

GENERAL WATERWORKS MANAGEMENT AND SERVICE COMPANY

December 15, 1986

Mr. Harvey Hubbs, Secretary  
Missouri Public Service Commission  
100 East Capitol Street  
Jefferson City, MO 65102

RE: Capital City Water Company  
Company Response to Data Request Incorporated in  
Case No. AO-87-48

Dear Mr. Hubbs:

Enclosed herewith is the Company's response to the data requests incorporated in Case No. AO-87-48. The Company's response consists of several exhibits and a narrative of the data contained on the exhibits.

Item No. 4 in the Order pertaining to Workpapers supporting the amount of excess deferred tax reserves attributable to the turnaround of tax/book timing differences cannot be answered at this time for the following reasons.

The Company does not maintain a ledger of utility plant in service by vintage year by asset account but rather maintains a ledger which accumulates total utility plant by asset account. In order for the Company to comply with Item No. 4 of the Order, it will be necessary for the Company to retrieve plant additions and retirements by year for the period 1970 through 1985, a significant undertaking. In addition to the above, our accounting department is in the process of compiling year-end data in order to close the Company's books at December 31, 1986. It is anticipated that the Company will respond to Item No. 4 when the Company submits its workpapers for year-end 1986 data by February 28, 1987 as requested in the order.

Correspondence pertaining to the data submitted herewith should be addressed to the undersigned.

Yours truly,

*Gerald M. Hill*

Gerald M. Hill  
Director of Rates

GMH/df  
Enclosures

**FILED**

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**PUBLIC SERVICE COMMISSION**

## CAPITAL CITY WATER COMPANY

### Explanation of Data Submitted to Commission

1. The elements of rate base and the operating income statement were obtained from the Missouri PSC report for 1985.
2. One adjustment was made to the income statement. Real estate taxes for 1985 were not recorded until 1986. The income statement was restated to reflect the 1985 level of real estate taxes.
3. Based on the Commission's decision in Case No. WP-83-165, the Company developed a rate base of \$4,346,358. The rate base is shown on Exhibit No. 2.
4. Based on the Commission's decision in Case No. WP-83-165, the Company used an overall rate of return of 12.32% consisting of 52.60% debt with a cost of 10.62% and 47.4% equity with a cost of 14.2%.
5. Based on the 1985 financial statement adjusted for real estate taxes and based upon a rate of return of 12.32% and a rate base of \$4,346,388 and the tax rate of 46%, the Company would have to increase its operating revenue by \$66,562. These results are shown on Exhibit No. 1.
6. Exhibit No. 1, consisting of three pages, shows the operating income statement per books at 12/31/85. Page 1 shows the operating income statement for calendar year 1985. Page 2 shows the calculation of federal and state income taxes. An effective state tax rate of 2.836% was used. The multiple surtax rate of 25.75% for the first \$100,000 of federal taxable income was not used in our calculations since the Tax Reform Act of 1984 eliminated the surtax for corporations whose taxable income exceeds \$1,000,000. This applies to Capital City Water Company since the consolidated return of which Capital City is a member exceeds that amount. Page 3 shows the calculation of interest expense and deferred tax expense.
7. Exhibit No. 3, consisting of three pages, shows the operating income statement per books at 12/31/85 similar to Exhibit No. 1. The income statement shows that there would be an increase of \$17,176 in the Company's revenue requirement as a result of the application of the new tax rates incorporated in the Tax Reform Act of 1986. Page 2 of Exhibit No. 3 shows the calculation of state and federal income taxes. Federal income taxes were computed at a rate of 40% for all taxable income. Lines 2 and 3 show additional items that become taxable income as a result of TRA 86.

Line 2 of Page 2 shows taxable CIAC of \$4,692. This amount represents the present value discount on \$35,586 of CIAC which must be grossed up for federal and state taxes. The \$4,692 was computed on Exhibit No. 4 and represents the benefit that must be passed back to the contributor of CIAC. This benefit represents the present value of a stream of depreciation expense arising from depreciable CIAC of \$35,586. A contractor who supplies \$35,586 of CIAC would have to pay \$66,617 (a gross up of 1.72) in order to supply the taxes related to \$35,586. However, the Commission has ordered the Company to reduce the gross up amount by a discount using the Company's last rate of return and applying that discount to the benefit of tax depreciation available to the utility. This amounts to \$4,692. Since the Company will not be made whole by the contractor by \$4,692, that amount becomes taxable income to the utility.

