BEFORE THE TENNESSEE PUBLIC UTILITY COMMISSION

NASHVILLE, TENNESSEE

January 31, 2023

IN RE:	)	
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PETITION OF TENNESSEE-AMERICAN WATER COMPANY REGARDING THE 2022 INVESTMENT AND RELATED EXPENSES UNDER THE QUALIFIED INFRASTRUCTURE INVESTMENT PROGRAM RIDER, THE ECONOMIC DEVELOPMENT INVESTMENT RIDER, AND THE SAFETY AND ENVIRONMENTAL COMPLIANCE RIDER	)	**DOCKET NO. 22-00072**

ORDER APPROVING *PETITION*

This matter came before Vice Chairman David F. Jones, Commissioner Robin L. Morrison, Commissioner Clay R. Good, Commissioner Kenneth C. Hill, and Commissioner John Hie of the Tennessee Public Utility Commission (the "Commission" or "TPUC"), the voting panel assigned to this docket, during a regularly scheduled Commission Conference held on November 7, 2022, for consideration of the *Petition* filed by Tennessee-American Water Company ("TAWC", "Tennessee-American" or the "Company") on July 8, 2022.

BACKGROUND

TAWC provides residential, commercial, industrial, and municipal water service to customers in Tennessee and North Georgia. TAWC is a wholly-owned subsidiary of American Water Works Company, Inc. On July 8, 2022, TAWC filed a *Petition* requesting Commission approval to change the tariff percentage rates for the Qualified Infrastructure Investment Program Rider ("QIIP" or "QIIP Rider"), the Economic Development Investment Program Rider ("EDI" or "EDI Rider"), and the

Safety and Environmental Compliance Rider ("Safety Rider" or "SEC").[1] The QIIP, EDI, and SEC (collectively, "Capital Riders") were previously approved by the Commission on April 14, 2014 in Docket No. 13-00130.[2]

In accordance with the tariffs approved in TPUC Docket No. 13-00130, on or before December 1 of each year, the Company shall submit to the Commission an annual filing that calculates the tariff Rider percentage rates for the upcoming calendar year.[3] In accordance with tariffs approved in TPUC Docket No. 13-00130 and subsequent Commission decisions in TPUC Dockets Nos. 14-00121, 15-00029, 15-00111, 16-00022, 16-00126, 17-00020, 17-00124, 18-00022, 18-00120, 19-00105, 20-00028, 20-00128, 21-00030, and 22-00021, the Company has made regular filings to adjust the Capital Rider rates.

PETITION

On July 8, 2022, TAWC filed the *Petition* for approval of its qualifiable projected 2022 investments and related expenses for its QIIP, EDI, and SEC Riders. The Company states it did not submit this filing, as required, on or before December 1, 2021, because it was actively engaged in good faith and cooperative discussions with the parties of record in Commission Docket No. 19-00103, a docket to consider issues and modifications to the Capital Riders of the Company.[4] Because of the late filing, this *Petition* was based upon the actual in-service amounts for January to May 2022, rather than a full year of projections for the QIIP, EDI, and SEC Riders. Further, the *Petition* requested the proposed Riders become effective August 8, 2022.

[1] *Petition*, pp. 1-3 (July 8, 2022).
[2] *See In re: Petition of Tennessee-American Water Company for Approval of a Qualified Infrastructure Investment Program, an Economic Development Investment Rider, a Safety and Environmental Compliance Rider and Pass-Throughs for Purchased Power, Chemicals, Purchased Water, Wheeling Water Costs, Waste Disposal, and TRA Inspection Fee*, Docket No. 13-00130, *Order Approving Amended Petition* (January 27, 2016).
[3] *Petition*, pp. 6-7.
[4] *Id.* at 7-8.

According to the *Petition*, the calculations include the credit from the implementation of the federal Tax Cuts and Jobs Act of 2017 ("TCJA") and the annual amortized Excess Accumulated Deferred Income Tax ("EADIT") credit from the implementation of the TCJA. Both credits are used as an offset to the increase in the Capital Recovery Riders charges for the forecasted 2022 investments.[5] The *Petition* includes the verification of Grant A. Evitts attesting to this filing's compliance with the Company's Capital Rider tariffs and relevant Commission orders. In support of the *Petition*, the Company submitted the Pre-Filed Direct Testimony of Tricia N. Sinopole.

