

Exhibit No. \_\_\_\_\_  
Issue: Reason for Ratecase  
Witness: W.L. Gipson  
Type of Exhibit: Direct Testimony  
Sponsoring Party: Empire District  
Case No.: ER-2002-424  
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Before the Public Service Commission  
of the State of Missouri

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Missouri Public  
Service Commission

**Direct Testimony**

**of**

**W.L. Gipson**

**February 2002**

DIRECT TESTIMONY  
OF  
W. L. GIPSON  
THE EMPIRE DISTRICT ELECTRIC COMPANY  
BEFORE THE  
MISSOURI PUBLIC SERVICE COMMISSION  
CASE NO.

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. William L. Gipson, 602 Joplin Street, Joplin, Missouri 64801.

3 Q. WHO IS YOUR EMPLOYER AND WHAT POSITION DO YOU HOLD?

4 A. The Empire District Electric Company ("Empire" or "Company") is my employer. I hold the  
5 position of Executive Vice President and Chief Operating Officer.

6 Q. PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND.

7 A. I hold a Bachelor of Science Degree in Business Management Technology and an Associate  
8 Degree in Computer Science from Missouri Southern State College in Joplin, Missouri.

9 Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.

10 A. Prior to joining Empire I worked for an international furniture manufacturing company and a  
11 regional bank. I joined Empire as a Computer Programmer in 1981. I have held positions in  
12 Information Services, Economic Development and Operations. My employment with  
13 Empire has been continuous since 1981.

14 Q. HAVE YOU PREVIOUSLY PRESENTED TESTIMONY BEFORE THIS OR ANY  
15 OTHER REGULATORY BODY?

16

1 A. Yes, I have presented testimony before the Missouri Public Service Commission  
2 ("Commission"), the Kansas Corporation Commission and the Arkansas Public Service  
3 Commission.

4 Q. MR. GIPSON, WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?

5 A. The purpose of my testimony is to provide the background for Empire's decision to request  
6 both interim and permanent rate relief.

7 Q. PLEASE DESCRIBE EMPIRE.

8 A. Empire is a Kansas corporation with its principal office and place of business at 602 Joplin  
9 Street, Joplin, Missouri 64801. Empire is engaged in the business of providing electrical  
10 utility services in Missouri, Kansas, Arkansas and Oklahoma; water utility services in  
11 Missouri; and has a certificate of service authority issued by the Commission to provide  
12 certain telecommunications services.

13 Q. WILL YOU PLEASE DESCRIBE THE AREA SERVED BY EMPIRE AND GIVE A  
14 BRIEF DESCRIPTION OF THE CUSTOMERS SERVED?

15 A. Empire provides electric service in an area of approximately 10,000 square miles in  
16 southwest Missouri and the adjacent corners of the states of Kansas, Oklahoma, and  
17 Arkansas. Empire's operations are regulated by the utility regulatory commissions of these  
18 four states as well as the Federal Energy Regulatory Commission. The area embraces 119  
19 incorporated communities in 23 counties in the four-state area.

20 The area economy is well balanced with small to medium manufacturing operations,  
21 medical, agricultural, entertainment, tourism, and retail interests all contributing to above-  
22 average customer growth.

23

1 At the end of 2001, Empire served 127,007 residential customers, 22,707 commercial  
2 customers, 336 industrial customers, 1,658 public authority customers, and 7 wholesale  
3 customers throughout our system. Most of the communities in the service area are small,  
4 with only 28 being in excess of 1,500 population. Only 9 communities have a population in  
5 excess of 5,000, and the largest city is Joplin, Missouri, with a population of approximately  
6 45,500.

7 In Missouri, at the end of 2001, Empire served 110,744 residential customers, 19,895  
8 commercial customers, 263 industrial customers, 1,349 public authority customers, and 3  
9 wholesale customers. In addition to electric service, Empire also provides regulated water  
10 service to approximately 4,500 customers in the Missouri communities of Aurora,  
11 Marionville, and Verona. We have made public our intention to exit this water business,  
12 and have been in discussions with several parties.

13 Q. PLEASE DESCRIBE EMPIRE'S TELECOMMUNICATION OPERATIONS.

14 A. Empire began installing fiber optics in 1996 for internal purposes; but, due to the economics,  
15 the cables contained excess capacity beyond that which Empire had plans to use. Some of  
16 this excess capacity has since been leased to customers such as cellular phone companies,  
17 long distance carriers, hospitals, schools, and manufacturing. This capacity is either a  
18 number of dedicated dark fibers or an amount of bandwidth on the SONET (Synchronous  
19 Optical Network) network. In January of 1998 Empire became certified (Missouri Case No.  
20 TA-98-233) as an intrastate interexchange and local exchange telecommunications  
21 company.

