STATE OF IOWA
DEPARTMENT OF COMMERCE
BEFORE THE IOWA UTILITIES BOARD

IN RE:	:	**DOCKET NO. RPU-2020-0001**
	:	**TF-2020-0250**
IOWA-AMERICAN WATER COMPANY	:	

REPLY TO OCA RESPONSE TO MOTION FOR CLARIFICATION

COMES NOW Iowa-American Water Company ("Iowa-American" or "Company") and files the following Reply to the July 23, 2021 Response ("Response") of the Office of Consumer Advocate ("OCA") to the Motion for Clarification ("Motion") filed with the Iowa Utilities Board ("Board") by the Company on July 9, 2021.

I. The Issue

The primary issue put before the Board by Iowa-American's Motion is how to fairly reflect the ratemaking adjustments necessitated by the Board's June 28, 2021 Final Decision and Order in this Docket ("Order"), which requires Iowa-American to return to customers a credit of the benefits of accelerated amortization of the unprotected Excess Accumulated Deferred Income Taxes ("EADIT") that, prior to the Tax Cuts and Jobs Act of 2017 (the "TCJA"), served as a reduction to the Company's rate base.[1] The proposals of both Iowa-American and OCA are discussed further in this Reply. Only Iowa-American's proposal results in:

* Returning to customers of the exact amount of unprotected EADIT credit, and no more, that previously served as a reduction to the Company's rate base;
* Correctly valuing Iowa-American's rate base going forward; and,
* Preventing the taking of the Company's property that would occur if the value of the credited EADIT continues to be recognized as a reduction to its rate base.

[1] As the Board knows, rate base represents the amount of investor-supplied capital used to supply property that is used and useful in providing utility service to the Company's customers. As discussed in the Company's testimony in this docket, EADIT represents income tax payments that are deferred in accordance with federal tax law. So, for accounting and ratemaking purposes, EADIT serves to reduce the value of the Company's rate base, i.e., it offsets the amount of investor-supplied capital that supports rate base. When those taxes are finally paid, or as in this case when they are paid at a tax rate lower than that under which they were deferred, the offset no longer exists, and rate base must be increased to recognize that the Company's investors are now supplying all of the capital used to supply the property that is used to provide service to customers. *See generally*, IAWC Wilde Direct Testimony ("Wilde Direct"), pp. 19-22; IAWC Wilde Reply Testimony ("Wilde Reply"), pp. 7-8.

OCA's proposal, on the other hand, will result in:

* A credit of amounts to the Company's customers in excess of the EADIT on Iowa-American's books;
* Undervaluing Iowa-American's rate base going forward; and
* A taking of the Company's property by failing to recognize that its rate base must be increased by the amount of EADIT credited.

Iowa-American's proposal should be approved by the Board.

I. Background

The EADIT issue was the subject of much testimony in this case.[2] Iowa-American and OCA both recognized that the EADIT credit should be returned to customers as a result of the TCJA. They disagreed on the period of time over which unprotected EADIT should be returned to customers.[3] Importantly for purposes of the Motion, both Iowa-American and OCA agreed that the Company's rate base must be increased when EADIT is credited to customers.[4] The parties also recognized that the precise amounts would need to be determined by additional calculations once the Board decided the period over which the return were to occur.[5] However, the Board's Order, which mandated that EADIT should be returned to the Company's customers over three years and which specifically recognized that rate base should be increased as a result[6], did not include the necessary adjustment.

Because the testimony in this case was unanimous in acknowledging the required rate base adjustment, Iowa-American assumed that the Board simply overlooked the necessity for the adjustment. On July 9, 2021, the Company filed its Motion, included the requisite PowerTax calculations that reflected the three-year EADIT credit and asked the Board to approve the schedules filed with the Motion and the methodology reflected therein. Iowa-American's Motion shows that as a result of the Board's Order to return the EADIT credit to customers over a three-year period, the Company's rate base will increase by $3,749,416 to $148,429,283 and that the revenue increase and revenue requirement should be increased to

[2] *See* Wilde Direct, pp. 5-22; Wilde Reply, pp.1-11; OCA Kruger Direct Testimony ("Kruger Direct"), pp. 28, 30, 36-42 ; OCA Kruger Rebuttal Testimony ("Kruger Rebuttal"), pp. 43-49; Tr. pp. 250-58.
[3] *See* Wilde Direct, pp.13-20; Wilde Reply, pp.3-7; Wilde Reply Exhibit 1; Kruger Rebuttal, p. 48; Tr. pp. 351-52.
[4] Wilde Direct, pp. 19-21; Wilde Reply, pp. 7-9; Kruger Direct, p. 28; Kruger Rebuttal, p. 45; Tr. p. 353
[5] Tr. pp. 353-56.
[6] Order, p. 66.

