Exhibit No. 310

OPC – Exhibit 310
Testimony of John S. Riley
Direct/Rebuttal
File No. WR-2024-0320

Exhibit No.: ____________
Issue(s): Adjusting Income Tax Calculations/ Cash Working Capital Adjustments/ Rate Case Expense/NOL in Rate Base/ Pre-Tax Rate of Return in WSIRA/ Tax Gross-up in Revenue Requirement
Witness/Type of Exhibit: Riley/Direct Rebuttal
Sponsoring Party: Public Counsel
Case No.: WR-2024-0320

DIRECT/REBUTTAL TESTIMONY

OF

JOHN S. RILEY

Submitted on Behalf of the Office of the Public Counsel

MISSOURI-AMERICAN WATER COMPANY

FILE NO. WR-2024-0320

** ______________________________ **
Denotes Confidential Information that has been redacted.

The information that is redacted in Public Counsel witness John Riley's direct testimony is redacted because another party has identified that information to be confidential in response to a discovery request. Rule 20 CSR 4240-2.135(5)(A).

December 6, 2024

PUBLIC

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DIRECT TESTIMONY

OF

JOHN S RILEY

CASE NO. WR-2024-0320

MISSSOURI AMERICAN WATER CO.

Q. What is your name and what is your business address?

A. John S. Riley, PO Box 2230, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am employed by the Missouri Office of the Public Counsel ("OPC") as a Utility Regulatory Supervisor.

Q. What is your educational background?

A. I earned a B.S. in Business Administration with a major in Accounting from Missouri State University.

Q. What is your professional work experience?

A. I was employed by the OPC from 1987 to 1990 as a Public Utility Accountant. In this capacity, I participated in rate cases and other regulatory proceedings before the Public Service Commission ("Commission"). From 1994 to 2000 I was employed as an auditor with the Missouri Department of Revenue. I was employed as an Accounting Specialist with the Office of the State Court Administrator until 2013. In 2013, I accepted a position as the Court Administrator for the 19th Judicial Circuit until April 2016 when I joined the OPC as a Public Utility Accountant III. I have also prepared income tax returns, at a local accounting firm, for individuals and small business from 2014 through 2017.

Q. Are you a Certified Public Accountant ("CPA") licensed in the State of Missouri?

A. Yes. As a CPA, I am required to continue my professional training by attending Missouri State Board of Accountancy qualified educational seminars and classes. The State Board of

Accountancy requires that I spend a minimum of 40 hours a year in training that continues my education in the field of accountancy.

Q. Have you previously filed testimony before the Missouri Public Service Commission?

A. Yes, I have. A listing of my case filings and certification is attached as JSR-D-1.

Q. What is the purpose of your direct testimony?

A. The purpose of this direct testimony is to adjust Missouri American Water Company's ("MAWC") income tax and rate case expense. I will also reduce the cash working capital balance ("CWC") as well as adjust rate base for the net operating loss carryforward ("NOLC" or "NOL"). I will also argue that a pre-tax rate of return is unnecessary when calculating WISRA revenues. Finally, I argue to eliminate the gross-up tax calculations that Staff performs to finalize the revenue requirement on Schedule 1 of the Accounting Schedules. All of these adjustments are due to the fact that MAWC does not owe a tax liability as a stand-alone company.

<u>ADJUSTMENTS TO NET INCOME TAX CALCULATIONS</u>

Q. What are you proposing to adjust in the income tax calculations?

A. The Company has failed to recognize MAWC specific impairments, retirements or gain/losses that have been recorded on the federal tax returns of American Water Works. These tax reductions should be recognized when performing the income tax calculations in the Staff accounting schedules.

Q. Could you provide some context to these impairments, retirements or gain/losses from sales of utility property?

A. Sooner or later, assets used in the course of providing utility service, will wear out, break down or be supplanted by better technology. These assets can be traded in, sold or merely

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discarded or retired. Often, this disposition is before the expected useful life is completed. Generally, any retirement or disposal prior to the asset being completely depreciated for tax purposes, will generate some sort of loss on the income tax return. Any loss recognition would be a deduction to taxable income.

