CONSOLIDATED WATER SERVICES, INC.

December 15, 1986

FILED
DEC 15 1986
PUBLIC SERVICE COMMISSION

State of Missouri
Public Service Commission
Truman Building-Room 530
301 E. High Street
Jefferson City, MO 65101

Attn: Mr. Harvey Hubbs
Secretary

Re: Case No. AO-87-48

Dear Mr. Hubbs:

Please find attached the filing of Missouri Cities Water Company in response to the Commission order in Case No. AO-87-48.

Sincerely,

John E. Eckart

John E. Eckart
Vice President

JEE/me

Attachment

cc: Mr. Lynn E. Bultman
Mr. Keith R. Cardey

RECEIVED
DEC 15 1986
MO. PUBLIC SERVICE COMM.

CONSOLIDATED WATER SERVICES, INC.
1000 N. Madison Avenue
P.O. Box 329
Greenwood, Indiana 46142
317-887-8653

MISSOURI CITIES WATER COMPANY

Summary Of
Operating Income For 1985
To Reflect
Changes From Tax Reform Act of 1986

Per Case No. AO-87-48

13.

INDEX

MISSOURI CITIES WATER COMPANY
Summary Of Operating Income For 1985
To Reflect Changes From Tax Reform Act Of 1986

		1985 @'86 Tax Rate	1985 @'87 Tax Rate	1985 @'88 Tax Rate
1.	Operating Revenue	$ 5,735,812	$ 5,735,812	$ 5,735,812
2.	Operating Revenue Deductions:			
3.	O & M	3,222,377	3,222,377	3,222,377
4.	Depreciation/Amort.	372,679	372,679	372,679
5.	Taxes-Other	275,832	275,832	275,832
6.	Income Taxes	496,619	472,439	404,598
7.	Total Deductions	4,367,507	4,343,327	4,275,486
8.	Operating Income	$ 1,368,305	$ 1,392,485	$ 1,460,326
9.	Rate Base	$14,200,535	$14,200,535	$14,200,535
10.	Actual Return on Rate Base (Line 8 ÷ Line 9)	9.64%	9.81%	10.28%
11.	Authorized Return on Rate Base	11.36%	11.36%	11.36%
12.	Required Operating Income (Line 9 x Line 11)	$ 1,613,181	$ 1,613,181	$ 1,613,181
13.	Revenue Excess (Deficiency) (Line 12 - Line 8 x Tax Factor)	$(477,263)	$(387,100)	$(243,804)

MISSOURI CITIES WATER COMPANY
Computation of State and Federal Incomes Taxes
Reflecting Tax Expense Per Tax Reform Act

	1986 Tax Law	1987 Tax Law	1988 Tax Law	Reference
Operating Revenue	$5,735,812	$5,735,812	$5,735,812	Note 6
Oper. Rev. Deductions				
Operating Expenses	3,222,377	3,222,377	3,222,377	
Depreciation For Taxes	649,349	649,349	649,349	
Taxes-Other	275,832	275,832	275,832	
Interest and Amortization	633,344	633,344	633,344	Note 1
Other	51,079	-0-	-0-	Note 2
Total	4,831,981	4,780,902	4,780,902	
Taxable Income	903,831	954,910	954,910	
Minus State Income Taxes	24,970	28,200	31,020	
Federal Taxable Income	878,861	926,710	923,890	
Federal Income Tax	404,275	370,700	314,125	
Sur-tax Exemption	20,250	-0-	-0-	
Federal Taxes	384,025	370,700	314,125	
State Income Taxes				
Net Taxable Income	903,831	954,910	954,910	
Less-Prov. For Fed. Inc. Tax	384,025	370,700	314,125	
ITC	20,369	20,369	20,369	Note 3
Missouri Taxable Income	499,437	563,841	620,416	
Prov. For State Tax @5%	24,970	28,200	31,020	

Summary:

	1986 Tax Law	1987 Tax Law	1988 Tax Law	Reference
State Income Taxes	24,970	28,200	31,020	
Federal Income Tax: Current	384,025	370,700	314,125	
Deferred	127,134	110,552	93,969	Note 4
Less: ITC	20,369	20,369	20,369	Note 3
Credit-CWC	19,141	16,644	14,147	Note 5
Total	$ 496,619	$ 472,439	$ 404,598	

Note 1 - Interest Expense

Interest is calculated by taking rate base times weighted cost of debt

Rate Base	$14,200,535
Weighted Cost of Debt	4.46%
Interest	$633,344

Note 2 - Other Deferred Federal Income Taxes

The following items were capitalized on the books but expensed in 1985 for both tax and rate purposes.

