

OFFICIAL EXHIBITS

FILED
May 12, 2020
INDIANA UTILITY
REGULATORY COMMISSION

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

IN THE MATTER OF 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 S 4

IURC
RESPONDENT'S

EXHIBIT NO.

5-28-20
DATE

REPORTER

RESPONDENT'S SUBMISSION OF TESTIMONY IN SUPPORT OF SETTLEMENT

Indiana-American Water Company, Inc. ("Respondent"), by counsel, hereby submits the Settlement Testimony of Gregory Shimansky. Mr. Shimansky's Workpapers are being filed and served in Excel format simultaneously herewith.

Respectfully submitted,

/s/ Hillary J. Close

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CERTIFICATE OF SERVICE

The undersigned attorney hereby certifies that a copy of the foregoing has been served upon the following via electronic mail this 12th day of May, 2020 to:

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INDIANA-AMERICAN WATER COMPANY, INC.

IURC CAUSE NO. 45032 S4

SETTLEMENT TESTIMONY

OF

GREGORY D. SHIMANSKY

**SETTLEMENT TESTIMONY
OF
GREGORY D. SHIMANSKY**

CAUSE NO. 45032 S4

1 **Q. Please state your name and business address.**

2 A. My name is Gregory D. Shimansky and my business address is 153 N. Emerson Avenue,
3 Greenwood, IN 46143.

4 **Q. What is your position?**

5 A. I am employed by American Water Works Service Company (“AWWSC” or “Service
6 Company”) as Director of Rates & Regulatory for Indiana and Michigan. The Service
7 Company is a subsidiary of American Water Works Company, Inc. (“American Water”) that provides support services to American Water’s subsidiaries, including Indiana-
8 American Water Company, Inc. (“Indiana American” or the “Company”).

10 **Q. Are you the same Gregory D. Shimansky who previously submitted rebuttal and
11 settlement testimony in the Phase 2 proceeding of this subdocket?**

12 A. Yes.

13 **Q. What is the purpose of your settlement testimony in this proceeding?**

14 A. My testimony supports and sponsors the settlement (which I will refer to as the “EADIT
15 Settlement Agreement”) reached among Indiana American, the Office of Utility Consumer
16 Counselor (“OUCC”) and the Indiana Industrial Group (“Industrial Group”) (collectively
17 the “Settling Parties” and each a “Settling Party”) in this Cause to resolve all remaining
18 issues pending in this proceeding. A copy of the EADIT Settlement Agreement, along with

1 its Appendices, is being filed simultaneously herewith.

2 **Q. Have all parties to this subdocket joined the Settlement Agreement?**

3 A. No. By Docket Entry issued May 8, 2020, Crown Point and Schererville both have until
4 May 15, 2020 to indicate whether they wish (1) to join the Settlement Agreement, (2) to
5 oppose the Settlement Agreement (either with testimony, cross-examination, or post-
6 hearing briefing), or (3) to take no position on the Settlement Agreement and waive cross
7 examination of witnesses.

8 **Q. On whose behalf are you testifying?**

9 A. I am testifying only on behalf of Indiana American. I am authorized by all Settling Parties
10 to inform the Commission for purposes of this proceeding that all Parties believe that: (a)
11 the EADIT Settlement Agreement as a whole presents a fair and reasonable resolution to
12 the remaining pending issues in this Cause; (b) approval of the EADIT Settlement
13 Agreement is in the public interest; and (c) all Settling Parties encourage the Commission
14 in this subdocket, after considering the evidence in support of the settlement, to find the
15 settlement to be reasonable and in the public interest and enter an order approving the
16 settlement. While the Settling Parties have reviewed and had an opportunity to provide
17 comments to Indiana American on the testimony I am providing prior to its filing, I note
18 that the other Settling Parties may not agree with all opinions and explanations contained
19 in my testimony. This is also the case with respect to Indiana American's view of the other
20 Settling Parties' testimony. However, neither my testimony nor that presented by any other
21 Settling Party changes the substance of the EADIT Settlement Agreement in any manner.

