Exhibit No.:	
Issues:	Plant Disallowance and Tariff
Witness:	James A. Merciel, Jr.
Sponsoring Party:	MO PSC Staff
Type of Exhibit:	Rebuttal Testimony
Case No.:	WR-2010-0131
Date Testimony Prepared:	April 15, 2010

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY OPERATIONS DIVISION

REBUTTAL TESTIMONY

OF

JAMES A. MERCIEL, JR.

MISSOURI AMERICAN WATER COMPANY

CASE NO. WR-2010-0131

Jefferson City, Missouri
April 2010

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of Missouri-American Water Company's Request for Authority to Implement a General Rate Increase for Water and Sewer Services Provided in Missouri Service Areas	)))))	Case No. WR-2010-0131

AFFIDAVIT OF JAMES A. MERCIEL, JR.

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

James A. Merciel, Jr., of lawful age, on his oath states: that he has participated in the preparation of the following Rebuttal Testimony in question and answer form, consisting of 10 pages of Rebuttal Testimony to be presented in the above case, that the answers in the following Rebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true to the best of his knowledge and belief.

James A. Merciel, Jr.

Subscribed and sworn to before me this 15th day of April, 2010.

NOTARY PUBLIC
NOTARY SEAL
STATE OF MISSOURI

SUSAN L. SUNDERMEYER
My Commission Expires
September 21, 2010
Callaway County
Commission #06942086

Notary Public

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MISSOURI AMERICAN WATER COMPANY

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Q. Please state your name.

A. My name is James A. Merciel, Jr.

Q. By whom are you employed?

A. I am employed by the Missouri Public Service Commission.

Q Are you the same James A. Merciel, Jr. who participated in the Staff Report on Cost of Service (Staff Report) that was filed on March 10, 2010?

A. Yes. My qualifications are within Appendix 1 of that document on pages 22 through 25.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of this rebuttal testimony is 1) to modify the Staff's recommended disallowance of the capital expense associated with a project to expand the capacity of the Cedar Hill Sand Creek Plant sewage treatment facility (Cedar Hill Plant). This issue was addressed in the Staff Report on pages 38 and 39; 2) to address various issues with respect to Missouri American Water Company's (MAWC or Company) proposal to revise its six (6) existing water tariffs and consolidate them into one water tariff, and; 3) to respond to testimony regarding quality of service in the Company's Platte County service area.

Cedar Hill Plant Disallowance

Q. Has the staff changed its position with regard to a plant disallowance for the Company's Cedar Hill Plant?

A. Yes.

Q. Please briefly describe the situation with regard to the Cedar Hill Plant?

A. The Cedar Hill Plant was originally constructed in the late 1980's or early 1990's by Cedar Hill Utility Co, Inc., the predecessor owner of this sewer system, with a capacity of 75,000 gallons per day. This treatment facility as was originally constructed has been adequate to serve existing customers until recently. Several years ago, MAWC constructed a replacement treatment plant (new facility) with a capacity of 150,000 gallons per day, because a new subdivision named O'Brien Place was proposed, for which the developer applied for service, and which would require additional capacity beyond that of the original treatment facility. Unfortunately, that subdivision has never developed beyond some initial ground preparation work, and so the additional capacity provided by the new facility was not utilized, except by a single new customer added after the new facility construction.

Q. What was the Staff's previous position?

A. In the Staff Report, and in previous cases, the Staff recommended disallowance of almost all of the cost associated with the construction of the new facility with the opinion that the expanded capacity provided by the new facility was not used and useful. The calculation used to arrive at the recommendation in the Staff Report was based on dividing the cost of the new facility by future customers.

Q. What was the Staff's reasoning in taking this position?

A. The reasoning was that the Cedar Hill Plant, as originally constructed with a capacity of 75,000 gallons per day, was adequate to serve existing customers. And, since there was only one new customer after the new facility project, the additional capacity provided by the new facility was not used and useful for ratemaking purposes. While the Staff has never considered construction of the new facility to be an imprudent capital expenditure, the Staff also never believed it to be reasonable that existing customers pay the cost of the new facility, since new customers, for which the plant was constructed, were never connected (except one). Thus, new customers were not available to pay rates to support the capital cost of the new facility and its expanded capacity.

Q. Why has the Staff now changed its position with regard to the Cedar Hill Plant disallowance?

A. The staff has received information that, with respect to utilized plant capacity, the Company has actually added customers, and also appears to be close to adding a 51-customer existing subdivision. Additionally, some upgrades to the plant clarifier component, and the disinfection system were required in order to meet the latest standards of the Missouri Department of Natural Resources (DNR). In light of this information, the staff now believes that the plant expansion is at the point of being necessary, used and useful.