Payroll Taxes Capitalized	$10,589
Other Cost Capitalized	40,490
	$51,079

In 1987 and thereafter, the above will be capitalized for tax and rate purposes.

Note 3 - Investment Tax Credit

The Investment Tax Credit in 1985 was $1,222,048 x .08 = $97,764. ITC is not available in 1986 and thereafter.

The Company amortizes ITC over 40 years. On its books, it takes no amortization in the year of the addition.

1985 Amortization	$20,369
1986 Additions	2,444
Total	$22,813

Note 4 - Deferred Federal Income Taxes

Deferred Federal Income Taxes are associated with the difference between ACRS and straight line depreciation on property additions in 1981-1985.

	ACRS Dep.	SL Dep.	Difference	Tax Rate	Deferred Taxes
1985	$320,596	$44,217	$276,379	46%	$127,134
1986				46	127,234
1987				40	110,552
1988				34	93,969

The excess tax reserve from the reduction of corporate tax rates will be reduced, using the average rate method, over the remaining lives of the property.

Note 5 - Credit from CWC

Missouri Cities Water Company represents about 12% of Consolidated Water Company's (CWC) investment in its operating subsidiaries and the credit is equal to the Federal Tax Rate on the interest on outstanding debt of CWC.

	Tax Rate	Credit
1985	46%	$19,141
1986	46	19,141
1987	40	16,644
1988	34	14,147

Note 6 - Unbilled Revenues

Unbilled revenues has been considered as taxable income so there is no change.

Note 7 - Taxes on CIAC and Advances

The impact on cash flow, rate base and operating income was not considered in this study.

MISSOURI CITIES WATER COMPANY

Tax Conversion Factor

		Federal Tax Rate		
		46%	40%	34%
1.	Revenue	1,000	1,000	1,000
2.	Less State Tax:			
3.	Tax @5%	50	50	50
4.	Income Before Fed. Tax	950	950	950
5.	Fed. Inc. Tax			
6.	@46%	437		
7.	@40%		380	
8.	@34%			323
9.	Income After Taxes	513	570	627
10.	Revenue Conversion Factor (Line 1 ÷ Line 9)	1.949	1.754	1.595

MISSOURI CITIES WATER COMPANY

Rate Base

Utility Plant	$27,121,552
Completed Projects Classified As Work In Progress	725,278
Reserve For Depreciation	(4,525,474)
Net Plant	23,321,256
Customer Advances	336,741
CIAC	8,859,808
Net Investment	14,124,707
Materials & Supplies	87,422
Less:	
ITC Prior to 1971	11,594
Rate Base	$14,200,535

MISSOURI CITIES WATER COMPANY

Capitalization And Cost Of Capital
December 31, 1985

	Capitalization		Cost		Weighted
	Amount	Percent	Rate	Amount	Cost
COMMON EQUITY	$ 7,298,182	47.60%	12.9%	$ 941,465	6.14
PREFERRED STOCK:					
5 7/8% Cum. Pfd.	396,000		5.875	23,265	
7 1/4% Cum. Pfd.	85,200		7.250	6,177	
	481,200	3.14	6.12	29,442	.19
LONG-TERM DEBT:					
5.75% Series D	270,000		5.75	15,525	
5.125% Series E	474,000		5.125	24,293	
6.00% Series F	486,000		6.00	29,160	
7.50% Series G	830,000		7.50	62,250	
8.375% Series H	1,025,000		8.375	85,844	
11.00% Series I	550,000		11.00	60,500	
9.125% Series J	700,000		9.125	63,875	
16.625% Series K	2,000,000		16.625	332,500	
5.00% Serial Debenture	37,500		5.00	1,875	
Amort-Debt Expense				8,461	
Sub-total	6,372,500	41.57	10.74	684,283	4.46
SHORT-TERM DEBT:					
Bank Loans	-0-	-0-	-	-	-
DEFERRED INCOME TAXES:	414,983	2.71	-	-	-
Sub-total	14,566,865	95.02	11.36	1,655,190	10.79
DEFERRED ITC	764,242	4.98	11.36	86,818	.57
TOTAL	$15,331,107	100.00%	11.36%	$1,742,008	11.36%