1 **Q. Was the EADIT Settlement Agreement the result of an arm's-length transaction**
2 **among the parties?**

3 A. Yes. The EADIT Settlement Agreement represents the result of arm's-length negotiations
4 by a diverse group of stakeholders with differing views on the issues raised in this
5 proceeding. Settling Party experts were involved with legal counsel in the development of
6 both the conceptual framework and the terms of the EADIT Settlement Agreement. The
7 Settling Parties devoted significant time to discussions, collaborative exchange of
8 information and settlement negotiations.

9 **Q. Please describe generally the parties' agreement as set forth in the EADIT Settlement**
10 **Agreement.**

11 A. For purposes of settlement, the Settling Parties agree the terms and conditions set forth in
12 the EADIT Settlement Agreement represent a fair and reasonable resolution of the
13 remaining issues in this subdocket, subject to incorporation into a final order of the
14 Commission in this subdocket that approves the terms set forth in the EADIT Settlement
15 Agreement without any modification or condition that is not acceptable to the parties. The
16 Settling Parties will cooperate to submit jointly to the Commission a form of a proposed
17 order that would approve the EADIT Settlement Agreement in this Cause No. 45032 S4.

18
19 **Q. Please discuss the key terms and conditions of the EADIT Settlement Agreement.**

20 A. Paragraph 1 sets forth the parties' agreement with respect to the amortization of Indiana
21 American's excess accumulated deferred income taxes ("EADIT"). The Settling Parties
22 have agreed that the Company will use the average rate assumption method ("ARAM"),
23 for the entirety of Indiana American's EADIT, including the deferred EADIT from January

1 1, 2018 through June 30, 2019. The adjustment resulting from this term of the EADIT
2 Settlement Agreement will be reflected in rates upon approval of the EADIT Settlement
3 Agreement as presented in the proposed form of tariff included in Appendix B to the
4 agreement. The EADIT Settlement Agreement notes that ARAM varies year to year, but
5 the estimate as of the date of the agreement is an amount that approximates an amortization
6 over 41.5 years.

7
8 Paragraph 2 of the EADIT Settlement Agreement provides that in Indiana American will
9 begin amortizing its contributions in aid of construction (“CIAC”) at a rate equal to Indiana
10 American’s Commission approved composite depreciation accrual rate (currently 2.61%),
11 through the first five years and as the same depreciation accrual rate may be changed from
12 time to time. The current depreciation rates would result in an amortization over a period
13 of 38.32 years. As of April 30, 2020, Indiana American’s CIAC balance was
14 \$178,395,755.05. However, actual amortization of CIAC pursuant to the EADIT
15 Settlement Agreement will not commence until approval of the settlement by Commission
16 order, and will be based upon the Company’s CIAC balance as of that date. In other words,
17 the amortization of CIAC will be prospective only (and such amortization will also include
18 all of Indiana American’s CIAC received on or after the date of approval of this Settlement
19 by Commission order) and no changes will be made to any amounts or accounts recorded
20 for periods prior to approval of the EADIT Settlement Agreement. Indiana American will
21 not record amortization of CIAC for periods prior to the date of approval of the EADIT
22 Settlement Agreement.

1 The final key term (other than standard and customary terms of settlement) expressly
2 acknowledges that the agreement to permit Indiana American to amortize EADIT using
3 ARAM is in exchange for Indiana American's agreement to amortize CIAC as I just
4 described. This term specifies that if a change in the law or regulatory treatment affects
5 the amortization of CIAC so as to deprive the non-IAWC parties of the benefit of the
6 bargain they have struck, a non-IAWC party may request the Commission determine
7 whether unprotected EADIT should continue to be amortized using ARAM and how to
8 secure the benefit of the bargain reached in the EADIT Settlement Agreement on CIAC.
9 In that event, a non-IAWC party could initiate a proceeding to obtain such a determination
10 by filing a petition with the Commission. Indiana American also expressly states in the
11 agreement that it is not aware of any reason or prospective change to the required treatment
12 of CIAC that would disturb the promises it has made to amortize CIAC.

