Exhibit No.:	
Issues:	Labor and Labor Related Expenses, Support Services, Production Costs, and Other Operating Expense
Witness:	Nikole L. Bowen
Exhibit Type:	Rebuttal-Revenue Requirement
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2017-0285 SR-2017-0286
Date:	January 17, 2018

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2017-0285
CASE NO. SR-2017-0286

REBUTTAL TESTIMONY
REVENUE REQUIREMENT

OF

NIKOLE L. BOWEN

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

IN THE MATTER OF MISSOURI-AMERICAN WATER COMPANY FOR AUTHORITY TO FILE TARIFFS REFLECTING INCREASED RATES FOR WATER AND SEWER SERVICE	)))))	**CASE NO. WR-2017-0285** **CASE NO. SR-2017-0286**

AFFIDAVIT OF NIKOLE L. BOWEN

Nikole L. Bowen, being first duly sworn, deposes and says that she is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony Revenue Requirement of Nikole L. Bowen"; that said testimony was prepared by her and/or under her direction and supervision; that if inquiries were made as to the facts in said testimony, she would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of her knowledge.

Nikole L. Bowen

Nikole L. Bowen

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
Before me this 16th day of January 2018.

Mary Beth Hercules
Notary Public

My commission expires:

MARY BETH HERCULES
Notary Public - Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires April 26, 2020
Commission # 96546828

REBUTTAL TESTIMONY
REVENUE REQUIREMENT
NIKOLE L. BOWEN
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2017-0285
CASE NO. SR-2017-0286

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REBUTTAL TESTIMONY
REVENUE REQUIREMENT

NIKOLE L. BOWEN

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Nikole L. Bowen and my business address is 727 Craig Road, St. Louis, Missouri 63141.

Q. Are you the same Nikole L. Bowen who previously submitted direct testimony in this proceeding?

A. Yes.

II. OVERVIEW

Q. What is the purpose of your revenue requirement rebuttal testimony in this proceeding?

A. The purpose of my revenue requirement rebuttal testimony is to address certain aspects of the Missouri Public Service Commission ("Commission") Staff Report – Cost of Service ("COS Report") and other interveners' testimony, regarding labor and labor related expense, support services, performance based compensation, production costs and other operating expenses.

Q. Please address the issues regarding future test year.

A. Unlike Missouri-American Water Company ("MAWC", "Missouri-American" or the "Company"), the Commission Staff did not use a future test year calculation in its direct case. Therefore, my rebuttal testimony will address the methodologies used by the

Staff to calculate various operating expenses, rather than attempt to reconcile the differences between the Staff's and Company's direct cases. Missouri-American witness James Jenkins further supports the use of a future test year and addresses concerns raised by Staff and interveners regarding the future test year in his revenue requirement rebuttal testimony.

III. LABOR AND LABOR RELATED EXPENSES

Q. Do witnesses from Staff and interveners address the Company's labor and labor related expenses?

A. Yes. Staff witness Jennifer Grisham outlines Staff's labor and labor related expense adjustment in the Staff COS Report. In, addition, MIEC witness Meyer also addresses staffing levels in his direct testimony. MAWC witness Andrew Clarkson addresses Mr. Meyer's testimony regarding staffing levels. My rebuttal will focus on the labor related expense calculated by Staff. Staff's labor and labor related expense was based on the test year amounts ending December 31, 2016, and adjusted for wage increases, and changes in employee levels through June 30, 2017. In addition, Staff applied an overtime adjustment, based on a three year average calculation by District. The expense was applied against the capitalization rate, calculated based on labor dollars for the period ended June 30, 2017 by district. Portions of specific employee salaries and related expenses associated with lobbying were also removed. Finally, Staff did not include 50% of the Company's Annual Performance Plan ("APP") costs or any of the Company's Long-Term Performance Plan ("LTPP") costs.

Q. Do you agree with Staff's recommended labor and labor related expense?

A. No. The Company does not agree with Staff's labor and labor related expense calculation in the following ways:

1) it uses the Company's staffing level as of June 30, 2017;

2) it uses 2,080 hours to calculate base wage expense for hourly employees;

3) it categorizes certain costs as lobbying and disallows a portion of wages for specific positions;

4) it did not include 50% of the cost incurred by MAWC for its APP or any of the expense for its LTPP (this will be addressed separately under Section V. Performance Based Compensation); and,

5) it did not include the portion of the expense related to the Employee Stock Purchase Plan ("ESPP").

In addition, the Company provides additional information to support more current capital and operations and maintenance ("O&M") percentages. I address each of these items separately below.

Q. Do you agree with the staffing level used by Staff in its labor and labor related expense calculation?

A. No. Staff's labor and labor related expense was calculated based on filled positions and salaries in effect as of June 30, 2017, resulting in a calculation of labor and labor related expenses based on 662 positions. Using more current information, however, as of December 31, 2017 (which the Commission has identified as a true-up date), Missouri-American had 694 full time equivalent ("FTE") employees. Furthermore, as noted in Andrew Clarkson's rebuttal testimony, one additional FTE is scheduled to begin work on January 24, 2018 and an offer has been made to fill a position in the engineering department to complete the full complement of 696 FTEs proposed by the Company in this case. In addition, the number of positions used by Staff does not include any of the 12 temporary summer positions employed by the Company during 2017. As Mr. Clarkson testifies, the Company has employed these temporary/seasonal workers in the past and MAWC plans to continue to employ the same number during the summer going forward. As such, it is reasonable to include MAWC's full complement of employee staffing levels of 696 employees, plus expenses for the 12 temporary summer workers, in the Company's labor and labor related expense. Please refer to the rebuttal testimony of Missouri-American witness, Andrew Clarkson for the operational support for the Company staffing levels.

Q. Please explain why Staff's use of 2,080 hours to calculate base wage expense for hourly employees is inappropriate.

A. The number of work hours in a twelve month period can vary from 2,080 to 2,096 work hours. Any twelve month period that begins on a Saturday or Sunday will have 2,080 work hours, with the exception of a leap year, which will have 2,088 hours. Any twelve month period that begins on a Monday through Friday will have 2,088 work hours, except the leap year, which will have 2,096. The table below provides an analysis of the work days and hours for 2017-2021.

2017 Work Days/Hours													
Month	January	February	March	April	May	June	July	August	September	October	November	December	Total
Work Days	22	20	23	20	23	22	21	23	21	22	22	21	260
Hours	176	160	184	160	184	176	168	184	168	176	176	168	2,080

2018 Work Days/Hours													
Month	January	February	March	April	May	June	July	August	September	October	November	December	Total
Work Days	23	20	22	21	23	21	22	23	20	23	22	21	261
Hours	184	160	176	168	184	168	176	184	160	184	176	168	2,088

2019 Work Days/Hours													
Month	January	February	March	April	May	June	July	August	September	October	November	December	Total
Work Days	23	20	21	22	23	20	23	22	21	23	21	22	261
Hours	184	160	168	176	184	160	184	176	168	184	168	176	2,088

2020 Work Days/Hours													
Month	January	February	March	April	May	June	July	August	September	October	November	December	Total
Work Days	23	20	22	22	21	22	23	21	22	22	21	23	262
Hours	184	160	176	176	168	176	184	168	176	176	168	184	2,096

2021 Work Days/Hours													
Month	January	February	March	April	May	June	July	August	September	October	November	December	Total
Work Days	21	20	23	22	21	22	22	22	22	21	22	23	261
Hours	168	160	184	176	168	176	176	176	176	168	176	184	2,088

The table shows the number of work hours in a calendar year, averaged over the five year period shown is 2,088. This analysis demonstrates why the Company used 2,088 hours to calculate base wages for hourly employees and supports the calculation used by the Company in developing labor and labor related expenses.

