Exhibit No.:	
Issues:	Policy
Witness:	Deborah D. Dewey
Exhibit Type:	Rebuttal Testimony
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2020-0344
Date:	January 15, 2021

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2020-0344

REBUTTAL TESTIMONY

OF

DEBORAH D. DEWEY

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, Deborah D. Dewey, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am President for Missouri-American Water Company, that the accompanying testimony has been prepared by me or under my direction and supervision; that if inquiries were made as to the facts in said testimony, I would respond as therein set forth; and that the aforesaid testimony is true and correct to the best of my knowledge and belief.

Deborah D. Dewey

January 15, 2021

REBUTTAL TESTIMONY
DEBORAH D. DEWEY
MISSOURI-AMERICAN WATER COMPANY
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REBUTTAL TESTIMONY

DEBORAH D. DEWEY

I. INTRODUCTION, PURPOSE OF TESTIMONY AND RECOMMENDATIONS

Q. Please state your name and business address.

A. My name is Deborah D. Dewey, and my business address is 727 Craig Road, St. Louis, Missouri 63141.

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

A. I am the President of Missouri-American Water Company, Inc. ("Missouri-American", the "Company", or "MAWC").

Q. Are you the same Deborah D. Dewey who previously submitted direct testimony in this proceeding?

A. Yes, I previously submitted direct testimony.

Q. What is the purpose of your Rebuttal Testimony?

A. The purpose of my rebuttal testimony is three-fold. First, in response to the criticisms raised by the Office of the Public Counsel ("OPC") regarding the timing of the Company's request, including the existing COVID-19 emergency, I will provide an overview of the immediate, proactive actions taken by the Company to assist customers while continuing to make investments to ensure the Company's commitment of delivering safe and reliable water/wastewater service to our customers, thus justifying the basis for timely rate relief.

Second, I will address how the ratemaking adjustments and policies advocated by certain parties in this case can and will adversely impact the Company's ability to achieve funding levels that are in the best interests of our customers. Specifically, and by far the most fundamentally flawed, is Staff and OPC's recommendation that the Commission use the American Water consolidated capital structure for ratemaking purposes. As detailed further in the testimony of Company witnesses James Merante and Ann Bulkley, there are a number of adverse consequences if the Commission were to adopt such an approach, not just for the Company, but its customers and the State of Missouri as well. Additionally, existing ratemaking policy has not afforded MAWC with a fair opportunity to earn the rate of return identified in its last general rate case. As detailed in the direct testimony of Company Witnesses John Watkins and Greg Roach, in an environment where capital investment and expenses are rising and usage per customer is declining, new rates based on an historical test year, even if selective items are adjusted in a True Up, will neither be fully reflective of the rate year relationships nor provide the Company with a realistic opportunity to earn its authorized rate of return even in the year they are implemented. (Watkins DT, p. 30).

Third, in response to Staff's recommended adjustments to the Company's labor expense, including performance pay, my rebuttal testimony will underscore the importance of competitive, total compensation packages that allow the Company to attract and retain qualified personnel, supporting testimony of Witness Robert Mustich on reasonable compensation.

II. THE COMPANY'S PROACTIVE RESPONSE TO COVID-19

Q. Since the filing of this case, how has the State, and MAWC customers in particular, been impacted by COVID-19?

A. As COVID-19 cases and hospitalizations continued to rise both in Missouri and across the Midwest, Governor Parson signed Executive Order 20-19 on November 19, 2020 extending the state of emergency in Missouri through March 31, 2021. While unemployment rates are no longer at the height we experienced in April and May of 2020, Missouri is still experiencing unemployment rates that are higher than pre-pandemic comparisons.[1]

Q. How has the Company assisted customers experiencing economic difficulties due to the COVID-19 emergency?

A. MAWC understands that the COVID-19 emergency has influenced, and will continue to influence, the personal, financial and community health of those we serve. Beginning March 12, 2020, the Company suspended all terminations and disruptions of service for active customers due to nonpayment, and waived all fees associated with late payments. Additionally, the Company ceased disconnection notices for past-due accounts. The Company also restored service to customers who were previously disconnected and waived the reconnection fees.

