Type of Exhibit: Rebuttal Testimony

Sponsoring Party: Empire District Electric

Case No. ER-2008-0093

Date Testimony Prepared: April 2008

**Before the Public Service Commission
of the State of Missouri**

Rebuttal Testimony

of

W. Scott Keith

April 2008

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OF
W. SCOTT KEITH
ON BEHALF OF
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION

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REBUTTAL TESTIMONY
OF
W. SCOTT KEITH
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2008-0093

1 **INTRODUCTION**

2 **Q. STATE YOUR NAME AND ADDRESS PLEASE.**

3 A. My name is W. Scott Keith and my business address is 602 Joplin Street, Joplin,
4 Missouri.

5 **POSITION**

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

7 A. I am presently employed by The Empire District Electric Co. ("Empire" or "the
8 Company") as the Director of Planning and Regulatory. I have held this position
9 since August 1, 2005. Prior to joining Empire I was Director of Electric Regulatory
10 Matters in Kansas and Colorado for Aquila, Inc. from 1995 to July 2005.

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

15 A. Yes.

16 **PURPOSE**

17 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

18 A. My rebuttal testimony will discuss issues that have been raised by several of the

1 other parties in this rate case in their direct case filings. Specifically, I will address
2 the following:

- 3 • Fuel Adjustment Mechanisms Proposed by the Missouri Public Service
4 Commission Staff (“Staff”) Mr. Brubaker on behalf of the Industrials and Ms.
5 Meisenheimer on behalf of the Office of Public Counsel (“OPC”)
- 6 • Bad Debt Expense-Staff
- 7 • Demand Side Management (“DSM”) or Energy Efficiency-Department of Natural
8 Resources (“DNR”)
- 9 • Vegetation Management Costs-Staff

10 **FUEL ADJUSTMENT MECHANISM**

11 **Q. HAVE YOU REVIEWED THE FUEL ADJUSTMENT CLAUSE (“FAC”)**
12 **POSITIONS TAKEN BY THE STAFF AND THE INDUSTRIAL**
13 **INTERVENORS IN THIS CASE?**

14 A. Yes. I reviewed the Staff Report, the direct testimony of Staff witness Watkins and
15 the rate design testimony filed by Mr. Brubaker on behalf of the Industrials.

16 **Q. PLEASE DESCRIBE YOUR CONCERNS WITH THE FAC POSITIONS OR**
17 **RECOMMENDATIONS MADE BY STAFF AND THE INDUSTRIAL**
18 **INTERVENORS IN THIS CASE.**

19 A. Empire is pleased that the Staff and Industrials’ have recommended the
20 implementation of a FAC for Empire, but Empire is concerned with some of the
21 specifics of each of the recommendations. More specifically, each of the proposals
22 contains a sharing recommendation that would significantly limit the amount of the
23 changes in energy costs that Empire could flow through the FAC. At page 63 of its

1 initial report, Staff has recommended that only seventy percent (70%) of the
2 changes in energy costs be passed on to the customers through the FAC. The
3 Industrials' through the direct testimony of Mr. Brubaker have recommended that a
4 FAC sharing mechanism be implemented that, if certain cost levels are reached in
5 the future, would result in the Empire shareholders absorbing up to \$3 million in
6 increased energy costs. Both the Staff and Industrial cost sharing recommendations
7 are unfair and unreasonable. Empire witness Dr. Overcast will respond to the FAC
8 sharing mechanisms recommended by the Staff and Industrials.

9 **Q. WHAT OTHER AREAS OF THE STAFF FAC RECOMMENDATION ARE**
10 **OF CONCERN TO EMPIRE?**

11 A. The Staff through the rate design report (page 8) in this case has recommended that
12 a seasonal base cost of energy be established in the FAC instead of an average
13 annual base cost of energy as proposed by Empire in this case. Empire has
14 reviewed the energy cost information that was submitted as part of its initial filing
15 to see if a significant average cost of energy differential exists between the
16 proposed accumulation periods. I have attached this analysis to my rebuttal
17 testimony as Rebuttal Schedule WSK-1. As indicated, in normal weather
18 conditions the average cost differential in the accumulation periods is slightly over
19 \$3 per megawatt-hour ("Mwh"), with the average cost of energy during the
20 accumulation period ending February at around \$27 per Mwh, and the energy cost
21 during the accumulation period ending August averaging slightly over \$30 per
22 Mwh. This \$3 average cost differential does not appear to rise to a level that would
23 dictate the need to establish a seasonal average base cost of energy in the FAC as

1 proposed by the Staff.

