Exhibit No.:	
Issues:	Effects of Enacted State and Federal Tax Legislation on Income Taxes and Deferred Income Taxes
Witness:	John R. Wilde
Exhibit Type:	Direct
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2020-0344 SR-2020-0345
Date:	June 30, 2020

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2020-0344
CASE NO. SR-2020-0345

DIRECT TESTIMONY

OF

JOHN R. WILDE

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, John R. Wilde, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am Vice President – Tax Compliance and Strategy 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.

John R. Wilde

John R. Wilde

June 30, 2020

Dated

DIRECT TESTIMONY
JOHN R. WILDE
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2020-0344
CASE NO. SR-2020-0345

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DIRECT TESTIMONY

JOHN R. WILDE

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is John R. Wilde and my business address is 1 Water Street, Camden, New Jersey 08102.

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

A. I am employed by American Water Works Service Company, Inc. ("AWWSC"). My title is Vice President – Tax Strategy and Compliance, and I oversee the tax function for American Water Works Company, Inc. ("American Water" or "AWW") and its subsidiaries.

Q. Please summarize your educational background and business experience.

A. I graduated from Saint Norbert College, De Pere, Wisconsin in 1984 with a Bachelor of Business Administration Degree in Accounting. I have a graduate certificate in state and local taxation, as well as a Master of Science Degree in Taxation from the University of Wisconsin-Milwaukee. I have over 35 years of experience as a tax and accounting professional serving utilities with regulated operations in multiple states. For the fifteen years before my employment with AWWSC, I was the head of the tax function for WEC Energy Group, Inc., formerly Integrys Energy Group, Inc., which included six utilities with operations in four states.

Q. What are your current employment responsibilities?

A. My duties include management and oversight of the corporate tax function for AWW and its consolidated subsidiaries including Missouri-American Water Company ("MAWC" or the "Company").

Q. Have you previously testified before a regulatory body?

A. Yes. I have previously testified before the Federal Energy Regulatory Commission ("FERC"), the California Public Utilities Commission, the Illinois Commerce Commission, the Indiana Utility Regulatory Commission, the Kentucky Public Service Commission, the Michigan Public Service Commission, the Missouri Public Service Commission (the "PSC" or the "Commission"), the Minnesota Public Utilities Commission, the Pennsylvania Public Utility Commission, the Tennessee Public Utility Commission, the Virginia State Corporation Commission, the Public Service Commission of West Virginia, and the Public Service Commission of Wisconsin.

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

A. The purpose of my Direct Testimony is to support and explain the impact of state and federal tax legislation enacted since the Company's last base rate case on the current and deferred income taxes calculated in the Company's filing. Specifically, I will discuss provisions of Missouri SB 884 enacted into law on June 1, 2018 ("MO SB 884"), and the federal Tax Cuts and Job ACT ("TCJA") enacted into law on December 22, 2017.

Q. Can you summarize the provisions of MO SB 884 affecting current and deferred income taxes in the filing?

A. Yes. Effective for tax years beginning on or after January 1, 2020, MO SB 884 reduces the Company's state income tax rate from 6.25%to 4.00%.

Q. Can you summarize the provisions of the TCJA affecting current and deferred income taxes in the filing?

A. Yes. The following four provisions of the TCJA will have an effect on current and deferred income taxes calculated for this filing: (1) effective for tax years beginning on or after January 1, 2018, the TCJA reduced the Company's federal income tax rate from 35 percent to 21 percent; (2) the TCJA provides that the tax normalization rules must be applied by the Company in including the excess accumulated deferred income taxes ("EADIT") due to the TCJA tax rate reduction in its deferred income tax calculations; (3) beginning September 27, 2017, the Company's ability to take advantage of bonus tax depreciation was phased out; and (4) with very limited exceptions, Contributions in Aid of Construction (CIAC) received by the Company after December 22, 2017 are taxable.

<u>II. CURRENT INCOME TAXES</u>

Q. What is the federal and state tax rate used to calculate current tax expense in the filing?

A. The Company used the 21% federal corporate income tax rate enacted as part of the TCJA, and the 4% Missouri corporate income tax rate enacted as part of MO SB 884. The federal benefit of the state income tax deduction is .84%, and the state benefit of federal income tax deduction is .3199%. This sums to the federal and state effective tax rate of 23.8401% used in this filing to calculate current income taxes.

