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 its Infrastructure System Replacement Surcharge (ISRS).	))))	**<u>File No. WO-2015-0059</u>** YW-2015-0090

<u>STAFF RECOMMENDATION</u>

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and in response to the Commission's September 5, 2014, *Order Directing Notice, Setting Intervention Deadline, and Directing Staff to File Recommendation*, states as follows:

1. On September 2, 2014, Missouri-American Water Company ("MAWC") filed a *Petition to Change its Infrastructure System Replacement Surcharge and Tariff*.

2. By this filing, MAWC requests an adjustment to its ISRS rates and charges for ISRS-eligible infrastructure system replacements and relocations made during the period of April 1, 2014 through September 30, 2014.

3. On September 2, 2014, the Commission set a deadline for intervention of September 25, 2014. No Parties have sought to intervene. The Commission further directed Staff to file a report on MAWC's application no later than October 15, 2015. Staff filed and the Commission granted an extension for filing the report until November 13, 2014. This filing complies with that Order.

4. Commission Rule 4 CSR 240-3.650(11) states that the staff of the Commission may examine information of a water utility to confirm the underlying costs related to the proposed ISRS and to confirm proper calculation of the proposed charge. The Staff "may submit a report regarding its examination to the

Commission no later than sixty days" after the petition is filed. In accordance with this rule and with the Commission's September 2, 2014 Order, Staff submits its *Memorandum,* incorporated herein as Attachment A.

5. Based on its examination and calculations as detailed in its memorandum, Staff recommends the Commission approve incremental ISRS surcharge revenues in the amount of $7,139,758. Please see Staff's Appendix B for the ISRS rate for each customer class.

WHEREFORE, WHEREFORE, Staff recommends that the Commission issue an order in this case that: 1) Finds that MAWC's filed petition is in compliance with the requirements of sections 393.1000 to 393.1006 RSMo; 2) Approves MAWC's Petition to implement ISRS rate schedules with the above adjustments to revenue requirement; 3) Approves the Staff's determination that the Company is entitled to receive cumulative ISRS surcharge revenues in the amount of $25,885,500 which includes $7,139,758 of ISRS revenues from MAWC's September 2, 2014 Application as shown in Attachment A; and 4) Approves the compliance filing of MAWC's revised ISRS tariff sheet P.S.C. MO. No.13, 5th Revised Sheet No. RT 10, Canceling 4th Revised Sheet No. RT 10 pending in Tariff File No. YW-2015-0090, to be effective on December 31, 2014.

Respectfully submitted,

<u>/s/ Cydney D. Mayfield</u>

Cydney D. Mayfield
Missouri Bar Number 57569
Senior Counsel
Attorney for the Staff of the
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102
573-751-4227 (Voice)
573-526-6969 (Fax)
cydney.mayfield@psc.mo.gov

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served, either electronically or by First Class United States Mail, postage prepaid, on this 13th day of November, 2014, to the parties of record as set out on the official Service List maintained by the Data Center of the Missouri Public Service Commission for this case.

<u>/s/ Cydney D. Mayfield</u>

MEMORANDUM

TO: Missouri Public Service Commission Official Case File
Case No. WO-2015-0059, Tariff Tracking No. YW-2015-0090
Missouri-American Water Company

FROM: Charles R. Hyneman, Regulatory Review, Utility Services - Auditing Unit
James J. Russo, Regulatory Review, Utility Operations – Water and Sewer Unit

/s/ Charles R. Hyneman 11/13/14 /s/Cydney Mayfield 11/13/14
Auditing Unit/ Date Staff Counsel's Office/ Date

/s/ James J. Russo 11/13/14
Water and Sewer Unit/ Date

SUBJECT: Staff Report and Recommendation Regarding MAWC's Petition to Change its Infrastructure Replacement Surcharge

DATE: November 13, 2014

BACKGROUND

On September 2, 2014, Missouri-American Water Company (MAWC or "Company") filed a Petition to Change its Infrastructure System Replacement Surcharge ("Application") with the Missouri Public Service Commission ("Commission") to implement a change in MAWC's Infrastructure System Replacement Surcharge (ISRS) and a revised Tariff Sheet with a proposed effective date of December 31, 2014.

Sections 393.1000, 393.1003 and 393.1006 ("ISRS statute") and Commission Rule 4 CSR 240-3.650 provide eligible water corporations with the ability to recover certain ISRS costs outside of a formal rate proceeding through a surcharge to ratepayer bills known as an ISRS. A petition must be filed with the Commission for review and approval before an ISRS can be established or a change to an ISRS can be effected.

