

Exhibit No.: _____
Issue(s): Southwest Power Administration Payment
Projects Written-Off and/or Non-Recurring
Witness/Type of Exhibit: Robertson/Rebuttal
Sponsoring Party: Public Counsel
Case No.: ER-2011-0004

REBUTTAL TESTIMONY

OF

TED ROBERTSON

Submitted on Behalf of the Office of the Public Counsel

EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2011-0004

April 18, 2011

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**REBUTTAL TESTIMONY
OF
TED ROBERTSON**

**EMPIRE DISTRICT ELECTRIC COMPANY
CASE NO. ER-2011-0004**

9 **I. INTRODUCTION**

10 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

11 A. Ted Robertson, PO Box 2230, Jefferson City, Missouri 65102-2230.

12
13 Q. ARE YOU THE SAME TED ROBERTSON THAT HAS PREVIOUSLY FILED
14 DIRECT TESTIMONY IN THIS CASE?

15 A. Yes.

16
17 **II. PURPOSE OF TESTIMONY**

18 Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

19 A. I will provide rebuttal to the Direct Testimony of Missouri Public Service
20 Commission (MPSC) Staff witnesses Mr. Mark L. Oligschlaeger and Mr. Paul R.
21 Harrison regarding the ratemaking treatment of the Southwest Power
22 Administration (SWPA) Payment and Company witness, Mr. W. Scott Keith,
23 regarding the write-off of costs associated with two projects no longer deemed
24 viable, expense booked that is associated with the Springfield, Missouri, Cities
25 Utilities Carbon Sequestration Project, and expense booked that is associated
26 with a software needs assessment project conducted by KPMG.

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III. SOUTHWEST POWER ADMINISTRATION PAYMENT

Q. WHAT IS THE ISSUE?

A. The issue concerns the ratemaking treatment of the Southwest Power Administration Payment discussed in my Direct Testimony.

Q. WHAT DID YOU RECOMMEND?

A. In my Direct Testimony, I recommended that the payment, net of appropriate tax impacts, be used as an offset to Company's rate base and that the unamortized balance be amortized to the income statement over the life of the associated replacement energy and capacity purchased.

Q. DOES YOUR RECOMMENDATION DIFFER FROM THAT OF THE MPSC STAFF?

A. Yes, but only with regard to the tax impact on the payment.

Q. WHAT IS THE MPSC STAFF POSITION?

A. On page 39 of the *Staff Report Cost Of Service* filed with the Direct Testimony of the MPSC Staff, Mr. Oligschlaeger states:

1 The approximate \$26.6 million payment is a prepayment from the
2 federal government to Empire for future economic damages related
3 to reduced hydroelectric capacity at Ozark Beach. Empire has
4 stated that it intends to flow back this payment to customers in the
5 future over an appropriate period of time. Accordingly, the Staff
6 recommends that the SWPA payment be included in Empire's rate
7 base as an offset in this case. The Staff does not believe that any
8 amortization of this amount as a reduction to expense is
9 appropriate until such time as the capacity restrictions go into effect
10 at Ozark Beach. Given its taxable status, the Staff is treating this
11 payment as a tax timing difference in its income tax accounting
12 schedule to recognize that taxes are currently due to the federal
13 and state governments regarding this payment, but that this amount
14 will not be reflected on Empire's income statement until later
15 periods. However, in recognition that receipt of this payment from
16 the SWPA is a one-time event, the Staff is proposing to spread the
17 tax effect of this payment over a three-year period. Reflecting a
18 portion of the tax effect of this item in Empire's rates will create a
19 deferred tax asset on Empire's balance sheet.
20
21

22 The MPSC Staff's proposed spreading of the tax effect over a three (3) year
23 period is also identified on page 86 of the *Staff Report Cost Of Service* wherein
24 income tax issues are discussed by MPSC Staff witness, Mr. Paul R. Harrison.
25

26 Q. DOES PUBLIC COUNSEL SUPPORT THE MPSC STAFF POSITION THAT THE
27 AMORTIZATION OF THE PAYMENT NOT OCCUR UNTIL SUCH TIME AS THE
28 CAPACITY RESTRICTIONS GO INTO EFFECT?

