

Exhibit No.:
Issues: ARO, AAO and
Tracker Policy,
Affiliate Transaction,
Corrections to Staff's
Direct Filing
Witness: Kimberly K. Bolin
Sponsoring Party: MoPSC Staff
Type of Exhibit: Rebuttal Testimony
Case No.: ER-2019-0374
Date Testimony Prepared: March 3, 2020

MISSOURI PUBLIC SERVICE COMMISSION
FINANCIAL AND BUSINESS ANALYSIS DIVISION
AUDITING DEPARTMENT

REBUTTAL TESTIMONY
OF
KIMBERLY K. BOLIN

THE EMPIRE DISTRICT ELECTRIC COMPANY

CASE NO. ER-2019-0374

Jefferson City, Missouri
March 2020

**TABLE OF CONTENTS OF
REBUTTAL TESTIMONY OF
KIMBERLY K. BOLIN
THE EMPIRE DISTRICT ELECTRIC COMPANY
CASE NO. ER-2019-0374**

1
2
3
4
5
6
7
8
9
10
11
12
13

EXECUTIVE SUMMARY1

ASSET RETIREMENT OBLIGATIONS2

REQUESTS FOR AAOS & TRACKERS/GENERAL OVERVIEW4

AAO REQUEST/FUTURE LOSS OF CUSTOMERS7

AAO REQUESTS/COSTS RELATED TO LED LIGHTS9

AFFILIATE TRANSACTION11

CORRECTIONS TO STAFF’S DIRECT FILING13

1 discussed by Office of the Public Counsel (“OPC”) witness Robert E. Schallenberg. Lastly, I
2 will provide a list of corrections to Staff’s direct revenue requirement calculation for Empire in
3 this proceeding.

4 **ASSET RETIREMENT OBLIGATIONS**

5 Q. What is an asset retirement obligation (ARO)?

6 A. An asset retirement obligation is an obligation, legal or non-legal, associated
7 with the retirement of a tangible, long-lived asset for the cost of returning a piece of property
8 to its original condition. Retirement obligations can be recognized either when the asset is
9 placed in service or during its operational life when its removal obligation is incurred.

10 Q. Are costs of removal/net salvage included in Empire’s Depreciation rates?

11 A. Yes. Empire’s depreciation rates include net salvage. Net salvage equals the
12 gross salvage value of an asset minus the cost of removing the asset from service.

13 Q. What is the relationship between AROs and cost of removal incurred by utilities?

14 A. Cost of removal is defined as the cost of demolishing, dismantling, tearing down
15 or otherwise removing plant. Staff’s understanding is that the cost of removal traditionally
16 included in customer rates would include ARO items, but would not be limited to AROs.

17 Q. Does the Uniform System of Accounts (“USOA”) for electric utilities provide
18 guidance on accounting for AROs?

19 A. Yes. General Instruction No. 25 A and B. states:

20 A. An *asset retirement obligation* represents a liability for the
21 legal obligation associated with the retirement of a tangible long-
22 lived asset that a company is required to settle as a result of an
23 existing or enacted law, statute, ordinance, or written or oral
24 contract or by legal construction of a contract under the doctrine
25 or promissory estoppel. An *asset retirement cost* represents the
26 amount capitalized when the liability is recognized for the long-

1 lived asset that gives rise to the legal obligation. The amount
2 recognized for the liability and an associated asset retirement cost
3 shall be stated at the fair value of the asset retirement obligation
4 in the period in which the obligation is incurred.

5 B. The utility shall initially record a liability for an asset
6 retirement obligation in account 230, Asset retirement
7 obligations, and charge the associated asset retirement costs to
8 electric utility plant (including accounts 101.1 and 120.6), and
9 nonutility plant, as appropriate, related to the plant that give rise
10 to the legal obligation. ***The asset retirement cost shall be***
11 ***depreciated over the useful life of the related asset that gives***
12 ***rise to the obligations.....***[Emphasis added.]

