

Exhibit No.:
Issues: Infrastructure System Replacement
Surcharge
Witness: Brian W. LaGrand
Exhibit Type: Direct
Sponsoring Party: Missouri-American Water Company
Case No.: WO-2018-0373
Date: November 13, 2018

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WO-2017-0373

DIRECT TESTIMONY

OF

BRIAN W. LAGRAN

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

MAWC Exhibit No. 1
Date 11-20-18 Reporter Bjt
File No. WO-2018-0373

**DIRECT TESTIMONY
BRIAN W. LAGRAND
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WO-2018-0373**

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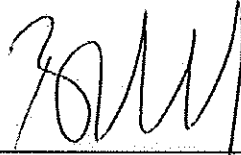
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**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

IN THE MATTER OF MISSOURI-AMERICAN) WATER COMPANY'S PETITION TO) ESTABLISH AN INFRASTRUCTURE) REPLACEMENT SURCHARGE))))))	CASE NO. WO-2018-0373
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AFFIDAVIT OF BRIAN W. LAGRAN

Brian W. LaGrand, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Direct Testimony of Brian W. LaGrand"; that said testimony and schedules were prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge.



Brian W. LaGrand

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
Before me this 12th day of November 2018.



Notary Public

My commission expires:



DIRECT TESTIMONY

BRIAN W. LAGRAND

I. INTRODUCTION

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Q. Please state your name and business address.

A. My name is Brian W. LaGrand, and my business address is 727 Craig Road, St. Louis, MO, 63141.

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

A. I am employed by Missouri-American Water Company (“MAWC”, “Missouri-American” or the “Company”) as the Director of Rates and Regulatory Support.

Q. Please summarize your educational background and business experience.

A. I received a Master of Business Administration degree from Washington University in St. Louis in 1998, with a concentration in Finance, and a Bachelor of Science in Business Administration degree from the University of Dayton in 1993, with a major in Accounting. After graduation from the University of Dayton, I was licensed in Ohio as a Certified Public Accountant, and was employed as an Auditor by J.D. Cloud and Associates until 1996. After graduating from Washington University, I spent two years at May Department Stores Company in the Capital Planning & Analysis department, focusing on the evaluation of capital investments. In 2000 I began working for Anheuser-Busch Companies as a Financial Analyst in the Treasury Group. My responsibilities included managing the foreign currency derivative portfolio in Risk Management and running the commercial paper and share repurchase programs in

1 Corporate Finance. In 2005 I moved into the Business & Wholesaler Development
2 Group as a Sr. Business Analyst, where I worked on acquisitions of craft breweries and
3 competitive analysis. In 2010 I joined American Water Works Service Company, Inc.
4 (“Service Company”) as a Manager in the Corporate Finance Group. My focus has
5 included evaluation of acquisition opportunities across the country and the execution
6 of many acquisitions, including several in Missouri. In November of 2016, I was
7 promoted to my current position as Director of Rates and Regulatory Support for
8 MAWC.

9
10 **Q. What are your current employment responsibilities?**

11 A. My responsibilities as Director of Rates and Regulatory Support include the following:
12 1) Preparing and presenting all rate change applications and supporting documents and
13 exhibits as prescribed by management policies, guidelines and regulatory commission
14 requirements; 2) Preparing rate analyses and studies to evaluate the effect of proposed
15 rates on the revenues, rate of return and tariff structures; 3) Executing the
16 implementation of rate orders, including development of the revised tariff pricing
17 necessary to produce the proposed revenue level; 4) Overseeing the preparation of
18 revenue and capital requirements analyses; and 5) Providing support for financial
19 analyses, including preparation of applicable regulatory commission filings.

20
21 **Q. Are you generally familiar with the operations, books and records of MAWC?**

22 A. Yes.

23

24 **Q. Have you previously testified before a regulatory body?**

1 A. Yes, I provided testimony before the Missouri Public Service Commission
2 (“Commission”) in MAWC’s most recent general rate case (WR-2017-0285),
3 Accounting Authority Order cases on Lead Service Lines (WO-2017-0296) & Property
4 Taxes (WO-2017-0351), and MAWC’s 2012 acquisition of Saddlebrooke Water and
5 Sewer (WA-2012-0066). I have also testified before the Illinois Commerce
6 Commission.

7

8 **Q. What is the purpose of your direct testimony in this proceeding?**

9 A. The purpose of my direct testimony is to sponsor and testify in support of MAWC’s
10 request to reestablish its ISRS. I will also comment on the Staff Recommendation filed
11 on October 19, 2018.

