

Exhibit No.:	
Issues:	Testimony Adoption, Engineered Coatings, Performance Pay
Witness:	Jeffrey T. Kaiser
Exhibit Type:	Rebuttal
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  
REVENUE REQUIREMENT**

**OF**

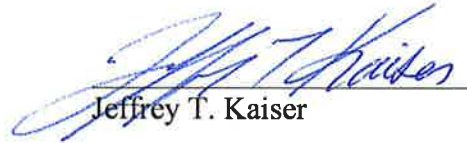
**JEFFREY T. KAISER**

**ON BEHALF OF**

**MISSOURI-AMERICAN WATER COMPANY**

## AFFIDAVIT

I, Jeffrey T. Kaiser, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am Director of Engineering and Acting Vice President of Operations 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.



Jeffrey T. Kaiser

January 15, 2021

**REBUTTAL TESTIMONY  
REVENUE REQUIREMENT  
JEFFREY T. KAISER  
MISSOURI-AMERICAN WATER COMPANY  
CASE NO. WR-2020-0344**

**TABLE OF CONTENTS**

I. INTRODUCTION .....	2
II. TESTIMONY ADOPTION .....	2
III. CAPITALIZATION OF ENGINEERED COATINGS ON STEEL TANKS.....	3
IV. MARKET BASED COMPENSATION: PERFORMANCE PAY. ....	6

## **REBUTTAL TESTIMONY**

**JEFFREY T. KAISER**

### **I. INTRODUCTION**

1 **Q. Please state your name and business address.**

2 A. Jeffrey T. Kaiser. My business address is 727 Craig Road, Creve Coeur MO 63141.

3 **Q. Are you the same Jeffrey T. Kaiser that previously submitted direct testimony is**  
4 **this proceeding?**

5 A. Yes.

6 **Q. What is the purpose of your rebuttal testimony in this proceeding?**

7 A. The purpose of my rebuttal testimony is to adopt the Direct Testimony of Grant A.  
8 Evitts and to respond to the Staff Report on Cost of Service (“COS Report”) filed by  
9 the Missouri Public Service Commission (“Commission”) Staff (“Staff”), and to the  
10 direct testimony of the Missouri Industrial Energy Consumers (“MIEC”) as to the  
11 following topics: 1) the capitalization of engineered coatings found in the direct  
12 testimony of MIEC witness Mr. Greg R. Meyer; and, 2) Staff’s treatment of the  
13 performance pay element of the Company’s total market based compensation.

14 **II. TESTIMONY ADOPTION**

15 **Q. Are you adopting any testimony in this case?**

16 A. Yes. I am adopting the Direct Testimony of Grant A. Evitts.

17 **Q. Is Mr. Evitts still with American Water?**

18 A. Yes. However, he was recently promoted to President of Tennessee-American Water  
19 Company and no longer has responsibilities for Missouri-American Water Company.

1 **Q. Are you currently responsible for the duties previously performed by Mr. Evitts?**

2 A. Yes, I am.

3 **III. CAPITALIZATION OF ENGINEERED COATINGS ON STEEL TANKS**

4 **Q. On page 32, line 18 of his direct testimony, MIEC witness Greg Meyer states that**  
5 **“Tank painting expenses are similar to power plant maintenance for an electric**  
6 **utility. Those maintenance expenses occur every five to six years ....” Do you agree**  
7 **with this comparison?**

8 A. No, I do not. Mr. Meyer refers to work that of itself occurs with a predictably short life  
9 cycle. Tank painting, or more accurately described as the application of engineered  
10 coatings, is not something that happens every five to six years. Rather, a properly  
11 prepared and applied coating should last in the range of 20 years. This is a life cycle  
12 that is much longer than many other capitalized items included in rate base.

13 **Q. On page 32, line 21 of his direct testimony, Mr. Meyer goes on to compare tank**  
14 **coatings to maintenance on a car. Specifically, “... the oil must be changed, the**  
15 **timing belt will need to be replaced and other maintenance items addressed.”**  
16 **Would you agree with this comparison to maintenance on a car?**

17 A. No, I would not. To begin, the coatings applied to our steel storage tanks have a longer  
18 expected life (20 years) than the entire car to which Mr. Meyer is comparing (typically  
19 5 to 10 years) and yet there is no question regarding capitalizing the car. Second, the  
20 “maintenance” items Mr. Meyer refers to are exactly that. They are maintenance items.  
21 Items that are designed to wear out and be replaced. His maintenance items are similar  
22 to bearing oil or grease in pumps and motors, drive belts on small equipment, and other  
23 wear items that MAWC includes in our maintenance expense. I would suggest that

1 coatings are more accurately compared to pump impellers, clarifier drive units, etc.  
2 These are items that are a major portion of the initial capital investment and a critical  
3 component of the overall working assembly. These items themselves have a significant  
4 value and life cycle, and as such are routinely capitalized when replaced.

