BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of The Empire District	)	
Electric Company's Request for	)	
Authority to File Tariffs Increasing	)	**Case No. ER-2019-0374**
Rates for Electric Service Provided	)	
To Customers in its Missouri	)	
Service Area	)	

STAFF'S RESPONSIVE BRIEF

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INTRODUCTION

Traditionally, in a general rate case, parties file Initial Briefs and Reply Briefs following an Evidentiary Hearing. In the present matter, the parties agreed to waive the Evidentiary Hearing, and the Commission approved of this action. Therefore, the parties are filing an additional brief, known as the Responsive Brief, to address certain additional matters arising from the lack of Evidentiary Hearing. This brief will respond to the Initial Briefs of the parties and also the Supplemental Testimony and Responses to Commission Questions provided by the parties along with the filing of Initial Briefs. Staff will not revisit its arguments made in its *Initial Brief*, but will reference key points where necessary to address the arguments made by other parties.

The *Global Stipulation and Agreement* is still the appropriate method for resolving all issues in this matter and ensuring that ratepayers do not experience a change at this difficult and unprecedented time in recent history. The arguments made here should in no way imply that Staff does not support the *Global Agreement* as a full and just resolution of all of the issues in this matter.

STIPULATION AND AGREEMENT

As stated in its *Initial Brief,* all of the parties to this matter, except OPC, have either signed onto or not opposed a *Global Stipulation and Agreement* ("Global Agreement" or "Agreement" or "Stipulation" or "Non-Unanimous Stipulation") in an effort to settle all issues in this matter. The *Agreement* is a just and full resolution of this case that is fair to both the ratepayers and to Empire, and the Commission should approve the *Agreement* in full, without modification.

ISSUES TO BE DECIDED BY THE COMMISSION

Staff in its *Initial Brief* outlined the issues that the Commission would need to decide based on OPC's objections to the *Global Agreement* and only if the Commission did not approve the *Agreement* in full. In their Initial Briefs, Empire and MECG addressed certain issues that Staff did not view as needing to be decided by the Commission, but to the extent that these remain at issue, Staff has included them at the end of this brief for the Commission's information.

Whitney Payne

Rate of Return—Return on Equity, Capital Structure, and Cost of Debt

a. Return on Common Equity – what return on common equity should be used for determining rate of return?

b. Capital structure – what capital structure should be used for determining rate of return?

c. Cost of debt – what cost of debt should be used for determining rate of return?

Introduction:

The rate of return ("ROR") is simply the profit returned to the Company's investors for the use of their private property – the rate base – in the public service. It is calculated using certain disputed inputs: the Return on Equity ("ROE"), the Capital Structure, and the Cost of Debt. The Company seeks the highest ROR it can get and OPC seeks the lowest ROR it can get. Only Staff provides the Commission with a neutral, "best practices" perspective.

	Murray OPC	**Chari Staff**	**Hevert Empire**	**Value of This Issue[1]**
ROE Range	**9.25%** **8.50% - 9.25%**	**9.25%** **9.05% - 9.80%**	**9.95%** **9.80% -10.60%**	**$6,696,760**
Cost of Debt	**4.65%**	**4.57%**	**4.85%**	**$2,445,516**
Capital Structure --Equity --Debt:	**46.00%** **54.00%**	**52.43%** **47.57%**	**53.07%** **46.93%**	**$492,129**
ROR	**6.77%**	**7.02%**	**7.56%**	**$9,106,721**

The *Global Stipulation* resolves the ROR issues by providing for a carrying cost rate of 7.3% on the balance created by the phase-in rate mechanism to be established pursuant to § 393.155.1, RSMo., with regard to plant-in-service and other rate-base-related items. The amortization period for what is captured by the phase-in mechanism will be determined in the next general base rate proceeding. Staff urges the Commission to resolve these issues in accordance with the *Global Stipulation.* However, if that resolution is not acceptable to the Commission, then Staff urges the Commission to adopt Staff's positions on each of the Cost of Capital issues.

Return on Equity:

The Commission should reject the bloated and excessive ROE proposed by Company expert Robert Hevert. As Staff explained in its *Initial Brief,* Mr. Hevert's recommendation is based upon flawed analyses in which the subjective components –

[1] *See* the *Final Reconciliation,* filed April 10, 2020. The values shown reflect the difference between the Company position and the Staff position. Not shown is an adjustment for capital structure impact on interest expense deduction.

the growth rate and the market risk premium – have been grossly inflated in order to produce unreasonably high results.[2] OPC's *Initial Brief* raised these same criticisms of Mr. Hevert's analyses and recommendation. On this issue, at least, Staff and OPC are aligned and both recommend an ROE of 9.25%.[3]

Once the matter of the manipulation of the inputs is understood, the issue of ROE – deceptively complex at first glance – becomes quite simple. The fundamental question, after all, is simply "What is the lowest return that will induce investors to invest?" This question is made more obscure in instances, like this one, where the subject company is wholly-owned by a parent and its shares are thus not traded. However, the shares of the various proxies are trading at values far below that proposed by Mr. Hevert. In its *Initial Brief,* Empire stated, "none of the arguments raised by Staff witness Chari's or OPC witness Murray's rebuttal testimonies caused Mr. Hevert to revise his recommendation."[4] That's hardly surprising, given that Mr. Hevert is well-paid for his testimony. His ability to work in the future would be seriously compromised were he to revise his recommendation downward in the face of criticism by opposing party experts.

Empire's *Initial Brief* quotes comments from Mr. Hevert's *Surrebuttal Testimony,* to the effect that the ongoing economic and financial crisis caused by the pandemic requires a *higher* ROE than would otherwise be the case.[5] Staff responds that the Commission in this case is setting rates that will endure for perpetuity if not changed in

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[2] As explained in *Staff's Initial Brief,* the analytical methods employed by the financial analysts include an objective, market-based component and a subjective, judgmental component. It is the latter that is subject to manipulation to obtain a desired result.
[3] Although Mr. Murray makes it clear that he considers this value to be greatly in excess of the minimum return actually required by investors.
[4] *Empire's Initial Brief,* P. 6.
[5] *Id.,* pp. 7-8.

another rate case. It is thus far too early to discern just what long-term response the present crisis requires in terms of an ROE. For the present case, the Commission should either resolve these issues in accordance with the *Global Stipulation* or adopt the 9.25% ROE proposed by Staff and OPC.

Capital Structure:

The Capital Structure issue has to do with the relative proportion of each type of capital in the Company's capital structure. Equity is more expensive than debt, and so it follows that OPC argues for a lower proportion of equity and the Company argues for a higher proportion of equity.

OPC criticizes Staff for its treatment of $395 million in debt held by Liberty Utility Financing, GP1 ("LUF"), and guaranteed by Empire's parent, LUCo. .[6] LUF is LUCo's financing affiliate responsible for issuing debt for use by all the regulated subsidiaries of Algonquin Power and Utility Corp. ("APUC"), the parent company of LUCo. Staff originally believed that this debt was attributable to APUC's regulated and non-regulated operations, a mistake Staff corrected in Mr. Chari's *Rebuttal Testimony*.[7] Staff now understands that this debt is attributable only to all of APUC's regulated subsidiaries..[8] Nonetheless, it would be entirely improper to assign this whole amount to Empire.[9] As Mr. Chari testified, "The debt should not be included in a capital structure to be used for the purpose of ratemaking because it would be unfair for both LUCo and Empire to

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[6] *OPC's Initial Brief,* pp. 20-21.
[7] Ex. 108*: Rebuttal Testimony of Peter Chari*, Pp. 15-16.
[8] *Id.*
[9] *Id.;* and *See* Ex. 108*: Rebuttal Testimony of Peter Chari*, Pp. 12-13.

use a capital structure that is not representative of the capital they use in their operations."[10] For that reason, Staff's proposed Capital Structure is unchanged.

Cost of Debt:

The Commission should adopt Staff's Cost of Debt rather than OPC's or Empire's. Staff adjusted its recommended Cost of Debt downward in consideration of a point raised by Mr. Murray.[11] Staff's recommended Cost of Debt, 4.57%, is the appropriate figure to use.

Conclusion:

The use of appropriate inputs, as recommended by Staff, results in a just and reasonable ROR for Empire of 7.02%. These inputs include a capital structure of 52.43% common equity and 47.57% long-term debt, an authorized ROE of 9.25%, and a cost of debt of 4.57%. As explained by Staff in detail in its Initial Brief, and restated above, the recommendations offered by Mr. Hevert and Mr. Murray should be discarded because they have been manipulated to skew either high or low, depending on the goals of the respective party.

Kevin A. Thompson

Rate Design, Other Tariff and Data Issues

Staff supports the *Global Stipulation and Agreement* as a full resolution of all of the issues in this matter. To the extent that the Commission does not approve the *Global Stipulation and Agreement* as a full resolution of all issues, Staff incorporates its

[10] Ex. 108*: Rebuttal Testimony of Peter Chari*, Pp. 16.
[11] Ex. 130*: Surrebuttal Testimony of Peter Chari*, Pp. 13-14.

positions as stated in Staff's Position Statements[12] and *Staff's Initial Brief*,[13] as well as the following response to arguments made by MECG regarding certain aspects of rate design.

<u>*Class Cost of Service ("CCOS")*</u>

Staff addressed in its *Initial Brief* the concerns it has with the underlying data used to develop the different CCOS Studies submitted in this case.[14] Staff recommends in the event the Commission does not approve the *Global Stipulation and Agreement*, that the Commission order Empire to adopt Staff's recommended class revenue allocation and rate design variations. Staff's recommendations are most appropriate when considering (1) the magnitude of the overall revenue requirement change contemplated in this case, (2) the results of Staff's CCOS Study in File No. ER-2016-0023, (3) the likely future investment in metering systems, (4) the intent to phase out the overly simplistic PFM rate schedule and transition all customers to modern time-variant rate designs, and (5) an overall goal of minimizing customer impacts associated with unnecessary bill swings from case to case. [15]

The following generally addresses these sub-issues together:

z. How should production-related costs be allocated to each rate class.

aa. How should plant accounts 364, 366 and 368 be classified?

bb. How should primary and secondary distribution plant facility costs be allocated to each rate class?

cc. How should General plant facility costs be allocated to each rate class?

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[12] Staff's Statement of Positions, filed April 17, 2020.
[13] *See Staff's Initial Brief*, Pp. 23-33.
[14] *Staff's Initial Brief*, Pp. 24-25.
[15] Ex. 136, *Surrebuttal testimony of Sarah L.K. Lange*, P.13.

In general, Staff does not recommend the Commission order a specific allocation method as the appropriate method will vary from case-to-case with utility characteristics and data availability.[16] However, in its Initial Brief, MECG mentioned at length that Staff's recommended allocation methods have changed over the years.[17] This is a fact that Staff will concede: Staff has not been stagnate on this issue. As the vertically-integrated utility landscape has shifted from standalone entities to more active participants in increasingly diverse and active energy and capacity markets, Staff's allocation recommendations have changed. Staff continues to look for the best allocation method to fit these changes as they happen.

Furthermore, MECG's assertion that other jurisdictions have not yet adopted Staff's recommended approach is not persuasive.[18] The basis for Staff's recommended approach is rooted in the recently-published RAP Manual.[19] That this approach is not yet widespread is illustrative of the fact that very few, if any, jurisdictions have had the opportunity to consider it.

