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Kansas Corporation Commission
/S/ Patrice Petersen-Klein

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by
State Corporation Commission
of Kansas

BEFORE THE KANSAS CORPORATION COMMISSION
OF THE STATE OF KANSAS

In the Matter of the Application of Mid-Kansas Electric Company, LLC for Approval of a Debt Service Coverage Ratemaking Pilot Plan for the Geographic Territory Served by its Member-Owner Southern Pioneer Electric Company.	)))))	Docket No. 13-MKEE-452-MIS

PREFILED DIRECT TESTIMONY OF

STEPHEN J. EPPERSON
PRESIDENT AND CHIEF EXECTUIVE OFFICER
SOUTHERN PIONEER ELECTRIC COMPANY

ON BEHALF OF

MID-KANSAS ELECTRIC COMPANY, LLC

January 8, 2013

I. INTRODUCTION AND BACKGROUND

Q. Please state your name and business address.

A. My name is Stephen J. Epperson. My business address for legal service is 1850 W. Oklahoma, Ulysses Kansas 67880 and for mail receipt is PO Box 430, Ulysses Kansas 67880-0430.

Q. What is your profession?

A. I am the President and Chief Executive Officer of Southern Pioneer Electric Company ("Southern Pioneer"), pursuant to the Services Agreement entered into between Pioneer Electric Cooperative, Inc. ("Pioneer") and Southern Pioneer on July 7, 2006. Our corporate office is located in Ulysses, Kansas, and our distribution-customer service offices are located in Liberal and Medicine Lodge, Kansas.

Q. Please describe your responsibilities with Southern Pioneer.

A. The President and CEO ("CEO"), along with other executive officers and vice presidents, are appointed by the Board of Directors. As the CEO, I work directly for the Board of Directors and am responsible for assisting in establishing policy, implementing strategic programs, establishing rates, and overseeing the overall operation of Southern Pioneer to ensure reliable service at a competitive cost, all while using generally acceptable industry business practices. As the CEO, I also serve as a Director on the Mid-Kansas Electric Company, LLC ("Mid-Kansas") Board and work in close cooperation with Mid-Kansas to provide reliable service at reasonable rates for the Mid-Kansas customers that Southern Pioneer services under contract with Mid-Kansas.

Q. What is the purpose of your testimony in this proceeding?

A. The purpose of my testimony is to support the Application of Mid-Kansas and Southern Pioneer requesting approval of a Debt Service Coverage ("DSC") Formula Based Ratemaking ("FBR") Pilot Plan (referred to herein as the "DSC-FBR Plan"). My testimony will (1) provide historical information on the formation of Mid-Kansas and Southern Pioneer and highlight why Southern Pioneer is unique from other regulated utilities; (2) discuss the operating challenges and regulatory frustrations facing Southern Pioneer; and (3) provide testimony supporting the Plan and its benefits to consumers, regulators, the lender and the companies.

Q. What is your educational background?

A. I graduated from Ozark Christian College, a cooperative program with Missouri Southern State University, in 1991 with a Bachelors Degree, which included double majors in Bible and Psychology. In 2002, I successfully completed the National Rural Electric Cooperatives' Management Internship Program through the University of Nebraska at Lincoln, Nebraska. In 2010, I received my Masters of Business Administration from Bradley University.

Q. What is your professional background?

A. I was appointed Southern Pioneer's CEO effective January 1, 2011. Prior to that date, I served as the President and CEO at McDonough Power Cooperative located in Macomb, Illinois from July 2006 to December 31, 2010. From August 2001 to July 2006, I served as the Senior Vice President of Northeast Rural Services, Inc., a subsidiary of Northeast Oklahoma Electric Cooperative. I have also served in other capacities, in both the utilities and the private not-for-profit sectors as a business supervisor, consultant, business development director and counselor, etc.

Q. Have you previously presented testimony before the Commission?

A. Yes. I provided prefiled direct and rebuttal testimony in Docket No. 12-MKEE-380-RTS, as well as live testimony in the evidentiary hearing for that docket. I also filed direct testimony supporting the pending Mid-Kansas spin-down application in Docket No. 13-MKEE-447-MIS.

