Exhibit No.:	
Issues:	Income Tax Calculations
Witness:	Linda Schlessman
Exhibit Type:	Direct
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2025-0345
Date:	December 30, 2025

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2025-0345

DIRECT TESTIMONY

OF

LINDA SCHLESSMAN

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, Linda Schlessman, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am the Director of Tax - Regulatory for American Water Works Service Company, that the accompanying testimony has been prepared by me or under my direction and supervision; that if inquiries were made as to the facts in said testimony, I would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of my knowledge and belief.

Linda Schlessman

____
Linda Schlessman

December 30, 2025
Dated

DIRECT TESTIMONY
LINDA SCHLESSMAN
MISSOURI-AMERICAN WATER COMPANY
CASE NO.: WR-2025-0345

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DIRECT TESTIMONY

LINDA SCHLESSMAN

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Linda Schlessman. My business address is 1 Water Street, Camden, NJ 08102.

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

A. I am employed by American Water Works Service Company, Inc. as the Director - Tax Regulatory. I am responsible for the oversight of calculating tax expense and accumulated deferred income taxes in rate cases and rate filings for American Water Works, Inc.'s subsidiaries, including Missouri-American Water Company ("MAWC" or the "Company").

Q. Please summarize your educational background and business experience.

A. I received a Bachelor of Business Administration Degree in Accounting from Miami University in 2006 and am a Certified Public Accountant in the State of Ohio. I have nineteen years of tax experience and seven years of utility tax experience. Prior to joining American Water in September of 2024, I was a Tax Accounting and Regulatory Support Manager at American Electric Power, Inc. Prior to that, I held positions in both public accounting and the private sector. My previous employers include GBQ Partners, LLC, HBD Industries, Inc. and L Brands, Inc., now Bath and Body Works, Inc.

Q. Have you previously filed testimony in any regulatory proceedings?

A. Yes. At American Water, I have filed testimony in rate proceedings before the Pennsylvania Public Utility Commission in Docket Nos. R-2025-3057983 and R-2025-

3058051, the California Public Utilities Commission in Docket No. 25-07-003, the Public Service Commission in of West Virginia in Case Nos. 25-0595-WS-DSIC, 25-0426-W-42T and 25-0428-S-42T, the Kentucky Public Service Commission in Case No. 2025-00122, the Missouri Public Service Commission in Case No. WR-2024-0320, the Tennessee Public Utility Commission in Docket Nos. 25-0040 and 24-00032, and the Iowa Utilities Commission in Docket No. RPU-2024-0002. While employed at American Electric Power I filed testimony in rate proceedings before the Oklahoma Corporation Commission in Case No. PUD 2022-000093, before the Arkansas Public Service Commission in Case No. 23-012-FR, before the Public Service Commission of Kentucky in Case No. 2023-00159, and before the Public Utility Commission of Texas in Docket No. 56165.

Q. What is the purpose of your Direct Testimony in this proceeding?

A. The purpose of my Direct Testimony is to address the Office of the Public Counsel's ("OPC") position regarding the gross-up on tax expense in the revenue requirement.

Q. Are you sponsoring any Schedules with your Direct Testimony?

A. No.

II. TAX GROSS-UP RATE

Q. What is an income tax expense gross-up?

A. Federal income tax expense is not deductible for federal income tax purposes and state income tax expense is not deductible for state income tax purposes. Therefore, when considering a revenue requirement for regulated rate-making purposes, the tax expense collected in rates must be adjusted to cover the required tax on the dollars collected in rates for tax expense. This is referred to as a tax gross-up.

Q. Is a tax gross-up rate used in establishing the revenue requirement in a general rate case?

A. Yes. A tax gross-up is needed for establishing the revenue requirement in a general rate case as well as the WSIRA.

Q. Does the tax expense collected through the tax gross-up in the revenue requirement belong to the Company?

A. No. Tax expense collected by the Company in the revenue requirement does not belong to the Company – it has an obligation to pay the taxes to the government. If the Company does not pay the government immediately for the tax (known as current tax expense) it must record a liability for the future payment of the tax (known as deferred income tax expense). In either case, the company must include both the current and deferred components of tax expense in the revenue requirement because they are either immediately due to the government or will be due to the government in the future. In both situations, whether deferred or current, the taxes are not deductible.

Q. What happens to the deferred income tax expense collected that you mention above?

A. The deferred income tax expense collected in the revenue requirement is recorded into an accumulated deferred income tax (ADIT) balance sheet account to later pay to the government. Until that time, the ADIT balance is a dollar-for-dollar reduction to rate base that benefits customers.

Q. OPC takes the position that a gross-up on tax is not required because the Company is not in a taxable situation.[1] Is this correct?

