

Exhibit No.:
Issue(s): *Incentive
Compensation, Rate
Case Expense, Inflation
Bonuses, Advertising
Expense, Income
Eligible Weatherization
Program*
Witness: *Lindsey Smith*
Sponsoring Party: *MoPSC Staff*
Type of Exhibit: *Surrebuttal / True-Up
Direct Testimony*
Case No.: *ER-2024-0189*
Date Testimony Prepared: *September 10, 2024*

MISSOURI PUBLIC SERVICE COMMISSION

FINANCIAL & BUSINESS ANALYSIS DIVISION

AUDITING DEPARTMENT

SURREBUTTAL / TRUE-UP DIRECT TESTIMONY

OF

LINDSEY SMITH

EVERGY MISSOURI WEST, INC.,

d/b/a Evergy Missouri West

CASE NO. ER-2024-0189

*Jefferson City, Missouri
September 10, 2024*

TABLE OF CONTENTS OF
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7	EXECUTIVE SUMMARY	1
8	SURREBUTTAL TESTIMONY.....	2
9	INCENTIVE COMPENSATION.....	2
10	RATE CASE EXPENSE	2
11	INFLATION BONUSES.....	6
12	ADVERTISING EXPENSE.....	9
13	TRUE UP DIRECT TESTIMONY	11
14	INCENTIVE COMPENSATION.....	11
15	INCOME ELIGIBLE WEATHERIZATION PROGRAM.....	11

1 **SURREBUTTAL TESTIMONY**

2 **INCENTIVE COMPENSATION**

3 Q. Did EMW file rebuttal testimony regarding incentive compensation?

4 A. Yes. According to the rebuttal testimony of EMW witness Ronald Klote,
5 EMW contends that a three-year average should be used for the capitalization rate that is
6 applied to the average incentive compensation calculation. For both long-term and short-term
7 capitalized incentive compensation, EMW also proposes, for consistency purposes, to amortize
8 the disallowed amounts, included in rate base, over a 20-year period by using a 5% rate in the
9 depreciation annualization.

10 Q. Does Staff agree with EMW's explained above?

11 A. Staff's position is to sync the capitalization rate methodology applied to the
12 average incentive compensation calculation with the methodology used to annualize payroll.
13 The reasons supporting Staff's methodology can be found in Sydney Ferguson's surrebuttal
14 testimony regarding payroll expense.

15 Regarding the rate base disallowance, Staff finds that using a 5% rate in the depreciation
16 annualization as well as in calculating the associated accumulated depreciation reserve for both
17 long-term and short-term capitalized incentive compensation over a 20-year period for
18 consistency purposes is reasonable. The 5% rate is reflected in Staff's incentive compensation
19 true-up adjustment.

20 **RATE CASE EXPENSE**

21 Q. What is Staff's recommendation for rate case expense in direct testimony?

22 A. In the current case, Staff recommends a three-year normalization of rate case
23 expenses incurred in ER-2022-0130, ER-2018-0146, and ER-2016-0156 after Staff's

1 recommended 50% sharing. Staff has also included normalized depreciation study and line loss
2 study expenses with no sharing.

3 Q. What is EMW's recommendation for rate case expense?

4 A. EMW witness Linda Nunn states in rebuttal testimony: "[t]he Company does
5 agree with using an average of the expenses over the last three cases, but disagrees with
6 taking 50% of those averaged costs".

7 Q. Does Staff agree with EMW's recommendation for rate case expense?

8 A. No, Staff continues to recommend sharing of rate case expense. Sharing 50%
9 of discretionary rate case expenses between customers and shareholders assigns the cost to the
10 beneficiaries of a rate case and encourages cost control for rate case expense.

11 Q. How does the rate case process benefit ratepayers and shareholders?

12 A. The rate case process allows the Commission to ensure consumers receive safe
13 and adequate service at just and reasonable rates and allows the Commission to ensure the
14 utility's shareholders have the opportunity to earn a reasonable return on their investment.

15 Q. Has the Commission acknowledged in any Report and Orders that ratepayers
16 and shareholders should share rate case expense?

17 A. Yes. The Commission has consistently supported some version of rate case
18 expense sharing in the last 10 years. Aside from any stipulations and agreements where rate
19 case expense was settled among the parties, the Commission has addressed rate case expense
20 sharing in the Empire general rate case docket ER-2019-0374 and in the Evergy Missouri Metro
21 (formerly Kansas City Power & Light ("KCPL")) general rate case docket ER-2014-0370.

1 Q. Did the Commission decision from the Report and Order in a previous Evergy
2 Missouri Metro rate case discuss the reasonableness of shareholders sharing a portion of rate
3 case expense?

