

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

In the Matter of the Propriety of the)
Rate Schedules for Electric Service of)
The Empire District Electric Company) File No. ER-2018-0228

and

In the Matter of the Propriety of the)
Rate Schedules for Gas Service of)
The Empire District Gas Company) File No. GR-2018-0229

RESPONSE TO COMMISSION ORDER

COME NOW The Empire District Electric Company (“EDE”) and The Empire District Gas Company (“EDG”) (collectively, “Empire”), and, in response to the *Order Scheduling Oral Argument Regarding the Issuance of Accounting Authority Orders to Address the Effect of Federal Tax Cuts* issued herein by the Missouri Public Service Commission (“Commission”) on April 18, 2018, respectfully state as follows:

1. The Commission has scheduled oral argument “to address the question of whether the Commission should issue an accounting authority order in each of these cases to preserve any excess revenues resulting from the income tax rate changes for possible adjustment in these or future rate cases.” The Commission also provided that any party wishing to submit written argument could do so by no later than May 17, 2018.

2. A non-unanimous stipulation and agreement (the “Stipulation”) was filed by EDE and certain other parties in Case Nos. EO-2018-0092 (EDE’s Customer Savings Plan) and ER-2018-0228 (EDE’s tax docket).¹ The provisions of the Stipulation related to the Tax Cuts and Jobs Acts of 2017 (the “Act”) are set forth below.

¹ The Office of the Public Counsel (“OPC”) objected to the Stipulation in both referenced cases. All other parties are either signatories to the Stipulation or did not object. A hearing was

24. Tax Reform. EDE shall file revised retail tariff sheets in an appropriate timeframe that would allow such tariffs to take effect October 1, 2018. The tariffs shall reflect a reduction in base rate revenue as the result of the implementation of the Tax Cuts and Jobs Act of 2017. The reduction in the annual revenue requirement represents the calculated revenue requirement utilized in current base rates utilizing a federal corporate income tax rate of 35%, compared to a recalculated revenue requirement using the reduced federal corporate income tax rate of 21%. The attached Appendix B displays the annual reduction, along with the revised annual revenue requirement as well as the allocation of the reduced revenue requirement to the individual rate classes.

25. Excess ADIT. EDE shall establish a regulatory liability to account for the tax savings associated with excess Accumulated Deferred Income Taxes (“ADIT”).

a. EDE will record a regulatory liability for the difference between the excess ADIT balances included in current rates, which was calculated using the 35% federal corporate income taxes, versus the now lower federal corporate income tax rate of 21%.

b. EDE is in the early stages of evaluating the cost and ability to use the Average Rate Assumption Method (“ARAM”) as a method for computing and normalizing excess ADIT. If EDE determines that it is unable to use the ARAM, EDE shall notify the Signatories within thirty (30) days of such determination. EDE shall provide testimony and support in its next general rate case of its proposed methodology in dealing with the balances.

c. The calculation of the Regulatory Liability of excess ADIT will begin as of January 1, 2018.

d. The Signatories intend to appropriately reflect excess ADIT in future customer rates using a methodology consistent with the tax normalization requirements specified by IRS normalization principles. The Signatories agree that, in the event the IRS asserts that the terms of this Stipulation create a violation of normalization requirements, this Stipulation shall be amended to cure and prevent any normalization violation.

26. The only issue remaining in File No. ER-2018-0228 is the design of rates to flow back to customers the annual revenue requirement reduction provided for above in paragraph 24.

3. The Stipulation provides for a known date for rate reductions for every class and category of electric service to reflect the percentage reduction in EDE’s federal-state effective income tax rate. Approval of the Stipulation would eliminate any questions about legislation,

held in Case No. EO-2018-0092 on May 9-11, 2018, with the Stipulation serving as the joint position statement of the signatories on all issues.

process, or legal issues surrounding implementation of the Act's tax rate reductions and would provide nearly \$18 million of immediate benefits to EDE's customers. Approval of the Stipulation would also eliminate the need to answer the question of whether the Commission should issue an accounting authority order for EDE related to the Act.