8. Exhibit No. 4 shows the calculation of the present value of the tax depreciation benefit on \$35,586 of CIAC. The discount benefit of \$4,692 would be deducted from the gross up of \$35,586 of CIAC as required by the Commission.

9. Exhibit No. 5, consisting of three pages, shows the operating income statement per books at 12/31/85 similar to Exhibit No. 1. This exhibit shows that revenue must be increased by \$109,876 for proforma expense adjustments of \$92,460. These adjustments consist of:

1. 1/1/86 pay increase	\$47,501
2. Health care increase	14,562
3. General insurance increase	<u>30,397</u>
	<u>\$92,460</u>

10. The Tax Reform Act of 1986 has the following impact upon the water utility.

- A) CIAC are considered taxable income for tax purposes. This will increase the Company's Cost of Service for the discount applied to the CIAC gross up.
- B) ITC is repealed. This lowers the Company's cash flow.
- C) Deferred taxes are reduced due to lower tax rates and higher depreciation lives. This lowers the Company's cash flow.
- D) AFUDC must be capitalized instead of expensed. This will increase income tax expense.
- E) Overheads capitalized per books must be capitalized for tax purposes also.
- F) Unbilled revenue is now taxable income.

G) State income tax expense will be greater due to lower federal income tax expense.

In summary, based upon current tax rates, the Company would have to raise its revenue requirement by \$66,562 in order to achieve a rate of return of 12.32% (Exhibit No. 1). Based upon TRA 86 tax rates, the Company would have to raise its revenue requirement by \$17,176 (Exhibit No. 3). Based upon increases in three expense categories the Company would have to increase its revenue requirement by \$109,876 (Exhibit No. 5).

CAPITAL CITY WATER COMPANY  
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STATEMENT OF OPERATING INCOME PER BOOKS  
-----  
TEST YEAR- DECEMBER 31, 1985  
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LINE #	DESCRIPTION	PER BOOKS 12/31/85	TEST YEAR ADJUSTMENT	ADJUSTED TEST YEAR	UNDER PROPOSED RATES ADJUSTMENTS	PRO FORMA
		(1)	(2)	(3)	(4)	(5)
1.	OPERATING REVENUES	2,583,086		2,583,086	66,562	2,649,648
	OPERATING EXPENSES:					
2.	OPERATION & MAINTENANCE	1,636,227	0	1,636,227		1,636,227
3.	DEPRECIATION	107,095		107,095		107,095
4.	TAXES OTHER THAN INCOME	75,997	40,299	116,296		116,296
5.	TOTAL OPERATING EXPENSES EXCLUDING INCOME TAXES	1,819,319	40,299	1,859,618	0	1,859,618
6.	OPERATING INCOME BEFORE INCOME TAXES	763,767	(40,299)	723,468	66,562	790,030
	INCOME TAXES:					
7.	CURRENT INCOME TAXES	204,178	(14,180)	189,998	31,638	221,636
8.	DEFERRED INCOME TAXES	37,235	1,206	38,441		38,441
9.	ITC AMORTIZATION	(5,635)	0	(5,635)	0	(5,635)
10.	TOTAL INCOME TAXES	235,778	(12,974)	222,804	31,638	254,442
10.	NET OPERATING INCOME	527,969	(27,325)	500,644	34,808	535,471
11.	RATE BASE			4,346,358		4,346,358
12.	RATE OF RETURN			11.52%		12.32%

CAPITAL CITY WATER COMPANY  
-----  
COMPUTATION OF STATE AND FEDERAL INCOME TAXES  
-----  
AT PRESENT RATES  
-----  
TWELVE MONTHS ENDED DECEMBER 31, 1985  
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LINE NO. -----		PRO FORMA	
		AT EXISTING RATES -----	AT PROPOSED RATES -----
1.	OPERATING INCOME BEFORE INCOME TAXES	723,468	790,030
2.	LESS: TAX DEDUCTIONS: -----		
3.	INTEREST EXPENSE (A)	242,793	242,793
4.	EXCESS TAX OVER BOOK	80,944	80,944
5.	TOTAL TAX DEDUCTIONS	323,737	323,737
6.	TAXABLE INCOME- STATE	399,731	466,293
8.	ST. INC. TAX @ 2.836% ***	11,336	13,224
9.	FEDERAL TAXABLE INCOME	388,395	453,069
10.	FD. INC. TAX-FIRST 100,000 @ 25.75%	0	0
11.	FD. INC. TAX-REMAINING TX. INC. @ 46%	178,662	208,412
12.	LESS: INVESTMENT TAX CREDIT	(5,635)	(5,635)
13.	TOTAL FEDERAL INCOME TAX	173,027	202,777
14.	TOTAL FEDERAL & STATE TAXES	184,363	216,001
		*****	*****

