Exhibit No.:	
Issues:	Financial Impact, Depreciation, Call Center and Shared Services, Acquisition Adjustment, Interruptible Rate
Witness:	James M. Jenkins
Sponsoring Party:	Missouri-American Water Company
Exhibit Type:	Rebuttal Testimony
Case No.:	WR-2003-0500
Date Prepared:	November 10, 2003

Missouri Public Service Commission

Case No. WR-2003-0500

FILED
JAN 23 2004
Missouri Public Service Commission

Rebuttal Testimony

of

James M. Jenkins

On Behalf of

Missouri-American Water Company

Jefferson City, MO

Exhibit No. 47
Case No(s). WR-2003-0500
Date 12/16/03 Rptr SLKM

EXHIBIT
MAWC 47

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

IN THE MATTER OF MISSOURI-AMERICAN WATER COMPANY FOR AUTHORITY TO FILE TARIFFS REFLECTING INCREASED RATES FOR WATER SERVICE	)))))	**CASE NO. WR-2003-0500**

AFFIDAVIT OF JAMES M. JENKINS

James M. Jenkins, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying rebuttal testimony entitled "Rebuttal Testimony of James M. Jenkins"; that said rebuttal testimony and schedule(s) were prepared by him and/or under his direction and supervision; that if inquires were made as to the facts in said rebuttal testimony, he would respond as therein set forth; and that the aforesaid rebuttal testimony and schedule(s) are true and correct to the best of his knowledge.

James M. Jenkins

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
before me this 5th day of November 2003.

DEBORAH S. HENDRIX
Notary Public-Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires: Aug. 11, 2007

Deborah S. Hendrix
Notary Public

My commission expires: 8/11/07

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REBUTTAL TESTIMONY OF

JAMES M. JENKINS

WITNESS INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. James M. Jenkins, 535 North New Ballas Road, St. Louis, Missouri.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am Vice President and Treasurer for Missouri American Water.

Q. STATE YOUR QUALIFICATIONS AND EXPERIENCE IN THE FIELD OF ACCOUNTING IN GENERAL AND IN THE FIELD OF UTILITY ACCOUNTING AND RATE REGULATION IN PARTICULAR.

A. My background and qualifications are summarized in Schedule JMJ-1, which is attached hereto and incorporated by reference.

PURPOSE

Q: WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A: The purpose of my testimony is to address certain issues and comments filed in the direct testimonies of Staff of the Missouri Public Service Commission (the Staff), Kimberly Bolin of the Office of the Public Counsel (OPC), Billie LaConte on behalf of the Missouri Energy Group and Michael Gorman on behalf of the Missouri Industrial Energy Consumers. I plan to focus my rebuttal testimony on certain issues individually, but the main purpose of my testimony is to emphasize the accumulated effect of the adjustments in this case on the future of this Company in Missouri. Mr. Thornburg has addressed this same subject of urgent concern about the Staff's recommendations in this case, but I have responsibility for the ultimate calculations resulting from the application of these Commission adjustments. I will address what will happen to the Company's financial statements unless some element of fairness and common sense is used to mitigate the inevitable consequences of these accumulated Staff recommendations.

Q. WHY DO YOU REFER TO THE ACCUMULATED STAFF RECOMMENDATIONS?

A. It is very unwise to look at these adjustments as a simple debate over the application of individual, detached, technical theories. Simply put, the adjustments have consequences that are not theoretical. Those consequences will be very real and inevitable, and if this fact is not brought out now, it will be too late to change the message about Missouri regulation that will be apparent to investors and everyone else when the Company's financial statements are realized.

Q: WHAT ISSUES WILL YOU ADDRESS?

A: I will address the financial impact of Staff's overall rate recommendation, respond to the depreciation positions taken in the direct testimonies of Staff Witnesses Macias and Began, and the National Customer Call Center and National Shared Services Center disallowances recommended by Staff Witness Cassidy. Finally, I will respond to the proposed treatment of acquisition adjustments related to the acquisitions of the water systems of United Water Missouri, Inc. (United Water) and the Cities of Webster Groves, Valley Park and Florissant.