4 A. Yes. The Commission decision beginning on page 70 of the Report and Order
5 from Case No. ER-2014-0370 provided a foundation for the reasonableness of shareholders
6 sharing a portion of rate case expense:

7 Instead, the Commission will consider whether it is reasonable that
8 KCPL shareholders cover a portion of KCPL's rate case expense. In one
9 sense, rate case expense is like other common operational expenses that
10 a utility must incur to provide utility service to customers. Since
11 customers benefit from having just and reasonable rates, it is appropriate
12 for customers to bear some portion of the utility's cost of prosecuting a
13 rate case.

14 However, rate case expense is also different from most other types of
15 utility operational expenses, in that 1) the rate case process is adversarial
16 in nature, with the utility on one side and its customers on the other;
17 2) rate case expense produces some direct benefits to shareholders that
18 are not shared with customers, such as seeking a higher return on equity;
19 3) requiring all rate case expense to be paid by ratepayers provides the
20 utility with an inequitable financial advantage over other case
21 participants; and 4) full reimbursement of all rate case expense does
22 nothing to encourage reasonable levels of cost containment.

23 The Commission has the legal authority to apportion rate case expense
24 between ratepayers and shareholders. Under Missouri law, the
25 Commission must set just and reasonable rates, and rates that include all
26 of the utility's rate case expense, for the reasons set forth above, may not
27 be just and reasonable.

28 Q. Did the Commission's Report and Order from the Empire electric utility docket
29 in Case No. ER-2019-0374 address the 50/50 split of rate case expense?

30 A. Yes. On page 83 of the Commission's Amended Report and Order states:

31 Therefore, it is just and reasonable that the shareholders and the
32 ratepayers, who both benefited from the rate case, share in the rate case
33 expense. The Commission finds that in order to set just and reasonable
34 rates under the facts in this case, the Commission will require Empire's

1 shareholders to cover a portion of Empire's rate case expense.
2 The Commission will assign Empire's discretionary rate case expense to
3 both ratepayers and shareholders based upon a 50/50 split.

4 Q. Has the Missouri Court of Appeals acknowledged that ratepayers and
5 shareholders should share rate case expense?

6 A. Yes, they have. Evergy Missouri Metro appealed the Commission's rate case
7 expense decision from Case No. ER-2014-0370 to the Missouri Western District Court of
8 Appeals. The court's decision in *Kansas City Power, Apel v. Mo Public Serv, Res, WD79125*
9 (2016), affirmed the Commission's decision and acknowledged rate case expense sharing
10 between ratepayers and shareholders. Page 31 of the decision states:

11 Regarding rate case expenses, the PSC recognized that rate cases are
12 both beneficial to shareholders of a utility and also utility customers, but
13 in different ways. Shareholders benefit from the rate case expenses as
14 the costs are incurred to increase the utility's revenues and profitability.
15 Customers benefit by having a healthy utility. In this case, the PSC
16 found that a standard prudence review of each expenditure in the rate
17 case would not be possible and, even if conducted, would not provide a
18 strong incentive for KCPL to impose cost controls because the utility
19 holds all the information needed to identify imprudence. Therefore, the
20 PSC did not identify any line item expense as explicitly imprudent,
21 but rather found that the costs incurred by KCPL, as a whole, in pursuing
22 its litigation strategy that in large part inured to the sole benefit of
23 shareholders, were imprudent. An expert testified for the Staff of the
24 PSC that, in similar context, highly discretionary costs that do not benefit
25 customers, such as charitable donations, political lobbying expenses,
26 and incentive compensation tied to earnings per share are typically
27 allocated entirely to shareholders.

28 Q. In Staff's payroll expense included in cost of service, did Staff include in-house
29 legal counsel and regulatory employees employed by EMW?

30 A. Yes.

31 Q. Is payroll expense shared between ratepayers and shareholders?

1 A. No. Payroll is included in cost of service and paid for solely by ratepayers.
2 In addition to legal counsel employees of EMW, several EMW witnesses assisting on rate cases
3 are employed by EMW and their payroll is included in cost of service paid for solely
4 by ratepayers.

5 Q. Has EMW provided written testimony or evidence in this case to prove their rate
6 case expenses are prudent and solely for the benefit of ratepayers to the extent there should be
7 no sharing?