29 A. Yes. Based on information known to-date, the implementation of the White River
30 Basin, Arkansas Minimum Flows Project may not be implemented until year 2013 or
31 later. Postponing the amortization of the Southwestern Power Administration

1 payment, while affording it rate base treatment in the current case, until the
2 Company's next general rate increase case will provide a better matching of the
3 payment and capacity restriction costs.
4

5 Q. DOES PUBLIC COUNSEL SUPPORT THE MPSC STAFF POSITION THAT THE
6 TAX EFFECT OF THE PAYMENT BE SPREAD OVER A THREE YEAR PERIOD?

7 A. No. Public Counsel recommends that no part of the SWPA payment be included in
8 the calculation of income taxes for the current case. My recommendation is based
9 on, 1) the Company has requested a private letter ruling from the Internal Revenue
10 Service to treat the payment as a like-kind exchange of assets. If the Internal
11 Revenue Service response to the Company's request is determined to be favorable,
12 no income taxes will be assessed against the payment. Thus, if any income taxes
13 are included in the current case for the SWPA payment, they would represent cash
14 flows from ratepayers for which no expense actually existed, 2) it is my
15 understanding that Company's final tax return for the year 2010 will not be finalized
16 until approximately September 15, 2011 so income tax owed, if any, on the SWPA
17 payment will not be fully known and measurable until then, and 3) the MPSC Staff's
18 proposal utilizes a three (3) year period to spread the tax effect of the SWPA
19 payment; however, Company has indicated that it does not expect its next general
20 rate change will occur for four (4) years (source: Company direct filing rate case
21 expense workpaper). Therefore, if the utility's next rate change does not occur for 4

1 years instead of 3 years, ratepayers would reimburse Company for an additional
2 year of tax expense which did not exist.

3
4 Q. WHAT IS PUBLIC COUNSEL'S RECOMMENDATION FOR RATEMAKING
5 TREATMENT OF ANY INCOME TAX ASSOCIATED WITH THE
6 SOUTHWESTERN POWER ADMINISTRATION PAYMENT?

7 A. Public Counsel recommends that should it come to pass that income taxes are
8 ultimately assessed and paid on the SWPA payment, the actual income tax paid by
9 the Company could be identified and incorporated into the development of rates in
10 its next general rate change case.

11
12 **IV. PROJECTS WRITTEN-OFF AND/OR NON-RECURRING**

13 Q. WHAT IS THE ISSUE?

14 A. The issue concerns Company's inclusion in the cost of service of expenditures
15 associated with several projects that have either been cancelled and/or are non-
16 recurring.

17
18 Q. DID MR. W. SCOTT KEITH PROVIDE DIRECT TESTIMONY REGARDING
19 THESE SPECIFIC COSTS?

1 A. Mr. Keith's written Direct Testimony does not actually discuss these specific issues,
2 but he is sponsoring the Company's Direct Filing Income Statement which includes
3 the costs.
4

5 Q. PLEASE CONTINUE.

6 A. Company's response to MPSC Data Request No. 11 identified costs for various
7 projects which have been identified as abnormal, written-off and/or non-recurring.
8 One project was for a software needs assessment project conducted by KPMG.
9 The scope of the needs assessment encompassed the Company's current People
10 Soft footprint (A/P, Inventory, Purchasing, Fixed Assets, HR and General Ledger).
11 The costs booked in 2009 were, \$105,321 and \$207,710 to Uniform System of
12 Accounts (USOA) Account 923045, and in year 2010, \$105,467 to USOA Account
13 923045 and \$78,177 to USOA Account 921477. Two other projects, Plum Point
14 Unit 2 Project - \$19,284.81 and Compressed Air Energy Storage (CAES) Project
15 - \$61,673.73, were identified as "no longer viable" and their associated costs were
16 transferred from USOA Account 183000 to operating expense USOA Account
17 923047 in December 2009. While a third project, the Springfield, Missouri, Cities
18 Utilities Carbon Sequestration Project, booked \$98,431 in November 2008 and
19 \$115,236 to USOA Account 930232 in March 2010. This project was identified
20 not as write-off, but as a cost for a research and development project for carbon
21 sequestration conducted by Springfield City Utilities that Empire helped fund.

