

**EXECUTIVE SUMMARY
FOR THE DIRECT TESTIMONY OF LAURIE DELANO
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO.**

Purpose of Testimony

The testimony recommends a tracker mechanism to recover Empire's other post-employment benefits, requests approval of future recovery of regulated assets regarding minimum pension liabilities, and to support the FAS 87 Regulatory Asset Amortization and deferred tax adjustments.

Summary

Empire collects FAS 106 costs in rates based on the test year level. As a result, increases or decreases in costs between rate cases are either over or under recovered. The tracker mechanism we are proposing eliminates this problem by ensuring the level of expense recognized for financial purposes is consistent with the level of expense included in rates.

We request the Commission authorize Empire to follow the accounting treatment prescribed by the Federal Energy Regulatory Commission regarding minimum pension liabilities, and authorize the transfer of any existing and future pension Other Comprehensive Income amounts to a regulatory asset on the Empire general ledger and the recovery of this amount in future rate cases.

In the last rate case, ER-2004-0570, the Commission approved an accounting mechanism to track FAS 87 Pension Expense. Since that rate case, Empire has accumulated \$970,387 of FAS 87 costs as a regulatory asset. In accordance with the accounting process authorized by the Commission, the FAS 87 regulatory asset has been recognized in the rate base of this case. Our proposed adjustment of \$158,214 reflects the amortization of the non-capital FAS 87 regulatory asset over a five-year period.

Prior to Case No. ER-94-174 Empire recovered only federal income tax expense related to timing differences created by accelerated tax depreciation. This provided a tax benefit of Missouri state income tax to ratepayers, thus lowering cost of service. Beginning with Case No. ER-94-174 deferred state income taxes were provided to the Company in rates. However, no mechanism was provided to allow for the recovery of the previously flowed through state income tax benefits to ratepayers nor have subsequent rate cases. Empire proposes to recover this amount over an eighteen year period.

Conclusion

Empire requests a tracker mechanism to recover Empire's other post-employment benefits and requests approval of future recovery of regulated assets as a result of the accounting treatment described by the Federal Energy Regulatory Commission for minimum pension liabilities. An adjustment of \$158,214 was reflected in the filing to recognize the amortization of the non-capital FAS 87 regulatory asset. An adjustment of \$130,431 was recorded in the deferred tax calculation to recognize the additional annual income tax expense as a result of the rate-making used prior to Case No. ER-94-174.

Exhibit No.:
Issues: FAS 106, FAS 87
Deferred Income Taxes
Witness: Laurie Delano
Sponsoring Party: Empire Dist. Electric Company
Type of Exhibit: Direct Testimony
Case No.:
Date Testimony Prepared: February 2006

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

Direct Testimony

Of

Laurie Delano

February 2006

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OF
LAURIE DELANO
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION

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DIRECT TESTIMONY
OF
LAURIE DELANO
THE EMPIRE DISTRICT ELECTRIC COMPANY
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MISSOURI PUBLIC SERVICE COMMISSION
CASE NO.

1 **INTRODUCTION**

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

3 A. My name is Laurie Delano. My business address is 602 Joplin Street, Joplin, Missouri
4 64802.

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

6 A. I am a Controller and Assistant Secretary/Treasurer of The Empire District Electric
7 Company (the “Company” or “Empire”).

8 **Q. PLEASE DESCRIBE YOUR EDUCATION AND BACKGROUND.**

9 A. I received a Bachelor of Science in Business Administration from Missouri Southern
10 State University and a Master of Business Administration from Missouri State
11 University. I joined the Company in 1979 and served as Director of Internal Auditing
12 from 1983 to 1991. I left the Company in 1991 and was employed as an Accounting
13 Lecturer at Pittsburg State University, and in management positions with TAMKO
14 Roofing Products, Inc. and Lozier Corporation before rejoining the Company in
15 December 2002.

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

17 A. The purpose of my testimony is to recommend a tracker mechanism to recover Empire’s
18 other post-employment benefits (“OPEB”), commonly referred to as FAS (Financial
19 Accounting Standard) 106 Costs. I am also requesting approval of future recovery of

1 regulated assets as a result of the accounting treatment for the recognition of minimum
2 pension liability as described by Federal Energy Regulatory Commission (FERC).

