BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Petition of The Empire	)	
District Election Company d/b/a Liberty	)	File No. EO-2022-0193
to Obtain a Financing Order that Authorizes	)	
the Issuance of Securitized Utility Tariff Bonds	)	
for Energy Transition Costs Related	)	
to the Asbury Plant.	)	

AMICUS CURIAE **BRIEF OF UNION ELECTRIC COMPANY D/B/A AMEREN MISSOURI**

COMES NOW Union Electric Company d/b/a Ameren Missouri ("Company" or "Ameren Missouri)" and for its *Amicus Curiae* Brief, states as follows:

INTRODUCTION

Issue 3)H) as presented by the parties to this case posed the following issue for the Commission's resolution:

> "What are the values of the Accumulated Deferred Income Tax (ADIT) and Excess ADIT?"[1]

This statement of the issue in part led to a serious mistake in the *Report and Order* (the "Empire Order") issued in this case. Indeed, the issue statement is inaccurate, at least in part, because for the most part, the question answered by the Commission in resolution of this issue is not – nor should it have been – a decision on the value of the ADIT balance (or the NPV of the ADIT balance)—that is, on the amount of deferred taxes Empire will ultimately owe the Internal Revenue Service ("IRS"). Instead, the question the statute requires the Commission to answer – the issue that should have been for the Commission's decision but was never presented by the parties as such, is "what is the credit due to customers against the balance to be securitized due to the tax

[1] File No. EO-2022-0193, Empire *Report and Order*, ¶. H, p. 52, issued August 18, 2022.

benefits arising from the ADIT itself?[2]

Had the Commission properly been presented with that issue – and then resolved it – it is a near certainty that a critical mistake that Empire has indicated will prevent it from proceeding with issuance of the securitization bonds – and that will likely prevent Ameren Missouri or any other electrical corporation from doing so either, assuming that the mistake would be applied to them – would never have been made.

Importantly, the mistake can be – and must be – corrected now, in order to implement the policy reflected in the General Assembly's adoption of the securitization statute in 2021.

ARGUMENT

Subsection 2(3)(c)m of §393.1700, RSMo,[3] which is reproduced in its entirety at pages 53 and 54 of the Empire Order, imposes two key requirements for any financing order. First, the ADIT associated with the plant investment being retired must be "excluded from rate base in future general rate cases." ADIT[4] is a future obligation to remit income taxes to a taxing authority. Traditionally, the time value of money benefit (i.e., the net present value of tax benefits arising from the ADIT) associated with a utility deferring income tax payments to future periods is provided to customers through a reduction in rate base. Since ADIT is removed from rate base when securitization is used, obviously customers cannot get the time value of money benefit in the same way.

Which brings us to the second key requirement, that is, to make sure that when securitization is used, customers do get the time value of money benefit arising from the ADIT in another way. To do this, the statute provides that the "amount to be recovered through the issuance of securitized utility bonds [i.e., the bond principal] shall be credited to retail customers by reducing the amount of

[2] As expressly provided for in Subsection 2(3)(c)m of §393.1700, RSMo.
[3] All statutory references are to the Revised Statutes of Missouri (Cum. Supp. 2022).
[4] In this instance more specifically accumulated deferred income tax liabilities, as opposed to accumulated deferred income tax assets.

such securitized utility tariff bonds.…" The statute specifically tells us what that reduction is when it mandates that the reduction (credit) of the sum to be securitized is equal to the "net present value of the tax benefits."[5]

And what is that tax benefit? It is the time value of money referenced earlier (i.e., the net present value or "NPV") arising from not paying those deferred taxes today, but instead paying them 1/13th at a time each year over the 13-year life of the securitization bonds. How does one determine that time value of money? The statute tells us that too: "[t]he customer credit shall include the net present value of the tax benefits, *calculated using a discount rate* [which produces the NPV] equal to the expected interest rate . . . [on the bonds], for the estimated [ADIT] at the time of securitization including the timing difference created by the issuance of [the bonds] amortized [in this case, over 13 years]."

To repeat what we said in the Introduction: the *tax benefit* is not, nor can it be, the ADIT itself because the ADIT itself is *not a benefit at all.* The ADIT is a federal income tax obligation – a *burden* – that will be paid in the future, over the life of the bonds. The only benefit the ADIT produces is the time value of money saved by spreading out its payment over 13 years. In other words: customers got that benefit in traditional ratemaking via a reduction in rate base (which had the effect of giving them the time value of money); customers get it in securitization via a reduction in the sum that is securitized, equal to the time value of money.

So, what went wrong when Staff recommended that the sums to be securitized be reduced (i.e., that the credit required by the statute equal) by $17,134,363?[6] What went wrong is that the Staff calculated the NPV <u>of the ADIT</u>, instead of the NPV <u>of the tax benefit</u> arising <u>from</u> the ADIT. Put another way, by using the NPV of the ADIT itself, Staff's position implicitly assumes that the

[5] See the third sentence of §393.1700.2(3)(c)m.

[6] Exhibit 111. This figure assumes the ultimate interest rate on the bonds ends up being 4% - as the Commission recognized, the dollar figure will change depending on the final interest rate.

taxes represented by the ADIT *will never be paid by Empire*.