FINANCIAL IMPACT - STAFF'S OVERALL RATE RECOMMENDATION

Q: WHAT ARE THE KEY ELEMENTS OF STAFF'S RECOMMENDATIONS THAT HAVE DIRECT IMPACTS ON MISSOURI AMERICAN'S FINANCIAL VIABILITY?

A: There are three categories of issues that directly impact the financial viability of Missouri American. These Staff issues are cost disallowances resulting in financial write-offs, the $20 million rate reduction proposal and the proposed rate of return (return on equity and the consolidated capital structure).

Q: WOULD YOU PLEASE DESCRIBE THE COST DISALLOWANCES TO WHICH YOU REFER?

A: Yes. In addition to Staff's proposed $20 million annual rate reduction, Missouri American would be required by the Staff recommendations to write-off approximately $10 million. This write-off is related to Staff Witness Cassidy's proposal to deny the transition costs related to the National Call Center ($5 million), to deny recovery of transition costs related to the National Shared Services Center ($4.5 million), and the retroactive recalculation of AFUDC ($0.5 million). If approved, the above disallowances would result in an after-tax write-off of approximately $6.2 million. A write-off of this magnitude represents over 25% of Missouri American's reported 2002 Net Income and would have negative financial consequences on the risk profile of Missouri American.

Q: WHAT IS THE POTENTIAL IMPACT OF ADOPTING STAFF'S PROPOSED RATE REDUCTION?

A: Staff's proposed reduction from existing rates of approximately $20 million annually represents a difference of $40 million between Missouri American's proposed revenue requirement and the revenue requirement proposed by Staff. This swing in allowed revenues will create unacceptable returns and, combined with the $10 million write-off discussed above, will make it difficult for Missouri American to secure capital for needed investment in our operating districts.

Q: HOW DOES THIS RELATE TO STAFF'S RECOMMENDED COST OF EQUITY?

A: Staff's recommended cost of equity after taking into account its proposed consolidated capital structure is 6.96% (mid point), a number that I feel would be too low to attract capital (a more detailed discussion of this matter is found in Company Witness Ahern's testimony). First, 6.96% does not provide an adequate premium for an investor to assume the added risk of an equity investment relative to the return available on A rated corporate bonds, which currently yield approximately 6.0% - 6.5%. Secondly, Staff's recommendation is an approximate 35% reduction from the allowed return on equity of 10.75% approved in our last St. Louis District rate case and a 30% reduction from the OPC return on equity of 10% (high end). Speaking as the Treasurer of Missouri American, I cannot recommend to my Board to make additional investments within Missouri if such a steep reduction in the cost of equity is ordered by the Commission.

Q: WILL THE CUSTOMER BE IMPACTED BY THIS IMPAIRED ACCESS TO CAPITAL?

A: Yes. Reduced access to the capital markets would force Missouri American to delay or scale back needed infrastructure replacement initiatives, and drive up operating costs through higher interest rates and greater working capital requirements.

DEPRECIATION

Q: IN THE LAST RATE-FILING BEFORE THE COMMISSION, MISSOURI AMERICAN RECEIVED A RULING ALLOWING FOR THE INCLUSION OF THE NET SALVAGE VALUE OF THE INSTALLED PLANT IN THE DEPRECATION CALCULATIONS. WHAT WERE THE CIRCUMSTANCES SURROUNDING THAT DECISION?

A: The Commission ruled that Missouri American should include in depreciation the net salvage value of installed plant. The market conditions that drove that decision have not changed. The aging infrastructure of the Missouri American operating districts will create a significant increase in demand for plant retirements and replacements over the foreseeable future. The Company continues to find itself in a high asset replacement mode, and the inclusion of net salvage value assigns a value and amortization of a cost that will occur in the future. In fact, the Company expects to spend more in infrastructure replacements in the next five years than we did in the last five years.

