

STATE OF KANSAS
BEFORE THE KANSAS CORPORATION COMMISSION MAY 09 2012

by
State Corporation Commission
of Kansas

Application of Mid-Kansas Electric Company, LLC for Approval to Make Certain
Changes in its Charges for Electric Service in the Geographic Service Territory
Served by Southern Pioneer Electric Company

Docket No. 12-MKEE-380-RTS

**PREFILED REBUTTAL TESTIMONY AND EXHIBITS OF
JAMES H. SMITH
The Blue Ridge Consultancy, LLC**

ON BEHALF OF

MID-KANSAS ELECTRIC COMPANY, LLC

BEFORE THE STATE CORPORATION COMMISSION
OF THE STATE OF KANSAS

REBUTTAL TESTIMONY
OF
James Howard Smith

DOCKET NO. 12-MKEE-380-RTS

I. INTRODUCTION AND BACKGROUND

1 **Q. Please state your name.**

2 A. My name is James Howard Smith.

3 **Q. By whom are you employed and what is your business address?**

4 A. I am a member of The Blue Ridge Consultancy, LLC ("TBRC"), *A Service Disabled*
5 *Veteran Owned Small Business*. My business address is 741 Ridgeview Road,
6 Brightwood, Virginia.

7 **Q. What is your present position at TBRC?**

8 A. I am Chief Executive Officer.

9 **Q. What prior positions have you held?**

10 A. Prior to joining TBRC, I was a managing director at Capital Management Associates,
11 Inc., a Principal at Arthur Andersen, LLP, and a Partner at Ernst & Young, LLP where I
12 served as Partner-in-Charge of tax and financial services in the firm's utility consulting
13 group. Prior to the private sector, I served as a tax law specialist under the Assistant
14 Commissioner, Technical at the National Office of the Internal Revenue Service in
15 Washington, DC.

1 **Q. Please describe your formal education.**

2 A. I received a BS degree (magna cum laude) from Belmont University in Nashville,
3 Tennessee in May 1973 and a Master of Business Administration in March 1979 from
4 Southern Illinois University at Edwardsville where I was elected to Beta Gamma Sigma.

5 **Q. Please describe your professional credentials.**

6 A. I have been a Certified Public Accountant since 1974 and have practiced in Tennessee,
7 Virginia and the District of Columbia. I am a member of the American Institute of
8 Certified Public Accountants, the Virginia Society of Certified Public Accountants, the
9 Tennessee Society of Certified Public Accountants, and the National Society of
10 Accountants for Cooperatives, among others.

11 **Q. Please describe your professional qualifications and experience.**

12 A. I teach Advanced Accounting and Finance, in the Master of Management - Co-operatives
13 and Credit Unions Programme in the Sobey School of Business of St. Mary's University,
14 Halifax, Nova Scotia. For over thirty-five years I have consulted with clients and their
15 representatives in general matters of taxation and finance. Most of the engagements have
16 involved issues of cooperative organizations and/or public utilities. In areas of taxation, I
17 consult with clients and their representatives on specific tax questions and tax planning;
18 assist in negotiations with the Internal Revenue Service ("IRS") at the national, regional,
19 and local levels; assist in the preparation, submission, and negotiation of Determination
20 Letters, Bankruptcy Code Section 505(b) Determinations, Closing Agreements, Private
21 Letter Ruling Requests and Technical Advice Requests before the Regional and National
22 Offices of the IRS; and assist in the evaluation and drafting of legislative initiatives. In
23 finance issues, I have been involved in financial workouts; privatizations; merger,

1 acquisition and corporate formations; equity management plans; and capital cost recovery
2 plans, in addition to traditional rate analysis for utilities. A detailed description of my
3 experience is contained in the resume attached to this testimony as **Exhibit JHS-1**.

4 **Q. Are you familiar with the federal income tax laws as they relate to cooperatives and**
5 **not-for-profit organizations, generally?**

6 A. Yes, I am. As you will note in **Exhibit JHS-1**, I have provided services to a number of
7 cooperative entities over the past thirty-five years. These organizations include numerous
8 forms of tax exempt organizations including tax-exempt cooperatives, cooperatives that
9 are taxable under Subchapter T of the Internal Revenue Code of 1986, as amended (26
10 C.F.R. Sections 1381 through 1388) (“IRC” or “the Code”), and both exempt and
11 nonexempt electric, telephone, gas and water cooperative and mutual organizations. I
12 frequently consult with cooperative clients on issues relating to maintaining tax-
13 exemption under IRS regulations and precedent. Furthermore, I have written, edited and
14 presented articles, speeches, seminars, and other materials on the taxation and finance of
15 electric and telephone cooperatives.

16 **Q. Have you testified before any regulatory commissions in the past?**

17 A. Yes. My testimony experience is listed in **Exhibit JHS-1**.

18 **Q. On whose behalf are you appearing in these proceedings?**

19 A. I am testifying on behalf of Mid-Kansas Electric Company, LLC (“Mid-Kansas” or
20 “MKEC”).

21 **Q. What is the purpose of your testimony in this proceeding?**

22 A. The purpose of my testimony is to respond to the direct testimony of Commission Staff,
23 the Citizens’ Utility Ratepayer Board (“CURB”), and Kansas Electric Power

1 Cooperative, Inc. (“KEPCo”), regarding the proposed treatment of Southern Pioneer’s
2 Income Taxes and issues regarding cooperative operation and structure.

3 **Q. Please summarize the main points and conclusions of your testimony.**

4 A. Staff Witness Bowman is recommending an alternative treatment of income taxes that
5 calls for a “flow through” adjustment based on actual taxes paid by Southern Pioneer.

6 My testimony demonstrates that such an adventure should not be undertaken unless and
7 until a number of issues are resolved.

8 KEPCO witness Stephen Daniel, and CURB witness Andrea Crane, testify that Southern
9 Power should not be entitled to an income tax component to its rates because it chose to
10 structure itself as a C-Corporation rather than a cooperative. My testimony explains why
11 this is a fallacious argument.

12
13 **II. RESPONSE TO STAFF’S RECOMMENDATION**

14 **Q. Please explain Staff’s recommendation on Southern Pioneer’s proposed recovery
15 of income taxes in this case.**

16 A. In his rebuttal Exhibit RJM-13, p.2, l. 17, Company witness Rich Macke included a
17 total income tax revenue requirement component of \$2,244,506 for the Test Year.

18 This cost of service item reflects the fact that Southern Pioneer is a taxable corporation
19 and by law is required to remit income taxes on corporate taxable income to the

20 Federal and State government. Given its historical tax rates, Mr. Macke determined
21 that in order to earn a post-tax DSC of 1.8, Southern Pioneer’s pre-tax margins would
22 need to be sufficient to pay a \$1,190,217 increase of income tax above the historical

1 amount recorded for 2010. (This calculation assumes the DSC Ratemaking Plan is
2 used.)

3 Staff Witness Bowman is recommending an alternative treatment of income
4 taxes that calls for a flow through adjustment based on actual taxes paid by Southern
5 Pioneer and in so doing, reduces taxes to zero (Exhibit LKB-2).

6 **Q. Do you agree with Ms. Bowman on the appropriateness of her alternative**
7 **treatment of recovering income taxes?**

8 A. No. While Ms. Bowman's recommendation may have some superficial appeal, I am
9 concerned that implementation of her recommendation could result in significant tax,
10 accounting, finance and regulatory issues for Southern Pioneer, each of which I have
11 explained below.