II. MID-KANSAS AND SOUTHERN PIONEER

Q. Please provide some historical information on Mid-Kansas and Southern Pioneer?

A. In March of 2005, Aquila, Inc. announced its intentions to sell its Kansas electric assets. Five member cooperatives of Sunflower Electric Power Corporation ("Sunflower") and Southern Pioneer, a wholly owned subsidiary of Pioneer, joined to form Mid-Kansas, a not-for-profit limited liability company, to acquire and serve the former Aquila service territory. Mid-Kansas and Aquila executed an Asset Purchase Agreement dated September 21, 2005. After KCC approval of the Aquila and Mid-Kansas Joint Application in Docket No. 06-MKEE-524-ACQ ("524 Docket"), effective April 1, 2007, Southern Pioneer began to serve and independently operate a designated geographic portion of the certificated territory transferred from Aquila to Mid-Kansas as described earlier.

Q. Please describe the business activities of Southern Pioneer.

A. As a Mid-Kansas member-owner, and pursuant to the July 2, 2007, Electric Customer Service Agreement approved by the Kansas Corporation Commission ("Commission" or "KCC") on December 21, 2007 in Docket No. 08-MKEE-099-MIS, Southern Pioneer provides retail service to approximately 17,300 consumers in 34 communities in the Mid-

Kansas Southern Pioneer Division. Southern Pioneer also provides sub-transmission service to 34.5kV sub-transmission users.

Q. On January 7, 2013, Mid-Kansas filed an application to transfer its Certificate to its member companies, including Southern Pioneer. How will that affect this Application for a DSC-FBR Plan?

A. The only impact I foresee is that Mid-Kansas will no longer be the applicant in this docket. Southern Pioneer will become the only named applicant in this case, as addressed and explained in more detail in the Application.

Q. Please describe Southern Pioneer's overall business philosophy in serving the Mid-Kansas Southern Pioneer Division customers and service territory.

A. Unlike any other regulated utility in Kansas, Southern Pioneer does not have shareholders. Rather, Southern Pioneer is governed by a Board of Directors that is comprised of cooperative members from the not-for-profit entity, Pioneer. Like Pioneer, Southern Pioneer's desire is to provide the Mid-Kansas customers with reliable service at a competitive price in order to sustain individual lifestyles and develop or strengthen the regional economy, all while managing long-term risk to the utility and its stakeholders.

Q. Could you please be more specific in describing why Southern Pioneer is unique or unlike any other utility in Kansas?

A. In the 524 Docket, the Commission approved the Stipulation and Agreement ("524 S&A") presented by the parties that contained a provision whereby Southern Pioneer agreed to operate as a not-for-profit, taxable entity and not remit dividends to its sole shareholder Pioneer without KCC and lender approvals. As a result, Southern Pioneer has no incentive to generate a rate of return for individual shareholders, to grow excess value in Southern

Pioneer at the expense of the consumers, or to inappropriately allocate or shift operating costs between Pioneer and Southern Pioneer. Southern Pioneer's financial goals are simply to earn adequate margins to meet lender loan covenants, achieve financial targets and cover operating costs and debt service. Southern Pioneer works hand-in-hand with Pioneer to eliminate redundant expenses to the benefit of the customers of both companies.

Q. Are you aware of any other public utility company in Kansas that operates as a not-for-profit C-Corporation owned by a member-owned cooperative?

A. No, I am not.

Q. The Commission approved establishment of Southern Pioneer as part of its approval of the Settlement Agreement submitted in the Mid-Kansas and Aquila acquisition case. Does this docket have any impact on the terms of the 524 S&A filed on January 10, 2007 and approved by the Commission on February 23, 2007?

