

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of Missouri-American Water)
Company's Request for Authority to Implement) Case No. WR-2008-0311
A General Rate Increase for Water and Sewer) SR-2008-0312
Service Provided in Missouri Service Areas.)

MAWC'S STATEMENTS OF POSITION

COMES NOW Missouri-American Water Company (MAWC or Company), and for its Statement of Position, states the following to the Missouri Public Service Commission (Commission) concerning the issues contained in the List of Issues, Order of Witnesses, Order of Cross-Examination and Order of Opening Statement, filed on October 21, 2008:

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I. REVENUE REQUIREMENT

A. Rate of Return Issues

Return on Common Equity: What return on common equity should be used for determining MAWC's rate of return?

MAWC Position: The authorized return on common equity used for determining MAWC's rate of return should be 11.25%. This figure is the midpoint in a range of business risk adjusted common equity cost rates of 11.075% to 11.425%, as determined by MAWC witness Pauline M. Ahern, CRRA. The range of common equity cost rates was established using the Discounted Cash Flow (DCF), the Risk Premium Model (RPM), the Capital Asset Pricing Model (CAPM) and the Comparable Earnings Model (CEM) cost of common equity models based upon the Efficient Market Hypothesis foundation of modern investment theory.

Ahern Dir., Reb. and Sur., all pages.

Capital Structure: What capital structure, MAWC stand alone or American Water consolidated, should be used for determining MAWC's rate of return?

MAWC Position: MAWC's stand-alone capital structure should be used for computing the Company's weighted average cost of capital. As of September 30, 2008, MAWC's actual stand-alone capital structure is comprised of 51.52% long-term debt, 1.26% short-term debt, 36% preferred stock and 46.86% common equity. The Commission should not use American Water's consolidated capital structure because MAWC is a separate corporate entity that issues its own debt and common stock, and therefore, maintains an independent capital structure. This independent, or stand-alone, capital structure represents the actual capital financing MAWC's jurisdictional

rate base to which the overall rate of return set in this proceeding will be applied. Also, MAWC's stand-alone capital structure is reasonable for ratemaking purposes based on it being consistent with the capital structure ratios maintained, on average, by other water companies.

Rungren Dir., Reb. and Sur., all pages.

B. Rate Base Issues

Cedar Hill Sand Creek Sewage Treatment Plant: Should the capital and depreciation expense costs associated with the capacity expansion project of Cedar Hill Sand Creek sewage treatment facility be disallowed for ratemaking in this proceeding?

MAWC Position: MAWC believes that prudently constructed facilities that are providing service to MAWC's customers should be included in MAWC's rate base such that MAWC is allowed to receive a return on and of (depreciation expense) its investment in that facility. The Cedar Hill Treatment Plant was prudently planned and constructed, is used and useful and satisfies MAWC's obligation to serve its customers. Staff agrees that the Cedar Hill Treatment plant was "prudently undertaken" and "necessary for future growth, which appeared imminent at the time the project was undertaken." Merciel Sur., p. 2.

However, Staff further suggests that \$2,179,907 of MAWC's investment in the treatment plant, district office, storage building and associated items should be reclassified in a non-earning asset account entitled "Plant Held for Future Use." If Staff's position is accepted, MAWC believes that generally accepted accounting principles will require it to recognize an almost \$2.2 million loss. Staff's recommendation would further result in a *negative rate base* for the Cedar Hill district.

In constructing capacity, MAWC is required by the Department of Natural Resources to consider both current and committed loads. MAWC's current and committed loads for the Cedar Hill district have already exceeded the capacity of the Cedar Hill Treatment Plant. Accordingly, while an "excess capacity" disallowance associated with the plant is being considered, DNR rules and regulations are pushing MAWC to begin planning the next expansion. MAWC should be allowed to include the existing Cedar Hill Treatment plant in rate base.

Dunn Reb., all pages; Williams Reb., pp. 2-5.

Cash Working Capital (Management Fee Lag): What is the appropriate amount to be included in MAWC's rate base for cash working capital as it relates to the management fees expense lag?

MAWC Position: Cash working capital is included in a company's rate base to compensate investors for "upfront" capital that is required in order to fund the daily operations of the business. The timing difference between incurring expenses and the receipt of the revenue will result in either a net (lead) or lag.

There is a difference between the parties in this case as to the appropriate lag for Service Company expenses to be used in the Lead/Lag Study. MAWC believes that the appropriate Service Company fee lag is a negative 2.65 days, as MAWC is billed in advance for services to be provided by the Service Company. This is similar to the PSC Fee Assessment that MAWC pays in advance to the Commission so that the Commission will have necessary funds available to operate and provide its services.

Bernsen Reb., pp. 2-4, Sch. TTB-1.

Rate Base for Security Deferral: Should the unamortized balance of deferred Security costs be included in rate base?

MAWC Position: In Commission Case No. WO-2002-273, the Commission authorized MAWC to defer certain costs associated with security measures instituted by MAWC in short order after September 11, 2001. The Company began to amortize the deferred expenses over a ten year period beginning in December of 2002.

The question for Commission decision is whether the unamortized balance should be given rate base treatment. The Commission has stated previously that this is a question that it may address on a case by case basis.

The subject expenditures were taken for the purpose of protecting MAWC's customers and the assets and the employees that serve them. Because MAWC is receiving recovery of its deferred costs over a ten year period, MAWC cannot receive a full recovery unless the unamortized amount is included in rate base such that MAWC will earn a return. Failure to provide rate base treatment ignores the time value of money.

Bernsen Reb., pp. 4-7; Bernsen Sur., pp. 1-6.

Accumulated Deferred Income Taxes Associated with the Security

AAO: Should accumulated deferred income taxes associated with the Security AAO be included as an offset to rate base? Does this change if the unamortized balance of the security AAO is not included in rate base?

MAWC Position: If the Commission determines that the unamortized balance of the Security AAO should not be included in rate base, then the accumulated deferred income taxes associated with the Security AAO should also not be included in rate base. The deferred tax liability is otherwise used to reduce the Company's rate base and essentially provide MAWC's customers with a return on these deferred taxes. It is neither fair nor reasonable to provide customers with a return on deferred taxes associated with an asset for which MAWC is not allowed to earn a return.

