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| *Exhibit No.:* | |
| *Issue:* | *Off-System Sales* |
| *Witness:* | *Janis E. Fischer* |
| *Sponsoring Party:* | *MoPSC Staff* |
| *Type of Exhibit:* | *Rebuttal Testimony* |
| *Case No.:* | *ER-2006-0315* |
| *Date Testimony Prepared:* | *July 28, 2006* |

**MISSOURI PUBLIC SERVICE COMMISSION**

**UTILITY SERVICES DIVISION**

# REBUTTAL TESTIMONY

# OF

# JANIS E. FISCHER

**THE EMPIRE DISTRICT ELECTRIC COMPANY**

**CASE NO. ER-2006-0315**

*Jefferson City, Missouri*
*July 2006*

** **Denotes Highly Confidential Information** **

**NP**

**BEFORE THE PUBLIC SERVICE COMMISSION**

**OF THE STATE OF MISSOURI**

| | | |
|---|---|---|
| In the matter of The Empire District Company of Joplin, Missouri for authority to file tariffs increasing rates for electric service provided to customers in Missouri service area of the Company. | ) ) ) ) | Case No. ER-2006-0315 |

AFFIDAVIT OF JANIS E. FISCHER

STATE OF MISSOURI ) <br> ) ss. <br> COUNTY OF COLE )

Janis E. Fischer, of lawful age, on her oath states: that she has participated in the preparation of the foregoing Rebuttal Testimony in question and answer form, consisting of 7 pages to be presented in the above case; that the answers in the foregoing Rebuttal Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.

Janis E. Fischer

Janis E. Fischer

Subscribed and sworn to before me this 27th day of July 2006.

Toni M. Charlton

TONI M. CHARLTON
Notary Public - State of Missouri
My Commission Expires December 28, 2008
Cole County
Commission #04474301

TONI M. CHARLTON
NOTARY SEAL
NOTARY PUBLIC
STATE OF MISSOURI

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**REBUTTAL TESTIMONY**

**OF**

**JANIS E. FISCHER**

**THE EMPIRE DISTRICT ELECTRIC COMPANY**

**CASE NO. ER-2006-0315**

Q. Please state your name and business address.

A. Janis E. Fischer, Governor Office Building, P. O. Box 360, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am a Regulatory Auditor with the Missouri Public Service Commission (Commission or PSC).

Q. Are you the same Janis E. Fischer who has previously filed direct testimony in Case No. ER-2006-0315?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of this rebuttal testimony is to respond to the direct testimony of The Empire District Electric Company (Empire or Company) witness Todd W. Tarter and Office of Public Counsel (OPC) witness Ralph C. Smith with regard to their off-system sales positions.

**<u>EXECUTIVE SUMMARY</u>**

Q. Please summarize your rebuttal testimony.

A. My rebuttal testimony provides the Staff's arguments in opposition to Empire and OPC's off-systems sales margin adjustments. Empire uses a five-year average of off-system sales to normalize off-system sales margins, after certain

American Electric Power (AEP) transactions are eliminated from the average. OPC's adjustment is also based on a five-year normalization of off-system sales margins, without adjustment for the AEP transactions. In contrast, the Staff's methodology is to use the off-system sales margin for the 12 months ending March 31, 2006, in this case.

**<u>OFF-SYSTEM SALES POSITIONS</u>**

Q. What is the Staff's position regarding off-system sales in this proceeding?

A. The Staff reviewed seven years of off-system sales data and determined that the twelve months ending March 31, 2006, level of off-system sales was representative of a reasonable level of off-system sales on an ongoing basis. March 31, 2006, is the end of the Commission-ordered test year update period in this case.

Q. What is Empire's position in this case regarding off-system sales?

A. Empire has made an adjustment (Empire Revenue Adjustment 15, W/P C1) to "normalize" off-system margin to an "adjusted" five-year average. Empire analyzed off-system sales costs, revenues and margins for the twelve months ending September 30 for the years 2001 through 2005. As part of Empire's analysis of off-system sales, the costs, revenues and margins associated with transactions with AEP were eliminated from the off-system sales totals for 2002 and 2003 because Empire classified these transactions as abnormal. These AEP transactions occurred from December 2001 through June 2003. The total AEP margins from December 2001 through June 2003 amounted to $6.3 million, and their elimination from Empire's analysis resulted in a $1.27 million reduction in the five-year average off-system sales margin.

Q. What is OPC's position in this case regarding off-system sales?

A. OPC witness Smith also normalizes Empire off-system sales by calculating a five-year average, but he did not remove the effect of the AEP transactions that were removed by Empire in determining their average. Mr. Smith calculates his adjustment by comparing it to the Empire off-system sales adjustment included in their initial filing.

Q. What is the Staff's view of Empire's approach to normalizing off-system sales?

A. The Staff asked Empire in Staff Data Request No. 230, to list all the reasons why the elimination of the AEP transactions from off-system sales was appropriate in its five-year analysis to normalize off-system sales margins. Empire's response to Staff Data Request No. 230 states:

> This was a single purchase transaction that took place from 12/1/01 to 6/30/03 generating approximately $6.4 million in gross profit within just a short timeframe. From 2001 to 2003 Empire's total off-system sales activity only generated gross profits of $8.9 million. The single non-asset backed purchased [sic] produced over 71 percent of the gross profit on off-system sales. Empire has not seen this type of transaction occur again.