13
14 **Q. Can you explain why Indiana American agreed to the "bargain" it struck in the**
15 **EADIT Settlement Agreement providing for amortization of EADIT using ARAM**
16 **and commencing amortization of CIAC?**

17 A. Yes. We know that the consumer parties in this Cause have sought to have EADIT passed
18 back more quickly than ARAM where it would not create a violation of the IRS
19 normalization rules to do so. We also know that the IRS indicated in its PLR that
20 amortizing EADIT associated with the repairs deduction more quickly than ARAM will
21 not create a normalization violation. However, for reasons I will describe in greater detail
22 below, Indiana American believes there remain strong policy reasons not to deviate from
23 ARAM for amortization of all EADIT, protected and unprotected. Knowing that, and

1 recognizing the consumer parties' desire to flow the benefits of EADIT to customers over
2 a period of five years, Indiana American began to consider alternative avenues for a
3 solution that would provide benefit for all parties. That is how we came up with the idea
4 to amortize CIAC in exchange for amortization of all EADIT using ARAM.

5
6 **Q. Can you quantify the benefit to customers of these terms of the EADIT Settlement**
7 **Agreement?**

8 A. Yes. The first piece is the amortization of CIAC. As shown in Appendix A, commencing
9 amortization of CIAC, using the current composite depreciation accrual rate of 2.61% to
10 produce an amortization period of 38.32 years, will result in an immediate reduction in
11 depreciation expense and rates of \$4,655,186.71 prior to gross up based on the CIAC
12 balance as of April 30, 2020. Indiana American has agreed that for the first five years of
13 the EADIT Settlement Agreement, amortization of the CIAC balance will be made at a rate
14 no lower than the current 2.61% composite depreciation accrual rate. After that time, CIAC
15 amortization may be adjusted through a base rate proceeding using the updated composite
16 depreciation rate determined in the Company's most recent Commission-approved
17 depreciation study.

18
19 **Q. Has amortization of CIAC been raised in this proceeding previously?**

20 A. No, although it has been an issue litigated in other proceedings. Amortization of CIAC is
21 something that has been requested by the OUCC on multiple occasions over the course of
22 the last 30 years or so. *Indiana-American Water Co.*, Cause No. 43680 (IURC 4/30/2010),
23 pp. 85-86; *Indiana-American Water Co.*, Cause No. 42520 (IURC 11/18/2004), pp. 91-93;

1 *Indiana-American Water Co.*, Cause No. 39595 (IURC 2/2/1994), pp. 21-23; and *Indiana-*
2 *American Water Co.*, Cause No. 37182 (PSCI 12/7/1983), p. 5. Indiana American has
3 always successfully resisted it because this is a significant source of internally generated
4 funds for ongoing construction. Cause Nos. 42520, p. 93; and Cause No. 39595, p. 23.
5 The Company continues to believe that not amortizing CIAC benefits customers of the
6 long term. However, when weighed against the intergenerational inequity and rapid down-
7 then-up fluctuation in rates that would be caused by a short amortization period for EADIT,
8 Indiana American concluded that reducing rates through amortization of CIAC is the right
9 move at this time.
10

11 **Q. Are there further reductions to rates associated with the other terms of the EADIT**
12 **Settlement Agreement?**

