

September 5, 2024

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Room on September 5, 2024 at 2:34 p.m.

David Foster, Director
Utilities Division
c/o Ectory Lawless, Docket Room Manager
Tennessee Public Utility Commission
502 Deaderick Street, 4th Floor
Nashville, TN 37243
TPUC.DocketRoom@tn.gov

RE: *Petition of Tennessee-American Water Company to Modify Tariff, Change and Increase Charges, Fees, and Rates, and for Approval of a General Rate Increase, TPUC Docket No. 24-00032*


Dear Mr. Foster:

Attached for filing please find *Tennessee-American Water Company's Response to First Staff Data Request* in the above-captioned matter.

As required, one (1) hard copy of this filing will be mailed to your office. Should you have any questions concerning this filing, or require additional information, please do not hesitate to contact me.

Very truly yours,

BUTLER SNOW LLP



Melvin J. Malone

cc: Bob Lane, TAWC
Shilina Brown, Consumer Advocate Division
Victoria Glover, Consumer Advocate Division
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**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 1:

Ledger Reconciliation-CWIP. Refer to file <2024 TAWC MFG Q011_Attachment.xlsx> and file <TAWC 2024 Rate Case-RB1 Rate Base Summary.xlsx>. The Company's balance sheet as of December 31, 2023, reported Construction Work In Progress (CWIP) of \$5.2 million. In the workbook RB-1 Summary, however, the Test Year per book value (Column H) does not include any CWIP. Please provide an explanation for why CWIP is not included in the test year per book value. If CWIP has been closed and rolled into the Utility Plant in Service, please provide supporting documents showing the posting date, amounts and related UPIS accounts.

Response:

TAWC's position is that plant is not part of rate base until it is, or is forecasted to be, in service and used and useful. Thus, Construction Work in Progress ("CWIP"), which is not yet "used and useful," has not been included in the rate base calculation. Please also refer to response to TAW_R_CADDR3_003_082724.

Please refer to the File <TAWC 2024 Rate Case - Capital & Depreciation Workpaper.xlsx>, Tab "RB2.3 In Service Activity CWIP", included with the Company's filing, for the in-service activity of projects with a CWIP balance as of December 2023.

**TENNESSEE AMERICAN WATER COMPANY
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Question 2:

UPIS-Asset Retirements. Refer to file <TAW_R_CADDR1_147_062524_Attachment.xlsx>. In Account 340315-Comp Software Spec Depr Rate, there are retirements of \$4,134,875 (Cell AR 531) and \$3,028,406 (Cell AI 531) for June 2023 and September 2023, respectively. Please specify the following details for each retirement: 1) name and function of the software program, 2) amount of loss associated with the retirement if any, 3) total costs of the program, 4) depreciation/amortization method, 5) estimated useful life, 6) years in service, 7) accumulated depreciation, and 8) reason of retirement.

Response:

Please see TAW_R_TPUCDR1_002_090524_Attachment.

Please note that the \$3.0M retirement referenced in the question pertains to September 2022 activity, not September 2023 as worded in the question, and the response reflects 2022 accordingly.

TENNESSEE-AMERICAN WATER
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF
RESPONSE TO QUESTION 2
TAW_R_TPUCDR1_002_090524_Attachment

	<u>Jun-23</u>	<u>Sep-22</u>
Retirements	\$4,134,875	\$3,028,406
1 Name and function of software program	SAP Implementation	
2 Amount of loss associate with retirement	no loss, NBV offset in accum depr	
3 Total Cost of Program	\$7,304,164	
4 Depreciation / Amort Method	Group Depreciation - 10%	
5 Estimated useful life	10 years	
6 Years In Service	10 years	
7 Accumulated Depr per NBV	\$4,095,551	\$3,001,822
8 Reason for retirement	Auto retirement	

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Question 3:

UPIS-Asset Addition. Refer to file <TAW_R_CADDR1_147_062524_Attachment.xlsx>. In account 340300-Computer Software, there is an addition of \$1,619,785 (Cell AX451) in December 2023. Please specify the name and function of the software program associated with this investment. Additionally, is this part of the Enterprise Solution Projects totaling \$3.2M described on page 9 of Kevin Kruchinski's testimony? Please explain.

Response:

Please see TAW_R_TPUCDR1_003_090524_Attachment for the identity and details of the requested assets.

Yes, the Enterprise Solutions portion of Kevin Kruchinski's testimony largely refers to these assets.

Software	Description	Original Cost
Alteryx	Implementation of data preparation, workflow and analytic tool for certain tax processes	29,173
Employee Central	Employee Central (SuccessFactors) implementation and subsequent enhancements and addition of modules	94,197
GIS	Implementation of Enhancements & additional functionality to our GIS software	38,560
Global Automation	Implementation of IT Test Automation tools	8,739
Integration for Discount Rates	Implementation of SEW Customer software	19,687
Intelligent Automation 2023	Development of Automations for finance, operations and customer groups.	99,116
Mapcall	Implement enhancements or additional functionality to on-premise work management system	150,314
Meter Data Mgmt. System	Implementation of Cloud for Energy software and associated platform	194,502
myAccess	Implementation and enhancements to identity access software	13,553
Mywater	Design, build and implementation of customer facing portal and associated enhancements	178,500
Powerplan/Powertax Upgrade & Enhancements	Upgrade Powerplan and PowerTax to supportable version as well as implement enhanced functionalities and capabilities including workflow process automation,	37,733
SAP Enhancements and Upgrades	SAP projects to implement additional functionality, significant enhancements , automation of processes as well as annual SAP upgrades	143,679
SCADA	Enhancements & upgrades to SCADA systems, including the implementation of vulnerability and intrusion detection software	291,021
SIEM Enhancements	Purchase and implementation of Security Information and Event Management Software	9,079
Waterly	Purchase and configuration and buildout of water quality Compliance Management Software	17,045
Design, build and test custom applications for the purposes of providing analytics as well as integration and implementation of necessary infrastructure to support the applications including build out of platform and data lakes		
Custom Applications:		
1 View	Custom Application	101,416
Data Platform, Analytics & Enablement	Custom Application	193,469
		<hr/>
		1,619,785

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Question 4:

UPIS-Asset Addition. Refer to file <TAWC 2024 Rate Case-Capital & Depreciation Workpaper.xlsx> tab: RB2.1 In Service Activity Total, Line numbers 8 & 9 Account 333000-Services. Please provide a brief description of the services capitalized in this account, and identify any associated projects referenced in Kevin Kruchinski's testimony.

Line	District	District				Utility Plant		
Number	#	Name	Project Type	Project #	Project Title	Account	Account Descriptio	
8	2602	Chattanooga	G	R26-02G1	Services and Laterals-New	333000	333000-Services	5,155,696
9	2602	Chattanooga	H	R26-02H1	Services and Laterals-Replaced	333000	333000-Services	1,197,774

Response:

Project type G (Line 8) is the cost collector for all materials, labor and restoration associated with installing new water service for new customers. A new water service is made up of all materials required to go from the water main to the customer's point of connection excluding the water meter. Project type H (Line 9) is essentially the same but it is the replacement of an existing service line. Services are generally replaced as a result of a water line replacement project or due to failure.

These costs are covered in Kevin Kruchinski's testimony regarding the Company's investment in Recurring Projects.

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DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 5:

Ledger Reconciliation-UPIS. Refer to file <TAWC 2024 Rate Case-Capital & Depreciation Workpaper.xlsx>, Tab "RB2 UPIS Balance" and file <2024 TAWC MFG Q010 Attachment.xlsx>, Tab "12.23", Trial Balance.

- a) The UPIS-Other P/E-Intangible of \$1.45M is included as a part of UPIS balance in the Company's balance sheet as of December 31, 2023. In the Company's Capital & Deprecation workpaper, tab "RB2 UPIS Balance," however, the total UPIS balance does not include an account described as "intangible" nor does it include an intangible asset account "33910." If intangible assets of \$1.45M has been included in the File<TAWC 2024 Rate Case-Capital & Depreciation Workpaper.xlsx>, Tab "RB2 UPIS Balance," please provide the associated accounts, account descriptions, and amounts.

10133910 UPIS - Other P/E- Intangible	1,450,17
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- b) For intangible asset account 10133910, please identify the two largest intangible assets by original booked dollar amount. Include the following details in the description: type of intangible asset (e.g., goodwill, patent, etc.), original amount, amortization method, estimated useful life, duration held, and remaining net book/unamortized value.

Response:

a) The intangible asset account balance is included in the workpaper in Chattanooga account 339600-Other P/E-CPS (line 45).

b) Please see TAW_R_TPUCDR1_005_090524_Attachment.

