

FILED

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Witness: Dennis M. Kalbarczyk
Sponsoring Party: The Empire District Electric Co.
Type of Exhibit: Surrebuttal Testimony
Case No.: WR-2003-0500
Date Testimony Prepared: December 5, 2003

MISSOURI PUBLIC SERVICE COMMISSION

THE EMPIRE DISTRICT ELECTRIC COMPANY

SURREBUTTAL TESTIMONY

OF

DENNIS M. KALBARCZYK

FILED³

JAN 23 2004

Missouri Public
Service Commission

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2003-0500

Exhibit No. 84
Case No(s) WR-2003-0500
Date 1-07-04 Rptr XF

1 **SURREBUTTAL TESTIMONY**

2 **OF**

3 **DENNIS M. KALBARCZYK**

4 **MISSOURI - AMERICAN WATER COMPANY**

5 **Case No. WR-2003-0500**

6
7 **Q. STATE YOUR NAME AND BUSINESS ADDRESS.**

8 A. My name is Dennis M. Kalbarczyk. My business address is 910
9 Piketown Road, Harrisburg, Pennsylvania 17112.

10
11 **Q. HAVE YOU PREVIOUSLY FILED DIRECT TESTIMONY REGARDING RATE**
12 **DESIGN ISSUES IN THIS PROCEEDING, CASE NUMBER WR-2003-0500?**

13 A. Yes, I am the same Dennis M. Kalbarczyk who filed direct
14 testimony on behalf of The Empire District Electric Company
15 ("Empire") in the instant proceeding known as the Missouri
16 American Water Company ("MAWC" or "Company") case number WR-
17 2003-0500.

18
19 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

20 A. The purpose of my surrebuttal testimony is to address rate
21 design and cost of service issues which are discussed in the
22 rebuttal testimony of MAWC's rate design and cost of service
23 witness Paul R. Herbert and Commission Staff witness Wendell
24 R. Hubbs.

25
26 **Q. PLEASE ADDRESS THE REBUTTAL TESTIMONY OF MAWC'S WITNESS MR.**
27 **PAUL R. HERBERT.**

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 A. Mr. Herbert in his rebuttal testimony notes that the Company
2 is not opposed to Empire's proposed interruptible rate of
3 \$0.666 per thousand gallons as long as Empire continues to
4 agree to purchase a minimum of \$500,000 of water per year.
5 However, he notes that the Company does not see any reason
6 why usage beyond the minimum \$500,000 level discussed in my
7 direct testimony should be based upon a lesser cost or as
8 noted in my testimony, the "fully-loaded production cost" of
9 water at \$0.357 per thousand gallons.

10
11 **Q. DO YOU HAVE A RESPONSE TO THE COMPANY'S POSITION IN THIS**
12 **REGARD?**

13 A. Yes. First, regarding Mr. Herbert's comment that Empire
14 continues to agree to purchase a minimum of \$500,000 of water
15 per year at \$0.666 per thousand gallons, a more accurate
16 reading of my direct testimony is that the \$500,000 is the
17 minimum annual level of revenues to MAWC. Simply put, Empire
18 is not required to buy volumes of water to equal the minimum
19 annual level of revenues but rather if the volumes purchased
20 do not equal the minimum annual level of revenues it is still
21 responsible to pay the difference to equal the minimum annual
22 level of revenues agreed upon. Second, Empire's proposed
23 industrial interruptible rate of \$0.666 per thousand gallons
24 represents the maximum rate, or not to exceed rate, one would
25 pay under the tariff or rider.

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 Q. DO YOU AGREE WITH THE COMPANY'S POSITION THAT ALL WATER
2 PURCHASED ABOVE THE MINIMUM ANNUAL LEVEL OF REVENUES SHOULD
3 BE BASED UPON \$0.666 PER THOUSAND GALLONS?

