EXHIBIT

Exhibit No.: ______

Issue(s):	Natural Gas
Witness/Type of Exhibit:	Busch/Surrebuttal
Sponsoring Party:	Public Counsel
Case No.:	ER-2004-0570

SURREBUTTAL TESTIMONY

FILED

DEC 2 8 2004

Missouri Public Service Commission

OF

JAMES A. BUSCH

Submitted on Behalf of the Office of the Public Counsel

THE EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2004-0570

November 24, 2004

Exhibit No. 87
Case No(s). ER-2004-0570
Date 12-06-04 Rptr KF

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the tariff filing of The Empire District Electric Company to implement a general rate increase for retail electric service provided to customers in its Missouri service area.	))))	Case No. ER-2004-0570

AFFIDAVIT OF JAMES A. BUSCH

STATE OF MISSOURI	)	
	)	ss
COUNTY OF COLE	)	

James A. Busch, of lawful age and being first duly sworn, deposes and states:

1. My name is James A. Busch. I am the Public Utility Economist for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony consisting of pages 1 through 6.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

J Busch

James A. Busch

Subscribed and sworn to me this 24th day of November 2004.

KATHLEEN HARRISON
Notary Public - State of Missouri
County of Cole
My Commission Expires Jan. 31, 2006

Kathleen Harrison

Kathleen Harrison, Notary Public

My commission expires January 31, 2006.

SURREBUTTAL TESTIMONY

OF

JAMES A. BUSCH

CASE NO. ER-2004-0570

EMPIRE DISTRICT ELECTRIC COMPANY

Q. Please state your name and business address.

A. My name is James A. Busch and my business address is P. O. Box 2230, Jefferson City, MO 65102.

Q. Are you the same James A. Busch that filed direct and rebuttal testimony in this proceeding?

A. Yes I am.

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to respond to the rebuttal testimony of Empire District Electric Company (Empire or Company) witness Mr. Brad Beecher.

Q. On page 12, lines 14 – 19 of his rebuttal testimony, Mr. Beecher points out a problem with a formula you used in your direct testimony concerning your natural gas price recommendation. Have you made this correction?

A. Yes. I made this correction in my rebuttal testimony.

Q. On page 13, lines 8 – 9 of his rebuttal testimony, Mr. Beecher states that he expects you to make an upward adjustment to your natural gas price recommendation for Empire, based on the "significant" upward price movement in natural gas since the filing of direct testimony in this proceeding. Would it be appropriate to increase your natural gas price recommendation for Empire at this time?

A. No. There are several reasons why it would not be appropriate to increase my natural gas price recommendation at this time.

1) Since October 27, 2004, the date utilized by Mr. Beecher in his rebuttal testimony, the futures price for natural gas has fallen dramatically. Based on the settlement price on the close of business on November 22, 2004, the 12-month NYMEX futures strip (December 2004 – November 2005) had fallen to $6.9034 per MMBtu. The 24-month NYMEX futures strip (December 2004 – November 2006) had fallen to approximately $6.76 per MMBtu. This is significantly lower than the $8.04 per MMBtu for the 12-month strip for 2005 and the $7.50 per MMBtu for the 24-month strip (January 2005 – December 2006) utilized by Mr. Beecher in his rebuttal testimony.

2) The physical price of natural gas, the actual price of natural gas paid for actual supplies of natural gas, is selling at a large discount compared to the futures market. On November 22, 2004, the price for December futures on the NYMEX closed at $6.762 per MMBtu. On the same date, spot prices for next day delivery (i.e. actual market prices for physical delivery) at the Henry Hub (this is the same point where futures prices are based) were $5.26 per MMBtu. This is a difference of $1.50 per MMBtu. This indicates to me that there are other forces (i.e.

speculators) that are artificially keeping natural gas futures prices above the level at which it is fundamentally supported.

3) I do not believe that the market can continue to bear prices in the $6 - $9 per MMBtu range. Consumers have chosen natural gas because it was a low price alternative. If prices remain at these inflated levels for prolonged periods of time, consumers will begin to curtail their usage of natural gas. This has been witnessed in the industrial sector with significant demand destruction over the past few years due to high natural gas prices.