MAWC's September 2, 2014 ISRS Application represents its 14th request. MAWC's first ISRS was filed on September 2, 2003 in Case Number WO-2004-0116. The following chart shows MAWC's cumulative ISRS cases:

Continued on next page

ISRS #	Case No.	Date Filed	ISRS Effective Date	Ordered Amount	ISRS Plant Start	ISRS Plant End	Rate Case	Rate Case Effective Date
1	WO-2004-0116	9/2/2003	12/31/2003	$3,628,576	Jan-01	Aug-03	WR-2003-0500	4/16/2006
2	WO-2006-0284	1/3/2006	4/7/2006	$4,850,176	Dec-03	Dec-05	WR-2007-0216	10/22/2007
3	WO-2007-0043	8/3/2006	10/12/2006	$1,961,076	Jan-06	Jul-06	WR-2007-0216	10/22/2007
4	WO-2007-0272	1/19/2007	4/15/2007	$2,580,388	Jan-04	Dec-06	WR-2007-0216	10/22/2007
5	WO-2008-0249	1/29/2008	4/27/2008	$2,670,761	Jan-07	Dec-07	WR-2008-0311	11/28/2008
6	WO-2009-0379	4/21/2009	7/18/2009	$2,652,705	Oct-08	May-09	WR-2010-0131	7/1/2010
7	WO-2010-0190	12/23/2009	3/30/3010	$3,156,668	Jun-09	Nov-09	WR-2010-0131	7/1/2010
8	WO-2011-0106	12/22/2010	3/21/2011	$3,624,121	May-10	Dec-10	WR-2011-0337	3/16/2012
9	WR-2011-0336	6/22/2011	10/16/2011	$2,180,730	Feb-11	Jul-11	WR-2011-0337	3/16/2012
10	WO-2012-0401	6/27/2012	9/25/2012	$4,189,656	Jan-12	Jul-12	NA	NA
11	WO-2013-0406	2/28/2013	6/21/2013	$5,441,344	Aug-12	Mar-13	NA	NA
12	WO-2014-0055	8/30/2013	12/14/2013	$4,307,496	Apr-13	Sep-13	NA	NA
13	WO-2014-0237	2/25/2014	5/30/2014	$3,667,776	Oct-13	Mar-14	NA	NA
14	WO-2015-0059	9/2/2014	NA	NA	Apr-14	Sep-14	NA	NA

In its September 2, 2014 Application for ISRS 14, MAWC asserted that it has continued to incur costs related to ISRS-eligible infrastructure system replacements. For the period from April 1, 2014 through September 30, 2014, MAWC claimed those costs entitled it to receive $11,221,435 in additional ISRS revenues. This amount includes $2.8 million in under-billed and therefore under-collected ISRS revenues from ISRS Nos. 10 through 13 and $1.4 million in additional ISRS revenues related to an income tax issue that will be discussed later. MAWC's proposed ISRS revenues were based in part on estimated ISRS plant additions for the months of August and September 2014.

In its ISRS 14 Application MAWC included estimated ISRS plant for August and September 2014 of $33.5 million. MAWC updated its ISRS 14 revenue requirement on October 21, 2014 to $11,325,974, which reflects actual (as opposed to estimated) August and September 2014 plant additions of approximately $38 million.

STAFF'S ISRS REVENUE REQUIREMENT CALCULATION

MAWC's ISRS 8 and ISRS 9 were in effect prior to MAWC's last general rate proceeding, Case No. WR-2011-0337 ("2011 rate case") and were rolled into MAWC's base rates in the 2011 rate case. Rates resulting from MAWC's 2011 rate case reflect the $5.7 million of ISRS revenues for ISRS 8 and ISRS 9 and all ISRS plant investments through December 31, 2011. The 2011 rate case *Non-unanimous Stipulation and Agreement* filed on February 24, 2012 and approved by the Commission on March 7, 2012, states:

> 14. Infrastructure System Replacement Surcharge (ISRS). As required by statute and Commission rule, MAWC's current ISRS shall be reset to zero upon the effective date of new rates in this

> case. The Signatories agree that, for any ISRS filings implemented between the date new rates are established in this proceeding and the effective date of new rates established in the Company's next general rate case proceeding, the overall rate of return shall be computed by utilizing a 10% return on common equity and the Company's actual capital structure as of December 31, 2011. Plant in-service additions to be included in a future ISRS may include those additions placed in service after January 1, 2012.

Since the 2011 rate case, the Commission has approved a new MAWC ISRS in ISRS 10 and the updates to this ISRS in ISRS 11, 12 and 13. MAWC's current ISRS reflects the Commission-approved ISRS revenues for ISRS 10 through 13 for a total current annual ratepayer surcharge of $17,606,271. In this application MAWC is proposing changes to the Commission-ordered ISRS revenuer requirements in ISRS 11,12 and 13.

ISRS	Case No.	MAWC
10	WO-2012-0401	$4,189,657
11	WO-2013-0406	$5,441,342
12	WO-2014-0055	$4,307,495
13	WO-2014-0237	$3,667,776
Total		$17,606,270

ISRS Legislation General Requirements:

Section 393.1003 has three requirements that must be met for a water corporation to establish an ISRS. These requirements are related to the timing of the ISRS filing in relation to the utility's general rate proceeding and to the size (both minimum and maximum) of the annual ISRS revenues.