4 A. No. While the Company notes that it does not see any reason
5 to drop below the tail-block rate of \$0.666 just because
6 Empire reaches the minimum annual revenue level the rationale
7 and reasons as set forth in my direct testimony are clear.
8 In brief, MAWC has overlooked the fact that Empire has its
9 own source of supply and storage. From an economic
10 standpoint, a utility customer who can obtain and/or develop
11 part of its needed utility supply and chooses to utilize
12 that supply can result in a smaller overall customer base to
13 the utility over which the remaining cost would be spread.
14 The economic benefits of an incentive rate such as proposed
15 by Empire to encourage the continued use of the Company's
16 water by a customer who can choose to use its own source of
17 supply is well accepted within the industry and is borne out
18 in this case. Once Empire meets the minimum annual revenue
19 level it is not necessary for it to purchase any more water
20 from MAWC. In that light, an additional incentive to procure
21 additional water but at a rate less than the \$0.666 base cost
22 volumetric rate from MAWC is appropriate. The economic
23 benefits to both the Company and its customers of an
24 incentive rate at the fully loaded production cost of water
25 at \$.357 per 1,000 gallons or \$.2678 per CCF is beneficial to
26 all concerned.

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 Q. DO YOU HAVE ANY OTHER COMMENTS WITH REGARD TO MR. HERBERT'S
2 REBUTTAL TESTIMONY?

3 A. Yes. As discussed above, Empire's proposed maximum
4 interruptible rate is based upon a rate of \$0.666 per
5 thousand gallons or in other words the "adjusted base cost of
6 water" as developed in the Company's as-filed cost of service
7 study. In my direct testimony I discussed the base-extra
8 capacity cost of service methodology as described by the
9 American Water Works Association ("AWWA"). Further, I noted
10 that the Company appropriately used the base-extra capacity
11 methodology in its cost of service study and appropriately
12 excluded the cost associated with small main sizes when
13 allocating cost to large industrial users. In short, the
14 resultant rate which produced the last tail block rate of
15 \$0.666 for the large industrial customers closely reflected
16 the "adjusted base cost of water" which excluded small main
17 cost. Mr. Herbert in his rebuttal testimony correctly notes
18 that Ms. Meisenheimer, witness for the Office of the Public
19 Counsel, who proposes the use of an "Economies of Scope and
20 Scale" adjustment to further adjust the allocation factors
21 for mains within the base-extra capacity method, is
22 inconsistent with the AWWA base-extra capacity methodology.
23 Finally, Mr. Herbert correctly notes that Ms. Meisenheimer's
24 proposal, in error, introduces marginal or incremental cost
25 concepts into the base-extra capacity methodology.

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 **Q. CAN YOU PLEASE EXPLAIN?**

2 A. Ms. Meisenheimer in her testimony states that "Economies of
3 Scope" refers to the ability to achieve cost savings by
4 utilizing the same equipment, e.g., the total cost of mains
5 is much less than what the sum of stand-alone costs for mains
6 would be if there was one company that served industrial
7 customers and another company that served residential
8 customers and so on. With regard to "Economies of Scale" Ms.
9 Meisenheimer implies that this describes the phenomenon where
10 larger scale production can achieve cost savings e.g., a 4"
11 pipe has a flow capacity of 6 times that of a 2" pipe meaning
12 that the cost of incremental capacity needed to serve during
13 higher demand periods is less expensive than the average cost
14 of capacity. Finally, Ms. Meisenheimer explains that this
15 principle attempts to ensure that no group of customers
16 should pay more than they would have paid if they were to
17 provide their own products and services using the best
18 available production technique and thus, the revenue
19 requirement for any customer class should be at least as
20 large as the incremental cost to provide services to this
21 class because otherwise somebody else will be forced to pay
22 for more than its stand-alone cost.

23
24 **Q. DO YOU AGREE WITH MS. MEISENHEIMER'S USE OF THE ECONOMIES OF**
25 **SCALE THEORY?**

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 A. No. As Mr. Herbert correctly points out in his rebuttal
2 testimony, Ms. Meisenheimer's methodology introduces the use
3 of incremental or marginal cost concepts into an embedded
4 cost methodology under the base-extra capacity method. There
5 is no discussion or support for such a methodology as
6 proposed by Ms. Meisenheimer in the well-accepted AWWA manual
7 for such a cost of service study theory. Further, such a
8 methodology sends all the wrong price signals by allocating
9 less cost to the extra capacity components implying that the
10 cost to meet peak rates of usage are not the expensive
11 components. Finally, if one were to address true incremental
12 cost, or, in other words, the floor or minimum system, they
13 would need to develop the cost of the minimum system. While
14 Mr. Herbert discusses this concept, the underpinning of such
15 an approach was more widely addressed in the gas and electric
16 industry cost of service study and rate design approach.

