

Exhibit No.:

*Issues: Accumulated Deferred
Income Taxes,
Annual Incentive Plan,
Tank Painting Expense,
OPEB Expense,
Cedar Hill Treatment Plant*

Witness: Kimberly K. Bolin.

Sponsoring Party: MoPSC Staff

Type of Exhibit: Surrebuttal Testimony

Case No.: WR-2010-0131

Date Testimony Prepared: May 6, 2010

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

KIMBERLY K. BOLIN

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2010-0131

*Jefferson City, Missouri
May, 2010*

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1 **SURREBUTTAL TESTIMONY**

2 **OF**

3 **KIMBERLY K. BOLIN**

4 **MISSOURI-AMERICAN WATER COMPANY**

5 **CASE NO. WR-2010-0131**

6 Q. Please state your name and business address.

7 A. Kimberly K. Bolin, 200 Madison Street, Suite 440, Jefferson City, MO 65102.

8 Q. By whom are you employed and in what capacity?

9 A. I am employed by the Missouri Public Service Commission (Commission) as a
10 Utility Regulatory Auditor V.

11 Q. Are you the same Kimberly K. Bolin who has filed direct and rebuttal
12 testimony in this case?

13 A. Yes.

14 Q. What is the purpose of your surrebuttal testimony?

15 A. My surrebuttal testimony will address the rebuttal testimony of
16 Missouri-American Water Company's (MAWC, Missouri-American or Company) witness
17 Dennis R. Williams regarding the inclusion of the Accumulated Deferred Income Taxes
18 (ADIT) associated with the Security Accounting Authority Order (AAO) as an offset to rate
19 base, the Company's annual incentive plan, other post-retirement employee benefits, and the
20 Commission's Staff (Staff) proposed Cedar Hill Treatment Plant disallowance. My
21 surrebuttal testimony also addresses the calculation of the accumulated deferred income taxes
22 as addressed in the Office of the Public Counsel's (OPC) witness Ted Robertson. Finally, I
23 will address the rebuttal testimony of Company witness Greg A. Weeks in regards to the

1 Company's proposal for the continuation of the tank painting tracker and the Company's
2 proposed level for such tracker.

3 **ACCUMULATED DEFERRED INCOME TAXES**

4 Q. On page 41 of Company witness Williams' rebuttal testimony he states, "In its
5 direct filing, Staff excluded the AAO from rate base and consistently exclude the associated
6 deferred taxes as well." Has the Staff adjusted its direct filing in regards to this issue and
7 what is the Staff's position regarding the inclusion of the deferred taxes associated with the
8 Security AAO?

9 A. Yes, the Staff has included the accumulated deferred income taxes associated
10 with the amortization of the Security AAO in its deferred tax calculation. Accumulated
11 deferred income taxes should be treated as an offset to rate base in the cost of service.
12 Deferred taxes are simply the result of timing differences between when a company deducts
13 certain expenses on its tax return and when it deducts the expense for ratemaking purposes.
14 Accumulated deferred income taxes are in effect, a prepayment made by customers of income
15 tax expense.

16 Q. Does the Staff agree with Missouri-American that to be consistent in regards to
17 this issue, the accumulated deferred income taxes associated with the Security AAO should
18 only be included as an offset to rate base if the unamortized balance of the AAO is included in
19 rate base?

20 A. No. Accumulated deferred income taxes associated with the Security AAO
21 should be included as an offset to rate base regardless of the rate base treatment given the
22 unamortized balance of the AAO.

1 Q. Mr. Williams claims that Staff's inclusion of the ADIT associated with the
2 Security AAO and exclusion of the Security AAO unamortized balance will create a
3 mismatch in the revenue requirement. Is this correct?

4 A. No. There is no impact on the Company's tax liability (current taxes and
5 deferred taxes) if the unamortized balance of the AAO is included in rate base or excluded
6 from rate base. Deferred income taxes are funded by the customers through income tax
7 expense. The Company's total income tax liability for ratemaking purposes is comprised of
8 deferred income taxes (tax payable at some date in the future) and current income taxes.
9 Since the Company has not paid the deferred income tax yet, but has collected the money for
10 the deferred tax through rates, it is only appropriate to include the ADIT as an offset to rate
11 base in recognition of the ratepayers funding of the deferred income taxes.

12 Q. Does Staff agree with OPC witness Robertson's calculation of the ADIT?

13 A. No. Mr. Robertson has used the amount of the AAO already amortized to
14 calculate his deferred income tax amount. The amortization of the AAO does not cause the
15 Company to incur deferred income taxes; the deferral of the AAO costs is the actual source of
16 the tax timing difference. Staff believes as of October 31, 2009 (the update period), the ADIT
17 associated with the Security AAO is \$640,108. Staff's calculation is based upon the
18 unamortized Security AAO balance as of October 31, 2009, of \$1,667,442, multiplied by the
19 combined state and federal tax rate of 38.39%.