A. There are certain provisions of the 524 S&A that would no longer be effective as a result of this Application. First, paragraph 29 requires Southern Pioneer to file a report by March 31st of each year supporting its TIER and DSC calculations for the preceding year's operations. This requirement under the 524 Docket should terminate since Southern Pioneer would be making its annual financial filings pursuant to the DSC-FBR Plan.

Second, paragraph 30 of the 524 S&A addresses the Revenue Refund Plan for Southern Pioneer which would essentially be replaced with the DSC-FBR Plan. As such, paragraph 30 should terminate if the DSC-FBR Plan is approved in this docket.

Q. Are there other terms of the 524 S&A that need to be considered?

A. Yes. I want to make clear that Southern Pioneer's agreement under paragraph 26 of the 524 S&A not to remit dividends to Pioneer absent Commission and lender approval will continue under the DSC-FBR Plan. To the extent Southern Pioneer needs to confirm this on-going commitment, I do so at that time.

I also want to confirm that Southern Pioneer will continue to comply with the Commission's requirement for customer advisory group meetings, initially addressed in paragraph 27 of the 524 S&A and later modified by the Commission's June 25, 2012 Order in Docket 12-MKEE-380-RTS.

IV. OPERATING AND REGULATORY CHALLENGES OF SOUTHERN PIONEER

Q. Could you please describe some of the challenges and frustrations facing Southern Pioneer as a uniquely situated regulated utility in Kansas?

A. Being regulated for ratemaking purposes is generally expensive, resource intensive, costly to ratepayers, financially challenging due to the prolonged approval process (up to 240-days), and results in the need for larger rate adjustment increases to account for regulatory lag. Southern Pioneer, when organized in 2005, was 100% debt financed with zero equity. Today, Southern Pioneer, still has near zero equity, consists of an aging infrastructure requiring large investments to ensure reliability, and is regulated much like a for-profit utility despite its obligation to operate like a not-for-profit.

Q. Please continue.

A. The challenges faced by Southern Pioneer result from the fact that we operate as a not-for-profit entity (making proactive investments in plant in an effort to provide long-term rate stability; thus, regional economic sustainability - the only reason we exist), but are treated for regulatory ratemaking purposes like an investor-owned utility ("IOU") that has an incentive to maximize its rate of return for the benefit of shareholders. This reality can incentivize an IOU to make short-term decisions resulting in less favorable reliability and the adoption of a reactive type of utility management – i.e., "when it breaks, we'll fix it." Southern Pioneer does not have this incentive. Additionally, IOU's are much better suited to manage regulatory disallowances of costs in revenue requests which occur in the ratemaking process. For example, in an attempt to minimize the overall rate increase in a rate case, the Commission Staff, the Citizens' Utility Ratepayer Board (CURB) or another intervener often propose disallowances for costs incurred by a utility and included in the company's engineer-prepared cost of service study. An IOU has some flexibility in managing these disallowances when they are adopted by the Commission. An IOU can choose to reduce its dividend to shareholders, it can reduce capital and operating expenses (which can result in greater expense long-term) or it can issue more stock to current shareholders as a means of raising capital to compensate for a revenue shortfall.

Q. Does Southern Pioneer have all these same options?

A. No and that is the challenge. Southern Pioneer does not have individual shareholders from whom it can extract this reduction while still providing the same level of service. In our case, any reduction in our revenue requirement request comes at the expense of providing service and continued reliability to our consumers and/or a further weakening the Company's financial status.

Q. Has this happened to Southern Pioneer recently?

A. Yes. In Docket No. 12-MKEE-380-RTS ("380 Docket"), based on the Company's cost of service study, Mid-Kansas requested an overall revenue increase of $7,992,522 for the Southern Pioneer division. Due to various recommended disallowances, Staff supported an increase of only $3,571,070, and CURB was even lower at $1,787,075. Ultimately, Mid-Kansas settled for $5,000,000 to avoid uncertainty and risk even beyond the $2.9 million given up in the settlement. Because the revenue request submitted in the application was based on a legitimate cost of service, and because Southern Pioneer does not have shareholders who can be forced to "eat" the short-fall, this $2.9 million deficit will have to be compensated for in some other way. The Company may have to consider reductions in "elective" services that it can control, such as tree trimming, annual pole inspection/treating or ongoing regular equipment maintenance or deferral of capital projects (most of which are proactive measures to minimize expense long-term). In addition, Southern Pioneer will continue as a near 100% debt financed company because the margins needed to build that equity simply do not exist. Building equity while at the same time investing in plant at Southern Pioneer's requested level places upward pressure on rates. A party seeking to minimize rate impact advocates for a position that ensures the Company cannot systematically improve its financial health and build equity while continuing to invest in plant.

