*Exhibit No.:*
*Issue(s):* *Revenue Requirement, Income Taxes*
*Witness:* *Matthew R. Young*
*Sponsoring Party:* *MoPSC Staff*
*Type of Exhibit:* *Rebuttal Testimony*
*Case No.:* *ER-2024-0189*
*Date Testimony Prepared:* *August 6, 2024*

# MISSOURI PUBLIC SERVICE COMMISSION

## FINANCIAL AND BUSINESS ANALYSIS DIVISION

## AUDITING DEPARTMENT

## REBUTTAL TESTIMONY

## OF

## MATTHEW R. YOUNG

## EVERGY MISSOURI WEST, INC.,

## d/b/a Evergy Missouri West

## CASE NO. ER-2024-0189

***Jefferson City, Missouri***
***August 6, 2024***

****** Denotes Confidential Information ******

**TABLE OF CONTENTS OF**

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# REBUTTAL TESTIMONY

# OF

# MATTHEW R. YOUNG

# EVERGY MISSOURI WEST, INC., d/b/a Evergy Missouri West

# CASE NO. ER-2024-0189

Q. Please state your name and business address.

A. My name is Matthew R. Young. My business address is 615 E. 13th Street, Kansas City, Missouri, 64105.

Q. Are you the same Matthew R. Young that filed direct testimony in this case?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. My rebuttal testimony responds to the direct testimony of The Office of the Public Counsel ("OPC") witness John S. Riley regarding income taxes. I will explain why it is appropriate to include the book balance of tax net operating losses as an offset to Accumulated Deferred Income Taxes ("ADIT"). I will also discuss the ratemaking mechanics of how customers are charged for income tax expense and why Staff concludes it is equitable to offset ongoing income tax expense with ordinary tax losses caused by asset dispositions. Additionally, I will provide an update to Staff's overall revenue requirement.

**<u>REVENUE REQUIREMENT</u>**

Q. Has Staff's revenue requirement changed since its direct filing?

A. Yes. Subsequent to filing, Staff's revenue requirement model increased to $102, $106, and $111 million at Staff's respective low, mid, and high range for rate of return.

The increase in revenue requirement was due to corrections of errors in Staff's adjustments for fuel, Nucor revenue, and depreciation clearings as well as other, less material corrections. Error corrections were made for depreciation expense that decreased Staff's revenue requirement. Please see the rebuttal testimonies of Staff witnesses Justin Tevie and Brodrick Niemeier for more detail.

**NET OPERATING LOSSES IN ADIT**

Q. What is a Net Operating Loss ("NOL")?

A. In a year that a corporate taxpayer's tax deductions exceed its revenue, income is calculated as a negative amount and a NOL exists. Instead of the taxpayer losing the benefits of the deductions causing the loss, the Internal Revenue Service ("IRS") will allow the taxpayer to save (defer) the excess tax deductions to offset revenue earned in another tax year. The balance of deferred deductions is recorded, and accumulated, on the corporation's books as a Net Operating Loss Carryforward ("NOLC") deferred tax asset in FERC account 190.

Q. Does Evergy Missouri West ("EMW") have a NOLC balance on its books?

A. Yes. EMW's books carry an NOLC that has been carried forward since the asset was inherited from EMW's predecessor, Aquila Inc.[1]

Q. Did Staff include this NOLC from Aquila Inc. in its calculation of the ADIT reduction to rate base?

A. No. This NOLC was generated by Aquila Inc.'s non-regulated operations and was not included in the recommended cost of service by Staff or EMW.

Q. Does EMW have a NOLC from its regulated operations?

A. No. EMW currently has $0 NOLC from regulated operations.

[1] Staff Data Request No. 0214.

Q. On page five of his direct testimony, Mr. Riley identified an NOLC included in EMW's ADIT. If EMW doesn't have a current NOLC from regulated operations, what is the amount Mr. Riley identified?

A. Mr. Riley is correct that EMW has an amount in FERC account 190 labeled as a federal NOL but this is not available to offset EMW's future tax liability and is not a conventional asset. From an accounting perspective, this amount would be more appropriately classified as a contra-liability rather than an asset. Ultimately, this amount is simply a byproduct of the passage of the 2017 Tax Cuts and Jobs Act ("TCJA").