Ms. Sinopole supported the calculation of the 2022 Capital Recovery Riders. With respect to the QIIP, the Company proposed a revenue requirement of $11,399,082, representing a 5.08% increase from the previously approved QIIP charge.[6] The proposed revenue requirement for the EDI was $900,637 with an impact of an increase of 0.66% from the previously approved EDI surcharge. Finally, the SEC under the Company's proposal would see an increase of 0.27% from the previously approved SEC charge with a proposed revenue requirement of $4,692,865.[7] Ms. Sinopole testified that the source of the data used to prepare the exhibits and calculations was acquired from the books and records of the Company.[8]

According to Ms. Sinopole, the Company's filing incorporated all changes and modifications previously ordered by the Commission. Ms. Sinopole attested that the Riders benefit customers by avoiding expensive rate cases, lessening rate shock to customers, supporting the maintenance and improvement of essential infrastructure and supporting economic opportunities. The Company benefits by eliminating the regulatory lag in order for the Company to earn its authorized return on equity.[9]

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[5] *Petition,* p. 10 (July 8, 2022).
[6] Tricia N. Sinopole, Pre-Filed Direct Testimony, p. 26 and Exh.-Summary-TNS (July 8, 2022).
[7] *Id*. at 27 and Exh. Summary-TNS.
[8] *Id.* at 3-4.
[9] *Id*. at 12-14.

Ms. Sinopole claimed the Riders use the cost of capital, depreciation rates, and property tax rate approved in the Company's preceding rate case, Docket No. 12-00049. The calculations incorporate a 21% Federal Income Tax rate based on the TCJA.[10] Ms. Sinopole explained that the authorized water service revenues from the last rate case are used for the projected revenues and no operating expenses are included in the calculations. When the actual investment rider revenue collected is different than the amount of revenue allowed, this difference is included in the Company's next annual reconciliation filing and collected or refunded as necessary.[11]

Ms. Sinopole testified that the QIIP Rider should recover $11,399,082 using a cumulative surcharge of 24.22%. This represents a revenue increase from the previous year of $2,388,563 and surcharge increase of 5.08%. The EDI Rider should recover $900,637 with a cumulative 1.91% surcharge representing a revenue increase from the previous year of $313,454 and surcharge increase of 0.66%. The SEC Rider should recover $4,692,865 with a cumulative surcharge of 9.97% which is a revenue increase of $128,556 from the previous year and Rider increase of 0.27%.[12]

Ms. Sinopole recommended, consistent with Commission Docket No. 18-00039, to use Excess Accumulated Deferred Income Tax ("EADIT") normalization resulting from the TCJA to offset the Riders. She attested that the current EADIT credit percentage is 4.54%, effective January 1, 2021, and the Company anticipates filing for an update in the EADIT percentage late in 2022 or early 2023. The Company also recommended continuing to use the TCJA savings as an offset to the Riders. The TCJA credit percentage as of September 1, 2019, is 6.62% and the Company anticipates filing an update before August 1, 2022.[13]

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[10] *Id.* at 20-21.
[11] *Id.* at 22-23.
[12] *Id.* at 26-28; Exh. -Summary-TNS.
[13] *Id.* at 27-28.

Ms. Sinopole testified the proposed rates in this filing will increase for the typical residential customer living in the City of Chattanooga by $1.30 per month or $15.60 per year. The total percentage increase of 6.01% will begin on August 8, 2022. Ms. Sinopole averred that customers would have seen an increase in their bills beginning January 1, 2022, if the Company had made a timely filing. The Company, however, is not proposing retroactive treatment to the Rider rates in this filing; therefore, customers will see less of an increase in 2022 than they normally would have.[14]

Mr. Grady Stout, P.E., filed testimony in support of the *Petition*. Mr. Stout is responsible for the planning, development, and implementation of all construction projects, including working with developers on all aspects of new projects and coordinates with other TAWC departments for technical assistance and oversees the capital budget development and implementation.[15] According to Mr. Stout, the Capital Investment Plan is developed addressing both short term and longer-term projects. The projects are prioritized using objective criteria and a key component of the planning is that it be flexible and can be adjusted. The Engineering Department develops the budget with input from Operations and Project Managers which is then presented to the officers of TAWC and shared with American Water Works Service Company ("AWW" or "Service Company"). TAWC has the ultimate decision of approval of the plan.[16]

Mr. Stout testified the Investment Projects ("IP") consist of projects greater than $250,000 and represent investments needed to meet environmental or water quality regulations, infrastructure capacity expansion or rehabilitation and to ensure a safe working environment. The IP starts with developing anticipated demand projections, the identification of improvements needed to meet those demands and a review of the current facilities located in the system, which are then documented in a

[14] *Id.* at 31.
[15] Grady Stout P.E., Pre-Filed Direct Testimony, p. 3 (July 8, 2022).
[16] *Id.* at 4.