13 A. Yes. Pursuant to the settlement previously approved in this subdocket on June 26, 2019,
14 EADIT has been amortized using an “ARAM-like” estimate of \$1,719,962.00. That
15 settlement and the June 26, 2019 Order contemplated that Indiana American would update
16 the EADIT balances using the actual ARAM calculation. Adjusted to 2020 levels, the
17 EADIT balances total \$1,886,577.13, as reflected in Appendix A. Amortizing all EADIT
18 – protected and unprotected – pursuant to ARAM, adjusted to the 2020 levels, results in an
19 additional reduction in the rates of \$166,615.13.
20

21 **Q. What is the additional reduction shown on Appendix A related to the “Pre-change**
22 **period”?**

23 A. As a result of the Commission’s January 3, 2018 Order in the main docket Cause No.

1 45032, Indiana American began deferring amortization of EADIT, with that deferral
2 continuing until July 1, 2019, when the Company's Step 1 rates in its recent general rate
3 case (Cause No. 45142) took effect and reflected the commencement of amortization of
4 EADIT pursuant to the terms of the settlement previously approved by the Commission's
5 order dated June 26, 2019 in this Cause No. 45032 S4. Indiana American has agreed to
6 include the deferred EADIT in the amounts to be amortized using ARAM. The amount of
7 the deferred EADIT is \$3,267,258.96, which results in an additional reduction in rates prior
8 to gross up of \$79,689.24 when amortized using ARAM pursuant to the terms of the
9 EADIT Settlement Agreement.
10

11 **Q. Why has Indiana American insisted on using ARAM to amortize all of its EADIT,**
12 **even where the IRS has indicated no normalization violation will result from a shorter**
13 **amortization period?**

14 A. As I mentioned earlier, Indiana American maintains there are strong policy reasons not to
15 return EADIT over a shorter period than ARAM produces. We believe it makes good sense
16 to provide tax benefits to ratepayers smoothly over the life of the investment. Indiana
17 American believes the flow-back should avoid inter-generational inequity and should
18 promote lower utility rates over the long term. We also believe it should be of the same
19 amount originally expected to be paid to the government.
20

21 **Q. How does Indiana American believe the pass back of excess deferred taxes affects**
22 **inter-generational equity?**

23 A. The normalization concept prevents the inter-generational inequity that can occur when the

1 flow-through method is used. If Indiana American uses an immediate or faster flow-
2 through method, current customers receive the entire refund and disproportionately benefit.
3 Indiana American also believes there is inequity for those later customers caused by the
4 weighted average cost of capital. The entirety of the zero cost EADIT will have already
5 been returned, meaning a higher weighted average cost of capital for the remainder of the
6 life of the asset giving rise to the benefit. It is Indiana American's opinion that
7 normalization ensures that tax benefits are spread to all customers who benefit from Indiana
8 American's long-life assets and not just current customers. Indiana American believes that
9 the normalization concept should be applied to unprotected property and the pass back of
10 these excess deferred taxes should use ARAM.

11 Under a policy of normalization for the return of excess deferred taxes, Indiana
12 American would be required to pay the money no longer owed to the government to its
13 ratepayers instead, but in approximately the same time pattern as Indiana American
14 originally expected to pay it to the government. A shorter period of time means that we
15 must secure the capital to pay back the funds more quickly. If required to pay the funds
16 back more quickly than originally anticipated, we must secure the capital to make those
17 payments from other sources – either external capital or internally generated funds. All
18 else being equal, the added need for capital will make capital more expensive, driving up
19 utility rates. In an era where water utilities need to attract capital for needed infrastructure,
20 this would not be a prudent use of funds.

21
22 **Q. Does amortizing CIAC not similarly deplete internally generated funds and lead to**
23 **the same added need for capital?**

1 A. It does, but amortization of CIAC using a period calculated from the composite
2 depreciation accrual rate avoids many of the other drawbacks I described when a shorter
3 period is used to amortize EADIT, and so does not create the issues associated with the
4 “cliff” that occurs when a shorter amortization period for EADIT is used and expires.