Bernsen Reb., pp. 4-7; Bernsen Sur., pp. 6-7.

C. Revenue Issues

Customer Water Usage Normalization (Usage per Customer per Day):

What is the appropriate method to use to normalize customer water usage?

MAWC Position: In order to properly calculate the Company’s revenue requirement, it is necessary to identify or calculate a “normal” level of customer usage for the test period. This normalized amount of usage per customer per day (UCD) is then multiplied by present rates to arrive at a normal level of test year revenues. The Company retained the services of Edward Spitznagel, Professor of Mathematics at Washington University, to perform a detailed statistical analysis of residential and commercial sales usages to arrive at a normalized level of usage per customer per day (UCD). Where Professor Spitznagel’s analysis showed there was a strong correlation between weather and usage, the Company used Professor Spitznagel’s weather normalization model to determine a normalized level of UCD. If there was no strong correlation between weather and usage, Professor Spitznagel analyzed historical information to see if there was a trend and, if so, the Company used a trend-line analysis. Staff, on the other hand, used a simple six year average. As a result, the Company and Staff disagree on the normalized level of sales for the following nine customer classes:

	<u>Company Method of Normalization</u>	<u>Staff Method of Normalization</u>
St. Louis Residential Quarterly	Weather Norm	6 yr average
St. Louis Commercial Quarterly	Weather Norm	6 yr average
St. Joseph Residential	Weather Norm	6 yr average
Joplin Residential	6 yr Trend	6 yr average

Joplin Commercial	Weather Norm	6 yr average
St. Charles Residential	Weather Norm	6 yr average
Jefferson City Commercial	6 yr Trend	6 yr average
Parkville Water Commercial	6 yr Trend	6 yr average
Warrensburg Commercial	6 yr Trend	6 yr average

The Company submits that its approach is statistically sound and, therefore, more accurately predicts a normalized level of UCD.

Grubb Dir., pp. 11-12; Grubb Reb., pp. 2-13, Sch. ELG-1; Grubb Sur., pp. 2-8; Spitznagel Dir., all pages; Spitznagel Reb., pp. 1-7; Spitznagel Sur., all pages.

Revenue Normalization (Weather): What is the appropriate weather-normalized revenue?

MAWC Position: As noted above, the Company retained Professor Spitznagel to perform a detailed weather normalization study for the St. Louis, St. Joseph, Joplin and St. Charles Districts, as these four districts represent over 91% of the total revenues of the Company. For five of the ten customer classes in these districts (as shown above), the appropriate weather normalized revenues are those that result from Professor Spitznagel's weather normalization model. Professor Spitznagel uses a multivariate model to predict customer usage which, among other things, considers temperature and cooling degree days which are strongly correlated with utilization. In addition, Professor Spitznagel's model takes into consideration soil moisture, as identified by the Palmer Drought Severity Index (PDSI), which is also strongly correlated with customer utilization. Professor Spitznagel has been using this model for developing weather normalized sales for the Company since its 2003 rate case. This model appropriately and accurately reflects the fact that variations in temperature and soil moisture lead to changes in water consumption. For example, more water will generally be used during

hotter and drier periods than will be used during cooler and wetter periods. The Company submits that Professor Spitznagel's weather normalization model is statistically sound and therefore superior in predicting normal usage than a six year average.

Grubb Dir., pp. 11-13; Grubb Reb., pp. 2-13, Sch. ELG-1; Grubb Sur, pp. 2-8; Spitznagel Dir., all pages; Spitznagel Reb., pp. 1-7; Spitznagel Sur., all pages.

Triumph Foods, LLC: Should an adjustment to revenues be made associated with the Special Service Contract rate paid by Triumph Foods, LLC in St. Joseph pursuant to the Economic Development Rider tariff?

MAWC Position: No. For purposes of this case, the Company included actual test year revenues it receives from Triumph Foods pursuant to the Special Service Contract rate approved by the Commission in Case No. WT-2004-0192. Public Counsel, in the rebuttal testimony of Barbara Meisenheimer, has proposed an adjustment to impute revenues that would have been received from Triumph Foods had this customer been paying for water service at the Industrial tariff rate. It appears from Ms. Meisenheimer's testimony, that she expects the Company to absorb this hypothetical revenue adjustment even though there's been no allegation of charging a wrong rate or other improper conduct on the Company's part.

First, such an adjustment should not be made in this case because Public Counsel has not properly raised the issue. The Company's Economic Development Rider tariff, on file with and approved by the Commission, requires the following:

“. . . that: (1) the Commission's Staff and the Office of Public Counsel have the right to request a Commission review of the continued appropriateness of the alternative rate set forth in the contract after the initial five years of the contract, with the purpose of such review being to determine whether the alternative rate continues to be in the best interest of all customers in the Company's service territory; (2) the Commission, acting on its own

volition, may also open an inquiry in this regard; (3) if, upon such review(s), the Commission finds that the contract, as implemented, no longer serves the public interest, it may allow the Company to continue providing service under the contract after adjusting the rate conditions to restore the interest of the Company's other customers in the service territory, or it may direct the Company to terminate the contract; and (4) the results of any review(s) conducted under these provisions shall be implemented in a general rate proceeding."

First, it is clear from the foregoing that the Special Service Contract rate is not reviewable until after the initial five years of the Contract. The Commission approved the Contract in an order issued in Case No. WT-2004-0192, effective November 25, 2004. Therefore, it is not clear that the Contract has been in effect for five years. Second, it is also clear that Public Counsel must request a "review" of the Contract. The mere filing of rebuttal testimony does not rise to the level of requesting a review. Third, neither Triumph Foods nor the City of St. Joseph was given notice of Public Counsel's assertion that the Contract is no longer in the public interest. These stakeholders, along with the Company, should be given a reasonable opportunity to fully inquire into and respond to the Public Counsel's position. Finally, if the Commission determines, after such a review, that the Contract no longer serves the public interest, its only two options are 1) to adjust the Contract rate to Triumph Foods to a level that restores the interest of the Company and other customers, or 2) to direct the Company to terminate the Contract. The remedy is not to impute revenues and punish the Company for charging a rate that has been approved by the Commission.