Q: IN HIS DIRECT TESTIMONY, STAFF WITNESS RACKERS SUGGESTS THAT THE INFRASTRUCTURE SYSTEM REPLACEMENT OF PLANT (ISRS), WHICH ALLOWS MISSOURI AMERICAN TO APPLY FOR APPROVAL FOR INFRASTRUCTURE REPLACEMENTS OUTSIDE OF THE SCHEDULED RATE MAKING PROCESS CHANGES THE CIRCUMSTANCES UNDER WHICH THE NET SALVAGE VALUE RULED TO BE INCLUDED WITHIN THE DEPRECIATION CALCULATION. DOES ISRS ELIMINATE THE NEED FOR

INCLUSION OF NET SALVAGE VALUE IN THE DEPRECIATION CALCULATION?

A: No. The purpose for inclusion of net salvage value in the depreciation calculation is based on one of the tenets of cost accounting which is to match expenses and costs with the assets and revenues at the time of use. The allocation of net salvage value across the useful life of an asset is a standard method of accounting that has been used in regulatory accounting for years. Further, proper use of this type of accrual can reduce the "price" shock on future ratepayers who would otherwise have to pay for both new assets and the removal of the old assets that did not serve them. The true cost of service for these assets includes the cost of salvage, and should be born by the ratepayer generation which is served by that asset. The ISRS only addresses the issue of cost recovery, and not the issue of timing, which is the central theme of the net salvage value question.

Q: WHAT WOULD BE THE IMPACT OF EXCLUDING NET SALVAGE VALUE FROM DEPRECIATION, AND PUTTING THE COST OF REMOVAL INTO THE PERIODS JUST PRIOR TO AND FOLLOWING ASSET REPLACEMENT?

A: The immediate impact would be artificially lower rates. This impact would slowly swing the other way over time, and create artificially higher rates as more assets are replaced. Adding the net salvage value, which is typically negative, to the cost of replacement will create a substantial shift in costs from the current rate payers to the next generation of rate payers. This additional cost and the use of amortization periods shorter than the estimated life of the asset will create peaks and valleys in the cost of service as assets are retired and replaced over the years. Further, given the uncertainty of recovering these costs, a business environment is created where a significant portion of Missouri American's cost is at-risk of recovery. This business environment unnecessarily increases the financial risk profile of the company.

Q: WHAT ARE THE TOTAL FINANCIAL IMPACTS OF STAFF WITNESSES MACIAS' AND BEGAN'S DEPRECIATION ADJUSTMENT?

A: The depreciation adjustment, including net salvage value, will have a significant detrimental impact on the company's financial condition. The depreciation adjustment represents a $12 million reduction in the annual cash flow of the Company. The reduction in revenues will reduce the cash flow available to fund capital projects, and increase the need for borrowing or issuance of equities. The $12 million impact represents 17.8% of the projected annual capital expenditures. This means an increase in financings of $60 million over the next five years. The additional financing requirement will further burden the balance sheet, and erode the Company's ability to access the capital market. Further discussion of the details with respect to why such a reduction in depreciation is not appropriate are addressed in Company Witness Spanos' rebuttal testimony.

NATIONAL CALL CENTER AND NATIONAL SHARED SERVICES CENTER

Q: STAFF WITNESS CASSIDY HAS PROPOSED A DISALLOWANCE OF THE CALL CENTER TRANSITION COSTS BECAUSE THEY DID NOT RESULT IN ASSETS ON THE BOOKS OF MISSOURI AMERICAN.

WHY DO YOU BELIEVE THESE TRANSITION COSTS SHOULD BE CAPITALIZED BY MISSOURI AMERICAN?