Q. Please address Staff's disallowance of a portion of labor and labor related expense it categorizes as lobbying.

A. Staff eliminated a certain percentage of various MAWC and Service Company employees' salaries and associated benefits from its labor and labor related expense calculation. Staff's COS Report does not provide any explanation or support for the percentage of salaries and associated benefits removed for any particular employee other than to say the adjustment relates to lobbying activities. The COS Report doesn't even identify the percentage of salaries and benefits removed for each particular employee. Nevertheless, by reviewing Staff's workpapers, MAWC was able to determine that while Staff claims to recommend disallowance of a percentage of seven employees, it actually removed a percentage of 10 employees' salaries and associated benefits. I will address the Missouri-American employees here. Service Company will be addressed later in my testimony.

Q. What Missouri-American positions were impacted by Staff's proposed disallowance?

A. Staff's workpaper indicates that Staff seeks to disallow 25% of the salary and associated benefits of MAWC's State President, 10% of the salaries and associated benefits of the two Managers of External Affairs, the Director Corporate Counsel, and the Manager of Government Relations, and 75% of the salary and benefits of the Director of Government Relations. Staff makes these adjustments without out providing any explanation for doing so.

Q. Please address the Staff's proposed disallowance of 25% of MAWC's President salary and benefits.

A. As MAWC President, Cheryl Norton, states in her direct testimony (page 2), her key responsibilities are establishing and maintaining standards of service, directing priorities for investment in the system, revenue generation and protection, establishing controls to accomplish delivery of operating and maintenance budgets, and ensuring the safety and integrity of the systems for the protection of the customers, employees and operations. None of these key responsibilities falls within the definition of lobbying activities.

Q. Please address the Staff's proposed disallowance of 10% of MAWC's Managers of External Affairs and Director Corporate Counsel salaries and benefits.

A. The key responsibilities of the Managers of External Affairs are to provide senior level communication counsel to the state president and the state senior management team and develop, coordinate, implement and manage all of the Company's external communication activities. This includes communicating with all of the Company's stakeholders, including customers, community leaders and regulators. Communicating with stakeholders does not constitute lobbying. The key responsibilities of the Director Corporate Counsel are to provide legal counsel and representation to the leadership team on a variety of legal risk and opportunities and other business matters. This, too, may including interacting with the Company's stakeholders, including customers, community leaders and regulators. It is unclear how any such activities would constitute lobbying. They do not. Staff has failed to provide any support that justifies disallowing any portion of the salaries and associated benefits for any of these positions.

Q. Is there an objective definition of lobbying the Commission can consider in evaluating whether work performed should be categorized as lobbying?

A. Yes. Section 105.470, of the Missouri Revised Statutes, clearly outlines the requirements for registration as a lobbyist, and defines the specific activities that shall be considered, and not considered, as lobbying. According to the Code, there are four categorizations for lobbying:

> (1) "Elected local government official lobbyist", any natural person employed specifically for the purpose of attempting to influence any action by a local government

official elected in a county, city, town, or village with an annual operating budget of over ten million dollars;

(2) "Executive lobbyist", any natural person who acts for the purpose of attempting to influence any action by the executive branch of government or by any elected or appointed official, employee, department, division agency or board or commission thereof and in connection with such activity meets the requirements of any one or more of the following:

a) Is acting in the ordinary course of employment on behalf of or for the benefit of such person's employer; or
b) Is engaged for pay or for any valuable consideration for the purpose of performing such activity; or
c) Is designated to act as a lobbyist by any person, business entity, governmental entity, religious organization, nonprofit corporation, association or other entity; or
d) Makes total expenditures of fifty dollars or more during the twelvemonth period beginning January first and ending December thirty-first for the benefit of one or more public officials or one or more employees of the executive branch of state government in connection with such activity.

(3) "Judicial lobbyist", any natural person who acts for the purpose of attempting to influence any purchasing decision by the judicial branch of government or by any elected or appointed official or any employee thereof and in connection with such activity, meets the requirements of anyone or more of the following:

a) Is acting in the ordinary course of employment which primary purpose is to influence the judiciary in its purchasing decisions on a regular basis on behalf of or for the benefit of such person's employer, except that this shall not apply to any person who engages in lobbying on an occasional basis only and not as a regular pattern of conduct; or

b) Is engaged for pay or for any valuable consideration for the purpose of performing such activity; or

c) Is designated to act as a lobbyist by any person, business entity, governmental entity, religious organization, nonprofit corporation or association; or

d) Makes total expenditures of fifty dollars or more during the twelve-month period beginning January first and ending December thirty-first for the benefit of one or more public officials or one or more employees of the judicial branch of state government in connection with attempting to influence such purchasing decisions by the judiciary.

(4) "Legislative lobbyist", any natural person who acts for the purpose of attempting to influence the taking, passage, amendment, delay or defeat of any official action on any bill, resolution, amendment, nomination, appointment, report or any other action or any other matter pending or proposed in a legislative committee in either house of the general assembly, or in any matter which may be the subject of action by the general assembly and in connection with such activity, meets the requirements of any one or more of the following:

a) Is acting in the ordinary course of employment, which primary purpose is to influence legislation on a regular basis, on behalf of or for the benefit of such person's employer, except that this shall not apply to any person who engages in lobbying on an occasional basis only and not as a regular pattern of conduct; or

b) Is engaged for pay or for any valuable consideration for the purpose of performing such activity; or

c) Is designated to act as a lobbyist by any person, business entity, governmental entity, religious organization, nonprofit corporation, association or other entity; or

d) Makes total expenditures of fifty dollars or more during the twelve-month period beginning January first and ending December thirty-first for the benefit of one or more public officials or one or more employees of the legislative branch of state government in connection with such activity.