The fact of the matter, however, is that the Contract is in the public interest. The Contract rate is in excess of the Company's variable cost of producing water. Accordingly, as long as Triumph Foods pays rates which exceed the Company's variable cost to produce water, there is a revenue contribution to the Company's fixed

cost of providing service in the St. Joseph District. Stated another way, if the Company did not provide service to Triumph Foods under the existing Special Service Contract rate, all other things being equal, the cost of service, and therefore the rates, to all of the other customers would increase.

Grubb Reb., pp. 28-29; Grubb Sur., pp. 19-24; Herbert Sur., pp. 2-3.

AWR Compensation to MAWC: Does MAWC provide services to American Water Resources? If so, what amount of revenues for services provided to American Water Resources by MAWC should be used to determine MAWC's revenue requirement?

MAWC Position: MAWC has no association with American Water Resources (AWR) today other than they are both subsidiaries of American Water. MAWC has taken note of Staff's stated concerns in past cases and, as a result, has over time taken steps to prohibit the use of the MAWC name or logo on service line protection communications and to stop AWR's use of MAWC customer lists. MAWC provides no services to AWR.

If the Commission would decide that some level of revenue imputation is appropriate, revenue imputation should be no greater than the amount of revenue MAWC receives pursuant to its agreement to assist with the St. Louis County service line protection program. This is a third party agreement negotiated at arm's length. Pursuant to that agreement, MAWC receives one percent (1%) of the gross revenues collected by St. Louis County in exchange for providing billing and collections services, to include the use of MAWC's mailing list.

Grubb Reb., pp. 20-24.

D. Expense Issues

Pension/OPEB Methodology: How should pension and OPEB expense be treated for purposes of the revenue requirement and how should it be accounted for on a going forward basis?

MAWC Position: MAWC recommends the use of the “corridor” approach to the handling of the unrecognized gains and losses as utilized by SFAS 87 (pensions) and SFAS 106 (OPEBs). The corridor approach defines the minimum amount of the amortization of unrecognized gains and losses required during the year. The corridor is equal to ten percent of the greater of the projected benefits that a company is obligated to pay an employee after retirement or the market-related value of the assets in the pension or OPEB fund. Only the amount of gains and losses that exceed the corridor are required to be amortized during the year. The amount of gains and losses identified by the corridor is then amortized over the remaining life of the plan participants.

This approach will smooth out volatility in the calculations of pension and OPEB costs. This is important as one of the factors that drives the level of these costs is the impact actual return generated by the financial markets has on the plan’s asset values. MAWC believes that the added level of monitoring required by the Staff’s approach is unnecessary as the use of the corridor approach will allow costs to be properly recorded on the books.

Grubb Reb., pp. 13-17; Grubb Sur., pp. 12-13.

Amortization of Pension/OPEB Assets: What is the appropriate level of expense to be included in MAWC’s cost of service related to recovery of the regulatory asset created by the transition to accrual accounting for pensions and OPEBs?

MAWC Position: MAWC does not oppose the Staff’s recommendation that the current asset balance related to the deferral of OPEB costs for the St. Joseph and Joplin Districts be included in the cost of service. However, the Company opposes the

Staff's recommendation to exclude the amortization of the deferral of the OPEB costs for the St. Louis District. These excluded costs are consistent with the treatment and approval of the St. Joseph and Joplin deferrals.

Grubb Reb., pp. 16-17.

Insurance Other than Group: What is the appropriate level of expense to be included in MAWC's cost of service related to insurance other than group?

MAWC Position: This issue involves the appropriate amount or percentage of insurance expense (other than group health insurance) that should be allocated to expense versus capital. The Company agrees with Staff that workers compensation and auto liability insurance expense should be allocated between expense and capital based upon a payroll operation and maintenance (O&M) allocation factor because these two types of insurance have a significant correlation to the activity of the Company's labor force. Staff's O&M payroll factor allocates 57.46% to expense and 42.54% to capital. However, Company and Staff disagree regarding the appropriate capitalization factor for general liability and property insurance. These policies are not related to the activities of the Company's labor force and should not be allocated between capital and expense based upon a labor O&M allocation factor. For purposes of this case, the Company estimated that 90% of its liability claims relate to either main breaks or trip and fall accidents and that only 10% of claims was related to capital projects. When it became apparent that Company and Staff could not resolve their differences regarding this issue, the Company performed an analysis of claims under these policies for years 2005 through 2007. Based upon this review, the Company found that 96.38% of the claims were O&M related and only 3.62% were related to capital. Therefore, the

Company's proposed allocation of 90%/10% (expense/capital) for the general liability and property insurance coverage is conservative and ought to be adopted.

Petry Reb., pp. 6-7.

Tank Painting Expense: What is the appropriate level of expense to be included in MAWC's cost of service related to tank painting expense?

MAWC Position: The MAWC proposes to increase the tank painting tracker from its current level of \$1,000,000 to \$1,600,000 (in 2007 dollars). As explained in its testimony, the Company has conducted an analysis of its tank coating life expectancies and repainting costs. Based on this analysis, the MAWC determined the optimal value at which to set the tracker, i.e., that value that supports an average tank painting frequency that matches the average life expectancy of a tank's paint coating. This optimum level is \$1,600,000 (in 2007 dollars) or \$1,700,000 (in 2009 dollars). The Company described the actions it would undertake to complete tank painting at levels consistent with the proposed tracker increase. In support of the same, MAWC provided six fully executed tank painting contracts for 2009, which have a total expense value of \$1,673,245.67, not including taxes.

Kartmann Reb., pp. 1-6; Kartmann Sur., pp. 1-6.

Annual Incentive Program (AIP): What is the appropriate amount of costs associated with MAWC's incentive compensation plan that MAWC should recover from its customers?

MAWC Position: The appropriate amount of costs associated with MAWC's incentive compensation plan to be recovered in rates is \$731,647. The company's AIP benefits ratepayers by helping MAWC to attract and retain competent personnel, reduce expenses, maintain the financial health of the Company, improve customer service and increase operational efficiencies.