A: Missouri American was faced with a choice of upgrading a call center whose core technologies were insufficient to satisfy the needs of our present entity within the state which consists of several previously separate organizations. Instead of taking on all of the capital cost and risk associated with creating a new call center, the Company was able to leverage existing assets, systems and processes within the corporate services organization. I believe the transition costs and one-time costs associated with migration and set-up in the new call center should be capitalized as an investment that was required to achieve the cost efficiencies and service improvements provided by this new call center. These efficiencies resulted in an annual per customer reduction as discussed by Company Witness Van den Berg. By investing in the migration to the national call center, Missouri American was able to achieve these customer benefits at a lower risk and cost than creating a duplicative operation in Missouri.

Q: WHAT IS THE IMPACT OF TREATING THESE TRANSITION COSTS AS HISTORIC EXPENSES VERSUS CAPITALIZED COSTS?

A: Staff's proposal to treat these costs as expenses would mean that all of the costs incurred to provide a future benefit to customers would be expensed in the interim period between the last rate case and this one. Therefore, those costs would go totally unrecovered and, as discussed above, written-off! This means the shareholders would not be compensated for an investment which provided better service at a lower cost for customers.

Q: WHY SHOULD THESE COSTS BE CAPITALIZED?

A: These transition costs create an intangible asset in the form of the Shared Service Center cost structure and service capability into the future. Therefore, such transition costs should be treated as an asset and recovered across time, not solely in the period it was incurred.

Q: ON PAGE 10 OF STAFF WITNESS BERNSEN'S TESTIMONY, A REQUEST IS MADE FOR ADDITIONAL REPORTING DATA FROM THE NATIONAL CALL CENTER. PLEASE RESPOND.

A: The Company is currently reviewing Staff's request and is willing to work with Ms. Bernsen to understand what is required and to determine if such information is readily available without any additional cost.

<u>**ACQUISITION ADJUSTMENT**</u>

Q: IN HIS DIRECT TESTIMONY, MR. RACKERS STATES THAT THE COMMISSION SHOULD DENY THE REQUEST FOR RECOVERY OF THE ACQUISITION ADJUSTMENTS BASED ON THE FACT THAT THE COMMISSION HAS HISTORICALLY DENIED SUCH RECOVERIES. DO YOU AGREE?

A: No. The Commission should make decisions based on a full recognition and comprehensive consideration of the relevant law, the specific circumstances related to the case, and the intended purpose of public policy. Reliance on limited historical precedent, absent any investigation of the specific case facts and circumstances, is not a sufficient basis for making such determination. Further, Mr. Rackers' interpretation of previous rulings confuses the issue. In his testimony, Mr. Rackers states "Recognition of acquisition premiums and discounts would also be counter to the Commission's historical position of allowing shareholders to retain any gains, or bear any losses, associated with the sale of utility property." Missouri American is asking the Public Service Commission to recognize the total benefits these transactions have created for consumers and to allow MAWC to recover the premium that it was required to pay to acquire the assets and bring those efficiencies to customers.

Q: WHY WOULD MERGERS AND ACQUISITIONS BENEFIT THE WATER AND WASTEWATER INDUSTRY?

A: The water and wastewater industry is a very capital-intensive industry characterized by a very high fixed asset levels relative to the incremental cost of the commodity. Typical asset to revenue ratios for water, gas and electric utilities are illustrated below:

Water Utilities (Fixed Assets/Revenue)	Natural Gas Utilities (Fixed Assets/Revenue)	Electric Utilities (Fixed Assets/Revenue)
1.88x	.31x	.95x

Asset-to-Revenue Ratio from OneSource data base – 2000-2002 industry averages

This high asset-to-revenue ratio reflects a significant amount of fixed costs, and requires significant balance sheet capability to fund asset construction, repair and replacement as systems grow or need to be replaced. This is why water utilities are structurally conducive to economies of scale. The incremental cost of serving customers in a territory is only marginal once the infrastructure is in place. This operational leverage against capital requirements is why mergers and acquisitions can be especially beneficial in the water and wastewater industry.

