STATE OF MISSOURI

PUBLIC SERVICE COMMISSION

TRANSCRIPT OF PROCEEDINGS

HEARING

June 1, 2001
Jefferson City, Missouri
Volume 7

In the Matter of The Empire District Electric Company's Tariff Sheets Designed to Implement a General Rate Increase for Retail Electric Service Provided to Customers in the Missouri Service Area of the Company.) Case No. ER-2001-299

BEFORE:

VICKY RUTH, Presiding,
REGULATORY LAW JUDGE.

SHEILA LUMPE, Chair,
CONNIE MURRAY,
KELVIN SIMMONS,
STEVE GAW,
COMMISSIONERS.

REPORTED BY:

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ASSOCIATED COURT REPORTERS, INC.

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P R O C E E D I N G S

JUDGE RUTH: Good morning. Today's date is June 1st, 2001. It's 8:30. We are ready to take up the hearing. We will begin with the issue of capital structure, rate of return.

Mr. Dottheim, did you have a housekeeping or preliminary matter?

MR. DOTTHEIM: Yes, just a couple of items. On Tuesday when you took entry of appearances, I failed to make an entry of appearance for Keith Krueger of the General Counsel's Office. So I would like to do so at this time, orally do that.

And another matter regarding the supplemental testimony that the Staff will be filing relating to a change of position regarding the fuel and purchased power expense. The Staff is prepared to file, along with the testimony, a pleading requesting that the testimony be received as late-filed.

If you would wish us to proceed in some other manner, we could do that also, but if that would be adequate, we would proceed in that manner.

JUDGE RUTH: No. It would be helpful if you do it like that, file a motion to accept the late pleading, and the other parties do the same.

MR. SWEARENGEN: That's also the intention of the Company. We would do the same thing. We will file our own motion seeking leave to file the additional testimony.

JUDGE RUTH: That sounds good. Thank you.

MR. DOTTHEIM: And the one other item that we addressed yesterday, Mr. Swearengen and I, on the issue that was originally scheduled to be heard yesterday, incentive compensation, the Staff is preparing the supplemental surrebuttal testimony of Jan C. Fischer, and we should have that filed by the end of today and have copies to the parties. It is not extensive. I think it's something right now on the range of something like eight pages.

JUDGE RUTH: And as I've mentioned before, I'd appreciate it if you provide me with a direct copy in addition to what you file with records.

MR. DOTTHEIM: Yes.

JUDGE RUTH: Thank you.

MR. DOTTHEIM: I think there's possibly one other preliminary matter. Mr. Frey, I think, may have a question or a progress report for you regarding the Revised Statement of Positions and List of Issues.

JUDGE RUTH: Okay. Mr. Frey?

MR. FREY: Thank you, your Honor. We put together a draft List of Issues and have very late last night only circulated it for the review of the parties. I'm sure there are going to be a series of edits to that list, but I believe we're fairly close to filing that document. I think it's possible that later on in the proceeding we may have a document that we could show you per our conversation with you yesterday prior to filing.

I do want to clarify one thing, though, as to whether or not we have the option to include Statements of Positions with that document. My guess right now is that we won't do that, that the individual parties will file Statements of Positions against those issues, but if we should decide to do that, is that an acceptable approach?

JUDGE RUTH: It's acceptable whether you do separate or joint.

MR. FREY: Okay. Thank you very much, your Honor.

JUDGE RUTH: Okay. Thank you for that progress report.

Are there any other preliminary or housekeeping motions?

(No response.)

Okay. Seeing none.

Empire, would you please call your witness.

MR. SWEARENGEN: I would call Mr. Murry to the stand at this time, Mr. Donald A. Murry.

JUDGE RUTH: Good morning, Mr. Murry. When you get seated, if you would please raise your right hand.

(Witness sworn.)

JUDGE RUTH: Okay. Thank you. Please proceed.

MR. SWEARENGEN: Thank you, your Honor.

DONALD A. MURRY testified as follows:

DIRECT EXAMINATION BY MR. SWEARENGEN:

Q. Would you state your name for the record, please.

A. My name is Donald A. Murry.

Q. Mr. Murry, by whom are you employed and in what capacity?

A. I am currently a professor emeritus at the University of Oklahoma, and I'm vice president of C.H. Guernsey & Company in Oklahoma City.

Q. And what is the business of that company generally?

A. It's a consulting engineering firm. I'm obviously an economist. We're a group of economists, financial analysts.

Q. And do you currently hold any academic positions?

A. I'm a professor emeritus, University of Oklahoma.

Q. And currently teaching there?

A. I'm not currently teaching. Well, I do teach some programs. Emeritus is a semi-honorary quasi-retired type of position.

Q. Okay. Thank you. Did you cause to be prepared for purposes of this proceeding certain direct, rebuttal and surrebuttal testimony in question and answer form?

A. Yes, I have.

Q. And is it your understanding that your direct testimony has been marked for purposes of identification as Exhibit 13?

A. Yes.

Q. And do you have a copy of that testimony with you this morning?

A. Yes.

Q. And do you need to make any changes in that testimony at this time?

A. I have a couple typographical changes.

Q. Why don't you call those to everyone's attention, if you would, please?

A. On page 6, line 1, the 1999 should be 2000. That's actually a correction we did not get edited out, so it popped up in a couple of places. The same thing on Schedule DAM-1, the words 1999 should be the words 2000, or the date 2000, and also on Schedule DAM-2 and also on DAM-19.

Q. The same change?
A. Same change. 1999 should be 2000.
Q. So that's Schedule 1, Schedule 2?
A. And Schedule 19.
Q. And Schedule 19?
A. That's correct. And then there's a -- because of the rebuttal testimony, the numbering, I ended up with two Schedules DAM-20. So I would propose in the rebuttal changing that to DAM-20-R, so to distinguish the 20 from my direct testimony from -- the DAM-20 in the direct testimony from the DAM-20 in rebuttal.
Q. So in other words, if someone's looking at all of your testimony, they're going to see two DAM-20s?
A. Exactly.
Q. And do you want to once again state on the record what you propose to do to clear that up?
A. I would change the one in rebuttal to DAM-20-R.
Q. Are there any other suggested changes with respect to your rebuttal testimony?
A. No, there are not.
Q. With respect to your surrebuttal, which I understand has been marked as Exhibit 26, are there any corrections or changes that you need to make there?
A. There's no change. There's a clarification,

and I -- I think I provided enough information, but I did not point it out in the testimony.

Q. What is that clarification?

A. Schedule 36 is a copy of a sheet from a publication Ibbotson Associates, and in the testimony it says, Evaluation Edition 2000 Yearbook, and if you notice -- and that is Schedule -- that's actually page 2. The cover sheet of that is page 2 of Schedule 36, and notice that does say the 2000 Yearbook.

The bottom of that page says Value Edition 1999 Yearbook and I just want to point that out. It did come from the 2000 Yearbook, and I presume that's an typographical error by Ibbotson Associates.

Q. So in other words, on Schedule DAM-36 on page 1 it says, Valuation Edition 1999 Yearbook?

A. At the bottom.

Q. At the bottom, but it's your testimony that that actually has come out of the Valuation Edition 2000 Yearbook?

A. That's correct, and the title page is page 2.

Q. And do you have that Valuation Edition 2000 Yearbook with you today in the hearing room?

A. Yes, I do.

Q. One last housekeeping matter perhaps with respect to Schedule DAM-24, which I believe is attached to your rebuttal testimony, Exhibit No. 16. On the copy that I have, and I think the copy perhaps provided to the Commission and the other parties, the bottom half of that schedule is missing.

It's my understanding that we have provided not a corrected copy, but I should say a complete copy of that schedule, and it has been marked separately as Exhibit 17. I just want to state that for the record, and that's my understanding of what we've done here. The complete Schedule DAM-24 has been marked as Exhibit 17.

Having said that, Mr. Murry, if I asked you the questions that are contained in your direct, rebuttal and surrebuttal testimonies this morning, would your answers as corrected be substantially the same?

A. Yes, they would.

Q. And would they be true and correct to the best of your knowledge, information and belief?

A. Yes.

MR. SWEARENGEN: With that, your Honor, I would tender the witness for cross-examination and offer Exhibits 13, 16, 26 and the corrected schedule which is DAM-24 and has been marked as Exhibit 17.

Thank you.

JUDGE RUTH: Okay. Mr. Swearengen has offered these four exhibits. Do the parties have any objection to them being admitted?

MR. KRUEGER: I don't have any objection, your Honor, but I think in his questioning Mr. Swearengen referred to rebuttal testimony as Exhibit 26. I think the correct reference is 16.

MR. SWEARENGEN: That's right.

JUDGE RUTH: Yes. I have Exhibit 13 as the direct testimony, Exhibit 16 the rebuttal, Exhibit 26 the surrebuttal, and Exhibit 17 is the corrected schedule or the complete schedule.

Okay. Seeing no objections, those four exhibits will be admitted into the record.

(EXHIBIT NOS. 13, 16, 17 AND 26 WERE RECEIVED INTO EVIDENCE.)

JUDGE RUTH: Praxair, would you like to begin cross-examination?

MR. CONRAD: Sure.

CROSS-EXAMINATION BY MR. CONRAD:

Q. Good morning, Mr. Murry or Dr. Murry, whatever the case may be.

A. Good morning.

Q. Did I understand that you had testified in the merger proceeding?

A. No.

Q. And I was also unclear in rereading your testimony last night, it seemed that you had spent a lot of time on Mr. Broadwater's testimony. Is Mr. Broadwater a witness in this case?

A. No, he's not, to my knowledge.

Q. Just a couple of quick things. Let's look at Exhibit 16, page 12. I wanted to check a couple of things with you if I was clear in understanding what your testimony is.

Look at the bottom of 12. The question begins at line 17, kind of carries over a little bit in the answer to the top of the next page. Are you there, sir?

A. Not quite. Page 12?

Q. Yes, sir.

A. Line, please?

Q. 17.

A. I have it.

Q. Now, the question that's there is you mentioned the fuel price pass-through provisions are a risk to Empire. Did I read that correct?

A. Yes.

Q. Do you mean in the question -- and I understand how this thing goes, that you really write the questions yourself. Do you mean to say that the absence of a fuel price provision is a risk to Empire?

A. Yes, that would be a fair characterization.

It's the provision applying to fuel price.

Q. So you'd agree with that correction, then?

A. No. I don't think it's necessary. I agree with the interpretation. I wouldn't change the language because I was referring to the provisions applying to pass-throughs as it's done in regulation.

Q. But the point of that, I guess, is that because there is no fuel clause or fuel pass-through or fuel rider by whatever name, that the risk to the company is higher; is that correct?

A. There is a differential in the risk when fuel is passed directly through to rates than there is if it's not, as I understand the policy in Missouri.

Q. What is that differential?

A. It's in the minds of the investors. The concept of risk here is the expectation on the part of the investors, what they can anticipate or whether or not they will achieve their investment objectives. And that risk is a level of uncertainty, and since there is a difference in provision, there's a difference in risk or perceptions of the likelihood of that recovery.

Q. Have you quantified that?

A. I have not.

Q. Would it be possible to do so?

A. I think it would be possible. I'd want to think about the methodology in doing that. Because of the limited number of jurisdictions in which there is such a provision, it would almost be limited to Missouri and perhaps a few other locations or special cases.

Then there's a length of time when you'd have to decide whether you're going to make that analysis as a cross section analysis among states or whether you would make it over time and then the question of history.

So I'd have to think about that methodology. It's certainly possible.

Q.   Conversely, if Missouri had a fuel charge, fuel pass-through, whatever the terminology, then that perception of that differential wouldn't exist, right?

A.   I don't think it would be a perception of differential, that's correct.

Q.   And that would be true if one particular company under Missouri regulation was able to negotiate something akin to a fuel rider; would that be true?

A.   I would want to know the specifics of that. It would certainly -- certainly be information that you could review.

Q.   Now, I noticed -- I believe this is still, sir, in your Exhibit 16. Kind of moving backwards here because that's how they are in my file. Page 6, line 7, in the answer that starts there you make reference to the situation in California?

A. Yes.

Q. Is it your -- you're not testifying, I guess, that Empire is on the near bankruptcy or bankrupt state, are you?

A. No, I wasn't testifying to that.

Q. Do you think there's some differences between Missouri and California other than the geography?

A. Oh, absolutely.

Q. And there were some particular circumstances out in California that affected Pacific Gas & Energy and SoCalEd; wouldn't you agree?

A. Absolutely. The reference in that sentence is to the coverage numbers, not anything else, or in that answer.

Q. The last group of questions I want to check with you is your list of companies that you used on your DCF appear on page 8, probably other places, too, in your schedules, but at least they appear on page 8 of Exhibit 13. That's your direct.

A. Yes.

Q. Where does C.H. Energy Group do business?

A. It's mostly in New York.

Q. Cleco Corporation?

A. It's Louisiana.

Q. Would I be safe in assuming that Hawaiian Electric does business in Hawaii?
A. Yes, on several of the islands.
Q. Now, just focus on Hawaii for just a second, it's been a while since I've done any work on the gas pipeline that runs out there. Are you familiar with that gas pipeline?
A. There is no gas pipeline into Hawaii that you expect. Of course, there's gas service on the islands.
Q. How do they get the gas out there?
A. There's a gas manufacturing plant, and there's a barge. It's currently owned by Citizens Utility. There's a barge system that barges gas among the islands.
Q. And where does that come from?
A. It's -- I think it's a lique-- I think it comes from liquid petroleum gas manufacture.
Q. There on the islands?
A. As I recall, it's in -- the manufacturing plant is in Honolulu.
Q. Now, the manufacturing plant that you're indicating is in Honolulu and you indicated that they liquefy --
A. I'm saying use liquefied products to produce gas, as I recall the process.
Q. Those products apparently come from the large

number of oil and gas wells that are on Hawaii; is that correct?

A. No. I'm sure you know that's an island. That's not -- that's volcanic. There's not petro -- petroleum deposits.

Q. So those resources would come from where before they were liquefied?

A. They're shipped in from several locations, some Asia, some United States, or from the other parts of the United States.

Q. What about coal, does Hawaiian Electric use coal?

A. I don't think there is any coal processing or any coal generation, if that's your question.

Q. So that's, in your understanding at least, an all-gas utility that uses liquefied products are barged or shipped in over several thousand miles of Pacific ocean, correct?

A. Are we talking about the electric now rather than the gas company?

Q. I'm talking about Hawaiian Electric.

A. Hawaiian Electric I think is primary -- I think their primary generation is fuel oil.

Q. Is fuel oil?

A. Yes.

Q. And also --
A. You were asking about gas. I was telling you about the gas company, which the gas company is an affiliate of Citizens Utility.
Q. But Hawaiian Electric then uses the No. 6 or No. 2; that's what your understanding is?
A. That's my understanding. I don't recall if it's a hundred percent of generation. I think it's the primary generation.
Q. And, again, in that case, that would have to be barged or shipped in across several thousand miles of Pacific Ocean, correct?
A. There is fuel oil that comes in across the -- most of that I think would come from the United States.
Q. Kind of the only way you can get to an island, isn't it, either that or by air? Does FedEx ship oil as far as you know?
A. Not to my knowledge.
Q. And you see, I guess, in listing that in your DCF group that that company is comparable risk and should be used in your list of comparables --
A. The comparables --
Q. Let me finish my question, if I might, sir, before you answer it.
That you believe that that is a comparable

utility to Empire District that's located in the center of the United States that has a direct connection with a major interstate pipeline and has immediate access to coal supplies as well as oil? You don't see any difference between those companies?

A. No. I think you pointed out the differences in the generation and the characteristics of the system, and I was very much cognizant of that when I used that as a comparable company. I did not select Hawaiian Electric for any reason other than its -- that when I was looking at company size as an independent company, it was an appropriate company.

Of course, the financial market in the United States and Alaska and Hawaii as well as the contiguous states, the financial market is not a problem of shipping money across those miles. And it was my judgment that because we're looking at financial impact, that it was an acceptable representative company to look at.

But I was very aware of your concerns, and I am -- we actually have an office in Honolulu and I'm somewhat aware of the energy situation in Hawaii.

Q. Appreciate your office there. I have done some work with Hawaiian Electric, too.

MR. SWEARENGEN: Stew, are you licensed in Hawaii?

MR. CONRAD: Is that a question?
MR. SWEARENGEN: I'm just asking.
JUDGE RUTH: Off the record you-all can discuss that. We're ready for Mr. Coffman.
MR. COFFMAN: Thank you.
CROSS-EXAMINATION BY MR. COFFMAN:
Q. Good morning, Mr. Murry.
A. Good morning.
Q. My name is John Coffman. I represent the Office of the Public Counsel. I just have a few questions. Mr. Conrad took care of some of my questions with regard to fuel adjustment clauses and so forth.
Let me clarify. Do you believe that an electric company's portfolio of generation facilities, sources of generation that it uses to produce electricity is relevant in gauging business risk?
A. Yes.
Q. And investors consider such matters?
A. Yes.
Q. Is the business risk different for a company that relies on a nuclear power plant for generation as opposed to one that does not?
A. The answer -- the answer I think is yes, and let me answer that question yes but let me clarify. I believe that distinction -- that's a distinction I've looked

at over the years, and I think that the way the electric industry is moving currently, that differential is becoming less and less important in the eyes of investors. I think it's other risks that are probably more or less swamping the differential.

Q. But you would agree --

A. Let me kind of clarify. I don't want to leave that misstatement. Historically, if you look at the financial differences between companies that have exposure to nuclear, that was clearly a perceived risk in the differential.

That differential is no longer as apparent when you look at the nuclear/non-nuclear company and you account for other sources of risk. I think it probably has to do with the fact there's now a recognized concern about environmental matters and the problems associated with California that now some of these other risks are becoming more important to investors.

Q. I wasn't asking about risks. I was asking about just the source of generation, and I want to make sure I understood you. You said something about a misstatement. Exactly what was it that was a misstatement? You said you wanted to clarify a misstatement.

A. No, no. If I said misstatement, that was a misstatement. I wanted to clarify that perception that the differential between nuclear and non-nuclear is not as great today as it was just a few years ago in the eyes of investors.

Q. And there's certainly different capital investment between nuclear power plants and other types of generation plants; do you agree with me there?

A. The size of the investment is much greater, of course.

Q. And it's true that two of the comparable companies that you used in your DCF analysis derive significant generation from nucs?

A. Yes.

Q. And that would be IUL Holdings and C.H. Energy Group?

A. I'll accept that. I could check it, but I'll accept that.

Q. Do any of the other of your comparable companies derive generation from nuclear power plants?

A. I don't think so.

Q. Okay. And to your understanding, these two companies which derive generation from nuclear power plants were not used in the comparable companies analyzed by either Staff or Public Counsel?

A. That would be true.

Q. Okay. And while we're talking about your comparable companies that you analyzed, you, I believe on page 7 of your direct testimony, discuss the methodology that you used to select your comparables, and one of the criteria that you said you applied -- let me make sure I have this correct. I believe it's page 7, lines 14 and 15. You say you selected only those companies with more than 50 percent of last year's total revenues derived from electricity; is that correct?

A.   Yes.

Q.   And by lowering the bar to say 50 percent, you are able to include one company that derives 46 percent of its total revenues from sources other than electricity; would that be correct?

A.   I guess I don't understand that statement, so I don't know the answer to that question.

Q.   Are you familiar with the percentage of revenues derived for IUL -- or rather UIL Holdings?

A.   I don't recall off the top of my head.

Q.   But I assume at one point you looked at that before you selected UIL Holdings?

A.   Right.

Q.   Would you be surprised if 46 percent of UIL Holdings' total revenues were derived from unregulated enterprises?

A.   No. They have a significant nonregulated activity.

Q. Do you know what percentage of Empire District Electric Company's total revenues are derived from regulated electric service?

A. I don't know precisely. It is very -- it is very high.

Q. Would it be as high as 99 percent?

A. It's in the 90s I'm sure.

Q. Okay. As a general statement, would you agree that if a company is able to reduce the variability of earnings that it receives, that that alters that company's risk profile?

A. Not necessarily, I wouldn't agree with that.

Q. Okay. And why not?

A. There's more to risk than variability of earnings, and it might have a -- well, it certainly is a factor, but it's not the -- it's not a factor that may change the perceptions of an investor.

Let me explain it this way. If you had a company with high variability in earnings but a rapid growth rate and projected rapid growth rate, that would be less risky to an investor in buying that stock today than a stock which did not have any variability at all, that suppose the variation was just zero, so it was just a long line but the line was downward.

In that case you would have one line without any variability pointing downward and one line with a lot of variability pointing upward. Any intelligent investor would take the one with the line pointing upward.

Q.   So variability is a factor as well as the direction?

A.   It's a factor to consider. It's not a governing factor, which was your question.

Q.   But it does affect the risk profile?

A.   It affects the judgment of the investor of what the risk would be.

Q.   However, it could be offset by other characteristics?

A.   But the point is certain -- a certain decline which is no variability is worse than an uncertain increase.

MR. COFFMAN: All right. Well, I think that takes care of my questions. Thank you very much.

JUDGE RUTH: Thank you, Mr. Coffman. And Staff.

MR. KRUEGER: Thank you, your Honor.

CROSS-EXAMINATION BY MR. KRUEGER:

Q.   Good morning, Dr. Murry.

A.   Good morning.

Q.   My name is Keith Krueger. I represent the Staff this morning.

I'd like to call your attention to page 2 of your surrebuttal testimony at lines 4 to 6.
A. Page 2, lines 4 to 6. Yes, sir, I have it.
Q. Now, did you state there that the most important problem with staff witness McKiddy's testimony is that she failed to perform a basic test to measure or assess the financial integrity of her recommendation?
A. Yes, that's the statement, line 6. I thought that was the major problem I had with her testimony.
Q. Okay. What did you mean when you used the term financial integrity?
A. Whether or not the recommended return would provide sufficient cash or sufficient solvency to the company that it could successfully borrow or raise equity capital in the capital markets to sustain itself in the future and various measures that would relate to that judgment.
Q. So you're saying that she didn't assess the question of whether the company would be able to successfully borrow in the capital market?
A. I thought her testimony was virtually devoid of the evaluation of the impact of her recommendation on the company's solvency.
Q. Now, do you contend that the Commission has some sort of obligation to ensure the financial integrity of

Empire District Electric through the rate of return that the Commission authorizes?

A. If I understand the question, my answer would be yes, but I'm not going to make an interpretation of the law or the judgment or the authorization of the Commission. But as an economist, that would be my interpretation of the role of regulation generally, and I would apply that to the Missouri Commission as I would understand its role. It certainly would apply to the natural gas decision.

Q. You think they have an obligation to ensure the financial integrity of the company?

A. Not an absolute obligation, if that's implied in the question. I think it's -- I'm not trying to get into a political science judgment here.

As I understand the role of regulation and my interpretation of what it means to raise and maintain healthy companies, I think the company -- I think the Commission certainly should, and if you want to use the word obligation, I don't think I object to that. I think the Commission should evaluate the impact of its decisions on the company's solvency, and I think that's an appropriate role in regulation.

Q. Okay. You say they should examine the impact of its decision on solvency, but you're not saying that it should ensure the financial integrity?

A. No. I don't think regulation has a hundred percent obligation to make certain a company remains solvent in each and every circumstance. No. That would be a misinterpretation, I think, of the role of regulation.
Q. Did you read the surrebuttal testimony of staff witness McKiddy?
A. Yes, I did.
Q. And specifically the quotation from Pennsylvania Electric Company versus Pennsylvania Utility Commission on page 3 of that testimony?
A. Yes, but I'd be glad to refer to it if you you'd like.
Q. Well, you may not need to refer to it. The question I want to ask is, do you disagree with the statement of the court there that the consequence of lack of profitability, to wit diminished financial integrity, rests upon the utility companies and not on their customers?
A. Is that in -- I'd like to look at that statement and make sure.
Q. Okay.
A. What page is that?
Q. It's on page 3 of Ms. McKiddy's rebuttal -- surrebuttal testimony.
A. Okay. I have it.
Q. I'd ask you to refer to, I think, the last

sentence of the first paragraph there and read downward from there. You don't have to read aloud, but just refer to that and then I'll restate the question.

A. It's the since the risk of nonprofitability?

Q. Correct.

A. That statement says that the financial integrity also rests upon utility companies, and if your question is, do I agree that the company has responsibility in maintaining its financial responsibility -- or its financial integrity as well as the Commission's role in reviewing that, I would certainly agree with that statement.

Q. Okay. Now, did you testify in your surrebuttal testimony at page 3, lines 1 to 7 -- I'll let you find that.

A. Page 3, lines 1 to 7?

Q. Of your surrebuttal testimony.

A. Yes, sir, I have it.

Q. Now, did you testify there that Moody's has recently downgraded its rating of Empire's debt to BAA1?

A. That's my understanding, yes, sir.

Q. Now, am I correct to understand that that rating is equivalent to a rating of BBB+ from Standard & Poor's?

A. I've always considered those about the same, yes.

Q. Am I also correct to understand that a Moody's rating of BAA1 and a Standard & Poor's rating of BBB+ would both be considered investment grade?

A. That would be borderline investment grade, yes. If you read on in that page, I'm not pointing out that -- I'm not claiming that it's not investment grade. I'm pointing out that all analyses and cost of capital, both equity and debt, indicate that A rated and AA rated are the least cost.

So by the company sliding into the lower range of investment grade, the company's costs of capital are going to increase, and that's almost an inevitable outcome.

Q. But my question was whether it is investment grade, and you are saying that it is investment grade?

A. Yes. I think the company can still find investment bankers and take its securities to market if that's the question, yes.

Q. Do you know how Standard & Poor's currently rates Empire's corporate debt?

A. I guess Standard & Poor's -- if I recall, Standard & Poor's still has the company on watch and is probably waiting to see the outcome, in part, of this proceeding.

Q. Isn't it rated A-, though?

A. I think it's A-, and it has not been

downgraded as Moody's -- it has not been downgraded the debt as Moody's has done.

Q. So that is also investment grade?

A. Yes.

Q. And it's higher rating than Moody's has given it?

A. Yes.

Q. Do you believe that the debt rating held by Empire is unusual for a company in the utility industry?

A. I think it's certainly not as unusual as it used to be, no. That's a hard term to judge. There are many other companies now or number of other companies that have slid into that category.

Q. Would you agree that 40 percent of the utilities hold a bond rating of BBB from Standard & Poor's?

A. I'm surprised it's that high, but I have not made that calculation.

MR. KRUEGER: May I approach the witness?

JUDGE RUTH: Yes. First you'll need to show counsel.

BY MR. KRUEGER:

Q. This document is entitled Standard & Poor's Utilities reprinted from RatingsDirect of April 20, 2001. Calling your attention to the highlighted portion there in the middle of page 3.

A. Yes. And if I may point out, it says that 6 percent, which is part of that 40 percent, is now no longer investment grade.

Q. I'm sorry. Does it say that that 6 percent is part of the 40 percent or is that an additional 6 percent?

A. Well, that was my reading of it.

Q. Okay.

A. I have not studied this, but let me just read it into the record. In just a 12-month period, the number of companies rated A and above has declined while the number of BBB and below has increased. In this regard, about 40 percent of the industry now carries a BBB category rating, and 6 percent is rated below investment grade.

So in my interpretation, that means that includes that.

Q. Doesn't Standard & Poor's define BBB as investment grade?

A. I think I've answered that, and the answer is yes, it's still investment grade. Investment grade means that the company's securities are recognized in the market, if I may characterize what I understand it to mean, and that the company can take its securities to the market.

So going below investment grade would be a very -- would not be a desirable step. Means the company no longer has marketable securities.

JUDGE RUTH: Mr. Krueger, I just have a question. Are you going to offer that document in any way?

MR. KRUEGER: No, I'm not, your Honor.

JUDGE RUTH: I would like to have a copy of it and mark it as Exhibit 100 for identification purposes only, and you can provide that at a break.

MR. KRUEGER: Okay.

JUDGE RUTH: To make sure I understand, can you title that? I realize it was something from Standard & Poor's, but what?

MR. KRUEGER: It's a copy from Standard & Poor's reprinted from RatingsDirect dated April 20, 2001.

JUDGE RUTH: Just a moment. And how many pages?

MR. KRUEGER: I think the relevant pages are probably the first four is all that's required.

JUDGE RUTH: Okay. Like I said, that will be marked for identification purposes only just for clarification in the record. You can provide copies at a break later today. Please proceed. Thank you.

BY MR. KRUEGER:

Q. So based on that, then, would you agree that 40 percent of the utilities hold a bond rating of BBB from Standard & Poor's?

A. Yes, I think I would accept that number from

Standard & Poor's.

Q. So such a rating is certainly not unusual, and, in fact, Empire's rating is A- from Standard & Poor's?

A. That's my understanding, yes.

Q. And it is not your contention that investment grade debt is insufficient to attract capital, is it?

A. No. I've testified to that.

Q. I believe in your testimony you cited Valueline Investment Survey that was published on April 6, 2001. So I assume you're familiar with that document. The place you referred to it was in your rebuttal testimony at page 26.

