Exhibit No.:	
Issue:	*Cash Working Capital, Accumulated Deferred Income Tax (ADIT), Incentive Compensation, AMR Meter Devices, Estimated Property Tax, Surveillance Reporting, Erroneous Depreciation Rates, True-Up*
Witness:	*Lisa M. Ferguson*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Surrebuttal - True-Up Direct Testimony*
Case No.:	*GR-2018-0013*
Date Testimony Prepared:	*May 9, 2018*

MISSOURI PUBLIC SERVICE COMMISSION

COMMISSION STAFF DIVISION

AUDITING DEPARTMENT

SURREBUTTAL/TRUE-UP DIRECT TESTIMONY

OF

LISA M. FERGUSON

LIBERTY UTILITIES (MIDSTATES NATURAL GAS) CORP., d/b/a LIBERTY UTILITIES

CASE NO. GR-2018-0013

Jefferson City, Missouri
May 2018

** Denotes Confidential Information **

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d/b/a LIBERTY UTILITIES

CASE NO. GR-2018-0013

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 Commission Staff (Staff) within the Auditing Department.

Q Are you the same Lisa M. Ferguson who contributed to Staff's *Revenue Requirement Cost of Service Report* filed March 2, 2018 in this case?

A. Yes, I am.

EXECUTIVE SUMMARY

Q. What is the purpose of your surrebuttal/true-up direct testimony in this proceeding?

A. My surrebuttal/true-up direct testimony will respond to the rebuttal testimony of the following Liberty Midstates – MO and The Office of the Public Counsel (OPC) witnesses regarding the following issues:

- Amanda C. Conner – OPC: Cash Working Capital (CWC) Tax Lags.
- John S. Riley – OPC: Current Income Tax and Accumulated Deferred Income Tax (ADIT).

- Jill Schwartz – Liberty Midstates - MO: Incentive Compensation, Surveillance Reporting, Automated Meter Readers (AMRs), Estimated Property Tax.

- James A. Fallert – Liberty Midstates - MO: ADIT, Erroneous Depreciation Rates.

Since the time that rebuttal testimony was filed, Staff has received true-up information from Liberty Midstates – MO as well as updates to a majority of Staff's data requests. Staff has reflected all known and measureable changes through the true-up period ending March 31, 2018, and for certain adjustments, such as the contractual union labor increase at June 1, 2018, that will occur outside of the true-up period. My surrebuttal/true-up direct testimony will therefore also address the results of the Staff's true-up audit and will also provide Staff's revenue requirement recommendation based upon the completion of its true-up audit.

<u>CASH WORKING CAPITAL – TAX LAGS</u>

Q. On page 10, lines 16-22 and page 11 lines 1-5 of OPC witness Amanda C. Conner's rebuttal testimony she discusses how Liberty Midstates – MO is currently experiencing a net operating loss where the Company's allowable tax deductions are greater than its taxable income. For this reason, she believes it is appropriate to remove the current income tax dollars from the calculation of CWC. Does Staff agree with this ratemaking treatment?

A. Yes. Liberty Midstates – MO is currently in a net operating loss (NOL) situation and as such has not made federal and state tax payments since 2014. Liberty Midstates – MO will be able to use its NOL moving forward to offset future tax. Staff has reviewed its CWC calculations and now believes the federal and state tax lags should be set to a net lag of zero. Cash working capital measures the <u>cash</u> inflows and outflows that are necessary to pay day to day expenses in order to provide utility service. Liberty Midstates – MO is not currently expending cash to federal and state taxing authorities and is not expected to do so in the near future and, as such, there is no investment of funds necessary for federal and state taxes.

ACCUMULATED DEFERRED INCOME TAX – EXCESS DEFERRED TAX

Q. On page 11, lines 10-13, OPC witness John S. Riley discusses how the reduced tax rate stemming from the Tax Cuts and Jobs Act (TCJA) that took effect January 1, 2018, has now resulted in an overstatement of ADIT in Liberty Midstates – MO's rate base. Does Staff support starting the flow back of excess deferred taxes to ratepayers in this rate case?

A. Yes, if possible. Staff supports the flow back of excess deferred taxes to ratepayers amortized over the appropriate time period, based on whether the excess deferred income taxes are "protected" or "unprotected."[1] Liberty Midstates – MO has informed Staff that as of the beginning of April 2018 it is in the early stages of evaluating the cost and ability to achieve a data plan that would allow the use of the Average Rate Assumption Method (ARAM) for computing excess protected ADIT. It is Liberty Midstates - MO's preference to utilize the ARAM method for this purpose, if it is not cost prohibitive and the necessary data records are obtainable. Liberty Midstates – MO plans to expediently determine whether the ARAM method is a viable option to determine the period of return of the excess deferred taxes; however, as of now there is no definite completion date as to when the decision of whether to use ARAM will be made.