The financial element of the AIP incents employees to meet overall financial goals. This is beneficial to ratepayers because a financially sound company is better positioned to achieve its public service obligations in that it can raise capital at a lower cost, respond to changes in business conditions and meet the occasional challenges presented by emergency circumstances.

The Company's Annual Customer Satisfaction survey provides a statistically meaningful measure of customer sentiment regarding service quality.

Grubb Reb., pp. 17-20; Spitznagel Reb., pp. 7-8.

External Affairs: What is the appropriate level of expense to be included in MAWC's cost of service related to its external affairs department/employees?

MAWC Position: The Staff seeks to exclude costs associated with certain employees based on the mistaken premise that these costs are associated with lobbying activities. Specifically, Staff removed 1) Service Company Management Fees related to the services of the Director of Communications and External Affairs; 2) costs incurred by MAWC for the Department of the Manager of Government Affairs; and 3) 25% of the costs of the MAWC president's payroll and benefits. Staff's adjustment should be rejected. As the Company clearly explained in testimony, Staff's adjustment appears to stem from a misunderstanding of the true nature of the activities of these employees. MAWC provided detailed information pertaining to the job responsibilities of these employees, providing clear reasoning for why the proposed adjustment reducing MAWC revenue requirement by \$165,190 is inappropriate.

Williams Reb., pp. 18-26.

Fuel & Power/Chemicals/Purchased Water Due to Unaccounted-for Water: What is the appropriate level or percentage for Unaccounted for Water as it relates to fuel & power/chemicals/purchased water expenses?

MAWC Position: MAWC proposes to utilize the actual test year Non Revenue Water (NRW) level for each district. In its filing, MAWC applied each districts' test year NRW percent values to pro forma sales volumes to arrive at pro forma system delivery volumes and production expense levels.

In contrast, Staff calculated its pro forma water sales volume by district and then increased this amount by the lower of either the loss factor exhibited during the test year, or its 15 percent loss factor cap. Staff justified this adjustment by referencing “a general, but unwritten policy of the Commission Staff that utilities take corrective actions to control the amount of water losses in their systems and limit excess line loss to 15 percent, and that rate recovery of water losses be limited to a 15% loss factor.” This position is problematic on several levels. Indeed, Staff displays what appears to be a misunderstanding of Unaccounted For Water (UFW) and its relation to NRW. Further, in limiting recovery of lost water, Staff has failed to include an increase in recovery for the expense and capital investment cost of the additional active leakage control activity required to eliminate lost water volumes over the limits it has calculated. Finally, a much more appropriate water loss performance indicator is the Infrastructure Leakage Index (ILI) performance indicator, which is an output of the International Water Association/American Waterworks Association (IWA/AWWA) best practice water audit methodology developed during the period 1997 – 2000. This methodology is also recommended as a best management practice by the AWWA Water Loss Committee. The ILI method is a much more thoughtful and rigorous approach to evaluating real

losses from a distribution system because it makes evaluations based on the factors that are related to real losses, recognizing these factors differ from distribution system to distribution system.

Based on the ILI values for each of the Company's districts and the evaluation of those values in the context of the AWWA Water Loss Committee – Leakage Management Target-Setting Guidelines table, it is the Company's position that the test year, and therefore its pro forma, system delivery values in its filing represent acceptable and reasonable distribution system performance.

Kartmann Reb., pp.18-32.

Belleville Lab: What is the appropriate amount of costs to be included in MAWC's cost of service for its use of the Belleville Laboratory facility?

MAWC Position: The Belleville Lab is a water quality testing facility operated by American Water Works Service Company that performs sample testing for the American Water operating companies, to include MAWC.

Lab costs directly attributable to an operating company are directly charged to it. The indirect lab costs are allocated system-wide to each of the operating companies based on customer count. Surveys have found outside testing laboratories to be from 6% to 52% more expensive.

Use of customer counts for the allocation of indirect costs is preferable because they are much less variable than other factors and do not change dramatically from year to year on a system-wide basis. For example, an examination of the number of tests (the allocation factor recommended by Staff) conducted over the last five years reveals a significant variation from year to year in the number of tests conducted by the Belleville Lab.

Applying different methods from state to state would also provide a risk of non-recovery of expenses and either drive up costs or, in the alternative, encourage the use of outside labs whose costs, while higher, would be more likely to be recovered in total. Grubb Reb., pp. 24-28, Sch. EJG-2.

Fire Hydrant Painting: What is the appropriate level of expense, if any, to be included in MAWC's cost of service related to fire hydrant painting? Should a tracker be established to track costs incurred for fire hydrant painting?

MAWC Position: The Company has included a pro forma adjustment to its test-year filing of \$1,417,000 of expense representing the annual estimated cost of its proposed lead based paint abatement project. This project is designed to eliminate lead based paint (LBP) coatings existing on approximately 17,000 of the fire hydrants located in St. Louis County. Proper treatment of these hydrants necessitates that these fire hydrant paint coatings be completely removed and replaced with a new prime coat and finish coat of non-lead containing materials. Removing the lead based paint coat requires a relatively expensive process involving containment and disposal of the spent materials that is compliant with EPA and MDNR regulations. While MAWC's proposed lead based paint abatement project is a multi-year project, it involves a one-time process for each hydrant that once performed, allow that hydrant to be returned to the more conventional surface preparation and repainting processes. MAWC conducted pilot programs with contractors to develop a comprehensive assessment of the work and costs involved. Further, the Company executed a contract for the work with one of these contractors for this project.

MAWC proposed that, like the tank painting tracker, a hydrant painting tracker could be established thereby encouraging the Company to perform the work and

enabling Staff the opportunity to readily audit the Company's performance in completing this work. If the work is not completed in accordance with such a tracker, then appropriate action can be taken to balance rate recovery and actual expenses. MAWC's proposal is a fair mechanism to allow recovery of necessary costs, while insuring that customers will pay dollar for dollar only those costs actually incurred to remove lead based paint, prime and repaint hydrants.

Kartmann Reb., pp. 6-11; Kartmann Sur., pp. 6-14.

Dues, Donations and Contributions: What dues, donations or contributions should be included in MAWC's cost of service?

MAWC Position: MAWC believes that \$188,726 attributable to dues, donations or charitable contributions excluded by Staff is appropriate for inclusion in cost of service.

