BEFORE THE
ARKANSAS PUBLIC SERVICE COMMISSION

IN THE MATTER OF THE APPLICATION OF	)	
OKLAHOMA GAS AND ELECTRIC COMPANY	)	
FOR APPROVAL OF A GENERAL CHANGE IN	)	DOCKET NO. 16-052-U
RATES, CHARGES AND TARIFFS	)	

DIRECT TESTIMONY

OF

BILL TAYLOR
PUBLIC UTILITY AUDIT SUPERVISOR
AUDIT SECTION

ON BEHALF OF THE GENERAL STAFF OF THE
ARKANSAS PUBLIC SERVICE COMMISSION

January 31, 2017

INTRODUCTION

Q. Please state your name and business address.

A. My name is Bill Taylor. My business address is Arkansas Public Service Commission (Commission), 1000 Center Street, Little Rock, Arkansas 72201.

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

A. I am employed by the General Staff of the Commission (Staff) as an Audit Supervisor in the Audit Section. In addition to providing supervisory support to the Manager of the Audit Section, I analyze utility company filings, conduct field audits, identify and evaluate accounting issues, develop positions on those issues and present those positions in written and oral testimony before the Commission, and perform other duties as assigned.

Q. What is your educational background and experience?

A. I hold a Bachelor of Science in Business Administration degree with a major in Accounting from Henderson State University, Arkadelphia, Arkansas, and a Master of Business Administration from the University of Arkansas, Fayetteville, Arkansas. I am a Certified Public Accountant, licensed to practice in Arkansas. Before joining Staff in March 2008, my employment included corporate management, private business ownership, chairing a community college department, and running my own practice as a public accountant providing audit, write-up, and income tax services to a variety of clients. Since joining Staff I have attended "The 50th Annual Regulatory Studies Program" sponsored by the Institute of Public Utilities of Michigan State University, in East Lansing, Michigan.

PURPOSE OF TESTIMONY

Q. What is the purpose of your Direct Testimony in this docket?

A. My testimony supports adjustments to Oklahoma Gas and Electric Company's (OG&E or Company) working capital assets (WCA). In addition, I discuss my examination of current, accrued, and other liabilities (CAOL) and accumulated deferred income taxes (ADIT). In so doing, I address the relevant Direct Testimony of Company witness Malini R. Gandhi.

MODIFIED BALANCE SHEET APPROACH

Q. What was the methodology used to determine WCA and CAOL amounts?

A. In developing its requested WCA and CAOL, the Company used the Modified Balance Sheet Approach (MBSA). In Order No. 7 of Docket No. 84-199-U, this Commission directed Staff to use the MBSA, either in the absence of a lead-lag study or as a check on a lead-lag study filed by the utility. Since that time, Staff has used the MBSA to determine working capital in evaluating rate case filings with continued acceptance by the Commission. Consistent with the Commission's directive, I used the MBSA and its embodied principles to determine revenue requirement. OG&E also used the MBSA in deriving its WCA and CAOL for inclusion in its filing.

Q. Please describe the MBSA.

A. The MBSA requires that assets, other than plant, that are not interest-bearing, which are necessary in providing utility service, and which are not considered elsewhere in the cost of service be included in a utility's rate base as WCA.

Additionally, all CAOL, which are a source of funds to the utility, should be included in the Company's capital structure at their appropriate cost. The MBSA recognizes two basic facts: (1) a utility has investments in assets other than plant which are necessary to provide utility service and on which a return should be allowed; and (2) a utility has sources of funds, other than equity and long-term debt, which should be included in the capital structure**.**

TEST YEAR

Q. What test year did OG&E use to determine its requested cost of service?

A. The Company's Application used a partially-projected test year ending June 30, 2016. In response to Staff data request APSC-1.5, OG&E provided updated information including twelve (12) months of historical data. Therefore, Staff's recommendation and my subsequent testimony are based on the updated test year.

WORKING CAPITAL ASSETS

Q. What level of WCA do you recommend and how does it compare to the Company's WCA recommendation?

A. I reduced the Company's actual test year-end balances of WCA from $1,391,230,900 to $432,959,295, a difference of $958,271,605, which is my Adjustment RB-10 amount. OG&E reduced test year-end balances from $1,391,230,900 to its *pro forma* level of $481,937,477, a difference of $909,293,423. OG&E and I both increased the updated test year-end account balances by $117,736,245 to the 13-month average balances. While the Company then decreased its 13-month averages by $791,557,178, I reduced the

13-month averages by $840,535,361, a difference of $48,978,183. Therefore, my recommended level of WCA is $48,978,183 less than the Company's.

