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 RA TE IMPLICATIONS UNDER PHASE 2 FOR AMERICAN SUBURBAN UTILITIES, INC.	))))))	**CAUSE NO. 45032 S15**

TESTIMONY

OF

MARGARET A. STULL - PUBLIC'S EXHIBIT NO. 1

ON BEHALF OF THE

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

September 7, 2018

Respectfully Submitted,

Tiffany T. Murray, Atty. No. 28916-49
Deputy Consumer Counselor

CERTIFICATE OF SERVICE

This is to certify that a copy of the foregoing ***Office of Utility Consumer Counselor Testimony of Margaret A. Stull*** has been served upon the following counsel of record in the captioned proceeding by electronic service on September 7, 2018.

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TESTIMONY OF OUCC WITNESS MARGARET A. STULL
CAUSE NO. 45032 S-15
AMERICAN SUBURBAN UTILITIES, INC.

I. INTRODUCTION

Q: Please state your name and business address.

A: My name is Margaret A. Stull, and my business address is 115 W. Washington St., Suite 1500 South, Indianapolis, Indiana, 46204.

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

A: I am employed by the Indiana Office of Utility Consumer Counselor ("OUCC") as a Chief Technical Advisor with the Water/Wastewater Division. My qualifications are set forth in Appendix A of this document.

Q: What is the purpose of your testimony?

A: Effective January 1, 2018, the Tax Cuts and Jobs Act of 2017 ("TCJA"), among other things, reduced the federal corporate income tax rate to 21%. I provide background on the Indiana Utility Regulatory Commission's ("IURC" or "Commission") investigation in Cause No. 45032 (the "Commission Investigation") and discuss impacts of the TCJA tax reduction on regulated utilities. I respond to American Suburban Utilities, Inc.'s ("ASU" or "Respondent") argument to defer returning excess accumulated deferred income tax ("ADIT") to customers until 2019, and I recommend ASU be required to reduce its rates in 2018 to incorporate the amortization of its excess ADIT. I respond to ASU's proposal regarding the refund of federal income tax expenses collected by ASU from January 1, 2018 through June 30, 2018, when ASU's base rates and charges were reduced to reflect the current federal income tax rate of 21% (Phase 1 of the Commission

Investigation).[1] I recommend the Commission direct ASU to refund the over-collected income tax expense over a three-month period from January through March 2019 regardless of when ASU files its Cause No. 44676 Phase 3 tariff. I respond to ASU's arguments that it should not be required to provide any refunds to customers due to alleged under-earning. Finally, I respond to the issues raised by ASU regarding the taxation of contributions-in-aid of construction.

Q: Please describe the examination and analysis you conducted in order to prepare your testimony.

A: I reviewed ASU's direct testimony, exhibits, workpapers, and other supporting documentation provided in this Cause. I reviewed ASU's 30-Day Filing, which was submitted in Phase 1 of the Commission Investigation. I prepared discovery questions and reviewed ASU's responses.

II. <u>TCJA BACKGROUND</u>

Q: What are the main effects of the TCJA on regulated utilities?

A: The main effects of the TCJA on regulated utilities are the reduction of the federal income tax rate to 21%, the elimination of bonus depreciation and the taxation of contributions in aid of construction for water and wastewater utilities. Regulated utilities are still allowed to deduct interest expense without limitation.

Q: What adjustments are necessary to reflect these effects in a regulated utility's rates and charges?

A: Three major adjustments are necessary: (1) reduction of federal income tax expense embedded in utility rates to reflect the new 21% corporate tax rate on a going

[1] The new tariff was approved in June 2018 and implemented with July billings per Mr. Lods' testimony in this subdocket (page 2, lines 11-18).

forward basis; (2) refunding of the federal income tax expense over-collected by the utility from January 1, 2018 until the federal income tax rate embedded in rates and charges is reduced to 21%;[2] and (3) reduction of federal income tax expense to reflect the return of excess ADIT created when ADIT was revalued at the 21% rate. Item (1) is a Phase 1 issue in the Commission Investigation and items (2) and (3) are considered Phase 2 issues in the Commission Investigation.

Q: How are the impacts of the TCJA on ASU's rates being addressed?

A: On March 26, 2018, ASU made a 30-Day filing in compliance with the Commission's February 16, 2018 order in this investigation. This 30-day filing was rejected by Commission staff due to the inclusion of estimated system development charge revenues as additional taxable income. ASU updated its 30-day filing on May 31, 2018, excluding the adjustment for additional taxable income. This revised 30-day filing implemented revised rates based on the new 21% income tax rate effective on July 1, 2018[1], resolving Phase 1 of the Commission Investigation. Phase 2 tax issues are being addressed in this subdocket (Cause No. 45032 S-15).

A. <u>ADIT</u>

Q: How are deferred income taxes generated?

A: Deferred income taxes are the result of temporary timing differences created by how revenues or expenses are recognized on a company's financial statements or its "books" and how those same revenues or expenses are recognized for tax

[2] Per the Commission's order dated January 3, 2018 in Cause No. 45032, all Indiana investor-owned utilities are required to begin using regulatory accounting, such as the use of regulatory assets and liabilities, for all calculated differences resulting from the TCJA and what would have been recorded if the TCJA did not go into effect.

purposes. For regulated utilities, the primary source of deferred income taxes is accelerated tax depreciation. But deferred income taxes can be generated by other revenues and expenses, such as unbilled revenue, accrued wages, unamortized rate case expense, pension expenses, bad debts, and capital loss carry forward. Deferred income taxes can be either a deferred liability (taxes paid are less than book taxes) or a deferred asset (taxes paid are more than book taxes).

Q: How does accelerated tax depreciation create deferred income taxes?