A. Yes.

Q. So you are familiar with that document or have seen it at least?

A. Yes.

Q. And you would rely upon that as an authoritative source of information about corporate finance?

A. I consider Valueline a well-recognized financial source. Valueline's made mistakes. It's not without error, but it's a recognized source and I use it, of course.

Q. Now, did that publication estimate that Empire's projected return on equity for 2001 would be 9.00 percent?

A. In the April 6 Valueline, it lowered the 2000 projection from 12 percent which it had been earlier to 9 percent. It's held -- for 2001 rather, and it has held a 2002 estimate at 12 percent.

Q. Did you take that revision of Empire's projected ROE into account, into consideration in preparing your testimony in any way?

A. I had this prior to or maybe -- I can't recall when I received it. I guess prior to writing either rebuttal or surrebuttal testimony. I couldn't have been -- I guess I at least had it prior to writing surrebuttal testimony. I certainly took it into account, that that was the new report, reported number and estimate by Valueline when I was preparing the surrebuttal.

Q. Did you mention it anywhere in your testimony?

A. I think you just said I referred to it, so I was aware of it. I don't recall now.

Q. My question was whether you had referred to that document, not specifically to that fact that the ROE projection had been revised downward.

My question now is, did you mention anything about the revised projection on its ROE in your testimony?

A. I don't recall that I did. I don't think so.

Q. In your direct testimony when you utilize the DCF method to estimate Empire's required ROE, you estimated the growth factor at 6.00 percent; is that right?

A. That was the estimate at the time I did my testimony, that's correct.

Q. Was that based primarily upon your conclusions of the estimated annual growth in earnings per share?

A. Certainly primarily.

Q. And did you base that on information published in Valueline about its projections for the growth of Empire's earnings per share?

A. Yes. I cited that in my testimony. That was the source of that number. Plus I used their -- there was both the 6 percent estimate plus the forecasted three-year earnings number, and I used -- which is approximately 6 percent. I think it was five something. I used those two numbers.

Q. Am I correct to say that in the April 6, 2001 edition of Valueline Investment Survey, Valueline made a downward adjustment to Empire's projected growth in earnings per share from 6.00 percent to 4.00 percent?

A. That's correct.

Q. Did you take that lower figure of 4.00 percent into consideration in determining the cost of capital for Empire?

A. Yes, I did.

Q. Is that reflected in your testimony anywhere?

A. Well, I didn't receive this until I was writing my rebuttal and surrebuttal testimony. I did recalculate all the earlier calculations that went into my testimony, and the down statement of the -- or the lowering the forecasted growth was more than offset by the decline in price.

The issue here is that when I wrote my original testimony, that was before the merger was ended, and the stock price dropped precipitously, as I pointed out in my rebuttal testimony, after that announcement. Of course, that drove the yield up very sharply.

And after doing a recalculation of the impact of the rising raised yield, that was more than offset -- or that more than offset the decline in growth rate even in the Valueline forecast. It was my judgment that there was no reason to update my recommendation based on that.

Q. But that change did drive down your estimate of the growth factor?

A. Estimated growth factor, yes.

Q. By how much?

A. I guess it would have been approximately 2 percent, but the price decline had been approximately 20 percent or greater.

MR. KRUEGER: That's all the questions I have, your Honor.

JUDGE RUTH: Thank you. Chair Lumpe, do you have questions?

CHAIR LUMPE: Just a few.

QUESTIONS BY CHAIR LUMPE:

Q. Dr. Murry in your surrebuttal testimony, you discuss about Empire being heavy into debt versus equity due to the merger, or that's somewhere mentioned I think in your surrebuttal testimony. And I assume that your -- you were meaning that that was a temporary condition?

A. Let me tell you, Commissioner, my interpretation of what took place, and I was not involved in the merger, so I'm reflecting my understanding based on conversations with the company and the documents I reviewed. That because -- in the merger the company altered its capital structure in conditions -- in response to the merger conditions.

Q. It was not allowed to sell any equity during that period?

A. As I understand it, there was a stand-still provision in the merger, and that's not unusual in a merger because there was a swapping of stock and so you freeze the positions.

And so in that case the company -- and the company was building, had this construction project, and so in taking its preferred stock off the market and holding its equity constant and increasing its debt, its debt ratio increased a great deal because of the merger.

Then when the merger unwound, the company by the end of year had a very low common equity ratio. It's my opinion in looking at the history of what the equity ratio had been previously and what the company says it's trying to go to, it appears to me the snapshot at the end of the year is not representative of where the company as an independent company needs to go and where it says it's going.

I'm not trying to make a judgment about the company's financing policies. That's outside the realm of --

Q. So your suggestion is that the capital structure at the end of the test year or during the test year is sort of a temporary condition, and are you suggesting, then, that one should go back to a previous condition or suggest some sort of forward condition? I'm trying to find out where you think it should go or what period of time should be reflected.

A. I understand your problem as a Commissioner because you have to have a basis to determine what's correct, and what has happened here is there is a history of a higher equity ratio. Then it declined, which is temporary, I hope, and the company says it wants to sell more equity and raise that equity ratio. And so the future is unknown and the past goes back at least a year before the merger.

I looked at both of those and concluded that this end of the year is an anomaly and should be, in my judgment, a temporary position. I think if I were looking for a rock to stand on, I'd probably go back to the history.

Q. To the pre-merger --

A. Pre-merger position --

Q. -- position?

A. -- and say, What's the history been over a period of time? And that at least represents facts of what the company's accomplished. I would accomplish that with what the company says it's trying to do.

Q. And add to that, okay, this is the previous prior pre-merger --

A. Yes.

Q. -- capital structure. This is an anomaly. Go back to that, but add on to it where the company says they want to be. Am I to average those two, where they want to be and where they were or --

A. That's a mechanical question. I don't think --

Q. You're not making a suggestion?

A. I think I'm stepping out a little far if I make that suggestion.

Q. Okay.

A. I think that -- I think those both should enter into the judgment of what's the appropriate capture. I mean, I guess as your role as a Commissioner you could certainly hold the company in the future as to how they respond to this. I think the company has too thin equity under the circumstances.

Q. Are there a number of models -- and I don't know what other word to use -- in using the DCF, we have always used the DCF and relied on it. Are there various models of that, to your knowledge?

A. Let me explain the best I can this way. The DCF theory is relatively simple. It's taking expected future returns and a known present value that's placed on the asset. And, see, this applies not only to common stock, it applies to the valuation of company or valuation of physical property that produces a return.

So we have a market price, and we know what people are willing to pay for what they think the future returns are. Now, we can look at the earnings and we can look at the dividend and the likelihood and we can relate the two, and then by relating the two we can determine what the cost of capital is.

The theory is very sound. There are many, many different ways to try to estimate those future numbers.

We know what the market price is. Sometimes it's very constricted. Sometime it's highly variable and the market price becomes an important question. Usually it's the growth rate that's not really known.

We know what the dividends are going to be on the company. This company hasn't changed dividends in eight or nine years. Under its cash position, it's not going to raise it's dividend. So we know what the dividend is. We know what the current price is. So there's no great mystery in the current price either.

But the growth rate is usually the issue, and there are many ways for people to say -- and what we're trying to do is determine what we think intelligent investors think, and that's why there's a lot of ways to estimate that.

Q. So the formula, everybody starts with the same formula. It's their assessment of what those pieces of the formula are that causes the differentials in what someone would come out with as compared to somebody else?

A. It's the mechanical estimation of what those pieces are, and the one that's usually most complicated to predict is growth because that is talking about and relating to the future.

Q. Okay. And I guess this is speculation, but if the merger had gone through, what was the anticipated -- I don't know the word I'm looking for. We were talking about investment grade, BBB and that Empire is A1. What would it have been had it merged?

A. I guess -- I guess it would have slipped to BBB.

Q. So had the merger taken place, it would have been what someone is suggesting it is now?

A. Because of UtiliCorp --

Q. Okay.

A. -- and its financial situation.

Q. And they're BBB?

A. And UtiliCorp has a very high level of nonregulated activities.

Q. Okay.

A. And they've been very aggressive in a number of areas.

Q. And am I correct in listening to the questioning that you used comparable companies as comparables, that only 50 percent or in that range of their activity is electricity as compared to Empire?

A. Revenues from electricity.

Q. Why would you not have used companies that are 90 percent electricity?

A. I would have if they existed.

Q. So this again is an anomaly, this company?

A. It's an expression of what's happening in the electric utility industry today. As states -- as the federal government deregulates wholesale power and as some states go to less regulation and companies see the -- for example, my comparable group, most of the companies have changed names in just recent years because they've created nonregulated divisions.

There are very few small companies. It's well established that small companies have higher capital costs than large companies. That's generally well accepted. It's important to look at size because of the recognition of the financial markets of just who is the borrower or who is raising the capital. So size is very important.

And obviously regulated and nonregulated is very important, but as more and more companies find greater pieces of their business are unregulated or they're even restructuring themselves to create unregulated sectors.

Q. Did you make adjustments, then, from your comparables to Empire because of that differential in what their activities are?

A. I didn't make a mechanical calculation I could report to. I used a judgment as to what this meant, as I was questioned about Hawaii.

Q. Okay.

A. I looked at Hawaii and I was surprised it was on the list, and if I found a good criterion for excluding Hawaiian Electric, I probably would have done so just because of the questions he raised, which I think were legitimate questions about the difference in the generation mix and obviously it's an island system.

Q. Okay.

A. But looking at it from a financial standpoint, they borrow the New York Stock Exchange and they're a recognized security, and financial markets don't have the problem of moving fuel across the ocean, as he was pointing out, I think, correctly in his cross-examination. So for that reason I left it in.

Judgmentally, if it had been much higher, I wouldn't have considered that important.

CHAIR LUMPE: Okay. Thank you, Dr. Murry.

JUDGE RUTH: Commissioner Murray.

COMMISSIONER MURRAY: Thank you.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good morning, Dr. Murry.

A. Good morning.

Q. Regarding your DCF analysis, on page 12 of your direct testimony, at line 21, you indicate that you used common stock prices for the year 2000 as recorded by Valueline, and also the current prices from a recent --

A. I'm sorry. I opened the wrong testimony.

Q. I'll wait.
A. That was page 12 did you say?
Q. Page 12 of your direct.
A. And the line number?
Q. 21.
A. All right. I have it.
Q. And you also used the current prices from a recent two-week period as reported in the Wall Street Journal?
A. That's correct.
Q. Does a two-week window give an accurate picture of the year or of current values?
A. It gives an accurate picture, I think, of current market conditions at the time I was writing the testimony, and I -- and I think it's better to use the pricing from a period of time rather than a single day.
I think the Federal Energy Regulatory Commission I believe is currently using four weeks, and I believe it used two weeks a few years ago. I think that's a judgmental question. It doesn't represent the entire year. It represents market conditions at the time I was writing my testimony.
Q. Do you know what the difference would have been had you used four weeks?
A. At the time I was writing my testimony?

Q. Yes.

A. No, I don't recall at this point.

Q. Okay. Your Schedules 9 and 10, they're also attached to your direct.

A. Yes.

Q. Can you tell me what -- what is the significance of those two schedules as compared to one another? I'm having a little trouble interpreting that.

A. Schedule 9 is the earnings per share growth, and I used the share prices for the entire year up to that point for the year 2000. And the earnings per share, if you see on page 9 -- or Schedule 9, the earnings per share, $1.24 for Empire, for example, from '94-'96 and $2 for 2003 to '05, those are average earnings numbers for those three-year periods. And I calculated a compound growth rate of 5.42 percent from the '94-'96 period to the Valueline estimate in 2003-2005.

The reason I used the average there is that Valueline estimates the average for a three-year period. Rather than going from the high end to the low end, I took the midpoint of that. So that's a compound growth rate that includes historical and projected.

Schedule 10 shows just earnings per share estimates of the future. If you see in the Empire District that's 6 percent, and at the time I did my testimony, as it was pointed out in cross-examination, when I did my testimony Valueline was projecting an earnings per share growth of 6 percent for Empire District.

Q. I'm sorry. On Schedule 8, are you speaking about Schedule 8?

A. No. I was speaking about 9 and 10. I thought that's what you asked me.

Q. Probably is. I'm sorry. You're right. I asked you about 9 and 10. Okay. Now I'm following you. Thank you.

A. Okay.

Q. On Schedule 9, I was puzzled as to why the years 1997 to 2002 were skipped. Go from '94 to '96 and then --

A. The $1.24 represents the average from '94, '95, '96, a three-year base. The reason I used a three-year base is so that there was not one year in which there was an odd number that would drive the growth rate, and so I averaged those three. That's in part also because Valueline forecasts a three-year estimate.

Q. Yes.

A. And so I went from a three-year historical base as a midpoint to a three-year midpoint growth and calculated the growth rate between those two points. The reason for doing this, this is a blending of the historical growth and the reasonable projected growth that would be in the minds of the investor at the time they purchased the security.

We don't know exactly what investors use, and we can expect that from time to time they would change their -- change what they consider is important to make their judgment about what they expect the security to do.

Q. I'm still puzzled as to why you go back to '96 for the historical data.

A. That creates almost an equal balance over a ten-year, five year historical, five-year forecasted period. The recognition here is that an investor is aware of what's happened recently to the security, and they're also aware of what the financial analysts are predicting for the future, and the two combined represent the investors' judgment of what they can expect in the future.

Q. And you think that's more accurate than taking, say, '98, '99 and 2000?

A. I've looked at this over the years in a number of different ways. I think the more recent numbers are more important if that's -- I'm not trying to evade the question. But if you're saying are more recent numbers likely to be a more important influence on investor than were --

Q. Yes.

A. -- older numbers, the answer to that is I think definitely. I was trying to balance the five-year growth versus a five-year history.

Q. On Schedule 8, you used an average of the high/low for the year 2000; is that correct?

A. Yes. I took the share price that would produce the highest yield and share price that produced the lowest yield and I just added those to the projected dividend growth rates to get a DCF calculation.

Q. And I think Ms. McKiddy used October through March of 2001, and I was wondering why that wouldn't give us a better current picture to use those months?

A. Well, I guess I'd like to answer that, if I may, in two ways. One is the 2000 calculation or the calculation of the longer period of time is a calculation I always make, and I think that it was relevant at the time I was preparing the testimony. That's why I included it in testimony.

That represents the range of what investors over previous months had been willing to pay for this security, and the range here was sizeable, probably because of the announced merger which occurred in May 2000, which drove the stock price up.

Now, for regulatory purposes and what I was trying to represent, that would be a misrepresentation because it doesn't reflect the earning power of the company.

It reflects the investors speculating on what the price is going to be when the merger occurs. But I included that in my testimony because I thought it was relevant to show where the market was at that point in time.

The disagreement I have with Ms. McKiddy was that she used a six-month period, approximately six-month period which included the period from before the merger to the period after the merger was terminated and -- because she knew at the time the merger had ended.

If I had known the merger was going to end, I would not have put any credence in these premerger numbers, because they don't represent what the real earning power of the company would be.

Q.   Okay. But you have --

A.   So I prepared this testimony before the merger ended.

Q.   Okay. Including both the premerger and the merger related --

A.   Exactly.

Q.   -- values?

All right. On page 18 of your rebuttal testimony, you refer to your Schedule 27, and on your Schedule 27 you used January through March 2001.

A.   Yes.

Q.   Whereas, I believe Ms. McKiddy included

October through December of 2000.

A. Yes. That's my recollection of her Schedule 14.

Q. And so you just used the -- well, you omitted the merger-related numbers completely from your Schedule 27; is that right?

A. That's correct. What I was trying to point out in my Schedule 27 in that discussion, that she had the benefit of knowing the merger was not going to proceed. I did not have that benefit, as I said in my testimony earlier, and that in my judgment that the October/November/December numbers were not appropriate for setting rates for the future of an independent company, Empire.

And so I just recalculated what had occurred after the announcement that the merger was not going to proceed and just used her numbers to make that calculation, and that's what my Schedule 27 is.

Q. And I had a question about your Schedule 28, but I didn't make good notes so I can't think what it was.

All right. That compares to Ms. McKiddy's Schedule 15; is that right?

A. Yes, that would be correct. Schedule 28 is simply taking together my Schedule 24 and my Schedule 27 and recalculating, recalculating using the same method

Ms. McKiddy used, recalculating resulting cost of common equity when I adjusted the growth rate for the period after the merger terminated, and I adjusted the yield for after the termination of the merger.

I was simply pointing out that if she had used numbers since the first of the year after the termination of the mergers, her cost of capital would have been approximately the same as mine, and I recommended 11 and a half to 12 percent.

Q. And it's your testimony that a three-month period is -- you had made the statement earlier that you always use a longer period when possible?

A. Well, I always made that calculation in other testimony. I don't like to change my testimony from case to case or change my methods. I will change what I think is important based on the circumstances.

In this case, I think the most important circumstance is the termination of the merger, which occurred after my direct testimony. And in that regard, I would, if I had -- I can't say what I would have done if I'd written testimony after the first of the year, whether I would have included the 2000 numbers or not in my testimony.

But I certainly would not have put much weight on them because of what it represented. I might have excluded them entirely.

Q. At the time you prepared your schedules using the 2001, three months in 2001, did you attempt to do any calculation using the entire year of 2000 and including the first three months of 2001?

A. I updated those numbers, but I didn't pay any -- I updated them just to update all the schedules. I actually had a person update them for me, and I don't even recall what they were. I did not consider them relevant because the period 2000 was announcement of the merger and termination of the merger. That's not a good representation of what the future holds.

COMMISSIONER MURRAY: Thank you.

JUDGE RUTH: Any further questions?

Thank you. We'll move to the recross. Mr. Conrad, do you have --

MR. CONRAD: Nothing further, your Honor. Thank you.

JUDGE RUTH: Mr. Coffman?

MR. COFFMAN: Yes, just a couple.

RECROSS-EXAMINATION BY MR. COFFMAN:

Q. First, just to clarify something for me, if you would, Mr. Murry -- oh, I guess I need to --

JUDGE RUTH: Yes. Move over, please.

BY MR. COFFMAN:

Q. You were asked a couple of questions about your Schedule DAM-9 and Commissioner Murray's question about the EPS years that you examined, and you said something about the fact that you had averaged or recognized a five-year period, and I was having trouble understanding that.

It looks as if you looked at three past historical years and three projected years, and I -- the whole time period is a ten-year period. I was trying to understand what you meant as for five years.

A. If you look at Schedule 9 under 1994-'96 EPS for Empire District there's $1.24. That's the average earning per share as reported by Valueline for those three years. If you look at the -- that's an actual, of course, or historical as reported. If you look at the 2003 to 2005, there's $2. That's the forecasted figure for Valueline.

If you look at the next column, growth rate 5.42 percent, that's the internal growth rate from $1.24 to $2 over that period of time. So that's a compounded growth rate from one base to another end point.

Q. I understand that. I'm just having trouble understanding what you meant by five years.

A. Oh, I think the question Commissioner Murray asked me was about the '94-'96 and whether it was more important than '98-'99, and I said that it was to proximate the balance the five-year growth rate, the three to five-year growth rate that Valueline forecasts. So there's an approximate weighting, equal weighting of historical numbers versus predicted numbers in this case.

Q. But you only looked at three years?

A. The actual number's calculated for three, that's correct.

Q. Let's see. You asked -- and also you were asked some questions by Commissioner Murray about past stock price, and I just wanted to make sure that I understood your testimony about what investors can't do. An investor cannot go back to the year 2000 and buy stock from the past, can they?

A. No.

Q. They have to buy stock at today's price if they want to?

A. Yes. With what's happened to the stock price, I'm sure they prefer buying it at today's price.

Q. That option's not available today?

A. That's correct.

Q. You were asked by Commission Chair Lumpe a question about capital structure, and if I recall your answer you said that if you wanted a rock to stand on, you would look to past history to make that capital structure.

A. I was -- I think I used the word factual, that that is a -- that is a representation of something that's actually identifiable and has occurred, and I thought I was responding to that almost in a policy circumstance, what does one do when the current capital structure's an anomaly because of the merger.

Q. Is the capital structure recommendation of Empire in this case one that's based on past historical information?

A. I don't think so. I think it represents what the company's intentions are, and that's based on my conversation with the company. To reach my judgment of what I thought was a number I could take and incorporate in my testimony, I did look at the history of what the capital structure had been.

MR. COFFMAN: Thank you. That's all.

JUDGE RUTH: Dr. Murry, Commissioner Murray has another question for you.

FURTHER QUESTIONS BY COMMISSIONER MURRAY:

Q. I apologize. I skipped one that I did intend to ask you. In your rebuttal testimony on page 12, you speak about the added risk of differing fuel cost pass-through provisions of Empire and other companies that Ms. McKiddy compared to Empire. You're on lines 11 and 12 there.

A. Yes.

Q. And you go on to say, Electric utilities in many jurisdictions have fuel cost pass-throughs. Empire does not, and this is a clear risk differential favoring those other companies.

Now, my question is related to the legislation that passed and/or the recommended IEC in this -- that some of the parties have recommended here. Does either one of those factors change your risk analysis for Empire?

A.   I don't think I know enough about either the legislation or that agreement to know what the full impact will be. I was drawing simply a parallel between the companies she selected to use as comparables and the risk differential and the, for example, Fitch in the downgrade, downgrade and noted that as a factor. But I don't think I can -- I don't think I know enough to comment on prospective changes.

Q.   Would a pass -- a fuel cost pass-through change your -- if Empire were to be able to use a fuel cost pass-through, would that change your risk analysis for Empire?

A.   I think it removes that differential for Empire. I mean, the final arbiter of what's important is the market, not me of course. But in my judgment, the financial analysts and people looking at the stock as intelligent investors would consider that favorable.

COMMISSIONER MURRAY: Thank you. Thank you, Judge.

JUDGE RUTH: Mr. Conrad, did you have any recross based on the additional question from the Bench?

MR. CONRAD: No, ma'am. Thank you.

JUDGE RUTH: And Mr. Coffman?

MR. COFFMAN: Nothing further.

JUDGE RUTH: Okay. Then Staff, Mr. Krueger?

MR. KRUEGER: Thank you, your Honor.

RECROSS-EXAMINATION BY MR. KRUEGER:

Q. Commissioner Murray asked you some questions about Schedule 28. I understood you to answer that that was based on Schedule 24 and 27; is that correct?

A. That was my statement, and that's what the footnote says, and I think that's correct.

Q. I'm looking at the Schedule DAM-28, and it says sources Schedules DAM-R4 and DAM-R7. Is that actually DAM-24 and 27 then?

A. Yes.

Q. Okay. Commissioner Lumpe -- Chair Lumpe asked you some questions about the capital structure, and as I understand it, Schedule DAM-1 is based on the capital structure as of December 31, 2000; is that right?

A. The December 31, 2000 was the pro forma. If you're referring to the correction I made, the title said 1999. That should have been edited out. That should be

2000.

Q. But it was actually December 31, 2000, and as of December 31, 2000 the long-term debt was 47. -- I mean the common equity was 47.5 percent?

A. This was the number that I used, and the source there cites the company work papers and those are the work papers I had available at the time, and my evaluation was whether that was consistent with the history and whether I thought that was an appropriate number to adopt.

Q. Was it your understanding that that was the actual capital structure as of that time?

A. No. My testimony was actually written before December 31, 2000.

Q. Okay. So the pro forma was projecting it to December 31, 2000?

A. That was my understanding, that was the recommended -- or the number the company was recommending for that point in time.

Q. And even as of that date, the equity was still 47.5, would still have been 47.5 percent?

A. I don't quite understand that question.

Q. At the time you wrote your testimony, the pro forma common equity as of the end of December 31 -- end of December last year would have been 47.5 percent?

A. At the time I wrote my testimony, that was my understanding, that the company was estimating an equity of 47.5 percent at that time.

Q. Has the capital structure changed since December 31?

A. I'm sure it has.

Q. And, in fact, the common equity has actually declined to 37.31 percent according to the testimony of witness David Gibson; is that right?

A. I would accept that. I was going to say, I don't think I have that number with me. I have a number that's approximately 40 percent.

Q. But would you accept my representation that in his testimony he did say that the actual --

A. I would accept that. I have no disagreement or any reason to disagree.

Q. To your knowledge, has Empire obligated itself in any way to do anything to increase its common equity in the future?

A. Not to my knowledge. As I testified or told the Commissioner, in my judgment the company has an equity ratio that's too thin for its present circumstances, but I'm not involved in the company's financial planning.

Q. So you just expect it will increase to 47.5 percent?

A. I hope it increases its equity ratio from where it is currently. It's my judgment the company should do so.

Q. So it's your hope rather than your knowledge of the company's --

A. It is my judgment that the company's equity ratio is currently too low for its circumstances.

MR. KRUEGER: Thank you. That's all the questions I have.

JUDGE RUTH: Mr. Swearengen, do you have redirect?

MR. SWEARENGEN: I do.

JUDGE RUTH: Please proceed.

REDIRECT EXAMINATION BY MR. SWEARENGEN:

Q. Dr. Murry, in response to a couple of questions from Commissioner Murray, she was asking you to look at page 12, I believe, of your direct testimony and then had some questions about Schedule DAM-8 to your direct testimony. Do you recall those questions --

A. Yes.

Q. -- concerning the, on the schedule the share prices, the high and low share prices for Empire for the period that you looked at?

A. Yes.

Q. First of all, I think you've cleared it up, but let's state it once again. This direct testimony that you filed in this case, when did you prepare it?

A. It was in the fall, and the date I have on the testimony was October 2000, and it was prepared approximately the previous four weeks of that.

Q. So it was prepared in the fall of 2000?

A. Yes.

Q. And I think you indicated that during that period of time the contemplated merger between UtiliCorp United, Inc. and the Empire District Electric Company was still under way; is that true?

A. Yes, it was, and to my knowledge, and I was -- I was not aware that -- I could not find any evidence that the -- that there was any likelihood that the merger would end or terminate.

And I would observe the -- had been watching both the price as well as the volume of stock traded at that point in time, and it looked like the transactions were being driven by the expectation the merger would proceed.

Q. I think you said, and maybe I misunderstood you, but I think you said it was your understanding that that merger, the UtiliCorp/Empire merger was announced in May of 2000, but is it not true that, in fact, the merger was announced in May of 1999? Do you recall?

A. That's correct.

Q. May of 1999?

A. Yes.

Q. And is it your understanding that the announcement that that merger was terminated, an announcement made by UtiliCorp, occurred at the close of stock trading on January 2nd, 2001?

A. Yes.

Q. Now, looking back at your Schedule DAM-8 to your direct testimony which Commissioner Murray was asking you about, the $27.10 high stock price shown on that schedule would reflect the merger premium; is that correct?

A. Absolutely.

Q. And turn, if you would, please -- I believe you had a question about Schedule DAM-27, which is attached to your rebuttal testimony. Do you have that schedule in front of you?

A. Yes, I do.

Q. Now, this testimony was filed in the spring of this year; is that correct?

A. That's correct.

Q. After the announcement that the merger had been terminated?

A. That's correct.

Q. On your Schedule DAM-27, am I correct in understanding that for the high stock price in January of 2001 you show $26.56?

A. Yes.
Q. Is the explanation for that $26 stock price contained on page 17 of your rebuttal testimony?
A. Yes. On page -- on lines starting really lines 10 to 12, I point out that the trading range prior to the merger and termination was over $22, over $30, and that's just citing Ms. McKiddy's Schedule 14, but after the termination of the merger, the stock dropped to the range of 17.50 to 20.18, $20.18.
And I point out on the -- down on line 15 that the stock closed at $25.47 on January 2nd, and on January 3rd it opened at $20.18 after the announcement.
Q. So from that can we conclude that there was trading on January 2nd, 2001 prior to the time that it was announced by UtiliCorp that the merger was going to be terminated?
A. Yes.
Q. So turning back then to your Schedule DAM-27 where you reflect the $26 stock price for January, am I correct that that would reflect trading which occurred on January 2nd before the termination was announced?
A. I'm sure that's the case. Those numbers I believe are from Ms. McKiddy's Schedule 14, but I'm sure those had to be January 2nd rates.
Q. Fine. Chair Lumpe asked you some basic

questions about the discounted cash flow or DCF formula or model, and I think you said it's a simple and sound model; is that correct?

A. Yes. Theoretically, I think virtually every analyst would say that's the relationship between expected returns and market price.

Q. Then I think you said that usually it's the growth rate component of the model that's not known?

A. That's the most difficult to mechanically estimate, yes, sir.

Q. And so usually that is an issue of some sort --

A. Yes.

Q. -- in a proceeding such as this?

A. The questions the Commissioner was asking me I think were predicated on the assumption there were a number of ways to make the calculation. I was pointing out that that's the most -- that is the component that requires the -- attracts the most complicated methods and number of alternatives to estimate because its an estimate of the future.