While some parties may wish to hone the Commission's attention in on various allocation methodologies used to develop the CCOS Studies in this matter, Staff does not believe that is useful or necessary given the circumstances.[20] The three CCOS Studies submitted by Staff, Empire, and MECG in this matter, utilizing different allocation methodologies, still reach similar conclusions regarding the directions of the shifts

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[16] *See Staff's Position Statement*, P. 13, filed April 17, 2020.
[17] *Initial Post Hearing Brief of Midwest Energy Consumers Group*, Pp. 23-24.
[18] *Id.*
[19] *See* Electric Cost Allocation for a New Era, A Manual, Schedule SLKL-d2, page 20-276. Appendix 3 of Ex. 104.
[20] *See Staff's Initial Brief*, Pp. 24-25 for a discussion of Staff's concerns regarding the unreliability of the underlying data used to develop the CCOS Studies submitted in this matter, which ultimately led Staff to conclude that no CCOS Study submitted is of the quality typically used for ratemaking purpose.

between and among customer classes.[21] But, for the reasons stated above, Staff's recommended revenue allocations and rate design variations, presented in Staff's CCOS Study, are most appropriate in the circumstances, and in the event the Commission does not accept the *Global Stipulation and Agreement*, Staff recommends the Commission order Empire to adopt Staff's revenue allocations and rate design variations.[22]

<u>*Revenue Allocation*</u>

d. How should Empire's revenue requirement be allocated amongst Empires' customer rate classes (class revenue responsibilities)?

r. How should any revenue requirement increase or decrease be allocated to each rate class?

In its Initial Brief, MECG acknowledges the terms of the *Global Stipulation and Agreemen*t, of which MECG is a signatory, results in no change to Empire's overall revenue requirement.[23] Nevertheless, MECG goes on to argue that if the Commission orders ***no change*** to Empire's overall revenue requirement, as contemplated in the *Global Stipulation and Agreement*, or if the Commission orders a ***reduction*** to Empire's overall revenue requirement, as was argued by some parties in this matter, the Commission should order an ***increase to the residential customer class***.[24] Specifically, in the event the Commission orders no change to Empire's overall revenue

[21] *See* Ex. 104, *Staff Direct Report – Class Cost of Service*; Empire CCOS- Ex.26, *Direct Testimony of Timothy S. Lyons*.; MECG CCOS- Ex. 650, *Direct Testimony of Kavita Maini*.
[22] MECG's presentation of Staff's results indicates the same ROE is presented by each rate schedule within the studied rate class for consolidated classes. This is not an accurate presentation as Staff did not study those rate schedules on a stand-alone basis. For example, it is not reasonable to conclude that CB and SH are providing the same return, nor that GP and TEB are providing the same return.
[23] *Initial Post Hearing Brief of Midwest Energy Consumers Group*, P. 39.
[24] *Id.*

requirement, again, as contemplated in the *Global Stipulation and Agreement*, MECG is advocating the Commission still order a 4.2% increase to the residential customer class.[25] Such an increase to the residential customer class was not agreed upon by the signatories to the *Global Stipulation and Agreement*, is not supported by the evidence presented in this case,[26] would not result in just and reasonable rates,[27] and should be rejected by the Commission.

In the event the Commission accepts the terms of the *Global Stipulation and Agreement* as a full resolution, Staff believes MECG's request for the Commission to order an increase to the residential class is irrelevant. No term or provision in the *Agreement* contemplates an increase to the residential class.[28] Furthermore, in the event the Commission does not accept the *Agreement* as a full resolution, but finds the evidence before it supports either an increase, no change, or decrease to Empire's overall revenue requirement, Staff recommends the Commission adopt Staff's recommended allocations rate designs as presented in testimony and described in *Staff's Initial Brief*.[29] As demonstrated by Staff's analysis of Customer Bill Histories, while MECG's recommended residential class increase comes with the stated intent to benefit the commercial and industrial rate class customers,[30] when coupled with the recommended

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[25] *Id.*
[26] *See* Ex. 104, *Staff Direct Report – Class Cost of Service*; *Staff's Initial Brief*, Pp. 23-33.
[27] Section 393.130, RSMo, in pertinent part, requires a utility's charges to be "just and reasonable" and not in excess of charges allowed by law or by order of the commission. Section 393.140, RSMo, authorizes the Commission to determine "just and reasonable" rates. A "just and reasonable" rate is one that is fair to both the utility and its customers; ***St. ex rel. Valley Sewage Co. v. Pub. Serv. Comm'n,*** 515 S.W.2d 845 (Mo. App., K.C.D. 1974).
[28] *See Global Stipulation and Agreement*, filed April 15, 2020.
[29] *Staff's Initial Brief*, Pp. 23-33.
[30] *Initial Post Hearing Brief of Midwest Energy Consumers Group*, P. 8: "..MECG addresses several key issues that will help guide the Commission in its efforts to make Empire's industrial rates more competitive."

MECG rate designs for those rate schedules, only very specific customers would see any benefit, exacerbating intraclass pricing disparities[31] and potentially decreasing the rate paid by some customers for energy below the cost of obtaining that energy from the SPP integrated market. Staff's allocation and rate design recommendations in this matter were not developed with the intent to benefit any particular class of customers, and specifically account for maintaining a customer's responsibility for the cost of the energy obtained at market to serve that customer.[32]

Jamie Myers

WNR and SRLE Adjustment Mechanisms

a. Should the Commission approve, reject, or approve with modifications Empire's proposed Weather Normalization Rider?

As the joint position of the Signatories of the *Global Stipulation* is to approve the SRLE as modified and described in the *Global Stipulation*, and Empire has stated that, in the event the *Global Stipulation* is not approved, the Commission should order Staff's' SRLE with four modifications,[33] and not the WNR, this issue is moot.

b. Is it lawful for the Commission to authorize Empire to implement a Sales Reconciliation to Levelized Expectations ("SRLE") mechanism, such as those Staff and Empire are proposing in this case?

c. Should the Commission adopt Staff's Sales Reconciliation to Levelized Expectations Proposal ("SRLE") or approve the SRLE with modifications as suggested by the Company?

Specifically, regarding MECG's recommended 4.2% for the residential class "Such a movement would lead to a 4.2% increase for the residential class and improve the competitiveness of all commercial and industrial classes." P. 38.

[31] Ex. 121, *Rebuttal testimony of Sarah L.K. Lange*, Pp.15-16.

[32] Ex. 104, *Staff Direct Report – Class Cost of Service*, Pp. 17-22.

[33] *Initial Brief of the Empire District Electric Company,* P. 15.

The Commission can, and should, lawfully adopt the SRLE as described in the *Global Stipulation*. The basis for that SRLE is the empirical analysis that Staff performed when designing the Staff SRLE. From this factual groundwork, Staff designed a rate stabilization mechanism (RSM) that effectuates the intent of Section 386.266.3, as well as balances the interest of the Company and its customers.

As stated in *Staff's Initial Brief*, the Commission can lawfully order the SRLE, much like it lawfully ordered Union Electric Company d/b/a Ameren Missouri's Volume Indifference Reconciliation to Normal Rider (VIRN), Spire's weather normalization rider (WNR), and Liberty's WNR, Liberty Utilities (Midstates Natural Gas) Corp. d/b/a Liberty Utilities' weather normalization adjustment rider (WNAR).[34] Section 386.266.3 does not impose special or different requirements upon electric utilities requesting a RSM that gas utilities do not face. OPC's arguments do exactly that, however. First, OPC argues that the Commission is not legally authorized to implement an RSM without rules in place.[35] Neither gas nor electric utilities have standalone RSM application requirements. Yet, as noted in *Staff's Initial Brief*, a general rate case is the only avenue for a utility to request a SRLE mechanism,[36] these application requirements also govern the SRLE request. It was under those application requirements that the Commission approved the three gas utilities' RSMs.[37] OPC supported two of those RSMs, even though no standalone gas RSM rules had been promulgated.[38] RSMs are not entitlements, like all single issue rate

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[34] *Staff's Initial Brief*, P. 37-38.
[35] *The Office of the Public Counsel's Initial Brief*, P. 28.
[36] 386.266(5) RSMo.
[37] *See* Case No. GR-2019-0077, Order Approving Stipulations and Agreements, and Compliance Tariff, effective September 1, 2019, Case No. GR-2017-0215 and GR-2017-0216, Amended Report and Order, issued March 7, 2018, and Case No. GR-2018-0013, Order Approving Stipulation and Agreement.
[38] *See* Case No. GR-2018-0013, Unanimous Stipulation and Agreement, filed May 24, 2018 and See Case No. GR-2019-0077, First Amended Non-unanimous Stipulation and Agreement, filed July 18, 2019.

making mechanisms,[39] but there is not a requirement for a utility to show it is not meeting its authorized ROE by some numerical value. Instead, the Commission should take all evidence in a case into account to determine if the authorization of a RSM is in the best interest of the utility and its customers. The Commission can lawfully authorize a RSM.

OPC also specifically claims that the SRLE is unlawful as it captures more than conservation impacts.[40] The SRLE mechanism does assume a broad interpretation of conservation.[41] It includes the adoption of energy efficiency measures whether funded by ratepayers or not, as well as any other factor inducing changes to the cost of energy sold.[42] That would include customer decisions and actions that reduce the consumption of energy, and also addresses the impact of what might be referred to as "negative conservation," or customer decisions and actions that increase the consumption of energy.[43] This same interpretation of conservation is also included in the recently-approved, non-appealed Ameren Missouri VIRN for its gas utility business.[44] OPC was a signatory to the stipulation that authorized Ameren Missouri's use of VIRN with the exact same impacts as the SRLE being captured.[45] Assumptions about how and why consumers use energy is not a foreign concept in Missouri ratemaking. A prime example is deemed savings for Missouri Energy Efficiency Investment Act (MEEIA) plans. When savings are deemed, it assumes customers are using energy efficiency measures in a certain manner, and that energy efficient measures were purchased solely for

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[39] *Id.*
[40] *Id.* P. 28.
[41] Ex. 160, *Supplemental Testimony of Robin Kliethermes*, P. 4.
[42] *Id.*
[43] *Id.*
[44] *Id.*
[45] *See* Case No. GR-2019-0077, First Amended Non-unanimous Stipulation and Agreement, filed July 18, 2019.

conservation. In MEEIA, as in a RSM, there is no guarantee that only reductions due to conservations are considered. Outside of surveying every customer on the reasons for each usage impacting action taken in a month, there is no perfect accounting method. And even surveying customers would not guarantee 100% accuracy, as imperfect recollection of why an action was taken, such as not recalling if usage in a certain period was lower due to conservation or due to a momentary change in schedule causing a member of the customer's household to be out of the house more than typical. OPC's standard would prohibit any utility from ever utilizing a RSM, an outcome the legislation clearly did not intend.