\*\*\* EFFECTIVE STATE TAX RATE

CAPITAL CITY WATER COMPANY  
-----  
COMPUTATION OF STATE AND FEDERAL INCOME TAXES  
-----  
INTEREST AND DEFERRED TAXES  
-----  
TWELVE MONTHS ENDED DECEMBER 31, 1985  
-----

LINE # -----		AMOUNT -----
1.	RATE BASE	\$ 4,346,358
2.	RATIO OF DEBT TO CAPITALIZATION	X 52.60%
3.	DEBT PORTION OF TOTAL CAPITALIZATION	\$ 2,286,184
4.	INTEREST RATE	X 10.62%
5.	TOTAL INTEREST	\$ 242,793 *****
6.	TAX DEPRECIATION EXPENSE	\$ 188,041
7.	BOOK DEPRECIATION EXPENSE	- 107,095
8.	EXCESS TAX OVER BOOK	\$ 80,946
9.	FEDERAL TAX RATE	X 47.49 %
10.	DEFERRED FEDERAL INCOME TAX	\$ 38,441 *****

CAPITAL CITY WATER COMPANY  
RATE BASE  
TWELVE MONTHS ENDED 12/31/85  
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EXHIBIT NO. 2

LINE #	DESCRIPTION	AMOUNT (A)
-----	-----	-----
1.	UTILITY PLANT	\$6,746,995
2.	PROVISION FOR DEPRECIATION	(\$1,556,871)
3.	ADVANCES FOR CONSTRUCTION	(\$446,633)
4.	CONTR. IN AID OF CONSTRUCTION	(\$426,290)
5.	MATERIAL AND SUPPLIES	\$86,462
6.	PREPAID EXPENSES	\$4,748
7.	DEFERRED EXPENSES	\$89,025
8.	DEFERRED TAXES	(\$153,998)
9.	CASH WORKING CAPITAL (B)	\$3,100
		-----
10.	RATE BASE	\$4,346,358
		=====

NOTE (A): AMOUNTS PER 1985 COMMISSION REPORT  
(B) PER LAST ORDER



CAPITAL CITY WATER COMPANY  
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STATEMENT OF OPERATING INCOME PER BOOKS  
-----  
TEST YEAR- DECEMBER 31, 1985  
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LINE #	DESCRIPTION	PER BOOKS 12/31/85	TEST YEAR ADJUSTMENT	ADJUSTED TEST YEAR	UNDER PROPOSED RATES ADJUSTMENTS	RATES PRO FORMA
		(1)	(2)	(3)	(4)	(5)
1.	OPERATING REVENUES	2,583,086		2,583,086	17,176	2,600,262
	OPERATING EXPENSES:					
2.	OPERATION & MAINTENANCE	1,636,227	0	1,636,227		1,636,227
3.	DEPRECIATION	107,095		107,095		107,095
4.	TAXES OTHER THAN INCOME	75,997	40,299	116,296		116,296
5.	TOTAL OPERATING EXPENSES EXCLUDING INCOME TAXES	1,819,319	40,299	1,859,618	0	1,859,618
6.	OPERATING INCOME BEFORE INCOME TAXES	763,767	(40,299)	723,468	17,176	740,644
	INCOME TAXES:					
7.	CURRENT INCOME TAXES	204,178	(34,609)	169,569	7,193	176,762
8.	DEFERRED INCOME TAXES	37,235	(3,215)	34,020		34,020
9.	ITC AMORTIZATION	(5,635)	0	(5,635)	0	(5,635)
10.	TOTAL INCOME TAXES	235,778	(37,824)	197,954	7,193	205,147
10.	NET OPERATING INCOME	527,989	(2,475)	525,514	9,957	535,471
11.	RATE BASE			4,346,358		4,346,358
12.	RATE OF RETURN			12.09%		12.32%