$2,654,290 and $44,215,409, respectively. This represents an increase in the Company's revenue requirement of $420,003 related to unprotected EADIT.

Because the Board had not ruled on the Company's Motion prior to the date set in the Final Order for Iowa-American to make its compliance filing to implement the Order, and because Iowa-American assumed the Board inadvertently overlooked the necessity to adjust rate base for the ordered EADIT return, the Company's compliance filing incorporated the adjustments proposed in the Motion. OCA's Response takes issue with the methodology and calculations proposed by the Company.

II. Iowa-American's Proposal - Rate Base Adjustment and Reconciliation

A. Legal Basis for the Proposal.

The Board's Order mandates that Iowa-American return the entire balance of EADIT credit - $4,488,678 - over a three-year period.[7] In a perfect world in which the Company's rate base could be adjusted outside of a general rate case, Iowa-American would increase its rate base by one-third of that amount in the test year and each of the two subsequent years to reflect the removal of each year's EADIT credit as a reduction to the Company's rate base. However, it is not legally permissible to make rate base adjustments outside of a general rate case due to the prohibition against single issue ratemaking. Therefore, unless the entire amount of the Company's EADIT credit obligation is removed as a reduction to rate base at the beginning of the test period, i.e., the first return year, Iowa-American's rate base will be undervalued in each of the two succeeding years. Further, because Iowa-American is effectively prohibited from filing another rate case until the conclusion of the subsequent proceeding anticipated by Iowa Code § 476.33(4)(b) and Board Rule 199 IAC 26.6 – approximately two years – the Company will be precluded from ever recovering the revenues lost by virtue of the failure to make the necessary rate base and revenue requirement adjustments outside of a general rate case. However, the Company recognizes that removal of the entire EADIT amount as a reduction to rate base at the beginning of the test period, in the absence of any reconciling adjustments, would result in customers paying rates based on a rate base that is higher than it

[7] Order, p. 67.

should be in light of the EADIT credits actually being made. Accordingly, as discussed in the following section of this Reply, the Company's proposal addresses that issue as well.

B. Iowa-American's Proposed Methodology

Iowa-American's Motion included schedules supporting a revenue requirement of $44,215,409. That revenue requirement reflects an increase of $420,209 that is related to the removal of the entire $4,488,678 in unprotected EADIT as a reduction to the Company's rate base[8]. The Company has stated in its testimony[9] and in its Motion[10] that the effects of the TCJA, including those related to unprotected EADIT and its relation to rate base, should be reconciled to actual. Iowa-American's goal with respect to the proposed reconciliation is that, at the end of the three-year EADIT credit return period, the Company's customers receive the full benefits of the TCJA and no more, the value of the Company's rate base is correct, and the Company's base rates are correct. The Company's proposal to implement the EADIT credit return accomplishes each of these intended goals.

Because the total amount of EADIT to be credited, and Iowa-American's legal obligation to return that amount, are legally fixed as a result of the Order, Iowa-American has proposed to create a regulatory liability in that amount, grossed up for taxes, on the first day of the future test period and to remove that amount as a reduction to the Company's rate base on that date, thereby increasing its rate base by that amount. Thereafter, in each of the three years following approval of final rates in this case (the first such year being the test year), Iowa-American will return to its customers in equal monthly installments, one-third of the EADIT regulatory liability credit. In addition, Iowa-American will reconcile the amounts paid by its customers that reflect the increase in rate base caused by the removal of the total EADIT liability to the amounts that would have been paid had rate base been increased by one-third of that liability in each of the three return years. The difference will then also be credited to the Company's customers and returned.

The tables below illustrate by way of example the mechanics of Iowa-American's proposal. The tables show that over the three-year EADIT return period, customers will receive: 1) a credit for the

[8] Motion page 3, item 3.
[9] IAWC Simmons Reply at page 30.
[10] Motion page 3, item 4.

unprotected EADIT, 2) a reconciliation credit for the revenue effect of the rate base difference, and 3) a credit or addition reflecting the over/under from the following year's reconciliation.

Table 1 reflects the calculation of the EADIT credit, its effect on customers and its effect on the Company. Table 2 reflects the unprotected EADIT credit, and the rate base credits that will flow through the Non-recurring Revenue and Expense Rider.

