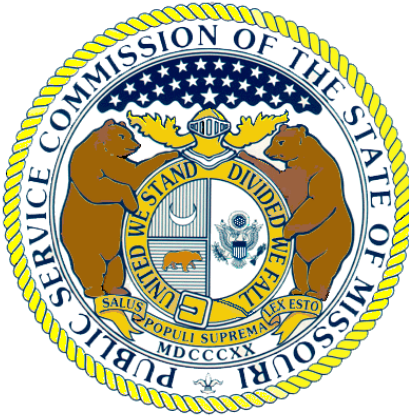


BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI



In the Matter of the Petition of Missouri-)
American Water Company for Approval) **File No. WO-2020-0190**
to Change an Infrastructure System) **Tariff No. YW-2020-0148**
Replacement Surcharge (ISRS))

REPORT AND ORDER

Issue Date: June 17, 2020

Effective Date: June 27, 2020

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OF THE STATE OF MISSOURI**

In the Matter of the Petition of Missouri-)	
American Water Company for Approval)	<u>File No. WO-2020-0190</u>
to Change an Infrastructure System)	Tariff No. YW-2020-0148
Replacement Surcharge (ISRS))	

APPEARANCES

Missouri-American Water Company:

Dean L. Cooper, Brydon, Swearingen & England, PO Box 456, Jefferson City, Missouri 65102.

Staff of the Missouri Public Service Commission:

Mark Johnson, Deputy Counsel, PO Box 360, 200 Madison Street, Jefferson City, Missouri 65102.

Office of the Public Counsel:

John Clizer, Senior Counsel, PO Box 2230, 200 Madison St., Ste. 650, Jefferson City, Missouri, 65102.

Regulatory Law Judge: Charles Hatcher

REPORT AND ORDER

I. Procedural History

On March 2, 2020, Missouri-American Water Company (MAWC) filed a petition requesting authority from the Missouri Public Service Commission (Commission) to change its Infrastructure System Replacement Surcharge (ISRS) for its St. Louis County service territory.

MAWC requested to adjust its ISRS rate to recover eligible costs incurred in connection with infrastructure system replacements made during the period October 1, 2019 through March 31, 2020. The Commission issued notice of the application and provided an opportunity for interested persons to intervene. No requests to intervene were received. The filed tariff sheet has an effective date of June 30, 2020.

MAWC's ISRS was established in WO-2018-0373 (MAWC ISRS 1), changed in WO-2019-0184 (MAWC ISRS 2), and changed again in WO-2019-0389 (MAWC ISRS 3). In this, the fourth MAWC ISRS case since its last general rate case, MAWC also proposes an adjustment to cure normalization violations resulting from the prior three ISRS cases.

On May 1, 2020, the Staff of the Commission (Staff) filed its recommendation and memorandum. Staff agreed with MAWC's calculation of its proposed adjustment to cure normalization violations. Staff recommended that the Commission reject the original tariff sheet and approve an ISRS rate for MAWC based on Staff's determination of the appropriate amount of ISRS revenues, which includes an adjustment of \$35,328 to cure normalization violations which occurred in MAWC ISRS cases 1, 2, and 3.

On May 11, 2020, MAWC filed a response agreeing with Staff's recommendation. On the same day, the Office of the Public Counsel (Public Counsel) filed its objections and a request for an evidentiary hearing. The Commission held an evidentiary hearing on June

3, 2020. In total, the Commission admitted the testimony of six witnesses and 13 exhibits into evidence. Post-hearing briefs were filed on June 8, 2020.

II. Findings of Fact

Any finding of fact for which it appears that the Commission has made a determination between conflicting evidence is indicative that the Commission attributed greater weight to that evidence and found the source of that evidence more credible and more persuasive than that of the conflicting evidence.

1. MAWC is a “water corporation” and a “public utility”, as defined in Sections 386.020(59) and (43), and 393.1000(7), RSMo 2016,¹ and is authorized to provide water service in St. Louis County.

