

STATE TAX COMMISSION OF MISSOURI

LACLEDE GAS COMPANY,)
)
 Complainant,)
)
)
 v.)
)
 TRACY BALDWIN, ASSESSOR)
 CLAY COUNTY, MISSOURI)
)
 Respondent.)

**DECISION AND ORDER
UPON APPLICATIONS FOR REVIEW FILED BY BOTH PARTIES
SETTING ASIDE DECISION OF HEARING OFFICER**

Introduction

On August 9, 2024, a Decision and Order of a Hearing Officer for the State Tax Commission (hereafter also “STC” or “Commission”) was published. Both parties filed Applications for Review. The Commission sets aside the Decision and Order of the Hearing Officer.

Jurisdiction

The STC has jurisdiction over this appeal and may correct any assessment which is shown to be unlawful, unfair, arbitrary, or capricious. Article X, Section 14, MO. Const. of 1945; Sections 138.430, 138.431, 138.431.4.

Historical Cost Less Depreciation Method

In 2012, and possibly earlier, the STC received requests from county assessors seeking guidance with respect to assessing properties owned by natural gas distribution companies. In particular, assessors sought a simplified and uniform way to assess these

properties. Consistent with the STC's duties to ensure compliance with Missouri law and in order to create more uniform, consistent and predictable assessments, the STC promulgated forms for natural gas distribution companies to use to report real property and tangible personal property in service as of January 1, 2013. (Written Direct Testimony of Randy Holman, former STC Commissioner, February 25, 2022.) At the same time, the STC provided guidance to assessors in its Assessor Manual that the forms "were prepared as a guide to assist the assessor in the gathering of data" and that "these forms are not a requirement, but merely represent a guide for the types of information to be gathered to assess natural gas distribution companies."

These forms differed from forms in use prior to that time, in that they recommended a specific depreciation schedule applicable to both personal and real property. With respect to business personal property, Section 137.122 sets forth a depreciation schedule to be used by assessors which is based, in part, on the depreciation guidelines in IRS Publication 946 which applies the Modified Accelerated Cost Recovery System ("MACRS"). Section 137.122 adopts the MACRS recovery periods applicable to specific types of personal property, but includes a percentage floor depending upon the MACRS class life of the property at issue. (Written Direct Testimony of Randy Holman).

With respect to real property, the STC determined (in 2013) that it would be logical and appropriate to apply the same depreciation schedule to gas transmission properties (i.e., gas main and service lines) that are statutorily defined as real property. Accordingly, the STC promulgated forms applicable to both personal and real property, requiring owners to report the historical/original cost of the properties (not trended to the

date of the appraisal) and recommending a uniform depreciation schedule to be applied by reducing the original cost of the properties listed each year based on the year placed in service according to the 20-year depreciation schedule set forth in Section 137.122, even though, by its terms, Section 137.122 applies only to personal property. (Written Direct Testimony of Randy Holman).

In *Union Electric Company v. Estes*, 534 S.W.3d 352 (Mo. App. W.D. 2017), valuation methodology pertaining to Union Electric/Ameren’s natural gas pipelines was extensively analyzed. In that assessment year (2013), Cole County and 15 other counties did not accept Union Electric/Ameren’s valuations. Union Electric/Ameren’s appeals from the 16 counties to the STC were consolidated for hearing and decision purposes. Although the methodologies used by the 16 county assessors did not account for depreciation, the STC nevertheless affirmed the decisions of the assessors and the county Boards of Equalization, and the Circuit Court of Cole County affirmed the STC’s Decision and Order. *Estes*, 534 S.W.3d at 363-64.

The Western District reversed and remanded. In doing so, it noted the requirements of Section 138.320, which “provides that ‘suitable forms and instructions’ prepared by the Commission and provided to county clerks and officers ‘shall be strictly complied with by the officers in the performance of their respective duties.’” *Estes*, 534 S.W.3d at 357. The parties did not contest that “the 2013 form and the related portions of the Assessor’s Manual required use of a ‘cost approach’ valuation methodology based on original or historical costs.” *Id.* at 358-59. According to the Court, the assessors’ expert witness “used a *different* valuation methodology from that required by the Commission’s

2013 form and Assessor's Manual." *Id.* at 362. (Emphasis in original.) More specifically, "Ameren thus did not challenge the Assessor's use of a cost approach valuation methodology based on original/historical costs, but instead challenged only that the Assessor applied this approach unlawfully by failing to consider depreciation." *Id.* at 366.