Q. What would be the basis for recognizing these reductions?

A. These assets that have created these losses were funded by the ratepayer. The assets provided a rate of return to the Company as well as generated taxes, deferred and current that will never be paid to a taxing authority due to early removal. This was all funded by the ratepayer. It is only just and reasonable that the ratepayer receive a benefit from the tax deduction that occurs when the asset, that the ratepayer has funded, is retired prematurely. Ignoring the tax benefit allows the Company an unrecognized chunk of income and essentially increases the Company's rate of return beyond what the Commission authorized by way of excess income tax expense and unreturned deferred taxes. The ratepayer is due a refund.

Q. How does Staff normally calculate income tax for a general rate case?

A. Staff has a standard set of line items that is added to or deducted from a starting taxable income number. Additions are made to reclaim some nondeductible expenses and the straight-line depreciation. This total is the Additions to net income.

Next, Tax depreciation, interest on debt, nuclear decommissioning and preferred dividends are subtracted. This allows an offset between ratemaking depreciation and accelerated depreciation for tax purposes. This keeps the income tax calculations in-line with the IRS normalization rules that basically state that for income tax expense in rates, straight line depreciation is used, and for income tax on the consolidated tax returns, accelerated depreciation is applied.

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Q. This is the point in the tax calculations where you believe the retirement, abandonment or general dispositions should be considered as a decrease to taxable income?

A. Yes. This loss deduction, which is usually found on Form 4797, should be treated as a reduction to taxable income as it was on the consolidated tax return. This will lower the income tax expense applied to the test year and ultimately the entire revenue requirement calculation.

Q. How would you propose to calculate this adjustment?

A. By reviewing the Company workpapers and the yearly consolidated federal tax return, an annual amount can be calculated. The 2023 and 2022 tax returns indicate that Form 4797 had a loss of **______________________ ,** respectively. The average could be applied as an annual, normalized level and reduce taxable income, when computing income tax for rates, by **_________ **

<u>CASH WORKING CAPITAL ("CWC") ADJUSTMENTS</u>

Q. Could you provide a brief explanation of the components of a CWC calculation?

A. Yes. Borrowing from a standard Staff definition as follows:

> Cash Working Capital (CWC) is a rate base component that represents a measurement of the amount of funds, on average, required for the payment of a utility's day-to-day expenses, as well as an identification of whether a utility's customers or its shareholders are responsible for providing these funds in the aggregate.

In a CWC calculation, both a revenue lag and an expense lead/lag are measured. The "lag" is the amount of time, measured in days, that it takes revenues to come in from the customer or the time it takes for the utility to pay out an expense. MAWC has calculated a 48.7 day lag for revenues to come in from their customers. Customer payments are standardized so the revenue lag is a consistent multiplier in the calculation. In contrast, each expense component of the CWC calculation has a different payment schedule based on when the individual expense needs to be paid. As a result, the expense lag is different for each line item.

Q. What is your first adjustment to this rate base item?

A. The income tax expense lag should be adjusted to reflect the collection of, yet nonpayment of income tax for the entire 365 day year.

Q. What is the lag time that the Company is using for the income tax calculations?

A. Company is using a standard IRS quarterly tax payment lag of 35.6 days. This would be the normal timeframe <u>if</u> the Company actual is required to pay quarterly taxes, however, MAWC is not currently required to submit quarterly payments.

Q. What expense lag are you proposing for federal and state income taxes?

A. The income tax expense lag should be 365 days. MAWC is not in a position where it is liable for federal or state income tax. Income tax expense is collected but not paid out to a taxing authority. The Commission has ruled that an expense lag of 365 days represents the nonpayment of these taxes collected through rates yet not paid out.[1]

Q. What other adjustments to the CWC calculations are you proposing?

A. Mr. Walker III, who also performed the CWC calculations in the 2022 case, has made an interesting adjustment to his 2024 report. The revenue lag has been extended three additional days and the overall revenue lag is now 48.7 as opposed to 45.7 in the 2022 case. This lag time should revert to the previous 45.7 day time frame.