Q: HOW DOES THIS OPERATIONAL LEVERAGE ENABLE BENEFITS CREATED BY MERGERS?

A: The high fixed costs and lower incremental commodity and operating costs to serve customers create the opportunity to add additional customers without a corresponding or ratable increase in operating costs. This is evidenced first in the municipal transactions with the addition of 22,000 customers with the addition of no additional employees and in the United Water (Jefferson City) transaction with the acquisition of over 11,000 customers where only 15 of the existing 26 employees were required.

Q: ARE THERE ANY OTHER FACTORS WHICH CONTRIBUTE TO THE DRIVE TOWARD CONSOLIDATION IN THE WATER AND WASTEWATER INDUSTRIES?

A: Yes. It has been well documented that the aging infrastructure of water utilities' inability to meet legislative requirements for clean water in the United States has created a large increase in the investment requirements in new and replacement plant. This situation has been further compounded by changes in the environmental laws which have served to increase the cost of those replacements, accelerate the retirement of some plant and created a burden to upgrade plant with significant life left on it. This increase in capital demand has placed further demands on industry participants' financial structure and created even greater benefits for companies who can achieve efficiencies and scale through acquisition or merger.

Q: WHY DO YOU BELIEVE ACQUISITION ADJUSTMENTS SHOULD BE INCLUDED IN RATES?

A: By creating a mechanism by which companies are allowed to recover their investments in those mergers and acquisitions which create improved operating economies, customer service, and financial strength, commissions can create a business environment which encourages investments that provide benefits to customers.

Q: CAN MISSOURI AMERICAN PROVE CUSTOMERS HAVE RECEIVED A NET BENEFIT SUBJECT ACQUISITIONS?

A: Yes. The companies were able to show net benefit to the consumer through demonstrating how the transaction created operating and financial benefits. These benefits are demonstrated through economies and cost savings achieved through consolidation of the two entities. Missouri American's cost savings or economies occurred in the areas of labor, corporate overhead, increased asset leverage and leverage of existing field infrastructure.

Q: COULD YOU PLEASE CHARACTERIZE THE BENEFITS OF THE ACQUISITIONS OF FLORISSANT, WEBSTER GROVES, UNITED WATER AND VALLEY PARK?

A: Yes. As mentioned, the acquisition of these operating districts have allowed Missouri American to create additional scale economies and direct cost savings for both the customers of these operating districts as well as Missouri American's other operating districts. Specifically, the Company was able to add these operating districts with only minimal additions to its existing staff. This represents a reduction of all operating employees who were previously serving these operating districts. Labor savings alone for the municipal transactions are estimated to exceed $880,000 per year:

Valley Park	Webster Groves	Florissant	Total
$105,669	$342,173	$432,786	$880,628

These are in addition to the over $510,000 in savings identified by Staff from the United Water acquisition. Again, these costs were eliminated as the operations of these districts were absorbed by the existing Missouri American operations This demonstrates how scale advantages can be brought to bear, especially in adjoining or nearby operating districts such as these.

Q: HOW DOES MISSOURI AMERICAN PROPOSE TO RECOVER THE ACQUISITION ADJUSTMENT IN THIS CASE?

A: Missouri American proposes to include the acquisition adjustment in rate base, and amortize this amount over a weighted average period of 37 years. The amortization period of 37 years was chosen because it reflects the average remaining life of Company's assets. The inclusion of the acquisition adjustment in rate base is most appropriate for several reasons. First, Missouri American has incorporated the related cost savings into the cost of service in the rate proposal this proceeding. Matching these savings with the costs necessary to create these savings is consistent with traditional rate making policies.