Comprehensive Planning Study ("CPS"). During this planning process TAWC continues to ensure customers will not be adversely impacted.[17]

According to Mr. Stout, the Company's infrastructure is between 50 and 100 years old and replacement of this aging infrastructure is a continuing concern of the Company. The QIIP allows the Company to recover the fixed costs of replacing this infrastructure in a timely manner resulting in a more reliable water distribution and production system. Mr. Stout testified the Company is focused on the replacement of small diameter mains and mains that have shown a chronic level of leaks which are responsible for much of the distribution system leaks and failures.[18]

The budget for the QIIP includes replacement, renewal or improvement of existing water mains, valves and other appurtenances which are non-revenue producing. The Company plans on spending approximately $2,250,000 in 2022 to replace approximately 14,235 feet of various water mains.[19] Mr. Stout identified two Capital Investment Projects which will be placed in service during 2022: (1) The Lookout Valley System Redundancy Piping Upgrades and (2) the Dunlap Interconnect. He asserted that the Lookout Valley System is one of the fastest growing zones for TAWC and there is a system capacity and aging infrastructure risk of not moving forward with this project. The Dunlap Interconnect is a project for the installation of a water main and interconnect meter vault between the City of Dunlap's water system and TAWC's Whitwell water system. According to Mr. Stout, the interconnection is to allow both systems to purchase water from the other during times of emergency. The Company projected spending approximately $1,997,450 for design, planning, permitting, and construction on multiple projects that will go into service after 2022.[20]

[17] *Id.* at 6-7.
[18] *Id.* at 12-13.
[19] *Id.* at 14-15.
[20] *Id.* at 26-28.

Mr. Stout asserted that the budget for EDI includes work associated with new water mains, valves, and other appurtenances which are necessary to assist in the growth of the community, including infrastructure necessary for fire protection, which is key to economic growth. The budget includes the installation of twenty-two new hydrants and ten valves at an approximate spend of $181,075. The Black Creek Tank Project is a new 150,000-gallon glass lined steel water storage tank which will provide needed water storage and fire flow capacity for the community at the top of Aetna Mountain.[21] Mr. Stout testified that the budget for SEC includes approximately $85,590 for installation or replacement of System Control and Data Acquisition ("SCADA") Equipment and Systems; $200,000 on upgrades to Security Equipment and Systems; $1,620,040 for replacement of Process Plant Facilities and Equipment; and $4,215,371 for the Whitwell Raw Water Intake Improvement projects. Mr. Stout averred these systems support the improvement of safety and enhance the environmental compliance of the TAWC system.[22]

POSITION OF THE CONSUMER ADVOCATE

On August 3, 2022, the Consumer Advocate Unit in the Financial Division of the Office of the Tennessee Attorney General ("Consumer Advocate") filed its *Petition to Intervene* and sought discovery in accordance with a procedural schedule. Following discovery and exchanges of information with TAWC, Mr. David N. Dittemore submitted Pre-Filed Testimony on September 19, 2022, on behalf of the Consumer Advocate which addressed the calculations of TAWC's proposed Capital Riders.

Mr. Dittemore recommended an annual capital rider increase of $2,781,703, resulting in a 5.9% increase in the capital rider surcharge.[23] The difference between Mr. Dittemore and the Company is due to his adjustment correcting the Company's duplication of its pro-rated 2022 tax

[21] *Id.* at 28-31.
[22] *Id.* at 32-35.
[23] David N. Dittemore, Pre-Filed Direct Testimony, p. 5 (September 19, 2022).

depreciation. The duplication understated the tax depreciation on qualifying assets installed in 2022, resulting in an understated Accumulated Deferred Income tax ("ADIT") balance included within the Company's 2022 forecasted rate base.

Mr. Dittemore asserted the duplication occurs due to the Company's use of the one-half year convention associated with its Modified Accelerated Cost Recovery ("MACRS") tax depreciation rate in conjunction with its further reduction in ADIT occurring in 2022 through a proration percentage calculation. Mr. Dittemore does not oppose the Company's use of the "MACRS half-year convention", an approach that allows taxpayers to use a tax rate equal to one-half the normal tax rate for any plant installed in that tax year.[24] However, Mr. Dittemore asserted the problem with duplication arises because the Company takes its already pro-rated 2022 MACRS tax depreciation and further pro-rates the annual balance as if the investments were placed in service throughout the year. Mr. Dittemore asserted the half-year MACRS convention already makes the assumption, so the Company's second pro-rata calculation results in an improper double count resulting in a diminished level of 2022 tax depreciation associated with qualifying assets installed in 2022.[25]

