

Exhibit No.: _____
Issue(s): Accounting Retirement Obligation
(ARO)/Test Revenues/PAYGO in the FAC/
Income Tax Offset in CWC/Asbury AAO
Witness/Type of Exhibit: Riley/Direct
Sponsoring Party: Public Counsel
Case No.: ER-2021-0312

DIRECT TESTIMONY

OF

JOHN S. RILEY

Submitted on Behalf of the Office of the Public Counsel

**THE EMPIRE DISTRICT ELECTRIC COMPANY
D/B/A LIBERTY**

FILE NO. ER-2021-0312

October 29, 2021

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Request of The)
Empire District Electric Company d/b/a)
Liberty for Authority to File Tariffs)
Increasing Rates for Electric Service)
Provided to Customers in its Missouri)
Service Area)

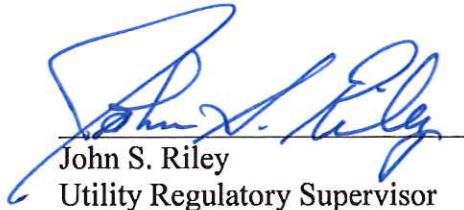
Case No. ER-2021-0312

AFFIDAVIT OF JOHN S. RILEY

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

John S. Riley, of lawful age and being first duly sworn, deposes and states:

1. My name is John S. Riley. I am a Utility Regulatory Supervisor for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my direct testimony.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

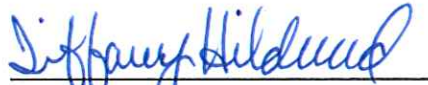


John S. Riley
Utility Regulatory Supervisor

Subscribed and sworn to me this 29th day of October 2021.



TIFFANY HILDEBRAND
My Commission Expires
August 8, 2023
Cole County
Commission #15637121



Tiffany Hildebrand
Notary Public

My Commission expires August 8, 2023.

TABLE OF CONTENTS

Testimony	Page
Asset Retirement Costs	2
Test Power Revenues	3
PAYGO	5
Income Tax Offset in CWC	6
Asbury's Ultimate Disposition	9

**DIRECT TESTIMONY
OF
JOHN S. RILEY
THE EMPIRE DISTRICT ELECTRIC COMPANY
CASE NO. ER-2021-0312**

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. By whom are you employed and in what capacity?**

4 A. I am employed by the Missouri Office of the Public Counsel (“OPC”) as a Utility Regulatory
5 Supervisor.

6 **Q. What is your educational background?**

7 A. I earned a B.S. in Business Administration with a major in Accounting from Missouri State
8 University.

9 **Q. What is your professional work experience?**

10 A. I was employed by the OPC from 1987 to 1990 as a Public Utility Accountant. In this capacity
11 I participated in rate cases and other regulatory proceedings before the Public Service
12 Commission (“Commission”). From 1994 to 2000 I was employed as an auditor with the
13 Missouri Department of Revenue. I was employed as an Accounting Specialist with the
14 Office of the State Court Administrator until 2013. In 2013, I accepted a position as the Court
15 Administrator for the 19th Judicial Circuit until April, 2016 when I joined the OPC. I have
16 also prepared income tax returns, at a local accounting firm, for individuals and small business
17 from 2014 through 2017.

18 **Q. Are you a Certified Public Accountant (“CPA”) licensed in the State of Missouri?**

19 A. Yes. As a CPA, I am required to continue my professional training by attending Missouri
20 State Board of Accountancy qualified educational seminars and classes. The State Board of
21 Accountancy requires that I spend a minimum of 40 hours a year in training that continues

1 my education in the field of accountancy. I am also a member of the Institute of Internal
2 Auditors (“IIA”) which provides its members with seminars and literature that assist CPAs
3 with their annual educational requirements.

4 **Q. Have you previously filed testimony before the Missouri Public Service Commission**
5 **(“Commission” or “PSC”)?**

6 A. Yes I have. A listing of my Case filings is attached as JSR-D-1

7 **Q. What is the purpose of your testimony?**

8 A. I present my opinions and the Office of the Public Counsel’s (“OPC”) positions on how the
9 following matters should be treated when developing Empire’s rates in this case:

- 10 • Asset Retirement Obligations (“ARO”) which are sometimes referred to as Asset
11 Retirement Costs (“ARC”),
- 12 • Net revenues generated by the wind projects before they are reflected in Empire’s
13 rates as rate-based assets (test power),
- 14 • How paygo associated with the wind projects should be treated,
- 15 • How the timing of when customers fund income tax payments and when those
16 payments are made should be treated for purposes of cash working capital, and
- 17 • How Empire’s Asbury AAO should be calculated and what the Commission should
18 do with the result, and Asbury, when designing Empire’s new rates.