Q. What is the Staff's position now?

A. Rather than dividing the cost of the new plant by future customers, the Staff now recommends a calculation that divides the cost of the new plant by both existing and future customers. This method allows the Company to recover the cost of the plant that is utilized for existing customers, but disallows only the portion of the plant needed for future customers. The Staff's revised worksheet is included with this testimony as Attachment 1.

The Staff's new proposed disallowance, calculated by using its revised methodology of dividing the cost by both existing and future customers instead of its previous methodology of dividing the cost only by future customers, is reduced from $2,179,908 to $1,050,282.

Consolidated and Revised Tariff

Q. What do you believe are potential issues with regard to the Company's proposed, revised and consolidated tariff?

A. As with most large documents, there will likely be a need for several iterations of review and revising for improvement of substantive content, grammar and clarity. The Staff has reviewed the Company's tariff draft as filed in this case, sent the Company some initial comments, and met with the Company to go over some of the Staff's suggested changes. Most of the Staff's suggestions consist of simple typographical corrections, minor re-writing of some rules for clarity or simplicity, and re-arranging of some rules. Also, both the Company and the Staff are still considering how to address a few items. I believe that these types of items will be satisfactorily resolved. However, there are four items that I think could become contested issues in this case, as follows:

- A new rule regarding fire protection, applying to all customers including residential.
- Company financial participation in water main extensions, sometimes called "Company Participation amount."
- "Fair share" payments by new customers and corresponding refunds to applicants funding water main extensions.
- Limits of liability defined in the tariff.

Q. Can you please describe the idea behind the new fire protection rule?

A. Yes. It is not uncommon for commercial and industrial premises to have private fire protection systems in the form of building sprinklers. Usually, but not always, the fire protection systems are served by a dedicated water main connection and a fire service line that is a 2” or larger pipeline. In recent years, it has become desirable, and products are being developed, to install fire protection sprinkler systems in residences.

Residential fire protection systems involve systems that are smaller than those for commercial buildings. Also, builders and developers are concerned about the extra cost of sprinkler system installation. As an issue that is in its infancy, the challenge is to create a rule and policies that balance the cost of two connections, two service lines and two meter settings, with the lower cost and simplicity of one connection, service line and meter setting; but that has disadvantages including the inability of the Company to turn off service without interrupting the fire protection service, and metering both domestic and fire flow through a water meter that is not rated for fire protection.

Q. Do you have a recommendation that will settle this issue?

A. Not at this time. I am interested in continuing to study the input of the Company and other interested stakeholders with regard to this matter before a final decision is made, and a rule is created.

Q. What is meant by “Company Participation amount” with regard to the water main extension rule?

A. Each of the Company’s tariffs for water service, as is common among water utilities, has a rule regarding water main extensions. That means when a developer, individual customer or a group of customers does not have a main available to serve their property, a water main extension must be constructed throughout a subdivision or in front of the individual lots, at the developer's or customers' expense. In some, but not all, of its districts, the Company invests some of its capital in the main extensions based on the revenue, perhaps an amount that is equal to three or four times the revenue associated with customers on the new main extension. The Company invests $200 per customer in its St. Louis Metro district, and none in its Warren County district. This investment is often called a Company Participation amount, and is invested by the Company as a developer or prospective new customers construct a water main extension. Subsequent to the main extension, if the developer or prospective new customers partially funded the water main extension, then the Company further invests the Company Participation amount as additional new customers connect to the main extension by refunding the developer or prospective new customers who originally paid for the extension.

Q. Has the Company proposed a change to this Company Participation provision in the extension rules?

A. Yes, the Company proposes to eliminate the Company Participation amount in a consolidated tariff.

Q. Are there disadvantages to eliminating the Company Participation amount, or otherwise standardizing a Company Participation amount among districts?

A. Yes, there are disadvantages, as follows:

- Elimination of the Company Participation amount affects the amount of funds developers must use to construct water mains, which in turn could adversely affect new development and growth within some of the communities.
- From the Staff's perspective, the Company Participation amount serves as an allowance from the Company to construct mains that resolve problems in older

developed areas where there could be inadequate customer service lines, citizens that do not have central water service or are served by a separate inadequate water system or shared wells. Sometimes, the improvements can be constructed at little or no cost to those affected citizens or customers.

- Standardization of Company Participation amounts could result in creating such in some service areas such as St. Louis County, resulting in a greater increase in rate base, and thus higher future rates in those areas. The Company could instead invest those funds in other needed improvements, resulting in better and more reliable service, for the same increase in rate base.

It should be noted that elimination of the Company Participation amount in areas where it presently exists could result in less rate base increases and thus lower rate increase amounts in the future. Alternatively, if the Company ceases investing capital funds in new main extensions but rather invests those same capital funds in system improvements, then more issues involving water pressure and fire protection could be addressed. This would be at a cost of ceasing to subsidize new development in the form of water mains constructed partially with Company investment.