4) Current market conditions are trending toward a continued drop in natural gas prices. First, storage reached record levels entering the winter withdrawal season (November – March) and has remained there early into the season. Second, the latest NOAA (National Oceanic and Atmospheric Administration) winter weather outlook has indicated that the temperatures overall may not be as cold as originally thought. (http://www.noaanews.noaa.gov/stories2004/s2342.htm) These two factors plus the huge difference between actual natural gas prices and futures natural gas prices, leads me to believe that prices for natural gas could fall throughout the winter.

5) I believe that the increase in natural gas prices between the filing dates of direct and rebuttal testimony was driven primarily by Hurricane Ivan, which

swept through the Gulf of Mexico. Approximately 25% of the United States' natural gas supplies come from the Gulf of Mexico. In September, Hurricane Ivan ripped through the Gulf causing severe damage to the natural gas infrastructure. This damage resulted in a major reduction in natural gas supplies. This fact coupled with the fear of a colder-than-normal winter led the futures market to skyrocket. However, since storage was able to reach record levels and the winter forecast has moderated slightly, the natural gas price has fallen.

6) Finally, Empire's hedging program has allowed Empire to hedge a significant portion of its anticipated natural gas needs for the next two years. This price is actually near my price recommendation from my direct testimony, as corrected in my rebuttal testimony. In fact, the current actual natural gas prices are near my price recommendation. Thus prices only have to moderate slightly for Empire to start seeing benefits from a built-in base rate of $4.68 per MMBtu.

Q. On page 11, line 1 of his rebuttal testimony, Mr. Beecher indicates that his overall natural gas price is $6.02 per MMBtu. Do you agree with his methodology and result?

A. No, I do not. First, his calculations rely solely on the futures price of natural gas as of October 27, 2004 to estimate the price that Empire expects to pay in the future for its currently unhedged natural gas needs. This heavy reliance on the futures market, in my opinion, distorts the price Empire could reasonable be expected to pay for natural gas due to short term market conditions and recent events. As discussed previously, Hurricane Ivan had a tremendous impact on the natural gas market and contributed to higher price increases. However, the hurricane's impact should be resolved before next year's injection period (April – October) begins, if not sooner. Thus, a short-term event has caused the futures price to rise, even though the event will have no bearing on future natural gas market fundamentals.

Second, Mr. Beecher calculates his price assuming a burn of 10,000,000 MMBtu, which I believe inflates Empire's expected burn. Over the past three years, Empire has only burned 7,215,789 MMBtu on average. If Mr. Beecher uses a more reasonable level of expected burn, such as 8,833,333, which is closer to what Empire has reported in its gas position report, I believe his price would be $5.82 per MMBtu, based on his overly high natural gas prices. But as I have shown in this testimony, prices have fallen substantially since Mr. Beecher's rebuttal was prepared.

Furthermore, in Mr. Beecher's rebuttal testimony, page 5, lines 12 – 15, page 6, lines 1 – 3, he indicates that various sources are calling for natural gas prices in the $5.94 - $6.60 per MMBtu range. These prices are substantially lower than the $7.50 per MMBtu price used by Mr. Beecher.

Q. Why do you oppose using Mr. Beecher's estimated burn of 10,000,000 MMBtus of natural gas?

A. As Mr. Beecher points out on page 4, lines 4 – 7 of his rebuttal testimony, factors, such as the price of natural gas will affect the actual amount of natural gas burned by Empire. At the inflated prices used by Mr. Beecher, I believe that Empire will not burn that high a level of natural gas.

Q. Mr. Beecher, on page 12, lines 11 – 13 of his rebuttal testimony, criticizes your use of historical prices in your analysis, calling your reliance on historical prices potentially disastrous for the Company. Please respond.

A. The historical prices that I utilized in my analysis are in line with current market conditions and expectations. The prices range from a low of $3.686 in October 2002 to a high of $9.133 in March 2003. The average for the 24-month period is $5.37 or 12 cents higher than the actual price of natural gas at the Henry Hub on November 22, 2004. Thus, my use of historical prices is a reasonable methodology to mitigate short-term fluctuations in the futures market in trying to estimate the price for natural gas in the future. In fact, it is the sole reliance on the futures market as an estimate of Empire's spot purchase prices (as done by Mr. Beecher in his rebuttal testimony) that could have disastrous results, for Empire's customers.

Whereas Mr. Beecher relies solely on futures prices in his analysis, my recommendation utilizes both futures prices and historical prices. The use of historical prices helps to offset the potential short-term impacts that can cause the futures market to spike, similar to what happened this past fall.

Q. Does this conclude your surrebuttal testimony?

A. Yes it does.