COMMENTS OF
GENERAL TELEPHONE COMPANY OF THE MIDWEST
CASE NO. AO-87-48

In response to Case No. AO-87-48 relating to the Tax Reform Act of 1986, General Telephone Company of the Midwest submits the following data:

Request 1: Based on the tax law in effect in 1986, calculate a revenue requirement showing the operating results of unadjusted calendar year 1985 (or more recent unadjusted historical test year).

Response 1: As shown on Exhibit 1, page 2 of 3, in the column labeled "1986 Tax Law", the additional intrastate income tax expense because of the 1986 changes applied to operating results ending June 30, 1986 is $18,000. General has an intrastate revenue shortfall of $4.3 million and an estimated rate of return (assuming all other things constant) of 8.05%. The workpapers detailing the change in total income taxes are shown on pages 1 and 2 of Exhibit 1.

Request 2: Based on the new tax law using the tax rate(s) and other known tax changes applicable to calendar year 1987 taxable income (e.g. a 40% phased tax rate for 1987), calculate a revenue requirement showing the operating results of unadjusted calendar year 1985 (or more recent unadjusted historical test year).

Response 2: As shown on Exhibit 1, page 2 of 3, in the column labeled "1987 Tax Law", the additional intrastate income tax expense because of the 1987 changes applied to operating results ending June 30, 1986 is $24,000. General has an intrastate revenue shortfall of $3.9 million and an estimated rate of return (assuming all other things constant) of 8.04%. The workpapers detailing the change in total income taxes are shown on pages 1 and 2 of Exhibit 1.

Request 3: Based on the new tax law using the tax rate(s) and other known tax changes applicable to tax years subsequent to calendar year 1987, calculate a revenue requirement showing the operating results of unadjusted calendar year 1985 (or more recent unadjusted historical test year).

Response 3: As shown on Exhibit 1, page 2 of 3, in the column labeled "1988 Tax Law", the reduction in intrastate income tax expense because of the 1988 changes applied to operating results ending June 30, 1986 is $393,000. General continues to have a large intrastate revenue shortfall of $2.9 million and an estimated rate of return (assuming all other things constant) of 8.64%. The workpapers detailing the change in total income taxes are shown on pages 1 and 2 of Exhibit 1.

14.

COMMENTS OF
GENERAL TELEPHONE COMPANY OF THE MIDWEST
CASE NO. AO-87-48

Request 4: Provide the workpapers supporting the amount of excess deferred tax reserves attributable to the turnaround of tax/book timing differences at a tax rate lower than the rate(s) at which the reserve has thus far been established.

Response 4: These amounts are identified on Exhibit 1, page 1 of 3, as "Reversal of Deferred Taxes Associated with Rate Change". Also a schedule supporting the calculation is included as Exhibit 2.

Request 5: All deferred tax expense and reserve information shall be presented in a fashion which will allow a ready disaggregation between the types of tax/book timing differences which gave rise to the deferred tax expense or reserve (e.g., accelerated depreciation, ITC, Schedule M items normalized, phase-in plans, etc.).

Response 5: These amounts have been identified on Exhibit 1, except for a calculation of ITC amortization, which is shown on Exhibit 3.

Request 6: Please provide further information which the Company deems necessary in examining the revenue requirement impact of the tax law change.

