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September 4, 2002

Secretary
Public Service Commission
P. O. Box 360
Jefferson City, MO 65102

FILED[3]
SEP 04 2002
Missouri Public
Service Commission

RE: Case No. WO-2002-273

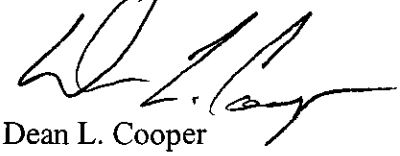
Dear Sir:

Enclosed for filing in the above-referenced proceeding please find an original and eight copies of the Highly Confidential Reply Brief of Missouri-American Water Company and an original of the NP Reply Brief. Please stamp the enclosed extra copy of each "filed" and return same to me.

If you have any questions concerning this matter, then please do not hesitate to contact me. Thank you very much for your attention to this matter.

Sincerely,

BRYDON, SWEARENGEN & ENGLAND P.C.

By: 

Dean L. Cooper

DLC/tli
Enclosures
cc: Keith Krueger
Ruth O'Neill
Stuart Conrad
James B. Deutsch
Jeremiah Finnegan

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Joint Application of Missouri-American Water Company, St. Louis County Water Company d/b/a Missouri-American Water Company and Jefferson City Water Works Company d/b/a Missouri-American Water Company for an accounting authority order relating to security costs.	)))))))	Case No. WO-2002-273

MISSOURI-AMERICAN WATER COMPANY'S

REPLY BRIEF

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MISSOURI-AMERICAN WATER COMPANY

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MISSOURI-AMERICAN WATER COMPANY
CASE NO. WO-2002-273

REPLY BRIEF

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I. INTRODUCTION

COMES NOW Missouri-American Water Company ("MAWC" or the "Company")[1] and, in reply to the initial briefs filed by the Missouri Public Service Commission Staff ("Staff"), the Office of the Public Counsel ("Public Counsel") and, the City of Riverside and St. Joseph Industrial Intervenors ("Riverside/SJII"), states the following to the Missouri Public Service Commission ("Commission"):

MAWC's positions in this matter as to the identified List of Issues are fully summarized in its Initial Brief. Accordingly, MAWC will not attempt to restate those positions in this Reply Brief. MAWC will instead seek to respond to, and clarify, certain matters found in the initial briefs of the Staff, Public Counsel and Riverside/SJII.

II. PREVIOUS TERRORISM CONCERNS/ ALLEGATIONS OF OPPORTUNISM

Both the Staff and Riverside/SJII attempt to divert the Commission's attention from the results of September 11, 2001, by pointing out that terrorism "has been a fact of daily life in Israel for many years", has led to attacks on Americans abroad at the "Khobar Towers in 1997" and in "Africa in 1998", and led to attacks on both "the World Trade Center in 1993" and the "Murrah Federal Office Building in Oklahoma City in 1995" (Stf. Brf., p. 3). Riverside/STII alleges that the Company "ignored previous terrorist attacks" (Riverside/STII Brf., p. 11). The inference apparently is these tragedies are similar to the events of September 11, 2001 and could have caused MAWC to make security upgrades sooner.

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[1] This case was initially filed by Missouri-American Water Company, St. Louis County Water Company d/b/a Missouri-American Water Company and Jefferson City Water Works Company d/b/a Missouri-American Water Company. Effective December 31, 2001, St. Louis County Water Company and Jefferson City Water Works Company were merged into Missouri-American Water Company. Thus, Missouri-American Water Company is the remaining applicant.

MAWC did not ignore these attacks. The American Water Works System had been assessing the security needs of its plant and facilities for some time (Tr. 191; Ex. 1, Kartmann Dir., p. 4). MAWC made security improvements over time that were commensurate with the level of risk recognized by the Company (Tr. 139)

However, September 11, 2001 was different from these earlier situations. Evidence of this difference is found in the reactions of entities all across the country. Most importantly, evidence that something different happened on September 11, 2001 is found in the reactions of both the State of Missouri and the federal government.