Q. How did the TCJA affect EMW's deferred tax assets and liabilities?

A. Although EMW has exhausted its balance of NOLC from regulated operations, EMW's regulated books carried a NOLC when the TCJA became law on January 1, 2018. On that date, a substantial portion of EMW's deferred tax liability was effectively forgiven by the federal government. The balance of ADIT liability that was no longer due to the IRS transitioned from an ADIT liability to Excess ADIT, and is being returned to ratepayers through an amortization. Likewise, the TCJA caused EMW's January 1, 2018 balance of NOLC deferred tax asset from regulated operations to lose a portion of its value and remains on EMW's books as on offset to the amortization of Excess ADIT. In short, the amount identified by Mr. Riley, while labeled an NOL, is not available to EMW and its affiliates to offset future tax liabilities and is instead tied to the amortization of Excess ADIT.

Q. Did Staff include the current balance of Excess ADIT, offset by the Excess NOLC, in its revenue requirement?

A. Yes. Staff included the *net* Excess ADIT as a reduction to rate base and amortized the balance per IRS regulations. Staff's methodology is consistent with paragraph 12 of the *Non-Unanimous Partial Stipulation and Agreement* approved by the Missouri Public Service Commission ("Commission") in EMW's rate case No. ER-2018-0146 and Staff's methodology in EMW's subsequent 2022 rate case.

Q. How long will EMW need to carry the Excess NOLC on its books?

A. Using the IRS amortization methodology causes the annual amortization of the Excess NOLC to be variable so the exact answer is not known. However, at the average pace of amortization experienced to date, the full amortization may take 30 to 40 years.

## TAX DEDUCTION FOR ASSET DISPOSAL

Q. Please summarize Mr. Riley's direct testimony on this topic.

A. In his direct testimony, Mr. Riley asserts that when EMW retires its assets early, 1) ratepayers do not receive the tax benefit EMW enjoys through the disposition loss reported on the federal returns and 2) ratepayers are not refunded the interest free loan EMW received during the time the asset was in-service.[2] As such, Mr. Riley recommends that EMW's disposition losses should be recognized in Staff's ratemaking income tax calculation.

Q. What is Staff's response to Mr. Riley's testimony?

A. While doing so is not reflected in Staff's revenue requirement, Staff concludes that it is equitable for the Commission to offset ongoing income tax expense with ordinary tax losses caused by asset dispositions in the current regulatory environment.

Q. How did Staff reach that conclusion?

A. Staff considered Mr. Riley's testimony by analyzing how ratepayers are mechanically charged income tax expense in Missouri's ratemaking methodology.

[2] Riley Direct, pages 13 and 14.

As I described in my direct testimony, ratepayers are charged for current income tax expense and a deferred tax expense in order to normalize ratemaking income taxes. In other words, Staff's current recommended revenue requirement includes amounts for taxes that are due currently *and* taxes that will become due in the future (deferred). Furthermore, the balance of money utilities have deferred to future tax periods is quantified as an ADIT deduction to rate base.

Q. Is the ADIT balance in rate base the interest free loan from ratepayers that Mr. Riley refers to?[3]

A. Not exactly. The interest free loan concept is slightly more nuanced than Mr. Riley presented.

Q. Please describe the nuances of interest free loans driven by taxation.

A. IRS tax regulations grant corporations the ability to defer tax payments from current periods to future periods and tax experts generally consider the act of deferring tax liabilities as an interest free loan from the federal government. The nuance to this is that a corporation does not need to be a regulated utility to enjoy an interest free loan and the concept is independent of what income tax expense is collected through the corporation's revenues. In other words, capital intensive industries such as airlines, railroads, and construction can enjoy substantial cost-free loans from the IRS even while in a competitive environment. Considering ADIT as an interest free loan from ratepayers implies that there is an income tax tracker that measures the income tax collected from utility customers versus what has been paid to taxing authorities.

[3] Riley Direct, page 4.

Q. Are you saying that Staff's recommended amount of ADIT in rate base is independent of the exact amount of income taxes EMW has collected from customers?

A. Yes. Staff included ADIT in rate base to recognize that ratepayers pay income tax expense prior to the taxes actually becoming due but the amount in rate base is a proxy of the ratepayer's actual prepayment of income tax. Staff's amount is based on EMW's book balance of the interest free loan it has received from the government, not the actual amount of prepaid income tax expense EMW has collected from ratepayers.