Q. And am I correct in saying that that's an issue in this case between the Company and the Staff and the Public Counsel?

A. Seems to be, yes.

Q. And Mr. Conrad, too, I'm sure.
Then I think you also said that the current price and yield are known?
A. I'd say in most cases they are -- they are known because the price, of course, is observed, and the yield is near term and because the dividends are not likely to change very much. In this particular case, the stock price dropped a lot at the first of the year, but the stock price is usually an observable number.
Q. So in this case, while the stock price and the yield are usually known and shouldn't be an issue, those matters are issues in this case between the Staff and the Company; is that correct?
A. That's correct.
Q. Now, you said the stock price dropped in January. Would you turn to your Schedule DAM-25, please, Schedule DAM-25 to your rebuttal testimony.
A. Yes.
Q. Is that schedule designed to show the drop in the stock price which occurred in January of 2001?
A. Yes, that schedule was designed to show the distinction between the before and after market valuation of Empire's stock before and after the merger termination.
Q. Now, in response to a question from Mr. Krueger, the Staff counsel, you made mention, and I

think it was with respect to page 2, 3 and 4 of your rebuttal testimony, if you could turn to that for a minute, pages 2, 3 and 4.

A. All right.

Q. May be the surrebuttal. Excuse me. I misspoke. It's pages 2, 3 and 4 of your surrebuttal testimony, which is Exhibit 26.

In response to one of Mr. Krueger's questions you mentioned the term lowest cost bond rating, and my question is, what did you mean by that?

A. There's no question that bond rating influences -- of course, it's a self-determination, that the same financial statistics that are used to determine bond rating also influence investors, and then when the bond rating is announced, the bond rating influences investors.

And there have been a number of analyses of which bond rating produces the lowest cost of capital, and there's a complicating factor because a higher equity ratio lowers -- is likely to lower the bond rating, will certainly increase interest coverage and other factors that no one wants to look, but it also raises the cost of capital because equity is a more costly component.

And so a number of analysts have looked at the bond rating to determine if there is, in fact, a lowest, they sometimes use the term optimal, rating. A AAA rating would be the lowest cost of borrowing but would probably require high cost equity to support a AAA bond rating.

And so most analysts have concluded the fact is only the results that I'm familiar with have shown that A and AA are the lowest cost of raising capital for a company, and that includes utilities, and that was what I was referring to.

Q. And how did you say that the Staff has dealt with the bond rating issue?

A. I would say the Staff has virtually ignored bond rating. I pointed it out in my rebuttal, and I was surprised that Staff did not really respond to that.

Q. What do you mean, the Staff has ignored the bond rating?

A. I think the Staff did not -- well, I was asked some questions about financial integrity. I think the Staff ignored the basic measures of financial integrity in evaluating the impact of the return recommendation.

And then when I was asked about this, I think I stated that's the biggest problem I had with the Staff testimony. And when I raised that as an issue in rebuttal testimony, I thought it was not even responded to in the surrebuttal in any meaningful way.

Q. Mr. Coffman for the Public Counsel asked you some questions about nuclear -- companies that had nuclear operations and how their risk would compare to a company such as Empire which does not have any nuclear operations, and I think you said that the nuclear risk is not as great today in the eyes of investors as it was just a few years ago. Do you recall making that statement?

A.   Yes, that's my judgment.

Q.   And what did you mean by that?

A.   Not very many years ago there was a sharp distinction in the cost of equity and the cost of really borrowing, but especially in the case of equity, of companies that had nuclear, they used the word at that time exposure, which meant that companies that owned nuclear plants or pieces of nuclear plants.

This is a carryover, I think, of the Three Mile Island problem, and I guess problem's probably understating what happened at Three Mile Island. But because of that there was a serious concern on the part of the investment community that companies that own pieces of nuclear plant have very high financial risk or business risk because of that.

And I'm saying it's my observation -- and I've not quantified it precisely. It's my observation that that differential is going away. It's eroding. I don't know exactly why that is. I think I tried to point that out.

I believe maybe nuclear is becoming a little more accepted as we have nuclear experience in the United States and certainly in other countries, and maybe it's the pressure of the need of generation in some locales. But financially that differential is not important as it was just a few years ago.

Q. I think it was Mr. Krueger was asking you about risk associated with the lack of a fuel adjustment clause, PGA clause or some automatic mechanism to permit Empire to pass on fuel costs in Missouri, and he asked you if your opinion on that would change if there was some legislation in place that might alleviate that and you indicated you didn't know anything about that legislation.

If I told you that that legislation has not yet become law and if it did become law it would terminate on its own within two years, how would that affect your opinion on that issue?

A. I think that would certainly diminish the mitigation of that risk in the eyes of most investors.

Q. Have any rating agencies or investment services recognized the lack of a mechanism to pass on fuel costs for this company, for Empire, as a problem in connection with their ratings perhaps?

A. The Fitch report at the time the announcement of the downgrading of the debt of Empire identified that as a problem.

MR. SWEARENGEN: That's all I have. Thank you.

One final thing. Not to be outdone by my good friend Mr. Conrad, Dr. Murry, I want you to know that I too have practiced law in Hawaii and, in fact, am licensed there. So if we can do anything for you there, we'd like to.

JUDGE RUTH: Okay. That will conclude, Mr. Murry, the questions for you.

(Witness excused.)

I think we should take a break. It's almost a quarter after 10. We'll start back up promptly at 10:30. We're off the record. Thank you.

(A recess was taken.)

JUDGE RUTH: Let's go ahead and go back on the record, please.

I believe we are now ready for Empire to call your next witness.

MR. SWEARENGEN: Yes, your Honor. Call Dave Gibson, G-i-b-s-o-n.

(Witness sworn.)

JUDGE RUTH: Please be seated.

DAVID GIBSON testified as follows:

DIRECT EXAMINATION BY MR. SWEARENGEN:

Q. Would you state your name for the record,

please, and spell it for the reporter.
A. Yes. David W. Gibson, G-i-b-s-o-n.
Q. Mr. Gibson, by whom are you employed and in what capacity?
A. I'm employed by Empire District, and I am Vice President of Finance.
Q. Did you prepare for purposes of this proceeding certain testimony in question and answer form, direct testimony, rebuttal testimony and surrebuttal testimony?
A. Yes, I did.
Q. And you have copies of that testimony with you this morning?
A. Yes, I do.
Q. You understand that your direct testimony has been marked as Exhibit No. 6, your rebuttal as Exhibit No. 14 and your surrebuttal and Exhibit No. 29?
A. Okay.
Q. Is that your understanding?
A. Yes.
Q. Are there any changes that you wish to make at this time with respect to your direct testimony, Exhibit 6?
A. No, not at this time.
Q. With respect to your rebuttal testimony, Exhibit 14, are there any changes which need to be made to

that testimony?

A. Yes. On page 4, it would be line No. 5, that percentage 48 percent should be 47.1 percent.

Q. That's page 4, line 5?

A. Yes.

Q. 47.1?

A. Yes.

Q. Anything else --

A. Yes.

Q. -- on that with respect to your rebuttal testimony?

A. No.

Q. Are there any changes that you need to make with respect to your surrebuttal testimony, Exhibit 29?

A. Yes. On page 3, line 8.

Q. And what is the change there?

A. The change would be also from 38 percent to 47.1 percent.

Q. Are there any other changes that need to be made with respect to your surrebuttal testimony?

A. No, there are not.

MR. SWEARENGEN: Your Honor, one thing I would call to the Commission's attention, and I apologize for it, it's our fault, the schedules attached to Mr. Gibson's surrebuttal testimony at least on my copy appear not to be identified by any number, and I thought we could rectify that right now if that would be okay with the Commission.

JUDGE RUTH: Yes. Let's do that, please.

MR. SWEARENGEN: I think his first schedule is a document that shows two graphs and the first one says Averaged Authorized Return on Equity. My suggestion is that be marked as Schedule DWG-2.

JUDGE RUTH: Okay.

MR. SWEARENGEN: And I believe, and Mr. Gibson can correct me if I'm wrong, that the next page behind it is part of that schedule; is that right?

THE WITNESS: Yes.

MR. SWEARENGEN: So that would be page 2 of that schedule. And that's a page at the top it says Electric Utility Summary Table.

Then the next document is a document entitled Fitch Downgrades Empire Electric Company to BBB+, and that's a two-page document, and I would suggest it be marked for purposes of identification as Schedule DWG-3.

And then the last attachment to his surrebuttal testimony is a document entitled Rating Agent -- Rating Action Empire District Electric Company, Moody's Downgrades Empire District Electric Company, SR secured to Baa1 Outlook Negative, and it's a two-page document, and I would suggest it be marked as Schedule DWG-4.

MR. CONRAD: Excuse me. What was the chart that you had? Was that DWG-1?

MR. SWEARENGEN: DWG-2. I think DWG-1 is attached to his direct testimony.

BY MR. SWEARENGEN:

Q. Mr. Gibson, one final housekeeping question here. If I asked you all the questions now that are in your three pieces of testimony, Exhibit 6, 14 and 29, would your answers today be the same as you have corrected them?

A. Yes, they would be.

Q. And would they be true and correct to the best of your knowledge, information and belief?

A. That is correct.

MR. SWEARENGEN: Your Honor, I would offer Exhibits 6, 14 and 29 into evidence at this time. I recognize that Exhibit 14 concerns some topics other than just return on common equity and capital structure. So we would obviously have no objection to you reserving ruling on the admission of that until some later time if that's the pleasure of the other counsel.

JUDGE RUTH: And which exhibit was that?

MR. SWEARENGEN: That would be Exhibit 14, the rebuttal testimony.

JUDGE RUTH: Let's take these individually, then. Exhibit 6 has been offered. It's the direct testimony of Mr. Gibson. Are there any objections to it being admitted into the record?

MR. CONRAD: Your Honor, I think it's not just 14 but also 6 that has cost of service material in it.

MR. SWEARENGEN: And that's fine.

MR. CONRAD: I will tell you, to make counsel's life easier, we do not have and will not have objection to that portion of 6, that portion of 14, and I think all of 29 -- although I appreciate you're not there yet -- that don't pertain to the cost of service issue but do pertain to the issue for which Mr. Gibson is proffered today.

And what we've done in the past, if it's of any help to your Honor, in other cases with different judges is rather than say, okay, I'm going to admit part of the testimony but not this, is we've just done as I think counsel is suggesting and just suspend or hold ruling on those until all of it has been dealt with, and that may be the cleanest way to do it.

JUDGE RUTH: I think that probably is the best way to handle it, and I understand then 6 and 14 both have some references to the cost of service material. So we will reserve ruling on whether those are admitted until later, but we'll need to make sure we don't forget them.

And I will ask if the parties have any

objection, then, to Exhibit 29? That's the surrebuttal testimony of Mr. Gibson.

(No response.)

Okay. Seeing no objections, Exhibit 29 is admitted into the record.

(EXHIBIT NO. 29 WAS RECEIVED INTO EVIDENCE.)

MR. SWEARENGEN: Thank you, your Honor. And with that, I would tender Mr. Gibson for cross-examination.

JUDGE RUTH: Thank you. Mr. Conrad, would you like to begin cross-examination?

MR. CONRAD: I would, your Honor, if I had questions for Mr. Gibson on the issues for which he is proffered today, but since I don't, I will decline the opportunity.

JUDGE RUTH: Okay. Thank you. Mr. Coffman?

MR. COFFMAN: Thank you.

CROSS-EXAMINATION BY MR. COFFMAN:

Q. Good morning, Mr. Gibson.

A. Good morning.

Q. Try to keep you straight with William Gipson. I know I had trouble with that in the past.

Were you involved, Mr. Gibson, in the case requesting authorization of the merger with UtiliCorp, Case No. EM-2000-369?

A. By involved, I was with the company.

Q. But you didn't file testimony?
A. No. No, I did not.
Q. Were you aware at that time that it was Empire's position that the proposed merger along with the regulatory plan was in the best interests of the ratepayers?
A. Did you say was it in the best interests?
Q. Wasn't that the position of Empire?
A. Yes.
Q. But you're telling us here today, and specifically in your rebuttal testimony, that ratepayers are actually benefiting from the fact that the merger failed; is that correct?
A. That's correct.
Q. How do you reconcile that?
A. Well, it's fairly simple. The way that the ratepayers are benefiting, if you look at the capital structure, if the merger had not failed, then our capital structure or common equity piece more particularly would have been almost 7 to 8 percent higher than what it was at the end of March.
So since that is -- since it has been pointed out, the common equity section is actually the higher cost component of your capital structure. Since that's lower, that means that your return is lower, which means that your revenue requirement is lower, which means that the

ratepayers do not pay as much.
Q. I think I understand your position there. Now, you're not recommending that the Commission use the actual capital structure in setting rates in this case?
A. No. What I am asking for is that they normalize the capital structure away from some of the effects of what took place with the merger. Namely, we were precluded from issuing additional common stock, things of that nature.
Q. And by normalize, are you asking the Commission to base it on some historical level?
A. Yes. That would be correct, yes.
Q. And this would be at some level that investors currently could not -- or that isn't reflected at the current time?
A. Yes.
Q. And would you agree with me that there's no guarantee that that would be the situation in the near future?
A. No. I agree with that.
MR. COFFMAN: That's all I have. Thanks.
JUDGE RUTH: Mr. Krueger?
MR. KRUEGER: Thank you, your Honor.
CROSS-EXAMINATION BY MR. KRUEGER:
Q. Good morning, Mr. Gibson.

A. Good morning.

Q. You testified, I believe, in both your rebuttal testimony and your surrebuttal testimony that the Company proposes that the Commission adopt a capital structure of 45 percent common equity, 7.9 trust preferred and 48 percent -- or I guess that's now corrected -- 47.1 percent long-term debt; is that correct?

A. Yes, that's correct.

Q. So if Mr. Robert Fancher testified that Empire's recommending a capital structure of 47.5 percent common equity and 52.5 percent long-term debt, that would be incorrect?

A. Yes. Those -- well, actually, that recommendation, the circumstances were quite a bit different. At that point in time, the merger with UtiliCorp was still going on, and that capital structure was set based on those -- that set of facts.

The one that I'm recommending in this instance, the revised capital structure, is based on the fact that the merger did not -- or actually failed.

Q. Okay. And so if the Position Statements mention those same figures, 52.5 percent debt and 47.5 percent common equity, that is no longer accurate either, and the same for Dr. Murry's?

A. Yes. Those were based on the circumstances at the time, like I said, and the, you know, the pending merger with UtiliCorp.

Q. I believe you testified that as of the end of March, the actual capital structure is 37.31 percent common equity. Do you need a reference?

A. No.

Q. Your rebuttal testimony, lines -- page 4, lines 8 and 9.

A. I have it in front of me.

Q. Okay. You testified there that the actual capital structure as of the end of March was 37.31 percent common equity and 7.92 percent trust preferred and 54.77 percent long-term debt?

A. Yes, that's correct.

Q. And you repeated that testimony in your surrebuttal testimony?

A. Yes, I did.

Q. And those figures are still accurate?

A. Yes, they are.

Q. What exactly is trust preferred stock?

A. Trust preferred is, it's -- I guess you could think of it as sort of a hybrid. It's treated as equity by Standard & Poor's. By that, you know, you reach a certain level when you're issuing debt, and what happens is the rating agencies, once you reach whatever that magical place that they feel they don't feel comfortable anymore, they will downgrade you.

The trust-preferred gives the company the benefit of receiving a tax deduction but still receiving equity treatment by the rating agencies or by Standard & Poor's. Just Standard & Poor's.

Q. In your rebuttal testimony on page 4, lines 18 and 19, you mention that the company had issued trust-preferred stock at a rate of 8.5 percent. What is the 8.5 percent?

A. 8.5 is the rate that is the issue price, if you will. It's sort of like if you look at bonds, they carry an interest rate. Well, this isn't really interest, but it's similar to that.

Q. Is it an obligation that must be paid prior to distributing anything to the holders of common equity?

A. Yes. Common equity are -- they're the ones that are the last, if you will, in a -- and I think what you're referring to is if there was a liquidation of the company, what would happen. The bond holders would be first, then the trust-preferred, and then whatever's left over is the common.

Q. So it would not be accurate to include that as common equity?

A. No.

Q. So the correct figure at the present time is still 37.31 percent common equity?

A. Yes, that's correct.

Q. Do you believe that's an unusual capital structure for a company that's operating in the electric utility industry today?

A. I believe it's unusual for Empire. Some of the things that have been mentioned, you know, the -- we have seen in the past we've had a more balanced capital structure.

This capital structure for us is not balanced. What we're looking to -- we're going to try to balance it more this year, and we're dealing that by -- we're reinstituting our DRIP plan which will raise common equity, and then we're also planning to issue common equity later this year.

So in the short term we have an abnormal capital structure, but we're moving towards a more balanced, what I would call a more balanced capital structure.

Q. Okay. But you said it's abnormal for Empire?

A. For us.

Q. But not necessarily for the electric utility industry?

A. I don't -- the data, some of the data that I reviewed, Regulatory Research Analysts, they put together some historical data based on rates of return and percent of equity that they were seeing in rate cases.

I took a look at that just to get some kind of feel for what was happening, mainly for the rates of return, but I also was looking at the common equity part just for the electric companies. And that I think for -- keep in mind, these are just reported companies. It seems that we were at the low end even on the common equity component.

Q. Would you be surprised to find that C.A. Turner Utility Reports reported that the average common equity for an electric utility as of March 2001 was 38 percent?

A. I wouldn't have any -- I don't have any knowledge of that.

Q. Okay. So you wouldn't be able to say then --

A. No.

Q. -- that that is atypical of the electric utility industry?

A. No, I wouldn't, but I also think that, you know, if we're -- in order to try to compare apples and apples, and it's not at -- best it's -- it takes a lot of judgment. I don't know if, you know, what C.A. Turner was looking at at that 38 percent, if that includes a lot of nonregulated industry or pieces of the electric utilities. I really don't know what would be in there.

The tendency is, what I was seeing is the more that a company moves into the nonregulated area, such as what UtiliCorp has done, they tend to be what I would term more debt heavy. They tend to issue more debt as opposed to common.

Q.   You wouldn't have any specific knowledge that --

A.   No.

Q.   -- that figure is inaccurate?

A.   No.

MR. KRUEGER: That's all the questions I have.

JUDGE RUTH: Commissioner Murray, do you have any questions?

COMMISSIONER MURRAY: Give me just a minute, please.

No, your Honor, I don't. Thank you.

JUDGE RUTH: Empire, do you have redirect?

MR. SWEARENGEN: Just a few.

REDIRECT EXAMINATION BY MR. SWEARENGEN:

Q.   Mr. Gibson, I think it was Mr. Coffman from the Public Counsel that asked you in discussing the capital structure and the fact that right now I think you indicated that it is an abnormal capital structure for the Empire District Electric Company and it should be something different in the future.

He asked you what guarantee you could give us that the Empire District Electric Company, in fact, will change its capital structure in the future. You said you couldn't guarantee that.

But my question is, does the company have in place a plan to change the capital structure?

A. Yes. I interpreted that question -- maybe I interpreted it wrong. I interpreted that to mean, you know, given the conclusion of the rate case and, you know, what happens in the future, that there would be guarantees that our capital structure will hit a point. That there aren't any guarantees. Just as in the past we set targets for a capital structure and we tried to hit those targets, sometimes we succeed and sometimes we don't.

But in general, the capital structure that the company had in place is the one that we're targeting in the future, and yes, we do have plans in effect to reinstitute, and it should be this month or maybe next month, to reinstitute the DRIP plan which will increase common equity.

Q. And what is the DRIP plan?

A. Dividend reinvestment plan. Empire had that plan in effect prior to the merger with UtiliCorp, and then we terminated that plan. Since the merger failed, we are now reinstituting that plan, and then also we are looking towards a financing of common equity in the latter part of this year.

Q. Okay. Thank you.

Mr. Krueger, I believe, for the Staff asked you the question as to whether Empire's present capital structure -- and he's talking about the one, I think, that you've testified to as of the end of March of this year which I think has a 37.31 percent common equity ratio -- whether or not that was normal or abnormal for the industry, and you indicated you weren't sure. But you did say it wasn't normal for the Empire District Electric Company; is that correct?

A. That's correct.

Q. In your mind is the Empire District Electric Company in this day and age a typical or normal electric utility?

A. No. Well, whether Empire has been typical for a number of years, and by number of years I mean for maybe the last ten years or so, that's a question in my mind. I really don't have an answer.

But Empire is not a typical industry the way that the -- or typical company the way the industry is going. Companies are getting larger and larger. They're moving into more and more nonregulated areas.

Empire, I think it was brought up or a question was asked about what part of Empire is nonregulated. It is -- over 99 percent of our business is regulated. That probably is not typical of what the industry is seeing now.

Q. What was the common equity ratio, if you recall, in the period prior to the announcement of the UtiliCorp/Empire merger which would have been the period prior to May of 1999?

A. At the end of May 1999, it was 44.7 common equity, 6.44 percent preferred, and 48.86 long-term debt.

Q. Mr. Krueger asked you about the trust-preferred securities, and you indicated that they had an 8.5 percent issue price; is that correct?

A. Yes, that's correct.

Q. And you also said that they must be paid off before the common shareholders are paid off?

A. That's correct.

Q. Would you characterize the trust-preferred securities as less risky than your common stock?

A. Yes, they are. They are less risky, and I think, you know, one of the -- even though they're 8.5 percent, the one thing when we looked at the financing early this year, actually in March of this year, we looked at common equity. That's really what we wanted to issue, but part of our charge as -- while running a company is to make decisions that benefit not only our stockholders but also our customers.

And that's the one thing I think we take very seriously at Empire is that we do tend to make decisions that benefit not only the stockholders and the employees but also the ratepayers, because ultimately if we don't succeed there, we'll be out of business. We'll be out looking for a job.

The trust-preferred really is a new entry for Empire. We have not issued that before, and it gives us -- as I mentioned before, it gives us the benefit of not being treated as debt by the rating agency, but at the same time we get a tax deduction. The net result is a lower cost for the ratepayers.

And, you know, that's something that I think we can't or we shouldn't overlook is that in the long run what we're trying to do is to minimize the cost to ratepayers by maintaining a capital structure that is responsible and that the market views as less risky.

MR. SWEARENGEN: Thank you. That's all I have.

JUDGE RUTH: Thank you. You may step down. Thanks.

(Witness excused.)

I want to go off the record for just a second.

(Discussion off the record.)

JUDGE RUTH: Empire, are you ready to call your next witness?

MR. SWEARENGEN: We are. At this time I would call Myron W. McKinney.

(Witness sworn.)

JUDGE RUTH: Thank you. Mr. Swearengen, you may proceed.

MR. SWEARENGEN: Thank you, your Honor.

MYRON W. McKINNEY testified as follows:

DIRECT EXAMINATION BY MR. SWEARENGEN:

Q. Would you state your name for the record, please.

A. Myron W. McKinney.

Q. And by whom are you employed and in what capacity?

A. Empire District Electric Company. I'm President and CEO.

Q. Did you prepare for purposes of this case certain direct, rebuttal and surrebuttal testimony in question and answer form?

A. Yes, I did.

Q. Do you understand your direct testimony has been marked as Exhibit 3, your rebuttal testimony as Exhibit 23, and your surrebuttal testimony as Exhibit 27?

A. That's correct.

Q. Do you have copies of those testimonies with you this morning?
A. Yes, I do.
Q. Do you need to make any changes with respect to your direct testimony?
A. No.
Q. With respect to your rebuttal testimony, are any changes necessary?
A. No.
Q. With respect to your surrebuttal, do you need to make any changes?
A. No.
Q. If I asked you the questions which are contained in Exhibits 3, 23 and 27, would your answers here this morning under oath be the same?
A. Yes, they would.
Q. And would they be true and correct to the best of your knowledge, information and belief?
A. To the best of my knowledge, yes.
MR. SWEARENGEN: Your Honor, with that, I would offer into evidence Exhibit 3, 23, 27, tender the witness for cross-examination, once again recognizing that, with respect to those testimonies, there are issues present which are not being litigated today. So I have no objection to you reserving ruling on the admission of those until

we're finished with the proceeding.

JUDGE RUTH: Let me clarify that with the parties, then. Do you have the same concern, Mr. Conrad or anyone else, as to these exhibits being admitted right now?

MR. CONRAD: These -- I believe, and counsel can correct me, but the only other issues that Mr. McKinney was offered on were the payroll and the incentive compensation issues.

MR. SWEARENGEN: I believe that's correct. I believe Mr. Conrad is right. I believe those are the only other remaining contested issues that Mr. McKinney has filed testimony on.

And I indicated to Mr. Dottheim, who is, in fact, handling the compensation issue for the Staff, that I would ask you to reserve ruling on those exhibits until we do litigate that issue next week.

JUDGE RUTH: Okay. And that is all three exhibits, then, that will need to be held back?

MR. SWEARENGEN: I can't say for sure with respect to Exhibit 3, which was his direct testimony. I don't believe there are any contested issues in that document. Someone else might have a difference of opinion. I was talking mainly about the rebuttal and surrebuttal testimony.

JUDGE RUTH: Then let me ask the parties then if they have any objections to Exhibit No. 3, the direct testimony, being admitted at this time?

MR. CONRAD: I do not.

MR. KRUEGER: No.

JUDGE RUTH: Then as there are no objections, we will admit Exhibit 3, the direct testimony. However, I will reserve ruling on rebuttal, Exhibit 23, and the surrebuttal, Exhibit 27.

(EXHIBIT NO. 3 WAS RECEIVED INTO EVIDENCE.)

MR. SWEARENGEN: Thank you. And I would tender the witness at this time.

JUDGE RUTH: Mr. Conrad?

CROSS-EXAMINATION BY MR. CONRAD:

Q. Good morning, Mr. McKinney.

A. Good morning, Mr. Conrad.

Q. I'll try to be very quick and hopefully bloodless for both of us.

A. That would be appreciated.

Q. On Exhibit 3, your direct testimony, page 5, I just simply need a hopefully very quick and easy clarification from you. I'm looking at the question and answer that begin on line 13 on that page.

A. Yes.

Q. And there you're discussing the implications or more properly, I think, if I correctly read your testimony there, the lack of relationship between this case and the failed merger?

A. That was the idea, yes.

Q. Are you able to confirm for me that it is -- CEO and president, as you mentioned, that it is the company's intent to exclude from this case any merger-related costs, any merger-related expenses?

A. Costs and expenses, yeah, that's absolutely our intent.

Q. I understand that the thrust of some of your testimony here is to be that you may not be able to do that as cleanly and smoothly with respect to the stock price and there may be some need to make some adjustments there, but the purpose, if I understand your testimony, is still to try to take the merger away?

A. Yes. And particularly at the time this direct was prepared, Mr. Conrad, I was thinking in terms of expenses and revenues, that those definitely did not need to reflect anything, any costs in particular that had to do with the merger, which had not failed at that point in time.

Q. So if anybody else in this proceeding should find any cost or expense item that really belonged to the merger and had been missed, it would still be your position that that should be excluded?

A. Yes, as long as they're clearly identified as being associated with the merger. That's been our position.

MR. CONRAD: Thank you, your Honor.

JUDGE RUTH: Mr. Coffman?

MR. COFFMAN: No questions.

JUDGE RUTH: Mr. Krueger?

MR. KRUEGER: No questions, your Honor.

JUDGE RUTH: Commissioner Murray?

QUESTIONS BY COMMISSIONER MURRAY:

Q.   Good morning, Mr. McKinney.

A.   Good morning.

Q.   I just have one question. On page 4 of your direct testimony, at line 18, you say, Unfortunately in Missouri there is no other means for achieving any relief from major construction expenditures or increased operating expense except the initiation of a general rate case. Do you see that?

A.   Yes.

Q.   In the other jurisdictions in which you operate, what other means are available?

A.   Particularly what I was referring to there probably more than anything else was recovery of fuel expense. In three other jurisdictions where we operate, Federal Energy Regulatory Commission, state of Arkansas and state of Oklahoma, there are mechanisms which allow the recovery of fuel expense without the processing of a general rate increase.

Q. So that was your only reference there?

A. Yes.

COMMISSIONER MURRAY: Thank you.

JUDGE RUTH: Okay. Do the parties have any recross based on the additional question from the Bench?

MR. CONRAD: No.

MR. KRUEGER: No, your Honor.

JUDGE RUTH: Seeing no questions, Empire, you may have redirect.

MR. SWEARENGEN: Just a couple, your Honor.

REDIRECT EXAMINATION BY MR. SWEARENGEN:

Q. Mr. McKinney, Mr. Conrad was asking you about your direct testimony which I think you indicated was prepared in, say, October of the year 2000. It was filed in November of 2000; isn't that correct?

A. That's correct.

Q. And at that time the merger with UtiliCorp was still under way; isn't that true?

A. It was very real at that point, yes.

Q. UtiliCorp had not announced that the merger was going to be terminated; is that right?

A. That's correct.

Q. And it was your intention in filing this case and it continues to be your intention not to reflect any costs associated with that merger in this proceeding; is that right?

