

Exhibit No.: _____
Issue(s): Tax Credits Reduction of Income Tax/
Income Tax Reduction to Sibley AAO
Witness/Type of Exhibit: Riley/Rebuttal
Sponsoring Party: Public Counsel
Case No.: ER-2022-0129 and ER-2022-0130

REBUTTAL TESTIMONY

OF

JOHN S. RILEY

Submitted on Behalf of the Office of the Public Counsel

**EVERGY METRO, INC. D/B/A
EVERGY MISSOURI METRO
AND
EVERGY MISSOURI WEST, INC. D/B/A
EVERGY MISSOURI WEST**

CASE NOS. ER-2022-0129 AND ER-2022-0130

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Denotes Confidential information that has been redacted

July 13, 2022

PUBLIC

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EVERGY METRO, INC D/B/A EVERGY MISSOURI METRO
EVERGY MISSOURI WEST, INC, D/B/A EVERGY MISSOURI WEST
CASE NOs. ER-2022-0129 & ER-2022-0130

1 **Q. Are you the same John S. Riley that filed direct testimony in this case on behalf of the**
2 **Office of the Public Counsel (“OPC”)?**

3 A. Yes.

4 **Q. Why are you filing rebuttal testimony in this case?**

5 A. I am filing testimony in order to identify Staff’s failure to include Evergy Metro’s general
6 business credits (“GBC”) in the Staff calculation of current income tax expense for this
7 general rate case. This recognition will also have an impact on the Federal and MO State
8 income tax offset within the Cash Working Capital calculations that adjust rate base. In
9 addition, it has come to my attention that Company and Staff have continued to include a
10 substantial Sibley AAO balance in Evergy West rate base. In direct testimony, I proposed
11 that the Form 4797 losses for Metro and Evergy West offset existing rate base net operating
12 loss (“NOL”) balances.¹ A great deal of the 4797 losses for Evergy West were due to the
13 closure of the Sibley Generating Plants. The tax benefits associated with the Sibley closure
14 should be reflected against the Sibley AAO balance rather than the Company’s NOL balance.
15 This will reduce the AAO balance included in rate base. I am therefore filing rebuttal to both
16 update my recommendation from direct testimony and to respond to Staff’s failure to include
17 the Form 4797 losses for Evergy West as an offset to the Sibley AAO balance.

¹ The Company sells or abandons unused business assets. The transaction results (gain/loss) are recorded on a tax form numbered 4797. The predominant amounts recorded are losses.

1 **TAX CREDITS APPLIED TO STAFF INCOME TAX CALCULATIONS**

2 **Q. Please explain the nature of a tax credit.**

3 A. Tax credits are creations of the federal government that are designed to encourage a particular
4 business activity. Tax credits are different than tax deductions in that a deduction is a
5 subtraction from taxable income. A credit is a direct subtraction from the tax liability that is
6 calculated on that taxable income. A credit can be much more lucrative. It is a dollar for
7 dollar reduction in tax. However, the GBC cannot be used to offset a company's tax liability
8 if it is already zero. In the event that a GBC is not fully used to offset a company's tax liability,
9 any unused amount is carried forward for up to a 20-year period.

10 **Q. The GBC is not just one type of tax credit. Can you provide some reference to what**
11 **credits comprise the balance of the GBC?**

12 A. **Investopedia** provides a clear, concise explanation of the GBC

13 The general business tax credit is unique in that it is not a single,
14 separate credit. Instead, it's a collection of specific tax credits that
15 promote various business activities, including research, oil recovery,
16 reforestation, and starting a pension plan.

17 Before filling out Form 3800. You must first claim the individual tax
18 credits on their relevant tax forms, each calculated under its own set
19 of rules. Next, carry over the resulting combined credit to the General
20 Business Credit Form 3800 to determine the overall allowable credit.²

21 Part III of the attached Form 3800 (confidential Schedule JSR-R-01) lists all the credits that
22 Everygy is eligible for. The prominent credits on the list are **Increasing research activities,**
23 **Low income housing** and **Renewable electricity, refined coal, and Indian coal**
24 **production.**³

² <https://www.investopedia.com/terms/g/general-business-tax-credit.asp>

³ Even though I mention the Staff Schedule 11 line item "Wind Production Credit," the general application is the GBC as a whole.

