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Witness: Mark L. Oligschlaeger

Sponsoring Party: MoPSC Staff

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MISSOURI PUBLIC SERVICE COMMISSION
FINANCIAL AND BUSINESS ANALYSIS DIVISION

REBUTTAL TESTIMONY
OF
MARK L. OLIGSCHLAEGER

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WO-2020-0190

Jefferson City, Missouri
May 2020

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1 Service (“IRS”) supports MAWC’s prior claims that the Commission’s ordered ratemaking
2 treatment of NOLs in prior Infrastructure System Replacement Charge (“ISRS”) cases
3 constitute violations of the IRS Code’s normalization provisions. Mr. Riley bases this argument
4 on contentions that MAWC did not request the “right” rulings from the IRS regarding the
5 Commission’s prior NOL decisions, and that the PLR assumes contradictory facts when
6 compared to prior Commission ISRS case orders and court decisions affirming the
7 Commission’s orders.

8 Q. In light of OPC’s stance in this case, please summarize the primary disagreement
9 among the parties in recent MAWC ISRS cases that the Commission, the courts, and ultimately
10 the IRS has been asked to decide.

11 A. In these cases, MAWC has argued that an amount of NOL must be used to offset
12 rate base in ISRS proceedings due to its claim that a “tax loss” occurs within the ISRS period
13 due to failure to collect ISRS revenues from customers concurrently with the addition to rate
14 base of ISRS plant additions. Staff and OPC disagreed with this claim, largely due to
15 uncontroverted evidence that MAWC’s overall NOL carryforward (“NOLC”) amounts were
16 estimated to decrease during the ISRS periods, thus showing no actual amount of NOL was
17 generated by MAWC during the ISRS periods, or was being reflected on its books. MAWC
18 responded to this argument by claiming that the alleged tax loss associated with ISRS plant
19 additions reduced its ability to use prior NOL amounts to offset taxable income going forward,
20 thus in MAWC’s view implicating the IRS Code normalization requirements.

21 The Commission ruled in Staff’s and OPC’s favor on this issue. While MAWC has
22 appealed these decisions, those orders have been affirmed to date by the courts.

1 In contrast, in its recent PLR the IRS has agreed with MAWC’s position that it incurred
2 a tax loss during the ISRS periods in prior cases due to the addition of ISRS plant, and that this
3 loss must be reflected in ISRS rates due to the IRS Code’s normalization requirements.

4 Q. Is Mr. Riley correct in stating at page 2, lines 14 – 21 and again at page 4, line
5 24 through page 5, line 7 of his direct testimony that the PLR is in conflict with prior
6 Commission orders and court proceedings?

7 A. Yes. From the standpoint that the IRS agreed that MAWC experienced a “tax
8 loss” with respect to ISRS expenditures, the PLR conflicts with past Commission orders.
9 However, the relevance of that conflict is not apparent due to differences between the roles of
10 utility regulators, appellate courts, and the IRS.

11 The Commission is empowered by statute to set rates for jurisdictional utilities,
12 including the component of rates intended to recover income tax expenses. The courts are
13 empowered to make rulings regarding whether the Commission carried out those obligations in
14 a lawful fashion.

15 However, the IRS is the agency designated to interpret its Code and to determine
16 whether the actions of taxpayers (and, for regulated utilities, the actions of its regulators) are in
17 compliance with the IRS Code. At MAWC’s request, the IRS has done so in this case. And,
18 while the IRS certainly has no direct power to set utility rates, the consequences of violating
19 the IRS Code in respect to the normalization requirements are of sufficient gravity to command
20 the attention of all parties to Commission proceedings, and the Commission itself in regard to
21 tax normalization issues in rate proceedings.

1 Q. What “requests for rulings” did MAWC recently make of the IRS?

2 A. MAWC made twelve separate requests for rulings, most connected to
3 appropriate treatment of NOLs in ISRS cases, in order to stay in compliance with the IRS
4 normalization requirements. These are listed in the PLR attached to Mr. Wilde’s testimony
5 (Schedule JRW-2) at pages 9 – 12 of 23.

6 Q. In his direct testimony, Mr. Riley generally alleges that MAWC did not ask the
7 IRS to rule on what he considers the key question in past ISRS cases; i.e., did an NOL exist in
8 the context of previous MAWC ISRS cases. Is he correct?

9 A. Mr. Riley is correct that no specific question was asked of the IRS using that
10 wording. However, in Staff’s view Mr. Riley does not sufficiently capture the fundamental
11 issue before the Commission in prior MAWC ISRS cases.