2 **Q. HOW MUCH DOES A \$3 DIFFERENTIAL IN ENERGY COSTS MAKE ON**
3 **A TYPICAL MONTHLY RESIDENTIAL BILL?**

4 A. It is not significant. Specifically, a \$3 per Mwh average cost differential between
5 the accumulation periods would ultimately result in a customer using 1000 Kwh
6 paying \$3 more or less per month. This level of cost differential would only equal
7 about 2.7 percent of a monthly summer bill for a residential customer using 1000
8 Kwh at the rates Empire has proposed in this proceeding. The average energy cost
9 differentials do not support the additional complexity required to implement the
10 Staff recommendation concerning a seasonal base in the FAC.

11 **Q. HAVE YOU INVESTIGATED THE SENSITIVITY OF THE FAC**
12 **PROPOSED BY EMPIRE TO COLDER AND WARMER THAN NORMAL**
13 **WEATHER?**

14 A. Yes. We have compared the impact of a warmer than normal summer coupled with
15 a mild winter and a colder than normal winter coupled with a mild summer to see
16 what could happen to average energy costs under these situations. These
17 comparisons are displayed on Rebuttal Schedule WSK-1. As indicated, the warmer
18 than normal summer increased annual average energy costs from \$28.72 per Mwh
19 to \$29.13 per Mwh. The colder than normal winter scenario resulted in an even
20 smaller increase in average power costs, with average costs increasing from \$28.72
21 per Mwh to \$28.81. Extreme weather conditions do not drive the need for seasonal
22 base costs of energy in the FAC.

23 **Q. DOES EMPIRE HAVE TWO PEAKING PERIODS?**

1 A. Yes. Unlike many of the utilities in the region, Empire has a summer peak and a
2 winter peak that comes very close to matching its summer peak. This year-round
3 energy use also contributes to relatively flat average energy costs and less
4 seasonality in energy costs that might be seen on a utility with a very strong
5 summer peak relative to its winter peak and a lower annual load factor.

6 **Q. DOES THE STAFF RECOMMENDATION THAT THE FAC USE A**
7 **SEASONAL BASE MAKE SENSE FOR EMPIRE?**

8 A. No, as I mentioned earlier, the accumulation period costs differentials are not
9 significant from the standpoint of average energy costs or from the standpoint of a
10 customer and the load characteristics of the Empire system, twin peaks and year-
11 round energy use make this added refinement unnecessary.

12 **Q. DOES THE STAFF REPORT CONTAIN OTHER COMMENTS WITH**
13 **RESPECT TO THE FAC THAT ARE UNCLEAR TO EMPIRE?**

14 A. Yes. At pages 7 and 8 of Staff's rate design report, Staff recommends
15 accumulation and recovery periods and the application of an interest calculation
16 that appear to be identical to those included in Empire's filing, yet the Staff's
17 recommendations are characterized as being different from Empire's proposal. It is
18 unclear to Empire just how Staff's proposal in this area differs from Empire's
19 proposal. In addition, Staff's rate design report did not have a FAC tariff sheet
20 attached so it is unclear just how Staff's FAC proposal would work. Empire
21 recommends that the Staff produce a draft tariff of the FAC proposal it is making in
22 this matter so that the parties to this proceeding can see exactly how the Staff's
23 proposed FAC works.

1 **Q. WHAT OTHER AREAS OF STAFF’S FAC RECOMMENDATION ARE**
2 **UNCLEAR TO EMPIRE?**

3 A. At page 8, Staff makes reference to adjusting costs “at the generator” to the
4 assumed metering voltage. It is unclear what this means, and without a proposed
5 FAC tariff it is impossible to see how this affects the tariff from an administration
6 standpoint or differs from Empire’s FAC proposal in this area. Empire’s FAC
7 proposal included the use of two expansion factors to capture the different levels of
8 line loss that occur at secondary deliveries versus deliveries made at primary and
9 above. Without a clear understanding of what is involved in Staff’s
10 recommendation in this area and a proposed Staff FAC tariff sheet, Empire cannot
11 respond to the Staff’s recommendation concerning voltage levels.

12 **Q. PLEASE DESCRIBE THE OTHER CONCERNS EMPIRE HAS WITH THE**
13 **FAC PROPOSALS MADE BY MR. BRUBAKER (INDUSTRIALS)?**

14 A. Empire is concerned with several of the cost exclusions proposed by Mr. Brubaker.
15 More specifically, Empire disagrees with Mr. Brubaker’s proposal to exclude unit
16 train costs, fuel handling costs, emission allowances and natural gas transportation
17 demand charges from the FAC. Empire witness Overcast will address the
18 exclusion of emission allowances and natural gas pipeline demand charges in his
19 rebuttal testimony.