TENNESSEE-AMERICAN WATER
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF
RESPONSE TO QUESTION 5b
TAW_R_TPUCDR1_005_090524_Attachment

Asset ID	130281287
Type of asset	Comprehensive Planning Study
Original Amount	\$106,902
Amort Method	Group Depreciation / 339600 - Other P/E - CPS
Estimated Useful Life	10 years
Duration Held (In serv date)	Sep-16
NBV @ 7/31/2024	\$27,735

Asset ID	142773385
Type of asset	Comprehensive Planning Study
Original Amount	\$1,049,122
Amort Method	Group Depreciation / 339600 - Other P/E - CPS
Estimated Useful Life	10 years
Duration Held (In serv date)	Nov-21
NBV @ 7/31/2024	\$762,981

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DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 6:

Ledger Reconciliation-Accumulated Depreciation. Refer to file <2024 TAWC MFG Q011_Attachment.xlsx>. The Company's balance sheet as of December 31, 2023, reported accumulated depreciation of \$133,769,104. In the workbook RB-1 Summary, however, the Test Year per book indicated the accumulated depreciation is \$112,144,198. The difference is \$21,654,906. Please explain the difference.

Response:

The accumulated depreciation component of Rate Base includes both accumulated life depreciation and accumulated cost of removal. The difference of \$21,654,906 represents the accumulated cost of removal balance which is a reduction to the accumulated life depreciation balance of \$133,769,104, which results in the overall accumulated depreciation of \$112,144,198.

**TENNESSEE AMERICAN WATER COMPANY
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DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 7:

Customer Advance Forecasting. Refer to file <RB1 Rate Base Summary.xlsx> and file <RB-8 CAC Bal-DD.xlsx>. Customer Advance activities have not been forecasted for the service areas of Suck Creek, Sequatchie, and Jasper Highlands to determine the 13-month average amount for the attrition year. Please provide an explanation for the exclusion.

Response:

Historically, TAWC has received customer advances only on projects in Chattanooga. For this reason, no customer advances were projected in the other districts.

**TENNESSEE AMERICAN WATER COMPANY
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DOCKET NO. 24-00032
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Responsible Witness: Dominic DeGrazia

Question 8:

Customer Advance. Refer to file <TAW_R_CADDR1_163_062524_Attachment.xlsx>, Tab: Advance, Cell T30. The workpaper shows that the Customer Advance activities for Jasper Highlands totaled \$1,035,895 in March 2021. Please provide an explanation of these activities. Additionally, is there a balance remaining in the Customer Advance account for Jasper Highlands as of December 2023? If so, please explain why Jasper Highland Customer Advance was excluded from the test year.

Response:

The customer advances for Jasper Highlands were received as part of the acquisition of the system.

Customer advances for Jasper Highlands currently have a balance of \$790,500. This was mislabeled as Sequatchie Valley in File <TAWC 2024 Rate Case - Capital & Depreciation Workpaper.xlsx>, Tab "RB8 CAC Balance", which was included with the Company's filing and is referenced here for additional information regarding the account balance.

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Question 9:

Customer Advance Forecast. Refer to the Company's Response to the Consumer Advocate's First Data Request, file <TAW_R_CADDR1_162_062524_Attachment.xlsx> and file <TAW_R_CADDR1_163_062524_Attachment.xlsx>. The total Customer Advance increased from 2022 to 2023 and from test year 2023 to attrition year 2025. The forecasted monthly Customer Advance activity is **negative** \$41,667 (indicating an increase in Customer Advances) for 2024 and 2025, while the average monthly Customer Advance in the past two years, 2022 and 2023, has been **positive** \$245,598 and \$20,056, respectively. Please confirm that the signs used in front of the activities in the Excel worksheets CAD 1-163 and CAD 1-162 are accurate and consistent. Additionally, please explain the rationale behind forecasting a \$1 million increase (or a monthly average of \$41,667) in Customer Advance from 2024 to 2025.

Response:

The positive amounts displayed in CAD 1-163 are intended to represent increases in Customer advances. Meanwhile, the negative amounts displayed in CAD 1-162 also indicate increases in Customer advances.

TAWC is experiencing significant growth and development in and around Chattanooga, resulting in expected greater customer advances.

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Question 10:

Deferred Income Tax. Refer to file <TAWC 2024 Rate Case- Deferred Tax.xlsx>, tab: Proration. The Company used remaining days/365 method to prorate forecasted 2025 ADIT activities, resulting in the forecasted 2025 activities decreasing from \$2,977,464 to \$1,379,287. Please explain the rationale behind this proration.

Response:

The rationale for the Company using the remaining days/365 method is based on Treasury Regulation Section 1.167(l)-1(h)(6)(ii), a copy of which is attached as TAW_R_TPUCDR1_010_090524_Attachment 1. See the highlighted portion on pages 14 and 15 of the Attachment, which provides support for the Company's method and states the following:

If solely a future period is used for such determination, the amount of the reserve account for the period is the amount of the reserve at the beginning of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during such period.

The pro rata portion of any increase to be credited or decrease to be charged during a future period (or the future portion of a part-historical and part-future period) shall be determined by multiplying any such increase or decrease by a fraction, the numerator of which is the number of days remaining in the period at the time such increase or decrease is to be accrued, and the denominator of which is the total number of days in the period (or future portion).

Code of Federal Regulations
Title 26. Internal Revenue
Chapter I. Internal Revenue Service, Department of the Treasury
Subchapter A. Income Tax
Part 1. Income Taxes (Refs & Annos)
Normal Taxes and Surtaxes
Computation of Taxable Income
Itemized Deductions for Individuals and Corporations

26 C.F.R. § 1.167(l)–1, Treas. Reg. § 1.167(l)–1

§ 1.167(l)–1 Limitations on reasonable allowance in case of property of certain public utilities.

Currentness

(a) In general—(1) Scope. Section 167(l) in general provides limitations on the use of certain methods of computing a reasonable allowance for depreciation under section 167(a) with respect to “public utility property” (see paragraph (b) of this section) for all taxable years for which a Federal income tax return was not filed before August 1, 1969. The limitations are set forth in paragraph (c) of this section for “pre-1970 public utility property” and in paragraph (d) of this section for “post-1969 public utility property.” Under section 167(l), a taxpayer may always use a straight line method (or other “subsection (l) method” as defined in paragraph (f) of this section). In general, the use of a method of depreciation other than a subsection (l) method is not prohibited by section 167(l) for any taxpayer if the taxpayer uses a “normalization method of regulated accounting” (described in paragraph (h) of this section). In certain cases, the use of a method of depreciation other than a subsection (l) method is not prohibited by section 167(l) if the taxpayer used a “flow-through method of regulated accounting” (described in paragraph (i) of this section) for its “July 1969 regulated accounting period” (described in paragraph (g) of this section) whether or not the taxpayer uses either a normalization or a flow-through method of regulated accounting after its July 1969 regulated accounting period. However, in no event may a method of depreciation other than a subsection (l) method be used in the case of pre-1970 public utility property unless such method of depreciation is the “applicable 1968 method” (within the meaning of paragraph (e) of this section). The normalization requirements of section 167(l) with respect to public utility property defined in section 167(l)(3)(A) pertain only to the deferral of Federal income tax liability resulting from the use of an accelerated method of depreciation for computing the allowance for depreciation under section 167 and the use of straight line depreciation for computing tax expense and depreciation expense for purposes of establishing cost of services and for reflecting operating results in regulated books of account. Regulations under section 167(l) do not pertain to other book-tax timing differences with respect to State income taxes, F.I.C.A. taxes, construction costs, or any other taxes and items. The rules provided in paragraph (h)(6) of this section are to insure that the same time period is used to determine the deferred tax reserve amount resulting from the use of an accelerated method of depreciation for cost of service purposes and the reserve amount that may be excluded from the rate base or included in no-cost capital in determining such cost of services. The formula provided in paragraph (h)(6)(ii) of this section is to be used in conjunction with the method of accounting for the reserve for deferred taxes (otherwise proper under paragraph (h)(2) of this section) in accordance with the accounting requirements prescribed or approved, if applicable, by the regulatory body having jurisdiction over the taxpayer's regulated books of account. The formula provides a method to determine the period of time during which the taxpayer will be treated as having received amounts credited or charged to the reserve account so that the disallowance of earnings with respect to such amounts through rate base exclusion or treatment as no-cost capital will take into account the factor of time for which such amounts are held by the taxpayer. The formula serves to limit the amount of such disallowance.

(2) Methods of depreciation. For purposes of section 167(l), in the case of a declining balance method each different uniform rate applied to the unrecovered cost or other basis of the property is a different method of depreciation. For

purposes of section 167(l), a change in a uniform rate of depreciation due to a change in the useful life of the property or a change in the taxpayer's unrecovered cost or other basis for the property is not a change in the method of depreciation. The use of "guideline lives" or "class lives" for Federal income tax purposes and different lives on the taxpayer's regulated books of account is not treated for purposes of section 167(l) as a different method of depreciation. Further, the use of an unrecovered cost or other basis or salvage value for Federal income tax purposes different from the basis or salvage value used on the taxpayer's regulated books of account is not treated as a different method of depreciation.