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1 **Q. Did Staff apply any tax credits to the income tax calculation within its Schedule 11 for**
2 **Evergy Metro?**

3 A. Yes. Staff applied a “Research and Development Tax Credit” of \$1,879,283 and a fuel tax
4 credit of \$4,899 to the initial calculation of Federal income tax.

5 **Q. Has Staff ever included additional business tax credits in its calculation of income taxes**
6 **in a general rate case?**

7 A. Yes. Staff had included an amount on the “Wind Production Credit” line to adjust the federal
8 income tax in the Ameren general rate case ER-2021-0240.⁴ I am not sure if that amount is
9 purely production tax credits (“PTC”) or is a GBC amount, which would include PTCs.

10 **Q. To your knowledge, had Staff applied this broad application of tax credits to general**
11 **rate cases prior to the Ameren case you mentioned?**

12 A. I don’t believe it has. One reason would be that PTCs are a fairly new development so Staff
13 didn’t even have a designated line on the tax calculation schedule until recent years. The
14 Research Credit and the refundable Fuel Tax credit appear to be the only ones applied in a
15 consistent manner in past cases.

16 **Q. Is there a limitation as to how much of a corporation’s tax liability that a general**
17 **business credit may offset?**

18 A. Basically, the GBC may offset 75% of the calculated tax liability of the Company.⁵ I am
19 including the Schedule J and the Form 3800 from Evergy’s 2020 consolidated federal income
20 tax return for reference, as confidential Schedule JSR-R-02. Line 4 of the Schedule J is the
21 calculated income tax. Line 5c is the General business credit applied to line 4. The credit is
22 equal to 75% of the calculated income tax amount. The remaining amount is the net total tax

⁴ The Ameren case resulted in a Stipulation & Agreement so no application of tax credits was ever formalized.

⁵ Simplistic explanation is easier to understand than the instructions of Form 3800 where line 13 is .25 of the Net Regular tax and the credit is equal to subtraction of line 15 from 11, if greater than zero.

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1 the Company ultimately owes for tax year 2020. The fact that Evergy applies these tax credits
2 to its preliminary tax liabilities should signal Staff that it should follow suit in its test year
3 calculations.

4 **Q. What adjustment did you apply to the federal and state income taxes that Staff has**
5 **calculated on Accounting Schedule 11?**

6 A. I began with Staff's Column C, **Test Year** federal income tax balance on line 22 of
7 \$37,701,890. Next, I calculated 75% of the balance as a General Business Credit, which was
8 \$28,276,418, and inserted that amount on the line 23, **Wind Production Credit**. This inserted
9 amount flows through the federal and state tax calculations and adjusts the income tax balance
10 added to net income on the Accounting Schedule 09, Income Statement. Because I am not
11 intending to walk through every change within the Accounting Schedules here in testimony,
12 I have included the adjusted Staff Accounting Schedules 1, 2, 8, 9 and 11 as JSR-R-03. To
13 summarize the effect, the Revenue Requirement Schedule 01 now indicates that an Additional
14 Net Income Requirement, for the mid-point, is a negative \$24,748,591.⁶

15 **Q. Does the adjustment to the federal and state income tax balances create a change in the**
16 **Cash Working Capital ("CWC") calculations?**

17 A. Yes. The federal balance will need to be adjusted downward, but I am uncertain as to the
18 exact value of the adjustment at this time. In addition, the Commission needs to order an
19 adjustment to the state tax component of the CWC calculation to reflect the fact that the
20 Company has not paid state income tax for at least three years, so the revenue lag associated
21 to the state income tax needs to be adjusted to be 365 days. This is keeping in line with
22 Commission order that recognized nonpayment of income taxes should be calculated with an

⁶ The Mid-Point reference is to the three columns of calculations that Staff presents in the EMS run. Mid-point is the middle column that uses the middle choice of its rate of return range. The mid-point is the 6.77%. Typically, Staff mentions the revenue requirement of this mid-range column as its adjustment.