3 Finally, I am supporting the FAS 87 Regulatory Asset Amortization adjustment and
4 Deferred Tax adjustment.
5

6 **TRACKER MECHANISM**

7 **Q. DOES EMPIRE CURRENTLY USE AN APPROVED TRACKER MECHANISM**
8 **TO RECOVER ITS FAS 87 COSTS?**

9 A. Yes, in our last rate case, a tracker mechanism was approved for the recovery of FAS 87
10 costs. In this rate case, we are requesting to implement a similar mechanism for the
11 recovery of our FAS 106 costs.

12 **Q. PLEASE EXPLAIN HOW THE TRACKER MECHANISM YOU ARE**
13 **PROPOSING FOR FAS 106 WILL WORK.**

14 A. The mechanism we are proposing will enable Empire to accumulate the difference
15 between the actual FAS 106 costs incurred in the future and the current test year costs as
16 either a regulatory asset or liability. The regulatory asset or liability that is recorded in
17 the future will then be included in rate base and amortized over five years in the next rate
18 case.

19 **Q. PLEASE EXPLAIN WHY EMPIRE DESIRES TO ESTABLISH SUCH AN**
20 **ACCOUNTING PROCEDURE.**

21 A. Currently, Empire collects FAS 106 costs in rates based on the test year level. As a result,
22 increases or decreases in costs between rate cases are either over or under-recovered. The
23 tracker mechanism we are proposing eliminates this problem by ensuring the level of

1 expense recognized for financial purposes is consistent with the level of expense included
2 in rates.

3 **Q. HOW WOULD YOU CHARACTERIZE THIS PROPOSAL?**

4 A. It is reasonable and appropriate. In this regard, Section 386.315, RSMo.2000 allows the
5 Company to recover FAS 106 costs. The statute says “ ... the commission shall not
6 disallow or refuse to recognize the actual level of expenses the utility is required by
7 Financial Accounting Standard 106 to record the postretirement [sic] employee benefits
8 for all the utility’s employees, including retirees, if the assumptions and estimates used
9 by a public utility in determining the Financial Accounting Standard 106 expenses have
10 been reviewed and approved by the commission . . .”

11 In order to recover FAS 106 costs in their entirety, Empire requests the Commission
12 authorize the implementation of our proposed FAS 106 tracker mechanism. (See
13 Exhibit LD-1 for a description of this mechanism).

14
15 **MINIMUM PENSION LIABILITY ADJUSTMENT**

16 **Q. WHAT IS A MINIMUM PENSION LIABILITY ADJUSTMENT?**

17 A. According to Financial Accounting Standard number 87 (“FAS 87”), a minimum
18 pension liability must be recorded on the Company’s books if the accumulated benefit
19 obligation exceeds the fair value of the assets set aside to meet the obligation.

20 According to Generally Accepted Accounting Principles (“GAAP”), the offset to the
21 pension liability is a charge (debit) to Other Comprehensive Income (“OCI”). FERC
22 Instruction No. 23 (paragraph 3), states that if it is probable that an item of OCI will be
23 included in rates in subsequent periods, a reclassification adjustment to a regulatory
24 asset is appropriate.

1 **Q. DOES FERC PROVIDE ANY OTHER GUIDANCE REGARDING MINIMUM**
2 **PENSION LIABILITY ADJUSTMENTS?**

3 A. Yes. On March 29, 2004, FERC issued a reply to a question regarding this issue in OED-
4 DRAP Docket No. AI04-2-000. A copy of this is attached as Schedule LD-2.

5 **Q. DOES THE ORDER ISSUED BY THE COMMISSION IN EMPIRE'S MOST**
6 **RECENT RATE CASE ALLOW FOR ADDITIONAL FUNDING TO THE**
7 **PENSION ASSET ACCOUNT TO PREVENT AN UNDER FUNDED POSITION?**

8 A. Yes, our current rate order allows us to recover the cost of additional funding if it is
9 made to avoid the write off of an existing prepaid pension asset (i.e. charge to OCI).
10 However, the Company could possibly find itself in a position, through market
11 conditions or future accounting or other legislation, where this funding would be
12 impractical.