Q: DO YOU AGREE WITH PUBLIC COUNSEL WITNESS BOLIN'S STATEMENT THAT ACQUISITION PREMIUMS SHOULD NOT BE MADE PART OF THE RATE BASE BECAUSE THEY HAVE NO BEARING ON THE OPERATIONS OF THE COMPANY, AND ARE ONLY SHAREHOLDER EXPENSES?

A: No. Acquisition adjustments and other acquisition costs are necessary costs incurred to create the benefits derived from these acquisitions. These benefits are typically created by combining operations of the two entities to achieve greater leverage of fixed costs such as corporate and human resources functions, engineering staff, legal and regulatory expenses and financing costs. Operationally, benefits are typically found in greater purchasing leverage and leverage of customer service functions. The costs of achieving these efficiencies, i.e., the acquisition adjustment and other out-of-pocket costs, should be treated similarly to any investment in cost reducing technologies, assets or processes. Savings created or enabled by Missouri American's transactions have been well documented, and even referred to by Staff Witness Rackers ($510,000) in his analysis of Missouri American's new cost structure. To argue for the exclusion of the investment cost while at the same time arguing for the reduction in expenses created by those investments is inconsistent.

Q: IN HIS DIRECT TESTIMONY, MR. RACKERS STATES THAT THE CUSTOMERS SHOULD NOT BE A PARTY TO ANY RECOVERY OF THE ACQUISITION ADJUSTMENT, BECAUSE THEY DID NOT BENEFIT FROM THE TRANSACTION, AND THEY HAD NO SAY OR

INFLUENCE IN THE TRANSACTION. HAVE CUSTOMERS ALREADY BENEFITED FROM THIS TRANSACTION, AND WILL SUCH BENEFITS CONTINUE INTO THE FUTURE?

A: Yes. I believe each of these transactions has created permanent benefits from scale economies for the acquired and incumbent customers. Further, the Florissant, Valley Park and Webster Groves companies were municipally owned, and therefore the customers were owners of the assets. As such, they either directly or indirectly benefited from the price paid by Missouri American. Funds received by those municipalities would have either gone into the general fund to reduce current and future tax requirements, reduce debt, or to fund other municipal projects in their community. It is therefore wholly realistic to assume that the customers in these districts have benefited either directly or indirectly from the purchase price already.

Q: ARE THERE OTHER WAYS CUSTOMERS CAN RECEIVE BENEFITS FROM AN ACQUISITION ADJUSTMENT OR OTHER TRANSACTION COST?

A: Yes, in addition to the application of cash generated through the transaction, customers will benefit from the improved cost structure of Missouri American. Many of these improvements have been documented and acknowledged by Mr. Rackers and others. On page 8, lines 5-10 of his Direct Testimony, Mr. Rackers acknowledges a $510,000 savings in payroll costs directly related with the United Water property transaction in his argument to reduce the rates of Jefferson City. Customers will continue to benefit from these savings identified by Mr. Rackers into the future as those positions and related costs have been permanently removed from the cost structure of the former United Water property (Jefferson City). Other recurring savings include reduced corporate and administrative costs, reduced fleet requirements and improved purchasing efficiencies. Similarly, permanent savings have occurred across all the operating entities as continued growth in scale across both the new and existing service territories spreads fixed costs across a larger customer group.

Q: WILL THE CUSTOMER CONTINUE TO RECEIVE THESE BENEFITS AFTER THE ACQUISITION ADJUSTMENT IS FULLY RECOVERED?

A: Yes. The nature of the benefits is such that they continue in perpetuity while the recovery of the acquisition premium will end at the conclusion of the amortization period. An example of this would be the elimination of a position which is made redundant by an acquisition. That position is removed from the company, and is never recreated. Further, the company also avoids the costs associated with that position as they would have escalated in the future. This creates an increasing nominal benefit across time that will continue to accrue to the customer.