The code also clearly states that a Judicial lobbyist,

> shall not include a member of the general assembly, an elected state official, or any other person solely due to such person's participation in any of the following activities:
>
> a) Appearing or inquiring in regard to a complaint, citation, summons, adversary proceeding, or contested case before a state court;
>
> b) Participating in public hearings or public proceedings on rules, grants, or other matters;
>
> c) Responding to any request for information made by any judge or employee of the judicial branch of government;
>
> d) Preparing, distributing or publication of an editorial, a newsletter, newspaper, magazine, radio or television broadcast, or similar news medium, whether print or electronic; or
>
> e) Acting within the scope of employment by the general assembly, or acting within the scope of employment by the executive branch of government when acting with respect to the department, division, board, commission, agency or elected state officer by which such person is employed, or with respect to any duty or authority imposed by law to perform any action in conjunction with any other public official or state employee;

The code also clearly states that a Legislative lobbyist,

> shall not include a member of the general assembly, an elected state official, or any other person solely due to such person's participation in any of the following activities:
>
> a) Responding to any request for information made by any public official or employee of the legislative branch of government;
>
> b) Preparing or publication of an editorial, a newsletter, newspaper, magazine, radio or television broadcast, or similar news medium, whether print or electronic;
>
> c) Acting within the scope of employment of the legislative branch of government when acting with respect to the general assembly or any member thereof;
>
> d) Testifying as a witness before the general assembly or any committee thereof;"

The State President, Managers of External Affairs and the Director Corporate Counsel are not registered lobbyists and do not participate in lobbying activities. Further, Staff has not demonstrated that any of their job responsibilities fall within any of the activities identified in the Code.

Q. Please address the Staff's proposed disallowance of 10% of MAWC's Manager of Government Relations salary and benefits.

A. In regard to this position, Staff ignores the information provided to it in proposing a 10% disallowance. During discovery, Staff requested details regarding lobbying activities for the Company's registered lobbyists, which includes the Manager of Government Relations. In response to MoPSC 0095, the Company provided a detailed log of lobbying activities that shows this employee spent 1.95% of their time conducting lobbying activities. Nevertheless, Staff seemingly arbitrarily removed 10% of this employee's salary and associated benefits.

In regard to this position, Staff ignores the information provided to it in proposing a 10% disallowance. During discovery, Staff requested details regarding lobbying activities for the Company's registered lobbyists, which includes the Manager of Government Relations. In response to MoPSC 0095, the Company provided a detailed log of lobbying activities that shows this employee spent 1.95% of their time conducting lobbying activities. Nevertheless, Staff seemingly arbitrarily removed 10% of this employee's salary and associated benefits.

The Manager of Government Relations serves an important function largely unrelated to lobbying. The Company must interact with the state and local governments on almost a daily basis. Not only are they often our customers, but they represent our customer base as a whole. Ensuring alignment of our interests is in the best interest of all our stakeholders (customers, government officials, regulators, legislators, etc.) In addition, we are an important member of the communities we serve and our activities can deeply affect our communities, not only by providing a service that is essential to human life but through our construction activities that have the potential to disrupt the lives of our customers. It is not in the best interest of our customers for MAWC not to interact effectively and continuously with our government partners. Given the minimal percentage of time, this position spends on lobbying activities and the additional support provided to the business, there is no justifiable basis to make any disallowance of the salary or benefits for this position.

Q. Please address the Staff's proposed disallowance of 75% of MAWC's Director of Government Affairs salary and benefits.

A. Again, Staff ignores the information provided to it in proposing a 75% disallowance of this employee's salary and benefits. In response to MoPSC 0095 noted above, the Company also provided a detailed log of lobbying activities for this employee that shows the employee spent 6.08% of their time on lobbying activities. Nevertheless, Staff removed 75% of this employee's salary and associated benefits – a significant and unjustifiable disallowance that is not supported by the record in this case. The Director of Government Affairs also plays a critical role for the Company beyond lobbying activities. This role is integral in ensuring that the Company is aligned with its stakeholders. To that end, it is critical that the Company communicate, engage and work with its stakeholders, including customers, regulators, legislators, community leaders, trade organizations and others, to ensure alignment that best supports the interests of all stakeholders. Even though some portion of this employee's time is spent on lobbying activities it is nowhere near 75% as proposed by Staff and this Director provides essential support to the business. As such, there is no justifiable basis to make the proposed disallowance of the salary or benefits for this position.

Q. Do you think it is appropriate to remove costs related to employee lobbying activities generally?

A. No, I do not. There is no reason to deny recovery for lobbying activities that are carried out by an employee of the Company. All companies, including utilities, must lobby the legislature to ensure that laws that are enacted are in the best interest of the Company and its customers. In some cases, the Company will lobby the legislature to prevent bills from being passed that would impose unnecessary costs or burden on operations that could add to the bills of our customers. In other cases, the Company lobbies to support legislation that protects our employees while they're in the field. There is no reasonable basis for denying recovery for activities that support the interests of the Company and its customers. Full recovery of all Missouri-American employees' salaries and associated benefits would result in an increase to Staff's proposed salaries and benefits expense by $103,506, which would subsequently impact payroll taxes and other benefits.

Q. Please address Staff's elimination of the Company's ESPP costs from its labor and labor related expense.

A. Staff eliminated the amount associated with the Company's ESPP for Missouri-American's labor expense. This resulted in a reduction of approximately $56,069 in Missouri-American. Staff recommends not allowing recovery of the ESPP expense because there is no actual cash outlay for this item made by MAWC. As I discuss below, while there may be no cash outlay, it is compensation.

Q. What is the ESPP plan?

A. The ESPP plan is open to all active, full- or part-time employees of American Water Works Company, Inc. ("American Water") and its subsidiaries, including MAWC, through payroll deductions. Employees who choose to participate in a purchase period elect a contribution of 1% to 10% of after-tax compensation, subject to a maximum of $25,000 per year. Under the ESPP plan, participants acquire shares of American Water common stock at a 10% discount.

Q. How are these transactions accounted for?

A. The discount portion of the transactions are accounted for as share-based payment arrangements with employees under Accounting Standards Codification ("ASC") Topic 718, *Compensation – Stock Compensation*. The objective of accounting for transactions under ASC 718 is to recognize in the financial statements the employee services received in exchange for equity instruments issued and the related cost to the entity as those services are consumed. ASC Topic 718 requires the Company to record expense over the three-month purchase period for employees' participation in the ESPP plan.

The expense is recorded based on individual employee participation in each subsidiary or state. Compensation expense is measured at grant date based on the number of shares that can be purchased using the estimated total payroll deductions and the grant date fair value of the stock at grant date (the beginning of the purchase period). Because the 10% discount and the ability to purchase shares at the lesser of the beginning or ending purchase-period price create option-like features, the Black-Scholes option-pricing valuation model is used to calculate the grant date fair value. The purchase-period withholdings for each participant are estimated at the beginning of each purchase period based on participant contribution elections. The estimated payroll deductions for each individual participant in each subsidiary or state are aggregated and used to calculate an estimated number of shares that can be purchased for participants in each state or subsidiary. Expense for the purchase period is calculated by multiplying the estimated number of shares to be purchased in the subsidiary or state by the grant date fair value. The expense (which represents the 10% discount to employees, but contributed by the Company) is recorded evenly over the three-month purchase period to one cost center or cost center and WBS element combination for each subsidiary or state.

Q. How do you respond to the argument that there is no specific cash outlay?

A. While there is no specific cash outlay by Missouri-American for the ESPP expense, the 10% discount received by employees purchasing shares is compensation. The fact it is not cash does not change the fact that it is an expense recorded on the Company's books. Just like the other benefits the Company provides to its employees, ESPP is a part of an employee's overall compensation, and the expense should be included in the Company's labor and labor related expense in this case.