The first requirement reflected in Section 393.1003 imposes a cap on the size of a water corporation's ISRS to 10% of the base revenues ordered by the Commission in its last rate case ("10% base revenue cap"). Section 393.1003(1) states:

> Notwithstanding any provisions of chapter 386 and this chapter to the contrary, as of August 28, 2003, a water corporation providing water service in a county with a charter form of government and with more than one million inhabitants may file a petition and proposed rate schedules with the commission to establish or change ISRS rate schedules that will allow for the adjustment of the water corporation's rates and charges to provide for the recovery of costs for eligible infrastructure system replacements made in such county with a charter form of government and with more than one million inhabitants; <u>provided that an ISRS, on an annualized basis, must produce ISRS revenues of at least one million dollars but not in excess of ten percent of the water corporation's base revenue level approved by the</u>

> commission in the water corporation's most recent general rate proceeding. (emphasis added).

Based on this requirement, the Staff calculated that MAWC's maximum ISRS revenues the Commission may allow in this ISRS 14 Application to keep under the Section 393.1003.(1) 10% base revenue cap is $**25,885,500** as calculated below:

Staff Adjusted Test Year Revenues in WR-2011-0337	$235,600,000
Commission ordered revenue increase WR-2011-0337	$23,255,000
Total Commission Ordered Base Revenues WR-2011-0337	$258,855,000
ISRS 10% Base Revenue Limit per Section 393.1003(1)	10%
Maximum ISRS allowed by Section 393.1003(1)	$25,885,500

A second general requirement of the ISRS statute is found in Section 393.1003.2 wherein it states:

> The commission shall not approve an ISRS for a water corporation in a county with a charter form of government and with more than one million inhabitants that has not had a general rate proceeding decided or dismissed by issuance of a commission order within the past three years, unless the water corporation has filed for or is the subject of a new general rate proceeding.

The Commission's order deciding MAWC's last general rate proceeding, Case No. WR-2011-0337 was issued on March 7, 2012. MAWC's current ISRS began with ISRS 10 which was approved effective September 25, 2012 and this current ISRS application falls within the three-year window allowed by Section 393.1003.2.

Finally, Section 393.1003.3 states:

> In no event shall a water corporation collect an ISRS for a period exceeding three years unless the water corporation has filed for or is the subject of a new general rate proceeding; provided that the ISRS may be collected until the effective date of new rate schedules established as a result of the new general rate proceeding, or until the subject general rate proceeding is otherwise decided or dismissed by issuance of a commission order without new rates being established.

MAWC began collecting its ISRS beginning with ISRS 10 on September 25, 2012. MAWC will not be allowed to collect its current ISRS past September 25, 2015 unless it files a general rate proceeding by or prior to that date.

Scope of Staff's ISRS Examination

The scope of Staff's ISRS examination is mandated by Section 393.1006 (2) (2) which states:

> The staff of the commission may examine information of the water corporation to confirm that the underlying costs are in accordance with the provisions of sections 393.1000 to 393.1006, and to confirm proper calculation of the proposed charge, and may submit a report regarding its examination to the commission not later than sixty days after the petition is filed. No other revenue requirement or ratemaking issues shall be examined in consideration of the petition or associated proposed rate schedules filed pursuant to the provisions of sections 393.1000 to 393.1006.

Section 393.1006.2(2) allows the Staff to perform an examination of an ISRS filing and make a report of its examination to the Commission. However, Section 393.1006.2(2) also places two significant restrictions on the Staff's ISRS examination. First, the Staff must submit a report regarding its examination to the Commission no later than sixty days after a utility files an ISRS application. Second, the Staff is prohibited from examining any other revenue requirement or ratemaking issue such as increases in water revenues or decreases in other costs that may partially or totally offset the need for an ISRS. A single-issue examination, such as the examination of the revenue requirement impact of only plant-related investments, as required by the Section 393.1006.2(2), is significantly different from a normal Staff rate case audit where all items of a utility's revenues, expenses, investments, gains and losses are examined and the resulting revenue requirement recommended by Staff is based on a comprehensive examination of utility operations.

The scope of Staff's examination of MAWC's ISRS application consisted of two parts. The first part was a review for the accuracy of the calculation of the ISRS revenue requirement components used to calculate the overall proposed ISRS revenue requirement. In general, this part of Staff's examination includes a review of MAWC's compliance with the ISRS statute as well as a review MAWC's calculation of the appropriate capital structure and capital cost rates, income tax rates, return on plant, depreciation expense, property taxes, depreciation reserve, deferred income taxes and a reconciliation of previous ISRS revenues.

The Staff verified MAWC's use of the appropriate capital structure and capital cost components as approved by the Commission in its March 7, 2012 *Order Approving Non-Unanimous Stipulation and Agreement* in Case No. WR-2011-0337. Paragraph 14 of the *Non-Unanimous Stipulation and Agreement* states that the signatories agree that "for any ISRS filings implemented between the date new rates are established in this proceeding and the effective date of new rates established in the Company's next general rate case proceeding, the overall rate of return shall be computed by utilizing a 10% return on common equity and the Company's actual capital structure as of December 31, 2011."