As demonstrated in Staff's *Class Cost of Service Report* and workpapers, Staff reviewed empirical data to determine a fact based block of normal usage. Based on Empire's cumulative frequency distribution data, the level of usage per customer per month that is constant all year is 400 kWh; therefore, this block can be reasonably assumed to be unaffected by weather or conservation.[46] The selection of the 400kWh level balances the opportunity for additional revenues associated with customer growth (and retaining customer risk associated with customer losses) with covering the changes in gross usage associated with the impacts of weather and conservation pursuant to the statute.[47] Staff repeated this analysis for small business classes, and reviewed the number of customers taking service on the CB and SH rate schedules per level of usage, as CB stand-alone, SH stand-alone, and with the classes combined.[48] The maximum level of consistent usage was 700 kWh per customer per

[46] *Staff Class Cost of Service Report*, P. 6 – 7.
[47] *Surrebuttal Testimony of Sarah L.K. Lange*, P. 2.
[48] *Staff Class Cost of Service Report*, P. 8.

month under all three approaches.[49] The SRLE works by, on an annual basis, reconciling the revenues realized from sales in excess of 400 or 700 kWh per customer per month, less the FAC base factor and any other applicable riders or rates charged or credited on a per-kWh basis to the revenues that were assumed to be realized in aggregate from those sales, less the FAC base factor and any other applicable riders or rates charged or credited on a per-kWh basis.[50] This aggregate amount will be trued-up against actual sales on an annual basis.[51] So if an atypically mild winter is experienced in the same annual period as an atypically warm summer, the resulting SRLE adjustment will net these offsetting impacts.[52] A similar approach has been working for Ameren Gas and its VIRN, which OPC supported.

Finally, OPC points to the estimated bill issue as a reason to deny the SRLE.[53] The SRLE actually trues-up the over or under estimation of normalized residential billing determinants used to set rates in this case, which is a benefit to customers.[54] Estimated bills are more problematic for the WNR.[55] The SRLE is an annual adjustment, while the WNR is a monthly "as the meter is read" adjustment.[56] Annual numbers inspire greater confidence for various reasons. First, the SRLE as modified by the *Global Stipulation* is based on Staff's billing determinants at the time of true-up.[57] This is because Staff's recommended billing determinants since its test period contains fewer estimated bills.[58]

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[49] *Id.*
[50] *Id.* P. 11-14.
[51] *Id.* P. 12.
[52] *Id.*
[53] *The Office of the Public Counsel's Initial Brief*, P. 29.
[54] Ex. 135, *Surrebuttal and True-Up Direct Testimony of Robin Kliethermes*, P. 4.
[55] *Id.* P. 4-5.
[56] *Id.*
[57] *Id.*
[58] *Id.*

At that point in the test year, almost all the meter reads are known, and more importantly, since meters are supposed to be read every three months even when estimated, Staff's annual adjustment will be less impacted by intermediate reads.[59] An accurate meter read every three months is more than sufficient for the SRLE to work.[60] Finally, it appears new information from Empire may change the level of estimated bills included in Staff's test year period.[61] During discussions with Empire, Empire asserts it recently discovered that the data originally provided to Staff contained errors and double counted certain customer bills.[62] Empire stated that it is reviewing all of the information and will provide supplemental responses to data requests 255 and 246 with the correct level of estimated bills, but Staff has yet to receive updates.[63] The lessened magnitude of estimated bills provide more confidence in the accuracy of Staff's billing determinants relied on for the SRLE.[64]

The Commission should approve the modified SRLE contained in the *Global Stipulation*. If the Commission does not approve the *Global Stipulation*, Staff recommends approval of Staff's original SRLE as filed in testimony. Staff does not recommend implementing Empire's modifications 1 and 4, as found on pages 15 to 17 on its Initial Brief. For modification 1, an adjustment to address the partial loss of new customer and sales revenues, Staff believes changing the line extension tariff is a superior method of handling this issue[65]. Customer growth or customer losses are not

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[59] *Id.*
[60] *Id.*
[61] *Rebuttal to Supplemental Testimony of Robin Kliethermes*, P. 1-2.
[62] *Id.*
[63] *Id.*
[64] *Id.* P. 4.
[65] Ex. 136, *Surrebuttal Testimony of Sarah L.K. Lange*, P. 3.

eligible for protection under 386.266.3 RSMo, but the selection of the 400kWh level represents balancing the opportunity for additional revenues associated with customer growth (and retaining customer risk associated with customer losses) with covering the changes in gross usage associated with the impacts of weather and conservation pursuant to the statute.[66] Staff would not oppose a reasonable modification to Empire's "Electric Distribution Policy" tariff provisions to reduce (1) the 1,000' of overhead electric service provided at no cost to residential customers not in a subdivision pursuant to Sheet 17a, (2) the Construction Allowance made available to refund to the developers of Residential Subdivisions pursuant to Sheet 17b, and (3) the estimated revenues considered for SH & CB customers pursuant to Sheet 17c, to exclude an approximation of the assumed revenue contribution of new residential customers in excess of 400 kWh per month, and 700 kWh per month for new commercial customers.[67] This reasonable adjustment would reduce the company's exposure to incremental costs caused by the addition of distribution facilities when new customers connect to the system.[68] As for modification 4 proposed by Empire,[69] reaching back to January 2020 would be retroactive ratemaking. Finally, Staff does not believe the Commission needs to issue an order for modification 3, implementing the SRLE on a temporary basis, as proposed by Empire.[70] Parties are free to argue for, against, or anything in between regarding the SRLE in the next rate case, so no formal order from the Commission is necessary for modification 3.

[66] *Id.* P.2.
[67] *Id.*
[68] *Id.* p. 3.
[69] *Initial Brief of the Empire District Electric Company,* p. 15 – 17.
[70] *Id.*

For the reasons listed in this *Responsive Brief* and Staff's *Initial Brief*, Staff requests the Commission authorize Empire the use of the SRLE found in the *Global Stipulation*.

Nicole Mers

FAC

a. What is the appropriate incentive mechanism in Empire's FAC for sharing between Empire and its retail customers the difference between its actual and base net fuel costs?

OPC presents no evidence that an 85% / 15% sharing mechanism incentivizes more efficient fuel operations better than the current 95% / 5% sharing, and sufficient incentive exists for Empire to prudently manage its fuel and purchased power costs.

The only evidence that OPC presents supporting its contention that an 85% / 15% sharing mechanism would cause Empire to more efficiently manage its fuel and purchased power costs is that Empire's gas hedging program experienced losses under the current 95% / 5% sharing mechanism.[71] OPC fallaciously claims that the "95/5 sharing was unable to dissuade Empire from altering its hedging protocols,"[72] although OPC witness Lena Mantle correctly testified that the Commission did not find imprudency in Empire's hedging practices.[73] According to OPC's argument, if the sharing mechanism had been 85% / 15%, Empire would not have experienced hedging losses. There is no causality between the 95% / 5% FAC sharing mechanism and Empire's

[71] *The Office of Public the Counsel's Initial Brief*, P. 32-34 (May 6, 2020).
[72] *The Office of Public the Counsel's Initial Brief*, P. 33 (May 6, 2020).
[73] Ex. 205, *Surrebuttal Testimony of Lena M. Mantle*, P. 4 (May 8, 2020).

hedging losses; nor does OPC produce evidence that Empire would not have had the hedging losses with an 85% / 15% FAC sharing mechanism.

The FAC statute requires utilities to undergo prudency reviews every 18 months and refund imprudently incurred costs plus interest.[74] OPC suggests that prudency reviews are insufficient incentive for Empire to not abuse its FAC by quoting the Commission's statement that "an after-the-fact prudence review is not a substitute for an appropriate financial incentive."[75] The threat of prudency reviews is real, as proven by the Commission ordering Ameren to refund $17,169,838, plus interest, to rate payers after it found that Ameren imprudently failed to flow off-system revenue received from contracts through its FAC.[76]

Prudency reviews are not the only carrot the Commission holds to prevent Empire from misusing its FAC. The most drastic carrot is elimination of its FAC.[77] Missouri law requires all electric utility FACs to be reviewed every four years,[78] so Empire has a constant reminder that it must wisely manage its FAC. Fuel expense is a very large cost category, such that the threat of the loss of a mechanism that has allowed capture of significant changes in prudently incurred fuel costs without the need to file general rate proceedings is a tremendously compelling incentive. Empire does not require further incentive to prudently manage its FAC.

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[74] § 386.266.5(4), RSMo.
[75] *The Office of Public the Counsel's Initial Brief*, P. 31 (May 6, 2020), quoting *Report and Order*, ER-2008-0318, P. 72 (Jan 27, 2009).
[76] *Report and Order*, ER-2010-0255, P. 22 (Apr 27, 2011).
[77] *Report and Order*, ER-2019-0335, P. 10 (Apr 29, 2020).
[78] § 386.266.5(3), RSMo.

The Legislature provided no guidance in the PISA statute regarding the appropriate FAC sharing mechanism.

OPC fails to address the Commission's finding in the recent Ameren rate case that the 85% / 15% sharing mechanism in the PISA statute has no bearing on the FAC statute:

> The state legislature's enactment of Section 393.1400, RSMo (the PISA statute) did not establish a legislative policy, presumption, or directive that supports imposing a 15% share of changes in net energy costs on utilities that have a FAC. Section 386.266 was not amended explicitly or implicitly by the enactment of the PISA statute.[79]

OPC's reliance on the PISA statute for authority to create a FAC 85% / 15% sharing mechanism continues to be misplaced. The PISA statute allows a utility to recover 85% of total depreciation expense and return associated with eligible plant additions in subsequent rate cases through an amortization. PISA applies to capital costs, while the FAC applies to fuel and purchased power costs. PISA amortizations will always be an expense – and they are a guaranteed recovery in the rate case, subject to any prudence disallowances. FAC can be either a ratepayer expense or refund. While PISA is a statutory 85% deferral, the Legislature specified no sharing mechanism in the FAC statute and gave the Commission discretion to craft FAC clauses. According to § 386.266, RSMo., the Commission cannot revise Empire's FAC without inquiry into whether a revised tariff allows Empire reasonable opportunity to realize its rate of return. The Commission may also consider business risk.[80] OPC claims that the Legislature provided guidance in the PISA statute and attempts to shoehorn the PISA statute deferral sharing mechanism into the FAC.[81] It does not fit.

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[79] *Report and Order*, ER-2019-0335, P. 11 (Apr 29, 2020).
[80] § 386.266.8., RSMo.
[81] *The Office of Public the Counsel's Initial Brief*, P. 34 (May 6, 2020).