22 Q. EXPLAIN, GENERALLY, EMPIRE'S NEED FOR A RATE INCREASE AT THIS TIME.

1 A. First, as the Commission is aware, an error in Empire's 2001 electric rate case, Case No.  
2 ER-2001-299, resulted in Empire not being able to recover \$3,562,983 in revenue. We  
3 asked the Commission to correct the error in Case No. ET-2002-210, but it declined to do  
4 so. Second, rates implemented in Empire's 2001 electric rate case reflect Empire's capital  
5 structure at June 30, 2001. Since then, in December 2001 the Company issued \$39,243,750  
6 in common equity in December 2001 and plans to issue about \$50 million in common equity  
7 in June 2002 and, at that same time, retire \$37.5 million in long-term debt. The end result  
8 will be a capital structure made up of approximately 47.5 percent common equity. Third,  
9 the Company continues to believe the 10 percent return on equity authorized by the  
10 Commission in Case No. ER-2001-299 is insufficient to meet the Company's ongoing  
11 obligations to its customers. And fourth, the Company would propose to rebase the Interim  
12 Energy Charge ("IEC") approved in Case No. ER-2001-299.

13 Q. HOW DO YOU PROPOSE TO DEAL WITH THE ERROR?

14 A. In addition to permanent tariffs, Empire is also filing interim tariffs designed to recover the  
15 \$3,562,983 resulting from the error. The amount is known and measurable. The amount is  
16 material, as it would represent approximately 21 percent (after tax) of the Company's 2001  
17 net income. The error was admitted and we believe the Company should be collecting this  
18 amount in rates. The Commission expressed a concern about 'single issue ratemaking' as a  
19 reason for not correcting the error when it was discovered. Although we disagreed with the  
20 Commission's interpretation because the amount was identified in the context of a rate case,  
21 the use of this interim filing takes away any basis for the Commission's concern. The  
22 Company would simply ask the Commission to allow these interim tariffs to be  
23 implemented immediately, subject to the refund conditions on the interim tariff.

1 Q. IS IT YOUR TESTIMONY THAT THE INABILITY TO RECOVER THIS \$3,562,983  
2 HAS SOMEHOW RESULTED IN AN "EMERGENCY" FOR EMPIRE?

3 A. No. Empire is not claiming that its financial integrity or ability to render safe and adequate  
4 service over the next several months will be jeopardized if the request is not granted.  
5 However, this should not matter.

6 Q. WHY?

7 A. First, it is my understanding, based on advice from counsel, that the Commission has very  
8 broad discretion to grant interim rate relief and that an "emergency" standard is not an  
9 absolute which must be applied in all circumstances. Second, and more importantly, what  
10 we have here is a very unique situation in which the Commission Staff and the Commission  
11 itself have acknowledged that an error was made in the calculation of Empire's revenue  
12 requirement in Case No. ER-2001-299. The amount of the error is \$3,562,983. This interim  
13 filing presents the Commission with the opportunity to correct this mistake in the context of  
14 a permanent case in which all relevant factors concerning Empire's revenue requirement will  
15 be considered. Correcting this mistake is simply the right thing to do.

16 Q. DO YOU HAVE ANY THOUGHTS ON THE INTERACTION OF THE RECOVERY OF  
17 THE INTERIM AMOUNT AND ADJUSTING THE LEVEL OF THE IEC?

18 A. Yes. Empire has previously suggested that the level of the current IEC might be reduced to  
19 offset the recovery of the \$3,562,983. While the Company is under no obligation to lower  
20 the IEC at this time, we are very interested in pursuing a means to implement the interim  
21 tariffs in conjunction with a possible voluntary lowering of the IEC. This could reduce the  
22 overall amount our ratepayers are required to pay for service. We think the best way to  
23 accomplish this on an expedited basis is for the Commission to order the parties to an early

1 pre-hearing conference to discuss the prospects. We will certainly make an effort to achieve  
2 something that is reasonable for all concerned.

3 Q. IS A 47.5 PERCENT COMMON EQUITY RATIO TYPICAL FOR EMPIRE?

4 A. Yes. As I mentioned above, current rates reflect Empire's actual capital structure at June 30,  
5 2001, which included about 37.76 percent common equity. That level of common equity  
6 was quite unusual for Empire and came about as a result of a proposed merger with  
7 UtiliCorp United Inc. Historically, Empire's common equity has ranged between 45 and 50  
8 percent of total (common and preferred equity plus long-term debt) capital structure. In his  
9 direct testimony, Empire witness David W. Gibson, details Empire's plans to achieve its  
10 more typical common equity level.

11 Q. WHAT IS THE COMPANY'S PROPOSED RETURN ON COMMON EQUITY ("ROE")  
12 IN THIS CASE?

13 A. The Company is proposing an ROE of 12 percent. In his direct testimony, Company  
14 witness Donald A. Murry explains why a 12 percent return is appropriate for Empire.  
15 Simply stated, Empire must meet its obligations to its customers to provide safe and reliable  
16 electric power service. The Company must be able to finance significant capital projects to  
17 meet this ongoing obligation. The Company must have the financial performance necessary  
18 to maintain or improve its bond ratings. Despite our best efforts, Empire cannot find a way  
19 to accomplish this with an inadequate return on common equity.