2. Public Counsel is a party to this case pursuant to Section 386.710(2), and by Commission rule 20 CSR 4240-2.010(10).

3. Staff is a party to this case pursuant to Section 386.071, and Commission rule 20 CSR 4240-2.010(10).

4. An ISRS allows water companies located in St. Louis County to charge customers for system replacements on infrastructure that is worn out or deteriorated, without a general rate case.²

5. On March 2, 2020, MAWC filed a petition for its St. Louis County service territory, requesting a change to its ISRS to recover eligible costs incurred for infrastructure system replacements made during the period October 1, 2019, through March 31, 2020, (ISRS Period).³

¹ Unless otherwise stated, all statutory citations are to the Revised Statutes of Missouri, as codified in the year 2016.

² Sections 393.1000 to 393.1006, RSMo.

³ MAWC's Petition to Change Its Infrastructure System Replacement Surcharge & Motion for Approval of Customer Notice.

6. In conjunction with its petition, MAWC filed a tariff sheet that would generate a total revenue requirement for MAWC's ISRS.⁴ MAWC's proposed ISRS revenue requirement was \$8,996,922.⁵

7. MAWC proposed the ISRS be adjusted to address an issue of a normalization violations in MAWC's three prior ISRS cases.⁶

8. Staff recommended approval of incremental pre-tax ISRS surcharge revenues in the amount of \$9,725,687.⁷ Staff's revenue requirement updates MAWC's requested revenue requirement of \$8,996,922 with actual costs for the months of February and March 2020, as the petition included estimated costs. MAWC revised its revenue requirement to match Staff's.⁸

9. Staff's recommended revenue requirement also included MAWC's proposed adjustment of \$35,328 to address normalization violations in MAWC ISRS 1 through 3.⁹ Public Counsel objected to this adjustment.¹⁰

10. An ISRS is reset after each general rate case. MAWC has had three ISRS cases since its most recent general rate case. In each of those three ISRS cases, MAWC has claimed a net operating loss (NOL) due to the ISRS replacements.¹¹

⁴ MAWC's Petition to Change Its Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendix B.

⁵ MAWC's Petition to Change Its Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendix C, p. 1.

⁶ MAWC's Petition to Change Its Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, paragraph 31.

⁷ Ex. 303, Supplement to Direct Testimony of Ali Arabian, Sch. AA-sd1, p. 4 and 8.; Ex. 302, Direct Testimony of Ali Arabian, p. 2, In. 5-6.

⁸ Ex. 101, Direct Testimony of Brian LaGrand, p. 4. In. 20.

⁹ Ex. 303, Supplement to Direct Testimony of Ali Arabian, Sch. AA-sd1, p. 5-7.

¹⁰ Response to Staff Recommendation and Request for an Evidentiary Hearing, filed May 11, 2020.

¹¹ Report and Order, WO-2018-0373, issued December 5, 2018; Report and Order, WO-2019-0184, issued June 5, 2019; Order Approving Partial Stipulation and Agreement and Approving Infrastructure System Replacement Surcharge, WO-2019-0389, issued November 21, 2019.

11. MAWC's theory of its NOL is the accelerated depreciation expense of the new infrastructure subtracted from zero new revenues on that infrastructure, produces a loss on the new infrastructure up until the time the new ISRS rates are effective.¹²

12. The Commission found no NOL existed in the first two MAWC ISRS cases.¹³ MAWC ISRS 3 (WO-2019-0389) settled via a stipulation to abide by the finding of the Internal Revenue Service (IRS). MAWC requested and received an advisory opinion from the IRS, called a Private Letter Ruling (PLR).¹⁴

13. The IRS is the agency designated to interpret the Internal Revenue Code and to determine whether the actions of taxpayers and regulators are in compliance with the Code.¹⁵

14. The Commission's decisions in MAWC ISRS 1 and 2 were based on its long-term understanding, and Internal Revenue Code definition, that the phrase "net operating loss" referred to year-end tax calculations, and any such loss would not be project-specific.¹⁶

15. Ruling 9 of the PLR states:

Under the circumstances described, in order to comply with the normalization method of accounting within the meaning of section 168(i)(9), the amount of depreciation-related ADIT reducing rate base used to determine the revenue requirement set in the Surcharge Case must be decreased to reflect a portion of the **NOL** for the test period for depreciation-related book/tax differences during the test period for the Surcharge Case which would not have arisen had Taxpayer not reported depreciation-related book/tax differences during the test¹⁷ period for the Surcharge Case and such decrease in depreciation-related ADIT must be an

¹² Transcript (Tr.) Vol 1, p. 65, ln. 4-14.