The Staff's grossed up for tax rate of return to apply to ISRS plant additions is 11.3196% as opposed to MAWC's 11.3352%. This adjustment, while reflected in the Staff's ISRS calculations, is not material to the overall ISRS revenue requirement.

The Staff also verified that the depreciation rates used by MAWC to calculate depreciation expense on the ISRS plant accounts (Account 316 Supply Mains 1.79% and Account 348 Fire

Hydrants 1.85%) were the same rates approved by the Commission its March 7, 2012 Order attached as Appendix B to the *Non-Unanimous Stipulation and Agreement* .

The Staff made several adjustments to MAWC's currently effective ISRS's 10 through 13 and its proposed ISRS 14. These adjustments will be described below:

Staff adjustments to ISRS 10

1. The Staff recalculated MAWC's proposed accumulated deferred income tax reserve for ISRS 10 which resulted in a net ISRS rate base decrease of $42,200.

2. The Staff recalculated MAWC's proposed depreciation reserve for ISRS 10 which resulted in a net ISRS rate base increase of $10,239.

Staff adjustments to ISRS 11

1. The Staff recalculated MAWC's proposed accumulated deferred income tax reserve for ISRS 10 and 11 which resulted in a net ISRS rate base decrease of $69,207.

2. The Staff recalculated MAWC's proposed depreciation reserve for ISRS 10 and 11 which resulted in a net ISRS rate base decrease of $2,323.

3. MAWC's ISRS 11 includes ISRS revenues designed to recover ISRS 11 property taxes of $218,759. Using MAWC's proposed property tax rate times the ISRS plant additions eligible for property tax in ISRS 11 the Staff calculated an annual property tax of $213,240 as opposed to the $218,759 included in ISRS 11. This adjustment results in an ISRS 11 ISRS revenue decrease of $5,519.

Staff adjustments to ISRS 12

1. The Staff recalculated MAWC's proposed accumulated deferred income tax reserve for ISRS 10, 11 and 12 which resulted in a net ISRS rate base increase of $2,504.

2. The Staff recalculated MAWC's proposed depreciation reserve for ISRS 10, 11 and 12 which resulted in a net ISRS rate base decrease of $31,300.

Staff adjustments to ISRS 13

1. The Staff recalculated MAWC's proposed accumulated deferred income tax reserve for ISRS 10 through 13 which resulted in a net ISRS rate base decrease of $92,716.

2. The Staff recalculated MAWC's proposed depreciation reserve for ISRS 10 through 13 which resulted in a net ISRS rate base decrease of $202,904.

Staff adjustments to ISRS 14

1. The Staff recalculated MAWC's proposed accumulated deferred income tax reserve for ISRS 10 through 14 which resulted in a net ISRS rate base decrease of $72,184.

2. The Staff recalculated MAWC's proposed depreciation reserve for ISRS 10 through 14 which resulted in a net ISRS rate base decrease of $116,267.

3. MAWC's ISRS 14 includes ISRS revenues designed to recover ISRS 14 property taxes of $375,176. However, the ISRS statute does not allow ISRS recovery for any property taxes for these specific plant additions.

Section 393.1000(5) defines ISRS costs as depreciation expenses and property taxes that will be due within twelve months of the ISRS filing. Commission Rule 4 CSR 240-3.650(E) defines ISRS costs as: annual depreciation expenses, and property taxes that will be due within twelve (12) months of the ISRS filing, on the total cost of eligible infrastructure system replacements, reduced by annual depreciation expenses and property taxes on any related facility retirements.

MAWC filed ISRS 14 on September 2, 2014. Twelve months from this ISRS filing is September 2, 2015. The property tax for the ISRS 14 plant additions made in April through September 2014 will be included in MAWC's property tax assessment in January 2015 but not payable until December 2015, a date later than September 2, 2015. Therefore any property tax on these ISRS plant additions should not have been included in this ISRS filing.

4. In its September 2, 2014 filing for ISRS 14 MAWC included $2,759,592 ISRS revenues related to what it termed "under collection from previous ISRS". Section 393.1006.5(2) states that "at the end of each twelve-month calendar period that an ISRS is in effect, the water corporation shall reconcile the differences between the revenues resulting from an ISRS and the appropriate pretax revenues as found by the commission for that period and shall submit the reconciliation and a proposed ISRS adjustment to the commission for approval to recover or refund the difference, as appropriate, through adjustment of an ISRS."

An ISRS reconciliation is a simple comparison between the monthly ISRS revenues authorized by the Commission and the amount of ISRS revenue billed by the utility to its customers for that month. In ISRS 14, MAWC is stating that over the period of its current ISRS (ISRS 10-13) it has under-billed its customers for $2,759,592 in ISRS revenues. MAWC updated this $2,759,592 under billing amount to $2,165,420.