13 Q. Does Staff disagree with Empire's requested inclusion of AROs in its
14 customer rates?

15 A. Yes. Empire has already received rate recovery of future asset removal costs
16 through application of depreciation rates which contain a cost of removal component. Allowing
17 recovery of ARO costs in addition to the cost of removal accruals included in Empire's
18 depreciation expense will likely result in double recovery of certain asset removal costs.

19 Q. Apart from the double recovery issue, would Staff support inclusion of the
20 specific ARO costs in rates sought by Empire in this case?

21 A. No, for two additional reasons. First, Empire has included two "expected" ARO
22 settlements which at this time are estimated amounts. If any rate treatment of an ARO is to be
23 considered, the amount should be known and measurable, not estimated. Also, Empire's direct
24 workpapers do not indicate if the AROs in question are legal or non-legal obligations. Staff's
25 position is that non-legal ARO obligations should not be included. Staff is awaiting a response
26 to a data request to determine if the AROs are legal or non-legal obligations.

1 **REQUESTS FOR AAOS & TRACKERS/GENERAL OVERVIEW**

2 Q. Is Empire requesting special accounting in the form of an AAO or tracker for
3 costs that are currently not given special accounting treatment?

4 A. Yes. Empire is requesting special accounting for three expenditures. The first
5 request is for either an AAO or discrete isolated adjustments to capture changes in allocated
6 costs and associated revenues due to the decision of three long-term contract customers not to
7 extend their contracts. The second request is to capture the costs associated with the mercury
8 vapor lights replacement program and track the difference between estimated and actual
9 revenues and costs of the LED light fixtures for municipal lighting customers. The third request
10 would defer and track the same revenues and costs from private lighting customers switching
11 to LED Lighting.

12 Q. Is Empire requesting an AAO to defer any cost impacts due to the retirement of
13 the Asbury plant?

14 A. In Sheri Richard's direct testimony on page 26, she indicates that Empire would
15 consider an AAO as an option to address the impact to operations and maintenance (O&M)
16 expense due to the retirement of the Asbury plant. If an AAO is granted, Staff believes that the
17 Commission should include all revenue requirement impacts of the closure of the Asbury plant
18 in the deferral, not just changes to O&M expenses. This would include items like the return on
19 the plant, depreciation expense, and changes to fuel inventories to also be tracked along with
20 the O&M expenses.

21 Q. Is Empire also requesting to continue its existing Riverton 12 Operations and
22 Maintenance Tracker?

Rebuttal Testimony of
Kimberly K. Bolin

1 A. Yes. However, Staff is opposed to continuing this tracker due to the fact that this
2 is no longer a new cost for which we have no history to use to determine a reasonable on-going
3 level of expense. Staff witness Ashley Sarver provides additional information in her Rebuttal
4 testimony on this issue.

5 Q. Please define “deferral.”

6 A. The accounting term “deferral” refers to treating certain financial impacts as a
7 “deferred asset/liability” or “regulatory asset/liability” on the utility’s balance sheet instead of
8 charging the cost as a period revenue or expense item on the utility’s income statement as would
9 be normally required under the Uniform System of Accounts (“USOA”) adopted by the
10 Commission for accounting purposes.

11 Q. What is the advantage to a utility of deferring costs?

12 A. By deferring a cost that would be charged against net income immediately, the
13 costs are preserved on the utility’s balance sheet and the full amount likely can be sought for
14 rate recovery in a future rate case. In other words, deferral of a cost allows the utility to avoid
15 immediate charging of costs against income, and also increases the probability that the company
16 can ultimately receive rate recovery of the costs in question even if the costs were incurred
17 outside the ordered test year, update period or true-up period in a general rate proceeding.

18 Q. How do utilities typically make deferral requests?

19 A. Utilities often request authority from the Commission to defer certain costs
20 through filing of “accounting authority order” (AAOs) requests, though such requests can also
21 be made in a general rate proceeding as Empire has done here.

22 Q. What are AAOs?

Rebuttal Testimony of
Kimberly K. Bolin

1 A. An AAO is an order from the Commission allowing a utility to account for a
2 reporting item in a different manner than normally prescribed in the utility's financial records.