Q. Please discuss the Company's capital and O&M percentages.

A. In order to eliminate costs associated with capital projects and programs from the labor and labor related expense, the Company multiplies labor and labor related costs by an O&M percentage that charges the appropriate percentage of labor and benefits to O&M

expense. The Company's calculation yielded a capital percentage of 42.3% and an O&M percentage of 57.7%. The Company's calculation was based on the period ended December 31, 2016 ratio of dollars charged to O&M verses capital. Staff's calculation yielded a capital percentage of 42.14% and an O&M percentage of 57.86%. Staff's calculation of the O&M percentage was based on the period ending June 30, 2017. The Company reviewed the Capital and O&M percentages for the 12 month period ended December 31, 2017, which yielded a capital percentage of 43.47% and an O&M percentage of 56.53%. The Company would anticipate a true-up to Staff's calculation using the period ending December 31, 2017.

Q. Despite the differences in staffing levels, and adjustments and/or methodologies used, what corrections should be made to Staff's labor and labor related expenses?

A. The first correction needed is in regards to the shift/premium pay calculation. Wage rate premiums (premium or shift pay) are a component of labor expense required by collective bargaining agreements ("CBAs") for employees who obtain special licenses, work particular shifts, operate backhoes, or work scheduled holidays such as Thanksgiving, Christmas, and the Fourth of July. The Company and Staff both included an adjustment for the shift/premium pay and the Company takes no issue with Staff's pro forma methodology. The Company, however, did identify an issue in the calculation where shift premium for the Joplin district, which would increase the expense by $3,901, was not included in the total calculation. It is the Company's understanding that this error will be corrected in the true up.

The second issue that needs to be addressed, which is threefold, relates to the overtime calculation and entry into Staff's EMS Model. It is my understanding that Staff intends to correct each of the overtime issues addressed here. Overtime, another component of the labor expense, was reviewed and adjusted by both Staff and the Company. The Company takes no issue with the pro forma adjustment methodology used by Staff, which is the same logic used by the Company. The Company, however identified an error in the Staff weighted average calculation for Districts 1, 2, and 3. It is the Company's understanding that Staff intended to calculate a three year weighted average. Apparently, however, a formula error for these districts resulted in an overstatement of overtime dollars. The error correction will result in a reduction of expense of $294,124 dollars. In addition, the Company discovered that one service area, Anna Meadows, was not included in Staff's overtime calculation. This will result in an increase in expense of $1,554. The Company also discovered an error in the entry of the total overtime dollars that were entered into Staffs EMS model, in which overtime expense was double counted, or entered twice. The correction of this issue will result in a reduction of expense in the amount of $1,685,932.

The third correction that needs to be made is relative to the APP expense. Apart from the difference between the Company's and Staff's position on APP expense, which is addressed later in my testimony, a correction needs to be made Staff's calculation. Staff's workpapers show that Staff calculated the APP pay at $1,380,098, and recommended allowing $690,049. Staff's adjustment model did not account for payroll taxes for the allowed portion of APP. As part of labor and labor related expense, APP is subject to the same payroll tax rates as regular labor dollars, and therefore, payroll taxes should be considered as part of the adjustment.

The fourth correction is relative to the Company's Defined Contribution Plan ("DCP"). DCP is a retirement savings program for employees not eligible for the defined benefit pension program. Under the DCP, Missouri-American contributes an amount equal to 5.25% of an employee's base pay into a retirement account. The Company's 2017 pro forma DCP expense was calculated by multiplying the 2017 pro forma regular time pay of each eligible employee by 5.25%. There is no indication that Staff included any allowance for DCP expense, outside of the expense included in the 2016 base year. Upon further discussion Staff did indicate it would review this expense element. The Company recommends that the level of expense be calculated based on the current rate of 5.25% of all eligible employees' wages, multiplied by the O&M Expense Factor proposed by the Company.

The fifth correction is to the interdistrict allocation of labor expense included in the labor and labor related adjustment calculated by Staff. In the normal course of business, there are occasions when specific employees work outside their primarily assigned district. These employees who are assigned to one district on these occasions perform work and direct charge their time to another district. In order to appropriately assign labor and labor related costs for each district both the Company and Staff calculated the percentage of time of these employees, using the 2016 base year labor dollars, and allocated the time accordingly. The net of the overall expense item should be zero, as it is simply an allocation. The Company determined in Staff's model the interdistrict allocation did not net to zero, and $121,558 dollars were erroneously added to the overall labor expense. This correction will result in an overall reduction in expense in the amount of $121,558.

Q. OPC witness Amanda Connor states in her direct testimony (page 6 line 15) that the Company booked $1,288,416, in severance expense in the 2016 base year, and subsequently failed to remove this from the going-forward expense in this case. Please respond to OPC witness Connor's allegation.

A. There are two points to address with regard to the severance expense. The first is relative to the expense amount cited by OPC. In its response to Staff DR 0104, the Company provided data showing the 2016 severance expense as $700,167, and the 2017 January through June severance expense was $536,230. This is a total combined expense of $1,236,397. At this time, it is unclear where OPC derived the $1,288,416 expense level noted in testimony. OPC goes on to state that the Company made no adjustment to remove severance from their expense levels. This statement is incorrect. As stated in the Staff DR 0104 response, the Company did not include severance in its going level expense calculation. The Company builds the labor and labor related model for Missouri-American expense based on the number of employees, salaries and wages, and corresponding benefits. This expense is then applied to the base year expense to determine the level of increase or decrease. Severance is automatically removed through this process. In addition, the Company made an adjustment to remove all severance expense from the base year for the Support Services expense. Any additional removal of expense as requested by OPC would result in a significant understatement of expense and erroneously remove dollars which have already been removed, and not included in going level expense. Consequently, to allow the OPC adjustment would be an improper double-count.

IV. <u>SUPPORT SERVICES</u>

Q. Please address the issues regarding support services.

A. There are two issues I would like to address regarding support services. The first involves Staff's reductions for alleged lobbying activities and the second involves performance based compensation.

Q. Please discuss Staff's reductions for alleged lobbying activities by Service Company employees.

A. Again, without any explanation to support their adjustment, Staff proposes to disallow 10% (or approximately $19,238) of the salaries and benefits associated with the following Service Company employees: Director Communications and External Affairs, Manager Rates and Regulatory State Support, Senior Director National Government & Regulatory Affairs, and the Senior Vice President of External Affairs & Business Development. None of these employees are registered lobbyists as defined above and these roles do not entail lobbying activities. For example, the Manager Rates and Regulatory State Support's primary focus is to develop, implement and coordinate the state rate and regulatory strategy. This position drives and influences all regulatory activities including the rate case process.

Thus, the Company requests the labor and labor related costs associated with these employees be allowed in full.

Q. Please address the second issue involving performance based compensation for Service Corporation employees.

A. The second issue relates to the Company's performance based compensation, which is discussed in Section V of my testimony.

Q. Despite the differences in staffing levels, and adjustment methodologies used what corrections should be made to Staff's labor and labor related expenses?

A. There is one issue I would like to address with respect to the Service Company expense. In reviewing Staff's workpapers and EMS model, the Company believes that Staff's model removed APP and LTPP Service Company expense at 100% rather than the 50% of APP and 100% of LTPP, respectively, as noted in the Staff Report - COS. It is the Company's understanding that Staff intends to review this matter and revise it accordingly.