A. That's correct.

Q. Now, Mr. Conrad was asking you about some related matters with respect to stock price and some things that would have to be done as a result of the merger.

Is it your view that the company's position with respect to capital structure and the stock price is consistent with your testimony here that you're not seeking to recover any costs of the merger?

A. I think my position is that our -- obviously our capital structure has changed subsequent to the merger, and our position is that we would like for the capital structure that's utilized in this case to reflect a more normalized capital structure, which would be obviously a lower amount of debt and a higher percent of common equity.

Q. So the capital structure that's existing now at the end of March is a direct result of the merger; is that true?

A. Yes, it is.

Q. And the way that that can be utilized in this proceeding would provide a benefit for the ratepayer --

A. Yes.

Q. -- over and above what your normal capital structure might have been; is that true?

A. That's correct.

Q. And the same is true if the stock price used in the DCF formula reflects the premium that UtiliCorp was going to pay for the Empire stock?

A. Yes. The stock price that's reflected in some of the testimony in this case obviously does have a -- was impacted by the pendency of the merger and the expectations of the Empire stockholder that they would receive a much higher price for their shares of stock.

That obviously is not the case since January 2nd of this year. Our stock has traded in the range of 17.50 to $20 a share, which is considerably less than was found in some of the testimony in this case.

Q. So using the inflated stock price would ultimately inure to the benefit of the ratepayer in this proceeding through the DCF formula; is that correct?

A. Yes, that's right.

Q. But you're not seeking to recover any of the costs of the merger in this case, are you?

A. Absolutely not.

MR. SWEARENGEN: That's all I have. Thanks.

JUDGE RUTH: Okay. Mr. McKinney, you may step down. Thank you.

(Witness excused.)

MR. SWEARENGEN: That's all we have on this issue, your Honor, as far as our witnesses are concerned.

JUDGE RUTH: And the next witness will testify on what issue? So this will be Staff's witness on this issue, and that's Ms. McKiddy?

MR. KRUEGER: Correct.

JUDGE RUTH: Call your witness, then.

MR. JOYCE: Staff calls Roberta McKiddy to the stand.

(Witness sworn.)

JUDGE RUTH: Please be seated.

ROBERTA MCKIDDY testified as follows:

DIRECT EXAMINATION BY MR. JOYCE:

Q. Ms. McKiddy, would you state your name for the record, please.

A. Roberta McKiddy, M-c-K-i-d-d-y.

Q. And where are you employed?

A. I'm employed with the Missouri Public Service Commission.

Q. And what is your job at the Commission?

A. I'm a Public Utility Financial Analyst.

Q. And did you prepare and cause to be filed in this case written direct, rebuttal and surrebuttal testimony that's been premarked as Exhibits 61, 62 and 63?

A. Yes, I did.

Q. And do you have any corrections or additions to those?

A. Yes, I do have some corrections to my direct testimony. The first correction is on page 2, at line 12, the range should be 8.13 to 8.52.

MR. SWEARENGEN: Excuse me. What was that again?

THE WITNESS: Page 2, line 12, the range should read 8.13 to 8.52.

MR. SWEARENGEN: Thank you.

THE WITNESS: And on page 11, at line 19, it should read 3.3 percent rather than 3.4 percent. Page 20 at line 4 should read 7.88 percent.

On page 23 I need to make some corrections in language to account for the schedule that I had mistakenly quoted the stock price -- or growth rate. Excuse me. On sentence one, beginning with Standard & Poor's Corporation should be stock guide instead of earnings guide.

MR. SWEARENGEN: What line are you on? I'm sorry.

THE WITNESS: Line 1, page 23. Should read Standard & Poor's Corporation's stock guide February 2001. And on line 2, should be provides rather than projects. Then it should read five-year historical EPS.

And then I need to add a sentence for clarification, which will read, Given the lack of a published five-year projected EPS growth rate by S&P, Staff believes that investors will use historical growth as a reliable indicator of projected growth.

JUDGE RUTH: I need you to repeat that much slower, please.

THE WITNESS: Sure. Given the lack of a published five-year projected EPS growth rate --

JUDGE RUTH: Okay. Hold on.

THE WITNESS: -- by S&P, Staff believes that investors will use historical growth as a reliable indicator of projected growth.

JUDGE RUTH: Thank you.

THE WITNESS: Then on page 34, at line 23, again the range should read 8.13 to 8.52. At page 35, line 2, again the percent should read 7.88 percent. And then on line 7, again the range should read 8.13 to 8.52.

My last correction will be to Schedule 13 of my direct testimony. Under the section entitled Projected Growth Rates From Outside Sources, the third source down should read, Five-year historical EPS growth rate. And the second line of that description should read, Standard & Poor's Corporation's Stock Guide.

MR. SWEARENGEN: Could you give me that first change again, please?

THE WITNESS: Sure. The first line of the third source there should read, Five-year historical EPS growth rate.

MR. SWEARENGEN: As opposed to projected?

THE WITNESS: Correct. That's to coincide with the language change I made earlier in the testimony.

MR. SWEARENGEN: Thank you.

THE WITNESS: And then in Footnote No. 2, the last sentence should be deleted, the line that reads, Standard & Poor's resumed reporting a projected EPS growth rate for EDE February 2001.

And that is all of my corrections.

BY MR. JOYCE:

Q.   Ms. McKiddy, if I asked you the questions contained in Exhibits 61, 62 and 63, would your answers be the same?

A.   Yes, they would.

Q.   And would they be true to the best of your knowledge, information and belief?

A.   Yes, they would.

MR. JOYCE: Your Honor, I offer into evidence Exhibit 61, 62 and 63. The issues in those -- in that information is solely considered under this issue.

JUDGE RUTH: Thank you. Do the parties have any objections to the direct testimony, which is Exhibit 61, or the rebuttal, Exhibit 62, or the surrebuttal, Exhibit 63 for Roberta McKiddy?

MR. KRUEGER: We do not.

MR. CONRAD: We do not.

JUDGE RUTH: As there are no objections, these three documents will be admitted into the record.

(EXHIBIT NOS. 61, 62 AND 63 WERE RECEIVED INTO EVIDENCE.)

MR. JOYCE: Thank you, your Honor. I now offer or tender Ms. McKiddy for cross-examination.

JUDGE RUTH: Thank you. Mr. Conrad?

MR. CONRAD: No questions, thank you.

JUDGE RUTH: Mr. Coffman?

MR. COFFMAN: No questions.

JUDGE RUTH: And Mr. Swearengen?

MR. SWEARENGEN: I have a few.

JUDGE RUTH: Please proceed.

CROSS-EXAMINATION BY MR. SWEARENGEN:

Q. Good morning, Ms. McKiddy. How are you?

A. Good morning. I'm fine.

Q. Let's get right to the DCF model. Let's start out with that. I'm looking at page 23 of your direct testimony. Do you have that?

A. Yes, I do.

Q. That's where you begin your discussion, I think, of the discounted cash flow or the DCF model; is that true?

A. Yes, I believe that is true.

Q. And beginning on line 16 you state that even though the DCF model requires the use of a current spot market price, for purposes of this case you have chosen to use a monthly high/low average market price of Empire's common stock; is that correct?

A. Yes, that's been our position.

Q. And more specifically, for purposes of your testimony in this case you have chosen the period, as I understand it, October 1, 2000 through March 4, 2001 to calculate the price of Empire's stock to use in your DCF model; is that correct?

A. Yes, that is correct. I chose that time period to accomplish what I called a normalization of the stock price. It appears my average is around $24, and the price of Empire stock previous to the merger announcement by six months previous was about $23.

Q. Let me ask you this question. Is it your understanding that, given the fact that this rate case was initiated by a tariff filing by Empire in November of 2000, and given the usual 11 months that it takes to process these contested cases, would you agree with me that the Commission's decision in this case and the implementation of new rates will not likely occur until the end of September or the first part of October of this year, in that neighborhood?

A. I believe the operation of law date is sometime in September.

Q. So the answer would be yes?

A. Yes.

Q. I think I heard somebody say earlier this week September 21. I haven't actually made that calculation. Would that be approximately one year removed from your October 1, 2000 starting point for calculating the stock price to use in your DCF model?

A. Looking solely at the time periods, yes.

Q. And your March 4, 2001 cutoff date for the stock price for purposes of this case is approximately seven months removed from the time the Commission will render its decision and presumably new rates will take effect; is that true?

A. Again, just looking at the dates, that is correct.

Q. Would you agree that with respect to the DCF model, that one of the basic principles is to use a recent enough stock price so that it is representative of current or present investor expectations?

A. Under normal circumstances, that is true. Given the circumstances surrounding Empire with the merger termination, I believe what I have done is appropriate.

Q. Well, that really wasn't my question. My question was with respect to the use of the DCF model in general, would you agree that one of the basic principles is to use a recent enough stock price so that it is representative of current or present investor expectations?

A. That is the basic premise of that calculation of that model, but I do not believe that the current stock price is what I would call normal stock price.

Q. I understand that. We'll get to that in a minute. But what I'm trying to establish here is your understanding of the basic principle of the DCF model, and I believe you said --

A. I will agree with your statement, yes.

Q. Thank you. Would you agree with me that Empire's stock price or prices at a point or points close to the time when the Commission makes its decision will likely capture investor expectations concerning Empire's stock price at the time of that decision?

A. It is assumed that it does.

Q. And isn't it a fact -- have you read Mr. Burdette's testimony, the Public Counsel witness in this case on this issue?

A. I've read it briefly, yes.

Q. Isn't it true that he has said in his testimony in this case that stock prices which are too old don't provide a current view of capital costs and are inappropriate to use in the DCF model?

A. I recall him making that statement.

Q. And do you agree with Mr. Burdette on that point?

A. I believe what I have done is more appropriate.

Q. Well, do you agree with Mr. Burdette on --

A. I would have to say no.

Q. Okay. So turning again to page 23 of your direct testimony at line 17, when you say there that the DCF model requires the use of a current spot market price, do you understand that to mean something other than the present price?

A. No. It does mean present price, but as Mr. Murry indicated in his testimony earlier, analysts have some discretion as how they choose to interpret those terms, and we choose to interpret them by doing an average of stock price.

Q. So I'm not sure what your answer is then. Are you saying that it means something other than the present price or it means the present price or --

A. Stock price is a price at a particular point in time. That's my answer.

Q. But you said in your testimony that the DCF model requires the use of a current spot market price.
A. That is what the basic model states, but as I indicated, there are analyst discretions in how to interpret what terms to put into a DCF calculation.
Q. And you've done it somewhat different than the normal standard; is that a fair statement?
A. Yes. I have followed what has been standard procedure for our department and has been recommended and accepted by this Commission in past cases.
Q. Would you take a look at page 24 of your direct testimony, please, and there -- well, it shows up several places, but on lines 19 and 20 you have a dividend yield of 5.50 percent; is that correct?
A. That is correct.
Q. And that comes off your Schedule 14 to your testimony?
A. Yes. That's the averaging of the high and low stock prices against the dividend for the period October through March.
Q. Have you continued to monitor Empire's stock price since you filed your direct testimony in this case back in April of this year?
A. Yes, I have.
Q. Would you agree with me, then, that since

March of this year, the stock has traded in a narrow range of say between 19 and $20?

A. It's traded on an average of about $19.90, yes.

Q. You've read Mr. Murry's testimony, Mr. Don Murry, the Empire witness in this case, I take it?

A. Yes.

Q. And am I correct that he noted, for example, on May 2nd, 2001 the stock closed at $19.10, and you would have no reason to dispute that, would you?

A. I would tend to agree with that, yes.

Q. Are you aware of what the stock closed at yesterday?

A. No, I am not.

Q. If I said $19.75, would you --

A. Well, like I say, I looked at it, but as far as can I recall it this morning, no. It's been staying fairly steady over the last several months.

Q. And steady in what range?

A. Steady in the $19.90 range.

Q. Thank you.

Looking again at page 24 where you make your DCF calculation there at the bottom, if you took a current spot market price for Empire's stock, say the $19 and -- what was your number?

A. $19.90.

Q. And let's just say you used that instead of the monthly high/low average market price for the period October 1, 2000 through March 4, 2001, as you have done in your testimony. Would that change the DCF calculation shown on page 24?

A. The DCF yield would show slightly higher than what I have stated in my testimony, but you'd also need to take into consideration that the growth rate projections have changed also, which would lower that, making the results pretty similar to what I currently have.

Q. Instead of the $19 and how much did you say? What's the number you're talking?

A. $19.90, approximately.

Q. Instead of that, let's just -- let's just round that up to $20, for example, and plug that in to your DCF calculation there on page 24. You said it would change the DC-- it would change the dividends yield; is that right?

A. That's correct.

Q. And that's what's shown in the first column; is that true?

A. That is correct.

MR. SWEARENGEN: Could I have an exhibit marked at this time?

JUDGE RUTH: Yes. I believe we're on No. 101.

Could you describe it for me, please.

MR. SWEARENGEN: It's -- well, I think I'll let the witness describe it. It's the direct testimony of Roberta McKiddy with a couple of changes.

(EXHIBIT NO. 101 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY MR. SWEARENGEN:

Q. Ms. McKiddy, you have in front of you what has been marked for identification as Exhibit 101, I believe, and let me tell you that if you would look at page 24 of your direct testimony, what I have attempted to do in this document is restate that testimony beginning with line 11 through line 23.

A. That appears to be what you have done here, yes.

Q. Making a change, and that is putting the $20 share price in place of your $20.11 to $29 range, and have recalculated the dividend yield and the resulting change to the cost of equity.

And my question is, does this look correct to you? Would this be a correct result if one made just that one change?

A. If you just make that one change, that would be the correct results. However, as I stated earlier, you true up one item in a formula, you need to true up all items, which would include a true-up of the growth rate.

Q. Well, we'll get to the growth rate a little bit later.

Let me ask you, if someone used or applied the DCF model in this case the way I have described it, the way you have described it, the way it is shown on Exhibit 101, using the $20 stock price instead of the price you used, would the resulting cost of equity be correct?

A. Yes. The way you show it, this is correct.

Q. Could the Commission reasonably rely on it in determining a cost of equity for Empire in this case?

A. As shown, yes, but as I also qualified earlier, you need to true up the growth rate to give a more accurate picture before the Commission can make a proper recommendation.

Q. But the Commission could rely on Exhibit 101?

A. If it had all the terms trued up, it could.

Q. Well, I thought you said first that they could rely on this, and then you stated your preference that something else be done. But my question is, Exhibit 101 the way it is, could the Commission rely on this in determining a cost of equity?

A. I do not believe so because the growth rate has not been trued up as the stock price has.

Q. So your testimony would be, then, if you trued

up the growth rate --
A. The results would be reliable, yes.
Q. Okay. Thank you.
So you would agree with me, then, I guess, that a reasonable person could conclude that some other stock price other than the one that you have put in your DCF formula could be used in the DCF model in this case, for example, of the $20 that I have put in here, which is actually a little bit higher than you say the price has been for the stock?
A. Well, I still believe that my normalization process that I did for the stock price is the most appropriate stock price to use. I do not believe that Empire's stock has traditionally traded at the $19 that it currently is, like I stated earlier. Five months to six months prior to the merger announcement it was trading at almost $23.
Q. I understand that, and I understand you're saying that this really isn't your referred method. But my question is, is this something that the Commission could reasonably rely on and do in this case? I realize it's not --
A. I believe they could consider it. Do I consider it to be most reliable recommendation? No, I do not.

Q. That wasn't my question. My question wasn't whether you thought it would be the most reliable. My question is, is this something that they could reasonably rely on?
A. In the form that you have it here?
Q. Yes, ma'am.
A. With the growth rate that you have, no, I do not believe it is reliable.
Q. And that -- let me make sure I understand why. You're not taking issue with the stock price on here, are you?
A. No.
Q. You're taking issue with the fact that you think another adjustment needs to be made over on the growth rate; is that true?
A. What I'm taking issue with is, if you want to true up the stock price, you must also true up the growth rate. You cannot choose to true up one and not the other because it represents two different time periods.
Q. So I want to make sure I understand. For the time period that we're talking about, which is June 1, 2001, the $20 a share price is okay as far as you're concerned so long as another adjustment is made reflecting the current growth rate; is that your testimony?
A. If staff will take the position to true up the

stock price, they would also want to take the position to true up the current growth rates, which are somewhat lower than what they were when testimony was filed.
Q. I don't think you're answering my question. My question is, you're comfortable with the $20 stock price as of this --
A. No, I'm -- as you have it stated here, I do not object to this being representative of what Empire's current stock price is trading at.
Q. Okay.
A. What I do object to is I do not feel it is a normal stock price for Empire based on the fact that they were trading at $23 a share prior to the merger announcement.
Q. That's a little bit different answer than what I understood you to say before. I thought I heard you say that the $20 stock price on here is okay and you could live with that so long as the growth rate was trued up, and now I'm hearing you say, no, the $20 stock price isn't any good.
A. No. I'm saying if Staff would agree with the position to true up ROE, which it has not taken that position, and you wanted to use current stock price, $20 would be an agreeable stock price because that is reflective of what it's currently trading at. What I'm not saying is that I feel that is a normal price for Empire to be trading

at.

Q. So you dispute the $20, then? You're saying --

A. I do not feel that is a normal trading price for Empire, no. I believe it is deflated because of the merger termination. In February I realize in looking at stock prices there was a very high volume of trading that day, which leads me to believe that investors have some feel that the stock is going to appreciate back up to its normal level, which I believe my averaging technique states the price as what I believe the investors believe that price will inflate to.

Q. So let me make sure I understand. Would it be your testimony, then, that no reasonable person could conclude that some other stock price other than the price you have put in your DCF model should be used in this case?

A. I don't believe I'm saying that at all. Analysts have discretion as to what inputs they want to put into the DCF formula. I just don't tend to agree with what you've done here.

Q. But a reasonable person could agree with what I've done here, that's what you're saying? You don't, but --

A. Depends on how you define reasonable.

Q. How would you define --

A. There's different levels of reasonable.
Q. Do you think the public --
A. I don't have an exact definition.
Q. Do you think the Public Service Commission is reasonable? Do you think these Commissioners are reasonable?
A. Well, I know they've accepted my position in past cases. So I would assume that my position is reasonable in their minds.
Q. So based on that, then, am I hearing you say that they're only reasonable if they accept your position and they can't accept somebody else's position?
A. No. I think what they do when they make their decision is they look at all recommendations put before them and they choose the one that they believe in their minds is most reasonable, and just happens to have been my position.
Q. Let me ask you this question, then. Let's just say that when this Report and Order comes out and the Commission discusses this and they have selected to use $20 as the stock price in the DCF formula. Let's not talk about anything else, just that they picked 20 bucks. Would you say they were unreasonable in doing that or would you say they were reasonable in doing that?
A. I make no judgment as to the Commission's decision. It's their job to provide rationalization for it.

Q. Okay. So in other words, under no circumstances could you support the $20 is what you're saying?

A. I don't believe it's appropriate.

Q. Okay. Now, I think you said you prepared or at least you filed your direct testimony on April 3, 2001; is that right?

A. I believe that is correct.

Q. And in putting together your direct testimony you considered Empire stock price up to the first part of March 2001 at a point in time about 30 days before you filed your testimony; is that correct?

A. That is correct.

MR. SWEARENGEN: Could I have another exhibit marked, please?

JUDGE RUTH: Yes. This will be marked as 102 for identification.

(EXHIBIT NO. 102 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

JUDGE RUTH: Let me ask, is this different from something that's been offered or --

MR. SWEARENGEN: Not yet. It may be before we're finished. May I proceed?

JUDGE RUTH: Yes.

BY MR. SWEARENGEN:

Q. Ms. McKiddy, I believe you have in front of you what has been marked for purposes of identification as Exhibit 102, and I will tell you that this is Schedule 25 to Empire witness Murry's testimony. So I assume you've seen it before. It's also, I think, Schedule 1 to Myron McKinney's testimony. I take it you've seen this; is this true?
A. Yes, I have.
Q. What is your understanding as to what this shows?
A. Looks to me to be Empire stock prices starting at October 2nd of 2000 up to March 26 of 2001.
Q. And those would be Empire daily closing prices?
A. That's what it says at the top of the page, yes.
Q. So during any given particular day, the stock would be above or below that particular point; is that true?
A. Restate your question.
Q. Well, it's Empire daily closing price. During any particular day, the stock could actually be higher than or lower than --
A. Yes.
Q. -- what is represented on this document?
A. That is true.

Q. Do you have any reason to doubt the accuracy of this? You've had it for some time.
A. No.
Q. You didn't take issue with it in your testimony?
A. No.
Q. I think you said during the five-month period that you considered, the October 1, 2000 through March 4, 2001 period, Empire stock ranged from a low of 19.80 to a high $30.75 per share; is that correct?
A. I believe that's fairly accurate.
Q. I think that's what you say on page 24 of your testimony, if I read it right.
For the three months since January 2nd, 2001, do you have any reason to dispute, as is shown on Exhibit 102, that the prices ranged from a low of approximately $17.50 per share to a high of approximately $20 a share?
A. That appears to be what this shows.
Q. Now, if I looked at your Schedule 14 to your direct testimony, I'm looking at column 3, the average of the high and low price, and if I add all those up and do the division, is it $24.26, is that the average price?
A. I believe that's close.
Q. And Mr. Murry in his testimony said that the

price of the stock was $19.10 on May 2nd, 2001. That would be $5.16 below your average price, the 24.26; is that right?

A.   Just looking at the numbers, that would be true.

Q.   And it's $11.65 below the $30.75 stock price which occurred during the five-month period that you considered; is that true?

A.   Again, just looking at the numbers, that would be true.

Q.   And you may have mentioned this earlier, but at page 23 again of your direct testimony, in that paragraph which begins on line 14 in explaining how you selected an Empire common stock price to use in the DCF model, you said that your averaging technique -- and I'm down on line 19 now -- is an attempt to -- excuse me. It's not on line 19.

You say it's an attempt to normalize the effect of the terminated merger between Empire and UtiliCorp United, Inc.; is that true?

A.   Yes, as it relates to the stock price.

Q.   And by normalize can I take it to mean that you're trying to make the stock price conform to a norm or to a standard?

A.   I was trying to make it appear similar to what it was prior to the merger announcement. I was trying to take the effect of the merger out of the picture.

Q. So you would agree, then, that the norm in this case would be to consider Empire absent the influence of what turned out to be a failed merger with UtiliCorp; is that true?
A. That's what I was attempting to do in looking at the stock price, yes.
Q. And then you repeat this at the bottom of page 6 of your rebuttal testimony. Do you have that handy?
A. Yes, I do.
Q. You say it's an attempt to minimize the effect of the terminated merger between Empire and UtiliCorp. And then again in your rebuttal at page 8, I believe, you make the same statement about minimizing the effects of the terminated merger; is that true? Look for example --
A. You're speaking of line 14 or --
Q. Lines 13 and 14, yes. This averaging technique is an attempt to minimize the effects on the dividend yield, which can occur due to daily volatility. It's also an attempt to minimize the effects of the terminated merger between Empire and UtiliCorp.
A. Yes, I am reiterating that point there.
Q. And once again turning to your surrebuttal testimony, Exhibit 63, on pages 5 and 6 of your surrebuttal you emphasize and make the same point. On page 5, line 18 you mention minimizing the impact of the merger termination,

normalize Empire stock price.

Can I take it from that, Ms. McKiddy, that normalizing or minimizing or eliminating the effects of the merger for purposes of determining a cost of capital in this case is an important goal in your mind?

A. I believe in this specific case it was important as a goal. Normally this circumstance does not exist so is not something that I have to state that it's a normalization, but we do in every case that we approach try to do a normalization of stock price.

Q. And that --

A. It's just not so prominently different as it is in Empire's particular case.

Q. I understand. That's why you emphasize this point in your testimony on at least four different occasions, as I've pointed out here.

A. That's true.

Q. And it may appear more often than that.

Would you agree with me that the effect of the pending merger with UtiliCorp caused Empire's stock price to go up?

A. I would say it probably in investors' minds had something to do with the appreciation of the stock price. I believe they probably thought there was better growth opportunities.

Q. Well, let me ask you this question. It's your understanding that UtiliCorp was going to pay a premium for that stock; is that true?
A. They were going to pay a premium. Now, whether the Commission was going to allow recovery of that premium, I don't believe that was the case.
Q. Let me ask, whether or not the Commission allowed it to be recovered in rates, wasn't the deal that Empire would -- shareholders would receive a premium for their stock from UtiliCorp?
A. Yes, I believe there was about a 36 premium in that price, I believe.
Q. The number I had in mind was 38.82. Would you have any reason --
A. That's accurate.
Q. Okay.
A. Since I calculated it.
Q. I was going to say, isn't that what you-all testified to in --
A. But that's also been over a year ago that I wrote that, so --
Q. -- in the Empire/UtiliCorp merger case?
And you've tried to normalize, I think, and you've been very candid about that. One last time, I guess, then. You would agree with me, would you not, that the

impacts of the failed merger should be eliminated or at least minimized for purposes of determining the cost of capital for Empire in this case because they don't represent the norm? You've tried to normalize?
A.   I would believe that would be an accurate statement.
Q.   And once again, would you agree with me that one of the basic principles of the DCF concept is to try to reflect current investor expectations?
A.   That is the basic premise of the DCF model. However, as I indicated earlier, analysts do have some discretion as to what they define as the appropriate terms to be inputted into that formula.
Q.   Analysts have discretion and so do witnesses before the Public Service Commission; is that right?
A.   That's absolutely true.
Q.   Let me ask you, currently, as far as you know, Empire has no merger pending?
A.   Not that I'm aware of.
Q.   Nothing has been publicly announced, to your knowledge?
A.   I've not seen anything.
Q.   Nobody's agreed to pay a 38 percent premium or any premium for Empire's stock?
A.   Have not seen anything, although I'm also not

aware that it may not still be on the wish list.
Q. Would you agree that, generally speaking again, whether or not you use a stock price from a particular point in time or an average from a period or various points in time, either is reasonable so long as it reflects current market conditions?
A. I believe publications on the cost of capital analysis provide both of those as alternatives.
Q. And would you agree with those, that whether you use a stock price from a particular point in time or an average from a period or various points in time, either is reasonable so long as the price reflects current market conditions? Would you agree with that?
A. I'll agree with that.
Q. For example, and you said you had glanced at or reviewed Mr. Burdette's testimony in this case. He used a six-week period for purposes of calculating the stock price, and I think it was from February 16, 2001 to March 23, 2001. Does that sound right?
A. I believe that's what he did.
Q. And he said in his testimony that he did that because in his view six weeks was long enough to avoid daily fluctuations and recent enough to represent current expectations. Do you recall his testimony on that?
A. I recall that he said that, yes.

Q. And using his approach, he came up with a $19.52 price to use in the DCF calculation for the Empire stock; is that your understanding?
A. I believe that was his result.
Q. Now, looking back at Exhibit 101, which we've had some discussion about earlier, we used a $20 per share price for that calculation in that exhibit. If we used the Public Counsel's $19.52 price and didn't change anything else, would that drive the cost of equity up over on the far right side above the 9.4 to 10.4 range?
A. Using a lower stock price than what I used in my calculation, yes, it would.
Q. Using a lower stock price than is shown on Exhibit 101, the $20?
A. Yes, it would drive it up somewhat on the dividend yield side.
Q. Would I be correct in assuming that it would produce a yield of about 6.6 percent and a resulting cost of equity range of 9.6 to 10.6? Does that sound about right?
A. That sounds about right, although I would like to say that I do not agree with Mr. Burdette's stock price because I feel that it totally reflects the termination of the merger and an abnormal stock price for Empire.
Q. Because it doesn't reflect the merger, it's abnormal; is that what you're saying?

A. Well, the stock price was driven down I believe because of the termination of the merger. I believe it's a temporary status. That's why I believe that my averaging the stock prices to bring it up to more normal level is more appropriate than what Mr. Burdette did.

Q. Let me ask you this question. Do you recall -- and I think you mentioned earlier you did because you wrote it or you participated in some of it at least -- the Staff testimony in the Empire and UtiliCorp merger case 2000-369?

A. Yes, I did participate in this case.

Q. And do you recall the Staff testimony which reflected a $21.25 price for Empire stock on May 10, 1999 just before the announcement of the proposed merger?

A. I believe that was the closing price at May 10, 1999 for Empire.

Q. How do you -- let me ask you, did you file testimony on that point?

A. Yes. That was part of my calculation of merger premium.

Q. Okay. My question then is, if Empire stock price before, just before the announcement of the proposed merger with UtiliCorp in May of 1999 was just a little bit over $20, 21.25, and when it was announced 18 months later on January 2nd, 2001 that the merger would not go through and the price fell to the $20 level again, doesn't that mean that the value of Empire as a stand-alone company is approximately $20 a share?