12 **Q. Are other important issues created by the proposed treatment of Southern Pioneer's**
13 **income taxes?**

14 A. Yes. Staff's recommendation results in an intergenerational inequity.

15 **Q. Please explain.**

16 A. Staff argues that Southern Pioneer did not pay income taxes during the test year, and
17 therefore, rates set for customers today should not include an income tax component.
18 However, the reason Southern Pioneer had no income tax payment during the test year is
19 because Southern Pioneer, like most taxable entities, takes advantage of accelerated
20 depreciation laws. This means that Southern Pioneer has greater depreciation expense at
21 the earlier stages of an asset's life than it would if it depreciated the asset equally
22 throughout its life (straight-line depreciation method). Because depreciation expense is
23 higher in the early years, income tax expense is lower. However, the income tax is not

1 avoided; it is simply deferred to a later time when the asset is in the later years of its life.
2 Eventually, this situation will reverse itself and Southern Pioneer's income taxes actually
3 paid will likely be higher than they would have been if the asset had been depreciated
4 equally through-out its life.

5 Southern Pioneer should be allowed to benefit from the income tax effects of
6 accelerated depreciation, however, for ratemaking, a normalization adjustment is needed
7 to ensure that present customers pay their actual share of the income tax expense.

8 Without this normalization, the income tax expense liability is shifted from present
9 customers to future customers. Present customers do not pay their fair share, and future
10 customers have to make it up by paying more than their fair share. Normalization
11 ensures intergenerational equity between present and future ratepayers; Staff's
12 recommendation unnecessarily removes normalization from the calculation of present
13 rates, to the unfair detriment of future ratepayers.

14 **Q. Does the State Corporation Commission of the State of Kansas ("Commission" or**
15 **"KCC") follow a policy of normalization to avoid intergenerational issues such as**
16 **the one related to accelerated depreciation and income taxes?**

17 A. Yes. This policy has been recently affirmed by the Commission in its Order for Westar
18 Energy, Inc. in Docket No. 12-WSEE-112-RTS. The Commission stated that it must
19 "balance the interests of: (1) utility's investors versus ratepayers; (2) *present ratepayers*
20 *versus future ratepayers*; and (3) the public interest." (Order dated April 18, 2012, p. 5,
21 emphasis added.) Specifically discussing the intergenerational concern, the Commission
22 stated, "[t]he balancing of present ratepayers vs. future ratepayers is referred to as an
23 intergeneration issue, which occurs when present ratepayers are expected to pay now for

1 something that will benefit future ratepayers. Staff stated it was not aware of any rate
2 design intergeneration issues in this docket.” (Id., at p. 32.) If the costs attributable to
3 one generation of ratepayer are passed to another generation, intergenerational inequity is
4 created. The KCC has conscientiously attempted to avoid the creation of such
5 intergenerational inequity in its ratemaking decisions. (See also *In the Matter of a*
6 *General Investigation by the Commission of the Projected Costs and Related Matters of*
7 *the Wolf Creek Nuclear Generation Facility at Burlington, Kansas*, Docket No. 120,924-
8 U, Order issued September 27, 1985, p. 85, paras.2.)

9 **Q. Has Ms. Bowman proposed a recovery mechanism to implement her actual**
10 **income tax flow through recommendation?**

11 A. No, and that is one fundamental problem with her recommendation. She does not address
12 the intergenerational inequity her recommendation causes, she does not explain how
13 customers of the Southern Pioneer Division would eventually pay the full amount of the
14 actual income tax expense, and she does not explain how Southern Pioneer Division will
15 be able to recover in subsequent periods amounts it pays for income taxes in earlier
16 periods without violating the public policy prohibition of retroactive ratemaking.

17 **Q. You stated above that implementation of Ms. Bowman’s recommendation could**
18 **result in significant tax, accounting, finance and regulatory issues for Southern**
19 **Pioneer. Please address these issues.**

20 A. Five primary issues must be successfully resolved to prevent the deleterious tax,
21 accounting, financial and regulatory consequences of Ms. Bowman’s proposed income
22 tax recovery recommendation. I will address each one in turn.

23

1 *1. Tax Issue:*

2 **Q. Please explain the Tax issues caused by Ms. Bowman's recommendation.**

3 A. As currently required under the federal income tax laws as set forth in the Internal
4 Revenue Code of 1986 as amended ("IRC"), Southern Pioneer depreciates its property
5 under the Modified Accelerated Cost Recovery System ("MACRS") (Section 168 *et*
6 *sec*). The law excludes from MACRS any public utility property for which the
7 taxpayer does not use a normalization method of accounting. The method of
8 accounting proposed by Staff is not a normalization method of accounting.

9 Consequently, all tax benefits of MACRS to Southern Pioneer would be at risk. If the
10 Internal Revenue Service were to find that the the property of Southern Pioneer was to
11 be considered "public utility property" under the federal income tax laws, and that a
12 normalization method of accounting is not being followed, then the use and benefits
13 of MACRS would be disallowed. This means that Southern Pioneer would pay higher
14 overall taxes; an outcome that harms all interests involved in this docket.

15

16 *2. Tax Accounting Issue:*

17 **Q. Please explain the Tax Accounting issues that need to be resolved before Ms.
18 Bowman's recommendation can be appropriately considered.**

19 A. As Southern Pioneer has been following the current method of accounting for depreciable
20 property for over two years, Southern Pioneer is precluded from changing from its
21 current method of accounting to a straight line method or to the regulatory life of the
22 assets method. This means that Southern Pioneer Division will not be able to adjust its
23 tax depreciation accounting method to more closely match its regulatory depreciation in

1 an attempt to ameliorate the adverse tax consequences of Staff's proposed income tax
2 treatment.

3
4 3. Regulatory Issue:

5 **Q. What is the Regulatory issue that needs to be resolved?**

6 A. If the Staff's proposed recovery method were implemented, then, in the future when
7 Southern Pioneer begins paying the income taxes that today are being deferred, Southern
8 Pioneer will be adversely affected by the regulatory lag of paying tax and only
9 subsequently having the KCC authorize collection. An annual rate case would be
10 necessary to continue adjusting rates to include the increasing income tax payment, but
11 even with annual rate cases, the harm caused by the delay in recovery cannot be
12 overcome. The KCC cannot authorize collection of an item that arose in a prior period,
13 as that would likely constitute retroactive ratemaking.