V. PERFORMANCE BASED COMPENSATION

Q. Please describe the adjustments proposed by Staff to the Company's performance based compensation costs.

A. Staff recommends disallowing fifty percent (50%) of annual performance plan ("APP") compensation for both MAWC and Service Company employees. Staff also recommends disallowing 100% of long-term performance plan ("LTPP") compensation for MAWC and Service Company employees. Taken together, the proposed adjustments would disallow $1,712,542 from the Company's operating expense in this case, approximately $1,022,493 of which is associated with the disallowance of Service Company charges and approximately $690,049 of which is associated with the disallowance of MAWC's labor expense.

Q. What are Staff's reasons for its proposed adjustments to both MAWC's and the Service Company's employee performance based compensation costs?

A. Staff alleges they: (1) have historically recommended the removal of performance based compensation awards tied to company financial performance; (2) have found "no connection between the financial results for which the incentives are awarded and any tangible benefits to [MAWC's] ratepayers"; and, (3) that the Commission does not recognize performance based compensation awards tied to company financial performance. (Staff Report Cost of Service, p. 66) Staff relies on the Commission's Report and Order in a *In re Southwestern Bell Telephone Company (SWB),* MoPSC Case No. TC-89-14 et al. (1989).. (Staff Report – Cost of Service, p. 66).

Q. Why should the Commission reject Staff's proposed adjustments to performance pay costs?

A. Staff's view of this issue is too narrow, and it ignores the evidence in this case. First, it's not appropriate to parse employee compensation costs when, as here, overall employee compensation is demonstrated to be reasonable. Second, it's incorrect to assume that financial goal-based performance pay doesn't benefit customers. Third, Staff's adjustments misinterpret Commission precedent related to recovery of performance based compensation costs. Unlike Staff, the Commission has not, and should not, take so narrow a view of performance pay cost recovery.

Q. Why is it inappropriate to parse employee compensation costs?

A. Employee compensation is a necessary cost of providing utility service. Therefore, it should be assessed under the same lens as other necessary operating costs: if it is prudently incurred and reasonable in amount, relative to what the industry pays for the same services, it should be recoverable through rates. Therefore, the Commission should concern itself when employee compensation is too high, which may unreasonably increase rates, and when employee compensation is too low, which may adversely impact service to customers through a number of factors including the failure to attract and retain motivated, competent employees. It is an undeniable fact that employees judge their compensation on its totality; including base wages, performance based wages and benefits. Management should have the incentive to design the compensation package that is most properly structured to compensate employees properly and to motivate efficiency, safety, courtesy and other valuable employee traits. To parse employee compensation as Staff has done, however, undermines utility management's discretion to design employee compensation, within reasonable cost levels, that best serves the utility and its customers.

Q. Has the Company shown that its employee compensation is reasonable?

A. Yes. The direct testimony of Company witness Robert V. Mustich explained that, when assessed against the market, MAWC employees' target total direct compensation—base pay plus short-term and long-term variable pay at target levels—is reasonable. In fact, Mr. Mustich's extensive compensation analysis shows that MAWC employees' target total direct compensation is actually *lower* than both Midwest regional market and national market median levels for comparable positions. (Mustich Dir., p. 9-10). So, even if MAWC employees receive their total target performance payout, their total compensation is still less than their market peers. And, as Mr. Mustich explained, if MAWC employees don't receive any performance pay, their base salaries alone would put them significantly below the market median. (Mustich Dir., p. 10). Staff does not even acknowledge this testimony, much less dispute it.

Q. Why shouldn't the Commission overlook this testimony?

A. Employee compensation is the key tool that MAWC uses to attract and retain the talented employees it needs to meet its service obligations to Missouri customers. Without performance pay, MAWC employee compensation would be insufficient to attract and sustain a qualified workforce. It is undisputed that MAWC's employees are not overcompensated. It is not appropriate, therefore, to disallow any portion of their compensation, including any financial-goal based performance pay. Again, performance pay is not in addition to MAWC employees' reasonable compensation; it makes MAWC employees' compensation reasonable.

Q. Staff appears to have disallowed half of the expenses for the APP because 50% percent of the award is tied to financial performance, which Staff claims does not benefit customers. Based on the same argument, Staff would disallow 100% of the LTPP. Is it incorrect to assume that financial goal-based performance pay doesn't benefit customers?

A. Yes, the assumption is incorrect because performance pay related to financial goals benefits customers in many ways. Importantly, to achieve performance pay financial goals, such as targeted earnings per share ("EPS") performance, demands attention to operating efficiency. That is, unless the utility controls or reduces its operating costs, it cannot achieve a targeted EPS. Staff simply overlooks this. But financial-goal based performance pay ensures that employees at all levels of the organization, and not just the upper ranks, remain focused on increasing efficiency, decreasing waste, and boosting overall productivity. As a result, incentivizing employees to control and reduce operating costs unquestionably benefits customers, because it mitigates rate increases. I would expect Staff to agree that customers receive a tangible benefit when a utility reduces or controls its operating expenses, to the extent the reduction in or control of expenses do not compromise the ability to provide safe and reliable service.

Q. Does providing an incentive to employees to control and reduce operating costs provide other customer benefits?

A. Yes. Where MAWC can reduce operating expenses, it can increase investment in infrastructure without increasing rates, because every dollar of operating expenses saved can fund over $7 of investment. Therefore, customers also benefit from MAWC's enhanced ability to invest in the infrastructure that it needs to meet its service obligations to customers. Thus, it is simply wrong to assume that MAWC's customers receive no appreciable benefit from financial-goal based performance pay.

Q. How else does financial-goal based performance pay benefit customers?

A. It mitigates the cost of service to customers another way. Water and wastewater operations are capital intensive. Using low-cost debt and internal funds to finance water and wastewater infrastructure investment mitigates the financing costs that customers ultimately pay through rates. The availability of those sources of capital at reasonable costs, however, depends on the utility's financial performance, including credit and bond ratings. So it's important to focus utility employees on the financial health of the organization. Simply put, a financially healthy utility benefits customers because it enables the utility to meet its service obligations at reasonable financing costs.

Q. Are there other ways that financial-goal based performance pay benefits customers?

A. Yes. Long-term financial-goal performance pay programs, like the LTPP, are particularly intended to reduce attrition at the higher ranks of the organization. Excessive instability at that level may have significant negative financial effects on the organization, such as on EPS, which ultimately impact customer rates, for the reasons I've explained. So, as MAWC witness Mustich explains, these types of performance pay programs are well-accepted in the industry. Importantly, the American Water LTPP achieves its goals of reducing leadership attrition at a lower cost to customers than simply increasing leadership's base pay, because performance pay under the LTPP is stock-based.[1] Because stock-based compensation vests on a phased basis in three installments over a prospective three-year period, employees must remain with the organization to realize the vesting of their awards.

