BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Application of Missouri-American Water Company for an Accounting Authority Order related to Property Taxes in St. Louis County and Platte County.	)))))	File No. WU-2017-0351

MAWC'S REPLY BRIEF

COMES NOW Missouri-American Water Company (MAWC or Company) and for its Reply Brief in the above-captioned matter states to the Missouri Public Service Commission (Commission) as follows:

Introduction

MAWC believes that none of the Initial Briefs filed by the other Parties in this case raise any issues not anticipated and fully addressed in MAWC's Initial Brief. Nevertheless, a reply is warranted as the Parties opposing MAWC's Application for an Accounting Authority Order (AAO) continue their efforts to trivialize and/or misrepresent the extraordinary actions taken by the St. Louis and Platte County Assessors in suddenly and materially changing the way in which they assess the value of MAWC's distributable assets for property tax purposes.

1. The dramatic and sudden changes in St. Louis and Platte Counties' tax assessment methodologies are an extraordinary event, not an ordinary one.

Each of the opposing Parties in this case argue that St. Louis and Platte Counties' shifts in their property tax assessment methodologies were not extraordinary in nature. Their arguments are largely summarized by the Office of Public Counsel's (OPC's) assertion that "Property taxes, when considered as a category of cost, are routine and ongoing, and should be considered to be among the most 'ordinary' of costs incurred by a utility."[1] This

[1] OPC Brief, p. 8.

characterization, however, fails to acknowledge the unique nature and magnitude of the counties' dramatic shift in their property valuation methodologies.

First, the counties' shifts in applying Modified Accelerated Cost Recovery (MACRs) class lives were one-time occurrences that are highly unlikely to occur again. Prior to their sudden and unilateral methodology changes, St. Louis and Platte Counties had assessed MAWC property using the same class lives for at least ten years, and it is extremely unlikely that MAWC will experience again such a similar, substantial increase in property tax based on a change in property tax methodology by either St. Louis County or Platte County.[2] Even Commission Staff (Staff) Witness Oligschlaeger concedes that St. Louis County's increase in recovery life span is "a rare situation", and that Platte County's increase "appears to be unprecedented."[3] And, as St. Louis County Witness Strain admits, there is nothing in the statutes that would appear to authorize Platte County's use of a fifty-year class life, further highlighting the unique and unprecedented nature of Platte County's actions.[4] Accordingly, the changes in assessment methodologies are not "reoccurring" or an ordinary event, but rather, a unique and foundational change in how these counties have assessed the MAWC property in question.

Furthermore, the counties' actions have caused a massive increase in MAWC's tax obligations, completely unlike ordinary property tax increases. The record is clear that these counties have not merely tweaked their existing assessment methodologies. Rather, St. Louis County has nearly tripled the applicable class life (i.e., from 7 to 20 years), and Platte County has implemented a 150% increase in its class life (from 20 to 50 years). These changes result in an approximately 92 percent increase in MAWC's St. Louis County property tax obligation, and an

[2] Exh. 5, LaGrand Sur., p. 5.
[3] Tr. 143; Exh. 6, Oligschlaeger Reb., p. 7.
[4] Tr. 198.

approximately 37 percent increase in Platte County.[5] Altogether, the changes result in $7.5 million in new property tax obligations for the period from January, 2017, through May, 2018, amounting to 9.6% of MAWC's 2016 annual income.[6] In short, the counties' actions, which are beyond the control of MAWC, have not merely increased MAWC's property tax obligations; they have imposed massive property tax increases that were unforeseeable at the time of MAWC's last rate case, thus highlighting the extraordinary nature of the actions taken by the counties.

Although not the case here, even an "ordinary" increase in property tax expense of significant size due to increased plant investment will give rise to extraordinary ratemaking treatment. In MAWC's 2000 rate case, the Commission found that MAWC's local property tax liability would increase substantially as a result of MAWC's new St. Joseph water treatment plant coming online. The Commission, therefore, allowed MAWC to recover the projected tax increase through a refundable surcharge to be reviewed and trued-up in its next general rate case.[7]

2. The fact that the ability to change taxing methodology is within the discretion of the county assessors does not preclude their actions from being extraordinary.

Some of the Parties argue that since taxing authorities have discretion to change their taxing methodologies, any such discretionary changes should not be considered extraordinary. For instance, Staff has argued that, "Changes in taxing methodology or increases in tax rates should be considered as part of the ordinary discretion available to those [taxing authority] bodies, and should not be considered inherently extraordinary in nature."[8] Staff appears to be

[5] MAWC Brief, p. 8.
[6] Exh. 5, LaGrand Sur., p. 8; Schedule BWL.
[7] *In the Matter of Missouri-American Water Company's Tariff Sheets Designed to Implement General Rate Increase for Water and Sewer Provided to Customers in the Missouri Service Area of the Company*, (WR-2000-281) (August 31, 2000).
[8] Staff Brief, p. 4.

arguing that government actions giving rise to extraordinary costs and a grant of an AAO must in some way be a result of unlawful or unwarranted action. However, this argument ignores the fact that the Commission has granted several AAOs in cases where the extraordinary costs were occasioned by lawful and discretionary changes undertaken by appropriate governmental authorities.