OPC is wrong in claiming that the Commission created Empire's sharing 95% / 5% sharing mechanism "out of whole cloth."[82] The Commission provided its reasoning why a 95% / 5% sharing mechanism encourages Empire to institute efficiencies. As it stated in the case establishing the Empire FAC:

> So some sort of financial incentive is needed to ensure that Empire pays close attention to its fuel and purchased power costs, and to remind Empire that a fuel adjustment clause is a privilege, not a right, which can be taken away if the company does not act prudently. Staff's proposal restricting Empire to a 70 percent pass-through ensures Empire will not be able to recover its reasonable and prudent costs of service if, as expected, fuel costs rapidly rise. Staff calculated that from 2002 through 2006, Empire absorbed $85.5 million in fuel and purchased power costs above the costs it was allowed to recover in rates. Under Staff's 70 percent pass-through incentive proposal, Empire would still be required to absorb 30 percent, or $25.65 million of those costs over the previous four-year period. Under Public Counsel's 60% pass-through proposal, Empire would have absorbed 40 percent, or $34.2 million of those costs over the previous four year period. Such a great percentage of reduction would effectively prohibit Empire from earning its return on equity and discourage investment at a tie when Empire needs tens of millions of dollars in new capital investment.
>
> …
>
> Brubaker's proposal from his surrebuttal testimony allows Empire to recover a greater proportion of its costs than would Staff and Public Counsel's proposals, but its flaw is in its unnecessary complexity. Absorption of five percent of any excess fuel costs above the base level by Empire is sufficient incentive to improve the efficiency and cost effectiveness of its fuel and purchased power procurement activities and to allow Empire the opportunity to actually earn the return on equity awarded by this Commission.[83]

Despite the fact that OPC has not argued that the FAC statute is ambiguous, it requests the Commission adapt the PISA statute deferral to the FAC. This violates well-established statutory interpretation rules that a judicial body will look beyond the statute for guidance "only when the meaning of a statute is 'ambiguous or would lead to

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[82] *The Office of Public the Counsel's Initial Brief*, P. 34 (May 6, 2020).
[83] *Report and Order*, ER-2008-0093, P. 45-46 (Jul 30, 2008).

an illogical result that defeats the purpose of the legislation.'"[84] The FAC statute is not ambiguous, and there is no reason for the Commission to consider the PISA deferral in interpreting it. Although the FAC statute does not specify a sharing mechanism ratio, it provides criteria for the Commission to consider. Had the Legislature meant for the PISA deferral to be included in the FAC statute, it would have done so. It could have easily amended the FAC statute to add the 85% / 15% sharing mechanism when it modified § 386.266, RSMo in other ways. This is not what the Legislature chose to do.

b. What is the appropriate base factor?

Although it has access to all of Empire's rate case testimony and worksheets, discovery request responses, prudency review, and FAC filings, OPC fails to suggest an appropriate base factor. However, OPC states that the base factor should be adjusted to take into account greater fuel and purchased power expenses and the revenues associated with Asbury's retirement.[85] Ms. Mantle estimates that Empire's annual fuel costs will increase by approximately $1.3 million due to Asbury's closure.[86]

Staff continues to support the *Global Stipulation and Agreement*. However, in preparing its fuel model, Staff assumed continued operation of Asbury, because Empire's planned retirement date for Asbury's was after the true-up date.[87] As noted in the *Global Stipulation and Agreement* and in Staff's initial brief, there is no agreement on the actual retirement date for Asbury so Staff's approach continues to be appropriate.[88]

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[84] ***Ben Hur Steel Worx, LLC v. Director of Revenue***, 452 S.W.3d 624, 626 (Mo. en banc 2015) (citations omitted).
[85] *The Office of Public the Counsel's Initial Brief*, P. 35-37 (May 6, 2020).
[86] Ex. 203, *Direct Testimony of Lena M. Mantle*, P. 23 (Jan 15, 2020).
[87] Ex. 101, *Staff Class Cost of Service Report*, P. 62 (Jan 29, 2020).
[88] *Global Stipulation and Agreement,* P. 3, Fn. 2 and P. 10, Para. 26 (Apr 15, 2020).

c. What costs and revenues should flow through Empire's FAC, including, but not necessarily limited to, the following?

i. What is the appropriate percentage of transmission costs for the FAC?

Staff's position is that if the Commission orders the *Global Stipulation and Agreement* in which there would be no change to the FAC base factor, there should be no change to the percentage of transmission costs included in the FAC.[89] Fifty percent of MISO costs, 34% of SPP costs, and no revenues would be included. Empire's position is that 100% of all transmission costs and revenues should be included in the FAC.[90] OPC's position as to costs is the same as Staff's – except that Asbury costs should be removed – but transmission revenues should flow through the FAC at the same percentage as costs.[91]

In preparing its fuel model, Staff assumed continued operation of Asbury, because Empire's planned retirement date for Asbury's was after the true-up date.[92] As noted in the *Global Stipulation and Agreement* and in Staff's initial brief, there is no agreement on the actual retirement date for Asbury so Staff's approach continues to be appropriate.[93]

Staff witness Brooke Mastrogiannis testified that Staff's position regarding transmission costs and revenues is consistent with prior Commission rulings and changing it would be inconsistent with other investor-owned utilities with FACs.[94] The Commission stated this in an Empire case, ER-2014-0351:

> The Commission recently issued a Report and Order in an Ameren Missouri rate case, File No. ER-2014-0258, where it determined it is unlikely that the drafters of

[89] *Global Stipulation and Agreement,* P. 3 (Apr 15, 2020).
[90] *Initial Brief of the Empire District Electric Company*, P. 19 (May 6, 2020).
[91] *The Office of Public the Counsel's Initial Brief*, P. 37-39 (May 6, 2020).
[92] Ex. 101, *Staff Class Cost of Service Report*, P. 62 (Jan 29, 2020).
[93] *Global Stipulation and Agreement,* P. 3, Fn. 2 and P. 10, Para. 26 (Apr 15, 2020).
[94] Ex.112, *Rebuttal Testimony of Brooke Mastrogiannis*, P. 3-4 (Mar 3, 2020).

the FAC envisioned a situation where a utility would consider all its generation either purchased power or off-power sales. In fact, the policy underlying the FAC statute is clear on its face: 0§ 386.266, "… is meant to insulate the utility from unexpected and uncontrollable fluctuations in transportation costs of purchased power." Nowhere in the record do the facts support a finding that all SPP IM related transmission costs are unexpected and uncontrollable. Furthermore, as has been the case since the FAC statute was created, the costs of transporting energy in addition to the energy generated by the utility or energy in excess of what the utility needs to serve its load are the costs that are unexpected and out of the utility's control to such an extent that a deviation from traditional rate making is justified. Therefore, the costs Empire incurs related to transmission that are appropriate for the FAC, from a policy perspective and by statute, are:

1) Costs to transmit electric power it did not generate to its own load ("true purchased power"); or

2) Costs to transmit excess electric power it is selling to third parties to locations outside of its RTO ("Off-system sales").[95]

ii. What, if any, portion of the MJMEUC contract should be included or excluded from the FAC?

Staff continues to support the *Global Stipulation and Agreement*, but Empire's FAC tariff explicitly excludes revenue from full and partial requirement sales to municipalities. OPC argues that the MJMEUC contract is not a full or partial requirements contract for individual municipalities, because MJMEUC will not receive energy directly from Empire, but through SPP.[96] This difference is specious. Furthermore, Empire stated that in defining full and partial requirements sales to municipalities, it relies upon FERC's explanation of requirement sales:

> Historically, electric utilities entered into long-term contracts to make wholesale requirement sales (bundled sales of generation and transmission) to municipal, cooperative and investor-owned utilities. Under these contracts, utilities often committed to provide all (full requirements) or part (partial requirements) of a customer's power needs for the contract period. [97]

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[95] *Report and Order*, ER-2014-0351, P. 27-28 (Jun 24, 2015) (internal citation omitted).
[96] *The Office of Public the Counsel's Initial Brief*, P. 39-41 (May 6, 2020).
[97] Empire response to Data Request 244.1, citing *Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, FERC Stats. & Reg. ¶ 32,507, p. 32,862 (1994), 59 Fed. Reg. 35274 (July 11, 1994).

iii. Should any short-term capacity costs flow through the FAC from the effective date of this rate case?

Consistent with the *Global Stipulation and Agreement*, Staff's position is that short-term capacity costs should not flow through the FAC from the effective date of this rate case. OPC is in agreement.[98]

Karen Bretz

Customer Service

Although Empire's customer service is below expectations, the Commission should not order a decreased return on equity at this juncture.

OPC recommends that the Commission reduce Empire's return on equity ("ROE") by 60 basis points due to inadequate customer service.[99] Staff agrees with OPC that customer service, particularly in contact center performance and the high number of estimated billings, is troublesome. However, Staff believes that Empire is taking appropriate actions to address these issues. As explained in Staff's initial briefing, Empire has agreed to take steps to affirmatively produce better results. Staff will continue meeting with Empire staff to monitor the situation and troubleshoot issues. Staff is not in favor of a drastic penalty, such as reducing Empire's ROE.

Karen Bretz

Credit Card Fees

In response to OPC's argument that it would be unduly discriminatory to include credit card fees in the revenue requirement toward people who do not use a credit card to pay

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[98] *The Office of Public the Counsel's Initial Brief*, P. 41 (May 6, 2020).
[99] *The Office of Public the Counsel's Initial Brief*, P. 73 (May 6, 2020).

their electric bill,[100] Staff quotes from the Commission's decision in GR-2017-0215/0216 when presented with this same issue:

> Public Counsel's argument is based on the premise that those who cause a cost should pay for that cost. That is an appropriate maxim to consider when designing utility rates, but it is not an absolute limitation on the structure of such rates. No customer has a right to pay only their particular costs for receiving utility service, because the cost to serve each customer is different. If nothing else, each customer lives a greater or lesser distance from the interstate pipeline and requires a greater or lesser length of distribution system to obtain their gas supply. If each customer paid only their own individualized costs, Spire Missouri would have to establish thousands of different rates.
>
> In this case, it is reasonable to allow Spire Missouri to recover fees resulting from the use of credit and debit cards to pay LAC bills from all LAC customers rather than from just those customers who use the credit or debit cards to pay their bills, just as it currently does for MGE customers. That policy does not result in an undue or unreasonable preference among customers because all customers can use the convenience of a credit or debit card if that tool is available to them. Ultimately, this a policy question for which the Commission finds in favor of allowing the company to recover these costs from all ratepayers rather than imposing these costs on only some customers.[101]

The same holds true in this case.

Karen Bretz

Rate Case Expense

The appropriate manner of handling rate case expense is to normalize a reasonable amount over a two-year period[102] after applying the sharing mechanism originally ordered by the Commission in a KCP&L rate case.[103] OPC agrees with Staff that the sharing mechanism is appropriate and specifies certain costs that it opposes, which Staff also

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[100] *The Office of the Public Counsel's Initial Brief,* P. 43 (May 6, 2020).
[101] *Amended Report and Order*, In the Matter of Laclede Gas Company's Request to Increase Its Revenue for Gas Service, Case Nos. GR-2017-0215 and GR-2017-0216, 70 (Mar 7, 2018).
[102] *Staff's Initial Brief*, P. 59.
[103] *Id*. at 61, *See* ***In Matter of Kansas City Power & Light Company's Request for Authority to Implement a General Rate Increase for Electric Service v. Missouri Public Service Commission***, 509 S.W.3d 757, 778 (2016).

removed from its calculations in its recommendation prior to settlement.[104] However, OPC proposes that the rate case expense should be normalized over three years instead of two which is inconsistent with Staff's experience and calculations.[105] In that same vein, Empire argues that the annualized level rate case expense should be an amortized instead of Staff's normalized approach.[106] Empire's proposal is inappropriate because amortizing the costs allows the Company to continue to include the amount of rate case expense in rates until it has recovered its entire amount. However, normalizing the costs puts a reasonable amount of the rate case expense into rates for the period in between a utility's rate case filings without permitting it to continue indefinitely. Staff has previously applied the normalization approach for larger utilities such as Empire and that is the appropriate methodology for the present matter.