¹³ Both MAWC ISRS 1 and 2 were appealed by MAWC. The Western District Court of Appeals affirmed those orders. *Missouri-American Water Company v. Mo. Pub. Serv. Comm'n.*, 591 S.W. 3d 465 (2019); *Missouri-American Water Company v. Mo. Pub. Serv. Comm'n.* No. WD 83067, 2020 WL 1918699.

¹⁴ Ex. 102c, Direct Testimony of John R. Wilde, Schedules JRW-1 and JRW-2.

¹⁵ Ex. 301, Rebuttal Testimony of Mark L. Oligschlaeger, p. 3, ln. 15-17.

¹⁶ WO-2018-0373, Report and Order, issued December 5, 2018; WO-2019-0184, Report and Order, issued June 5, 2019.

¹⁷ Original reads "text"

amount that is no less than the amount computed using the With-and-Without Method.¹⁸ (emphasis added)

16. In Ruling 9, the PLR uses the term NOL to refer to a specific project and a specific time period, which is a different working definition of NOL in the context of ISRS rate cases than used by the Commission in the past.¹⁹

17. Ruling 9 identifies the NOL claimed by MAWC as “the portion of the NOL for the test period for the Surcharge Case which would not have arisen had Taxpayer not reported depreciation-related book/tax differences during the te[s]t period for the Surcharge.”²⁰

18. The term “net operating loss” is defined as “the excess of operating expenses over revenues.”²¹ An NOL results when a utility does not have enough taxable income to utilize all of the tax deductions to which it would otherwise be entitled. When this situation occurs, the amount of the unused deductions is referred to as an NOL and is booked to a deferred tax asset account.²²

19. The tax normalization requirements of the IRS Code mandate that utility rates be set so that customers do not receive the tax benefit of accelerated depreciation deductions any faster than over the estimated straight-line book lives authorized for the utilities’ assets.²³

20. The IRS agreed with MAWC’s NOL theory that the NOL amount applicable to ISRS plant additions should be determined using the so-called “with-and-without” method.²⁴

¹⁸ Ex. 102c, Direct Testimony of John R. Wilde, Schedule JRW-2, p. 20.

¹⁹ Tr. Vol 1, p. 118, Staff witness Mark Oligschlaeger.

²⁰ Ex. 202, Rebuttal Testimony of John R. Wilde, p. 4, In. 8-12.

²¹ Ex. 100, Stipulation of Facts, paragraph 13.

²² Ex. 300, Direct Testimony of Mark L. Oligschlaeger, p. 5, In. 4-7.

²³ Ex. 300, Direct Testimony of Mark L. Oligschlaeger, p. 3-4. In. 21-4; Ex. 102, Direct Testimony of John R. Wilde, p. 5, In. 11-15, and p. 11, In 7-10.

²⁴ Ex. 301, Rebuttal Testimony of Mark L. Oligschlaeger, p. 4-6, In. 21-23.