<u>III. DEFERRED INCOME TAXES</u>

Q. Please discuss the concept of deferred income taxes ("DIT") and accumulated deferred income taxes ("ADIT").

A. Generally speaking, ADIT is the product of accumulated book to tax timing (temporary) differences related to like assets and liabilities of the Company. A book to tax temporary difference accumulates and reverses as a balance based on the difference in timing between the tax period when an item of income or expense related to the underlying asset or liability is recognized on the Company's books and provided for in customer rates, and the tax period when an item of income or expense is recognized on a state or federal tax return filed by the Company. As the book to tax difference in the basis of an asset or liability accumulates, ADIT is recorded as a debit or credit to the balance sheet with an offsetting debit or credit to DIT on the income statement. DIT is as a component the Company's cost of service, and the ADIT related to assets and liabilities included in rate base is a component of rate base. ADIT is classified as either deferred income tax liabilities or deferred income tax assets. A deferred tax <u>liability</u> ("DTL"), *i.e.*, a future tax liability, occurs when the Company realizes the tax benefit before it is recognized on its books. When this happens, the Company generally reduces rate base because the funds are not considered investor-supplied. It is important to note that while the funds made available by DTLs are not investor-supplied, neither are they customer-supplied. They are in fact provided by the government – in concept like an interest-free loan – by deferral of tax collections that would otherwise be due. Conversely, a deferred tax <u>asset</u> ("DTA"), *i.e.* a future tax benefit, occurs when MAWC realizes the tax benefit <u>after</u> it recognizes the item on its books. DTAs are therefore part of the interest free loan balance as an amount due from the government All deferred tax balances, whether they are assets or liabilities, reverse over time and converge to zero over the life of the underlying asset or liability balance giving rise to the deferred tax balance. Most utilities, including the Company, carry a net deferred tax liability.

Q. Did the corporate income tax reductions enacted as part of the TCJA and MO SB 884 affect MAWC's ADIT balances for financial accounting purposes?

A. Yes. At December 31, 2017, MAWC had a net federal ADIT liability balance that was the product of the temporary book to tax difference accumulated as of that date multiplied by the effective tax rate computed using an enacted federal tax rate of 35%. At December 31, 2018, MAWC had a state ADIT liability balance that was the product of the temporary book to tax difference accumulated as of that date multiplied by the effective tax rate computed using an enacted state tax rate of 6.25%. Therefore, pursuant to ASC 740 (Accounting for Income Taxes), the respective ADIT balances were re-computed as of each date using the newly enacted federal tax rate of 21% and state tax rate of 4.0%, reducing the respective ADIT as of each date, and pursuant to ASC 980 (Accounting for Regulated Operations) the relevant portion of the reduction of ADIT liability balance was offset by an increase to a regulatory liability representing net excess ADIT (EADIT).

Q. How were the corporate income reductions enacted as part of the TCJA and MO SB 884 treated for regulatory accounting purposes with respect to the ADIT balance included in rate base and DIT included in cost of service?

A. The treatment of the EADIT balance that resulted from the recently enacted changes in federal and state tax rates was deferred pending resolution of the Company's next rate case, *i.e.*, this filing. Therefore, the EADIT balance included in ADIT and rate base will remain unchanged until the amortization of the EADIT into DIT begins as of June, 01 2021.

Q. Has the Company determined the estimated EADIT reserve balance that resulted from the TCJA reduction of the federal corporate income tax rate and the MO SB 884 reduction of the state corporate income tax rate?

A. Yes. The estimated EADIT reserve balance that resulted from the state and federal reductions in the Corporate income tax rate is $148,103,888, of which $150,978,768 is attributable to utility plant investments (plant related), and ($2,874,880) is attributable to other aspects of utility operations (non-plant related). These EADIT balances are shown on Schedule JRW-1 attached to this Direct Testimony.