For instance, as Commissioner Rupp has noted, the Commission has granted an AAO to an electric company whose tree-trimming expenses rose to an unforeseeable level after a discretionary new Commission regulation.[9] The Commission has also granted AAOs to companies who faced higher uncollectible expenses following discretionary government amendments to the Cold Weather Rule.[10] Finally, the Commission has granted AAOs to companies seeking to comply with amended Financial Accounting Standards, discretionary standards applied to utilities through the Federal Securities and Exchange Commission.[11] In each of these cases, a governmental body, or an agency with authority over governmental policy, used its lawful discretionary ability to amend its preexisting policy. Each of these discretionary actions gave rise to unanticipated and extraordinary expenses, and accordingly, the Commission granted the utilities AAOs. Here, the circumstances are indistinguishable, with the St. Louis and Platte Counties' discretionary assessment methodology changes giving rise to extraordinary new expenses. The Commission's past cases show that it is willing to grant AAOs

[9] *In the Matter of Union Elec. Co., d/b/a Ameren UE's Tariffs to Increase Its Annual Revenues for Elec. Service*, (475 ER-2008-0318) (Jan. 27, 2009).
[10] *In the matter of the Application of UtiliCorp United Inc., d/b/a Missouri Public Service and St. Joseph Light and Power Company for an Accounting Authority Order Relating to Commission Rule 4 CSR 240-13.055(13),* 11 Mo. P.S.C. 3d 78 (GA-2002-285) (January 10, 2002); *In the Matter of the Application of Missouri Gas Energy, a Division of Southern Union Company, for an Accounting Authority Order Relating to Commission Rule 4 CSR 240-13.055(13),* 2002 Mo. P.S.C. 3d 317 (GA-2002-377) (June 13, 2002).
[11] *In Re Union Electric*, 1 Mo.P.S.C.3d 328, 330 (EO-92-179) (June 12, 1992); *In Re St. Joseph Light and Power Company*, 2 Mo.P.S.C.3d 248, 270 (ER-93-41, EC-93-252) (June 25, 1993); *In Re Missouri Gas Energy*, 3 Mo.P.S.C.3d 203 (GO-94-255) (September 28, 1994); *In Re Empire District Electric Company* (EO-93-35) (February 2, 1993).

to companies for expenses incurred because of discretionary government action, regardless of whether the discretionary government action was unquestionably permissible or potentially unconstitutional. Accordingly, the Commission should act in accordance with its precedent and grant the AAO in recognition of the extraordinary nature of St. Louis and Platte Counties' actions.

3. St. Louis County was not simply "rectifying a mistake."

Staff and St. Louis County claim that St. Louis County's decision to move from a seven (7) year MACR class life to a twenty (20) year MACR class life was not a change in tax assessment methodology, but simply "rectifying a mistake."[12] In a similar vein, Public Counsel asserts MAWC was incorrectly reporting its property value,[13] and the Missouri Energy Consumers Group (MECG) accuses MAWC of "misapplying" the appropriate lives in its property tax filings.[14] As a result of these mischaracterizations, these Parties then conclude that St. Louis County's change from seven (7) to twenty (20) year class lives was not unexpected[15] and should have been foreseen.[16]

First, the Parties incorrectly believe that it is MAWC's responsibility to apply the correct MACR class life to its distributable property. Rather, as St. Louis County witness Strain admits, and §137.122, RSMo., clearly provides, the responsibility of applying the appropriate class life to the original cost of the property rests solely with the Assessor.[17]

Second, the MACR class lives listed in §137.122, RSMo., do not apply to the property in question. As St. Louis County witness Strain explained, the property at issue is distribution

[12] Staff Brief, p. 3; St. Louis County Brief, p. 4.
[13] OPC Brief, p. 10.
[14] MECG Brief, p. 10.
[15] Staff Brief, p. 3.
[16] OPC Brief, p. 9.
[17] Exh. 12, Strain Reb., p. 6.

assets (i.e., pipes, pumps, and hydrants) that are located on property owned by other entities. Technically, this is considered real property,[18] but pursuant to St. Louis County's custom and practice, it has been assessed as personal property.[19]

Third, Ms. Strain also testified that, in applying §137.122, the Assessor has discretion to apply a range of lives as short as seven (7) years or as long as twenty (20) years.[20] As the record in this case shows, MAWC was advised by Ms. Leahy of the St. Louis County Assessor's office to use the existing depreciation schedules in its 2007 property declaration, which were based on a seven (7) year class life.[21] MAWC thereafter filed its property tax declarations for not only 2007, but for all years through 2017, using a seven (7) year class life, and all of those declarations, with the exception of the current year, were accepted by the St. Louis County Assessor without question.[22]

St. Louis County's attempt to dismiss its failure to recognize and correct MAWC's annual filing because it was one of approximately 40,000 other business tax declaration filings is misleading. Given the specific correspondence between MAWC and Ms. Leahy regarding the proper class life, one would have expected Ms. Leahy to closely review MAWC's 2007 property declaration to make sure that MAWC was using the appropriate class lives.