[1] Spire Missouri, CASE NO. GR 2021-0108, Amended R&O pages 27-31.

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Q. What is the main cause for this three day difference?

A. The billing lag, which is the time to prepare and mail out the bills after the meter has been read, was established to be 2 days in the 2022 rate case but has been extended to 5 days for this study. This delay is the root cause of the three day increase in the overall revenue lag.

Q. What could be the cause of this additional lag time?

A. It is hard to say. One would expect that the meter reading/billing time would be as efficient as the 2022 study given the fact that MAWC touts the remote reading ("AMI") meters as a leap forward in efficiency. With AMI meters, one could expect a speedier process. The usage information can be downloaded at night and be ready for dissemination to the customer by way of bill generation the next day. This additional 3 day delay would seem to be solely Company generated.

Q. What would the reset of the revenue lag back to 45.7 days do to the CWC balance?

A. The overall CWC balance adjusts from a Company generated negative $2,015,024 in rate base to a negative $4,223,270. An additional $2,208,246 reduction to rate base.

Q. What would the OPC adjustment be with the previous 45.7 revenue lag and the 365 day income tax expense?

A. The CWC balance to include in the rate base calculations should be a negative $21,567,773.[2] The difference to the Company's CWC balance is ($19,552,749). I should point out here that the income tax balance is a fluid number that will change until the final tabulation and calculation of the revenue requirement. Any CWC income tax adjustment will be a close approximation until the final calculations.

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[2] Fed income tax = ($15,176,965), State = ($2,672,452) with a 365 expense and a 45.7 revenue lag.

Q. Do you have any other revenue requirement adjustments that are related to CWC calculations?

A. Yes. I will be making an adjustment to rate case expense for the cost of the CWC study and the consulting fee from Mr. Walker. This outside generated study wasn't necessary.

Q. What would be the amount of the rate case expense adjustment?

A. The cost of the CWC study and Mr. Walker's consulting fee have not been provided yet due to the Company's failure to provide answers to my data request, in a timely manner. I will file supplemental testimony or include the actual adjustment in the next round of testimony when I have a reasonable idea of the cost involved.

Q. Why this particular disallowance in this case?

A. There was no Company testimony filed for CWC in either the 2015 or the 2017 case so my assumption is that the CWC was compiled in-house. A study was commissioned for the 2022 rate case, which pans out to at least seven years without a commissioned study. It may very well have been overdue by 2022 but why commission another CWC study for a case two years later? Creating a whole new study was unnecessary. The Company could just as easily put together a new CWC calculation, inhouse, by updating the balances. The revenue lag in the 2017 case was 45.60[3] which compares very favorably with the commissioned study in 2022 and would be spot on with the revenue lag in this case if the Company stuck to the more efficient billing lag of 2 days. Payment and collections methods should be getting more efficient, not less. If anything, one would expect a faster revenue lag due to credit card payments and electronic bill pay. I have not been able to find where the Commission ordered

[3] The calculated revenue lag was 46.44 but when the "lockbox float" is eliminated then the lag is very similar to 2022 of 45.7.

a new study and I don't see rapidly changing financial conditions to justify a study two years later.[4]

Q. Could you summarize the CWC issues?

A. First, the income tax lag: It was established by the Commission several years ago that an absence of an income tax liability necessitates a 365 expense lag. Second, reset the billing lag. There is no justification in testimony for the change in billing lag which is the root cause of the 3 day increase in the overall revenue lag from 2022 to now. Finally, rate case expense should be reduced by the cost of the CWC study and Mr. Walker's fee. This new study was unnecessary as the Company could very well have updated the 2022 balances and been as confident in the rate base as was apparently done in 2015 and 2017.