Q. Could these estimates change?

A. Yes. While these estimates are based on actual tax positions taken on tax returns for tax years before the dates the legislation was enacted, the IRS may issue guidance that would cause MAWC to propose adjustments affecting the amount of EADIT accrued prior to the date of enactment. Similarly, the IRS may audit returns for those years and propose adjustments that would change the amount of accrued EADIT. Therefore, the underlying tax positions and EADIT balances are subject to change through the statute of limitations period, which is three years after the date the Company files its income tax return. In addition, Congress could enact another change in the tax rate during the life of the underlying property. This is in part why I state above the EADIT will be realized over the life of the underlying property.

Q. Will the excess ADIT reserve be credited to customers?

A. Yes. The EADIT will be credited or flowed back to customers through rates over time. It is important to note, however, that the EADIT is not ready cash that is sitting in a bank account. These moneys are already invested in plant, and customers have received the benefit of those deferred taxes through the deduction of the net ADIT balance from rate base. To flow EADIT back to customers will require cash from some other source – perhaps a combination of internally generated funds, debt issuance or equity infusions or issuances. In any event, the flowback of EADIT will put strains on cash flow and, depending on the rate of the flowback, could raise the cost of capital for the Company. The Direct Testimony of MAWC witness Ann Bulkley discusses the financial impacts of the TCJA, including the requirement to flowback EADIT, on American Water and other utilities.

Q. Does the TCJA place any restrictions on the rate that the EADIT reserve is flowed back to customers?

A. Yes. The TCJA requires that federal EADIT generally associated with property, and specifically connected to the accelerated depreciation of property, be amortized into customer rates in a precisely-prescribed manner designed to match the amortization period with the remaining life of the underlying assets—a process referred to as "normalization." The portion of the EADIT reserve subject to the normalization rules is sometimes known as "protected" EADIT. Under the TCJA's normalization requirement, protected EADIT may be amortized by a corresponding reduction in the revenue that the utility collects from customers *no more rapidly* than the reserve would be reduced using the average rate assumption method ("ARAM") to compute depreciation.[1] "Unprotected" EADIT – that is, excess ADIT that is not subject to the IRS normalization rules – may be amortized over any reasonable period selected by the governing state commission.

Q. Has the IRS indicated that it will issue additional guidance with respect to normalization requirements for EADIT?

[1] The TCJA recognizes that utilities that compute depreciation using composite methods may not have the records necessary to compute depreciation using ARAM. If qualified, those utilities may refund the EADIT using an alternate method commonly referred to as the reverse South Georgia method ("RSGM") to compute depreciation. MAWC has the ability to use ARAM due to modifications of American Water's PowerTax and PowerPlant systems completed in 2019.

A. Yes. On May 7, 2019, the IRS released its Notice 2019-33, announcing its intention to issue guidance under section 168 of the Internal Revenue Code to clarify the normalization requirements for excess tax reserves resulting from the TCJA's corporate tax rate decrease. The Notice set forth the general normalization requirements for the reserves mandated by the TCJA and also requested comment on the need for, or desirability of, the issuance of specific guidance on a variety of situations.

Q. Has MAWC broken down its balances into so-called "protected" and "unprotected" EADIT?

A. Yes. Subject to certain limitations due to lack of specific IRS tax guidance, the information has been provided. Schedule JRW-1 contains a column that provides this information. Based on available tax guidance, the inventory indicates the EADIT balances that should be treated as protected for tax purposes (that is, subject to tax normalization), and which should be treated as unprotected for tax purposes. "Protected" line items are identified as "Protected"; "Unprotected" line items are identified as such; and line items for which additional guidance is needed and expected to be issued in the future are labeled "Uncertain."

The balance labeled "Method / Life" is the EADIT related to differences generated by applying book depreciation methods and lives versus tax depreciation methods and lives. IRS guidance is clear that this balance is to be treated as subject to tax normalization, and the Company accordingly has coded it as "Protected."

The negative balance labeled "Cost of Removal" is the EADIT related to the difference between how cost of removal is accounted for book purposes versus tax purposes. There is conflicting IRS guidance with respect to whether this item should be treated as “protected” or “unprotected,” and various commenters have requested guidance with respect to its treatment in response to IRS Notice 2019-33. The Company has indicated the need for additional guidance with the notation “Uncertain.”