(3) Application of certain other provisions to public utility property. For rules with respect to application of the investment credit to public utility property, see section 46(e). For rules with respect to the application of the class life asset depreciation range system, including the treatment of the use of "class lives" for Federal income tax purposes and different lives on the taxpayer's regulated books of account, see § 1.167(a)–11 and § 1.167(a)–12.

(4) Effect on agreements under section 167(d). If the taxpayer has entered into an agreement under section 167(d) as to any public utility property and such agreement requires the use of a method of depreciation prohibited by section 167(l), such agreement shall terminate as to such property. The termination, in accordance with this subparagraph, shall not affect any other property (whether or not public utility property) covered by the agreement.

(5) Effect of change in method of depreciation. If, because the method of depreciation used by the taxpayer with respect to public utility property is prohibited by section 167(l), the taxpayer changes to a method of depreciation not prohibited by section 167(l), then when the change is made the unrecovered cost or other basis shall be recovered through annual allowances over the estimated remaining useful life determined in accordance with the circumstances existing at that time.

(b) Public utility property—(1) In general. Under section 167(l)(3)(A), property is "public utility property" during any period in which it is used predominantly in a "section 167(l) public utility activity". The term "section 167(l) public utility activity" means the trade or business of the furnishing or sale of—

(i) Electrical energy, water, or sewage disposal services,

(ii) Gas or steam through a local distribution system,

(iii) Telephone services,

(iv) Other communication services (whether or not telephone services) if furnished or sold by the Communications Satellite Corporation for purposes authorized by the Communications Satellite Act of 1962 (47 U.S.C. 701), or

(v) Transportation of gas or steam by pipeline,

if the rates for such furnishing or sale, as the case may be, are regulated, *i.e.*, have been established or approved by a regulatory body described in section 167(l)(3)(A). The term "regulatory body described in section 167(l)(3)(A)" means a State (including the District of Columbia) or political subdivision thereof, any agency or instrumentality of the United States, or a public service or public utility commission or other body of any State or political subdivision thereof similar to such a commission. The term "established or approved" includes the filing of a schedule of rates with a regulatory body

which has the power to approve such rates, even though such body has taken no action on the filed schedule or generally leaves undisturbed rates filed by the taxpayer involved.

(2) Classification of property. If property is not used solely in a section 167(l) public utility activity, such property shall be public utility property if its predominant use is in a section 167(l) public utility activity. The predominant use of property for any period shall be determined by reference to the proper accounts to which expenditures for such property are chargeable under the system of regulated accounts required to be used for the period for which the determination is made and in accordance with the principles of § 1.46–3(g)(4) (relating to credit for investment in certain depreciable property). Thus, for example, for purposes of determining whether property is used predominantly in the trade or business of the furnishing or sale of transportation of gas by pipeline, or furnishing or sale of gas through a local distribution system, or both, the rules prescribed in § 1.46–3(g)(4) apply, except that accounts 365 through 371, inclusive (Transmission Plant), shall be added to the accounts enumerated in subdivision (i) of such paragraph (g)(4).

(c) Pre-1970 public utility property—(1) Definition. (i) Under section 167(l)(3)(B), the term “pre-1970 public utility property” means property which was public utility property at any time before January 1, 1970. If a taxpayer acquires pre-1970 public utility property, such property shall be pre-1970 public utility property in the hands of the taxpayer even though such property may have been acquired by the taxpayer in an arm's-length cash sale at fair market value or in a tax-free exchange. Thus, for example, if corporation X which is a member of the same controlled group of corporations (within the meaning of section 1563(a)) as corporation Y sells pre-1970 public utility property to Y, such property is pre-1970 public utility property in the hands of Y. The result would be the same if X and Y were not members of the same controlled group of corporations.

(ii) If the basis of public utility property acquired by the taxpayer in a transaction is determined in whole or in part by reference to the basis of any of the taxpayer's pre-1970 public utility property by reason of the application of any provision of the code, and if immediately after the transaction the adjusted basis of the property acquired is less than 200 percent of the adjusted basis of such pre-1970 public utility property immediately before the transaction, the property acquired is pre-1970 public utility property.

(2) Methods of depreciation not prohibited. Under section 167(l)(1), in the case of pre-1970 public utility property, the term “reasonable allowance” as used in section 167(a) means, for a taxable year for which a Federal income tax return was not filed before August 1, 1969, and in which such property is public utility property, an allowance (allowable without regard to section 167(l)) computed under—

(i) A subsection (l) method, or

(ii) The applicable 1968 method (other than a subsection (l) method) used by the taxpayer for such property, but only if—

(a) The taxpayer uses in respect of such taxable year a normalization method of regulated accounting for such property,

(b) The taxpayer used a flow-through method of regulated accounting for such property for its July 1969 regulated accounting period, or

(c) The taxpayer's first regulated accounting period with respect to such property is after the taxpayer's July 1969 regulated accounting period and the taxpayer used a flow-through method of regulated accounting for its July 1969

regulated accounting period for public utility property of the same kind (or if there is no property of the same kind, property of the most similar kind) most recently placed in service. See paragraph (e)(5) of this section for determination of same (or similar) kind.

(3) Flow-through method of regulated accounting in certain cases. See paragraph (e)(6) of this section for treatment of certain taxpayers with pending applications for change in method of accounting as being deemed to have used a flow-through method of regulated accounting for the July 1969 regulated accounting period.

(4) Examples. The provisions of this paragraph may be illustrated by the following examples:

Example 1. Corporation X, a calendar-year taxpayer subject to the jurisdiction of a regulatory body described in section 167(l)(3)(A), used the straight line method of depreciation (a subsection (l) method) for all of its public utility property for which depreciation was allowable on its Federal income tax return for 1967 (the latest taxable year for which X, prior to August 1, 1969, filed a return). Assume that under paragraph (e) of this section, X's applicable 1968 method is a subsection (l) method with respect to all of its public utility property. Thus, with respect to its pre-1970 public utility property, X may only use a straight line method (or any other subsection (l) method) of depreciation for all taxable years after 1967.

Example 2. Corporation Y, a calendar-year taxpayer subject to the jurisdiction of the Federal Power Commission, is engaged exclusively in the transportation of gas by pipeline. On its Federal income tax return for 1967 (the latest taxable year for which Y, prior to August 1, 1969, filed a return), Y used the declining balance method of depreciation using a rate of 150 percent of the straight line rate for all of its nonsection 1250 public utility property with respect to which depreciation was allowable. Assume that with respect to all of such property, Y's applicable 1968 method under paragraph (e) of this section is such 150 percent declining balance method. Assume that Y used a normalization method of regulated accounting for all relevant regulated accounting periods. If Y continues to use a normalization method of regulated accounting, Y may compute its reasonable allowance for purposes of section 167(a) using such 150 percent declining balance method for its nonsection 1250 pre-1970 public utility property for all taxable years beginning with 1968, provided the use of such method is allowable without regard to section 167(l). Y may also use a subsection (l) method for any of such pre-1970 public utility property for all taxable years beginning after 1967. However, because each different uniform rate applied to the basis of the property is a different method of depreciation, Y may not use a declining balance method of depreciation using a rate of twice the straight line rate for any of such pre-1970 public utility property for any taxable year beginning after 1967.

Example 3. Assume the same facts as in example (2) except that with respect to all of its nonsection 1250 pre-1970 public utility property accounted for in its July 1969 regulated accounting period Y used a flow-through method of regulated accounting for such period. Assume further that such property is the property on the basis of which the applicable 1968 method is established for pre-1970 public utility property of the same kind, but having a first regulated accounting period after the taxpayer's July 1969 regulated accounting period. Beginning with 1968, with respect to such property Y may compute its reasonable allowance for purposes of section 167(a) using the declining balance method of depreciation and a rate of 150 percent of the straight line rate, whether it uses a normalization or flow-through method of regulated accounting after its July 1969 regulated accounting period, provided the use of such method is allowable without regard to section 167(l).

(d) Post-1969 public utility property—(1) In general. Under section 167(l)(3)(C), the term “post-1969 public utility property” means any public utility property which is not pre-1970 public utility property.

(2) Methods of depreciation not prohibited. Under section 167(l)(2), in the case of post-1969 public utility property, the term “reasonable allowance” as used in section 167(a) means, for a taxable year, an allowance (allowable without regard to section 167(l)) computed under—

(i) A subsection (l) method,

(ii) A method of depreciation otherwise allowable under section 167 if, with respect to the property, the taxpayer uses in respect of such taxable year a normalization method of regulated accounting, or

(iii) The taxpayer's applicable 1968 method (other than a subsection (l) method) with respect to the property in question, if the taxpayer used a flow-through method of regulated accounting for its July 1969 regulated accounting period for the property of the same (or similar) kind most recently placed in service, provided that the property in question is not property to which an election under section 167(l)(4)(A) applies. See § 1.167(l)(2) for rules with respect to an election under section 167(l)(4)(A). See paragraph (e)(5) of this section for definition of same (or similar) kind.