Presumably, both the federal and state governments had notice of the same terrorist attacks that made the Staff and Riverside/STII so acutely aware of the risk of terrorism in their daily lives. In spite of this, only after September 11, 2001, did:

- The federal government create the position of homeland security advisor and contemplate a complete overhaul of its agencies responsible for security and continue to provide terrorist alerts;
- The State of Missouri become the first state to appoint a special advisor for homeland security and convene the Missouri Security Panel whose purpose was, as rapidly as possible, to conduct an intensive statewide security audit, and to propose recommendations for improvements to public safety (Ex. 2, Kartmann Sur., Sch. FLK-1);
- The State of Missouri implement new security measures at large state office buildings (*Id.*);
- The Missouri Security Panel Utility Committee, the Department of Natural Resources and this Commission specifically recommend to utilities certain "Best

Practices" for security (Ex. 2, Kartmann Sur., pp. 3-5);

- The President and the Federal Bureau of Investigation ("FBI") both warn that public water facilities were a specific target that had been studied by terrorists (*Id.* at p. 6; Ex. 1, Kartmann Dir., p. 3);
- Information related to counter terrorism and security training in the water industry cite an FBI agent who indicated that there have been credible threats in EPA Region VII (Ex. 2, Kartmann Sur., p. 8).

Employees of the FBI even visited MAWC in the aftermath of September 11, 2001, and reviewed MAWC's facilities. The FBI suggested what to look for and what to secure against and encouraged MAWC to make improvements (Tr. 143).

None of the above events, or even similar events, took place after the terrorist events cited by the Staff. The overwhelming change in the way our governments do business and the information shared by those governments changed significantly the perception of the risk.

Riverside/SJII alleges that "the 'risk' that existed prior to 9/11 and the 'risk' that existed the day after September 11, 2001, were exactly the same; it was simply management's perception of that risk that changed" (Riverside/SJII, p. 14). The change in perception, however, was not unique to MAWC's. Changes in security precautions were found in rapid fashion everywhere from airports, to sporting events, and even at amusement parks such as Six Flags (Tr. 331). Even this Commission took steps to open a case to examine utility preparedness (Ex. 2, Kartmann Sur., p. 4-5). Faced with these circumstances, it is unclear why persons would want to belittle efforts made to secure a system which provides a substance ingested by customers and which is necessary to

sustain life itself.

The OPC and Riverside/SJII would have the Commission believe that MAWC's concern for security was created from some sort of "opportunism" (OPC Brf., p. 1) designed to "exploit" September 11, 2001, in the name of "profit" (Riverside/SJII Brf., p. 1). The question -- How? – comes quickly to mind. **

.** No one has challenged the fact that dollars have been spent and that more will be spent. This case is about the mere opportunity to defer these spent monies so that they can be presented to the Commission for possible recovery in the next rate case. There is currently no opportunity to "recover additional funds from captive ratepayers in the name of security" (Riverside/SJII Brf., p. 11). As a scheme to "recover additional funds," MAWC's substantial investment in security is not a very good plan.

Additionally, because actions have been so wide spread among government entities, as well as this Commission, apparently the OPC and Riverside/SJII would also ascribe this opportunism to those entities. What profit opportunity is the State of Missouri seeking? To believe the OPC and Riverside/SJII, there must be something other than concern for security behind their actions.

Riverside/SJII also continues to promote the idea that MAWC should wait for damage to its system before making security improvements. Riverside/SJII states that "[h]ad a Missouri utility suffered some damage to its physical facilities as a result of the

horrific 9/11 terrorist attacks on the United States, these intervenors would have no difficulty with that utility seeking appropriate specialized accounting treatment. . ." (Riverside/SJII Brf., p.1.). MAWC views this event differently. MAWC believes waiting for direct damage to its facilities before securing against such attacks as not prudent (Tr. 331)

September 11, 2001 was a defining event for this country in terms of awareness of security needs and dangers of terrorism in a way that had never before been seen. MAWC's actions were appropriate and commensurate with the actions of governmental bodies and other entities across this country. It would have been irresponsible to not increase security measures in the wake of the events of September 11, 2001 (Tr. 218)

III. WHY FILING A GENERAL RATE CASE IS NOT AN OPTION - PRUDENTLY INCURRED EXPENSES WILL NOT BE RECOVERED

Much discussion in the briefs of other parties revolves around MAWC's ability to recover certain amounts in a rate case. However, it is an undeniable fact that without the grant of an accounting authority order NONE of the expenses which MAWC seeks to defer in this case will ever be recovered by it (Tr. 381). It is possible that certain future expenses related to capital investments may be recovered in future rates. However, no PAST expenditures, related to capital investments or otherwise, will be recovered by MAWC without an accounting authority order. This is because of the nature of the rate making process.