Today, while the Company has resumed its notice and collection practices, it has implemented several additional customer protections to provide immediate financial support for our customers. For example, the Company began offering an enhanced installment plan that can be extended from the traditional 6-month term to a 12-month term. The enhanced installment plan also eliminates the requirement for an upfront minimum payment to any customer who has not defaulted on a previous installment plan in the prior

[1] https://labor.mo.gov/data; https://meric.mo.gov

12 months. Furthermore, the Company has temporarily increased the past due amount that initiates the notice and collection practices from $100 to $150, in recognition of possible continued COVID-19 related financial impacts on our customers.

To further assist those customers experiencing financial hardships during the COVID-19 emergency, the Company made and additional contribution of $250,000, over and above its annual contribution of approximately $100,000 to its Help to Others (H2O) Fund, which provides emergency billing assistance for eligible customers.

Q. Have MAWC's practices in response to the COVID-19 emergency positively impacted customers?

A. Yes, they have. We believe that the enhanced installment plan and availability of financial support through community programs to which MAWC has provided additional funding are helping customers who are experiencing negative financial impacts from the COVID-19 emergency. For example, in the final third of 2020, the Company had an average of 81,359 customers with past due accounts, an average of 17,079 customers that had received disconnection notices, and an average of 5,119 customers on installment payment plans. For the similar pre-COVID-19 period in 2019 (September 1, 2019 through December 31, 2019), the Company had an average of 81,050 of past due accounts, 18,709 customers that received disconnection notices, and 2,786 customers on installment plans. As demonstrated above, the number of customers on installment payment plans has almost doubled, while the average number of customers with past due accounts has remained relatively flat. Notably, the average number of customers receiving disconnection notices also decreased. Based on the foregoing, customers are taking advantage of MAWC's enhanced practices including, specifically, greater flexibility and availability of payment plans for those that are experiencing financial hardship.

Q. In this case, OPC witness Geoff Marke argues that there is "nothing just and reasonable about increasing rates at this time". (Marke DT, p. 6). Do you agree with this statement?

A. No, I do not. As explained further in the testimony of Company witnesses LaGrand and Kaiser, the majority of the investments upon which the revenue request in this case is based were installed and placed in service before the COVID-19 emergency began. The Company is obligated and committed to ensuring the continuation of safe, efficient and reliable water and wastewater service for the benefit of its customers and is not relieved of doing so while we manage the impacts of COVID-19. MAWC continues to make investments to replace aging infrastructure and meet all relevant Federal and State environmental laws. The Company also has and continues to assume debt and attract funding from investors to enable MAWC to make such investments and continue to serve customers. Ensuring safe and reliable water and wastewater services is of paramount importance to MAWC, especially when dealing with a global pandemic.

III. INABILITY TO ATTRACT ADEQUATE FUNDING TO SERVE THE LONG-TERM BEST INTEREST OF CUSTOMERS

Q. Are there any recommendations advocated by the parties to the case that could adversely impact the Company's ability to achieve funding levels that are in the long-term best interest of customers?

A. The most significant and by far the most egregious recommendation made by Staff and OPC is that the Commission impose the consolidated capital structure of the American Water companies on MAWC for ratemaking purposes. As detailed further in the testimony of Company witnesses James Merante and Ann Bulkley, there are a number of adverse consequences if the Commission were to adopt such an approach for not just the Company, but its customers and ultimately Missouri as well.

