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Witness: Michael E. Palmer
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Case No.
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**Before the Public Service Commission
of the State of Missouri**

Direct Testimony

of

Michael E. Palmer

November 2006

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DIRECT/REBUTTAL TESTIMONY
OF
MICHAEL E. PALMER
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. EO-2007-0029 AND EE-2007-0030

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

2 A. Michael E. Palmer, 602 Joplin Street, Joplin, Missouri.

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

4 A. The Empire District Electric Company as Vice President – Commercial Operations.

5 **Q. PLEASE BRIEFLY DESCRIBE YOUR PROFESSIONAL EXPERIENCE.**

6 A. I have worked for Empire for over 20 years in a variety of capacities.

7 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE MISSOURI PUBLIC
8 SERVICE COMMISSION?**

9 A. Yes.

10 **Q. ON WHOSE BEHALF ARE YOU SPONSORING TESTIMONY IN THIS
11 PROCEEDING?**

12 A. The Empire District Electric Company.

13 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

14 A. The purpose of my testimony is to provide evidence in support of the application for
15 approval of a proposed territorial agreement jointly filed by Empire and Ozark Electric
16 Cooperative on July 18, 2006, and the accompanying application for variance Empire
17 filed at the same time. I will also respond to comments that have been made about the

1 two applications by the Staff of the Missouri Public Service Commission in the
2 memorandum and recommendation that was filed on October 10, 2006.

3 Generally speaking, my testimony will be that when the entirety of the situation is
4 considered, I believe there is sufficient good cause for the Commission to approve the
5 variance being sought by Empire so that the proposed First Territorial Agreement
6 between Empire and Ozark can be approved and implemented.

7 **Q. HAVE YOU READ THE STAFF'S MEMORANDUM AND**
8 **RECOMMENDATION IN THIS CASE?**

9 A. Yes, I have.

10 **Q. WHAT IS YOUR REACTION TO IT?**

11 A. I think the Staff is focusing on details that are important from its perspective but, in
12 the process of doing that, is failing to see the "big picture." For example, the Staff
13 says on the last page of the Memorandum that "In the Staff's view, the territorial
14 agreement is acceptable if it is not tied to the variance request." In my view, the
15 proposed territorial agreement is the Big Picture here, not the variance request. The
16 Staff obviously does not have a problem with the territorial agreement that will cover
17 almost ten square miles and determine the electric supplier for many hundreds of
18 customers for many years. Instead, the Staff spends most of its time in the memo
19 focused on the cost of some wiring and decorative streetlights in one subdivision. The
20 reason I say the territorial agreement is the "Big Picture" is that it eliminates a lot of
21 problems for a diverse set of interests, including the City of Republic, real estate
22 developers, and future customers.

23 **Q. HOW DID EMPIRE BECOME INVOLVED IN THIS SITUATION?**

1 A. The City of Republic called on us to help them solve some problems. This is not
2 something that Empire originated or is pushing for its own benefit. As their franchised
3 supplier of electricity, we were happy to try to help the City. We were invited to
4 attend a meeting at a City facility at the end of March of this year. I attended, along
5 with two other representatives of Empire.

6 **Q. COULD YOU SUMMARIZE WHAT TOOK PLACE AT THE MEETING?**

7 A. I will tell you what I remember of it because it was essentially an all-day affair. We
8 listened to the other parties, including the City, explain their positions and we offered
9 information or clarification when we thought it was appropriate. There was discussion
10 about various topics. One of the main topics that I remember was the fact that if the
11 City were to annex these developments, there were two important considerations that
12 were causing some consternation with the developers. One had to do with the
13 compensation that had to be paid to any fire district that was affected by the
14 annexation. My understanding of that discussion was that the state-required
15 compensation is much less when the property is undeveloped, which argues for
16 annexation to occur before a lot of houses are built.