A: Accelerated tax depreciation uses a higher depreciation rate than the depreciation rate used for book purposes.[3] This higher rate of tax depreciation results in more expense being recognized earlier in an asset's life for tax purposes than is recognized for book purposes.

A higher rate of tax depreciation coupled with a lower depreciation expense rate for book purposes results in a higher taxable income on the company's financial statements and, therefore, a higher income tax expense for book purposes. A higher accelerated depreciation expense for tax purposes lowers the net income on which the utility is taxed, thereby decreasing the income taxes paid. With accelerated tax depreciation, the utility avoids taxes in the early years, and this temporary timing difference is recognized as deferred income tax. The accumulated deferred income tax begins to reverse when accelerated tax depreciation is exhausted. The temporary

[3] The Modified Accelerated Cost Recovery System ("MACRS") is the current tax depreciation system in the United States (i.e. depreciation for tax purposes). For ASU, the depreciation rate used for book purposes is the Commission's sewer composite rate of 2.5%.

timing difference is eliminated over the remaining life of the asset. Table 1 sets forth an example of how this process works.

Table 1: Accumulated Deferred Income Tax Example

$30,000 Asset with 10-year book depreciable life and 3-year MACRS life.

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Total
Tax	10,000	10,000	10,000	-	-	-	-	-	-	-	30,000
Book	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	3,000	30,000
Deferred Taxe:	(7,000)	(7,000)	(7,000)	3,000	3,000	3,000	3,000	3,000	3,000	3,000	-
ADIT	(7,000)	(14,000)	(21,000)	(18,000)	(15,000)	(12,000)	(9,000)	(6,000)	(3,000)	-	

B. Excess ADIT

Q: What is excess ADIT, and why is it necessary to return it to the ratepayers?

A: Under tax normalization rules, a utility's income tax expense embedded in rates is based on its book depreciation expense rather than its tax depreciation expense. Because utilities use accelerated depreciation rates for tax purposes, the amount of current income tax expense paid by the utility is generally less than the amount of income tax expense recovered from customers through rates and charges. The difference between these two expense amounts is recorded as ADIT, a long-term liability on the utility's balance sheet.[4] The value recorded for ADIT is based on the utility's income tax rate and calculated by taking the difference between book and tax expense and multiplying by the current tax rate.

When tax rates change, ADIT balances must be revalued at the new tax

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[4] Temporary tax differences can create either a deferred tax asset or a deferred tax liability, depending upon whether the tax expense is less than (asset) or greater than (liability) the book expense. For purposes of my testimony in this case when I mention a deferred tax liability, I am referring to the utility's <u>net</u> deferred tax liability.

rates. The difference between the ADIT balance valued at the old income tax rate and the ADIT balance at a new lower income tax rate is known as excess ADIT. Excess ADIT represents the amounts that a utility has collected from ratepayers to pay future taxes that, as a result of the reduction in tax rates, will not now be imposed. Essentially, ADIT represent a "loan" from ratepayers to the utility. When the income tax rate decreases, the amount of the "loan" from ratepayers is reduced and needs to be "repaid" or returned to the ratepayers. Excess ADIT represents the amount of the "loan" to be repaid to ratepayers.

C. Protected vs. Unprotected ADIT

Q: Are there different classifications of ADIT?

A: Yes, there are two types of ADIT - protected and unprotected. "Protected" ADIT refers to all temporary federal income tax differences generated by the difference between book and tax depreciation rates or depreciation methods used. All other temporary federal income tax differences, including asset basis differences, are considered "unprotected."

Q: Why is the distinction between "protected" and "unprotected" ADIT important?

A: This distinction is important because it affects how excess ADIT will be returned to ratepayers. Congress has imposed rules regarding how any "protected" excess ADIT should be returned to ratepayers in order for the utility to comply with tax normalization rules. "Unprotected" excess ADIT is not subject to these normalization rules, and how these amounts are returned to ratepayers is left to the discretion of the jurisdictional regulating body.

Q: How is "protected" excess ADIT returned to ratepayers?

A: "Protected" excess ADIT must be returned to ratepayers using the average rate assumption method ("ARAM"). If the utility does not have adequate data to apply ARAM, the "Reverse South Georgia" method may be used as an alternative. In general, both the ARAM and the Reverse South Georgia method spread the flow-through of excess ADIT over the remaining lives of the property that gave rise to the excess.

Q: Are there any other regulatory impacts as a result of TCJA?

A: Yes. In Indiana, accumulated deferred income taxes may be included in a utility's capital structure as a zero-cost source of capital. This has the effect of reducing the utility's weighted average cost of capital. In future rate cases, the amount of accumulated deferred income taxes included in the capital structure will be reduced due to the amortization of excess ADIT, thereby increasing the weighted average cost of capital (all other things being equal).

III. AMORTIZATION OF EXCESS ADIT

A. ASU's Proposal

Q: What is ASU's excess ADIT as of 12/31/2017?

A: Mr. Lods states ASU's ADIT as of 12/31/2017 was $533,026 and that approximately $213,000 of this is excess ADIT. According to Mr. Lods' direct testimony, he calculated this amount by taking (35-21) /35 (40%) of $533,026. In response to OUCC discovery, ASU stated "there is no more detailed calculation than explained in testimony" (Attachment MAS-1). Mr. Lods assumes an annual reduction in income tax expense of $5,300 per year based on a 40-year remaining life for ASU's assets (based on a 2.5% depreciation rate). In response to OUCC discovery regarding whether the estimated $5,300 amortization of excess ADIT was grossed-up for taxes and fees, ASU responded that the calculation is fully explained in the testimony (Attachment MAS-1). Finally, Mr. Lods stated that all of ASU's ADIT is due to accelerated depreciation expense and, therefore, protected. (Lods' Direct Testimony, page 3, lines 13-14.)