The Court in *Estes* succinctly summarized its view as follows:

The form and Assessor's Manual promulgated by the Commission for use by all assessors in 2013 to assess the true value in money of real property and tangible personal property owned by natural gas distribution companies in service as of January 1, 2013 **required** use of the reproduction cost approach, as it was based on original, historical costs, **reduced by depreciation**. It was within the Commission's sound discretion to **require** use of the reproduction cost approach to determine the true value in money of natural gas pipeline real property and tangible personal property. "The commission has some discretion in deciding which approach best estimates the value of a particular property." *Estes*, 534 S.W.3d at 367, quoting *Snider v. Casino Aztar/Aztar Missouri Gaming Corp.*, 156 S.W.3d 341, 346 (Mo. banc 2005). (Emphasis supplied.)

In the same manner and on the same grounds that Union Electric/Ameren appealed Clay County's 2013 assessment, it appealed the other counties' assessments, and those appeals were taken up in the Eastern and Southern District Courts of Appeals. The results were the same as in *Estes*.¹ In short, appellate courts in all three Missouri appellate districts have uniformly enforced the historical cost less depreciation method for assessing gas transmission pipelines.²

¹ The Eastern and Southern Districts expressed their agreement with the *Estes* decision as to both result and analysis. See *Union Electric Company v. Adams*, 539 S.W. 3d 799 (Mo. App. E.D. 2017); *Union Electric Company v. Elfrink*, 544 S.W.3d 246 (Mo. App. S.D. 2017).

² Although depreciation must be considered when valuing property using the reproduction cost approach, *Estes*, 534 S.W.3d at 376, citing *Stephen & Stephen Props., Inc. v. State Tax Comm'n*, 499 S.W.2d 798, 803 (Mo. 1973), **the courts have never ruled that only a 20-year depreciation period and no other period is acceptable with respect to pipelines assessed as real property**. Rather, it was "the

When discussing the historical cost less depreciation method, Missouri courts have alternatively used the phrase “reproduction cost approach”.³ The phrase “reproduction cost approach” as used by Missouri courts describes a method that is well-understood: the historical cost less depreciation method. It is both common and appropriate to use the historical cost less depreciation method to value the assets of rate-based regulated utilities. This is because the method reflects market realities. Market participants buy and sell rate-based regulated property with historical cost less regulatory depreciation typically representing the maximum price. Buyers tend not to pay more than this amount because utility rates allowed by the Public Service Commission (PSC) are set based upon historical cost less regulatory depreciation data. If a buyer paid more than historical cost less depreciation for the asset, the buyer would not be able to build the price premium into its rate base and, therefore, would not earn a return on that portion of its investment. (Testimony of Robert Reilly, Hearing Transcript, June 15, 2022, at pp. 179-182).

Historical (original) costs as a ratemaking standard was approved as early as 1944 in *FPC v. Hope Natural Gas*, 320 U.S. 591 (1944).

Procedural History of These Appeals

These appeals relate to assessments of Complainant’s business personal property in Clay County as of January 1, 2014 and its business personal and real property in Clay County as of January 1, 2015. The STC determined the true value in money (“TVM”) of

Assessor’s failure to apply *any* depreciation [that] was legally erroneous.” *Estes*, 534 S.W.3d 352, 378. (Emphasis in original.)

³ E.g., *Rinehart v. Laclede Gas Company*, 607 S.W.3d 220, 228 (Mo. App. W.D. 2020) (“We held that ‘[d]epreciation must be considered when valuing property using the reproduction cost approach.’ Id. (citing *Stephen & Stephen Props., Inc. v State Tax Comm’n*, 449 S.W.2d 798, 803 (Mo. 1973)).”