5 **Q. Could you provide another example of an item similar to engineered coatings that**  
6 **is capitalized when replaced?**

7 A. Absolutely. A more accurate comparison would be a building roof. Roofing materials  
8 typically have a life cycle of around 20 years, much like a well applied tank coating  
9 system. The roofing also protects the underlying structure from the environment much  
10 like a coating system. However, when a roofing system is replaced it has historically  
11 been treated as a capital expenditure and is included in rate base. Using Mr. Meyer's  
12 own argument about tanks, the building which could be expected to last 100 years,  
13 would much sooner fail and need replacement if the roofing is not replaced on a regular  
14 basis.

15 **Q. Could you describe the typical process for application of engineered coatings?**

16 A. Yes, as described in my testimony the application of engineered coatings is a significant  
17 undertaking. It typically requires the removal of the existing coating systems (interior  
18 and exterior) by abrasive blasting to a clean metal surface, then the application of a  
19 three-coat engineered coating system. Ancillary work such as the construction of  
20 containment for overspray and dust control is also sometimes required. For tanks with  
21 existing lead-based paint systems, specific measures for the containment of lead  
22 particles and air monitoring is required as well as the proper disposal of the lead paint  
23 waste.

1 **Q. On page 33, line 9 of his direct testimony, Mr. Meyer concludes that Company**  
2 **witness Brian LaGrand is proposing “...an annual level of tank painting expense**  
3 **of approximately \$5.2 million.” Is this correct?**

4 A. No. What Mr. LaGrand has proposed is an annual expenditure of \$3,328,924. Mr.  
5 Meyer incorrectly added this on top of a \$1.8 million expense in 2019.

6 **Q. This still appears to be an amount greater than what MAWC has experienced in**  
7 **the past. Why is there a need for an increase?**

8 A. MAWC currently has more than 106 steel tanks throughout its water systems. These  
9 structures tanks MAWC are continuing to age and many of these tanks are nearing the  
10 life expectancy of their existing coating systems. Many others tied to recent  
11 acquisitions have not been properly maintained for some time and will require new  
12 coating systems to extend the life of the structure.

13 **Q. What would you estimate to be a typical annual expenditure for engineered**  
14 **coating systems in the future?**

15 A. As stated previously, MAWC currently has more than 106 steel tanks throughout its  
16 systems. With pending acquisitions and new construction, MAWC will likely add at  
17 least 10 more steel tanks in 2021 and it is likely that MAWC will continue to add steel  
18 tanks to its systems as we grow through acquisitions and new construction in the future.  
19 With 120 steel tanks and an average coating system life cycle of 20 years, MAWC will  
20 need to paint on average, 6 tanks per year. While some small tanks can be addressed  
21 with relatively small expenditures under \$100,000, the cost for recoating many of the  
22 large tanks such as those in St. Louis county can approach \$1 million. Experience  
23 across the Midwest would indicate that average costs will be in the range of \$400,000

1 to \$600,000 per tank for a typical 1 million to 2 million gallon elevated or ground storage  
2 tank. Using these average costs, recoating 5 to 6 tanks per year will require between  
3 \$2M and \$3.6 M annually.

4 **Q. On page 34, line 3 of his direct testimony, Mr. Meyer states that “The significant**  
5 **swings in tank painting expense would seem to justify the use of a multi-year**  
6 **average of tank painting expense.” Would you agree with this assumption?**

7 A. No, I would not. Mr. Meyer is correct that these costs can vary greatly from year to  
8 year. This is a result of a large number of tanks, many different sizes and configurations,  
9 and the conditions of those tank coating systems from year to year. However, the fact  
10 that the costs vary significantly would indicate to me that an average would not be  
11 appropriate. With the variability of this expense, the Company would be either over  
12 collecting or under collecting every year, and neither the Company nor the customers  
13 would be well served by this approach. A much more accurate treatment would be to  
14 capitalize the coating expenditures and accurately reflect those costs in rates.

15

16 **IV. MARKET BASED COMPENSATION: PERFORMANCE PAY**

17 **Q. Have Staff, OPC, or the other intervenors taken any position regarding the**  
18 **Company’s recovery of performance pay?**

19 A. Yes. Staff recommends disallowing 50% of the Annual Performance Plan (“APP”) and  
20 all of the Long Term Performance Plan (“LTPP”) sought by the Company.