Q: Does ASU propose to refund protected excess ADIT to its customers?

A: No. Mr. Lods stated ASU is "contemplating whether we should amend our tax returns so as to do away with accelerated depreciation and pay all of the ADIT back to the Internal Revenue Service as current income taxes payable." (See Lods Direct Testimony, page 4, lines 11- 15.) ASU requested it be allowed until its 2018 tax return is due to make this decision; Mr. Lods' testimony states that ASU's 2018 federal tax return is due on April 15, 2019, but in response to OUCC discovery ASU responded that date is an "error" and Mr. Lods meant to say that "he would like until after the return is due before we must make a decision." (See Attachment MAS-2.)

If ASU amends its returns, no refund would be provided to its customers and ASU would provide proof that the additional tax has been paid. If ASU does not choose to amend its tax returns, ASU proposes to file a tariff reflecting the reduction in rates that would be required. (See Lods' Direct Testimony, pages 3-4.) If ASU does not amend its federal tax returns, it proposes that interest be accrued on the excess ADIT at a rate of 4% per annum from January 1, 2019 until the revised tariff is submitted for approval. (Lods' Direct Testimony, pages 4 lines 22-24 through page 5, lines 1-2.)

Q: What method does ASU propose to use if it does reduce rates to refund its excess EDIT?

A: ASU does not specify the method it would use to calculate the annual amount of excess EDIT it would pass back to its customers. Mr. Lods states "ASU would propose to file a tariff reflecting the reduction in rates that would be required either by ARAM or RSGM [Reverse South Georgia Method], <u>whichever one we should choose to use</u>." (See Lods' Direct Testimony, page 4, lines 18-20, emphasis added.) In response to OUCC discovery regarding whether ASU believes it has a choice of methods, Respondent stated "ASU does not know yet what will be required." (See Attachment MAS-3.)

Q: Does ASU's response raise any concerns?

A: Yes. Despite having had eight months to review and research what is required under the TCJA, ASU still has no idea what the law requires and asks this Commission to provide even more time. ASU has provided no evidence that it has taken any steps to date to determine the requirements of the TCJA or that its contemplated change in tax accounting methodology is prudent or reasonable.

Q: Are you aware of any investor-owned utilities that do not use accelerated depreciation for tax purposes?

A: No. I am unaware of any investor-owned public utility that does not take advantage of accelerated depreciation for tax purposes.

B. OUCC Response

Q: Do you accept ASU's proposal regarding its excess ADIT?

A: No. I disagree with the amount of excess ADIT identified by Mr. Lods as well as ASU's proposal to delay making a decision on this issue.

Q: Why do you disagree with the amount of excess ADIT claimed by Mr. Lods?

A: The amount of ADIT at 12/31/17 is slightly less than what Mr. Lods asserted. According to ASU's 12/31/17 trial balance, the amount of ADIT is $532,070 rather than $533,026. (Attachment MAS-4.) It appears Mr. Lods' figure includes taxes other than income. The bigger problem with the ADIT figure in Mr. Lods' direct testimony is the amount of the annual amortization of the excess ADIT and the fact that Mr. Lods did not gross-up his amount for taxes and fees that have been embedded in rates and should be removed when rates and revenues are decreased.

Q: What is your recommendation regarding excess ADIT?

A: I recommend ASU be required to return excess ADIT to its customers starting no later than January 1, 2019. Given the OUCC's previous experience in reviewing ASU's recordkeeping, it is unlikely ASU has the detailed information necessary to calculate ARAM. Therefore, my annual amortization calculation is based on using the Reverse South Georgia Method ("RSGM"), which results in an annual amortization of $7,094 (before gross-up), or $9,980 (after gross-up). Using information obtained from ASU's 2017 IURC annual report (Attachment MAS-5), the remaining useful life of ASU's utility plant is 30 years, not the 40 years assumed by Mr. Lods. Table 2 reflects my calculation of the remaining useful life of ASU's utility plant and annual amortization of excess ADIT.

Table 2: Calculation of Excess ADIT Amortization

UPIS - Original Cost at 12/31/17		$ 26,893,575
Less: Land		(215,245)
Depreciable UPIS		$ 26,678,330
Less: Accum. Depreciation		(6,657,261)
Net UPIS		$ 20,021,069
Divided by: Annual Depreciation Expense	(A)	666,958
Amortization Period		30.02
(rounded up to 30 years)		
Excess ADIT		$ 212,828
Divided by Amortization Period		30
Annual Amortization of Excess ADIT		7,094
Times: Gross Revenue Conversion Factor		137.59
Reduction to Revenue Requirement		$ 9,980
Percent Reduction to Customer Rates	(B)	0.27%

(A) Depreciable UPIS times 2.5%
(B) $9,980 / $3,708,109 (Revenues per Revised 30-Day Filing dated May 31, 2018.)

Q: Why do you disagree with ASU's proposal to delay customer refunds for ADIT while ASU considers whether it will continue using accelerated depreciation for tax purposes?

A: As I discuss above, ASU has known about the TCJA and the impacts to its operations since December 2017. It is unclear what information ASU will have when it files its 2018 tax return that it doesn't have today. ASU has always hired an outside tax consultant to assist in tax decisions and preparation of its tax returns (Attachment MAS-6) and determining the impact of the TCJA is no different. As demonstrated in Table 2 above, determining the period under RSGM is straight forward and relatively easy to calculate. Further, unlike ARAM, this calculation only has to be calculated once and the amortization amount remains the same for the remainder of the amortization period. It is an unfair burden to customers to delay refunds simply because ASU has not prioritized making a decision on its tax accounting methodology.