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Q. WHY WERE COSTS INCURRED FOR THE KPMG NEEDS ASSESSMENT PROJECT?

A. Company was in the process of evaluating its business processes and software needs.

Q. ARE THE COSTS ASSOCIATED WITH THE KPMG NEEDS ASSESSMENT PROJECT RECURRING?

A. Public Counsel does not believe that the costs are recurring on an annual basis since they were associated with activities in which Company made major changes to software systems which are usually utilized for many years before becoming outdated or obsolete.

Q. HOW SHOULD THE KPMG NEEDS ASSESSMENT PROJECT COSTS BE TREATED FOR RATEMAKING PURPOSES?

A. Public Counsel recommends that the costs be capitalized and recovered over the life of the capital investment implemented pursuant to the project.

Q. WHY WERE COSTS INCURRED FOR THE PLUM POINT UNIT 2 AND CAES PROJECTS?

1 A. Company's response to OPC Data Request No. 1107 states that as part of its
2 ownership interest in Plum Point Unit 1 Empire had the contractual right to
3 participate in the development of Plum Point Unit 2 whereas for the CAES
4 Project, Company wanted to investigate alternatives to store energy generated
5 from its wind farm resources during off-peak hours and season.

6
7 Q. WERE MOST OF THE COSTS FOR THE TWO PROJECTS INCURRED IN
8 YEARS PRIOR TO THE TEST YEAR OF THE INSTANT CASE?

9 A. Yes. Company's response to OPC Data Request No. 1007 identified that all of
10 the costs associated with the Plum Point Unit 2 Project were incurred in 2007
11 while \$46,441.08 (75%) of the total CAES Project cost was incurred in 2007 and
12 2008.

13
14 Q. ARE THE COSTS OF THE PLUM POINT UNIT 2 AND CAES PROJECTS NON-
15 RECURRING?

16 A. Yes. The Company's response to MPSC Staff Data Request No. 11 identified
17 the costs of the projects as written-off because operations personnel determined
18 they were no longer viable. Further, Public Counsel sought additional information,
19 OPC Data Request No. 1102, as to why Company believed that the costs of the two
20 abandoned projects should be included in the Company's annual cost of service on
21 a going forward basis. Company's response stated:

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These costs were included in the cost of service, but were identified as a non-recurring item in data request 11.

Q. IF COSTS ARE NOT RECURRING AND/OR PROVIDE NO BENEFIT TO RATEPAYERS, SHOULD THEY BE ALLOWED IN THE DETERMINATION OF A UTILITY'S COST OF SERVICE?

A. No. Clearly, the projects have been written-off and Company has not provided any information that the projects benefited ratepayers. Therefore, Public Counsel recommends that the Commission disallow recovery of the costs in the instant case.

Q. WHY WERE COSTS INCURRED FOR THE CITIES UTILITIES CARBON SEQUESTRATION PROJECT?

A. Company's response to OPC Data Request No. 1108 states that the goal of the project was to explore the possibilities of carbon sequestration at power plant sites in Missouri.

Q. WERE ANY OF THE COSTS FOR THE PROJECT INCURRED IN YEARS PRIOR TO THE TEST YEAR OF THE INSTANT CASE?

1 A. Yes. As identified in the earlier Q&A, Company booked \$98,431 in November
2 2008.

3
4 Q. ARE THE COSTS OF THE CITIES UTILITIES CARBON SEQUESTRATION
5 PROJECT NON-RECURRING?

6 A. Yes. Company's response to OPC Data Request No. 1109 states that the
7 funding expenditures provided by Empire are the final expenditures and there will
8 be no additional costs incurred for this project.

9
10 Q. IF THE COSTS ARE NOT RECURRING AND/OR PROVIDE NO BENEFIT TO
11 RATEPAYERS, SHOULD THEY BE ALLOWED IN THE DETERMINATION OF
12 COMPANY'S COST OF SERVICE?

13 A. No. Based on Company's response to OPC Data Request No. 1109 the costs
14 are not recurring. Furthermore, Company has not provided any information that
15 the project has actually benefited ratepayers. Therefore, Public Counsel
16 recommends that the Commission disallow recovery of the costs in the instant
17 case.

18
19 Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

20 A. Yes, it does.