Empire also argues that the sharing mechanism should not be applied[107], but as Staff has already argued, the sharing mechanism was upheld by the appellate courts in the KCPL case and has been applied by the Commission in several succeeding general rate cases, and therefore, it should also be applied in this proceeding.[108]

Whitney Payne

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[104] Ex. 101, *Staff Direct Report*, P. 73.
[105] Ex. 140, *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 8.
[106] *Initial Brief of the Empire District Electric Co.*, P. 25.
[107] *Initial Brief of the Empire District Electric Co.*, P. 26.
[108] ***In Matter of Kansas City Power & Light Company's Request for Authority to Implement a General Rate Increase for Electric Service v. Missouri Public Service Commission***, 509 S.W.3d 757, 778 (2016).

Management Expense

Staff still has not seen proper support for the $3.7 million adjustment OPC proposes should be made to management expense, so Staff does not have an independent position on this matter.[109]

Whitney Payne

Allowance for Funds Used During Construction

OPC alleges that Staff has included excess AFUDC changes in its calculations for this case.[110] It bases its allegations on the belief that high-cost, long-term debt and equity capital were the two items to which the allowance for funds was applied and that this resulted in an excess amount.[111] Its proposed solution to this allegation is that the Commission should apply the cost of short term debt to the entire construction work in progress amount on Empire's books instead, or essentially to assume that all of Empire's construction activities are funded using short term debt.[112] Staff disputes that it included any excess AFUDC amounts in its calculations and instead would argue this solely amounts to a difference in methodology. Staff's treatment of AFUDC in this case is fully consistent with the requirements for calculation of AFUDC amounts found in the Uniform System of Accounts. OPC has failed to provide proper support for its calculations so Staff has been unable to find justification to support its arguments. Staff continues to support the *Global Agreement* as a full and just resolution of this matter and would argue that it accounts for all issues and should be approved.

Whitney Payne

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[109] *Staff's Initial Brief*, P. 62.
[110] *The Office of the Public Counsel's Initial Brief*, P. 45.
[111] *Id.*
[112] *Id.*

Cash Working Capital

As Staff has already laid out, in regards to cash working capital (CWC) the proper lag for income tax expense is 39.38 days based on the provisions of the Internal Revenue Code and Empire's specific payment schedule.[113] OPC has alleged that Empire is not responsible for income tax liability and has proposed instead that Empire should add 365 days of lag to account for that lack of income tax liability.[114]

OPC has further alleged that the Company should face a $14 million reduction to its CWC account due to its not paying income tax for the past four years.[115] OPC's Initial Brief does not actually cite a single source to support this argument, and Staff therefore, cannot review said source to determine how OPC arrives at these allegations. Staff continues to support its initial position as laid out in its *Initial Brief*.[116]

Empire has argued that Staff did not consider specific stratum in its considerations and thereby its calculation of lead days for cash vouchers is incorrect.[117] However, in Surrebuttal Staff clearly explained that the Company created the stratums based on its own outlook and only considered the number of invoices in each category, not the amount of the invoices.[118] Staff, however, considered the dollar amounts of the invoices compared to the population and proportionately applied the resulting factor to calculate its lag time.[119] Thus Staff continues to argue that its lag days proposed for Cash Vouchers and based on the Internal Revenue Code is the most proper authority to follow in this

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[113] *Staff's Initial Brief*, P. 63.
[114] *The Office of the Public Counsel's Initial Brief*, P. 45.
[115] *Id.*
[116] *Staff's Initial Brief*, P. 63.
[117] *Initial Brief of the Empire District Electric Co.*, P. 30.
[118] Ex. 132, *Surrebuttal Testimony of Jared Giacone*, P. 6.
[119] *Id.*

regard and continues to support the remainder of its position contained in its *Initial Brief*.[120]

Finally, Empire in its *Initial Brief* has argued that the Commission should include the Company's bad debt write-off in CWC.[121] Again in surrebuttal testimony, Staff clearly addressed this issue and outlined that bad debt is a non-cash flow item and should not be included in CWC; the Company does not make any payments associated with bad debt that would appropriate to capture in the lag days.[122] Staff continues to support that position as articulated in surrebuttal.[123]

Whitney Payne

<u>Accumulated Deferred Income Tax</u>

Staff supports the *Global Stipulation and Agreement* as a full resolution of all of the issues in this matter. However, OPC has identified this as an issue which must be decided by the Commission. To the extent that the Commission does not approve the *Global Stipulation and Agreement* as a full resolution of all issues, Staff incorporates its positions as presented in Staff's Initial Brief,[124] as well as the following response to arguments made by OPC regarding net operating loss ("NOL").

a. ***Should Empire's booked accumulated federal income tax include a reduction for net operating loss?***

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[120] Staff's Initial Brief, P.
[121] *Initial Brief of the Empire District Electric Co.*, P. 30.
[122] Ex. 132, *Surrebuttal Testimony of Jared Giacone*, P. 4.
[123] *Id.*
[124] *Staff's Initial Brief*, Pp. 64-66.

OPC argues that "When Empire was included as part of the consolidated group in Liberty's consolidated tax returns, it no longer had the use of specific NOL tax deductions."[125] However, OPC fails to point out how or why Empire's consolidation with Liberty would prevent it from being affected by an NOL situation. As argued by both Staff and Empire, the NOL amounts arise from the prior use of accelerated tax depreciation by Empire, and recognition of NOLs for rate purposes is in accordance with numerous IRS private letter rulings.[126] Nothing filed before the Commission provides persuasive reasoning for excluding Empire's current NOL balance from its Accumulated Deferred Income tax amount in rate base.

Travis Pringle

Tax Cut and Jobs Act of 2017 federal income tax rate reduction from 35% to 21% impact for the period January 1 to August 30, 2018

a. *How should the Commission treat the 2017 TCJA regulatory liability the Commission established in Case No. ER-2018-0366 when setting rates for Empire in this case?*

Staff's proposed treatment of the TCJA "stub period" revenues is fair and should be adopted. OPC's proposal, by contrast, is frankly punitive and not likely to be sustained on appeal. Why is that? The "stub period" revenue was collected by Empire in good faith, pursuant to lawful, approved tariffs. The Missouri Supreme Court has said:

> However, to direct the commission to determine what a reasonable rate would have been and to require a credit or refund of any amount collected in excess of this amount would be retroactive ratemaking. The commission has the authority to determine the rate to be charged, §393.270. In so determining it may consider past excess recovery insofar as this is relevant

[125] *Office of the Public Counsel's Initial Brief*, Pp. 48.
[126] *Staff's Initial Brief*, Pp. 65-66; *see also Initial Brief of the Empire District Electric Company*, Pp. 32.

> to its determination of what rate is necessary to provide a just and reasonable return in the future, and so avoid further excess recovery. It may not, however, redetermine rates already established and paid without depriving the utility (or the consumer if the rates were originally too low) of his property without due process.[127]

The treatment accorded the "stub period" revenues was thus expressly proscribed by the Court.

The Court's disapproval of retroactive ratemaking was founded on the Constitution and not upon the Missouri statutes.[128] Therefore, enactment of § 393.137, RSMo., passed during the 2018 session as part of Senate Bill 564, is and was not sufficient to authorize the involuntary deprivation of the "stub period" revenues from Empire. Staff believes Empire will accept its more equitable treatment. But if Empire appeals the issue, there is a reasonable chance that Empire will prevail.

Kevin A. Thompson

<u>Tax Cut and Job Acts Revenue</u>

a. ***What is the appropriate amount of tax cut and job act revenue to remove from test year revenues?***

b. ***Should revenues associated with the tax cut and job act stub period be removed from revenue?***

The following addresses all sub-issues under this issue together. Although listed as an issue in its brief, OPC did not actually address this issue in its initial brief – not even as a corollary to the Asbury issue. Staff addressed each of the sub-issues under this issue in its *Initial Brief* filed herein and would refer the Commission to that initial brief for

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[127] ***State ex rel. Util. Consumers' Council of Missouri, Inc. v. Pub. Serv. Comm'n,*** 585 S.W.2d 41, 58 (Mo. banc 1979).
[128] *Id.*

the appropriate resolution of these sub-issues (rather than that proposed by Empire in its initial brief) in the event that the Commission does not accept the terms of the *Global Stipulation* as a complete resolution of this case.

Jeffrey Keevil

<u>Asbury</u>

a. ***Is it lawful to require Empire's customers to pay for Asbury costs through new rates?***

b. ***Is it reasonable to require Empire's customers to pay for Asbury costs through new rates?***

c. ***If it is unlawful and/or unreasonable to include the costs of the retired Asbury plant in rates, what amount should be removed from Empire's cost of service?***

The following addresses all sub-issues under this issue together. In its initial brief OPC claims that Asbury costs cannot be included in rates because it is not "used and useful" and then spends several pages quoting from an old Missouri Power & Light Company case involving tree trimming expense. However, the tree trimming case is not the "smoking gun" OPC makes it out to be. There is no question that Asbury was "used and useful" during the test year, update, and true-up periods involved in this case – even using OPC's alleged Asbury retirement date of December 12, 2019. Using Empire's Asbury retirement date of March 1, 2020, it was used and useful even beyond the end of the true-up period. However, as recognized in Empire's initial brief, there is no agreement regarding the retirement date, and Empire is exploring opportunities related to the closure of the Asbury plant. Further, quoting Empire's initial brief, it would be "unjust and unreasonable to attempt to make isolated adjustments to the revenue requirement in this case due to the retirement of Asbury, as many of the components are not known and measurable at this time." This is a very similar argument to that made by Staff in its initial brief when addressing the uncertainty surrounding the Asbury retirement. The Commission should approve the Global Stipulation, which

provides for an accounting authority order to be issued to capture all financial impacts from Asbury's retirement from January 1, 2020 forward, as the only just and reasonable resolution of this matter.

Jeffrey Keevil

Fuel Inventories

What is the appropriate number of burn days to use for Asbury fuel inventory?

OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in Staff's initial brief, OPC should not prevail on the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the Global Stipulation supported by Staff, Empire, and numerous other parties to this case, the Commission need not even reach this issue.

In the event that the Commission does not accept the terms of the Global Stipulation as a complete resolution of this case, Empire argues in its initial brief for 60 days as the appropriate number of burn days to use for Asbury fuel inventory. Although 60 days of coal inventory has been used in the past, Staff believes that 60 days is no longer appropriate to represent an ongoing level for Asbury based on its reported-by-Empire retirement date of March 1, 2020.[129] Based on the Company's responses to data requests, Staff believes it is appropriate to use the most current information as of the end of the true-up period of January 31, 2020 to represent an appropriate level of coal inventory of 18 days for Asbury.[130]

Jeffrey Keevil

Operation and Maintenance Normalization

a. ***What is the appropriate level of operation and maintenance expense to be included in the cost of service?***

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[129] Ex. 138-C, *Surrebuttal/True-up Testimony of Amanda C. McMellen*, Pp. 1-2.
[130] *Id.* at p. 2.

b. ***Should inflation factors be used to calculate operation and maintenance expense?***

c. ***What is the appropriate normalized average of years to be used for the Riverton, State Line Combined Cycle Unit, the Common Unit and State Line 1 Unit?***

The following addresses all sub-issues under this issue together. OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in Staff's initial brief, OPC should not prevail on the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the Global Stipulation supported by Staff, Empire, and numerous other parties to this case, the Commission need not even reach this issue.