To correct this error, Mr. Dittemore eliminated the Company's second pro-rata calculation and adopted the initial MACRS half-year convention to compute the 2022 tax depreciation on newly installed assets. As a result, he calculated individual and total capital rider surcharges of the QIIP surcharge of 24.24%, the EDI surcharge of 1.91%, and the SEC surcharge of 9.94% as presented in his Exhibits DND-2, 3, 4, and 5.[26] These individual surcharges total 35.99% with a total revenue requirement of $16,943,714, which is an increase of $2,781,703 from the amount adopted in Commission Docket No. 20-00128.[27]

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[24] *Id.* at 6.
[25] *Id.* at 6-7.
[26] *Id.* at 8.
[27] *Id.* at 8-9.

<u>REBUTTAL AND SUPPLEMENTAL TESTIMONY OF THE COMPANY</u>

On October 18, 2022, Mr. Robert C. Lane submitted Pre-Filed Rebuttal Testimony on behalf of the Company. Mr. Lane adopted the previous Pre-Filed Testimony of Ms. Tricia Sinopole. Mr. Lane reiterated that the Company is requesting a total surcharge of 36.1%, which will generate an annual increase of $2,830,573 in the Capital Recovery Riders and rejected the Consumer Advocate's proposal for a $2,781,703 increase. The Company maintained its request of a 6.01% increase in the surcharge.[28] In response to the Consumer Advocate, Mr. Lane asserted the Company used the MACRS half-year convention for all assets placed in service during 2022. This method assumes the property went into service in July rather than calculating a monthly depreciation for each asset based on when it was acquired. The Company also used a proration factor to adjust ADIT because rates went into effect before the end of the applicable rate year. The Consumer Advocate does not object to the use of the MACRS convention; they do however recommend the proration adjustment be removed because it is duplicative.[29]

Mr. Lane testified that the difference between tax depreciation using MACRS and book depreciation for ratemaking purposes results in a change in the ADIT balances and claimed ADIT must be prorated when rates are effective before the end of the applicable rate year. This proration is separate and unrelated to using MACRS but the Consumer Advocate nonetheless proposes to remove it from ADIT.[30] Mr. Lane asserted that MACRS is used to calculate tax depreciation which is the difference from the book depreciation used in ratemaking. This difference between tax and book depreciation, times the applicable tax rate, is what is accounted for in ADIT. TAWC is required by

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[28] Robert C. Lane, Pre-Filed Rebuttal Testimony, p. 2 (October 18, 2022).
[29] *Id.* at 2-3.
[30] *Id.* at 4.

the IRS to prorate the incremental deferred income tax and adjust ADIT balances. According to Mr. Lane, the Company correctly utilized the proration adjustment when calculating the 2022 Riders.[31]

Mr. Lane argued that the Company's removal of the proration adjustment, as suggested by the Consumer Advocate, would be inconsistent with Internal Revenue Code §1.167(1)-1(h)(6), a section of the tax code that addresses exclusions of normalization reserve from rate base. According to Mr. Lane, the Company followed this code directive by calculating the ADIT that is excluded from rate base.[32] Mr. Lane claimed the Consumer Advocate's proposed removal of the proration adjustment is a different issue than the one which arose in the 2021 Capital Rider Reconciliation in Commission Docket No. 22-00021, in which the Company was already using the proration method, and it was not necessary to also divide the prorated amount for twelve months by two. Mr. Lane asserted that in this docket TAWC did not divide the prorated amount by two, which is consistent with what the Company agreed to in the 2021 Reconciliation Docket.[33]

On October 26, 2022, Mr. Lane filed supplemental testimony clarifying TAWC's ADIT calculation is consistent with the method agreed to by the parties and approved by the Commission in the 2021 Capital Rider Reconciliation, Docket No. 22-00021. In Docket No. 22-00021, TAWC agreed with the Consumer Advocate that the ADIT amount should not be divided by two when the proration method is used to calculate ADIT for 2021. He clarified that in this matter, the Company did not divide the prorated amount by two and will not do so in future Capital Rider Reconciliations dockets.[34]

<u>JOINT LETTER OF OCTOBER 26, 2022</u>

[31] *Id.*
[32] *Id.* at 4-5.
[33] *Id.* at 6.
[34] Robert C. Lane, Pre-Filed Supplemental Testimony, pp. 2-3 (October 26, 2022).

