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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 FOR INDIANA AMERICAN WATER COMPANY, INC.	))))))	CAUSE NO. 45032 S4

INDIANA INDUSTRIAL GROUP'S EXCEPTIONS

The Indiana Industrial Group ("Industrial Group") provides the following Exceptions to Indiana-American Water Company, Inc.'s ("Indiana-American") Proposed Order and Brief in Support.

Protected and Unprotected Excess ADIT

The Internal Revenue Code ("the Code") separates Excess Accumulated Deferred Income Tax ("EADIT") balances into two categories: 1) "protected" EADIT, which is comprised of those balances associated with depreciable property, plant, and equipment, and 2) "unprotected" EADIT, which covers all other plant-related (such as repairs) and non-plant-related amounts. For EADIT balances that are protected in nature, the Code requires the use of the Average Rate Assumption Method ("ARAM"), if available, to calculate the annual amortization amounts to be flowed back to customers. For unprotected EADIT balances, the Code does not mandate the use of a particular methodology to determine the appropriate amount of amortization in a given year.[1] As such, unprotected EADIT can be amortized over any period approved by the Commission.

[1] Indiana-American's proposed order at page 6 appears to indicate agreement by the parties with respect to their responses to Commission's Docket Entries concerning the repairs deduction. Those responses speak for themselves, but the Industrial Group submits that only Indiana-American agrees that EADIT associated with repairs must be refunded to customers over the ARAM.

Indiana-American argues that its Consent Agreement with the IRS requires it to use a normalized method of accounting for the repairs deduction. However, nothing in the Consent Agreement discusses whether those normalization requirements apply to its requested change in routine repair and maintenance costs. It is important to note that Indiana-American requested two separate changes as set forth in the Consent Agreement: one to change its method of accounting for repairs, and two, to change its disposition of certain tangible depreciable property identified on Form 3115. Wilde Direct at JRW-2, pages 3-4. With respect to repairs, Indiana-American proposed to change its accounting from a normalized accounting methodology under Section 168(a) of the Code to ordinary and necessary business expenses under Section 162. Accordingly, the Conditions of Consent, which were cited by Indiana-American and reference Section 168, do not apply to the repairs deduction, since the Consent Agreement states that accounting for repairs would be treated under Section 162 going forward. The references in the Consent Agreement to Section 168 relate to Indiana-American's second request regarding the disposition of tangible depreciable property listed on its Form 3115, not repairs.

Mr. Wilde admits that repairs are unprotected. *See* Wilde Rebuttal at 9. In his direct testimony, Mr. Wilde's sole explanation for why repairs should be normalized is found on page 7:

> Given the repairs deduction that is subject of the Consent Agreement relates to public utility property, we must utilize a normalization method of accounting with the meaning of the Internal Revenue Code.

The test for normalized/non-normalized accounting is not whether an item is plant-related. Repairs are certainly plant-related, but as admitted to by Mr. Wilde, are also unprotected. *See, e.g.*, Smith Direct, Attachment LA-2, page 2, line 25 (Vectren Utility Holdings, Inc. listing of repairs as unprotected). The Code provides that unprotected plant-related EADIT does not need to be returned using ARAM, but may be returned over any period approved by the Commission. Indiana-American's interpretation of the Consent Agreement to apply to repairs is incorrect, contrary to the Code, and should be rejected. Further, Indiana-American's proposed treatment of repairs in this subdocket contradicts the relief it requested as set forth in the Consent Agreement, which was to cease normalized accounting of repairs and instead treat them as ordinary business expenses.

By virtue of the change in accounting method for repairs, Indiana-American was able to decrease its taxable income by a net amount of $461,238,422 for 2008, versus taking that deduction over a normalized period.[2] Now that the TCJA has created a liability of excess ADIT, Indiana-American argues for a much slower return of the excess ADIT associated with those repairs, which is the exact opposite of what it requested and received from the IRS in 2010.

Indiana-American also contends that aside from the Consent Agreement, generational inequities and administrative burden support normalized accounting for protected and unprotected EADIT. With respect to the argument on generation inequities, a majority of EADIT is protected, and a smaller percentage of all EADIT is classified as unprotected and subject to a shorter amortization period. In and of itself, the distinction in how protected and unprotected EADIT can be returned provides a balanced approach in addressing short-term and long-term benefits to ratepayers. It is also important to note that Indiana-American will continue to maintain significant amount of ADIT as part of its capital structure; Phase 2 of this investigation only addresses the impact of the reduction of federal income tax from 35% to 21%.