The "normal rate case process" does not provide for the recovery of past expenditures. Even if expenses are found in a test year, a utility is not allowed to go back and recover those prior year's expenses (Tr. 400, 466). The test year is utilized as a basis for setting rates for future periods (*Id.*).

This is true even for capital investment where depreciation and carrying cost expenses may find their way into a test year. The Company will have lost the ability to recover the depreciation and carrying costs associated with capital investments that have been placed in service, even if they are incurred during a test period (Tr. 401-402).

Because the capital investments referenced in this case span multiple projects, the Staff's statement that "the Company was equally free to file a rate case to coincide with the conclusion of the *project*" (Stf. Brf., p. 20) (emphasis added) is far too simplistic. MAWC begins to incur depreciation and carrying costs expenses on each individual project as soon as that project is placed in service. In fact, some of the projects were completed and placed in service in 2001. It is unclear with which of these multiple projects the Staff would like MAWC's rate case filing to coincide.

For the same reasons, it is misleading to state, as the Staff does, that there are no "conditions present in this case that would preclude MAWC from recovering its prudently incurred security-related capital addition costs through a traditional rate case filing" (Stf. Brf., p. 16).

A Commission finding that expenses are "non-recurring" also may prohibit recovery (Tr. 400-401). Because the test year is designed to set future rates, those expenses that will not be incurred in the future are not recovered through the setting of those future rates. The loss of these portions of the proposed deferral are permanent and unyielding.

Thus, filing a general rate case is not a viable option for recovery of the amounts MAWC seeks to defer.

IV. TYPES OF EXPENSES

The use of the terms "on-going" and "one time" on certain MAWC schedules was

identified by the Staff as "confusing" (Stf. Brf., p. 12). Riverside/SJII tries to seize on this issue as if it were determinative of the outcome of this case. It is not. These terms refer to the nature of the expenses during the security review and implementation project.

"On-going" expenses are those that continue through the projects, but not beyond. ** [redacted] .** While "one time" expenses are those that, even during the course of the projects, represented a one time expenditure. ** [redacted] .**

** [redacted] .**

** [redacted]

**

In regard to the capital investments, Riverside/SJII seizes on the logical extension of the arguments that are being made and states that "[a]lmost by definition, an AAO should not be used to defer capital expenditures that are going to be included in rate base in some relatively current period" (Riverside/SJII Brf., p. 15). Certainly the interpretation of "non-recurring" promoted by the other parties would necessitate this result. However, this is entirely contrary to the interpretation afforded the uniform system of accounts in the past, as well as the terms of the Staff's proposed AAO criteria.

The Commission has issued accounting authority orders for expenses related to capital investments.[2] In fact, the items which the Commission authorized to be deferred in the often cited Sibley Case[3] were depreciation and carrying costs associated with capital investments.

Staff proposed AAO Criteria Three also specifically provides for "extraordinary capital additions" as a type of investment that is appropriate for an accounting authority order (Ex. 6, Fischer Reb., p. 11). Thus, the mere fact that a proposed deferral is associated with a capital investment does not alone disqualify it for an accounting authority order.

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[2] For example, the Commission granted accounting authority order for capital improvements associated with gas safety efforts in Cases No. GO-92-67, GO-92-185, GO-94-133, GO-97-301, and GO-94-234.

[3] *In the Matter of the Application of Missouri Public Service*, 1 M.P.S.C. (N.S.) 200, 213, Case Nos. EO-91-358 and EO-91-360 (December 20, 1991) ("That Missouri Public Service . . . be hereby authorized to defer and record in Account 186 depreciation expense and carrying costs associated with the life extension and coal conversion projects at he Sibley Generating Station.").

Riverside/SJII attempts analogize MAWC's request to that of an electric utility expanding its system at the same time it repairs damage from an ice storm (Riverside/SJII Brf., p. 16). The investments made by the Company here are nothing of this sort. None of these investments expand MAWC's system, add customers or provide for additional revenues.

What is "non-recurring" in this case is MAWC's need to adopt new procedures, update existing procedures and install facilities to further safeguard its water plant and systems with a sense of urgency and in an extremely short period of time (Ex. 1, Kartmann Dir., p. 4). Assessing the security status of the ten MAWC operating districts, which provide service to over 400,000 customers, in a relatively short period of time and then making prudent improvements, in a relatively short period of time, was an extraordinary, unusual, unique and non-recurring undertaking. These were not normal construction projects These were projects driven by external factors. A review of security and substantial, rapid improvements are not likely to occur again in the near future.