MAWC and its employees belong to professional and trade organizations that promote industry education, exchange of knowledge, training and economic development and whose programs improve employee knowledge, provide services to consumers or create opportunity for community betterment. The Company's participation in these organizations benefits MAWC customers in a number of ways.

MAWC's contributions to local organizations, charities and low-income programs are part of its commitment to the communities it serves. The level of contributions is reasonable and provides a direct benefit to persons in the Company's service territory. Its funding of the H₂O Help Program and the Children's Theatre Conservation Education Program are emblematic of the Company's commitment to assist low income customers and to educate the public about water conservation and proper management of watershed properties. Contributions such as these are normal cost of business and,

because regulation is intended to emulate a competitive market, a reasonable level of expense associated with such contributions should be included in the Company's cost of service.

Williams Reb., pp.10-18.

Advertising: What is the appropriate level of expense to be included in MAWC's cost of service?

MAWC Position: Advertising is a necessary and normal cost of doing business and a reasonable level of expense associated with this activity should be allowed in rates

Rate Case Expense: Should rate case expense be normalized or amortized and should prior rate case expense be recovered in this rate case? What is the appropriate level of rate case expense to be included in MAWC's cost of service?

MAWC Position: The Commission has previously found that a regulated utility is "entitled to recover its reasonable and prudently incurred cost of presenting this rate case to the Commission. Such costs are routinely accepted as a cost of doing business for which the company will be allowed to recover its costs in rates" *Missouri Gas Energy*, 12 Mo. PSC 3d 581, 623 (September 21, 2004). "Disallowing prudently incurred rate case expense can be viewed as violating the company's procedural rights." *In re St. Joseph Light & Power Company*, 2 Mo.P.S.C.3d 248, 260 (1993); *See also In re St. Joseph Light & Power Company*, 3 Mo.P.S.C.3d 207, 214 (1994).

MAWC has amortized the rate case expenses associated with its last rate case (Case No. WR-207-0216). By the end of February 2009, \$483,807 will remain unamortized and will represent rate case expenses that have not been recovered.

MAWC proposes to amortize this remaining balance over the next three years along with the expenses associated with this case.

Staff has proposed to instead use the rate case expenses associated with this case, divided by three years, in order to “normalize” rate case expenses on a going forward basis. Staff would make no provision for the unrecovered balance of rate case expenses, which would require MAWC to write off the unamortized amount.

The use of a three year “normalization” period would further deny MAWC recovery of a portion of its expenses from this case. Because MAWC continues in the process of replacing old infrastructure in order to provide quality customer service and to meet its obligation to serve, the most recent rate case cycle of approximately two years is not expected to lengthen. Accordingly, use of a three normalization will result in a “planned disallowance of approximately one-third of MAWC’s current costs.

Rate case expenses are easily measured and do not require estimation. Further it is difficult to predict the cost to develop, prepare and present a rate case as those costs may differ depending upon whether a settlement is reached or a hearing is held, with its requisite expert witnesses, uncertainty as to issues may be raised by the parties and legal briefs. For this reason, rate case expense is appropriate for amortization rather than normalization.

Williams Reb., pp. 5-10.

Property Tax: What is the appropriate level of property tax to be included in MAWC’s cost of service?

MAWC Position: Property tax should be trued up to reflect utility plant as of September 30, 2008. Failure to do this will ignore property taxes associated with the approximately \$133 million dollars of utility plant that have been placed into service

since December 31, 2007. MAWC will begin to incur actual property tax expenses associated with this additional plant on its books as of January, 2009.

Petry Reb., pp. 8-9.

Waste Disposal: What is the appropriate level of waste disposal expense to be included in MAWC's cost of service?

MAWC Position: MAWC believes that the waste disposal expense for the Warren County sewer system was improperly calculated because certain waste disposal costs were booked to a different account than that which was examined. Use of the accurate expenses would result in an increase in the waste disposal expense for this district.

Petry Reb., pp. 9-10.

Corporate Costs Allocations: What is the appropriate basis upon which to allocate MAWC Corporate Administrative and General Expenses to the various districts?

MAWC Position: The Company incurs corporate administrative and general expenses that are not directly attributable to a particular district and therefore these costs must be allocated to the districts on a reasonable basis. The primary purpose of allocating these corporate costs to each district is to assign those costs to the customers that receive the benefit from the incurrence of those costs. It is also important to use an allocator that is relatively stable over time and will not fluctuate greatly between rate cases. In this case, the Company has reviewed all of the corporate costs for the test year and determined that for the most part the number of customers served by each district (in relation to total customers) is still the most appropriate allocator that should be used. In fact, the Company is proposing to use the number of customers as an allocator for approximately 70% of its corporate

administrative and general expenses. Other costs that are allocated on a different basis include pension expense, which is allocated on payroll; OPEBs, which is allocated based on number of employees; and transportation expense, which is allocated based on number of vehicles. The number of customers has been (and continues to be) the primary allocator because the Company believes that most of the costs it incurs are for the direct benefit of the customers it serves. In addition, the number of customers served by each district does not fluctuate greatly over time and therefore has the additional benefit of being relatively stable. If the Commission, however, determines that another allocation factor(s) or method is appropriate, it is important that such allocation factor(s) be used for allocating expenses to all districts. In other words, the Commission should not use different factors to allocate corporate administrative and general expenses to different districts such that the Company would recover more or less than its total corporate administrative and general expense.

Grubb Dir., pp. 20-22, Sch. ELG-2 and Sch. ELG-3; Grubb Sur., pp. 8-10.

Management Fee – SOX Compliance: What is the appropriate level to be included in MAWC’s cost of service for SOX compliance costs allocated to MAWC from the Service Company through management fees?

MAWC Position: MAWC believes that one-time SOX compliance costs allocated to the Company should not be included in its revenue requirement.

Grubb Dir., pp. 15-16.

Management Fee – Labor Costs: What is the appropriate level to be included in MAWC’s cost of service for labor costs allocated to MAWC from the Service Company through management fees?

MAWC Position: MAWC’s revenue requirement should include \$416,384, related to wage increases for Service Company personnel.

Grubb Dir., p. 16.