Q. Does the system served by Southern Pioneer already suffer from a lack of proper maintenance?

A. Yes. This practice of not adequately investing in plant so as to reward shareholders and/or minimize rates was evident in the the condition of the acquired system when it was owned and operated by Aquila. As a matter of fact, the Commission in 2001, through Docket No. 02-GIME-365-GIE ("365 Docket"), *Adequacy of Quality of Retail Service Provided by Kansas Electric Public Utilities and the Prudence of Developing Electric Service Quality Standards*, created a regulatory framework and required all regulated utilities, including Aquila (formerly d/b/a UtiliCorp United Inc. and West Plains Energy at the time), to subscribe to certain service quality standards and annually submit to the Commission a plan to address these service and reliability deficiencies and the estimated cost to do so. To date, because of its proactive business practices utilized by member-owned electric cooperatives or utilities owned by cooperatives, Mid-Kansas and its member-divisions have been exempt from complying with the 365 Docket. Southern Pioneer does not want its level of service, maintenance and reliability to digress or be suppressed so that Southern Pioneer is viewed as similar to its predecessor Aquila. Nor does the Company, due to service complaints, want the Commission to have to mandate investing in plant or preventative maintenance programs as in the 365 Docket, especially since Southern Pioneer had included these components it in its engineer-prepared construction work plan, in its revenue requirements, and as one of its commitments in the 524 Docket.

Q. Please clarify why being treated like a for-profit IOU is frustrating for Southern Pioneer and Pioneer?

A. This treatment is frustrating because the IOU paradigm of maximizing its rate of return conflicts with the not-for-profit utility paradigm. The conflict exists because, while IOUs work to maximize profits in order to provide dividends to shareholders, the main goal of the not-for-profit utility is to make strategic, long-term investments in an effort to minimize rate adjustments, and to sustain or develop economic conditions that will benefit rural customers. While we are often cast in the same light as the IOUs, Southern Pioneer's and Pioneer's interests are aligned with its customers'/members' interests. Great service at the lowest possible rate provides regional economic sustainability and growth. Without it, industries leave, local communities fail, and the utilities serve no one. In short, our customers/members created us to provide them the ability to make life and business viable in south central and southwest Kansas, and for no other purpose.

Q. What other regulatory challenges limit Southern Pioneer's ability to meet its operational obligations and goals?

A. In the 380 Docket, Southern Pioneer incurred approximately $441,167 for consulting and legal fees, including costs assessed for Commission Staff and CURB. This amount is ultimately paid by ratepayers and does not even reflect costs associated with the internal Mid-Kansas or the allocated costs of the Pioneer utility staff personnel who assisted in the filing.

Q. Does the traditional regulatory rate case process increase overall costs to customers?

A. Unfortunately, "after the fact" cost recovery in a traditional rate setting, such as the 380 Docket, results in larger rate increase requests to carry the utility to the next filing. This is because there are more costs to recover (rate case expense), and because Southern Pioneer's lender (CoBank) is less flexible in relaxing loan covenants when future revenue recovery is less stable and more at risk. For example, with a DSC-FBR Plan in place, CoBank is more open to a lower DSC ratio because there is more stability and predictability in the Company's revenue stream. A lower DSC ratio – such as a 1.8 instead of a 2.0 - lowers the amount of the revenue requirement. Without the DSC-FBR Plan, the lag time in cost recovery and the fact that the utility historically receives only a portion of its request to fund its cost of service, as testified to above, produces both financial and rate relief uncertainty for the utility, which can affect capital costs, service levels and timely completion of capital projects.