12

13

II. ISRS APPLICATION

14 **Q. Would you summarize MAWC’s ISRS Application?**

15 A. Yes. On August 20th, 2018, MAWC filed an Application to establish a new ISRS with
16 a revenue requirement of \$7,437,064. This revenue requirement includes ISRS-eligible
17 investments, net of Contributions in Aid of Construction, made between January 1,
18 2018 and September 30, 2018, and annualized net depreciation expense. In the initial
19 Application, the investment amounts for August and September were estimated.

20

21 **Q. Did MAWC include property taxes in the ISRS Application?**

22 A. No. While the Company will recognize property tax expense on these investments, no
23 property tax will be paid on these investments during the 12 months after the ISRS
24 takes effect. Therefore, property tax was excluded from the Company’s Application.

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Q. Has the Company made any revisions to the ISRS revenue requirement?

A. Yes. During Staff's audit, in which they reviewed invoices and other supporting documentation on the investment costs, Staff identified a few invoices that are properly excluded from the Application. Additionally, MAWC updated the August and September investments to include actual numbers, rather than estimates. As a result of this process, the Company and Staff are now in agreement as to the amount of investment that should be included in the ISRS rate base. The Company's revised revenue requirement is now \$7,264,876. Please see Schedule BWL-1.

Q. Do the Company and Staff agree on the total revenue requirement?

A. No. Staff's revenue requirement is \$6,377,959, which is \$886,917 lower than the Company's calculation.

Q. What is the difference between the Company and Staff's calculations?

A. The Company and Staff both included in rate base the incremental Deferred Tax Liability that arises due to temporary timing differences in the book and tax depreciation expense. However, the Company also included in rate base the incremental Deferred Tax Asset that arises from the Net Operating Loss created by the tax deductions related to the repairs deduction and accelerated depreciation.

Q. Why did the Company include the Deferred Tax Asset in rate base?

A. Section 393.1000(1)(a), RSMo, defines Appropriate Pretax Revenues as "the revenues necessary to produce net operating income equal to the water corporation's weighted

1 cost of capital multiplied by the net original cost of eligible infrastructure replacements,
2 including recognition of accumulated deferred income taxes and accumulated
3 depreciation associated with eligible infrastructure system replacements which are
4 included in a currently effective ISRS.” Accumulated deferred income taxes include
5 both Deferred Tax Assets and Deferred Tax Liabilities. As explained in greater detail
6 in the direct testimony of Company witness John Wilde, the Company’s position is that
7 including the Deferred Tax Asset is consistent with the statutes that authorize the ISRS
8 and that failure to do so creates a tax normalization violation. By reducing the rate base
9 by the Deferred Tax Liability, which reduces the revenue requirement, and ignoring
10 the Deferred Tax Asset, the customer receives the benefit of the tax deduction now via
11 a lower ISRS rate. However, because the Company has a Net Operating Loss, the
12 benefit of those tax deductions will only be received by the Company at some time in
13 the future. Because the customer is getting the benefit of the tax deductions before the
14 Company receives the benefit, there is a normalization violation. The consequence of
15 this normalization violation is explained in the Direct Testimony of MAWC witness
16 John Wilde.

17
18 **Q. Does this conclude your direct testimony?**

19 **A. Yes.**

1	Infrastructure System Replacement Surcharge Revenue Requirement	
2		
3	Water Utility Plant Projects--Replacement Mains, and Associated Valves and Hydrants (RM) RSMo 393.1000 (8a):	
4	<u>Task Orders Placed in Service (TOPS):</u>	
5	STLC-Replacement Mains and Associated Valves and Hydrants	\$62,895,855
6	Net Contributions in Aid of Construction	(2,318)
7	Deferred Taxes	473,307
8	Accumulated Depreciation	(425,978)
9		
10	Total Net 393.1000 (8a)	\$62,940,867
11		
12	Water Utility Plant Projects--Main Cleanings and Relinings (RM) RSMo 393.1000 (8b):	
13	<u>Task Orders Placed in Service (TOPS):</u>	
14	STLC-Main Cleanings and Relinings	\$0
15	Net Contributions in Aid of Construction	0
16	Deferred Taxes	0
17	Accumulated Depreciation	0
18		
19	Total Net 393.1000 (8b)	\$0
20		
21	Water Utility Plant Projects--Facilities Relocations (FR) RSMo 393.1000 (8c):	
22	<u>Task Orders Placed in Service (TOPS):</u>	
23	STLC-Relocated Facilities	\$1,263,074
24	Net Contributions in Aid of Construction	(1,052,050)
25	Deferred Taxes	1,564
26	Accumulated Depreciation	(6,622)
27		
28	Total Net 393.1000 (8c)	\$205,967
29		
30	Accumulated Depreciation and Deferred Taxes on Investment in Current ISRS	
31	Accumulated Depreciation - Prior ISRS	\$0
32	Deferred Taxes - Prior ISRS	0
33		
34	Total	\$0
35		
36	Total ISRS Rate Base	\$63,146,834
37		
38	Overall Pre-Tax Rate Of Return per Last Order	9.44%
39		
40	Revenue Requirement on Capital	\$5,961,061
41	Depreciation Expense	826,505
42	Property Taxes ISRS 17	0
43	Revenue Cap Adjustment	0
44		
45	Total Revenue Requirement	\$6,787,566
46		
47	Adjustments:	
48	Undercollection from ISRS reconciliation	477,310
49		
50	Adjusted Total Revenue Requirement	\$7,264,876
51		
52	Allocation of Revenue by Class	
53	Rate A	\$7,253,544
54	Rate B	3,222
55	Rate J	8,110
56		
57	Grand Total Revenues Collected In Proposed ISRS	\$7,264,876