Q. Has the Company shown that customers receive a tangible benefit from its performance pay program?

A. Yes, including that portion of the program related to financial goals. Notably, as Company witness Clarkson explained in his direct testimony, the Company's 2016 operating expenses were only one percent (1%) higher than 2010 operating expenses (exclusive of the additional O&M expense related to new acquisitions). This level of cost control is the result of improvements in operating efficiency, as Company witness Clarkson explains, driven by employees that are incentivized, through the Company's carefully constructed compensation plan, to find ways to be more productive and efficient.

[1] The Staff Report - COS (p.66) indicates that the LTPP is made up of stock options, restricted stock units and performance stock units. As of 2017, the LTPP no longer includes stock options. See MoPSC 0098 Attachment 1 CONFIDENTIAL.

Q. Is there other evidence of the tangible benefit to customers from MAWC's performance pay programs?

A. Yes. Again, it's important to consider the impact of a utility's financial health on its ability to access reasonable cost capital. MAWC's customers have benefitted from the Company's access to capital at favorable rates that has resulted from American Water Capital Corp.'s ("AWCC") and American Water Works Corporation, Inc.'s ("American Water") recent ratings upgrades. Because utilities are capital intensive, and must constantly and consistently access the capital markets at reasonable costs, plainly, customers benefit when their utility has the financial health to do so.

Also, customers receive a benefit when a utility retains a talented workforce, because a stable workforce avoids the costs of hiring and training new employees. Because MAWC's performance pay program makes MAWC employees' total compensation reasonable, as Mr. Mustich explains, the Company's performance pay helps ensure a stable workforce.

Q. Please explain why it is particularly inappropriate for Staff to disallow Service Company charges related to performance pay.

A. As has been explained, the Service Company provides services to American Water's affiliates at cost and at prices that are more advantageous than could be obtained in the market place. The Service Company, for example, provides legal, finance, accounting, engineering, design, environmental, and customer services to MAWC and its regulated utility affiliates. The overall question that a regulator should ask regarding these services is whether they are reasonable when compared with services that the Company can obtain in the market. If, for example, MAWC were to obtain operating services from the market, like an outside engineering firm, you would not expect an adjustment for that firm's performance based compensation plan, even if the plan included financial goals. Rather, the Commission would assess the reasonableness of the engineering firm's costs relative to the market, as it did Service Company costs.

Q. Are MAWC's Service Company charges reasonable?

A. Yes. In his direct testimony, Company witness Mr. Patrick Baryenbruch, testifies on the value of Service Company costs and demonstrates that they are equal to or less than the costs we would have to pay for equivalent services. In addition, as I explained in my direct testimony, despite inflation, the Service Company charges sought by MAWC in this case are only about two percent (2%) higher than 2016 expenses, which represents about a one-half percent annual increase from 2016 through the future test year. Accordingly, no party challenges the reasonableness of any Service Company rates relative to the market rate for such services. Staff, however, makes no mention of either when it imputes a performance pay cost disallowance to Service Company charges. The Service Company is providing MAWC—and its customers—enhanced value, at a reasonable cost. It is inappropriate to disallow a component of that cost simply because it doesn't comport with Staff's view of employee compensation.

Q. Staff appears to place great reliance on the *Southwestern Bell Telephone* ("SWB") case cited at page 66 of its report. Does it appear that Staff is ignoring several key findings in the SWB case that have relevance here?

A. Yes, it appears so. For example, in the SWB case, much was made of the fact that Southwestern Bell had a goal to compensate employees at a level of at least 75 percentile level of those companies with which it competed for employees on a national level. The Commission, found, however, that Southwestern Bell was actually compensating its management employees at the 50% percentile level. Given that evidence, the Commission observed that the aspiration to compensate at the 75% level was irrelevant and the fact that compensation was at the 50% level dispelled claims that the compensation was unreasonable. In this case, in dramatic contrast, it is clear that, even when including performance-based compensation, MAWC's employees are not even at the 50th percentile level. Under the SWB standard invoked by the Staff, MAWC's total compensation (base and performance pay) is indisputably reasonable.

Q. Is it fair to rely here, as Staff does for MAWC, on the SWB case for the principle that "the results of the parent corporation, unregulated subsidiaries, and non-Missouri portions of SWB, are only remotely related to the quality of service or the performance of SWB in the state of Missouri?"

A. No, I do not believe it is fair to do so. For example, Staff extensively discusses the beneficial impact of American Water's credit ratings on MAWC (Staff Report - COS, pp. 32-33). By having access to capital at the favorable rates available to AWCC, MAWC customers directly benefit from the financial performance that permitted the recent credit upgrades to American Water. Further, as MAWC witness Bulkley and Rungren point out, Staff also improperly disregards MAWC's capital structure and has reflected an American Water parent company capital structure. (Staff Report - COS, pp. 33-35); Under the circumstances, Staff's recommendation to remove fifty percent of the Company's APP and all of the Company's LTPP on the basis that financial performance is "only remotely related to the quality of service or the performance of SWB in the state of Missouri" appears to be unsupportable.

Q. Is there a connection between the financial results that trigger the funding of performance based compensation and tangible benefits to MAWC's customers?

A. Yes, there is. As discussed above, given the capital intensive nature of water and wastewater operations, it is appropriate to consider the impact of financial performance on the availability of internally-generated funds and maintaining credit ratings at a level necessary to access capital at reasonable rates. The use of internal capital or low-cost debt mitigates the Company's financing costs for its substantial ongoing investment in new and replacement facilities. In addition, attention to cost controls is determinative to a considerable extent in achieving financial goals and the resulting positive impact on financial metrics can help the Company mitigate its requested rate increase. Consequently, when financial performance is achieved through efficiency, as is the case for MAWC, the interests of customers and shareholders are aligned.

Q. Please summarize why it is fair and appropriate that the costs of the Company's performance based compensation be included in rates.

A. The Company's performance based compensation plans contain tangible goals that are designed to do several things. First, they measure and reward employees for performance based on delivering clean, safe, reliable and affordable water service and providing good customer service when doing so. The operational components measure performance that can most directly influence customer satisfaction, health and safety, environmental performance, and operational efficiency. Customers derive a direct benefit from our focus on these key measures in the plan. Further, well-grounded financial measures keep the organization focused on improved performance at all levels of the organization, particularly in increasing efficiency, decreasing waste, and boosting overall productivity.

By rewarding superior performance in every function, all of these aspects of overall performance provide direct and tangible benefits to our customers. MAWC's performance based compensation is not only a means of focusing its employees on the organization's goals, but also a means of measuring attainment of those goals.

To the extent that a financially healthy utility focused on efficiency and customer satisfaction is able to attract the capital investments necessary to provide safe and reliable service and to maintain the technological expertise necessary to operate the company and comply with increasing water quality standards. A financially healthy utility is very much in the interest of MAWC's customers, as it helps ensure MAWC the ability to provide safe and reliable service at the lowest reasonable cost.[2]

Most important, however, the evidence in this case demonstrates that, even with performance pay, our overall non-bargaining unit compensation is below the 50th percentile ranking. Consequently, our total compensation (base and performance pay) is necessary to attract and retain employees. Furthermore, the LTPP component is vital to retain employees who might otherwise seek higher compensation elsewhere but who are provided an incentive to remain with the Company. The retention of a highly trained and demonstrably effective and productive workforce is, without question, in the best interest of our customers.