(3) **Examples.** The provisions of this paragraph may be illustrated by the following examples:

Example 1. Corporation X is engaged exclusively in the trade or business of the transportation of gas by pipeline and is subject to the jurisdiction of the Federal Power Commission. With respect to all its public utility property, X's applicable 1968 method (as determined under paragraph (e) of this section) is the straight line method of depreciation. X may determine its reasonable allowance for depreciation under section 167(a) with respect to its post–1969 public utility property under a straight line method (or other subsection (l) method) or, if X uses a normalization method of regulated accounting, any other method of depreciation, provided that the use of such other method is allowable under section 167 without regard to section 167(l).

Example 2. Assume the same facts as in example (1) except that with respect to all of X's post–1969 public utility property the applicable 1968 method (as determined under paragraph (e) of this section) is the declining balance method using a rate of 150 percent of the straight line rate. Assume further that all of X's pre–1970 public utility property was accounted for in its July 1969 regulated accounting period, and that X used a flow-through method of regulated accounting for such period. X may determine its reasonable allowance for depreciation under section 167 with respect to its post–1969 public utility property by using the straight line method of depreciation (or any other subsection (l) method), by using any method otherwise allowable under section 167 (such as a declining balance method) if X uses a normalization method of regulated accounting, or, by using the declining balance method using a rate of 150 percent of the straight line rate, whether or not X uses a normalization or a flow-through method of regulated accounting.

(e) **Applicable 1968 method—(1) In general.** Under section 167(l)(3)(D), except as provided in subparagraphs (3) and (4) of this paragraph, the term “applicable 1968 method” means with respect to any public utility property—

(i) The method of depreciation properly used by the taxpayer in its Federal income tax return with respect to such property for the latest taxable year for which a return was filed before August 1, 1969,

(ii) If subdivision (i) of this subparagraph does not apply, the method of depreciation properly used by the taxpayer in its Federal income tax return for the latest taxable year for which a return was filed before August 1, 1969, with respect to public utility property of the same kind (or if there is no property of the same kind, property of the most similar kind) most recently placed in service before the end of such latest taxable year, or

(iii) If neither subdivision (i) nor (ii) of this subparagraph applies, a subsection (l) method.

If, on or after August 1, 1969, the taxpayer files an amended return for the taxable year referred to in subdivisions (i) and (ii) of this subparagraph, such amended return shall not be taken into consideration in determining the applicable 1968 method. The term “applicable 1968 method” if such new method results to any public utility property, for the year of change and subsequent years, a method of depreciation otherwise allowable under section 167 to which the taxpayer changes from an applicable 1968 method if such new method results in a lesser allowance for depreciation for such property under section 167 in the year of change and the taxpayer secures the Commissioner's consent to the change in accordance with the procedures of section 446(e) and § 1.446-1.

(2) Placed in service. For purposes of this section, property is placed in service on the date on which the period for depreciation begins under section 167. See, for example, § 1.167(a)-10(b) and § 1.167(a)-11(c)(2). If under an averaging convention property which is placed in service (as defined in § 1.46-3(d)(ii)) by the taxpayer on different dates is treated as placed in service on the same date, then for purposes of section 167(l) the property shall be treated as having been placed in service on the date the period for depreciation with respect to such property would begin under section 167 absent such averaging convention. Thus, for example, if, except for the fact that the averaging convention used assumes that all additions and retirements made during the first half of the year were made on the first day of the year, the period of depreciation for two items of public utility property would begin on January 10 and March 15, respectively, then for purposes of determining the property of the same (or similar) kind most recently placed in service, such items of property shall be treated as placed in service on January 10 and March 15, respectively.

(3) Certain section 1250 property. If a taxpayer is required under section 167(j) to use a method of depreciation other than its applicable 1968 method with respect to any section 1250 property, the term “applicable 1968 method” means the method of depreciation allowable under section 167(j) which is the most nearly comparable method to the applicable 1968 method determined under subparagraph (1) of this paragraph. For example, if the applicable 1968 method on new section 1250 property is the declining balance method using 200 percent of the straight line rate, the most nearly comparable method allowable for new section 1250 property under section 167(j) would be the declining balance method using 150 percent of the straight line rate. If the applicable 1968 method determined under subparagraph (1) of this paragraph is the sum of the years-digits method, the term “most nearly comparable method” refers to any method of depreciation allowable under section 167(j).

(4) Applicable 1968 method in certain cases. (i)(a) Under section 167(l)(3)(E), if the taxpayer evidenced within the time and manner specified in (b) of this subdivision (i) the intent to use a method of depreciation under section 167 (other than its applicable 1968 method as determined under subparagraph (1) or (3) of this paragraph or a subsection (l) method) with respect to any public utility property, such method of depreciation shall be deemed to be the taxpayer's applicable 1968 method with respect to such public utility property and public utility property of the same (or most similar) kind subsequently placed in service.

(b) Under this subdivision (i), the intent to use a method of depreciation under section 167 is evidenced—

(1) By a timely application for permission for a change in method of accounting filed by the taxpayer before August 1, 1969, or

(2) By the use of such method of depreciation in the computation by the taxpayer of its tax expense for purposes of reflecting operating results in its regulated books of account for its July 1969 regulated accounting period, as established in the manner prescribed in paragraph (g)(1)(i), (ii), or (iii) of this section.

(ii)(a) If public utility property is acquired in a transaction in which its basis in the hands of the transferee is determined in whole or in part by reference to its basis in the hands of the transferor by reason of the application of any provision of the Code, or in a transfer (including any purchase for cash or in exchange) from a related person, then in the hands of the transferee the applicable 1968 method with respect to such property shall be determined by reference to the treatment in respect of such property in the hands of the transferor.

(b) For purposes of this subdivision (ii), the term “related person” means a person who is related to another person if either immediately before or after the transfer—

(1) The relationship between such persons would result in a disallowance of losses under section 267 (relating to disallowance of losses, etc., between related taxpayers) or section 707(b) (relating to losses disallowed, etc., between partners and controlled partnerships) and the regulations thereunder, or

(2) Such persons are members of the same controlled group of corporations, as defined in section 1563(a) (relating to definition of controlled group of corporations), except that “more than 50 percent” shall be substituted for “at least 80 percent” each place it appears in section 1563(a) and the regulations thereunder.

(5) Same or similar. The classification of property as being of the same (or similar) kind shall be made by reference to the function of the public utility to which the primary use of the property relates. Property which performs the identical function in the identical manner shall be treated as property of the same kind. The determination that property is of a similar kind shall be made by reference to the proper account to which expenditures for the property are chargeable under the system of regulated accounts required to be used by the taxpayer for the period in which the property in question was acquired. Property, the expenditure for which is chargeable to the same account, is property of the most similar kind. Property, the expenditure for which is chargeable to an account for property which serves the same general function, is property of a similar kind. Thus, for example, if corporation X, a natural gas company, subject to the jurisdiction of the Federal Power Commission, had property properly chargeable to account 366 (relating to transmission plant structures and improvements) acquired an additional structure properly chargeable to account 366, under the uniform system of accounts prescribed for natural gas companies (class A and class B) by the Federal Power Commission, effective September 1, 1968, the addition would constitute property of the same kind if it performed the identical function in the identical manner. If, however, the addition did not perform the identical function in the identical manner, it would be property of the most similar kind.

(6) Regulated method of accounting in certain cases. Under section 167(l)(4)(B), if with respect to any pre-1970 public utility property the taxpayer filed a timely application for change in method of accounting referred to in subparagraph (4)(i)(b)(1) of this paragraph and with respect to property of the same (or similar) kind most recently placed in service the taxpayer used a flow-through method of regulated accounting for its July 1969 regulated accounting period, then for purposes of section 167(l)(1)(B) and paragraph (c) of this section the taxpayer shall be deemed to have used a flow-through method of regulated accounting with respect to such pre-1970 public utility property.

(7) Examples. The provisions of this paragraph may be illustrated by the following examples:

Example 1. Corporation X is a calendar-year taxpayer. On its Federal income tax return for 1967 (the latest taxable year for which X, prior to August 1, 1969, filed a return) X used a straight line method of depreciation with respect to certain public utility property placed in service before 1965 and used the declining balance method of depreciation using 200 percent of the straight line rate (double declining balance) with respect to the same kind of public utility property placed in service after 1964. In 1968 and 1970, X placed in service additional public utility property of the same kind. The applicable 1968 method with respect to the above described public utility property is shown in the following chart:

Property held in 1970	Placed in service	Method on 1967 return	Applicable 1968 method
Group 1.....	Before 1965	Straight line	Straight line.
Group 2.....	After 1964 and before 1968.	Double declining balance.	Double declining balance.
Group 3.....	After 1967 and before 1969.	Do.
Group 4.....	After 1968	Do.