17 The second major topic was the state law on rural electric cooperatives operating
18 in non-rural areas. The developers that spoke at the meeting had all signed agreements
19 to take service from Ozark Electric Cooperative. They had obviously not been aware
20 that when their property was annexed by the City, Ozark would not be permitted to
21 serve new structures after annexation because annexation changes the area from
22 "rural" to non-rural. Since Republic has a population greater than 1,500, it is not a
23 rural area where cooperatives are normally allowed to serve. This topic, in particular,

1 produced a lot of consternation with the developers. I recall at least one of the
2 developers saying that he would consider bringing a lawsuit to stop the annexation.

3 At some point, I said that Empire would do what it could to try to help solve the
4 problems. The representatives from Ozark essentially said the same thing. At that
5 point, we broke up into smaller groups and started talking about possible solutions.

6 **Q. WHAT HAPPENED THEN?**

7 A. After a couple hours of talks, and working together, the parties managed to hammer
8 out a preliminary framework for an agreement that was acceptable to everyone. As a
9 part of the deal, we were asked to agree to meet some incentives that Ozark had
10 offered one of the developers, so that developer would not be economically harmed by
11 the overall transaction. We made it clear that the only way Empire could lawfully
12 agree to meet that condition was to seek a variance from the Commission's rules and
13 our tariff.

14 With Empire obtaining the ability to serve The Lakes at Shuyler Ridge
15 development under this proposal, it was logical and reasonable to draw an exclusive
16 service area on the southwest side of the City around that development, since Empire
17 was already serving some customers in that general area, and was serving customers
18 inside the city limits just to the north of there. This then naturally led to the drawing
19 of some boundaries for an exclusive service area for Ozark on the southeast side of the
20 City where they had some facilities and customers.

21 **Q. AT THE END OF THE MEETING, DID YOU CONSIDER THE TENTATIVE**
22 **AGREEMENT TO BE A REASONABLE AND WORKABLE APPROACH TO**
23 **SOLVE THE PROBLEMS THAT HAD BEEN VOICED?**

1 A. I felt very comfortable that I could recommend it to management of Empire. It
2 appeared to be a very fair compromise since both Ozark and Empire would obtain
3 exclusive service territories in a rapidly developing area, the developers would
4 generally get the benefit of their previous bargains with Ozark, and the City would
5 presumably be able to annex the areas easier than if it had to fight some lawsuits. It
6 was apparent to me that the City had done a lot of infrastructure planning for these
7 areas and that the annexation was the key to making those plans a reality.

8 I knew that the Commission was generally in favor of territorial agreements. We
9 attempted to make this one as non-controversial as possible by not forcing the existing
10 Ozark customers to change their supplier. I also knew that the Commission had
11 granted variances to Empire in the past in order for us to meet unregulated
12 competition, so it sounded to me like a workable solution to a lot of problems.

13 **Q. IS THE GRANTING OF THE VARIANCE IMPORTANT TO THIS**
14 **PROPOSED TRANSACTION?**

15 A. Very much so. Even though I have called the territorial agreement the "big picture"
16 since it covers approximately nine-and-one-half square miles and would be in effect
17 for the indefinite future, I think the variance is the key element holding everything else
18 together.

19 **Q. WHAT DO YOU MEAN BY THAT?**

20 A. If Empire is not granted the variance and allowed to meet, but not exceed, what Ozark
21 Electric Cooperative has already offered the one developer in the way of underground
22 facilities and decorative street lights, then that developer has no logical reason to take
23 electric service from Empire. Frankly, he can get a better deal on the wiring and

1 streetlights from Ozark. This is because Ozark is not regulated by the Commission
2 and, therefore, Ozark makes its own business decisions as to how it will treat
3 developers. In contrast, the Commission tells Empire specifically how its tariff will
4 read when it comes to dealing with developers. Empire's tariff is simply not designed
5 to meet the competition for new service that Ozark presents.

