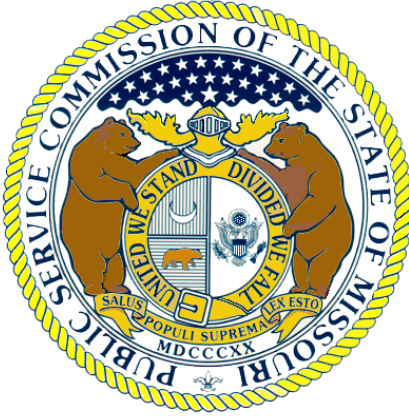


BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI



In the Matter of Petition of Missouri-American
Water Company for Approval to Establish an
Infrastructure System Replacement Surcharge
(ISRS).

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File No. WO-2018-0373
Tariff No. YW-2019-0018

REPORT AND ORDER

Issue Date: December 5, 2018

Effective Date: December 15, 2018

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

In the Matter of Petition of Missouri-American Water Company for Approval to Establish an Infrastructure System Replacement Surcharge (ISRS).)
) **File No. WO-2018-0373**
) **Tariff No. YW-2019-0018**
)

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, and **Ron Irving**, Legal Counsel, PO Box 360, 200 Madison Street, Jefferson City, Missouri 65102.

Office of the Public Counsel:

Lera Shemwell, Senior Public Counsel, and **John Clizer**, Associate Public Counsel, PO Box 2230, 200 Madison St., Ste. 650, Jefferson City, Missouri, 65102-2230.

Regulatory Law Judge: Charles Hatcher

REPORT AND ORDER

I. Procedural History

On August 20, 2018, Missouri-American Water Company (“MAWC”) filed an application and petition with the Missouri Public Service Commission (“Commission”) to establish an Infrastructure System Replacement Surcharge (“ISRS”).

MAWC requests to establish an ISRS rate to recover costs incurred in connection with infrastructure system replacements made during the period January 1, 2018, through September 30, 2018. The Commission issued notice of the application and provided an opportunity for interested persons to intervene. The Empire District Electric Company filed a *Motion to Intervene*, which it subsequently withdrew. No other parties sought to intervene. The Commission suspended the filed tariffs until December 18, 2018.

On October 19, the Staff of the Commission (“Staff”) filed its Recommendation and Memorandum proposing a number of corrections and adjustments to MAWC’s calculations. 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.

On October 29, MAWC filed a motion objecting to Staff’s recommendations. Also on October 29, the Office of the Public Counsel (“OPC” or “Public Counsel”) filed its response in support of the Staff Recommendation. The Commission held an evidentiary hearing on November 20. In total, the Commission admitted the testimony of six witnesses and 10 exhibits into evidence and took notice of a select prior Commission decision. Post-hearing briefs were filed on November 27, and the case was deemed submitted for the Commission’s decision on that date.¹

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

¹ “The record of a case shall stand submitted for consideration by the commission after the recording of all evidence or, if applicable, after the filing of briefs or the presentation of oral argument.” Commission Rule 4 CSR 240-2.150(1).

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 an investor-owned water utility providing retail water service to large portions of Missouri, and specific to this case, most of St. Louis County.²

2. MAWC is a “water corporation” and a “public utility”, as defined in Sections 386.020(59) and (43), and 393.1000(7), RSMo 2016.³

3. OPC “may represent and protect the interests of the public in any proceeding before or appeal from the public service commission.”⁴ The Public Counsel participated in this matter.

4. Staff is a party in all Commission investigations, contested cases and other proceedings, unless it files a notice of its intention not to participate in the proceeding within the intervention deadline set by the Commission.⁵

5. On August 20, 2018, MAWC filed a petition (“Petition”) for its St. Louis County service territory, requesting an ISRS to recover eligible costs incurred for infrastructure system replacements made during the period January 1, 2018, through July 30, 2018, initially filed with pro forma ISRS costs for August 1 through September 30 (“2018 ISRS Period”).⁶

6. The ISRS request exceeds one million dollars, but is not in excess of ten percent of the base revenue levels approved by the Commission in the last MAWC rate case.⁷

² MAWC’s Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, p. 2.