Response 6: The magnitude of the tax impact will vary widely across companies. To presume that the tax change has a direct relationship with authorized earnings would unfairly penalize or reward companies. General believes that the Commission should examine each company individually by comparing the actual earnings level of each to its authorized return level. In addition, General strongly points out that the tax reform impacts included in this package are based upon unadjusted earnings for the twelve months ending June 30, 1986 and the industry environment as it existed during that time. The Tax Reform impacts and base level of earnings ending June 30, 1986 in no way represents General's future earnings and anticipated Tax Reform impacts. There are a myriad of other changes that will be taking place over the next twelve to eighteen months. For example, six months after the new tax rate is fully effective, the revised Uniform System of Accounts (USOA) will be implemented. The revised accounting system generally has the effect of increasing revenue requirement by expensing items that were previously capitalized. Any decrease in tax liability may be useful in meeting the revenue requirement caused by USOA. The Missouri Commission has also issued an order deregulating embedded customer premise equipment (CPE) on December 31, 1987. Therefore, the contribution that CPE has made to local service rates will disappear and this will also increase General's revenue requirement. In addition there are a number of events evolving in the toll/access arena, such as changes in compensation plans and the crucial need to transition nontrafficsensitive costs to the local ratepayer.

Response 6: (Cont'd)

General also believes it very important for the Commission to consider that future pricing of toll or access will reflect these changes in the income tax laws. Therefore, it would appear prudent for the Commission to only analyze the impact of the tax law changes on companies local operations only. General has segregated this information on Exhibit 1.

General recognizes that the Commission is concerned that utilities not unfairly benefit by the changed tax laws. However, only by reviewing each company's earnings on a case by case basis and considering the other changes occurring throughout the telecommunication's industry can the Commission make an appropriate evaluation. This method would be equitable to both ratepayers and stockholders.

GENERAL TELEPHONE COMPANY OF THE MIDWEST
CASE NO. AO-87-48
TAX REFORM ACT OF 1986

TAX REFORM ----- EFFECT ON MISSOURI INTRASTATE/LOCAL OPERATIONS (THOUSANDS OF DOLLARS

	BASE CASE					1986 TAX LAW					1987 TAX LAW					1988 TAX LAW				
	BOOK	INTRASTATE		LOCAL		BOOK	INTRASTATE		LOCAL		BOOK	INTRASTATE		LOCAL		BOOK	INTRASTATE		LOCAL	
	TOTAL	PCT	AMT	PCT	AMT	TOTAL	PCT	AMT	PCT	AMT	TOTAL	PCT	AMT	PCT	AMT	TOTAL	PCT	AMT	PCT	AMT
OPER. REV.	57453		40525		20341	57453		40525		20341	57453		40525		20341	57453		40525		20341
OPER. EXP.	40289		30699		15677	40289		30699		15677	40289		30699		15677	40289		30699		15677
OTHER OP TAX	3082		2182		1104	3082		2182		1104	3082		2182		1104	3082		2182		1104
	14082		7644		3560	14082		7644		3560	14082		7644		3560	14082		7644		3560
ADD:																				
DEPR ADJ	2467	70.26%	1733	36.87%	910	2467	70.26%	1733	36.87%	910	2419	70.26%	1700	36.87%	892	2322	70.26%	1631	36.87%	856
BAD DEBTS ADJ	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	54	70.26%	38	36.87%	20	54	70.26%	38	36.87%	20
MEALS/ENTERTAINMENT	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	46	70.26%	32	36.87%	17	46	70.26%	32	36.87%	17
INTEREST CAPITALIZED	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	267	70.26%	188	36.87%	98	267	70.26%	188	36.87%	98
PROP TAX CAPITALIZED	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	86	70.26%	60	36.87%	32	86	70.26%	60	36.87%	32
OTHER CAPITALIZED EXP	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	0	70.26%	0	36.87%	0	0	70.26%	0	36.87%	0
LESS:																				
FIXED CHARGES	-3926	70.26%	-2758	36.87%	-1448	-3926	70.26%	-2758	36.87%	-1448	-3926	70.26%	-2758	36.87%	-1448	-3926	70.26%	-2758	36.87%	-1448
PENSION COSTS	-486	70.26%	-341	36.87%	-179	-486	70.26%	-341	36.87%	-179	-89	70.26%	-63	36.87%	-33	-89	70.26%	-63	36.87%	-33
PAYROLL TAXES	-182	70.26%	-128	36.87%	-67	-182	70.26%	-128	36.87%	-67	0		0		0	0		0		0
SALES TAXES	-280	70.26%	-197	36.87%	-103	-280	70.26%	-197	36.87%	-103	0		0		0	0		0		0
EXCESS DEPRECIATION	-3997	70.26%	-2808	36.87%	-1474	-3997	70.26%	-2808	36.87%	-1474	-4570	70.26%	-3211	36.87%	-1685	-5687	70.26%	-3996	36.87%	-2097
ADJUSTED INCOME	7678		3145		1199	7678		3145		1199	8369		3630		1454	7155		2777		1006