[1] Protected excess ADIT is the portion associated with accelerated depreciation tax timing differences that must be "normalized" for rate making purposes and where the flow back of excess ADIT cannot be returned to customers any more quickly than over the estimated life of the assets that gave rise to the ADIT. Unprotected excess ADIT is the portion of the deferred tax reserve that resulted from normalization treatment of tax timing differences other than accelerated depreciation.

Q. On page 11, lines 15-21 OPC witness John S. Riley explains that the protected portion of excess ADIT should be returned to customers using the ARAM method, and that the unprotected portion can be returned over a period that is at the discretion of the Commission. If Liberty Midstates – MO cannot calculate the amount using the ARAM then the average life or composite rate should be used for the protected portion. Absent either of those calculations, the amount should be refunded over the 20 year for protected excess ADIT and 10 year life for unprotected ADIT used in the recent Spire Missouri rate case. Does Staff agree with OPC's position on these points?

A. Generally, yes. The TCJA provides for the use of ARAM for determining the timing of the return of the excess deferred taxes, but allows the utility an alternative calculation if the utility does not have the data or asset vintage information necessary to compute ARAM, such as the Reverse South Georgia method. Performing the calculations necessary to determine the amortization period for return of protected ADIT is a complicated and data intensive process, and several utilities have expressed concerns that the approach used to flow back protected excess ADIT not violate IRS normalization principles. The 20 year and 10 year life amortization periods that were developed by Spire Missouri were based on Company specific information and assumptions. Staff's position is that any deferral of excess deferred taxes should begin with the date of the tax change, January 1, 2018, and continue to be deferred until Liberty Midstates – MO's next rate case. This should allow the utility time to develop its recommendations as to an appropriate method for returning the excess deferred tax. Liberty Midstates – MO should also notify the Commission as soon as the Company can determine whether it is able to comply with ARAM accounting. If Liberty Midstates – MO determines at that time it will not be able to utilize ARAM, in its notification it should explain why it cannot utilize ARAM, and what alternative method is being used to determine the return of excess deferred taxes. This approach is generally consistent with the terms of the *Stipulation and Agreement* approved in the latest Missouri American Water Company rate case, No. WR-2017-0285.

Q. Is the amount of excess protected and unprotected ADIT known?

A. Yes. Staff can calculate the amount of excess protected and unprotected deferred taxes that are to be flowed back to customers; however Staff requires additional information to determine whether certain components of unprotected ADIT should be included in Staff's calculation. However, the amortization period for return of those deferred taxes is unknown at this time.

ACCUMULATED DEFERRED INCOME TAX – CALCULATION DIFFERENCES

Q. On page 4, lines 3-10 of Liberty Midstates – MO witness James A. Fallert's rebuttal testimony, he describes the major differences between Staff and Company's calculation of ADIT. Has Staff reviewed these calculation differences?

A. Yes. Staff has reviewed the calculation differences and will address each separately below.

TAX DEPRECIATION FORMULA DIFFERENCE: Staff agrees with Liberty Midstates – MO witness Fallert that because of how the tax depreciation calculation is set up, the tax depreciation for each year should not be added to the previous year's tax basis prior to multiplying by the tax depreciation rate for each month before summing multiple years' tax depreciation. Staff will modify this calculation and include the corrected amount as part of the true-up audit.

BOOK PLANT AND RESERVE DIFFERENCES: Staff unintentionally used different book plant and reserve amounts for its tax depreciation calculations, as compared to how Staff determined the net plant inclusion in the rate base calculation. Staff will include the cost of removal information when updating this calculation for true-up.

MIDSTATES ALLOCATION ISSUE: When Staff calculated the depreciation related tax timing differences for the general plant that is allocated to Liberty Midstates – MO, Staff erroneously allocated this difference using the Midstates allocator, rather than the Missouri district allocator. Staff will utilize the correct allocation methodology as part of the true-up audit.

EXCLUSION OF NEGATIVE BALANCES: As part of direct, Staff removed some negative cost basis balances when calculating the tax depreciation. Staff removed these amounts until it could determine what these negative balances represented. Staff now understands these negative basis balances are corrections/adjustments of previously recorded additions and not, in fact, retirements. Staff will include these negative amounts as part of its calculation of tax depreciation when determining ADIT for purposes of the true-up audit.

