Exhibit No.:	
Issue.:	Interim Rates
Witness:	David W. Gibson
Type of Exhibit:	Direct Testimony
Sponsoring Party:	The Empire District Electric Company
Case No.:	ER-2001-452
Date Testimony Prepared.:	February 15, 2001

DIRECT TESTIMONY
OF
DAVID W. GIBSON
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION

I. Introduction

Q. STATE YOUR NAME AND ADDRESS PLEASE.

A. David W. Gibson. My business address is 602 Joplin Street, Joplin, Missouri.

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

A. The Empire District Electric Company, ("Empire" or "Company"). I am General Manager of Finance and Assistant Secretary.

Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I was graduated from the University of Nebraska in May of 1972 with a Bachelor of Science degree in Business Administration with a major in accounting. After graduation, I worked for the public accounting firm of Price Waterhouse & Co., for a period of approximately two years in the auditing section. From that time until 1979, I held positions as assistant controller or controller with various retail and manufacturing companies.

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In April, 1979 I accepted a position with Empire in the internal audit department. Since that time, I have been the Director of Corporate Planning, Director of Financial and Regulatory Accounting and Director of Financial Services and Assistant Secretary. Effective January 8, 2001, I became General Manager of Finance and Assistant Secretary. The Empire Board of Directors has elected me Vice President - Finance and Principal Financial Officer effective March 1, 2001.

II. Purpose and Scope

Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

A. The purpose of my testimony is to describe the impact of rising gas prices on the financial condition of the Company and the calculations used to determine the amount of interim rate relief that is being requested.

Q. WHY IS EMPIRE REQUESTING INTERIM RATE RELIEF?

A. Although the Company filed a "permanent" electric rate case on November 3, 2000, the impact of increasing natural gas prices will have an adverse financial impact on the Company such that its financial integrity will be jeopardized before the permanent rates become effective.

III. Financial Considerations

Q. WHY DIDN'T THE COMPANY FILE FOR RATE RELIEF SOONER IF IT IS FACING DETERIORATING FINANCIAL CONDITIONS?

A. The Company had lost many experienced personnel from the time that the proposed merger with UtiliCorp United Inc. ("UtiliCorp") was announced up until the time that work began on preparation for the permanent rate case that was to coincide with the addition of the new State Line Combined Cycle ("SLCC") plant. This meant that other personnel, who were not as experienced, were used to help in the preparation of the permanent rate case. As a consequence, the time needed for the preparation of the permanent case was longer than usual. After the unanticipated termination of the merger in January 2001 and the dramatic rise in natural gas prices, the need for immediate rate relief became a matter of utmost importance.

Q. WHAT ARE THE CONDITIONS THAT WILL CONTRIBUTE TO THE ADVERSE FINANCIAL IMPACT ON THE COMPANY?

A. As indicated, the rate relief that is being requested in the permanent rate case is timed to coincide with the addition of our new SLCC generating plant which is anticipated to be in service on June 1, 2001. In order to complete the unit, our anticipated expenditures during 2001 will be approximately $25 million. Our current short-term debt is approximately $80 million so we will need additional permanent financing during the first quarter of this year to complete the unit. With our current capital structure represented by approximately 60% debt, any adverse financial results which Empire experiences will result in higher costs for our customers.

Q. HOW WOULD YOU CHARACTERIZE EMPIRE'S CURRENT CAPITAL STRUCTURE?

A. It is not normal.

Q. PLEASE EXPLAIN.

A. As part of the merger agreement with UtiliCorp, we redeemed our outstanding preferred stock and were precluded from issuing any additional common stock. The Company did issue $100 million in unsecured notes at the end of 1999. Prior to the merger announcement, we had a target of approximately 45-50% common equity, 5-

10% preferred and 45-50% long-term debt. In order to achieve these targets and pay off our short-term debt of $85,000,000, we would have to issue approximately $62,000,000 of common stock and $67,000,000 of preferred stock plus decrease the long-term debt by approximately $44,000,000.