As summarized in the testimony of Company witness Merante, the use of the American Water consolidated capital structure for ratemaking will: 1) create an incentive for MAWC to increase the dividend to AWK to align its actual capital structure with the ratemaking capital structure, 2) weaken MAWC's credit metrics and therefore, limit the ability for MAWC to attract capital from outside sources; 3) create a disincentive to invest discretionary capital in the state of Missouri; and 4) not result in the lowest cost option for ratepayers in the long run. (Merante RT, pp. 5-6). Please see the rebuttal testimony of Company witnesses Merante and Bulkley for further discussion regarding the recommended capital structure and its impact in this case.

Q. What other ratemaking adjustments and policies advocated by the parties could adversely impact the Company's ability to achieve funding levels that are in the long-term best interest of customers?

A. Staff and other parties to the case have objected to the use of a future test year as proposed in the Company's initial filing, which will create greater regulatory lag.

Q. On what basis has the Company sought to use a future test year in this case?

A. Use of a future test year is intended to support the more efficient use of water and more efficient investment in our system. (Watkins DT, p.27). Rate base will not stay the same as in the historical test year even if adjusted in a narrow true-up period. The Company will continue to make investments and subsequently incur additional expenses that will not be recognized in rates until a future general rate case is filed, and rate adjustments are approved by the Commission.

Q. Does the Infrastructure System Replacement Surcharge ("ISRS") address this issue?

A. While the ISRS mechanism has helped reduce regulatory lag for investments made to replacing aging water mains in St. Louis County, investments in the remainder of distribution system assets, investments in plant facilities and investments in MAWC's systems outside of St. Louis County are not included in this mechanism. Based on the historic frequency of filing general rate cases, there could be a period as long as three (3) years from the time these investments are made and/or additional expenses are incurred before they may be included in an authorized revenue adjustment. Thereby creating regulatory lag. Regulatory lag may prevent MAWC from earning its authorized return, which can create a disincentive to investment when compared to other investment opportunities available to American Water. Consequently, limiting funding for replacement of aging infrastructure or other investments that the Company believes is in the best long-term interests of its customers.

Q. What is the impact of regulatory lag on the Company?

A. MAWC has failed to achieve the rate of return authorized by the Commission in the prior rate proceeding. In 2018 and 2019, the earned rate of return averaged 8.57%, as compared to a stipulated to estimated rate of return range of 9.5%-10%. The National Association of Regulatory Utility Commissioners ("NARUC") has recognized the merits of the future test year since 2005 with resolutions deeming it a best practice, as covered by testimony of Company Witness Watkins. (Watkins DT, p. 31). It is not enough simply to set a proper rate of return. MAWC must be provided with an actual and real opportunity to earn that rate of return. I am concerned that a combination of stale policies and specific recommendations in this case by Commission Staff, OPC and other parties will continue to deprive MAWC of any realistic opportunity to earn its authorized rate of return. This case, therefore, provides the Commission with a unique opportunity to revisit and reconsider policies that have become obsolete or unwarranted and to address adjustments and policies that ultimately hamper our ability to attract investment, to the detriment of our customers and the State of Missouri.

Given the approximate 11 months from filing this rate case to the anticipated date of implementing a rate adjustment, the Company will make additional investment and incur anticipated increases to operating costs, depreciation expenses and other expenses that will not be included in establishing a revenue requirement in this case. The basis for ratemaking proposed by Commission Staff (McMellen DT, p. 5) and the OPC (Marke DT, p. 10) would eliminate the entirety of the Company's post December 31, 2020 additions. Approximately five months of plant additions will actually be in service, serving our customers, but will be ignored until some future rate filing. Telling our investors that they should invest in the Company but forego any return on those investments, particularly those that are in service (i.e., used and useful), until some indeterminate future date is hardly a strategy that is best-calculated to attract investment to the State.

Q. Could regulatory lag have an effect on the frequency of rate case filings?

A. Regulatory lag could drive the decision to file more frequent rate cases in an effort to decrease the amount of lag. More frequent rate case filings would increase the cost of the regulatory process, which would be reflected in customer rates. This would increase rates for regulatory activity that is not directly tied to providing water and sewer service. Thus, negatively impacting the efficiency of the regulatory process and the resulting cost to customers.