³ *Id.*

⁴ Section 386.710(2), RSMo 2016; Commission Rules 4 CSR 240-2.010(10) and (15) and 2.040(2).

⁵ MAWC’s Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice; Commission Rules 4 CSR 240-2.010(10) and (21) and 2.040(1).

⁶ Staff Recommendation, Appendix A, p. 1.

⁷ Section 393.1003.1, RSMo 2016; Staff Recommendation, Appendix A, p. 2.

7. This is MAWC's first ISRS filing since their most recent general rate case, File Number WR-2017-0285, *Report and Order* issued May 2, 2018, and *Order Approving Tariffs* issued May 15, 2018.⁸ As part of that general rate case, MAWC's existing ISRS was reset to zero.⁹

8. Water corporations are permitted to recover certain infrastructure system replacement costs outside of a formal rate case through a surcharge on its customers' bills.¹⁰ In conjunction with its Petition, MAWC filed a tariff sheet that would generate a total revenue requirement for MAWC's ISRS.¹¹ MAWC's proposed ISRS revenue requirement was later updated by MAWC to \$7,264,876.¹²

9. MAWC attached supporting documentation to its Petition for completed plant additions. This included documentation identifying the type of addition, utility account, work order description, addition amount, depreciation rate, accumulated depreciation, and depreciation expense.¹³ The company also provided estimates of capital expenditures for projects completed through September 2018, which were subsequently replaced with updated actual cost information and provided to Staff.¹⁴

⁸ Report and Order, *In the Matter of Missouri-American Water Company's Request for Authority to Implement General Rate Increase for Water and Sewer Service Provided in Missouri Service Areas, WR-2017-0285*, issued May 2, 2018; Order Approving Tariffs, *In the Matter of Missouri-American Water Company's Request for Authority to Implement General Rate Increase for Water and Sewer Service Provided in Missouri Service Areas, WR-2017-0285, et al.*, issued May 15, 2018.

⁹ Section 393.1006.6, RSMo 2016.

¹⁰ Sections 393.1000 to 393.1006, RSMo 2016.

¹¹ MAWC's Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendix B.¹² Staff Recommendation, Appendix A, p 3; Staff's Post-Hearing Brief, p. 4.

¹² Staff Recommendation, Appendix A, p 3; Staff's Post-Hearing Brief, p. 4.

¹³ MAWC's Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendices D, E, and F.

¹⁴ Staff Recommendation, Appendix A, p. 2; Direct Testimony of Brian W. LaGrand, p. 5.

10. MAWC's updated filing removed such items as: repairs to customer owned appliances and equipment; duplicate charges; installation of new service lines; and customer owned lead service line replacement costs.¹⁵

11. MAWC's supporting documents included an amount for Accumulated Deferred Income Taxes (ADIT).¹⁶ MAWC also included a proposed calculation for a Deferred Tax Asset relating to an assumed net operating loss ("NOL") for 2018 in the amount of \$9,577,697.¹⁷

12. 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. The amount of unused deductions is the NOL.¹⁸ An NOL is a tax return adjustment and not a regulatory item.¹⁹

13. On October 19, Staff submitted its *Staff Recommendation*. Staff's recommended revenue requirement is \$6,377,959.²⁰

14. Staff and MAWC are in agreement with the *Staff Recommendation* except on one issue, specifically whether there is an NOL, and, if so, what impact it may have on the ISRS.²¹

15. Staff recommended removing approximately \$9.3 million in Deferred Tax Asset²² from MAWC's ISRS calculations because it was not an NOL resulting from the

¹⁵ Staff Recommendation, Appendix A, p. 4.

¹⁶ MAWC's Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendix C.

¹⁷ MAWC's Petition to Establish an Infrastructure System Replacement Surcharge & Motion For Approval of Customer Notice, Appendix C. See also Direct Testimony of Lisa Ferguson at p. 3.

¹⁸ Ex. 3, Oligschlaeger Direct, p. 5.

¹⁹ Hearing Transcript, p. 78 (John Riley); Direct Testimony of John S. Riley, p. 2.