Q: IN THEIR TESTIMONY, MR. GORMAN AND MS. LACONTE STATE THAT THEY ARE NOT OPPOSED TO RECOVERY OF THE ACQUISITION ADJUSTMENT IN SO FAR AS THE FUNDING OF THE RECOVERY IS ACCOMPLISHED THROUGH VERIFIABLE SAVINGS. WHY HAVE THEY NOT ENDORSED MISSOURI AMERICAN'S PROPOSAL THUS FAR?

A: In her Direct Testimony, Ms. Laconte states that "The Commission should disallow the return of and on the acquisition adjustment until the Company can prove that there is a measurable benefit to its customers of acquiring these properties at a price above book value." However, Ms. Laconte has limited her analysis of the measurable benefits to the United Water acquisition, while applying the costs associated with the acquisition adjustment recovery to all of the acquisitions. As discussed earlier in this testimony, the net benefit demonstrated is at least $1.39 million annually. This exceeds the annual cost of recovery shown in Ms. LaConte's testimony of $842,663. This indicates both a near term and continuing net benefit to the customer justifying the inclusion of the acquisition adjustment.

In his Direct Testimony, Mr. Gorman states: "Therefore, the Commission should only consider an acquisition premium cost if the utility makes a clear and verifiable demonstration that the merger or acquisition produced savings that would not have otherwise been produced, and the savings significantly exceeded the merger or acquisition cost. With this type of policy the public interest would be preserved, because rates would have been reduced as a result of the acquisition and the Company will be provided an opportunity to recover acquisition adjustments, but only from a share of verifiable savings."

In this statement, Mr. Gorman is agreeing that the public interest is served, and good public policy is created when acquisition adjustments are recovered through a portion of the verifiable savings. Mr. Gorman, like Ms. LaConte, has simply underestimated the benefits created by these transactions.

Q. HOW HAVE THE BENEFITS BEEN UNDERESTIMATED?

A. First, Mr. Gorman states that Missouri American's costs have gone up due to increased allocations of corporate costs due to the higher customer number. While the total dollar amount of the allocation may increase with the increase in customer numbers, the <u>per customer</u> amount is reduced for the existing and new customers by the addition of new customers to the allocation pool. Additionally, general cost increases are allocated across a larger customer pool thereby reducing the impact of cost increases to the customers.

The acquisition related savings of $1.39 million and the per customer cost are sufficient to ensure that the transactions created benefits to the customer which justify the cost and public policy issues that Mr. Gorman detailed in the above quotation.

Q: IN HIS DIRECT TESTIMONY, MR. RACKERS ARGUES THAT MISSOURI AMERICAN HAS SOLEY BENEFITED FROM INCREASED REVENUES FROM RETAIL VERSUS WHOLESALE SERVICE FOR THE MUNICIPALITIES, FLORISSANT, WEBSTER GROVE AND VALLEY PARK. DO YOU AGREE WITH THIS ARGUMENT?

A: No. Mr. Rackers is simply comparing two numbers and equating the revenue differential between the wholesale and retail services without consideration of the additional costs involved at the retail level. These costs include customer service, distribution assets, billing and service among others. A simple analysis of the net impact of the wholesale revenue offset is demonstrated in Schedule JMJ-2. The analysis shows the incremental costs associated with providing retail services in these operating districts are approximately $1.9 million per year.

Q: HAS THE COMPANY ALREADY RECOVERED THE ACQUISITION ADJUSTMENT THROUGH REGULATORY LAG AS IMPLIED BY MR. RACKERS?

A: No. Missouri American was not afforded this opportunity in this case as the operating costs of the legacy companies exceeded their revenues, and the benefit of merger related savings were absorbed by the higher operating costs. These costs include investments in new plant which went into service since the 1999 test year without a corresponding change in rates. During this interim period, MAWC has put over $146 million of new plant into service. This investment represents an approximate 29% incremental capital investment level on a rate base of approximately $500 million. MAWC will not begin recovering the costs associated with these investments until the new rates take effect in 2004.

INTERRUPTIBLE RATE

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY ON THIS ISSUE?