Q. **Do the policy recommendations of Staff and others in this proceeding impact the Company's ability to achieve funding levels that are in the long-term best interest of customers?**

A. Yes. The Company must maintain its ability to attract capital in order to continue its investment in infrastructure and have timely recovery of these expenditures. Part of my job involves making the case to American Water for investment in Missouri. Every affiliate employs someone in a capacity comparable to mine, and part of that person's job is to make the case for investment in their respective state. Because the collective need for discretionary capital inevitably exceeds the resources available from American Water, the various states are effectively competitors. This type of competition is healthy because it forces the utilities to identify and develop projects that produce the greatest benefits as efficiently as possible. But it is competition nonetheless, and the utility's return on investment is a factor that definitely influences capital investment decisions.

Q. Would Staff and OPC's proposed use of a consolidated capital structure, if adopted by the Commission, impact the availability of discretionary funding afforded to MAWC for ongoing investments?

A. Yes. As discussed further in detail in the testimony of Company witness Merante, while American Water will always ensure that MAWC has the funds available to continue to invest in order to provide safe and reliable service, discretionary investment in MAWC will likely be reduced if a consolidated capital structure is adopted by the Commission.

Q. Likewise, will you be able to achieve funding levels to continue to provide safe, reliable service without a reduction in regulatory lag?

A. We continue to maintain adequate sources of supply, treatment, pumping, transmission, and distribution facilities, as well as to comply with applicable laws and regulations – that is our public service obligation and our ongoing commitment. But the funding level sufficient to ensure the safety and integrity of the systems is not the same as the funding levels that best serve the long-term interests of our customers. It is a minimum funding level. From the perspective of long-term sustainable customer service and pricing, the Company's goal is to continue providing high quality water service in the most cost-effective way through the replacement, operation, maintenance, and rehabilitation of assets for present and future customers.

Q. What would be the impact of this minimum level of funding as compared to the more optimal funding level that MAWC has been investing in Missouri?

A. The Company has invested an average of nearly $190 million annually in system improvements and infrastructure over the past 6 years. In 2020, the Company's investment in its water and sewer systems exceeds $270 million. As stated in my direct testimony (Dewey DT, p.8), since the Company's last rate case, the Company has or plans to invest nearly $950 million in its water and sewer facilities since its last rate case through May 31, 2022. This level of investment in the State has tremendous statewide impacts including jobs, spending on goods and services, enhanced system reliability and improved customer service. In particular, a Water Research Foundation report indicates every $1million spent on water and wastewater projects supports the creation of approximately 15 jobs across the economy.[2] Less discretionary dollars ultimately yields fewer jobs for Missouri. Likewise, we are highly focused on safety, diversity, and the customer experience. If the Company were to spend less, it would not have achieved the same level of replacement of aging infrastructure or investments to support operating efficiency and customer service.

The Commission is being asked to consider recommendations related to imposing a consolidated capital structure and policies that maintain or increase regulatory lag on hundreds of millions of dollars in investment and tens of millions of dollars in expenses devoted to serving our customers. If the Commission follows such recommendations and outdated policies, there could be regrettable consequences, starting with the unraveling of the benefits achieved through investment that positioned the Company to where it is today. When such investments and expenses are not recognized in rates, the dollars to continue to support them will flow elsewhere.

This is about aligning customer and shareholder interests. We have a multi-decade-long investment need that is funded up-front by shareholders and lenders and recovered from customers over a 40 plus-year time frame. American Water is acutely aware that utility statutes and regulatory schemes vary from state to state; regulatory commissions have different policies, administrative procedures, and precedents; and these differences affect American Water's investment decisions. Investors have choices. The choices investors make must necessarily consider the returns available on invested capital. When investors have an incentive to invest, they will, and when they do not, they won't. Imposing

2 http://thevalueofwater.org/sites/default/files/Economic%20Impact%20of%20Investing%20in%20Water%20Infrastructure_VOW_FINAL_pages.pdf

conditions and applying outdated policies as proposed by Staff and other parties to the proceeding may have the temporary effect of lowering rates, but that practice ultimately imposes long-term costs that cannot be measured in dollars alone. Discouraging discretionary funding that serves the long-term interests of customers, in the name of "protecting" those customers, ultimately harms the constituency the policy is meant to help.

