Exhibit No.: 12
Issues: Pension, OPEBs, SERP
Witness: James A. Fallert
Type of Exhibit: Rebuttal Testimony
Sponsoring Party: The Empire District Electric Company
Case No.: ER-2019-0374
Date Testimony Prepared: March 2020

Before the Public Service Commission
of the State of Missouri

Rebuttal Testimony

of

James A. Fallert

on behalf of

The Empire District Electric Company
a Liberty Utilities Company

March 2020

TABLE OF CONTENTS
REBUTTAL TESTIMONY OF
JAMES A. FALLERT
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2019-0374

SUBJECT **PAGE**

1

REBUTTAL TESTIMONY
OF
JAMES A. FALLERT
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2019-0374

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME, BUSINESS AFFILIATION, AND BUSINESS ADDRESS.

A. My name is James A. Fallert. I am doing business as James Fallert Consultant LLC and my business address is 3507 Burgundy Way Dr., St. Louis, MO 63129.

Q. ON WHOSE BEHALF IS YOUR REBUTTAL TESTIMONY PRESENTED?

A. The Empire District Electric Company, a Liberty Utilities company ("Liberty-Empire" or the "Company").

Q. ARE YOU THE SAME JAMES A. FALLERT THAT SUBMITTED DIRECT TESTIMONY ON BEHALF OF LIBERTY-EMPIRE IN THIS CASE IN AUGUST 2019?

A. Yes.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS CASE?

A. The purpose of this testimony is to respond to Staff's direct case in regard to pensions, OPEBs, and SERP. Staff's witness in regard to these matters is Ashley Sarver.

Q. ARE YOU SPONSORING ANY SCHEDULES IN CONNECTION WITH YOUR TESTIMONY?

A. Yes. I am sponsoring Rebuttal Schedule JAF – 1.

III. ONGOING PENSION AND OPEB EXPENSE

Q. HOW DID LIBERTY-EMPIRE DETERMINE THE APPROPRIATE AMOUNT OF ONGOING PENSION AND OPEB EXPENSE FOR ITS DIRECT FILING?

A. The ongoing expense amounts were based on the most recent available 2019 regulatory expense amounts as calculated by the Company's actuary, CBIZ Cottonwood.

Q. PLEASE EXPLAIN WHAT YOU MEAN BE REGULATORY EXPENSE AMOUNTS?

A. When The Empire District Electric Company was acquired by Liberty Utilities, the accounting rules required that certain pension and OPEB balances be eliminated as part of the acquisition accounting. However, these balances should remain in place for regulatory purposes. As a result, CBIZ Cottonwood provides two actuarial valuations. One valuation is based on acquisition accounting and is used for external financial reporting purposes. The second valuation is done as if the acquisition did not occur and is used for regulatory purposes. The Company's direct filing was based on the valuation for regulatory purposes.

Q. WHAT WAS THE BASIS FOR STAFF'S DIRECT CASE?

A. Staff used the acquisition accounting amounts for 2018 rather than regulatory accounting amounts. It appears that there may have been some confusion regarding the appropriate valuation to be used, and this should be corrected by Staff. Additionally, Staff's use of 2018 amounts should be updated to 2019.

IV. TEST YEAR EXPENSE

Q. HOW DID STAFF DETERMINE TEST YEAR EXPENSE USED IN ITS ADJUSTMENT?

A. Staff pulled test year expense amounts for FERC 926 accounts and applied an allocation percent to determine Missouri test year expense.

Q. WAS THIS AN APPROPRIATE METHODOLOGY?

A. At one time, this methodology would have worked. However, a recent change to the accounting rules requires that non-service pension and OPEB costs that were previously charged to FERC account 926 must now be charged to FERC account 426 instead. Staff's methodology needs to be updated to recognize this change, and Staff needs to include the FERC 426 accounts.