12 Q. Why do you say that?

13 A. In Staff’s perspective, and supported by the language in the Commission Orders
14 in Case Nos. WO-2018-0373 and WO-2019-0184, the key questions facing the Commission
15 were: (1) was an NOL generated during the ISRS periods in those cases and, if so, (2) was any
16 of that NOL amount attributable to ISRS plant additions made during that period? Staff and
17 OPC took the position that no NOL amount was generated during the ISRS periods for MAWC,
18 from ISRS plant additions or any other kind of plant additions. The Commission agreed with
19 Staff and OPC in these cases.

20 Q. Did the IRS rule on these questions in its PLR?

21 A. Yes. Within the PLR, it is clear to Staff that the IRS expressed agreement with
22 MAWC’s contentions that an NOL was generated during the ISRS periods at issue due to ISRS

1 plant additions, and that the NOL amount applicable to ISRS plant additions should be
2 determined using the so-called “with-and-without” method.

3 Q. Citing to the PLR itself, why does Staff take the position that the IRS agreed
4 with some of the arguments made by MAWC in prior ISRS cases?

5 A. Within the PLR (Schedule JRW-2, page 7 of 23), in the section entitled “Facts,”
6 the following language appears:

7 In the course of the Surcharge case, Taxpayer and other participants in
8 the proceeding analyzed the expenditures for which Taxpayer sought
9 recovery via the surcharge and debated the proper regulatory treatment
10 of Taxpayer’s NOLC and tax loss incurred through the rate base
11 determination date of the Surcharge case with respect to the costs
12 incurred that are recoverable in the Surcharge case. The revenue
13 requirement approved in the Commission’s order issued on Date 1 was
14 lower than the revenue requirement sought by Taxpayer and is entirely
15 attributable to the differing ADIT calculations with respect to the NOLC
16 and the resulting effects on rate base and allowed return. The approved
17 revenue requirement in the surcharge case was based on a rate base
18 computation that reflects the gross ADIT liabilities associated with
19 depreciation-related and repair-related book/tax differences, **but did not**
20 **reflect an ADIT asset for any portion of the Taxpayer’s NOLC as of**
21 **the date that rate base was determined (Date 9), including the tax**
22 **loss resulting from the infrastructure expenditures addressed in the**
23 **Surcharge Case.** [Emphasis added.]

24 Later, on the same page of the PLR:

25 ...As of the date of the rate base determination, **none of the surcharge**
26 **revenues had been billed to customers, and, thus, as of this date a**
27 **taxable loss of approximately \$ε had been incurred in respect to the**
28 **plant-related expenditures with rates set by the Surcharge Case.**
29 [Emphasis added.]

30 The bolded language indicates the IRS chose to accept MAWC’s claims that the inability of
31 MAWC to capture customer revenues for ISRS plant additions prior to the ordering of new
32 ISRS rates caused a tax loss for the utility. Understanding this point is necessary to interpret
33 the IRS language adopting MAWC’s requested ruling 9.

1 First, the language in MAWC's requested ruling 9 is as follows:

2 Taxpayer requests that the Service also rule: in order to comply with the
3 normalization method of accounting within the meaning of Section
4 168(i)(9), the amount of depreciation-related ADIT reducing rate base
5 used to determine the revenue requirement set in the Surcharge Case
6 must be decreased to reflect a portion of the NOL for the test period for
7 the Surcharge Case that would not have arisen had Taxpayer not reported
8 depreciation-related book/tax differences during the test period of the
9 Surcharge case and such decrease in depreciation-related ADIT must be
10 an amount that is no less than the amount computed using the With-and-
11 Without method. (Schedule JRW-2, pages 10 – 11 of 23).

12 Within the PLR the IRS granted MAWC's request for ruling 9 using the same language
13 suggested by MAWC above, at page 21 of 23 of Schedule JRW-2.

14 Further underscoring the IRS' acceptance of requested ruling 9, the PLR states the
15 following in respect to requested ruling 10, which had been posed by MAWC as an alternative
16 to granting ruling 9:

17 Ruling request 10 is moot because we grant ruling 9 in accordance with
18 Taxpayer's analysis. (Schedule JRW-2, page 21 of 23).

19 Q. Having reviewed the PLR in detail, is there serious doubt in your mind that the
20 IRS effectively found the Commission's prior actions in MAWC ISRS proceedings to
21 constitute violations of its normalization provisions?