However, the IRS disagreed with MAWC's position from the prior ISRS cases than an NOL should also be applied to repairs to plant.²⁵

21. The With and Without Method is directed by the PLR to be used in calculating the NOL amount.²⁶

22. The With and Without Method is a comparison of the accelerated depreciation to the straight line depreciation amount (with accelerated depreciation compared to without accelerated depreciation). Lines 62-63 of MAWC's attached schedule BWL-2 shows the comparison.²⁷

23. The guidance of the PLR was not available to the Commission in decisions MAWC ISRS 1 through 3 as it was not filed with the Commission by MAWC until December 9, 2019,²⁸ which is after the issuance of the decisions in MAWC ISRS 1 through 3.²⁹

24. In MAWC ISRS 1, MAWC's updated revenue requirement using actual receipts for the nine month ISRS period was \$7,264,876. This ISRS calculation included accumulated deferred income taxes (ADIT) and a proposed NOL. Staff recommended the removal of the \$9.3 million deferred tax asset (NOL). The impact of this removal was an \$866,917 reduction in the ISRS. Staff's proposed ISRS including the NOL reduction and other adjustments was \$6,377,959.³⁰

25. In MAWC ISRS 2, the updated revenue requirement using actual receipts for the nine month ISRS period was \$9,706,228. This ISRS calculation included ADIT and a proposed NOL. Staff proposed the removal of the \$8.85 million deferred tax asset (NOL). The impact of this removal was an \$827,383 reduction in the ISRS. Staff's updated ISRS

²⁵ Ex. 102c, Direct Testimony of John R. Wilde, Schedule JRW-2, p. 19-20, Ruling 5.

²⁶ Ex. 102c, Direct Testimony of John R. Wilde, Schedule JRW-2, p. 20, Ruling 9.

²⁷ Ex. 101, Direct Testimony of Brian W. LaGrand, Schedule BWL-2, p. 2, ln. 62-63.

²⁸ WO-2018-0373, Notice Concerning Receipt of Private Letter Ruling, filed December 9, 2019 (the Commission takes notice of this filing).

²⁹ Respectively: December 5, 2018; June 5, 2019; and November 21, 2019.

³⁰ WO-2018-0373, Report and Order, issued December 5, 2018.

revenue requirement, including the NOL reduction and other adjustments, was \$8,878,845.³¹

26. In MAWC ISRS 3, the updated revenue requirement using actual receipts for the six month ISRS period was \$6,782,250.³² This ISRS calculation included ADIT and a proposed NOL.³³ Staff proposed the removal of the \$7.1 million deferred tax asset (NOL).³⁴ The impact of this removal was a \$670,027 reduction in the ISRS. Staff's updated ISRS revenue requirement, including the NOL reduction and other adjustments, was \$6,112,222.³⁵

27. Implementing Ruling 9 results in a \$35,328 adjustment for the normalization violations that occurred over the three prior ISRS cases.³⁶

28. Not including an offset for an NOL amount in computing the ISRS surcharge constituted a violation of the IRS Code's normalization restrictions, by effectively passing accelerated depreciation deduction benefits on to customers prematurely.³⁷

29. The IRS requires violations to be remedied at the next available opportunity, and if not remedied could lead to severe sanctions by the IRS on MAWC such as the loss of the ability to claim accelerated depreciation.³⁸ The inability to utilize accelerated depreciation could result in higher rates for MAWC customers.³⁹

³¹ WO-2019-0184, Report and Order, issued June 5, 2019.

³² WO-2019-0389, Staff Recommendation, Appendix A, p. 4 (the Commission takes notice of Appendix A).

³³ WO-2019-0389, Staff Recommendation, Appendix A, p. 3.

³⁴ WO-2019-0389, Staff Recommendation, Appendix A, Attachment 1.

³⁵ WO-2019-0389, Staff Recommendation, Appendix A, Attachment 1.

³⁶ Ex. 102, Direct Testimony of Brian W. LaGrand, Schedule BWL-3.

³⁷ Ex. 300, Direct Testimony of Mark L. Oligschlaeger, p. 7-8, In. 19-2; and p. 8 In. 16-20; Ex. 102, Direct Testimony of John R. Wilde, p. 5, In. 1-26.

³⁸ Ex. 102, Direct Testimony of John R. Wilde, p. 5-6, In. 17-8.

³⁹ Ex. 102, Direct Testimony of John R. Wilde, p. 7-8, In. 19-2.