Q. Aren't these simply the realities of being a regulated public utility?

A. They may be a reality of traditional regulation, but to the extent they are unnecessary to protect customers, they should be avoided because they are costly and burdensome. That is the point I am making here; the costs and burdens of heavy-handed regulation are not necessary in the case of Southern Pioneer.

V. THE DSC-FBR PLAN AND ITS BENEFITS

Q. What is the purpose of this Mid-Kansas filing?

A. The purpose of this filing is to introduce a DSC-FBR Pilot Plan for Southern Pioneer that includes implementation of an alternative regulatory framework over a definitive timeframe.

Q. Is the proposed Plan similar to the DSC ratemaking plan contained in the most recent Mid-Kansas/Southern Pioneer rate case in the 380 Docket?

A. It is similar, but not identical. Furthermore, the DSC ratemaking plan in the 380 Docket was never decided by the Commission. Staff objected to the DSC plan and the settlement reached between the parties in that case did not include the DSC plan. This case will be the Commission's first opportunity to evaluate and decide the issue, and we believe it will be a better opportunity than in a rate case where many issues are being addressed at the same time.

Q. What has changed since the 380 Docket that supports re-submitting the Plan now for consideration?

A. There are a number of changed circumstances since the filing in the 380 Docket. In addition, as a result of experiencing the 380 Docket, I believe there is a better understanding now by Staff and the Commission of Southern Pioneer's financial challenges and governance status.

Q. Please explain.

A. First, one of the reasons Staff chose not to adopt a DSC ratemaking plan for Southern Pioneer in the 380 Docket was because Staff did not believe Southern Pioneer was in "dire financial health".[1] Staff felt that financial instability was a prominent basis for why the Michigan Public Service Commission had implemented DSC ratemaking for many of its cooperatives, and Staff did not think this status was applicable to Southern Pioneer.[2] During settlement discussions in the 380 Docket, however, it became clear that there was some misunderstanding among the parties regarding the financial obligations of Southern Pioneer and its need in the short-term to borrow capital and make capital investments. Southern Pioneer is capitalized with essentially 100% debt, and although I would not call its financial scenario "dire", I do believe that Staff now recognizes the financial challenges the company faces.

Second, Staff rejected consideration of an alternative ratemaking plan in the 380 Docket on the basis of Staff's continued belief that Southern Pioneer should have been organized as a cooperative instead of a C-corporation. Because Southern Pioneer opted for the C-corporation structure, Staff did not think Southern Pioneer should be allowed special treatment, such as an alternative ratemaking procedure.[3] In its Order in the 380 Docket the Commission resolved this issue, finding that the appropriateness of the organizational structure chosen by Southern Pioneer should not be an issue in future dockets. As such, one of Staff's primary reasons for rejecting consideration of the DSC ratemaking plan in the 380 Docket no longer exists.

Q. Have there been other changes since the 380 Docket?

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[1] Bowman Direct Testimony in the 380 Docket, pp. 16- 17.

[2] The weak financial condition of the Michigan cooperatives was actually not a major consideration of the Michigan Public Service Commission in adopting the DSC ratemaking methodology. Company witness, Mr. Richard Macke discusses this in more detail in his Direct Testimony in this docket.

[3] Bowman Direct Testimony in the 380 Docket, pp. 17-18.