Q. DO YOU HAVE ANY CONCERNS WITH THE ALLOCATION PERCENTAGE PROPOSED BY STAFF AS IT RELATES TO TEST YEAR PENSION ACCOUNTS?

A. Yes. Staff is recommending an allocator of 87.91% (O&M expense composite rate) to general ledger account 926149. However, this account is specifically used to capture the amortization expense of the FAS87 Missouri Regulatory Asset and therefore should be direct assigned to Missouri at 100%. In addition, Company witness Sheri Richard discusses in greater detail other issues related to Staff's proposed allocation rates.

V. SERP

Q. HOW DID LIBERTY-EMPIRE CALCULATE SERP EXPENSE FOR ITS DIRECT FILING?

A. The ongoing expense amount included in the Company's filing was based on the actuarial calculations of expense provided by CBIZ Cottonwood. These calculations were done in a manner consistent with the calculation of ongoing FAS 87 pension and OPEB expense.

Q. HOW DID STAFF DETERMINE ONGOING SERP EXPENSE?

A. Rather than use the actuarially determined annual expense amount provided by CBIZ Cottonwood, Staff followed its long-standing approach of basing recovery on actual payments made from the plan. Staff used a 5 year average of SERP payments to determine its proposed rate recovery.

Q. WHAT REASONING DOES STAFF PROVIDE FOR BASING SERP RATE RECOVERY ON PAYMENTS RATHER THAN ACTUARIALLY DETERMINED EXPENSE?

A. On page 69 of its Cost of Service Report, Staff notes that the SERP is a non-qualified plan. Beginning at line 7, Staff states "In a non-qualified plan, the expense is not 'pre-funded' and only the amounts paid to beneficiaries are tax deductible. Therefore, Staff's policy has been to limit utilities' rate recovery of this item to actual benefit payments to employees, if reasonable."

Q. PLEASE COMMENT.

A. It is not at all unusual for expense items used to determine rates to vary from the tax deductions related to those items. One only has to look at the numerous deferred tax items listed in any case to verify this observation. The methodology to single out SERP expense to be accounted for differently is inconsistent with other Staff proposed adjustments and not a well-supported approach.

Q. WHY IS BASING SERP RECOVERY ON EXPENSE PREFERABLE TO A PAYMENT BASIS?

A. The expense amount is independently determined by the company's actuary. It is consistent with the calculation of similar items (qualified pensions and OPEBs). The recognition of SERP on an expense basis, rather than a payment basis, more closely matches the benefits provided to customers.

Q. DO YOU HAVE ANY ADDITIONAL COMMENTS REGARDING STAFF'S CALCULATION OF NORMALIZED SERP FOR INCLUSION IN RATES?

A. Yes. This item is best recovered on an expense basis due to the reasons expressed above. However, if the Commission decides to continue to use a payment basis for this item, then certain changes should be made to Staff's calculation of the payment basis amount.

Q. PLEASE CONTINUE.

A. Staff determined normalized expense by reviewing SERP payments over the past 5 years and then applying an allocation percent to the amount in the update period of the 12 months ending September 30, 2019. The Company has no issue with this calculation. However, the allocation percent used by Staff needs adjustment.

Q. PLEASE EXPLAIN.

A. Staff's allocation of total SERP cost to Missouri expense is based on the percentage of total ongoing FAS 87 pension cost to the portion of this cost allocated to Missouri expense. This methodology is problematic because it applies an allocation percentage developed for one category of expense (qualified FAS 87 pension expense) to a completely different category (non-qualified SERP expense). It would be much more appropriate to use an allocation percentage directly applicable to SERP.

Q. HAVE YOU QUANTIFIED THE EFFECT OF YOUR PROPOSED CHANGE TO STAFF'S ALLOCATION METHOD?

A. Yes. The proposed methodology using SERP-specific activity increases the allocation percentage from 33.03% included in Staff's adjustment to 82.15%. The quantification is included as Rebuttal Schedule JAF-1.