ELIMINATE NOL FROM EXCESS DEFERRED TAX CALCULATIONS

Q. Please explain the characteristics of a net operation loss ("NOL").

A. An NOL is a tax return item produced by taxable expenses exceeding taxable revenues, producing a loss on the tax return. For example: if XYZ, Inc. has taxable revenues of $1 million and taxable expenses of $2 million, then XYZ, Inc. has a NOL of $1 million to be carried forward to the next tax return ($1 million taxable revenue - $2 million in taxable expense = $1 million NOL). Losses accumulate so long as there is no taxable income to offset. If XYZ, Inc. loses $1 million in 2022, suffers a $2 million loss in 2023, and has taxable income in 2024 of $2 million, then, after the 2024 return is filed, XYZ, Inc. will have an NOL balance of $1 million. ($3 million balance less $2 million applied to the income.) The $1 million will continue to be carried forward until the Company has taxable income again to apply the NOL balance as an offset and is thus referred to as a net operating loss carryforward ("NOLC"). Companies argue that any NOLC balance should be an offset to the accumulated

[4] Case No. WR-2017-0285, direct testimony of Company witness Brian LaGrand stated that a lead/lag method to calculate its working capital requirements has been utilized by the Company for the last several cases. Page 25

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deferred income tax (" ADIT") balances that are included as a reduction to the rate base balance of a company. If included in this manner, the NOLCs reduce ADIT, thereby increasing rate base.

Q. Has MAWC included an NOLC in its rate base balance?

A. Initially, the Company indicated in the answer to OPC data request 1301 that there were no NOL balances included, however, in the response to 1306 it was outlined what was included in the excess deferred income tax balance (EADIT). Federal and State NOL balances which were incurred prior to the enactment of the Tax Cut and Jobs Act (TCJA) were included.

Q. Please explain how EADIT came to be.

A. The federal government spurs investment by providing tax incentives to companies so they will invest and provide economic development. Allowing a company to accelerate the depreciation of an asset creates a reduced tax liability situation putting more money in the company coffers to spend on assets. ADIT, which is Accumulated Deferred Income Tax is the collection of tax subsidies created by the difference between straight-line depreciation and tax return accelerated depreciation. This balance represents a liability because accumulated tax deferrals will eventually swing full circle and be paid back to the ratepayer. Before that happens, though, the increase in income tax expenses used on a tax return (as compared to what was included for ratemaking purposes) provides an interest free loan to the utility in the form of a temporary tax break. Example: Straight-line depreciation for ratemaking is $100. For tax purposes the company can apply $200. This $100 difference represents a deferred income tax of $21 after applying the 21% corporate tax rate ($100 X 21% = $21). How is this $21 funded? The ratepayer pays taxes as if there is no accelerated depreciation which allows the company to claim the $21 windfall. This balance accumulates so long as the accelerated depreciation is greater than the straight-line. So, for this example, five years of accelerated depreciation would be $105 in ADIT. The tax benefits are applied in the early years while tax payback happens many years down the road meaning that the ratepayers have effectively loaned the company $105 without interest by the grace of the federal government.

If the tax rate is reduced while there is an ongoing ADIT balance, then the new reduced rate essentially puts some tax liabilities in limbo. The effected ADIT balance is referred to as excess accumulated deferred income tax ("EADIT"). For almost all companies currently in operation, any EADIT on their books was generated by the 2017 TCJA which changed the tax rates from the 38% to 21%. Deferred taxes collected at 38% will now be paid back at 21%. Returning to the example, above, the amount of the EADIT can be calculated by subtracting the ADIT at the lower tax rate from the ADIT that would have been generated at the higher tax rate. $100 x 38% = $38, $100 x 21% = $21. A $17 difference which won't be returned to the ratepayers if the Commission doesn't recognize the lost difference. The Commission set up an Excess Deferred Income Tax balance. The orphaned $17 was placed in the EADIT balance. In our example, there is still $38 of deferred tax, however, it is now split between the new ongoing ADIT balance of $21 and the $17 EADIT. Both balances are amortized so the ratepayer who financed the deferred taxes will eventually receive its funding returned.

