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June 8, 2020
Data Center
Missouri Public
Service Commission Exhibit 201P
Net Operating Loss (NOL)
Riley/Direct
Public Counsel
WO-2020-0190

Exhibit No.:
Issue(s):
Witness/Type of Exhibit:
Sponsoring Party:
Case No.:

DIRECT TESTIMONY

OF

JOHN S. RILEY

Submitted on Behalf of the Office of the Public Counsel

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WO-2020-0190

**

**

Denotes Confidential Information has been redacted

May 22, 2020

PUBLIC

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

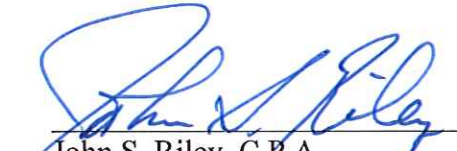
In the Matter of the Petition of Missouri-American)
Water Company for Approval to Change an) Case No. WO-2020-0190
Infrastructure System Replacement Surcharge)
(ISRS))

VERIFICATION OF JOHN S. RILEY

John S. Riley, under penalty of perjury, states:

1. Attached hereto and made a part hereof for all purposes is my direct testimony in the above-captioned case.

3. My answer to each question in the attached direct testimony is true and correct to the best of my knowledge, information, and belief.



John S. Riley, C.P.A.
Public Utility Accountant III
Office of the Public Counsel

DIRECT TESTIMONY
OF
JOHN S. RILEY
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WO-2020-0190

1 **Q. What is your name and what is your business address.**

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

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

4 A. I am employed by the Missouri Office of the Public Counsel (“OPC”) as a Public Utility
5 Accountant III.

6 **Q. What is your educational background?**

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

9 **Q. What is your professional work experience?**

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

Direct Testimony of
John S. Riley
Case No. WO-2020-0190

1 **Q. Are you a Certified Public Accountant (“CPA”) licensed in the State of Missouri?**

2 A. Yes. I am also a member of the Institute of Internal Auditors (“IIA”).

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

4 A. Yes I have. A listing of my Case filings is attached as JSR-D-1.

5 **Q. What is the purpose of your direct testimony?**

6 A. I will be responding to the Commission Staff (“Staff”)’s recommendations that the
7 Commission accept Missouri American Water Company (“MAWC”)’s contention that the
8 Internal Revenue Service (“IRS”) acknowledged in its Private Letter Ruling (“PLR”) that the
9 Company should adjust the Infrastructure System Replacement Surcharge (“ISRS”) specific
10 accumulated deferred income taxes (“ADIT”) by a hypothetical net operating loss (“NOL”).

11 **Q. This argument concerning an NOL adjustment to ADIT has been the subject of**
12 **MAWC’s last three ISRS cases.¹ Would you please provide a summary as to why this**
13 **subject is being contested in the current case?**

14 A. In Case No. WO-2019-0184, a full blown hearing was conducted, testimony presented,
15 witnesses questioned, and briefs filed. In its *Report and Order*, the Commission concluded
16 that MAWC did not have an NOL during the ISRS period. This was the same findings that
17 the Commission concluded in the prior Case No. WO-2018-0373. In short, it found that an
18 NOL is a tax return item and not asset specific and that rates are set prospectively so MAWC’s
19 argument that it received no revenues to offset its expenditures was an incorrect assumption.
20 Both of these cases were appealed to the Western District where the Court affirmed the
21 Commission’s findings.²

¹ Commission case numbers WO-2018-0373, WO-2019-0184, and WO-2019-0389.

² The most recent Western District decision is *Mo. Am. Water Co. v. Mo. Pub. Serv. Comm’n*, No. WD83067, 2020 Mo. App. LEXIS 498, (Mo. App. WD Apr. 21, 2020).