8 A. No. EMW witness Linda Nunn's rebuttal testimony only claims that without
9 periodic rate cases, the shareholders would not have the opportunity for a reasonable return that
10 they are supposed to be afforded, and it would make no sense to disallow, in the absence of any
11 evidence or allegation of imprudence, costs which benefit both the shareholders and the
12 customers. This does not prove their rate case expenses are prudent, and EMW holds the
13 information that would be needed to identify imprudence. It would be an expensive,
14 far-fetched, and exhaustive effort to try and peel away the onion layers of rate case expense and
15 EMW's rate case strategy to determine a level of imprudence that would ultimately still be
16 subjective. The discovery process would also impact EMW with added employee time and
17 distracted effort. Rate case expense sharing has consistently been applied to EMW because of
18 the heightened level of rate case expense they choose to incur. The 50% sharing approach is
19 the most commonly implemented method that allows for some type of cost control for rate
20 case expense.

21 **INFLATION BONUSES**

22 Q. What is Staff's recommendation regarding inflation bonuses?

1 A. Staff recommends a full removal from the cost of service of one-time inflation
2 bonuses paid during the test year.

3 Q. What is EMW’s recommendation for inflation bonuses?

4 A. While EMW did not identify the bonuses in direct testimony or explicitly request
5 recovery of the cost, it is Staff’s understanding that EMW recommends an amortization over a
6 4-year period of the inflation bonuses that were paid in February 2023, thus one-fourth of the
7 total EMW allocated amount is included in the cost of service in the direct filing.

8 Q. Does Staff agree with EMW’s recommendation?

9 A. No. Staff recommends that the inflation bonuses paid in February 2023 should
10 be removed from the cost of service.

11 Q. What is Staff’s reasoning behind their recommendation?

12 A. First, inflation bonuses are not a reoccurring cost of doing business thus the
13 bonuses should not be including in ongoing rates. These bonuses were a one-time cost for
14 EMW that were in response to an irregularly high economic inflationary period. In response to
15 Data Request no. 0438, EMW states, “No other bonuses specific to inflation have been
16 contemplated to date.” EMW is requesting recovery for a one-time past cost that should not be
17 reflected in on-going rates.

18 Second, the rebuttal testimony of Mr. Klote states, “[t]he inflation bonuses were
19 designed to ensure the Company’s total compensation package continued to provide employees
20 with an appropriate and consistent standard of living.” Staff already reflected all increases in
21 payroll, and incentive compensation, in its recommended revenue requirement so there is no
22 need to charge customers additional costs.

1 Third, EMW is inconsistent in its attempt to characterize the inflation bonuses as a
2 recurring cost of business but at the same time, identifies the cost for special ratemaking
3 recovery. Even when recurring costs increase in amount, ratemaking theory suggests other
4 costs have decreased to offset the increase. EMW is essentially identifying a cost increase for
5 special recovery and ignoring other offsetting changes in its cost of service.

6 Lastly, EMW's direct filing provides very little support in its testimony and workpapers
7 regarding inflation bonuses. Further, the direct testimony Ms. Nunn provided conflicts with
8 the rebuttal testimony of Mr. Klote. In Ms. Nunn's direct testimony, she states, "[t]hese costs
9 for which the Company is not seeking recovery includes officer long-term incentive
10 compensation, officer expense report items, and test year bonuses/severances." Ms. Nunn
11 claims the costs for inflation bonuses are costs which EMW is not seeking recovery for in direct
12 testimony. However, Mr. Klote's rebuttal testimony claims EMW is requesting recovery for
13 these costs amortized over a 4-year period. EMW's CS-11 workpaper supporting its direct case
14 grouped these bonuses into the same category as severance costs and categorized the adjustment
15 to "Remove non-recoverable items from the test year." The only inferred request made by
16 EMW in its direct case was describing the test year adjustment as "Amortize bonuses &
17 severance (excluding Executives) over 4 years."

18 These inconsistencies caused Staff to submit Data Request 0409 in order to discover the
19 nature of the bonuses, clarify EMW's position on cost recovery, and the exact dollar amount
20 for the inflation bonuses separate from severance payments. Generally, if EMW requests cost
21 recovery for a non-recurring expenditure, it is proper that it submit testimony as part of its
22 case-in-chief describing the cost and why it is equitable to include in the cost of service. In this
23 case, EMW did not do so.

1 For the reasons stated above, Staff recommends full removal of inflation bonuses paid
2 in the test year from the cost of service.

3 **ADVERTISING EXPENSE**

4 Q. What did Staff recommend for advertising expense in direct filing?

5 A. In its direct filing, Staff identified several advertisements that were institutional
6 advertisements, or advertisements that promoted EMW's image, specifically from the
7 YOUtility campaign. However, EMW is unable to identify the costs of each public image
8 advertisement through direct workpapers, Data Requests, or the general ledger. Therefore, in
9 its direct case Staff excluded all expenses recorded under the vendor responsible for the
10 YOUtility campaign EMW conducted during the test year period 12 months ending
11 June 30, 2023, from the cost of service. Staff also requested the Commission to order EMW to
12 change their accounting procedures for advertising to establish an auditable paper trail and a
13 transparent approach to advertising expense that bridges the information gap between the
14 booked advertising expense in the general ledger and the invoices/advertisements EMW
15 provides to support the costs.