## CAPITAL CITY WATER COMPANY

EXHIBIT NO. 3

PAGE 2 OF 3

## COMPUTATION OF STATE AND FEDERAL INCOME TAXES

AT PRESENT RATES

TWELVE MONTHS ENDED DECEMBER 31, 1985

LINE NO.		PRO FORMA	
		AT EXISTING RATES	AT PROPOSED RATES
1.	OPERATING INCOME BEFORE INCOME TAXES	723,468	740,644
2.	TAXABLE CIAC-COMPANY SHARE (A)	4,692	4,692
3.	AFUDC	489	489
4.	TOTAL TAXABLE INCOME	728,649	745,825
	LESS: TAX DEDUCTIONS:		
5.	INTEREST EXPENSE (A)	242,793	242,793
6.	EXCESS TAX OVER BOOK	80,944	80,944
7.	TOTAL TAX DEDUCTIONS	323,737	323,737
8.	TAXABLE INCOME- STATE	404,912	422,089
9.	ST. INC. TAX @ 3.13% ***	12,674	13,211
10.	FEDERAL TAXABLE INCOME	392,238	408,877
11.	FD. INC. TAX-FIRST 100,000 @ 25.75%	0	0
12.	FD. INC. TAX-REMAINING TX. INC. @ 40%	156,895	163,551
13.	LESS: INVESTMENT TAX CREDIT	(5,635)	(5,635)
14.	TOTAL FEDERAL INCOME TAX	151,260	157,916
15.	TOTAL FEDERAL & STATE TAXES	163,934	171,127

\*\*\* EFFECTIVE STATE TAX RATE

(A) ON \$35,586 OF CIAC, THE GROSS-UP WOULD BE \$61,208, WHICH WOULD BE REDUCED BY THE PRESENT VALUE DISCOUNT OF \$13,589.

CAPITAL CITY WATER COMPANY  
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COMPUTATION OF STATE AND FEDERAL INCOME TAXES  
-----  
INTEREST AND DEFERRED TAXES  
-----  
TWELVE MONTHS ENDED DECEMBER 31, 1985  
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LINE # ----	AMOUNT -----
1. RATE BASE	\$ 4,346,358
2. RATIO OF DEBT TO CAPITALIZATION	X 52.60%
3. DEBT PORTION OF TOTAL CAPITALIZATION	\$ 2,286,184
4. INTEREST RATE	X 10.62%
5. TOTAL INTEREST	\$ 242,793 *****
6. TAX DEPRECIATION EXPENSE	\$ 188,041
7. BOOK DEPRECIATION EXPENSE	- 107,095
8. EXCESS TAX OVER BOOK	\$ 80,946
9. FEDERAL TAX RATE	X 42.028 %
10. DEFERRED FEDERAL INCOME TAX	\$ 34,020 *****

## EXHIBIT NO.4

## CAPITAL CITY WATER COMPANY

## CALCULATION OF PRESENT VALUE

ASSET COST        \$35,586.00

YEAR	DEPR RATE	DEPRECIATION	TAX SAVINGS	PRESENT VALUE
1	3.75%	1,334	534	475
2	7.22%	2,569	873	692
3	6.68%	2,376	808	570
4	6.18%	2,199	747	470
5	5.72%	2,034	691	387
6	5.29%	1,881	640	319
7	4.89%	1,740	592	262
8	4.32%	1,610	547	216
9	4.46%	1,587	540	190
10	4.46%	1,587	540	169
11	4.46%	1,587	540	150
12	4.46%	1,587	540	134
13	4.46%	1,587	540	119
14	4.46%	1,587	540	106
15	4.46%	1,587	540	94
16	4.46%	1,587	540	84
17	4.46%	1,587	540	75
18	4.46%	1,587	540	67
19	4.46%	1,587	540	59
20	4.46%	1,587	540	53
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		34,793	11,910	\$4,692
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CAPITAL CITY WATER COMPANY  
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STATEMENT OF OPERATING INCOME PER BOOKS  
-----  
TEST YEAR- DECEMBER 31, 1985  
-----