As stated in Staff's initial brief, before Jurisdictional Allocations are applied the appropriate normalized level for operation and maintenance expense to be included in cost of service is $28,877,386.[131]

In the event that the Commission does not accept the terms of the Global Stipulation as a complete resolution of this case, Empire argues in its initial brief that Staff's proposed O&M level is not reasonable as Staff averaged each of the plant's O&M costs based on incorrect maintenance schedules. However, as testified by Ms. Sarver, although Staff may have recorded Empire's plant major overhaul schedule incorrectly, Staff also reviewed the maintenance accounts and analyzed each plant separately to determine the trend, so *mistakenly recording the major overhaul schedule did not affect the final analysis or recommendation*.[132]

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[131] Ex. 124, *Staff True-up Accounting Schedules*; Ex. 143, *Surrebuttal/True-up Testimony of Ashley Sarver*, Pp. 6-8.

[132] Ex. 143, *Surrebuttal/True-up Testimony of Ashley Sarver*, p. 6.

Inflation factors should not be used to calculate O&M expense. It is not appropriate to adjust actual utility expenses for ratemaking purposes based on overall economic indexes that are not Company or utility-specific; general economic indicators (such as Empire's proposed inflation factors) are not specific to Empire's O&M expenses.[133]

The appropriate normalized average of years to be used for Riverton is 3 years. The appropriate normalized average of years for State Line Combined Cycle Unit, the Common Unit and State Line Unit 1 unit is 5 years.[134]

Jeffrey Keevil

Depreciation and Amortization Expense

What is the appropriate level of depreciation and amortization expense of plant to include in the cost of service?

b. ***Should depreciation expense for transportation equipment that was charged through a clearing account be removed from depreciation expense?***

i. What are the authorized depreciation rates for accounts 371 & 373 to be used in the cost of service?

The following addresses all sub-issues under this issue together. OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in Staff's initial brief, OPC should not prevail on the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the *Global Stipulation* supported by Staff, Empire, and numerous other parties to this case, the Commission need not even reach this issue.

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[133] *Id.* at p. 7.
[134] See Ex. 101, *Staff's Direct Report*, Pp. 71-72 and Ex. 143, *Surrebuttal/True-up Testimony of Ashley Sarver*, Pp. 6-8.

In the event that the Commission does not accept the terms of the *Global Stipulation* as a complete resolution of this case, as stated in Staff's *Initial Brief*, the appropriate amount of depreciation expense to allow is $71,423,882 and the appropriate amount of amortization of electric plant is $3,387,871 rather than the amounts supported by Empire in its Initial Brief.[135]

Yes, depreciation expense for transportation equipment that was charged through a clearing account should be removed from depreciation expense. This is because the amounts in the clearing accounts are charged to construction projects that will eventually be plant in service, in which the costs will be recovered through depreciation over the life of the assets.[136] Finally, the depreciation rates for accounts 371 and 373 should remain at the ordered rates of 4.67% and 3.33%, respectively.[137]

Jeffrey Keevil

Retail Revenue

a. ***What is the appropriate amount to remove from retail revenue for unbilled revenue, franchise tax revenue, and FAC revenue?***

b. ***What is the level of billing determinants per rate schedule that should be used to calculate retail rate revenue in this case?***

c. ***Should the billing adjustment and the retail revenues be trued up to January 31, 2020 in the cost of service?***

The following addresses all sub-issues under this issue together. OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in Staff's initial brief, OPC should not prevail on

[135] Ex. 124, *Staff True-up Accounting Schedules*.
[136] See Ex. 101, *Staff's Direct Report*, p. 90.
[137] Depreciation rates were last ordered in Case No. ER-2016-0023.

the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the *Global Stipulation* supported by Staff, Empire, and numerous other parties to this case, the Commission need not even reach this issue.

Staff addressed each of the sub-issues under this issue in its initial brief filed herein and would refer the Commission to that initial brief for the appropriate resolution of these sub-issues in the event that the Commission does not accept the terms of the *Global Stipulation* as a complete resolution of this case.

Jeffrey Keevil

Property Taxes

a. ***What is the appropriate amount of property taxes to include in the cost of service?***

b. ***What is the proper method to be used for calculating the property tax amount to be included in the cost of service?***

The following addresses all sub-issues under this issue together. OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in Staff's initial brief, OPC should not prevail on the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the *Global Stipulation* supported by Staff, Empire, and numerous other parties to this case, the Commission need not even reach this issue.

In the event that the Commission does not accept the terms of the *Global Stipulation* as a complete resolution of this case, Empire addressed these sub-issues in its Initial Brief. Therefore, Staff feels compelled to respond briefly. Regarding sub-issue (a), the appropriate amount of property tax expense is $25,138,294. Staff determined this annualized level by applying Empire's tax rate to plant in service

balances as of December 31, 2019, which are the most current known and measurable balances used in the property tax assessment process.[138]

Regarding sub-issue (b), Staff calculated the property rate by dividing the 2019 property taxes paid by the December 31, 2018 total property. This property tax rate was then applied to the total property as of December 31, 2019 to determine annualized property tax. Not included in the property tax calculation is the 2019 Plum Point taxes paid, Staff added this to the annualized property tax to determine the total annualized property tax.[139] It should also be noted that Staff updated property tax expense to reflect plant-in-service as of December 31, 2019. The ratio of property taxes paid at year-end 2019 to the balance of plant-in service as of January 1, 2019 was applied by Staff to the December 31, 2019 plant-in-service balance.[140]

Jeffrey Keevil

Common Property Removed from Plant and Accumulated Depreciation

a. ***What is the appropriate method and amount for removal of common property from plant in service and accumulated depreciation?***

OPC's position on this issue is entirely dependent on OPC prevailing on the Asbury issue discussed elsewhere herein. As shown herein and in *Staff's Initial Brief*, OPC should not prevail on the Asbury issue; therefore, OPC should not prevail on this issue. In fact, if the Commission approves the *Global Stipulation* supported by Staff,

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[138] *See* Ex. 101, *Staff's Cost of Service Report*, Pp. 78-79; Ex. 127, *Surrebuttal/True-up Testimony of Courtney Barron*, Pp. 1-3; Ex. 124, *Staff True-up Accounting Schedules*.
[139] See Ex. 101, *Staff's Direct Report*, Pp. 78-79; Ex. 127, *Surrebuttal/True-up Testimony of Courtney Barron*, Pp. 1-3.
[140] Ex. 127, *Surrebuttal/True-up Testimony of Courtney Barron*, P. 3.

Empire, and numerous other parties to this case, the Commission need not even reach this issue.

In the event that the Commission does not accept the terms of the *Global Stipulation* as a complete resolution of this case, Empire takes issue in its initial brief with Staff's calculation of the amount for removal of common property from plant in service and accumulated depreciation. Empire argues that Staff should have first applied an allocation factor (the "mass rate") to common plant then applied a jurisdictional allocation to the remaining general plant. This is in fact what Staff did. Staff applied the Company's mass rate percentage to its January 31, 2020 plant in service and accumulated depreciation balances for general plant accounts 389 through 398. The appropriate amount for removal of common property from plant in service and accumulated depreciation is $11,059,772.[141]

Jeffrey Keevil

Affiliate Transactions

Introduction:

As noted in Staff's initial brief, it views the *Global Stipulation and Agreement* as a resolution of all issues in this rate case including all matters related to Affiliate Transactions. While Affiliate Transactions are not specifically addressed within the *Agreement*, it resolves all revenue requirement issues by providing that there will be no changes to Empire's retail base rates, and thus, Staff continues to recommend its

[141] See Ex. 101, *Staff's Direct Report*, p. 19; Ex. 127, *Surrebuttal/True-up Testimony of Courtney Barron*, Pp. 3-4.

approval. However, should the Commission choose not to approve the *Agreement,* Staff argues as follows:

Argument

a. Are Empire's transactions with its affiliates imprudent?

As stated in *Staff's Initial Brief*, it is Staff's position that the interest rate charged to Empire by its affiliate, LUCo, associated with its June 1, 2018, refinancing of its $90 million first mortgage bonds made by executing a 15-year $90 million unsecured promissory note is imprudent. Empire's major critique of this position is that it claims LUCo has not permanently financed the 4.53% 15-year long-term promissory note with short-term debt, and therefore, a short-term rate of debt should not be ascribed to it.[142] Generally, Staff would agree with the premise that long-term debt should be refinanced with long-term debt; however, that is not what has actually occurred in this instance. As explained by Empire Witness Mark T. Timpe, in his rebuttal testimony, LUCo aggregates financing until it gets to a scale to be able to take it out in the debt capital markets efficiently, because LUCo believes this methodology is the most efficient and cost effective way to finance for all of its customers.[143] However, the result of the employment of this method was that LUCo obtained the capital to refinance Empire's $90 million of first mortgage bonds by accessing its credit facility, and *actually* obtained an interest rate significantly lower than the 4.53% it charged to Empire.[144] And, while it may be LUCo's intent to do so, it has yet to issue its own long-term debt to

[142] *Empire's Initial Brief*, P. 75.
[143] Ex. 43: *Rebuttal Testimony of Mark T. Timpe*, P. 4.
[144] Ex. 129: *Surrebuttal Testimony of Staff Witness Kimberly K. Bolin,* P. 11.

refinance the lending.[145] Therefore, it is Staff's position that Empire's customers should be provided the benefit of the lower rate, as it is the rate that LUCo is actually incurring.

OPC, in its Initial Brief, also contends that LUCo charging a $450,000 origination fee in conjunction with the execution of the 15-year note, was also imprudent, and as such, Empire's revenue requirement should be reduced by its effect. Staff has not adjusted its recommended cost of debt to account for the removal of the $450,000 origination fee in this case. However, as LUCo incurred no origination fee in conjunction with the refinancing of Empire's $90 million of first mortgage bonds, Staff agrees with OPC's recommendation.