5
6 **Q. How does the impact on customers of the EADIT Settlement Agreement compare to**
7 **what has been requested in the prefiled testimony of the parties in this subdocket?**

8 A. Using the breakdown between protected and unprotected EADIT in my revised Verified
9 Declaration filed in support of the Petition to Reopen the Record in this Cause, and
10 assuming the 5-year amortization period previously urged by the OUCC were ordered,
11 rates would be reduced by approximately \$3 million prior to gross up (\$20 million
12 amortized over 5 years, plus 2020 protected EADIT amortized using ARAM, less the \$1.7
13 million in current rates). In addition, the result under the EADIT Settlement Agreement
14 produces a rate reduction for a much longer period than 5 years as the amortization of
15 CIAC continues, which should be seen as a win for consumers. It bears noting that to date
16 the shortest amortization period approved by the Commission for unprotected EADIT has
17 been six years

18
19 **Q. What is the purpose of allowing the non-IAWC parties to ask the Commission to**
20 **revisit the amortization of unprotected EADIT if a change in the law or regulatory**
21 **treatment affects amortization of CIAC?**

22 A. This term was important to the non-IAWC parties in order to ensure that the benefits of the
23 compromise reached in the EADIT Settlement Agreement remained intact. The Settling

1 Parties recognized that regardless of the agreement reached, sometimes the legal landscape
2 changes, particularly when an agreed commitment is intended to span as long a period as
3 the EADIT Settlement Agreement. The term reflects that the non-IAWC parties'
4 acceptance of ARAM to calculate amortization of all categories of EADIT is conditioned
5 on the Company's commitment to amortize CIAC. That said, Indiana American cannot
6 agree to continue a particular course of action if subsequent changes in law or regulations
7 prohibit that action. As such, the Settling Parties provided a mechanism for the non-IAWC
8 parties to seek relief from the Commission if a change in law or regulatory treatment would
9 deprive them of the benefit of the bargain they have struck.
10

11 **Q. What other terms are included in the EADIT Settlement Agreement?**

12 A. Paragraph 3 of the EADIT Settlement Agreement addresses the effect and scope of the
13 settlement, the approval being sought for the agreement and applicable conditions to the
14 effect of the agreement. Specifically, Paragraph 3 makes clear that the EADIT Settlement
15 Agreement is the result of negotiations and compromise reached during those negotiations,
16 and that neither the making of the settlement agreement nor any of its provisions shall
17 constitute an admission or waiver by any Settling Party in any proceeding other than this
18 subdocket, now or in the future, nor shall it be cited as precedent.

19 The EADIT Settlement Agreement is a compromise and will be null and void unless
20 approved in its entirety without modification or further condition that is unacceptable to
21 any Settling Party. The EADIT Settlement Agreement also includes provisions concerning
22 the substantial evidence in the record supporting the approval of the EADIT Settlement
23 Agreement, recognizes the confidentiality of settlement communications and reflects other

1 terms typically found in settlement agreements before this Commission.

2 **Q. In your opinion, is Commission approval of the EADIT Settlement Agreement in the**
3 **public interest?**

4 A. Yes. The EADIT Settlement Agreement is supported by and within the scope of the
5 evidence presented by the Settling Parties. In particular, it represents the result of extensive,
6 good faith, arm's-length negotiations reflecting a fair and balanced outcome of the
7 remaining issues in this subdocket. The Company's and the other Settling Parties'
8 testimonial positions were modified through the negotiations. The EADIT Settlement
9 Agreement reasonably addresses the concerns raised in this proceeding. Indiana American
10 asks the Commission to issue an order approving the EADIT Settlement Agreement as
11 described herein.

12 **Q. Does this conclude your settlement testimony?**

13 A. Yes.

VERIFICATION

I, Gregory Shimansky, Director Rates & Regulatory, American Water Works Service Company, Inc., affirm under penalties of perjury that the foregoing representations are true and correct to the best of my knowledge, information and belief.



Gregory Shimansky

Date: May 11, 2020