20 **Q. WHY DOES EMPIRE DISAGREE WITH MR. BRUBAKER’S EXCLUSION**
21 **OF UNIT TRAIN AND FUEL HANDLING COSTS?**

22 A. Mr. Brubaker first mentions these exclusions at page 2 of his rate design testimony
23 in this case and discusses each item later in his rate design testimony at page 17.

1 Empire does not agree that just because these costs are more stable than the cost of
2 natural gas for example that they should be excluded from the FAC.

3 The exclusion of unit train costs which are directly related to the cost of
4 transporting fuel to the Empire generating stations would be particularly
5 complicated from an administrative standpoint.

6 **Q. WHY?**

7 Unit train costs are included as a component of coal costs and flow through the fuel
8 inventory to the income statement as the coal is consumed. Under Mr. Brubaker's
9 proposal, the coal costs included in the FAC would not track the Empire financial
10 statements, and this differential would contribute to additional complexity when it
11 came time to file for a fuel adjustment change or during the periodic audits that will
12 take place during the duration of the FAC. For example, the differences between
13 the fuel costs (coal) recorded on the books and those included in the FAC would
14 have to be reconciled each time a filing was made. This added complexity is
15 unwarranted given the level of the unit train costs, approximately 1 percent of
16 overall energy costs and their relative stability compared to gas price fluctuations.

17 Mr. Brubaker's proposal to exclude the costs associated with fuel handling and
18 sales of fly ash would contribute to similar problems of reconciliation between
19 Empire's general ledger costs and those costs included in the FAC. Again given
20 the magnitude of the costs involved and their stability compared to the other costs
21 included in the FAC, the exclusion of this small area of costs from the FAC is not
22 necessary and only serves to make the ongoing administration and audit of the FAC
23 more difficult.

1 **Q. HAVE YOU ALSO REVIEWED THE TESTIMONY OF THE OFFICE OF**
2 **THE PUBLIC COUNSEL’S WITNESS MEISENHEIMER REGARDING**
3 **EMPIRE’S PROPOSED FAC?**

4 A. Yes, I have. Ms. Meisenheimer argues in her testimony that Empire is prohibited
5 from requesting or having an FAC approved in this case because of commitments
6 made by the Company and reflected in stipulations in two previous cases: Case
7 Nos. ER-2004-0570 and EO-2005-0263. Empire disagrees with Ms.
8 Meisenheimer’s position because the Company believes all issues regarding those
9 stipulations, at least as they relate to the abandonment of Empire’s previous Interim
10 Energy Charge and the Company’s ability to request an FAC in this case, were
11 decided by the Commission in Empire’s last rate case, Case No. ER-2006-0315. In
12 addition, because Empire believes the arguments that Ms. Meisenheimer has raised
13 are legal arguments, I will not be providing any rebuttal testimony addressing Ms.
14 Meisenheimer’s claims.

15 **BAD DEBT EXPENSE**

16 **Q. HAVE YOU REVIEWED THE STAFF ADJUSTMENT TO BAD DEBT**
17 **EXPENSE?**

18 A. Yes. I have reviewed the adjustment to bad debt expense discussed at page 51 of
19 the Staff’s report and reviewed the supporting workpapers provided by Staff.

20 **Q. DO YOU AGREE WITH THE STAFF ADJUSTMENT?**

21 A. No.

22 **Q. WHY?**

23 A. The Staff adjustment to uncollectible expense did not take into account the level of

1 bad debt expense that is associated with the Staff's recommended increase in
2 revenue.

3 **Q. WHAT PROCESS DID THE STAFF USE TO ADJUST BAD DEBT**
4 **EXPENSES?**

5 A. The Staff adjustment incorporates a five-year history of bad debt activity to arrive
6 at an effective uncollectible rate of 0.543072 percent. This rate was then applied to
7 the annualized revenue produced by the current rates to arrive at a normalized level
8 of bad debt expenses for purposes of the overall jurisdictional revenue requirement.
9 This part of the process used by the Staff is acceptable to Empire. What is missing
10 from the analysis is the application of the effective uncollectible rate to the
11 recommended increase in rates.

