Exhibit No.:	
Issues:	FAS 87 and FAS 106 cost of Pension and OPEB Plans
Witness:	DONALD D. SCHISLER, JR.
Type of Exhibit:	DIRECT Testimony
Sponsoring Party:	Empire Dist. Electric Company
Case No.:	GO-2006-0205
Date Testimony Prepared:	November 2005

DIRECT TESTIMONY

OF

DONALD D. SCHISLER, JR.

ON

BEHALF OF

THE EMPIRE DISTRICT ELECTRIC COMPANY

Joplin, Missouri
November 2005

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ON BEHALF OF
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BEFORE THE
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INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Donald D. Schisler, Jr. My business address is 101 South Hanley, Suite 900, St. Louis, Missouri 63105.

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

A. I am a Consultant with Towers Perrin. I serve as an actuary and employee benefits consultant to a number of clients in the firm's St. Louis office.

Q. PLEASE DESCRIBE TOWERS PERRIN.

A. Towers Perrin is an international management and actuarial consulting firm with offices in 79 locations throughout the world. We serve approximately 7,000 clients worldwide in virtually every industry as well as in the government, education, and not-for-profit sectors.

Q. PLEASE DESCRIBE YOUR EDUCATION.

A. I received a Bachelor of Science degree in actuarial science from Maryville University, St. Louis in 1979. I completed the examination requirements for designation as an Associate of the Society of Actuaries and received such designation in November 1988. I completed both the examination and experience requirements for designation as an Enrolled Actuary under the Employee Retirement Income Security Act of 1974 (ERISA) and received such designation in 1985. I have been a Member of the American Academy of Actuaries since 1987.

Q. PLEASE DESCRIBE YOUR QUALIFICATIONS.

A. I have been employed with Towers Perrin as a consulting actuary since 1985; I was employed by General American Life Insurance Company in St. Louis from 1979 to 1985. I have substantial technical and consulting experience relative to employee benefit plans including the design, funding, accounting, and communication of pension and postretirement welfare programs.

PURPOSE

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to provide details regarding the regulatory accounting requests made by The Empire District Electric Company ("Empire") relative to the pension and other post-employment benefits ("OPEB") costs due to the acquisition of the Missouri gas assets of Aquila ("The Business"). Empire's proposal has three primary components:

a. Regulatory accounting treatment for certain prepaid pension costs of the Business that is consistent with the regulatory accounting treatment given those costs when Aquila owned the property immediately prior to Empire's acquisition.

b. Regulatory accounting treatment for the pension benefit costs of the Business based on Empire's actuarial assumptions and the regulatory accounting methodology authorized per the Stipulation and Agreement in Case No. ER-2004-0570, calculated without regard to the purchase accounting adjustments required under U.S. GAAP.

c. Regulatory accounting treatment for the OPEB benefits of the Business calculated without regard to the purchase accounting adjustments required under U.S. GAAP.

Q. IS EMPIRE REQUESTING AN INCREASE IN THE AMOUNT OF PENSION OR OPEB COSTS INCLUDED IN THE RATES CURRENTLY BEING PAID BY MISSOURI GAS CUSTOMERS?

A. No. The rates charged to the customers will remain unchanged. This request deals with the methodology that will be used to determine pension and OPEB costs, including the treatment of unrecognized amounts and prepaid pension cost. The pension proposal also establishes a "tracker" to account for increases or decreases in the level of pension costs actually incurred versus the level of pension costs included in current rates. The cumulative differences will be considered in the next gas rate case.

OPEB COSTS

Q. PLEASE EXPLAIN YOUR REQUEST REGARDING THE OPEB COSTS OF THE BUSINESS.

A. Under Missouri regulation and to the extent funded, OPEB costs are included in the cost of service based on the cost recognized under FAS 106. A portion of the FAS 106 cost recorded is related to the amortization of amounts not fully recognized in prior years, such as actuarial gains or losses. In an acquisition, the purchase accounting treatment (required by U.S. GAAP) dictates that any previously unrecognized amounts (either gains or losses), as well as any differences due to changes in the economic environment or actuarial assumptions, be recognized as part of the cost of an acquisition. Under Empire's regulatory accounting request, FAS 106 costs for rate purposes will be determined without regard to purchase accounting. This is illustrated on Schedule 1 attached to my testimony.