²⁰ Staff's Post-Hearing Brief, p. 4.

²¹ MAWC's Response to Staff's Recommendation, p.1-2. Staff's Post-Hearing Brief, p. 2 and footnote 2 (noting that \$9,272 removed by Staff should remain included).

²² The \$9.3 million figure is derived from the Net Operating Loss/Taxable Income of \$36.7 million as shown on Schedule BWL-1, p. 2 of the Direct Testimony of Brian W. LaGrand.

2018 ISRS Period.²³ This removal results in an \$866,917 reduction in recoverable ISRS costs.²⁴

16. Only costs directly associated with qualifying ISRS plant that became in-service during the nine months of the 2018 ISRS Period should be reflected in ISRS rates.²⁵

17. MAWC has an NOL carryover from prior years.²⁶

18. No net amount of net operating loss has actually been generated for income tax purposes by MAWC on an aggregate basis since January 1, 2018, the beginning of the 2018 ISRS Period.²⁷

19. The Internal Revenue Service (“IRS”) Private Letter Rulings cited by MAWC to support its position²⁸ address time periods in which the utility in question was generating NOL amounts.²⁹

20. MAWC did not generate any NOL in the 2018 ISRS Period.³⁰

21. MAWC projects that it will be able to reflect all of its net accelerated depreciation benefits associated with ISRS plant additions on its books during the next two years without the need to record any new offsetting NOL amount.³¹

22. MAWC’s NOL as of December 31, 2017, are currently reflected in MAWC’s base rates as a result of MAWC’s last general rate case, File Number WR-2017-0285, *Report and Order* issued May 2, 2018, and *Order Approving Tariffs* issued May 15, 2018.³²

²³ Staff Recommendation, Appendix A, p. 4.

²⁴ Staff’s Post-Hearing Brief, p. 4.

²⁵ Direct Testimony of Mark L. Oligschlaeger, p. 6; Direct Testimony of Lisa M. Ferguson, p. 6

²⁶ Hearing Transcript, p 48 (Brian LaGrand); Direct Testimony of John R. Wilde, p. 12; Direct Testimony of Lisa M. Ferguson, p. 5.

²⁷ Hearing Transcript, p. 90 (Mark Oligschlaeger); Direct Testimony of Lisa M. Ferguson, p. 6; Direct Testimony of John S. Riley, p. 3.

²⁸ Direct Testimony of John R. Wilde, Schedule JRW-2 through JRW-6, ; Private Letter Ruling are issued by the IRS to the taxpayer who requested it.

²⁹ Hearing Transcript, p. 90 (Mark Oligschlaeger).

³⁰ Hearing Transcript, p. 40 (John Riley); Direct Testimony of John Riley, p. 3; Direct Testimony of Lisa M. Ferguson, p. 7.

³¹ Direct Testimony of Mark L. Oligschlaeger, p. 7; Direct Testimony of Lisa M. Ferguson, p. 5-6; Direct Testimony of John R. Wilde, p. 13.

23. A taxpayer cannot utilize an NOL carryforward amount from a prior tax year without first exhausting all of the deductions available to it for the current tax year.³³

III. Conclusions of Law

MAWC is a “water corporation” and “public utility” as those terms are defined by Section 386.020, RSMo 2016.³⁴ MAWC is subject to the Commission’s jurisdiction, supervision, control, and regulation as provided in Chapters 386 and 393, RSMo. The Commission has the authority under Sections 393.1000 through 393.1006, RSMo, to consider and approve ISRS requests such as the one proposed in the Petition. Since MAWC brought the Petition, it bears the burden of proof.³⁵ The burden of proof is the preponderance of the evidence standard.³⁶ In order to meet this standard, MAWC must convince the Commission it is “more likely than not” that its allegations are true.³⁷

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.” Section 393.1000(1) defines “appropriate pretax revenues” to include “recognition of accumulated deferred income taxes and accumulated depreciation associated with eligible infrastructure system replacements which are included in a currently effective ISRS.”

³² Hearing Transcript, p. 87 (Mark Oligschlaeger); Direct Testimony of Lisa M. Ferguson, p. 5 and 7.