Q. What are the similarities and differences between an NOL and ADIT?

A. The IRS maintains that ADIT or EADIT created by accelerated depreciation must be amortized over the life of the asset. Therefore, if a 50-year asset created $1,000 in ADIT, that $1,000 would be amortized over 50 years and thus would cause an amortization of $20 a year ($1,000/50 years = $20 per year). ADIT is asset specific and is driven by accelerated depreciation where as an NOL is tax return driven by way of adding <u>all</u> taxable revenues and offsetting them with <u>all</u> taxable expenses. Often, an NOL is created by the combination of tax breaks, accelerated depreciation being the most prevalent.

The IRS demands that ADIT be amortized over the life of the asset so that the tax break does not immediately get returned by flowing the break right back through rates. ADIT represents the tax <u>adjusted</u> balance of accelerated depreciation. The $100 from my example is tax adjusted to $21 and that is the adjustment to rate base. An NOL is a dollar amount difference between taxable revenue and expenses. It does not get amortized, and, for tax return application, it does not get tax adjusted. Back to our examples, $100 in taxable income less $200 in expense creates a $100 tax loss. If you find the section of MAWC's consolidated tax return that tracks the ongoing total operating losses, you will find it to be an unadjusted $100 not $21. The reason the NOLC are displayed as unadjusted is because the creation of or the application of an NOL is not affected by income tax rates. Further, as already explained NOLs are carried forward and do not get amortized. NOLs accumulate until the company has a tax return that produced taxable income and then a portion of the NOL is applied to the taxable income. For ratemaking purposes, an NOL is considered a deferred tax asset because it can be applied to a possible tax liability and offset it.

Q. Are you taking issue with the Company including an NOLC in the EADIT balance adjusting rate base?

A. Yes. The way the Company has calculated its EADIT in a way that suspended the use of the NOL and amortized it within the EADIT balance. I contend that the NOL in question no longer exists and the EADIT balance should be uninhibited by a fictitious deferred tax asset.

Q. What is the amount of the adjustment?

A. I have attached the Company EADIT workpaper as Schedule D-02. The NOL balances that have been amortized from Jan. 2018 to the end of 2024 amount to $21,371,624. The EADIT balance should be adjusted by the $21 million to correct the inclusion.

Q. You had mentioned that the NOL consumption was suspended. Could you please explain?

A. As I pointed out previously, an NOL is not amortized, it sits until needed. If the company is in a profitable situation, there isn't a choice as to foregoing the use of the NOL. It is applied to the net income. My point here is that American Water Works had an overall consolidated net income in at least 2017 through 2021. This is the same timeframe as the creation of the EADIT with NOLCs included. Due to a corporate Tax Allocation Agreement ("TAA"), those profits would have consumed the corporation's overall NOL balances. MAWC has stated that it did not intend to include an NOL balance in rate base[5], however, it chose to include NOL balances in the EADIT and amortize it like the deferred liability. This is an incorrect methodology for two reasons. The first is that NOLs are not amortized and secondly, the profits of 2017 through 2021 would have reduced these possible NOL balances to zero.

Q. Could you summarize your position concerning NOL balances within the EADIT rate base component?

A. If the Company didn't intend to include an NOLC in rate base, why try to slide questionable balances in the EADIT? It appears that the consolidated corporation allocated all of its available NOL balances during the 2017-2021 timeframe so the NOLC included in the EADIT balances doesn't exist. The rate base should be decreased by $21,371,624.

<u>REDUCE THE PRE-TAX RATE OF RETURN IN WSIRA</u>

Q. Could you provide an overview of the WSIRA process?

A. The water and sewer infrastructure rate adjustment ("WSIRA") is an interim rate adjustment that allows costs related to the replacement of water pipe (infrastructure) to be summarized and added to the company's rate base. A rate of return is calculated on the additional rate base and included in the WSIRA revenue requirement. These proceedings and revenue requirement additions are conducted in between general rate cases.