LINE #	DESCRIPTION	PER BOOKS 12/31/85	TEST YEAR ADJUSTMENT	ADJUSTED TEST YEAR	UNDER PROPOSED RATES ADJUSTMENTS	PRO FORMA
		(1)	(2)	(3)	(4)	(5)
1.	OPERATING REVENUES	2,583,086		2,583,086	109,876	2,692,962
	OPERATING EXPENSES:					
2.	OPERATION & MAINTENANCE	1,636,227	92,460	1,728,687		1,728,687
3.	DEPRECIATION	107,095		107,095		107,095
4.	TAXES OTHER THAN INCOME	75,997	40,299	116,296		116,296
5.	TOTAL OPERATING EXPENSES EXCLUDING INCOME TAXES	1,819,319	132,759	1,952,078	0	1,952,078
6.	OPERATING INCOME BEFORE INCOME TAXES	763,767	(132,759)	631,008	109,876	740,884
	INCOME TAXES:					
7.	CURRENT INCOME TAXES	204,178	(73,329)	130,849	46,014	176,862
8.	DEFERRED INCOME TAXES	37,235	(3,215)	34,020		34,020
9.	ITC AMORTIZATION	(5,635)	0	(5,635)	0	(5,635)
10.	TOTAL INCOME TAXES	235,778	(76,544)	159,234	46,014	205,247
10.	NET OPERATING INCOME	527,989	(56,215)	471,774	63,697	535,471
11.	RATE BASE			4,346,358		4,346,358
12.	RATE OF RETURN			10.85%		12.32%

CAPITAL CITY WATER COMPANY  
-----  
COMPUTATION OF STATE AND FEDERAL INCOME TAXES  
-----  
AT PRESENT RATES  
-----  
TWELVE MONTHS ENDED DECEMBER 31, 1985  
-----

LINE NO.		PRO FORMA	
		AT EXISTING RATES	AT PROPOSED RATES
1.	OPERATING INCOME BEFORE INCOME TAXES	631,008	740,884
2.	TAXABLE CIAC-COMPANY SHARE (A)	4,592	4,692
3.	AFUDC	489	489
4.	TOTAL TAXABLE INCOME	636,189	746,065
	LESS: TAX DEDUCTIONS:		
5.	INTEREST EXPENSE (A)	242,793	242,793
6.	EXCESS TAX OVER BOOK	80,944	80,944
7.	TOTAL TAX DEDUCTIONS	323,737	323,737
8.	TAXABLE INCOME- STATE	312,452	422,328
9.	ST. INC. TAX @ 3.13% ***	9,780	13,219
10.	FEDERAL TAXABLE INCOME	302,672	409,109
11.	FD. INC. TAX-FIRST 100,000 @ 25.75%	0	0
12.	FD. INC. TAX-REMAINING TX. INC. @ 40%	121,069	163,644
13.	LESS: INVESTMENT TAX CREDIT	(5,635)	(5,635)
14.	TOTAL FEDERAL INCOME TAX	115,434	158,009
15.	TOTAL FEDERAL & STATE TAXES	125,214	171,227

\*\*\* EFFECTIVE STATE TAX RATE

(A) ON \$35,586 OF CIAC, THE GROSS-UP WOULD BE \$61,208, WHICH WOULD BE REDUCED BY THE PRESENT VALUE DISCOUNT OF \$13,589.

CAPITAL CITY WATER COMPANY  
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COMPUTATION OF STATE AND FEDERAL INCOME TAXES  
-----  
INTEREST AND DEFERRED TAXES  
-----  
TWELVE MONTHS ENDED DECEMBER 31, 1985  
-----

LINE # ----		AMOUNT -----
1.	RATE BASE	\$ 4,346,358
2.	RATIO OF DEBT TO CAPITALIZATION	X 52.60%
3.	DEBT PORTION OF TOTAL CAPITALIZATION	\$ 2,286,184
4.	INTEREST RATE	X 10.62%
5.	TOTAL INTEREST	\$ 242,793 =====
6.	TAX DEPRECIATION EXPENSE	\$ 188,041
7.	BOOK DEPRECIATION EXPENSE	- 107,095
8.	EXCESS TAX OVER BOOK	\$ 80,946
9.	FEDERAL TAX RATE	X 42.028 %
10.	DEFERRED FEDERAL INCOME TAX	\$ 34,020 =====