4. Upon Commission approval of the Stipulation in Case Nos. EO-2018-0092 (EDE's Customer Savings Plan) and ER-2018-0228 (EDE's tax docket), Empire would propose to resolve Case No. GR-2018-0229 (EDG's tax docket) on similar terms (filing of revised retail tariff sheets to reflect a reduction in base rate revenue as the result of the implementation of the Act in an appropriate timeframe that would allow such tariffs to take effect October 1, 2018, and establishment of a regulatory liability for excess ADIT). Such a resolution would eliminate legal issues surrounding implementation of the Act's tax rate reductions, would provide nearly \$775,000 of immediate benefits to EDG's customers, and would eliminate the need to answer the question of whether the Commission should issue an accounting authority order for EDG related to the Act.

5. In the event the Stipulation is not approved in Case Nos. EO-2018-0092 (EDE's Customer Savings Plan) and ER-2018-0228 (EDE's tax docket) and/or Case No. GR-2018-0229 (EDG's tax docket) is not resolved on similar terms, thus requiring the need to answer the question of whether the Commission should issue an accounting authority order ("AAO") for EDG and/or EDE related to the Act, Empire notes that an AAO may be authorized by the Commission only in certain circumstances. The Commission previously found as follows regarding AAOs:

An AAO allows the "deferral" in the booking of a current expense to a utility's balance sheet as an asset. The cost is booked by a utility based upon the possibility that a regulatory authority will agree to allow recovery of the cost in a future rate case. This allows costs to be recorded in a period other than that in

which they were actually incurred. An AAO gives a utility the opportunity to obtain future rate recovery of extraordinary costs, even if those costs were not actually incurred within an ordered test year for a general rate proceeding.

2014 Mo. PSC LEXIS 665, *4-5.

6. Whether the Commission is considering an AAO for a regulatory asset or a regulatory liability, the standard for granting an AAO is the same. An AAO, which is authorized by the Uniform System of Accounts (“USOA”), is to deal with the financial effects of extraordinary items or events. The USOA defines an “extraordinary item” as one:

related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence . . . they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company and which would not reasonably be expected to recur in the future.

7. Pursuant to the USOA, the Commission has applied the following criteria for granting an AAO: (1) the costs are associated with an event that is extraordinary, unusual, and unique, and (2) the costs are material in terms of financial impact on the utility. The materiality question would be a fact-specific inquiry requiring evidence from each utility. Company-specific evidence may also be required on the issue of whether the tax rate reduction would qualify as extraordinary, unusual, and unique. Recently, the Commission determined in a Missouri-American Water Co. case that “[t]here is nothing unusual or extraordinary about paying property taxes to warrant an AAO. It is a recurring expense.” Report and Order issued December 20, 2017, in File No. WU-2017-0351.

8. The Commission’s order of April 18, 2018, raises the question of “whether the Commission should issue an accounting authority order in each of these cases to preserve any excess revenues resulting from the income tax rate changes for possible adjustment in these or future rate cases.” The Commission’s order of February 21, 2018, however, directed each utility

to “quantify and track all impacts of the Tax Cuts and Jobs Act of 2017 potentially affecting electric service rates from January 1, 2018, going forward.” It is important to note that “AAOs are not the same as ratemaking decisions, and that AAOs create no expectation that deferral terms within them will be incorporated or followed in rate application proceedings.” *Missouri Gas Energy v. PSC*, 978 S.W.2d 434, 438 (Mo.App. W.D. 1998). Even if the criteria of materiality and exceptionality are satisfied and an AAO is issued, a rate change may only operate prospectively, and rates may not be confiscatory.

WHEREFORE, EDE and EDG respectfully submit this Response to Commission Order and request such relief as is just and proper under the circumstances.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that the above and foregoing document was filed in EFIS on this 17th day of May, 2018, with notice of the same being sent to all counsel of record.

Diana C. Carter