19 **ASSET RETIREMENT COSTS**

20 **Q. What is an asset retirement cost?**

21 A. The projected cost of retiring an asset in the future.

1 **Q. Should AROs be included in a utility’s revenue requirement?**

2 A. The short answer is “no.”

3 **Q. Why not?**

4 A. Although recording ARO liability is required by the financial accounting services board
5 (“FASB”), as a generally accepted accounting principle (“GAAP”), for the financial
6 accounting purpose of transparency about future obligations that a company eventually will
7 have to satisfy, because the company has expended nothing to create this liability, for
8 ratemaking purposes, as it has in past cases, the Commission should continue to exclude
9 AROs from Empire’s revenue requirement.¹ No amount should be included in Empire’s
10 revenue requirement for dismantling its wind projects because the Commission will recognize
11 Empire’s costs to retire these wind projects in rates when it is time to actually dismantle them.

12 **Q. What is Empire’s ARO for dismantling the wind projects?**

13 A. Company work papers indicate that it is \$23,593,959, Missouri jurisdictional. This entire
14 amount should be excluded from the Company’s plant-in-service, and none of it should affect
15 Empire’s revenue requirement.

16 **TEST POWER REVENUES**

17 **Q. What are test power revenues?**

18 A. Test power revenues are the net revenues from a new generation resource from the time the
19 utility takes ownership until that resource is reflected in a utility’s rates as a rate base asset.

¹ ER-2019-0374, Amended Report & Order, page 149, Decision

1 **Q. Are there test power revenues from the wind projects?**

2 A. Yes. According to Empire witness Ms. Sanderson an estimated \$4.2 million² of net revenues.

3 **Q. How has the Commission treated test power revenues in the past?**

4 A. It is my understanding that the net revenues generated prior to the plant being included into
5 rates have been treated as an offset to the final cost of (investment in) the generating facility,
6 i.e., as a reduction to rate base.³

7 **Q. What is the logic for offsetting the capital cost of the project as the Commission has done**
8 **in the past?**

9 A. Consistency. Prior to rate base inclusion, expenses are typically capitalized into the associated
10 asset. It stands to reason that revenues prior to rate inclusion should be capitalized also.
11 Revenues generated prior to the new rates, it should be a direct reduction to the cost of the
12 project.

13 **Q. Does the fact that Empire has elected plant in-service accounting (“PISA”) affect that**
14 **logic?**

15 A. It does not.

16 **Q. Why not?**

17 A. PISA is an accounting mechanism to recognize a portion of plant costs after it is placed in
18 service. Test revenues offset the capital costs prior to rate base inclusion.

² I expect this amount to be updated throughout the proceedings.

³ In the matter of Kansas City Power & Light Company, June 17, 1981 Case No. ER-81-42, ER-80-48, Report & Order, Last line of Page 26

1 **PAYGO**

2 **Q. What is Paygo?**

3 A. Paygo (also described as pay-as-you-go) is a product of the tax equity agreements signed
4 between Empire and the tax equity partners for each wind project. As both Sanderson and
5 Mooney explain in their footnotes, paygo is “based on actual production in excess of a
6 threshold”⁴. Production is the amount of Megawatt hours (“MWhs”) produced by the wind
7 project. Each tax equity partner agreement has an established threshold amount of MWhs
8 produced before the tax equity partner must begin to deliver paygo payments. Once the
9 threshold is exceeded then the tax equity partner begins forwarding “Deferred Contributions”
10 to the wind project companies. I have included a Highly Confidential schedule JSR-D-02 that
11 provides the partnership agreement definition page that explains “deferred contributions” as
12 well as the corresponding agreement schedule that lists the thresholds, expected PTC
13 (production tax credit) values⁵ and adjustment schedule that would be used to calculate the
14 amount of the Paygo payments. Let me be clear. These payments are being made due to an
15 overearning above the preset rate of return established in the agreements for the tax equity
16 partner. The tax equity partner cannot keep the windfall, it must return it to the project.