I also question the reasonableness and prudency of the decision being contemplated by ASU. ASU claims it is planning to make a change in accounting method for tax purposes and is assuming that this change can be implemented retroactively. But ASU has provided no evidence or support that its plan is the proper way to implement a change in tax accounting methodology. Further, ASU has done no cost benefit analysis of the impacts this decision could have, only that it will take time to make the decision. (Attachment MAS-7.) If ASU has contacted the IRS regarding this change in tax accounting methodology, it has provided no evidence supporting this plan, such as a private letter ruling or other response regarding how such an accounting change should be implemented. It is possible that this tax accounting change would be prospective only and impact only future tax years, not past tax years – which means ratepayers would still be owed excess ADIT refunds. Either way, it is unclear why ASU would want to pay more income taxes than are necessary simply to avoid providing a refund to its customers.

Q: Does ASU have a choice between ARAM and RSGM?

A: No. In accordance with IRS normalization rules, a utility must use ARAM if it has the necessary information to do so. If not, then the RSGM or similar method may be used to calculate the remaining useful life of a utility's assets. If the RSGM is used, the annual amortization amount will remain the same throughout the remaining useful life of ASU's assets. While the OUCC has presumed ASU does not have the records necessary to support an ARAM calculation, if ASU does have such detailed information, which should have been included in Mr. Lods' direct testimony, it must use ARAM to calculate the amortization period for its excess protected ADIT.

Q: Is ASU's 2018 income tax return due on April 15, 2019 as stated by Mr. Lods?

A: No. A C corporation tax return is due on March 15, 2019 but can be extended to September 15, 2019. Therefore, Mr. Lods is potentially requesting a delay in initiating customer refunds for excess ADIT until the end of September 2019. I do not consider such a delay reasonable or necessary. (See also Attachment MAS-2.)

Q: Do you have any comments regarding ASU's proposal to accrue interest on excess ADIT?

A: Yes. If ASU is granted more time before it is required to return excess ADIT to customers, interest on excess ADIT should begin accruing as of January 1, 2018 and should continue to accrue until such time as the revised tariff is approved and refunds begin flowing back to customers. Further, the rate to be used to accrue interest should be ASU's weighted average cost of capital approved by the Commission in its most recent base rate case, Cause No. 44676, or 8.31%.

IV. <u>OVER-COLLECTED FEDERAL INCOME TAX EXPENSE</u>

A. <u>ASU Proposal</u>

Q: What is ASU's proposal regarding its over-collected federal income tax expense in this Cause?

A: ASU estimated it over-collected $79,042.72 of federal income tax expense during the period January through June 2018 (Lods' Direct Testimony, page 5, lines 8-10). ASU proposes to refund this amount to its customers during the period January through March 2019 as an offset to its Cause No. 44676 Phase 3 tariff to be submitted before the end of 2018 (*Id.*, lines 12-22).

Q: What does ASU propose if it has not filed its Phase 3 tariff before March 31, 2019?

A: In that event, Mr. Lods stated ASU will "file a standalone bill credit tariff on April 1, 2019, to reflect a 100% refund of the deferred liability in one month's bill." (See Lods' Direct Testimony, page 6, lines 3-4.)

B. OUCC Response

Q: Do you accept ASU's proposal?

A: No. I disagree with the amount of the refund proposed, as well as ASU's proposal to offset the refund against its Cause No. 44676 Phase 3 rate increase.

Q: Why do you disagree with the amount of the refund proposed by ASU?

A: Even though ASU over-collected income tax expense for six months (January through June 2018), its estimate is based on only five months of 2018 revenues - February through June 2018. Further, ASU used an estimated 5% Phase 1 rate reduction in its calculation even though the actual rate decrease was 5.63%. In response to OUCC Data Request No. 3.10, ASU provided the actual revenues billed from January through June 2018 ($1,893,822). Therefore, the actual amount to be refunded to customers is $106,622 ($1,893,822 x 5.63%). (See Attachment MAS-8.)

Table 3: Calculation of Over-Collected Federal Income Tax Expense

Cumulative 2018 Revenues billed through June 2018	(A)	$	1,893,822
Times: Phase I Decrease to rates	(B)		5.63%
Over-Collected Federal Income Tax Expense		$	106,622.18

(A) Attachment MAS-1 (ASU Response to OUCC Data Request No. 3.10.)
(B) Revised Phase I 30-Day Filing #50134 dated 5/31/18.

Q: Why did ASU exclude January 2018 revenues from its calculation?

A: Mr. Lods stated that "ASU bills in arrears." Presumably, Mr. Lods believed it was appropriate to exclude January billings, which relate to December usage, from the calculation.

Q: Why do you disagree with Mr. Lods' exclusion of January billings?

A: Almost all utilities bill in arrears and ASU is not unique in this regard. Regardless of the month the revenues were earned in, they were billed in January 2018, after the income tax rate was reduced to 21%. Regardless of whether the billings are for the period December 2017 through May 2018 or January through June 2018, ASU over-collected income tax expense for six months. The calculation of the over-collection should be based on six months of revenues, not five months.

Further, in response to OUCC discovery, ASU admitted that it did not accrue December revenues in December for either 2017 or 2016. In other words, ASU's annual revenues are based on actual usage during the 12 month period December through November. (See Attachment MAS-9.)

Q: Why do you disagree with ASU's proposed methodology for providing the refund of over-collected federal income tax expense?