The balance labeled “Repairs” is the EADIT related to a book/tax difference arising from the Company’s method of accounting for tax repairs deductions. The IRS has indicated that applicable provisions of the Internal Revenue Code do not require normalization of this EADIT, and, therefore, it has been labeled “Unprotected” in Schedule JRW-1.

The negative balance labeled “Taxable CIAC” is the EADIT related to the taxes paid by the Company on CIAC. This balance is subject to normalization and thus is labeled “Protected.”

The balance labeled “All Other Federal” is not subject to normalization and therefore has been designated “Unprotected.”

The negative balance labeled “Federal Benefit of State” is the state tax deduction taken in the federal tax calculation. Similarly, the positive balance labeled “State benefit of Federal” is the 50% federal tax deduction taken in the state tax calculation. These balances are not subject to normalization and thus have been coded “Unprotected.”

The balanced labeled “State” is the excess ADIT created by MO SB 884. This balance is not subject to normalization and thus has been coded “Unprotected.”

The negative balance labeled “Federal Net Operating Loss Carryover” is related to the federal net operating loss carryforward as of December 31, 2017, and while the IRS has consistently indicated that a taxpayer subject to the tax normalization rules must determine what portion of that balance is related to having claimed protected items and thus is also protected, MAWC is unaware of IRS guidance specific to a rate change like what occurred in the context of the TCJA, and various commenters have requested guidance with respect to its treatment in response to IRS Notice 2019-33. Therefore, the Company coded this balance as "Uncertain" to indicate that more guidance is needed.

The negative balance labeled "State Net Operating Loss Carryover" is related to the state net operating loss carryforward as of December 31, 2019. This balance is not subject to normalization and thus has been coded "Unprotected".

All other plant-related balances (Plant Customer Advances, Plant CWIP, CIAC WIP, Plant 481, and CAC Reserve) are not subject to the normalization requirements and thus are designated "Unprotected." While the Company has labeled plant related EADIT balances as "protected" or "unprotected" in recognition of the fact that this Commission has ordered other utilities to use flow through method of accounting be used to account for unprotected plant related EADIT balances, MAWC has proposed the amortization of, and has accounted for, all plant related EADIT balances using a normalized method accounting, consistent with the normalized method of accounting that established these ADIT balances in prior cases, and consistent with the normalized method of accounting that other MO utilities continue to use for ADIT.

Finally, the negative balance for non-plant related EADIT is not subject to normalization and therefore is designated "Unprotected."

Q. How does the Company propose to flow its EADIT reserves to customers?

A. The Company proposes to use ARAM to determine the amortization and normalization period for all federal EADIT related to plant-in-service ("Protected," "Unprotected," and "Uncertain") as of the date of the enactment of the TCJA. The Company proposes a 20 year period to amortize the EADIT related to non-plant items (the "Non-Plant Other" regulatory asset balance on Schedule JRW-1). In both cases, the normalization/amortization was computed beginning January 1, 2018, the effective date of the TCJA. For the period from January 1, 2018 until the start of the credit on June 1, 2021 (the "catchup" period), the normalization/amortization was treated as deferred. The Company proposes to amortize and flow through the deferred "catchup" period EADIT amortization over a five-year period, from June 1, 2021 through May 31, 2026. The Company proposes the same treatment for the state EADIT as of the enactment of MO SB 884. As shown on Schedule JRW-1, the ongoing normalization/amortization will produce an annual credit of $3,932,609, and the amortization of the catchup period balance will produce an annual credit of $1,494,552 for five years. The total EADIT amortization for the rate year of June 1, 2021 through May 31, 2022 will thus be $5,427,161.

Q. Why does MAWC propose to use ARAM to normalize all EADIT related to plant in service (Unprotected and Uncertain as well as Protected), when the IRS normalization rules only require ARAM to be used for Protected EADIT?