Q. WHY SHOULD FUTURE FAS 106 COSTS BE DETERMINED WITHOUT REGARD TO PURCHASE ACCOUNTING?

A. The GAAP purchase accounting treatment would result in these previously unrecognized amounts being excluded from future FAS 106 cost calculations and, therefore, excluded from the cost of service in the future. Since the amortization of these types of costs have been reflected in the FAS 106 costs by the prior owner, Aquila, Empire is proposing that the amortization of unrecognized amounts continue to be included in the FAS 106 cost in the future. By continuing to calculate the FAS 106 cost excluding the impact of purchase accounting, the regulatory treatment associated with these unrecognized amounts remains consistent with that used by the prior owner, Aquila.

Q. ARE YOU REQUESTING ANY OTHER REGULATORY APPROVALS RELATED TO THE REGULATORY ACCOUNTING TREATMENT FOR THE OPEB COST OF THE MISSOURI GAS EMPLOYEES?

A. No.

<u>PENSION COST</u>

Q. HOW ARE THE PENSION BENEFIT COSTS OF THE BUSINESS CURRENTLY CALCULATED?

A. It is our understanding from the information given to us by Aquila that the pension benefit costs of the Business are currently calculated based upon a 5-year average of the ERISA minimum required contribution, plus amortization of a prepaid pension asset. From the information given to us by Aquila, these two items equal approximately $225,000 in annual pension expense and $600,000 in pension amortization costs.

Q. WHAT IS THE PREPAID PENSION ASSET THAT IS BEING AMORTIZED AQUILA?

A. Based upon our discussions with Aquila, it is our understanding that the prepaid pension asset is related to certain prepaid pension costs that were recognized as "pension income" in years before the pension cost calculation of the Business was changed to the ERISA minimum contribution basis.

Q. IS EMPIRE REQUESTING A CHANGE IN THE TREATMENT OF THE PREPAID PENSION ASSET OF THE BUSINESS?

A. No. Prior to the acquisition by Empire, the cost of the pension benefits of the Business included the amortization of this prepaid pension asset. Empire proposes that it be allowed to continue this amortization on the same basis as Aquila.

Q. WHY IS EMPIRE REQUESTING A CHANGE IN THE METHODOLOGY USED TO DETERMINE PENSION COST, FROM ERISA MINIMUM TO FAS 87?

A. It is essentially a consistency issue. Earlier this year, Empire received approval from the Missouri Public Service Commission to determine its pension benefit cost (including FAS 87) using a methodology that is described in a Stipulation and Agreement entered into in Case No. ER-2004-0570. Empire proposes to use a methodology consistent with this agreement to determine the pension cost of the Business.

Q. PLEASE DESCRIBE THIS METHODOLOGY.

A. Generally, pension costs will be based on the cost calculated per FAS 87. The mechanism authorized by the Commission in the last Empire District Electric rate case also included a feature that tracks any differences between Empire's actual pension cost and the pension cost currently reflected in rates. The cumulative cost differences are recorded as regulatory assets or liabilities and will be amortized over 5 years beginning at the time of the next rate case. This tracking feature ensures that pension costs lower than those reflected in current rates will be reflected in the rates paid in the future, and pension costs greater than those reflected in current rates will be reflected in future rates. In this case the tracker would be calculated using the $825,000 in pension costs currently being incurred by Aquila on the gas operations.

Q. PLEASE DESCRIBE SCHEDULE 2 TO YOUR TESTIMONY.

A. Schedule 2 is an excerpt (Appendix A) related to pension accounting from the Stipulation and Agreement reached in Case No. ER-2004-0570. It displays in detail all of the pension regulatory accounting procedures agreed to in Case No. ER-2004-0570.

Q. HOW WILL THIS SWITCH TO EMPIRE'S APPROVED PENSION ACCOUNTING METHODOLOGY AFFECT THE TREATMENT OF THE PREPAID PENSION ASSET CURRENTLY BEING AMORTIZED AND REIMBURSED IN RATES?

A. Under Empire's proposal the prepaid pension asset will be treated in the same manner as the prepaid pension asset that existed at the time of the Stipulation and Agreement in Case No. ER-2004-0570. Generally, this means that once the amount of the prepaid pension asset has been amortized, Empire will fund all amounts recovered in rates for pension costs directly into the pension trust. This Empire regulatory treatment is more fully described in Schedule 2 attached to my testimony.