Example 2. Corporation Y is a calendar-year taxpayer engaged exclusively in the trade or business of the furnishing of electrical energy. In 1954, Y placed in service hydroelectric generators and for all purposes Y has taken straight line depreciation with respect to such generators. In 1960, Y placed in service fossil fuel generators and for all purposes since 1960 has used the declining balance method of depreciation using a rate of 150 percent of the straight line rate (computed without reduction for salvage) with respect to such generators. After 1960 and before 1970 Y did not place in service any generators. In 1970, Y placed in service additional hydroelectric generators. The applicable 1968 method with respect to the hydroelectric generators placed in service in 1970 would be the straight line method because it was the method used by Y on its return for the latest taxable year for which Y filed a return before August 1, 1969, with respect to property of the same kind (*i.e.*, hydroelectric generators) most recently placed in service.

Example 3. Assume the same facts as in example (2), except that the generators placed in service in 1970 were nuclear generators. The applicable 1968 method with respect to such generators is the declining balance method using a rate of 150 percent of the straight line rate because, with respect to property of the most similar kind (fossil fuel generators) most recently placed in service, Y used such declining balance method on its return for the latest taxable year for which it filed a return before August 1, 1969.

(f) Subsection (l) method. Under section 167(l)(3)(F), the term “subsection (l) method” means a reasonable and consistently applied ratable method of computing depreciation which is allowable under section 167(a), such as, for example, the straight line method or a unit of production method or machine-hour method. The term “subsection (l) method” does not include any declining balance method (regardless of the uniform rate applied), sum of the years-digits method, or method of depreciation which is allowable solely by reason of section 167(b)(4) or (j)(1)(C).

(g) July 1969 regulated accounting period—(1) In general. Under section 167(l)(3)(I), the term “July 1969 regulated accounting period” means the taxpayer's latest accounting period ending before August 1, 1969, for which the taxpayer regularly computed, before January 1, 1970, its tax expense for purposes of reflecting operating results in its regulated books of account. The computation by the taxpayer of such tax expense may be established by reference to the following:

(i) The most recent periodic report of a period ending before August 1, 1969, required by a regulatory body described in section 167(l)(3)(A) having jurisdiction over the taxpayer's regulated books of account which was filed with such body before January 1, 1970 (whether or not such body has jurisdiction over rates).

(ii) If subdivision (i) of this subparagraph does not apply, the taxpayer's most recent report to its shareholders for a period ending before August 1, 1969, but only if such report was distributed to the shareholders before January 1, 1970, and if the taxpayer's stocks or securities are traded in an established securities market during such period. For purposes of this subdivision, the term “established securities market” has the meaning assigned to such term in § 1.453–3(d)(4).

(iii) If subdivisions (i) and (ii) of this subparagraph do not apply, entries made to the satisfaction of the district director before January 1, 1970, in its regulated books of account for its most recent accounting period ending before August 1, 1969.

(2) July 1969 method of regulated accounting in certain acquisitions. If public utility property is acquired in a transaction in which its basis in the hands of the transferee is determined in whole or in part by reference to its basis in the hands of the transferor by reason of the application of any provision of the Code, or in a transfer (including any purchase for cash or in exchange) from a related person, then in the hands of the transferee the method of regulated accounting for such property's July 1969 regulated accounting period shall be determined by reference to the treatment in respect of such property in the hands of the transferor. See paragraph (e)(4)(ii) of this section for definition of “related person”.

(3) Determination date. For purposes of section 167(l), any reference to a method of depreciation under section 167(a), or a method of regulated accounting, taken into account by the taxpayer in computing its tax expense for its July 1969 regulated accounting period shall be a reference to such tax expense as shown on the periodic report or report to shareholders to which subparagraph (1)(i) or (ii) of this paragraph applies or the entries made on the taxpayer's regulated books of account to which subparagraph (1)(iii) of this paragraph applies. Thus, for example, assume that regulatory body A having jurisdiction over public utility property with respect to X's regulated books of account requires X to reflect its tax expense in such books using the same method of depreciation which regulatory body B uses for determining X's cost of service for ratemaking purposes. If in 1971, in the course of approving a rate change for X, B retroactively determines X's cost of service for ratemaking purposes for X's July 1969 regulated accounting period using a method of depreciation different from the method reflected in X's regulated books of account as of January 1, 1970, the method of depreciation used by X for its July 1969 regulated accounting period would be determined without reference to the method retroactively used by B in 1971.

(h) Normalization method of accounting—(1) In general. **(i)** Under section 167(l), a taxpayer uses a normalization method of regulated accounting with respect to public utility property—

(a) If the same method of depreciation (whether or not a subsection (l) method) is used to compute both its tax expense and its depreciation expense for purposes of establishing cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account, and

(b) If to compute its allowance for depreciation under section 167 it uses a method of depreciation other than the method it used for purposes described in (a) of this subdivision, the taxpayer makes adjustments consistent with subparagraph (2) of this paragraph to a reserve to reflect the total amount of the deferral of Federal income tax liability resulting from the use with respect to all of its public utility property of such different methods of depreciation.

(ii) In the case of a taxpayer described in section 167(l)(1)(B) or (2)(C), the reference in subdivision (i) of this subparagraph shall be a reference only to such taxpayer's "qualified public utility property". See § 1.167(l)–2(b) for definition of "qualified public utility property".

(iii) Except as provided in this subparagraph, the amount of Federal income tax liability deferred as a result of the use of a different method of depreciation under subdivision (i) of this subparagraph is the excess (computed without regard to credits) of the amount the tax liability would have been had a subsection (l) method been used over the amount of the actual tax liability. Such amount shall be taken into account for the taxable year in which such different methods of depreciation are used. If, however, in respect of any taxable year the use of a method of depreciation other than a subsection (l) method for purposes of determining the taxpayer's reasonable allowance under section 167(a) results in a net operating loss carryover (as determined under section 172) to a year succeeding such taxable year which would not have arisen (or an increase in such carryover which would not have arisen) had the taxpayer determined his reasonable allowance under section 167(a) using a subsection (l) method, then the amount and time of the deferral of tax liability shall be taken into account in such appropriate time and manner as is satisfactory to the district director.

(2) Adjustments to reserve. (i) The taxpayer must credit the amount of deferred Federal income tax determined under subparagraph (1)(i) of this paragraph for any taxable year to a reserve for deferred taxes, a depreciation reserve, or other reserve account. The taxpayer need not establish a separate reserve account for such amount but the amount of deferred tax determined under subparagraph (1)(i) of this paragraph must be accounted for in such a manner so as to be readily identifiable. With respect to any account, the aggregate amount allocable to deferred tax under section 167(l) shall not be reduced except to reflect the amount for any taxable year by which Federal income taxes are greater by reason of the prior use of different methods of depreciation under subparagraph (1)(i) of this paragraph. An additional exception is that the aggregate amount allocable to deferred tax under section 167(l) may be properly adjusted to reflect asset retirements or the expiration of the period for depreciation used in determining the allowance for depreciation under section 167(a).

(ii) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. Corporation X is exclusively engaged in the transportation of gas by pipeline subject to the jurisdiction of the Federal Power Commission. With respect to its post-1969 public utility property, X is entitled under section 167(l)(2)(B) to use a method of depreciation other than a subsection (l) method if it uses a normalization method of regulated accounting. With respect to such property, X has not made any election under § 1.167(a)–11 (relating to depreciation based on class lives and asset depreciation ranges). In 1972, X places in service public utility property with an unadjusted basis of \$2 million, and an estimated useful life of 20 years. X uses the declining balance method of depreciation with a rate twice the straight line rate. If X uses a normalization method of regulated accounting, the amount of depreciation allowable under section 167(a) with respect to such property for 1972 computed under the double declining balance method would be \$200,000. X computes its tax expense and depreciation expense for purposes of determining its cost of service for rate-making purposes and for reflecting

operating results in its regulated books of account using the straight line method of depreciation (a subsection (l) method). A depreciation allowance computed in this manner is \$100,000. The excess of the depreciation allowance determined under the double declining balance method (\$200,000) over the depreciation expense computed using the straight line method (\$100,000) is \$100,000. Thus, assuming a tax rate of 48 percent, X used a normalization method of regulated accounting for 1972 with respect to property placed in service that year if for 1972 it added to a reserve \$48,000 as taxes deferred as a result of the use by X of a method of depreciation for Federal income tax purposes different from that used for establishing its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account.