30. Ruling 9 is limited in its applicability to utilities that are in an NOL carryover position at some point during the ISRS period.⁴⁰

31. Ruling 9 is limited in its applicability as PLR's are applicable only to the taxpayer that requested it. It is also limited as to the facts asserted within the PLR and findings based on those asserted facts. Ruling 9 is further limited in its applicability as PLR's cannot be used as precedent.⁴¹

32. The IRS is required to check if the facts described in the PLR are accurate when processing the taxpayer's return.⁴²

33. PLR's will be revoked if the IRS finds the facts supplied by the taxpayer to be incorrect and can even have the revocation be retroactive.⁴³

34. MAWC's submitted request to the IRS for the PLR included: a written discussion by Staff's Director of Operations Mark Oligschlaeger, Staff's final response to the request, and the Commission decisions in MAWC ISRS 1 and 2.⁴⁴

35. MAWC's tariff directs that Contributions In Aid of Construction (CIAC) be segregated into a deferred account for inclusion in rate base in MAWC's next general rate proceeding. Additionally, CIAC is already included in the deferred taxes calculation in taxable income reconciled for 2018, 2019, and 2020.⁴⁵

⁴⁰ Ex. 102, Direct Testimony of John R. Wilde, p. 11, ln. 15-17; Ex. 103, Rebuttal Testimony of John R. Wilde, p. 9, ln. 11-16.

⁴¹ Ex. 102c, Direct Testimony of John R. Wilde, Schedule JRW-2, p. 22.

⁴² Brief of the Missouri Office of the Public Counsel, p. 10, citing 26 CFR § 601.201(l)(2); Rev. Proc. 2019-1, I.R.B. 2019-01 § 11.03 (I.R.S. January 2, 2019).

⁴³ Brief of the Missouri Office of the Public Counsel, p. 10, citing 26 CFR § 601.201(l)(2),(4),(5); Rev. Proc. 2019-1, I.R.B. 2019-01 §§ 11.03,11.04,11.05 (I.R.S. January 2, 2019).

⁴⁴ Ex. 102, Direct Testimony of John R. Wilde, p. 10, ln. 9-15; Ex. 301, Rebuttal Testimony of Mark L. Oligschlaeger, p. 7, ln. 9-18; Ex. 103, Rebuttal Testimony of John R. Wilde, p. 4, ln. 8-12, and p. 8, ln. 7-10, and p. 10, ln. 6-12; Tr. Vol 1, p. 51-52, ln. 25-17.

⁴⁵ Tr. Vol 1, p. 68, ln. 4-16; and p 77, ln. 13-18.

36. ISRS revenues to be counted are limited to those occurring due to the ISRS replacements, and cannot be counted as both revenue under the existing rates and revenue to offset an NOL.⁴⁶

37. The PLR requires the NOL include only losses related to accelerated depreciation based upon the With-and-Without Method and MAWC applied that Method in calculating the \$35,328 adjustment for the prior three ISRS cases.⁴⁷

38. The IRS was aware that MAWC had taxable income in 2018.⁴⁸

39. MAWC's initial ISRS calculation included the repairs to plant in the deferred income taxes for purposes of calculating the ISRS.⁴⁹ According to the PLR, repairs to plant is not subject to the normalization method of accounting.⁵⁰ Therefore, repairs to plant is not included in the NOL deferred tax asset for purposes of calculating the ISRS.⁵¹ All parties have agreed that recognition of deferred taxes associated with accelerated depreciation tax timing differences for all plant additions should be included for this ISRS Period.⁵²

40. The NOL reduces ADIT. In the ISRS rate calculation for the current case, the NOL adjustment for MAWC ISRS 1 through 3 is an adjustment added to the total revenue requirement.⁵³

41. Staff witness Barnes recommended that the cost of service allocation is based on the revenue requirement being spread to each class based on billing determinants agreed to in MAWC's previous general rate case. The rate design, limited per statute to St. Louis County, is an increase per 1,000 gallons of \$0.30155 for Rate A,

⁴⁶ Section 393.1000(6); Tr. Vol. 1, p. 70, ln. 5-21, p. 81; ln. 9-14; p. 82, ln. 8-11; and p. 83, ln. 4-20.

