

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

In the Matter of the Petition of                                     )  
Missouri-American Water Company for                                     )           File No. WO-2018-0373  
Approval to Establish an Infrastructure                                     )  
System Replacement Surcharge (ISRS).                                     )

**APPLICATION FOR REHEARING  
AND  
MOTION TO DEFER RULING**

COMES NOW Missouri-American Water Company, and pursuant to §386.500, RSMo., submits its Application for Rehearing and Motion to Defer Ruling of a *Report and Order* issued by the Commission in the above-captioned matter on December 12, 2018. In support hereof, MAWC states as follows:

**Introduction**

1.       The intent of Congress in creating the normalization rules is to provide the utility an interest free source of funds to invest in utility property. (IRS Revenue Proc. 2-17-47 (“Congress enacted the ITC and accelerated depreciation to stimulate investment.”)) This intent may be thwarted if Net Operating Losses are not taken into account in this case.

2.       MAWC recognizes that the tax issues addressed in this case are very technical and complex. Further, they are very unique in that the subject concerns a direct interaction between the Internal Revenue Service and the Commission that is not found in other matters that find their way before the Commissions. Accordingly, in addition to its rehearing application, MAWC has included a Motion to Defer Ruling. The purpose of that Motion is to allow the party that ultimately will have the final word on this issue (the IRS) to provide guidance to MAWC and the Commission.

### Application for Rehearing

3. The Order of the Missouri Public Service Commission is unlawful, unreasonable, unjust, arbitrary and an abuse of discretion for one or more or all of the reasons hereinafter set forth. For the reasons stated in the following paragraphs, the decision of the Commission should be reheard and the Order in this case should be amended or superseded to address and correct the matters of error raised by the Company.

4. In MAWC's Infrastructure System Replacement Surcharge Application, the Company included an ADIT<sup>1</sup> Asset created by the Net Operating Loss ("NOL") from the ISRS investments that were the subject of its Application consistent with the ISRS statute.<sup>2</sup> While the Commission concedes that the ISRS statute "requires recognition of ADIT, which might include reflection of an NOL,"<sup>3</sup> it concluded that the Company had not presented evidence sufficient to support that it will have a NOL in 2018, rejected the tariff sheet filed by MAWC on August 20, 2018<sup>4</sup>, and authorized it to file new tariffs omitting an ADIT Asset created by an NOL.<sup>5</sup> In support of its decision, the Commission states, among other things, that MAWC "will not generate a new NOL" to offset its taxable income in 2018 and 2019.<sup>6</sup>

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<sup>1</sup> Accumulated Deferred Income Tax.

<sup>2</sup> Section 393.1000(1)(a), RSMo, defines "Appropriate Pretax Revenues" as:

[T]he revenues necessary to produce net operating income equal to: (a) The water corporation's weighted cost of capital multiplied by the net original cost of eligible infrastructure replacements, including recognition of accumulated deferred income taxes and accumulated depreciation associated with eligible infrastructure system replacements which are included in a currently effective ISRS. (emphasis added)

<sup>3</sup> Order at p. 8.

<sup>4</sup> Tariff Tracking No. YW-2019-0018.

<sup>5</sup> Order at pp. 8-9.

<sup>6</sup> Order at p. 8.

5. The Commission's Order disregards evidence in the record showing that the MAWC Deferred Income Tax Asset balance over the period of December 2017, through September 2018 increased between May 2018, and June 2018 (not decreased as alleged by Staff), and that a NOL actually was incurred during the period of the ISRS plant at issue. Company witnesses LaGrand and Wilde testified that the Company included depreciation and interest expense that occurred during the ISRS period, accelerated depreciation, and the repairs deduction and that these large deductions, taken against no revenue, create a large NOL.<sup>7</sup> Consequently, the Commission's finding that there was "no evidence" of an NOL being generated during the 2018 ISRS period<sup>8</sup> is without basis because there is ample evidence in the record showing a NOL from the ISRS investments that were the subject of its Application.