Complainant's personal property was \$7,100,000 in 2014 and \$8,900,000 in 2015. It found the TVM of Complainant's real property was \$52,500,000 in 2015. The Circuit Court of Clay County affirmed the STC's findings.

The Western District reversed and remanded in *Rinehart v. Laclede Gas Company*, 607 S.W.3d 220 (Mo. App. W.D. 2020), on the grounds that neither the Complainant nor the Respondent, nor the STC itself, complied with "the reproduction cost approach **as mandated by Commission publications** for the 2014 and 2015 tax years." *Id.* at 230. (Emphasis supplied.)

At the first hearing in these appeals, the Complainant's valuation did not comply with STC publications because Complainant's appraiser "combined income, market, and cost approaches . . ." *Id.* As in *Union Electric Company v. Adams*, "the assessor combined, 'income, market, and cost "new" approaches – every possibility *except* the original (historical) cost approach mandated by the Commission for the year in question' to calculate the value of a natural gas distribution company." *Id.* at 230, quoting *Union Electric Company v. Adams*, 539 S.W.3d 779, 783 (Mo. App. E.D. 2017). (Emphasis in original.) On the other hand, Respondent's valuation did not comply with STC publications because Respondent "accounted for some, but not all, depreciation." *Id.* at 228. "The Assessor admitted that she did not properly apply the depreciation schedule, even though she had the necessary information to properly make those calculations, and this resulted in a higher assessed value." *Id.* at 229. The Court determined that "we must reverse and remand for a determination of TVM by properly applying the reproduction

cost approach as mandated by Commission publications for the 2014 and 2015 tax years.” *Id.* at 230.⁴

Respondent’s Evidence Upon Remand

At the hearing following remand which was held on June 15-16, 2022, each party submitted updated evidence regarding valuation. The evidence and exhibits presented and admitted into the record are listed and described in the Hearing Officer’s Decision and Order issued on August 9, 2024 and such listings and descriptions are incorporated by reference herein.

Respondent submitted testimony from John Ryan, a Certified Assessment Evaluator and a state licensed general real estate appraiser in the State of Missouri. Ryan summarized his view of the Court’s instructions upon remand as follows:

The Court decision said that the value must be determined following the Reproduction Cost Approach methodology, as prescribed by the State Tax Commission through their adoption of the 2013 version of their model reporting form. The methodology requires that the value determination starts with the Original Historical Costs and then those values are reduced by the appropriate depreciation factors. In this matter the STC’s instructions state to use the Historic Cost for valuing the real property and personal property. The form identifies certain asset types, which are based on Federal Energy Regulatory Commission’s accounting codes and the reported original cost of the property is based on the year it was placed in service, or Vintage Year, and that the determination of depreciation is left to the Assessor. For personal property placed in service after 1/2/2006, Missouri law requires that the depreciation be that as determined by the Internal Revenue Service.” (Written Direct Testimony of John F. Ryan, Ex. 20.)

⁴ See also *Union Electric Company v. Estes*, 534 S.W.352, 362 (Mo. App. W.D. 2017) (“Mr. Sansoucy used a different valuation methodology from that **required by** the Commission’s 2013 form and Assessor’s Manual.”)(Emphasis supplied.)

Ryan determined TVM for the tangible personal property to be \$24,803.525 as of January 1, 2014, \$24,825,566 as of January 1, 2015, and the TVM for the real property to be \$213,234,215 as of January 1, 2015.

Although Ryan understood and accurately described the historical cost less depreciation methodology directed by STC forms and by the courts, Ryan did not follow the methodology. According to Ryan, “[i]f the goal is to obtain the True Value in Money, starting with the Original Cost of the property, then yes, the original, historical cost must be trended, or adjusted to current levels.” (Respondent’s Rebuttal Written Direct Testimony.) In his view, it would be error for an appraiser to fail to “trend” the original costs in applying a reproduction cost approach, unless the appraiser finds a specific, written jurisdictional exception. (Respondent’s Rebuttal Written Direct Testimony.) Apparently, Ryan did not believe that the STC’s forms and guidance to appraisers, nor prior court decisions mandating compliance with the reproduction cost approach, were sufficient to justify recognition of a jurisdictional exception. Ryan also doubted the accuracy of the costs that Complainant reported. Regardless, the STC cannot accept an appraisal such as Ryan’s that does not comply with mandated methodology.