[5] MAWC's answer to data request 1301S

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Q. What is the adjustment you are proposing?

A. My proposal is for the Commission to calculate WSIRA revenues using only the standard rate of return that is established in the general rate case and not using a "pre-tax rate of return."

Q. Does the Commission normally apply what is referred to as a "pre-tax rate of return?"

A. Yes, in some form or another. That is the established rate of return with a calculated tax amount built into the percentage. If the rate of return for the general rate case is 7.74%, then dividing the rate by an inverse of the applicable corporate tax rate (1-tax rate (23.84%)) would make the pre-tax rate of return 10.16%. In WSIRA cases, the Commission applies this adjusted rate to the rate base or else Staff calculates the taxes using the composite tax rate. The Commission applies tax because the statute states that "Appropriate pretax revenues" should consider income taxes, depreciation and property taxes in order to produce net operating income. What the Commission has overlooked, however, is the fact that MAWC does not have a tax liability. Therefore, it is not necessary to calculate a tax on the interim revenues generated by the WSIRA simply because there are no "taxes applicable" to the revenues. To put the matter simply, because the Company pays no taxes, the appropriate pretax revenue required by the statute does not need to include any taxes so there is no reason to utilize a "pre-tax" rate of return (which is just a way of including taxes in the rate of return).

Q. If taxes are not included in the interim WSIRA cases, when would they be calculated?

A. The proper tax calculations will be performed on the combined revenues in the next general rate case. In order to produce the proper net operating income, depreciation and property taxes are the only expenses that should be addressed prior to the next general rate case.

Q. What is the effect of the Commission including income taxes in the WSIRA calculations?

A. Essentially, the Company is afforded a rate of return over and above the established rate from the last rate case. Look at it this way. If the Commission applies tax to the WSIRA revenues

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with no tax due, then the tax is now nothing more than additional revenues (profit). The operating income is actually more than the Commission allowed because the tax expense becomes additional income.

Q. How is that different than income tax calculated and included in revenue requirement of a general rate case knowing that the Company will never pay the taxes to the government?

A. First off, per the IRS code, income taxes have to be calculated and applied in a general rate case to prevent the dreaded normalization violation. That is the IRS determination. Why is it different for an interim rate case? The whole point of a WSIRA is to defeat regulatory lag. That objective has been accomplished. But there is no lag on income taxes in the interim because there aren't any due. The revenues that were developed in the WSIRA don't have an income tax liability that has to be calculated in the interim. The WSIRA revenues will be included and taxed in the next general rate case.

Q. Could you summarize your WSIRA income tax argument?

A. The Commission should not add income tax expense to the WSIRA revenue calculations due to the absence of a current tax liability. Including additional revenues to cover nonexistent taxes amounts to an increase over the stated rate of return. The taxes that must be calculated and collected on these revenues will be managed in the next general rate case.

TAX GROSS UP ON THE REVENUE REQUIREMENT

Q. What adjustment to the overall revenue requirement are you proposing?

A. Due to the Company's NOL position, the Company is not in a situation where additional income taxes need to be calculated to sustain the Commission's established return on equity. In simple terms, the tax gross up does not need to be applied to the income tax calculations when determining the revenue requirement that should be ordered by the Commission.

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Q. Please explain what a tax gross-up is and how it applies in a rate case.