As part of its ISRS examination the Staff performed an analysis of MAWC's authorized ISRS charges from September 2012 through September 2014. This analysis shows that

> MAWC was authorized to bill ISRS revenues form ISRS 10 through 13 of $19,934,439 but it had only billed customers $16,633,039 resulting in an under billing of $3,301,400. The amount is then reduced by the amount of ISRS revenues in the current ISRS ($253,280 in ISRS 10 and $1,841,374 in ISRS 12) that are being applied to the cumulative under-billing of the ISRS revenue. The net amount of ISRS revenues Staff included in ISRS 14 is $1,206,746.

In its ISRS 14 Application, MAWC seeks to include an increase of $1,433,600 in ISRS revenues due to a correction of the accumulated deferred income tax reserves reflected in ISRS 11, ISRS 12 and ISRS 13. Those ISRS calculations reflect an application of a 50 percent bonus depreciation tax deduction for 2013, which increased the amount of the ISRS rate base offset for the accumulated deferred income tax reserve. Although its ISRS 13 revenue requirement reflected the Company's expectation that it would utilize the bonus depreciation tax deductions in 2013, MAWC now claims that it did not generate sufficient taxable income to take advantage of the bonus depreciation opportunity in 2013. MAWC's ISRS 10 does reflect a 50% bonus depreciation deduction for 2012 and that is not affected by this proposed adjustment. No bonus depreciation was available to MAWC in 2014.

The Staff has treated income tax expense in ISRS filings under the normalization method of accounting, the same method used to calculate a utility's income tax expense in a general rate proceeding. While no determination has been made that the use of the normalization method of accounting is required to be used in ISRS cases, the Staff has no immediate plans to change this method of accounting but it may, in the future, consider whether a change in this method is appropriate.

The normalization method of accounting for income tax expense is explained by Internal Revenue Service in its January 30, 2006 Internal Revenue Bulletin No. 2006-5, page 389:

> Section 168 of the Code permits the use of accelerated depreciation methods. Section 168(f)(2) provides, however, that accelerated depreciation is permitted with respect to public utility property only if the taxpayer uses a normalization method of accounting for ratemaking purposes. Under a normalization method of accounting, a utility calculates its ratemaking tax expense using depreciation that is no more accelerated than its ratemaking depreciation (typically straight-line).
>
> In the early years of an asset's life, this results in ratemaking tax expense that is greater than actual tax expense. The difference between the ratemaking tax expense and the actual tax expense is added to a reserve (the accumulated deferred federal income tax reserve, or ADFIT). The difference between ratemaking tax expense and actual tax expense is not permanent and reverses in the later years of the asset's life when the ratemaking depreciation method provides larger depreciation deductions and lower tax expense than the accelerated method used in computing actual tax expense.

> This accounting treatment prevents the immediate flow-through to utility ratepayers of the reduction in current taxes resulting from the use of accelerated depreciation. Instead, the reduction is treated as a deferred tax expense that is collected from current ratepayers through utility rates, and thus is available to utilities as investment capital. When the accelerated method provides lower depreciation deductions in later years, only the ratemaking tax expense is collected from ratepayers and the difference between actual tax expense and ratemaking tax expense is charged to ADFIT.

The Staff has a policy that income tax benefits available to a utility by the income tax code will be reflected in cost of service unless the utility in not able to take advantage of the benefit due to the financial results of its regulated operations. For example, if a utility's regulated operations generated sufficient taxable income to reflect the bonus tax depreciation as a reduction in income tax expense, the Staff would reflect that income tax deduction in cost of service. If the utility's taxable income was not sufficient due to non-regulated or other revenues, expenses, gains and losses not reflected in regulated costs of service, the Staff would likely impute the tax deduction and reflect the lower income tax expense in cost of service.

In the responses to Staff Data Request Nos. 6, 7 and 8, the Staff obtained income tax documents and tax returns filed by MAWC. Based on its review of these documents the Staff found that MAWC did have taxable income in 2013 in an amount sufficient to absorb all or at least part of the 50% bonus depreciation for 2013 ISRS plant investments. However, in discussions with MAWC on this issue Staff was advised that MAWC did not take the bonus depreciation deduction on its 2013 tax return in order to preserve used of its net operating loss (NOL) carryforwards in future tax years. Staff was also advised that these NOL carryforwards were generated mainly by MAWC's regulated operations in the form of large repairs and maintenance income tax deductions and bonus depreciation in 2008 through 2010.

Given the limited time for a Staff ISRS examination, the complexity of this income tax issue, and other considerations, the Staff has decided to accept MAWC's proposed adjustments (reductions) to the accumulated deferred income tax reserves in ISRS 11, 12 and 13. In addition the Staff will reflect in ISRS 14 the related ISRS revenues that would have been authorized had the bonus depreciation deduction for 2013 not been reflected in the individual ISRS calculations. Other considerations include the fact that, with the ISRS statute 10% base revenue cap limiting the amount of ISRS increase in ISRS 14, MAWC's ratepayers would not receive the full benefit of a reduction in the ISRS that would result if the Staff imputed the 2013 bonus depreciation deduction in this ISRS. The Staff's acceptance of MAWC's proposed adjustment for purposes of this Application preserves future income tax deductions for this ISRS plant in any future ISRS and in base rates in MAWC's next general rate proceeding. The Staff will review this issue further in MAWC's next general rate proceeding and make any necessary adjustments, if needed, in the rate case or in subsequent MAWC ISRS filings.