A. No, that does not. What that tells me is the stock price trading on that particular day was $21.25. As I stated earlier, for the six-month period previous to the merger announcement they were trading at approximately $23 per share.

Q. Would you agree that Empire share price data for the 18-month period prior to the termination of the merger on January 2nd, 2001 is really not representative of the current or present value of Empire stock?

A. I didn't calculate to see what the average was over that period of time.

Q. My question is, would you agree that Empire share price data for the 18-month period prior to the termination of the merger on January 2nd, 2001 is not really representative of the current or present value of Empire's common stock?

A. I would say at most points in that year the stock price was inflated to what they are currently trading at.

Q. So would you agree, then, that that data is not really reflective or representative of the current or present value of Empire stock?

A. I would say the way I have used it it is appropriate to consider it. To consider only the time period where the stock price was inflated I don't believe would have been appropriate on my part.

Q. And you haven't done that? You've used a period of time after the merger; is that what you're saying?

A. I tried to use a balancing of a period before and after the merger.

Q. After the merger termination?

A. Correct. When I initially started my analysis, our normal procedure would be to cut off the stock prices at the end of the test year, which would have been December 2000.

However, that created an extremely low result for the DCF, so I chose to try to find an alternative that would provide a normalization of the price given the specific circumstances surrounding Empire.

Q. Is it fair to say that you recognize there's a problem in using stock price data which reflects the impacts of the pending merger?

A. I don't believe the way I used it there is a problem.

Q. But there could be a problem in this case? You've attempted to deal with it, but --

A. It would be difficult for me to say whether there is or isn't.

Q. Well, let me ask you, then, why did you not just simply use the stock price for Empire during the period of time May of 1999 to the end of 2000?

A. Because that's not a current enough period for me.

Q. That's not current enough?

A. Not May of '99 up to this point, no.

Q. Up to the end of 2000 is not current enough?

A. No.

Q. But you have used some of that data in your calculation; is that correct?

A. I have used some prior to the termination of the merger and post termination, and I've done so in order to create a normalization of the price, which is around $24.

Q. And the data which you have used prior to the termination of the merger reflects the anticipated 38 percent merger premium, does it not?

A. It anticipates an inflated price. Now, whether it is the full 38 percent, I don't know. It depends on what the stock price was at that point in time. I think 38 percent was based on a base price of $21.25 with a premium offered of $29.50.

Q. Would you agree, though, that that data for the period prior to the termination of the merger reflected the inflated price as you described it in anticipation of the merger?

A. Looking solely at the stock prices prior to the termination of the merger, yes, that would be correct. That would --

Q. And you've tried to fix that problem?

A. By using stock prices after the termination to create a normalization, yes.

Q. And I understand that and I appreciate that, what you have tried to do. Would you agree, however, that even with your method you're still continuing to reflect the impact of the merger in your calculation?

A. No, I don't believe that I am.

Q. Even though you're using stock price data that anticipated the merger would occur?

A. No, because I believe the average stock price that I have used in which to calculate the dividend yield is around $24, which is very comparable to the six-month average prior to the merger announcement of $23.

Q. Let me ask you this question. Your ultimate return on equity recommendation of 8.5 to 9.5 is based on your Empire-specific DCF analysis; is that correct?

A. That is correct. It's the position of Staff to use the most company-specific data possible.

Q. So you just looked at Empire; is that true?

A. No, I did not. When I did my test of reasonableness, I did a comparable companies analysis.
Q. Okay. You performed alternative analyses on your group of comparable companies to test the validity of your --
A. We do a test of reasonableness, yes, to test the validity of our DCF results.
Q. Now, after you did that, after you tested your DCF results, you didn't make any adjustments to your Empire-specific DCF analysis, did you, as a result of that comparison?
A. Are you speaking to my comparable group analysis?
Q. Any of your analysis.
A. No. I believe both my CAPM and my risk premium did support the upper range of my DCF analysis specific to Empire. And although the comparable companies group ended up with a somewhat higher return on equity estimate, that was due to the differences in growth rate.
Q. So would I be correct in concluding that you reject the notion of giving way to the results of the costs of the comparable group?
A. No, I did not reject the results of the comparable group. I just took into account that it was a higher result simply because of the fact that it had a

higher growth rate.
Q. And you didn't give -- but you didn't give any weight to that? In other words, you did your DCF company-specific calculation for Empire, you compared it to your comparable group, and you just stayed with what you had done for Empire specifically?
A. Yes, because I believe the comparable group results still supported my DCF analysis.
Q. I understand that. So, and let's just say for purposes -- and I know you didn't do this, but let's just say you did the DCF analysis and didn't look at anything, any of the comparable companies. Your result would have been the same, right?
A. If that's the approach Staff would take, that would be true, but Staff does not approach a case that way.
Q. But if you had done that in this particular case, the result would have been the same if you hadn't even looked at any other companies?
A. Again, if Staff chose not to do any other analysis looking simply at DCF, the results would have been what I proposed.
Q. Well, that really wasn't my question. My question was, if you just did an Empire-specific DCF analysis and then didn't look at anything else --
A. Well, I can't answer your question the way you

want me to answer it because that's not how we approach cost of capital analysis.

Q. I understand.

A. We would never do that.

Q. I understand you did the analysis and you did the comparison, but you didn't make any change to your company-specific DCF analysis as a result of your comparison; is that true?

A. No, because there was no need to.

Q. Okay. And so my question is, the result would have been the same whether or not you had done any comparison; is that true?

A. Again, you're assuming that I would only do one calculation and --

Q. Let's just assume you've done this one calculation.

JUDGE RUTH: Just a moment. Can you both slow down for the court reporter and for us, because you're starting to talk over one another.

MR. SWEARENGEN: We'll try not to do that.

JUDGE RUTH: And since I've interrupted, I'll give you a minute or two and then we need to break for lunch. You can either break now or finish your --

MR. SWEARENGEN: Let me finish this question, if I could.

BY MR. SWEARENGEN:

Q. I understand that you say you would never do it that way and I appreciate that. I'm not arguing with you about that. All I'm trying to find out is, would you agree that if you did do it that way hypothetically, that the result would have been the same? In other words, I could have done a DCF-specific analysis, never looked at any other companies and had the same result?

A. Using your approach of only doing one calculation --

Q. Right.

A. -- the results would be what they are.

Q. Right.

MR. SWEARENGEN: Okay. Let's stop there, then. Thank you.

JUDGE RUTH: Thank you. I note that it's 5 minutes after 12. We will break for lunch and come back, start at 1:20, 1:15. We'll make it 1:15. Did you have something?

MR. COFFMAN: I was actually going to request 1:30 if possible. We have an event in our office.

JUDGE RUTH: That's fine. We'll start back up at 1:30 promptly. Off the record.

(The noon recess was taken.)

JUDGE RUTH: Let's go back on the record. We were in the middle of cross by Empire of witness Roberta McKiddy.

MR. SWEARENGEN: Thank you, your Honor. As a preliminary matter, Mr. Duffy asked me to inquire of the Commission as to whether or not Ms. Rolph and Mr. Wilson need to be here on this coming Monday with respect to what I understand is the stipulation on the Stateline capital costs which I believe the Commission has accepted. They're willing to come, but we need to let them know so they can make travel plans.

JUDGE RUTH: Those witnesses will need to attend. Some of the Commissioners may have questions for them.

MR. SWEARENGEN: Thank you. We will get that word to them.

JUDGE RUTH: Please continue.

BY MR. SWEARENGEN:

Q. Ms. McKiddy, before we broke for lunch we were having a discussion about the fact that you did what we called an DCF-specific analysis for the Empire District Electric Company, and you looked at some comparable companies but didn't make any adjustments as a result of that review, and that's true, right?

A. Yes. I did a comparable company analysis only to test the reasonableness of my DCF Empire specific.

Q. And you concluded after that analysis that your DCF-specific analysis for Empire was reasonable; is that right?
A. Yes, I did.
Q. Is it your understanding that the Public Counsel basically followed the same approach, the same general approach, that is performed an Empire-specific DCF analysis and then made no adjustments to that?
A. I believe that traditionally their recommended range is based more on comparable companies analysis than --
Q. So you don't know the answer?
A. No.
Q. And also prior to lunch we were discussing the fact that you said you used, I believe, stock price information during the period of time that the merger with UtiliCorp was still pending between October -- is it October 10?
A. Yes. My stock prices ran from October of 2000 to March of 2001.
Q. Okay.
A. Period prior -- both prior and post merger.
Q. Okay. And you did that, you used pre-merger stock prices and post-merger stock prices to normalize the stock price, right?
A. Yes. I was trying to create a stock price

that was more comparable to the stock price that Empire was trading at prior to the merger announcement.

Q. And I asked you -- and prior to the merger announcement would have been what period of time?

A. Approximately six months prior to the May '99 merger announcement date.

Q. And that would go what period of time, then?

A. That would be probably October of '98 through April of '99.

Q. And so whatever the stock price was in the October '88 (sic) to April '99 time frame, that's what you're trying to replicate here; is that a fair statement?

A. The average stock trading price at that point in time, yes.

Q. I asked you why you didn't just use May '99 to December 30, '99 -- excuse me -- December 30, 2000 data, and I think you said the early part of the data was not current and the entire period reflected the merger; is that correct?

A. Correct.

Q. What data in that period of time, May '99 to December of 2000, was not current enough?

A. I would say anything earlier than October of 2000, which is the time period I chose to start with, would be not current enough.

Q. So let me make sure I understand. You would say any stock price data prior to October of 2000, which is the start point for your study, would not be current enough to use for purposes of your DCF model; is that right?

A. In the specific circumstance of Empire, I believe that is true because it does reflect the inflated stock price as a result of the merger announcement.

Q. What reflects the inflated stock price?

A. The time period May '99 through October.

Q. And anything earlier than that you say is not current enough to use; is that right?

A. In the context in which you say it is, that is correct. But with the circumstance that Empire has found themselves in, I felt that the only appropriate comparable for me to determine what I would categorize as a normalized stock price would have been some stock price average prior to the merger announcement.

Q. So make sure I understand now. You're saying that you wouldn't go before October of '99 for your DCF calculation because that stock price isn't current enough, but yet what you're trying to do is replicate the period October '98 to April '99?

A. No, that's not exactly what I'm saying. What I'm saying is absent the merger announcement, I'm trying to come up with what I believe would have been a stock price that Empire would have been trading at, and the best indicator that I would have of that would be some time period prior to the merger announcement, which is what I've looked at.

Q. Which is your October -- you said October '98 to April '99?

A. Correct.

Q. So you're comfortable with your calculation because your result averages $24, which you think is near the average price for the period of time October '98 to April '99?

A. Absent the merger announcement, I believe that Empire stock would still be trading somewhere in that neighborhood.

Q. So you think that November '98 to May '99 data is current, then?

A. Only because I've had to use that to derive what I would feel would be a normalized stock price absent the merger. Under normal circumstances, I would never look at that time period.

Q. And why is that?

A. Because it is too old.

Q. I think you testified that since January of this year that stock has traded between a low of about 17.50 to a high around $20 and more recently has been in the 19 to $20 range; is that true?

A. I believe that's an accurate characterization.

Q. But you think the price ought to be $24?

A. I believe that absent a merger announcement, that Empire stock would still be trading at a level that they traded at previous to the merger announcement. I believe that the stock price is depressed at this current point in time because it created a certain level of uncertainty with the termination of the merger.

Q. So you would say that the Empire stock price is under value presently?

A. I believe it's a high probability it is, and also, as I noted earlier today, the trading volume of Empire stock in February or immediately preceding the termination of the merger was at some three times the level it normally trades at in volume-wise.

So I believe that those investors do believe that the stock is going to appreciate at some point in time back up to its normal levels.

Q. Based on something that occurred in February?

A. Yes.

Q. And what was that?

A. The stock volume traded on that particular month was about 1.5 million shares, according to the information I have. Empire's normal volumes run in the 3 to 500,000 shares.

Q. What is your source of that information?
A. Standard & Poor's.
Q. Is there a specific document that we could refer to? Is there something you could supply us later?
A. It's something I can supply you with off of Ratings Direct, or Wall Street actually.
Q. Let me ask you this. Turn to page 20, if you would, please, of your direct testimony. There down around line 14 discussing the DCF model you talk about the theory that security prices adjust continually over time so that an equilibrium price exists and the stock is neither under-valued nor over-valued. It can also be stated that stock prices continually fluctuate to reflect the required and the expected return for the investor.
Is that your testimony?
A. That is. Under normal circumstances, I do believe that is true. Empire does find itself in a unique situation.
Q. So you think there's something about Empire District Electric Company that is unique and that this rule that you cite on that page of your testimony doesn't apply to their stock price?
A. It would be accurate to say that I don't believe that rule necessarily applies to Empire at this point in time, although it is an underlying assumption of

the DCF.

Q. Would you agree with me that a key principle of the DCF model is to calculate the cost of capital based on an anticipated stream of earnings or dividends?

A. That is correct.

Q. Turn to Schedule 27 of your direct testimony, would you please. Do you have that in front of you?

A. Yes, I do.

Q. I'm looking at the far right column, 2001 projected return on common equity for your nine comparable companies. That's what's shown there, is it not?

A. That is correct.

Q. And the average estimated or projected return on common equity for the year 2001 for those nine comparable companies that you have chosen is 15.5 percent; is that correct?

A. As of July 7, 2000, that is a correct number.

Q. And then below that you show a 12 percent figure for the Empire District Electric Company. Would that be the projected return on common stock equity of Empire?

A. Yes. Again, as of July 2000, that was the projection given by Valueline.

Q. And I think you testified earlier, and I think it's in your surrebuttal testimony, that you note that a Valueline survey dated April 6, 2001 estimated Empire's projected return on equity to be 9 percent in 2001; is that right?

A. Yes. That is now the new revised projection submitted by Valueline.

Q. Let me ask, in your opinion, is the 12 percent that you show on your Schedule 27 for Empire comparable to the 15.5 percent that you show for your other nine companies?

A. I believe it shows there is a difference.

Q. So is it -- are they comparable or not comparable?

A. You're talking a difference of 350 basis points. I would call that a pretty big difference.

Q. And then I guess you would agree that the 9 percent isn't comparable either to the 15.5? If the 12 percent isn't comparable, then the 9 percent certainly isn't comparable?

A. Looking solely at return on equity, no, it's not.

Q. According to my calculations, 12 is about 30 percent lower than 15.5, and 15.5 is about 1.7 times greater than 9. Does that sound about right to you?

A. That sounds about right.

Q. Why did that estimated return drop from 12 to 9 percent, do you know?

A. I have no exact answer as to why Valueline changed their revisions or their projections.

MR. SWEARENGEN: Could I have another exhibit marked, please?

JUDGE RUTH: Yes. This is 103.

(EXHIBIT NO. 103 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY MR. SWEARENGEN:

Q. Ms. McKiddy, you have in front of you what has been marked for identification as Exhibit 103. Are you familiar with this document?

A. Yes, I am.

Q. And is this the Valueline report dated April 6, 2001, that you referred to in your surrebuttal testimony?

A. Yes, it is.

Q. Okay. Looking towards the -- in the middle part of that document, about two-thirds of the way down, you see the words Empire District Electric Company's prospects for 2001 are not bright? It actually says Empire District --

A. I see where you're at.

Q. -- Electric's prospects are not bright.

A. Yes.

Q. You see that language?

A. Yes, I do.

Q. Have you reviewed this document previously?

A. Yes, I have, and I believe what that's referring to there is the natural gas and fuel costs.

Q. And does this explain why perhaps it dropped from 12 percent to 9 that you refer to?

A. I cannot say that for sure.

Q. Let me ask you this. How does a reduction in projected return on equity, a reduction in it support your 8 1/2 percent to 9 1/2 percent range?

A. Well, the 9 percent projected return on equity clearly falls within my recommended range of 8 1/2 to 9 1/2.

Q. That's your answer?

A. Yes.

Q. Let me ask you this question. Doesn't this make Empire even less comparable to your nine comparable companies, this fact?

A. If you're looking solely at projected return on equity, yes, it does, but I look at more than just the return on equity when looking at my comparable company analysis, and again, I only use my comparable company analysis as a test of reasonableness.

And as stated earlier, the difference in the return on equity calculations between my Empire District specific and the comparable group was attributed to the difference in growth rate.

Q. That took us back to our discussion earlier this morning, and I'm not sure where we left it, but we were talking about the $20 stock price, and at one point you said you thought that might be okay so long as we use some new growth rates, and then I think later you changed your story and said, No, I don't like that. I want the $24. Is that what you're talking about?

A. No. I think what I said earlier this morning was if the Staff chose to agree with the company that ROE should be trued up, that if you're going to true up stock price, would which have averaged at the $20 rate, you would also have to true up the growth rate. But I do not believe that is an appropriate approach, and it has been discussed with division management.

Q. Once again, if the Commission would decide that they were going to accept your DCF formula except insert the $20 stock price, which I think shows up on one of the exhibits we talked about earlier, I think it was Exhibit 101, you have no opinion as to whether or not that would be a reasonable result?

A. I make no determination as to how the Commissioners define reasonable.

Q. In your own mind, would it be a reasonable result?

A. To use just your $20 stock price with the growth rates you had on that exhibit? I do not believe that was a reasonable result.

Q. How about to use the $20 stock price and the growth rate that -- which you had in your prefiled testimony which is on that exhibit, you're saying that's not a reasonable result?

A. I do not believe it is.

Q. That's fine. Have you ever heard of the term regulatory risk?

A. Yes. It's one of the things Standard & Poor's looks at when they do define a credit rating to a corporation.

Q. And how would you define that term?

A. Regulatory risk? I would think that would be defined as the amount of rate relief that this Commission authorizes to a corporation.

Q. Could it have anything to do -- and I'm looking at Schedule DWG, which is the document attached to Empire witness David W. Gibson's surrebuttal testimony.

MR. SWEARENGEN: Can I approach the witness and show her that document, please?

JUDGE RUTH: Yes. First go ahead and show it to counsel.

BY MR. SWEARENGEN:

Q. Ms. McKiddy, perhaps you could just read into the record the first paragraph of that document, please.

A. Okay. Fitch has downgraded and removed from rating watch negative the debt ratings of Empire District Electric (EDE) as follows: Senior secured debt downgraded from A+ to BBB+, preferred stock from A to BBB-, and commercial paper from F1 to F2. Approximately $415 million of debt is affected.

The downgrade reflects the significant erosion of company's credit protection measures in the past two years in a regulatory environment in Missouri that exposes EDE to margin erosion from increased fuel costs. The rating outlook for the company is now stable.

Q. Thank you. That statement about increased fuel costs, would you consider that to be regulatory risk?

A. If you're inferring regulatory risk that should be reflected in my cost of capital analysis, I would say no, because that risk is reflected in stock price.

Q. And why is that risk reflected in the stock price?

A. Because it's public information that the consumers and investors are apparently aware of. It goes to the efficient market hypothesis, to create a more simple answer. Assumes that all public information is known by investors.

Q. I thought you said earlier that you didn't think that hypothesis applied to Empire in this case?

A. No, I don't believe I said that.

Q. What did you say?

A. It depends on what reference you're making.

Q. Well, I asked you if you thought Empire's stock was under-valued, and you said that you thought it was and that hypothesis that you just described, which I think appears in your testimony on page 20, lines 12 through 17, didn't apply to Empire in this case.

A. I don't believe I'm saying that efficient market hypotheses does not hold in the DCF calculation. I think what I'm saying is because of the unique situation Empire finds themselves in with the termination of the merger, that the stock is at a low price compared to what they traditionally traded at prior to the merger announcement.

Q. But you testified about the DCF theory that this results from the theory that security prices adjust continually over time so that an equilibrium price exists and the stock is neither under-valued or over-valued. That's your testimony.

A. And I believe I said under normal circumstances that is the presumption of the DCF calculation. By me doing what I call a normalization of stock price, I don't think I'm saying that the efficient market hypothesis does not still hold.

Q. Is that what you describe there in your testimony, the efficient market hypothesis?

A. I believe it does.

Q. But you don't think it applies to Empire in this case?

A. That's not what I've said.

Q. Once again I'm confused because you say the price is under-valued, but according to the efficient market hypothesis it wouldn't be. It says it's neither under-valued nor over-valued.

A. An I don't believe I said under-valued. I just said that it is a stock price that is trading out now that is not normal compared to what it would have been trading at absent the merger.

Q. Isn't it the current -- well, I agree that if the merger had occurred, the stock price is trading at a much higher level because of the premium that was going to be paid. But didn't you say that basically since January of this year it's traded in a range of 19 to $20?

A. And I believe I attributed that to the uncertainty of the future of the stock and the company.

Q. And you think it ought to be $24?

A. I believe absent the merger, that Empire stock would have continued to trade at a level around $23.

Q. And absent the merger, you're looking at a period of time prior to May of 1999 which you said was too far away to look at to determine a current price for purposes of the DCF calculation?

A. Which I also said was a time period that I would not normally look at but was forced to look at because of the circumstance Empire currently finds themself. There's a difference.

Q. So you don't look at current stock price and the efficient market hypothesis doesn't apply to Empire; is that right?

A. I did not say that.

Q. That's the impression that I got.

A. That's not what I'm saying.

Q. Let's talk about growth rate a little bit. Would you agree with me -- and I really thought price was not a problem, but would you agree with me that, generally speaking, the growth rate is the most controversial aspect of the DCF model?

A. Under normal circumstances, yes, that is true.

Q. But these aren't normal circumstances?

A. I don't believe they are.

Q. Okay.

A. It's required more analysis on my part, I will say that.

Q. Would you agree that by growth rate we mean what investors anticipate with respect to the growth of cash flows?

A. Yes.

Q. And would you also agree that it can be very difficult to determine a growth rate which investors rely on when they evaluate a stock?

A. That is true, and that's why Staff chooses to do an average of historical and projections in determining their range.

Q. Would you agree, then, that the selection of a growth rate in the DCF calculation involves a considerable degree of subjectivity?

A. I would prefer to call it judgment.

Q. Okay. That's fine. Would you agree that there is often a difference of opinion as to the growth rate because of the uncertainty concerning future earnings?

A. I would say that's true.

Q. And would you agree that the selection of a growth rate has a significant impact on the allowed return?

A. It can have, yes.

Q. All other factors being equal, a higher growth rate results in a higher return on equity for the utility; isn't that true?

A. All things else being equal, yes, that would be true.
Q. Turn if you would, please, to page 32 of your direct testimony. Are you there?
A. Yes.
Q. Thank you. I'm looking down at line 15 where you admit that your estimated growth rate for Empire in this case is the reason for the difference in your ROE recommendation of 8 1/2 to 9 1/2 percent and the 10.15 to 11.65 estimated range for your nine comparable companies; is that correct?
A. That is true.
Q. So the growth rate which you selected in this case for the Empire District Electric Company for your DCF calculation is critical to the end result; is that not true?
A. It's a major component of the DCF calculation, yes.
Q. Would you say it's critical to the end result?
A. It impacts the end result, and it is a critical component of the formula.
Q. Earlier in discussing Exhibit 101 where what we did was simply go to your testimony, page 24, lines 11 through 23, and change the price from your range to $20 a share which increased the yield range -- excuse me -- the yield of 6.4 percent, when we had your discussion about that

this morning, at one point I had you biting on that number, the $20 per share, but your caveat was, I want to change the growth rate?

A. Yes. In my opinion, if you're going to true up one component of the formula, you have to true up all components. And as we all know, the growth rate projections for Empire has dropped since that original testimony was filed.

Q. Okay. And so the point of that was, I mean, you would go with the 6.4 percent yield based on the $20 stock price if you could get some other growth rate; is that a fair statement?

A. I --

Q. You said you true it up.

A. Well, I believe what I said is if my division management so agreed to true up return on equity, that that would be an appropriate stock price.

Q. That's an appropriate way of doing it. If we're going to true up stock price, we ought to true up growth rate?

A. Right. But as I've stated earlier, we did have that discussion with division management, and they decided that it was inappropriate to do such a true up.

Q. So back to my original question, it's pretty critical to your calculation the growth rate you accept;

isn't that true? I mean, you can -- with this growth rate shown on Exhibit 101, the resulting cost of equity of 9.4 to 10.4, but if you tinker with the growth rate, which right now you have 3 to 4 percent, if you do the same thing with that, you can take the cost of equity back down, is that right, or you can raise it?

A. Well, the growth rate on my direct testimony did have a range of 3 to 4 percent.

Q. Right.

A. Since the revision by Valueline, I have looked at that revision in growth rate and it would be a much lower number, but yet the end result with the increase in dividend yield would still fall within the range that I have projected and recommended. So I did not feel it was necessary to --

Q. I understand. What would the growth rate be, though, that you think ought to go with that $20 stock price? You've talked about it several times. You said it's come back down.

A. I'm trying to remember what I calculated yesterday. It would probably be in the range of 2 to 3 percent.

Q. As opposed to 3 to 4?

A. As opposed to the 3 to 4, yes.

Q. And as I understand how this works, an increase or decrease in growth rate percentage translates into a direct increase or decrease in cost of equity percentage?

In other words, on Exhibit 101, if you take the growth rate of 4 percent and take it down to 3, then the 10.4 return becomes 9.4?

A. Correct.

Q. Okay. Thanks. Would you agree with me that, assuming there's something wrong with the selection of your growth rate in this case, and I don't expect you to agree that there is, but just for the hypothetical, for example an inconsistency in your use of data or a misrepresentation of some sort or incorrect data or some other problem, that that could detract from the credibility of your cost of equity recommendation?

A. Well, I'm not sure what your question is asking, but what I think you're getting to is the fact that in place of a projected five-year EPS I used a five-year historical from Standard & Poor's. Is that what you're implying?

Q. No. I'm just asking generally speaking. I'm not talking about any specific mistake, and I'm not suggesting that you made one. I'm just saying, if you have, if there's something wrong with your growth rate, an inconsistency in data, a misrepresentation, incorrect data, some other problem, could this detract from the credibility of your recommendation?

A. If given your statement -- and I'm not sure how you're going to define or identify a mistake in my numbers -- it could potentially impact the end result.

Q. Let me ask you this question. Could a reasonable person conclude that some other growth rate other than your 3 to 4 percent should be used in the DCF model for purpose of calculating a cost of common equity for Empire in this case?

A. Well, as I stated earlier, people define reasonable different, and as seen in this case, Mr. Murry does have a different growth rate and a different result than what I have. So yes, there are more than one option to have an end result.

Q. Could a reasonable person conclude that the growth rate ought to be 5 percent, then, for example?

A. I don't believe it would be reasonable to assume that Empire could achieve or could be expected to achieve a 5 percent, and I base that on the fact that Valueline back in 1996 projected a 5.5 future growth rate in earnings per share.

And as we can tell in the April 6th data sheet, Valueline has done a compound growth rate and only indicated that over the past five years Empire has achieved

2.5. So right there you have a 250 basis point difference in actuality versus projection.

Q. So you would say five is probably too high. You've got 3 to 4 percent in your testimony. Would 4 1/2 percent be reasonable?

A. I don't believe so.

Q. How about 4.25 percent?

A. I believe the range I've recommended is appropriate based on past performance and projections.

Q. But you said earlier, I think, in response to my earlier question a reasonable person could conclude that something other than 3 or 4 percent should be used?

A. And again, I said that reasonable is defined differently by each individual. What may be reasonable to Mr. Murry may not be reasonable to me.

Q. So that's what I was trying to test you to find out what you meant by that, but what I'm finding out is that really your answer to that question would be no, that a reasonable person could not conclude that some other growth rate ought to be used, because you've just said that five is no good, four and a half's no good, four and a quarter is not good and 4.1 is no good.

A. I believe that that range is overly optimistic based on past performance.

Q. What range?

A. The 4 1/2 to 5 percent that you have indicated.

Q. Okay. How about 4.25 percent?

A. I still believe that's overly optimistic based on the fact that Empire has only over the last five years achieved about a 2.5 percent growth in --

Q. It's overly optimistic and, therefore, unreasonable?

A. It's not what I believe is an appropriate recommendation.

Q. Okay. And what about 4.1 percent?

A. No.

MR. SWEARENGEN: Could we take just a minute, please?

JUDGE RUTH: Yes. We'll go off the record for five minutes.

(A recess was taken.)

MR. SWEARENGEN: May I approach the witness?

JUDGE RUTH: Yes, but show whatever you have in your hand to counsel first, please.

BY MR. SWEARENGEN:

Q. Ms. McKiddy, I'm going to hand you a book entitled The Cost of Capital, a Practitioner's Guide, by David C. Parcell. Is this the text or the practitioner's guide that you refer to numerous times in your testimony?

A. Yes, it is.

Q. It's the 1997 edition?

A. I believe that's correct.

Q. Would you first of all just read the author's note on the cover into the record, please, for me.

A. Author's note. This manual has been prepared as an educational reference on cost of capital concepts. Its purpose is to describe a broad array of cost of capital models and techniques. No cost of equity model or other concept is recommended or emphasized, nor is any procedure for employing any model recommended. Furthermore, no opinions or preferences are expressed by either the author or the Society of Utility and Regulatory Financial Analysts.