Example 2. Assume the same facts as in example (1), except that X elects to apply § 1.167(a)–11 with respect to all eligible property placed in service in 1972. Assume further that all property X placed in service in 1972 is eligible property. One hundred percent of the asset guideline period for such property is 22 years and the asset depreciation range is from 17.5 years to 26.5 years. X uses the double declining balance method of depreciation, selects an asset depreciation period of 17.5 years, and applies the half-year convention (described in § 1.167(a)–11(c)(2)(iii)). In 1972, the depreciation allowable under section 167(a) with respect to property placed in service in 1972 is \$114,285 (determined without regard to the normalization requirements in § 1.167(a)–11(b)(6) and in section 167(l)). X computes its tax expense for purposes of determining its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account using the straight line method of depreciation (a subsection (l) method), an estimated useful life of 22 years (that is, 100 percent of the asset guideline period), and the half-year convention. A depreciation allowance computed in this manner is \$45,454. Assuming a tax rate of 48 percent, the amount that X must add to a reserve for 1972 with respect to property placed in service that year in order to qualify as using a normalization method of regulated accounting under section 167(l)(3)(G) is \$27,429 and the amount in order to satisfy the normalization requirements of § 1.167(a)–11(b)(6) is \$5,610. X determined such amounts as follows:

(D)epreciation allowance on tax return (determined without regard to section 167(l) and § 1.167(a)–11(b)(6)).....	\$114,285
(E)ne (1), recomputed using a straight line method.....	57,142
(B)ifference in depreciation allowance attributable to different methods (line (1) minus line (2)).....	\$57,143
(A)mount to add to reserve under this paragraph (48 percent of line (3)).....	27,429
(A)mount in line (2).....	\$57,142
(E)ne (5), recomputed by using an estimated useful life of 22 years and the half-year convention.....	45,454
(D)ifference in depreciation allowance attributable to difference in depreciation periods.....	\$11,688
(A)mount to add to reserve under § 1.167(a)–11(b)(6)(ii) (48 percent of line (7)).....	5,610

If, for its depreciation expense for purposes of determining its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account, X had used a period in excess of the asset guideline period of 22 years, the total amount in lines (4) and (8) in this example would not be changed.

Example 3. Corporation Y, a calendar-year taxpayer which is engaged in furnishing electrical energy, made the election provided by section 167(l)(4)(a) with respect to its “qualified public utility property” (as defined in § 1.167(l)–2(b)). In 1971, Y placed in service qualified public utility property which had an adjusted basis of \$2 million, estimated useful life of 20 years, and no salvage value. With respect to property of the same kind most recently placed in service, Y used a flow-through method of regulated accounting for its July 1969 regulated accounting period and the applicable 1968 method is the declining balance method of depreciation using 200 percent of the straight line rate. The amount of depreciation allowable under the double

declining balance method with respect to the qualified public utility property would be \$200,000. Y computes its tax expense and depreciation expense for purposes of determining its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account using the straight line method of depreciation. A depreciation allowance with respect to the qualified public utility property determined in this manner is \$100,000. The excess of the depreciation allowance determined under the double declining balance method (\$200,000) over the depreciation expense computed using the straight line method (\$100,000) is \$100,000. Thus, assuming a tax rate of 48 percent, Y used a normalization method of regulated accounting for 1971 if for 1971 it added to a reserve \$48,000 as tax deferred as a result of the use by Y of a method of depreciation for Federal income tax purposes with respect to its qualified public utility property which method was different from that used for establishing its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account for such property.

Example 4. Corporation Z, exclusively engaged in a public utility activity did not use a flow-through method of regulated accounting for its July 1969 regulated accounting period. In 1971, a regulatory body having jurisdiction over all of Z's property issued an order applicable to all years beginning with 1968 which provided, in effect, that Z use an accelerated method of depreciation for purposes of section 167 and for determining its tax expenses for purposes of reflecting operating results in its regulated books of account. The order further provided that Z normalize 50 percent of the tax deferral resulting from the use of the accelerated method of depreciation and that Z flow-through 50 percent of the tax deferral resulting therefrom. Under section 167(l), the method of accounting provided in the order would not be a normalization method of regulated accounting because Z would not be permitted to normalize 100 percent of the tax deferral resulting from the use of an accelerated method of depreciation. Thus, with respect to its public utility property for purposes of section 167, Z may only use a subsection (l) method of depreciation.

Example 5. Assume the same facts as in example (4) except that the order of the regulatory body provided, in effect, that Z normalize 100 percent of the tax deferral with respect to 50 percent of its public utility property and flow-through the tax savings with respect to the other 50 percent of its property. Because the effect of such an order would allow Z to flow-through a portion of the tax savings resulting from the use of an accelerated method of depreciation, Z would not be using a normalization method of regulated accounting with respect to any of its properties. Thus, with respect to its public utility property for purposes of section 167, Z may only use a subsection (l) method of depreciation.

(3) Establishing compliance with normalization requirements in respect of operating books of account. The taxpayer may establish compliance with the requirement in subparagraph (l)(i) of this paragraph in respect of reflecting operating results, and adjustments to a reserve, in its operating books of account by reference to the following:

(i) The most recent periodic report for a period beginning before the end of the taxable year, required by a regulatory body described in section 167(l)(3)(A) having jurisdiction over the taxpayer's regulated operating books of account which was filed with such body before the due date (determined with regard to extensions) of the taxpayer's Federal income tax return for such taxable year (whether or not such body has jurisdiction over rates).

(ii) If subdivision (i) of this subparagraph does not apply, the taxpayer's most recent report to its shareholders for the taxable year but only if (a) such report was distributed to the shareholders before the due date (determined with regard to extensions) of the taxpayer's Federal income tax return for the taxable year and (b) the taxpayer's stocks or securities are traded in an established securities market during such taxable year. For purposes of this subdivision, the term "established securities market" has the meaning assigned to such term in § 1.453-3(d)(4).

(iii) If neither subdivision (i) nor (ii) of this subparagraph applies, entries made to the satisfaction of the district director before the due date (determined with regard to extensions) of the taxpayer's Federal income tax return for the taxable year in its regulated books of account for its most recent period beginning before the end of such taxable year.

(4) Establishing compliance with normalization requirements in computing cost of service for ratemaking purposes.

(i) In the case of a taxpayer which used a flow-through method of regulated accounting for its July 1969 regulated accounting period or thereafter, with respect to all or a portion of its pre-1970 public utility property, if a regulatory body having jurisdiction to establish the rates of such taxpayer as to such property (or a court which has jurisdiction over such body) issues an order of general application (or an order of specific application to the taxpayer) which states that such regulatory body (or court) will permit a class of taxpayers of which such taxpayer is a member (or such taxpayer) to use the normalization method of regulated accounting to establish cost of service for ratemaking purposes with respect to all or a portion of its public utility property, the taxpayer will be presumed to be using the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing its cost of service for ratemaking purposes with respect to the public utility property to which such order applies. In the event that such order is in any way conditional, the preceding sentence shall not apply until all of the conditions contained in such order which are applicable to the taxpayer have been fulfilled. The taxpayer shall establish to the satisfaction of the Commissioner or his delegate that such conditions have been fulfilled.

(ii) In the case of a taxpayer which did not use the flow-through method of regulated accounting for its July 1969 regulated accounting period or thereafter (including a taxpayer which used a subsection (l) method of depreciation to compute its allowance for depreciation under section 167(a) and to compute its tax expense for purposes of reflecting operating results in its regulated books of account), with respect to any of its public utility property, it will be presumed that such taxpayer is using the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing its cost of service for ratemaking purposes with respect to its post-1969 public utility property. The presumption described in the preceding sentence shall not apply in any case where there is (a) an expression of intent (regardless of the manner in which such expression of intent is indicated) by the regulatory body (or bodies), having jurisdiction to establish the rates of such taxpayer, which indicates that the policy of such regulatory body is in any way inconsistent with the use of the normalization method of regulated accounting by such taxpayer or by a class of taxpayers of which such taxpayer is a member, or (b) a decision by a court having jurisdiction over such regulatory body which decision is in any way inconsistent with the use of the normalization method of regulated accounting by such taxpayer or a class of taxpayers of which such taxpayer is a member. The presumption shall be applicable on January 1, 1970, and shall, unless rebutted, be effective until an inconsistent expression of intent is indicated by such regulatory body or by such court. An example of such an inconsistent expression of intent is the case of a regulatory body which has, after the July 1969 regulated accounting period and before January 1, 1970, directed public utilities subject to its ratemaking jurisdiction to use a flow-through method of regulated accounting, or has issued an order of general application which states that such agency will direct a class of public utilities of which the taxpayer is a member to use a flow-through method of regulated accounting. The presumption described in this subdivision may be rebutted by evidence that the flow-through method of regulated accounting is being used by the taxpayer with respect to such property.

(iii) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. Corporation X is a calendar-year taxpayer and its “applicable 1968 method” is a straight line method of depreciation. Effective January 1, 1970, X began collecting rates which were based on a sum of the years-digits method of depreciation and a normalization method of regulated accounting which rates had been approved by a regulatory body having jurisdiction over X. On October 1, 1971, a court of proper jurisdiction annulled the rate order prospectively, which annulment was not appealed, on the basis that the regulatory body had abused its discretion by determining the rates on the basis of a normalization method of regulated accounting. As there was no inconsistent expression of intent during 1970 or prior to the due date of X's return for 1970, X's use of the sum of the years-digits method of depreciation for purposes of section 167 on such return was proper. For 1971, the presumption is in effect through September 30. During 1971, X may use the sum of the years-digits method of

depreciation for purposes of section 167 from January 1 through September 30, 1971. After September 30, 1971, and for taxable years after 1971, X must use a straight line method of depreciation until the inconsistent court decision is no longer in effect.