V. 5% MATERIALITY TEST

The Staff states its belief that "the Company's evidence fails to show that the costs incurred by the Company are at least five percent of the Company's regulated Missouri income before extraordinary items" (Stf. Brf., p. 11-12). What the Staff really means is that if it removes enough expenditures from the calculation, the remaining dollars will not equal five percent. However, doing so is not consistent with the evidence.

MAWC witness Grubb provided a comparison of the proposed deferral to regulated net income for 2001 (Ex. 4, Grubb Sur., Sch. EJG-6). This comparison revealed that the proposed deferral represents a materiality impact that is well above the five percent level

the Staff is recommending. Only when the Staff now changes its computation method from that used in its Rebuttal Testimony is there any remaining disagreement as to this issue. Staff witness Fischer stated during direct examination that had she known the Company would meet the materiality test the way she calculated it the first time, she would have changed the method (Tr. 412-413). Therefore it is clear that the methodology was selected on its ability to prevent a finding of materiality.

The proposed deferral exceeds 5% of MAWC's Missouri net operating income under the method first used by the Staff. This should be sufficient. Remember, this test did not exist before this case, and still has not been approved by the Commission. Continually moving the target is fundamentally inappropriate, and should not be the basis for denial of MAWC's application.

VI. STAFF PROPOSED AAO CRITERIA TWO - WHOSE BURDEN TO GO FORWARD WITH EVIDENCE

The Staff's Initial Brief states that in regard to its proposed Criteria Two "the information available to the Staff in this case is not sufficient to enable the Staff to form a judgment as to whether the Company is able to cover the alleged extraordinary cost and yet earn its authorized rate of return" (Stf. Brf., p. 15). MAWC would point out that it believes this is a fundamental flaw with proposed Criteria Two. It is likely that there will never be an accounting authority order case where a rate of return can be established with certainty. Rate of return is difficult to quantify and is best done within the bounds of a rate case. It is of little value to have an AAO criteria which cannot be applied.

Additionally, however, the Staff states in its Initial Brief that its inability to compute a rate of return for MAWC "does not support the granting of an accounting authority order"

because "under the Staff's proposal the Company must show that it satisfies all four of the proposed criteria" (Stf. Brf., p. 16). It is certainly true that generally the applicant carries the burden of proof in Commission proceedings. However, two factors should be considered by the Commission.

First, while an applicant may have the burden of proof, it does not always have the burden of coming forward with evidence.[4] The standard proposed by the Staff creates a situation where parties believing that the applicant's rates are sufficient must first come forward with evidence of that fact. Staff witness Fischer describes proposed Criteria Two as follows:

> If the Commission can determine, by examining surveillance reports and other information provided by the utility, *that existing rates appear sufficient* to cover the extraordinary cost and still provide the utility with a reasonable expectation of earning its authorized rate of return, *then the AAO request should be rejected.*

(Ex. 6, Fischer Reb., p. 11) (emphasis added). It is significant that this proposed criteria states that if "rates appear to be sufficient" "then the AAO requested should be rejected." As the applicant would never come forward with evidence that rates are *sufficient*, the language of the criteria establishes a presumption that the applicant's rates are not sufficient. Thus, the burden of coming forward with evidence is first on those parties

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[4] *See In the Matter of Missouri-American Water Company*, Case No. WR-2000-281 (August 31, 2000) ("In the context of a rate case, the parties challenging the conduct, decision, transaction, or expenditures of a utility have the initial burden of showing inefficiency or improvidence, thereby defeating the presumption of prudence accorded the utility. The utility then has the burden of showing that the challenged items were indeed prudent.").

opposing the subject application. In this case, no party has provided evidence of the sufficiency of MAWC's rates.[5] MAWC has no evidence to which in can respond on this issue.

Second, there is a fundamental fairness issue related to placing a burden of proof on the Company related to a standard that did not exist when the case was filed. As of this date, it is still uncertain whether or not the Commission will adopt Staff proposed Criteria Two. It is unclear just what MAWC's burden is in relation to an unadopted standard on which no other party has come forward with evidence. It would be very surprising to find out that a party could propose a standard without providing any evidence that its opponent fails to meet this standard and then be victorious because of the absence of evidence.