A. A tax gross-up is an additional amount of money added to a utility's revenue requirement to cover the income taxes that the utility will owe on its revenue requirement. In a rate case, the Commission sets the revenue requirement for the utility. This is essentially done by multiplying the utility's rate base by the ordered rate of return ("ROR") and then adding in non-capital expenses and taxes. The Commission's staff then calculates what the Company is currently making with its existing rates and determines how much additional net income is required to raise the Company's income to the established Rate Base/ROR level. This additional income is generally referred to as the "revenue requirement." To illustrate, let's use an example of a $250,000 operating income requirement and a Commission staff accounting schedule that calculates the current utility income at $150,000. This would point to a $100,000 shortfall, so the Schedule lists a $100,000 in additional net income is needed to reach the total net operating income requirement. It's important to understand that the Commission has established this income to be the Company's total cost of operations (including profit), and that amount would be <u>net</u> of taxes. That means that taxes have already been included in this amount. However, per the IRS, income taxes must also be applied to the additional $100,000 revenue requirement because the $100,000 additional income is, in itself, additional taxable revenues. Therefore, it becomes necessary to determine how much more income is necessary to cover the taxes owed on the additional income that the Company will need to continue its operations (including pay the additional taxes). This additional income included to cover the taxes owed on the increased revenue the Company needs (which includes the amounts needed to pay taxes) is the tax gross-up. Stated simply, it is the tax calculated on a tax.

The established composite tax rate (federal and state tax rates combined) is 23.84%. To calculate the tax on tax, a nifty formula was created to produce a single multiplying factor to determine how much income tax should be included in the cost of service.

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The current gross-up factor is 1.313. 1/1- (tax rate)

1/ (1-238401285)
1/ (.761598715)
= 1.313027425

So, the calculated tax on a given addition to the revenue requirement would be $100,000 X 1.313 = $131,302.74 or an additional tax of $31,302.74. The straight tax calculation is $100,000 multiplied by the composite tax rate of 23.84% to produce $23,840 in tax.

Q. What changes are you proposing to the calculations you demonstrated earlier?

A. Because MAWC's tax obligation is zero, the tax calculation should be just a simple composite tax of 23.84%, not a 1.313 gross-up.

Q. Are these tax calculations required by the IRS?

A. No. The IRS does require that the tax calculations for a utility rate case must avoid using accelerated depreciation in order to avoid the dreaded normalization rule violations. However, the Staff accounting schedules already apply straight-line depreciation to the income tax schedule, so accelerated depreciation is not used. There is no additional requirement that the Commission ignore the reality that the accelerated depreciation has put the Company in a net operating loss position when calculating what, if any, amount of tax gross-up is required.

Q. Are you proposing that Staff apply 23.84% to the "additional Net Income Required" instead of the 1.313 that is built into the calculation?

A. For MAWC, who is in an NOL situation and isn't required to pay taxes, I am. Referring back to my $100,000 example, the point of a gross-up is to make the Company whole in regard to

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the $100,000 addition.[6] The IRS required tax to be collected on the $100,000 additional income but the Company doesn't owe any additional tax (tax on tax) to make its $100,000 income addition whole. Therefore, no tax gross-up needs to be performed.

Q. Please summarize this issue.

A. The whole point of a tax gross-up is to satisfy the cost of the tax on tax that is created by the original income tax calculation. A Company that is not in a taxable situation does not need a gross-up to make its required ROR whole.

Q. Does this conclude your direct testimony?

A. Yes.

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[6] The Commission grants the Company an additional $100,000 profit, not $100,000 less the taxes. To keep the $100,000 intact, the taxes will need to be collected from the ratepayer.

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Missouri-American Water Company's Request for Authority to Implement a General Rate Increase for Water and Sewer Service Provided in Missouri Service Areas	))))	Case No. WR-2024-0320

AFFIDAVIT OF JOHN S. RILEY

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

John S. Riley, of lawful age and being first duly sworn, deposes and states:

1. My name is John S. Riley. I am a Utility Regulatory Supervisor for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my direct/rebuttal testimony.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

John S. Riley
Utility Regulatory Supervisor

Subscribed and sworn to me this 5th day of December 2024.

TIFFANY HILDEBRAND
NOTARY PUBLIC - NOTARY SEAL
STATE OF MISSOURI
MY COMMISSION EXPIRES AUGUST 8, 2027
COLE COUNTY
COMMISSION #15637121

Tiffany Hildebrand
Notary Public

My Commission expires August 8, 2027.