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[1] OPC Response to Staff Recommendation, p. 3.

A. No. The Company does have tax expense and is including the amount in the revenue requirement. Tax expense includes both current and deferred taxes. The absence of current tax expense does not mean the Company is not in a taxable situation. The Company has deferred tax expense which it must pay to the government in the future and therefore has taxes to collect from customers. The gross-up on tax expense ensures that the Company is made whole because taxes collected in the revenue requirement are not deductible. Therefore, each dollar of tax collected in the revenue requirement will also be taxed.

Q. OPC suggests that the Company will not be in a taxable situation within the next three years. Is that the case?

A. No. While not included in the last rate case, the Corporate Alternative Minimum Tax was recently implemented and will require MAWC to make cash payments (current tax expense) to the parent to be paid to the government. It is projected that this will be the case for the next three years.

Q. Is the fact that the Company may not have current tax expense relevant to the use of a gross-up factor on tax expense?

A. No. As discussed previously, tax expense includes both current and deferred tax expense in accordance with ASC 740 and ASC 980 guidelines. Tax expense is included in the revenue requirement and the collection of this revenue will be taxed regardless of the nature of the tax being current or deferred.

Q. What is the flaw in OPC's logic regarding the gross-up of taxes?

A. OPC incorrectly assumes that the gross-up of taxes is only necessary for the Company to immediately pay the liability to the government. However, this is not the case. The gross-up is necessary for the Company to pay the liability both today (current tax expense) and in the future (deferred tax expense).

Q. Will the Company meet its authorized after-tax rate of return of 7.00%[2] using the 8.12% pre-tax rate of return as proposed by Mr. Riley?

A. No. The calculation below demonstrates that Company will not meet its authorized after-tax rate of return of 7.00% using a pre-tax rate of return of 8.12%. The calculation compares the after-tax return result using the OPC's proposed pre-tax rate of return and the Company's proposed pre-tax rate of return. The OPC's proposed pre-tax rate of return of 8.12% results in an after-tax rate of return of 6.73%. Comparatively, the MAWC pre-tax rate of return of 8.47% results in the authorized after-tax rate of return of 7.00%.

			OPC	MAWC
A	Rate Base		$123,010,057	$123,010,057
B	Pre-Tax Rate of Return		8.12%	8.47%
A x B = C	Pre-Tax Return		$9,988,417	$10,418,952
A x 2.3% = D	Interest Expense	2.30%	$2,829,231	$2,829,231
C - D = E	Taxable Income		$7,159,185	$7,589,721
E x 23.84% = F	Income Taxes	23.84%	$1,706,750	$1,809,389
E - F = G	Net Income		$5,452,436	$5,780,331
D	Interest Expense		$2,829,231	$2,829,231
G + D = H	After Tax Return		$8,281,667	$8,609,562
H / A	**After Tax Rate of Return**		**6.73%**	**7.00%**

Q. The OPC states the rationale for excluding a tax gross-up in the pre-tax rate of return is because neither WSIRA statutes nor any IRS guidelines require the use of the tax gross up calculation.[3] Are these logical reasons to exclude a tax gross-up?

A. No. First, a tax gross-up is a fundamental ratemaking principle and the exclusion of the term in the WSIRA statue does not preclude the concept in WRISA ratemaking. In fact,

[2] The authorized return for WSIRA purposes is addressed in the Direct Testimony of Company witness Brian LaGrand

[3] OPC Response to Staff Recommendation, p. 2.

as referenced by the OPC, the WSIRA statues require inclusion of the state, federal, and local income or excise taxes applicable to such revenues.[4] We have previously discussed that state and federal taxes are not deductible for tax purposes and therefore require a gross-up for proper inclusion in the revenue requirement. The exclusion of a gross-up on the taxes would indicate that they are not being fully collected as required by statute. Second, the lack of mandate from the IRS on the use of a gross-up rate does not preclude the use of the gross-up on taxes in ratemaking. The Company will file and pay its taxes properly as required by the IRS regardless of the inclusion or exclusion of a gross-up in ratemaking. The gross-up simply ensures that tax expense is properly included in the revenue requirement so that the Company can earn its authorized rate of return.

Q. What do you propose regarding the use of a gross-up rate?

A. I propose the Commission reject the OPC's proposed 8.12% pre-tax rate of return, because it would prohibit the Company from having an opportunity to earn the authorized 7.00% after-tax rate of return, and approve the use of the 8.47% pre-tax rate of return, which includes a gross-up for tax expense as included in the Company's filing.

Q. Does this conclude your Direct Testimony?

A. Yes, it does.

[4] OPC Response to Staff Recommendation, p. 3.