17
18 **Q. PLEASE EXPLAIN WHAN YOU MEAN.**

19 A. Briefly, the concept of the minimum or "skeleton" system
20 would determine the cost of a distribution system required
21 simply to attach customers to the system, regardless of their
22 capacity or demand requirements. The cost as pointed out by
23 Mr. Herbert would be the cost of material and labor related
24 to trenching, backfilling, paving and restoration, to also
25 include material and labor for the minimum size pipe. While
26 some may disagree on the minimum size pipe, I believe most

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 would agree that the major portion of cost is not in the cost
2 of the pipe size but rather in the other ancillary cost items
3 just described. The determined minimum cost would then be
4 considered a customer-related cost since its costs depend
5 primarily on the number of customers rather than usage or
6 demand. In general, all customers would share equally in the
7 cost of the minimum or skeleton system and the cost would be
8 reflected in the customer charge rather than the volumetric
9 rates. In short, Ms. Meisenheimer does not attempt to
10 determine the cost of a minimum system or the floor for the
11 purpose of incremental pricing nor does her methodology
12 recognize the true impact such a methodology would have on
13 the final rate design process. In my opinion, the use of
14 such a methodology as proposed by Ms. Meisenheimer should be
15 rejected in lieu of the well accepted base-extra capacity
16 method used by the water industry and as applied by the
17 Company in this proceeding.

18
19 **Q. DO YOU HAVE ANY OTHER COMMENTS WITH REGARD TO MR. HERBERT'S**
20 **REBUTTAL TESTIMONY?**

21 **A.** Yes. As a final comment Mr. Herbert in his rebuttal
22 testimony notes that Mr. Wendell R. Hubbs incorrectly omitted
23 the small mains adjustment from his cost of service study
24 allocations. As discussed in my direct testimony and earlier
25 in my surrebuttal testimony, the Company appropriately
26 applied a small mains adjustment to prevent such cost from

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 being allocated to the larger industrial customers. The
2 application of a small mains adjustment recognizes that large
3 industrial customers are connected to the transmission system
4 and not the distribution system. In my opinion, the
5 Commission should accept the use of the small mains
6 adjustment as appropriately applied by the Company's cost of
7 service witness, Mr. Herbert.

8
9 **Q. PLEASE ADDRESS THE REBUTTAL TESTIMONY OF COMMISSION STAFF**
10 **WITNESS MR. WENDELL R. HUBBS.**

11 A. Mr. Hubbs takes exception to the establishment of an
12 industrial interruptible rate based upon his surprise that
13 that the Company and Empire entered into a contract for a
14 type of service that the Commission has not approved, noting
15 that the Company signed a contract to provide limited service
16 and did not come to the Commission to seek a more appropriate
17 rate. He also opines that just hearing of the contract does
18 not provide adequate time for Staff to respond to the
19 proposal, that it normally takes Staff months to investigate
20 and process other proposals and that Staff lacks the
21 resources and time to see whether they could support approval
22 of the proposed contractual service much less attempt to set
23 a rate for such a service. Further, he proposes that the
24 Commission reject the industrial interruptible rate until
25 such time as the Company and Empire file for approval of the
26 special service contract service. Finally, he opines that

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 the tariff class proposed is only for one customer and rates
2 for service should be of a special tariff rate instead of
3 being applicable to a class of similar customers.