14
15 4. Accounting Issue:

16 **Q. What is the Accounting Issue caused by Ms. Bowman's recommendation?**

17 A. Southern Pioneer follows accepted accounting standards in keeping its books and records
18 and will satisfy the requirement that it report its tax expense on the universally accepted
19 and mandated accounting for comprehensive interperiod tax allocation (as explained in
20 more detail below.) Southern Pioneer should collect current and deferred taxes in the
21 revenue requirement for the year to which the taxes are attributable, not the year in which
22 they are actually paid. Not only are consumers benefited by charging items of expense
23 to the period in which they occur, this accounting standard is required by the Rural

1 Utilities Service (“RUS”), and by the Uniform System of Accounts (“USOA”) as
2 established by the Federal Energy Regulatory Commission (“FERC”). The USOA has
3 been adopted and/or officially followed by virtually all regulators in the United States,
4 including the KCC.¹

5 The RUS standard is contained at 7 CFR part § 1767.15 and reads as follows:

- 6 (1) *Comprehensive interperiod income tax allocation.* (1) Where there are timing
7 differences between the periods in which transactions affect taxable income and
8 the periods in which they enter into the determination of pretax accounting
9 income, the income tax effects of such transactions are to be recognized in the
10 periods in which the differences between book accounting income and taxable
11 income arise and in the periods in which the differences reverse using the deferred
12 tax method.
- 13 (2) Comprehensive interperiod tax allocation should be followed whenever
14 transactions enter into the determination of pretax accounting income for the
15 period even though some transactions may affect the determination of taxes
16 payable in a different period.
- 17 (3) Utilities are not required to utilize comprehensive interperiod income tax
18 allocation until the deferred income taxes are included as an expense in the rate
19 level by the regulatory authority having rate jurisdiction over the utility.
- 20 (4) Where comprehensive interperiod tax allocation accounting is not practiced the
21 utility shall include as a note to each financial statement, prepared for public use,
22 a footnote explanation setting forth the utility’s accounting policies with respect
23 to interperiod tax allocation and describing the treatment for rate making purposes
24 of the tax timing differences by regulatory authorities having rate jurisdiction.
- 25 (5) Should the utility be subject to more than one agency having rate jurisdiction, its
26 accounts shall appropriately reflect the ratemaking treatment (deferral or flow
27 through) of each jurisdiction.
- 28 (6) Once comprehensive interperiod tax allocation has been initiated either in whole
29 or in part it shall be practiced on a consistent basis and shall not be changed or
30 discontinued without prior RUS approval.

¹ *In the Matter of a uniform system of accounts to be prescribed and kept by electric companies*, Docket No. 5142, Order issued December 17, 1947 (the Federal Power Commission’s Uniform System of Accounts was established as the rules and regulations of the Kansas Commission.) See also, K.A.R. 82-1-231(c)(4)(D) and (E).

1 (7) Tax effects deferred currently will be recorded as deferred debits or deferred
2 credits in Accounts 190, Accumulated Deferred Income Taxes; 281, Accumulated
3 Deferred Income Taxes—Accelerated Amortization Property; 282, Accumulated
4 Deferred Income Taxes—Other Property, and 283, Accumulated Deferred
5 Taxes—Other, as appropriate.

6 (8) The resulting amounts recorded in these accounts shall be disposed of as
7 prescribed in this system of accounts or as otherwise authorized by RUS.

8 The USOA sets forth a similar requirement in general instruction 18:

9 *18. Comprehensive Interperiod Income Tax Allocation.*

10
11 A. Where there are timing differences between the periods in which transactions
12 affect taxable income and the periods in which they enter into the determination of
13 pretax accounting income, the income tax effects of such transactions are to be
14 recognized in the periods in which the differences between book accounting income
15 and taxable income arise and in the periods in which the differences reverse using the
16 deferred tax method. In general, comprehensive interperiod tax allocation should be
17 followed whenever transactions enter into the determination of pretax accounting
18 income for the period even though some transactions may affect the determination of
19 taxes payable in a different period, as further qualified below.

20 B. Utilities are not required to utilize comprehensive interperiod income tax
21 allocation until the deferred income taxes are included as an expense in the rate level
22 by the regulatory authority having rate jurisdiction over the utility. Where
23 comprehensive interperiod tax allocation accounting is not practiced the utility shall
24 include as a note to each financial statement, prepared for public use, a footnote
25 explanation setting forth the utility's accounting policies with respect to interperiod
26 tax allocation and describing the treatment for ratemaking purposes of the tax timing
27 differences by regulatory authorities having rate jurisdiction.

28 C. Should the utility be subject to more than one agency having rate jurisdiction, its
29 accounts shall appropriately reflect the ratemaking treatment (deferral or flow
30 through) of each jurisdiction.

31 D. Once comprehensive interperiod tax allocation has been initiated either in whole
32 or in part it shall be practiced on a consistent basis and shall not be changed or
33 discontinued without prior Commission approval.

34 E. Tax effects deferred currently will be recorded as deferred debits or deferred
35 credits in accounts 190, Accumulated Deferred Income Taxes, 281, Accumulated
36 Deferred Income Tax- es—Accelerated Amortization Property, 282, Accumulated
37 Deferred Income Taxes—Other Property, and 283, Accumulated Deferred Income
38 Taxes—Other, as appropriate. The resulting amounts recorded in these accounts shall

1 be disposed of as prescribed in this system of accounts or as otherwise authorized by
2 the Commission.

3 Clearly, the Staff's recommendation is inconsistent with these standards.

4 5. Financial Issue:

5 **Q. Please explain the Financial Issue that must be resolved before Ms. Bowman's**
6 **recommendation can be appropriately considered by the Commission.**

7 A. Under Staff's recommendation, Southern Pioneer would be precluded from collecting its
8 income tax liability until a future period, and even then, will only collect the increasing
9 amount it if an annual rate case is filed. Due to this fact, Southern Pioneer will have to
10 pay its tax bill but not collect the revenue for this obligation for approximately twelve
11 months after it has been incurred (assuming that recovery is allowed by the Commission).
12 This will likely cause the need for increased borrowing and could easily result in cash
13 flow difficulties.

14 Of particular concern to Southern Pioneer is that Staff has indicated its preference
15 for Southern Pioneer, at some point in time, to become a non-profit cooperative, perhaps
16 by transferring its assets to Pioneer, to a new cooperative entity or by recapitalization of
17 Southern Pioneer into a cooperative. If Staff's recommendation on income tax is
18 accepted and Southern Pioneer is not allowed to collect its tax liability as it is incurred,
19 then when Southern Pioneer transfers its assets to a non-profit cooperative in the future,
20 the Company will have no resources to pay the tax imposed on this future transfer of its
21 assets to a non-profit.

1 **Q. Please explain.**

2 A. As set forth in Internal Revenue Regs. Section 1.337(d)-4(a)(1), at the time a for-profit
3 company transfers its assets to a non-profit, taxes must be paid on the appreciated value
4 of the company. Section 337(d) of the Code authorizes the Secretary to prescribe
5 regulations as may be necessary or appropriate to carry out the purposes of the
6 amendments made by subtitle D of title VI of the Tax Reform Act of 1986, including
7 regulations to ensure that such purposes may not be circumvented through the use of a
8 tax-exempt entity. The legislative history concerning a 1988 amendment to section
9 337(d) explains that the grant of authority in section 337(d) "includes rules to require the
10 recognition of gain if appreciated property of a C corporation is transferred to . . . a tax-
11 exempt entity in a carryover basis transaction that would otherwise eliminate corporate
12 level tax on the built-in appreciation." S. Rep. No. 445, 101th Cong., 2d Sess. 66 (1988)
13 (footnote omitted).

14 Section 1.337(d)-4(a)(1) of the regulations sets forth the general rule that if a
15 taxable corporation transfers all or substantially all of its assets to one or more tax-
16 exempt entities, the taxable corporation must recognize gain or loss immediately before
17 the transfer as if the assets transferred were sold at their fair market values.

18 **Q. Could Southern Pioneer avoid this problem by recapitalizing into a "taxable" not**
19 **for profit entity?**

20 A. No. Section 501(c)(12)(A) of the Code provides, in part, for the exemption from federal
21 income tax of mutual or cooperative telephone companies, or like organizations; but only
22 if 85 percent or more of the income consists of amounts collected from members for the
23 sole purpose of meeting losses and expenses. IRC section 501(a) provide that

1 organizations described in subsection (c) (which includes section 501(c)(12)), “shall” be
2 exempt. This suggests that an organization satisfying the qualifications of section
3 501(c)(12) MUST be exempt, regardless of the desires of the taxpayer, as the term “shall”
4 in the IRC is mandatory.