6. The practical effect of the Order (i.e., to eliminate the recognition of the ADIT Asset which is comprised of the NOL) is inconsistent with a normalized method of accounting because the impact of ignoring the Deferred Tax Asset provides customers with the benefit of the tax deduction now, through a lower ISRS rate, even though the Company is unable to benefit from those tax deductions at this time.

7. The non-recognition of the NOL associated with these ISRS investments creates a peril for the Company and its customers concerning its income tax accounting. It likely will cause a deviation from the normalization requirements of the IRS Code. Specifically a finding by the IRS that MAWC has violated the tax normalization rules, or the terms of its Consent Agreement<sup>9</sup>, could cause the loss of significant tax benefits that currently are enjoyed by its

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<sup>7</sup> Exh. 1, LaGrand Dir., Sched. BWL-1, p. 2 of 7; Exh. 2, Wilde Dir., p. 12; Tr. 70, Wilde.

<sup>8</sup> Order at pp. 6, 8.

<sup>9</sup> The record shows that in 2010, the Company entered into a consent agreement with the IRS which authorized the Company's requested Change in Accounting Method to allow the utilization of the repairs deduction/method. One of the requirements of that consent agreement is

customers, such as the ability of the company to claim accelerated depreciation deductions and tax repair deductions which serve to keep rates lower than otherwise would be the case because these tax features serve to reduce rate base. The Commission's disregard of a private letter ruling (PLR 201548017) stating unambiguously that "an NOLC must be taken into account for normalization purposes" is premised on its erroneous factual determination that there is no NOL being generated.<sup>10</sup>

### **Motion to Defer Ruling on this Application for Rehearing**

8. There is no requirement that the Commission rule on this Application for Rehearing by a date certain. Given the seriousness of the matters summarized in paragraph 5, *supra.*, MAWC requests that the Commission take this Application for Rehearing under advisement and *not* issue a ruling thereon until such time as the Company can request, obtain and proffer a private letter ruling from the IRS on whether application of the findings by the Commission for the period in question would cause a violation of tax normalization rules. As noted in MAWC's prehearing brief, the "inadvertent error" safe harbor exception relied upon by Staff witness Ferguson<sup>11</sup> does not, in the Company's view, save the Company from the adverse consequences that may flow should the IRS determine that the Company's practices in furtherance of the Order are inconsistent with tax normalization requirements or obligations.

9. The possible adverse consequences flowing from the Order are of such a magnitude, and have such a potential adverse consequence on cost of service for ratemaking

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that MAWC use a normalized method of accounting, even though a tax repairs deduction is not otherwise specifically subject to that the tax normalization rules.

<sup>10</sup> Order at. p. 8.

<sup>11</sup> Rev. Proc. 2017-47.

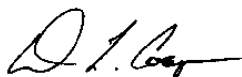
purposes, that sound policy supports a delay in finality in order to obtain more clarity on the income tax consequences that may result.

**Conclusion**

MAWC requests that the Commission defer ruling on this Application for Rehearing until such time as the Company can request, obtain and proffer a private letter ruling from the IRS concerning whether application of the findings by the Commission for the period in question would cause a violation of tax normalization rules.

Thereafter, for the reasons stated herein, MAWC respectfully requests that the Commission grant the Company's Application for Rehearing for the reasons aforesaid, and upon rehearing, issue a superseding or correction order directing that ISRS tariffs be filed sufficient to recover ISRS revenues in the amount of \$7,264,876 by including the Deferred Tax Asset in the ISRS calculations and making such other findings as are consistent with the matters set forth above.

Respectfully submitted,



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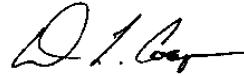
ATTORNEYS FOR MISSOURI-AMERICAN  
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**CERTIFICATE OF SERVICE**

I hereby certify that copies of the foregoing have been transmitted by electronic mail to the following on this 14<sup>th</sup> day of December, 2018:

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