6 So, if that developer of The Lakes at Shuyler Ridge has no incentive to take
7 service from Empire because he can get a better deal from Ozark, then a key portion of
8 the territory Empire would obtain under the proposed territorial agreement would be
9 served by Ozark instead of Empire. If that happens, we do not have a relatively even
10 division of the territory on the south side of the City. With that, Empire's interest in
11 the territorial agreement rapidly disappears because we would be giving up a large
12 portion of potential territory to Ozark for perhaps decades or more, for basically
13 nothing in return. I cannot in good conscience say that is a good thing for either
14 Empire's customers or shareholders. I look at this situation as the variance being a
15 relatively small price to pay for the many benefits to many parties that come from the
16 certainty of exclusive service areas for the future on the south part of the City of
17 Republic.

18 **Q. WHAT IS YOUR UNDERSTANDING OF THE REASON THAT EMPIRE**
19 **FILED FOR THE VARIANCE?**

20 A. My understanding is that to comply with the law, we had to request the variance, just
21 as to comply with the law, we had to seek Commission approval of the territorial
22 agreement. As I said earlier, Empire has a tariff approved by the Commission that
23 dictates how we deal with real estate developers who want our service. We are not

1 permitted to deviate from the terms of the tariff without permission from the
2 Commission. So we could not agree to match what Ozark offered the developer of
3 The Lakes at Shuyler Ridge without the permission of the Commission.

4 The Commission also has a set of rules on "promotional practices" that are found
5 in Chapter 14 of the Commission's rules. In general, those rules prohibit Empire, and
6 any other regulated utility, from giving "free stuff" to builders, architects, developers,
7 and others in order to induce those people to take utility service from us.

8 I also know, though, that the Chapter 14 rules say that for "good cause shown" the
9 Commission will grant a variance from the rules, and I know that the Commission has
10 granted variances to Empire from these rules in the past. The Staff mentioned some of
11 them in its memorandum.

12 **Q. WHAT DO YOU KNOW ABOUT THE ORIGIN OF THE PROMOTIONAL**
13 **PRACTICES RULES?**

14 A. Although I was not in the public utility business in 1971, I have read the text of the
15 Commission's General Order No. 51 that it issued in late June of 1971. There was a
16 "declaration of public policy" that appeared in section 1 of General Order 51. It says:
17 Electric and gas utilities operating within this state have engaged in promotional
18 practices in an effort to attract additional business and to retain existing business. The
19 promotion of goods or services offered the public is an inherent and important part of
20 the economy of this state and nation. Only when such promotion becomes excessive
21 is it subject to prohibition. The laws of this state require the rates of a public utility to
22 be just and reasonable and in conformity with the rules, regulations and orders of the
23 Commission. They prohibit a public utility from, directly or indirectly, demanding or

1 receiving from anyone a greater or lesser rate for service than that specified in its
2 tariff. They prohibit, with respect to rates and services, the granting of unreasonable
3 preferences or advantages to anyone, or subjecting anyone to unreasonable prejudice
4 or disadvantage. Accordingly, the Commission declares that the adoption and
5 enforcement of these rules and regulations are in the public interest because they seek
6 to advance the welfare of all consumers by defining promotional practices which
7 violate the public utility laws of this state and by permitting the employment of
8 promotional practices which will stimulate fair and vigorous competition among
9 utilities and others.”

10 **Q. DO YOU SEE ANYTHING IN THAT DECLARATION OF PUBLIC POLICY**
11 **THAT YOU THINK PERTAINS TO THIS CASE?**

12 A. Yes. There are a couple of important points. First, it's apparent to me from the first
13 sentence of the statement that prior to 1971, electric and gas utilities regulated by the
14 Commission were offering incentives to builders, developers and others in order to get
15 new customers. In other words, a gas company might offer free piping, or a trip to the
16 Bahamas, in order to get a developer to put natural gas furnaces and water heaters in a
17 subdivision instead of electric ones, or vice versa. Next, in the third sentence, I get the
18 distinct impression that the Commission thought these business practices were so
19 widespread that they were getting out of hand, and they wanted to regulate it, which is
20 what they did with General Order 51.