Joplin True-up Issue: What items should be examined for the true-up audit? What is the appropriate true-up date? Instead of a true-up, should a fully adjusted test year be utilized?

MAWC Position: The true-up process allows the Commission to establish rates based upon the most current data available, while maintaining the proper balance of rate elements. The true-up process is a widely accepted tool that has been utilized in the state of Missouri for many years to accomplish the goal of establishing a reasonable expected level of earnings, expenses and investments at a time as close as possible to the period when the rates in question will be in effect.

The question as to the true-up date and whether some process other than the true-up should be utilized has been settled by the Commission's Order Regarding True-Up Date and Setting True-Up Procedural Schedule issued in this case on October 20, 2008. Therein, the Commission directed that the case be trued up through September 30, 2008, and set a procedural schedule for the filing of direct and rebuttal true-up testimony.

The remaining issue is what items should be examined in the true-up. MAWC's April 15, 2008 true-up request included a proposed package of revenue, expense and investment intended to maintain the proper matching of revenue, expense and rate base. Staff and the Company have agreed that tank painting expense, fire hydrant expense and waste disposal should be removed from this list. The item that remains in dispute is property tax, which will be addressed separately in the list of issues and in this Statement of Position.

Lastly, an adjustment should be made to address lease expense. Staff made an adjustment to test year levels of lease expense to remove all amounts associated with leases that showed an expiration date prior to the end of the update period. However, Staff has failed to reflect any costs of the new leases that MAWC has entered into to replace the expired leases. This situation should be corrected in the true-up.

Williams Sur., pp. 1-9.

Jefferson City Issue on Joint Task Force Case No. WO-2008-0167:

What rate impacts, if any, are being evaluated within the Task Force created by stipulation in Case No. WR-2007-0126?

MAWC Position: The Jefferson City Joint Task Force filed its Joint Report on October 20, 2008, in Case No. WO-2008-0167. MAWC believes that there is nothing for the Commission to decide in this case in regard to this issue.

II. RATE DESIGN/COST OF SERVICE

Inter-District Support or Revenue Contribution: Should or may any district provide a support so that another district may be provided service that is priced below that district's cost of service? If so, which district(s) should receive support and which district should be required to provide that support?

MAWC Position: Not only may one district provide support to another district but, given the facts in this case, it is clearly appropriate to do so. An inter-district revenue contribution in the setting of rates is appropriate as it addresses a number of goals including: 1) avoiding rate shock; 2) promoting gradualism toward cost-based rates; 3) promoting fairness; and 4) avoiding the impact of a drastic change in the existing rate structure. In the current case, the Company's proposal attempts to avoid rate shock and to gradually move towards cost-based rates for four (4) districts.

Specifically, the Company is proposing a revenue contribution for the Brunswick District, Parkville Water District, Cedar Hill Sewer District and Warren County Sewer District in the amounts of \$390,896, \$623,083, \$345,572, and \$669,187, respectively. The Company's proposal for this revenue contribution was based on its belief that the smaller districts should receive a revenue contribution if their percentage rate increase, on a purely district specific basis, was significantly above the overall percentage rate increase for the Company. For example, if the revenue contribution is not permitted, then the increases for those four districts would be 217.7% (Brunswick), 46.24% (Parkville Water), 156.8% (Cedar Hill Sewer) and 526.7% (Warren County Sewer), based on Company's filed case. The Company's proposed revenue contribution would limit the percent increases for these four districts to 29.7%.

The Company proposes that this contribution come from the St. Louis Metro District as that is the largest district and the impact of such revenue contribution on that district would be minimal. For example, the average impact per day for the 167 Rate J (i.e., Industrial) customers is \$1.53. The average impact of the revenue contribution per day for the 17,900 customers of Jefferson County Water Districts No. 1, 3 and 10 is one-half a penny a day. For the Rate A (i.e., Residential) customers in St. Louis County, the impact would be a penny per day for a customer using 24,000 gallons of water per quarter. Thus, the size of the St. Louis Metro District allows this revenue contribution to be spread over a much larger customer base.

Grubb Dir., pp. 27-28; Grubb Reb., pp. 30-32; Grubb Sur., pp. 13-14.

St. Louis Metro District: Should the St. Louis County, St. Charles, and/or Warren County water districts be combined?

MAWC Position: Yes. In this case, the Company is proposing to merge the rates for the existing St. Louis County, St. Charles and Warren County Water Districts to reflect the fact that these three systems are either physically connected or are integrated from an operational and management perspective. For example, the St. Louis County and St. Charles systems are physically interconnected and, as a result, the St. Louis County District provides nearly 100% of the water to the St. Charles District. The Warren County Water system, while not physically connected to either the St. Charles or St. Louis County systems, is nevertheless operated and managed by the St. Charles and St. Louis County employees. The Warren County Water District's relative small size should also be a consideration in the decision process. Warren County has but one-tenth of 1% of the total customer base of the St. Louis County and St. Charles Districts and merging it with those two districts will have a negligible effect on the rates in those districts. If the Warren County District is not included in the St. Louis Metro District, MAWC believes Warren County should receive inter-district support or revenue contribution similar to those districts discussed in the preceding issue.

Grubb Dir., pp. 26-27; Grubb Sur., pp. 14-15.

Allocations: What is the appropriate basis upon which to allocate costs to each customer class?

MAWC Position: The Company retained the services of Paul Herbert, President of the Valuation and Rate Division of Gannett Fleming, Inc., to perform a class cost of service (CCOS) study for this case. The purpose of the CCOS study is to allocate the district specific cost of service to each of the customer classes in those operating districts. In Mr. Herbert's CCOS study, the district specific costs were allocated to the

residential, commercial, industrial, other public authorities, sales for resale, private fire protection and public fire protection customer classes in accordance with the Base-Extra Capacity Method, as described in the 2000 and prior Water Rates Manuals published by the American Water Works Association (AWWA). The Base-Extra Capacity Method is a recognized method for allocating the costs of providing water service to customer classifications in proportion to the classifications' use of the commodity, facilities and services. It is generally accepted as a sound method for allocating the cost of water service and has been used by the Company in previous cases. Mr. Herbert's CCOS Study results in indications of the relative cost responsibilities of each class of customers in each operating district. The allocated cost of service is one of several criteria appropriate for consideration in designing customer rates to produce the required revenues. Other criteria to consider in designing rules include the impact of changes from the present rate structure, the understandability and ease of application of the rate structure, community and social influences and the value of service.

