

Exhibit No.:	
Issues:	True-Up Items and Timing, Phase-In Proposal
Witness:	Dennis R. Williams
Exhibit Type:	Surrebuttal
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2008-0311 SR-2008-0312
Date:	October 16, 2008

MISSOURI PUBLIC SERVICE COMMISSION

**CASE NO. WR-2008-0311
CASE NO. SR-2008-0312**

**SURREBUTTAL TESTIMONY
OF
DENNIS R. WILLIAMS
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)	CASE NO. WR-2008-0311
RATES FOR WATER AND SEWER)	CASE NO. SR-2008-0312
SERVICE)	

AFFIDAVIT OF DENNIS R. WILLIAMS

Dennis R. Williams, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Surrebuttal Testimony of Dennis R. Williams"; that said testimony and schedules were prepared by him and/or under his direction and supervision; that if inquires were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge.


Dennis R. Williams

State of Missouri
County of St. Louis
SUBSCRIBED and sworn to
Before me this 15th day of October 2008.


Notary Public

My commission expires:

Staci A. Olsen
Notary Public - Notary Seal
State of Missouri
St. Charles County
Commission # 05519210
My Commission Expires: March 20, 2009

**SURREBUTTAL TESTIMONY
DENNIS R. WILLIAMS
MISSOURI-AMERICAN WATER COMPANY
CASE NO.WR-2008-0311
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1 **SURREBUTTAL TESTIMONY**

2
3 **DENNIS R. WILLIAMS**

4
5
6 **I. WITNESS INTRODUCTION AND PURPOSE**

7
8 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

9 A. My name is Dennis R. Williams and my business address is 727 Craig Road, St.
10 Louis, Missouri 63141.
11

12 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

13 A. I am employed by American Water Service Company, Inc. as Senior Manager -
14 Rates and Regulation.
15

16 **Q. ARE YOU THE SAME DENNIS WILLIAMS THAT FILED REBUTTAL TESTIMONY**
17 **ON BEHALF OF MISSOURI AMERICAN WATER COMPANY ("MAWC") IN THIS**
18 **PROCEEDING?**

19 A. Yes, I am.
20

21 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

22 A. The purpose of my surrebuttal testimony is to discuss true-up issues that were
23 raised in testimony by Staff Witness Kimberly Bolin and Joplin Witness Michael
24 Ileo. I will also address Dr. Ileo's suggestion regarding a phase-in of the
25 proposed increase in this case.
26

27 **II. TRUE-UP ITEMS AND TIMING**

28
29 **Q. WHAT IS THE PURPOSE OF A TRUE-UP PERIOD?**

1 A. A fundamental principle of ratemaking is that the Company's revenue
2 requirement should be based upon the annualized cost of providing utility service
3 at the time rates are put into effect. Missouri utility regulation typically follows the
4 practice of establishing rates based upon a historical test year. Adjustments are
5 made to that test year in an attempt to make revenues and costs more reflective
6 of current levels. However, a long period of time ensues between the end of a
7 historical test year and the time new rates go into effect (in this case fourteen
8 months). A true-up period is often necessary to reflect the most current
9 information possible. This is particularly true when a significant change in costs
10 or revenues takes place after the end of the test year, such as in the event of
11 placing into service a major component of new plant.

12
13 **Q. HOW IS THE TRUE-UP DATE SELECTED?**

14 A. Prior to filing, the Company makes an assessment of when major construction
15 projects will be completed and placed into service. It then attempts to file its
16 case at a time that will minimize regulatory lag but at the same time balance the
17 interests of parties that need to review and audit the Company's filings. True-up
18 proceedings have long been considered appropriate in Missouri because of the
19 length of the ratemaking process and reliance upon a historical test year. The
20 true-up process has been utilized in at least the past four MAWC general rate
21 cases. MAWC takes this procedural precedent into account when determining its
22 test year selection and rate case timing.