A. Yes. Of utmost importance is the increasing pressure being placed upon Southern Pioneer and other utilities by the oil and gas industry to construct facilities in a responsive manner to allow Kansas oil and gas developers the opportunity to participate in the growth we are seeing in the industry, and particularly in the counties in Southern Pioneer's territory and the surrounding area. The KCC, on their web site, reports that in just the last six months as of mid-December 2012 there has been a total of 226 Notices of Intents to drill filed in eight of the ten counties in which Southern serves directly through its distribution system or indirectly through its 34.5kV sub-transmission system. More specifically and as an example, just in the first ten months of 2012, Southern Pioneer has added infrastructure to serve 29 new wells totaling 2,300 horsepower or just under three megawatts, has expanded substations to support the additional load, and is working with another consumer to serve a three megawatt oil pipeline pumping load. This load is what we know today and does not include what may be speculated or the results of the Intents to Drill in the future by developers, something not readily known in advance by the serving utilities. The regulatory delays and costs associated with the standard rate-setting model, coupled with Southern Pioneer's highly leveraged financial status, is posing a serious challenge to the company's ability to react and invest as needed in this fast moving new oil and gas environment. Although some of the direct costs related to construction for the new oil & gas exploration can be recovered up-front from the customer requesting the facilities, this is not always the case. Furthermore, facility investment related to the secondary level of economic development – housing and commercial expansion and improvements in public services triggered by increased oil & gas activity – must be financed by the Company without up-front contributions from customers. The economic development for rural

Kansas related to this new exploration boom should be facilitated, not hindered by regulatory lag and uncertainty. Mid-Kansas witness, Mr. Don Gulley, addresses this factor in more detail in his testimony.

Finally, as stated previously, Mid-Kansas has now filed to transfer its Certificate to its member companies, including Southern Pioneer. Upon approval of that application, many of the complications that have been inherent in the structure of the Mid-Kansas members will become more simple and straight-forward. This long-anticipated occurrence should aid the Commission and its Staff in its future efforts to oversee and regulate Mid-Kansas and its members, including future regulation of Southern Pioneer under the proposed DSC-FBR Plan.

Q. In addition to your testimony, is Mid-Kansas offering other testimony in support of the DSC-FBR Plan Application?

A. Yes. Mr. Don Gully and Mr. Rich Macke are also providing testimony in support of the Application. With regard to the proposed DSC-FBR Plan, Mr. Rich Macke discusses these concepts in detail in his direct testimony.

Q. Even though Mr. Macke provides a detailed explanation of the DSC-FBR Plan, will you please provide a conceptual description of the proposal?

A. Conceptually, the DSC-FBR Plan is intended to be an annual mechanism used to adjust retail rates based on the utility's cost to provide service and a pre-agreed DSC based formula within defined limits. If approved and implemented, its primary purpose is to allow, for a definitive period, timely adjustments to retail rates without the unnecessary expense, risk and lag related to preparing and presenting to the KCC a traditional, full rate case every year. As proposed, the DSC-FBR Plan has a DSC Floor, DSC Ceiling and graduated DSC Target.

Q. Please explain what occurs if the adjusted DSC falls between the Floor and Ceiling, or if it falls outside these thresholds?

A. If the annual adjusted DSC is between the Floor and Ceiling, i.e. within the DSC Quiet Zone, there is no revenue adjustment. However, if the annual adjusted DSC is greater than the DSC Ceiling, then rates are decreased so that after-tax revenues are brought back to a level that returns the company to the DSC Target. Conversely, if the annual adjusted DSC is less than the DSC Floor, then after-tax revenues are increased allowing the company to meet the DSC Target. This Plan works very similar to the model followed by non-profit cooperatives where excess margins go directly to the benefit of customers through capital credits (equity) and/or forward-looking rate reductions.

Q. Should regulators or customers be concerned that the DSC-FBR Plan results in relaxed regulatory oversight beyond that which is customarily exercised in traditional rate cases?

A. Not in the case of Southern Pioneer. Any concern that Mid-Kansas and Southern Pioneer will be operating devoid of adequate regulatory oversight is unwarranted. In crafting the DSC-FBR Plan, we have ensured that provisions are in place to inform and protect consumers, and ensure regulatory review and approval each year. As an example, if a requested revenue adjustment, including the gross-up for taxes, exceeds 10% in any year, Mid-Kansas (or Southern Pioneer once the Certificate transfer occurs) will be required to file a standard or traditional rate case with the Commission. Also, as part of the Plan, customers will be notified each year when the annual DSC-FBR filing is made with the KCC. The Commission Staff will review the annual compliance filing to confirm compliance with the Plan. In the event rate adjustments are necessary, said adjustments will not be instituted without Commission approval.