Q. What specific WCA adjustments did you make which differ from or were not made by the Company?

A. In addition to the adjustments made by the Company, I reduced WCA by an additional $48,978,183 which includes the following adjustments:

(1) I removed $2,414,879 of accounts which earn interest;

(2) I removed $1,231,900 of a labor overhead amount from the Plant Materials and Operating Supplies which is provided for elsewhere in the Cost of Service;

(3) I removed a non-retail accounts receivable in the amount of $32,539,425;

(4) I removed $11,483,165 related to plant projects that are not in service;

(5) I removed $2,250,315 which was related to an update error of the Company;

(6) I removed $108,010 from an account that represents joint interest billing;

(7) I removed $594,130 from an account related to the deferral of Arkansas Pricing Education expenses from OG&E's previous rate case, Docket No. 10-067-U;

(8) I increased the regulatory asset accounts for Federal and State Income Taxes recoverable in future rates and decreased the regulatory asset for allowance for funds used during construction recoverable in future rates to test year end balances, a net increase of $1,114,869, which is more representative than the 13-month averages; and

(9) I restored the eighteen months of amortization expense the Company inadvertently removed related to Smart Grid-retired meters in the amount of $528,772.

CURRENT, ACCRUED, AND OTHER LIABILITIES

Q. How does your recommended CAOL compare to the Company's requested amount?

A. I reduced test year-end balances of CAOL from $2,864,536,111 to $302,724,921, a difference of $2,561,811,190. OG&E reduced its test year-end balances by $2,597,683,961 to its *pro forma* level of $266,852,150. My recommended level of CAOL is $35,872,771 more than the Company's. I provided my calculated amount of CAOL to Staff witness Regis Powell for inclusion in the capital structure at zero cost.

The Company and I both decreased the updated test year-end balances by $104,357,074 to the average balances for the 13 months ending June 30, 2016. Next, I decreased the average balances by $2,457,454,117 to eliminate accounts that should not be included in CAOL. The Company's comparable adjustment was a decrease of $2,493,326,888, which is $35,872,771 more than my adjustment.

Q. What specific adjustments did you make to CAOL that differed from or were not made by the Company?

A. In addition to the eliminations and adjustments made by the Company, I included accrued interest payable of $41,790,315 in CAOL. My calculation is based on *pro forma* debt and interest information provided by Staff witness Powell and uses the average daily balance and the average lag days between interest payment dates. The Company has use of the interest accrual at zero cost for the period of time between its daily receipt of revenues and its required payment of interest, for example, semi-annually in the case of long-term debt. Therefore, it is appropriate to include an amount in CAOL which is related to Staff's debt amounts included in the capital structure.

I also included in CAOL dividends payable on common stock of $23,674,658 based on my calculation of the number of days between OG&E's declaration date and the date paid along with the total amount of dividends paid during the *pro forma* year. It is appropriate to include dividends payable in CAOL recognizing the time between when the dividend is declared (recorded as a liability) and when it is paid (liability is removed).

I excluded from CAOL the 13-month average balances at June 30, 2016, of $62,520,232 related to Asset Retirement Obligations, consistent with Staff's treatment in plant.

I included three accounts totaling, $32,928,030, which OG&E excluded. The first account was described as FERC Formula related non-retail and the two others were described as Other Regulatory Liabilities related to Oklahoma only and therefore not Arkansas jurisdictional. My inclusion of these accounts is based on fungibility, which is an important principle embodied in the MBSA that has been utilized by the Commission for more than thirty years. Under the principle of fungibility, a distinction cannot be made as to which funding source is financing any particular asset or assets. Therefore, all current, accrued and other liabilities are included in the capital structure along with all other sources of funds at their respective costs, not just Arkansas jurisdictional amounts, in order to determine a weighted cost of capital for financing all assets of a company. When the resulting rate of return is applied to the Arkansas jurisdictional rate base, the proportionate level of funding for Arkansas is determined.

ACCUMULATED DEFERRED INCOME TAXES

Q. Please discuss your recommendation for ADIT.

A. I recommend $1,876,825,392 *pro forma* year end ADIT. The Company included projected ADIT of $1,714,085,478. I calculated my *pro forma* level of ADIT using the Company's *pro forma* level with three adjustments.

First, I synchronized ADIT with Staff's recommended plant additions by reducing ADIT by $20,132,011. Using Staff witness William L. Matthews' *pro forma* plant additions of $278,792,571 and the Company's requested *pro forma* plant additions of $382,217,287, I developed a ratio of 72.94%. I applied this ratio to OG&E's *pro forma* depreciation-related increase in ADIT, for a reduction of $20,132,011. In my Surrebuttal Testimony, I will evaluate the need, if any, to update ADIT based on Staff's updated plant recommendation.

The other two adjustments I made are due to OG&E's reduction of ADIT related to costs recovered from load serving entities for Base Plan Upgrade in the amount of $167,685,088 and Windspeed related ADIT of $15,186,827. I have increased ADIT by these amounts and would point out that the Company's proposal is contrary to the basic theory of fungibility, which is that the distinction cannot be made as to which source is funding a particular asset. All liabilities and equity capital represent fungible (i.e., of such a nature that one part may be equally interchangeable with another part of the whole) sources from which all company assets are funded. Once the ADIT was recognized on the Company's books it became part of the Company's source of funds and could no longer be tied to a particular asset.

Q. Does this conclude your testimony?

A. Yes.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing has been served on all parties of record by electronic mail via the Electronic Filing System on this 31st day of January, 2017.

/s/ Justin A. Hinton
Justin A. Hinton