23
24 **Q. YOU MENTIONED BALANCING THE INTERESTS OF THE VARIOUS**
25 **PARTIES. PLEASE EXPLAIN WHAT YOU MEAN.**

1 A. The negative impact of regulatory lag on the Company as a result of large plant
2 additions can be significant. MAWC has put into service over \$135 million of new
3 plant additions since the end of the test year (i.e., December 31, 2007).
4 Regulatory lag associated with these additions for just the five months between
5 the true-up date and the operation of law date will amount to the loss of over \$5
6 million dollars in net income to MAWC – or about \$1 million dollars per month. At
7 the same time, MAWC recognizes that the parties need an adequate amount of
8 time to conduct an audit of the Company records, normalize the test period, and
9 participate in hearings, if necessary. Recognition of past practice allowed the
10 Company to determine an appropriate filing date and make what it considers an
11 appropriate true-up recommendation.
12

13 **Q. JOPLIN WITNESS ILEO COMPLAINS THAT THE TRUE-UP APPROACH AND**
14 **LACK OF DOCUMENTATION CREATES GREAT UNCERTAINTY AND**
15 **PREVENTED PERFORMANCE OF MEANINGFUL ANALYSIS. DO YOU**
16 **AGREE?**

17 A. No. Staff has made it perfectly clear in both testimony and conferences that its
18 true-up estimate was largely, if not entirely, a result of anticipated plant additions
19 subsequent to the end of the test year. Staff, in fact, quantified its estimate for
20 the Joplin district in Accounting Schedules accompanying direct testimony. The
21 only significant uncertainty is whether recovery of those plant additions will be
22 disputed. Dr. Ileo is correct that, in Missouri, utilities are not allowed to begin
23 recovery of plant investment until they can show that their investments are
24 prudent, used and useful and in service. No party has suggested, however, that
25 plant additions for which the Company is seeking rate base inclusion are

imprudent. Moreover, the City of Joplin is well aware of the significant plant additions that have been constructed in that district, including a \$31.8 million investment in new treatment facilities placed into service in September, and is quite capable of forming an opinion and stating a position as to whether recovery of those additions is appropriate. As a party to this case, Joplin certainly could have employed resources on a timely basis so as to make its own determination and recommendation to the Commission, without relying solely on the Staff. Finally, the City of Joplin needs to keep in mind that it is the Commission, and not the Staff, that ultimately determines the outcome of disputed issues in a rate case. Even if the Staff or another party did challenge MAWC's request to recover the Joplin plant additions, the range of potential outcomes would still exist and the certainty that Dr. Ileo desires would still be unknown until the Commission issues a final decision.

Q. WOULD THE RECOMMENDATION TO INSTITUTE A REQUIREMENT THAT ADJUSTMENTS TO THE TEST YEAR BE LIMITED TO SIX MONTHS AVOID THE ISSUES RAISED BY DR. ILEO?

A. No. Calendar year test years are often used as a matter of convenience for all parties. If Dr. Ileo's procedure was adopted, a utility would still respond by adjusting its test year selection and timing of filing to try to minimize regulatory lag. In this case, for example, MAWC would likely have utilized a March 31, 2008 test year in its direct filing. Selection of a non-calendar year as the test year could actually increase the length of time necessary to conduct an audit. Furthermore, even under a proposal to limit adjustments to six months after the end of a test year, Staff would still be required to conduct a retrospective audit.

1

2 **Q. WHY WOULD THAT BE NECESSARY?**

3 A. If Dr. Ileo's proposal had been adopted and in effect for the current rate case,
4 Staff would have conducted its initial review of the test year or test year update at
5 March 31 and then have had to take a retrospective look at June 30 data.

6

7 **Q. USING THE PROPOSED SCENARIO, COULDN'T THE STAFF SIMPLY HAVE**
8 **CONDUCTED ITS INITIAL AUDIT AS OF JUNE 30TH?**

9 A.. I do not believe so. Staff conducts a complete and thorough audit. That review
10 must be completed, however, in the limited amount of time available prior to the
11 deadline for filing direct testimony. Even though a March 31, 2008 update period
12 was utilized in this case, Staff's direct testimony had to be filed by August 18,
13 2008. If the review had been delayed three months, the other procedural steps
14 in the process would have similarly been delayed, and it is difficult to see how the
15 Commission could issue an Order within the operation of law date.

16

17 **Q. IS THERE TYPICALLY A DIFFERENCE BETWEEN STAFF'S INITIAL AUDIT**
18 **AND A TRUE-UP AUDIT?**

19 A. Yes, there is a vast difference. The initial audit is designed by Staff to verify the
20 Company's financial statements, review the Company's filing and adjustments,
21 and develop its own methods of adjusting a test year period to reflect, as closely
22 as possible, normalized or annualized revenues and costs at what it believes are
23 appropriate levels. This necessarily takes a considerable amount of time and
24 generally results in a number of issues among the Company, the Staff and other
25 parties. In contrast, by the time the true-up procedure is completed, most

1 differences among the parties have either been resolved by agreement among
2 the parties or fully litigated in hearings before the Commission. Since in its initial
3 filing, the Company requested recovery of anticipated plant additions as of the
4 true-up date, even general matters of prudence, cost control and management
5 efficiency would have been addressed. The true-up audit, then, is more a
6 verification process to determine that the revenues and costs that are booked are
7 verifiable, properly supported and actually incurred.

