

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Propriety of the)
Rate Schedules for Electric Service of)
The Empire District Electric Company)

Case No. ER-2018-_____

**MOTION TO OPEN RATE CASE AND TO
REQUIRE COMPANY TO SHOW CAUSE**

COMES NOW the Staff of the Missouri Public Service Commission and hereby prays that the Commission will open a rate case to consider the continued propriety of the rate schedules heretofore established for electric service provided by The Empire District Electric Company (“Empire Electric”); and, in that regard, to order Empire Electric to show cause, if any it has, why the Commission should not forthwith order it to file tariffs reducing its rates for every class and category of service by the percentage reduction in the federal-state effective income tax rate. In support of its *Motion*, Staff states:

Introduction

1. This motion requests the Commission to establish a rate case to determine the continued propriety of Empire Electric’s existing rate schedules for electric service in view of the recent enactment of the Tax Cuts and Jobs Act of 2017 (“TCJA”), which reduced the federal corporate income tax rate from 35% to 21%. In establishing this rate case, Staff further requests that the Commission order Empire Electric to show cause, if any it has, why the Commission should not forthwith order it to file tariffs reducing its rates for every class and category of electric service by the percentage reduction in the federal-state effective income tax rate.

Parties

2. The Empire District Electric Company is a Kansas general business corporation, headquartered at 602 South Joplin Avenue, Joplin, Missouri 64801. Empire Electric's registered agent is Dale W. Harrington, 602 South Joplin Avenue, Joplin, Missouri 64801. Empire Electric is a wholly-owned subsidiary of Liberty Utilities (Central) Company, a Delaware general business corporation, public utility holding company, and a wholly-owned subsidiary of Liberty Utilities Company and an indirect subsidiary of Algonquin Power & Utilities Corporation, a Canadian public utility holding company.

3. In addition to the Staff, Movant herein, Staff hereby moves that the Commission make all of the parties to Empire Electric's last rate case parties to this proceeding.

Jurisdiction

4. Empire Electric is engaged in the business of providing electric service to the general public in certain Missouri cities, towns, and counties pursuant to rate schedules approved by the Commission. Empire Electric is thus an electrical corporation, § 386.020(15), RSMo., and a public utility, § 386.020(43), RSMo., subject to regulation by the Commission. Section 386.250, RSMo.

5. The Commission may, on its own motion, open a rate proceeding to determine the reasonableness of the rates and charges of any electrical, gas, heat, water, or sewer corporation. Section 386.390.1, RSMo.; ***State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission***, 585 S.W.2d 41, 48 (Mo. banc 1979) ("***UCCM***"). Within a rate case, the Commission

may investigate any matter necessary to enable it to ascertain facts requisite to the exercise of its powers. Section 393.270.1, RSMo., **UCCM**, at 48.

Facts

6. The TCJA reduced the federal corporate income tax rate from 35% to 21%, effective January 1, 2018. When the Commission set Empire Electric's rates, it used a composite federal-state effective tax rate of 38.39% in calculating current and deferred income tax expense. The impact of the TCJA on the composite effective tax rate is a reduction from 38.39% to 25.45%, amounting to a reduction of 12.94% or approximately one-third of the prior effective tax rate. Incorporation of the federal corporate tax rate reduction in Empire Electric's cost of service will result in material over earning by Empire Electric unless its rate schedules are re-calculated using the new composite federal-state effective tax rate.

7. Empire Electric's booked financial results during 2018 will reflect the new tax rates and rules enacted by the TCJA, and thus will reflect higher earnings than in 2017 and previous years, all other things being equal.

8. When Empire Electric pays its 2018 taxes in 2019, the composite federal-state effective tax rate will be 25.45%.

9. Beginning on January 1, 2018, Empire Electric began collecting payments from its customers pursuant to rates calculated using a composite federal-state effective tax rate of 38.39%.

10. Although Empire Electric's customers are charged and make payments pursuant to rates calculated using a composite federal-state effective tax rate, Empire Electric does not pay the total amount collected from customers over to the

taxing authorities immediately. Instead, a portion of Empire Electric's tax liability has been deferred and the money collected for customers against this liability has been used by Empire Electric as capital. The net amount of this Accumulated Deferred Income Tax ("ADIT") has been deducted from rate base when Empire Electric's rate are set in order to provide a return to ratepayers on the monies provided.

11. Due to the TCJA, deferred taxes that were collected in years past from customers assuming a 38.39% composite federal-state effective tax rate will now actually be paid to the taxing authorities by Empire Electric in the future at a 25.45% composite federal-state effective tax rate. This means that the current ADIT reserve balance recorded by Empire Electric on its balance sheet and reflected in its rate base is overstated and that, unless some action is taken by the Commission to flow back excess ADIT to customers, Empire Electric will permanently retain this customer-provided capital.

12. The ADIT balance on Empire Electric's books at this time can be divided into two categories: protected ADIT and unprotected ADIT.

13. Protected ADIT is the portion associated with accelerated depreciation tax timing differences that must be "normalized" for ratemaking purposes. "Tax normalization" effectively means the utility receives an immediate benefit from the accelerated depreciation tax timing difference, with that benefit then being gradually passed on to customers over the estimated life of the utility asset giving rise to the accelerated depreciation deduction. Under the TCJA, Staff's understanding is that the Commission is restricted from flowing back protected excess ADIT to customers in rates any more quickly than over the estimated average remaining life of the assets that gave

rise to the ADIT. This amortization period is expected to be quite lengthy, with approximately 20 years being a reasonable estimate for most utilities.