5 **Q. Does Staff make any other recommendations you would like to address from an**
6 **income tax perspective?**

7 A. Yes. In summarizing Staff reasons for disallowing the DSC Ratemaking Plan advanced
8 by Southern Pioneer, Staff Witness Bowman (page 17, lines 8-18), relying on a
9 discussion in Docket No. 06-MKEE-524-ACQ (524 Docket), concludes that if Southern
10 Pioneer had been “organized as a cooperative, the company would be eligible for
11 deregulation as soon as the MKEC spin down is complete, consequently, “it does not
12 seem appropriate to allow them the special treatment that would be received through the
13 formula rate plan.” This conclusion is flawed in that it assumes there is no tax effect
14 under IRC section 337(d) in converting a taxable organization (Aquila WPK) into a tax
15 exempt organization (the tax exempt owners of Mid-Kansas Electric Company). It
16 further assumes that there is no tax effect to the cooperative MKEC owners in receiving
17 partnership distributions. To my knowledge, such assumptions are not supported in the
18 record.

19
20 **III. RESPONSE TO KEPCO AND CURB**

21 **Q. You indicated earlier in your testimony that KEPCo witness Daniels and CURB**
22 **witness Crane make negative recommendations in this case on the basis of the**

1 **organizational form chosen by Southern Pioneer. Would you please respond to**
2 **their testimony?**

3 A. Yes. Mr. Daniel and Ms. Crane testify that Southern Pioneer should not be entitled to an
4 income tax component to its rates because it is a for-profit corporation rather than a
5 cooperative. Their argument is specious and reflects a lack of understanding of the tax
6 laws and the general and specific requirements that are imposed on cooperatives..

7 **Q. Please explain.**

8 A. Mr. Daniels, in advancing his notion of “balancing of respective interests of
9 MKEC/Southern Pioneer and customers” seems to suggest that all would be well if only
10 Southern Pioneer were not a taxable entity, and he states that its failure to be a not- for-
11 profit entity creates an “unjustifiable negative effect on those customers.” (Page 13, lines
12 8-9.) Similar comments pervade Ms. Crane’s testimony. Mr. Daniels then concludes
13 that,

14 Southern Pioneer chose a for-profit, taxable structure, which has led to increased
15 rates due to the necessity to collect a component of costs for imputed income
16 taxes. Southern Pioneer chose a C-corporation business structure, which results
17 in all equity earnings accruing to the benefit of the sole stockholder, Pioneer.
18 This contrasts sharply with a cooperative structure where the equity interest
19 created through rates would accrue to the members/ratepayers. Under the
20 cooperative structure, the members/ratepayers ultimately would receive patronage
21 capital assignments and eventual refunds. Southern Pioneer’s customers,
22 however, will not.” (p. 26, ll. 4-11.)

23
24 This argument - that a non-profit cooperative business structure is the only prudent
25 method of doing business, and that the tax issue is the only relevant consideration in
26 making this decision - is naïve. Taken to its logical conclusion, the Commission should
27 be pursuing the creation of public utility districts to seize control of all investor owned
28 utilities in the nation to eliminate taxable debt, property tax, equity returns on stock,

1 income tax and regulation. Of course, this is not reasonable because there are many
2 factors to consider when evaluating the prudence of a management decision regarding the
3 appropriate operational structure of an entity. Two of the more important factors are the
4 ability to raise capital to finance the entity and the overall income tax impacts related to
5 the transaction.

6 **Q. Please elaborate on the concepts underlying cooperative operation.**

7 A. Cooperatives are characterized by their form of operation, not by a particular structure.
8 Consequently, partnerships and virtually all corporate forms could chose to “operate” on
9 a cooperative basis. But first and foremost, a cooperative, as defined by the International
10 Co-operative Alliance (ICA), is “an autonomous association of persons united
11 *voluntarily* to meet their common economic, social, and cultural needs and aspirations
12 through a jointly-owned and democratically-controlled enterprise.” (Emphasis added.)
13 (The ICA recognizes seven principles of cooperative operation.) The notion of “free” or
14 “voluntary association” is a requirement of federal income tax law that is expressed as
15 “mutual joinder of interest”, meaning that an adequate number of cooperators exist to
16 constitute a large enough group to operate cooperatively. Beyond the mutual joinder of
17 interest, the three fundamental principals involved in operating on a cooperative basis and
18 required for federal income tax purposes are defined in *Puget Sound Plywood, Inc. v.*
19 *CIR.*, 44 T.C. 305 (1965), *acq.* 1966-1 C.B. 3. They are:

- 20 (1) Subordination of capital (return *of* capital rather than return *on* capital),
- 21 (2) Democratic control (i.e. one member, one vote), and
- 22 (3) Operation at cost (achieved by returning margins to patrons on a patronage
23 basis).

1 **Q. How are cooperatives generally formed?**

2 A. Cooperatives are generally formed by the cooperators that become member/patrons of the
3 organization they voluntarily form. That fundamental and basic notion of cooperatives is
4 what makes much of the “if onlys” in Mr. Daniel’s testimony fallacious. There is a
5 cooperative in the mix in this case – Pioneer, and it is Pioneer whose original members
6 were the cooperators. Pioneer has a cooperative culture and heritage and is protective of
7 those attributes. In considering ownership of the Aquila assets, the Pioneer Board sought
8 counsel and considered not only the potential deleterious tax, finance, accounting and
9 operating consequences to Pioneer, but also the radical changes in its governance and
10 ethos that could occur. The Pioneer Board acted responsibly to its cooperative members
11 by not only performing its due diligence in seeking legal and tax advice, but also by
12 choosing to create Southern Pioneer as a C-Corporation. Forced association is not free
13 association and the suggestion by Mr. Daniels that imposing his bizarre notion of
14 cooperative operation on these entities is the *deus ex machina* for his client’s rate issue, is
15 feckless.

16 **Q. Does that conclude your prefiled testimony.**

17 A. Yes.

18

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Background

Jim Smith is a Certified Public Accountant and Chartered Global Management Accountant who specializes in cooperative finance, operations and taxation, concentrating on issues of rural development. He consults in matters of the finance and taxation of rate regulated utilities and cooperatives. In the area of taxation, he consults with clients and their representatives on specific tax questions and tax planning; assists in negotiations with the Internal Revenue Service (IRS) at the national, regional, and local levels; and aids in the preparation, submission and negotiation of determination letters, private ruling requests, technical advice requests, and closing agreements before the Internal Revenue Service.

In areas of finance, Mr. Smith's experience includes recapitalizations, bankruptcies, financial workouts, privatization, merger, acquisition and corporate formations, equity management plans, and capital cost recovery plans, in addition to traditional rate analysis for utilities.

He follows matters of tax and energy policy before the committees of Congress and maintains communication with the IRS, the Treasury Department, the Rural Utilities Service, the Energy Department and other agencies on tax policy, administrative and energy issues. Due to the nature of issues that give rise to tax legislation, Mr. Smith also maintains liaison with other congressional and executive offices and committees at the Federal and State levels of government.