12 **Q. HOW SHOULD THE STAFF'S UNCOLLECTIBLE RATE BE APPLIED**
13 **TO THE PROPOSED RATE INCREASE?**

14 A. It should be applied in the same manner that is used to reflect the additional income
15 taxes that are associated with the rate increase. For example if \$10,000,000 of
16 additional revenue is recommended this will need to be increased by the effect of
17 the Staff's bad debt factor to arrive at the overall net increase required of
18 \$10,000,000. Using the Staff's effective bad debt rate of 0.543072%, this
19 calculation would result in an overall increase of \$10,054,604. The net result is a
20 \$10,000,000 increase after deducting the \$54,604 in additional bad debts that will
21 be incurred.

22 **DEMAND-SIDE MANAGEMENT**

23 **Q. HAVE YOU READ THE DIRECT TESTIMONY OF BRENDA WILBERS**

1 **THAT WAS FILED ON BEHALF OF THE MISSOURI DEPARTMENT OF**
2 **NATURAL RESOURCES (“DNR”) IN THIS CASE?**

3 A. Yes.

4 **Q. DO YOU AGREE WITH MS. WILBERS’ STATEMENT AT PAGE 7 LINE 2**
5 **THAT EMPIRE IS NOT MAKING SUBSTANTIAL PROGRESS**
6 **TOWARDS MEETING ANY OF DNR’S PROPOSED ENERGY**
7 **EFFICIENCY TARGETS?**

8 A. No, I do not. First, the DNR DSM budget targets included in the Regulatory Plan,
9 Case No. EO-2005-0263, were not adopted by the Customer Program Collaborative
10 (“CPC”) so any comparison by DNR to those particular budget targets is not
11 relevant. The DSM programs and the related budgets that are relevant to this case
12 were established by the CPC, and Empire has made considerable progress towards
13 the implementation of the programs authorized by the CPC. Empire’s witness
14 Sherry McCormack will present more details concerning Empire’s DSM programs
15 in her rebuttal testimony in this case. Finally, Ms. Wilbers suggestions in the DSM
16 area are better suited for consideration at the CPC, not this rate case.

17 **Q. MS. WILBERS MAKES REFERENCE TO AN EMPIRE INTEGRATED**
18 **RESOURCE PLANNING (“IRP”) CASE, EO-2008-0069 IN HER DIRECT**
19 **TESTIMONY AT PAGE 7, AND CLAIMS THAT IT IS RELEVANT TO**
20 **THIS RATE CASE, DO YOU AGREE WITH THIS POSITION TAKEN BY**
21 **DNR?**

22 A. No. Empire’s IRP case, which is ongoing, has nothing to do with Empire’s rate
23 case and any concerns DNR has about Empire’s IRP should be addressed in the

1 IRP case. Ms. Wilbers indicates at page 7 line 15 that the parties to the IRP case
2 are currently in negotiations to resolve deficiencies in the IRP filing. While I can
3 agree that the parties are in the process of resolving differences of opinion on the
4 contents of the compliance report Empire filed in the IRP proceeding, there has not
5 been a finding by the Commission that Empire's IRP compliance filing in EO-
6 2008-0069 is deficient at this point.

7 **VEGETATION AND INFRASTRUCTURE MANAGEMENT COSTS**

8 **Q. DOES EMPIRE HAVE A RECOMMENDATION ASSOCIATED WITH**
9 **THE COMMISSION'S PROPOSED RULES ON VEGETATION**
10 **MANAGEMENT AND INFRASTRUCTURE?**

11 A. Yes. As outlined in Empire witness Palmer's testimony, the implementation of a
12 new Commission vegetation management could have a significant financial impact
13 upon Empire, with vegetation management expenditures increasing by over six
14 times depending upon the final draft of the rule. The proposed rule are closer to
15 becoming official and Empire believes that will incur around an additional \$4 to \$6
16 million per year to comply with these new rules when it existing internal
17 procedures are modified to comply with the Commission's rules in both of these
18 areas.

19 **Q. WHAT WAS THE STAFF'S POSITION ON HOW TO ADDRESS THE**
20 **INCREASE IN VEGETATION MANAGEMENT COSTS THAT WILL**
21 **COME ABOUT DUE TO THE NEW COMMISSION RULE ON**
22 **VEGETATION MANAGEMENT?**

23 A. The Staff at page 50 of its Staff Report indicated that it is willing to discuss the use

1 of a cost tracking mechanism similar to a procedure used by AmerenUE. The
2 tracking mechanism employed by AmerenUE came out Case ER-2007-0002.
3 Empire is prepared to discuss the implementation of a similar tracking mechanism
4 with the Staff.

5 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

6 A. Yes.

LIST OF SCHEDULES

| Schedule No. | <u>Description</u> |
|-------------------------|--------------------------|
| Rebuttal Schedule WSK-1 | Analysis of Energy Costs |