Again, it is important for the Commission to view compensation as a whole. As MAWC witness Mustich explains, MAWC's total compensation today (base plus

[2] MAWC's performance based compensation plans meet the criteria established in the Commission's Report and Order for *In re Union Electric Co.*, Case No. EC-87-114: "…an acceptable management performance plan should contain goals that improve existing performance, and benefits of the plan should be ascertainable and reasonably related to the plan." 29 Mo. P.S.C. (N.S.) 313, 325 (1987).

performance pay) results in employee compensation levels that are either at, or below the market median. In other words, MAWC's employees are not overcompensated relative to their peers, even with the inclusion of performance pay. So, it is not appropriate to disallow a portion of their compensation. Further, where, as I've explained, both the financial performance and the individual metrics provide benefits to our customers, and the resulting overall compensation levels are also demonstrably reasonable, it would not be just or reasonable to disallow a portion of those expenses, regardless of how they are categorized. The question is "are MAWC's total salaries and benefits reasonable?" Mr. Mustich has demonstrated unquestionably that they are. Staff, therefore, is proposing to disallow a reasonable operating expense. To do so, would both result in a labor expense that is understated, and deprive MAWC and its customers of an important tool that has produced clear and proven gains in productivity and efficiency improvements. Moreover, as Mr. Baryenbruch confirms, the Service Company charges are demonstrably reasonable. Accordingly, it is inappropriate to reduce them, whether directly or through the artifice of a reduction for performance based compensation.

VI. PRODUCTION COSTS

Q. What is the basis for Staff's adjustments to production costs?

A. Staff adjusts fuel and power expense using a different methodology than the methodology it uses to calculate chemical expense. In both cases, Staff used its five-year average usage figures, applied to a non-revenue water percentage to derive its pro forma system delivery. However, Staff used different logic to calculate the non-revenue water percentage used in the system delivery calculation, which resulted in two different system delivery numbers.

Q. Do you believe similar methodologies should be used to calculate fuel, power and chemical costs?

A. Yes. Fuel, power and chemical costs are all production costs that vary based on the Company's system delivery. System delivery should not vary between production costs. The system delivery numbers between the two expenses would have no variance.

Q. Do you agree with Staff's use of a five-year average of usage to calculate system delivery?

A. No, I do not. Company witness Greg Roach's rebuttal testimony explains in detail the Company's concerns around Staff's calculation of average usage. The Company believes that witness Roach's sales figures should be used in developing system delivery numbers used to calculate production costs.

Q. Is there additional information the Staff should consider related to chemical expense?

A. Yes. At the time of their filings, Staff and Missouri-American both utilized the 2017 cost per pound. The 2018 chemical costs per pound are now available. Utilization of the 2018 chemical costs more accurately represents the costs that the Company will incur for chemical expense in an ongoing basis.

Q. Does Staff's and the Company's calculation of purchased water expense differ?

A. Yes. The Company calculated the expense for purchased water using a three-year average of purchased water usage. This average was then applied to current and projected cost levels to determine the purchased water expense by district. Staff divided the base year purchased water quantities by base year system delivery. This resulted in a ratio of usage to system delivery. Staff then took a five-year average multiplied by the percentage derived from usage to system delivery in the base year. This calculated usage was then multiplied by the contract price to determine the annualized purchased water expense by district. Staff's adjustment for purchased water utilizes base year purchased water usage as a basis for the calculation to develop the percentage/ratio outlined above.

Q. Given that the Company's and Staff's numbers are not significantly different, which method should be adopted?

A. MAWC is willing to accept Staff's approach for purposes of limiting the contested issues in this case.

Q. Do you agree with Staff's calculation of production costs for waste disposal?

A. No, I do not. First, Staff utilized an 18-month average of historical actual charges without providing any explanation or support for doing so. This is inconsistent with both past practice by Staff as well as inconsistent with the Company's methodology. While the Company does not agree with Staff's past practice because it significantly understated the Company's waste disposal expense,[3] the Company believes it is important to point out that in this case, by using historical expense levels, Staff is overstating the Company's waste disposal expense in this case. The Company considered historical and anticipated cleaning schedules, actual cost and anticipated costs increases to calculate the waste disposal expense for the future test year, and spread the cost over the number of months scheduled between cleanings. Staff calculated waste disposal expense at $2,411,042 for the period ended June 30, 2017.

[3] In Case No. WR-2015-0301, Staff used actual expense from the base year, removing any accruals from the expense, ignoring cleaning cycles of the lagoons and accrued expenses for the Company, thus drastically understating the expense levels.

The Company calculated waste disposal expense for the period ended May 2018 at $1,732,876 and the period ended May 2019 at $1,762,514.

VII. <u>OTHER OPERATING EXPENSES</u>

Q. Please address the issues regarding Other Operating Expense, Postage and Accounting

A. The Company calculated on going postage expense based on the number of mailings in the 2016 base year, adjusted for customer growth, acquisitions, and conversion from quarterly to monthly billing for St Louis County. Staff calculated its adjustment based on the number of mailings in 2016, applied to the postage rates for 2017, to calculate a total cost, which was then further allocated by district based on the number of mailings per district to total mailings. Staff made no adjustment to the number of mailings to include customer growth, acquisitions and most importantly the change from quarterly to monthly billing for St Louis County. The increase in mailings would have been partially captured in the 2016 base year for those customers converted; however, this number would not be annualized to capture the full impact of the conversion. The direct testimony of MAWC witness Andrew Clarkson discusses the AMI and subsequent billing conversion in greater detail.

Q. What adjustments would the Company recommend to Staff's calculation?

A. The Company would expect the number of mailings to be trued-up to the 2017 actual mailings in the true-up filing. In 2017, the Company was scheduled to convert roughly 100,000 customer from quarterly to monthly billing. For these customers alone, the number of annual bills would increase from 400,000 to 1.2 million. An adjustment should be made to annualize the 2017 conversion mailings to accommodate the quarterly to monthly conversion.

Q. Please address Staff's position regarding Other Operating Expense, Advertising, Customer Education and Community Relations.

A. There were a number of expenses under customer education and community relations that Staff recommended disallowing under the determination of Staff that they didn't fall into one of following categories:

1. General: informational advertising that is useful in the provision of adequate service;
2. Safety: advertising which conveys the ways to safely use electricity and to avoid accidents;
3. Promotional: advertising used to encourage or promote the use of electricity (water conservation);
4. Institutional: advertising used to improve the company's public image;
5. Political: advertising associated with political issues.

The Company believes that approximately $44,730 of these expenses should be allowed as Staff has not categorized these expenses at all. The uncategorized expenses included items such as, MR-340 River Race on the Missouri, Trash Bash, and Wings over Water. In addition, there is another $29,654 in expense that Staff has categorized as Institutional and excluded. These include expenses for things like Earth Day, and a Day Without Water. The Staff has improperly categorized these items. Based on the categories identified by Staff, all of these items should be categorized as General because they are informational in nature..