Q. Do you have a recommendation with regard to this issue?

A. At this point, my recommendation is to develop a consolidated extension rule with a Company Participation amount that is customized for each service area, based on the practice presently in use and approved in existing tariffs. However, I believe that the concerns of the municipalities, who are interested in new development in their areas, should be taken into consideration.

Q. What is a Customer Fair Share charge and refund?

A. The Customer Fair Share charge applies, in addition to any other connection charges that might apply, as a charge to new customers who connect to water mains constructed and paid for by other applicants. Then, the Company refunds that amount to the applicants who paid for the main extension. Customer Fair Share provisions presently exist only in the Company's tariffs applying to its St. Louis Metro District and Warren County District. This provision does not apply, however, to developers with respect to their own subdivision lots.

Q. Has the Company proposed a change to the Customer Fair Share provisions in its consolidated tariff?

A. Yes, the Company proposes to eliminate the Customer Fair Share charges and refunds.

Q. Are there disadvantages to the elimination of this provision?

A. Yes. After a customer, particularly an individual customer, has paid for a main extension past other lots to get to their own lot, it is not reasonable in my opinion for other customers to immediately be able to connect to that new water main at no cost. This could apply to people constructing new homes, or could apply to situations where there are older, inadequate water systems or long service lines running along a street, and where the citizens would like to connect to an adequate water main that is owned by the Company.

Q. What is your recommendation with regard to the Customer Fair Share matter?

A. Similar to the matter of Company Participation for capital funding of main extensions, I recommend that the Customer Fair Share provision not be eliminated from the tariff with respect to the service areas in which it presently applies. Although it requires the Company to keep good records on the main extension projects, this refund is very important, in my opinion, to customers who find themselves spending very large amounts of money in order to get water to their properties, and then see others around them take free advantage.

Further, in the event that the Company Participation amounts were eliminated from the Company's tariff for any of the service areas, then I believe a Customer Fair Share provision should be instituted in order to preserve refunds to customers who pay for main extensions.

Q. Will you please explain your concern with regard to liability limits provisions in the tariff?

A. Yes. In other recent tariff revision projects, both the Staff and the Office of the Public Counsel have taken the position that tariffs cannot limit any liability a utility incurs in providing service, or with regard to any discrepancies with utility service. As it is a legal issue, I will not offer analysis or arguments in this testimony. In comments provided to the Company for various parts of its proposed tariff, I have offered alternative wording that states what the Company agrees to do, or not do, rather than limit civil liability.

City of Riverside Fire Protection

Q. Have you reviewed the direct testimony filed by Gordon Fowlston, Fire Chief, and Michael Duffy, Director of Community Development, on behalf of intervenor City of Riverside?

A. Yes.

Q. Do you have any opinions or recommendations with regard to fire protection within the City of Riverside?

A. Yes. For the City of Riverside (City), similar to other communities with particularly older parts of town with old water systems, it may well be desirable to improve water flow and pressure to meet the needs of modern fire protection and water use for new development or re-development. Although I believe the City and the Company have been meeting and discussing the issues, it may be beneficial for the Staff to meet with the City and Company and become involved in evaluating the water system, the needs, and possible resolutions. This could be done either informally, or as a spinoff case similar to WO-2008-0167, in which the Commission created a task force to study similar needs for Jefferson City. The participants could include not only the City, Company and Staff, but other interested parties such as the Office of the Public Counsel. It should be noted that the Company's Platte County service area is comprised of not only the City, but other communities and areas of the county. This could be a factor in the amount of capital funds the Company can expend in the City, from a practical standpoint, while impacting rates in other parts of its service area.

Q. Does this conclude your rebuttal testimony?

A. Yes.

WR-2010-0131
Cedar Hill Sand Creek Plant Adjustment

Merciel - Rebuttal

CHUC Expanded plant capacity

	gpd		$		
185 pre-existing customers	66,000				357 gal/customer
		88%			
old plant	75,000		$ 100,000		
expansion	75,000		$ 2,192,626	$ 14.62 per gallon	
total capacity	150,000				
15% reserve cushion	22,500				
capacity limit for ratemaking	127,500			357 customer limit for ratemaking	

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		$ 540.54	rate base per pre-existing customers on old plant
Total new capacity	150,000 gal		
capacity used pre-existing	66,000		
reserve cushion	22,500 gal		
Available capacity limit	61,500		
total customer capacity for rates	357	$ 2,192,626	Plant expansion cost
		$ 6,142	cost per all customers to 85% capacity (all customers, existing and future share in plant expansion)
potential new customers	172		
actual new customers	1	ciac $ 1,500	residential

plant disallowance for rate case is
cost per future customers 171 future customers

Capital Disallowance $ 1,050,282