³³ Hearing Transcript, p. 68-69 (John Wilde).

³⁴ Unless otherwise stated, all statutory citations are to the Revised Statutes of Missouri 2016.

³⁵ “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.

³⁶ *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).

³⁷ *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).

IV. Decision

The issue presented in this case is whether MAWC should be allowed to reduce its ADIT to reflect an NOL. To address this issue, we must answer two questions: 1) is MAWC generating an NOL in the applicable 2018 ISRS recovery period; and 2) if it is generating an NOL, is that NOL associated with the replacements included in the proposed ISRS.

Is there an NOL for MAWC in 2018?

MAWC has not provided evidence to support that it will in fact have an NOL in 2018. On the contrary, the evidence indicates MAWC is generating more revenue for 2018 than it is generating expenses that qualify for deductions. Thus, MAWC is expected to utilize prior NOL carryovers to offset its taxable income in 2018 and 2019, but will not generate a new NOL. Since the IRS Private Letter Rulings only address periods where an NOL is generated, there is no legal support for MAWC's position that an exclusion of an NOL would violate normalization requirements of the IRS Code.³⁸

Because MAWC is expected to have taxable income in 2018, it is reasonable to conclude that MAWC is not generating an NOL during the 2018 ISRS Period at issue, either. And in fact, there was no evidence of an NOL being generated during the 2018 ISRS Period. In short, although the ISRS statute requires recognition of ADIT, which might include reflection of an NOL, we cannot allow MAWC to reduce its ADIT balance to reflect an NOL that does not exist.

If there is an NOL, is it associated with the replacements included in the currently effective ISRS?

Since there is not an NOL in the 2018 ISRS Period, the question of whether an NOL is associated with the proposed ISRS is moot.

³⁸ Hearing Transcript, p. 87, 89, 90, and 92. (Mark Oligschlaeger).

Based on Staff's adjustments to exclude the ineligible costs, the corrected ISRS calculation will result in MAWC collecting ISRS revenues in the amount of \$6,377,959. 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, however, for the reasons previously stated, the recovery should not include NOL. The Commission concludes that MAWC shall be permitted to establish an ISRS to recover ISRS surcharges for these cases in the amount of \$6,377,959. Since the revenues and rates authorized in this order differ from those contained in the tariffs the company 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 December 18, 2018, so the Commission will make this order effective on December 15, 2018.

THE COMMISSION ORDERS THAT:

1. Missouri-American Water Company is authorized to establish an Infrastructure System Replacement Surcharge ("ISRS") sufficient to recover ISRS revenues in the amount of \$6,377,959. Missouri-American Water Company 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 Missouri-American Water Company on August 20, 2018, and assigned Tariff Tracking No. YW-2019-0018, is rejected.

3. Missouri-American Water Company is authorized to file new tariffs to recover

the revenue authorized in this Report and Order.

4. This order shall become effective on December 15, 2018.



BY THE COMMISSION

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

Morris L. Woodruff
Secretary

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

Hatcher, Regulatory Law Judge

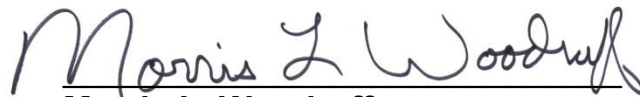
STATE OF MISSOURI

OFFICE OF THE PUBLIC SERVICE COMMISSION

I have compared the preceding copy with the original on file in this office and I do hereby certify the same to be a true copy therefrom and the whole thereof.

WITNESS my hand and seal of the Public Service Commission,
at Jefferson City, Missouri, this 5th day of December 2018.




Morris L. Woodruff
Secretary

MISSOURI PUBLIC SERVICE COMMISSION

December 5, 2018

File/Case No. WO-2018-0373

**Missouri Public Service
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Enclosed find a certified copy of an Order or Notice issued in the above-referenced matter(s).

Sincerely,



**Morris L. Woodruff
Secretary**

Recipients listed above with a valid e-mail address will receive electronic service. Recipients without a valid e-mail address will receive paper service.