16 Q. Have there been new developments regarding advertisement expense since
17 direct filing?

18 A. Yes. EMW witness Linda Nunn's rebuttal testimony, on page 19, stated EMW
19 was working with Staff to address concerns and "ascertain the reasoning behind the advertising
20 campaigns." This led to a meeting on August 14, 2024, where Staff and EMW met to discuss
21 general advertising expense. EMW informed Staff that their books do not allow for Staff to
22 reach the cost of each individual advertisement EMW releases. Individual advertisement costs
23 are grouped together and recorded under full campaign costs rather than individually.

1 Although individual advertisement costs are not recorded in EMW's books, EMW was able to
2 clarify different campaign creatives under the scope of the YOUtility campaign and explained
3 to Staff how to filter through advertisements to reach a more refined adjustment for
4 advertising expense.

5 Q. Does Staff have a new recommendation for advertising expense in the current
6 rate case?

7 A. Yes. With the additional information provided by EMW, Staff was able to
8 identify two campaign creatives under the scope of YOUtility campaign that had institutional
9 advertisements in them: the ValProp Evolution and the Community Impact campaign creatives.
10 Individual advertisement costs could not be captured, but Staff found the total number of
11 advertisements in each campaign creative along with the total number of institutional
12 advertisements per campaign creative. Staff found the percentage of each campaign creative
13 considered institutional advertisements and removed that from the test year amount.

14 Q. Does Staff have a revised recommendation for advertising expense in future
15 rate cases?

16 A. Yes. Although EMW was able to clarify different campaign creatives under the
17 scope of a larger campaign, it still lumped the cost of campaigns together and made it difficult
18 for Staff to audit properly. Staff is aware that finding individual costs for each advertisement
19 would be time-consuming and expensive. Therefore, Staff now requests the Commission to
20 order EMW to change their accounting procedures for advertising and account for campaigns
21 separately along with specific advertisements in each campaign in order to establish an
22 auditable paper trail that bridges the information gap between the general ledger and

1 invoices/advertisements EMW provides to support the costs. This would allow Staff to make
2 a more refined and accurate adjustment for advertising expense.

3 **TRUE UP DIRECT TESTIMONY**

4 Q. Please identify the true-up adjustments you are sponsoring.

5 A. In Staff's true-up revenue requirement, I sponsor the true-up of incentive
6 compensation, and the income eligible weatherization program.

7 **INCENTIVE COMPENSATION**

8 Q. How did Staff modify its adjustment for incentive compensation in its
9 true-up case?

10 A. As I described in my direct testimony, Staff added an additional year (2024) to
11 its average for the Power Marketing incentive compensation plan to normalize the payouts over
12 a 4-year period, including 2021, 2022, 2023, and 2024. Staff also updated the depreciation rate
13 for both long-term and short-term capitalized incentive compensation to 5%.

14 **INCOME ELIGIBLE WEATHERIZATION PROGRAM**

15 Q. Please explain Staff's true-up adjustment for the Income Eligible Weatherization
16 Program ("IEW").

17 A. Staff updated the unspent funds balance to reflect the balance at June 30, 2024.
18 Staff included the IEW program liability as of June 30, 2024, as a deduction to EMW's
19 rate base.

20 Q. Does this conclude your Surrebuttal / True-up Direct testimony?

21 A. Yes it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Evergy Missouri West, Inc.)
d/b/a Evergy Missouri West's Request for)
Authority to Implement A General Rate)
Increase for Electric Service) Case No. ER-2024-0189

AFFIDAVIT OF LINDSEY SMITH

STATE OF MISSOURI)
)
COUNTY OF Jackson) ss.

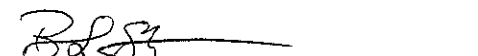
COMES NOW LINDSEY SMITH and on her oath declares that she is of sound mind and lawful age; that she contributed to the foregoing *Surrebuttal / True-Up Direct Testimony of Lindsey Smith*; and that the same is true and correct according to her best knowledge and belief.

Further the Affiant sayeth not.


LINDSEY SMITH

JURAT

Subscribed and sworn before me, a duly constituted and authorized Notary Public, in and for the County of Jackson, State of Missouri, at my office in Kansas City, on this 37th day of September 2024.


Notary Public

B. L. STIGGER
NOTARY PUBLIC - NOTARY SEAL
STATE OF MISSOURI
MY COMMISSION EXPIRES JANUARY 2, 2026
JACKSON COUNTY
COMMISSION #24332661