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1 annual lag due to the ratepayer paying for the tax liability but the Company not paying to the
2 taxing authority.⁷

3 **Q. Do you have some reservation as to the accuracy of the EMS run calculations in its**
4 **present form?**

5 A. Yes. I'm concerned that the original inserted GBC amount of \$28,276,418 which adjusted
6 the test year tax amount of \$37,701,890 should be reduced when it offsets the mid-point
7 federal tax of \$31,123,547 (75% = \$23,342,660 credit). As I pointed out earlier, the credit
8 amount should reflect 75% of the amount of tax due or \$23,342,660. This would increase the
9 net federal income tax from \$2,842,230 to \$7,780,887. A \$4,938,657 increase. I don't claim
10 to have extensive knowledge of the "behind the scenes" workings of the EMS software and
11 will consult Staff personnel on my adjustments to the EMS run. I would hope to have an
12 accurate adjustment to the revenue requirement for surrebuttal testimony.

13 **Q. Keeping in mind that the actual adjustments may need some further tweaking, could**
14 **you summarize your position on the application of tax credits to the income tax liability**
15 **calculated by Staff?**

16 A. Yes. Staff should recognize that Evergy is applying General Business Credits in an amount
17 up to 75% of the corporation's federal income tax computations and should do the same in its
18 case. As I pointed out in direct testimony, Evergy Metro has a sufficient balance of GBC to
19 apply to income taxes until the next general rate case. Staff should be applying tax credits in
20 any case where the utility has sufficient credits to do so.

⁷ Case GR-2021-0108, Report & Order, page 29

TAX REDUCTIONS APPLIED TO SIBLEY AAO

Q. Does Staff generally calculate and include in its test year, assessments for the income tax effect of the sale or abandonment of a utility’s plant or other assets?

A. Not to my knowledge. The revenues included in the income statement calculations of a general rate case consist of the sales to the utility’s customers. Any tax calculations that could be attributed to something other than sales revenues appear to be ignored.

Q. What effect did the sale/abandonment of Sibley generating plants have on the taxable income of Evergy West/GMO?

A. Company answer to OPC data request 1316 (confidential Schedule JSR-R-04) indicates that the Sibley premature retirement (loss on sale/abandonment) was a reduction to taxable income in 2018 of ****_____****. This reduction should be applied to the AAO balance since it directly relates to Sibley plants.

Q. What would be the tax effect of this income reduction?

A. Using a composite tax rate of 23.84%, the tax liability associated with the closure of Sibley would be ****_____****. Applying the WACC of 7.25% to this balance for all of 2019, 2020, 2021 and 2022 (48 months) would cause the balance to increase by ****_____**** in interest. So any AAO balance pertaining to Sibley should be adjusted downward by ****_____****.

Q. Are there other tax balances that should be applied to the Sibley AAO balance?

A. Accumulated and excess deferred taxes and the associated WACC for 48 months should also be a reduction to the balance. I have only offered income tax losses in my testimony because I am confident that neither the Company nor Staff have adjusted any balances for the income tax affect. I have not yet reviewed the deferred tax balances that Company and Staff have applied to Sibley so I will make adjustments in surrebuttal if needed.

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1 **Q. Could you summarize your adjustment on the Sibley AAO?**

2 A. The retirement of Sibley allowed the Company a taxable benefit that will not be recognized
3 by Staff's accounting schedules. The Commission should recognize this benefit of
4 **_____** and reduce the Sibley AAO balance accordingly.

5 **Q. Does this conclude your rebuttal testimony?**

6 A. Yes, it does.

7