8
9 **Q. DOES DR. ILEO RECOMMEND IMPLEMENTATION OF HIS PROPOSAL IN**
10 **THIS PROCEEDING?**

11 A. I do not believe so. Dr. Ileo recommends at page 6, line 29 of his rebuttal
12 testimony that the Commission adopt his proposal "for ratemaking in the future".
13

14 **Q. IF THE FUTURE IS INTERPRETED AS BEING IN THE CONTEXT OF THE**
15 **CURRENT CASE, IS THERE ANY OTHER REASON THAT THE CITY OF**
16 **JOPLIN MIGHT MAKE THIS PROPOSAL?**

17 A. Yes. The City of Joplin is well aware of the completion of significant
18 improvements to that district's water treatment facilities subsequent to June 30,
19 but prior to the true-up date in this case. Application of a June 30th cut-off for
20 known and measureable adjustments would preclude MAWC's recovery of
21 substantially all of its prudently incurred investment in the Joplin area simply
22 because that facility was not in service at June 30, the true-up date conveniently
23 chosen by Joplin. If the City of Joplin recommendation was utilized in the current
24 case, MAWC would, upon conclusion of this case, be required to immediately file
25 another rate case in order to recover those prudently incurred investments. The

1 period of time during which the Company could not recover a return on or of its
2 investment - an investment that is currently providing service to Joplin customers
3 - would be extended from the existing 5 month regulatory lag period to a lag of
4 potentially 16 months (i.e., 5 months + 11 months)..
5

6 **Q. DOES EVERY ITEM OF REVENUE AND EXPENSE NEED TO BE**
7 **REVIEWED IN A TRUE-UP PROCEEDING?**

8 A. No. Only those revenues or costs that might have substantially changed from
9 the updated test period to September 30, 2008 need to be reviewed. The goal
10 should be to develop a revenue requirement that is reasonably reflective of
11 costs and revenues at the time rates go into effect. Use and normalization of
12 a test year period make it unnecessary to update many items.
13

14 **Q. DO YOU AGREE WITH THE ITEMS SELECTED BY STAFF TO REQUIRE**
15 **CONSIDERATION IN THE TRUE-UP PROCESS AS SET OUT IN THE**
16 **REBUTTAL TESTIMONY OF STAFF WITNESS BOLIN?**

17 A. Not entirely. On April 15th of this year, MAWC proposed a list of items that it
18 believed would require true-up in this case. The Staff has accepted this list
19 with the exclusion of five items – tank painting expense, fire hydrant expense,
20 uncollectible expense, waste disposal, and property taxes.
21

22 **Q. PLEASE ADDRESS EACH OF THESE ITEMS INDIVIDUALLY.**

23 A. Tank Painting Expense – I agree with Staff witness Bolin that this item does
24 not require true-up in this case. There is a difference between Staff and the
25 Company regarding the appropriate expense level that should be established

1 for the operation of a tank painting tracker. However, that issue will be
2 addressed outside the true-up, during the rate case hearing. Evaluation of the
3 balance in the regulatory asset account will be reviewed during the true-up.

4 Fire Hydrant Expense – For the current proceeding, I agree with Ms. Bolin that
5 this item does not require true-up. There is an issue between Staff and
6 MAWC as to the appropriate expense level for hydrant painting and what level,
7 if any, should be established for a hydrant painting tracker. However, this will
8 be addressed during the rate case hearing.

9 Uncollectible Expense – MAWC believes there is a direct relationship between
10 the level of revenues and uncollectible accounts expense. As a result, the
11 Company believes that if revenues are increased or decreased during the
12 true-up, that uncollectible expense should be adjusted accordingly. Staff does
13 not believe that there is a relationship between revenue levels and
14 uncollectibles. The underlying issue of whether a direct relationship exists will
15 be determined by the Commission and should determine whether
16 uncollectibles expense is an account that is appropriate for true-up.

17 Waste Disposal – I agree with Ms. Bolin that true-up of waste disposal costs is
18 not necessary in this case. Waste disposal, or sludge removal, is conducted
19 as needed. The interval between required waste disposal events is
20 dependent upon specific conditions at different treatment facilities. In order to
21 normalize a test year, the cost of waste disposal at each treatment plant is
22 divided by the number of years duration between cycles. If waste disposal
23 occurs after the update period that is significantly above or below historical
24 costs, the normalized average should be included in a true-up. That did not
25 occur this year.