Q. Thank you. Let me ask you to read one more thing into the record from this text, if you would, please. I'm looking at Section 8-7 under growth rate, and if you would read this paragraph 8-17 and right through to the top of the next page for me, please.

A. An almost limitless array of techniques have been used in rate proceedings to estimate the constant growth rate component. Since the dividend discount model is technically concerned with growth in dividends, many methods are concerned directly with dividend growth.

On the other hand, other methods examine factors other than dividend growth to estimate G. The objective of each of these methods is to estimate the growth of dividends (cash flow) within the DCF context. The DCF model is forward-looking in that it is designed to reflect the perceptions of investors as they set the current price of the company's stock.

Q. That's fine. Thank you. Appreciate it.

And I want to get into a line of questioning now, Ms. McKiddy. I think earlier this morning you made some corrections to some of your testimony and schedules, and I kind of just want to go through that, the background of that with you for a few minutes, if I could, please.

If you turn to Schedule 13 of your direct testimony, that's where you made some changes, if I'm not mistaken.

A. That is correct.

Q. On Schedule 13 you showed 2 percent for the five-year projected EPS growth rate Standard & Poor's Corporation's Earnings Guide for February 2001, and then you changed that to stock guide; is that right?

A. Yes.

Q. Do you recall your answer to Empire's Data Request 29A that when asked for a copy of the relevant page from the Corporation's Earnings Guide February 2001 which you cite on that schedule as the source of your 2 percent number you responded, The information requested is supplied by subscription service through Standard & Poor's Corporation Earnings Guide February 2001. Therefore, it will not be possible to furnish a copy as requested. Do you recall that?

A. Yes. That is true.

Q. Is it true that Mr. Murry in his rebuttal testimony at page 15, lines 4 to 5, pointed out that there was no 2 percent forecasted or projected earnings per share growth rate in Standard & Poor's Earnings Guide?

A. That is true, there is no five-year projected. However, I did explain that by saying that due to lack of projected information, Staff believed that the historical information was an appropriate substitute.

Q. You said that later?

A. Yes.

Q. All right. Is it also true that Mr. Murry also pointed out in his rebuttal testimony, page 15, line 6 to 8, that in Standard & Poor's Stock Guide, February 2001, there is a 2 percent earnings growth rate for Empire, but it is an historical growth rate and not a forecasted or projected growth rate as your Schedule 13 indicates?

A. I believe that is what he states, and as I've indicated in my testimony, we believed that a substitute of the five-year historical was the best predictor of a five-year projected.

Q. In response to a subsequent Empire Data Request 36D, do you recall your answer when asked about the 2 percent earnings per share growth rate in Schedule 13 of your direct testimony and you responded, Mr. Murry is correct that there is no 2 percent five-year EPS growth rate for Empire District Electric in Standard & Poor's Corporation Earnings Guide February 2001. This correction has been noted in Item A above.

Mr. Murry is also correct that the 2 percent five-year EPS growth rate for Empire District Electric in the Standard & Poor's Stock Guide is for a historical period. However, Staff believes that investors will use historical growth rate as a reliable predictor of projected growth. This belief can be conformed by statements made in Staff's source document entitled, The Cost of Capital, a Practitioner's Guide, at page 8-18, written by David c. Parcell, prepared and published by the Society of Utility and Regulatory Financial Analysts 1997 edition.

Due to a lack of published projected growth rates, Staff chose to use S&P's historical five-year growth rate as a substitute based on the methodology prescribed in the aforementioned publication?

A. Yes, that was my answer.

Q. To the data request. Then on page 7, lines 4 through 6 of your surrebuttal testimony you state, Due to a lack of published projected growth rate information on Empire District Electric, Staff chose to use Standard & Poor's historical five-year growth rate as a substitute; is that correct?

A. That's correct.

Q. Now, isn't it true that nowhere in either your direct or rebuttal testimony did you reveal that your projected growth rates are actually historical growth rates?

A. No. At that point I was unaware of the mistake I had made on my schedule, although I was aware that the number I was pulling at the time was a historical number. And as I indicated previously, Staff believes that with a lack of projected information, that the historical is an appropriate predictor of future growth.

Q. Could one fairly conclude that you decided to reveal that you had substituted historical growth rates for forecasted growth rates but continued to refer to them as projected or forecasted growth rates only after reading Dr. Murry's rebuttal testimony or after receiving Empire's Data Request 36?

A. Well, I think you're implying that I on purpose misled. I think it was just an oversight on my part as to putting it down as a historical rather than a projected number. I was well aware that it was a historical number. I just wrote it wrong on my testimony.

Q. And you didn't correct it until it was called to your attention?

A. That is true, I did not correct it until it was brought to my attention, but it would have been uncovered because I do a review of my testimony before coming to the hearing.

Q. Is it true that you did not make this same switch in Schedule 23 of your direct testimony? That's the schedule concerning the comparable companies. And by that I mean you did not substitute historical growth rates for projected growth rates?

A. No. All of those growth rates listed on Schedule 23 are projected because the information was available.

Q. So for the nine comparable companies, you really are using projected growth rates, but for Empire you're using historical growth rates; is that true?

A. Only because there's a lack of published projected information for Empire due to the merger.

Q. On your Schedule 13 to your direct testimony, you go back and forth on your historical growth rate analysis there between ten and five years; is that right?

A. That is true.

Q. Some you take ten years, some you take five, and then you average them all together; is that true?

A. Right. The only reason that a five-year DPS for Empire does not exist is because their dividends per share has not increased since 1992, so it's a zero amount.
Q. Your 2.10 percent average of historical growth rates is averaging some that are ten and some that are five?
A. That is correct.
Q. For example, the first line is ten, the next one is five, next one is ten, next one's five, last one's ten?
A. Correct.
Q. And on Schedule 12, the prior schedule, am I correct that you go back 12 years -- excuse me -- ten years looking at growth rates?
A. Correct. That has been the approach of Staff in all its cases.
Q. Is it your testimony that an investor can reasonably be expected to look at ten-year-old growth rates to estimate what future growth rates will be?
A. I believe it's a possibility they will look at past performance.
Q. You think a smart investor would look at ten-year-old growth rates to estimate what future growth rates would be?
A. I make no judgment as to what each individual investor would look at. I would say that some would

probably look at ten year while others would not. There's no way for me to know exactly what every investor would do.

Q. Well, that wasn't really my question. My question was, would a smart or intelligent investor in your own mind look at ten-year-old growth rates to determine what future growth rates would be?

A. I make no judgment as to an investor's intelligence level.

Q. Well, what would you do if you were an investor? Would you rely on ten-year-old information?

A. Possibility I would.

MR. SWEARENGEN: Okay. Could I have another exhibit marked, please?

JUDGE RUTH: Yes. This would be Exhibit 104.

(EXHIBIT NO. 104 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

JUDGE RUTH: For the record, can you give us this title?

MR. SWEARENGEN: Sure. Direct testimony of Roberta McKiddy, page 24, with some adjustments.

(EXHIBIT NO. 104 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY MR. SWEARENGEN:

Q. Ms. McKiddy, would you take a look first of all at Exhibit -- excuse me -- Schedule 23 to your direct testimony.

A. Okay.

Q. And there over on the right-hand side, with respect to your nine comparable companies, you have a proposed range of growth of 5 percent to 6 1/2 percent; is that not true?

A. That is correct.

Q. Now, you have in front of you what has been marked for identification as Exhibit 104, which I will tell you builds on Exhibit 101, both of which are lines 11 through 23 of your direct testimony. Exhibit 104 you will recall substituted the $20 share price for your price range. Excuse me. That was Exhibit 101.

Exhibit 104 makes that substitution as well and also includes the 5 to 6 1/2 percent proposed range of growth from your own Schedule 23. Would you agree with what I've just said?

A. Yes. Those are numbers -- this 5 to 6 1/2 does represent the range I came up with on my comparable company group.

Q. And have I done the DCF calculation correctly on Exhibit 104? That is, if you use a dividend yield of 6.4 percent and the 5 to 6 1/2 growth rate, you end up with a cost of equity range of 11.4 to 12.9 percent?

A. Yes, using the assumptions you have defined, that would be correct.

Q. I understand you wouldn't agree with those assumptions.

A. No, I would not.

Q. And I'm not asking you to do that. But this would be illustrative of what the Commission would do if they took a $20 stock price and the growth rate range of the comparable companies; is this true?

A. If that's what the Commission chose to do, yes, that would be correct.

Q. This would correctly reflect that.

If you would turn to page 17 of your direct testimony. Are you there?

A. Yes.

Q. At lines 11 to 17, you quote from the Standard & Poor's Utilities Rating Service; is that correct?

A. Yes, I do.

Q. And would you agree that this discussion by S&P would cover or encompass the ratings of Empire's bonds?

A. I believe that's what Empire is -- or Standard & Poor's is referring to, how it views the outlook for the bond rating.

Q. Would you agree that S&P's reference to rating stability and its negative outlook means that S&P believes that Empire's bond rating could be lowered?

A. Negative outlook would indicate that there's a possibility, but it doesn't provide a guarantee that it will be.

Q. At your rebuttal testimony, on page -- excuse me. I'm thinking about your merger rebuttal testimony. Do you have that with you today?

A. My merger testimony, no.

Q. I don't think I'll get into that with you, then.

A. I don't think it's relevant here anyway.

Q. Let's take a look at Schedule 19 of your direct testimony, please. Am I correct in understanding that the pretax interest coverage that's shown on that schedule for your range of recommended allowed return in this case is 2.16 times to 2.29 times?

A. Based on the revenues that would be generated by common equity, that would be true.

Q. And that's shown in line 9 -- or column -- or not column.

A. Item 9, yes.

Q. Item 9. Thank you.

A. Uh-huh.

Q. And the 2.1 percent relates to your 8.5 ROE; is that right?

A. That is correct.

Q. And the 2.29 relates to your 9.5 ROE; would that be true?

A. That is correct. And again, that's a pretax interest coverage based only on the revenues that would be generate by common equity.

Q. Do you recall your answer to Empire's Data Request No. 37D when you were asked if you were aware of any electric utilities that had a pretax coverage in the range of 2.16 times to 2.29 times, and your response was, I have performed no empirical study of pretax interest coverage for individual companies with the electric utility industry; is that correct? Do you remember your answer?

A. That is true. And again, the pretax coverages shown here do not reflect all the revenues. Therefore, it does not reflect what actually the pretax interest coverage has a possibility of being for Empire.

Q. Is it true that you did not present in your testimony any analysis to demonstrate whether the coverages that you calculated in Schedule 19 are sufficient to maintain an A bond rating for Empire?

A. I'm not implying that it does.

Q. Are you aware of any utilities that indicate -- excuse me.

Are you aware of any studies that indicate that there is an optimal or a least cost bond rating for a utility?

A. I have performed no study.

Q. Are you aware of any studies that indicate that?

A. Well, I think it's general knowledge that the higher rated a bond is, the less the cost is to the company. But again, I think you're trying to imply that the pretax interest coverage is the only thing that plays into the bond rating calculation by Standard & Poor's and it is not.

MR. SWEARENGEN: Could I approach the witness again?

JUDGE RUTH: Yes. Same book you're going to use?

MR. SWEARENGEN: Same book.

JUDGE RUTH: Go ahead.

BY MR. SWEARENGEN:

Q. Ms. McKiddy, I'm going to hand you again Mr. Parcell's Practitioner's Guide and ask you to look at Section 514, Optimal Ratings, and just read those two paragraphs into the record, would you, please. Thank you.

A. Higher security ratings/rankings are generally associated with lower cost of the respective capital components. On the other hand, in order to maintain higher ratings, larger revenue requirements are frequently required in order to maintain higher ratios. Thus, there is a tradeoff between the lower capital costs associated with higher ratings and the higher capital costs associated with greater coverage ratios.

Q. Thank you. Why don't you read the next paragraph as well, please.

A. Sure. Is there an optimal bond (or other security) rating which will result in minimizing capital cost? Such a determination could be used as an objective rating for the purposes of estimating fair rate of return. Studies have concluded there is no single best bond rating for a utility to maintain at all times.

At any point in time the structure of the relationship between the cost of debt, the cost of equity and the cost of preferred stock will determine which bond rating is best for the utility to maintain. Other studies have concluded that AA bond ratings result in the lowest pretax cost of capital for electric utilities.

Q. Thank you.

Are you aware of any studies showing that a bond rating lower than an A rating is the lowest cost bond rating?

A. No, I'm not.

Q. Are you aware that since the time that you filed your direct testimony, that Empire's debt has been downgraded by both Fitch and Moody's?

A. It has been downgraded by Fitch and Moody's, but not by Standard & Poor's.

Q. Isn't it true that Fitch identified Empire's pretax interest coverage as a factor in its bond downgrade?

A. I don't recall that specifically. I do recall references to the fuel costs.

Q. Would you agree with this statement: All else being equal, a lower bond rating would indicate a higher risk. In turn, investors would require a higher return in order to compensate them for accepting such higher level of risk.

A. You're saying that simply because of a difference in bond rating, investors would require a larger rate of return?

Q. No. I'm asking whether or not you agree with that statement.

A. State it again, please.

Q. All else being equal, a lower bond rating would indicate a higher risk. In turn, investors would require a higher return in order to compensate them for accepting such higher level of risk.

A. Not necessarily. It depends on the investors' objectives and their investment opportunity.

Q. So you don't agree with that statement, then?

A. I don't believe it would always be true, no.

Q. Do you think it would ever be true?
A. Sure.
Q. Okay. But it would not always be true?
A. Not necessarily, no.
Q. Okay. And you would never make that statement?
A. No, I would not.
MR. SWEARENGEN: Can we have just a minute?
JUDGE RUTH: Yes. Do you need a five-minute recess?
MR. SWEARENGEN: No. About two minutes.
JUDGE RUTH: Just stay on the record, then.
MR. SWEARENGEN: May I approach the witness?
JUDGE RUTH: Yes.
BY MR. SWEARENGEN:
Q. Ms. McKiddy, I'm going to hand you a copy of your rebuttal testimony in Case EM-2000-369, Jefferson City, Missouri, June 2000, and ask you to read into the record the answer that begins on line 13.
A. All else being equal, a lower bond rating would indicate a higher level of risk. In turn, investors would require a higher return in order to compensate them for accepting such higher level of risk.
Q. Thank you.
Turning back to Schedule 19 of your direct

testimony, after the words S&P Corporation's Utility Rating Service 7/7/00 Electric Utilities, there's a line showing 3.65 times under the word median. Do you see that?

A. That is correct.

Q. By median in this line, do you mean that half of the A-rated electric utilities have a pretax interest coverage higher than 3.65 times?

A. I don't believe that's specifically what that's saying. I think it's saying that in the context of that range of 2.95 to 4.13, that is what the median would be. I don't believe that it necessarily encompasses all utilities. It's talking about this particular level of rating, bond rating. It's the utilities that would fall within an A rating.

Q. And that would be half of the utilities?

A. Not necessarily. It depends on how many utilities are rated A bond rating.

Q. Let me ask you, in that same line on your Schedule 19 there's an item that says, lower quartile and 2.95 times, correct?

A. Correct.

Q. And does this lower quartile mean the lowest 25 percent?

A. Of that particular category, yes.

Q. Does the lower quartile associated with the

2.95 times in your Schedule 19 mean that 75 percent of the A-rated electric utilities have a pretax coverage of 2.95 times or higher?
A. State that again, please.
Q. Does lower quartile as you use it there in your Schedule 19 mean that 75 percent of the A-rated electric utilities have a pretax coverage of 2.95 times or higher?
A. I don't know that I could give a definite answer to that.
Q. Would you agree that lower quartile would be the lower 25 percent?
A. Of that particular category, I believe.
Q. And your recommended return of 8.5 percent for Empire in this case would produce a pretax coverage of 2.16 times; is that correct?
A. Again, the 2.16 times is based only on the revenues generated by common equity. The 2.95 times in the benchmark area reflects all revenues that would be generated by a company with an A rating.
Q. Do you recall being asked in Empire's Data Request 37A about what percentile the 2.16 times pretax interest coverage would be for the electric utilities?
A. And I believe my response was that I did not understand what Mr. Murry was referring to when he said

percentile rather than quartile.

Q. Right. You said, I am not sure what Mr. Murry is referring to when he uses the word percentile. I have used no such data in any of my testimony and am unaware of the existence of any such data being published by S&P or any other source used for purposes of my cost of capital analysis, correct?

A. That's what I stated, yes.

Q. Are you aware of any electric utilities in the United States that are in good financial health which have a pretax bond coverage as low as the 2.16 times that you are recommending in this case?

A. Again, you're trying to infer that the 2.16 times is reflective of all the revenues that would be generated by a corporation. So I would have to answer no to that in two counts. No. 1, I've done no study of other companies' pretax interest coverages, and you're trying to misrepresent the number that I've calculated there.

Q. At the time that you wrote your direct testimony, which is dated April 2001, did you know that Valueline's estimated pretax interest coverage for Pacific Gas & Electric Company was 2.0 times?

A. Again, you're trying to compare my number, which does not reflect all revenues, to a pretax interest coverage of a company that's in default. I believe it's inappropriate.

Q. Which company's in default? Which company's --

A. You said PG&E, did you not?

Q. Yes.

A. My understanding, it's in default. It has a D rating.

Q. Turn to page 30 of your direct testimony, if you would, please. There at lines 12 to 17 you state that your equity range in this case provides enough earnings power for Empire to meet its net earnings requirement of two times the amount of annual interest requirements pursuant to its supplemental indenture; is that true?

A. Yes. What I'm stating there is that the revenues that would be generated off of common equity by themselves are sufficient to cover the indenture. That does not mean that that is the total A revenues that would be generated by Empire.

Q. Once again, you're familiar with the Parcell's Guide.

MR. SWEARENGEN: Could I approach the witness one more time, please?

JUDGE RUTH: Yes.

BY MR. SWEARENGEN:

Q. And would you agree that there's several ways described in the Parcell's Guide to calculate cost of capital?

A. Yes. He offers several methodologies, which among them are the DCF, the CAPM and the risk premium.

Q. Why don't you read into the record this, please (indicating)?

A. It's a section entitled Models Preferred by Commissions. What models do the various regulatory agencies consider? Table 1 summarizes the most recent NERUC survey on rate of return methods. As this indicates, most commissions use multiple methods, and several models appear to be widely used.

Q. And what are the models that are listed under there?

A. They list the discounted cash flow, comparable earnings, risk premium, capital asset pricing model, earnings to price ratio, and then there's another category no one method, all are considered, which I believe is what this Commission does.

Q. Which is what?

A. We use several methods.

Q. Of all those methods that are discussed in Mr. Parcell's guide which you cite as authority, can you show me where he states that a return which simply permits a utility to meet its bond indenture requirement is an adequate return to allow an electric utility in a rate proceeding such as this one?

A. I don't know that he states that anywhere in his book, and I'm not implying in my testimony that that is the only basis for our recommendation.

Q. On pages 3 and 4 of your direct testimony you discuss what I will refer to as the Bluefield Water Works case and the Hope Natural Gas case; is that correct?

A. That is correct.

Q. And I assume that you've read both of those cases; is that true?

A. At some point in time, yes, I have read them.

Q. When did you first become familiar with those cases? Was it prior to the time you accepted employment with the Public Service Commission?

A. Oh, I would say not. I was employed by the Public Service Commission in May of '95. I would say I was aware of it within a year after my employment.

Q. Would you say that those cases are important with respect to your ultimate recommendation in this proceeding concerning a fair and reasonable return for the Empire District Electric Company?

A. Of course they are. They provide the framework of our analysis.

Q. You say they provide the framework of your analysis. Let me just ask you this: On a ranking of one to ten, ten being the highest, one being the lowest, how would you rank the principles of those decisions in terms of their importance with respect to your recommendation concerning a fair and reasonable return for Empire?

A. I don't rate one case any more important than the other. I find them all equally important. That's why they're all cited in my testimony.

Q. Those two cases, the Bluefield -- I'm talking about the Bluefield case. How would you rank the principles in that case in terms of importance on a ranking of one to ten, ten being the highest?

A. I don't have an opinion on that. Like I say, I look at them all equally in importance.

Q. You said there are benchmarks in those cases or principles; is that true?

A. I believe it defines a -- how do I want to say this? It provides parameters and objectives that we should keep in mind when recommending a range of return on equity.

Q. And what are those parameters that are defined by the Bluefield case? Can you say just generally?

A. Generally, we need to balance all interests in the case, as well as to provide reasonable rates.

Q. And what about the Hope case, is that an important case as well, the Hope Natural Gas case?

A. As I stated earlier, all the cases commented on in my testimony are of equal importance.
Q. Okay. So at page 5 you talk about a Pennsylvania Supreme Court case involving a Pennsylvania electric company. So you would rank that decision or case on par with the Bluefield Water Works case and the Hope Natural Gas case --
A. I believe --
Q. -- with respect to your recommendation here?
A. Again, I believe all the cases cited in my testimony are of equal importance.
Q. Okay. And linking this back to your DCF model that you've obviously discussed many times in this case, where would you rank it in terms of importance with respect to your overall recommendation in this case vis-a-vis those cases that you just cited? Is the DCF on a par with those cases?
A. I'm not sure I'm understanding what you're asking me.
Q. Well, my question is, where do you rank the DCF model in terms of its importance with respect to your recommendation in this case?
A. It's been the past position of Staff to use the DCF as its primary model, but as I've stated, we do use other models to test the reasonableness of that result. So

I don't provide a specific ranking to it, but I do use it as my primary tool.

Q. Is it as important as the cases that you've just cited, the Bluefield case, the Hope case and the Pennsylvania Supreme Court case?

A. I guess I would have to say that they're of equal importance.

Q. Okay. That's fine.

On page 5 of your direct testimony you talk about this Pennsylvania case, and you cite it a number of times in your testimony. I think the Hope and Bluefield case only appears once or twice, but you cite the Pennsylvania case in your direct, your rebuttal and surrebuttal testimony.

But at page 5 of your direct testimony at line 27, you say that the Pennsylvania Supreme Court decision extends the Hope case decision beyond balancing the interests of the investors and consumers; is that correct?

A. Yes.

Q. You make that statement?

A. Yes, I do make that statement.

Q. So can I conclude from your statement that it would be your testimony that the Pennsylvania Supreme Court case somehow has broadened the decision of the United States Supreme Court in the Hope case?

A. I believe it's more supporting the decision rather than broadening it.
Q. Well, you use the word extends, extends the Hope case decision beyond balancing the interests of investors and consumers.
A. I believe maybe what I'm inferring there is that by balancing the interest as well as maintaining reasonable rates may be what the Pennsylvania case has done to take it beyond what the Hope case has.
Q. I know you're not a lawyer, but is it your understanding that a Pennsylvania Supreme Court decision is binding on or takes precedence over a decision of the United States Supreme Court?
A. I'm not an attorney, so I don't know.
Q. And would you have any idea as to whether or not a decision of the Supreme Court of Pennsylvania is binding on the courts of Missouri or the Missouri Public Service Commission?
A. I don't know.
Q. Look at page 6 of your direct testimony, lines 8, 9 and 10, if you would, please. And when I read that, my sense is that your testimony concerning the Pennsylvania decision is there to illustrate the point that captive ratepayers of public utilities should not be forced to bear the brunt of wrongful management which results in

unnecessarily higher costs. Is that a fair characterization of what you say in your testimony?

A. That's what is stated there, yes.

Q. And that's really the reason you cited that case in your testimony, is it not?

A. Well, this same language appears in all cases that we do before the Commission. It does not necessarily apply explicitly to Empire. It's a general statement.

Q. And that's the reason, though, that you cited the case, the Pennsylvania case in this case involving Empire for that proposition, that captive ratepayers of public utilities should not be forced to bear the brunt of wrongful management which results of unnecessarily higher costs?

A. Again, that statement is made in every case we file, not necessarily specific to this particular case. It's in all proceedings.

Q. I understand, but that's the reason you put it in here, is it not, for that principle?

A. I did not have any specific reason in mind for putting it there except that it provides a legal framework for our analysis.

Q. What wrongful management decision did the Pennsylvania case address, do you know?

A. I believe the main issue of that case was a determination of used and useful assets, but it made an indirect implication to rate of return and the setting thereof.

Q. That was going to be my question. Didn't it really turn on an application of the used and useful, the Pennsylvania decision?

A. Yes, it did, but I believe what it also implied was that in the determination of used and useful, should an item become disallowed in rate base, it should not be the obligation of the Commission to make a so-called adjustment to rate of return to make up the difference for that.

Q. Right. The public should not be required to pay for properties not beneficial to them?

A. Correct.

Q. And in that case it was the Three Mile Island nuclear units; is that right?

A. I believe that was mentioned in the case, yes.

Q. So there really wasn't any wrongful management issue in that case, was there?

A. I did not really study it to determine whether there was or was not.

Q. Do you think that the used and useful concept is a concept that is unique to the state of Pennsylvania or would you agree that this Commission would also likely enforce that concept?

A. Being that used and useful is an issue in this case, I believe this Commission does use that as part of their standard.

Q. When you say used and useful is an issue in this case, would you say that the Commission would endorse that standard, if something isn't used or useful the ratepayer ought not to pay for it?

A. I believe if an item is considered and judged by this Commission not to be used and useful, that it is not included in rate base and, therefore, does not provide a revenue requirement.

Q. Would the same be true for so-called wrongful management decisions which result in higher costs? No regulatory commission that I'm aware of will allow such costs to be passed on. Are you aware of any that will allow such costs to be passed on to ratepayers?

A. I'm not specifically aware of what other commissions do.

Q. Do you think this Commission would?

A. I know that this Commission judges cases for prudency issues, and I believe that used and useful would fall under that, cost overruns per se.

Q. And what about wrongful management decisions that result in higher costs, this Commission wouldn't allow those costs to be passed on, would it?

A. I don't know what type of judgment this Commission would make in determining whether something was wrongful or not.

Q. Would you agree with me that the present rates which the Empire District Electric Company is charging for electric service in Missouri are just and reasonable and have been approved by the Commission?

A. I would say rates currently in place for Empire have been approved by this Commission and deemed reasonable at their direction.

Q. And would you agree that those rates do not reflect the costs of any wrongful management on the part of Empire or the cost of any property that is not used and useful?

A. If you're defining wrongful as prudent, I would say that there are probably not costs included in those rates that were not considered prudent.

Q. Well, you used the word wrongful in your testimony at page 6, lines 8, 9 and 10, and so I will ask you, what did you mean by the use of that word?

A. And again, that was a term used by the opinion in the Pennsylvania case. To my knowledge, it's not necessarily a term that I derived.

Q. So are you suggesting that Empire's rates do reflect the cost of wrongful management on the part of the company?

A. Again, I'm not the one that determines wrongful. If you're defining wrongful as prudent, I would say that this Commission has included costs in rate base and rate design that are considered prudent.

Q. What is your understanding of the use of that word, because you're the one that used it in your testimony?

A. And again, I used it in a general sense. I did not use it to specifically describe Empire or its operations.

Q. Would it be fair to say that in none of your testimony in this proceeding do you offer any evidence of any wrongful management decisions on the part of Empire which have resulted in higher costs for its customers?

A. And that is true. I have not offered any evidence because it is not my responsibility to determine whether something is wrongful or not or prudent.

Q. Actually, wouldn't you agree that, relatively speaking, Empire is a low-cost provider of electric utility service?

A. I would believe it would be true to say that Empire is a conservative and low-cost provider.

Q. At page 34 of your direct testimony you said that it has a competitive rate structure. What did you mean by that?

A. What line are you at, please?

Q. Page 34 of your direct testimony.

A. At line 12?

Q. I don't know. Does it appear -- do you say that on page 34 of your direct testimony? Do you recall making that statement?

A. Yes, and I believe what I was probably referring to there, that it was competitive in comparison to companies of similar operation.

Q. And what do you mean, companies of similar operation?

A. Examples of the comparable companies I used in my comparable analysis.

Q. So is it your testimony that Empire is competing in electric utility service with your nine comparable companies?

A. No, I'm not saying that at all.

Q. Back to the Pennsylvania decision, would you agree with me it really doesn't have anything to do with wrongful management, and in any events you have no evidence of wrongful management on the part of Empire in this case?

You said the Pennsylvania case was really a used and useful concept.

MR. JOYCE: Your Honor, could I object to this line of questioning as to wrongful management? There is no suggestion on the part of the witness in her testimony that the company has conducted any wrongful management. I don't see the relevance on the rate of return testimony.

JUDGE RUTH: So your objection would go to relevance?

MR. JOYCE: Yes.

JUDGE RUTH: Response?

