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Exhibit No. 4

MAWC – Exhibit 4
Linda Schlessman Testimony
Rebuttal
Case No. WR-2025-0345

Exhibit No.:	
Issues:	Income Tax Calculations
Witness:	Linda Schlessman
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Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2025-0345
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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2025-0345

REBUTTAL TESTIMONY

OF

LINDA SCHLESSMAN

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

PUBLIC

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

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Linda Schlessman

January 15, 2026

Dated

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

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REBUTTAL TESTIMONY

LINDA SCHLESSMAN

I. INTRODUCTION

Q. Please state your name and business address.

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

Q. Are you the same Linda Schlessman who previously submitted Direct Testimony in this proceeding on behalf of Missouri-American Water Company ("MAWC" or "Company")?

A. Yes.

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

A. The purpose of my Rebuttal Testimony is to respond to Office of Public Counsel's ("OPC") Witness Riley regarding the necessity of a tax gross-up rate in ratemaking.

II. TAX GROSS-UP RATE

Q. OPC witness Riley illustrates the math of a tax gross-up calculation in his direct testimony based on an example of $100,000 of Commission approved revenues.[1] Do you agree with his illustrative math used to calculate a tax gross-up?

A. Yes. I agree with the math used in the illustrative example to calculate a tax gross-up rate. As stated in Mr. Riley's direct testimony regarding the $100,000 example, "in ratemaking, the Commission intends for the utility to retain $100,000 after taxes are calculated. Therefore, additional money is included in the revenue requirement to ensure the Company

[1] Direct Testimony of John S. Riley Pages 3-6.

keeps $100,000 after taxes".[2] The example goes on to show that if the combined federal and state rate is 23.84%, the Company would need to collect not $23,840 ($100,000 x 0.2384) for taxes, but rather $31,300 ($100,000 x 1/(1-0.2384)) in order to have an opportunity to recover the authorized revenues of $100,000. In other words, the Company would need to collect $131,300 to be left with the authorized revenues of $100,000. While not included in Mr. Riley's illustrative example, the following illustration demonstrates that this will be accomplished.

131,300	Revenue Requirement
23.84%	Federal and State Combine Rate
31,300	Revenue Requirement x Tax Rate =Tax Expense
100,000	Revenue Requirement - Tax Expense = Authorized Revenues

Q. Mr. Riley defines the tax rate of 23.84% in his example as the "standard composite rate."[3] What does that mean?

A. The "standard composite tax rate" is the combination of the federal and state tax rates that are in effect under current law. Included in the rate is the benefit of the deductibility of state taxes for federal purposes and the deductibility of federal taxes for state purposes.

Q. Is this rate based on the cash tax rate, in other words, is it based on the cash outlay for taxes during the current period?

A. No. The rate is based on the statutory rate in effect for federal and state purposes. This is because tax expense is based on the statutory rate, not cash taxes paid.

Q. Is the cash tax rate used in a tax gross-up calculation?

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[2] Direct Testimony of John S. Riley Page 3, Lines 4-7.
[3] Direct Testimony of John S. Riley Page 3, Line 4.

A. No. The cash tax rate is not used because cash taxes are based on differences in timing of deductions (known as tax timing differences) between book accounting and the tax return. However, regardless of timing, the deduction is the same and does not change the amount that is taxed. In the illustration, all $100,000 will be taxed.

Q. Are you able to provide an example of this?

A. Yes. To demonstrate this fact, I have built upon the illustration discussed above with an example of cash taxes, also known as current tax expense. In this example the company has placed a $250,000 piece of equipment into service. For ease of illustration, the book life is 5 years with a straight-line depreciation rate. The equipment qualifies as a repair for tax purposes and is immediately deductible on the tax return. This example demonstrates that over the life of the asset current tax expense equals total tax expense. In year one the company would not pay tax, but over the life of the property, the company owed the same amount of tax regardless of the tax treatment of the property. This Illustration of Tax Expense with Tax Timing Difference is depicted below:

Illustration of Tax Expense with Tax Timing Difference

Plant and Equipment	250,000
Book Depreciation Rate	SL 5 Year
Tax Treatment	Repair Expense
Tax Rate	23.84%

	Year 1 Book	Year 2 Book	Year 3 Book	Year 4 Book	Year 5 Book	Total
Approved Revenues	100,000	100,000	100,000	100,000	100,000	
Cost of Service - Book Depreciation	50,000	50,000	50,000	50,000	50,000	
Book Depreciation Expense	(50,000)	(50,000)	(50,000)	(50,000)	(50,000)	
Net Income	100,000	100,000	100,000	100,000	100,000	
Tax Expense	**23,840**	**23,840**	**23,840**	**23,840**	**23,840**	**119,200**