VII. NOT CONSISTENT WITH RECENT COMMISSION DECISIONS/NOT A "RESTATEMENT"

Staff attempts to represent its proposed AAO criteria as something that the Commission has done before. Staff erroneously states:

- that the "new four-part test is consistent with recent Commission decisions in AAO cases" (Stf. Brf., p. 2);
- that the Staff's proposed criteria "might also be likened to a restatement of the principles that the Commission has strived to apply, on a case-by-case basis, in deciding upon applications for AAOs over the past ten years or so" (Stf. Brf., p. 8); and,

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[5] The only figures provided related to MAWC's rate of return included both regulated and non-regulated revenues (Tr.403). Additionally, this does not reflect some security costs as these were deferred pending the outcome of this case (Tr. 289).

- that Staff's proposed criteria "do not significantly change the standard for granting an AAO, but rather summarize the standards that the Commission has strived to apply in deciding AAO cases in recent years" (Stf. Brf., p. 20).

This is not an accurate explanation of the Staff proposed criteria. As MAWC explained in its Initial Brief, complete with cites and quotes from past Commission decisions, at least three of the four proposed criteria are directly contrary to Commission decisions issued in "recent years."

Staff's proposed Criteria One creates a strict 5% materiality test where the Commission has previously indicated that materiality is not case dispositive.[6] Staff witness Fischer confirmed that the concept of a strict five percent materiality requirement has been rejected by the Commission in past cases (Tr. 425). Beyond that, the 5% materiality language from the *electric and natural gas* uniform systems of accounts upon which the Staff relies for its strict 5% test, is not even found in the *water* uniform system of accounts adopted by this Commission[7] (Tr. 433).

Staff's proposed Criteria Two's focus on rate issues was rejected by the

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[6] *In the Matter of Missouri Gas Energy*, Case No. GO-99-258 (March 2, 2000) ("materiality is an issue that may be considered when determining whether to allow deferral of expenses. However, a finding of materiality is not necessary to allow deferral. Inasmuch as the Commission finds that both the event causing the expenditures and the expenditures themselves are extraordinary, the Commission need not find that the expenditures are material to allow deferral.").

[7] The only test found in the NARUC uniform system of accounts for water corporations is that "Commission approval must be obtained to treat an item as extraordinary" (Ex. 17).

Commission as far back as the Sibley Case.[8] A similar attempt to Staff's proposed Criteria Three to more rigidly define what is and is not an extraordinary event has also been resisted by the Commission.[9]

Riverside/SJII correctly pointed out in its Initial Brief that "the traditional test in one way or another is derived from the language of the uniform system of accounts" (Riverside/SJII Brf., p. 22). However, the unmistakable conclusion that extends from this observation is that the Staff's proposed AAO criteria in this case *are not derived from the language of the uniform system of accounts.*

The Commission adopted uniform systems of accounts for each of its regulated industries through the rulemaking process. These uniform systems of accounts have been in place for many years and have provided a process for the possible deferral of costs from one accounting period to another for many years.[10]

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[8] *In the Matter of the Application of Missouri Public Service*, 1 M.P.S.C. (N.S.) 200, 206, Case Nos. EO-91-358 and EO-91-360 (December 20, 1991) ("Staff's emphasis on whether the utility was earning above its authorized rate of return at the time of deferral, whether the expenditures are reasonable and prudently incurred, and whether to include carrying costs in the recovery, are rate case issues and best left for rate case review.").

[9] *In the Matter of the Application of Missouri Public Service*, 1 M.P.S.C. (N.S.) 200, 207-208, Case Nos. EO-91-358 and EO-91-360 (December 20, 1991) (". . . to limit extraordinary events to these situations is too restrictive. There may be instances which occur that are neither acts of God nor threaten the provision of service but that are nonetheless unusual, unique and nonrecurring, where deferral would be justified and reasonable.").

[10] OPC refers to certain testimony by Company witness Grubb which took issue with OPC witness Bolin's description of the AAO process as being a deviation from the "traditional method of setting utility rates" (OPC Brf., p. 11-12). This is primarily a fight over semantics. While MAWC is aware that prior Commission decisions have referred to accounting authority orders in this manner, MAWC takes issue with that description. Deferral of costs from one period to another in extraordinary

While the Commission certainly has the authority to interpret and apply its lawfully promulgated regulations, as it did when it developed the "traditional test" for accounting authority orders based upon the promulgated uniform system of accounts, it does not have the authority to change the rules without going through the rulemaking process.