3 Q. What is the Commission's expressed criteria for granting utility
4 deferral requests?

5 A. In prior cases, the Commission has held that a cost can be deferred by a utility
6 only if it is associated with an extraordinary event. As a secondary consideration, the
7 Commission will also consider whether the cost is material in amount.

8 Q. What are "extraordinary events?"

9 A. Extraordinary events are events that are unusual, unique, and non-recurring. The
10 classic example of an extraordinary event impacting utility operations and costs are the
11 occurrence of natural disasters, or so-called "acts of God," such as severe wind and ice storms,
12 and major flooding.

13 Q. What is a "tracker"?

14 A. The term "tracker" refers to rate mechanisms under which the amount of a
15 particular cost of service item actually incurred by a utility is "tracked" and compared to the
16 amount of that item currently included in a utility's rate levels. Any over-recovery or
17 under-recovery of the item in rates compared to actual expenditures made by a utility is then
18 booked to a regulatory asset or liability account, and would be eligible to be included in the
19 utility's rates set in its next general rate proceeding through an amortization to expense.

20 Q. Should use of trackers be a common occurrence in Missouri rate regulation
21 of utilities?

22 A. No. Rates are normally set in Missouri to allow a utility an opportunity to
23 recover its cost of service, measured as a whole, on an ongoing basis from the utility's

1 customers. However, under this approach, with rare exceptions, neither utilities nor utility
2 customers are allowed to be reimbursed through the rate case process for any prior under or
3 over-recovery of costs experienced by the utility in rates, either measured for its cost of service
4 as a whole or for individual cost or service components. For this reason, use of trackers in order
5 to provide reimbursement in rates to utilities or customers of any over or under-recovery of
6 individual rate component items is rare and should be dependent on unique and unusual
7 circumstances.

8 Q. Under what criteria might Staff consider the use of a tracker?

9 A. Use of trackers may be justified under the following circumstances: (1) when
10 the applicable costs demonstrate significant fluctuation and up-and-down volatility over time,
11 and for which accurate estimation is difficult; (2) new costs for which there is little or no
12 historical experience, and for which accurate estimation is accordingly difficult; and (3) costs
13 imposed upon utilities by Commission rule. In addition, in all cases the costs should be material
14 in nature.

15 **AAO REQUEST/FUTURE LOSS OF CUSTOMERS**

16 Q. What is Empire requesting in this matter?

17 A. Empire is requesting either an AAO to capture changes in allocated costs and
18 associated revenues for review in the next rate case or an out-of-period adjustment to capture
19 the impact of three long-term municipal wholesale contract customers who have decided not to
20 extend their contracts.

21 Q. Please summarize the direct testimony of Empire witness Sheri Richard
22 regarding this issue.

1 A. Beginning on page 26, line 19 through to page 28, line 9, Ms. Richard asserts
2 that a reduction in the Company's native load is anticipated to occur after the true-up period in
3 this case but prior to the effective date of rates. This reduction in native load is said to be due
4 to the expiration of current ten-year contractual agreements with a group of municipal electric
5 customers. Ms. Richard contends that the loss of these contracts results in an approximate
6 six percent reduction in kWhs to which Empire currently allocates associated costs and thus
7 will result in an increase to the amount of costs that is allocated to Empire's other jurisdictions,
8 including Missouri retail customers. Ms. Richard requests that either an AAO be authorized to
9 capture these anticipated changes in cost allocations or a discrete out-of-period adjustment be
10 determined for inclusion in this case.

11 Q. Does Staff agree with either of these proposals?

12 A. No. Staff agrees that Empire is currently allocating approximately six percent
13 of the associated costs and revenues to this group of municipal electric customers. However, I
14 do not believe that the anticipated expiration of these contracts necessitates that the Commission
15 should grant an AAO or that a discrete out-of-period adjustment is warranted in this instance,
16 as the reported loss of the existing contracts will occur well outside of the test year, update
17 period and true-up period established for this case. Moreover, the Company has entered into a
18 new contract for wholesale service that is reported to have an initiation date of June 1, 2020
19 according to the Company Response to Staff Data Request No. 0083. While it is not clear what
20 level of revenues to expect from this new contract, it would nonetheless represent an offset to
21 all or part of the alleged reductions identified with the aforesaid reduction in native load. Hence,
22 the suspected effect of the anticipated loss of native load, as described, will be diminished.