	Tax	Tax	Tax	Tax	Tax	Total
Net Income	100,000	100,000	100,000	100,000	100,000	
Book Depreciation Expense	50,000	50,000	50,000	50,000	50,000	
Tax Repair Deduction	(250,000)	-	-	-	-	
Taxable Income (Loss)	(100,000)	150,000	150,000	150,000	150,000	
Current Tax Expense: Cash Taxes	**(23,840)**	**35,760**	**35,760**	**35,760**	**35,760**	**119,200**
Deferred Tax Expense	47,680	(11,920)	(11,920)	(11,920)	(11,920)	-
Tax Expense	23,840	23,840	23,840	23,840	23,840	119,200

Q. OPC witness Riley makes several statements alleging that MAWC "does not currently owe income taxes to the IRS, therefore it does not pay income taxes. It will be in this situation for the foreseeable future." (Riley Dir. p. 2, ln. 13-14; p. 7, ln. 3-4, ln. 12-13; p. 8, ln. 15; p. 10, ln. 5-7). Do you believe the status of MAWC's current income tax payments is determinative as to how the tax gross-up should be performed?

A. No. As demonstrated in my above illustration what is ultimately owed and currently payable are different, but equal over the life of the timing difference. Because the Company has an obligation to pay the government in the future, a deferred tax liability is recorded on the balance sheet to signify that obligation.

Q. Having said that, is Mr. Riley's statement that MAWC will not pay income taxes for the foreseeable future, correct?

A. No. Regardless of my foremost disagreement that the presence of, or lack of, current cash tax payments to the government is a reason to exclude a tax gross-up, as I indicated in my Direct Testimony, MAWC and its parent, American Water Works Company ("AWWC") are required to make Corporate Alternative Minimum Tax ("CAMT") payments starting with the 2024 tax return. That return was filed in October of 2025.[4] AWWC's CAMT was $151.6M with MAWC's stand-alone CAMT being $16.0M.[5] The CAMT resulted in an additional payment of $84.0M above the regular tax liability for AWWC, of which MAWC's share was $7.7M. The Company estimates that it will be in an alternative minimum tax payment situation for the next three years.

Q. Briefly, what is the Corporate Alternative Minimum Tax ("CAMT")?

A. CAMT was part of the Inflation Reduction Act of 2022 ("IRA"). CAMT was established for applicable corporations with adjusted financial statement income ("AFSI") above $1 billion. The IRA imposes a tax equal to the excess of 15% of the corporation's AFSI (tentative minimum tax) for the taxable year over its regular income tax liability. The AFSI test states that if a corporation's average annual AFSI exceeds $1 billion over the preceding three-year period, then the corporation and its subsidiaries are applicable corporations. Beginning with tax year 2024, AWWC, along with its subsidiaries, is an applicable corporation.

Q. OPC witness Riley states that MAWC's future liability for income taxes "is shown in Staff Accounting Schedules along with MAWC's Pro Forma Current income tax Schedules from its most recent rate case, Case Number WR-2024-0320. It is also

[4] Schlessman RT – Schedule LS-1 – Confidential.
[5] Schlessman RT – Schedule LS-2 – Confidential.

shown in MAWC's 2023 Annual Report to the Commission." (Riley Dir., p. 7, ln. 13-16; p. 9, ln. 16-18). What do those items show?

A. The WR-2024-0320 Test Year End 12/31/2023 Revenue Requirement schedule (JSR-D-04, Page 1) shows the change in current income tax due to the change in pre-tax income, after initial filing, during the most recent rate case. The change in pre-tax income does not affect deferred income tax and therefore is not shown in this schedule. The WR-2024-0320 Test Year End 12/31/2023 Cash Working Capital schedule (JSR-D-04, Page 2) shows the negative current taxes used in calculating the Cash Working Capital requirement; however, the schedule does not show deferred income taxes. Neither of these schedules take into consideration deferred income tax, which as discussed previously is a critical component of the overall tax obligation. The 2023 Annual Report (JSR-D-04, Page 4) shows both the current and deferred taxes. While the current taxes are negative, the deferred taxes are positive and result in a total tax expense of $1,608,321 for state and $10,146,794 for federal.

Q. Mr. Riley accuses you of "twisting the situation" based on your description of tax expense including "both current and deferred taxes." (Riley Dir., p. 8, ln. 20 – p. 9, ln. 13). What is significant about your response?

A. First, I am not twisting the tax or tax gross-up situation. Tax expense is the total of current and deferred taxes because regardless of whether the tax bill is due in the current year, it will be due in the future as shown in the Illustration of Tax Expense with Tax Timing Difference, above. In fact, Mr. Riley's tax gross-up calculation illustration uses total (both current and deferred) tax expense rate as well.