Ryan testified that Lisa Hobart provided expert review for aspects of the personal property valuation methodology used in his report. Lisa Hobart has the ASA designation from the American Society of Appraisers and the Certified Assessment Evaluator and Personal Property Specialist credentials from the International Association of Assessing Officers. She is a certified general appraiser in the state of Michigan. However, she did not, herself, form an opinion of value as to the tangible personal property in this appeal.

(Written Direct Testimony of Lisa A. Hobart.) Neither did she attempt to correct the methodology used by Ryan.

Because Respondent failed to assess Complainant's assets upon remand using the methodology directed by the STC's forms and by the courts, the Hearing Officer correctly rejected Respondent's methodology and Respondent's valuations.⁵ Moreover, the rebuttable presumption in favor of the Clay County Board of Equalization's valuation has been overcome by Complainant's evidence, more fully discussed below.

Complainant's Evidence Upon Remand

Upon remand to the STC, Complainant's appraiser, Robert Reilly, reviewed the Laclede Gas application of the STC depreciation forms with respect to the subject property. According to these forms, the historical cost less depreciation of Complainant's personal property as of January 1, 2014 was \$6,323,332.92. As of January 1, 2015, it was \$6,468,289.36. The historical cost less depreciation of Complainant's real property as of January 1, 2015 was \$41,536,392.70.

Mr. Reilly also developed a summation principle property appraisal to estimate the TVM of the subject property. (Complainant's Exhibit V at p. 6.) Reilly began with historical cost data – the same data that had been audited by a major national accounting firm, that had been reported to and accepted by the Federal Energy Regulatory Commission (FERC), and that had been reported to and accepted by the PSC.

⁵ Complainant correctly points out that Respondent may not advocate a valuation higher than that value finally determined by the assessor or the value determined by the board of equalization, whichever is higher, for that assessment period. Section 138.060.1 RSMo. Respondent asserts that he is not seeking a higher valuation than the BOE, but rather, to provide evidence that the TVM is *at least that amount* which was determined by the BOE.

(Testimony of Robert Reilly, Hearing Transcript, June 15, 2022, at p. 105-106).

Consistent with the reproduction cost approach used in Missouri, Reilly did not trend the cost data. Further, he relied on the accumulated depreciation reserve in the company's continuing property record based upon the PSC's allowed lives and rates. (Testimony of Robert Reilly, Hearing Transcript, June 15, 2022, at p. 111). For example, with respect to certain steel pipes in the ground that correspond with Account 376-01 (one of the FERC accounts listed in Complainant's filing with the PSC), the PSC-approved depreciation factor is 1.44 percent, implying a life of 80 years. (Hearing Transcript, June 15, 2022, at pp. 125-127). According to Mr. Reilly, every time there is a rate case, which typically happens every five years or so, the PSC has the option of changing the life and depreciation rate for each FERC account. When the PSC does change depreciation rates, the utility is required to change accumulated depreciation prospectively, but not retroactively. (Hearing Transcript, June 15, 2022, at pp. 128-129).

Using the summation principle property appraisal based on the historical cost less depreciation approach, Reilly determined TVM for the tangible personal property to be \$6,600,000 as of January 1, 2014 and \$7,800,000 as of January 1, 2015, and the TVM for the real property to be \$39,200,000 as of January 1, 2015 (all figures rounded).

(Complainant's Exhibit V at pp. 6-7.)

The Hearing Officer found that evidence of valuation derived from Mr. Reilly's development of the summation principle property appraisal was substantial and persuasive and concluded that the TVM of the subject personal property was \$6,600,000 as of January 1, 2014 and \$7,800,000 as of January 1, 2015. She concluded that the

TVM of the subject real property as of January 1, 2015 was \$39,200,000. In reaching these conclusions, the Hearing Officer found that this method complied with the mandate of the *Rinehart* court to use the historical cost less depreciation methodology.