13 **Q. IS THE COMPANY SEEKING COMMISSION APPROVAL TO RECORD A**
14 **MINIMUM PENSION LIABILITY AS A REGULATORY ASSET?**

15 A. Yes. We request that the Commission authorize Empire to follow the accounting
16 treatment prescribed by the FERC regarding minimum pension liabilities, and authorize
17 the transfer of any existing and future pension OCI amounts to a regulatory asset on the
18 Empire general ledger.

19 **Q. HOW DO YOU PROPOSE THAT THE COMMISSION ACCOMPLISH YOUR**
20 **REQUEST?**

21 A. The final order issued in this case should clearly state that Empire is authorized to
22 follow the accounting treatment prescribed by the FERC regarding minimum pension
23 liabilities, and that Empire is authorized to transfer any existing and future pension OCI

amounts to a regulatory asset on the Empire general ledger and amortized in future rate proceeding.

FAS 87 REGULATORY ASSET AMORTIZATION ADJUSTMENT

Q. DID EMPIRE MAKE AN ADJUSTMENT TO THE TEST YEAR EXPENSES TO REFLECT THE AMORTIZATION OF THE FAS 87 REGULATORY ASSET?

A. Yes. In the last rate case, Case No. ER-2004-0570, the Commission approved an accounting mechanism to track FAS 87 Pension Expense. Since that rate case, Empire has accumulated \$970,387 of FAS 87 costs as a regulatory asset. In accordance with the accounting process authorized by the Commission in the last rate case, the FAS 87 regulatory asset has been recognized in the rate base of this case. Furthermore, per the order, Empire is to begin the amortization of this asset in its next rate case. Our proposed adjustment of \$158,214 reflects the amortization of the non-capital FAS 87 regulatory asset accumulated since the last rate order over a five-year period. Empire requests that the Commission accept this amount for ratemaking purposes.

DEFERRED TAX ADJUSTMENT

Q. PLEASE DESCRIBE THE ADJUSTMENT TO DEFERRED TAXES PROPOSED FOR THIS RATE CASE.

A. An additional annual income tax expense of \$130,431 has been added to the deferred tax calculation related to state income taxes previously flowed through to the benefit of rate payers.

Q. PLEASE DESCRIBE THE CHANGE IN DEFERRED TAXES DUE TO THE STATE INCOME TAX RATES.

1 A. Prior to Case No. ER-94-174 which authorized new rates effective August 15, 1994,
2 Empire had been provided revenues which recovered only federal income tax expense
3 related to timing differences created by accelerated tax depreciation.
4 The Company booked this deferred income tax at the federal income tax rate as provided
5 in previous rate cases. The effect of providing rates for only the federal income tax rate
6 was to flow through a tax benefit of Missouri state income tax to ratepayers, thus
7 lowering cost of service.

8 **Q. PLEASE CONTINUE.**

9 A. Beginning with Case No. ER-94-174, deferred state income taxes were provided to the
10 Company in rates. However, no mechanism was provided to allow for the recovery of
11 the previously flowed through state income tax benefits to rate payers. Subsequent rate
12 cases have also not addressed the issue.

13 **Q. HOW DOES EMPIRE PROPOSE TO REMEDY THIS DISCREPANCY?**

14 A. The Company has made detailed computations of the amount of the state income tax
15 benefits that ratepayers received prior to Case No. ER-94-174. Empire proposes to use
16 the South Georgia method to recover this amount over an eighteen year period beginning
17 with the effective date of this case. As previously mentioned, an additional annual
18 income tax expense of \$130,431 was recorded in the deferred tax calculation.

19 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

20 A. Yes. At this time, it does.

AFFIDAVIT OF LAURIE DELANO


STATE OF MISSOURI)
) ss
COUNTY OF JASPER)

On the 31st day of January, 2006, before me appeared Laurie Delano, to me personally known, who, being by me first duly sworn, states that she is the Controller and Assistant Secretary/Treasurer of The Empire District Electric Company and acknowledges that she has read the above and foregoing document and believes that the statements therein are true and correct to the best of her information, knowledge and belief.



Laurie Delano

Subscribed and sworn to before me this 31st day of January, 2006.



Pat Settle, Notary Public

My commission expires: _____