21 Given that background as to why the rules exist, I would draw a contrast between
22 the harm that the Commission was obviously trying to prevent in passing General
23 Order 51 and what is going on in this case. By that, I mean that Empire did not go out

1 and try to offer something that is beyond Empire's tariff to get the developer of The
2 Lakes at Shuyler Ridge to use Empire's service. That developer voluntarily chose to
3 take service from Ozark. That developer has agreed to take service from Empire
4 instead, in order to make this territorial agreement work, so long as the developer
5 doesn't come out worse than he would have by staying with Ozark. So the conduct
6 that the Commission was trying to prevent with the promotional practices rules did not
7 take place here. This is a special situation where a variance is necessary to make a
8 much larger transaction occur, namely a territorial agreement.

9 **Q. DO YOU THINK TERRITORIAL AGREEMENTS IN GENERAL ARE IN**
10 **THE PUBLIC INTEREST?**

11 A. I think that generally they are. I also think that because the Missouri legislature passed
12 a law in 1988 specifically allowing them, that the legislature also considers them to be
13 in the public interest.

14 **Q. DO YOU THINK THAT THIS PROPOSED TERRITORIAL AGREEMENT IS**
15 **IN THE PUBLIC INTEREST?**

16 A. Yes. As I noted earlier, it solves or eliminates a lot of potential problems and paves
17 the way for orderly development in the area south of the City of Republic. Empire has
18 entered into several territorial agreements in the past with other rural electric
19 cooperatives and I would say that they have worked very well. This would be the first
20 one we would have with Ozark Electric Cooperative.

21 **Q. THE STAFF INDICATES IN ITS MEMORANDUM THAT THE VARIANCE**
22 **SOUGHT BY EMPIRE SHOULD BE DENIED. DO YOU HAVE AN OPINION**

1 **OF WHAT WOULD HAPPEN IF THE REQUESTED VARIANCE WERE**
2 **DENIED?**

3 A. As I indicated earlier, I think the only way this overall plan will work is with the
4 variance. If the variance is denied, I foresee the whole thing unraveling and that will
5 put everyone back into the same situation that we had at the March meeting with the
6 City. It would wipe out all the work that has gone into the proposed territorial
7 agreement.

8 **Q. DO YOU SHARE THE STAFF'S VIEW THAT GRANTING THE VARIANCE**
9 **WOULD BE DISCRIMINATORY?**

10 A. No. I am not a lawyer, but I understand that the statutes pertaining to utilities use
11 terms like "undue or unreasonable preference." It would seem to me that the
12 legislature created the Public Service Commission to administer these laws, and left it
13 to the Commission's discretion to determine what was "reasonable" in any given
14 situation.

15 I am generally aware of situations where the Commission has approved specially-
16 tailored solutions to real-world problems where the overall benefits are viewed as
17 outweighing the perceived discriminatory aspects. First of all, there are the situations
18 mentioned in the Staff Memorandum where the Commission has granted variances
19 from the promotional practices rules in order to meet unregulated competition. The
20 Commission even included a reference in those rules to the process for obtaining a
21 variance.

22 Some other examples that come to mind are flexible tariffs for gas companies that
23 were faced with customers constructing physical by-passes of the distribution system

1 and approval of special contracts for large industrial type electric customers. In each
2 of these situations, an argument could be made that what the Commission approved
3 was "discriminatory." But these special mechanisms approved by the Commission
4 allowed the utilities to alter their tariff rate to a reasonable degree in order to retain the
5 customer or otherwise serve to accomplish an end result that was viewed as being in
6 the public interest.

7 I want to make clear that Empire is willing to file a compliance tariff that defines
8 the boundaries of the variance if the Commission deems that to be necessary. We
9 view this as a special situation and it would not be Empire's intention to repeat this
10 process on a regular basis.

11 **Q. DO YOU HAVE ANY COMMENTS ON THE NUMERICAL CALCULATIONS**
12 **THAT THE STAFF HAS PUT IN ITS MEMORANDUM?**

13 A. I do not. Empire has another witness, Martin Penning, who has examined those
14 numbers and has tried to put them into perspective.

15 **Q. DOES THIS CONCLUDE YOUR PREPARED TESTIMONY IN THIS CASE?**

16 A. Yes.