Q. HAS EMPIRE BEEN ABLE TO RAISE THE REQUIRED CAPITAL IN THE PAST?

A. Yes. One interesting note is that since our growth rate has been higher than other utilities in Missouri, almost all of our increase in common equity has come from additional common stock issues, not by retaining earnings. To put it another way, the rate increases that we have had since 1992 have not been to benefit the common stockholders, but to help finance additional customer needs. In addition to this, the Company has not raised the dividend rate since 1992 and the stock price has gone down by approximately 6% for the same period. In spite of these circumstances, the Company has been able to raise the needed common stock in order to finance its customer growth.

Q. WHAT IS THE PROJECTED TIME LINE FOR FINANCING DURING 2001?

A. The Company anticipates issuing approximately $50 million in permanent financing in the first quarter of 2001 and an additional $30-35 million in the fourth quarter of the year.

Q. WHAT ARE THE CURRENT CREDIT RATINGS FOR EMPIRE?

A. Since the merger with UtiliCorp was terminated in January, 2001, the Company has been taken off the CreditWatch list by Standard & Poor's, but with negative implications. Moody's did not change our rating of review for downgrade due to the financial demands associated with our SLCC construction program. Both rating agencies cite the need for adequate rate relief in order to maintain current credit ratings. If our earnings decrease, then so will our ratings. If this happens, any debt that would be issued would carry higher costs which would then be passed on to our customers. In addition, the Company has a requirement, due to its Indenture, to maintain at least a 2X interest coverage ratio. If we are not able to generate additional income, we will be precluded from issuing any other debt.

Q. IS THE INTEREST COVERAGE FOR THE COMPANY ABOVE THE 2X RATIO AT THIS TIME?

A. Yes. The coverage ratio is approximately** ____ **at the end of 2000. The only reason that the ratio is as high as it appears is because we exclude unsecured debt in the calculation for the Indenture coverage.

Q. PLEASE EXPLAIN WHY THE UNSECURED DEBT IS EXCLUDED.

A. The coverage ratio for the Indenture deals only with those bonds that use property in order to guarantee payment. The $100 million that Empire issued in 1999 was unsecured and as such, excluded from the calculation. Other parties, such as rating agencies, look at total interest which would include the unsecured debt. With the unsecured debt included, the ratio would be** ____ x.** It would take only a $** ____ **million drop in income to put us below the 2X requirement. In addition, with the current ratio and the same income, the Company would only be able to issue approximately $** ____ ** million in long-term debt.

Q. WHY DOESN'T THE COMPANY ISSUE COMMON OR PREFERRED STOCK?

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A. The same factors that affect the rates we pay for long-term debt and short-term commercial paper also would have an effect on the issuance of common or preferred stock. If earnings are not sufficient to cover dividends, at least in the short term, then the issue price of the stock would decrease. The result of this would be to further stress the financial condition of the Company.

Q. PLEASE EXPLAIN.

A. If the price per share is decreased, then we would have to issue more shares in order to raise the same amount of capital. When this happens, earnings per share would decrease. If we were to issue preferred stock, the higher interest rate would result in less earnings available for the payment of common stock dividends which would also result in lower earnings per share.

Q. HAS THE COMPANY CONSIDERED OTHER FINANCING ALTERNATIVES?

A. Yes, we are currently considering other alternatives including the issuance of some type of Trust Preferred Stock. Trust Preferred Stock in the range of $50 million would be treated as equity capital by most rating agencies. This may give us an opportunity to obtain financing while waiting for potential rate relief prior to the issuance of additional common stock.

Q. YOU MENTIONED THAT THE COMPANY HAS A PERMANENT RATE CASE PENDING. WON'T THE PERMANENT RATE CASE PROVIDE THE RATE RELIEF THAT IS NEEDED?

A. As previously mentioned, the permanent rate case was filed in order to coincide with the completion of the new SLCC unit. We have seen during 2000 and into 2001 a material increase in the price of natural gas (see the testimony of Stan Kaplan for a discussion of gas prices). We are projecting that the increase in gas prices will have a detrimental effect on Empire during 2001 before the new permanent rates would be in place. In this instance, the magnitude of the change in gas prices and its effect on the return on equity necessitate our receiving the interim increase in a timely manner.

Q. PLEASE EXPLAIN.

A. Our projected earnings for 2001 show a deteriorating return on equity. Table 1, set out below, summarizes what will happen primarily as a result of increasing gas prices.