A. It is the long-term best interest of MAWC's customers to use ARAM to normalize both "protected" and "unprotected" plant-related EADIT, for several reasons. First, using ARAM to normalize all EADIT related to plant in service promotes inter-generational equity. All of the plant-related EADIT are unrealized permanent tax benefits that accrued as a result of the Company making investments in plant in service and claiming tax deductions in excess of book at a time when the federal corporate income tax rate was 35%, that will be realized as the reverse at an enacted rate that is currently assumed to be 21%. Now, however, as a result of the TCJA, the tax benefits will reverse as book depreciation is recovered as a cost from customers when the tax rate will be 21%. These unrealized permanent benefits, which relate to the deduction of costs not yet recovered in rates from customers, should be returned ratably to those same customers who will be required to pay the costs of the plant to which the benefits relate as those tax benefits are realized. The use of ARAM closely aligns the normalization of these benefits to the investments that gave rise to the benefits, and thus to the customers who will bear the costs of those investments over their lives. Second, the use of ARAM reduces the total cost of capital recovered from customers over the underlying useful life of the plant in service investment. Third, the use of ARAM also will add to the stability of cost of service rates over the useful life of the property. Alternatively, severing the amortization of unprotected EADIT balances from the related plant in service would distribute a tax benefit to customers that is disproportionate to the cost to which the benefit relates, and thus benefit customers during the abbreviated amortization period to the detriment of customers who continue to pay for these investments over the property's remaining useful life. Using a shorter period to amortize unprotected plant-related EADIT also would increase the cost of service recovered from customers over the life of the property.

Q. Please explain further how using ARAM to normalize EADIT promotes inter-generational equity.

A. The normalization concept prevents the inter-generational inequity that can occur when the flow-through method is used. If MAWC uses an immediate or close-to-immediate flow-through method, current customers receive the entire refund and benefit disproportionally. This occurs even if tax rates change again before the timing difference reverses. For example, assume an EADIT balance has been generated with respect to the tax benefits associated with an asset with a book depreciation life of 35 years. If a shorter flow-through method is used for the EADIT, customers who take service during the flow-through period realize 100% of the benefit from the TCJA, whereas the customers paying for the asset during the remainder of its life realize none of the benefit. The asset giving rise to the benefit, however, will serve all of them. What is also inequitable for those later customers is the accelerated increase in rate base. The entirety of the EADIT will have already been returned over the flow-through period, resulting in a larger rate base and thus a greater revenue requirement for the remainder of the life of the asset giving rise to the benefit. Future customers are unfairly penalized, and doubly so, because they may not receive any refund, and yet pay for the cost of the utility asset over its remaining useful life. Even worse, if tax rates are raised in the future, future generations will have to pay for the deficient ADIT because any prior excess will have been refunded to prior customers. Normalization ensures that tax benefits are spread to all customers who benefit from the Company's long-lived assets and not just current customers. MAWC therefore believes that the normalization concept should be applied to all plant-related EADIT (including state EADIT) and its amortization should be calculated pursuant to ARAM without regard to its status as protected or unprotected.

Q. Why did the Company use a 20-year period to amortize non-plant-related EADIT balances?

A. A 20-year amortization period is consistent with the life of the underlying assets and liabilities, thus it is intended to normalize the EADIT tax benefit over the underlying life of the assets and liabilities to which it related. These EADIT balances are related to deductions claimed with respect to two primary types of assets and liabilities: regulated deferred assets and liabilities, and assets and liabilities related to providing employee benefit programs. The vast majority of the EADIT balance that falls into these categories would be associated with assets and liabilities that will reverse over periods greater than 20 years. Thus, it is reasonable to match the reversal or recovery period of the incurred costs that gave rise to the EADIT to the period the EADIT is amortized.

Q. Are current customers harmed by normalizing or amortizing EADIT over longer rather than shorter periods?

A. No. First, rate base is the sum of plant, less accumulated book depreciation, and less ADIT. EADIT is a component of the ADIT in rate base, and thus, until EADIT is flowed-back to customers, it provides customers with a return equal to the utility's weighted average cost of capital. Second, as I have explained, EADIT is simply a portion of a temporary benefit that was made permanent by the federal government's passage of the TCJA; the cost that gave rise to the benefit was a component of plant in service and relates specifically to the portion of plant in service that has not yet been paid for, consumed or used by current customers. The permanent nature of the benefit is still dependent on future events, such as a 21% federal tax rate remaining the enacted rate for the 35 years or more over which the underlying temporary differences will reverse and the benefit of the lower tax rate will be realized. The customers who will pay for and use the investment should receive the benefit that arose when the utility put the asset in place.