1 Property Taxes – I do not agree that it is appropriate to exclude property taxes
2 from true-up. As noted in the rebuttal testimony of Company Witness Don
3 Petry, property taxes are assessed upon plant placed into service by the
4 Company. MAWC will begin accruing in January 2009, which is prior to the
5 operation of law date in this proceeding, property tax expense associated with
6 plant additions made in 2008. The Staff has agreed that plant additions
7 through September 30, 2008 should be included in true-up. Likewise, the
8 ongoing level of property tax expense associated with those plant additions
9 should be included in true-up.

10
11 **Q. ARE THERE ANY OTHER ITEMS THAT SHOULD BE INCLUDED IN THE**
12 **LIST OF TRUE-UP ITEMS?**

13 A. Yes. Due to the manner in which Staff treated lease expense in their direct
14 filing, it is necessary to include that expense item in the true-up. Staff made
15 an adjustment to test year levels of lease expense to remove all amounts
16 associated with leases that showed an expiration date prior to the end of the
17 update period. This adjustment was appropriate but Staff failed to then reflect
18 any costs of new leases entered into to replace the expiring leases. At
19 prehearing, Staff indicated that this would be corrected during the true-up
20 process. It is my belief that is still Staff's intent and that leases were
21 inadvertently excluded from the list of true-up items.

22
23
24 **III. PHASE-IN PROPOSAL**

25 **Q. HAVE YOU READ CITY OF JOPLIN WITNESS ILEO'S DISCUSSION**

1 **COMPARING THE RECOVERY OF INVESTMENT PROJECTS BY NON-**
2 **REGULATED COMPANIES VERSUS REGULATED UTILITIES?**

3 A. Yes, I have.

4
5 **Q. DO YOU AGREE WITH HIS ASSESSMENT?**

6 A. I agree with his conclusion that the two procedures are different. Companies
7 operating in a competitive market environment do make decisions based upon
8 market conditions. Regulation exists in place of competition. Thus, regulated
9 companies are subject to more oversight, including prudence reviews and
10 other regulatory standards that Dr. Ileo mentions. If Dr. Ileo is concluding or
11 implying that this is a bad thing, I do not agree. It is simply different. In regard
12 to recovery of investments, regulated utilities lack certainty due to possible
13 disallowance and timing of recovery. Non-regulated companies face
14 uncertainty of recovery due to competitive forces, but they also have the
15 benefit of having greater control over the timing of recovery.

16
17 **Q. HOW IS THAT?**

18 A. Expanding on the City of Joplin's illustration, assume that a non-regulated
19 company constructs or retools a new manufacturing plant. The decision on
20 how much and when to increase prices to recover that plant investment rests
21 entirely with that company. It is likely, in fact, that in order to smooth or phase-
22 in price increases to recover its investment the non-regulated entity will
23 increase prices gradually, including some price increases prior to the
24 completion of the new facility.

1 **Q. IS THIS AN OPTION THAT IS AVAILABLE TO MISSOURI UTILITIES?**

2 A. No. Missouri utilities have been required to place plant into service prior to
3 being allowed to recover any costs associated with new plant investment. The
4 balance of construction work in progress is not allowed to be included in rate
5 base. If it was, the utility ratemaking process could flow increases to
6 customers more gradually.

7
8 **Q. WHY IS THAT IMPORTANT?**

9 A. It is important because of the perception of our customers. I attended a
10 number of public hearings in this proceeding, including the one in Joplin, that
11 were held so that customers and others members of the public would have an
12 opportunity to directly participate and provide testimony. There were a
13 number of customers that indicated they would have preferred more frequent
14 small increases over the years rather than a large increase now.

15 Construction in the utility industry is cyclical. Plant is placed into service and
16 begins to immediately depreciate. As it depreciates, the reduction in book
17 value is reflected in revenue requirement determinations so that, absent
18 significantly high inflation, rates generally remain stable or decline for a period
19 of time until it is necessary to replace that plant. Unlike the non-regulated
20 company in the earlier example, the utility cannot gradually increase prices in
21 recognition of current or future construction requirements, but is allowed to
22 increase rates only after costs have been incurred or investments placed into
23 service. There is nothing fundamentally wrong with this approach. It is simply
24 the way regulation works, but a process that is not well understood by the
25 public.