Table 1

TABLE 1 HAS BEEN DEEMED HC

** **

As can be seen, our return on equity will decrease to extremely low levels (approximately** __%**) during the last half of 2001. Even with the implementation of the requested permanent increase, our earnings for 2001 will not be sufficient and are projected to be only $** __** per share of common for the year. This compares to $** __** for 2000 and $1.46 for 1999, both of which exclude merger costs.

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Q. YOU MENTIONED THAT THE PRIMARY CAUSE OF THE DECREASE IN EARNINGS IS DUE TO GAS PRICES. HOW DO RISING GAS PRICES CAUSE SUCH A DRAMATIC DROP IN EARNINGS?

A. Along with the rising gas prices, Empire is becoming more dependent on the use of gas to serve customers. The new SLCC unit uses natural gas as its fuel. With this unit coming on line, we will own approximately 600 MW of generation which uses gas. So, it is not only the rise in prices, but also the increase in the quantity of gas used that is causing the drop in earnings.

IV. Rate Relief Calculations

Q. HOW DO YOU PROPOSE THAT THE INTERIM RATES BE STRUCTURED?

A. I propose that the rates be increased on an interim basis first to recognize the rising gas prices and then on July 1, 2001 to recognize the addition of the SLCC.

Q. PLEASE DESCRIBE HOW THE AMOUNT OF INTERIM RATE RELIEF WAS DETERMINED.

A. In order to determine the amount of interim rate relief that is needed, I compared the cost of natural gas used during the period of March, 2000 through September, 2000 with the projected cost for the same period during 2001. The result is that our natural gas cost is projected to increase by $**________**during the period of March, 2001 through September, 2001. Table 2, set out below, shows how this amount was determined. This represents a decrease of approximately $** **___ in earnings per share.

Table 2

(A) Projected Total NSI -Kwh	(B) Cost of Gas Projected 2001	(C) Cost of Gas Actual 2000

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Mar
Apr
May
Jun
Jul
Aug
Sep
March through September

** Portions of Table 2 Have Been Deemed to be HC **

Additional cost (column B - C)

Cost per kwh March through September (Additional cost / total column A)

Recovery amounts:	(1) Total NSI -Kwh (A)	(2)	(3) Cost of Gas
Mar		0.00619	
Apr		0.00619	
May		0.00619	
Jun		0.00619	
Jul		0.00619	
Aug		0.00619	
Sep		0.00619	

Projected data is from the 2001 demand and energy forecast.

Q. IS PART OF THE INCREASE DUE TO INCREASED USE OF NATURAL GAS AFTER JUNE 2001?

A. Yes. As I indicated previously, we anticipate an increase in the use of natural gas once the SLCC is placed into service and the current purchased power contracts expire.

Q. PLEASE DESCRIBE THE SECOND PART OF THE PROPOSED INCREASE.

A. The second part of the proposed interim increase was determined by the amount of

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production plant that will be placed in service with the new SLCC unit less the amount for capacity charges that will be eliminated once the plant is in service. Table 3, set out below, shows how the amount was determined.

Table 3

Portions of Table 3 Have Been Deemed to be HC

	** **
Amount of State Line Combined Cycle Plant (1)	
Return on Rate Base (2)	
Pre-Tax Return (3)	(1*2)
Income Tax Gross-Up Factor (4)	
Required Revenue (5)	(3 * 4)
Less: Decrease in Capacity Charges (6)	
Net Revenue Requirement (7)	(5 - 6)
Amount per Kwh (8)	(7 / 9)
NSI for 2001 (9)	
NSI for July - September (10)	
% to be recovered (11)	(10 / 9)
Revenue to be required (12)	(7 * 11)
Adjustment per Kwh (13)	(12 / 10)

Q. HOW DO YOU PROPOSE TO ALLOCATE THIS INCREASE TO EMPIRE'S CUSTOMERS?

A. Since the cost of natural gas is dependent on the amount that is used, we are suggesting that the amount be allocated to our customers based on Kwh usage. This will result in an additional $.00619 per Kwh used. Effective July 1, 2001, we will increase the rider by $.00222 to reflect the SLCC coming on line. This will mean that there will be approximately $** ____ ** million recovered and subject to refund prior to the conclusion of the permanent rate case. Table 4, set out below, depicts how the amounts were determined.