The Staff does not consider the AEP transactions to be abnormal events. These transactions were of a large dollar magnitude, yet to remove these transactions from the calculation of the off-system sales margin percentage for the twelve months ending September 2002 and 2003 creates an unreasonable result. (See Fischer Highly Confidential Schedule 1) For example, the off-system sales margin percentages of margin to revenue for 2002 and 2003 without inclusion of the AEP transactions drop to ** ______ ** and ** ______ ** respectively. Of the eighty-seven months included in the Staff's analysis of off-system sales, these off-system sales margin percentages were exceeded in all but three months. This would indicate that the exclusion of the AEP transactions would result in off-system sales margin levels below what is normally experienced by Empire.

With the AEP transactions included, the off-system sales margin percentages for 2002 and 2003 are ** _______ ** and ** _______ ** respectively. These off-system sales margin percentages were at the mid-point of the eighty-seven months included in the Staff's analysis of off-system sales margins. This would indicate that the inclusion of the AEP transactions results in more typical off-system sales margin percentages. Eliminating the impact of the AEP transactions from Empire's multi-year average calculation of off-system sales serves only to artificially deflate the resulting off-systems sales margin number.

Q. What led the Staff to conclude that the update period (twelve months ending March 31, 2006) level of Empire's off-system sales margin was more appropriate to use than a multi-year average as an ongoing level of off-system sales margin?

A. The Staff reviewed monthly Empire off-system sales data going back to January 1999 and found that there is considerable fluctuation over time in the sales, costs and margins associated with off-system sales. While consideration of a multiple year average approach is appropriate for off-system sales, in this particular case the update period level of off-system sales margin appears to be the most reasonable ongoing amount for inclusion in the cost-of-service. The Staff has compiled the off-system sales revenues, costs and margins over the eighty-seven month analysis on charts attached as Fischer Highly Confidential Schedule 2. The charts visually demonstrate the Staff's position.

Q. Are there any other reasons that the Staff chose to include the update period level of off-system sales in the cost-of-service?

A. Yes. The Staff's RealTime® production cost model included for this case purchase power and fuel costs replicating current costs (test year and update period and 2006 natural gas hedges). The use of the update period level of off-system sales provides a better matching of off-system sales with all other generation related costs included in the Staff's revenue requirement.

Q. What has been the impact of recent increased fuel and purchase power costs on Empire's off-system sales?

A. Empire has been able to increase its off-system sales margin dollars per MWH for each MWH sold for the last half of the test year and through the update period ending March 2006. This is in comparison to the years 1999 through 2004 in which the margin dollars per MWH, stayed at a fairly consistent level except for occasional spikes in the margin dollars per MWH that lasted for a single month**.** This demonstrates that recent increases in fuel and purchased power costs have positively impacted Empire's off-system sales.

Q. What does the off-system sales margin dollars per MWH represent?

A. The off-system sales margin dollars per MWH represents the difference between the average cost and sale price per MWH of off-system sales by month. When you multiply the off-system sales KWHs by the margin dollars per MWH the product is the profit that Empire realizes from off-system sales for the month.

Q. What other indications have led the Staff to believe that Empire's current off-system sales levels will continue?

A. Empire has noted that recent coal supply constraints have increased off-system sales in its March 31, 2006, Quarterly Report (10-Q) to the United States Securities and Exchange Commission (SEC):

> Revenues were higher during the twelve months ended March 31, 2006 as compared to 2005 primarily due to increased sales of our gas-fired generation in the third and forth quarters of 2005 due to a shortage of available coal-fired generation on the open market. Companies that normally would have coal-fired energy to sell in the market were not doing so due to the coal shortages, pushing demand onto the gas-fired units. **[Page 26]**

Empire had previously stated in its March 2006 filing of its 2005 Annual Report (10-K) to the SEC on page 22, "We expect that the railroads' congestion problems and resulting delivery delays will continue for an indefinite period."

This information also supports the Staff's position that the twelve month ending March 31, 2006, off-system sales margin is appropriate for inclusion in the cost-of-service in this case.

Q. What other factors led the Staff to conclude that the updated test year level of off-system sales margin was appropriate for an ongoing basis and inclusion in the Staff's cost-of-service in this case?

A. The analysis of 1999 through March 2006 monthly data when charted clearly shows a more consistent relationship among off-system sales revenues, costs and margins in the short term (January 2005 through March 2006) than in the long term (1999 through March 2006). (See Fischer Highly Confidential Schedule 2.)

Q. What is the Staff's position on the OPC proposed multi-year average methodology used to determine its adjustment to Empire's off-system sales?

A. The Staff, while preferring the use of update period off-system sales in determining the cost-of-service in this case, would prefer OPC's methodology in determining a five-year average to Empire's approach. OPC does not remove the AEP transactions from its five-year analysis, and its resulting adjustment is therefore more representative of the actual off-system sales activity at Empire. OPC did not, however, include the off-system sales that occurred from October 2005 through March 2006 in its five-year analysis. The Staff prefers that any multiple year average analysis include the update period ending March 31, 2006, rather than the September 30, 2005, ending period to reflect more current conditions.

Q. Does that conclude your testimony?

A. Yes, it does.

Schedule 1 has been deemed Highly Confidential in its entirety.

Schedule 2 has been deemed Highly Confidential in its entirety.