Moreover, MAWC is not like the other 40,000 businesses filing property tax returns. As Ms. Strain admits, there are only two entities in St. Louis County that make these unique tax declaration filings – that is, MAWC and Laclede Gas Company. So, it is difficult to believe that MAWC's filings were lost in the shuffle of other business tax filings.

[18] Section 137.010(4), RSMo.
[19] Tr. 175-177.
[20] Tr. 199.
[21] Exh. 2, Wilde Sur., p. 2; Schedule 4.
[22] Exh. 2, Wilde Sur., p. 2-3.

In addition, as Ms. Strain readily concedes, it is easy to determine from MAWC's property tax filings that it was using a seven (7) year recovery period because the filing only had seven columns of data. If MAWC had been using a twenty (20) year recovery period, the filing would have had twenty columns of data.[23] Thus, the record evidence clearly reveals that St. Louis County was aware, or should have been aware, of the fact that MAWC was using a seven (7) year recovery period, and St. Louis County's decision to shift to a twenty (20) year recovery period was not an oversight, but rather a conscious decision to review and change the applicable MACR class life in light of recent State Tax Commission cases involving Ameren and Laclede Gas Company.

4. AAOs do not run afoul of the prohibition against single issue ratemaking.

MECG begins its Initial Brief by suggesting that AAOs somehow run afoul of the prohibition against single issue ratemaking. However, MECG then grudgingly acknowledges that this Commission and the Missouri Court of Appeals have clearly rejected that argument.[24] MECG, nevertheless, spends the next several pages of its Initial Brief complaining about AAOs because, in MECG's view, they eliminate some of the key aspects of traditional regulation through formal rate cases.[25]

MECG argues that deferral accounting avoids the "matching concept" inherent in traditional ratemaking and "ignores the possibility of offsetting costs and revenues from that prior period." MECG even speculates, without any evidence, that MAWC can offset the extraordinary increase in its property tax expense by somehow increasing its revenues and/or decreasing its costs. This argument fails to acknowledge that the massive increase in MAWC's

[23] Tr. 179, " . . . it's something that St. Louis County should have definitely have caught."
[24] MECG Brief, pp. 2-4.
[25] MECG Brief, pp. 4-6.

property tax expense (i.e., $7.5 million, or 9.6% of its 2016 income) is due to unilateral decisions by the St. Louis and Platte County Assessors, over which neither MAWC nor the Commission have control. In other words, MAWC did not make a management decision to increase its expenses by $7.5 million. To now speculate that MAWC can somehow increase its revenues and/or reduce its expenses to the magnitude necessary to offset this $7.5 million increase is simply ludicrous. Additionally, MECG's assertion that the implementation of trackers imposes "regulatory burdens on other stakeholders" is without any evidentiary support and is simply wrong. There is no evidence to suggest that by allowing MAWC to defer these one-time property tax increases it will create any additional administrative burdens on MAWC or on the parties to its pending rate case. In fact, if AAOs have created such administrative burdens, the Commission would have acknowledged these burdens in its myriad of prior orders granting and denying AAOs, but it has not done so.

5. The increase in property tax expense is material.

No Party has disputed the fact that the increased property tax expense associated with St. Louis County's decision to move from a seven (7) year to a twenty (20) year recovery period has a material impact on MAWC's financial position, at least in regard to its 2017 tax obligations. Staff and OPC oppose MAWC's proposal to combine the property tax impact to be experienced in Platte County with that to be experienced in St. Louis County as two allegedly separate and distinct events. However, as St. Louis County witness Strain testified, both Platte County's and St. Louis County's decisions to review and then increase the class lives associated with MAWC's distributable property was directly the result of recent State Tax Commission decisions involving the property tax assessments of Ameren's and Laclede Gas Company's distributable

property.[26] Thus, it is clear that these State Tax Commission cases are the "common cause" that links both the actions taken by Platte County and St. Louis County to increase the recovery periods to be applied to MAWC's distributable property. Moreover, as MAWC witness LaGrand testified, the Company does not experience the financial impact of these changes in its property taxes in isolation. The changes in tax assessment methodology occurred at virtually the same time and are a result of each county's decision to increase the recovery periods to be applied to MAWC's distributable property.[27]