The case cited by the Staff further supports this assertion:

> Implicit in the concept of the word "rule" is that the agency declaration has a potential, however, slight, of impacting the substantive or procedural rights of some member of the public. Rulemaking, by its nature, involves an agency statement that affects the rights of individuals in the abstract.[11]

Staff's stated goal for its proposed AAO criteria reveals the rulemaking intent of its effort. The Staff states that the proposed AAO criteria "would enable utilities to have a better idea, in advance, when their situation meets the requirements for an AAO, and would discourage utilities from filing applications that have no merit" (Stf. Brf., p. 9-10). While Staff wants to say that its proposed AAO criteria will be applied on a "case-by-case" basis and that the Commission is not bound by *stare decisis* (Stf. Brf., p. 10-11), the truth is that the Staff is looking for a decision of general applicability that will apply in the abstract. Nothing else will provide the utilities with an idea, in advance, of the standard to be applied and "discourage utilities from filing applications."

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situations has been a part of accounting industry pronouncements since 1947 (Ex. 4, Grubb Sur., p. 1-2). An accounting process that has been utilized in the regulatory arena for approximately 55 years should be safely within the "traditional method of setting utility rates."

[11] Staf. Brf. , p. 10; *Baugus v. Director of Revenue*, 878 S.W.2d 39, 42 (Mo. 1994).

"Failure to follow rule making procedures renders void purported changes in statewide policy." *NME Hospitals, Inc. v. Department of Social Services*, 850 S.W.2d 71, 74 (Mo. banc 1993). The Staff has announced a *change* in statewide policy and statement of general applicability in asserting that it plans to apply its four criteria to future accounting authority order applications. The Staff proposed AAO criteria would be unlawful if adopted by the Commission outside a rule making proceeding.

VIII. THERE IS A VAST DIFFERENCE BETWEEN ADDRESSING TERRORISM CONCERNS AND COMMON VANDALISM

The Staff indicates in its Initial Brief that "Missouri utilities . . . have always had to be concerned about security, whether it be to protect against vandalism, graffiti and the unauthorized dumping of trash, or the protection of their facilities against terrorist attacks" (Stf. Brf., p. 4). This again raises an astounding idea that somehow the threat of graffiti and trash dumping and the resources warranted to protect against such is somehow akin to the dangers associated with potential terrorist efforts with the intent to harm large numbers of persons.

As Captain Young indicated, "you cannot even begin to compare" the "prank," "dare" and "laziness" behind vandalism and trash dumping "to possible threats of contamination to your community's drinking water supply" (Ex. 5, Young Sur., p. 6). Even OPC witness Bolin indicated that while some of the measures used to fight terrorist acts might also prevent vandalism, the underlying costs might not be warranted or prudent if one was only addressing vandalism threats (Tr. 483).

It is undeniable that the appropriate response to threats of graffiti and trash dumping is different than the appropriate response to:

- an alert from the FBI, such as that received by the Company in October of 2001, indicating that the FBI had information suggesting that the nation's drinking water was at risk (Tr. 234);
- statements from the President and the FBI warning that public water facilities were a specific target that had been studied by terrorists (*Id.* at p. 6; Ex. 1, Kartmann Dir., p. 3); and,
- information related to Missouri Department of Natural Resources sponsored counter terrorism and security training in the water industry citing an FBI agent who indicated that there have been credible threats in EPA Region VII (Ex. 2, Kartmann Sur., p. 8).

IX. IF AN AAO IS GRANTED, SOME DECISION AS TO THE AMORTIZATION PERIOD IS NECESSARY

Staff suggests that the if "[t]he Commission should not make a rate decision, about the length of the amortization period, as a part of its decision in this AAO case" (Stf. Brf., p. 23).

Certainly the Commission can reserve rate case decisions for a rate case. MAWC has taken the position in its Supplemental Statement of Position, filed on June 21, 2002, that an order granting an accounting authority order in this case should contain the following provision:

> That nothing in the Order shall be considered a finding by the Commission of the value for rate making purposes of the deferred expenditures.[12]

[12] MAWC witness Grubb further confirmed during cross-examination that if the Commission so desired, the Company would not object to including the phrase "or

This having been said, some period of time must still be selected for the amortization, if an accounting authority order is granted. To start an amortization, one must know what period to use in order to know how much to amortize in a given year (Tr. 97). This is a separate question from how the amounts may be treated in a future rate case (Id.).