CALCULATION OF CURRENT FEDERAL INCOME TAX

	BASE CASE					1986 TAX LAW					1987 TAX LAW					1988 TAX LAW				
	BOOK TOTAL	INTRASTATE PCT	INTRASTATE AMT	LOCAL PCT	LOCAL AMT	BOOK TOTAL	INTRASTATE PCT	INTRASTATE AMT	LOCAL PCT	LOCAL AMT	BOOK TOTAL	INTRASTATE PCT	INTRASTATE AMT	LOCAL PCT	LOCAL AMT	BOOK TOTAL	INTRASTATE PCT	INTRASTATE AMT	LOCAL PCT	LOCAL AMT
ADJUSTED INCOME	7678		3145		1199	7678		3145		1199	8369		3630		1454	7155		2777		1006
LESS: STATE TAX	359		151		59	358		151		59	381		165		71	331		128		51
FEDERAL TAXABLE INC	7319		2994		1140	7320		2994		1140	7988		3465		1383	6824		2649		955
FED RATE	46%		46%		46%	46%		46%		46%	40%		40%		40%	34%		34%		34%
FED TAX	3367		1377		524	3367		1377		524	3195		1386		553	2320		901		325
LESS:																				
ITC AMORTIZATION	-1192	70.26%	-837	36.87%	-439	-1166	70.26%	-819	36.87%	-430	-1075	70.26%	-755	36.87%	-396	-946	70.26%	-665	36.87%	-349
TOT FED TAX BEFORE REVERSAL OF EXCESS DEFERRED TAXES	2175		540		85	2201		558		94	2120		631		157	1374		236		-24
REVERSAL OF DEFERRED TAXES ASSOCIATED W/RATE CHANGE	NA		NA		NA	NA		NA		NA	-133	70.26%	-93	36.87%	-49	-266	70.26%	-187	36.87%	-98
TOTAL CURRENT FIT	2175		540		85	2201		558		94	1987		537		108	1108		49		-122

Exhibit 1
Page 1 of 3

TAX REFORM ----- EFFECT ON MISSOURI INTRASTATE/LOCAL OPERATIONS (CONTINUED)

CALCULATION OF CURRENT STATE INCOME TAX

	BASE CASE					1986 TAX LAW					1987 TAX LAW					1988 TAX LAW				
		INTRASTATE		LOCAL			INTRASTATE		LOCAL			INTRASTATE		LOCAL			INTRASTATE		LOCAL	
	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT
ADJUSTED INCOME	7678		3145		1199	7678		3145		1199	8369		3630		1454	7155		2777		1006
LESS: FEDERAL TAX	504		125		20	510		129		22	741		321		36	538		209		-6
NET OF FED	7174		3020		1179	7168		3016		1177	7628		3309		1418	6617		2568		1012
STATE SIT RATE	0.05		0.05		0.05	0.05		0.05		0.05	0.05		0.05		0.05	0.05		0.05		0.05
CURRENT STATE INCOME TAX	359		151		59	358		151		59	381		165		71	331		128		51
TOTAL CURRENT INCOME TAX	2534		691		144	2559		709		153	2368		703		179	1439		177		-71