Grubb Dir., pp. 25-26; Herbert Dir., all pages, Sch. PRH-1.

A. Should there be a small mains adjustment?

MAWC Position: Yes. Mr. Herbert in performing his CCOS Study modified the allocation of costs associated with distribution mains to exclude consumption for certain large customers connected primarily to large mains (commonly referred to as transmission mains). Mr. Herbert made this "small mains adjustment" in the Joplin, St. Joseph and the St. Louis Metro Area Districts to reflect the fact that many of the large users in those districts are served primarily from large transmission mains (generally

larger than ten inch) and, thus, do not benefit from the smaller mains in the distribution system. In larger systems, large users (such as industrial and sales for resale customers) are located on transmission mains and take water from those mains before it reaches the distribution system. Mr. Herbert's study recognizes this fact and excludes certain large users from the allocation of costs associated with small mains.

Conversely, by not employing a small mains adjustment, higher costs will be allocated to industrial and sales for resale customers in these districts. This will unfairly allocate costs to these large customers, will have an adverse impact on industry in these districts and will make it more difficult for the Company to meet competitive pressures.

Herbert Dir., pp. 9-10; Herbert Reb., pp. 6-8; Herbert Sur., pp. 3-4.

B. What is the appropriate basis upon which to allocate purchase power expense?

MAWC Position: For purposes of his CCOS Study, Mr. Herbert allocates the demand charge portion of the Company's electric bills (i.e., purchase power expense) on his factor No. 1, which is based on average daily sales. MIEC witness Michael Gorman suggests that the demand charge portion of the Company's electric bills be allocated on an extra capacity basis using factor No. 6. The result of MIEC's proposal would be to allocate less purchase power costs to the Rate J (i.e., Industrial) customers and more to the remaining classes of customers. While Company agrees with the concept of this proposal, it does not agree to the extent proposed by MIEC. Mr. Herbert analyzed a sample of the Company's power bills in the St. Louis District and determined that the bills include a monthly demand charge regardless of the level of service. Therefore, Mr. Herbert would support a refinement to his cost allocation that would

allocate 9.3% of purchase power costs to the extra capacity function. However, this refinement results in a very minor revision. For example, the result of allocating 9.3% of the power costs, on an extra capacity basis, reduces the industrial class cost of service by \$19,234, or about one-quarter of 1% of the total Rate J costs.

Herbert Reb., pp. 3-4.

Rates:

A. Commodity Charge

i) Should the commodity charge be set as a declining block rate or should the commodity charge be uniform for all levels of usage?

MAWC Position: The Company is proposing single or uniform block rates for residential customers and declining block rates for non-residential classes of customers. Declining block rates allow for larger customers, who generally experience better load factors, to pay a lower tail block rate to reflect the lower cost to serve them. The basic idea behind a declining block rate structure is that large customers will pay for all the extra capacity costs in the initial blocks which allows for the payment of the lower, base costs in the tail block. This is an appropriate rate design and justified from a cost standpoint because larger customers, with more favorable load factors, will pay less per unit as their volumes increase.

Herbert Dir., pp.13-14; Herbert Reb., p. 13; Herbert Sur., pp. 12-13.

ii) Should commodity rates be uniform across all classes in a district?

MAWC Position: No. While the Company has proposed a single block for the residential class, it does not believe that a single or uniform block is appropriate for other classes of service as discussed in Issue Ai) above.

Herbert Reb., pp. 13.

B. Customer Charge

i) What is the appropriate way to establish the customer charge?

MAWC Position: An appropriate customer charge is one that recovers the “fixed” cost of providing service, before any commodity (i.e., water) is provided. In Mr. Herbert’s CCOS Study, he allocates the costs related to meters, services and customer billing and collecting (which also includes meter reading) to the customer charge.

These costs are then divided by the number of meters or service equivalents or the number of customers and then divided by twelve (12) to determine the monthly customer charge for a 5/8 inch meter. This is consistent with the AWWA Rates Manual. Herbert Dir., pp. 12-13; Herbert Sur., p. 7.

ii) Should the customer charge be uniform across the districts?

MAWC Position: The Company has proposed a uniform \$13.00 per month customer charge for 5/8 inch meters in all districts except for St. Louis Metro District. In the St. Louis Metro District, the Company has proposed a \$10.00 per month customer charge. Uniform customer charges are supported from a cost and administrative standpoint. Uniform customer charges make sense because all customers have a service line and meter. All customers have their meter read each month (except for St. Louis County quarterly billed customers) and are billed from a common billing center.

Furthermore, common customer charges are easier to administer and explain to customers.

Herbert Dir., pp. 12-13; Herbert Reb., pp. 12-13; Herbert Sur., pp. 7-8.

iii) Should the customer charge include some amount of usage?

MAWC Position: No. The customer charge should only reflect the fixed costs of providing service not any costs related to the cost of providing the commodity (i.e., water). The CCOS Study conducted by Mr. Herbert and the customer charges proposed therein are consistent with the AWWA cost of service and rate design principles and are consistent with methods used to determine customer charges in prior cases. If a certain amount of water consumption is to be included in the customer charge, then the variable costs associated with providing that water will also have to be included in the customer charge in order to properly reflect the fixed charges of providing service as well as the variable costs associated with the provision of the commodity.

Herbert Sur., p. 9.

Class Identification/Cost of Service: What is the appropriate way in which to identify the customer classes?

MAWC Position: Appropriate customer classes are identified in the AWWA Water Rates Manual and include residential, commercial, industrial, resale and fire protection customer classes. The Company classifies customers into these categories based on the characteristics of the customer. This is a common practice in the water industry and consistent with the AWWA Rates Manual.

Grubb Reb., pp. 29-30; Herbert Reb., pp. 10-11; Herbert Sur., pp. 12-13.

Phase-in:

(A) Is a phase-in of rates appropriate or lawful?

MAWC Position: No. A phase-in of rates is neither lawful nor appropriate.