A. Mr. Kalbarczyk, witness for Empire Electric has proposed an interruptible rate in his Direct Testimony. The Company does not oppose the concept of the rate, but does oppose Mr. Kalbarczyk's recommendation of a reduced rate after Empire's annual revenues exceeds the minimum level of revenues that is specified in the contract between the Company and Empire. Company Witness Herbert is addressing the technical reasons why the interruptible rate should not be reduced from the proposed level of $.666 per thousand gallons down to $.357 per thousand gallons.

Q. WHAT IS THE IMPACT ON THE COMPANY'S EXPENSES SHOULD THE COMMISSION APPROVE THE INTERRUPTIBLE RATE?

A. If the interruptible rate is approved at the $.666 rate per thousand, then the sales level necessary to reach the minimum level of revenues required under the contract increases by approximately 65.4 million gallons. This results in additional fuel and power and chemical costs of $9,542. This additional amount must be reflected in the cost of service.

Q. WHAT COMMENTS DOES THE COMPANY HAVE REGARDING THE PROPOSED TARIFF FOR THE INTERRUPTIBLE RATE?

A. The Company is suggesting that the tariff be tailored specifically for Empire Electric. Also, the Company would like to work directly with Empire and the Staff to develop the tariff language for the tariff.

Q: DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A: Yes, it does.

SCHEDULE JMJ-1

Background and Qualifications of James M. Jenkins

My name is James M. Jenkins. I am Vice President and Treasurer for Missouri American Water. I am currently responsible for directing the finance, treasury, business development, and rate administration functions.

I graduated from the University of Illinois, at Urbana/Champaign in 1983 with a Bachelor of Science Degree in Accounting and in 1992 received a M.B.A. Degree, with highest honors, from the University of Illinois, at Springfield. I have been a Certified Public Accountant since 1985.

Between 1983 and 1984 I was employed by McGladrey and Pullen as a Staff Accountant participating in financial audits and completing tax returns for firm clients.

Between 1984 and 1993 I was employed by the Illinois Commerce Commission and worked on a wide range of regulatory issues in the electric, gas, telephone, and water industries. I joined the Illinois Commerce Commission's Accounting Department as a Staff Accountant in November 1984. In April 1987, I was promoted to the position of Auditing Section Chief responsible for directing the Auditing Staff's review of rate case filings, fuel reconciliation clauses, and miscellaneous regulatory accounting issues. In November 1989, I was promoted to Director of Accounting responsible for all administrative, policy, and supervisory functions within the Accounting Department. I held the position of Director of Accounting until joining St. Louis County Water Company in June 1993.

I began my career in the water industry with St. Louis County Water Company in June 1993 as an Assistant Manager in the Corporate Accounting Department. In December 1994, I was promoted to Manager of Rates within the Rates and Operations Analysis Department. At St. Louis County Water Company, I was responsible for the numerous accounting and financial areas contained within Company rate case filings, performing both technical and supervisory functions.

In June 1999 after the acquisition of St. Louis County Water Company by American Water Works, I was elected Vice President and Treasurer for Missouri American Water.

I am a member of the American Institute of Certified Public Accountants and past member of the NARUC Staff Subcommittee on Accounts.

SCHEDULE JMJ-2

Missouri American Water
Case: WR-2003-0500
Net Benefit Calculation
($ 000's)

Florissant		
Net of Wholesale Revenue Increase	$	2,051
Depreciation	$	249
ROR *($9.8 million rate base @ 8.3%)*	$	813
Net Benefit	$	989
Webster Groves		
Net of Wholesale Revenue Increase	$	1,531
Fuel Power & Pumping	$	119
Depreciation	$	165
ROR *($6.5 million rate base @ 8.3%)*	$	540
Net Benefit	$	707
Total Additional Cost to Serve	$	1,886
Total Net Benefit for Acquisitions	$	1,696