22 A. No. Staff believes the IRS was sufficiently clear in the PLR on this
23 particular point.

24 Q. In his direct testimony, at page 3, line 14 through page 4, line 14, Mr. Riley
25 argues that the PLR seems to accept as fact MAWC's assertions regarding the existence of an

1 NOL in prior ISRS periods as opposed to making an independent determination that such an
2 NOL existed. Does Staff agree with this characterization?

3 A. The PLR does appear to accept that an NOL existed in prior ISRS periods.
4 However, it is not clear what practical difference Mr. Riley's assertion is supposed to make.
5 While the PLR does not necessarily provide any evidentiary support or extensive explanation
6 for the basis for the IRS' conclusions and rulings, it is quite clear that the IRS views an NOL
7 to be applicable to MAWC's past ISRS cases, and that the NOL must be recognized in some
8 fashion in order to comply with the IRS Code's normalization requirements.

9 Q. Was Staff asked to provide input into MAWC's PLR request?

10 A. Yes, as discussed in Mr. Wilde's direct testimony. Staff's understanding is that
11 input from a utility's primary regulator regarding the relief sought is a standard part of the
12 PLR process for regulated companies.

13 Q. In its comments, did Staff address the question of whether an NOL was
14 generated during prior MAWC ISRS periods, and whether ISRS plant additions gave rise to
15 any such amounts at that time?

16 A. Yes. Staff provided a detailed explanation and justification for Staff's positions,
17 and those reflected in Commission orders regarding these matters. Staff's comments can be
18 found in their entirety in Schedule JRW-1 attached to Mr. Wilde's testimony, pages 118 - 128.

19 Q. Did the IRS take the Staff's comments into consideration in issuing the PLR?

20 A. I cannot say for certain. Other than noting that Staff did file comments that were
21 attached to MAWC's PLR request, there is no discussion within the PLR regarding those
22 comments or why the IRS chose not to rely on them.

1 Q. Please summarize your testimony rebutting Mr. Riley's direct testimony in
2 this proceeding.

3 A. Since Case No. WO-2018-0373, MAWC has raised the possibility that the
4 Commission's actions regarding the purported existence of an NOL might not be in compliance
5 with the IRS Code's normalization restrictions. When Staff, OPC, and finally, the Commission,
6 disagreed with these assertions, MAWC took the step of seeking clarification from the IRS
7 through the PLR process as to whether the normalization restrictions were, in fact, being
8 violated. While Staff may sympathize with OPC's frustration regarding the less than clear
9 language in parts of the PLR, and with the lack of support for the IRS' findings within the
10 document, Staff nonetheless finds the language in the PLR to be adequate in demonstrating
11 IRS support for the applicable contentions made by MAWC in recent ISRS cases.

12 As a result, Staff recommends that the Commission take the prudent and reasonable
13 action in the specific circumstances of this case of increasing MAWC's ISRS revenue
14 requirement by approximately \$35,000 in order to resolve any potential adverse consequences
15 from disregarding the IRS' guidance in this matter.

16 **RESPONSE TO MAWC**

17 Q. What aspects of Mr. Wilde's direct testimony do you disagree with?

18 A. Within his testimony, at page 11, line 14 through page 12, line 6, Mr. Wilde
19 states that the IRS' language concerning ruling 8 and ruling 9 support MAWC's position
20 regarding calculation of ADIT in this and past ISRS proceedings. Staff disagrees with
21 Mr. Wilde's assertion regarding ruling 8.

22 Q. What is ruling request 8?

1 A. As shown in the PLR (page 10 of 23, Schedule JRW-2), MAWC's request reads:

2 ...Taxpayer requests that the Service also rule: in order to comply with
3 the normalization method of accounting within the meaning of Section
4 168(i)(9), the amount of depreciation-related ADIT reducing rate base
5 used to determine the revenue requirement set in the Surcharge case is
6 limited to the amount of depreciation-related deferred tax expense
7 recovered in rates as of the Surcharge Case rate base determination date.

8 The IRS granted MAWC's request for ruling 8 using the same language as shown above
9 (Schedule JRW-2, page 21 of 23).

10 Q. Please explain Staff's interpretation of what MAWC was seeking through its
11 requested ruling 8.

12 A. In regard to ruling 8, Staff stated the following in its comments attached to
13 the PLR:

14 ** _____
15 _____
16 _____
17 _____
18 _____
19 _____
20 _____
21 _____
22 _____ ** (Schedule JRW-1, page 119).

23 While Staff is not totally certain what MAWC was intending to accomplish through requesting
24 ruling 8, ** _____

25 _____
26 _____

27 _____ .** If accepted, this interpretation would be a fundamental

_____ ¹ While MAWC's request for ruling 8 in the PLR is stated in reference to single-issue rate proceedings only, the logic of MAWC's request could also apply to general rate proceedings.