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Table 4

	Total NSI -Kwh	Natural Gas Recovery @ 0.00619/Kwh	Plant Recovery @ 0.00222/Kwh
Mar			
Apr			
May			
Jun			
Jul			
Aug			
Sep			
Less 1/2 of month rider is phased in			
Amount recovered			
Total Company recovered and subject to refund			

Portions of Table 4 Have Been Deemed to be HC

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It should be noted that only one half of the increase will be recognized in March for the natural gas recovery portion and in the month of July for the net plant addition.

Q. WHY IS THIS?

A. The reason is because the interim rates will be for service rendered on and after March 1 or on and after July 1. This results in approximately one half of the resulting revenues being recognized in the first month.

Q. WHAT WILL BE THE IMPACT ON THE EARNINGS IF THE REQUESTED INCREASE IS RECOVERED THROUGH THE INTERIM RIDER?

A. The Missouri portion of $20,491,807 ($17,450,117 + $3,041,690) is $16,770,495 or 81.84% would result in earnings moving from $** ____ ** per share to approximately $** ____ ** for the year.

Q. WHAT RETURN ON EQUITY WOULD THAT PRODUCE, OR HOW WOULD THAT CHANGE YOUR TABLE 1?

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A. If the Company were to increase revenues by the total amount of approximately $16.8 million, its return on average equity would increase to approximately** ____%.**

Q. DO YOU PROPOSE ANY OTHER RECOMMENDATIONS FOR THE COLLECTION OF THE INTERIM RATES?

A. Yes, since the amounts collected are on an interim basis, any overcollection plus interest, would be refunded to our customers. The refund would be applied to each customer's bill during the month of November, 2001. The reason for the lag is so that we may determine the amount of overcollection, if any. For those customers who have moved out of the service territory, a check for the amount of overcollection will be issued during the month of November, 2001. The interest rate to be used would be based on the Company's short-term interest rates. Any undercollection in revenue would be absorbed by the Company.

Q. IS THE REQUEST FOR INTERIM RATE RELIEF AN ATTEMPT TO OFFSET THE REGULATORY LAG THAT THE COMPANY NORMALLY EXPERIENCES WHEN FILING FOR A RATE INCREASE?

A. Not entirely. The Company has been experiencing increased gas prices during 2000 and into 2001. We are not asking for an increase in the base cost of natural gas, only the projected increase over 2000 prices. The difference between the costs experienced during 2000 and the costs built into our base rates are still subject to regulatory lag. The additional costs between the costs reflected in base rates and current costs will be absorbed by the Company. We are not asking that the Commission "make us whole" by allowing rate recovery of the total increase in gas costs.

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Q. DESCRIBE THE INTERIM RATE SHEETS FILED IN THIS CASE.

A. Interim Rider INT contains provisions to charge, for all rates, an additional $.00619 per Kwh effective March 1, 2001 and an additional $.00222 per Kwh effective July 1, 2001. It is scheduled to expire September 30, 2001 or when new permanent rates are put into effect as a result of Case No. ER-01-269.

Q. IS A REFUND PROVISION A PART OF THE INTERIM RIDER?

A. Yes, as I previously indicated, interest will be paid for any over recovery of revenues at a rate equal to the short-term debt rate experienced by the Company.

Q. DO YOU HAVE ANY OTHER COMMENTS CONCERNING THE INTERIM FILING?

A. Yes, since the Staff of the Commission is currently on site at the Company and due to the urgency of this filing, the Commission may want to explore the possibility of using outside auditors in order to assist the Staff in this interim case.

Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY AT THIS TIME?

A. Yes.

AFFIDAVIT

STATE OF MISSOURI)
) ss
COUNTY OF JASPER)

On the 15th day of February, 2001, before me appeared David W. Gibson, to me personally known, who, being by me first duly sworn, states that he is the General Manager of Finance and Assistant Secretary of The Empire District Electric Company and acknowledged that he has read the above and foregoing document and believes that the statements therein are true and correct to the best of his information, knowledge and belief.

David W. Gibson

Subscribed and sworn to before me this 15th day of February, 2001

Patricia A. Settle, Notary Public

My commission expires: August 16, 2002

PATRICIA A SETTLE
Notary Public - Notary Seal
STATE OF MISSOURI
JASPER COUNTY
MY COMMISSION EXP. AUG. 16,2002