Q. PLEASE EXPLAIN WHY THIS DIFFERENCE IS SO SUBSTANTIAL.

A. Recent changes to the accounting rules specify that only the service cost component of net periodic pension cost can be allocated to capital accounts. The qualified FAS 87 cost used for Staff's allocation calculation includes a significant service cost component, which results in an allocation to capital and therefore lower allocation to expense. There is no longer any service cost component to Liberty-Empire's SERP costs which results in no allocation to capital and hence a higher allocation to expense.

VI. TRACKER BALANCES

Q. DO YOU HAVE ANY COMMENTS REGARDING THE TRACKER BALANCES INCLUDED IN STAFF'S ADJUSTMENT?

A. Yes. Two adjustments to Staff's balances are necessary.

Q. PLEASE DESCRIBE THE FIRST ADJUSTMENT.

A. The balance for account 182359 as of September 30, 2019 included in Staff's adjustment is too high. Staff rolled forward from March 31, 2016 (the date of balances cited in the Stipulation and Agreement from Case No. ER-2016-0023). It appears that activity for the month of April 2016 was inadvertently excluded from the calculation, and a few of the subsequent months had incorrect signs.

Q. WHAT IS THE IMPACT OF THIS CORRECTION?

A. The September 30, 2019 balance for account 182359 included in the pension tracker should be reduced from $1,855,037 to $894,410.

Q. PLEASE DESCRIBE THE SECOND ADJUSTMENT.

A. In September 2019, $47,256 was reclassified from account 254111 to account 182358. Staff's adjustment included the effect of this entry on account 254111, but Staff did not include account 182358. The balance in account 182358 should be included, which increases the OPEB tracker balance by $47,256.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. Yes.

AFFIDAVIT OF JAMES FALLERT

STATE OF MISSOURI)
) **ss**
COUNTY OF ST. LOUIS)

On the 2nd day of March, 2020, before me appeared James A Fallert, who, being by me first duly sworn, states that he is doing business as James Fallert Consultant LLC and acknowledges that he has read the above and foregoing document and believes that the statements therein are true and correct to the best of his information, knowledge and belief.

Jas A. Fallert
James A. Fallert

Subscribed and sworn to before me this 2nd day of March 2020

Notary Public

My commission expires: 9/25/2020

STEVEN C FUCHS
Notary Public - Notary Seal
State of Missouri, St Louis County
Commission Number 16962162
My Commission Expires Sep 25, 2020

Q. WHY IS BASING SERP RECOVERY ON EXPENSE PREFERABLE TO A PAYMENT BASIS?

A. The expense amount is independently determined by the company's actuary. It is consistent with the calculation of similar items (qualified pensions and OPEBs). The recognition of SERP on an expense basis, rather than a payment basis, more closely matches the benefits provided to customers.

Q. DO YOU HAVE ANY ADDITIONAL COMMENTS REGARDING STAFF'S CALCULATION OF NORMALIZED SERP FOR INCLUSION IN RATES?

A. Yes. This item is best recovered on an expense basis due to the reasons expressed above. However, if the Commission decides to continue to use a payment basis for this item, then certain changes should be made to Staff's calculation of the payment basis amount.

Q. PLEASE CONTINUE.

A. Staff determined normalized expense by ~~averaging~~ reviewing SERP payments over the past 5 years and then applying an allocation percent to ~~that average~~the amount in the update period of the 12 months ending September 30, 2019. The Company has no issue with ~~the~~ this calculation ~~of the 5 year average~~. However, the allocation percent used by Staff needs adjustment.

Q. PLEASE EXPLAIN.

A. Staff's allocation of total SERP cost to Missouri expense is based on the percentage of total ongoing FAS 87 pension cost to the portion of this cost allocated to Missouri expense. This methodology is problematic because it applies an allocation percentage developed for one category of expense (qualified FAS 87 pension expense) to a