For the past several years, Jim has expanded his scope of services to include not only rural utilities but also a myriad of needs to achieve rural development – focusing on the unique needs of localities, rural health care, cooperative business formations, State and local tax and fiscal policy.

Education, Professional and Academic Associations and Publications

- Education

Masters Business Administration, Concentration in Finance, Southern Illinois University at Edwardsville, March 1979

B.S., Accounting (Magna Cum Laude), Belmont University, Nashville, Tennessee
May 1973

Member of Gamma Beta Sigma & Blue Key

- Professional Associations

Certified Public Accountant and Chartered Global Management Accountant. Member of the American Institute of Certified Public Accountants, The Virginia Society of Certified Public Accountants, the Tennessee Society of Certified Public Accountants, the National Society of Accountants for Cooperatives and the Virginia Government Finance Officers Association.

- Academic Associations

Lecturer—Advanced Accounting and Finance, Master of Management--Co-operatives and Credit Unions Programme ("MMCCU"), Sobey School of Business of St. Mary's University, Halifax, Nova Scotia

<http://www.smu.ca/academic/sobey/programs/mmccu/welcome.html>

- Governmental and NGOs

Virginia State S.A.L.T. Council – Treasurer. Technical Advisor to the Attorney General of the Commonwealth of Virginia and Board of Directors as well as local and regional TRIAD organizations (SALT (Seniors and Law Enforcement Together) address the needs of senior citizens and law enforcement in combating financial fraud and abuse to senior citizens (2006—present) <http://www.oag.state.va.us/Programs%20and%20Resources/TRIAD/index.html>;

Contract Review Task Force for the Board of Supervisors, Madison County, Virginia (2012—present)

Financial Advisory Committee to Board of Supervisors, Madison County Virginia (2008—2010)

- Publications

Smith, J.H., "MC Finances at Tipping Point?," The Madison Eagle, Madison, VA, November 2011 <http://www2.madison-news.com/news/2011/nov/03/mc-finances-tipping-point-ar-1433272/>

Robb, Alan J., Smith, James H., Webb, J Tom, "Co-operative Capital: What it is and Why Our World Needs It," *Financial Co-operative and Local Development*, edited by Silvio Goglio and Yiorgos Alexopoulos, Routledge, Abingdon, Oxfordshire UK, Spring, 2012

Robb, Alan J., Smith, James H., Webb, J Tom, "Co-operative Capital: What it is and Why Our World Needs It," *Financial Co-operative Approaches to Local Development Through Sustainable Innovation*, European Research Institute on Cooperative and Social Enterprises, Trento Italy, June 2010

Smith, J. H., Stone, H., "Setting the Record Straight on Cooperative Acquisitions" Energy Central's online publication, EnergyPulse, January, 2004.

Smith, J. H., Stone, H., "Cooperative IPOs: Distinguishing Fact from Fantasy," Public Utilities Fortnightly, October 15, 2001.

Smith, James. H., "Electric Cooperatives and FERC Order 2000," The Cooperative Accountant , Summer 2000.

Eddy, T., Smith, J., Stone, H., "Rural Electric Cooperatives and FERC Order No. 2000," CMA White Paper, April 2000.

Smith, James H., "IRS Proposes Examination Guidelines for Rural Electric Cooperatives," The Cooperative Accountant, Fall, 1996.

Smith, James H., Dolan, Kevin P., "Tax Traps for the Unwary - RUS Section 12 Deferrals," The Cooperative Accountant, Spring 1995.

Smith, James H., "The Federal Income Taxation of Rural Electric Cooperatives," Ernst & Whinney, 1979, Washington, DC

Smith, James H., "Depreciation, Salvage, and Cost of Removal—A Critical Analysis," Ernst & Whinney, 1983

His professional affiliations and history include:

The Blue Ridge Consultancy, LLC (*A Service Disabled Veteran Owned Small Business*)—Owner (2005-- present) A financial and management consultancy.

James Howard Smith, CPA, PLLC (*A Service Disabled Veteran Owned Small Business*) – Owner (2005-- Present) A professional services firm providing accountancy services.

Wabash Valley Power Association— Outside Audit Committee Member of this \$750 million in revenues and \$1Billion total asset SEC registered electric utility operating as a not-for-profit membership association and a generation and transmission cooperative. (2004--present)

Master of Management--Co-operatives and Credit Unions Programme ("MMCCU"), Sobey School of Business of St. Mary's University, Halifax, Nova Scotia – Lecturer (2003—present)
(<http://www.smu.ca/academic/sobey/programs/mmccu/welcome.html>)

Capital Management Associates (Managing Director) A financial advisory and consultancy. (1999—2004)

Arthur Anderson, LLP (Principal, Office of Federal Tax Services) An international consultancy where I assisted in creating the most successful cooperative utility practice in the nation, focusing on client development as well as staff training and development. (1994—1999).

Ernst & Young, LLP (Partner) Partner in charge of tax and financial services, Ernst & Young Utility Group. Created the practice, beginning with no client base, to become the premier financial services group attending to the needs of rural electric and telephone cooperatives. (1977—1993)

Internal Revenue Service, National Office (Tax Law Specialist) Prepared and published authoritative publications for reliance on and use by the IRS, Tax Professionals and taxpayers. (1973—1977)

Projects that Mr. Smith has directed include:

Telephony

- 2011 National Telephone Cooperative Association Annual Meeting Conference -- conducted By-law Review for Board of Directors regarding cooperative operation, cooperative equity and taxation.
- 2006 Canadian Directors Conference for the National Telephone Cooperative Association (NTCA) regarding bylaw review
- Assisted various telephone cooperatives in addressing technical tax and cooperative issues, often before the National Office of the Internal Revenue Service.
 - Grand River Mutual Telephone Corporation
 - Chariton Valley Telephone Corporation
 - Northeast Missouri Rural Telephone Company
 - Guadalupe Valley Telephone Cooperative
 - Citizens Telephone Cooperative
 - Pioneer Telephone Cooperative
 - West Kentucky Rural Telephone Cooperative
 - DeKalb Telephone Cooperative
 - Citizens Telephone Cooperative
- Assisted National Telephone Cooperative Association in various tax issues at the National level and make presentations to its members
- Assisted National Exchange Carrier Association (NECA) in toll settlement negotiations regarding cooperative issues

Broadband

- Assisting a wireless internet service provider serving the Commonwealth of Virginia from the Blue Ridge Mountains to the Chesapeake Bay
- Assisting several start-up as well as established enterprises in applying for RUS Broadband Loans

Cooperative Equity

- Matanuska Telephone Association, Inc. and Copper Valley Telephone Cooperative, Inc., testimony before the Regulatory Commission Of Alaska regarding cost of equity
- Assisted numerous electric and telephone cooperatives in addressing equity management plans that include present value payment of capital credits

Class Action

- Represent cooperative before State and Federal court in addressing payment of capital credits on a present value basis