The second part of Staff's examination consisted of a review of the plant work order documentation supporting the inclusion of the costs of specific water plant projects in MAWC's ISRS application.

Section 393.1000(1)(3) defines eligible infrastructure system replacements as water utility plant projects that:

> (a) Replace or extend the useful life of existing infrastructure;
>
> (b) Are in service and used and useful;
>
> (c) Do not increase revenues by directly connecting the infrastructure replacement to new customers; and
>
> (d) Were not included in the water corporation's rate base in its most recent general rate case;

Only certain types of water utility plant projects are eligible to be included in an ISRS. Section 393.1009 (5) restricts the types of water utility plant projects that may be included in the ISRS to projects that consist only of:

> (a) Mains, and associated valves and hydrants, installed as replacements for existing facilities that have worn out or are in deteriorated condition;
>
> (b) Main cleaning and relining projects; and
>
> (c) Facilities relocations required due to construction or improvement of a highway, road, street, public way, or other public work by or on behalf of the United States, this state, a political subdivision of this state, or another entity having the power of eminent domain provided that the costs related to such projects have not been reimbursed to the water corporation.

Staff reviewed certain documentation from 168 ISRS 14 work orders at MAWC's offices in St. Louis on October 28 and 29, 2014. The work orders reviewed were related to the proposed ISRS plant additions in ISRS 14 from April through September 2014. In this examination the Staff did not review ISRS plant work orders for ISRS plant additions included in ISRS 10 through 13.

Staff's total recommended ISRS revenue requirement for MAWC as a result of this application is $25,885,500 and for its updated ISRS 14 application, $7,139,758, as shown below:

ISRS	MAWC	staff adj	STAFF	10% Base Rev Cap	Adjusted
10	$4,189,657	($199,790)	$3,989,867		$3,989,867
11	$5,847,623	($20,447)	$5,827,176		$5,827,176
12	$4,818,996	($3,678)	$4,815,317		$4,815,317
13	$4,151,583	($38,201)	$4,113,382		$4,113,382
14	$11,325,974	($1,364,046)	$9,961,929	($2,822,170)	$7,139,758
Total ISRS	$30,333,832	($1,626,162)	$28,707,670		$25,885,500

MAWC seeks total ISRS revenues of $30,333,832 through this application. After the Staff's adjustments that were described above, the Staff finds that MAWC's pre-cap ISRS 10 through 14 cumulative authorized ISRS revenues should be $28,707,670. Applying the 10% base revenue cap adjustment as explained above, this amount is reduced by $2,822,170 resulting in a total ISRS revenue requirement of $25,885,500 and broken down by the ISRS updates 10 through 14 as noted above. The cumulative ISRS revenuer requirement of $25,885,500 reflects an authorized ISRS revenue requirement of $7,139,758 for MAWC's proposed ISRS 14. The Staff adjustments for ISRS 10 through ISRS 14 are reflected in Schedule CRH-1 to this document.

Staff has verified that MAWC has filed its 2013 annual report and is not delinquent on any assessment. Staff is not aware of any other matter before the Commission that affects or is affected by this filing.

The ISRS Rate Schedules

The proposed ISRS rate schedules include a volumetric rate for each affected customer class with the rate to be determined through the use of the customer class billing determinants from the Company's last rate case, No. WR-2011-0337 and the ISRS revenues allocated to each affected customer class. The Staff has utilized the Company's methodology for calculating the ISRS rates, but has determined such rates based on the Staff's calculation of the revenue requirement as reflected in Attachment B to this Memorandum.

RECOMMENDATION

Based upon the rationale stated above, Staff recommends the Commission issue an order in this case that:

1. Rejects MAWC's ISRS tariff sheet revised Tariff Sheet filed September 2, 2014;

2. Approves the Staff's recommended ISRS surcharge revenues in the incremental amount of annual pre-tax revenues of $25,885,500 including ISRS revenues of $7,139,758 for MAWC's currently proposed ISRS 14;

3. Authorizes MAWC to file a revised ISRS tariff sheet P.S.C. MO. No. 13, 5th Revised Sheet No. RT 10, Canceling 4th Revised Sheet No. RT 10 pending in Tariff File No. YW-2015-0090, to be effective December 31, 2014 that reflects the rates for each customer class as reflected in Attachment B.