Rates are intended to provide a utility with the opportunity to earn an adequate after-tax return on the portion of the utility's investment in plant that is financed with equity. The after-tax return is grossed up to produce its pre-tax equivalent. That amount is the same regardless whether a portion of the tax will be deferred or not. The tax code allows some or all of the tax that would be otherwise be due on pre-tax earnings to be deferred as an incentive to the utility to invest, and in some cases Congress has explicitly acted to prevent flow through of a tax benefit intended to be an investment incentive and not a rate subsidy. A prime example of Congress's protection of certain tax incentives to utilities is the tax normalization rules applicable to ADIT and EADIT.

Q. Have any other public utility commissions approved the amortization of unprotected plant-related EADIT balances pursuant to ARAM?

A. Yes. The Pennsylvania Public Utility Commission has approved a settlement providing that the utility, Duquesne Light Company, will flow back unprotected EADIT related to prior tax repairs and other deductions pursuant to ARAM.[1] Duquesne Light Company described this settlement term and the reason the Pennsylvania Office of Consumer Advocate did not oppose it in its publicly-filed Statement in Support of the Joint Petition for Settlement as follows:

> Under the TCJA, certain excess deferred taxes must be returned to customers over the life of the property, with the unreturned or unamortized amounts deducted from rate base, thereby benefiting customers (the Average Rate Assumption Method or ARAM). While other excess deferred taxes are not subject to this requirement, and OCA proposed accelerated return of such amounts, the Company demonstrated in its rebuttal that accelerated return would increase rates by over $52 million. … In surrebuttal, OCA withdrew the adjustment. … The Settlement provision affirms that all EDIT related to plant will be returned under the ARAM procedure and that unamortized balances will be deducted from rate base in future base rate proceedings, thereby benefiting customers.[2]

[1] *Pennsylvania Public Utility Commission v. Duquesne Light Company,* Docket No. R-2018-3000124 *et al.*, 2018 WL 6931959 at *8, *22 (Pa. Pub. Util. Comm'n Dec. 20, 2018).

[2] *Pennsylvania Pub. Util. Comm'n v. Duquesne Light Co.*, Docket No. R-2018-3000124 (Pa. Pub. Util. Comm'n), Duquesne Light Company's Statement in Support of Joint Petition for Approval of Settlement Stipulation ¶ 6 at 11 (filed Sept. 14, 2018) (record citations omitted). Duquesne Light Co.'s Statement in Support was filed as Appendix G to the parties' Joint Petition for Approval of Settlement Stipulation filed with the Pennsylvania Commission on September 14, 2018.

Most recently, the Indiana Utility Regulatory Commission approved a settlement that provides that MAWC's affiliate, Indiana-American Water Company, Inc. shall amortize all of its EADIT, protected and unprotected, pursuant to ARAM.[3]

As explained above, amortizing MAWC's unprotected plant-related EADIT over an amortization period shorter than that produced by ARAM would increase the cost of service recovered from customers over the life of the property. Like the settlement approved by the Pennsylvania Commission in the **Duquesne Light Company** case, the Company's proposal "affirms that all EDIT related to plant will be returned under the ARAM procedure and that unamortized balances will be deducted from rate base in future base rate proceedings, thereby benefiting customers." Therefore, it is in the long-term best interests of the Company's customers and should be approved.

IV. ACCUMULATED DEFERRED INCOME TAX – RATE BASE REDUCTION

Q. Does the Company reduce Rate Base by the amount of ADIT?

A. Yes. ADIT represents a "loan" from the federal and state governments, which is essentially a zero cost source of capital. As such it is appropriate to reduce rate base by these amounts.

Q. How does the Company determine the amount of ADIT used to reduce rate base?

A. In general, all plant-related ADIT that have been normalized are included as a reduction to rate base. The primary source of the information for determining ADIT comes from the calculation of ADIT performed in PowerTax, which is the tax module in the software accounting suite developed and sold by PowerPlan Consultants Inc. ("PowerPlan").

