Exhibit No.:
Issue: Income Taxes
Witness: Lisa M. Ferguson
Sponsoring Party: MoPSC Staff
Type of Exhibit: Rebuttal Testimony
Case No.: GR-2017-0215 & GR-2017-0216
Date Testimony Prepared: October 17, 2017

MISSOURI PUBLIC SERVICE COMMISSION

COMMISSION STAFF DIVISION

AUDITING DEPARTMENT

REBUTTAL TESTIMONY

OF

LISA M. FERGUSON

SPIRE MISSOURI, INC., d/b/a SPIRE

LACLEDE GAS COMPANY and MISSOURI GAS ENERGY
GENERAL RATE CASE

CASE NOS. GR-2017-0215 and GR-2017-0216

Jefferson City, Missouri
October 2017

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Q. Please state your name and business address.

A. Lisa M. Ferguson, 111 N. 7th Street, Suite 105, St. Louis, MO 63101.

Q. By whom are you employed?

A. I am employed by the Missouri Public Service Commission (“Commission”) as a member of the Auditing Staff ("Staff").

Q Are you the same Lisa M. Ferguson who contributed to Staff’s *Revenue Requirement Cost of Service Report* filed September 8, 2017 in this case?

A. Yes, I am.

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

A. My rebuttal testimony will respond to LAC and MGE witness Chuck J. Kuper’s direct testimony and sponsored workpapers concerning income taxes. I will also explain Staff’s position on the appropriate tax timing differences that should be included as part of LAC’s and MGE’s current normalized income tax calculation. These tax timing differences are added and subtracted from net operating income in order to calculate taxable income, to which the current statutory tax rates are then applied. My rebuttal testimony will also address the deferred tax expense that typically results from the normalization of certain tax timing differences.

TAX TIMING DIFFERENCES

Q. What was Staff's position regarding income tax expense as part of its direct testimony filing?

A. Staff explained in direct testimony that Spire Missouri had not provided the supporting calculations for LAC's and MGE's proposed direct filed tax timing differences (flow through adjustments) at the time of Staff's direct testimony filing. As such, Staff included LAC's and MGE's calculations merely as placeholders for direct testimony due to lack of support, until such calculations could be provided and analyzed. Staff has now received and reviewed the data LAC and MGE has provided, and has had discussions with LAC and MGE about each individual tax timing difference proposed in LAC and MGE's direct testimony. Based upon this additional review, Staff is now proposing changes to Staff's calculation of income tax expense.

Q. Will Staff continue to review the income tax issue through the true-up date in this proceeding?

A. Yes.

Q. What are the individual tax timing differences that LAC and MGE proposed as part of direct testimony in this rate case, and which Staff used as placeholder values in its direct filing?

A. LAC included the following as add backs and subtractions to net operating income before taxes:

Add Backs:

Uncertain Tax Position Adjustment (FIN 48)	$ 1,535,988
Other non-operating, non-deductible expense	$ 1,882,787

Other miscellaneous, non-deductible expense	$ 290,372
Meals & Entertainment at 50%	$ 325,000
Missouri Affordable Housing Assistance Program Credits (AHAP)	$ 286,621

Subtractions:

ESOP (Employee Stock Option Plan)	$ 4,046,571
Life Insurance Premiums/Proceeds	$ 732,956
Nontaxable Insurance – Cash Surrender Value	$ 816,715
Investment Tax Credit Write-off	$ 547,036
Depreciation – IRC Section 263A	$15,633,509
Administrative & General non-deductible adjustment	$ 1,731,345

MGE included the following as add backs and subtractions to net operating income:

Add Backs:

Meals and Entertainment at 50%	$ 64,917
Other miscellaneous on-deductible	$ 97,127
Uncertain Tax Position Adjustment (FIN 48)	$ 49,067

Subtractions:

Depreciation – IRC Section 263A	$11,094,517

Q. Does Staff agree that the tax timing differences proposed by LAC and MGE are correct and should be included in LAC's and MGE's revenue requirements for regulatory purposes?