A: The timing of the customer refund for excess federal income tax expense has no relation to the implementation of ASU's Cause No. 44676 Phase 3 tariff, and it is not necessary to coordinate the two. ASU's proposal to provide a bill credit over a period of three months is acceptable but this bill credit should be based on a date certain and not dependent on when, or if, ASU files its Phase 3 tariff. The implementation of ASU's Phase 3 tariff filing could be delayed by the review process and customers' refunds should not be "held hostage." I recommend the refund be provided to customers over the three month period January to March, 2019.

Q: Are you opposed to using the refund as an offset to ASU's Cause No. 44676 Phase 3 rate increase?

A: If ASU makes its Phase 3 tariff filing in a timely manner in 2018 and it is approved to be implemented by January 2019, then the refund will offset the Phase 3 rate increase as proposed by ASU.

V. TAXATION OF CONTRIBUTIONS-IN-AID OF CONSTRUCTION

Q: What is ASU's proposal regarding contributions-in-aid of construction ("CIAC")?

A: ASU elected Option 2 "where ASU pays the tax on contributed facilities." With respect to its system development charge, "ASU plans to file a 30-day filing to increase for the income tax." (Lods' Direct Testimony, page 6, lines 7-12.) ASU further proposes that amounts paid by ASU for income taxes be reflected as a debit to CIAC.

Q: Is ASU's request consistent with the Commission's instructions in its prehearing conference order in this Cause dated February 16, 2018?

A: No. In determining how to recover income taxes on CIAC, ASU makes a distinction between main extensions (plant contribution) and system development charges (cash contribution). However, nothing in the Commission's prehearing conference order or the Commission's administrative rules makes this distinction. The Commission's prehearing conference order instructed respondents with CIAC to choose one of the options as set forth in 170 IAC 6-1.5-33 or 170 IAC 8.5-4-32. I believe the Commission intended that respondents choose one option for all CIAC, and not for respondents to choose one option for plant contributions and another for cash contributions. To allow ASU to require those making cash contributions to pay the associated income taxes, while not requiring the same from those making plant contributions, would be discriminatory and should not be allowed. ASU does not explain why it is willing to pay the income taxes on plant contributions but is unwilling to pay the income taxes on cash contributions (system development charges).

Q: Do you accept ASU's proposal to debit CIAC for any income taxes paid on contributions?

A: Yes. I consider this to be the proper treatment of any income taxes paid by ASU related to contributions.

Q: Does Option 2 provide any other instructions?

A: Yes. Option 2 states the applicant (or contributor) is required to pay the main extension exclusive of the tax associated with the main extension and that the applicant shall *receive refunds as provided in sections 36 through 37 of this title.* In other words, the contributor is still entitled to receive subsequent connector fees for ten years.

VI. OTHER CONCERNS

Q: Does ASU address any other issues in its testimony?

A: Yes. Mr. Lods states he does not believe ASU's rates were unreasonable before the Phase 1 reduction and that its 2017 IURC annual reports shows that "our actual net operating income for 2017 was more than $600,000 below our authorized net operating income and that our actual rate of return was 2.92%. I do not believe that we would be over-earning even if we had kept rates the same." (See Lods' Direct Testimony, page 3, lines 6-9.) Mr. Lods brings this issue up again on page 5, lines 12 – 13 of his testimony, stating "I do not believe it is proper that any money should be refunded because ASU is not over earning."

Q: Is ASU's comparison of its 2017 net income to its authorized return a fair comparison to determine whether it is under-earning?

A: No. Mr. Lods compares the Phase 2 revenue requirement approved in Cause No. 44676 to ASU's net income as reported in its 2017 IURC annual report. What Mr. Lods fails to mention is that 2017 does not represent a full year of its Phase 2 rate increase. ASU's Phase 2 tariff was effective on March 17, 2017 and would have been implemented with April 2018 billings. Therefore, 2017 represents only 9 months of the Phase 2 rate increase and Mr. Lods' statements regarding ASU's under-earning are overstated.

Q: Even if more accurately stated, would ASU's earnings have any bearing on whether its customers are entitled a refund due to excess ADIT?

A: No. Income taxes are a pass-through expense, and utility rates must reflect actual, not hypothetical, expenses.

Q: How did the Commission address arguments regarding under-earning in its 1987 tax investigation in Cause No. 38194?

A: In Cause No. 38194, the Commission discussed the reasonableness of adjusting a utility's rates and charges as a result of a change in only the federal income tax expense. In its deliberations, it stated that income taxes have no bearing on whether a utility is or is not earning its authorized return:

> This Commission realizes that a change in the Federal Income Tax Rate should have no substantive bearing on whether a utility is or is not earning its authorized return. Federal Income Tax Expense, like many other utility expense items, is a pass through expense. In other words, the utility's Federal Income Tax obligation is passed-through as a cost of doing business to its ratepayers. <u>Because of the pass-through nature of this expense, a change in the Federal Income Tax rate should have no effect on a utility's net operating income and therefore its ability to earn its authorized return.</u> Further, this Commission has often stated that public utilities are in no fashion guaranteed to earn their authorized return, or any return at all, but, are only provided an opportunity to earn such return.

Cause No. 38194, Interim Order, June 1, 1987, page 27. (Emphasis added.)

VII. <u>RECOMMENDATIONS</u>

Q: Please summarize your recommendations.

A: I recommend the Commission deny ASU's request for more time to determine whether it should amend prior tax returns and require ASU to refund its excess ADIT, all of which is protected, to its customers based on my calculation shown in Table 2. I recommend the Commission approve the OUCC's proposed ratemaking treatment of the tax regulatory liability created by ASU's over-collection of income tax expense in 2018 as well as the actual value of the over-collection to be refunded

- $106,622 – as reflected in Table 3. Finally, I recommend the Commission require ASU to choose one CIAC option for both plant and cash contributions.