With respect to Indiana-American's argument concerning administrative burden, every other major utility in this investigation has been able to distinguish protected depreciable plant

[2] Indiana-American estimates its ARAM to be approximately 41.49 years, which would be the equivalent normalized period proposed by Indiana-American.

balances from plant-related non-protected balances, such as repairs. The Code specifically provides for different treatment of protected and unprotected EADIT, and every other major utility has been able to address the differing amortization periods. Further, the Commission has approved every settlement relating to unprotected EADIT.

Accordingly, the Industrial Group proposes that all EADIT should be reflected in Indiana-American's Step 1 rates. The Industrial Group requests that protected EADIT be amortized over the period reflective of ARAM, and the Commission should authorize appropriate regulatory accounting to address any difference between the actual ARAM and the amortization of the protected amount over the ARAM timeframe. With respect to unprotected EADIT, which includes repairs, the OUCC proposed a five-year amortization of the unprotected plant-related and non-plant-related balances. See OUCC Response to Commission's November 28, 2018 Docket Entry, at 4. This is consistent with the amortization of unprotected EADIT approved by the Commission for other large investor-owned utilities, and the Commission may take administrative notice of its Orders in those Causes. *See Indiana Michigan Power Co.*, Cause No. 44967 at 25 (approving TCJA provision of settlement, which included a 6-year amortization for non-normalized EADIT).

The Commission should order Indiana-American to quantify its plant-related repairs that it currently has included within its total normalized EADIT balance of $71,378,974,[3] and after offsetting the unprotected repairs with the ($305,118) of unprotected non-plant balance, amortize the unprotected balance over a five-year period starting with the implementation of Indiana-American's Step 1 rates in Cause No. 45142.[4] Finally, the Industrial Group would propose that

[3] In its Response to the Commission's November 28, 2018 Docket Entry, the OUCC estimated that the unprotected EADIT from repairs is $34,121,123.
[4] In the alternative, if the Commission wanted additional evidence concerning an appropriate amortization period, the Commission could defer that issue to Cause No. 45142.

the 2018 amortization of protected EADIT, which has not been returned to customers, be added to the unprotected balance and amortized over the same five-year period, or otherwise requests that the Commission expressly provide that amount to be addressed in Indiana-American's pending rate case. *See Commission Investigation*, Cause No. 45032 S2 at 12 (IURC Aug. 22, 2018) (approving treatment of $59.4 million of 2018 and 2019 protected EADIT amortizations to be addressed in next rate case).

Regulatory Liability

The regulatory liability at issue in this Cause represents the over-collection of federal income taxes through Indiana-American's base rates for the period from January 1, 2018, to July 31, 2018, when the Commission ordered Indiana-American to reduce its base rates to reflect the 21% corporate income tax rate.

Indiana-American has proposed using the entirety of this regulatory liability, which totals $5,821,888, for its customer-owned lead line replacement program. The Industrial Group opposes Indiana-American's proposal, and agrees with the non-utility parties that bill credits provide an equitable resolution of this issue.

First, Indiana-American overlooks the fact that almost half of the regulatory liability was funded by customer classes that will not benefit from lead line replacement. Accordingly, Indiana-American's proposal to subsidize its program using funds that were over-collected from large volume customers is inconsistent with cost-of-service principles and should be rejected.

Second, while Indiana-American argues that its proposal effectively lowers the cost of its program, Indiana-American has failed to rule out the possibility of other low-cost financing. For instance, in Cause No. 44826, the City of East Chicago was able to obtain State Revolving Fund bonds at a lower rate if it included its lead line replacement program, which meant that the program could be implemented at no additional cost to ratepayers. *City of East Chicago, Indiana*, Cause No. 44826 at 20 (IURC Apr. 26, 2017). Further, Indiana-American has not demonstrated that it is unable to fund this program without using this ratepayer-owed deferral, and certainly did not propose approval of its program be conditioned on that premise in Cause No. 45043. Accordingly, Indiana-American has not shown that the use of the regulatory liability is necessary to implement the program or even implement the program at the lowest cost.

Instead, the Commission should order Indiana-American to refund the regulatory liability to customers as a bill credit over no more than seven months, the period over which the liability was created.

Conclusion

For the above reasons, the Commission should reject Indiana-American's proposed Phase 2 tax treatment and order Indiana-American to address its EADIT and regulatory liability as set forth herein.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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