Q. On page 6, lines 3-6 of Company witness James A. Fallert’s rebuttal testimony, he states “…Staff’s, worksheet inappropriately included these items (unprotected tax timing differences) as a deferred tax liability when they should have been recorded as a deferred tax asset.” Does Staff agree with this assessment?

A. Yes. This statement appears to be correct when looking at Company’s response to Staff Data Request No. 0129. However, Staff has since received additional detail underlying Liberty Midstates – MO’s historical protected and unprotected tax timing differences (specifically underlying the response to Data Request No. 0129). Staff has concerns with Liberty Midstates – MO's quantification of unprotected ADIT and, as of this filing, has not included an amount of unprotected ADIT as part of its true-up calculation. If Liberty is able to provide a reasonable and supported quantification of unprotected ADIT, Staff will consider including that amount in rate base.

INCENTIVE COMPENSATION

Q. On page 20, lines 11-13 of Liberty Midstates – MO witness Jill Schwartz's rebuttal, she states, "In discussions subsequent to the filing of its direct case, the Staff indicated its intention to withdraw its adjustments relating to incentive compensation paid to the Company's VVP Program." Is Liberty Midstates – MO witness Schwartz accurate with this statement?

A. Yes. Staff reviewed the labor contracts and specifically stated among the terms of the bargaining agreement is the Variable Pay Plan, or VPP, which is the incentive compensation plan for union employees. While Staff maintains the belief, as well as direction from the Commission, that earnings based incentive compensation should be disallowed from customer rates, it is understood that Staff must comply with the revised statutes of the State of Missouri – specifically Chapter 386.315. Staff will include all union incentive compensation costs as part of its cost of service updated for true-up.

Q. What has been Staff's and the Commission's long-standing position on earnings based compensation?

A. The Commission has consistently disallowed costs relating to incentive programs where the measurement of the incentive program was based on the financial metrics achieved by the utility in many instances.[2] The Commission has done so "because at best, a utility's level of profitability has little or no benefit for ratepayers. At worst, an increase in the utility's profitability may be harmful to ratepayers if that profitability is obtained by cutting customer service or system maintenance to cut costs and thereby increase earnings per share…because eligibility for…long-term compensation plans are based on measures of the financial return achieved by the utility, the cost of those plans should fall on the shareholders who will primarily benefit from the company's increased financial return."[3]

Each utility has the ability to design its own incentive compensation plans and the Commission's stance on financial metric based incentive compensation has been long established. Each utility should be aware that if they design their incentive compensation plan with earnings based metrics as a basis for earning that compensation, then that compensation will be at risk for exclusion from rate recovery. This does not mean that the Company cannot include financial based metrics as part of its "balanced" incentive compensation plan; it simply means it should not expect to recover the costs associated with those metrics in customer rates.

Q. Did Staff make a full assessment of whether Liberty Midstates – MO's incentive compensation scorecards were indeed "balanced"?

A. No. Liberty Midstates – MO witness Schwartz states in her rebuttal testimony, that "Staff repeatedly refers to the scorecard used for the VVP, SBP and STIP plans as being 'balanced,' a conclusion that is further confirmed by the fact that Staff has only identified

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[2] Some of these instances include EC-87-114, Union Electric; TC-89-14, Southwestern Bell; TC-93-224, Southwestern Bell; GR-96-285, Missouri Gas Energy; GR-2004-0209, Missouri Gas Energy; ER-2006-0314, Kansas City Power & Light; ER-2007-0291, Kansas City Power & Light; ER-2008-0318, Ameren UE; and most recently affirmed in the amended report and order in cases GR-2017-0215 & GR-2017-0216 filed by the Commission on March 7, 2018.

[3] AmerenUE, *Report and Order*, ER-2008-0318, page 86.

18.5 percent of the costs associated with these plans as being financial or earnings-based." However, Staff never made such an assessment. Staff's direct testimony simply identifies that the criteria utilized by Liberty Midstates – MO was what the utility considered to be a "balanced scorecard" for the relevant region or station within the Company. Staff also stated in its direct testimony that additional data and responses to Staff data requests were required from the Company in order to calculate the exact disallowance of expensed and capitalized earnings based incentive compensation, and that the issue would be revisited as part of the true-up audit in this case. These statements certainly do not align with the Company's assertion that Staff believes the scorecards are "balanced;" this is further confirmed by the fact that Staff proposed an adjustment in its direct testimony.