4
5 **Q. DO YOU AGREE WITH MR. HUBBS' CHARACTERICATION AND OPINION**
6 **WITH REGARD TO EMPIRE'S PROPOSED INDUSTRIAL INTERRUPTIBLE**
7 **TARIFF?**

8 A. No. First, it is important to note that Empire entered into
9 the service contract arrangement as required by the Company
10 to obtain service. As noted in my direct testimony, Empire
11 agreed to take service at current rates as approved by and
12 subject to the regulation of the Commission under the
13 industrial rate class. Further, the agreement provided that
14 Empire could seek, and the Company would support, an
15 interruptible tariff during any applicable subsequent rate
16 proceeding by the Company. Empire submitted its proposal at
17 its first opportunity. Simply put, the Company's tariff does
18 not provide for an interruptible tariff. While Mr. Hubbs may
19 take exception to the proposed interruptible tariff due to
20 his surprise or believe that there is limited time to review
21 such a proposal, Empire believes that its request is both
22 timely and supported by well-accepted ratemaking concepts.

23
24 **Q. PLEASE EXPLAIN.**

25 A. Empire does not view the concept of an interruptible tariff
26 or rider as new or novel within the water industry or even

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 the regulated industry as a whole, and it certainly is not
2 unusual for new tariffs or rate concepts to be introduced
3 during a rate case proceeding. Empire submits that its
4 request before the Commission for an industrial interruptible
5 tariff or rider as submitted in my direct testimony provided
6 the rationale for such a tariff or rider in a clear and
7 transparent format which would provide all interested parties
8 an opportunity to accept, reject, and/ or comment favorably
9 or unfavorably on its proposal. In that light, Empire
10 submits that the rate process at this time provides the ideal
11 time for all interested parties to respond accordingly.

12
13 **Q. WHAT IS YOUR RESPONSE TO MR. HUBBS' COMMENT THAT IT WOULD BE**
14 **DIFFICULT TO ARRIVE AT AN INTERRUPTIBLE RATE FOR EMPIRE IN**
15 **THIS PROCEEDING?**

16 **A.** As I explained in my direct testimony, the basic premise is
17 that rates should reflect the cost of providing water
18 service. A sound analysis of the development of any proposed
19 rate should reflect the allocation of costs commensurate with
20 the service requirements of furnishing the different types of
21 service based upon the total volume of water and peak rates
22 of use or demand, as well as other factors. Thus, one relies
23 upon a cost of service study which allocates the total cost
24 of service or revenue requirement among the customer classes
25 based upon their respective service characteristics, demand
26 patterns, including whether service is provided on a firm or

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1 non-firm basis, along with other considerations. A customer
2 class cost of service study is a reasonable and objective
3 tool for the design and establishment of rates among the
4 customer classes that, when relied upon, demonstrates that
5 rates are nondiscriminatory and meet as nearly as possible
6 the cost of providing service to such customer classes.
7 Further, the Company prepared such a cost of service study
8 based upon its pro forma operating cost for the instant rate
9 case filing so that all interested parties could review and
10 comment. I as well as others have utilized that cost of
11 service study and pro forma proposed operating cost in
12 developing an appropriate interruptible rate which Empire
13 could take service under. In short, the instant rate case
14 proceeding provides the most current data to include all
15 differences of opinion between the various parties which the
16 Commission can rely upon in approving an appropriate maximum
17 industrial interruptible rate.

18
19 **Q. DO YOU AGREE WITH MR. HUBBS' RECOMMENDATION THAT THE**
20 **COMMISSION SHOULD REJECT THE INDUSTRIAL INTERRUPTIBLE TARIFF**
21 **UNTIL SUCH TIME AS THE COMPANY AND EMPIRE FILE FOR APPROVAL**
22 **OF A SPECIAL SERVICE CONTRACT?**

23 **A.** No; as noted earlier and as explained in my direct testimony,
24 the instant proceeding provides the parties and the
25 Commission a reasonable opportunity to explore the rationale
26 and general language which should be included in an

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 industrial interruptible tariff or rider. Simply put, as
2 illustrated in Empire's specimen industrial interruptible
3 tariff or rider, it merely provides for the general
4 applicability and availability of the tariff or rider and the
5 qualifications one must meet in order to qualify under the
6 industrial interruptible tariff or rider and sets forth the
7 last block rate in the industrial class as the maximum
8 industrial interruptible rate. Once qualified under the
9 industrial interruptible tariff or rider, the Company and
10 industrial customer would then enter into a service agreement
11 noting the applicable rate and service terms.
12