Direct Testimony of
John S. Riley
Case No. WO-2020-0190

1 The one difference we have now is that the Company requested a PLR from the IRS since the
2 end of the last case. The IRS's *Response* to the request has been received and analyzed by all
3 the parties involved. MAWC and Staff have interpreted the PLR to bolster the Company
4 contention that an NOL should be included in the ISRS calculations. This is incorrect. The
5 IRS only **acknowledged** the NOL that MAWC set forth in its factual representations to the
6 IRS and then responded to the questions presented by the Company based on those factual
7 representations. The IRS did **not** affirm that an NOL existed during the ISRS timeframe
8 because the IRS was **never asked** to confirm the existence of an NOL.

9 **Q. Was OPC allowed to provide input into the wording of the request to the IRS?**

10 A. No, we were not consulted.

11 **Q So the Company was allowed to frame the facts and questions to the IRS as it chose?**

12 A. Yes. Staff may have been privy to the wording of the request prior to its delivery but we were
13 not given that opportunity.

14 **Q. What does the IRS do with the facts that are presented to them by MAWC?**

15 A. The IRS takes the facts presented by the taxpayer at face value and applies them to the
16 situations that the taxpayer wishes to have the Service clarify. In this case, it was asked to
17 answer 12 specific questions.

18 **Q. **** _____

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9 **Q. Is this assessment of the facts correct?**

10 A. No. As I said before, the IRS takes the facts at face value, so it assesses the situation exactly
11 as it is presented by the taxpayer requesting the letter. But the Commission did not find that
12 MAWC had incurred a taxable loss in either of the prior cases in the manner that these facts
13 allege. In fact, the emphasized portion is literally the exact opposite of what this Commission
14 found in cases WO-2018-0373, WO-2019-0184.

15 **Q. Staff has filed its recommendations in this case. Could you summarize its conclusions?**

16 A. To quote Staff's memorandum:

17 Staff has reviewed the PLR for its potential impact on this proceeding,
18 and through its analysis concludes that within the PLR the IRS
19 determined that the Commission's actions in reflecting a full
20 deduction of applicable accelerated depreciation amounts without
21 offset for an NOL amount in ISRS did constitute a violation of the
22 Code's normalization restrictions.

23 **Q. Is Staff correct?**

24 A. No. Staff's assessment is incorrect because the IRS was never asked to **confirm** that an NOL
25 existed. That particular question has been the focal point of the past three MAWC ISRS
26 decisions. This Commission **twice** determined that MAWC did not have an NOL and those
27 decision were each separately appealed and affirmed by the Western District. Staff's decision
28 to ignore this fact makes absolutely no sense. What the IRS actually did is exactly what

1 MAWC asked of them: determine if there was a normalization violation **if one assumed an**
2 **NOL exists**. But MAWC should never have asked the IRS to assume an NOL existed because
3 this Commission flatly rejected that idea, twice. It is utterly unfathomable to me that a
4 company should put this much effort into a PLR request and then never ask the question that
5 all of these court proceedings have concerned, yet it is somehow even more difficult to
6 understand why Staff would fail to appreciate that the central question to these cases was
7 never even asked in the first place.

8 **Q. What leads you to believe that the request did not ask this key question?**

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9 It is certainly interesting that there had been two ISRS cases with two Commission decisions
10 stating that there was no NOL during the ISRS period and that both of those decisions have
11 been appealed to and confirmed by the Western District, yet MAWC still asserted that it was
12 a “fact” that there is a tax loss in a PLR request to the IRS.

