

Exhibit No.

Issue: Staff Corrections, Healthcare, Life
Insurance, On-System Municipal
Sales, Retail Revenue and Rate
Design

Witness: Jayna R Long

Type of Exhibit: Rebuttal Testimony

Sponsoring Party: Empire District

Case No. ER-2006-0315

Before the Missouri Public Service Commission

Rebuttal Testimony

of

Jayna R. Long

July 2006

TABLE OF CONTENTS
OF
JAYNA R. LONG
ON BEHALF OF
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION

<u>SUBJECT</u>	<u>PAGE</u>
INTRODUCTION.....	1
EXECUTIVE SUMMARY.....	2
STAFF CORRECTIONS.....	4
HEALTHCARE AND LIFE INSURANCE.....	8
INCENTIVE PAYROLL.....	10
ON-SYSTEM MUNICIPAL SALES.....	12
RETAIL REVENUE.....	13
RATE DESIGN.....	15

REBUTTAL TESTIMONY
OF
JAYNA R. LONG
ON BEHALF OF
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2006-0315

1 **I. INTRODUCTION**

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

3 A. My name is Jayna R. Long. My business address is 602 Joplin Street, Joplin,
4 Missouri.

5 **Q. BY WHOM ARE YOU EMPLOYED?**

6 A. I am employed by The Empire District Electric Company. (“Empire” or
7 “Company”).

8 **Q. ARE YOU THE SAME JAYNA R. LONG THAT FILED DIRECT**
9 **TESTIMONY IN THIS CASE?**

10 A. Yes, I am.

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

12 A. I am filing this testimony in response to corrections that have been agreed to by
13 The Missouri Public Service Commission Staff (“Staff”) but have not yet been
14 reflected in documents filed with the Commission. In addition, I will address:
15 1)the proposed Staff adjustments to healthcare and life insurance; 2)the Staff
16 adjustments made to incentive payroll; 3)the Staff level of On-System Municipal

1 sales; 4)the Staff adjustments to retail revenue; and, 5) the rate design
2 recommended by the Company in response to OPC and Staff recommendations.
3

4 **II. EXECUTIVE SUMMARY**

5 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS**
6 **CASE BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION**
7 **(“COMMISSION”)?**

8 A. This testimony addresses corrections that have been agreed informally to by Staff,
9 but have not been filed with the Commission. In addition it addresses the
10 proposed Staff adjustments to healthcare and life insurance, the Staff adjustments
11 made to incentive payroll, the Staff level of On-System Municipal sales, the Staff
12 adjustments to retail revenue and the rate design recommended by the Company
13 in response to OPC and Staff’s recommendations.

14 **Q. PLEASE DISCUSS THE STAFF “CORRECTIONS.”**

15 Staff has indicated to the Company that it has made three corrections to its version
16 of Empire’s Missouri revenue requirement. These corrections include the Staff
17 adjustment to normalize the State Line Combined Cycle maintenance contract, the
18 correction to the allocation factor used to allocate payroll costs between capital
19 and expense, and a correction to the jurisdictional allocation factor the Staff used
20 on taxes other than income taxes.

21 **Q. WHAT IS EMPIRE’S RESPONSE?**

22 A. Empire agrees with the corrections for the first two items, but not the third.

23 **Q. PLEASE EXPLAIN.**

1 A. While Empire believes this is an improvement in the Staff allocation factor, it
2 does not complete the correction process associated with this particular allocation
3 factor and Empire does not completely accept the Staff revised jurisdictional
4 allocation factor. Empire recommends that its method be used for allocating taxes
5 other than income taxes.

6 **Q. PLEASE DISCUSS THE OTHER ISSUES YOUR TESTIMONY**
7 **ADDRESSES.**

8 A. They are as follows:

- 9 ▪ Staff made an adjustment to decrease healthcare expenses at Empire due
10 to “declining expenses”. Empire does not believe the healthcare cost to be
11 “declining” nor does the Company agree with Staff’s method to normalize
12 the healthcare cost within the test year and therefore no adjustment was
13 necessary.
- 14 ▪ The Staff made an adjustment for life insurance expense as a result of a
15 one time premium decrease. Empire does not consider this one time
16 decrease to be normal and therefore should not be used to normalize the
17 test year.
- 18 ▪ Staff inadvertently duplicated its adjustment to eliminate the costs
19 associated with the stock option portion of the MIP plan. Staff has
20 indicated that it will reverse the duplicate entry of \$248,739. Empire
21 accepts the correction.

- 1 ▪ The Staff did not incorporate an adjustment for the growth of the
2 municipal customers and therefore understated the total Company NSI in
3 its rate case filing.