20 Q. WOULD YOU ELABORATE ON EMPIRE'S BOND RATINGS?

21 A. Yes. Currently Empire's senior debt is rated A- by Standard & Poor's and Baal by  
22 Moody's. The Moody's rating is a result of a May 2001 downgrade from A2, where they  
23 cited as reasons "the Company's deterioration in credit measures....the Company's

1 heightened regulatory risk associated with its efforts to obtain necessary levels of rate  
2 increases from the Missouri Public Service Commission (MPSC) to recover the Company's  
3 ongoing capital expenditures and increased operating expenses." Both agencies continue to  
4 maintain a "negative outlook" for the Company, which means we remain a candidate for  
5 further downgrades. We remain in close contact with Moody's and Standard & Poor's and  
6 are seriously concerned that one or both agencies could downgrade our debt even further.  
7 Further details on Empire's bond ratings can be found in Mr. Gibson's direct testimony.

8 Q. MOODY'S MENTIONED CREDIT MEASURE DETORIORATION; CAN YOU  
9 EXPLAIN?

10 A. Specifically, Moody's is concerned about interest expense coverage ratios and the Company  
11 is as well. Our first mortgage bond indenture requires an interest coverage ratio of two  
12 times the annual interest requirement. This ratio dropped below this threshold in September  
13 2001 and remains there. And, since it is below two-times, for the first time in the  
14 Company's history, we are prohibited from issuing any additional first mortgage bonds.  
15 Further details on this issue can be found in Mr. Gibson's direct testimony.

16 Q. WHAT IS THE COMPANY DOING TO MITIGATE THESE PROBLEMS?

17 A. All personnel vacancies must be approved by me prior to being filled. Travel and seminars  
18 or conferences have been curtailed. In fact, any travel involving air travel or overnight  
19 accommodations requires senior officer approval. Other expenses, both capital and  
20 operating, have been reduced or delayed to the greatest extent possible. We have embarked  
21 on an extensive restructuring in Commercial Operations (Customer Service, Engineering,  
22 Transmission and Distribution) that is designed to maintain excellent customer service and  
23 reduce ongoing expenses.



1 Q. WHAT CHANGES DO YOU PROPOSE TO THE IEC?

2 A. The Company continues to believe that the end results of the IEC are positive for both  
3 Empire's customers and its shareholders. Neither is harmed (in fact, both are protected)  
4 when actual and prudently incurred fuel and purchased power costs are recovered as a cost  
5 of service item. However, Empire has witnessed some moderation in the cost of natural gas  
6 as a fuel source and therefore is proposing to rebase the IEC at \$21.69 base and \$24.16  
7 ceiling (NSI, with demand charges). In his direct testimony, Empire witness Brad P.  
8 Beecher will detail the Company's proposed changes to the IEC.

9 Q. ARE THERE ANY OTHER PROPOSALS THE COMPANY IS MAKING IN THIS  
10 FILING?

11 A. Yes. The Company is proposing an Experimental Low Income Rider ("ELIR"), as well as,  
12 Rider "SR" to collect costs associated with security enhancements (if government-mandated  
13 as a result of the terrorist attacks on September 11, 2001) and a change in the summer/winter  
14 differential for residential customers. In her direct testimony, Empire witness Kelly Walters  
15 will detail these three proposals.

16 Q. ARE THERE OTHER COMMENTS YOU WOULD LIKE TO MAKE?

17 A. Yes. Historically, Empire customers have enjoyed rates which were among the lowest in the  
18 state. We realize that the magnitude of this increase will likely move our rates closer to the  
19 statewide average. However, the return on rate base for the test year is 7.72 percent without  
20 rate relief and, with the full amount requested, the return on rate base would be 9.94 percent.  
21 The Company has worked diligently to make the proper decisions regarding the addition of  
22 new plant and the control of all expenses. I would implore the Commission to give this  
23 request a full and impartial review.

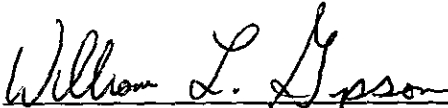
1 Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY AT THIS TIME?

2 A. Yes it does.

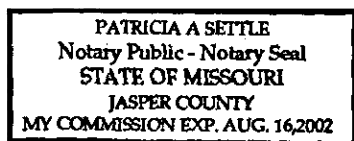
AFFIDAVIT

STATE OF MISSOURI )  
 ) ss  
COUNTY OF JASPER )

On the 25th day of February, 2002, before me appeared W.L. Gipson, to me personally known, who, being by me first duly sworn, states that he is the Executive Vice President and Chief Operating Officer 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.

  
W.L. Gipson

Subscribed and sworn to before me this 25th day of February, 2002



  
Patricia A. Settle, Notary Public

My commission expires: August 16, 2002