Q. What other investment decisions may be impacted by limitations on discretionary capital?

A. In addition to the potential to drop investment levels down to, or closer to, the minimum level for the existing infrastructure, limitations on available discretionary capital is a factor when considering acquisition of small, troubled systems. Missouri American Water owns and operates 27 systems that serve less than 1,000 customer connections. Twenty-four of those systems serve 500 customers or less. Of the 1,423 community water systems across the state, nearly 67% serve 1,000 or fewer customer connections and nearly 55% serve fewer than 500 connections. In addition, nearly 4,000 wastewater/sewer systems across the state of Missouri are classified as small or very small, capable of serving less than approximately 300 customer connections. Many owner/operators of these small systems, whether municipal or private, are facing the need for investment to replace aging infrastructure and/or to bring the systems into compliance with regulations to protect public health and the environment. MAWC is often seen as a solutions provider for these small, distressed systems to make investment efficiently with less impact on rates, as a result of its economies of scale and larger customer base.

American Water's other regulated subsidiaries are also seen as solutions providers in the states in which they operate. Just as there is internal competition for investment dollars to invest in the existing, aging infrastructure, there is competition for investment dollars to invest in acquiring and bringing small, distressed systems into compliance.

Q. Are there additional benefits to customers that are derived from the availability of discretionary funds to support the Company's continuous, planned investments in infrastructure?

A. Planned replacement of aging infrastructure allows level loading of resources, proactive material purchases and contractor service agreements that provide a more efficient use of these resources than emergency repair/replacement. Furthermore, waiting until failure to replace plant that is at the end of its designed service life increases cost and increases the disruption to customer service. The Environmental Protection Agency (EPA) estimated a need of $8.9 billion in water infrastructure investment from 2015 through 2035 in Missouri.[3] The American Society of Civil Engineers (ASCE) 2018 Infrastructure Report Card for Missouri reports an estimated need of $9.6 billion in wastewater and stormwater infrastructure invest needed over the period 2012 through 2042.[4] MAWC has been on the forefront of addressing this issue. MAWC's goal is to get to the level of replacing 1% of aged infrastructure that has reached the end of its designed service life per year, equating to 100-year service life. We have increased annual investment significantly over the past five years but are still not at the 1% replacement level. Should the Commission accept the recommendations of Staff and other parties to the case, which will prevent us from having a fair opportunity to earn our authorized return, it is probable that the investment in Missouri will have to decrease back to minimum levels, "kicking this can down the road"

[3] https://www.epa.gov/dwsrf/epas-6th-drinking-water-infrastructure-needs-survey-and-assessment

[4] https://www.infrastructurereportcard.org/wp-content/uploads/2016/10/ASCE-Report-Card-Missouri-FINAL-Report.pdf, p.56

and moving us further away from efficiently replacing aging infrastructure.

Q. Does American Water have better ratemaking policy in other states in which it has regulatory operations?

A. American Water owns the common stock of regulated water and wastewater utilities in 14 jurisdictions, including Missouri.

As stated in Witness Watkins' direct testimony (Watkins DT, p. 31), 10 of the 14 jurisdictions in which American Water regulated companies operate authorize the use of a future test year. Furthermore, 10 of 11 jurisdictions in which American Water regulated companies operate in that have an infrastructure mechanism, are not restricted to just water mains in a select geographic region of the state, as in Missouri. These mechanisms vary somewhat but most cover all distribution assets, for all water systems across the state and several also include wastewater systems.