A. Not completely. Staff does not agree that inclusion of all tax timing differences provided by LAC and MGE are appropriate to include as part of the normalized income tax calculations. Further, for those differences that Staff agrees should be included as part of the cost of service calculation, Staff believes the values of the tax timing differences proposed by LAC and MGE are not the correct values to include. The values of all tax timing differences provided by LAC and MGE as part of their direct testimony filing are based on estimations. LAC and MGE have fiscal years that end on September 30 of each year. The test year in this current proceeding is the twelve months ending December 31, 2016. As part of their direct filings, LAC and MGE calculated estimated tax timing difference amounts for the twelve months ending December 31, 2016, rather than including the actual tax timing differences that were used to calculate their filed income tax return as of September 30, 2016. Prior to the filing of Staff's direct testimony, Staff requested supporting calculations of these estimated tax timing difference amounts, but LAC and MGE informed Staff that it was not possible to provide these calculations due to the fact that these amounts were estimated. Staff then requested the supporting calculations for the actual tax timing differences at September 30, 2016. Those calculations would include the same information that was used to complete Spire's consolidated FY 2016 tax return for the Missouri utilities. LAC and MGE later provided to Staff the requested information regarding the actual tax timing difference amounts at September 30, 2016, with the supporting calculations; however, it was not in sufficient time to be included in direct testimony.

Q. What is Staff's position concerning the appropriate measurement of tax timing difference amounts for reflection in rates in this case?

A. Staff's position is that it is appropriate to include the tax timing differences that are based on actual values at September 30, 2016, rather than estimates determined at December 31, 2016, for which no supporting calculations can be obtained.

Q. What is Staff's position regarding the tax timing differences amounts that should be used for LAC in this proceeding?

A. Staff recommends including the following tax timing difference amounts in LAC's normalized tax calculation:

Add Backs:

Book Depreciation	$48,793,472
Uncertain Tax Position Adjustment (FIN 48)	$ 1,152,392
Other Miscellaneous, Non-deductible Expense	$ 69,769
Meals & Entertainment at 50%	$ 261,087

Subtractions:

Interest Expense	$24,051,191
Tax Straight-line Depreciation	$48,793,472
MACRS and Bonus Depreciation in Excess of Book	$16,685,905
ESOP (Employee Stock Option Plan)	$ 3,773,840
Depreciation – IRC Section 263A	$16,196,036
Administrative & General Non-deductible Adjustment	$ 1,272,903

Q. What is Staff's position regarding the tax timing difference amounts that should be used for MGE?

A. Staff recommends including the following tax timing difference amounts in MGE's normalized tax calculation:

Add Backs:

Book Depreciation	$31,986,384
Meals and Entertainment at 50%	$ 69,121
Uncertain Tax Position Adjustment (FIN 48)	$ 49,067

Subtractions:

Interest Expense	$14,543,904
Tax Straight-line Depreciation	$31,986,384
MACRS and Bonus Depreciation in Excess of Book	$41,798,586
Depreciation – IRC Section 263A	$10,850,002

Q. Were there certain tax timing differences that Staff did not include in its normalized tax calculation for LAC and MGE?

A. Yes. Staff did not include the following tax timing differences for LAC: the other miscellaneous nondeductible items such as luxury skybox expense, lobbying expense, and fines and penalties; other non-operating nondeductible expenses such as a valuation allowance against charitable contribution carryforwards, life insurance premiums/proceeds, nontaxable insurance – cash surrender value, and AHAP credits. Staff did not include the following tax timing differences for MGE: the other miscellaneous nondeductible items such as luxury skybox expense, lobbying expense, and fines and penalties.

Q. Please explain why Staff did not include these tax timing differences in its tax calculation.

A. Staff did not include these tax timing differences for the other miscellaneous nondeductible items and non-operating nondeductible items listed above because an add back of expenses for tax purposes should only occur if the expense exists in the income statement. Staff's position has been that expenses such as those above are not allowable for ratemaking and has consistently excluded them from its recommendations for utilities' costs of service. To be consistent with Staff's cost of service, the above add backs and subtractions should be removed for the items not included in the cost of service to begin with.