Q. Why should the advertisements related to these events be included in the Company's revenue requirement?

A. The MR340 River Race, Trash Bash and Wings over Water advertisements reinforce the importance of river preservation to quality drinking water and wildlife conservation. These events provide educational information to customers and what they can do every day to preserve the quality of water in our rivers. This information increases understanding of water quality issues among customers and supports our provision of service. The Watershed and Earth Day advertisements encourage customers to attend our watershed educational programs. The programs educate customers on how to keep rivers clean through simple steps such as recycling and not overusing lawn chemicals etc. This information is valuable to customers so they need to understand the role they play in protecting our watershed and the provision of safe, high quality water service. A Day Without Water educates customers on the importance of using water efficiently, which in the customers' best interest.[4] For the reasons noted above, the advertising, community relations, and customer education expenses that have been disallowed by Staff should be classified as General Informational and/or Safety. In addition, those that have not been categorized, should be categorized as General Informational and the expense should be allowed.

Q. Please address the issues regarding Other Operating Expense, Maintenance Supplies and Services.

A. There are two issues with the Other Operating Expense, Maintenance Supplies and Services. The first is relative to main break expense and the second is associated with the hydrant painting expense. In regards to main break expense, the Company and Staff both use a three-year average of costs, and a three-year average number of breaks in order to derive the going level of main break expense. In Staff's calculation,

[4] Although Staff claims water conservation materials and events are covered under the promotional advertising category, it is inappropriate to do so. Water conservation is the antithesis of encouraging the use of water. Encouraging customers to use water efficiently is in the best interest of customers and should not be excluded from cost recovery.

however it reduced the average number of main breaks by carving out the 2014 main breaks associated with what was considered a "polar vortex" - Rather than using 2014 data, Staff uses an average of January, February, and March from the prior three years to replace the 2014 main break counts.

Q. Does the Company agree with excluding the polar vortex months for the 2014 period?.

A. No, the removal of these breaks from the average is inappropriate.[5] The purpose of using an average is to smooth out variations and address anomalies. This accomplished for the 2014 polar vortex simply by using the three year average method. Arguably, Staff's underlying assumption that the 2014 polar vortex related main breaks are a

Q. What resolution would the Company like to see for this issue?

A The Company believes Staff's adjustment should be recalculated to reflect the actual average for the period identified in the three year historical average. As an alternative solution, Staff could agree to update periods used to calculate the average number of main breaks, holding to the three-year average, using 2015, 2016, and 2017. This would correct the issue for this case. It is entirely inappropriate to only utilize select periods when using the averaging method. Doing so thwarts the precise purpose of using the average.

Q. Does discuss Staff's calculation of the tank painting expense?

A Staff calculated tank painting expense based on a 5 year historical average of tank painting expense. The Company projected tank painting expense based on planned

[5] While the Company agreed to accept Staff's calculation in the 2015 rate case, WR-2015-0301, in an attempt to reduce the number of issues, it is not the appropriate method for calculating main break expense,

paintings by location. Staff calculated tank painting expense for the 12 months ended June 30, 2017 at $1,462,518. The Company calculated tank painting expense for the 12 months ended May 2018 at $2,050,647 and $2,626,213 for the period ended May 2019.

Q. Does the Company have concerns regarding the hydrant painting expense?

A Yes. This is discussed in the rebuttal testimony of MAWC witness Andrew Clarkson in regard to maintenance expense.

Q. Please address the issues regarding Other Operating Expense, Insurance Other Than Group ("IOTG").

A. The Company has four issues with Staff's calculation of the IOTG expense. First, Staff excluded all cost of the Directors and Officers ("D&O") insurance coverage. Second, Staff also removed expense associated with contingency risk. Third, Staff has excluded any expense associated with acquisitions. Finally, Staff has applied a capitalization rate equal to that which was calculated in its labor model to each component of IOTG.

Q. Do you agree with Staff's elimination of D & O coverage expenses?

A. No. In review of Staff's work papers, it appears that Staff removed the expense associated with premiums for D&O coverage and D&O Brokerage Fees. Staff provides no explanation for the removal of this expense. The D&O Policy is important as it would be extremely difficult to recruit qualified persons to serve on a Board of Directors or in the capacity of executive management without a policy of insurance to indemnify and defend the Board of Directors and Corporate Officers. The Company recommends full recovery of the cost for this insurance coverage. This would result in an increase of expense of $33,871 dollars.

Q. Do you agree with Staff's elimination of the Special Contingency Risk coverage expense?

A. No. Staff has removed expense associated with the Special Contingency Risk policy. Again, Staff has provided no explanation for the removal of this expense. This policy coverage provides protection against kidnapping and extortion threats against senior executives. Similar to the D & O coverage, this coverage is crucial in the Company's ability to recruit and maintain qualified individuals to serve on its Board of Directors and in the capacity of officers. The Company recommends full recovery of this policy. This would result in an increase of expense of $491 dollars.

Q. What expenses associated with acquisitions have been excluded?

A. There were a number of acquisitions - Wardsville, Pevely Farms, and Arnold - in which the Company included IOTG expense and Staff made no apparent adjustment to expense for these costs and provided no explanation as to why they should be excluded. The Company recommends inclusion and full recovery of this expense. This would increase the operating expense calculated by Staff in the amount of $22,593 dollars.

Q. Please address the capitalization rate Staff used to calculate IOTG expense?

A. Staff applied a capitalization rate to their calculated IOTG expense equal to that used in their labor model. The Company applied a capitalization rate to their calculated IOTG expense equal to that in their labor model only for workers compensation, and then used a 10% capitalization rate for all other categories. In Case No. WR-2007-

0216 Staff recommended that 10% of IOTG costs be capitalized annually. The stipulation did not specifically mention this, however the reconciliation of the stipulation and Staff Witness Hagemeyer's IOTG workpaper for the 2007 case both reflect this treatment. It is the Company's understanding following additional conversations that Staff intends to update their calculation.

Q. Please address Staff's position regarding Other Operating Expense, PSC Assessment Fee.

A. The Company calculated a ratio of the annual PSC fee to revenues based on the fiscal year 2016 actual revenues and PSC fee amounts. This ratio was then applied to forecasted revenues to determine the going level expense. Staff's expense was based solely on the most recent PSC assessment fee, issued on July 1, 2017. It will not reflect the level of expense the Company will experience during the rate year. MAWC witness Jim Jenkins addresses the Company's position on future test year and forecasted rate making methodologies in his direct and rebuttal testimonies. .

Q. OPC witness Conner, on page 5 of her testimony, removes approximately $200,000 of MAWC and Service Company expenses that she deems to be "excessive, unreasonable and imprudent charges." Do you agree this level of expense should be removed?

A. No, I do not. MAWC and Service Company employees often incur expenses related to meals and travel as they carry out their work-related duties and responsibilities. Moreover, while OPC identified a few expenses it deems to be imprudent, they do not provide an explanation for why such costs are imprudent or come anywhere near identifying costs adding up to $200,000. Without an explanation or understanding of the full scope of OPC's disallowance, the Company cannot provide support for the charges reasonableness. Consequently, the expenses should be deemed prudent and reasonable.

Q. Does this conclude your revenue requirement rebuttal testimony?

A. Yes, it does.