Example 2. Assume the same facts as in example (1), except that pursuant to the order of annulment, X was required to refund the portion of the rates attributable to the use of the normalization method of regulated accounting. As there was no inconsistent expression of intent during 1970 or prior to the due date of X's return for 1970, X has the benefit of the presumption with respect to its use of the sum of the years-digits method of depreciation for purposes of section 167, but because of the retroactive nature of the rate order X must file an amended return for 1970 using a straight line method of depreciation. As the inconsistent decision by the court was handed down prior to the due date of X's Federal income tax return for 1971, for 1971 and thereafter the presumption of subdivision (ii) of this subparagraph does not apply. X must file its Federal income tax returns for such years using a straight line method of depreciation.

Example 3. Assume the same facts as in example (2), except that the annulment order was stayed pending appeal of the decision to a court of proper appellate jurisdiction, X has the benefit of the presumption as described in example (2) for the year 1970, but for 1971 and thereafter the presumption of subdivision (ii) of this subparagraph does not apply. Further, X must file an amended return for 1970 using a straight line method of depreciation and for 1971 and thereafter X must file its returns using a straight line method of depreciation unless X and the district director have consented in writing to extend the time for assessment of tax for 1970 and thereafter with respect to the issue of normalization method of regulated accounting for as long as may be necessary to allow for resolution of the appeal with respect to the annulment of the rate order.

(5) Change in method of regulated accounting. The taxpayer shall notify the district director of a change in its method of regulated accounting, an order by a regulatory body or court that such method be changed, or an interim or final rate determination by a regulatory body which determination is inconsistent with the method of regulated accounting used by the taxpayer immediately prior to the effective date of such rate determination. Such notification shall be made within 90 days of the date that the change in method, the order, or the determination is effective. In the case of a change in the method of regulated accounting, the taxpayer shall recompute its tax liability for any affected taxable year and such recomputation shall be made in the form of an amended return where necessary unless the taxpayer and the district director have consented in writing to extend the time for assessment of tax with respect to the issue of normalization method of regulated accounting.

(6) Exclusion of normalization reserve from rate base. (i) Notwithstanding the provisions of subparagraph (1) of this paragraph, a taxpayer does not use a normalization method of regulated accounting if, for ratemaking purposes, the amount of the reserve for deferred taxes under section 167(l) which is excluded from the base to which the taxpayer's rate of return is applied, or which is treated as no-cost capital in those rate cases in which the rate of return is based upon the cost of capital, exceeds the amount of such reserve for deferred taxes for the period used in determining the taxpayer's tax expense in computing cost of service in such ratemaking.

(ii) For the purpose of determining the maximum amount of the reserve to be excluded from the rate base (or to be included as no-cost capital) under subdivision (i) of this subparagraph, if solely an historical period is used to determine depreciation for Federal income tax expense for ratemaking purposes, then the amount of the reserve account for the period is the amount of the reserve (determined under subparagraph (2) of this paragraph) at the end of the historical period. If solely a future period is used for such determination, the amount of the reserve account for the period is the amount of the reserve at the beginning of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during such period. If such determination is made by reference both to an historical portion and to a future portion of a period, the amount of the reserve account for the period is the amount of the reserve at the end of the historical portion of the period and a pro rata portion of the amount of any projected increase to be credited or decrease to be charged to the account during the future portion of the period. The pro rata portion of any increase to be

credited or decrease to be charged during a future period (or the future portion of a part-historical and part-future period) shall be determined by multiplying any such increase or decrease by a fraction, the numerator of which is the number of days remaining in the period at the time such increase or decrease is to be accrued, and the denominator of which is the total number of days in the period (or future portion).

(iii) The provisions of subdivision (i) of this subparagraph shall not apply in the case of a final determination of a rate case entered on or before May 31, 1973. For this purpose, a determination is final if all rights to request a review, a rehearing, or a redetermination by the regulatory body which makes such determination have been exhausted or have lapsed. The provisions of subdivision (ii) of this subparagraph shall not apply in the case of a rate case filed prior to June 7, 1974 for which a rate order is entered by a regulatory body having jurisdiction to establish the rates of the taxpayer prior to September 5, 1974, whether or not such order is final, appealable, or subject to further review or reconsideration.

(iv) The provisions of this subparagraph may be illustrated by the following examples:

Example 1. Corporation X is exclusively engaged in the transportation of gas by pipeline subject to the jurisdiction of the Z Power Commission. With respect to its post-1969 public utility property, X is entitled under section 167(l)(2)(B) to use a method of depreciation other than a subsection (l) method if it uses a normalization method of regulated accounting. With respect to X the Z Power Commission for purposes of establishing cost of service uses a recent consecutive 12-month period ending not more than 4 months prior to the date of filing a rate case adjusted for certain known changes occurring within a 9-month period subsequent to the base period. X's rate case is filed on January 1, 1975. The year 1974 is the recorded test period for X's rate case and is the period used in determining X's tax expense in computing cost of service. The rates are contemplated to be in effect for the years 1975, 1976, and 1977. The adjustments for known changes relate only to wages and salaries. X's rate base at the end of 1974 is \$145,000,000. The amount of the reserve for deferred taxes under section 167(l) at the end of 1974 is \$1,300,000, and the reserve is projected to be \$4,400,000 at the end of 1975, \$6,500,000 at the end of 1976, and \$9,800,000 at the end of 1977. X does not use a normalization method of regulated accounting if the Z Power Commission excludes more than \$1,300,000 from the rate base to which X's rate of return is applied. Similarly, X does not use a normalization method of regulated accounting if, instead of the above, the Z Power Commission, in determining X's rate of return which is applied to the rate base, assigns to no-cost capital an amount that represents the reserve account for deferred tax that is greater than \$1,300,000.

Example 2. Assume the same facts as in example (1) except that the adjustments for known changes in cost of service made by the Z Power Commission include an additional depreciation expense that reflects the installation of new equipment put into service on January 1, 1975. Assume further that the reserve for deferred taxes under section 167(l)¹ at the end of 1974 is \$1,300,000 and that the monthly net increases for the first 9 months of 1975 are projected to be:

January 1–31.....	\$310,000
February 1–28.....	300,000
March 1–31.....	300,000
April 1–30.....	280,000
May 1–31.....	270,000
June 1–30.....	260,000
July 1–31.....	260,000
August 1–31.....	250,000

September 1–30.....	240,000
	<hr/> \$2,470,000

For its regulated books of account X accrues such increases as of the last day of the month but as a matter of convenience credits increases or charges decreases to the reserve account on the 15th day of the month following the whole month for which such increase or decrease is accrued. The maximum amount that may be excluded from the rate base is \$2,470,879 (the amount in the reserve at the end of the historical portion of the period (\$1,300,000) and a pro rata portion of the amount of any projected increase for the future portion of the period to be credited to the reserve (\$1,170,879)). Such pro rata portion is computed (without regard to the date such increase will actually be posted to the account) as follows:

\$310,000 x 243/273 =.....	\$275,934
300,000 x 215/273 =.....	236,264
300,000 x 184/273 =.....	202,198
280,000 x 154/273 =.....	157,949
270,000 x 123/273 =.....	121,648
260,000 x 93/273 =.....	88,571
260,000 x 62/273 =.....	59,048
250,000 x 31/273 =.....	28,388
240,000 x 1/273 =.....	879
	<hr/> \$1,170,879

Example 3. Assume the same facts as in example (1) except that for purposes of establishing cost of service the Z Power Commission uses a future test year (1975). The rates are contemplated to be in effect for 1975, 1976, and 1977. Assume further that plant additions, depreciation expense, and taxes are projected to the end of 1975 and that the reserve for deferred taxes under section 167(l) is \$1,300,000 for 1974 and is projected to be \$4,400,000 at the end of 1975. Assume also that the Z Power Commission applies the rate of return to X's 1974 rate base of \$145,000,000. X and the Z Power Commission through negotiation arrive at the level of approved rates. X uses a normalization method of regulated accounting only if the settlement agreement, the rate order, or record of the proceedings of the Z Power Commission indicates that the Z Power Commission did not exclude an amount representing the reserve for deferred taxes from X's rate base (\$145,000,000) greater than \$1,300,000 plus a pro rata portion of the projected increases and decreases that are to be credited or charged to the reserve account for 1975. Assume that for 1975 quarterly net increases are projected to be:

1st quarter.....	\$910,000
2nd quarter.....	810,000
3rd quarter.....	750,000
4th quarter.....	630,000
Total.....	<hr/> \$3,100,000

For its regulated books of account X will accrue such increases as of the last day of the quarter but as a matter of convenience will credit increases or charge decreases to the reserve account on the 15th day of the month following the last month of the quarter for which such increase or decrease will be accrued. The maximum amount that may be excluded from the rate base is \$2,591,480 (the amount of the reserve at the beginning of the period (\$1,300,000) plus a pro rata portion (\$1,291,480) of the \$3,100,000 projected increase to be credited to the reserve during the period). Such portion is computed (without regard to the date such increase will actually be posted to the account) as follows:

\$910,000 x 276/365 =.....	\$688,110
810,000 x 185/365 =.....	410,548
750,000 x 93/365 =.....	191,096
630,000 x 1/365 =.....	1,726
	<hr/> \$1,291,480

(i) Flow-through method of regulated accounting. Under section 167(l)(3)(H), a taxpayer uses a flow-through method of regulated accounting with respect to public utility property if it uses the same method of depreciation (other than a subsection (l) method) to compute its allowance for depreciation under section 167 and to compute its tax expense for purposes of reflecting operating results in its regulated books of account unless such method is the same method used by the taxpayer to determine its depreciation expense for purposes of reflecting operating results in its regulated books of account. Except as provided in the preceding sentence, the method of depreciation used by a taxpayer with respect to public utility property for purposes of determining cost of service for ratemaking purposes or rate base for ratemaking purposes shall not be considered in determining whether the taxpayer used a flow-through method of regulated accounting. A taxpayer may establish use of a flow-through method of regulated accounting in the same manner that compliance with normalization requirements in respect of operating books of account may be established under paragraph (h)(4) of this section.