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 its Infrastructure System Replacement Surcharge (ISRS)	))))	File No. WO-2015-0059

AFFIDAVIT OF CHARLES R. HYNEMAN

STATE OF MISSOURI)
) ss.
COUNTY OF JACKSON)

Charles R. Hyneman, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Staff Recommendation in memorandum form, to be presented in the above case; that the information in the Staff Recommendation was developed by his; that he has knowledge of the matters set forth in such Staff Recommendation; and that such matters are true and correct to the best of his knowledge and belief.

Charles R. Hyneman

Subscribed and sworn to before me this 12th day of November, 2014.

Notary Public

NOTARY PUBLIC NOTARY SEAL STATE OF MISSOURI

BEVERLY M. WEBB
My Commission Expires
April 14, 2016
Clay County
Commission #12464070

ISRS #	10 MAWC	staff adj	10 STAFF	11 MAWC	staff adj	11 STAFF	12 MAWC	staff adj	12 STAFF	13 MAWC	staff adj	13 STAFF	14 MAWC	staff adj	14 STAFF	Total MAWC	staff adj	Total STAFF
ISRS Plant Addition - Replacements	$35,156,769	$0	$35,156,769	$50,381,279	$0	$50,381,279	$23,995,938	$0	$23,995,938	$31,258,421	$0	$31,258,421	$58,533,810	$0	$58,533,810	$199,326,217	$0	$199,326,217
ISRS Plant Addition - Relocations	$1,961,631	$0	$1,961,631	$1,768,253	$0	$1,768,253	$318,422	$0	$318,422	$333,803	$0	$333,803	$119,337	$0	$119,337	$4,501,446	$0	$4,501,446
Total ISRS Plant Additions	$37,118,400	$0	$37,118,400	$52,149,532	$0	$52,149,532	$24,314,360	$0	$24,314,360	$31,592,224	$0	$31,592,224	$58,653,147	$0	$58,653,147	$203,827,663	$0	$203,827,663
Net Contributions in Aid of Const	($1,199,371)	$0	($1,199,371)	($1,062,361)	$0	($1,062,361)	$115,945	$0	$115,945	($231,731)	$0	($231,731)	($333,411)	$0	($333,411)	($2,710,929)	$0	($2,710,929)
Net ISRS Plant Additions	$35,919,029	$0	$35,919,029	$51,087,171	$0	$51,087,171	$24,430,305	$0	$24,430,305	$31,360,493	$0	$31,360,493	$58,319,736	$0	$58,319,736	$201,116,734	$0	$201,116,734
Accumulated Deferred Income Tax 10	($6,860,629)	($42,200)	($6,902,829)	($23,901)	($6,681)	($30,581)	($40,677)	$505	($40,172)	($33,898)	($6,274)	($40,172)	($40,677)	$505	($40,172)	($6,999,782)	($54,146)	($7,053,927)
Accumulated Deferred Income Tax 11	$0	$0	$0	($6,623,015)	($62,526)	($6,685,540)	($68,488)	$10,306	($58,183)	($101,382)	($20,606)	($121,988)	($121,659)	($328)	($121,987)	($6,914,544)	($73,154)	($6,987,698)
Accumulated Deferred Income Tax 12	$0	$0	$0	$0	$0	$0	($62,523)	($8,307)	($70,830)	($101,209)	($20,745)	($121,954)	($121,451)	($503)	($121,954)	($285,183)	($29,556)	($314,739)
Accumulated Deferred Income Tax 13	$0	$0	$0	$0	$0	$0	$0	$0	$0	($62,597)	($45,092)	($107,689)	($80,546)	($1,170)	($81,716)	($143,143)	($46,262)	($189,405)
Accumulated Deferred Income Tax 14	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	($100,746)	($70,687)	($171,433)	($100,746)	($70,687)	($171,433)
Accumulated Depreciation ISRS 10	($287,623)	$10,239	($277,384)	($322,317)	($17,075)	($339,392)	($241,738)	($12,807)	($254,544)	($201,448)	($53,096)	($254,544)	($241,738)	($12,806)	($254,544)	($1,294,864)	($85,546)	($1,380,409)
Accumulated Depreciation ISRS 11	$0	$0	$0	($487,047)	$14,752	($472,295)	($341,602)	($17,707)	($359,309)	($284,668)	($74,641)	($359,309)	($341,602)	($17,707)	($359,309)	($1,454,919)	($95,302)	($1,550,221)
Accumulated Depreciation ISRS 12	$0	$0	$0	$0	$0	$0	($181,160)	($786)	($181,946)	($131,046)	($39,876)	($170,922)	($157,255)	($13,667)	($170,922)	($469,461)	($54,330)	($523,791)
Accumulated Depreciation ISRS 13	$0	$0	$0	$0	$0	$0	$0	$0	$0	($178,873)	($35,291)	($214,164)	($216,471)	($4,985)	($221,456)	($395,344)	($40,276)	($435,620)
Accumulated Depreciation ISRS 14	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	($285,027)	($67,102)	($352,129)	($285,027)	($67,102)	($352,129)
ISRS Rate Base (Net)	$28,770,777	($31,961)	$28,738,816	$43,630,892	($71,530)	$43,559,362	$23,494,117	($28,796)	$23,494,116	$30,265,372	($295,620)	$29,969,752	$56,612,564	($188,451)	$56,424,113	$182,773,722	($616,359)	$182,186,158
Rate of Return (ROE =10%)	11.34%		11.32%	11.34%		11.32%	11.34%		11.32%	11.34%		11.32%	11.34%		11.32%	11.34%		11.32%
Return on Net Rate Base	$3,261,233	($8,122)	$3,253,111	$4,945,661	($14,928)	$4,930,733	$2,663,112	($3,678)	$2,659,433	$3,430,649	($38,201)	$3,392,448	$6,417,163	($30,195)	$6,386,968	$20,717,817	($95,124)	$20,622,693
Annual Depreciation Exp	$483,476	$0	$483,476	$683,203	$0	$683,203	$314,510	$0	$314,510	$432,942	$0	$432,942	$812,101	$0	$812,101	$2,726,232	$0	$2,726,232
Reconciliation of previous ISRS	$253,280	$0	$253,280	$0	$0	$0	$1,841,374	$0	$1,841,374	$0	$0	$0	$2,165,420	($958,674)	$1,206,746	$4,260,074	($958,674)	$3,301,400
Annual Property Tax-10	$191,668	($191,668)	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$191,668	($191,668)	$0
Annual Property Tax-11	$0	$0	$0	$218,759	($5,519)	$213,240	$0	$0	$0	$66,908	$0	$66,908	$0	$0	$0	$285,667	($5,519)	$280,148
Annual Property Tax-12	$0	$0	$0	$0	$0	$0	$0	$0	$0	$144,298	$0	$144,298	$0	$0	$0	$144,298	$0	$144,298
Annual Property Tax-13	$0	$0	$0	$0	$0	$0	$0	$0	$0	$76,786	$0	$76,786	$122,514	$0	$122,514	$199,300	$0	$199,300
Annual Property Tax-14	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$375,176	($375,176)	$0	$375,176	($375,176)	$0
Restate Bonus depreciation ISRS 11	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$406,281	$0	$406,281	$406,281	$0	$406,281
Restate Bonus depreciation ISRS 12	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$543,512	$0	$543,512	$543,512	$0	$543,512
Restate Bonus depreciation ISRS 13	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$483,807	$0	$483,807	$483,807	$0	$483,807
ISRS Revenue Requirement	$4,189,657	($199,790)	$3,989,867	$5,847,623	($20,447)	$5,827,176	$4,818,996	($3,678)	$4,815,317	$4,151,583	($38,201)	$4,113,382	$11,325,974	($1,364,046)	$9,961,929	$30,333,832	($1,626,162)	$28,707,670
10% Base Revenue CAP adjustment	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0		($2,822,170)			($2,822,170)
Net ISRS Revenue Requirement	$4,189,657	($199,790)	$3,989,867	$5,847,623	($20,447)	$5,827,176	$4,818,996	($3,678)	$4,815,317	$4,151,583	($38,201)	$4,113,382	$11,325,974	($1,364,046)	$7,139,758	$30,333,832	($4,448,332)	$25,885,500