Q. In your direct testimony, you indicated that the deferred taxes represent a temporary timing difference that unwinds as taxpayers settle their deferred tax liability. Earlier in this testimony, you stated that ratepayers are charged for deferred tax expense. What effect does deferred tax expense have on the revenue requirement?

A. Deferred tax expense is calculated by comparing the book depreciation of an asset to the tax depreciation of the same asset. During the initial deferral of income tax liabilities, ratepayers will be charged a positive deferred tax expense which increases the revenue requirement. When the utility begins paying down its liability, the deferred income tax expense tied to a single asset becomes negative which reduces the revenue requirement. Stated another way, the revenue requirement both increases and decreases depending on the current stage of the asset's book depreciable life. The running total of tax timing differences are included as ADIT in the utilities rate base. Figure 1 illustrates the revenue requirement impact of a single asset assuming annual revenue of $500,000, a $100,000 asset, a 10-year book life, and a 5-year tax life.

**Figure 1:**

| $100,000 Asset with 10-year book life, 5-year tax life | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Year | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | | |
| Annual Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | a | |
| Annual Depreciation Expense | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | b | $100k / 10 years |
| Net Income | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | c | a - b |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | d | |
| Book Income Tax Expense | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | e | c * d |
| | | | | | | | | | | | | |
| Tax Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | f | |
| Annual MACRS Deduction | (20,000) | (32,000) | (19,200) | (11,520) | (11,520) | (5,760) | - | - | - | - | g | $100k * MACRS |
| Taxable Income | 480,000 | 468,000 | 480,800 | 488,480 | 488,480 | 494,240 | 500,000 | 500,000 | 500,000 | 500,000 | h | f - g |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | i | |
| Income Tax Payable | 120,000 | 117,000 | 120,200 | 122,120 | 122,120 | 123,560 | 125,000 | 125,000 | 125,000 | 125,000 | j | h * i |
| | | | | | | | | | | | | |
| **Annual Deferred Income Tax** | **2,500** | **5,500** | **2,300** | **380** | **380** | **(1,060)** | **(2,500)** | **(2,500)** | **(2,500)** | **(2,500)** | k | e - j |
| **ADIT (Rate Base)** | **2,500** | **8,000** | **10,300** | **10,680** | **11,060** | **10,000** | **7,500** | **5,000** | **2,500** | **-** | l | k + prior year |

Q. How does an asset's early retirement, which is the subject of Mr. Riley's direct testimony, flow through the revenue requirement mechanics?

A. Generally, when an asset is retired early accounting adjustments are made to remove the plant asset and the accumulated depreciation reserve. Since the asset's cost is removed from plant, the utility's ongoing book depreciation expense is reduced due to this retirement. The retirement is similarly reflected in the utility's tax records. As a result, the depreciation caused by the asset is effectively removed from ongoing book depreciation and tax depreciation and deferred income taxes are reduced to $0. The elimination of deferred tax expense effectively prevents the utility from refunding the accumulated amount of ratepayer's prepaid income taxes on this particular asset. In the following illustration (Figure 2), $10,300 of prepaid income taxes has been collected in the first three years but there will be no future negative deferred income tax expense to refund the amount.

Q. Mr. Riley states that upon early retirement, "IRS regulations require the company to remove the asset and the associated ADIT from the regulatory books." Do you agree with this assessment?

A. No. the IRS does not have jurisdiction of a utility's regulatory books. Further, a retirement that results in a disposition loss actually increases the ADIT in regulated rate base instead of decreasing the balance.[4] Figure 2 shows the effect a tax disposition loss has on the ADIT in rate base.

**Figure 2:**

| $100,000 Asset with 10-year book life, 5-year tax life, Retired at the End of Year 3 | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Year | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | | |
| Annual Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | a | |
| Annual Depreciation Expense | (10,000) | (10,000) | (10,000) | - | - | - | - | - | - | - | b | $100k / 10 years |
| Net Income | 490,000 | 490,000 | 490,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | c | a - b |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | d | |
| Book Income Tax Expense | 122,500 | 122,500 | 122,500 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | e | c * d |
| | | | | | | | | | | | | |
| Tax Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | f | |
| Annual MACRS Deduction | (20,000) | (32,000) | (19,200) | - | - | - | - | - | - | - | g | $100k * MACRS |
| Disposition Loss Deduction* | | | (28,800) | | | | | | | | | |
| Taxable Income | 480,000 | 468,000 | 452,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | h | f - g |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | i | |
| Income Tax Payable | 120,000 | 117,000 | 113,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | j | h * i |
| | | | | | | | | | | | | |
| **Annual Deferred Income Tax** | **2,500** | **5,500** | **2,300** | - | - | - | - | - | - | - | k | e - j |
| **ADIT (Rate Base)** | **2,500** | **8,000** | **39,100** | **39,100** | **39,100** | **39,100** | **39,100** | **39,100** | **39,100** | **39,100** | l | k + prior year |
| | *Not reflected in ratemaking deferred income tax expense but reflected in ADIT | | | | | | | | | | | |