On October 26, 2022, the Company submitted a letter representing that both parties agree there are no outstanding disputes between the parties. In the letter, the parties jointly support the approval of the Company's *Petition* based on the communications between the parties and the clarifying supplemental testimony of the Company. The parties waived opening statements and cross-examination.

NOVEMBER 7, 2022 HEARING AND APPEARANCES

A Hearing in this matter was held before the voting panel of Commissioners during the regularly scheduled Commission Conference on November 7, 2022, as noticed by the Commission on October 28, 2022. Making appearances were the following:

> Tennessee-American Water Company – Melvin J. Malone, Esq. Butler Snow LLP, 150 3rd Avenue South, Suite 1600, TN 37201; Robert C. Lane, Senior Manager of Rates and Regulatory for Tennessee and Kentucky, 109 Wiehl Street, Chattanooga, TN 37403; Grady Stout, Engineering Manager, 1500 Riverside Drive, Chattanooga, TN 37406.
>
> Consumer Advocate – Karen Stachowski, Esq. Office of the Tennessee Attorney General and Reporter, Post Office Box 20207, Nashville, Tennessee, 37219

Robert C. Lane appeared and summarized his pre-filed testimony on the record in support of the *Petition*. In addition, Grady Stout appeared and summarized his pre-filed testimony on file in the record. The Commissioners opened the floor for public comment, but no member of the public sought recognition to give comment.

FINDINGS AND CONCLUSIONS

Upon review of the entire evidentiary record in this matter, the panel found that the proposed capital expenditures as filed by the Company are reasonable and consistent with previously approved methodologies. For the Qualified Infrastructure Investment Program, the hearing panel voted unanimously to approve a bill surcharge of 24.22%, which is an increase from last year's surcharge of 19.14%. The new surcharge will generate $11,399,082 in annual revenues and represents a $2,388,563 increase from the previous year.

For the Safety and Environmental Compliance Program, the hearing panel voted unanimously to approve a bill surcharge of 9.97%, which is an increase from last year's surcharge of 9.70%. The new surcharge will generate $4,692,865 in annual revenues and represents a $128,556 increase from the previous year. For the Economic Development Investment Rider, the hearing panel voted unanimously to approve a bill surcharge of 1.91%, which is an increase from last year's surcharge of 1.25%. The new surcharge will generate $900,637 in annual revenues and represents an increase of $313,454 from the previous year.

Approval of these Capital Recovery Riders will result in a total cumulative surcharge of 36.10% since inception of the mechanisms. However, consistent with the Commission's decision in Phase I of Docket No. 18-00039, this amount is currently offset by 6.62% in tax savings resulting from the 2017 Tax Cuts and Jobs Act ("TCJA"). Moreover, based on the Commission's decision in Phase II of the same docket, this total Capital Rider Surcharge is further offset by 4.54% for TCJA Excess ADIT. In total, the bill surcharge credits resulting from the Company's tax savings are currently 11.16%. Therefore, the hearing panel voted unanimously to approve a Capital Recovery Rider Surcharge of 36.10% and a total tax credit of 11.16%.

Further, the hearing panel found that these three programs continue to benefit both consumers and Tennessee-American. The programs allow the utility timely recovery of investment related expenses to ensure safe and reliable drinking water and the promotion of economic development, while also benefitting consumers through reduced rate case and legal expenses which might otherwise result, absent these rider mechanisms. Finally, the hearing panel found the TCJA Excess ADIT credit of 4.54% should be continued through December 31, 2022, and the Company was directed to file an updated Excess ADIT credit adjustment in January 2023.

IT IS THEREFORE ORDERED THAT:

1. The *Petition* filed by Tennessee-American Water Company on July 8, 2022 is approved.

2. A Qualified Infrastructure Investment Rider of 24.22% is adopted.

3. A Safety and Environmental Compliance Rider of 9.97% is adopted.

4. An Economic Development Investment Rider of 1.91% is adopted.

5. An additional surcharge credit of 11.16% representing tax savings from the 2017 Tax Cuts and Jobs Act is approved.

6. Any person who is aggrieved by the Commission's decision in this matter may file a Petition for Reconsideration with the Commission within fifteen (15) days from the date of this Order.

7. Any person who is aggrieved by the Commission's decision in this matter has the right to judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty (60) days from the date of this Order.

FOR THE TENNESSEE PUBLIC UTILITY COMMISSION:

Vice Chairman David F. Jones,
Commissioner Robin L. Morrison,
Commissioner Clay R. Good,
Commissioner Kenneth C. Hill, and
Commissioner John Hie concurring.

None dissenting.

ATTEST:

Earl Taylor

Earl R. Taylor, Executive Director