CALCULATION OF DEFERRED INCOME TAX

	BASE CASE					1986 TAX LAW					1987 TAX LAW					1988 TAX LAW				
	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT	BOOK TOTAL	PCT	AMT	PCT	AMT
EXCESS DEPRECIATION	3997					3997					4570					5687				
RATE	0.4842					0.4842					0.4274					0.3705				
	1935	70.26%	1360	36.87%	714	1935	70.26%	1360	36.87%	714	1953	70.26%	1372	36.87%	720	2107	70.26%	1480	36.87%	777
TOTAL INCOME TAX	4469		2050		857	4495		2068		867	4322		2075		899	3546		1658		705
INCREASE (DECREASE) IN TOTAL INCOME TAXES DUE TO TAX REFORM								18		10			24		41			-393		-152

Exhibit 1
Page 2 of 3

GENERAL TELEPHONE COMPANY OF THE MIDWEST

MISSOURI CASE NO. AO-87-48
TAX REFORM ACT OF 1986

REVENUE REQUIREMENT
(DOLLARS IN THOUSANDS)

	BASE CASE		1986 TAX LAW		1987 TAX LAW		1988 TAX LAW	
	INTRASTATE	LOCAL	INTRASTATE	LOCAL	INTRASTATE	LOCAL	INTRASTATE	LOCAL
RATE BASE	69260	35090	69260	35090	69260	35090	69260	35090
RATE OF RETURN	11.28%	11.28%	11.28%	11.28%	11.28%	11.28%	11.28%	11.28%
RETURN	7813	3958	7813	3958	7813	3958	7813	3958
ADJUSTED NET INCOME	5594	2703	5576	2693	5570	2662	5987	2855
INCOME DEFICIT	2219	1255	2237	1265	2243	1296	1826	1103
GROSS UP FACTOR	1.9391	1.9391	1.9391	1.9391	1.7467	1.7467	1.5000	1.5000
ADD'L REVENUE REQUIREMENT	4302	2434	4337	2453	3917	2264	2900	1753
INCREASE/(DECREASE) IN TOTAL REVENUE REQUIREMENT DUE TO TAX REFORM:								
INCOME TAX EXPENSE			35	19	42	72	(624)	(241)
GROSS UP FACTOR			-	-	(427)	(242)	(770)	(440)
EARNED RATE OF RETURN	8.08%	7.70%	8.05%	7.67%	8.04%	7.59%	8.64%	8.14%

MISSOURI
CASE NO. AO-87-48
EFFECTS OF TAX REFORM
(000)

REVERSAL OF DEFERRED TAXES ATTRIBUTABLE TO THE TURNAROUND OF TAX/BOOK TIMING DIFFERENCES AT RATES LOWER THAN THE RATE AT WHICH THE RESERVE HAS THUS FAR BEEN ESTABLISHED.

TO DETERMINE THE AMOUNT OF REVERSAL, A STUDY WAS MADE OF THE REVERSALS WHICH OCCURRED IN THE 1985 TAX YEAR. THIS IS THE MOST RECENT YEAR THAT ACTUAL INFORMATION IS AVAILABLE.

AMOUNT OF THE REVERSAL IN 1985 IN EXCESS OF THE 34% RATE	294
AMOUNT OF THIS REVERSAL ATTRIBUTABLE TO A RATE IN EXCESS OF THE CURRENT 46% RATE. (THIS AMOUNT IS NOT ATTRIBUTABLE TO THE TAX REFORM ACT.)	-28
AMOUNT IN 1985 ATTRIBUTABLE TO THE RATE CHANGE FROM 46% TO 34% OUTLINED IN THE TAX REFORM ACT.	266
ONE-HALF EFFECT FOR 1987, WHERE RATE IS 40%	133

MISSOURI
CASE NO. AO-87-48
EFFECTS OF TAX REFORM

CALCULATIO OF ITC AMORTIZATION LOST AS A RESULT OF THE TAX REFORM ACT OF 1986:

VINTAGE	ITC CLAIMED RATE	ADDITIONS	CLAIMED	AMORTIZATION * 1986	1987	1988
1986	0.088	17708	623	26	52	52
1987	0.088	17708	1558		65	129
1988	0.088	17708	1558			65
				26	117	246
ORIGINAL ITC AMORTIZATION				1192	1192	1192
				-1166	-1075	-946

* AMORTIZATION COMPUTED AT 8.3% OF AMOUNT CLAIMED WITH HALF YEAR CONVENTION