Q: Does this conclude your testimony?

A: Yes.

APPENDIX A

Q: Please describe your educational background and experience.

A: I graduated from the University of Houston at Clear Lake City in August 1982 with a Bachelor of Science degree in accounting. From 1982 to 1985, I held the position of Gas Pipeline Accountant at Seagull Energy in Houston, Texas. From 1985 to 2001, I worked for Enron in various positions of increasing responsibility and authority. I began in gas pipeline accounting, was promoted to a position in financial reporting and planning, for both the gas pipeline group and the international group, and finally was promoted to a position providing accounting support for infrastructure projects in Central and South America. In 2002, I moved to Indiana, where I held non-utility accounting positions in Indianapolis. In August 2003, I accepted my current position with the OUCC. In 2011, I was promoted to Senior Utility Analyst. In 2018, I was promoted to Chief Technical Advisor. Since joining the OUCC I have attended the National Association of Regulatory Utility Commissioners ("NARUC") Eastern Utility Rate School in Clearwater Beach, Florida, and the Institute of Public Utilities' Advanced Regulatory Studies Program in East Lansing, Michigan. I have also attended several American Water Works Association and Indiana Rural Water Association conferences. I have also attended several NARUC Sub-Committee on Accounting and Finance Spring and Fall conferences. I have participated in the National Association of State Utility Consumer Advocates ("NASUCA") Water Committee and the NASUCA Tax and Accounting Committee. In March 2016 I was appointed chair of the NASUCA Tax and Accounting Committee.

Q: Please describe your duties and responsibilities at the OUCC.

A: I review Indiana utilities' requests for regulatory relief filed with the Commission. I also prepare and present testimony based on my analyses, and make recommendations to the Commission on behalf of Indiana utility customers. I have been involved with the Commission's investigation in Cause No. 45032 since its inception, conducting analysis of the Tax Cuts and Jobs Act of 2017 and the effect this Act has on the rates of the various utilities involved in the investigation.

Q: Have you held any professional licenses?

A: Yes. I passed the CPA exam in 1984 and was licensed as a CPA in the State of Texas until I moved to Indiana in 2002.

Q: Have you previously testified before the Indiana Utility Regulatory Commission ("Commission")?

A: Yes. I have testified before the Commission as an accounting witness in various causes involving water, wastewater, electric, and gas utilities.

OUCC DR 3-14

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

On page 4, lines 1-9, Mr. Lods discussed his determination of the excess ADIT. Please provide the detailed calculations supporting Mr. Lods' $213,000 and the $5,500 per year.

Information Provided:

There is no more detailed calculation than explained in the testimony.

OUCC DR 3-15

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

In the calculations discussed on page 4, lines 1-9 of Mr. Lods' testimony, did Mr. Lods gross-up the excess ADIT for taxes and fees? Please explain.

Information Provided:

The calculation is fully explained in the testimony.

OUCC DR 3-6

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

On page 4, line 15, Mr. Lods said ASU's 2018 federal tax return is due on April 15, 2019. Please confirm this date correct. Why isn't ASU's federal income tax return due on March 15, 2019 when other C corporation returns are due, or September 30, 2019, if an extension is requested?

Information Provided:

It's in error. What Mr. Lods meant to say was that he would like until after the return is due before we must make a decision.

OUCC DR 3-8

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

On page 4, line 20, Mr. Lods said ASU would file a tariff reflecting the reduction in rates that would be required by ARAM or RSGM, "whichever one we should choose to use." Why does ASU believe it has a choice of methods to determine the annual amount of excess deferred taxes to credit its customers?

Information Provided:

ASU does not know yet what will be required.

OUCC DR 3-1

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Please provide a detailed trial balance as of 12/31/2017.

Information Provided:

Please see attached.

Attachments:

OUCC DR 3-1.pdf

American Suburban Regulatory
Trial Balance
12/31/17

Acct	Description	Activity	Balance
1017	131 Checking Acct, Horizon	(98,635.69)	949.78
1018	131 Const Escrow Acct, HRZ	4,194,927.73	4,195,027.73
1020	131 Payroll Account, LB&T	(14,827.69)	5,769.54
1200	141 Customer Accts Receivable	(29,767.02)	136,403.50
1320	174 Income Tax Refund Rec	77,266.00	103,611.38
1600	101 Plant in Service, Sewer	488,117.00	25,563,188.60
1601	351-Organization	0.00	68,247.00
1700	101 Furniture & Equipment	25,317.98	836,184.96
1705	101 Vehicles	0.00	425,954.59
1896	108.1 Less: Acc Depr. Vehicle	0.00	(115,355.10)
1897	108.1 Less: Acc Depr. F&E	0.00	(243,536.44)
1898	108.1 Less: Acc Depr. Sewer	(88,209.90)	(6,298,620.56)
1901	105 CWIP CE-3	1,670,990.00	1,896,814.62
1990	186.1 Defer Rate Case Expense	(7,167.00)	333,246.00
2010	236 Deferred Income Taxes	(248,549.00)	(532,070.00)
2031	236 Accrued Taxes, Payroll	(992.38)	(351.18)
2032	231 Accrued Expenses	(109,529.49)	(109,529.49)
2036	211 Loan From Shareholder-Cur	(787,928.45)	0.00
2170	263 401K Plan, SS&B	0.00	(1,153.98)
2175	263 Section 125	0.00	(66.02)
2605	211 Loan From Shareholder-Cur	0.00	(482,518.15)
2634	232 N/P Horizon Bank 2017	(5,100,000.00)	(5,100,000.00)
2708	252 Adv for Const, Fieldstone	(2,068.96)	(7,758.60)
3000	201 Common Stock	0.00	(15,814.00)
3460	211 Dividends Paid	0.00	378,947.37
3480	211 L3 Paid in Capital	0.00	(1,367,481.85)
3500	211 Additional Paid in Capital	(24,344.79)	(3,958,890.45)
3610	271 CIAC, Sewer	(488,117.00)	(8,644,510.96)
3615	271 CIAC, SDC	(81,300.00)	(221,519.13)
3616	272 Accum Amortization of CIAC	15,446.73	495,032.76
3800	214 Retained Earnings	0.00	(6,860,877.62)
4020	521.1 Unmetered Res Sewer	(140,934.31)	(1,577,467.27)
4030	521.5 Unmetered Multi-Family	(143,547.74)	(1,639,255.75)
4040	521.2 Unmetered Comm Sewer	(18,936.10)	(217,319.09)
4050	522.5 Metered Multi-Family	(2,015.26)	(18,590.13)
4060	522.2 Metered Commercial Sewer	(6,929.61)	(103,767.63)
4500	421 Connection Charge	(6,040.00)	(140,822.75)
4505	419 Interest Income	(2,754.73)	(2,754.73)
4950	532 Forfeited Discounts, Sewer	0.00	(10,718.20)
6010	741 Rent	1,794.16	55,794.16
6020	408.11 Property Tax	0.00	119,931.46
6030	775 Utilities, G&A	1,346.69	14,970.36
6032	715 Purchased Power, Sewer	26,769.82	197,431.68
6040	775 Telephone	1,993.57	19,911.67
6049	775 Safety Equipment	19.70	5,444.19
6050	775 Shop Supplies	5,529.61	10,332.84
6051	775 Software Expense	568.00	5,473.88
6052	775 Office/Safety Equipment	0.00	668.73
6053	775 Office Supplies	1,698.23	9,526.08
6056	775 Office Furniture	0.00	3,310.00
6060	775 Repairs & Maintenance	0.00	1,134.73
6071	775 Off Road Maintenance	0.00	2,581.71
6074	750 Vehicle Expense	2,805.25	8,046.45
6075	750 Fuel & Supplies	4,823.84	31,609.61
6080	775 Postage	1,985.40	20,667.55
6090	775 Bank Charges	40,082.02	46,149.97
6111	757 General Liability Ins	22,463.42	40,974.66
6115	756 Vehicle Insurance	4,834.49	10,056.83
6118	758 Workmans Compensation Ins.	5,787.79	12,660.39
6120	701 Wages	36,951.43	408,343.21
6125	703 Wages, Officers	52,230.78	194,000.04
6127	704 Employee Pensions/401K	72,604.67	108,237.09
6130	408.12 Payroll Taxes	3,872.59	48,844.57
6131	703 Directors Fees	0.00	1,797.00
6133	704 Employee Relations	2,700.00	3,300.00
6160	775 Dues & Subscriptions	945.60	5,910.19
6170	775 License & Fees	2,081.26	13,246.60

Acct	Description	Activity	Balance
6171	775 IDEM Fees	1,612.50	20,261.25
6200	775 Contributions	58.85	1,268.51
6219	775 Travel/Meeting Expense	7,939.49	34,537.13
6220	775 Education & Training	415.00	3,356.90
6225	775 Uniforms	186.70	6,290.22
6230	775 Small Tools	3,730.90	11,268.39
6240	742 Equipment Rental	128.05	3,132.64
7311	731 Cont-Eng, Collect Oper	16,040.83	61,621.35
7314	731 Cont-Eng, Pump Maint	1,333.34	11,933.35
7315	731 Cont-Eng, Treat Oper	1,333.33	16,496.50
7328	732 Cont-Acct, G&A	4,813.85	77,572.48
7338	733 Cont-Legal, G&A	118,833.69	285,110.10
7355	735 Cont-Test, Treatment	4,500.00	56,931.99
7361	736 Cont-Other, Coll Oper	8,631.28	48,636.16
7365	736 Cont-Other, Treat Oper	1,110.50	14,738.00
7366	736 Cont-Other, Treat Main	24,173.37	97,297.38
7500	718 Chemicals, Sewer	33.35	28,757.09
7510	720 Materials/Supp-Collec Oper	0.00	7,291.09
7515	720 Materials/Supp-Collec Main	4,190.04	12,933.40
7520	720 Materials/Supp-Pump Oper	0.00	127.60
7525	720 Materials/Supp-Pump Maint	0.00	130.11
7530	720 Materials/Supp-Treat Oper	1,420.93	39,210.76
7535	720 Materials/Supp-Treat Maint	49.26	21,443.22
7540	720 Materials/Supp-Cust Acct	3,292.38	6,937.67
9020	272 CIAC Amortization	(15,446.73)	(185,360.76)
9510	403 Depreciation, Sewer	88,209.90	672,339.38
9540	766 Amortization of Rate Case	7,167.00	86,004.00
9600	427. Interest Expense	17,901.00	17,901.00
9905	408.13 Utility Receipts Tax	13,699.55	51,565.69
9910	409.10 Fed. Corp. Income Tax	272,206.00	272,206.00
9920	409.11 State Corp. Income Tax	49,077.00	49,077.00
	Ledger Debits	7,418,041.85	37,856,109.84
	Ledger Credits	7,418,041.85	37,856,109.84

OUCC DR 3-2

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

What is the value of ASU's depreciable utility plant in service as of 12/31/2017? For purposes of this question, "depreciable" means the value of utility plant in service that is depreciated, excluding land and other non-depreciable utility plant.

Information Provided:

Please see the attached Annual Report to the Commission.