4 The total Company fuel and purchased power is derived from the total
5 Company NSI. Furthermore, the total Company fuel and purchased power
6 expense are allocated to jurisdictions. If the total Company fuel and
7 purchased power are understated the Missouri jurisdictional fuel and
8 purchased power will be understated as well. The Company recommends
9 that a two percent growth rate be used for this class of customers based on
10 a customer class regression.

- 11 ▪ Empire disagrees with the weather normalization adjustments calculated
12 by Staff. As a result of the difference in the weather normalization, the
13 other Staff revenue adjustments are compounded causing a further
14 difference between Empire and Staff in the growth and rate increase
15 adjustment. Empire disagrees with the customer response functions used
16 by Staff in their weather model.

- 17 ▪ With respect to rate design, Empire continues to support the equal
18 percentage increase to each rate class.

19 **III. STAFF CORRECTIONS**

20 **Q. PLEASE DESCRIBE THE CORRECTIONS THAT STAFF HAS MADE**
21 **TO ITS REVENUE REQUIREMENT POSITION, BUT HAVE NOT YET**
22 **BEEN REFERENCED IN FILED DOCUMENTS.**

1 A. Staff has indicated to the Company that it has made three corrections to its version
2 of Empire's Missouri revenue requirement. The corrections to the Staff case have
3 not been filed with the Commission as of the date of this rebuttal testimony.
4 These corrections include the Staff's adjustment to normalize the State Line
5 Combined Cycle maintenance contract, the correction to the allocation factor used
6 to allocate payroll costs between capital and expense, and a correction to the
7 jurisdictional allocation factor the Staff used on taxes other than income taxes.

8 **Q. PLEASE DESCRIBE THE STAFF'S ADJUSTMENT TO THE STATE**
9 **LINE COMBINED CYCLE MAINTENANCE CONTRACT.**

10 A. Staff's adjustment S-34.4 for (\$1,573,759) purports to adjust test year expense to
11 more accurately reflect the actual maintenance costs associated with Empire's
12 contract with Siemens Westinghouse Power Corporation ("Siemens") for
13 maintenance of the State Line Combined Cycle turbine for the twelve months
14 ending March 2006. In doing its analysis of the costs associated with this
15 maintenance contract Staff incorrectly identified the amount of expense recorded
16 by the Company in its December 31, 2005 year ending income statement. The
17 Company has provided additional information concerning this contract to the
18 Staff. The additional information provided to the Staff displays the correct
19 amount of this expense as reported by the Company for the twelve months ending
20 December 31, 2005. Staff has reviewed the additional information and indicated
21 it will revise its filed adjustment of (\$1,573,759) to a corrected amount of
22 (\$105,710). Schedule JRL-1 is a spreadsheet received via email from Staff

1 witness Boateng on July 18, 2006 identifying this change. Empire agrees with the
2 Staff's revised adjustment of (\$105,710).

3 **Q. PLEASE EXPLAIN THE REVISION STAFF HAS INDICATED IT WILL**
4 **MAKE TO THE FACTOR USED TO ALLOCATE LABOR BETWEEN**
5 **CAPITAL AND EXPENSE.**

6 A. Staff originally derived its allocation factor between capital and operating expense
7 by performing a five-year historical analysis of electric Operations and
8 Maintenance ("O&M") expense. The O&M allocation factor was used in the
9 payroll annualization adjustment and the FAS 87 adjustment to rate base. Staff's
10 original filing contained an O&M allocation factor of 72.56%. Upon further
11 review of the calculation, Staff has indicated it will revise the O&M allocation
12 factor to 75.00%. This revision is shown in Schedule JRL-2, a work paper
13 prepared by Staff witness McMellen. Empire accepts the revision to the Staff
14 O&M allocation factor, which will result in additional revenue requirement when
15 applied to both the payroll annualization adjustment and FAS 106 adjustment to
16 rate base.

17 **Q. PLEASE DESCRIBE THE CHANGES STAFF HAS INDICATED IT WILL**
18 **MAKE TO THE JURISDICTIONAL ALLOCATION FACTOR FOR**
19 **TAXES OTHER THAN INCOME TAXES.**

20 A. Taxes other than income taxes includes three components: property tax, payroll
21 tax, and franchise taxes. The original factor used by Staff in its filing to allocate
22 the Missouri jurisdictional portion of taxes other than income taxes was the O&M
23 payroll composite allocation factor. As shown in the work papers of Staff witness

1 Eaves (Schedule JRL- 3), this factor was derived by taking the Missouri O&M
2 payroll divided by total Company O&M payroll. Thus, Staff incorrectly
3 calculated the factor for all components based on total Company payroll. Staff
4 has indicated it will adjust this allocation factor to 85.47%. This is an
5 improvement in the Staff allocation factor, but it does not completely correct this
6 particular allocation factor and Empire does not accept the Staff revised
7 jurisdictional allocation factor.

8 **Q. PLEASE EXPLAIN WHY EMPIRE DOES NOT ACCEPT STAFF'S**
9 **REVISED JURISDICTIONAL ALLOCATION FACTOR.**

10 A. As previously mentioned, Empire separates taxes other than income taxes into
11 three components before allocating the Missouri portion: property taxes, payroll
12 taxes, and franchise taxes. The property tax component is then allocated to the
13 Missouri retail jurisdiction based upon total plant in service. Property taxes
14 constitute approximately 55% of the other taxes. Payroll taxes are allocated to the
15 Missouri retail jurisdiction based upon the total of production, transmission,
16 distribution, customer accounts, customer assistance and the sales expense
17 accounts. Payroll taxes constitute approximately 10% of taxes other than income
18 taxes. The remaining 35% of taxes other than income taxes is related to franchise
19 taxes. Because these tax expenses are directly related to jurisdictional retail
20 revenue, Empire directly assigns these expenses by jurisdiction. Empire
21 recommends the Commission accept the Company's methodology for the
22 allocation of other taxes to the Missouri jurisdiction, rather than the Staff's

1 proposal to use a single allocation factor. The change to a three factor method
2 will result in an increase in the Missouri revenue requirement of \$303,683.

3 **IV. HEALTHCARE AND LIFE INSURANCE**

4 **Q. PLEASE EXPLAIN THE ADJUSTMENTS STAFF MADE TO THE**
5 **HEALTHCARE EXPENSE.**

6 A. Staff's adjustment S-85.7 for (\$1,241,734) was made to reflect what Staff
7 characterizes as the "declining" healthcare expenses at Empire. Empire does not
8 believe its healthcare costs are declining. The Company also does not agree with
9 Staff's methodology to normalize the healthcare cost within the test year.

10 **Q. PLEASE EXPLAIN WHY THE COMPANY DISAGREES WITH STAFF'S**
11 **NORMALIZATION METHODOLOGY.**

12 A. Staff's healthcare adjustment was based on an annualization of first quarter 2006
13 healthcare expense. Using a single quarter to annualize such a significant expense
14 is not reasonable because it ignores the volatility of the expense associated with
15 health care claims. For instance, a single quarter may be fairly mild with respect
16 to participant utilization of the medical plan, while another quarter within the year
17 may be impacted by several large claims.
18 Participant healthcare claims were down in the first quarter of 2006. In part, this
19 was due to the Company's change in third party administrators ("TPA"). The
20 new TPA did not pay a normal amount of claims during the initial set up time in
21 January.

1 **Q. PLEASE IDENTIFY OTHER FACTORS THAT WILL DISTORT THE**
2 **RESULT PRODUCED BY THE STAFF'S NORMALIZATION**
3 **METHODOLOGY.**

4 A. The Company has made several changes to its healthcare program in an effort to
5 reduce the rate of increase in healthcare costs. These changes include lowering
6 contracted provider rates, increasing employee cost sharing, step therapy, and
7 introducing specialty pharmacy programs in the prescription drug program.

8 **Q. THE STAFF SINGLED OUT THE WELLNESS PROGRAM AS A**
9 **REASON FOR DECLINING HEALTHCARE COSTS AT EMPIRE (PAGE**
10 **19 OF STAFF WITNESS MCMELLEN'S TESTIMONY). DO YOU**
11 **AGREE WITH THIS CONTENTION?**

12 A. No. Empire anticipates that in the long-term, the wellness program will result in a
13 reduction in the rate of increase in healthcare costs, not an outright decline in
14 healthcare costs. However, the near term impact of the wellness program is
15 expected to be an increase in healthcare cost as participants take advantage of
16 routine annual exams aimed at detecting potential medical conditions at an earlier
17 stage. This near term increase in costs is expected to help avoid the more
18 expensive treatments associated with conditions that are not detected earlier.

19 **Q. WHAT ADJUSTMENT FOR HEALTHCARE DOES THE COMPANY**
20 **BELIEVE SHOULD BE MADE IN THIS RATE CASE?**

21 A. The Company believes the test year level of expense in this instance is
22 appropriate and that no downward adjustment is necessary. The Company

1 believes this level of expense best reflects the successes that have been achieved
2 in the efforts to mitigate the upward trend in healthcare cost.

3 **Q. WHAT ADJUSTMENT DID STAFF MAKE FOR LIFE INSURANCE**
4 **EXPENSE?**

5 A. The Staff's adjustment S-85.8 of (\$170,955) for life insurance expense was a
6 result of a one-time premium decrease. The one time decrease occurred in
7 November 2005. The Company's life insurance carrier, Standard Insurance, has
8 informed the Company that rates will be increasing effective January 1, 2007.

9 **Q. WHAT ADJUSTMENT DOES THE COMPANY PROPOSE?**

10 A. Due to the impending premium increase, the Company believes the test year level
11 of \$258,237 in expense is appropriate and that no adjustment is necessary.

12 **V. INCENTIVE PAYROLL**

13 **Q. PLEASE DESCRIBE EMPIRE'S INCENTIVE COMPENSATION PLANS.**

14 A. Empire has three incentive compensation plans: the management incentive
15 compensation plan ("MIP") for executives of the Company; a compensation
16 incentive award program for salaried non-executive employees; and the "Lighting
17 Bolts" offering certain employees lump-sum payment bonuses.

18 **Q. ARE YOU ADDRESSING STAFF'S ADJUSTMENTS TO ALL THREE OF**
19 **THE PLANS?**

20 A. No. Company witness Bauer will address the Staff's adjustments made to all
21 three of the plans in detail. My testimony will address what appears to be a
22 duplicate adjustment proposed by Staff. This resulted in a double elimination of
23 the costs associated with the stock option portion of the MIP plan.

1 **Q. PLEASE EXPLAIN THE DUPLICATION.**

2 A. Staff made a series of adjustments related to the employee compensation plans,
3 including incentive compensation. The first set of Staff's adjustments was used to
4 annualize the payroll for the test year. The second Staff adjustment S-79 was
5 used to remove the stock option portion of the MIP from the test year level of
6 \$248,739.

7 **Q. PLEASE EXPLAIN HOW THE DUPLICATION OCCURRED.**

8 A. The first set of Staff's adjustments annualized the Empire payroll. This first set of
9 adjustments also included the Staff recommended allowance for all three of the
10 Company's incentive compensation plans. Staff then compared the amount of
11 annualized payroll, including its recommended allowance for incentive
12 compensation, to the amount of payroll expense recorded during the year ended
13 December 31, 2005. The difference between these amounts was the
14 recommended Staff adjustment. In this first payroll annualization adjustment,
15 Staff did not include any of the stock option portion of the MIP. Thus, the first
16 Staff adjustment eliminated the stock option portion of the MIP in its entirety and
17 there is no need to make an additional adjustment to operating expenses to
18 eliminate this particular incentive compensation cost again. However, that is not
19 what the Staff did when it put its case together. The Staff made an additional
20 adjustment to disallow the stock option portion of the MIP for \$248,739. This
21 second Staff adjustment created a duplicate elimination of this incentive cost.

22 **Q. WHAT DOES EMPIRE RECOMMEND?**

1 A. Empire has worked with Staff on this issue and they have agreed to reverse the
2 duplicate entry of \$248,739.

3 **VI. ON-SYSTEM MUNICIPAL SALES**

4 **Q. WHAT ARE ON-SYSTEM MUNICIPAL SALES?**

5 A. Empire serves four on-system municipal customers. The rates charged to these
6 customers are regulated by the Federal Energy Regulatory Commission
7 (“FERC”). Although the revenues from these customers are not included in the
8 Missouri revenue requirement, the sales made to these customers impact the total
9 Company net system input (“NSI”) and therefore the total fuel and purchased
10 power expense filed in this rate case.

11 **Q. PLEASE EXPLAIN THE IMPACT THIS ISSUE HAS ON THE MISSOURI**
12 **JURISDICTIONAL REVENUE AND EXPENSE.**

13 A. The total Company fuel and purchased power expense is derived from the total
14 Company NSI. Furthermore, total Company fuel and purchased power expense is
15 allocated to each of the several jurisdictions of Empire. If the total Company fuel
16 and purchased power expense is understated, the Missouri jurisdictional fuel and
17 purchased power will be understated as well.

18 **Q. DID STAFF INCLUDE THESE CUSTOMERS IN ITS PRODUCTION**
19 **COST SIMULATION AND IN ITS PROJECTION OF NSI COSTS?**

20 A. Yes. Staff made an Adjustment to NSI for (4,075,784) kWh to weather-normalize
21 the on-system municipal sales. However, Staff did not incorporate an adjustment
22 for the growth of these customers as it does with all of the classes of on-system

1 customers. As a result, Staff has understated the total Company NSI in its rate
2 case filing.