[3] *In re: The Indiana Utility Regulatory Commission's Investigation into the Impacts of the Tax Cuts and Jobs Act of 2017 and Possible Rate Implications under Phase 1 and Phase 2 for Indiana American Water Company, Inc.*, Cause No. 45032 S4, slip op. (Ind. Util. Regulatory Comm'n June 24, 2020).

Q. Please describe what the ADIT balance generated by PowerTax represents and what other amounts or adjustments are made to get to the rate base reduction for ADIT used in MAWC's rate filing.

A. PowerTax tracks the ADIT on "in service" Property Plant and Equipment. It was set up with ADIT calculated at the most recent pre-TCJA income tax rates. Therefore, the ADIT tracked by PowerTax includes in the ADIT balance the EADIT produced by the TCJA's tax rate reduction that has not yet been amortized pursuant to ARAM. PowerTax was populated with estimated plant additions and book depreciation for relevant periods after December 31, 2019. To that number, the Company adds ADIT on plant-related items such as construction work in progress, customer advances for construction, etc., that are not maintained in the PowerTax system. In addition, certain other non-plant related items are included in rate base. Therefore, the related ADIT has been included. These items include ADIT related to regulated asset/liability trackers for deferred tank painting, pension, OPEB and regulated asset deferrals. Finally, because income tax rates on PowerTax items are at the pre-TCJA level, there are other sources of excess and deficient ADIT that are not related to the TCJA's rate reduction. Those elements of non-TCJA-related EADIT, for which the ARAM is not used, are addressed and amortized (using the Reverse South Georgia Method) and, to the extent they are unamortized, are included in the ADIT balance that is deducted from rate base.

Q. Are there any other adjustments to ADIT that have been made?

A. Yes. The Company is setting rates for a future test year, and is using supporting data for that period of time to calculate its proposed rates. Under IRC normalization rules changes to the ADIT during that period after new rates go in effect are subject to a proration formula under Treas. Reg. § 1.167(l)-1(h)(6).

Q. Can you address the effect that the phase out of bonus depreciation has on income taxes calculated in the filing?

A. Yes, as of the beginning of the test year used by the Company in this filing bonus depreciation is not available to the Company. On a comparative basis, the loss of bonus depreciation reduces the amount of current tax originating from existing utility operations that can be deferred by investing in additional utility plant, increasing current tax obligations payable to federal and state governments. This in turn reduces the DIT and ADIT accruals, which is a reduction in the amount of zero cost capital available to finance investments in utility plant as reflected in the increase in rate base in this proceeding.

Q. Can you address the effect of CIAC not being taxable on income taxes calculated in the filing?

A. Yes, on a comparative basis, CIAC being taxable reduces the amount of current tax originating from existing utility operations that can be deferred by investing in additional utility plant, increasing current tax obligations payable to federal and state governments. This in turn reduces DIT and ADIT accruals, which is a reduction in the amount of zero cost capital available to finance investments in utility plant as reflected in the increase in rate base in this filing.

Q. Does the reduction in the state and federal income tax rate, the amortization of EADIT, the loss of bonus depreciation, and the taxation of CIAC all have a similar effect on DIT and ADIT balances as computed in the filing?

A. Yes, all reduce DIT and ADIT amounts computed in the filing, decreasing the amount of zero cost capital available to finance investments in utility plant and increasing the rate base in this filing.

Q. Would using a method and period that results in an amortization amount for plant-related EADIT greater than that produced by using ARAM further reduce the amount of zero cost capital available to finance investment in utility plant and further increase rate base?

A. Yes, an increase in the amortization of EADIT reduces DIT and ADIT accruals, which results in a reduction in the amount of zero cost capital available to finance investments in utility plant and an increase in the Company's rate base.