20 **ANNUAL INCENTIVE COMPENSATION**

21 Q. What is the Staff's position on the inclusion in rates of payment to employees
22 through the Company's Annual Incentive Plan (AIP) based upon achievement of
23 financial goals?

1 A. The Staff has not included any AIP compensation paid out to any MAWC
2 employees that was based upon the Company meeting certain financial goals, as the
3 incentives' purpose is to improve the Company's bottom line for shareholders, verses a focus
4 on customer benefits. This includes goals based upon the parent company's financial goals or
5 the local/state financial goals. The Commission has consistently excluded incentive plan
6 payouts to employees for meeting financial goals in prior rate proceedings. For example, in
7 the Report and Order for Case No. GR-2004-0209, et. al., Missouri Gas Energy (MGE), the
8 Commission stated:

9 *The Commission agrees with Staff and Public Counsel that the financial*
10 *incentive portions of the incentive compensation plan should not be*
11 *recovered in rates. Those financial incentives seek to reward the company's*
12 *employees for making their best efforts to improve the company's bottom*
13 *line. Improvements to the company's bottom line chiefly benefit the*
14 *company's shareholders, not its ratepayers. Indeed, some actions that might*
15 *benefit a company's bottom line, such as a large rate increase, or the*
16 *elimination of customer service personnel, might have an adverse effect on*
17 *ratepayers.*

18
19 *If the company wants to have an incentive compensation plan that rewards*
20 *its employees for achieving financial goals that chiefly benefit shareholders,*
21 *it is welcome to do so. However, the shareholders that benefit from the plan*
22 *should pay the costs of the plan. The portion of the incentive compensation*
23 *plan relating to the company's financial goals will be excluded from the*
24 *company's cost of service revenue requirement.*
25

26 **OTHER POST-RETIREMENT EMPLOYEE BENEFITS (OPEB)**

27 Q. Does the Staff have comments regarding proposed amortization of regulatory
28 assets associated with prior deferrals of OPEB costs for St. Joseph, Joplin and
29 St. Louis County Water district, as discussed by Mr. Williams on pages 20 and 21 of his
30 Rebuttal Testimony?

1 A. Yes. The Staff has researched and reviewed these two proposed OPEB
2 deferrals. The first deferral mentioned by Mr. Williams was a result of a prior
3 Missouri-American rate case, Case No. WR-95-205. In that proceeding, the Commission
4 ordered a 20-year amortization of an OPEB deferral relating to the St. Joseph and Joplin
5 districts. Consistent with that Order, the Staff has recognized and included \$31,901 into the
6 Company's OPEB expense level in this case. However, the Staff could not find any similar
7 evidence of a Commission ordered rate treatment for the second OPEB deferral that is
8 associated with the St. Louis County district. The only discussion of this deferral that the
9 Staff found was in Case. No. WR-94-166 (St. Louis County Water Company), by the
10 St. Louis County Water Company witness James Jenkins in his direct testimony on pages 44-
11 45. The Staff can find no evidence that witness Jenkins' proposal to include this amortization
12 in the cost of service was adopted in either the Stipulation and Agreement or the
13 Commission Order for that case. Also, the Staff has not found any evidence in subsequent
14 rate cases that the Commission has ordered an amortization or rate base treatment of this
15 proposed deferral. As it is the Staff's policy to exclude costs incurred by the Company
16 previous to the current rate case's test year, the Staff recommends no amortization of
17 regulatory assets associated with prior deferrals of OPEB costs for the
18 St. Louis County Water district.

19 **CEDAR HILL WASTEWATER PLANT**

20 Q. On page 34 of Company witness Williams' Rebuttal testimony in this case, he
21 cites that an internal review of this issue and outside counsel from a member of the
22 Financial Accounting Standards Board (FASB) suggest that the Company would have to
23 write-off the plant balance less contributions (Staff's proposed adjustment). This is

1 supposedly based upon FASB's Statement of Financial Accounting Standards (FAS) No. 90,
2 entitled "Regulated Enterprises – Accounting for Abandonments and Disallowances of Plant
3 Costs." Does the Staff agree with this interpretation of FAS 90?