3 **Q. WHAT GROWTH RATE DOES EMPIRE RECOMMEND FOR THIS**
4 **CLASS OF CUSTOMERS?**

5 A. The Company recommends that a two percent growth rate be used for this class of
6 customers. Empire has performed a regression analysis of these customers that
7 shows an annual growth of approximately two percent. The regression analysis
8 uses historical data for sales, degree days, and the year as variables to forecast
9 future growth. A projected growth rate of two percent appears to be consistent
10 with the rate of growth seen in prior years. Schedule JRL-4 contains the data
11 input and results of the regression.

12 **VII. RETAIL REVENUE**

13 **Q. WHAT STAFF RETAIL REVENUE ADJUSTMENTS DOES EMPIRE**
14 **DISPUTE?**

15 A. Empire disagrees with the weather normalization Adjustments S-1 amounting to
16 (\$3,498,117) calculated by Staff's witness Lange. As a result of the difference in
17 the weather normalization adjustments, the other Staff revenue adjustments are
18 erroneously compounded. For example, the Staff weather normalization
19 erroneously compounds the impact of the customer growth and rate increase
20 adjustments made by Staff.

21 **Q. PLEASE EXPLAIN WHY EMPIRE DISAGREES WITH STAFF'S**
22 **PROPOSED WEATHER NORMALIZATION.**

1 A. Empire disagrees with the customer response functions developed in Helm
2 (Electric Power Research Institute Hourly Electric Load Model) that is used by
3 both Staff and Empire to calculate the weather normalization adjustment. Empire
4 has retained Nexus Energy as a consultant to review the differences in the
5 customer response functions used by the Company and the Staff. Due to time
6 constraints associated with the rate case, Empire was unable to file rebuttal
7 testimony from the consultant.

8 **Q. HOW DOES STAFF'S WEATHER NORMALIZATION ADJUSTMENT**
9 **IMPACT THE CUSTOMER GROWTH AND RATE INCREASE**
10 **ADJUSTMENT?**

11 A. The customer growth (S-1) and rate increase (S-1) adjustments are both computed
12 based on weather-normalized sales. Because the starting point (i.e. the
13 normalized sales) for Empire and Staff are different, the results of the customer
14 growth and rate increase adjustments will be different as well. Thus, Staff's
15 higher normalized sales levels result in a customer growth adjustment of \$665,989
16 and rate increase adjustment of \$663,635 that are higher than those that Empire
17 would forecast at March 31, 2006.

18 **Q. DID EMPIRE ELIMINATE THE IMPACT OF IEC REVENUE FROM ITS**
19 **RATE FILING ON FEBRUARY 1, 2006?**

20 A. No. Unlike the Staff IEC elimination rate case, Empire's original rate filing
21 treated the IEC as a source of revenue and calculated its requested change to its
22 rates accordingly. Although Empire does not necessarily disagree with Staff's
23 method of IEC presentation, it does differ from the methodology and presentation

1 used by Empire and will create an additional gap between the parties in terms of
2 the overall revenue produced by existing rates, including the IEC.

3 **Q. HOW DOES THE IEC NORMALIZATION METHODOLOGY DIFFER**
4 **BETWEEN EMPIRE AND STAFF?**

5 A. Empire chose to normalize the IEC revenue by applying the IEC rate to the
6 normalized, adjusted total Missouri retail sales. This reduced the amount of
7 revenue increase requested by the Company in this rate case. The Staff chose to
8 eliminate the IEC from the test year. Therefore, the revenue requirement
9 presented by Staff represents the increase in base electric rates, excluding IEC
10 revenue.

11 **Q. DOES THIS IMPACT THE RATE CASE?**

12 A. Not really. This is merely a presentation difference. If Empire had chosen to
13 present its filing in a similar manner as Staff, the additional base electric revenue
14 required would increase approximately \$8 million. Empire only addresses this to
15 assist the Commission when it compares the revenue requirement presented by
16 the Company and by Staff.

17 **VIII. RATE DESIGN**

18 **Q. WHAT RATE DESIGN DID EMPIRE RECOMMEND IN ITS FILING?**

19 A. In Company witness Keith's direct testimony, page 22 lines 12-15, it was
20 recommended that "due to the very short life of the rates coming out of the last
21 rate case, ER-2004-0570, Empire has proposed to spread the rate increase to all of
22 the charges in its tariffs in the form of an across-the-board increase, with an equal
23 percentage increase to each rate class."

1 **Q. DOES EMPIRE MAINTAIN THIS OPINION?**

2 A. Yes, Empire continues to support the equal percentage increase to each rate class.

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

4 A. Yes.