MR. SWEARENGEN: Well, she talks about the Pennsylvania case every opportunity she gets. It shows up in her direct, rebuttal and surrebuttal. I'm just trying to find out what it's all about. It's a mystery to me. I've read the case. It's a used and useful case. There's nothing in there about mismanagement.

And in any event, there's no evidence of that with respect to the Empire District Electric Company. Their present rates just and reasonable. Nobody's saying that they've done anything that could conceivably be considered wrongful management, and I'm just trying to find out why we keep reading about this Pennsylvania case.

MR. JOYCE: I believe the witness has responded on numerous occasions that it's a general case quoted in Staff testimony for rate of return and there was no intention to single out.

MR. SWEARENGEN: And that's fine. I

appreciate counsel stating that, and I'll stop my questions about it with that. Thank you.

JUDGE RUTH: If you're going to withdraw your questions on that, I'm not going to --

MR. SWEARENGEN: I'm not going to ask any more questions about it.

JUDGE RUTH: Right. If you're not going to ask any more questions, I won't rule on the objection.

MR. SWEARENGEN: I was at the end anyway on that hot topic.

BY MR. SWEARENGEN:

Q. Let me ask you this, Ms. McKiddy: Are you familiar with Missouri Gas Energy, which is a division of Southern Union Company?

A. Yes, I am.

Q. And is it your understanding that Missouri Gas Energy is a gas corporation regulated by this Commission?

A. That is true.

Q. And what is its service territory? Are you generally familiar with it?

A. I believe Missouri Gas Energy operates primarily in the Kansas City and the Joplin areas.

Q. So operating in the Joplin area, it would be a competitor of the Empire District Electric Company; is that true?

A. In direct competition with the electric users? It's a possibility, depending on what choice of service the residents choose to use.
Q. And they might want gas heat or electric heat and they wouldn't have a choice, is that possible?
A. Or they have both units and choose to use whatever's cheaper at that point in time.
Q. Let me ask you this. Could empire and MGE or Southern Union be competitors in the area of finance and that is both seeking capital from the same markets?
A. I guess it's always a possibility, but I wouldn't look at that in my analysis.
Q. You wouldn't consider them a comparable company, is what you're saying?
A. No, because MGE's primary service is gas distribution.
Q. Would it be possible that someone who was considering investing in Empire would also possibly consider investing in Southern Union or MGE?
A. It's a possibility.
Q. Let me ask you this: You were present, were you not, when I took the deposition of your colleague, David Murry, in Case GR-2001-292 involving MGE's pending rate case; is that right?
A. Yes, I was there.

Q. And Mr. Murry had recommended a 9.45 to 10.25 ROE for MGE. Do you recall that?
A. I believe that was his original recommendation, yes.
Q. And then since then he's adjusted it. Since his deposition it's been increased to 9.6 to 10.5; is that right?
A. Yes. I believe there was a number in his schedule that he has since corrected.
Q. Do you recall from your involvement in that case and his deposition that Southern Union has outstanding preferred stock with a cost of 9.93 percent?
A. I'm not aware of that specifically.
Q. Would you agree that preferred stock is less risky than common stock?
A. Can be.
Q. Have you read the rebuttal testimony of Empire witness Dave Gibson concerning capital structure and return on equity?
A. I've read it briefly, yes.
Q. And it's your plan to true up Empire's capital structure as of June 30, 2001; is that correct?
A. That is true.
Q. And there's been some testimony about this, and Mr. Gibson has suggested it in his testimony and you've

talked about it today. You won't agree to true up Empire's stock price for the most recent five months as Mr. Gibson has suggested; is that true?

A.   I as well as my division management do not believe it is appropriate.

Q.   That's the Staff position, not to true up Empire stock price; is that true?

A.   Correct.

Q.   Is it your understanding that Empire issued trust-preferred securities in March of 2001?

A.   I believe that is true.

Q. $50 million at a rate of 8.5 percent? I think we heard that earlier.

A.   Yes, they issued some toppers.

Q.   Would you agree that the trust-preferred securities are less risky than Empire's common stock?

A.   I don't make any particular determination of that.

Q.   You don't have an opinion on that?

A.   No, I do not.

Q.   On page 3 of you your rebuttal testimony, if you would turn to that for a moment, please. And you'll be glad to know I'm almost finished. You discuss capital structure; is that true?

A.   Yes, that is true.

Q. And you discussed the fact that Empire's capital structure changed as a result of the pending merger with UtiliCorp?
A. I do state that Empire made a conscious decision to change their capital structure, yes.
Q. As a result of the pending merger with UtiliCorp?
A. Yes.
Q. And again, at page 2 of your surrebuttal testimony you admit that Empire's actual capital structure is different from its historic levels; is that true?
A. That's true.
Q. And make sure I understand your position and the position of the Staff is that this merger-induced capital structure is the one that should be used for purposes of setting rates in this case; is that right?
A. Yes. The Staff's position is that the only time a hypothetical capital structure should be used is when it is anomalous to the industry average. This adjusted capital structure, even though it was caused by the merger, is in line with the average industry capital structure at this time.
Q. So you didn't attempt to normalize the capital structure as you say you tried to do with the stock price; is that right?

A. No, I did not, because it is not Staff's position to do so.

Q. You didn't seek to minimize the effect of the merger on Empire's a capital structure?

A. No, again, because the decision was at the discretion of management. They could have chosen not to adjust the capital structure just as easily as they choose to adjust it.

Q. But it was adjusted in response and in connection with their obligations under the merger agreement; isn't that true?

A. I believe it was in terms of the merger agreement with UCU.

Q. Are you familiar with the Staff cost of capital testimony in the Empire/UtiliCorp merger case? You said you filed testimony.

A. I filed testimony only on merger trends.

Q. Do you remember Mr. Broadwater's testimony that the merger would created 2.5 million per year savings or reduction in capital costs?

A. I don't recall that specifically.

Q. Do you think that Empire should be allowed a return in this case achieved by other companies with corresponding risks and uncertainties?

A. I believe that's the main premise of the Hope case.

Q. And what's your opinion, then? Do you believe in that?

A. I believe what I have recommended is appropriate for the cost of capital for Empire.

Q. Do you think Empire should be allowed a return in this case achieved by other companies with corresponding risks and uncertainties?

A. Again, that's the premise of the calculation. To truly define a company that has comparable risk is a very difficult proposition.

Q. Do you agree that Empire should be allowed a return in this case achieved by other companies with corresponding risks and uncertainties? Can you answer that yes or no and then explain?

A. Again, it's hard to give you a clear answer. I have calculated a cost of capital that defines what I believe Empire's cost of capital to be. I have done a comparable companies analysis, but, again, to try to take one company in my comparable group and determine that it absolutely possesses the same risks as Empire is something that's very difficult to do.

Q. Is your answer yes, no, or I don't know?

A. I base my recommendation on that premise which is an underlying assumption of the DCF.

JUDGE RUTH: You will need to try to answer yes, no or --

THE WITNESS: I'm trying, but it's hard to -- state it again and I'll see if I can answer yes or --

BY MR. SWEARENGEN:

Q. Do you think that Empire District Electric Company should be allowed a return in this case achieved by other companies with corresponding risks and uncertainties?

A. I'll answer yes.

Q. Okay. Thank you.

MR. SWEARENGEN: That's all I have of the witness. I guess I would offer into evidence Exhibits 101, 102, 103 and 104. I believe that was the extent of those exhibits that I had marked.

JUDGE RUTH: Let's deal with those one at a time, please. I have Exhibit 101 is the direct testimony of Roberta McKiddy with some changes made. It's page 24, and the changes on this I believe had to do with the 6.4 under yield and 9.4 and 10.4 under equity. Am I looking at the right page?

MR. SWEARENGEN: You are.

JUDGE RUTH: That's been offered as Exhibit 101. Parties, do you have any objections?

MR. KRUEGER: We object to Exhibit 101 because there's not a proper foundation for it. The witness didn't testify to the numbers that were substituted to the numbers that she had included in her own testimony.

JUDGE RUTH: Can you repeat that? I'm not sure I understand. I thought there was testimony regarding those numbers.

MR. KRUEGER: I'm objecting on the basis of proper foundation because the witness did not identify those numbers as appropriate.

Mr. Swearengen asked her to assume that those numbers were appropriate and then to say that if those numbers were appropriate, if the inputs were appropriate, if the $20 was appropriate, do you end up with the rest of the document ending up the same way, and she never acknowledged that the $20 was an appropriate figure.

JUDGE RUTH: True. Instead, it was based on hypothesis, right, to assume that that was appropriate?

MR. KRUEGER: Correct.

MR. SWEARENGEN: That's not exactly correct, your Honor. I mean, I think the evidence was that the stock has been in the 19 to $20 range for quite some time. She admitted that. It closed yesterday under $20. For purposes of my example we just took the 20. All this is designed to do is to reflect what change in the stock price from her range to $20 will do to her DCF calculation. It's just a simple mathematical calculation. You divide the 20 into

$1.28. She said that 6.4 percent resulting is correct. And the result of the cost of equity that would be from that calculation is correct. So it's simply a mathematical calculation.

I understand she's not supporting this or endorsing it, but it's designed to illustrate what a change in her testimony just on that one particular point would do, taking the share price from her range of 20 to 29, which includes the merger, and taking it back to a $20 price, which we think is much more reasonable given what's going on in the last five months, how that affects her range of rate of return, which according to her ought to be 8 1/2 to 9 1/2. And if you just adjust that one item, it takes it up to 9.4 to 10.4. I think she's explained that. I don't know any more foundation that you could be laid to lay that out.

JUDGE RUTH: I've heard the objection and the response and I am going to allow it to be admitted in. So Exhibit 101 is admitted into the record.

(EXHIBIT NO. 101 WAS RECEIVED INTO EVIDENCE.)

JUDGE RUTH: What I've marked Exhibit 102 for purposes of identification was the Schedule DAM-25. Mr. Swearengen, could you clarify as to whether or not this is the identical schedule?

MR. SWEARENGEN: It is the identical schedule. I had some plans to something with it and I didn't. I think it's in evidence in two other places. I don't think it would hurt to put it in one more time as Exhibit 102, but that's up to you.

JUDGE RUTH: It's already in and you made no changes, right?

MR. SWEARENGEN: That's right.

JUDGE RUTH: I don't think it's necessary to admit it in, so that --

MR. CONRAD: It's cumulative.

MR. SWEARENGEN: I'll withdraw. It's cumulative, yes. Mr. Conrad who keeps me in line says it's cumulative, and that's fine.

JUDGE RUTH: Exhibit 103 was the Empire District page from the -- is that New York Stock Exchange.

MR. SWEARENGEN: This is the Valueline that the witness, I think, referred to in her own testimony, and I just wanted to clarify that. This is what she was referring to as the source for some of her changes, I believe.

JUDGE RUTH: Were there any objections to this page being admitted into the record?

MR. JOYCE: No objection.

JUDGE RUTH: Seeing no objection, then Exhibit 103 is admitted into the record.

(EXHIBIT NO. 103 WAS RECEIVED INTO EVIDENCE.)

JUDGE RUTH: Exhibit 104 is direct testimony from Roberta McKiddy with some adjustments. It's a similar page to Exhibit 101, but changes -- additional changes were made under the growth rate, and that also changed the cost of equity.

MR. SWEARENGEN: That's correct. Once again, it's simply a mathematical calculation. I understand that the witnesses doesn't agree with the final result, and that's fine.

The growth rate calculations were taken from her Schedule 23, and the whole purpose of this is to show the impact of that change on the resulting cost of equity, and I think she went over it in detail and explained it.

MR. KRUEGER: I would object to that for the same reasons I objected to Exhibit 101. I haven't checked the math. I assume the math is correct. But in addition, I would voice another objection that the yield figures that are shown there are based on changing the yield of Empire, and the growth rate figures are based on changing it to the data from comparable companies.

MR. SWEARENGEN: That's exactly right. That's what it shows. We went over that in Exhibit 101 and explained we were changing the yield for Empire, and the growth rate comes right off the growth rate for the comparable companies. That's what it shows, and it's just a mathematical calculation and I think she explained it.

JUDGE RUTH: Mr. Coffman, did you have a comment?

MR. COFFMAN: Yeah. I would join in Mr. Krueger's objections. I think it is a complete distortion of what she was trying to do. I agree with Mr. Krueger. It just seems highly inappropriate to allow into evidence an adjustment to someone's testimony, label it as Ms. McKiddy's testimony when her answers on the stand were clear that these were not her -- this is not her testimony.

And I feel Mr. Swearengen could have had one of his witnesses do the math based on different assumptions of different parties. But to put in the record something that puts different words in a witness' mouth or rather different numbers in a witness' mouth just seems highly inappropriate.

MR. SWEARENGEN: If you were here this morning and you thought I was putting words in her mouth, I think you're mistaken. I don't think that happened at all. I think she made her position pretty clear on what she thought about the bottom line result of that.

It's simply designed to illustrate what happens when you make those changes, and that's the whole purpose. I'm not suggesting I'm changing her testimony.

I'm clearly not doing that. I made it clear from the start, and she wouldn't let me do that anyway. I think it's appropriate to show the results.

JUDGE RUTH: Mr. Conrad, I couldn't tell if you had an objection also.

MR. CONRAD: Well, I'm not sure I have a dog in this fight.

JUDGE RUTH: I just couldn't tell if you were --

MR. CONRAD: I guess I am -- I'd have to say to you, as my esteemed colleague at the bar Mr. Swearengen points out, if it is just mathematical calculation, you could make a mathematical calculation over here on one of these pads and have that marked as an exhibit and have the witness agree with the mathematical calculation.

I think the problem and the troublesome aspect of it is to attempt to do it on the page from the witness' own testimony and thus imply that it is the witness' work. I was here. I did have to step out of the room for a little bit, but at least on -- I know you've already admitted 101, which has the same problem. But I know in what I heard there that Ms. McKiddy was saying as many flags as she could possibly run up the flagpole saying, I see what you've done, but I don't agree with it.

And repeatedly when a witness says, I don't agree with what you've done, and you're attempting to do it on their testimony, that strikes me as being a little bit over the top.

I don't know that that's a technical objection. But if it's just a mathematical calculation, we can do it over here on a pad.

MR. SWEARENGEN: I don't think it makes any difference where you do it. That's a good place to do it because that's where it comes into play, her DCF calculation, just show it where it is, and that's all I did.

MR. KRUEGER: Your Honor, I'd like to add one more thing. The last words on the bottom of this piece of paper above the footnote say Direct Testimony of Roberta A. McKiddy page 24. That's not her direct testimony.

MR. SWEARENGEN: I think we explained that. I mean, I went over it very carefully when I introduced the exhibit what was going on. I think she --

JUDGE RUTH: I've heard the objections. I believe the item can be admitted, but it will need to be changed in that I have read the title as Direct Testimony of Roberta A. McKiddy with Company Adjustments. I think it is more appropriate to change the title to Company Changes to Direct Testimony of Roberta A. McKiddy, which will help make it more clear that it is not the testimony of Roberta McKiddy, it is the company changes.

Then on the bottom I will have the court reporter write at the conclusion of the hearing "Company Changes to" before the line that says "Direct Testimony of Roberta A. McKiddy. That will just clarify that.

And I will ask that the same thing be done to Exhibit 101. The changes at the bottom will be Company Changes to Direct Testimony, and the title will be Company Changes to Direct Testimony.

And with that, the objection is overruled. Exhibit 101 was already admitted into the record, and Exhibit 104 is now admitted into the record.

(EXHIBIT NO. 104 WAS RECEIVED INTO EVIDENCE.)

MR. SWEARENGEN: I have one other housekeeping question. I heard earlier yesterday I think you said that when we had witnesses read from documents that you would like to get copies of those, and I had her do that on two separate occasions. One was Ms. McKiddy's rebuttal testimony in Case EM-2000-369, which she read into the record, and I believe you indicated it was your testimony; is that correct?

THE WITNESS: Correct.

MR. SWEARENGEN: And did you want a copy of that? And the other was the information from the Parcell's text, and I can make those available to you if you would like. It's just a question of what the Commission desires on that.

JUDGE RUTH: I do not need copies of the text. I think we have available that if I need to go beyond. But your reading from what testimony?

MR. SWEARENGEN: Robert A. McKiddy testimony in the UtiliCorp United/Empire case, Case No. EM-2000-369, her rebuttal testimony.

JUDGE RUTH: Do you already have those copies made?

MR. SWEARENGEN: No, I don't, but I will. She just read in a paragraph from that testimony.

JUDGE RUTH: We have access to that also, so in this case I will not ask that you provide copies.

MR. SWEARENGEN: Okay. Thank you.

JUDGE RUTH: I wanted to go ahead and take a break now unless there was an urgent matter that we needed to address before the break.

MR. KRUEGER: Your Honor, I have the copies of that Exhibit 100 that you asked that it be identified even though it was not offered.

JUDGE RUTH: Okay. That was the S&P reprint?

MR. KRUEGER: Correct.

JUDGE RUTH: And that was marked for identification purposes only; is that correct?

MR. KRUEGER: Correct.

JUDGE RUTH: Yes. Go ahead and pass those copies out, please.

Okay. We will take a break until 25 after 3. Off the record.

(A recess was taken.)

(EXHIBIT NO. 100 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

JUDGE RUTH: We're returning after a short break. Empire has finished cross-examination of witness Roberta McKiddy, and Chair Lumpe has requested that I ask a couple of questions. If you'll bear with me, I'll try and read what she wrote.

QUESTIONS BY JUDGE RUTH:

Q. First of all, is it correct that you, you being Staff and the parties, are going to true up the capital structure?

A. Yes, we have agreed to true up capital structure. I guess I should clarify that. It's an agreement to true up, but the discrepancy as to what level to true that up to, whether it be an actual or a hypothetical proposed by the company.

Q. Okay. There was earlier quite a bit of discussion about the comparables that you used to compare to Empire.

A. Yes.

Q. Can you explain again what criteria you used to select those companies?

A. I believe that criteria can be found on my Schedule 20. One of the criterion was that it needed to appear in, I believe, Valueline, needed to have no nuclear operations, and also needed to have revenues of greater than 70 percent attributable to electricity operations.

I believe one of the other criterion was that it needed to have a total capitalization of less than 6 billion. Let me refer to my schedule to be exact.

Q. That was Schedule 12?

A. Yes, 20-1. Yes, it was all of that criterion as well as a bond rating from S&P of between BBB and A+, and then one of the other criterions was that it had a positive dividend per share annual compound growth between the years 1990 and 2000, and finally, that none of the comparable companies had Missouri operations.

JUDGE RUTH: Okay. Thank you. Commissioner Murray, did you have any questions?

COMMISSIONER MURRAY: A few. Thank you.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Good afternoon, Ms. McKiddy.

A. Good afternoon.

Q. I want to make sure I understand Staff's position here. I think I understand you to have said that

Staff is not going -- is not normalizing capital structure to omit the effects of the merger; is that correct?

A. That is correct. We do not believe we should normalize Empire's capital structure because the capital structure was adjusted based on management's decision, and the resulting capital structure is not that varied from what is normal to the electric utility industry.

Q. And it's Staff's position that you are going -- you are normalizing the stock price to omit the effects of the merger; is that correct?

A. Yes. In essence, that's what we were doing. I use the term normalize, but the procedure that I use is actually the procedure that we always use in rate of return analysis. The reason I characterize it as normalize was because of the effects of the merger that terminated.

Q. What I'm trying to get to, I think I understand your explanations of why you've done both of those things or not done those things.

But my question is, if it is necessary to normalize the stock price to take into account or to omit any effects from the merger, wouldn't it also be logical to normalize the capital structure to omit the effects of the merger?

A. I don't particularly believe that it is appropriate to normalize the capital structure. Again, the

capital structure was adjusted at the discretion of the management, and since the termination of the merger there has been no action that I'm aware of except to the issuance of the toppers in March to change capital structure.
Q. So is it your position that the company could have changed its capital structure after the termination of the merger and prior to today's date?
A. I believe they had full discretion to do so.
Q. Do you believe they're going to do so before the true-up period?
A. I have no proof that they will do that.
Q. Now, is it also Staff's position that you will make adjustments to the capital structure for true-up?
A. Yes. We will make an adjustment to include the toppers that was issued in March.
Q. And that you will not make an adjustment for the stock price for true-up?
A. No. It's been management's decision at the Commission not to do that.
Q. But the stock price has nothing to do with the management, the company management's decision that they have control over at this point, right?
A. Stock price is driven by the market.
Q. So management -- or Staff's position to not adjust the stock price for true-up is not based upon

anything the company has or has not done?

A. State that again, please.

Q. Staff's position that you should not make an adjustment of the stock price for true-up purposes is not based upon anything that the company has or has not done?

A. I would say that is correct.

Q. I believe I heard you say that, absent the merger, the company stock would have continued to trade around the $23 range. Is that what you said?

A. I believe it would have, yes.

Q. But doesn't your -- isn't your analysis based upon an average $24.26 in your Schedule 14?

A. Yes, because what I tried to do was look at a period post-merger and pre-merger termination.

Q. So why would you have come up with $1.26 per share more than you say you think the company would have continued to trade at absent the merger?

A. I believe that $1.26 an probably attributable to appreciation in the stock price due to the hope of the pending merger, because the stock price at some points was even above the offer price of $29.50.

Q. So are you saying that your -- the stock price that you want to use based on an average of $24.26 does include some merger effect?

A. Yes. There are at least three months worth of merger effect in there, and by balancing it with the three months past the merger termination I believe has brought it to a normal level or something close to. I believe the $24 in my opinion is more comparable to the pre-merger trading value rather than the $19 and whatever that the company is proposing to use.

Q. On your Schedule 14 --

A. All right.

Q. -- in every month that is included there except the month of March are you using an entire month to arrive at the high stock price and the low stock price?

A. I believe what Wall Street City does is it looks at the entire trading activity for that particular month and picks out the high and low trading dollars and quotes that as of the last day of each month.

Q. So why did you only use the date of March 4th for the month of March?

A. Because that was the last date available to me prior to the filing of my testimony. Normally I would use a month-end period.

Q. And do you know if March 4th was, in fact, the highest day of the month?

A. I have no idea.

Q. So for the -- that Staff is not going to do any adjustment for true-up on the stock price; is that correct?

A. Not to stock prices, no.

Q. So you're not even going to take it up to the end of March for an average for March for your calculations?

A. Correct. I guess I could caveat that with the fact that I have been tracking the stock prices and the changes in projected growth since the filing of testimony and have done some basic DCF calculations to see if the validity of my recommended rate still holds true, and as of yesterday the results of all those calculations have fallen within my projected range.

Q. And that is because you are -- your projected growth rate has gone below --

A. If has declined. Right, it has declined. Now it is in a range of 2 to 3 percent.

Q. And I realize that is the most subjective of the items that you have that you looked at.

A. The growth rate?

Q. The growth rate.

A. Traditionally, yes.

Q. Can you tell me how you determine what you're estimating the growth rate to be?

A. Well, as you'll see on, I believe it's my Schedules 12 and 13, we look at a ten-year period of dividends per share, earnings per share and book value per share, and we calculate both a historical compound growth and trend line growth.

Q. And I believe Mr. -- I'm drawing a blank on his name.

A. Mr. Murry.

Q. Company counsel was asking you some questions I believe about that.

A. Do you want me to finish my answer?

Q. Yes. Go ahead. I'm sorry.

A. What I do after I calculate the compound and the trend line growth rates on the historical numbers, I do an averaging of those results to come up with an overall average of the dividends per share, earnings per share and book value per share on a historical basis. In this instance it resulted in a 2.10 percent.

What I then do is look at several sources of projected earnings per share, which in this case has been somewhat of a problem due to the lack of tracking by credit agencies. I did use a five-year projected EPS growth rate that was published by Valueline. There really were no other sources from which to obtain a projected five-year earnings per share.

So based on experience and discussions with management here at the Commission, in particular my supervisor, we determined that investors would look at a five-year historical EPS growth rate as a good predictor of what they thought five-year projected earnings per share might be.

So we took an average of the 2 percent and the 6 percent and then again compared that with a historical result of 2.1 percent and defined our range.

Q. And then how did you determine that your range would now be in the range of 2 to 3 percent?

A. Again, basically the historical data that I used on my Schedule 13 would not change. It still runs up through the end of December 2000. The only things that would change would be the projected five-year earnings per share published by Valueline. They decreased it from a 6 percent projection to a 4 percent projection.

So when you average the 2 percent, which represents the five-year historical earnings per share from Standard & Poor's, with Valueline's 4 percent projection, its revised projection, you would come up with an average of 3 percent. So on the low end you would have your 2 percent historical and your 3 percent projected as your high end.

Q. On page 34 of your direct, at lines 11 and 12 --

A. Yes.

Q. -- you state, In my opinion, the market views Empire as less risky than the industry due to its competitive rate structure and strong service area.

A. Yes.

Q. On what do you base that opinion?

A. Just experiences in doing cost of capital analysis.

Q. Just experience doing cost of capital analysis. Okay. Your experience must have you look at some criteria to determine whether the company is more or less risky. What criteria are you using that tells you that Empire is less risky or viewed as less risky?

A. Well, I think when you're looking strictly at the cost of capital analysis that I've performed in this instant case, the difference in growth rate is something that determines a difference in level of risk.

The comparable companies group I believe had an average 6 to 6 1/2 percent growth, where Empire only has a growth of 3 to 4 percent in my recommendation.

Q. So if the growth rate, the estimated growth rate is coming down, are you saying it's even less risky?

A. I'm just simply saying that its cost of capital is declining.

Q. And how does that relate to risk?

A. Well, growth is something that is viewed by Standard & Poor's when assigning a rating. It looks at capital structure and funds flows and regulatory decisions in defining risk for a particular bond rating.

Growth, of course, impacts potential growth in cash flows, which is something that's used to measure risk.

COMMISSIONER MURRAY: That's all. Thank you.

THE WITNESS: You're welcome.

JUDGE RUTH: Commissioner Gaw?

COMMISSIONER GAW: I don't have any questions right now.

JUDGE RUTH: I saw Mr. Conrad a moment ago. I guess he has left the room. So we'll move on and see if Public Counsel has any recross.

MR. COFFMAN: No recross.

JUDGE RUTH: I guess I have to ask Mr. Swearengen if you have any questions for recross?

MR. SWEARENGEN: I do have a couple questions based on Commissioner Murray's cross-examination, and I'll have to approach the witness, if I could, please.

JUDGE RUTH: Yes. What are you going to show the witness?

MR. SWEARENGEN: I'm going to show the witness Schedule DAM-26. It's a schedule to Donald A. Murry's rebuttal testimony which has been admitted into evidence.

JUDGE RUTH: Show it to counsel, please.

RECROSS-EXAMINATION BY MR. SWEARENGEN:

Q. Ms. McKiddy, I'm going to show you, hand you

Schedule DAM-26 to Mr. Donald A. Murry's rebuttal testimony, which is a chart that shows the Empire District Electric Company high/low close for its stock during March of 2001.
And I thought I heard you say in response to a question from Commissioner Murray that you took March 4 as the last date that you were able to use in that month for your March 2001 stock price for purposes of your testimony in this case; is that correct?
A. That's the point at which I cut off my testimony, yes.
Q. And according to this chart, March 4 would have been a Sunday. So there would not have been any trades on that day; is that right?
A. I'm not sure what day of the week that was.
Q. Okay. Would this chart indicate that there weren't any trades on that day?
A. It appears.
Q. And what about March 3rd, would that be a Saturday and there wouldn't be any trades on that day either and that's why no trades are shown on that day?
A. I'm assuming that's true.
Q. And then on -- so can I assume that what you probably used was March 2nd, the trades on that day for purposes of your analysis?
A. I would assume that that probably is a

March 2nd date. However, in Wall Street City the data appeared as March 4th.

Q.   And on March 2nd the actual trades were about $20.25; would that be fair to say?

A.   The average on that day, yes, was around that.

Q.   And that would have been the highest average for the entire month; is that right? It went down from there down to as low as $17.50; is that right?

A.   That looks about right.

Q.   Okay. Thank you.

One other question. In response to Commissioner Murray you were asked about Empire's risk, and you said that your opinion was based upon your experience as a financial analyst; is that right?

A.   Yes.

Q.   And your testimony about risk is on page 34, lines 7 through 12 of your direct testimony; is that right?

A.   What line again, please?

Q.   Line 7 through 12 where you say in there, I think on line 12, In my opinion, the market views Empire as less risky than the industry due to its competitive rate structure and its strong service area. That's the statement that Commissioner Murray was asking you about.

A.   Yes, I do make that statement.

Q.   And if I went back to Staff witness David

Broadwater's testimony in case ER-97-81, would you agree with me that he came to precisely the same conclusion in his case, in that case using precisely the same language in his direct testimony at page 41, lines 8 to 10, except quoting different predictions from Valueline?

A. I would not know without looking at Mr. Broadwater's testimony.

Q. You would not know without checking that?

A. No.

Q. Did you read Mr. Murry's testimony that pointed that fact out?

A. I believe he made reference to it. I did not verify whether that was a true statement or not.

MR. SWEARENGEN: Thank you.