Further, Staff has learned through meetings and Staff data request responses that the Shared Bonus Pool (SBP) and Short Term Incentive Plan (STIP) programs are based on four categories of factors: efficiency, stakeholder, business process, and people. The adjustments made by Staff are related to earnings based compensation that was a part of the efficiency category, of which is weighted 70% for the SBP plan and 50%-65% for the STIP plan, depending on the position of the employee. For comparison, the other three categories have a weighting of 10% - 20%, depending on the whether the plan is STIP or SBP. These weightings demonstrate that earnings based compensation has a heavier weight in determining the overall incentive compensation payout than the other categories of factors.

Liberty Midstates – MO relies on the Commission's Report and Order from Case No. ER-2008-0318 as a basis for inclusion of the earnings based metrics for the SBP and STIP plans because of their assessment of the incentive compensation plans as a "balanced" inclusion of both performance based as well as earnings based compensation. The SBP and

STIP plans do have fewer performance metrics for earnings as compared with the LTIP plans; however, inclusion of those earnings based metrics would ignore the weighting of the earnings based portion of the plans, as discussed above, and ignore the most recent Commission ruling from the Spire Missouri rate case.[4] Earnings based incentive compensation should be disallowed no matter the proportion of that type of incentive compensation to the plan as a whole.

The VPP plan cannot be used as a benchmark for inclusion of earnings based compensation because of the revised Missouri statute. Staff would have disallowed any earnings based incentive compensation related to the VPP plan if not for this statute.

Q. On page 24, lines 4-7 Liberty Midstates – MO witness Jill Schwartz states "I believe it is fundamentally inappropriate to disallow such capitalized incentive costs. Such costs were capitalized in good faith and it was not until the recent Spire cases that there was any indication from the Commission that such costs were subject to disallowance." Does capitalizing earnings based incentive compensation, rather than expensing it, change the nature of the costs?

A. No. Earnings based compensation costs are earnings based compensation costs no matter how they are recorded on a utility's books and records. The long history of the Commission's treatment of earnings based compensation should have given adequate warning to every utility that those costs will likely not be recovered from ratepayers, no matter if they are expensed or capitalized. Staff proposed conceptually the same capital and expense adjustments, in many other recent rate cases as well as in Liberty Midstates – MO's last rate

[4] The Commission Order in Case Nos. GR-2017-0215 & GR-2017-0216 disallowed all earnings based incentive compensation, no matter the combination of earnings based and performance based metrics that were used to develop each plan.

case, GR-2014-0152, of which the utility stipulated to rate base values that included Staff's expense and capital adjustments for earnings based incentive compensation.

Q. Did Staff's proposed adjustments disallow all capitalized earnings based compensation and not just the amount for test year forward?

A. Yes, in Staff's direct case. Staff built off of the capitalized earnings based incentive compensation adjustments that were included in the stipulated rate base amounts as agreed to by the parties in the 2014 rate case and continued to remove reserve associated with those disallowed capital amounts. Staff also disallowed the capital and reserve associated with earnings based incentive compensation costs that were paid out subsequent to the effective date of rates from the 2014 rate case through the update period of December 31, 2017. Staff disallowed these costs on the premise that no earnings based compensation should be recovered in rates. Staff's direct position was filed on March 2, 2018, and the Commission's *Amended Report and Order* in the Spire Missouri case was issued on March 7, 2018, stating "…incentive compensation expense will not be included in rates and no part of the earnings based or equity based incentive compensation for the current case (test year through true-up period) should be capitalized in rate base going forward".

In order to best reflect the Spire Missouri amended order as well as taking into account the facts and circumstances in this case, Staff will now update its incentive compensation calculations to remove only the earnings based incentive compensation that was capitalized beginning with the start of test year in this case, July 1, 2016, through the true-up cutoff of March 31, 2018.

SURVEILLANCE REPORTING

Q. On page 33, lines 15-19 Liberty Midstates – MO witness Jill Schwartz states "The Company also wants to examine the surveillance reporting requirements, including those relating to the provision of general ledger information, that were recently agreed upon by the Staff, OPC and Spire in the latter's recent rate cases to determine if that approach will work for Liberty Utilities." Is Staff amenable to working with Liberty Midstates - MO to reach an agreement on surveillance reporting requirements?