Table 1 – Calculation of Revenue Credit
(Revenue Requirement: $44,215,409)

	Description	Year 1	Year 2	Year 3	Year 4
	Unprotected EADIT Credit Effects on Revenue Requirement:				
1	Amount of Revenue Requirement Increase Resulting from EADIT Removal as a Reduction to Rate Base	$420,209	$420,209	$420,209	$420,209
2	1/3 EADIT Credit Effect on Revenue Requirement.*	$(70,035)	$(210,105)	$(350,174)	$(420,209)
3	Non-Recurring Expense Rider Credit/(Expense)	$350,174	$210,105	$70,035	$0
	Effects on Customer and Company:				
4	Revenue Requirement Effect of Rate Base Increase to Customers (Base Rates and Rider)	$70,035	$210,105	$350,174	$420,209
5	Company Financial Loss	$0	$0	$0	$0

* $11,672 ($420,209/36 months) per month in earned revenue requirement minus 6 months to reach year midpoint.

Table 2 – Non-Recurring Expense Item Reconciliation

	Description	Year 1	Year 2	Year 3	Year 4
1	Unprotected EADIT	$(2,099,730)	$(2,099,730)	$(2,099,730)	$0
2	EADIT Rate Base Effect on Revenue Requirement from Table 1 Line 3.	$(350,174)	$(210,105)	$ (70,035)	$0
3	Total Unprotected EADIT Credit	$(2,449,905)	$(2,309,835)	$(2,169,765)	$0

These tables show that under Iowa-American's proposal, in the fourth year following implementation of rates the revenue requirement is correct, base rates are correct and the unprotected EADIT has been fully returned to customers with credits for its effect on rate base. Iowa-American's Motion assumed, based on the Joint Statement of Issues filed prior to the hearing in this case, which designated this issue as uncontested,[11, 12] that the reconciliation would be conducted, and the resultant amounts including rate base adjustments would be added to the following year as a reconciliation item. If the Board prefers a more contemporaneous approach, the Company can easily edit the filed proposed Non-Recurring Revenue and Expense Rider to flow back an estimate of the credit in each current return year (as shown in Table 2 above in the amount of $350,174) which would then be reconciled, subject to Board and OCA review, in the following return year. Such an approach has been taken in Iowa, for example in Energy Efficiency Cost Recovery Mechanisms, where an estimate is included in riders which is then reconciled after the end of the period.

III. OCA's Proposal - Rate Base Adjustment and Rider

OCA asserts that the revenue requirement in the Board's Order[13] is correct even though it reflects the full amount of unprotected EADIT as a reduction to rate base.[14] OCA's position is that rate base should

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[11] Joint Statement of Issues, Section VI, NONRECURRING EXPENSES, ¶ C.

[12] Company Witness Wilde's testimony, filed well before the Joint Statement of Issues was filed, explicitly stated that such adjustments would be required. *See* Wilde Reply, p. 10, stating that a true-up should "include a true up of the revenue requirement both from the change in ADIT amortization and from the resulting change in rate base."

[13] $43,813,200. *See* Order, p. 80.

[14] Response, p. 1. Notably, Witness Kruger admitted at hearing that he made only a cursory attempt at estimating the impact of the EADIT impact on rate base. *See* Tr., pp. 353 et. seq.

only reflect the credit and return made during the test year[15] and that rate base should reflect the amount of outstanding EADIT not yet returned to customers as a reduction to rate base for the test year.[16] However, OCA's proposal ignores the rate base effects of the EADIT credits that occur the two years subsequent to the test year and will result in the permanent financial loss to the Company of $1,032,215 over four years.[17]

The tables below illustrate by way of example the results of OCA's proposal.[18]

Table 3 – Calculation of Revenue Credit
(Revenue Requirement: $43,813,200)

	Description	Year 1	Year 2	Year 3	Year 4
	Unprotected EADIT Credit Effects on Revenue Requirement:				
1	Amount of Revenue Requirement Increase Resulting from EADIT Removal as a Reduction to Rate Base	$0	$0	$0	$0
2	1/3 Credit Effect on Revenue Requirement.*	$70,035	$ 210,105	$350,174	$ 420,209
3	Non-Recurring Expense Rider Credit/(Expense)	$0	$0	$0	$0
	Effects on Customer and Company:				
4	Revenue Requirement Effect of Rate Base Increase to Customers (Base Rates and Rider)	$(70,035)	$(210,105)	$(350,174)	$(420,209)
5	Company Financial Loss	$70,035	$210,105	$350,174	$420,209

* $11,667 ($420,209/36 months) per month in earned revenue requirement minus 6 months to reach year midpoint.

[15] Response p. 2, ¶ 3.
[16] Response p. 4, ¶ 5.
[17] Shown in Table 3 as the sum of Line 5.
[18] In contrast to Tables 1 and 2, the amounts of the Company's rate base, revenue requirement and base rates used as a starting point for Tables 3 and 4 do not account for the any of the effects of the EADIT credit to rate base.