1 change to the standard ratemaking process used in both ISRS cases and general rate proceedings
2 in this jurisdiction for many years, including multiple MAWC ISRS and MAWC general rate
3 cases. For MAWC to argue at this juncture that this standard ratemaking practice somehow
4 conflicts with normalization restrictions that have also been in place for decades strikes Staff
5 as, frankly, incredible.

6 Q. Does Staff take the position that ruling request 8 should lead the Commission to
7 change its ratemaking policies in ISRS or other cases now or in the future?

8 A. No, for two reasons: (1) the underlying issue has never been brought to the
9 Commission by MAWC for its consideration; and (2) the language used in ruling 8 by the IRS
10 is extremely vague in any case.

11 Q. Please explain your first point.

12 A. Unlike the NOL issue that has been before the Commission in multiple prior
13 ISRS cases, MAWC has never taken any position before the Commission in ISRS cases that
14 the traditional method of reflecting ADIT in rate base for plant additions posed any
15 normalization violation concerns whatsoever. Staff only became aware of this argument during
16 the latter stages of MAWC's drafting of the PLR request, and had very limited time to respond
17 to this new argument in its comments to the IRS. As a routine matter, copies of relevant
18 materials from prior Commission proceedings are included in utility PLR requests, which at the
19 very least suggests that the IRS believes that access to the Commissions' evidentiary record for
20 the issues before the IRS is important in order to understand and assess the arguments of the
21 parties regarding the IRS Code. However, no such evidentiary record from this Commission
22 exists at all in regard to ruling 8. As a matter of procedural fairness, MAWC should have
23 presented its concerns on this point to the Commission in the recent ISRS proceedings, and then

1 asked for a PLR to seek clarification from the IRS if the Commission’s decision legitimately
2 raised issues of compliance with the normalization requirements.

3 Q. Did Staff address this particular point with the IRS in its comments
4 regarding ruling 8?

5 A. Yes, as follows:

6 ** _____
7 _____
8 _____
9 _____
10 _____
11 _____ ** (Schedule JRW-1, page 119).

12 Q. Notwithstanding the procedural objections you have as to how MAWC
13 presented this issue to the IRS, does Staff believe there is any theoretical merit behind
14 MAWC’s request for ruling 8?

15 A. Not at all. The Staff’s comments in full regarding ruling 8 can be found at
16 pages 119 – 121 of Schedule JRW-1, attached to Mr. Wilde’s direct testimony.

17 Q. Why do you state that the language in the PLR regarding ruling 8 is vague
18 and ambiguous?

19 A. The language in the PLR states that the deduction for ADIT associated with
20 accelerated depreciation timing differences in ISRS cases should be limited to the amount of
21 deferred tax expense that was “recovered in rates” as of the rate base determination date. It is
22 a fundamental premise of both financial reporting and regulatory accounting for utilities that a
23 cost does not have to be directly included in a rate calculation in order to be considered to be
24 “recovered in rates” at a subsequent time. The suggestion that the normalization provisions in

1 the IRS Code should, after many years, be interpreted in a directly contrary manner to normal
2 financial and regulatory accounting standards is certainly both novel and odd.

3 For this reason, much greater clarity should be required of MAWC of what the term
4 “recovered in rates” actually means before the very vague wording in the PLR can be reasonably
5 argued to mandate changes to the Commission’s long-held ratemaking practices.

6 Q. If MAWC desires its ISRS rates or base rates to be calculated using its
7 interpretation of ruling 8, how should it proceed?

8 A. MAWC should present this position directly to the Commission, both justifying
9 the change to historic treatment of ADIT on its own terms and, if applicable, argue that such
10 change is necessary to comply with the IRS’ normalization restrictions. For the reasons stated
11 above, the language in the PLR regarding ruling 8 should not be considered sufficient to
12 mandate a change in the Commission’s ratemaking practices.

13 Q. Does this conclude your rebuttal testimony?

14 A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

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

Case No. WO-2020-0190

AFFIDAVIT OF MARK L. OLIGSCHLAEGER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

COME NOW Mark L. Oligschlaeger and on his oath declares that he is of sound mind and lawful age; that he contributed to the foregoing *Rebuttal Testimony*; and that the same is true and correct according to his best knowledge and belief, under penalty of perjury.

Further the Affiant sayeth not.

/s/ Mark L. Oligschlaeger
Mark L. Oligschlaeger