Financings

- Due diligence and other advisory services
 - Farm Credit Administration--Assisting the FCA's Office of Secondary Market Operations ("OSMO") in developing a knowledge base of the rural electric cooperative industry and adopt underwriting criteria consistent with the enterprise risk associated with the industry to evaluate rural electric cooperative mission-related transactions performed by the U.S. Federal Agricultural Mortgage Corporation ("FarmerMac"). (2006--)
 - Rural Utilities Service-- Completed the Wholesale Power Contract Report for the Rural Utilities Service covering a description of various wholesale power market participants, transmission market institutions and participants, wholesale power transactions including the so-called Master Purchase and Sale Agreements, contracting risks and risk mitigation techniques, evaluation of contract practices, and legal, accounting, financial and tax related issues pertaining to modifications of the all requirements contract. (2004)
- Project Financing--Assist power marketers, investors, etc. in constructing merchant and traditional investments for use by electric cooperatives
 - Reliant Energy Corporation (1999—2000)
 - ATCO Electric (2001-- 2004)
 - CMS (2000—2004)
- Corporate Formations and Initial Public Offerings
 - Kwajalein Atoll Development Authority--Assisted KADA in submitting a loan application to the REA for new distribution and generation facilities. (1989)
 - Redwood Properties--Assisted this real estate developer in maximizing its opportunities by creation of water/waste water utilities as an alternative to the harsh consequences imposed on contributions-in-aid-of construction by the Tax Reform Act of 1986. (1988)
 - Tri County Gas--Assisted this investor group in attaining regulatory approval and construction financing for this start-up gas distribution company. (1988-1989)
 - Palm Beach County Utilities Corporation--Assisted in the financial analysis, review and reporting requirements of this company's initial public offering. (1986-1989)

- RUS Prepayments--Assisted several distribution cooperatives in analyzing the financial and tax benefits/costs of prepaying their Rural Utilities Service debt. Analyzed the tax consequence of RUS debt prepayment and recommended the statutory remedy for prepayment for the use of:
 - Bank for Cooperatives (1987-1989)
 - U.S. Dept. of Agriculture Rural Utilities Service (1987-1989)
 - Bluebonnet Electric Cooperative (1987-1989)
 - Guadalupe Valley Electric Cooperative (1987-1989)
 - Jones Onslow Electric Membership Cooperative (1995 -1996)
 - Pitt & Green Electric Membership Cooperative (1995 -1996)
 - Bossier Electric Cooperative (1994 -1995)
 - Vinson & Elkins (1987-1989).

- Tax Exempt Financings
 - Florida Municipal Power Agency (1982)
 - Pollution Control Financings (1981-present)
 - Bond Defeasance - San Miguel Electric Cooperative (1985)

- Traditional Lease Financings--Evaluation of tax and finance issues for:
 - Allegheny Electric Cooperative
 - Big Rivers Electric Cooperative
 - Cajun Electric Power Cooperative
 - Various Others (1981-present)

- "Safe Harbor" Lease Financings--Evaluation of tax and finance issues involving approximately \$1.5 billion in assets. (1981-1983)
 - Associated Electric Cooperative
 - Cajun Electric Power Cooperative
 - Plains Electric Generation and Transmission Cooperative
 - Sam Rayburn Generation and Transmission
 - South Mississippi Electric Power Association
 - Tri State Generation and Transmission Association.

Mergers, Acquisitions, Divestitures, Restructuring, and Recapitalizations

- Mergers
 - Directed the merger of Northern Michigan Electric Cooperative and Wolverine Electric Cooperative (1980-1981)

 - Assisted Tri-State Generation and Transmission Association in tax aspects of a merger with Colorado-Ute (1989-1991).

 - Assisted numerous distribution cooperatives in obtaining post-merger benefits offered under regulations of the Rural Utilities Service.

- Acquisitions--Finance, regulatory, pricing and tax analysis for asset and/or stock acquisitions on behalf of:
 - Investor Groups (1981-present)
 - Florida Municipal Power Agency (1981-1982)
 - Old Dominion Electric Cooperative (1982)
 - Midwest Energy (Kansas) (1985-1995)
 - Palm Beach County Utilities Corporation (1986-1990)
 - Pee Dee Electric Cooperative (1990)
 - Cotton Electric Cooperative (1990)
 - Guadalupe Valley Electric Cooperative (1990)
 - Public Service Colorado (1990)
 - Licking Rural Electrification acquisition of National Oil and Gas (1998)
 - Flathead Electric Cooperative (1998--1999).

- Divestitures--Finance, regulatory, pricing and tax analysis for asset and/or stock divestitures on behalf of:
 - Bossier Electric Cooperative (1994 -1995)
 - Central Iowa Power Cooperative (1998)
 - Halifax Electric Membership Cooperative (1998)
 - Eastern Illini Electric Cooperative (1999)
 - Northeast Missouri Rural Telephone Company (2000)

- Restructurings--Assisted organizations in the conversion from for profit to cooperative or vice versa.
 - Voluntary Hospital Association (VHA) (1986-1991)
 - Catholic Health Alliance (1990)
 - LTV (1990)
 - Yellow Cab Company (1990)
 - Network Associates (1995)
 - CU Cooperative Systems (1995)
 - DeKalb Telephone Cooperative (1999)
 - Licking Rural Electric Cooperative (1999)
 - New World Energy (2000)
 - The Energy Cooperative (2000)

- Recapitalizations
 - Assisted numerous organizations in converting from for-profit companies to cooperatives
 - Assisted cooperatives in conversions from exempt to taxable and vice versa
 - Assisted cooperatives in recapitalizing debt/equity to achieve market and finance goals
 - Assisting Generation and Transmission and Distribution cooperatives in recapitalizing their "rotatable" equity into permanent equity

- Service Expansion--Assisted rural electric and telephone cooperatives in expanding their services

- Other Services While Maintaining Tax Exempt Status
- Other Services Through Taxable Subsidiary Operations
- Complimentary Services Through New Cooperatives

Restructurings, Insolvencies and Workouts

- Palm Beach County Utilities Corporation--Assisted PBCUC in its Chapter 11 proceeding. (1990)
- Cajun Electric Power Cooperative--Assisted Cajun as creditor in the Chapter 11 proceeding of its member, Washington-St. Tammany, and assisted Cajun in its own debt restructuring (1988-1990)
- Sunflower Electric Cooperative, Inc.--Assisted in analyzing and formatting financial data for purposes of cash management and reorganizing debt under an informal restructuring. (1986)
- New Hampshire Electric Cooperative--Assisted the cooperative in its debt restructuring and financial workout. (1989-1991)
- Public Service Company of New Hampshire--Assisted the State of New Hampshire in evaluating certain issues of Public Service's business environment and reorganization options in this Chapter 11 proceeding. (1988)
- Cajun Electric Power Cooperative--Assisted Cajun as debtor in possession and assisting the Court Appointed Trustee of Cajun in its Chapter 11 proceeding (1994-2001)
- Big Rivers Electric Corporation--Assisted Big Rivers in exploring its financial options and devising and executing a plan to address its options; providing finance and tax assistance to Big Rivers as debtor in possession (1994--1999)
- Central Iowa Power Cooperative-- Assisted CIPCO in exploring its financial options including the sale or lease of its assets (1997--)
- Kansas Electric Power Cooperative-- Assisted KEPCO in exploring its financial options including the sale or lease of its assets and restructuring its debt. (1997--)
- Saluda River Electric Cooperative-- Assisted SREC in exploring its financial options including the sale or lease of its assets and restructuring its debt. (1997-- 1998)
- Brazos Power Cooperative-- Assisted Brazos in exploring its financial options including the sale or lease of its assets and power swap arrangements. (1997--1998)
- Denton County Electric Cooperative (CoServ)-- Assisted CoServ as debtor in possession in its Chapter 11 proceeding (2002--2003)

