BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of the Application of	)	
Missouri-American Water Company for	)	Case No. WO-2004-0116
Approval to Establish an Infrastructure System	)	
Replacement Surcharge (ISRS)	)	

MISSOURI ENERGY GROUP REPLY
TO MISSOURI-AMERICAN WATER COMPANY
RESPONSE TO STAFF REPORT AND RECOMMENDATIONS

COMES NOW the Missouri Energy Group ("MEG"), in accordance with the Order of the Missouri Public Service Commission ("Commission") dated October 16, 2003, and states the following in reply to the Missouri-American Water Company ("Company") Response to the Commission Staff's ("Staff") report and recommendations:

1. **Accumulated depreciation**: **MEG concurs with the Company on this issue**. The Staff has calculated the amount of accumulated depreciation for the ISRS rate base based on a ratio of the Company's total investment in plant to the total change in the amount of MAWC's investment in plant in service, since the last rate case. HB 208 states that the ISRS rate base should be calculated using: "The water corporation's weighted cost of capital multiplied by the net original cost of eligible infrastructure system replacements, including recognition of accumulated deferred income taxes and accumulated depreciation associated with eligible infrastructure system replacements which are included in a currently effective ISRS;" (393.1000 (a)). The MEG agrees with the Company's understanding of the legislation as to the method of calculating the net ISRS rate base. The Company's method calculates the actual accumulated depreciation for each ISRS eligible infrastructure asset that the Company placed into service

since January 1, 2002 and presents an accurate picture of the actual net plant for the ISRS rate base.

2. <u>**Accumulated Depreciation-Net Salvage Cost:**</u> **MEG concurs with the Staff on this issue.** The Company increased the amount of investment to reflect the change in the accumulated depreciation reserve associated with the net salvage cost. The Staff recommends that this amount should not be included in the amount of investment. In its response, the Company contends that it should be included. MEG disagrees.

The Company forecasts the cost of net salvage and collects this amount over the life of the plant. This is kept in the accumulated depreciation reserve. The Company is correct when it states that its total net investment *increases* when plant is retired. When a plant is retired, the gross amount of the plant is removed from the total gross plant account and the associated depreciated value is removed from the accumulated depreciation reserve. The effect of this on the net plant amount is zero. However, the cost of the net salvage is charged to the accumulated depreciation reserve. When the accumulated depreciation reserve is lowered, the value of net plant is increased. But this doesn't occur *until the plant is retired.* When the plant is retired, then the Company should be allowed to earn a return on the increased net plant. The MEG agrees with the Staff that this amount, $1,036,534, should not be included in the total ISRS rate base.

3. <u>**Facilities Relocations Amount:**</u> **MEG concurs with the Staff and the Company on this issue.** The Staff recommends that the facilities relocations amount be reduced by approximately $1,962,266, to recognize reimbursements by customers. The Company stated in its reply that it agrees with this adjustment.

4. <u>**Property Taxes:**</u> **MEG concurs with the Staff on this issue.** The legislation states that ISRS costs should include "property taxes that will be due within twelve months of the

ISRS filing." The date of the Company's ISRS filing is September 2, 2003. Property taxes for property placed into service ***after*** January 1, 2003 are not due until December 31, 2004, which does not fall within the required twelve- month time frame. The Staff recommends that the property taxes associated with the plant placed into service after January 1, 2003 should not be included in the ISRS costs. The MEG agrees with the Staff's understanding of the legislation as to the amount of property taxes that should be included and recommends that property taxes for property placed into service after January 1, 2003 should not be included in the ISRS costs.

5. **Deferred Income Taxes: MEG concurs with the Staff and the Company on this issue**. The Staff adjusted the level of deferred taxes to reflect an adjustment for state-deferred income taxes. The Company agrees with this adjustment.

6. **ISRS Rate Schedules: MEG has no opinion regarding this issue.** The Staff recommends that the percentage add on for the ISRS should be applied only to the usage portion of a customer's bill. The Company states that the percentage adjustment will be applied to the customer's total bill, (i.e. service charge plus commodity charges).

7. Based upon the foregoing positions and comments, the MEG recommends that the amount of the ISRS to be allowed to the Company for cost recover should be $3,628,576 (see attached schedule).

WHEREFORE, the MEG respectfully requests that the Commission issue an order in this case approving the Company's application to establish an ISRS surcharge in the amount of $3,628,576 per year.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Pursuant to 4 CSR 240-2.080 of the Commission's Rules of Practice and Procedure, I hereby certify that I have this day caused an electronic copy of the foregoing to be served on all persons on the official service list in Case No. WO-2004-0116.

Dated at St. Louis, Missouri this 14th day of November, 2003:

Lisa C. Langeneckert

MEG SCHEDULE

Missouri-American Water Company
ISRS Revenue Requirements Calculation

St. Louis District
MEG Recommendation

ISRS Activity:		Total for ISRS-1 Filing
Water Utility Plant Projects--Replacement Mains, and Associated Valves and Hydrants (RM) RSMo 393.1000 (8a):		
STLC-Replacement Mains and Associated Valves and Hydrants	$	20,723,376
Deferred Taxes		(1,633,436)
Accumulated Depreciation		(664,466)
Total Net 393.1000 (8a)		18,425,474
Water Utility Plant Projects--Main Cleanings and Relinings (RM) RSMo 393.1000 (8b):		
STLC-Main Cleanings and Relinings		0
Deferred Taxes		0
Accumulated Depreciation		0
Total Net 393.1000 (8a)		0
Water Utility Plant Projects--Facilities Relocations (FR) RSMo 393.1000 (8c):		
STLC-Relocated Facilities		8,324,597
Reimbursements		(1,962,266)
Deferred Taxes		(727,525)
Accumulated Depreciation		(127,711)
Total Net 393.1000 (8c)		5,507,096
Total ISRS Rate Base		23,932,570
Overall Rate Of Return per Last Order (WR-2000-0844)		8.59%
UOI Required		2,055,808
Income Tax Conversion Factor		1.623077
Revenue Req. Before Interest Deductibility		3,336,735
Total ISRS Rate Base		23,932,570
Embedded Cost of Debt per Last Order (WR-2000-0844)		3.440%
Interest Expense Deduction		823,280
Combined Federal and State Income Tax Rate		38.388626%
Income Tax Reduction due to Interest		316,046
Tax Conversion Factor		1.623077
Revenue Req Impact - Interest Deductibility		512,967
Total Revenue Requirement on Capital		2,823,768
Depreciation Expense		564,043
Property Taxes		240,765
Total ISRS Revenues	$	3,628,576