

**MEMORANDUM**

FILED

TO: Missouri Public Service Commission Official Case File  
Case No. EF-98-120, The Empire District Electric Company JAN 20 1998

FROM: Ronald L. Bible *RB*  
Financial Analysis Department

MISSOURI  
PUBLIC SERVICE COMMISSION

*R.E. Schallenberg 12-18-97*  
Director - Utility Services Division / Date

*Steven J. Potts 1/16/98*  
General Counsel's Office / Date

*PWS 12/31/97*

SUBJECT: Staff's Recommendation for approval of the Application of The Empire District Electric Company for Authority to issue Debt in the form of First Mortgage Bonds.

DATE: December 18, 1997

**The Empire District Electric Company**

1. (a) **Type of Issue:** First Mortgage Bonds (hereinafter referred to as "Bonds")
- (b) **Amount:** Not to exceed \$80,000,000
- (c) **Rate:** The interest cost of the Bonds, including any applicable discounts, will not exceed 2.00 percentage points above the yield on 30-year U.S. Government Treasury Bonds as published in the Wall Street Journal on the day prior to the date on which the terms and conditions of the Bonds are determined.
- (d) **Other Provisions:** A document setting forth the aggregate principal amount to be sold, price information, estimated expenses of each issuance and the portion of the issuance subject to the fee schedule will be filed when terms become specific.
2. **Proposed Date of Transaction:** Any time over a two year period starting as soon as the Commission so authorizes.
3. (a) **Statement of Purpose of the Issue:** To be added to general funds for use in connection with the acquisition of property, the construction, completion or improvement of its plant or system, or the improvement or maintenance of service, or the discharge or lawful refunding of its obligations, or the reimbursement of moneys actually expended from income, or other moneys in the treasury not secured or obtained from the issuance of stocks, bonds, notes or other evidences of indebtedness.
- (b) **From a financial perspective, does Staff deem this purpose reasonable? :**  
Yes  No

4. **Type of Transaction:** The Company anticipates it will issue and sell each new series of Bonds in any of the following ways: (a) in a public offering through an underwriter or underwriters or dealer or dealers, (b) in a private placement directly to a limited number of purchasers or a single purchaser or (c) in an offering through agents.
5. **Copies of executed instruments defining terms of the proposed securities:**
- \_\_\_ (a) If such instruments have been previously filed with the Commission, a reference to the Case Number in which the instruments were furnished.
- X (b) If such instruments have not been executed at the time of filing, a statement of the general terms and conditions to be contained in the instruments which are proposed to be executed.
- \_\_\_ (c) If no such instruments are either executed or to be executed, a statement of how the securities are to be sold.
6. **Certified copy of resolution of the directors of applicant, or other legal documents authorizing the issuance of the securities reviewed:**
- Yes X No \_\_\_
7. **Pro-forma Balance Sheet and Income Statement reviewed:**
- Yes X No \_\_\_
8. **Capital expenditure schedule reviewed:**
- Yes X No \_\_\_
9. **Journal entries are required to be filed by the Company to allow for the Fee Schedule to be applied:**
- Yes X No \_\_\_
10. **Recommendation of the Financial Analysis Department:**
- X Grant by session order (see Comments)
- \_\_\_ Conditional Approval granted pending receipt of definite terms of issuance (see Comments)
- \_\_\_ Require additional and/or revised data before approval can be granted (see Comments)
- \_\_\_ Formal hearing required (see Comments)
- \_\_\_ Recommend dismissal (see Comments)

**COMMENTS:**

The Empire District Electric Company of Missouri, (Empire, Company) is a public utility engaged in providing services to customers in Missouri. The Company has filed an application requesting the Missouri Public Service Commission (Commission) authorize it to issue and sell under its existing Indenture of Mortgage Deed of Trust up to and including \$80,000,000 principal amount of its First Mortgage Bonds in one or more series.

The Company's Application, respecting the purpose of the Bonds, states:

That the Commission is without jurisdiction under state law to regulate the issuance of stocks, bonds, notes or other evidences of indebtedness of public utilities, like Empire, which are organized and existing under or by virtue of the laws of a state other than the State of Missouri. *See, Public Service Commission v. Union Pacific Railroad Company*, 271 Mo. S. W. 40 (1917); *Re Suburban Service Company*, 14 Mo. P.S.C. 114 (1923). The Commission's sole basis of jurisdiction in this case is the creation by Empire of a lien or encumbrance on its Missouri properties to secure payment of bonded indebtedness. *See*, §393.190.1, RSMo 1994. Thus, Empire seeks approval from the Commission to mortgage its Missouri properties to secure the Bonds.

...that Empire contemplates that the proceeds from the sale of each series of the Bonds will be used to provide financing for its construction program, to refinance outstanding indebtedness, including the payment of applicable redemption premiums, and for other corporate purposes; that refinancing of long term indebtedness will be done only where doing so will result in a lower or no additional net annualized interest cost to Empire; that the money, property or labor to be procured or paid for by the issuance and sale of bonds is reasonably required for the purposes specified in this application and that such purposes are not in whole or in part reasonably chargeable to operating expenses or income.

The Staff finds these terms reasonable.