Q. HOW WILL EMPIRE'S PROPOSED PENSION COST "TRACKER" OPERATE SINCE THE PENSION COST OF THE BUSINESS FOR REGULATORY ACCOUNTING PURPOSES IS NOT CURRENTLY BASED ON FAS 87 COST?

A. The differences between the FAS 87 cost under Empire's approved methodology and assumptions and the amount currently reflected in rates will be accumulated as a regulatory asset or liability. This regulatory asset or liability will be amortized over 5 years at the time of the next rate case. The operation of the authorized Empire tracker is described in item 6 of Schedule 2.

PURCHASE ACCOUNTING

Q. WHAT PURCHASE ACCOUNTING ADJUSTMENTS ARE REQUIRED UNDER U.S. GAAP RELATIVE TO THE PENSION PLAN?

A. U.S. GAAP requires that purchase accounting be followed for the pension plan following an acquisition, just as it is required for the OPEB plan. This means that any previously unrecognized amounts (such as actuarial gains or losses), as well as differences due to changes in the economic environment or actuarial assumptions, must be recognized as part of the cost of the acquisition. Empire is proposing that for regulatory accounting purposes future FAS 87 costs be determined without regard to purchase accounting. By calculating FAS 87 cost without regard to purchase accounting, the regulatory accounting treatment of these unrecognized amounts will be consistent with the amount of the prepaid pension asset currently being amortized.

Q. PLEASE EXPLAIN YOUR LAST COMMENT CONCERNING CONSISTENCY WITH THE AMOUNT OF THE PREPAID PENSION ASSET.

A. I will explain by referencing the illustration shown as "Pension Funded Status" in Schedule 1 attached to my testimony.

1. Under FAS 87, the difference between the projected benefit obligation and the fair value of plan assets is called the plan's "funded status".
2. The amounts shown as "Unrecognized Prior Service Cost", "Unrecognized Transition Obligation" and "Unrecognized (Gains) Losses" in Schedule 1 comprise what I have previously referred to as the "unrecognized amounts".
3. The sum of the funded status plus these unrecognized amounts is equal to the plan's accrued or prepaid pension cost under FAS 87.

In order for the plan's accrued or prepaid pension cost under FAS 87 to be consistent with the prepaid pension cost currently being amortized (i.e., the "prepaid pension asset"), the unrecognized amounts must be included in the regulatory accounting.

Q. IS THERE ANYTHING ELSE THAT NEEDS TO BE CLARIFIED CONCERNING THE EMPIRE PENSION AND OPEB ACCOUNTING PROPOSALS?

A. Yes. The pension and OPEB costs recorded on the books of the Business must be kept separate from the pension and OPEB costs calculated for other Empire employees. That is, the FAS 87 and FAS 106 costs associated with the gas employees must be calculated independently from Empire's FAS 87 and FAS 106 costs for other employees. To accomplish this, the FAS 87 and FAS 106 assets and liabilities of the Business will be tracked separately, and the FAS 87 and FAS 106 costs of the Business will be accounted for independently.

Q. **DOES THIS CONCLUDE YOUR TESTIMONY?**

A. Yes it does.

Schedule 1

EMPIRE DISTRICT ELECTRIC COMPANY

Illustration of Regulatory Treatment of Unrecognized Amounts

(All Amounts in $Millions)

The following amounts are illustrative only. Actual amounts will be determined at closing date.

OPEB Funded Status	Amounts prior to Acquisition	Requested Regulatory Treatment
APBO (Accumulated Projected Benefit Obligation)	(2.500)	
Fair Value of Plan Assets (VEBA)	0.500	
Funded Status	(2.000)	
Unrecognized Prior Service Cost	0.800	Consistent with Aquila
Unrecognized Transition Obligation	1.000	Consistent with Aquila
Unrecognized (Gains) Losses	0.200	Consistent with Aquila
(Accrued) / Prepaid Postretirement Benefit Cost	0.000	

Pension Funded Status		
PBO (Projected Benefit Obligation)	(16.000)	
Fair Value of Plan Assets	12.000	
Funded Status	(4.000)	
Unrecognized Prior Service Cost	2.000	Consistent with ER-2004-0570
Unrecognized Transition Obligation	0.500	Consistent with ER-2004-0570
Unrecognized (Gains) Losses	5.500	Consistent with ER-2004-0570
(Accrued) / Prepaid Pension Cost [1]	4.000	Consistent with Aquila's prepaid pension asset.[1]

[1] The Plan's prepaid pension cost must equal the amount of the prepaid pension asset currently being amortized.