Complainant Laclede Gas Company's Application for Review

Despite having prevailed upon remand, Complainant filed an Application for Review of the Hearing Officer's Decision and Order. According to Complainant, the "Application for Review concerns the limited issue of applying MACRS depreciation as directed and recommended by the Natural Gas Form." (Complainant Laclede Gas Company's Application for Review, para. 23.) In essence, Complainant argues that application of MACRS depreciation as recommended by the STC's forms should be mandatory.

Complainant advances five arguments in support of its request. These arguments are summarized as follows:

1. It is within the STC's authority to promulgate its natural gas forms and to mandate the use of the historical cost less depreciation approach, including MACRS depreciation.
2. Application of the STC's natural gas forms, including MACRS depreciation, is an effective and fair way for both county assessors and natural gas distribution companies to consistently value and assess property using their own employees.
3. The STC's natural gas forms, including MACRS depreciation, help to assure that the same type of property is uniformly valued and assessed on a county-by-county basis.

4. Use of the natural gas forms provides a reasonable indication of TVM of real and business personal property owned by natural gas distribution companies, on average.

5. A decision by the STC addressing the (mandatory) use of MACRS depreciation in connection with the historical cost less depreciation approach would provide much needed clarity to taxpayers and county assessors and would help to greatly reduce pending and future litigation this area.

Respondent Tracy Baldwin's Application for Review

In response to Complainant, and in support of his own Application for Review, Respondent advances numerous arguments. These arguments include:

1. Missouri law places the duty to value property on the assessor, not on the taxpayer.
2. The forms require every assessor to accept the taxpayer's figures without the ability to question them.
3. Complainant suddenly and dramatically reduced the cost basis of assets that it acquired from another company (MGE).
4. The STC's forms don't have a space for important information such as the total miles of pipe and the total number of meters within a county.
5. The data on the forms can be manipulated, the same as under accounting rules.
6. The forms don't require Complainant to report its total miles of pipe and its total number of gas meters.
7. It was never the intent of the STC to require assessors to strictly follow the Assessor's Manual or forms.

8. Prior court decisions notwithstanding, the STC's Assessor's Manual and forms do not carry the force of law and are not mandatory for use because they were not promulgated pursuant to the STC's rulemaking authority.

9. Even if used, the forms provide only a starting point, not a final conclusion, regarding depreciation and valuation.

10. To apply MACRS to gas pipeline real property but not to other categories of real property is fundamentally unfair and violates the uniformity which Complainant suggests it furthers.

11. Application of a historical costs less depreciation method that does not consider the time value of money defies "common sense".

12. Complainant has not reported all of its taxable assets within Clay County.

13. Complainant has "double-dipped" by taking deductions for both "regulatory" depreciation and economic obsolescence and has relied on the PSC's accounting rules to assign a negative salvage value to real property which is still in use, before it has actually been retired.

14. MACRS is neither required, nor appropriate, to depreciate real property. To recover its costs through ratemaking, Complainant depreciates plastic mains over seventy years and plastic service lines over forty-four years. MGE depreciates mains over fifty years. Complainant's own self-commissioned depreciation study (Ex. 23) lists lives of up to 100 years for steel pipes.⁶ Complainant uses a class life of 70 years in its

⁶ Complainant's depreciation study used Iowa-Type Survivor Curves. (Ex. 21, pp. 15-16, 27-33).

claimed depreciation before the PSC. *Laclede Gas v. Office Pub. Counsel*, 539 S.W.3d 835, 839 n.3 (Mo. App. W.D. 2017). Respondent proposes a 50-year class life for real property as a “modest balance” between the 40-year life of plastic pipes and the 100-year life of steel. (Respondent’s Ex. 1, p. 28.)

15. The Decision and Order under review rejected without explanation Complainant’s second appraisal which applied MACRS. Thus, although Respondent does not think that MACRS depreciation should apply, the Decision and Order creates confusion as to the appropriate method of depreciation. Instead of applying MACRS depreciation (consistent with the STC’s own forms), the Decision and Order approved an approach which applies both regulatory depreciation and then also applies additional depreciation in the form of economic obsolescence.