A review of Empire's current and pro forma financial statements submitted with the Application indicates the Company's current capital structure is that of an investment grade electric utility as defined by Standard & Poor's Corporation. Empire's current capital structure consists of 15.71 percent short-term debt, 35.16 percent long-term debt, 5.89 percent preferred stock and 43.24 percent common equity. In the pro forma financial statement as of July 31, 1997, Empire has shown what effect their stated bond issues have on their debt, preferred stock and common stock. Long-term debt, preferred stock and common stock increase to 38.98 percent, 6.12 percent and 44.45 percent respectively. Short-term debt decreases substantially, by 33%, to 10.45% (see Attachment A).

A ratio analysis reveals that Empire's Pre-Tax Interest Coverage Ratio, Funds From Operations Interest Coverage Ratio and Funds From Operations to Total Debt Ratio are increased with the pro

forma adjustments. In addition, Total Debt to Total Capital Ratio decreases from 51% to 49%, which is an improvement (see Attachment B).

It is the opinion of the Financial Analysis Department's Staff that the pro forma adjustments, as stated, would not have a negative impact on the Company's credit worthiness or its ability to attract new capital. Instead, these changes would improve Empire's financial position.

Based on its review, the Staff recommends that the Commission approve the Application submitted by Empire subject to the following conditions:

1. That the Company file with the Commission the final terms and conditions, including the aggregate principal amount to be sold, price information, estimated expenses and portion subject to the fee schedule, concerning each issuance of Bonds;
2. That the Company file with the Commission any information concerning communication with credit rating agencies concerning this debt;
3. That the Company file with the Commission any information concerning deviations from their stated use of the funds from the Bond issuances that would materially change the pro forma capitalization and financial ratios; and
4. That the Company file with the Commission any information concerning use of the funds from the Bond issuances with regard to redemption of any outstanding long-term debt, including Net Present Value calculations indicating the amount of interest cost savings.

**The Staff respectfully requests that this matter be placed on the Commission's Agenda as soon as possible.**

Attachments:

A: Pro Forma Capitalization  
B: Ratio Analysis

Copies: Director - Utility Operations Division  
Director - Policy and Planning Division  
Manager - Financial Analysis Department  
Office of the Public Counsel  
Myron W. McKinney, The Empire District Electric Company

Director - Utility Services Division  
Manager - Electric Department  
General Counsel  
Paul A. Boudreau, Company Counsel

**Pro Forma Capitalization as of July 31, 1997  
for The Empire District Electric Company**

| Capital Component | Percentage<br>of Capital | Capital<br>Dollars | Pro Forma<br>Adjustments | Pro Forma<br>Capital<br>Dollars | Pro Forma<br>Percentage<br>of Capital |
|-------------------|--------------------------|--------------------|--------------------------|---------------------------------|---------------------------------------|
| Common Equity     | 43.24%                   | \$241,548,210      | \$33,820,000             | \$275,368,210                   | 44.45%                                |
| Preferred Stock   | 5.89%                    | 32,901,800         | 5,000,000                | 37,901,800                      | 6.12%                                 |
| Long-Term Debt    | 35.16%                   | 196,440,931        | 45,000,000               | 241,440,931                     | 38.98%                                |
| Short-Term Debt   | 15.71%                   | 87,758,561         | (23,000,000)             | 64,758,561                      | 10.45%                                |
| Total             | 100.00%                  | \$558,649,502      | \$60,820,000             | \$619,469,502                   | 100.00%                               |

**Financial Ratio Benchmarks  
Total Debt / Total Capital**

| Standard & Poor's Corporation's<br>Utilities Rating Service, |           | AA    | A     | BBB   |
|--|-----------|-------|-------|-------|
| Financial Statistics   | Range(%)  | 39-51 | 41-54 | 44-59 |
| Electric Utilities   | Median(%) | 43    | 47    | 50    |
| June 30, 1997  |           |       |       |       |

**Selected Pro Forma Financial Ratios  
for The Empire District Electric Company**

| <b>RATIO ANALYSIS</b>                    | <u>Ratios as<br/>of 6-30-95</u> | <u>Pro-Forma<br/>Ratios</u> | <u>S&amp;P Guidelines<br/>"AA" Rating (1)</u> | <u>S&amp;P Guidelines<br/>"A" Rating</u> | <u>S&amp;P Guidelines<br/>"BBB" Rating</u> |
|--|---------------------------------|-----------------------------|---|--|--|
| Pre-Tax Interest Coverage:               | 2.99 x                          | 3.62 x                      | 3.58-4.29 x                                   | 2.94-3.83 x                              | 2.23-3.03 x                                |
| Funds From Operations Interest Coverage: | 2.78 x                          | 3.50 x                      | 4.64-5.21 x                                   | 3.74-4.75 x                              | 2.95-3.96 x                                |
| Funds from Operations to Total Debt:     | 15%                             | 20%                         | 27.87-32.24 %                                 | 20.84-28.33 %                            | 15.30-22.86 %                              |
| Total Debt to Total Capital:             | 51%                             | 49%                         | 39-51 %                                       | 41-54 %                                  | 44-59 %                                    |

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**Notes:**

(1) Standard & Poor's Utilities Rating Service, Financial Statistics, June 30, 1997