⁴⁷ Tr. Vol. 1, p. 61, ln. 20-25.

⁴⁸ Tr. Vol. 1, p. 79 - 81, ln. 15-14 (p. 81).

⁴⁹ Ex. 101, Direct Testimony of Brian LaGrand, Schedule BWL-2, p. 1, ln. 7 and 25; and p. 2, n. 32, 41, and 84.

⁵⁰ Ex. 102c, Direct Testimony of John R. Wilde, Schedule JRW-2, p. 19-20, Ruling 5.

⁵¹ Tr. Vol. 1, p. 67-68.

⁵² OPC Brief, p. 50, MAWC Brief, p. 24, Staff Brief, p. 17.

⁵³ Ex. 101, Direct Testimony of Brian LaGrand, Schedule BWL-2, p. 1.

resulting in an ISRS rate of \$0.96287 per 1,000 gallons. The increases for Rates B and J were \$0.00239 and \$0.00229, respectively, per 1,000 gallons, resulting in ISRS rates for Rates B and J of \$0.01463 and \$0.01399, respectively, per 1,000 gallons.⁵⁴ No party objected to Mr. Barnes' proposed rate design.

42. In MAWC ISRS 3, MAWC and Staff entered into a stipulation and agreement that in the event the IRS ruled in MAWC's favor regarding the disputed NOL amounts in that case and MAWC ISRS 1 and 2, then MAWC would file an Accounting Authority Order (AAO) to cure the normalization violation.⁵⁵ The signatories were ordered by the Commission to comply with the agreement.⁵⁶

III. Conclusions of Law

A. The Commission has the authority under Sections 393.1000 through 393.1006, RSMo, to consider and approve ISRS requests. Since MAWC brought the action, it bears the burden of proof.⁵⁷ The burden of proof is the preponderance of the evidence standard.⁵⁸ In order to meet this standard, MAWC must convince the Commission it is "more likely than not" that its allegations are true.⁵⁹

B. Section 393.1006.2(4) provides that where the Commission finds that a petition complies with the statutory requirements, the Commission "shall enter an order authorizing the water corporation to impose an ISRS that is sufficient to recover "appropriate pretax revenues."

C. Section 393.1000(1) defines "appropriate pretax revenues" to include "recognition of accumulated deferred income taxes and accumulated depreciation

⁵⁴ Ex. 304, Direct Testimony of Matthew J. Barnes, p. 2-3, In. 7-11(p. 3)

⁵⁵ WO-2019-0389, Order Approving Partial Stipulation and Agreement and Approving Infrastructure System Replacement Surcharge, issued November 21, 2019, p 2.

⁵⁶ WO-2019-0389, Order Approving Partial Stipulation and Agreement and Approving Infrastructure System Replacement Surcharge, issued November 21, 2019, Ordered paragraph 4.

associated with eligible infrastructure system replacements which are included in a currently effective ISRS.”

D. Sections 393.1003.3 and 393.1006.6 provide that an ISRS is not final until reset at the next general rate case.

E. Section 393.1006.8 reads in pertinent part: “Commission approval of a petition...to establish or change an ISRS...shall in no way be binding upon the commission in determining the ratemaking treatment to be applied to eligible infrastructure system replacements during a subsequent general rate proceeding...”

F. Section 393.1003.1 provides that an ISRS is subject to refund.

G. Stare decisis does not bind the Commission to past Commission decisions.⁶⁰

IV. Decision

The underlying ISRS request for the fourth ISRS period since MAWC’s most recent general rate case is uncontested. The only disputed issue in this case is the inclusion of a \$35,328 adjustment to cure alleged normalization violations from MAWC ISRS 1 through 3. MAWC ISRS 1 established the ISRS. MAWC ISRS 2 and 3 changed the ISRS. MAWC ISRS 4, the current case, seeks to further change the ISRS. The currently enacted ISRS as a whole has not been reset since it was established in MAWC ISRS 1. Thus, the Commission can use the current case, MAWC ISRS 4, to address the violations from

⁵⁷ “The burden of proof, meaning the obligation to establish the truth of the claim by preponderance of the evidence, rests throughout upon the party asserting the affirmative of the issue”. *Clapper v. Lakin*, 343 Mo. 710, 723, 123 S.W.2d 27, 33 (1938); see also Section 393.150.2.