A. Yes. Along with the surveillance reported data, Staff also requested that Liberty Midstates - MO provide its general ledger and subledger data for both direct and allocated costs on a quarterly basis. Staff also recommends the Commission order Liberty Midstates – MO start recording the accumulated depreciation reserve by FERC account in the general ledger. Currently, Liberty Midstates – MO only books the accumulated depreciation reserve as a single total amount to account 108. This practice does not allow for Staff to monitor if accumulated reserve is being calculated correctly on an account basis and recording the depreciation reserve by account also helps in verifying that retirements and additions are being correctly recorded. In addition, Staff recommends the Commission order Liberty to adjust its books and records to match the ordered rate base by district in this rate case, including the impact of any Commission adoption of rate base adjustments recommended by Staff or other parties to this case. Staff has provided a financial surveillance monitoring report template to Liberty Midstates – MO and plans to work with Liberty Midstates – MO to ensure it understands the reporting information that is being sought. It is not Staff's intention to require Liberty Midstates - MO to expend additional resources to accumulate and report additional data; this information is already created monthly through normal bookkeeping processes and is readily available. The information being sought would be helpful to not only Staff and OPC, but also Liberty Midstates - MO in its continual monitoring of division earnings. It is especially important that Staff and OPC be able to receive this information and monitor it because of Liberty Utilities and affiliates' ongoing acquisition strategy. It is apparent from Staff's review of Liberty's response to Staff Data Request No. 0020 and Staff Data Request No. 0246 that ** ______________________________ ** In the event that Liberty Utilities acquires additional utilities in between rate cases, as it already has with the acquisition of The Empire District Electric Company, among others, this activity could have a profound effect on customers' future utility rates as well as the earnings that Liberty Midstates – MO realizes due, at least in part, to changes in allocation of costs. Once Staff and Liberty Midstates - MO have an agreed upon format for providing the desired information, Staff requests that Liberty Midstates - MO begin providing this to the Commission starting with the first quarter starting January 1, 2019.

Q. On page 34, lines 1-7 of Company witness Jill Schwartz states, "I think it is fair to say that the Commission Staff is seeking multiple commitments from the Company to provide information in multiple ways. There are ongoing, information-related recommendations that Staff has made in the context of providing additional surveillance information, and recommendations that it has made in the proceeding to consider a Cost Allocation Manual for utility operations in Missouri." Does Staff believe that the information it is seeking that is described above is more appropriately provided as part of the rate case rather than the cost allocation manual (CAM) docket?

A. Yes. As stated above, Staff's goal is to work with Liberty Midstates – MO to determine the appropriate information and appropriate interval in which to provide said information. However, a CAM docket deals with general concepts such as determining the basis for how cost allocations will be determined; how to assign costs of goods and services; how services and costs will flow between affiliates; rules for retention of documents; establishment of contracts amongst affiliates; discussion of what rule compliance is necessary and how to comply; definitions of terms; how to determine the basis of costing goods and services; what variances will be needed from the rules and what good cause has been shown for those variances, etc. CAM review cases do not necessarily involve detailed review of cost specific allocation factors and results. The main goal of a CAM docket is to set out what costs and resources are allocated amongst all Company affiliates, what method is appropriate for allocation of costs and resources and provides for establishing transparency of transactions with affiliates. There is no statutory established time frame for which a CAM docket must be completed, as there is for a rate case, so there would be no definitive time period for which the Company would be required to provide data. Staff believes it is appropriate for Liberty Midstates – MO to provide any general and descriptive reporting requirements as part of the CAM docket while providing necessary ledger data, allocation data and quantitative calculations as part of the rate case docket.

AUTOMATED METER READING (AMR) DEVICES

Q. On page 39, lines 4-7 of the rebuttal testimony of Liberty Midstates – MO witness Jill Schwartz states "The Company's new AMR system will become fully operational in April 2018, which is after the update period used by the Staff in its Direct Case. We expect that this rate base addition will be reflected in both the Staff's true-up schedules and in the

Company's true-up schedules on an actual rather than pro-forma basis." Will Staff include AMR devices as part of its true-up audit?

A. Yes. At the time of this filing Staff has included all AMR investment through March 31, 2018. In response to Staff Data Request No. 0305, Liberty Utilities stated that it has installed approximately 47,167 AMR devices by the true-up cutoff date of March 31, 2018. Staff has discovered during discussion with Liberty Midstates – MO representatives that a minor amount of AMRs were put in service subsequent to the true-up cut-off date of March 30, 2018, but prior to April 16, 2018. If provided with this data, Staff will include this minor amount of AMR investment in the cost of service.

It was also relayed to Staff that approximately 2,000-3,000 more AMR devices remain to be installed; mostly in the Southeast Missouri (SEMO) district and that these devices will be installed over time prior to the end of 2018. The AMRs that have been installed as of April 16, 2018 are used and useful and the associated cost is known and measureable and, thus these costs will be included in Staff's plant and accumulated reserve balances in the true-up audit.