17 **Q. Will any part of the paygo payments ultimately flow to Empire?**

18 A. That is the intent.

19 **Q. Does Empire have a between general rate case mechanism whereby it can flow the paygo
20 benefit it receives to its customers?**

21 A. I believe that presently it does not. The paygo is generated by the Tax Equity partner and not
22 within the general frame of ratemaking. Empire’s only mechanisms for changing its rates

⁴ Taken from previous footnote quote

⁵ The IRS adjusts the amount of the production tax credit for inflation.

1 between general rate cases are its FAC and its MEEIA DISM. Neither were designed to allow
2 paygo to flow through them.

3 **Q. Then how should the Commission treat paygo in this case?**

4 A. The Commission should include an amount for paygo when determining Empire's revenue
5 requirement, then track the actual paygo against that estimate. Company spreadsheets indicate
6 that the tax equity partner will submit an estimated \$11 million annually to the Wind Holding
7 Company. Erring on the side of caution, I recommend that the Commission include an
8 estimate of \$4 million⁶ in paygo payments in Empire's annual revenue requirement, and track
9 the difference between Empire's actual paygo revenues against that \$4 million per year, and
10 address the difference when designing Empire's rates in its next general rate case.

11 **INCOME TAX OFFSET IN CWC**

12 **Q. What is cash working capital ("CWC"), and how does it affect cost-of-service?**

13 A. Staff often use the following definition in its Cost of Service Report to explain CWC.

14 Cash Working Capital (CWC) is a rate base component that
15 represents a measurement of the amount of funds, on average,
16 required for the payment of a utility's day-to-day expenses, as well
17 as an identification of whether a utility's customers or its
18 shareholders are responsible for providing these funds in the
19 aggregate.

20
21 The aggregate CWC, whether it is a negative or positive amount, is included in a utility's
22 rate base used to determine its cost-of-service.

⁶ The \$4 million may seem to be a low offer, however, the modeling for the \$11 million is based on a 50% probability modeling. I want to insure that the ratepayer isn't in an overpayment situation.

1 **Q. What do income taxes have to do with CWC?**

2 A. There is a timing difference between when a utility gets cash from its customers for paying
3 its income taxes and when that utility actually pays those income taxes. That timing difference
4 impacts the utility's CWC.

5 **Q. What if a utility does not pay income taxes?**

6 A. If its customers pay for income taxes in rates that the utility does not pay to the taxing
7 authorities, then those customers should get a lag benefit in the utility's CWC.

8 **Q. Does Empire incur income tax?**

9 A. Yes, but due to several tax advantages; it does not pay income tax.

10 **Q. What do you mean when you say that Empire does not pay income tax?**

11 A. My review of past The Empire District Electric Company federal and state income tax returns,
12 as well as the recent returns of its new parent, Liberty, indicates that Empire will not be
13 responsible for any income tax liability in the foreseeable future.

14 **Q. Did Empire provide you with pro forma (stand-alone) income tax returns?**

15 A. Yes. The tax returns are prepared as if Empire District Electric was its own separate company
16 and not part of the Liberty consolidated group. The Company does this exercise to separate
17 Empire District Electric information for rate making purposes.

18 **Q. Do the pro forma returns indicate whether Empire District Electric would have had a
19 tax liability if it were a stand-alone company?**

20 A. Due to a pro forma net operating loss carryforward ("NOLC") that is attributable to Empire
21 District Electric, it will not have incurred a federal tax liability in at least three years.

1 **Q. Has the Empire’s company, Liberty Utilities, incurred a federal tax liability on the tax**
2 **returns that you reviewed?**

3 A. Yes. In both 2018 and 2019, Liberty had a tax liability of over \$3 million each year.

4 **Q. Should some portion of Liberty Utilities’ tax liability be allocated to Empire District**
5 **Electric?**

6 A. Normally the answer to that question would be “yes,” but this entire liability is due to a new
7 tax provision in the Tax Cuts and Jobs Act (“TCJA”). It is referred to as the base erosion and
8 anti-abuse tax (“BEAT”). I have included a Tax Policy Center explanation of BEAT as JSR-
9 D-03 but the basic purpose of BEAT is to require multinational corporations to pay a
10 minimum tax to the US government. Liberty Utilities is owned by a Canadian Corporation,
11 so the amount of tax paid with these returns represents the calculated BEAT.