Note: this scenario yields a tax disposition loss of $28,800, the un-deducted cost of the asset.

Q. Has Staff accounted for the tax impacts of early plant retirements in past utility rate cases?

A. No. In Missouri, a majority of a utility's assets are accounted for under what is called "mass asset accounting" and Staff's approach to taxes is and was consistent with the mass asset accounting theory.

Q. How so?

A. Essentially, utility accounts are depreciated instead of the individual assets in those accounts. For example, Staff's accounting schedules apply a 5% depreciation rate to EMW's FERC account 370.020 – Meters – AMI. When a meter is retired from the account, it is assumed that the meter has reached its full 20-year life regardless of when it was

[4] Staff Data Request No. 0439.

actually installed. The mass asset methodology relies on the premise that some assets in the account will be retired early, but early retirements are offset by other assets exceeding the 20-year life in the same account. Accordingly, the depreciation on a mass asset that has exceeded the book life continues to generate a negative deferred tax expense beyond expectations as illustrated in Figure 3.

**Figure 3:**

| $100,000 Asset with 10-year book life, 5-year tax life, Retired at the End of Year 13 | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Year | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | | |
| Annual Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | a | |
| Annual Depreciation Expense | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | b | $100k / 10 years |
| Net Income | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | c | a - b |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | d | |
| Book Income Tax Expense | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | e | c * d |
| | | | | | | | | | | | | |
| Tax Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | f | |
| Annual MACRS Deduction | (11,520) | (11,520) | (5,760) | - | - | - | - | - | - | - | g | $100k * MACRS |
| Taxable Income | 488,480 | 488,480 | 494,240 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | h | f - g |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | i | |
| Income Tax Payable | 122,120 | 122,120 | 123,560 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | 125,000 | j | h * i |
| | | | | | | | | | | | | |
| **Annual Deferred Income Tax** | **380** | **380** | **(1,060)** | **(2,500)** | **(2,500)** | **(2,500)** | **(2,500)** | **(2,500)** | **(2,500)** | **(2,500)** | k | e - j |
| **ADIT (Rate Base)** | **10,680** | **11,060** | **10,000** | **7,500** | **5,000** | **2,500** | **-** | **(2,500)** | **(5,000)** | **(7,500)** | l | k + prior year |

Q. Are you saying that Staff's approach to income taxes has been balanced in past rate cases?

A. Yes. Similar to the premise underlying mass asset accounting, Staff's approach to deferred taxes has assumed that negative deferred income tax expenses lost by early retirements are supplemented by excessive negative deferred income tax expense generated by late retirements.

Q. What is the tax deduction for asset disposal that Mr. Riley discusses in his direct testimony?

A. On the IRS tax Form 4797 (supported by Form 8886), EMW reported a significant amount of losses on asset disposition in recent years. The tax losses are equal to the original cost of the retired asset that has not yet been deducted from taxable income through tax depreciation. Referring back to Figure 2, $71,200 of tax depreciation has been deducted when the asset is retired at the end of year three so the loss on disposition of the $100,000 asset is the remaining $28,800.

| | | |
|---|---|---|
| Original Cost: | | $ 100,000 |
| Year 1 Depreciation | $ (20,000) | |
| Year 2 Depreciation | $ (32,000) | |
| Year 3 Depreciation | $ (19,200) | |
| Total Depr Deducted | | $ (71,200) |
| **Tax Loss on Disposition** | | **$ 28,800** |

Q. Does the tax deduction for the disposition loss have a direct relation to the amount of prepaid income taxes EMW has collected from ratepayers?