Q. Does Mr. Riley make other assertions regarding your prior testimony?

A. Yes. Mr. Riley highlights three statements regarding my arguments in the last MAWC rate case (Case No. WR-2024-0320) for use of a tax gross-up rate regardless of the current cash tax position. First, he states "she mentions income tax expense is built into the revenue requirement. However, it is understood from Staff accounting schedules, MAWC work papers, income tax returns and the Annual Report, that MAWC does not currently pay income tax to the IRS."[6] Again, he has incorrectly equated current tax expense with total tax expense and has excluded deferred income tax. Second, he states that "MAWC has already collected deferred taxes from its ratepayers in advance, that is what Accumulated Deferred Income Taxes are. When these deferred taxes eventually come due then the necessary tax gross-up will be applied."[7] This is also incorrect. Deferred tax expense in the revenue requirement is limited to the deferred tax expense generated in the period, not deferred tax expense from a prior period, which has already been paid by customers. Furthermore, the gross-up will not be applied to the taxes when owed. That would equate to charging a cash tax gross-up rate as opposed to a standard composite rate and, as I discussed previously, would not be appropriate. Finally, he states that because MAWC does not have current taxes that "deductibility is not an issue"[8], or in other words deferred taxes are not deductible. This is also not true. Income taxes, whether current or deferred, are not deductible. The deferred taxes that are collected today from customers will not be deductible when remitted to the government.

[6] Direct Testimony of John S. Riley Page 9, Lines 15-18.
[7] Direct Testimony of John S. Riley, Pages 9, Line 21 – Page 10, Line– 2.
[8] Direct Testimony of John S. Riley, Page, 10, Line 7.

Q. OPC witness Riley further states "MAWC does not pay to the IRS any of the taxes included in the revenue requirement to ensure that it is 'made whole.'" (Riley Dir., p. 10, ln. 11-12). Do you agree with that statement?

A. No. Again, Mr. Riley is ignoring deferred tax expense that will be due in the future and will not be deductible. Therefore, for MAWC to be made whole for the fact that taxes are not deductible, a tax gross-up rate is included in ratemaking.

Q. Mr. Riley also concludes that "ratepayers" have provided MAWC "with an interest free loan on its deferred tax and when those deferred taxes reverse, its ratepayers will be charged those taxes when they become due." (Riley Dir., p. 10, ln. 12-14). Do you agree that deferred taxes represent an interest free loan from customers?

A. No. I disagree that customers are charged taxes when they become due and I disagree with the characterization that deferred taxes represent an interest free loan from customers. First, customers pay taxes in the revenue requirement when the legal obligation associated with the taxes arises, not based on when they are paid to the government. Second, deferred taxes represent an interest free loan from the government to the company, not a loan from the customer to the company resulting from federal tax policy.

Q. If deferred taxes are an interest free loan from the government to the Company, does the Company pass this benefit to customers?

A. Yes. The Company acknowledges that the deferred tax collected in cost of service in the revenue requirement will be paid in the future and not in the current year. Therefore, the Company includes, as a reduction to rate base, the accumulated deferred income tax (ADIT) balance.

Q. What is the revenue requirement implication of that reduction to rate base?

A. Because the rate base is reduced, the return associated with the Company's investment is also reduced, resulting in a lower revenue requirement.

Q. Does Mr. Riley discuss the correlation of deferred taxes in the revenue requirement and the offset of ADIT in rate base?

A. No. Mr. Riley ignores this correlation. He accuses the Company of over collecting taxes through the tax gross-up rate because they are not immediately due to the government, while failing to recognize that until the payment is made, the accumulation of deferred income taxes provide a reduction to rate base.

Q. OPC witness Riley alleges that "not all cases require" a tax gross-up because a "tax gross-up is only necessary when taxes are actually paid because tax payments necessitate additional (gross-up) tax payments." (Riley Dir., p. 10, ln. 17-20). How do you respond to this allegation?

A. I disagree with this allegation. Income taxes in ratemaking must be looked at holistically. Cost of service in the revenue requirement includes income tax expense based on the obligation to pay the government both today and tomorrow. Because the tax expense owed to the government is not deductible now or in the future, a tax gross-up is included so that the Company is not harmed by the inability to deduct income tax expense. Because not all the tax collected in cost of service will be paid immediately to the government, an accumulated deferred income tax liability is recorded and reduces rate base, which in turn reduces the revenue requirement. One cannot simply pick and choose when to charge a tax gross-up rate based on isolating one element of ratemaking. In this case, Mr. Riley has chosen to isolate current tax expense without considering deferred tax expense and ultimately the reduction to rate base that the deferred tax expense provides to customers.

IV. CONCLUSION

Q. What is your recommendation for the Commission?

A. I recommend the Commission reject Mr. Riley's proposal to remove the tax gross-up rate from the pre-tax rate of return because it would prohibit the Company from having an opportunity to earn its authorized after-tax rate of return.

Q. Does this conclude your Rebuttal Testimony?

A. Yes.

Schedule LS-1 has been marked CONFIDENTIAL in its entirety in accordance with Commission Rules 20 CSR 4240-2.135(2)(A).5

Schedule LS-2 has been marked CONFIDENTIAL in its entirety in accordance with Commission Rules 20 CSR 4240-2.135(2)(A).5