12 **Q. Are you saying that Empire District Electric should not be allocated any of Liberty**
13 **Utilities’ BEAT tax liability?**

14 A. Yes. Absent the BEAT, Liberty, and ultimately Empire District Electric, have no tax liability.
15 This tax payment is the sole responsibility of the ultimate foreign parent company Algonquin.
16 Missouri ratepayers should not be responsible for BEAT taxes through Empire’s cost-of-
17 service merely because its parent company is a foreign entity.

18 **Q. What are you proposing for the tax offset to Empire’s CWC in this case?**

19 A. The ultimate dollar amount to use in the calculations will change as the Commission sets the
20 final cost of service amount but the expense lag needs to reflect the fact that ratepayers fund
21 the federal and Missouri state income tax expense built into rates but the money earmarked
22 for these expenses are not being paid out due to tax deferrals. The expense lag can be
23 viewed as the amount of time needed to pay out the expense to the vendor. I am
24 recommending an expense lag of 365 days. The income tax is never paid to either the United
25 States or Missouri governments during the test year so an entire year must be reflected in the

Direct Testimony of
John S. Riley
Case No. ER-2021-0312

1 expense lag⁷. Based on the information I currently have, I am recommending a negative
2 \$21,290,450 be included in Empire's rate base for the tax offset to Empire's CWC.⁸

3 **Q. Has the Commission made any recent decisions concerning the unpaid balance of**
4 **income tax expense within CWC calculations?**

5 A. Yes, in the recently published Report & Order from Spire Inc.'s rate case, Case No. GR-2021-
6 0108. The Commission accepted my argument that unpaid income taxes expense included in
7 the cost of service should be provided a 365 day expense lag to reflect the yearlong collection
8 but unremitted funds earmarked for income taxes.⁹

9 **ASBURY'S ULTIMATE DISPOSITION**

10 **Q. Would you provide some history and explanation about the Asbury Accounting**
11 **Authority Order?**

12 A. The Company retired the Asbury facility prior to the operation of law date of the last rate case
13 ER-2019-0374. Since the plant would not be operational, yet the assets and expenses would
14 still be included in rates, the Commission ordered an Accounting Authority Order ("AAO")
15 be established to track the assets and expenses from January 1, 2020 to June 30, 2021.

16 **Q. What is your opinion and the OPC position on the Asbury retirement?**

17 A. Asbury was a fully operational, profitable baseline power plant that was closed 15 years before
18 the scheduled retirement date. We are now looking at nearly \$160 million in stranded plant.
19 This was not a case of obsolesces and the ratepayer's should not be left holding this bag. If
20 the Commission determines that there are any amounts stranded after all costs are netted
21 against each other, then that amount should be excluded from rate base and only the

⁷ As pointed out earlier in testimony the tax payments are due to the foreign ownership of the Missouri utility.

⁸ The calculations are $\$5,255,954 * (45.04-365)/365 = (\$4,607,384)$ and $\$19,031,501 * (45.04-365)/365 = (\$16,683,066)$ totaling a negative \$21,290,450. The tax amounts will change until the final cost of service is determined. 45.04 being the revenue lag.

⁹ Spire, Case No. GR-2021-0108 Report & Order, Issue 8, Cash Working Capital, page 29

1 amortization of that remaining balance be included in rates. The OPC is opposed to any return
2 on the remaining balance of the Asbury facility.

3 **Q. What assessments do you have concerning Empire's presentation and revenue**
4 **requirement adjustments from the AAO calculations?**

5 A. Ms. Sanderson does a fairly good job of explaining what the Commission wanted tracked in
6 the AAO. On page 17 of her testimony she has summarized the regulatory assets and liability
7 in a clear and concise format. Ms. Sanderson provides a close approximation to the costs that
8 were to be tracked but I do want to point out that these balances will change over the course
9 of this rate case. I will argue the adjustments to the retired Asbury plant costs using the
10 balances in Sanderson's Figure 4 as a starting point.

11 **Q. Could you provide a brief narrative on your adjustments to Ms. Sanderson's page 17**
12 **exhibit, starting from the top?**

13 A. Yes. Ms. Sanderson lists the Asbury plant in service balance and then a separate portion of
14 the Asbury facility that would remain in service to administrate the wind farm generation. I
15 deducted the \$2,277,616 from the plant in service total to reflect the reduced amount of retired
16 Asbury plant.