Q. Does this conclude your Direct Testimony?

A. Yes, it does.

Missouri American Water
TCJA Excess ADIT

Plant										Catchup Amortization Jan 2018 - May 2021	Jun 2021 - May 2026	Annual	Total Amortizatior
Utility Plant in Service (PowerTax)													
Item	**Amortization Method**	**Period**	**Categorization pursuant to Tax Normalization rules**	**Net Excess Accumulated Deferred Income Taxes**	**2018 Amortization**	**2019 Amortization**	**2020 Amortization**	**2021 Amortization**	**2022 Amortization**	**Total**	**5 Yr amortization**	**June 1 2021 - May 31, 2022**	**June 1 2021 - May 31, 2022**
Method / Life	ARAM	Asset Life	Protected	88,399,376	1,392,333	1,622,510	4,369,309	1,591,308	2,377,784	8,047,197	1,609,439	1,919,007	3,528,446
Cost of Removal	ARAM	Asset Life	Uncertain	(3,760,653)	(1,240,398)	(765,677)	(869,689)	-	-	(2,875,764)	(575,153)	-	(575,153)
Repairs	ARAM	Asset Life	Unprotected	72,455,741	1,540,916	1,825,452	2,751,206	2,507,646	2,565,517	7,162,427	1,432,485	2,531,759	3,964,245
Taxable CIAC	ARAM	Asset Life	Protected	(5,233,286)	(310,249)	(310,315)	(310,245)	(310,245)	(310,245)	(1,060,078)	(212,016)	(310,245)	(522,261)
All Other Federal	ARAM	Asset Life	Unprotected	11,359,061	147,891	79,450	(2,535,377)	232,303	375,954	(2,211,243)	(442,249)	292,158	(150,091)
Federal Benefit of State	ARAM	Asset Life	Unprotected	(10,170,006)	(95,621)	(153,178)	(339,053)	(403,050)	(503,945)	(755,790)	(151,158)	(445,090)	(596,248)
State Benefit of Federal	ARAM	Asset Life	Unprotected	4,244,708	-	-	85,144	103,474	129,955	128,258	25,652	114,508	140,159
State	ARAM	Asset Life	Unprotected	23,836,804	-	-	605,621	733,049	921,703	911,059	182,212	811,655	993,867
Sub-Total (UPIS)				181,131,746	1,434,873	2,298,243	3,756,917	4,454,485	5,556,725	9,346,068	1,869,214	4,913,751	6,782,965
CWIP, CAC, and other Non-UPIS Plant items													
Item	**Amortization Method**	**Life**											
Plant Customer Advances	ARAM	Asset Life	Unprotected	(2,966,611)	(25,949)	(41,563)	(63,424)	(75,017)	(93,491)	(162,194)	(32,439)	(82,714)	(115,153)
Plant CWIP	ARAM	Asset Life	Unprotected	22,445	(19)	(31)	449	544	685	625	125	603	728
CIAC WIP	ARAM	Asset Life	Unprotected	(164,075)	(1,390)	(2,226)	(3,501)	(4,144)	(5,166)	(8,844)	(1,769)	(4,570)	(6,339)
Plant 481	ARAM	Asset Life	Unprotected	940,523	8,818	14,123	20,193	23,847	29,701	53,070	10,614	26,286	36,900
Federal Net Operating Loss Carryover	ARAM	Asset Life	Uncertain	(22,818,613)	(213,929)	(342,650)	(489,925)	(578,564)	(720,597)	(1,287,572)	(257,514)	(637,744)	(895,258)
State Operating Loss Carryover	ARAM	Asset Life	Unprotected	(5,166,647)	-	-	(103,909)	(125,772)	(158,140)	(156,314)	(31,263)	(139,259)	(170,522)
Sub-Total (Non-UPIS)				(30,152,978)	(232,470)	(372,348)	(640,118)	(759,106)	(947,008)	(1,561,229)	(312,246)	(837,398)	(1,149,644)
Sub-Total Plant				150,978,768	1,202,403	1,925,895	3,116,799	3,695,379	4,609,717	7,784,839	1,556,968	4,076,353	5,633,321
Non-Plant Other	Normalization	20 Years	Unprotected	(2,874,880)	(54,221)	(54,221)	(143,744)	(143,744)	(143,744)	(312,080)	(62,416)	(143,744)	(206,160)
Total				148,103,888	1,148,182	1,871,674	2,973,055	3,551,635	4,465,973	7,472,759	1,494,552	3,932,609	5,427,161