Table 4 – Non-Recurring Expense Item Reconciliation

	Description	Year 1	Year 2	Year 3	Year 4
1	Unprotected EADIT	($2,099,730)	($2,099,730)	($2,099,730)	$0
2	EADIT Rate Base Effect on Revenue Requirement from Table 3, Line 3.	$0	$0	$0	$0
3	Net Unprotected EADIT Credit	($2,099,730)	($2,099,730)	($2,099,730)	$0

Line 4 of Table 3 shows clearly that the customers are not paying, in either base rates or through a rider, the revenue requirement effects resulting from application of the Board's Order to return the unprotected EADIT credit. Moreover, the OCA's proposal does not allow for any reconciliation. The cumulative result of OCA's proposal is that Iowa-American will credit more money to its customers, through the rider and base rates taken together, than the unprotected EADIT credit to which they are entitled. This, combined with the fact that under OCA's proposal the Company lose any opportunity to recover revenue lost by virtue of the inability to make the necessary rate base during the years subsequent to the test year, renders OCA's proposal unreasonable.

V. An Alternative -Rates as Ordered with Rate Base Reconciliation

An alternative methodology that would operate to keep both the Company and its Customers whole would be to reflect, in the non-recurring item rider, all rate base effects caused by the return of EADIT credit, and then roll them into base rates in a future general rate case. At the end of year three, the rate base effects would remain in the rider and be collected by the Company until such time as the Company has a new rate case to set base rates, at which time, the rider amount would reset to zero. The effect would be a base rate item, i.e., a revenue requirement change caused by rate base, recovered in a rider. This option leaves everyone whole but would result in some rate volatility, as the tables below illustrate.

Table 5 – Calculation of Revenue Credit
(Revenue Requirement: $43,813,200)

	Description	Year 1	Year 2	Year 3	Year 4
	Unprotected EADIT Credit Effects on Revenue Requirement:				
1	Amount of Revenue Requirement Increase Resulting from EADIT Removal as a Reduction to Rate Base	$0	$0	$0	$0
2	1/3 EADIT Credit Effect on Revenue Requirement*	$70,035	$210,105	$350,174	$420,209
3	Non-Recurring Expense Rider Credit/(Expense)	$(70,035)	$(210,105)	$(350,174)	$(420,209)
	Effects on Customer and Company:				
4	Revenue Req. Effect of Rate Base to Customers (Base rates and Rider)	$70,035	$210,105	$350,174	$420,209
5	Company Financial Loss	$0	$0	$0	$

* $11,667 ($420,209/36 months) per month in earned revenue requirement minus 6 months to reach year midpoint.

Table 6 – Non-Recurring Expense Item Reconciliation

Description	Year 1	Year 2	Year 3	Year 4
Unprotected EADIT	($2,099,730)	($2,099,730)	($2,099,730)	$0
EADIT Rate Base Effect on Revenue requirement from Table 5, Line 3.	$70,035	$210,105	$350,174	$420,209
Net Unprotected EADIT Credit	$(2,029,696)	$(1,889,626)	$(1,749,556)	$420,209

VI. Conclusion and, if Needed, Request for Technical Conference

The foregoing discussion demonstrates that Iowa-American's EADIT proposal is the *only* option that results in customers receiving the full TCJA benefits related to EADIT and no more, the correct valuation of the Company's rate base going forward, and correct base rates. To accomplish the Company's proposal, it would only need to revise the Non-Recurring Expense Rider to include an estimate of the rate base credit from the tariffs and exhibits filed on July 16, 2021. The third option, containing an increasing rate base charge through the rider would require revised rates, cost of service, revenue requirement and rider. Iowa-American's proposal is not only the most reasonable, but the most efficient. OCA's proposal, on the other hand, would not result in reasonable and lawful ratemaking. Rather, OCA's proposal would clearly result in customers being unduly benefited and the Company being unduly disadvantaged. As such it is not reasonable or lawful.

For the reasons set out in the Reply and Motion, the Company's proposal should be approved. However, in the event that the Board or its staff have additional questions concerning the Motion and the proposal set forth therein, Iowa-American suggests that the Board conduct a technical conference at which those questions might be addressed. Given that Iowa-American's new rates will not become effective until the Board rules on the Motion and the Company's July 16, 2021 Compliance Filing, Iowa-American requests that such a technical conference be scheduled as soon as possible.

WHEREFORE, Iowa-American Water Company asks the Board for clarification of its Final Decision and Order as described in the Company's July 9, 2021 Motion.

Dated this 28th day of July 2021.

Respectfully submitted,

BROWN, WINICK, GRAVES, GROSS & BASKERVILLE, P.L.C.

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