In regard to the remainder of Empire's transactions with affiliates, Staff continues to recommend that the vast majority were prudently incurred, and no additional adjustment outside of those proposed by Staff in its Direct Report[146] are necessary. On page 61 of its Initial Brief, after the inclusion of a substantial portion of the Missouri Supreme Court's opinion issued in *Office of the Public Counsel v. Mo. PSC, 409 S.W.3d 371* ("the Atmos case"), OPC contends that the record is "barren of evidence" showing its transactions with affiliates were entered into prudently.[147] Its position is founded on the principle established in the Atmos case that, "the presumption of prudence is inapplicable to affiliate transactions." In other words, OPC claims that because Empire has failed to meet its burden to show its transactions with affiliates are prudent, the

[145] EX. 129: *Bolin Surrebuttal*, P. 10.
[146] *See* Ex. 101: *Staff's Direct Report*, P. 29; Staff applied an adjustment to remove affiliate charges related to Bonus (Short Term Incentive Plan), Long Term Incentive Plan ("LTIP"), and Stock Options for APUC executives allocated by APUC to its business units. Staff's review of how these incentives are awarded to the executives found that they were awarded for increasing shareholder value, not as a benefit to the ratepayers. Therefore, Staff applied adjustments to remove from the test year the portions of these expenses that were both directly and indirectly allocated to Empire.
[147] *OPC Initial Brief,* P. 61

associated costs cannot be recovered. However, as was discussed in *Staff's Initial Brief*,[148] the record in this matter is not "barren of evidence" concerning the prudency of Empire's affiliate transactions, OPC simply has chosen to ignore it. Staff will not burden the Commission with a recitation of all of the facts in evidence ignored by OPC, but a summary of such shows the following:

- Most of Empire's transactions with its affiliates Empire are for corporate support services;[149]
- These services are provided by Empire's affiliates on a shared basis where there is an opportunity to realize economies of scale or other efficiencies;[150]
- Through the shared services model, Empire receives services vital to the day-to-day conduct of the utility;[151]
- Provision of corporate services to a number of affiliates on a centralized basis should be inherently more cost-effective than having each affiliate provide them for themselves;[152]

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[148] *Staff's Initial Brief*, P. 96.
[149] Commission Rule 20 CSR 4240-20.015(1)(D) defines "corporate support" as joint corporate oversight, governance, support systems and personnel, involving payroll, shareholder services, financial reporting, human resources, employee records, pension management, legal services, and research and development activities.
[150] Ex. 24: *Schwartz Direct*, P. 3.
[151] Ex. 24 *Schwartz Direct*, P. 9.
[152] Ex. 114, *Oligschlaeger Rebuttal*, P. 6; Of note, the Federal Energy Regulatory Commission ("FERC") shares in this opinion. In FERC Order 667, one of several rulemaking orders implementing regulations facilitating the repeal of the Public Holding Company Act of 1935 and the enactment of the Public Utilities Holding Company Act of 2005, it stated, "Fundamentally, we agree with commenters such as American Transmission Company and Progress Energy that centralized provision of accounting, human resources, legal, tax and other such services benefits ratepayers through increased efficiency and economies of scale. Further, we recognize that it is frequently difficult to define the market value of the specialized services provided by centralized service companies. Accordingly, the Commission will apply a rebuttable presumption that costs incurred under "at cost" pricing of such services are reasonable." *Repeal of the Public Utility Holding Company Act of 1935 and Enactment of the Public Utility Holding Company Act of 2005*, 70 FR 75592-01. As noted on page 93 of Staff's Initial Brief, APUC, LUC, and LUSC are "centralized service companies" subject to the jurisdiction of FERC, and are required to transact with affiliates at cost.

- Empire has seen noticeable cost reductions relating to treasury services, internal audits, and human resources, all of which are now provided on a centralized basis.[153]
- The upstream affiliate charges for these services are calculated at cost, with no profit margin included,[154] and allocated to Empire, either directly or indirectly in accordance with a series of affiliate services agreements[155] and with its Cost Allocation Manual ("CAM").[156] Thus, as explained by Staff witness Mark L. Oligschlaeger, these transactions do not carry the same risk of impropriety as transactions with competitive affiliates seeking a profit.
- Staff conducted a full audit of Empire in the course of this case, including a review of the costs allocated to it from upstream affiliates, and, with the exception of certain incentive compensation plans, has found those costs to be reasonable.[157]

Not only does OPC incorrectly assert that there is no evidence in the record supporting the prudency of Empire's transactions with affiliates, it also does not even raise the specter of actual harm[158] to Empire's ratepayers resulting from them.[159] Assuming, however, there was harm to Empire's ratepayers, OPC offers no evidence to the

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[153] Ex. 24: *Schwartz Direct,* P. 10.
[154] Ex. 114: *Oligschlaeger Rebuttal*, P. 6; Schedule RES-D-6 of Ex. 220: *Schallenberg Direct*, P. 7.
[155] Ex. 25: *Schwartz Rebuttal*, P. 4.
[156] Ex 101: *Staff Direct Cost of Service Report*, P. 29.
[157] Ex. 101: *Staff Direct Cost of Service Report*, Pp. 29-32.
[158] As explained in *Staff's Initial Brief*, in order to disallow a utility's recovery of costs from its ratepayers, the Commission must find both that "(1) the utility acted imprudently, [and] (2) such imprudence resulted in harm to the utility's ratepayers." ***State ex rel. KCP&L Greater Missouri Operations Co. v. Missouri Pub. Serv. Comm'n***, 408 S.W.3d 153, 163 (Mo. Ct. App. 2013)(Citing ***State ex rel. Ass'd Nat. Gas Co. v. Publ. Serv. Com'n of State of Mo.***, 954 S.W.2d 520, 529(Mo. App., W.D. 1997)).
[159] Other than in regard to Empire's June 1, 2018 $90 million refinancing of first mortgage bonds.

Commission regarding what the prudent level of expense related to affiliate transactions would be. Instead, OPC proposes reducing Empire's revenue requirement in this case by approximately $100 million to exclude from recovery in rates what it contends is the entirety of costs associated with Empire's transactions with affiliates; costs for services that are necessary to support the operation of the utility.[160] Staff proposes that a more reasonable adjustment would be to include in rates a level of costs reflective of Empire operating as a stand-alone utility. As OPC has failed to do this, Staff contends a similar result can be accomplished by approval of the *Global Stipulation and Agreement*; "[i]f the settlement is approved in its entirety, the O&M expenses being recovered from customers would contain zero O&M costs associated with affiliate transactions from APUC, as these costs will remain at the authorized levels prior to the acquisition."[161]

b. Do Empire's transactions with its affiliates comply with Commission Rule 20 CSR 4240-20.015 (Affiliate Transactions)?

Empire contends in its Initial Brief that its $90 million refinancing of first mortgage bonds with LUCo complied with the Commission's Affiliate Transaction Rule, stating that the affiliate transactions rule does not apply to a specific point in time for refinancing maturing long-term bonds.[162] It contends that the fully distributed cost of the $90 million promissory note with LUCo are not represented by short-term debt, refers to the surrebuttal testimony of its witness John Cochrane, where he states …[t]he good or service required by the Company in this situation was long term debt",[163] and concludes

[160] Ex. 114: *Oligschlaeger Rebuttal* P. 3; Ex. 24: *Schwartz Rebuttal*, Pp. 4-6.
[161] Ex. 1017: *Richard Supplemental Testimony*, P. 22.
[162] *See* 20 CSR 4240-20.015.
[163] Ex. 44: *Cochran Surrebuttal Testimony*, P. 6.

that the FDC for this transaction should be the fair market terms obtained through LUCo's most recent $750 million competitively bid issuance of long-term notes through a private placement on March 24, 2017.[164] However, Empire mischaracterizes the transaction. While it portrays tit as one of refinancing long-term debt with a new issuance of long-term debt, in reality the transaction was one of temporarily refinancing long-term debt with short-term debt, with the intent to further refinance the temporary short-term debt with long-term debt in the future. As outlined in OPC's Initial Brief, at the time this transaction was entered into, Empire had its own commercial paper program, and potentially could have utilized it to pay off its long-term debt temporarily. Then, once LUCo had available sufficient short-term debt to aggregate to obtain better long-term bond terms, it could have refinanced its short-term commercial paper debt by executing long-term debt with LUCo on the same terms.[165] However, it did not. Empire also did not obtain competitive bids when it entered into the agreement with LUCo, nor did it justify why bids were unnecessary.[166] Instead Empire signed a 15-year promissory note with LUCo with an interest rate of 4.53% and a $450,000 origination fee, while LUCo incurred a substantially lower rate of debt and no origination fee. Thus, as Empire compensated LUCo for a good or service above the lesser of fair market price or fully distributed cost,[167] it provided a financial advantage to an affiliate entity in violation of 20 CSR 4240-20.015.

Staff recommends the remainder of Empire's affiliate transactions sufficiently comply with the Commission's Affiliate Transaction Rules. Conversely, it is OPC's position that

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[164] *Empire's Initial Brief*, P. 74.
[165] The *Office of the Public Counsel's Initial Brief* P. 63.
[166] 20 CSR 4240-20.015(2)(A)1. Requires that, for rate purposes, the cost of an electric utility's transactions to acquire goods or services be the lesser of fully distributed cost or fair market price.
[167] *See* 20 CSR 4240-20.015(2)(A)1.

all of the transactions Empire enters into with its affiliates violate the Rules. On page 65 of its Initial Brief, as support for this, OPC infers that the CAM utilized by Empire to charge and allocate costs should not be relied upon in this case. In part, OPC claims that the CAM's reliance on the Massachusetts' Formula to assign costs is improper, referring to its witness Robert E. Schallenberg's direct testimony indicating that the factors utilized by the formula are unrelated to the nature or quantity of the goods and services provided to Empire. However, what OPC fails to mention is that the Massachusetts' Formula is a common multi-factor formula used to allocate residual corporate support service costs that has been accepted as reasonable by state and federal regulatory authorities.[168] While OPC presents the use of the Massachusetts' Formula as if it were the primary method of allocation prescribed by Empire's CAM, the fact is that per the terms of said CAM, the Massachusetts' Formula will only be used as a "last resort" to allocate common costs that apply to Empire Electric and its regulated affiliates in Missouri when neither direct nor indirect measures of cost causation can be found to charge a cost to a specific entity.[169] The use of the Massachusetts' Formula as a general allocator of "last resort" does not make all of Empire's affiliate transactions noncompliant with the rule. In fact, the use of an allocator is considered by the Rule; 20 CSR 4240-20.015(D) states:

> In transactions involving the purchase of goods or services by the regulated electrical corporation from an affiliate entity, the regulated electrical corporation will use a commission-approved CAM which sets forth ***cost allocation***, market valuation and internal cost methods… (Emphasis added).

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[168] *See* ***Midwestern Gas Transmission Co. v. Federal Power Com***. 32 FPC 993 (1964).
[169] Ex. 221, AO-2017-0360 app. (APUC CAM), Appendix 9 to APUC CAM, p.10 of 24.

While Empire has yet to secure Commission approval of its CAM,[170] as stated in *Staff's Initial Brief* (and above), in the course of its audit of the Company in this case, Staff conducted a full review of Empire's costs allocated to it from upstream affiliates. OPC conducted no such analysis. Further, if OPC, or any party, believes the Massachusetts' Formula is not the optimal method for allocated common costs that cannot be directly or indirectly assigned, then Case No. AO-2017-0360 would be an appropriate forum to raise those concerns and suggest alternative approaches.

OPC also interprets the Affiliate Transaction Rules in a way that would seemingly prohibit regulated utilities from using a shared corporate structure for the provision of corporate support functions. 20 CSR 4240-20.015(2)(B) states:

> Except as necessary to provide corporate support functions, the regulated electrical corporation shall conduct its business in such a way as not to provide any preferential service, information or treatment to an affiliate entity over another party at any time.