A. No, not directly. As I've attempted to illustrate above, the income taxes ratepayers have prepaid are accounted for in ratemaking by increasing or decreasing deferred income tax expense. Additionally, the amount EMW includes in its ADIT accounts is the running total of depreciation recorded on the books compared to the total tax deductions claimed, including deductions for asset dispositions. For example, in Figure 2 above, I illustrate that the tax disposition loss of $28,800 is not the same as the $10,300 of prepaid income taxes the utility has collected at the end of year three.

Q. Will tax disposition losses always be greater than the amount of prepaid income taxes at a given point in time?

A. No. As shown in the following Figure 4, a retirement that occurs after an asset has completed its tax life but before it reaches its book life strands $7,500 of prepaid taxes but does not have an associated disposition loss, as the asset's cost has already been fully deducted for income tax purposes.

**Figure 4:**

| $100,000 Asset with 10-year book life, 5-year tax life, Retired at the End of Year 7 | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Year | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | | |
| Annual Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | a | |
| Annual Depreciation Expense | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | (10,000) | - | - | - | b | $100k / 10 years |
| Net Income | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 490,000 | 500,000 | 500,000 | 500,000 | c | a - b |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | d | |
| Book Income Tax Expense | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 122,500 | 125,000 | 125,000 | 125,000 | e | c * d |
| | | | | | | | | | | | | |
| Tax Revenue | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | 500,000 | f | |
| Annual MACRS Deduction | (20,000) | (32,000) | (19,200) | (11,520) | (11,520) | (5,760) | - | - | - | - | g | $100k * MACRS |
| Taxable Income | 480,000 | 468,000 | 480,800 | 488,480 | 488,480 | 494,240 | 500,000 | 500,000 | 500,000 | 500,000 | h | f - g |
| Tax Rate | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | 25% | i | |
| Income Tax Payable | 120,000 | 117,000 | 120,200 | 122,120 | 122,120 | 123,560 | 125,000 | 125,000 | 125,000 | 125,000 | j | h * i |
| | | | | | | | | | | | | |
| **Annual Deferred Income Tax** | **2,500** | **5,500** | **2,300** | **380** | **380** | **(1,060)** | **(2,500)** | **-** | **-** | **-** | k | e - j |
| **ADIT (Rate Base)** | **2,500** | **8,000** | **10,300** | **10,680** | **11,060** | **10,000** | **7,500** | **7,500** | **7,500** | **7,500** | l | k + prior year |

Q. How much have EMW's reported asset disposition losses been in prior years?

A. The following table shows EMW's share of Evergy Inc.'s disposition losses reported on IRS Form 4797 since 2010:

| **Year** | **Form 4797 Gain / (Loss)** |
|---|---|
| 2010 | ** [redacted] ** |
| 2011 | ** [redacted] ** |
| 2012 | ** [redacted] ** |
| 2013 | ** [redacted] ** |
| 2014 | ** [redacted] ** |
| 2015 | ** [redacted] ** |
| 2016 | ** [redacted] ** |
| 2017 | ** [redacted] ** |
| 2018 | ** [redacted] ** |
| 2019 | ** [redacted] ** |
| 2020 | ** [redacted] ** |
| 2021 | ** [redacted] ** |
| 2022 | ** [redacted] ** |

Q. Why is your table missing 2023?

A. EMW will not submit its 2023 tax return to the IRS until October 15, 2024. Staff considers 2023 amounts estimated until that time.

Q. Why are your amounts slightly different than Mr. Riley's?

A. I believe Mr. Riley's numbers are from Form 8886, which only quantifies production, distribution, and transmission asset retirements in the tax years he cited. I listed amounts from Form 4797 which is the net loss incurred from all asset dispositions.

Q. What is driving the change in losses reported beginning in 2019?

A. On January 1, 2019 EMW elected to opt-in to the Plant In-Service Accounting ("PISA") offered by Section 393.1655 RSMo. The intent of the statute was to encourage utility capital spending so it is intuitive that EMW's tax forms show a change in asset retirements that correlates to its grid modernization activities.

Q. How does the amount of ongoing tax losses due to asset disposition reflect on Staff's historical approach for the effect of early retirements on deferred tax expense?

A. As explained earlier, Staff's approach is premised on the assumption that prepaid income taxes stranded by early retirements are balanced by additional negative deferred income taxes generated by late retirements. The increase in asset disposition losses beginning in 2019 weakens the premise Staff relies on as it suggests retirement timing has become one-sided since EMW's adoption of PISA.