That obviously cannot be and is not correct. It is axiomatic that the state of Missouri cannot, by virtue of passing a securitization statute, cancel federal income taxes owed under the Internal Revenue Code to the IRS. Nor can the Commission, by issuing a financing order, cancel those taxes. Given that clearly the taxes (the ADIT) are *still owed and will be paid*, removing the NPV of the ADIT itself from the securitization bond principal, which is what Staff recommended and the Empire Order does, means that Empire will be forced to refund to customers sums that had properly been reflected in the revenue requirements on which its base rates were set to cover the tax obligation everyone recognizes Empire must pay over time. Under the Empire Order, customers are not being credited with the net present value of tax benefits arising from the ADIT, as the statute logically requires, but are being gifted the deferred taxes themselves (more accurately, the NPV of those deferred taxes), yet Empire will have to pay them but will have been deprived of the funds to do so since the securitization bonds will have been reduced by that same sum. Basic utility ratemaking recognizes that part of customers' obligation is to pay rates based on a revenue requirement that reflects the tax liability their payments for service create for the utility, since those taxes are prudently incurred (indeed unavoidable) operating expenses, just like the other expenses a utility must incur if it is to provide service.

This is in no way to say customers should not get the <u>benefit the ADIT provides</u>, and since stretching the payment of the taxes out over 13 years will save Empire money on a present value basis, customers should get that benefit. As earlier discussed, under traditional financing and recovery, when the ADIT remains in rate base, customers get the benefit that ADIT provides – that time value of money – one year at a time since rate base is reduced by the ADIT and correspondingly the annual revenue requirement is reduced by that time value of money. With securitization, the Commission needs to figure the entire benefit from the ADIT over the 13 years during which the

bonds will be repaid, so it can calculate, in the words of the statute, the "net present value of the tax benefits." The principal amount of the bonds will be reduced (credited) by that sum, by the time value of money benefit (i.e., the NPV of the tax benefits). Everyone is made whole by such treatment, which is fair and logical, as the statute requires.

So, how did the fundamental mistake in the Empire Order occur? Ameren Missouri believes it occurred for two primary reasons.

First, as noted earlier, the phrasing of the issue put before the Commission for decision caused a focus on the "value of the ADIT" itself instead of on the value of the tax benefit *from* the ADIT. Second, it appears that no one recognized that the disagreement on the credit required by §393.1700.2(3)(c)m was not grounded in a dispute about methodology (the math), as everyone (the Commission concluded) assumed. Instead, the disagreement that was really at issue was simply caused by the Staff mistakenly using the wrong figure; the discounted ADIT balance itself rather than the NPV of the tax benefit from ADIT. Indeed, Staff completely failed to even calculate the NPV of the tax benefit, as shown by Staff witness Bolin's workpaper (Exhibit 111), that only contains the NPV of the ADIT itself (but using simple subtraction it is calculable from Staff's workpaper (Exhibit 111) by subtracting the NPV of the ADIT from the undiscounted ADIT balance). This likely goes back to the misstatement of the issue, because the workpaper does answer the issue that was posed – the (discounted) value of the ADIT. As noted, the issue that was posed is simply the wrong issue to have put before the Commission for resolution since the issue to be resolved was the value of the *tax benefits* arising *from* the ADIT.

How do we know that the focus on a supposed dispute between Staff's methodology versus Empire's methodology was misplaced? Because Staff and Empire <u>used the same methodology.</u> That

is to say that both Staff's and Empire's calculations can be perfectly reconciled mathematically.[7]

Attached hereto as Exhibit 1 is a workpaper which includes a reproduction of Staff witness Bolin's workpaper[8] and that otherwise uses information that is part of the evidentiary record in this case. One can see the $17,134,363 which she calculated[9] that, if the bond interest rate did turn out to be 4% which was the underlying assumption from Staff's Exhibit 111, would be the credit against the sums to be securitized that the Empire Order currently would require. The key thing on which to focus appears in row 36. First, in Cell B36, we see the reduction in the bond principal the Empire Order currently requires (assuming a 4% bond rate) – it is taken straight from the Bolin workpaper, Exhibit 111, as are all of the figures leading to the Outputs from Staff Calculation on the left side of the workpaper. It is the only NPV Staff witness Bolin calculated. For the reasons discussed earlier, it was the wrong figure to use because it is the NPV of the <u>ADIT itself</u> and not the NPV of the <u>tax benefits</u>. Had Staff witness Bolin calculated the right figure – in Cell B38, the math – simple subtraction from the figures from her own workpaper – demonstrates that she would have gotten $5,172,324.[10] Not coincidentally, that is precisely the figure Empire gets if it uses the same inputs – see Cell G38. And what that confirms is that there is no methodological dispute here, at least not one that matters.

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[7] While it is true that the order in which Empire approached the math is arguably more directly in line with the exact wording of the statute, the mathematics of both methodologies get one to exactly the same place, making a fight about methodology much ado about nothing.

[8] Exhibit 111, page 2.