First, there is no statutory authority for the Commission to mandate the phase-in of a rate increase without the agreement of the water utility. The only express authority which allows the Commission to authorize a rate increase which is less than the full amount of a utility's revenue deficiency is found in Section 393.155 RSMo, which only applies to electrical corporations. Thus, there is no express statutory authority for the Commission to phase-in rates for a water utility, such as MAWC.

In addition, the phase-in of rates is neither appropriate nor necessary. The only party that has proposed a phase-in in this case is Joplin. While the proposed percent of increase is relatively high for the Joplin District, the resulting rates for water service are not out of line with rates being paid by other districts. For example, taking into account last year's rate increase as well as the Company's present proposal, Joplin's average residential rate (for 5500 gallons of water) will still be in the lower half of comparable residential rates for all of the Company's other districts.

Joplin's specific phase-in plan is also technically flawed and unfair. The Joplin proposal is not designed to make the Company whole. Even though Joplin recognizes that the Company should be allowed to earn a return on that portion of revenue increase that is deferred, its actual proposal does not accomplish that goal. Instead, it is a give-back plan where Company shareholders are required to forego a considerable portion of earnings that they would otherwise be entitled to. Even after correcting for the technical flaws in Joplin's proposal and making the Company whole, the rates paid

by Joplin customers over the term of the phase-in plan will be higher than had no phase-in been implemented. This is because customers will be required to pay carrying costs associated with deferring the rate increase.

There are also serious accounting issues associated with a phase-in. The Company is concerned whether a regulatory asset could be established under the type of phase-in plan proposed by Joplin. If not, there would be an annual negative impact on the Company's current year earnings. Additionally, the Company faces uncertainty as to whether a phase-in plan would comply with generally accepted accounting principles. If not, the financial impact of a phase-in plan would be more egregious. Finally, there is the very real problem regarding cash flow. A phase-in proposal as suggested by Joplin obviously restricts cash flow. Declining cash flows, especially in these times of tight cash markets, would negatively impact the Company's financial capabilities.

Williams Reb., pp. 9-16.

(B) Which, if any, districts should have their rate increase phased in?

MAWC Position: As indicated in Section (A) above, a mandatory phase-in is neither lawful nor appropriate.

(C) How should any carrying cost associated with a phase-in deferral be recovered and from whom?

MAWC Position: As indicated in Section (A) above, a mandatory phase-in is neither lawful nor appropriate.

MSD Rate: What is the appropriate rate to charge MSD for customer usage information?

MAWC Position: Company is proposing no change in the existing tariff which sets the compensation to be paid by the St. Louis Metropolitan Sewer District (MSD) for certain billing and usage data which it needs to bill its customers for sewer service. The existing tariff rate was the product of a Stipulation in the Company's last case. In addition, as part of that Stipulation, the Company agreed to conduct an incremental cost study for providing the billing data to MSD. The Company completed such a study and attached it as a proprietary Schedule (EJG-4) to the direct testimony of Edward Grubb. This cost study not only identified the incremental cost of providing water usage and customer identification data to MSD (which is significantly less than the tariff rate) it also calculated an allocation of operating costs between MAWC and MSD on the basis of which utility (MAWC and MSD) directly benefits from the data (which is significantly higher than the existing rate). The existing rate (i.e., \$350,000 per year) is roughly half way between the incremental costs and the fully allocated operating costs identified in the study. While MSD does not necessarily agree with the results of the Company's cost study, it nevertheless determined that for purposes of this case it did not want to expend the resources and incur the costs in challenging the existing rate. Therefore, it entered into a nonunanimous Stipulation with the Company to maintain the existing tariff rate or status quo. The Company believes that this is a reasonable result and the nonunanimous Stipulation should be accepted by the Commission. If the Commission, however, determines that MSD should pay a different rate for this information, then the revenue requirement for the rest of the St. Louis County District (and the rates to be paid by other customers in that district) must be adjusted accordingly.

Grubb Dir., pp. 22-25; Grubb Sur., pp. 15-17.

Allocation of Costs to Contract Sales Customers: What, if any, adjustment should be made to the Class Cost of Service Studies associated with contract sales?

MAWC Position: In Mr. Herbert's CCOS Study, he excluded the volumes associated with contract sales and deducted the contract sales revenue from the cost of service from all customer classes in proportion to the result of each classes' cost of service. (Contract customers include Triumph Foods in the St. Joseph District and Rate G and H customers in the St. Louis Metro District). This adjustment recognizes that contract customers have been retained on the system to the benefit of the remaining tariff customers and should offset the cost of service in proportion to each customer classes' cost of service. It is the Company's understanding that Staff and Public Counsel did not make this refinement in their CCOS Studies and, as a result, they effectively allocate the entire difference between the cost allocated to the contract customers and the actual contract revenue to the remaining customers in that customer classification rather than to all customer classes.

Herbert Reb., pp. 8-9.

Revenue Imputation: If a Triumph Foods revenue imputation is approved, how should the imputation be treated in offsetting costs to determine class revenue requirements?

MAWC Position: If the Commission determines that the Special Service Contract rate paid by Triumph Foods is no longer in the best interest of all customers in St. Joseph, then, according to the Economic Development Rider tariff, the Commission has one of two options: It may either adjust the rate to be paid by Triumph Foods or direct the Company to terminate the contract. There is no provision for a revenue imputation and such a remedy would unfairly and unlawfully penalize the Company.

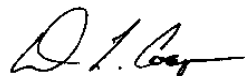
Grubb Sur., pp. 17-24.

City of Riverside Services Issue: Should the Parkville rate be reduced due to inadequate water service in the City of Riverside?

MAWC Position: No. The water service provided to the City of Riverside meets all state and federal quality of service requirements. There is no evidence of any inadequate water service in the City of Riverside. The City of Riverside's attempt to inject this issue into the proceeding is untimely and denies the Company the ability to engage in discovery and present meaningful rebuttal. The Company will also address this in its objection to the City of Riverside's Motion for Leave to File Testimony Out of Time.

WHEREFORE, MAWC respectfully requests that the Commission consider these statements of position.

Respectfully submitted,



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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been sent by electronic mail this 23rd day of October, 2008, to:

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