1 Q. Is there an additional reason for denying the Company's request for an AAO or
2 other discrete out-of-period adjustment?

3 A. The effective date of the new contract is June 2020 which is at least four
4 months outside of the true-up period for this case. In this proceeding, the Commission will not
5 consider inclusion of isolated adjustments for the Asbury generation station's retirement at
6 March 1, 2020, which is also outside of the test year. The Company has indicated that it will
7 be filing another rate case soon after the operation of law date in this case. Allocations will be
8 reexamined for all changes in the next rate case.

9 **AAO REQUESTS/COSTS RELATED TO LED LIGHTS**

10 Q. Is Empire requesting deferrals for costs associated with replacing mercury vapor
11 lights with LED light fixtures?

12 A. Yes, Empire is requesting two deferrals, one to capture the costs associated with
13 the mercury vapor lights replacement program and to track the difference between estimated
14 and actual revenues and costs of the LED light fixtures for municipal lighting customers, and
15 the other to defer and track the same revenues and costs from private lighting customers
16 switching to LED Lighting.

17 Q. Does Staff agree that deferrals should be established for the replacement of
18 mercury vapor light with LED fixtures for the municipal customers?

19 A. No. While moving to LED lights is a better choice than replacing lights with
20 mercury vapor lights, Empire is wanting to switch all 8,500 mercury vapor lights even if the
21 lights are still in working condition. Empire can control the timing of the replacement of the
22 mercury vapor lights.

Rebuttal Testimony of
Kimberly K. Bolin

1 Q. Over what time period does Empire propose to replace the 8,500 mercury vapor
2 light fixtures with LED light fixtures?

3 A. In Empire witness McGarrah's Direct¹ testimony Empire proposes to replace
4 all 8,500 mercury vapor light fixtures over a 12-18 month time period.

5 Q. How many LED light fixtures have been replaced thus far?

6 A. In witness McGarrah's direct testimony on page 4, lines 23 and 24, he states that
7 Empire replaced "approximately 167 light fixtures with LED light fixtures since implementing
8 the Municipal Street Lighting Service LED Tariff on July 27, 2018 with most of these being
9 replaced in the last 6 months."

10 Q. Is the replacement of the mercury vapor lights material?

11 A. No, the impact of installing the LED lights is not material. In a deferral or AAO,
12 Empire would get to collect the return and depreciation expense on the new assets that is not
13 currently included in the revenue requirement. If the Company replaced all 8,500 mercury
14 vapor lights within a one year time frame, the most the annual cost of replacing the municipal
15 mercury vapor lights with LED lights would be approximately \$ 448,195.

16 Q. Does Empire's cost of service currently reflect depreciation expense and a return
17 for the mercury vapor lights that are currently in service?

18 A. Yes. Empire is currently collecting in its cost of service depreciation expense
19 and a return on mercury vapor lights. The continued rate recovery of depreciation expense and
20 return for these mercury vapor lights following this case would offset at least in part the
21 depreciation expense and return Empire would defer for new LED lights under its proposal.

¹ Page 6, line 12-21 of Samuel S. McGarrah's Direct Testimony.

1 Q. Does Staff oppose the tracking of the revenues lost from municipal lighting
2 customers switching to LED Lighting?

3 A. Yes. If the Company converts all 8,500 mercury vapor lights to LED lighting
4 the annual amount of lost revenue from the municipal lighting customers is estimated to be
5 \$127,415, which is also not a material amount to Empire.

6 Q. Does Staff agree with Empire's proposal to track the cost of replacing mercury
7 vapor lights and also the revenue and costs of the LED lights for its private lighting service?

8 A. No. In its direct testimony, Empire did not provide the number of lights that
9 would be replaced with LED lights. Staff has requested this information, so Staff can determine
10 the materiality of the Empire's request. Furthermore, the same reasons listed above for not
11 tracking the impact of LED installation would also apply to private lighting.

12 **AFFILIATE TRANSACTION**

13 Q. In OPC witness Schallenberg's Direct testimony² he claims Empire has violated
14 the Commission's affiliate transactions rule by refinancing its \$90 million first mortgage
15 bonds with an affiliate, Liberty Utilities Company (LUCo). Does Staff agree with witness
16 Schallenberg's claim?

17 A. After further review, Staff's position is that the refinancing transaction is very
18 likely a violation of the affiliate transactions rule. Empire signed a promissory note with LUCo
19 that had a 4.53% interest rate. LUCo obtained the funds to loan Empire the \$90 million by
20 accessing LUCo's credit facility. LUCo obtained the money at a significantly lower interest
21 rate than 4.53%.

² Page 11, line 12 through page 16 line 14 of Robert Schallenberg's Direct Testimony filed in Case No. ER-2019-0374.

Rebuttal Testimony of
Kimberly K. Bolin

1 Q. Why does Staff consider this a potential violation?

2 A. This is a violation because LUCo is charging its affiliate, Empire, a higher
3 interest rate for money it obtained at a lower rate. This violates 20 CSR 4240.015 (2) (A),
4 which states,

5 A regulated electrical corporation shall not provide a financial
6 advantage to an affiliated entity. For the purpose of this rule, a
7 regulated electrical corporation shall be deemed to provide a
8 financial advantage to an affiliated entity if–

9 1. It compensates an affiliated entity for goods or services above
10 the lesser of –

11 A. The fair market price; or

12 B. The fully distributed cost to the regulated electrical
13 corporation to provide the goods or service for itself;

14 While LUCo claims to have charged a market-based interest rate to Empire, Staff is still
15 reviewing if Empire could have secured on the open market cheaper financing. However, even
16 if cheaper financing could not have been obtained directly by Empire, the fact that LUCo is
17 charging Empire a higher interest rate than what LUCo is currently paying is at least a possible
18 prudence issue.

19 Q. Does Staff agree with witness Schallenberg's calculation of the amount Empire
20 is overpaying LUCo annually for this financing?

21 A. Mr. Schallenberg reviewed the interest rates for LUCo's credit facility for the
22 time period of May 31, 2018, through May 31, 2019, and conservatively used the highest
23 interest rate during this period to calculate the overpayment. Staff is still reviewing the interest
24 rates that were available to LUCo through its credit facility since the date the promissory note
25 was signed (June 1, 2018) through January 31, 2020, the true-up date in this proceeding. The
26 interest rates for the credit facility fluctuate over time, so an average of the rates since the note

1 was issued may be an appropriate rate to use to calculate an adjustment for Empire's
2 over-payment for the money obtained by LUCo and loaned to Empire.

3 **CORRECTIONS TO STAFF'S DIRECT FILING**

4 Q. Is Staff aware of corrections that need to be made to Staff's direct
5 revenue requirement?

6 A. Yes. After the direct filing on January 15, 2020, Staff became aware of certain
7 corrections that need to be made to the direct revenue requirement amount.

8 Q. What are the corrections?

9 A. The following issues will be corrected and reflected in Staff's True-Up revenue
10 requirement to be filed in this case on March 27, 2020:

- 11 o DSM Cost Recovery – Include 2019 costs for ADEC, MLIF, LIDI – See
12 Caroline Newkirk's rebuttal testimony for further explanation
- 13 o Ice Storm Amortization – Staff originally included 13 months in the annual
14 amortization amount
- 15 o Rate Case Expense – Updated rate case expense to reflect new information
- 16 o Asbury Plant Retirement – As order by this Commission, Staff will not include
17 an isolated adjustment to reflect the retirement of the Asbury plant
- 18 o Incentive Compensation – Possible corrections pending more information from
19 Empire – See Caroline Newkirk's rebuttal testimony for further explanation
- 20 o Materials and Supplies – remove the correct amount of Water Inventory from
21 Materials and Supplies balance
- 22 o Retail Rate Revenue – See Michelle A. Bocklage's Rebuttal testimony for
23 further explanation of possible corrections

Rebuttal Testimony of
Kimberly K. Bolin

1 Q. Does this conclude your rebuttal testimony?

2 A. Yes.