Appendix B

Missouri-American Water Company
Case No. WO-2015-0059
ISRS Rate Design Calculation
St. Louis District

Additional ISRS Revenues:

	ISRS Recovery Revenue Requirement	Sales (CCF)	Rates per CCF	Rates per 100 gallons
Rate A & K	$ 7,137,093	48,612,209	$ 0.1468	$ 0.01963
Rate B	$ 1,130	2,365,075	$ 0.0005	$ 0.00006
Rate J	$ 1,536	5,752,615	$ 0.0003	$ 0.00004
Total	$ 7,139,759			

New ISRS Rate:

	Current Rate per CCF	Proposed Rate per CCF
Rate A & K	$ 0.3477	$ 0.4945
Rate B	$ 0.0241	$ 0.0246
Rate J	$ 0.0134	$ 0.0137

	Current Rate per 100 gallons	Proposed Rates per 100 gallons
Rate A & K	$ 0.04644	$ 0.06607
Rate B	$ 0.00325	$ 0.00331
Rate J	$ 0.00176	$ 0.00180

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 its Infrastructure System Replacement Surcharge (ISRS)	))))	Case No. WO-2015-0059

AFFIDAVIT OF JAMES M. RUSSO

STATE OF MISSOURI)
) **ss**
COUNTY OF COLE)

James M. Russo, of lawful age, on oath states: that he participated in the preparation of the foregoing Staff Recommendation in memorandum form, to be presented in the above case; that the information in the Staff Recommendation was provided to him; that he has knowledge of the matters set forth in such Staff Recommendation; and that such matters are true to the best of his knowledge and belief.

James M. Russo

Subscribed and sworn to before me this 12th day of November, 2014.

LAURA BLOCH
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: June 21, 2015
Commission Number: 11203914

Notary Public