⁵⁸ *Bonney v. Environmental Engineering, Inc.*, 224 S.W.3d 109, 120 (Mo. App. 2007); *State ex rel. Amrine v. Roper*, 102 S.W.3d 541, 548 (Mo. banc 2003); *Rodriguez v. Suzuki Motor Corp.*, 936 S.W.2d 104, 110 (Mo. banc 1996).

⁵⁹ *Holt v. Director of Revenue, State of Mo.*, 3 S.W.3d 427, 430 (Mo. App. 1999); *McNear v. Rhoades*, 992 S.W.2d 877, 885 (Mo. App. 1999); *Rodriguez*, 936 S.W.2d at 109 -111; *Wollen v. DePaul Health Center*, 828 S.W.2d 681, 685 (Mo. banc 1992).

⁶⁰ *State ex rel. AG Processing, Inc. v. Public Serv. Comm'n*, 120 S.W.3d 732, 736 (Mo. banc 2003).

MAWC ISRS 1 through 3 because the ISRS itself is not final until it is reset in a general rate case.

The NOL reduces ADIT. In the ISRS rate calculation for the current case, the NOL adjustment for MAWC ISRS 1 through 3 is an adjustment added to the total revenue requirement. As the ISRS is not final until reset in a general rate case, the eligible infrastructure system replacements from MAWC ISRS 1 through 3 continue to be included in a currently effective ISRS, as that ISRS was established in MAWC ISRS 1 and has not yet been reset, meaning it is within the statutory meaning of currently effective ISRS.

MAWC and Staff offered evidence of the normalization violation by way of a statement issued by the IRS, the agency responsible for producing and enforcing the Internal Revenue Code. The statement issued by the IRS was a PLR. The PLR agreed with MAWC, and identified an NOL in the loss of accelerated depreciation during the ISRS time periods. The Commission defers to the interpretation of the Internal Revenue Code by the IRS, the agency charged with its enforcement.

In general, the deferred tax asset (NOL) proposed by MAWC included all plant additions, including repairs to plant in all three prior MAWC ISRS cases. It was PLR Ruling 5 which stated that repairs to plant is not subject to normalization accounting that led to the NOL adjustment from MAWC ISRS 1 through 3 being considerably less than what was removed by Staff in those cases.

All plant additions including repairs to plant are included in ADIT because they have accelerated depreciation for tax purposes. In the case of repairs to plant the entire amount is depreciated for tax purposes in the year it is placed in service. For purposes of the ISRS all plant additions are included in the ADIT deduction but only plant additions other than repairs to plant are included in the NOL calculation as an offset to ADIT. The With and

Without Method (applied only to plant additions other than repairs to plant) looks at the difference between straight line depreciation used for rates and accelerated depreciation used for income tax reporting and multiplies this amount by the income tax rate to determine the NOL.

Public Counsel raised three objections: 1) the PLR did not verify any facts, only repeated the facts given them, and the IRS may not have even received Staff's input; 2) even if the Commission accepts the veracity of the PLR, the adjustment calculation did not include CIAC; 3) even if the Commission accepts the veracity of the PLR, the adjustment calculation did not include continuing revenues.

As to challenge one, the only evidence offered was the testimony that the submission to the IRS did include Staff's comments and the previous case decisions. Public Counsel also questioned whether the IRS confirmed the existence of an NOL, or merely repeated the facts given in MAWC's submission. Public Counsel raised questions, but ultimately offered no evidence of impropriety. The testimony together with the Commission's reading of the PLR are sufficient to deny Public Counsel's first challenge as to the submission of documents and the IRS interpretation of the facts given.