17 Sanderson has included a fuel inventory of \$2.4 million in Net Rate Base, however, the
18 Commission included this amount in the last case even though Asbury had no burnable coal
19 after December 12, 2019. I deducted the balance from my column to reflect the nonexistent
20 coal.

21 I have eliminated the Cash Working Capital balance due to my inability to substantiate the
22 amount. I would be hard pressed to calculate a positive CWC knowing that income taxes,
23 property taxes and interest associated with the plant all carry a substantial negative CWC
24 balances.

1 I also eliminated the ADIT balances from the asset section and listed the total ADIT and
2 EADIT below the liability total to perform a final reduction to the rate base balance.

3 Some liabilities were added to the list. Since the \$2.4 million in fuel inventory was included
4 in the last rate case; the return associated with the asset should be recognized.¹⁰ The non-labor
5 retirement costs were removed in an effort to separate the proposed plant retirement with the
6 current cost of removal (“COR”) expenses that will be included in the case.

7 When all adjustments have been made, there should be \$150,261,425 in assets and
8 \$49,067,814 in liabilities in the AAO bringing a net asset balance of \$101,193,611. With the
9 reduction of both ADIT and excess ADIT, the balance remaining is just less than \$52.8
10 million.

¹⁰ I applied a simple estimate of 7% to the \$2,414,632 however, all of these numbers will be updated and carrying cost applied through the law date of the new rates.

Direct Testimony of
 John S. Riley
 Case No. ER-2021-0312

Asbury AAO	Empire	OPC Adjustments
Plant in Service	\$(217,663,073.00)	\$217,663,073.00
Remaining Plant	\$(2,277,616.00)	\$(2,277,616.00)
Accumulated Depreciation	\$62,618,776.00	\$(62,618,776.00)
Remaining Plant Accumulated Depreciation	\$(90,624.00)	\$(90,624.00)
Fuel Inventories	\$(2,414,632.00)	\$(2,414,632.00)
Cash Working Capital	\$(128,983.00)	\$ -
ADIT	\$(63,372.00)	\$ -
Excess ADIT	\$878,783.00	\$ -
Net Rate Base/ Regulatory Asset	\$(159,140,741.00)	\$150,261,425.00
Return on Asbury	\$(14,486,088.00)	\$(14,486,088.00)
Revenue from Scrap Removal	\$(10,248.00)	\$(10,248.00)
SPP rev/exp outside of the FAC	\$ -	\$ -
Depreciation Expense	\$(13,914,240.00)	\$(13,914,240.00)
Other O&M Expenses	\$(5,931,161.00)	\$(5,931,161.00)
Return on Fuel Inventory		\$(169,024.00)
Property Taxes	\$(2,860,004.00)	\$(2,860,004.00)
Non labor Asbury Retirement Costs	\$3,290,545.00	\$ -
	\$(33,911,196.00)	\$(37,370,765.00)
	1.31	1.313
Regulatory Liability	\$(44,526,314.00)	\$(49,067,814.45)
Net Regulatory Asset		\$101,193,610.56
ADIT		\$(32,338,406.00)
Excess ADIT		\$(16,055,610.00)
Removal of AQCS improvements		\$(122,412,831.00)
Remaining Asbury Plant to Amortize		\$(69,613,236.45)

1 Now, consider OPC witness Dr. Geoff Marke's contention that any cost associated to the
 2 installation of the AQCS system should be borne by the Company.¹¹ This would reduce the

¹¹ Please refer to Marke direct testimony for AQCS exclusion

1 rate base starting point from \$150,261,425 to \$27,848,594. After all other deductions are
2 considered, the net value of Asbury could be considered a negative \$69.6 million.

3 **Q. The Company is proposing a 26 year amortization period. Is this a fair timeframe?**

4 A. No, it is not. First of all, after installing some very expensive AQCS equipment in 2014,
5 Asbury was to be retired in 2035. 13 years from the new rates in this case. The Company
6 would like the Commission to believe that its suggestion of 26 years is for the benefit of the
7 customer. However, Empire expects a profit built into rates for this retired plant. Asking
8 customers to provide 26 years of return on a nonexistent plant is unreasonable. If the
9 Commission determines that there is stranded plant that should be amortized, then the 13 years
10 period should be used.

11 **Q. Does this conclude your direct testimony?**

12 A. Yes.