14. Unprotected excess ADIT is the portion of Empire Electric's deferred tax reserve that resulted from normalization treatment of tax timing differences other than accelerated depreciation deductions. Staff understands that unprotected excess ADIT can be flowed back to customers through an amortization period of the Commission's choosing.

15. Based upon Staff's preliminary analysis of potential excess protected and unprotected ADIT flow back, Staff believes this component of tax reform will also have a material revenue requirement impact on Empire Electric.

16. The nature of the action that the Commission should take with respect to Empire Electric's current ADIT reserve balance is not yet known. Staff urges the Commission to require Empire Electric to quantify and track its excess protected and unprotected ADIT from January 1, 2018 forward for future flow back to ratepayers in this proceeding or in subsequent general rate proceedings.

17. There may be other material impacts of the TCJA on Empire Electric that are not yet known. Staff will provide information on other impacts of the TCJA on Empire Electric as they become known.

The Commission's Authority to Set Rates

18. However a rate case is initiated, the Commission is required to consider all relevant factors in setting just and reasonable prospective rates for utility service rendered. ***UCCM***, at 49.

19. Nonetheless, it is possible that the consideration of all relevant factors is unnecessary in this case. The Commission is authorized to treat an item of operating expense differently where it is just and reasonable to do so. ***State ex rel. Midwest Gas Users' Association v. Public Service Commission***, 976 S.W.2d 470, 478 (Mo. App., W.D. 1998), *citing* ***UCCM and State ex rel. Hotel Continental v. Burton***, 334 S.W.2d 75 (Mo. 1960). In ***Hotel Continental***, the Court upheld the Commission's determination that the gross receipts taxes collected by a utility and paid over to taxing authorities was different in nature from other operating expenses such that it was permissible to establish a Tax Adjustment Clause ("TAC") that provided for the automatic adjustment of rates between rate cases to reflect intervening changes in the rate of the gross receipts tax. ***Hotel Continental***, 334 S.W.2d at 79. In ***UCCM***, the Court distinguished ***Hotel Continental***, and held that the fuel costs incurred by electric utilities were not different in nature from other operating expenses and that a Fuel Adjustment Clause ("FAC") that provided for the automatic adjustment of rates between rate cases to reflect changes in the cost of fuel was therefore not permissible. ***UCCM***, at 51. Finally, in ***Midwest Gas Users' Association***, *supra*, the Western District of the Missouri Court of Appeals revisited ***Hotel Continental*** and ***UCCM***'s review and analysis of that case and upheld the Commission's use of the "Purchased Gas Adjustment (PGA)/Actual Cost Adjustment (ACA)" system for natural gas costs.

20. It may be that the impact of the TCJA is like the gross receipts tax analyzed in ***Hotel Continental*** and the natural gas commodity costs considered in ***Midwest Gas Users' Association*** and that the Commission may order a reduction in utility rates without the necessity of considering all relevant factors in an extended

general rate case. In *Midwest Gas Users' Association*, the Court applied the principles gleaned from *Hotel Continental* and *UCCM* to the PGA/ACA and determined that it was permissible: it was not single-issue ratemaking because the commodity price of natural gas does not include labor or other components subject to management economizing, so that savings in one area can offset cost increases in another. Much of the commodity price of gas is set by the FERC and simply passed on to customers much like the gross receipts tax considered in *Hotel Continental*. It was not retroactive ratemaking because the price already charged and paid was not changed and any shortfall was collected prospectively from future customers. It did not violate the filed-rate doctrine because the utility was required to put an actual rate in the tariff, not merely a formula as was the case with the FAC in *UCCM*. Any customer could examine the tariff and see how much she would have to pay for gas service. Finally, it was not an abdication of the Commission's regulatory duties because, in the ACA phase, the amounts paid for gas and charged to customers were subject to audit, prudence review and true-up by the Commission. For these reasons, the PGA/ACA was approved. *Midwest Gas Users' Association*, 479-483.

WHEREFORE, on account of all of the foregoing, Staff prays that the Commission will:

(A) Giving such notice as it deems appropriate, open a rate case on its own motion in order to investigate the propriety of Empire Electric's rates for electric service in light of the enactment of the TCJA, and to set the prospective just and reasonable rates therefor;

(B) Make Staff, the Office of the Public Counsel, and all intervenors that were parties to Empire Electric's last rate case parties to the new rate case;

(C) Direct Empire Electric to show cause, if any it has, why the Commission should not forthwith order it to file tariffs reducing its rates for every class and category of service by the percentage reduction in the federal-state effective income tax rate stated in this *Motion*;

(D) Direct Empire Electric to quantify and track all TCJA rate impacts from January 1, 2018, going forward;

(E) Direct Empire Electric to quantify and track its excess protected and unprotected ADIT for future flow back to ratepayers and to advise the Commission how best that flow-back might be accomplished;

(F) Direct Empire Electric to advise the Commission whether or not the impact of the TCJA is like the gross receipts tax analyzed in *Hotel Continental* and the natural gas commodity costs considered in *Midwest Gas Users' Association* and whether the Commission may order a reduction in utility rates without the necessity of considering all relevant factors in an extended general rate case;

(G) Direct Empire Electric to identify and quantify all other impacts of the TCJA not already discussed herein;
and grant such other and further relief as the Commission determines is just in the circumstances.

Respectfully submitted,

/s/ Kevin A. Thompson

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CERTIFICATE OF SERVICE

I certify that a true and correct copy of the foregoing was served electronically upon Empire Electric and the Office of the Public Counsel on this 16th day of February, 2018.

/s/ Kevin A. Thompson