4 A. No. The Staff believes this statement would not require the Company to write
5 the asset off in light of an ordered disallowance. Paragraph No. 60 of FASB Statement of
6 Financial Accounting Standards No. 90 states the following:

7 *60. Some respondents to the Exposure Draft requested that the Board*
8 *address "excess capacity" disallowances. Those disallowances relate to*
9 *part of the cost of service of a recently completed plant and are based on a*
10 *finding that the utility's reserve capacity exceeds an amount deemed to be*
11 *reasonable. If an "excess capacity" disallowance is ordered by a regulator*
12 *without specific finding that the enterprise should not have constructed that*
13 *capacity or should have delayed the construction of that capacity, the rate*
14 *order raises question about whether the enterprise meets the criteria for*
15 *application of Statement 71, in that it is not being regulated based on its own*
16 *cost of service. However, because such a rate order itself is neither a direct*
17 *disallowance nor an explicit, but indirect, disallowance of part of the cost of*
18 *the plant, this Statement does not specify the accounting for it. If an*
19 *"excess capacity" disallowance if ordered by a regulator with a specific*
20 *finding that the enterprise should not have constructed that capacity or*
21 *should have delayed the construction of that capacity, the rate order may be*
22 *an explicit, but indirect, disallowance of part of the cost of the plant, and the*
23 *enterprise should account for the substance of that order as set forth in*
24 *paragraph 7 of this statement.*

25
26 Q. Therefore, if the Commission were to accept Staff's disallowance of a portion
27 of the Cedar Hills treatment plant, would the Company have to write the assets off the books?

28 A. No. According to paragraph no. 60 of FASB Financial Accounting Standards
29 No. 90, if the Commission orders the disallowance without a finding that the construction
30 should not have been completed or should have been delayed, then Statement No. 90 would
31 not apply and the Company would not be required to write the assets off it books.

32 Q. Does the Staff believe the construction of the Cedar Hill plant in question was
33 unreasonable or imprudent, or should not have been completed or the construction delayed?

1 A. No. The Staff is not contesting the prudence or timing of the construction of
2 the plant. Staff witness James Merciel's Rebuttal testimony filed in this rate proceeding states
3 the reasons for the Staff's proposed disallowance.

4 Q. Has the Staff removed Contributions in Aid of Construction (CIAC) that were
5 given to MAWC for the purposes of constructing the Cedar Hills plant from its
6 cost of service?

7 A. Yes. Staff removed \$491,820 from Contributions in Aid of Construction. This
8 amount was received by the Company from a developer and Northwest High School for the
9 construction of the addition to the Cedar Hill treatment plant.

10 **TANK PAINTING EXPENSE AND TRACKER**

11 Q. On page 3 of Company witness Weeks Rebuttal testimony he states that Staff's
12 Annualized expense for tank painting is \$1,084,842. Is this correct?

13 A. No, not entirely. The Staff has used a two year average of tank painting costs
14 that were completed in the calendar years 2008 and 2009 to arrive at an annualized amount of
15 \$1,362,620. Staff then subtracted from its annualized tank painting expense \$277,778, which
16 is the Staff's proposed annual amortization of the past tank painting tracker. As of
17 October 31, 2009, the tank painting tracker was a liability in the amount of \$833,333. Staff's
18 is proposing a three-year amortization of the tracker.

19 Q. Mr. Weeks states that one of the reasons a tracker mechanism is appropriate
20 for tank painting expense is that tank painting is a seasonal expense. Does Staff agree with
21 this statement?

22 A. No. In fact, the seasonality of tank painting expense can have a huge impact
23 on the tracker when the Company comes in for a rate case. For example, in this very case the

1 | tank painting tracker is a liability as of October 31, 2009. However, the Staff is aware that as
2 | of April 30, 2009, this tracker will be an asset. This shift in the tracker will impact the
3 | Company's cost of service.

4 | Q. If the Commission were to find a tank painting tracker was appropriate, does
5 | the Staff agree with the Company's proposed annual tracker level of \$1,600,000?

6 | A. No. If a tank painting tracker was deemed appropriate by this Commission, the
7 | Staff believes its annualized amount (before the tracker amortization) of \$1,362,620 should be
8 | the level used to set the tank painting tracker instead of the Company's level of \$1,600,000.

9 | Q. Why does the Staff believe the Company's level for the tank painting tracker
10 | is inappropriate?

11 | A. The Company has based their proposed amount upon the 2009 level of tank
12 | painting expense incurred. The Staff reviewed the past five years of tank painting expense
13 | when determining its annualized level of tank painting and found that a two year average of
14 | tank painting expense was an appropriate annual amount when compared to the costs incurred
15 | during the other years.

16 | Q. Does this conclude your surrebuttal testimony?

17 | A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

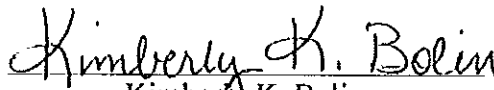
In the Matter of Missouri-American Water
Company's Request for Authority to
Implement a General Rate Increase for Water
and Sewer Services Provided in Missouri
Service Areas

Case No. WR-2010-0131

AFFIDAVIT OF KIMBERLY K. BOLIN

STATE OF MISSOURI)
)
COUNTY OF COLE) ss.

Kimberly K. Bolin, of lawful age, on her oath states: that she has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 8 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by her; that she has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of her knowledge and belief.


Kimberly K. Bolin

Subscribed and sworn to before me this 6th day of May, 2010.


Notary Public