ERRONEOUS DEPRECIATION RATES FROM CASE GR-2014-0152

Q. Please summarize the issue regarding Liberty Midstates - MO's ordered depreciation rates for computer hardware and software accounts (399 accounts).

A. In Liberty Midstates – MO's last general rate case Case No. GR-2014-0152, it litigated depreciation rates for its hardware and software accounts. The Commission ultimately ruled in favor of Liberty Midstates – MO on this issue; however, a depreciation chart was never attached to any order or stipulation filed in that rate case. Staff compared its accounting schedules developed in Case No. GR-2014-0152 based upon the Commission's

Report and Order, with Liberty Midstates – MO's rebuttal testimony and position statements in that case. Staff found that the Company utilized incorrect depreciation rates for three of the 399 accounts when developing its tariffs. To further complicate matters, Liberty Midstates – MO is using depreciation rates related to its corporate account 399.0 and direct plant accounts 399.3, 399.4, and 399.5 that are different than those stipulated to in GR 2014-0152; these rates were included correctly in Staff's accounting schedules in the last case.

Q. What is Staff's current position regarding the use of erroneous depreciation rates for the above accounts since the last rate case?

A. Staff will remove its reserve adjustments for the three accounts (Corporate Accounts 399.1, 399.3, and 399.5) that were incorrectly included in Staff's Report and Order accounting schedules in the last rate case. Tariffs were designed based on these accounting schedules, and since it was Staff that included the erroneous rates, Staff withdraws its proposed adjustments for those litigated accounts. However, for the stipulated accounts that were correctly included in the Staff Report and Order accounting schedules, but were not used by Liberty Midstates – MO (Corporate Account 399.0, Direct Account 399.3, 399.4, 399.5), Staff still recommends that depreciation reserve adjustments be adopted to reflect the correct depreciation rates, and will update those adjustments through the true-up cutoff date of March 31, 2018. Staff will ensure that a chart of Commission approved depreciation rates is part of the record in this rate case and Staff requests that the Commission order Liberty Midstates – MO to correct the reserve amounts for the stipulated accounts above in their books and records on a going forward basis.

Q. On page 8, lines 18-23, Liberty Midstates – MO witness James A. Fallert states, "As I mentioned earlier, when we split these accounts between system and PC assets consistent with the Commission's order in GR-2014-0152, Staff's $1.7 million increase in the reserve actually becomes a $0.2 million decrease. The differences between Staff's approach and the Company's approach are illustrated on Schedule JF-R1 attached to this testimony." Does Staff believe the Company's quantification shown on Schedule JF-R1 is a more appropriate calculation rather than Staff's quantification of the depreciation rate discrepancy in the direct filing of approximately $1.7 million?

A. No. First, the amount is moot because, as discussed above, Staff will be removing the reserve adjustments it proposed in direct testimony for corporate accounts 399.1, 399.3, and 399.5. Further, these rates will be corrected on a prospective basis with Staff's proposed depreciation rates for these accounts. Please see the surrebuttal/true-up direct testimony of Staff witness Stephen B. Moilanen for discussion of proposed depreciation rates in this case. Second, in the last rate case the depreciation rate for corporate account 399.0 was never litigated, but rather was stipulated. The appropriate rate of 4.75% was utilized in Staff's Report and Order accounting schedules and reflected in tariffed rates; however, Mr. Fallert is incorrectly claiming in Schedule JF-R1 that the appropriate rate is 14.29%, which is the rate that was used to set tariffed rates.

ESTIMATED PROPERTY TAX

Q. On page 10, lines 11-16 of Liberty Midstates – MO witness Jill Schwartz's rebuttal testimony, she states "At the same time, as Mr. Tim Lyons also explains in his rebuttal testimony, this historic opportunity to flow-through federal tax benefits in this case also provides an opportunity and, we believe, an obligation to re-examine and adopt a new approach for recognizing the ongoing impact of local property tax increases that are occurring in this case and that, like the impacts of federal Tax Act, will occur in the future." Does Staff believe it is appropriate to include estimated property tax that will not be assessed nor billed until after March 31, 2018, as part of the current rate case because of the TJCA enactment or for any other reason?

A. No. Staff was unable to find any rebuttal testimony from Mr. Lyons that expounds on the new proposal for inclusion of estimated property taxes as discussed by Ms. Schwartz above. Estimated property tax is not known and measureable and should not be included in the cost of service in this case. Further, its inclusion in cost of service would also be a violation of the principle of matching revenue, expense, and investment at the same period in time.