1 Book/Tax Depreciation Temporary Difference							
2							
3							
		Replacements		Relocations		Total All Property	
		2018	2019	2018	2019	2018	2019
4							
5 Plant Additions							
6	Plant Additions	62,895,855	-	1,263,074	-	64,158,929	-
7	Contributions	(2,337)	-	(1,059,928)	-	(1,062,265)	-
8	Net Plant Additions	62,893,518	-	203,146	-	63,096,664	-
9							
10 Total Tax Depreciation Items							
11							
12 Repairs Deduction							
13	Net Plant Additions	62,893,518	-	203,146	-	63,096,664	-
14	Repairs %	55.4%	-	55.4%	-	-	-
15	Total Repairs Deduction	34,849,591	-	112,564	-	34,962,156	-
16							
17 Bonus Depreciation							
18	Net Plant Additions After Repairs	28,043,927	-	90,582	-	28,134,509	-
19	Bonus Depreciation %	0.0%	-	0.0%	0.0%	-	-
20	Total Bonus Depreciation	-	-	-	-	-	-
21							
22 Regular Depreciation							
23	Net Plant Additions After Repairs and Bonus	28,043,927	-	90,582	-	28,134,509	-
24	Year 1 Depreciation Rate	2.0%	2.0%	2.0%	2.0%	-	-
25	Months Included	11.0	-	11.0	-	-	-
26	Total Regular Depreciation	514,139	-	1,661	-	515,799	-
27							
28	Total Tax Deductions	35,363,730	-	114,225	-	35,477,955	-
29							
30 Total Book Depreciation Items							
31							
32 Net Book Depreciation							
33	Book Depreciation	425,978	-	6,622	-	432,599	-
34	Book Amortization	(19)	-	(7,878)	-	(7,897)	-
35	Total Net Book Depreciation	425,959	-	(1,257)	-	424,702	-
36							
37	Book/Tax Depreciation Temporary Difference	(34,937,771)	-	(115,481)	-	(35,053,253)	-
38							
39	Total per Type of Property		(34,937,771)		(115,481)		(35,053,253)
40	% per Type of Property		99.671%		0.329%		100.000%
41							
42 Net Operating Loss / Taxable Income							
43							
44 Operating Results Through Effective Date of New ISRS							
						2018	2019
45	ISRS Revenues					\$0	-
46							
47	Depreciation Expense					424,702	-
48	Interest Expense					1,441,326	-
49	Property Tax					-	-
50	Total Expenses					1,866,029	-
51							
52	Pre-Tax Income					(1,866,029)	-
53	Book/Tax Depreciation Temporary Difference					(35,053,253)	-
54	Pre-NOL Taxable Income / (Loss)					(36,919,281)	-
55	NOL					36,919,281	-
56	Taxable Income					\$0	\$0
57							
58 Net Deferred Income Taxes							
59							
		Replacements		Relocations		Total All Property	
		2018	2019	2018	2019	2018	2019
61							
62	Book/Tax Depreciation Temporary Difference	(34,937,771)	-	(115,481)	-	(35,053,253)	-
63	Effective Tax Rate	25.4%	25.4%	25.4%	25.4%	-	-
64	Deferred Tax Liability	(8,891,053)	-	(29,388)	-	(8,920,441)	-
65							
66	NOL	36,797,652	-	121,629	-	36,919,281	-
67	Effective Tax Rate	25.4%	25.4%	25.4%	25.4%	-	-
68	Deferred Tax Asset	9,364,360	-	30,952	-	9,395,313	-
69							
70	Net Deferred Income Taxes	473,307	-	1,564	-	474,872	-