21 **Q. Do you agree with these adjustments?**

22 A. No, I do not. As stated in the Direct Testimony of Company witness Evitts, which I  
23 adopt herein, the Company’s compensation philosophy is to provide a combination of



1 compensation elements – base salary, annual performance pay via the APP and long  
2 term performance pay – the sum of which represents total market based compensation.  
3 Denying recovery of any element of that compensation package denies full recovery of  
4 the cost of service. Staff would have MAWC absorb a valid expense that is incurred  
5 to provide service to our customers. It is not unlike any other expense that is incurred  
6 by the Company and should not be treated any differently in setting rates.

7 Company Witness Mustich, in his direct testimony, demonstrates that the policy of  
8 excluding any portion of at-risk compensation is out of date, unproductive and in need  
9 of a policy change. As Mr. Mustich explains, almost every American company - and  
10 even non-profits - employ performance-based compensation.

11 As stated more fully in the direct testimony of Company witness Evitts, adopted herein,  
12 performance-based compensation has created a motivated workforce that has kept our  
13 expenses essentially flat over the last decade. If we continued to be denied recovery  
14 and thus, eliminate performance pay, our total market based compensation would fall  
15 below the median band and would not be competitive with our peers. Similarly, if we  
16 eliminated performance pay but kept base salaries at the overall level, we would lose  
17 the benefits gained from performance pay. It is now long past time to recognize that  
18 performance payments are not bonuses but an essential element, the at-risk element, of  
19 total market based compensation that provides tangible benefits to customers.

20 **Q. Is the Company's total market based compensation, including performance**  
21 **compensation, a prudently incurred expense?**

22 **A.** Yes. If we compensated our employees based entirely on base wages and salaries, and  
23 those expenses were within the reasonable range of salaries and wages for similarly

1 situated companies, those expenses should be considered prudently incurred. The fact  
2 that part of that total market based compensation package is based on performance does  
3 not increase the level of overall compensation expense. As Mr. Mustich has  
4 demonstrated in his Direct Testimony, MAWC’s overall total market based direct  
5 compensation – which includes base compensation and all performance compensation  
6 – is within the competitive market range. Therefore, MAWC’s total market based  
7 compensation expense is reasonable and prudently incurred.

8 **Q. It was stated in Mr. Evitts direct testimony that Union employees’ performance**  
9 **pay was established through collective bargaining and is based on the achievement**  
10 **of plan goals. (Evitts DT, p. 36). Did Staff’s positions give any consideration to**  
11 **the applicability of Section, 386.315.1, RSMo?**

12 A. It did not. Section, 386.315.1 provides that “In establishing public utility rates, the  
13 commission shall not reduce or otherwise change any wage rate, benefit, working  
14 condition, or other term or condition of employment that is the subject of a collective  
15 bargaining agreement between the public utility and a labor organization.” At a  
16 minimum, it would appear that any disallowance of those APP amounts paid to union  
17 employees as a result of the collective bargaining agreement must be included in  
18 MAWC’s revenue requirement.

19 **Q. What amount of the performance pay paid to union employees as a result of the**  
20 **collective bargaining agreement was disallowed by Staff?**

21 A. \$574,028.

1 **Q. Staff has recommended the removal of “incentive compensation awards” tied to**  
2 **company performance on the basis that “no connection has been found between**  
3 **the financial results for which incentives are awarded and tangible benefits to**  
4 **ratepayers.” (COS Report, p. 51). Do you agree with this conclusion?**

5 A. No, I do not. There are clear direct and indirect benefits to customers included within  
6 the cost of service at-risk compensation driven by financial performance measures.  
7 Financial goal-based performance pay mitigates the long-term cost of service to  
8 customers.

9 First, the ability of the Company to meet financial performance targets demonstrates  
10 its ability to gain efficiencies and control its operating expenses and capital  
11 expenditures, which ultimately manifests itself in long-term savings for **customers.**  
12 Finding these efficiencies and incenting employees via at-risk compensation helps to  
13 delay rate cases by providing a greater opportunity for the utility to earn its allowed  
14 return.

15 Second, water and wastewater operations are capital intensive with requirements to  
16 attract capital to finance these investments. The financial performance of the Company  
17 is a key component of support for external credit metrics, which drive the Company’s  
18 ability to obtain external financing at reasonable cost rates. Moody’s current rating  
19 methodology for utilities has significant focus on financial strength and liquidity, along  
20 with the utility’s ability to recover costs and earn allowed returns. These financing  
21 costs impact customers directly via the Company’s cost of debt, and it is important to  
22 focus utility employees on the financial health of the organization to provide that  
23 performance stability for external financing.