Schedule 2

EMPIRE DISTRICT ELECTRIC COMPANY

Appendix A-Stipulation and Agreement

Case No. ER-2004-570

The intent of this settlement is to:

A. ensure that the Company recovers the amount of the "prior prepaid pension asset" per the Stipulation and Agreement from the Company's last rate case, Case No. ER-2002-424, and to include this "prior prepaid pension asset" in rate base; and

B. ensure that the amount collected in rates is based on the FAS 87 cost recognized by the Company for financial reporting purposes, using the methodology described below in item 2; and

C. ensure that, once the amount in A has been collected in rates by the Company, all pension cost collected in rates is contributed to the pension trust; and

D. ensure that all amounts contributed by the Company to the pension trust per items 3 and 5 below are recoverable in rates; and

E. ensure that the Company will receive no more or less than the amount in A before the Company is required to fund the plan.

To accomplish these goals, the following items are agreed upon as part of this settlement:

1. The Company's FAS 87 cost will be recognized in rates and for financial reporting purposes.

2. FAS 87 cost will be calculated based on the following methodology:

   a. Market Related Value for asset determination, smoothing all asset gains and losses that occur on and after January 1, 2004.

   b. No 10% Corridor

   c. Amortization period of 10 years for unrecognized gains and losses. (With a 5 year MRV amortization - all gains/losses are reflected in 15 years.)

3. Any FAS 87 amount (as calculated above) which exceeds the Minimum ERISA contribution will reduce the prior prepaid asset currently recognized in rate base. When the prior prepaid pension asset currently recognized in rate base is reduced to zero, any amount of FAS 87 (as calculated above) which exceeds the minimum ERISA level must be funded.

4. In the case that FAS 87 expense becomes negative, the Company is ordered to set up a regulatory liability to offset the negative expense. In future years, when FAS 87 expense becomes positive again, rates will remain zero until the prepaid pension asset that was created by negative expense is reduced to zero. The regulatory liability will be reduced at the same rate as the prepaid pension asset. This regulatory liability is a non-cash item and should be excluded from rate base in future years.

5. The Company will be allowed rate recovery for contributions made to the pension trust in excess of the FAS 87 expense for the following reasons: the minimum required contribution is greater than the FAS 87 expense level, avoidance of PBGC variable premiums, and avoidance of write-off of an existing prepaid pension asset (i.e. charge to other comprehensive income).

6. A regulatory asset or liability will be established on the Company's books to track the difference between the level of FAS 87 expense during the rate period and the level of pension expense built into rates for that period. If the FAS 87 expense during the period is more than the expense built into rates for the period, the Company will establish a regulatory asset. If the FAS 87 expense during the period is less than the expense built into rates for the period, the Company will establish a regulatory liability. If the FAS 87 expense becomes negative, a regulatory liability equal to the difference between the level of pension expense built into rates for that period and $0 will be established. Since this is a cash item, the regulatory asset or liability will be included in rate base and amortized over 5 years at the next rate case.

7. Any future prepaid pension asset occurring after the cutoff date for the prior, agreed upon, fixed Prepaid Asset to be amortized will not be included in Rate Base in any future rate case. The regulatory assets/liabilities identified in this settlement will address all Rate Base amounts.

AFFIDAVIT

STATE OF MISSOURI)
) ss
COUNTY OF ST. LOUIS)

On the 8 day of November, 2005, before me appeared Donald D. Schisler, Jr., to me personally known, who, being by me first duly sworn, states that he is a Consultant at Towers Perrin, 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.

Donald D Schisler Jr.
(Name)

Subscribed and sworn to before me this 8th day of November, 2005.

Diana M. Niemeyer
(Name), Notary Public

My commission expires: 4-29-09.

DIANA M. NIEMEYER
Notary Public-Notary Seal
State of Missouri, Saint Louis City
Commission # 05701672
My Commission Expires Apr 29, 2009