The Missouri AHAP tax credit is used as an incentive for Missouri businesses and/or individuals to participate in the production of affordable housing. This state tax credit is earned by an eligible donor for the donation of cash, equity, services, real-estate or personal property to the Truman Heritage Habitat For Humanity ("THHFH") for assistance in building homes. The AHAP tax credit for an eligible donor equals 55% of the total value of the donation to THHFH. LAC buys into an equity fund associated with THHFH and then those funds are used by THHFH for construction of affordable housing. Staff did not include these tax credits as part of the normalized tax calculation due to the fact that the cost of purchasing into that equity fund would not be included as part of the income statement as part of the cost of service.

BOOK TO TAX RATIO/DEFERRED TAXES

Q. How did LAC and MGE develop their tax calculations?

A. LAC and MGE began by subtracting operating expenses from operating revenues to develop an amount of net operating income. LAC and MGE then reduced net operating income by the amount of their flow through adjustments as well as interest on long term debt to determine the amount of net taxable income. The taxable income was then multiplied by the effective tax rate to determine the amount of current income tax in LAC's and MGE's direct cost of service.

Q. Did LAC or MGE take into account book depreciation, tax depreciation or excess depreciation (temporary tax timing differences) as part of their calculation?

A. No. LAC's and MGE's workpapers do not include a separate calculation where the amount of tax that is calculated due to the "book-tax" difference in depreciation moves from the current period to a deferred period. In effect, this calculation creates a reduction in current tax while at the same time increasing deferred tax by the same amount.

Q. Does Staff normalize depreciation related temporary tax timing differences?

A. Yes, any temporary tax timing differences, such as those created by depreciation, would create a reduction to current taxes with an offsetting increase to deferred taxes. However, Staff is concerned about the "book to tax depreciation ratio" calculation that was provided by LAC and MGE at Staff's request. The values provided to Staff do not seem appropriate based on past rate cases for Laclede, MGE and other Missouri utilities. Staff has worked with LAC and MGE and has determined what it considers an appropriate value for the depreciation related tax timing differences.

Q. Did LAC or MGE include a calculation for deferred taxes as part of their direct cost of service filing?

A. As far as Staff is aware, LAC and MGE did not include an annualized level of deferred tax expense as part of their direct filing.

Q. What is Staff's position regarding the correct level of deferred taxes to include in the cost of service calculation?

A. Staff recommends including deferred taxes for the tax timing differences related to MACRS[1] and bonus depreciation that is in excess of book depreciation. Due to

[1] Modified Accelerated Cost Recovery System - the current tax depreciation system in the United States.

Staff normalizing these tax timing differences for purposes of this rate case, a normalized level of deferred taxes must also be established for these items. As stated above, Staff has worked with LAC and MGE and has determined what it considers an appropriate value of deferred taxes for inclusion in the cost of service related to the depreciation related tax timing differences.

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Request to Increase Its Revenues for Gas Service	)))	Case No. GR-2017-0215
In the Matter of Laclede Gas Company d/b/a Missouri Gas Energy's Request to Increase Its Revenues for Gas Service	)))	Case No. GR-2017-0216

AFFIDAVIT OF LISA M. FERGUSON

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

COMES NOW LISA M. FERGUSON and on her oath declares that she is of sound mind and lawful age; that she contributed to the foregoing Rebuttal Testimony; and that the same is true and correct according to her best knowledge and belief.

Further the Affiant sayeth not.

Lisa M. Ferguson
LISA M. FERGUSON

JURAT

Subscribed and sworn before me, a duly constituted and authorized Notary Public, in and for the County of Cole, State of Missouri, at my office in Jefferson City, on this 13th day of October, 2017.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: December 12, 2020
Commission Number: 12412070

D. Suzie Mankin
Notary Public