Credits

[T.D. 7315, 39 FR 20195, June 7, 1974]

SOURCE: T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 31, 1960, unless otherwise noted.

AUTHORITY: Section 1.1411-10 also issued under 26 U.S.C. 367.

HISTORICAL NOTES

Effective and Applicability Notes

Reg. § 1.167(l)-1 has not been updated to reflect subsequent legislation.

Notes of Decisions (1)

Current through September 3, 2024, 89 FR 71188. Some sections may be more current. See credits for details.

Footnotes

- 1 So in original; probably should read “167(l)”.

End of Document

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**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 11:

Deferred Income Tax. Refer to file <TAWC 2024 Rate Case- Deferred Tax.xlsx>, tab: Book-TAX Diff. and file <TAW_R_CADDR2_011_073024_Attachment.xlsx>, tab: Reconciliation.

Please provide a comparison of the Book-TAX differences for fiscal years 2022 and 2023, as well as a deferred tax reconciliation for the same years. Use the same format as in the forecasted 2024 and 2025 deferred tax reconciliation. For your reference, the 2024 format is included below.

Federal				
<u>2024 Activity</u>				
	Tax	Book	Net	
Depreciation	(10,784,901)	12,742,377	1,957,476	
Gain/Loss	(3,488,104)	-	(3,488,104)	
Repairs	(10,042,577)	-	(10,042,577)	
Taxable CIAC	147,452	-	147,452	
Total Book/Tax Difference	(24,168,130)	12,742,377	(11,425,753)	(Deduction)

	2024	
	Federal	Tennessee
Net Book to Tax Difference	11,425,753	12,808,594
Tax Rate	21.00%	6.50%
FAS 109 Deferred Tax	2,399,408	832,559
Excess ADIT & Other FT	(237,105)	5,063
Exclude AFUDC FT	8,309	2,572
TN - Federal Benefit of State	(158,496)	
Total Tax	2,012,115	840,193
Deferreds Effective Rate	17.61%	6.56%

Response:

Please see TAW_R_TPUCDR1_011_090524_Attachment (provided in excel only).

**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 12:

Deferred Income Tax. Provide the balance of protected Excess ADIT as of December 2023. Also, confirm whether the unprotected Excess ADIT is zero (fully amortized) as of the December 2023.

Response:

In the file 'TAWC 2024 Rate Case - Deferred Tax', please see the tab labeled '2024 Rpt 261'. This report from the PowerTax system provides the EADIT balance at 12/31/2023 (column labeled Beginning Excess Balance). The balance is a net liability of \$11,685,737. The column labeled Ending Excess Balance is the liability balance at 12/31/2024.

As determined in TPUC Docket No. 18-00039, the protected EADIT includes the lines in the report labeled as the following:

1026 Fed - M/L	11,401,966
1026 Fed – COR	571,492
1026 Fed - Taxable CIAC	(287,720)

In addition, there is a protected piece related to the Federal NOL (net operating loss) that is not included in the PowerTax report. The balance for this line as of 12/31/2023 is an asset of \$692,610.

The remaining EADIT items are considered unprotected. The unprotected amounts were returned to the customers over a three-year period. The balance is zero as of 12/31/2023.

**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 13:

UPIS Plant Retirements. Refer to file <MFG Q051_Attachment.xlsx>, Tab “MFG 51-Attachment”, included with the Company’s filing. Specifically refer to retirements for year 2021, columns (E) and (K), row #'s 80-122 “Retirements of Normal Projects.” Please explain why there are number values with positive balances in the retirements data.

Response:

The retirements process was automated beginning in 2019. It was later discovered that recent vintages with higher average costs were being retired instead of older assets. The negative amounts in 2021 specifically relate to reversals and corrections of the retirements.

**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 14:

UPIS Plant Retirements. Below is a table showing staff's calculation of the average annual UPIS retirements for 2020 through 2023 based on data provided by the Company in its Response to Consumer Advocate DR 1-147. The table also shows forecasted annual retirements for 2024 and 2025 presented in <Exhibit RB-2.4-UPIS-DD>. The average annual retirements for 2020 through 2023 is \$3,001,580. In light of this higher average, please explain the rationale for the Company's forecast of annual retirements for 2024 of \$1,526,031 and annual retirements for 2025 of 1,523,489.

Year	Annual Retirements	Source
2020	(\$1,739,103)	CA DR1-147
2021	(\$712,976)	CA DR1-147
2022	(\$3,441,357)	CA DR1-147
2023	(\$6,112,882)	CA DR1-147
Average Annual Retirements 2020-2023 (\$3,001,580)		
2024	(\$1,526,031)	Exh.RB-2.4-UPIS-DD
2025	(\$1,523,489)	Exh.RB-2.4-UPIS-DD

Response:

Approximately \$7M of computer software assets were fully retired during the historical period used to project future retirements. As they were fully retired and not replaced, that activity was excluded from the amounts used to project future retirements.

**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: John Watkins

Question 15:

Capital Leases. Per Company Exhibit EXP-8-Support Services-JW, adjustments have been made for capital lease-related depreciation and interest. What are the primary capital leases for which expenses are embedded into the Company's forecasted Support Services charges in its attrition year?

Response:

The adjustments related to depreciation and interest as referenced in the Company's Exhibit EXP-8-Support Services-JW are broken out as follows:

Description	Amount
Adjustment for Depreciation through 2024	\$98,038
Adjustments for LOP Capital interest through 2024	24,220
Adjustment for Depreciation through 2025	(95,716)
Adjustments for LOP Capital interest through 2025	(6,830)
Total	\$19,712

Laurel Oak Properties (LOP) procures equipment and other personal property for American Water Works Service Company ("AWWSC") and leases those assets at cost to AWWSC through capital leases. The primary capital leases for which expenses are embedded into the Company's adjustments to Support Services in its attrition year are related to the following assets:

- Networking Equipment (Computer Hardware & Software)
- Software Licenses – SCADA
- Desks (Cubicles, Benches, Interior & Perimeter Offices)
- Technology peripherals for work areas
- Divisible and non-divisible workspaces

**TENNESSEE AMERICAN WATER COMPANY
TENNESSEE PUBLIC UTILITY COMMISSION
DOCKET NO. 24-00032
FIRST DISCOVERY REQUEST OF THE TPUC STAFF**

Responsible Witness: Dominic DeGrazia

Question 16:

O&M Expense. On Company Exhibit EXP-2-Purchased Power-DD, the Company includes a \$1,893,020 adjustment (increase) to its test period cost for “Removal of PCOP expense transfer.” Provide a thorough explanation for this proposed adjustment, including the justification for why it is included in the calculation of the attrition year forecast.

Response:

In Docket 13-00130, the Tennessee Regulatory Authority approved a “Production Costs and Other Pass-Throughs (PCOP) Rider”. The purpose of the rider is to apply a surcharge to all customers to either recover or refund the difference in these expense levels from the amounts authorized. The PCOP rider is calculated as the difference between the actual expenses in the previous 12-month period, and the amount of expense authorized in the most recent rate proceeding. This difference is then applied as a percentage of customer charges to the subsequent 12-month period. Should the expense exceed the authorized level, the expense will be recovered in the subsequent 12-months as a surcharge. If the expense should be less than that authorized level, the difference will be refunded in the subsequent 12-month period. The PCOP Rider will be reset to zero during the next general accounting period and for the attrition year following the next general rate proceeding.

Each month the Company records a journal entry to move the applicable portion of the power expenses related to the PCOP from power account 51510000 to a regulatory liability account 25689900. To get the true level of power expense for the attrition year, these entries had to be included back into purchased power expense. Not including them would have understated the amount of purchased power expense in the attrition year.

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was served via U.S. Mail or electronic mail upon:

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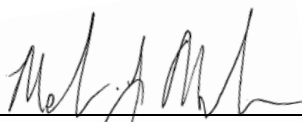
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This the 5th day of September 2024.



Melvin J. Malone