JUDGE RUTH: Okay. Mr. Krueger, do you have redirect?

MR. KRUEGER: Just a couple questions, your Honor.

REDIRECT EXAMINATION BY MR. KRUEGER:

Q. In response to a question from Commissioner Murray, you mentioned that you'd done a calculation of the cost of capital using the DCF method yesterday, I believe; is that correct?

A. Yes. That was the last time I had done that calculation. I have been monitoring it on a weekly basis.

Q. Can you tell me how you calculated the yield when you did this yesterday? What stock price did you use?
A. When I did the calculation yesterday, I used a single point in time calculation using the stock price at close of yesterday's business.
Q. And what factor did you use for growth?
A. For growth, I used the 2 to 3 percent range that is based on the description of change and adjustments in growth that I described to the commission earlier this afternoon.
Q. What was the result of this calculation?
A. It was within the range that I have proposed. I don't have an exact number on top of my head.
Q. Okay.
A. I believe it was in the upper end of my range, though, about 9.3 percent.
Q. Mr. Swearengen just showed you the Schedule DAM-26. Do you remember that or do you want me to show it to you?
A. No. It was a chart showing the volatility in stock prices for the month of March.
Q. Do you know what has happened to the price of Empire stock since then?
A. Since March?
Q. Since the end of March, which is the last date

shown on this chart.

A. Well, I know that from February to the end of April the stock price averaged around $19.90. What it's done from a month-to-month basis, I've not done that kind of comparison.

Q. Do you recall what the most recent price is?

A. I believe Mr. Swearengen asked me that earlier, and although I looked at it yesterday, I don't think I could quote it to you today.

MR. KRUEGER: That's all the questions I have.

JUDGE RUTH: Okay. Ms. McKiddy, you may step down, then.

(Witness excused.)

At this time I would like to recall Empire's Mr. McKinney.

MR. SWEARENGEN: We can call him at this time. Myron McKinney.

JUDGE RUTH: I just have one question that Chair Lumpe had asked me to ask.

Mr. McKinney, I'll remind you that you still are under oath, and I have just one quick question, like I said, from Chair Lumpe.

She noted that earlier counsel for Empire had inquired of a witness regarding whether she was aware of any merger opportunities that Empire might be contemplating, and she would like to know whether you know whether Empire is contemplating any new merger opportunities at this time?

MR. McKINNEY: Empire's strategic direction at this point is to continue to operate as an independent company. We are publicly traded. I'd have to discuss merger should anyone call. No one has called recently.

JUDGE RUTH: Thank you. That was the question. Now, let's see. Mr. Conrad's still not here. Public Counsel, do you have any recross based on additional question from the Bench?

MR. COFFMAN: No, your Honor.

JUDGE RUTH: And Staff?

MR. KRUEGER: No, your Honor.

JUDGE RUTH: Mr. Swearengen, do you have any redirect for this witness based on that one question?

MR. SWEARENGEN: Well, whatever I asked him these guys would object to at this late hour, so I'll pass at this time.

JUDGE RUTH: I want to encourage you to ask your question if you have any question you wish to ask.

MR. SWEARENGEN: No. That's fine.

JUDGE RUTH: Then, Mr. McKinney, you may step down. Thank you very much.

(Witness excused.)

My notes indicate that the next witness up would be Public Counsel's Burdette; is that correct?

MR. COFFMAN: That is correct. We would call to the stand Mark Burdette.

JUDGE RUTH: Thank you.

(Witness sworn.)

JUDGE RUTH: Please be seated.

MARK BURDETTE testified as follows:

DIRECT EXAMINATION BY MR. COFFMAN:

Q. Would you please state your name and title for the record.

A. Mark Burdette. I'm a Public Utility Financial Analyst.

Q. Employed by?

A. Missouri Office of the Public Counsel.

Q. Okay. And are you the same Mark Burdette that has caused to be filed in this case prepared direct and rebuttal testimony marked as Exhibits 86 and 87 respectively?

A. Yes.

Q. Do you have any corrections to your direct testimony?

A. Yes, I have a couple.

Q. And are all your corrections the result of one mathematical error?

A. Yeah. I have one wrong calculation on a schedule, but it filtered through to a few different places in testimony.

Q. Okay. Why don't we proceed with whatever corrections you think need to be made to the text of your direct testimony.

A. Okay. Page 15, line 20, where it says, Overall average equals, the 4.57 should be 4.65.

Q. Do you have any other corrections to the text?

A. Page 15, line 30.

Q. Same page, line 30?

A. Under projected growth earnings per share, there's a 6.88 percent. Should be 7.72 percent.

Q. And does this correction of a mathematical error then flow through to some of your schedules?

A. Yes. And I have one other text error that I can do last. Do you want me to finish the schedules first?

Q. Okay. Fine.

A. Schedule MB --

Q. Yeah.

MR. COFFMAN: And I guess if anyone's interested, Mr. Burdette has reprinted out the three schedules affected. I hadn't planned on making this an exhibit, but I'll give you copies.

JUDGE RUTH: Now, these are -- tell me again what these are and how they're different.

MR. COFFMAN: These three pages are Mr. Burdette's Schedule MB-6, page 1 MB-6 page 4 and MB-8, and these -- there's just a few corrections that need to be made. These pages would then be the corrected schedules, just for your help, just to help out the parties.

JUDGE RUTH: To make the record cleaner, I'm going to go ahead and mark this as Exhibit 105 offered by Public Counsel, and it is the corrected schedules, three pages.

(EXHIBIT NO. 105 WAS MARKED FOR IDENTIFICATION BY THE REPORTER.)

BY MR. COFFMAN:

Q. Would you please, Mr. Burdette, walk us through the changes to these schedules for the record?

A. Yes. MB-6, page 1, the middle section of numbers there under projected growth, the second column which is Valueline/First Call Earnings Per Share, the current value for average that's 6.88 should be 7.72.

That same page, the bottom section of numbers under ranges, the second company there listed C-l-e-c-o, Cleco Corporation, overall average is listed an 3.92. Should be 4.38.

Right next to that, 6 percent should be 8.88. The last two numbers in that column, 4.25 should be 5.65. 4 should be 4.25.

Okay. Same page, same section of the page, under average, the number there is 4.57. Should be 4.65. A number right next to it, 9.32 should be 9.79. Last two numbers in that row right there, 5.24 should be 5.48. 4.16 should be 4.2.

Okay. Then Schedule MB-6, page 4, line 36, the 3.75 there should be 8.8 percent, and this is the error that's driving all the others.

Q. And do you have a correction on the --

A. Schedule MB-8. Again, just for the second company there, Cleco Corporation, there is -- the third number in the row is 6 percent. Should be 8.8 percent. The final number in that row is 9.86. Should be 12.66.

And then the very last column there, cost of equity high, the current average says 13.87. Should be 14.34. And then the comparison companies DCF high/low average, the overall number is currently 9.8. Should be 10.03.

And then the final correction I have is on page 30.

Q. I'm sorry. The one you just did, cost of equity, shouldn't that be 12.66 percent?

A. The 12.66 replaces 9.86 on the second entry in the final column.

Q. Okay.

A. The final entry in the final column is 14.34 replacing the 13.87. And then the final number on that schedule currently is 9.8. It should be 10.03.

Then the final correction is on page 30, and I have --

Q. This is of your text?

A. Yes. I'm sorry. Page 30, text.

Q. Of your direct testimony.

A. I have seven criteria there and I'm missing one that was used for selection but it didn't make it on this list for testimony, and that is -- I guess it would be like a line 11 1/2. No. 8 would read, No nuclear operations. And that is all the corrections I have.

Q. Okay. And let me ask you about what's been marked as Exhibit 105. These three pages were prepared by you?

A. Yes.

Q. And do these represent your schedules after that one mathematical correction has been made?

A. Yeah. They show the corrections already in place.

Q. The ones that you just walked through?

A. Yes.

Q. And let me just ask you if this one mathematical error after running it through your schedules in any way changes the result of your return on common equity recommendation?

A. No.

Q. And if I were to ask you the same questions contained in Exhibits 86 and 87 today, with the corrections that you've made now on the record, would your answers be the same today?

A. Yes.

Q. Based on your knowledge, information and belief?

A. Yes.

Q. Okay. And if I might just ask one more clarifying question. It had been brought up earlier. It might be important here. Public Counsel's recommendation regarding capital structure, is it your recommendation, similar to that of the Staff's, that the capital structure should be trued up as of June 30 and revised through the true-up process?

A. The real capital structure, yes. The actual capital structure.

Q. Should be determined at the true-up cutoff date?

A. Yes.

MR. COFFMAN: I would now tender Mr. Burdette for cross-examination and offer into the record Exhibits 86, 87 and 105.

JUDGE RUTH: Okay. Let's look at Exhibit 86 first, the direct testimony of Mr. Burdette. Are there any objections?

MR. SWEARENGEN: We have none.

MR. KRUEGER: No, your Honor.

JUDGE RUTH: Seeing no objections, it is admitted into the record.

(EXHIBIT NO. 86 WAS RECEIVED INTO EVIDENCE.)

JUDGE RUTH: Exhibit 87 is the rebuttal testimony of Mr. Burdette. Are there any objections to this?

MR. KRUEGER: No, your Honor.

JUDGE RUTH: Seeing no objections, it is also admitted into the record.

(EXHIBIT NO. 87 WAS RECEIVED INTO EVIDENCE.)

JUDGE RUTH: Exhibit 105 are the three pages of corrected schedules from Mr. Burdette's direct testimony. Are there any objections to this document?

MR. KRUEGER: No.

JUDGE RUTH: Okay. It is also admitted into the record.

(EXHIBIT NO. 105 WAS RECEIVED INTO EVIDENCE.)

JUDGE RUTH: And we'll begin cross-examination with Staff.

MR. KRUEGER: No questions, your Honor.

JUDGE RUTH: Mr. Conrad is not in the room right now for Praxair. So Empire, do you have cross?

MR. SWEARENGEN: Yes, I do, just a couple very brief questions, your Honor.

CROSS-EXAMINATION BY MR. SWEARENGEN:

Q. I'm looking at your -- Mr. Burdette, I'm looking at your Schedule MB-10 to your direct testimony. Do you have that in front of you?

A. I do.

Q. And there you have calculated something called pretax interest coverage; is that correct?

A. Yes.

Q. And let me ask you this. Would I be correct if I said pretax interest coverage equals net income plus interest plus income tax, net income plus interest plus income tax divided by interest? Is that how you calculate pretax interest coverage net income plus interest plus income tax divided by interest?

A. Yes, I believe so.

Q. Okay. You were here today and you heard Ms. McKiddy's testimony about pretax interest coverage, did you not?

A. I did.

Q. Are there any other revenues in this calculation other than the formula that you just gave us?

A. To my understanding, pretax interest coverage is calculated from net income, and that would already include all other expenses being taken out.

Q. Let me ask you this question. You made several corrections to your testimony, and I think you said that those corrections didn't change your ultimate conclusion, but it did change some of the numbers, did it not?

A. Correct.

Q. For example, the cost of equity for your comparable companies, the high side was -- the average was 13.87 and it went up to 14.34; is that not correct?

A. Yes, I believe that's the correction I just made.

Q. And the growth factor, the high was 9.32, and with your change it would go up to 9.79?

A. Yes.

MR. SWEARENGEN: Okay. Thank you. That's all I have.

JUDGE RUTH: Commissioner Murray, do you have questions?

COMMISSIONER MURRAY: Just a moment.

QUESTIONS BY COMMISSIONER MURRAY:

Q. Mr. Burdette, what stock price are you using for your calculations?

A. It's on Schedule MB-7. The average price I calculated for Empire, which is what I used for my dividend yield calculation, is $19 and -- 19.515. Basically, $19.52.

Q. Okay. So is that your understanding that that is fairly much in line with the current stock price?

A. Yeah. I believe Empire closed yesterday at 19.91, I think.

Q. I'm sorry. Which schedule did you say that's from?

A. MB-7. The first set of calculations there are the average stock price for Empire and the comparable group.

Q. And the capital, the capital structure, you're saying that you will true it up to whatever is the real capital structure as of the cutoff date; is that what you said?

A. Yes.

Q. So I'm pretty sure I'm clear that your position is that it should be based on actual capital structure?

A. Correct.

Q. Not a hypothetical that has not been achieved yet?

A. Correct.

Q. Do you think that the company could have adjusted its capital structure or could adjust its capital structure more in line with what its projections are before the end of the cutoff for the true-up period?

A. I don't know the details on how quickly Empire can turn around on financing, but certainly if that cutoff was unavailable, they could have easily delayed filing a rate case. It was fully within the company's decision to come in for a rate case with the capital structure that they had in place.

Q. Of course, they came in for the rate case when the merger was pending, and many things have changed since then, correct?

A. That's true.

Q. And the changes that you made, you did make the change that Mr. Murry -- or Dr. Murry, rather, pointed out in his rebuttal testimony where you had made a calculation error and the value should be 8.8 percent?

A. Yes. There were two numbers on that schedule. On Schedule MB-6, page 4, there are two numbers at the bottom. Under endless estimate there's the Valueline number and the first call number, and the bottom number should have been an average. The mistake was that I clicked on the wrong cell. So that 3.75 is half of 7.5 because I averaged 7.5 divided by two rather than adding 7 1/2 and 10.1 and dividing by two.

Q. And that was related to one corporation, correct?

A. Yes, one growth rate on one corporation.

Q. And that change made a small enough effect overall that it did not change your overall calculation?

A. Correct.

Q. I'm sure you have read Mr. Gibson's testimony, his surrebuttal testimony?

A. I have, yes.

Q. Do you have a copy of his surrebuttal with you?

A. Yes. Give me a second to find it, but I've got it. Okay.

Q. On page 4 of his surrebuttal, Mr. Gibson states that, and I'm looking at line 7, From a review of the rate cases that were concluded during the last decade, the high average return on equity was 12.7 percent in 1990 while the law was 10.77 in 99. In 2000 the return averaged 11.43. The average return for the first quarter of 2001 was 11.38 percent. The recommendation by Ms. McKiddy is so low that it would not even show up on this chart, and the high end of the recommendation by Mr. Burdette would barely make the chart and is still approximately one and one-quarter percent below the numbers.

And those were numbers that Mr. Gibson took from the Regulatory Research Associates. Can you tell me why you think that the recommendation that you are making is reasonable even though it falls -- your high end falls below, still below the average?

A. I don't make a recommendation based on what other commissions do. I make the recommendation based on market conditions and my analysis of the company, and that's what I based my recommendation on.

Q. Do you have any knowledge of how your recommendation compares with or do you do any analysis as to how your recommendation compares with the last decade in Missouri?

A. The last decade in Missouri? No.

COMMISSIONER MURRAY: I believe that's all. Thank you.

JUDGE RUTH: Commissioner Gaw?

COMMISSIONER GAW: Thank you.

QUESTIONS BY COMMISSIONER GAW:

Q. Mr. Burdette, if you wouldn't mind for me, can you give me an overview of the -- let me ask you this question first. Have you seen the testimonies and schedules of the witnesses for the company and for the Staff with regard to this issue on return on equity?

A. Yes.

Q. Can you give me an analysis or an overview of comparing why -- what leads to the differences in the results between your results and the other two? I realize that requires probably a substantial explanation, but if you could give me some brief points to begin with and then let me see if I want to explore any of them.

A. Well, at the fundamental level of the formulas, the DCF formula requires a stock price, dividend and growth rate. There can be disagreement on the stock price. It's been rare that I've seen disagreement on the expected dividend, but there is certainly a lot of disagreement on the growth rate. So that's two of those three variables contribute to differences there.

After the fact, after the fundamental formula has been calculated, usually in my experience companies find various adjustments. They'll increase, find various ways to increase the recommendation.

Q. In this particular case, when you're looking at two of those three factors being different among the analysis of those that are here, can you run through those, too, and tell me the differences in the entries on the assumptions that are made in this case on stock prices for instance begin with?

A. Stock price is primarily the time period. I used what I believe was a very recent. In fact, I believe it was the last Friday before I filed testimony. So on stock price, it was different periods of time.

Q. Yours was slightly below 20?

A. $19.52, yes.

Q. And Staff's was around 24-something?

A. I believe so. I don't know off the top of my head the exact number.

Q. And the company's was, do you recall approximately?

A. I do not. We have relatively similar dividend yields. So I'm assuming Mr. Murry was around $20, 19 to $20.

Q. All right. And the other issue of difference?

A. Growth rate.

Q. Yes. Tell me where the parties are on that.

A. Ms. McKiddy and I are -- I recommended 3 1/2. Three recommended a range of 3 to 4. So I would say we're pretty much right on there. Mr. Murry's growth rate is higher than that, I believe in the neighborhood of 5 1/2 to 6 percent.

Q. All right. Now, in your analysis of growth rate, can you tell me why you believe that your analysis is more accurate than the company's in this case, if you have an opinion?

A. I believe I do an objective analysis. I look at about as many growth rates as I can fined, different calculations of compound, historical, projected, and try to put my place -- put myself in the place of the investment community at large.

And what the DCF calls for is a sustainable growth rate. That's not the next year. That's not the next five years. I've seen a lot of analysts latch on to high five-year anticipated growth rates, and that isn't necessarily appropriate.

Q. So in this particular case, tell me what factors you believe support your analysis and how those relate to, either in a positive or a negative way, those that appear to be relied upon by the company.

A. I believe the company is focusing primarily on high projected growth rates. I do -- I don't believe that the -- I mean, looking at my calculations, I just don't see a 6 percent growth rate there, or a 5 1/2 percent growth rate.

Q. Why not? Can you be more specific?

A. The numbers don't show that. Well, let's go to testimony.

Q. That's what I'd like for you to do.

A. Page 15, my direct testimony, beginning on lines page -- I'm sorry. Beginning on line 11, growth rate summary for Empire, overall average of everything I calculate was 2.19 percent. And if you look through those numbers, there's not a number there above 4.77, and the overall average is 2.19.

So me looking at everything I calculated and considering where those numbers are and what I believe reasonable for the company is how I come to a conclusion.

Q. All right. From this -- and you say you and Staff are fairly close in that category; is that correct?

A. My recommendation is the middle of Staff's range.

Q. On your conclusion or on that factor?

A. On the growth rate.

Q. Okay. Now, in regard to stock prices --

A. Yes.

Q. -- give me an analysis of why you believe that your figure of around $19 is a better figure, at $19.52 is a better figure to rely upon than what Staff proposed at $24 and some odd cents?

A. Because I think the stock price and dividend yield calculations should be what is available to the investor. I cannot go out -- I mean, if I go out today to buy Empire stock, I'm going to pay 19 to 20 bucks for it, and that's what my yield is going to be based on going forward.

Q. And you believe that taking the last point in time is better than any kind of historical data on what the price of the stock has been over the course of months or years?

A. Well, I average over six weeks. So I can't really say month because I'm at a month and a half. The stock price in December of 2000 is completely irrelevant to the stock price tomorrow.

Q. All right. In this case, if we go back over time, we run into the question of this merger as being a factor on stock prices. Would you agree with that?

A. Oh, yes.

Q. Does that impact what you're doing in this case or is this just your standard way of examining the stock prices as a factor?

A. This is standard.

Q. For you?

A. Yes.

Q. Would you say that your method is more or less likely to be the standard in reviewing this than the standard used by Staff or company?

A. Well, the DCF formula calls for a current stock price. By definition, I would say that probably, if you wanted to get technical, you'd use a spot price. You would use today's price today and calculate the DCF cost of equity.

But due to variability in prices day-to-day, just things the market reacts to, you take a single-day price and I don't believe it's representative. So I spread it over six weeks to hopefully get away from some of that day-to-day kind of fluctuation.

Q. Your final -- your final result on return on equity compares to Staff's and company's how? And I know this is in the material, but if you can tell me now, I'd appreciate it.

A. Ms. McKiddy's range is 8 1/2 to 9 1/2. I recommend 10 to 10.25. And I believe Mr. Murry's, the last schedule I saw had 11 1/2 percent.

Q. All right. Have you found yourself in this position before?

A. No, I haven't. The closest -- the closest I've ever been is in the top half of Staff's range. But for Public Counsel to be above Staff, I think this might be a first.

Q. Just checking. I know that's not necessarily relevant.

A. Actually, I think that's a good thing.

COMMISSIONER GAW: I believe that's all the questions I have. Thank you. Thank you, Mr. Burdette.

JUDGE RUTH: Staff, do you have recross?

MR. KRUEGER: No, I don't, your Honor.

JUDGE RUTH: Mr. Conrad is still out of the room. So Empire?

MR. SWEARENGEN: No, ma'am. Thank you.

JUDGE RUTH: Public Counsel, redirect?

MR. COFFMAN: I think most of my redirect was taken care of.

JUDGE RUTH: Mr. Coffman, you'll need to move.

MR. COFFMAN: Sorry about that.

REDIRECT EXAMINATION BY MR. COFFMAN:

Q. I think most of my questions were actually covered by Mr. Gaw's thorough questions, Commissioner Gaw's.

I guess to complete the contrast, Mr. Burdette, on the stock price, your $19.52 was taken over a six-week period just prior to your filing testimony, correct?

A. Correct. The last Friday I could get data.

Q. And the $24 price of Staff was taken over what time period?

A. October 2000 to early March 2001.

Q. And does that one component make up the most substantial reason that Public Counsel differs from Staff's recommendation on this issue?

A. Yes. Yes.

Q. Okay. And when you're preparing your recommendation in a rate case, and you've done many of these cases, do you attempt to find a number that lowballs other recommendations? Do you attempt to do the?

A. No. I attempt to do an objective analysis.

MR. COFFMAN: Okay. That's all I have. Thank you.

JUDGE RUTH: Okay. Mr. Burdette, you may step down.

(Witness excused.)

That concludes the witness questioning for today, but I think we have just a couple of housekeeping measures.

I did want to state on the record that Empire had earlier requested that witness Lyons be excused from testifying today, and the other parties agreed to that and the Commission did grant or did allow Mr. Lyons to be excused.

I wanted to ask if the parties had any kind of status update regarding the revised list of issues?

MR. FREY: I do, your Honor. Could we go off the record for a second?

JUDGE RUTH: We'll go off the record for just a moment, but I'll need to go right back on and summarize what we do.

(AN OFF-THE-RECORD DISCUSSION WAS HELD.)

JUDGE RUTH: We will just note that Mr. Frey indicated Staff is continuing to work with all the parties on the status of the revised list of issues. They briefly showed me just the format they plan to be use, and I found that to be acceptable.

Mr. Frey, was there something else?

MR. FREY: I believe Mr. Dottheim has something to say and then I have something to add as well. Okay. Thank you. Shall I go over some of the highlights of this, Judge Ruth, or is that unnecessary?

JUDGE RUTH: Well, you're going to file that on Monday, correct?

MR. FREY: Yes.

JUDGE RUTH: I don't think you need to go over the document on the record right now. I was expecting it Monday.

MR. FREY: Okay. And with regard to the need to file order of cross, that's -- on the fuel issue that's --

JUDGE RUTH: That's right. You had mentioned that the parties need an extension until Monday to file the order of witnesses for the fuel issue, and that is granted.

MR. FREY: Thank you.

I would just mention one other thing, then, with regard to this document, and it's really more of a -- it goes beyond the document, and that is that there was a suggestion that we put in under Monday, June 4th, or it has been suggested and perhaps it was contemplated yesterday that we put in some language in there to the effect that we're going to be prepared to answer questions on the In-Service Stip and Agreement.

Mr. Duffy wants to make sure first of all if we're going to do that so he can notify appropriate witnesses for that exercise. It's possible at this point in the proceeding that that will not be necessary depending on what has developed.

I personally have heard rumors that there has been an Order to the effect that it's been approved. I have not seen such an Order, but I was -- I would ask you to comment on that then, Judge Ruth.

JUDGE RUTH: During the agenda session yesterday the Commissioners stated that they did not have any questions for the parties regarding the in-service agreement. An Order has not yet been issued. I have been otherwise engaged, but thank you for reminding me of that. And that is what the Commissioners said yesterday, and they've not indicated in any way that they've changed their mind.

MR. FREY: Thank you. Then we will not reflect any such exercise.

JUDGE RUTH: Since I have you here, though, can you remind me what witnesses you do plan or the parties plan on calling Monday?

MR. FREY: Yes. As to capital costs, the witnesses that are available for Empire would be Ms. Rolph, Mr. Wilson, Mr. Beecher. Staff witnesses are Mr. Featherstone, Mr. Oligschlaeger and Mr. Elliott.

On the operating and maintenance expense, the witnesses would be for Empire Mr. Groninger, Mr. Beecher; for Staff, again Mr. Featherstone, Mr. Elliott and Mr. Phil Williams. And that's all we have at this point for Monday.

Let me just check. I may have -- I see I'm reading off an earlier iteration of the document. Let me just check. Mr. Beecher under capital costs will adopt the testimony of Mr. Brill, as I understand it; is that correct? Yes. And I think the rest of the information I gave you is correct.

JUDGE RUTH: And like I stated earlier, for the witnesses that have testimony in regards to the issues settled in the Unanimous Stip and Agreement, the Commissioners indicated they may have questions. They want those witnesses available, but it's possible on Monday they'll choose not to ask those witnesses any questions.

MR. FREY: I believe that's understood, your Honor.

JUDGE RUTH: Okay. Was there another matter, Mr. Frey?

MR. FREY: Mr. Dottheim I believe has a point. Thank you, your Honor.

MR. DOTTHEIM: Judge, I have a number of housekeeping items and a progress report. The Staff did file late this afternoon testimony respecting the fuel and purchased power expense issue.

The Staff filed supplemental testimony in support of the Staff's change of position regarding fuel and purchased power expense of Cary G. Featherstone and James K. -- excuse me -- James C. Watkins. And the Staff filed revised staff surrebuttal testimony of Cary G. Featherstone and Janice Pyatte.

As far as Mr. Featherstone, his testimony is on fuel and purchased power expense, and Ms. Pyatte's revised surrebuttal testimony is on rate design.

In the instance where there's revised testimony, they have substituted language which was ruled as being objectionable yesterday. They have substituted what is hoped to be nonobjectionable language for the objectionable language.

There is no substantive change in the testimony. Minor changes may have occurred in a couple of instances for purposes of clarity, but again, no substantive changes. And again, what occurred with the revised testimony was the removal of certain language.

Regarding the supplemental testimony in support of the Staff's change of position regarding fuel and purchased power expense, that was also in relation to the ruling yesterday in response to the pleading filed on Tuesday by Praxair, and I have a complete set of that filing for you.

JUDGE RUTH: Thank you very much.

MR. DOTTHEIM: And I'll give that to you in just a moment. There was one other piece of testimony, and that was the supplemental surrebuttal testimony of Janice E. Fischer on incentive awards, incentive compensation. That testimony is complete.

Unfortunately, I was not able to complete the pleading to accompany it for filing today, but that testimony is complete and copies have been provided to the company and Mr. Conrad. I've yet to provide copies to Mr. Coffman.

So even though that supplemental surrebuttal testimony has not been filed, the company and Praxair have received copies and I will give copies to the Office of the Public Counsel and it will be filed on Monday.

Now, I do have additional copies of that if for any reason you would like that. I do have copies.

JUDGE RUTH: I'll wait 'til it's filed. Thank you.

MR. DOTTHEIM: And I should note that the testimony that was filed that I previously mentioned, copies have been hand delivered to the company. A copy was hand delivered to Mr. Conrad.

We are sending by Federal Express for delivery tomorrow a set of that testimony to Mr. Conrad's expert witness. I don't know if he'll be in the office to receive it, but we're making an effort to see that he receives a copy, too. And that's all I have at this point.

JUDGE RUTH: Okay. Thank you.

Mr. Swearengen, did you have --

MR. SWEARENGEN: Just to complete the record on this, I'm advised that Mr. Duffy this afternoon filed a Motion for Leave to File Supplemental Testimony as well as the supplemental testimony of Brad P. Beecher regarding Empire's change in position on fuel and purchased power expense calculation and methodology on behalf of the Empire District Electric Company.

Thank you.

JUDGE RUTH: I don't suppose you have a copy for me.

MR. SWEARENGEN: I'll tell you what, I'll give you Mr. Beecher's copy.

JUDGE RUTH: Are you sure?

MR. SWEARENGEN: Sure.

JUDGE RUTH: Any other parties have anything? Then I'm going to go ahead and note for the record that these are the filings that we had previously discussed. I had requested that the parties go ahead and file motions for leave to late file these for the record, and I am going to just grant Staff's motion to late file right now on the record, and the same for Empire's.

I assume there will be no objections to that since we have previously discussed this matter. If I'm wrong, say so now. Okay. Then those -- the motions to late file are both granted.

I have nothing further. That means we'll go off the record. Start back up on Monday at 8:30 a.m.

WHEREUPON, the hearing of this case was adjourned until Monday, June 4, 2001.

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