Analysis

Though the parties fundamentally disagree on just about every other point, the one point that the parties agree on is that valuation of Complainant’s property via application of the historical cost and depreciation data as reported in the STC-recommended natural gas distribution forms is preferable to adoption of Mr. Reilly’s values determined through his summation principle appraisal. The Commission agrees.

Having promulgated recommended forms for use by assessors and gas distribution companies since 2013, and the courts having uniformly approved use of the forms, it would be anomalous at best for the STC to reject valuations determined by use of the STC’s own forms. Although Reilly’s use of summation principle is consistent with cost approach valuation, and although consideration of economic obsolescence is consistent

with Missouri law (see 137.122.4 RSMo), Respondent correctly points out that application of economic obsolescence resulting from loss of income injects elements of income approach valuation.

Missouri courts have not recognized or approved an income shortfall methodology in conjunction with the historical cost less depreciation approach. Once the door is opened to consideration of loss of income as economic obsolescence, then all of the factors surrounding loss of income must be considered, including the possibility that loss of income results in whole or in part from inefficient management, imprudent ratio of equity to borrowed capital, and other management policies. This kind of analysis is fairly fact-intensive and sophisticated. In contrast, a simple approach to regulatory depreciation minimizes administrative burden and provides greater predictability for energy sector stakeholders. Simplicity of use, minimization of administrative burden and predictability for stakeholders are the very reasons why the STC promulgates its recommended forms and guidance.

In addition, the Commission finds that Reilly's use of an expected 7% rate of return (for purposes of economic loss calculation) is not supported by substantial evidence. Reilly was unable to provide any capitalization or investment rate studies or to specifically explain how he determined that an investor would expect a 7% return.

As explained above, Respondent urges numerous objections to use of the STC's natural gas distribution company forms. Some of Respondent's objections fall under the broad rubric of oversimplification. (E.g., the forms don't contain sufficient information concerning miles of pipe or number of meters within a county, compared to total miles of

pipe and number of meters; the forms don't require companies to report underlying data with respect to cost and depreciation; the forms allow a taxpayer to take deductions allowed by PSC's accounting rules and assign a negative salvage value to real property which is still in use.) Some of Respondent's objections challenge the fact that the courts have construed application of the cost approach set forth in the STC's forms to be mandatory, at least so long as such forms are published. (E.g., Missouri law places the duty to value property on the assessor; the forms don't reflect the True Value in Money of the property; the forms don't consider the time value of money; it was never the intent of the STC to require assessors to strictly follow the manual or forms; the forms were not promulgated pursuant to the STC's rulemaking authority; the forms provide only a starting point, not a final conclusion, regarding depreciation and valuation.) However, given the courts' approval of the STC's forms and guidance, none of these objections are meritorious.

Respondent does, however, advance one argument with which the STC agrees: MACRS is neither required, nor appropriate, to depreciate real property. The STC agrees with Respondent that a 50-year depreciation period, which is more consistent with depreciation reported for regulated utility ratemaking purposes, would best serve the goals of simplicity, consistency and fairness with respect to assessment of natural gas distribution company property that is assessed as real property. To that end, the STC has promulgated modified forms and has amended its Assessor Manual, effective January 1, 2025, to guide assessors and natural gas distribution companies to record original costs by year placed in service and to determine depreciation on a straight line basis over a 50-

year average life, with a 20% residual, for natural gas local distribution company property assessed as real property. However, the STC has not made these amended forms and guidance retroactive. Thus, they have no application to appeals for tax years prior to 2025.

For the foregoing reasons, the Commission sets aside the Decision and Order of the Hearing Officer dated August 9, 2024. The Commission determines, by substantial and persuasive evidence, that the TVM of the subject properties as of January 1 of the indicated years were as follows:

2014 Tangible Personal Property	\$6,323,332.92
2015 Tangible Personal Property	\$6,468,289.36
2015 Real Property	\$41,536,392.70

SO ORDERED February 19, 2025.

Gary Romine, Chairman

Debbi McGinnis, Commissioner

Gregory Razer, Commissioner

Certificate of Service

I hereby certify that a copy of the foregoing has been electronically mailed and/or sent by U.S. Mail on February 20th, 2025 to:

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