13 **Q. If the IRS was not asked to confirm the presence of an NOL, why did it make a**
14 **determination on how an NOL should be addressed in an ISRS?**

15 A. PLRs answer specific questions with specific answers. MAWC asked the IRS to answer
16 twelve specific questions. ** _____
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9 **Q. So the IRS answered the questions posed without questioning the facts that frame those**
10 **questions?**

11 A. That is correct, they did not. They took what was given to them and made a determination.

12 **Q. So can we circle back to the Staff memorandum you quoted earlier in your testimony?**
13 **Where does this put Staff’s analysis?**

14 A. Staff’s analysis is incorrect because the IRS never concluded that there was an NOL. Staff’s
15 assessment in the prior cases that there was no NOL remains correct but, for whatever reason,
16 Staff has decided to over-read the PLR to include a determination that the IRS was never
17 asked to make, but rather, was instead presented as a proven fact. Further, because the IRS
18 was presented with a “fact” despite being contrary to the Commission’s own findings and the
19 IRS simply relied on that “fact” without question, the Commission was never actually
20 contradicted by the IRS. Was there a NOL? The IRS certainly did not say there was one and
21 the Commission has twice found that there was not one. If there is no NOL, then there is no
22 normalization violation, even if one accepts the IRS’s PLR in full. Without the confirmation
23 that there was an NOL, this PLR is just an expensive “what if” proposition.

24 **Q. Given all the foregoing, what is your recommendation to the Commission?**

Direct Testimony of
John S. Riley

Case No. WO-2020-0190

1 A. The Commission should reject MAWC's ISRS tariff sheet proposed in this case and accept the
2 Staff's recommended ISRS updated surcharge calculations less the MAWC proposed \$35,000 revenue
3 increase for the NOL inclusion. The pre-tax incremental revenues would then be \$9,690,687.

4 **Q. Does this conclude your testimony?**

5 A. Yes.

John S. Riley, CPA
Summary of Case Participation

ST LOUIS COUNTY WATER COMPANY	CASE NO. WR-88-5
SOUTHWESTERN BELL TELEPHONE COMPANY	CASE NO. TC-89-21
EMPIRE DISTRICT ELECTRIC COMPANY	CASE NO. ER-2016-0023
KCP&L GREATER MISSOURI OPERATIONS COMPANY	CASE NO. ER-2016-0156
KANSAS CITY POWER & LIGHT COMPANY	CASE NO. ER-2016-0285
AMEREN MISSOURI	CASE NO. ER-2016-0179
EMPIRE DISTRICT ELECTRIC PRUDENCE REVIEW	CASE NO. EO-2017-0065
LACLEDE GAS COMPANY	CASE NO. GR-2017-0215
MISSOURI AMERICAN WATER COMPANY	CASE NO. WU-2017-0351
MISSOURI AMERICAN WATER COMPANY	CASE NO. WR-2017-0285
LIBERTY (MIDSTATE NATURAL GAS)	CASE NO. GR-2018-0013
KANSAS CITY POWER AND LIGHT	CASE NO. ER-2018-0145
KCP&L GREATER MISSOURI OPERATIONS COMPANY	CASE NO. ER-2018-0146
EMPIRE DISTRICT ELECTRIC PRUDENCE REVIEW	CASE NO. EO-2018-0244
EMPIRE DISTRICT ELECTRIC COMPANY	CASE NO. ER-2018-0228
EMPIRE DISTRICT ELECTRIC COMPANY	CASE NO. ER-2018-0366
EMPIRE DISTRICT ELECTRIC COMPANY	CASE NO. EO-2018-0092
AMEREN GAS COMPANY	CASE NO. GR-2018-0227
MISSOURI AMERICAN WATER COMPANY	CASE NO. WO-2018-0373
LIBERTY UTILITIES EMPIRE ELECTRIC CO	CASE NO. EA-2019-0010
SUMMIT NATURAL GAS OF MISSOURI, INC	CASE NO. GR-2018-0230
SPIRE NATURAL GAS, EAST/WEST ISRS	CASE NO. GO-2019-0115
MISSOURI AMERICAN WATER COMPANY	CASE NO. WO-2019-0184

John S. Riley, CPA
Summary of Case Participation

AMEREN GAS

CASE NO. GR-2019-0077

UNION ELECTRIC COMPANY

CASE NO. ER-2019-0335

LIBERTY EMPIRE ELECTRIC CO.

CASE NO. ER-2019-0374