Tax, Rate, Accounting and Financial Issues

- Brazos Electric Power Cooperative, Inc. and South Texas Electric Cooperative, Inc.-Proceeding to consider protocols to implement a nodal market in the Electric Reliability Council of Texas pursuant to Subst. R. 25.501. (2005)
- Flathead Electric—Assisted in performing the financial, economic, and regulatory due diligence of a proposed long-term source of power. (2001)
- South County Gas--Developed accounting procedures to account for transactions between a regulated utility and its unregulated affiliates. (1989)
- Pitt & Green--Assisting the cooperative in developing a comprehensive finance/equity management and rotation plan (1997 - 1999)
- Cajun Electric Power Cooperative--Performed detailed analysis of the tax law regarding patronage dividends and assisted in developing an integrated finance/equity management plan. (1983-2001)
- Agrico Chemical Company--Performed detailed analysis of certain tax issues of an integrated gas producer/distributor in a rate intervention. (1982-1983)
- City of Vero Beach--Analyzed the City's utility tax structure in the context of the objectives of utility taxes in general and related those findings to the methods other Florida municipalities used in establishing utility taxes. (1981)
- Department of Energy--Analyzed the tax issues related to the methods for calculating return on equity and cost of capital that will enable the Division of Coal Regulation to use these measures for determining the economic impact of coal conversion on firms applying for exemption to the Power Plant and Industrial Fuel Use Act of 1978 (PIFUA). (1979-1980)
- Other accounting, tax, rate, and financial issues have been addressed by Mr. Smith for:
 - Palm Beach County Utilities Corporation (1986-1989)
 - Long Island Lighting Company (1984-1989)
 - Indianapolis Power & Light Company (1984)
 - Trans Louisiana Gas Company (1982-1989)
 - Williams Natural Gas Company (1982-1989)
 - Edison Sault Electric Company (1985)
 - Faustina Pipeline (1982-1985)
 - Louisiana Interstate Gas (1982-1988)
 - Louisiana Natural Gas (1982-1988)
 - Ontario Natural Gas Association (1985)
 - Mountain Fuel Supply Company (1984)
 - Big Rivers Electric Cooperative (1983-present)
 - Empire Electric Association (1985)
 - Western Fuels Association (1981-1994)
 - Midwest Energy (1984-1986)

- San Miguel Electric Cooperative (1984-1988)
 - Mississippi River Transportation Company (1986-1987)
 - Cajun Electric Power Cooperative (1980-present)
 - Brazos Electric Power Cooperative (1980-1998)
 - Allegheny Electric Power Cooperative (1980-1998)
 - Plains Electric Generation and Transmission Cooperative (1981-1998)
 - Greeley Gas Company (1991).
- Margin Stabilization Plans--Assisted in the establishment of margin stabilization plans and, in some cases, the securing of a ruling from the IRS, for:
 - Dairyland Power Corporation (1982)
 - Allegheny Electric Corporation (1990)
 - Tri State Generation & Transmission Association (1988)
 - Brazos Electric (1998).

Depreciation and Cost of Removal

- Lea County Electric Cooperative--Analyzed the effect of removal costs through traditional plant and depreciation accounting and recommended a method to correct existing account balances and accrue future costs of removal as a current cost of service. (1981-1982)
- Plains Electric Generation & Transmission Cooperative, Inc.--Analyzed financial and accounting implications of adopting units of production vs. straight line remaining life given life extension assumptions. (1988-1989)
- Empire Electric Association--Testified that the cost of removal for contributed property should be borne by the party contributing and using the property. (1985-1986)
- NOVA, An Alberta Corporation--Analyzed various methods of depreciation including those based upon reserve life, remaining physical life, license life, contract life, and equal life groups for this gas transmission company. (1981-present)
- CSX--Assisted this railroad to establish historical plant records for its assets. (1983)
- Cajun Electric Power Cooperative--Assisted in analyzing the tax, financial, and accounting implications of adopting units of production depreciation. (1988)
- Powder River Energy Corporation--Assisted in analyzing the tax, financial, and accounting implications of addressing large amounts of contributions in aid of construction and contributed plant and submitted testimony on the issues. (2001)

Retirement Unit Studies

Performed retirement unit studies for generation and transmission properties for:

- Cajun Electric Power Cooperative (1983)
- Big Rivers Electric Cooperative (1983-1984)
- Tri-State Generation and Transmission (1981-1983)
- San Miguel Electric Cooperative, Inc.
- Plains Electric Generation and Transmission Cooperative, Inc. (1981-1982)

Nuclear Decommissioning Trusts

Analyzed finance and tax issues regarding nuclear decommissioning (1986-present) for:

- Financial Institutions
- Allegheny Electric Cooperative
- Cajun Electric Power Cooperative (IRS ruling request)
- New Hampshire Electric Cooperative
- Central Iowa Power Cooperative
- Kansas Electric Power Cooperative
- North Carolina Electric Membership Corporation
- Saluda Rural Electric Corporation
- Oglethorpe Power Corporation

Management Audits

- New Jersey Board of Public Utilities--Directed the tax-related aspects of a management audit of New Jersey Natural Gas. Performed the financial aspects and directed the tax aspects of a management audit of Jersey Central Power and Light. (1985-1986)
- California Public Utilities Commission--Directed the tax-related aspects of a management audit of San Diego Gas & Electric Company. (1983)
- Pennsylvania Public Utility Commission--Directed the tax-related aspects of a management audit of Pennsylvania Power & Light. (1986-1987)
- North Carolina Utilities Commission--Directed the tax-related aspects of a management audit of the Piedmont Natural Gas Company. (1980)

Participation Agreements

- South Mississippi Electric Power Association--Analyzed tax aspects and certain rate aspects of SMEPA's ownership agreement. (1983)
- Old Dominion Electric Cooperative--Directed the review, analysis, and negotiations (which resulted in a substantial price adjustment) of Old Dominion's purchase of an undivided interest in a nuclear power station. (1982-1983)

- Florida Municipal Power Agency--Assisted the agency in evaluating the Federal income tax arising from its participation in a generating facility being constructed by an investor-owned utility. (1981-1982)
- Analyzed tax and/or rate aspects of participation and ownership agreements for the following rural electric cooperative corporations:
 - Brazos (1981-present)
 - Northern Michigan (1981)
 - Wolverine (1981)
 - Allegheny (1981-1991)
 - Cajun (1981-present)
 - Pacific Northwest Generating (1982)
 - Tri-State G&T (1981-1991)
 - North Carolina EMC (1981)
 - Kansas Electric Power Cooperative (1983)

Tax Legislative Initiative

- Assisted in drafting and advancing provisions to address the tax and competitive issues facing rural electric cooperatives in utility industry restructuring and appeared before tax writing committees and U.S. Treasury department in "scoring" the provisions, e.g.
 - Nuclear provisions for cooperatives contained in H.R. 4520, the American Jobs Creation Act of 2004;
 - Provisions regarding contributions in aid of construction for rural electric cooperatives;
 - Several remedial provisions regarding the tax issues arising from the prepayment of RUS loans; and
 - numerous other provisions.
- Appeared before Virginia Task Force on State and Local Taxation of Electrical Utilities

Other Utility and Energy-Related Projects

- Tax Services to G&Ts--Assisted over half the nation's G&T cooperatives in tax planning and compliance matters, such as reorganizations, review of participation agreements, review of tax exempt status, analysis of proposed lease transactions, establishment of equity management plans, establishment of tax accounting systems, etc. (1979-present)
- Corporate Strategic Planning and Reorganization--Assisted several G&T systems in evaluating corporate planning/ restructuring options identifying the extent of its financial problems and in evaluating debt restructuring options. (1980-present)

- Ad Hoc National Tax Study Group of Generation & Transmission (G&T) Cooperative Managers--Performed a detailed analysis of the tax and operational issues related to the exempt or non-exempt Federal income tax status of G&T cooperatives. A majority of the nation's G&T cooperatives were involved in this project through individual case studies, participation in the generic portion of the study, or participation in fact-finding meetings. (1980-1981)
- Water Cooperatives and Companies--Assisted developers, investors, and water companies in evaluating and addressing tax law issues contributions in aid of construction. Assisted in refinancing of debt, privatization of systems, and acquisition of water companies and cooperatives by other utilities and investors.