MAWC suggests that an order granting an accounting authority order in this case should direct that MAWC begin to amortize the deferred amounts, on a twenty year basis, beginning with the effective date of a Report and Order in this case. The use of a twenty year period is consistent with the recommendation made by the OPC (if the accounting authority order is granted) (OPC Brf., p. 20).

X. PROCEEDINGS IN OTHER STATES

The OPC, after clearly stating that the "Missouri Commission is not bound by the decisions of other state commissions," goes on to review certain proceedings in other states concerning other subsidiaries of American Water Works Company (OPC Brf., p. 13-17). MAWC has not, of course, relied upon any proceedings from other states in relation to the Commission's decision in this matter. Now that they have been raised, MAWC will respond as best it can as to the relevance these other proceedings may have.

The purpose of this exercise for the OPC may be to show that there are ways other than an accounting authority order to address the concerns found in the National Association of Regulatory Utility Commissioners' ("NARUC") resolutions which were discussed in this case, as the OPC states that "those other jurisdictions also received

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the prudence thereof" in the proposed condition to further clarify its intent (Tr. 271).

information from NARUC which has been discussed in this case" (OPC Brf., p. 14).

The Resolution on Commission Procedures Related to the Increased Security Measures Undertaken by Water Utilities (Ex. 1, Kartmann Dir., Sch. FLK-2) suggested that commissions consider methods of efficient cost recovery of security expenses, including "deferral of expenses for accounting purposes only until a more comprehensive rate case expense review can take place. . . ."[13]

In the cases reviewed by the OPC, commissions in Ohio and Indiana had ongoing rate cases and according to the information presented by the OPC were able to address recovery of security items within those rate cases. Iowa is a state not mentioned by the OPC that was also able to take this approach.[14] In West Virginia, because the rate case was too far along to include security items, a deferral of expenses (i.e. an accounting authority order) was authorized.

The area where MAWC takes issue with the OPC's review of the results in other states concerns its description of what transpired in Kentucky. The OPC correctly states that an order in Kentucky-American Water Company's application to approve the RWE transaction is relevant. However, OPC's statement that "Kentucky-American withdrew a pending request for recognition of security costs in exchange for approval of the pending

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[13] The NARUC Resolution on Guidelines for State Commission Procedures Involving the Handling of Security Sensitive Documents and the Recovery of Prudently Incurred Security-Related Costs also states, in part, that state commissions are encouraged to "identify and/or establish procedures for timely recovery of prudently incurred security related costs" (Ex. 4, Grubb Sur., Sch. EJG-3).

[14] *Iowa-American Water Company Application for Revision of Rates*, Order Approving Amended Settlement Agreement, Iowa Utilities Board Docket No. RPU-01-04; TF-01-118 (February 21, 2002).

merger" (OPC Brf., p. 14) is not a complete statement of what transpired. The recovery mechanism that was at issue in Kentucky was an application for a separate cost recovery method (a "pass through" or surcharge) related to the security costs. This application for a separate cost recovery mechanism is what was withdrawn, not a "request for recognition of security costs." Kentucky-American has subsequently filed for authority to defer those same costs. MAWC is not aware of any state where it has withdrawn or otherwise indicated that it will not seek recognition in rates of costs related to security measures.

The reviewed cases show that deferral of expenses, or an accounting authority order, is one of the ways that state commissions can provide for efficient cost recovery. Because of the existence of ongoing rate cases in some states, some commissions were able to jump over deferral and directly to consideration of recovery issues. However, in Missouri there is no existing MAWC rate case. Accordingly, the accounting authority order is the best tool available to provide MAWC with the opportunity to present these costs for Commission consideration in a rate case.

WHEREFORE, for the reasons set forth herein and in its Initial Brief, MAWC respectfully requests the Commission issue its order granting MAWC an accounting authority order authorizing it to maintain on its books in Account 186 a regulatory asset which represents the operation and maintenance expenses, carrying costs, and depreciation expenses associated with the adoption of new procedures, updating existing procedures, and the installation of facilities to further safeguard MAWC's water plant after the events of September 11, 2001, subject to the following conditions:

A. MAWC shall amortize the amount deferred over a twenty-year period beginning with the effective date of this order; and,

B. That nothing in the Order shall be considered a finding by the Commission of the value for rate making purposes of the deferred expenditures.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing document was sent by U.S. Mail, postage prepaid, or hand delivered, on this 4th day of September, 2002, to the following:

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