1 **Q. Staff has further recommended disallowing the entirety of the LTPP amount for**  
2 **both MAWC and AWWSC “as they are primarily tied to the company financial**  
3 **performance.” (COS Report, p. 52). Do you agree with Staff’s conclusion?**

4 A. No, I do not. Long-term financial-goal performance pay programs, such as the LTPP,  
5 are particularly intended to reduce attrition at the higher ranks of the organization.  
6 Additionally, senior management turnover and the loss of expertise can degrade the  
7 continuity of strategy and execution. So, as Company witness Mustich explained in  
8 his direct testimony, these types of performance pay programs are well accepted in the  
9 industry. Importantly, the LTPP achieves its goals of reducing leadership attrition at  
10 a lower cost to customers than simply increasing leadership’s base pay, because  
11 performance pay under the LTPP is stock based. Employees must remain with the  
12 organization to realize the vesting of their awards.

13 **Q. Have MAWC’s customers benefited from MAWC’s achievement of the safety,**  
14 **customer satisfaction, environmental leadership, and operational efficiency goals**  
15 **under its performance pay program since its last rate case?**

16 A. MAWC’s performance in these areas over the last several years makes clear the  
17 operational improvements that benefit customers.

18 Reducing OSHA incidents increases safety—customer safety and employee safety. No  
19 one can credibly dispute the benefits of improved safety. Further, reduced accidents  
20 reduce the attendant costs—workers’ compensation, damage repair, etc.—which  
21 mitigates the operating costs that customers pay through rates. MAWC has gone from  
22 70+ recordable injuries per year in the 2006-2008 timeframe to less than 10 in 2020.  
23 MAWC continues to improve its performance in reporting near misses, another

1 illustration of the Company's high-performing safety culture. In 2020, MAWC  
2 employees identified and reported over 1,200 near miss conditions, 99% of which were  
3 addressed within 30 days. Exceptional safety performance reflects an engaged  
4 workforce that is focused on providing safe, reliable, and affordable service to  
5 MAWC's customers.

6 Maintaining and improving high quality customer satisfaction and service quality also  
7 provide customer benefits. MAWC's customer satisfaction performance goals measure  
8 customer contacts at MAWC's call centers and in the field. They are benchmarked  
9 against other utilities' performance, as reported by third-party customer satisfaction  
10 surveys. For 2019 and 2020, MAWC was ranked second in the Midwest Region for  
11 customer satisfaction in J.D. Power's Water Utility Residential Customer Satisfaction  
12 Study. J.D. Power's Overall Water Utility Satisfaction Index measures key  
13 performance indicators in six areas: delivery (including quality), price, conservation,  
14 billing and payment, communications, and customer service.

15 MAWC's environmental compliance performance is another indicator that providing  
16 competitive compensation to attract and retain skilled and knowledgeable experts  
17 benefits the customers. MAWC has not had a Notice of Violation for drinking water  
18 standards in nearly 8 years. By contrast, since 2017 roughly one third of the community  
19 water system in Missouri received at least one violation per year. MAWC has received  
20 the Partnership for Safe Water award recognizing water quality at all of our surface  
21 water facilities. We also received the Champions Award from the St. Louis Green  
22 Business Challenge in 2018, 2019 and 2020.

23 Finally, increases in operational efficiency equate to controlled or reduced operating  
24 costs. Reduced or controlled operating expenses benefit customers by reducing or

1 controlling the costs ultimately recovered through rates and increasing the time  
2 between rate cases. Financial performance goes hand-in-hand with the operational  
3 efficiencies that mitigate costs and, therefore, rate increases.

4 **Q. How would you summarize the impact of such compensation incentives?**

5 A. MAWC's O&M expenses have remained relatively flat for the last 10 years. We have  
6 maintained O&M costs per customer and number of customers per employee that put  
7 us in the top quartile for these benchmarks per the 2018 AWWA Benchmark Report.  
8 (Dewey DT, p. 14). This is the result of improvements in operating efficiency driven  
9 by employees that are incentivized, through compensation, to find ways to be more  
10 productive and efficient.

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

13 A. Yes, customers receive a benefit when a utility retains a talented workforce, because a  
14 stable workforce avoids the costs of hiring and training new employees. Because  
15 MAWC's performance pay program makes MAWC employees' total market based  
16 compensation reasonable, as detailed further by Company witness Mustich, the  
17 Company's performance pay helps ensure a stable workforce.

18 **Q. Does incentivizing employees to control and reduce operating costs provide other**  
19 **customer benefits?**

20 A. Yes. Where MAWC can reduce operating expenses, it can increase investment in  
21 infrastructure without increasing rates, because every dollar of operating expenses  
22 saved can fund over \$8 of investment. Therefore, customers also benefit from

1 MAWC's enhanced ability to invest in the infrastructure that it needs to meet its service  
2 obligations to customers. Thus, it is simply wrong and short-sighted to assume that  
3 customers receive no appreciable benefit from financial goal-based performance pay,  
4 which is a component of the reasonably incurred total market based compensation  
5 package.

6 **Q. Does this conclude your rebuttal testimony?**

7 A. Yes, it does.