The Commission granted an estimated level of property taxes associated with the AMR devices in the recently decided Spire Missouri rate case, GR-2017-0215. Similar to that case, Liberty Midstates – MO has also installed AMR devices for which the property taxes will not be assessed or incurred prior to the true-up cutoff in this case. Also similar to the Spire Missouri rate case, Liberty Midstates – MO will have recovered the estimated property tax through regulatory lag. In the Spire Missouri rate case, renegotiation of the AMR contract allowed Spire Missouri to recoup the estimated property taxes for the AMR devices prior to the effective date of rates in that case. Liberty Midstates – MO will also be able to recover any estimated property taxes through regulatory lag if an increase in revenue from ** ________________ ** occurs subsequent to rates being set in this case. If inclusion of estimated property taxes is included in this case, there is a possibility for double recovery if those estimated property taxes are recovered in this current case as well as when they are actually incurred and included in the cost of service in a future rate proceeding.

The timing of Spire Missouri's rate case was also different than Liberty Midstates – MO. Spire Missouri's true-up cutoff date was prior to the TCJA going into effect. The Commission chose to reach past the true-up cutoff in that rate case to reflect the lower federal corporate tax rate in the cost of service and, because of that, also included an amount for estimated property taxes in rates. In this current case for Liberty Midstates – MO, the TCJA was enacted into law approximately three months prior to the true-up cutoff in this case. For this reason, there is no need to reach beyond the true-up cutoff to pick up any estimated property taxes.

Q. What level of annualized property taxes did Staff include in this case?

A. Staff included the actual property tax paid by Liberty Midstates – MO at December 31, 2017, only three months prior to the true-up cutoff in the current rate case.

TRUE-UP - SUMMARY

Q. Please summarize your true-up direct testimony.

A. This true-up direct testimony presents an overview of Staff's true-up audit and the associated revenue requirement for Liberty Midstates – MO. Staff's true-up accounting schedules support its recommendations for the amounts of the rate revenue increases the Commission should approve for Liberty Midstates – MO. Staff's recommended revenue requirement for Liberty Midstates – MO is based on actual historical information through the period ending March 31, 2018. Staff considered all relevant and material components of the revenue requirement calculation when developing the true-up revenue requirement. The components generally consist of capital structure and return on investment, rate base investment, and income statement results, including revenues, depreciation expense and income taxes.

Q. Do the areas addressed in Staff's true-up reflect the Commission's November 30, 2017, Order Adopting Procedural Schedule in this case?

A. Yes, with minor exception. The Commission stated the following on paragraph 6 and 7, page 8 of said Order:

> 6. Anticipated true-up items include changes to plant-in-service, depreciation reserve, all other rate base items, revenues (all categories), customer growth, uncollectible expense, pensions and other post-retirement employee benefit costs, payroll (including changes in pay rates, number of employees, overtime, etc.), other employee benefits, payroll taxes, allocations, rents and lease expense, insurance expense, rate case expense, depreciation expense, amortizations, income taxes, property taxes, capital structure, capital costs, and other significant items that must be considered to maintain a proper relationship of revenues, expenses, and rate base. Significant in the context of this paragraph will be measured by the smallest adjustment made during the true-up audit from the list of items indicated in this paragraph.
>
> 7. No party is precluded from proposing an additional item for true-up that causes a significant increase or decrease in Liberty's cost of service, i.e., in its revenues, expenses or investment, or proposing that any item(s) listed above not be trued-up.

Q. What area in paragraph 6 did Staff not address as part of its true-up audit?

A. Staff did not true-up property taxes as that is not an issue that Staff typically includes in its true-up audit. In Staff's direct filing, the actual property tax paid as of December 31, 2017, was included in Staff's case. This amount is the highest amount paid by Liberty Midstates - MO since owning the former Atmos properties and is a known and measureable amount that was paid a mere three months prior to the true-up cutoff. Because it will not be known what Liberty Midstates – MO will pay for property taxes at year-end 2018 for many months; any attempt to "true-up" property taxes through the end of the true-up period in this case would rely solely upon speculative values.

Q. Did Staff address any additional items as part of its true-up audit?

A. Staff has included the isolated union labor increase that goes into effect in June 2018 of which was established by the union bargaining agreement, subsequent to our true-up cut-off. The amount is known and measureable and is appropriate to include in Staff's cost of service. ** ____________________

____________________ **

Q. Did Staff include costs in Liberty Midstates – MO's cost of service that were not included at the time Staff filed its Direct Testimony on March 2, 2018?