	ISRS Revenue Requirement	Customer Usage (000g) ¹	Required Rate per 1,000 Gallons	
1				
2	Rate A	\$7,253,544	32,207,358	\$0.22521
3	Rate B	3,222	1,609,828	\$0.00200
4	Rate J	8,110	4,227,969	\$0.00192
5	Total	\$7,264,876	38,045,155	

¹ Per billing determinants in Case WR-2017-0285

	Current Rate	Proposed Rate	Adjustment to Current Rate	
9				
10	Rate Per 1,000 Gallons			
11	Rate A	\$0.00000	\$0.22521	\$0.22521
12	Rate B	\$0.00000	\$0.00200	\$0.00200
13	Rate J	\$0.00000	\$0.00192	\$0.00192

	Current Rate	Proposed Rate	Adjustment to Current Rate	
15				
16	Rate Per 100 Gallons			
17	Rate A	\$0.00000	\$0.02252	\$0.02252
18	Rate B	\$0.00000	\$0.00020	\$0.00020
19	Rate J	\$0.00000	\$0.00019	\$0.00019

1	Property Tax Estimate - St. Louis County	
2	Year Placed in Service	2018
3	Vintage Year	1
4		
5	Total Investment	64,158,929
6	% Good	96.250%
7	Subtotal	61,752,969
8		
9	Total Retirements	(3,802,317)
10	% Good	20.000%
11	Subtotal	(760,463)
12		
13	Net Plant to be Assessed	62,513,433
14		
15	Assessment Rate	32.000%
16		
17	Assessed Value	20,004,298
18		
19	Tax Rate	8.400%
20		
21	Tax Due on ISRS Investment	1,680,361
22		
23	Due within 12 months from filing?	<input type="text" value="No"/>
24		
25	Property Tax Expense to Include in ISRS	0

27 **20 Year MACRS Table**

Year	MACRS	% Good
1	3.750%	96.250%
2	7.219%	89.031%
3	6.677%	82.354%
4	6.177%	76.177%
5	5.713%	70.464%
6	5.285%	65.179%
7	4.888%	60.291%
8	4.522%	55.769%
9	4.462%	51.307%
10	4.461%	46.846%
11	4.462%	42.384%
12	4.462%	37.922%
13	4.461%	33.461%
14	4.462%	28.999%
15	4.461%	24.538%
16	4.461%	20.077%
17	4.462%	20.000%
18	4.461%	20.000%
19	4.462%	20.000%
20	4.461%	20.000%
21	2.231%	20.000%

52 Notes: 1) MACRS % from IRS Publication 946, Table A-1
 53 2) There is a 20% floor on the % Good

	Base Revenues WR-2017-0285	Share of Base Revenue
1		
2	\$194,983,761	94.64%
3	3,141,065	1.52%
4	7,906,028	3.84%
5		
6	Total	100.00%

	Plant Additions	Share of Plant Additions
8		
9	\$60,781,551	94.736%
10	1,510,894	2.355%
11	Subtotal - Small Mains and Hydrants	97.091%
12		
13	1,866,484	2.909%
14		
15	Total	100.000%

	Share of Small Mains & Hydrants	Share of Large Mains
17		
18	100.000%	94.638%
19	0.000%	1.525%
20	0.000%	3.837%
21		
22	Total	100.000%

	Share of ISRS Revenues	Base Revenues WR-2017-0285	Percent Increase
24			
25	7,253,544	194,983,761	3.720%
26	3,222	3,141,065	0.103%
27	8,110	7,906,028	0.103%
28			
29	Total	206,030,853	3.526%

	Jan-18 - Jul-18	Aug-18 - Sep-18	Total
Mains, Valves and Hydrant Replacements			
Reimbursements	(\$2,337)	\$0	(\$2,337)
Amortization	\$19	\$0	\$19
Net CIAC	(\$2,318)	\$0	(\$2,318)

	Jan-18 - Jul-18	Aug-18 - Sep-18	Total
Relocations			
Reimbursements	(\$1,059,928)	\$0	(\$1,059,928)
Amortization	\$7,878	\$0	\$7,878
Net CIAC	(\$1,052,050)	\$0	(\$1,052,050)

	Replacements	Relocations	Total
1			
2			
3			
4			
5			
6			
7			
8			
Base Depreciation Expense	\$880,961	\$17,794	\$898,755
Reimbursements' Amortization	(32)	(14,733)	(14,765)
Depreciation Expense Associated with Retirements			(57,484)
Net Depreciation Expense			\$826,505