Exhibit No.
Issue: Depreciation, Pension Expense
Witness: Gregory A. Knapp
Type of Exhibit: Surrebuttal Testimony
Sponsoring Party: Empire District
Case No. ER-2004-0570

Before the Public Service Commission
Of the State of Missouri

Surrebuttal Testimony

Of

Gregory A. Knapp

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SURREBUTTAL TESTIMONY
OF
GREGORY A. KNAPP
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2004-0570

Q. Please state your name, position and business address.

A. Gregory A. Knapp. I am Vice President – Finance and Chief Financial Officer of The Empire District Electric Company ("Empire" or "Company"). My business address is 602 Joplin Street, Joplin, Missouri.

Q. Are you the same Gregory A. Knapp who caused to be filed rebuttal testimony in this proceeding before the Missouri Public Service Commission ("Commission")?

A. Yes.

Q. Please state the purpose of your surrebuttal testimony?

A. The purpose of this testimony is to respond, generally, to the rebuttal testimony submitted by the other parties on the issue involving pension expense and net cost of removal.

Q. Please explain the Company's position on pension expense.

A. The Company agrees with Dr. Vogl's FAS 87 methodology. However, if the Commission decides not to adopt this method, at a minimum the following language should be adopted which will support the Company's efforts to remain financially sound. The following language allows consistency between financial reporting and the pension expense collected in rates.

The Parties agree that, effective _____, the rates established in this case for The Empire District Electric Co. pension plan are $3 million which represents the continued amortization of the Prepaid Pension Asset as ordered in Case No. ER-2002-424.

The Company shall also be authorized to record as a regulatory asset/liability, as appropriate, the difference between the $3 million used in setting rates and the level of FAS 87 pension expense determined for book purposes.

In the subsequent rate case, this regulatory asset/liability will be amortized over 5 years into rates and will be funded, following such amortization, to the pension trust by the Company to the extent that it has not already been funded.

The FAS 87 pension expense used for book purposes will be determined using the following methodology: (a) Market Related Value of assets, with smoothing of gains/losses implemented prospectively over a five-year period, and (b) Amortization of unrecognized gains or losses, only to the extent that they fall outside of the 10% corridor described in FAS 87, over the average future service of active plan participants.

Q. Do you agree with Staff Witness Gibbs' rebuttal testimony that Empire can simply ignore FAS 87, which governs pension accounting, by invoking FAS 71 which speaks to the accounting for certain types of regulation?

A. No, I do not. The Company is required to follow accounting principles generally accepted in the United States of America (GAAP) for financial reporting. Financial reports prepared following GAAP include reports read by stockholders, bondholders, and prospective investors in the Company. FAS 87, which is GAAP, specifies the accounting and reporting requirements the Company must follow for its pension costs. FAS 71, which is also GAAP, is

unrelated and provides for the establishment of regulatory assets and liabilities if certain conditions are met. FAS 71, paragraph 9, allows the deferral of costs as long as it is probable, as defined in FAS 5, that those costs will be recovered in future rates. The company is not allowed to pick and choose which FAS to follow for pensions. FAS 87 must be followed.

Q. What is the Company's position on the issue of Cost of Removal?

A. Empire supports the position set out by Company witness Roff on the treatment of net cost of removal. However, if the Commission does not accept this approach, at a minimum the following language should be adopted.

> Empire's rates include a provision for jurisdictional net cost of removal of $1,600,000 annually. Empire shall book for its electric operations, actual levels of annual cost of removal as an expense up to the amount listed above. Company is authorized to record the difference between the rate case provision of $1,600,000 and the actual levels of annual net cost of removal as a regulatory asset and/or liability. This regulatory asset and/or liability is intended to track the difference between the provision for net cost of removal provision included in rates in this case and the Company's actual levels of annual net cost of removal after the effective date of rates established in this case. This regulatory asset and/or liability will be included in rate base in the Company's next rate case and amortized over a five (5) year period. The Company is authorized to make such additional entries as are appropriate under FAS71 for this item. This methodology will be reviewed in Empire's next rate case in which its retail electric distribution rates are under review to determine whether the methodology will be continued.

This language is consistent with the language which was adopted in Case No. GR-2004-0209 involving Missouri Gas Energy.

Q. Do you have any final remarks?

A. Yes. As the Company continues its tradition of reliable service to its customers, it will need to continue to grow its infrastructure and meet upcoming baseload needs. With that in mind, it is imperative that Empire go into this growth in sound financial condition. The decisions of this Commission have a direct impact on the Company's financial health. Including in rates pension expense and full net cost of removal is a move in the right direction to establish and maintain the sound financial health of the Company.

Q. Does this conclude your testimony?

A. Yes.

AFFIDAVIT

STATE OF MISSOURI)
) ss
COUNTY OF JASPER)

On the 22nd day of November, 2004, before me appeared Gregory A. Knapp, to me personally known, who, being by me first duly sworn, states that he is the Vice President – Finance and Chief Financial 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.

Gregory A. Knapp

Subscribed and sworn to before me this 22nd day of November, 2004

Patricia A Settle
Pat Settle, Notary Public

My commission expires:

Patricia A. Settle
Notary Public - Notary Seal
State of Missouri
County of Jasper
Expires February 09, 2006