[9] See Cell B36.

[10] The Commission should not allow itself to be confused about the different tax benefit numbers reflected in Empire's rehearing application, in tables 2 to 4 (Column H), because Empire continues to use the 2.47% discount rate that it sponsored in its direct case, while Staff is using a forecast from May 2022 (which Ameren Missouri used in Exhibit 1 to this brief, to demonstrate that with the same inputs the same result occurs). As the Empire Order properly recognizes, the discount rate will be what it will be, but can't be known until the bonds are underwritten, placed, and issued. Also, Empire's rehearing application numbers assume intra-year cash flows occur on the last day of the year while Staff is assuming those same cash flows occur on the first day of the year. But from a methodological standpoint – when both parties use the same inputs and assumptions in the math – both parties will get the same answer, as Exhibit 1 shows.

To be fair, everyone appears to have failed to appreciate that the math used by Staff and by Empire lead to the same result, which is probably understandable since Staff never calculated the NPV of the tax benefit at all as it should have done, and given that at various stages in the case's development different inputs were being used. And since the fact that the math was the same was not fully appreciated and not calculated by the Staff, the Commission had no way to know that the math used by both Staff and Empire was in fact the same. And as noted, the parties and the Commission could also have been diverted into this mistake by the debate the Staff and Empire were having about the discount rate, with Staff arguing that 4% should be used since by the time of hearing the expectations had changed (see Exhibit 118) and Empire arguing for using the 2.47% bond rate on which it had based its direct case. Using different interest rates, even though as it turns out Staff and Empire were doing the same math, produced different figures, all of which caused there to be lots of numbers floating around in the record that appears to have led to confusion, and in turn, the mistake at issue here.[11]

Moreover, and this may have injected the most confusion of all, is the debate that took place about whether figures had improperly been discounted twice (i.e., "double-discounted") with Staff claiming that "Empire's methodology" indeed did reflect improperly discounting the ADIT twice.[12] In fact, this supposed double-discounting is the only basis cited by the Empire Order for deciding that the "methodology used by Staff witness Kim Bolin" is the correct methodology.[13] But the fact that Staff and Empire are using the exact same math and that, when using the same inputs, get the exact same answer shows that there of course is not and never was any double-discounting. Empire did not "inappropriately discount the ADIT twice" any more than Staff did. They both discounted

[11] As noted in footnote 9, Liberty's rehearing application still uses different inputs but in terms of the mistake at issue, the inputs do not matter; what matters is that the NPV of the tax benefit and not of the ADIT itself must be used as the reduction of the bond principal.
[12] Empire Order, p. 52 (citing Ex. 102).
[13] Empire Order, ¶ 108 (p. 52) and the Commission's Decision on the issue, p. 54.

the ADIT once – leading to the exact same $17,134,363 NPV of the ADIT itself (Exhibit 1) when the same inputs are used. What happened here is that Staff simply failed to calculate the NPV of the tax benefits themselves, which is the only benefit customers would have gotten had this case never been filed and traditional financing and recovery been used instead. But the math used by both parties agrees exactly when that necessary calculation is made (again, using the same inputs) -- $5,172,324.[14]

CONCLUSION

Any dispute about methodology doesn't matter; both Staff and Empire used exactly the same math. They advocated for use of different inputs, to come up with what all agree were illustrative outputs, since the actual interest rate on the bonds cannot be known at this time, but when the same inputs are plugged into both Staff's and Empire's approaches on the ADIT issue, the exact same outputs emerge. This means there cannot have been double-discounting, as Staff feared, and the double-discounting allegation appears to have led the Commission to accept Staff's mistaken recommendation to reduce the securitized sums by the ADIT itself rather than by the tax benefit from the ADIT.

The deferred taxes are owed; they will be paid, and it is plainly error to reduce the bonds by the amount of those deferred taxes since that is not a tax benefit it is, in fact, a detriment caused by the tax code: the detriment, which we all feel every April 15, is that one must pay the taxes. Neither adoption of the securitization statute nor issuance of the Empire Order can cancel those taxes. Consequently, the bond principal should not be reduced by them. Doing so was a clear mistake.

The fix is an easy one. Order that the NPV of tax benefits arising from the ADIT, discounted using whatever the bond rate turns out to be, reduce (be credited against) all of the other sums the Commission has authorized be included in the sums to be securitized. If the bond interest rate does

[14] Exhibit 1, Cells B38 and G38.

turn out to be 4%, that credit will be $5,172,324. If the bond interest rate turns out to be 2.47%, that credit will be $3,423,891. But whatever that interest turns out to be, the credit will give customers all of the benefit – the only benefit – of the ADIT, and the bonded sum will not improperly be reduced by the ADIT itself.

It is critical the Commission correct this mistake in order for the benefits the General Assembly sought to create when it adopted the securitization statute can be realized because if this mistake were carried forward to other utilities, including Ameren Missouri, it is unlikely securitization can be useful.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned certifies that true and correct copies of the foregoing have been e-mailed or mailed, via first-class United States Mail, postage pre-paid, to the service list of record of this case on this 30th day of August, 2022.

James B. Lowery
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