13 **Q. DO YOU AGREE WITH MR. HUBBS' CHARACTERIZATION THAT THE TARIFF**
14 **CLASS PROPOSED IS ONLY FOR ONE CUSTOMER AND RATES FOR SERVICE**
15 **SHOULD BE OF A SPECIAL TARIFF RATE INSTEAD OF BEING**
16 **APPLICABLE TO A CLASS OF SIMILAR CUSTOMERS?**

17 **A.** No. As I explained in my direct testimony, Pennsylvania
18 American Water Company, one of MAWC's sister companies, has
19 six tariff rates which provide for such consideration in its
20 rates. They are as follows: Industrial Curtailment Rate,
21 Resale and Electric Generation Standby Rate, Industrial
22 Standby Rate, Rider DIS - Demand Based Industrial Service,
23 Rider DRS - Demand-Based Resale Service, and Rate EGS -
24 Electric Generation Service. As noted, the specifics of each
25 tariff or rider was designed to recognize the unique
26 characteristics of how the applicable customer(s) operates,

**Surrebuttal Testimony of
Dennis M. Kalbarczyk**

1 along with the demands placed on the utility's system, and
2 balances the economics of maintaining and/or attracting them
3 as a utility customer(s). Thus, Empire's specimen tariff
4 merely reflected an Electric Generation Interruptible Service
5 Rider Tariff as illustrative of what the rider tariff may
6 look like. Empire is not opposed to the rider being listed
7 as an Industrial Interruptible Service Rider Tariff. The
8 more important point, which I believe addresses Mr. Hubbs'
9 concern, is that while the rider would set the maximum
10 industrial interruptible rate it still requires a special
11 service contract setting forth the applicable rates. In
12 summary, I believe Empire's proposal fairly and reasonably
13 sets forth an industrial interruptible tariff or rider which
14 explains what criteria must be met to qualify and then
15 further requires the Company and customer to enter into a
16 service agreement for the applicable rate.

17
18 **Q. DO YOU HAVE ANY OTHER COMMENTS?**

19 A. Yes. Should the Commission make changes to MAWC's proposed
20 filing, I would recommend that the cost of service study be
21 re-run, and consistent with my analysis discussed above, the
22 adjusted base cost of water and fully loaded production cost
23 of water for Empire's interruptible rate would be
24 recalculated, exclusive of any change to the minimal annual
25 charge reflected in the contractual agreement between Empire
26 and MAWC.

Surrebuttal Testimony of
Dennis M. Kalbarczyk

- 1 Q. DOES THAT CONCLUDE YOUR SURREBUTTAL TESTIMONY?
- 2 A. Yes.

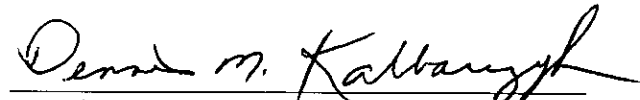
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the General Rate Increase for)
Water Service Provided by Missouri-American)
Water Company.) Case No. WR-2003-0500

AFFIDAVIT OF DENNIS M. KALBARCZYK

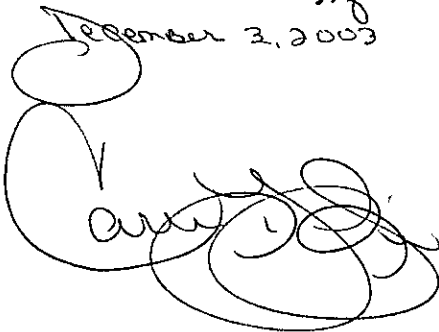
COMMONWEALTH OF PENNSYLVANIA)
)
COUNTY OF DAUPHIN)

Dennis M. Kalbarczyk, being of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 14 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.


Dennis M. Kalbarczyk

Sworn To And Subscribed
Before Me This Day, 9

December 2, 2003



NOTARIAL SEAL
Carrie Jean Singer, Notary Public
Lower Paxton Twp. Dauphin County
My Commission Expires September 7, 2006