Challenge two raises the issue that CIAC was not counted as income to offset the NOL as the contributions occurred during the ISRS periods. The testimony of MAWC and Staff show that CIAC is already being counted and that MAWC's tariff directs that CIAC is included in general rate cases. Furthermore, the PLR Ruling 9 specifically states that the NOL deducted against the depreciation related ADIT must be an amount that is no less than the amount computed using the With-and-Without Method. This calculation does not provide for revenue offsets of any type. The PLR applicable to MAWC's ISRS, does not

consider NOL treatment in the same context that would be applied for traditional income tax calculation purposes. Challenge two is denied.

Challenge three raises the issue that continuing revenue is not counted as an offset to an NOL. Public Counsel's theory is that the replacement pipe, once placed into the ground, is generating revenue from the continued sale of the water flowing through it from the time of installation until the new ISRS rates become effective. As MAWC and Staff point out, this revenue is earned under the prior rates and thus cannot be double counted as revenue. Challenge three is denied.

In the end, Public Counsel believes that an NOL is a tax return item that requires a tax return be completed. Public Counsel witness John Riley testified to such and further stated his belief that one cannot have an NOL on an interim basis, nor can an NOL be asset specific. Staff witness Mark Oligschlaeger testified that Staff does not necessarily disagree with this position; however, the IRS clearly found in MAWC's favor. Thus, the Public Counsel's position appears to be in direct contradiction to the IRS's interpretation of its own Internal Revenue Code in Ruling 9.

The IRS requires a normalization violation to be corrected at the next available opportunity. The stipulation and agreement from MAWC ISRS 3 requires that MAWC file an AAO. The Commission sees no benefit to waiting for an AAO versus addressing the normalization violation in the present case. Making the adjustment in the current case allows for administrative economy, certainty for MAWC in its tax dealings with the IRS, and as the IRS has the power to retroactively revoke the PLR based on incorrect facts, the Commission will grant the request to relieve MAWC of its commitment to file an AAO pursuant to the stipulation and agreement in MAWC ISRS 3.

V. Conclusion

Based on Staff's and MAWC's adjustments, the updated ISRS calculation will result in MAWC collecting ISRS revenues in the amount of \$9,725,687. The Commission also concludes that the appropriate rate design is that which was testified to by Matthew J. Barnes and to which there were no objections.

MAWC has complied with the requirements of the applicable ISRS statutes to authorize its use of an ISRS. The Commission concludes that MAWC shall be permitted to establish an ISRS to recover ISRS revenues for this case in the amount of \$9,725,687. Since the revenues and rates authorized in this order differ from those contained in the tariffs MAWC first submitted, the Commission will reject those tariffs. The Commission will allow MAWC an opportunity to submit new tariffs consistent with this order.

Section 393.1015.2(3), RSMo, requires the Commission to issue an order to become effective not later than 120 days after the petition is filed. That deadline is June 30, 2020. To allow MAWC time to file a tariff sheet in compliance with this Order, the Commission will make this order effective in less than thirty days.

THE COMMISSION ORDERS THAT:

1. MAWC is authorized to change its ISRS sufficient to recover ISRS revenues in the amount of \$9,725,687. MAWC is authorized to file an ISRS rate for each customer class as described in the body of this order.

2. The tariff sheet filed by MAWC on March 2, 2020, and assigned Tariff Tracking No. YW-2020-0148, is rejected.

3. MAWC is authorized to file a new tariff sheet to recover the revenue authorized in this Report and Order.

4. As described in the body of this order, MAWC is relieved from the terms of the

Partial Stipulation and Agreement approved by the Commission in WO-2019-0389. This order shall become effective on June 27, 2020.



BY THE COMMISSION

A handwritten signature in black ink that reads "Morris L. Woodruff".

Morris L. Woodruff
Secretary

Silvey, Chm., Kenney, Rupp, Coleman, and
Holsman CC., concur.

Hatcher, Regulatory Law Judge