1
2 **Q. CAN YOU PROVIDE AN EXAMPLE OF THIS?**

3 A. Yes. In Joplin, for example, residential rates had not increased between 1995
4 and the increase last year that Dr. Ileo mentions in his testimony. In fact,
5 residential customer rates decreased by 3.5% in 1997, dropped an additional
6 1.5% in 2000, and declined another 2.9% in 2004. Therefore, Joplin
7 residential customers benefited for twelve years (i.e. from 1995 to 2007) from
8 steady or declining prices. Even after consideration of last year's rate
9 increase and the Company's present proposal, Joplin's residential rates are
10 among the lower half of all our districts. This is demonstrated in the below
11 table, which assumes an average customer consumes 5,500 gallons monthly.

<u>District</u>	<u>Ave. Monthly Bill at Proposed Rates</u>
St. Louis	\$20.88*
St. Charles	25.37
Warren County	25.37
Warrensburg	30.00
Joplin	34.62
St. Joseph	34.78
Jefferson City	35.44
Mexico	42.37
Parkville	43.36
Brunswick	61.57

*St. Louis district is billed quarterly -
amount is restated to reflect monthly bill

12
13 In a non-regulated environment a Company may well have decided to
14 increase prices during these earlier years to avoid the "rate shock" associated
15 with the construction of a new plant that they knew would ultimately be
16 required. A regulated utility in Missouri does not have this option.

17 MAWC does take what actions it can to control the impact of infrastructure
18 replacement on rates. The water plant infrastructure in Joplin (and throughout

1 the United States for that matter) is old and much of it needs to be replaced.
2 Replacement of infrastructure is not avoidable. In order to control rate
3 increases to the extent possible, MAWC schedules main replacements over
4 time throughout its districts so that no one district is unduly impacted in any
5 single year. On the other hand, replacement of large capital projects such as
6 water treatment plants, cannot be spread over a long period of time or among
7 districts as long as separate district pricing is in effect.

8
9 **Q. CAN DR. ILEO'S PROPOSED RATE INCREASE PHASE-IN PLAN**
10 **ELIMINATE THIS PROBLEM?**

11 A. No. Phase-in plans are difficult to design fairly and difficult to implement. Dr.
12 Ileo's proposal specifically is technically flawed and unfair.

13
14 **Q. PLEASE EXPLAIN.**

15 A. The proposal made by Dr. Ileo is not a phase-in plan designed to make the
16 Company whole. Instead, it is a "give-back" plan where Company
17 shareholders are required to forego a considerable portion of earnings
18 authorized by the Commission. Thus, the Company will never have the
19 opportunity to receive all of the revenue to which the Commission has
20 determined it is entitled.

21
22 **Q. CAN YOU DEMONSTRATE THE BASIC FLAW IN THE CITY OF JOPLIN'S**
23 **PROPOSAL?**

24 A. Yes. For illustrative purposes, I will build upon Dr. Ileo's assumptions that the
25 Commission has authorized a \$2.797 million annual increase effective on

January 1st of 2009 and carrying costs are 7.59%. Dr. Ileo suggests that a portion of the authorized increase be deferred and that carrying costs should be allowed on that deferred portion. But there is no ultimate recovery of authorized revenues, in fact, there is a permanent disallowance. The table below demonstrates what revenues would actually be received under Dr. Ileo's plan versus what that Company was authorized to receive.

Authorized		Ileo Proposal		
<u>Year</u>	<u>Annual Revenues Received</u>	<u>Annual Rate Level Start of Year</u>	<u>Rate Increase</u>	<u>Annual Revenues Received</u>
2009	\$2.797		0.799	0.799
2010	2.797	0.799	0.799	1.598
2011	2.797	1.598	0.799	2.397
2012	2.797	2.397	0.799	3.196
	<u>\$11.188</u>			<u>7.990</u>

Dr. Ileo's proposal results in the Company giving up over \$3 million of its authorized revenues even though the Company has theoretically received carrying costs on the revenues deferred. The error in logic is that while Dr. Ileo made provision for a regulatory asset in the initial year, he made no provision to establish regulatory assets for the deferred revenues in subsequent years.