Adopting policies that fail to recognize timely recovery of expenses and investment as is typically recovered by other American Water subsidiaries, as well as other utilities generally, would directly and adversely impact the Company's ability to secure discretionary funding. While American Water always ensures that each of its water and wastewater utilities is afforded funding to provide safe and adequate service, investment funding is not limitless. American Water is competing with other companies and industries in the marketplace for capital, and American Water's subsidiaries are competing within the American Water system for discretionary allocations of American Water's investment and financing capacity.

Q. How does Missouri regulatory policy compare with other states in which American Water has regulated operations?

A. While I am not an expert on analyzing and interpreting market related data, and defer to our experts on such matters including Company witness Ann Bulkley, S&P Global Market Intelligence issues a ranking of states based on regulatory commission policy and actions. Above Average indicates a relatively more constructive, lower risk regulatory climate from an investor viewpoint and Below Average indicates a less constructive, higher-risk regulatory climate from the investor viewpoint.[5] Within the three principal rating categories of Above Average, Average and Below Average, where the accompanying designation 1 indicates a stronger, more constructive rating, 2 indicates a mid-range rating, and 3 indicates a weaker, less constructive rating, S&P Global ranks Missouri at an Average 3. Ten of the 14 states where American Water has regulated operations rank higher than Missouri. Ultimately, if we do not begin to see a more constructive regulatory climate in Missouri, it will impact the decision making relative to allocation of discretionary capital within the American Water footprint.

Q. Does the Company plan on proposing discrete adjustments to the true-up period, consistent with the Commission's Order, in the alternative of seeking a full future test year?

A. Yes. The Company plans to propose adjustments that are known and measurable, including plant in service between January 2021 and May 2021, as well as expense increases that are tied to executed contracts, cost increase notices from vendors, and depreciation associated with the above-mentioned plant in service. For example, the proposed adjustments will

[5] S&P Global Market Intelligence; RRA Regulatory Focus; State Regulatory Evaluations; August 19, 2020; spglobal.com/marketintelligence

include wage increases required by bargaining unit labor contracts, production cost increases such as those for chemicals, energy/electric power, etc. that have been applied by vendors/service suppliers, and other expense increases that are all known and measurable. Refer to the rebuttal testimony of Company Witness Brian LaGrand for further discussion of these proposed adjustments.

IV. MARKET BASED TOTAL COMPENSATION

Q. Are there other elements of Staff, OPC and/or other parties' recommendations that concern you?

A. Yes, the recommended disallowance of 50% of the at risk portion of employees' total compensation, referred to as the Annual Performance Plan ("APP"), and all of the Long Term Performance Plan ("LTPP") is of great concern as it is part of employees' total market-based compensation. The Company's compensation philosophy is to provide a combination of compensation elements – base salary, annual performance pay via the APP and long-term performance pay – the sum of which represents total market-based compensation. In order to provide safe, reliable and adequate service for our customers, it is important that we attract and retain employees with the appropriate experience, skills and leadership abilities. This is additionally important, as 25% of the MAWC workforce will be eligible for retirement over the next 5 years. Market based compensation is critical to attract and retain employees who can provide the level of service that our customers expect and deserve. The Company, and most importantly, our customers, benefit when a utility retains a talented and experienced workforce, because a stable workforce avoids the costs of hiring and training new employees.

As supported further in the testimony of Company witnesses Evitts and Kaiser, performance payments are not bonuses but an essential element, the at-risk element, of total market-based compensation that provides tangible benefits to customers. It is not unlike any other expense that is incurred by the Company and should not be treated any differently in setting rates.

Q. How should MAWC's employee compensation expense be assessed?

A. Employee compensation is a necessary cost of providing utility service and should be assessed through 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. The focus should be on the reasonableness of the Company's overall level of market based compensation, giving management the discretion to design the compensation package that is best structured to compensate employees properly and to motivate efficiency, safety, courtesy and other valuable employee traits.

Q. Does this conclude your Rebuttal Testimony?

A. Yes, it does.