Q. Given all of the above information, would it be reasonable for the Commission to include a normalized amount of tax disposition losses to offset income tax expense?

A. Yes. Considering the current regulatory environment that allows ratepayers to absorb a substantial portion of regulatory lag associated with grid modernization and the same environment induces a large number of assets to be retired before the book life has been reached, which weakens the premise underlying past ratemaking for deferred income taxes, it is reasonable to flow the tax benefits of early retirements to customers as they are experienced by the utility. The Commission has consistently been a proponent of passing all costs incurred due to government action to ratepayers so it would be consistent for the Commission to order benefits incurred due to the PISA legislation to be provided to ratepayers.

Q. In this testimony, you explained that the tax disposition losses do not have a direct relationship with the balance of ratepayers' prepaid income taxes. How would including the tax losses in rates address the income tax expense ratepayers have advanced to EMW?

A. Unlike most other cost of service components that are based on the utility's actual financial experience, proxy amounts are used for ratemaking income tax items instead of actual taxes. For example, the current income tax expense has an indirect relationship with the current tax payable utilities are actually incurring. Instead, ratemaking income tax expense is normalized to comply with IRS regulations. Also, as I explained earlier the ADIT in rate base does not represent the actual amount of taxes ratepayers have supplied above the amount of income taxes EMW has paid. Instead, the current balance of EMW's loan from the federal government is substituted as a representation of ratepayer's prepaid income taxes. Likewise, it would be rational to use a normalized amount of EMW's tax losses as a proxy representation of the ADIT ratepayers have supplied but are stranded by early retirements. As I illustrated, retirements that generate a tax loss above the balance of ADIT tied to an asset will theoretically be balanced by tax losses below the balance of ADIT.

Q. Wouldn't it be more logical to use the book losses incurred by early retirements as a basis of valuing the tax benefit?

A. An attribute of mass asset accounting is that retired plant is assumed to have reached its book useful life, so an equal amount of plant-in-service and accumulated depreciation reserve is retired from the books. Unlike the retirement of plant from the tax records that includes the recognition of a loss, the retirement on the books usually cannot produce a gain or a loss.

Q. What consequence would flowing through tax disposition losses to customers have on the ADIT in rate base?

A. As illustrated in the Figures above, the ADIT balance holds the stranded or excess deferred income taxes after an asset is retired. If the Commission were to reduce income tax expense by the disposition loss deduction to return stranded ADIT, it could be construed that recognizing the tax benefit is mechanically returning stranded ADIT to ratepayers so, going forward, it would be appropriate to reflect the refund in the rate base ADIT balance.

Q. If the Commission were to adopt Mr. Riley's recommendation, how would Staff's revenue requirement change?

A. The Commission should note that the amounts in Mr. Riley's direct testimony would be treated as tax deductions, and only a percentage of a tax deductions flow through to the revenue requirement. Including Mr. Riley's normalized tax deduction in the calculation of income taxes would decrease Staff's direct revenue requirement, at the midpoint rate of return, by approximately $14.5 million.

Q. Does this conclude your rebuttal testimony?

A. Yes it does.

**BEFORE THE PUBLIC SERVICE COMMISSION**

**OF THE STATE OF MISSOURI**

| | | |
|---|---|---|
| In the Matter of Evergy Missouri West, Inc. d/b/a Evergy Missouri West's Request for Authority to Implement A General Rate Increase for Electric Service | ) ) ) ) | Case No. ER-2024-0189 |

**AFFIDAVIT OF MATTHEW R. YOUNG**

STATE OF MISSOURI )
) ss.
COUNTY OF Clay )

**COMES NOW MATTHEW R. YOUNG** and on his oath declares that he is of sound mind and lawful age; that he contributed to the foregoing *Rebuttal Testimony of Matthew R. Young*; and that the same is true and correct according to his best knowledge and belief.

Further the Affiant sayeth not.

Matt Young
**MATTHEW R. YOUNG**

**JURAT**

Subscribed and sworn before me, a duly constituted and authorized Notary Public, in and for the County of Clay, State of Missouri, at my office in Gladstone, on this 5 day of August 2024.

Notary Public

CLAYRE BARKEMA
Notary Public - Notary Seal
Clay County - State of Missouri
Commission Number 21747041
My Commission Expires Dec 19, 2025