Q. COULD THIS EXAMPLE BE CORRECTED?

A. Yes. To correct the proposed mechanism, additional columns would have to be added to Dr. Ileo's example to provide for a return of the deferred revenues foregone by the Company. Utilizing his other assumptions, I have presented such a table below:

1

(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(I)
			<u>Revenues</u>					
	<u>Annual</u>	<u>Unrecovered</u>	<u>&</u>		<u>Annual</u>	<u>Unrecovered</u>	<u>Carrying</u>	<u>Cumulative</u>
	<u>Revenues</u>	<u>Balance</u>	<u>Carrying</u>	<u>Rate</u>	<u>Revenues</u>	<u>Balance</u>	<u>Costs at</u>	<u>Unrecovered</u>
<u>Year</u>	<u>Authorized</u>	<u>from Prior</u>	<u>Costs</u>	<u>Change</u>	<u>Recovered</u>		<u>7.59%</u>	<u>Balance</u>
		<u>Year</u>	<u>Due</u>					
2009	2.797	0.000	2.797	0.799	0.799	1.998	0.152	2.150
2010	2.797	2.150	4.947	0.799	1.598	3.349	0.254	3.603
2011	2.797	3.603	6.400	0.799	2.397	4.003	0.304	4.307
2012	2.797	4.307	7.104	0.799	3.196	3.908	0.297	4.204
2013	2.797	4.204	7.001	0.799	3.995	3.006	0.228	3.234
2014	2.797	3.234	6.031	0.799	4.794	1.237	0.094	1.331
2015	2.797	1.331	4.128	(0.666)	4.128	0.000	0.000	0.000
	<u>19.579</u>				<u>20.907</u>		<u>1.328</u>	

2

3 **Q. WHAT CONCLUSIONS CAN YOU DRAW FROM THE ABOVE**
4 **CORRECTED TABLE?**

5 A. There are still a number of concerns to such a corrected phase-in approach.
6 First, the table above assumes that no additional rate cases would be filed and
7 no rate increases granted for at least 7 years. As previously noted, water
8 infrastructure is in serious need of replacement and it is not practical to
9 assume that there will be a 7 year period during which MAWC can absorb the
10 costs of those necessary investments. If a rate increase or rate increases did
11 occur in the interim that would only serve to significantly increase the period of
12 deferral and exacerbate other concerns about this type of phase-in.

13

14 **Q. PLEASE DISCUSS THOSE ADDITIONAL CONCERNS.**

15 A. A second concern is that rates paid by customers over the term of the phase-
16 in plan will necessarily be higher than had no phase-in plan been in effect.
17 This is because customers would be required to pay carrying costs associated
18 with deferring the rate increase. Some customers may be willing to pay that
19 premium but others may be opposed to this result. Third, there is an

1 intergenerational equity issue that arises as the result of the phase-in plan. All
2 other things being equal (e.g. no additional rate increases), rates would begin
3 at a level lower than authorized but would quickly escalate to a level that
4 would be greater than if the phase-in had not been in place. In this example, it
5 would not be until 2016 that rates returned to their originally authorized levels.
6 Customers in years 2012 through 2015 would be subsidizing current
7 customers. Fourth, there are serious accounting issues associated with any
8 kind of a phase-in plan. There is a concern whether a regulatory asset could
9 be established under the type of phase-in proposal made by Dr. Ileo. If
10 MAWC could not, there would be an annual negative earnings impact of \$1.23
11 million (\$1.998 million net of tax) or over 10 percent of the Company's current
12 year earnings. Of course, this impact would be substantially greater if the
13 phase-in plan was extended to districts in addition to Joplin. More importantly,
14 the Company faces uncertainty as to whether such a phase-in would comply
15 with generally accepted accounting principles. If it did not, the financial impact
16 would be even more egregious. Finally, there are serious concerns regarding
17 cash flow. A phase-in proposal as suggested by Dr. Ileo obviously restricts
18 cash flow significantly. Declining cash flows, especially in these times of tight
19 cash markets, would negatively impact the Company's financial capabilities.

20
21 **Q. DR. ILEO ALSO SUGGESTS THE ALTERNATIVE OF IMPLEMENTING A**
22 **BIFURCATED PROCESS, WHEREBY SEPARATE RATE CASE PHASES**
23 **WOULD ADDRESS COST OF SERVICE AND RATE DESIGN. DO YOU**
24 **SUPPORT THIS RECOMMENDATION?**

25 **A.** No. The true-up process has worked well in Missouri for a considerable

1 period of time. It has been utilized not only for water utility proceedings but in
2 the regulation of other regulated industries as well for over 20 years. There is
3 no need to change the existing process, particularly to one that would create
4 more work, take more time, prove confusing to the public and unnecessarily
5 increase rate case expense.

6
7 **Q. DOES THIS CONCLUDE YOUR PREFILED SURREBUTTAL TESTIMONY?**

8 **A.** Yes, it does.