Public Counsel tries to further minimize the materiality of these property tax increases by suggesting that each year should be considered separately. However, OPC witness Riley, in citing FERC's USOA definition of extraordinary items, actually provides support for the fact that the impact in 2017 and 2018 should be considered in the aggregate. The FERC USOA definition of extraordinary items provides, in relevant part, that:

> "The effects of a series of a related transaction arising from a single specific and identifiable event or plan of action should be considered in the aggregate."[28]

And, as Staff witness Oligschlaeger stated in response to Commission Rupp:

> ". . . it's okay to look at the fiscal impact for both years together in comparing it for the materiality standard."[29]

Thus, the actions of the St. Louis and Platte County Assessors arose from a specific and identifiable event, i.e., the State Tax Commission cases involving Ameren and Laclede Gas Company, and should be considered as a single linked event with a material impact on MAWC.

6. The Commission should not address the amortization of any deferred debt in this case.

[26] Tr. 201.
[27] Exh. 5, LaGrand Sur., p. 8.
[28] Exh. 10, Riley Reb., p. 4.
[29] Tr., p. 145.

Public Counsel proposes that if the Commission grants MAWC an AAO to defer the property tax increase in this case, it should also begin amortization of that deferred debit immediately.[30] Staff recommends that MAWC be ordered to start amortizing any deferral authorized in this proceeding no later than April 1, 2018.[31] However, both OPC and Staff are putting the cart before the horse. In order to begin amortization of the deferred debit, MAWC needs to know the appropriate period over which the deferred debit is to be amortized (e.g., three (3) years, four (4) years, etc.). Establishing an appropriate amortization period is a decision the Commission should make in the context of MAWC's pending rate case where all relevant factors can be considered. It is indeed ironic that OPC and Staff would argue that the Commission should not make any ratemaking determinations in the context of this AAO case but, at the same time, suggest the Commission establish and begin amortization of the deferred debit in the context of this case. The better course of action is to defer decision on this amortization issue until the Company's pending rate case, which will become effective no later than late May, 2018.

7. Contrary to Public Counsel's assertions, all MAWC is seeking in this case is authority to defer certain expenses on its books to NARUC USOA Account 186.

Public Counsel confuses an Accounting Authority Order that permits the Company to defer these expenses at issue in Account 186 with an order granting the Company the right to create a "regulatory asset." All MAWC is seeking in this case is authority to defer these expenses on its books in NARUC USOA Account 186. MAWC understands that the decision of whether or not to classify this deferred debit as a regulatory asset is a decision that it will make in consultation with its outside auditors. The extraordinary nature and materiality of these expenses warrants the Company bringing this issue to the Commission for confirmation that

[30] OPC Brief, p. 12.
[31] Staff Brief, p. 7.

these costs are appropriate for deferral until rate treatment for these expenses can be addressed in the Company's pending rate case.[32]

In issuing an AAO, the Commission must determine that the costs at issue are extraordinary. And, as OPC witness Riley notes, the NARUC USOA General Instruction Number 7 requires, "Commission approval must be obtained to treat an item as extraordinary."[33] Staff witness Oligschlaeger confirms that what MAWC is seeking in this case is identical to what utilities have been seeking from the Commission for decades:

> ". . . There is nothing in the USOA's or other Commission rules that prohibit utilities from seeking Commission authorization to implement desired accounting treatments, such as deferral of extraordinary costs. It has been a long-standing practice in this jurisdiction that utilities, in most circumstances, will petition the Commission that AAO Applications for authorization to book regulatory assets. Receiving express Commission authorization for booking of deferrals strengthens the ability of utilities to justify reflection of the regulatory assets on their public financial statements in conformity with GAAP standards."[34]

Accordingly, OPC's suggestion that the grant of an AAO to defer these extraordinary expenses is unnecessary is misplaced, contrary to precedent, and should be rejected.

Conclusion

The increased property taxes MAWC will incur due to the sudden and dramatic change in the tax assessment methodologies employed by St. Louis County and Platte County Assessors is extraordinary, unique, unusual, and non-recurring. They are also material. Accordingly, the Commission should grant MAWC an AAO to defer the incremental increase in its property tax expense for the period January 1, 2017, through the effective date of a Report and Order issued

[32] Exh. 5, LaGrand Sur., p. 14.
[33] Exh. 10, Riley Reb., p. 5, l. 8-9.
[34] Exh. 7, Oligschlaeger Sur., p. 7.

in MAWC's pending rate case associated with the change in the assessment methodologies employed by St. Louis and Platte Counties.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned certifies that a true and correct copy of the foregoing document was sent by electronic mail or by U.S. Mail, postage prepaid, on December 1, 2017, to the following:

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