A. Yes. Staff has included costs related to Liberty Midstates – MO's purchase and installation of AMRs and also the storage shop constructed in Hannibal, MO. Staff also included the most current employee benefit rate levels and most current level of labor costs based on actual employees and their most recent salary levels. The labor and employee benefit issues are addressed in more detail in Staff witness Asad A. Shakoor's true-up direct testimony. The issue regarding the Hannibal shop is discussed in more detail in Staff witness John P. Cassidy's true-up direct testimony and the AMR and property tax issues are discussed earlier in this testimony.

Q. How did Staff conduct its true-up audit?

A. Staff updated Liberty Midstates – MO's cost of service through March 31, 2018, using the same methods and approach it used in its initial filing in this proceeding.

Q. What capital structure and return on equity is Staff using as of March 31, 2018?

A. Staff is using Liberty Utilities Company (LUCo) capital structure as of March 31, 2018, which consists of 42.83% common equity and 57.17% long term debt and a return on equity of 10.00%. Staff's true-up recommendations concerning capital structure and debt rates are discussed in the surrebuttal/true-up direct testimony of Staff witness David Murray of the Financial Analysis Unit.

Q. Based on changes discussed above, what is Staff's recommended true-up revenue requirement for Liberty Midstates – MO?

A. Staff is recommending a revenue requirement increase in the range of $3.1million to $3.4 million, based on the low, mid and high end of Staff's recommended return on equity of 9.50%, 9.75%, and 10.00%. Based on a recommended return on equity of 10.00%, Staff's revenue requirement increase by district is shown below:

DISTRICT	REVENUE REQUIREMENT
NEMO	$1,442,036
SEMO	$1,682,411
WEMO	$287,597
TOTAL COMPANY	$3,412,044

TRUE-UP – DETAILED ISSUES

a. Vegetation Management

Q. How did Staff true-up vegetation management/right of way expenses?

A. Staff included the actual level of vegetation management expenses incurred as of the 12 months ending March 31, 2018.

b. Income Tax

Q. How did Staff true-up income taxes?

A. Staff continued to utilize the corporate tax rate of 21% and applied that percentage to Staff's true-up taxable income.

c. Incentive Compensation

Q. How did Staff true-up incentive compensation?

A. Staff modified its disallowance adjustments in response to Liberty Midstates – MO witness Jill Schwartz, as discussed in my surrebuttal testimony above, by removing any disallowances for earnings based incentive compensation prior to the beginning of the test year established in this case in order to be consistent with the recent Spire Missouri Amended Report and Order. Staff also recalculated the reserve associated with those capitalized earnings based incentive compensation adjustments through March 31, 2018.

d. Accumulated Deferred Income Tax (ADIT)

Q. How did Staff true-up the accumulated deferred income tax?

A. Staff calculated the corrections to protected ADIT in response to Liberty Midstates – MO witness James A. Fallert, as discussed in my surrebuttal testimony above. Staff also recalculated its tax depreciation by including bonus depreciation on all allocated plant additions put in service prior to the tax reform change that occurred January 1, 2018. Staff will update the unprotected ADIT associated with non-depreciation related tax timing differences as of March 31, 2018 once a reasonable amount is determined.

e. Erroneous Plant and Reserve Adjustments

Q. How did Staff true-up the erroneous plant and reserve adjustments?

A. Staff updated the accumulated reserve associated with each erroneous plant adjustment through the true-up cutoff of March 31, 2018.

f. State Corporate Income Tax Rate

Q. Are there any other potential tax reform changes that Staff is aware of that could affect Liberty Midstates – MO's cost of service?

A. Yes. There is currently legislation being discussed regarding a potential reduction to the Missouri corporate income tax rate. Staff continues to monitor this issue and will determine if further adjustments are appropriate later in the pendency of this proceeding.

Q. Does this conclude your surrebuttal/true-up direct testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Liberty Utilities (Midstates Natural Gas) Corp. d/b/a Liberty Utilities' Tariff Revisions Designed to Implement a General Rate Increase for Natural Gas Service in the Missouri Service Areas of the Company	))))))	Case No. GR-2018-0013

AFFIDAVIT OF LISA M. FERGUSON

STATE OF MISSOURI)
) ss.
CITY OF ST. LOUIS)

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 Surrebuttal Testimony and True-Up Direct 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 City of St. Louis, State of Missouri, at my office in St. Louis, on this 7th day of May, 2018.

DEZTKNE LYTTLE
Notary Public - Notary Seal
State of Missouri
Commissioned for St. Louis City
My Commission Expires: May 04, 2021
Commission Number: 17743376

Notary Public