Attachment:

OUCC DR 3-2.xls

American Suburban Utilities
NAME OF UTILITY

YEAR OF REPORT
December 31, 2017

UTILITY PLANT (ACCTS. 101-106)

ACCT NO. (a)	(b)	REF. PAGE (c)	TOTAL (d)
	Plant Accounts:		
101	Utility Plant In Service	S-3(b)	$26,893,575
102	Utility Plant Leased to Others		
103	Property Held for Future Use		
104	Utility Plant Purchased or Sold		
105	Construction Work In Progress		1,896,815
106	Completed Construction Not Classified		
	Total Utility Plant		$28,790,390

UTILITY PLANT ACQUISITION ADJUSTMENTS (ACCTS. 114-115)

Report each acquisition adjustment and related accumulated amortization separately. For any acquisition adjustment approved by the Commission, include the Order number.

(a)	TOTAL (b)
Acquisition Adjustments (114):	
Total Plant Acquisition Adjustments	
Accumulated Amortization (115):	
Total Accumulated Amortization	
Net Acquisition Adjustments	

American Suburban Utilities
NAME OF UTILITY

YEAR OF REPORT
December 31, 2017

ACCUMULATED DEPRECIATION (ACCT. 108)

(a)	TOTAL (b)
Balance beginning of year:	$5,961,962
Credit during year:	
Accruals charged:	
to Account 108.1	672,339
to Account 108.2	
to Account 108.3	
Accruals charged other accounts *(specify)*	
add back depreciation kimberly lift station	22,960
Salvage	
Other credits *(specify)*	
Total credits	695,299
Debits during the year:	
Book cost of plant retired	
Cost of removal	
Other debits *(specify)*	
Total debits	
Balance end of year	$6,657,261

ACCUMULATED AMORTIZATION (ACCT. 110)

(a)	TOTAL (b)
Balance beginning of year	
Credits during year:	
Accruals charged:	
to Account 110.1	
to Account 110.2	
Other credits *(specify)*	
Total credits	
Debits during year:	
Book cost of plant retired	
Other debits *(specify)*	
Total debits	
Balance end of year	

American Suburban Utilities
NAME OF UTILITY

YEAR OF REPORT
December 31, 2017

WASTEWATER UTILITY PLANT ACCOUNTS

ACCT. NO. (a)	ACCOUNT NAME (b)	PREVIOUS YEAR (c)	ADDITIONS (d)	(RETIREMENTS) (e)*
351	Organization	$68,247		
352	Franchises			
353	Land and Land Rights	215,245		
354	Structures and Improvements	57,162		
355	Power Generation Equipment	3,795		
360	Collection Sewers - Force	256,571		
361	Collection Sewers - Gravity	14,871,584	3,432,288	
362	Special Collecting Structures			
363	Services to Customers	4,690		
364	Flow Measuring Devices	1,195		
365	Flow Measuring Installations			
370	Receiving Wells	73,847		
371	Pumping Equipment	81,356	89,066	
380	Treatment and Disposal Equipment	6,586,100	26,112	
381	Plant Sewers	10,965		
382	Outfall Sewer Lines			
389	Other Plant and Miscellaneous Equipment	197,180		
390	Office Furniture and Equipment	271,591	11,143	
	Computers	3,240	4,012	
391	Transportation Equipment	375,320	50,635	
392	Stores Equipment			
393	Tools, Shop and Garage Equipment	169,257	32,974	
394	Laboratory Equipment			
395	Power Operated Equipment			
396	Communication Equipment			
397	Miscellaneous Equipment			
398	Other Tangible Plant			
	Total Wastewater Utility Plant In Service	$23,247,345	$3,646,230	

*Enter retirements as negative entries

OUCC DR 3-3

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Has ASU ever had a "tax person" on its staff? For purposes of this question, "tax person" means a qualified income tax specialist who filed tax returns with the Indiana Department of Revenue and the IRS.

Information Provided:

No.

OUCC DR 3-4

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

If ASU has not had a tax person on its staff, please explain how ASU has handled income tax related issues such as filing returns and paying taxes?

Information Provided:

ASU has used an outside firm.

OUCC DR 1-7

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Has ASU or Mr. Lods performed a cost benefit analysis of doing away with accelerated depreciation? If so, please provide.

Information Provided:

No. This is a management decision of the utility and it will take time to make this decision. This is why ASU has requested until April 15, 2019 to decide.

OUCC DR 1-8

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Please identify all costs of doing away with accelerated depreciation.

Information Provided:

Unknown at this point.

OUCC DR 1-9

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Please identify all benefits of doing away with accelerated depreciation.

Information Provided:

Unknown at this time but it is known that ASU would not need to deal with the issue of excess ADIT.

OUCC DR 3-10

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Please state the total revenues billed to customers for each month January 2018 through June 2018.

Information Provided:

January 2018	$312,968
February 2018	$315,077
March 2018	$314,932
April 2018	$316,918
May 2018	$316,344
June 2018	$317,583

OUCC DR 3-11

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Did ASU accrue December 2017 revenues (billed in January 2018) in its December 2017 general ledger? If yes, please provide the journal entry for this transaction. If no, please explain why not.

Information Provided:

No.

OUCC DR 3-12

DATA REQUEST
American Suburban Utilities, Inc.

Cause No. 45032 S15

Information Requested:

Did ASU reverse December 2016 accrued revenues in its January 2017 general ledger? If yes, please provide the journal entry for this transaction. If no, please explain why not.

Information Provided:

No; ASU did not accrue December 2016 revenues in January 2017.

AFFIRMATION

I affirm, under the penalties for perjury, that the foregoing representations are true.

Margaret A. Stull

By: Margaret A. Stull
Cause No. 45032 S15
Indiana Office of
Utility Consumer Counselor

9/6/18

Date: