

Exhibit No.: _____
Issue(s): Staff Tax Benefit Omission/
Tax Recognition on Carrying Costs/Company
Improper Application of Pre-tax Rate
Witness/Type of Exhibit: Riley/Surrebuttal
Sponsoring Party: Public Counsel
Case No.: EF-2022-0155

SURREBUTTAL TESTIMONY

OF

JOHN S. RILEY

Submitted on Behalf of the Office of the Public Counsel

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

CASE NO. EF-2022-0155

July 22, 2022

TABLE OF CONTENTS

Testimony	Page
Staff Lack of Tax Reduction Recognition	2
Recognizing Tax Benefits on Carrying Charges	4
Bond Issuance is a Tax Free Transaction	6

SURREBUTTAL TESTIMONY
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EVERGY MISSOURI WEST, INC.
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1 **Q. What is your name and what is your business address.**

2 A. John S. Riley, PO Box 2230, Jefferson City, Missouri 65102.

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

5 A. Yes.

6 **Q. Why are you filing surrebuttal in this case?**

7 A. I am responding to Staff witnesses concerning the inclusion of taxes on both the Winter Storm
8 Uri (“Storm Uri”) costs and the carrying charges in the total proposed securitization amount.
9 I am not arguing what amount of carrying charges should be included. I am proposing that
10 the federal and state tax effects of the carrying charges should be recognized by reducing the
11 securitization amount to reflect those taxes.

12 I am also pointing out to the Commission that the Company’s proposed use of the pre-tax
13 weighted average cost of capital (“WACC”) is misguided due to the fact that the bonds to be
14 issued are a tax free financial transaction.

1 **STAFF LACK OF TAX REDUCTION RECOGNITION**

2 **Q. Staff witness Kim Bolin proposed in rebuttal testimony that Evergy Missouri West, Inc.**
3 **(“Evergy West” or the “Company”) should be allowed to securitize approximately**
4 **\$302.8 million¹. Is this an accurate representation of the costs the Company will incur**
5 **to securitize to Storm Uri?**

6 A. No. Staff does not recognize a cost reduction for the income tax benefit the Company has
7 received for either the unreimbursed fuel and purchased power costs or the accrued carrying
8 charges associated with those costs.²

9 **Q. What happens to the income tax benefit if Staff does not reduce its proposed**
10 **securitization balance to recognize that tax benefit?**

11 A. As I pointed out in rebuttal testimony, if the securitization balance is not reduced to recognize
12 the tax benefit the ratepayer will be penalized twice for Evergy West’s windfall. One for
13 being denied the benefit as a reduction to the securitization balance and two having to pay for
14 the Company’s tax benefits they were denied in the bond payments.

15 **Q. Evergy West tax accountant Melissa Hardesty provided an answered to Staff data**
16 **request 0094 that deferred taxes were recorded for Storm Uri costs. (Attached as JSR-**
17 **S-01.) Do you agree with these accounting entries?**

18 A. No. Ms. Hardesty’s answer to the data request is misleading. The term “deferred taxes”
19 implies that tax is due at a later date, in short a timing difference of some sort. Storm Uri costs
20 were expense items, not depreciable asset additions. The expenses were incurred in February
21 2021 and the income tax benefits will occur on the 2021 consolidated tax returns. There

¹ Kim Bolin rebuttal, page 4, line 21, page 5, table 2.

² The taxability of carrying charges will be discussed later in this testimony.

1 should be no amortization or depreciation or timing difference associated with these storm
2 costs.

3 As Company witness, Mr. Ron Klote, CPA stated on page 23 of his direct testimony and I
4 stated in rebuttal testimony, there are no deferred income taxes associated with this Storm Uri
5 securitization. The deduction I propose to the securitization amount should be a one-time
6 deduction that matches the Company tax deduction and should not need updating with any
7 annual true-up mechanisms.

8 **Q. How would the tax calculations play out using Staff's proposed securitization amount?**

9 A. A rough calculation from Staff's proposed \$302.8 million shows that Evergy³ stands to
10 receive a one-time tax reduction of \$72.2 million for the unreimbursed fuel and purchased
11 power costs⁴. Without a reduction in the proposed securitization amount to recognize this tax
12 reduction, the ratepayer will get nothing. To pour salt on the wound, the ratepayer will fund
13 the inclusion in the bond proceeds of this \$72.2 million and pay for Evergy West's windfall
14 for 15 years. Under this scenario, this \$72.2 million will become \$135 million when including
15 the tax gross up of \$32.17 million in the revenue requirement payments. I have payment
16 amortization tables set up on JSR-S-02 to illustrate the inequality of accepting Staff and
17 Evergy West calculations.

18 To summarize the disparity, Evergy West proposes a deferred tax liability to compensate the
19 ratepayer. As can be seen on the amortization table in JSR-S-02, this liability (\$72.2 million
20 in this example) would only cost the Company approximately \$48 million in lost revenue
21 requirement. Evergy West saves \$24 million over 15 years plus it still has the tax benefit of
22 \$72.2 million. That is over \$96 million. So under this scenario, the ratepayers get to pay for

³Evergy West is a member of a consolidated tax group, Evergy Inc.

⁴ $302,800,000 * 23.84\% = \$72,187,520$.

1 a tax write-off of \$72.2 million that by the end of 15 years costs them \$135 million.
2 Essentially, over \$207 million out of the ratepayer's pocket. This an untenable position.

3 **Q. You stress a one-time tax reduction. Has Evergy received this tax benefit?**

4 A. Yes and no. The reduction will be on the Company's 2021 consolidated federal and state
5 income tax returns which were due to be filed April 18 of this year, however, the Company
6 submitted a filing extension so the return won't be filed until October 15, 2022.⁵ Evergy made
7 the management decision to delay filing but the benefits are already available.

8 I will argue for recognizing taxes on the carrying charges also, however, those expenses will
9 be spread over both the 2021 and 2022 tax returns.

10 **RECOGNIZING TAX BENEFITS ON CARRYING CHARGES**

11 **Q. Why did you not mention tax calculations concerning carrying charges in your rebuttal**
12 **testimony?**

13 A. I originally struggled with the idea that taxing the interest expense would possibly be a double
14 calculation. I was concerned that Staff would include the interest in the next rate case and
15 taxes would be offset by the increased interest deduction. I now realize that any interest
16 associated with Storm Uri costs would not be a long term debt in the cost of service and would
17 not be in any Staff general rate making calculation going forward. The company tax windfall
18 on the Storm Uri costs and the carrying charges will be a stand-alone calculation and will not
19 be in the next rate case.

⁵ Answer to OPC data request 1300 indicates that 2021 tax returns will be forwarded after the returns are filed. I have not received a copy of the 2021 tax returns.

1 **Q. How would these tax calculations be separate from the next general rate case?**

2 A. There are several witnesses presenting their ideas of how carrying charges should be
3 calculated and included. I am not one of them.

4 My contention is whatever the Commission decides should be included as a carrying charge,
5 that amount should be recognized as a tax deduction. These charges are separate due to the
6 fact that the Company has identified and separated this interest as an expense specific to the
7 Storm Uri costs. In short, if the Company can claim these costs as ongoing and accumulating
8 specifically to Storm Uri, then the costs can be claimed on its tax return and a composite tax
9 rate can be applied. When the Company comes back in for a general rate case, this interest
10 will not be in the capital structure but will be included in the securitization bonds being funded
11 by a separate line item on each ratepayer's bill.

12 **Q. The amount of your tax adjustment will be based on the decision by the Commission. Is**
13 **there a ball park figure that can be considered?**

14 A. Yes. I used Staff's overall cost estimate in the amortization table in my Schedule JSR-S-02.
15 However, Company witness Ron Klote has included with his direct testimony, schedules that
16 include a calculated amount of carrying charges. Based on his proposed carrying charge
17 amount in Schedule RAK-3, the income tax reduction for the carrying charges alone would
18 be approximately \$13 million.

19 Just as income taxes are a fluid expense in a general rate case, until the Commission makes
20 its decision, taxes will be fluid in this case. As I proposed in rebuttal testimony, the
21 approximate \$296 million that Evergy West seeks for fuel and purchased power will be
22 reduced by the \$70 million tax advantage. This reduction will reduce carrying charges. The
23 reduction in carrying charges in turn will lower the tax effect of those carrying charges.

1 **Q. Including the tax reduction to the Storm Uri fuel and purchased power costs and the**
2 **reduction associated with the carrying charges, what is your approximate reduction to**
3 **the securitization amount to account for taxes?**

4 A. Depending on the Commission's decision, the tax reduction to the proposed securitization
5 amount will be between \$72 million and \$82 million.

6 **Q. Will the Company be denied this estimated amount?**

7 A. No. This is just a shift in payment responsibility. The Company will be made whole. The
8 estimated tax reduction to the proposed securitization amount will save the Company in tax
9 liability. The remaining amount will be reimbursed through the securitized bonds. Evergy
10 West loses nothing. But, the ratepayer gains by not having to fund the tax savings and the
11 interest associated with those tax savings for 15 years.

12 This will not be a deferred tax either. Evergy West is in a taxable situation so the tax benefit
13 will be consumed with its 2021 tax returns.

14 **BOND ISSUANCE IS A TAX FREE TRANSACTION**

15 **Q. Ms. Bolin disagrees with Company's use of an 8.9% WACC to calculate carrying**
16 **charges. Do you agree that the rate proposed by Evergy West witness Ron Klote is**
17 **inappropriate?**

18 A. Yes, it is not the proper rate to apply to any costs in this securitization case.

19 **Q. Would you explain why the Company's attempt to calculate carrying charges using a**
20 **pre-tax WACC of 8.9% is inherently erroneous?**

21 A. I am not testifying as to what interest rate should be used to calculate the carrying charges on
22 the period of time before the costs are securitized. But, I am objecting to the Company's use
23 of an interest rate that builds a tax collection into that percentage. Using the 8.9% rate would

1 infer that the Company must calculate and collect income tax on the carrying charge allowed
2 on the Storm Uri costs. No taxes will be collected until the securitization is included on the
3 ratepayers' monthly bills. Therefore, the Company does not need to include a pre-tax WACC.

4 **Q. You have already explained that there is a tax benefit that should be recognized. Can**
5 **you explain what the Company stands to gain if its proposed WACC is used in the**
6 **calculations?**

7 A. I have already explained in rebuttal testimony that the issuance of these bonds does not have
8 a tax affect. The transaction is tax free. Based on this premise, building a tax amount into the
9 interest rate is bonus money to the Company.

10 I've stated that there is a tax reduction from the carrying charges that the ratepayer should
11 receive as a deduction in the securitization amount. By proposing to use WACC to determine
12 the carrying costs in this matter, the Company is attempting to include a reimbursement of
13 taxes where none exist. I have argued that the Company will receive an estimated \$13 million
14 tax benefit. Accepting the 8.9% rate will quietly allow the Company a bonus on top of that
15 amount.

16 **Q. Please summarize.**

17 A. The rate used to calculate carrying charges should not have a tax calculation built in as if there
18 will be a tax cost to this transaction. There are no tax costs on this tax free transaction only a
19 tax benefit.

20 **Q. Does this conclude your surrebuttal testimony?**

21 A. Yes.