Q. Is this concept of using a financial ratio to either increase rates or refund revenues new, and has it been used in Kansas or elsewhere?

A. No, it is not new, and yes, it has been used in Kansas and elsewhere. As outlined in Mr. Macke's testimony, a variation of this ratemaking methodology has been implemented and reaffirmed for the regulation of electric distribution cooperatives in Michigan. Also, as a condition in the 524 Docket, it was agreed to by the parties and approved by the Commission that in the event Southern Pioneer's Times Interest Earned Ration ("TIER") exceeded 2.2, Southern would file with the Commission a Revenue Reduction Plan to return revenues to consumers at a rate that would return Southern Pioneer to its target TIER of 2.0. Such an approach is a variation of formula-based ratemaking using a TIER ratio. Further, Transmission Formula Based Ratemaking is currently utilized in Kansas and at FERC, and FERC also uses Formula-Based Wholesale Ratemaking.

Q. What are the benefits the DSC-FBR Plan provides to consumers, regulators, the lender, and the utility if approved and implemented?

A. In regards to consumers, while maintaining regulatory oversight and consumer input, the DSC-FBR Plan, as proposed, will directly reduce the legal and consulting costs passed on to ratepayers, and will provide rate stability by adjusting rates in smaller increments, thus making it easier for consumers to budget. Further, the Plan will allow Southern Pioneer to be more responsive to the emerging customer demands for new facilities associated with the extensive oil and gas exploration occurring in the Mississippian Lime formation in Southern Pioneer's south central Kansas service area. This economic development includes a secondary tier related to the oil and gas boom, such as housing, commercial expansion and improvements in public services. Finally, the Plan will provide Southern Pioneer the ability to more reliably serve the thirty-four communities and 17,300 consumers in its service territory.

Q. How does the DSC-FBR Plan benefit regulators?

A. Because the Plan utilizes a pre-determined formula that has been approved by the Commission, the annual compliance filings reduce time demands on both the KCC Staff and Commission by eliminating the need for full-blown annual rate case filings. Plus, during the Plan's approved life, it can accommodate the implementation of any voluntary or mandated cost-effective Energy Efficiency and Conservation Programs without necessarily disrupting overall rate recovery, since, by using a DSC formula, these changes can seamlessly be implemented as part of the pre-approved formula

Q. Please explain the benefits of the DSC-FBR Plan to the utility and its lenders.

A. Due to regulatory certainty afforded by the implementation of a DSC-FBR Plan, Southern Pioneer will be able to more effectively plan for and provide long-term, safe and reliable service. A DSC-FBR Plan allows rates to be set using a lower DSC ratio since lenders are faced with fewer unknowns than when a company must file annual rate cases. It allows Southern Pioneer to systematically achieve financial targets and grow much-needed equity over a period of time, benefitting the utility's lender by establishing stabilized and adequate rate recovery to fulfill loan covenants and cover debt service. Because Pioneer is currently required to guarantee Southern Pioneer's debt, the implementation of the DSC-FBR Plan is extremely important to both companies because as Southern Pioneer achieves financial health, the risk to Pioneer's members is removed as loan guarantees can be eliminated.

Q. Does this conclude your Direct Testimony?

A. Yes, it does.

VERIFICATION

STATE OF KANSAS)
) ss
COUNTY OF GRANT)

The undersigned, Stephen J. Epperson, upon oath first duly sworn, states that he is an officer of Southern Pioneer Electric Company, and that he has prepared the foregoing testimony, that he is familiar with the contents thereof, and that the statements contained therein are true and correct to the best of his knowledge and belief.

Stephen J. Epperson

Subscribed and sworn to before me this 4th day of January, 2013.

Notary Public

NOTARY PUBLIC - State of Kansas
BRANDI FOWLER
My Appt. Exp. 12/3/16

My appointment expires: 12/3/16