Prior experience of Mr. Smith includes twenty-one years with "big 5" accounting firms where he has served at the Partner/Principal level. He was associated with both national tax and national utilities practice offices with both firms. Before entering public accounting, Mr. Smith was a tax law specialist in the National office of the Internal Revenue Service under the Assistant Commissioner, Technical, where he prepared and reviewed authoritative tax material for publication in the Internal Revenue Bulletin.

Mr. Smith is a frequent speaker concerning tax, finance, and operational issues related to rural electric cooperatives and utilities in general and has frequently spoken at tax conferences for both tax professionals and laymen, including a two-day seminar, which he produced. He is the author of The Federal Income Taxation of Rural Electric Cooperatives and several articles concerning tax issues related to utilities. In addition, he has lectured on the tax aspects of depreciation before managers and regulators of public utilities at the George Washington University and is the author of Depreciation, Salvage, and Cost of Removal -- A Critical Analysis. His articles have been published in *The Cooperative Accountant* and *Public Utilities Fortnightly*.

Jim is active in community activities. He is serving or has served in the following capacities:

- Adjutant, American Legion Post 157, Madison, VA
- Rappahannock Rapidan Medical Reserve Corps Volunteer;
- Boy Scouts of America -- Commissioner, Cubmaster, Scoutmaster, Adult
- Trainer, and Chairman, Patawomeck District; Co-Chair-Chain Bridge District Eagle Review Board; Chair, Project Sales Committee; Chair, Friends of Scouting, Community Campaign, Executive Board, National Capital Area Council, and Commissioner for Madison County;
- Northern Virginia Lacrosse League -- Organizer & Coach;
- Missing Children of Greater Washington and Adam Walsh Child Resource Center -- Board Member;
- Army & Navy Club of Washington, DC -- member
- Military Order of the Purple Heart

Also, Jim served in the USN/USMC 1967—1970, with Honorable Discharge. His decorations included Bronze Star Medals with Combat "V", Purple Heart, the American Spirit of Honor Medal presented by the Citizens Committee for the Army, Navy and Air

Force and various other personal and unit awards, citations and decorations including the Congressional Veteran Commendation in 2010.

Jim and his wife, Kimberly, live on a small farm in Madison County in the foothills of the Blue Ridge Mountains, north of Charlottesville, Virginia.

Testimony of Mr. Smith Before Regulatory Commissions, et al

Company	Jurisdiction	Order No.	Year
Big Rivers Electric Corp.	Kentucky	7917	1983
Empire Electric Association, Inc.	Colorado	6386	1984
Louisiana Public Service Commission	Federal Energy Regulatory Commission	ER#-85-646-005 & ER#-85-647-003	1986
New Orleans Public Service, Inc.	New Orleans City Council	<i>Preferred Stock Recapitalization</i>	1989
North Carolina Electric Membership Corporation & Saluda River Electric Cooperative	North Carolina	<i>Fourth Proceeding in Arbitration Duke Power</i>	1991
Cajun Electric Power Cooperative	District Court for the Middle District of Louisiana	Civil Action No. 94-2763-b2 Chapter 11 Case No. 94-11474	1995--1997
Virginia, Maryland and Delaware Electric Cooperative Association	Virginia Task Force on State and Local Taxation of Electrical Utilities	Senate Joint Resolution 259	1997
Big Rivers Electric Corporation	Public Service Commission of Kentucky	PSC Case No. 97-204	1997
Big Rivers Electric Corporation	Public Service Commission of Kentucky	<i>In the Matter of Big Rivers Electric Corporation's Request for Approval of Transaction Documents and 1988 Amendments to Station Two Contracts</i> Case No. 98-267	1998

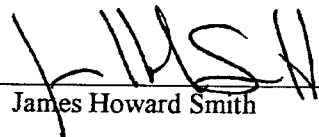
Deseret Generation & Transmission Cooperative	Federal Energy Regulatory Commission	<i>Cities of Anaheim and Riverside, California v. Desert Generation and Transmission Cooperative, Inc.</i> Docket No. EL97-57-001	1999
Powder River Energy Corporation	Public Service Commission of Wyoming	Docket No.10014-CR-01-53	2001
Pegasus Satellite TV, et al	Central District Of California (Western Division - Los Angeles)	<i>National Rural Telecommunications Cooperative, Inc, V. DirecTV, Inc., Hughes Communications Galaxy, Inc. and DOES 1-10</i>	2002
Brazos Electric Power Cooperative, Inc. and South Texas Electric Cooperative, Inc	Public Utility Commission Of Texas	Docket No. 31540 <i>Proceeding to Consider Protocols to Implement a Nodal Market in the Electric Reliability Council of Texas Pursuant to Subst.R.25.501</i>	2005
Matanuska Telephone Association, Inc. and Copper Valley Telephone Cooperative, Inc.	The Regulatory Commission Of Alaska	<i>In the Matter of the Consideration of the Access Charge Revenue Requirement of Matanuska Telephone Association, Inc. (U-08-87) and Copper Valley Telephone Cooperative, Inc. (U-08-113)</i>	2009

Denton County Electric Cooperative, Inc. d/b/a CoServ Electric	16th Judicial District Court, Denton County, Texas	<i>Denton County Electric Cooperative, Inc. d/v/a CoServ Electric v. Mark Glover</i> , in the 16th Judicial District Court, Denton County, Texas, Cause No. 2009-10087-16	2009
Denton County Electric Cooperative, Inc. d/b/a CoServ Electric	U.S. District Court for the Eastern District of Texas, Sherman Division	<i>Janice Brady and Duncan Duval v. Denton County Electric Cooperative, Inc. d/b/a CoServ Electric</i> , Cause No. 4:09-cv-130; <i>Paul Confer v. Denton County Electric Cooperative, Inc. d/b/a CoServ Electric</i> , Cause No. 4:09-cv-131	2009
Mid-Kansas Electric Company, LLC	Kansas Corporation Commission	<i>Application for Revised Rates, Tariffs, and Rate Design Changes of Mid-Kansas Electric Company, LLC</i> Docket No. 09-MKEE-969-RTS	2009

VERIFICATION

STATE OF VIRGINIA)
) ss:
COUNTY OF MADISON)

James Howard Smith, being first duly sworn, deposes and says that he is James Howard Smith referred to in the foregoing document entitled "Rebuttal Testimony of James Howard Smith" before the State Corporation Commission of the State of Kansas and that the statements therein were prepared by him or under his direction and are true and correct to the best of his information, knowledge and belief.



James Howard Smith

SUBSCRIBED AND SWORN to before me this 8 day of May, 2012.



Notary Public

My Appointment Expires: 2-28-13