OPC contends that a plain reading of this section shows the exception is directed at activities the utility performs, not those of an affiliate.[171] Staff disagrees. While it is clear that the general prohibition of the provision of preferential service,[172] information,[173] or treatment to affiliates over third parties is directed towards a regulated utility, corporate support services can be both provided *by* and provided *to* a regulated utility. To limit this exception to the provision of preferential service for the provision of corporate support

[170] *See Staff's Initial Brief*, Pp. 89-92 for background regarding Empire's actions to gain Commission approval of its CAM.
[171] *The Office of the Public Counsel's Initial Brief*, P. 67.
[172] 20 CSR 4240-20.015(1)(H) defines "preferential service" as information or treatment or actions by the regulated electrical corporation which places the affiliate entity at an unfair over its competitors.
[173] 20 CSR 4240-20.015(1)(G) defines "information" as any data obtained by a regulated electrical corporation that is not obtainable by nonaffiliate entities or can only be obtained at a competitively prohibitive cost in either time or resources.

services by a regulated utility to its non-regulated affiliates could prevent regulated utility customers from realizing potential cost savings inherent in the economies of scale provided by centralized service providers subject to FERC jurisdiction. Further, when considering the Commission's Order of Rulemaking for 4-CSR 240-20-015,[174] and the included comments and Commission responses, it is clear this exception was included to ensure potential cost savings were passed on to ratepayers. Comment eight stated:

> Comments were received suggesting that a definition be provided for the term "corporate support" in order to allow greater flexibility to obtain economies in certain areas.[175]

In response, the Commission stated:

> The Commission accepts this suggestion and has added a definition for this term in section (1). Subsection (2)(B) has been modified to provide greater flexibility in that standard.

Considering the Commission's explanation for adding this exception to the Rule was to allow "great flexibility in the standard;" i.e., to allow for greater flexibility to obtain economies of scale in the provision of corporate support functions, it would seem limiting such flexibility to the provision of corporate support functions *by* a regulated utility to non-regulated affiliates would not fully effectuate to the intent of the Commission's change. The use of "centralized service companies" to provide corporate support functions to utilities, such as Empire, on a shared basis, is allowed by FERC. Further, as stated in Staff's *Initial Brief,*[176] FERC requires these centralized service companies to transact at cost. Preventing a utility from providing preferential service to such an affiliate when contracting for the provision of corporate support services on a centralized basis,

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[174] The predecessor to 20 CSR 4240-20.015 prior to the Commission's move to the Department of Commerce and Insurance.
[175] Order of Rulemaking MO REG Vol. 25 No. 1, p. 56; EX-99-442, EFIS ITEM 71.
[176] *See Staff's Initial Brief*, Pp. 100-101.

and thus taking advantage of the inherent economies of scale and passing on efficiencies to its ratepayers, would be inconsistent with the intent of the Commission's Affiliate Transaction Rules.

What amount should be included in Empire's revenue requirement for its transactions with affiliates?

Staff maintains its position that all issues relating to Empire's transactions with affiliates are reasonably resolved by approval of the *Global Stipulation*. However, if the *Global Stipulation* is not approved by the Commission, Staff recommends an appropriate cost of debt for Empire's $90 million refinancing of first mortgage bonds is 2.15%, and has reflected its adjustment in the cost of debt used to determine Empire's rate of return. Further Staff agrees with OPC's recommendation that Empire's revenue requirement should be reduced by the effect of the $450,000 origination fee charged by LUCo to Empire for the refinancing. As Staff recommends the remainder of Empire's transactions with affiliates substantially complied with the Commission's Affiliate Transactions Rule, and were prudently incurred, Staff recommends the Commission make no further adjustments to Empire's revenue requirement related to affiliate transactions.

Mark Johnson

ISSUES ADDRESSED BY PARTIES IN INITIAL BRIEFS

Staff views the *Global Stipulation and Agreement* filed in this matter April 15, 2020, to be the most appropriate resolution of this case; providing a just result to both the ratepayers and the Company. OPC has objected to the *Agreement* and made specific arguments as to certain issues in the case, which it believes the Commission must decide. In their Initial Briefs, Empire, MECG and the SERP Retirees, addressed some arguments which

Staff considered resolved, due to the *Agreement* and the fact that OPC had not objected to those elements specifically. Therefore, Staff addresses those arguments here, and reserves the right to address those arguments in its Reply Brief, to be filed May 18th as necessary.

Pension and OPEB

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that it accounted for all appropriate pension and other post-employment benefits (OPEB) in its calculations and that it corrected any errors in its surrebuttal testimony.[177]

Riverton 12 O&M Tracker

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that the Riverton 12 operations and maintenance (O&M) tracker has not shown a significant upward or downwards trend over the time period since the last rate case.[178] Therefore, Staff included a reasonable amount in its case to account for the ongoing expense of the O&M but does not see any reason why the tracker should be continued.[179]

Software Maintenance Expense

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that it included a normalized amount of expense related to software expense in its case.[180]

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[177] Ex. 143, *Surrebuttal Testimony of Ashley Sarver*, P. 2.
[178] *Id*. at 5.
[179] *Id*.
[180] *Id*. at 9.

Staff updated its number based on the update period in this case, but it does not include this item in its true-up as not all items can be trued-up.[181] Staff followed its proper procedure and has corrected any errors identified by the Company.[182]

Whitney Payne

Advertising Expense

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that $129,196 is the appropriate amount to include in the revenue requirement for advertising expense.[183] Empire alleges that Staff has not supported its adjustment for advertising expense and that it has not defeated the presumption of prudence the Company is granted when it comes to expenses.[184] Staff removed $30,211 from Empire's initial request as detailed below:

- $25,669 in invoices which lacked information to justify inclusion
- $1,972 in institutional/goodwill advertising
- $1,800 in invoices paid during the test year but dated months earlier
- $770 recorded to below the line accounts 182303 and 182318

Staff disallowed $25,669 in invoices when Empire did not provide a copy of the advertisement or specify which advertisement was invoiced. Staff could not evaluate whether these invoices were allowable according to *In re Kansas City Power and Light Company*, Case Nos. EO-85-185 and EO-85-224.[185]

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[181] *Id.*
[182] *Id.*
[183] *Statement of Positions*, P. 30 (Apr 17, 2020).
[184] *Initial Brief of the Empire District Electric Co.*, P. 48.
[185] Ex. 140: *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 4 (Mar 27, 2020).

Consistent with *In re Kansas City Power and Light Company*, Staff disallowed $1,972 in institutional/goodwill advertising. Institutional/goodwill advertising promotes the company's public image and does not benefit customers.[186]

Staff also disallowed $1,800 in invoices that although paid in the test year, were invoiced in 2017 (two were invoiced in August 2017).[187]

Staff disallowed $770 in invoices recorded to below the line accounts 182303 and 182318, because they are being recovered through the demand side management amortization in Staff's revenue requirement. It would be a double recovery to allow them to be recovered as advertising expense.[188] Staff has fully supported each adjustment it made to its recommended amount of included advertising expense and has certainly overcome the presumption of prudence granted the Company.

Karen Bretz

Materials and Supplies

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire and MECG raised this issue in their *Initial* briefs, Staff responds that the appropriate amount of materials and supplies to be included in this matter is $32,773,580. This reflects the appropriate 13-month average of costs as provided by Empire as of January 31, 2020, after applying the Missouri jurisdictional

[186] Ex. 101: *Staff Cost of Service Report*, P. 80 (Jan 15, 2020).
[187] Ex. 140: *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 4 (Mar 27, 2020).
[188] Ex. 140: *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 4 (Mar 27, 2020).

allocation factor.[189] All calculations used the most recent data provided by the Company.[190]

AROs

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that the *Global Agreement* has a proper resolution of this issue as the item Empire describes as an asset retirement obligation (ARO) is not what staff would classify as an ARO. The Initial Brief of MECG describes the situation appropriately in saying, "During settlement discussions, the parties received a better understanding of the costs in question. In fact, unlike an ARO which addresses future speculative costs, the costs in question had already been incurred and were related to the asbestos and ash pond remediation associated with certain Empire generating units. Given this, the Signatories included a provision in the Non-Unanimous Stipulation which provides for the treatment of such costs as a regulatory asset, but not as an Asset Retirement Obligation."[191] It appears that this is what Empire intends in its *Brief* as well but Staff provides this language for clarification of its position and its support of the terms of the *Global Agreement*.

LED Replacement Tracker

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that it is not proper to establish a tracker for this program as the amount of revenue that

[189] Ex. 140: *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 6.
[190] Ex. 140: *Surrebuttal/True-Up Testimony of Angela Niemeier*, P. 6.
[191] *Initial Posthearing Brief of Midwest Energy Consumers Group*, P. 12.

Empire could stand to lost if it replaces all of its mercury vapor lights in the next year is not material.[192]

Tornado AAO

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that the unamortized balance should not be included in rate base because as explained in surrebuttal testimony, Empire has already received benefits from the AFUDC carrying rate it applied to all new capital investments related to the tornado construction.[193] Additionally, the Commission in similar scenarios regarding AAOs in other cases determined that including an unamortized AAO in rate base effectively shields the shareholders from the risk of natural disasters while placing the burden entirely on the ratepayers.[194] Staff continues to stand by its position in surrebuttal that a reasonable amount should be recovered in an annualized amortization for the tornado AAO.

Iatan/Plum Pt Carrying Costs

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that Empire has agreed with Staff's recommendations and Staff continues to support the recommendations made in its direct case.

[192] Ex. 129, *Surrebuttal/True-Up Testimony of Kimberly K. Bolin*, P. 8.
[193] *Id.* at 3-4.
[194] *Id.* at 4.

Incentive Comp

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that while Staff respects Empire's argument that some costs are necessary to retain good employees, "Staff is not arguing that the Company should not be allowed to offer goals that increase profits in their incentive program – only that they should not be recoverable in rates since they do not directly and proportionately benefit customers."[195]

Customer Demand Program

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that the correct amount is $4,267,998 total with an amortization of $1,447,308.[196] Empire did not directly refute any of Staff's arguments in relation to the program, only cites to different amounts. Staff is unclear where the difference in Empire's number originates from, but the difference in numbers is minute so Staff continues to support its position.

Bad Debt

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that Empire did not directly refute any of Staff's arguments in relation to the program. Staff continues to support its position that the appropriate amount of bad debt expense is $1,883,442.

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[195] Ex. 139, *Surrebuttal/True-Up Testimony of Caroline Newkirk*, P. 3.
[196] Ex. 152, *Supporting Evidence of Caroline Newkirk.*

Other Rev

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that it does not believe that there is a dispute on this issue, but it reserve the right to respond further in its Reply Brief.

Injuries and Damages

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that while Empire argues that the total company amount of injuries and damages should be included, allocating 50% or half the injuries and damages payments to account for non-electric Empire activities is appropriate.[197]

Retention Bonuses

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that, similar to the argument made for incentive compensation, it is not proper to charge ratepayers for indirect incentives to keep employees. [198] Also, Empire has yet to implement this program, thus the program should not be included.

Dues and Donations

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that Empire raised this issue in its *Initial Brief*, Staff responds that it is a longstanding position of Staff that the Edison Electric Institute dues should not

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[197] Ex. 101, *Staff Direct Report*, P. 81.
[198] Ex. 139, *Surrebuttal/True-Up Testimony of Caroline Newkirk*, P. 3.

be included in rates due to its primarily political nature of providing lobbying services to electric utilities.

Retirement Provisions

Staff did not address this issue in its *Initial Brief*, because we believed this issue was not in dispute. To the extent that the SERP Retirees raised this issue in its *Initial Brief*, Staff responds that the *Global Agreement* properly resolves the issue raised by organizing a discussion between all interested parties to provide guidance for future funding of the SERP retirement program through a Rabbi Trust method.[199]

Whitney Payne

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served by electronic mail, or First Class United States Postal Mail, postage prepaid, on this 12th day of May, 2020, to all counsel of record.

/s/ Whitney Payne

[199] *Global Stipulation and Agreement*, P. 11.