Exhibit No.:	
Issues:	Cost of Service, Rate Design, Consolidated Tariff Pricing, Revenue Stabilization Mechanism
Witness:	Charles B. Rea
Exhibit Type:	Surrebuttal
Sponsoring Party:	Missouri-American Water Company
Case No.:	WR-2020-0344
Date:	February 9, 2021

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-2020-0344

SURREBUTTAL TESTIMONY

OF

CHARLES B. REA

ON BEHALF OF

MISSOURI-AMERICAN WATER COMPANY

AFFIDAVIT

I, Charles B. Rea, under penalty of perjury, and pursuant to Section 509.030, RSMo, state that I am Directory, Rates & Regulatory for American Water Works Service Company, Inc., 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.

Charles B. Rea
____
Charles B. Rea

February 9, 2021
Dated

SURREBUTTAL TESTIMONY
CHARLES B. REA
MISSOURI-AMERICAN WATER COMPANY
CASE NO. WR-2020-0344

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SURREBUTTAL TESTIMONY

CHARLES B. REA

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Charles B. Rea. My business address is 5201 Grand Avenue, Davenport, IA 52801.

Q. Are you the same Charles B. Rea who previously submitted direct testimony and rebuttal testimony in this proceeding on behalf of Missouri-American Water Company ("Missouri-American", the "Company", or "MAWC")?

A. Yes.

Q. What is the purpose of your Surrebuttal Testimony in this proceeding?

A. The purpose of my Surrebuttal Testimony is to address issues raised in the rate design rebuttal testimony of Missouri Industrial Energy Consumers ("MIEC") witness Jessica York, Missouri Public Service Commission Staff ("Staff") witness Matthew J. Barnes, Staff Witness James Busch, and the Rebuttal Class Cost of Service and Rate Design Proposal ("Rebuttal Staff CCOS Proposal") as to:

- Class Cost of Service
- Rate Design
- Large User Tariffs
- Consolidated Tariff Pricing
- Revenue Stabilization Mechanism

II. COST OF SERVICE

Q. Have you reviewed the Rebuttal Staff CCOS Proposal provided in Staff's rebuttal testimony?

A. Yes, I have.

Q. Do you have any comments regarding the Rebuttal Staff CCOS Proposal?

A. Generally speaking, the methodologies used by the Company and Staff to derive class cost of service are comparably different. The Company's approach to cost of service is a two-step process that allocates revenue requirements by account to different business functions and then allocates each of the business function revenue requirements to customer classes using a single allocation methodology consistent with those described in the American Water Works Association ("AWWA") M-1 Manual. Staff's approach allocates revenue requirements by account directly to customer classes in a one-step process.

The Company's approach is more intuitive than the methodology used by Staff and yields more information. As I stated in my rebuttal testimony (Rea RT, p. 7, lines 1-5), the Company changed its approach to cost of service from a one-step process to a two-step process because the two-step process is more understandable and is more reflective of how the business actually operates, without sacrificing any accuracy or precision and without sacrificing any adherence to cost causation principles that a cost of service study should rely on. Therefore, the Company's class cost of service study and approach to cost of service should be adopted in this case.

III. RATE DESIGN

Q. Please identify the issues that you will be addressing in your Surrebuttal Testimony related to Staff's proposed rate design in this case.

A. I will be discussing three issues in my Surrebuttal Testimony related to Staff's proposed rate design. These issues are:

- Proposed monthly meter service charges;
- Proposed volumetric charges for Rate A; and
- Proposed volumetric charges for Rate J.

Q. Beginning with monthly meter service charges, please summarize Staff's proposal for monthly meter service charges in this case.

A. Staff's proposal for 5/8" monthly meter charges in this case is to set 5/8" monthly meter charges for St. Louis County customers at $7.74 per month, which is a reduction of $2.26 per month from the current level of $9.00 per month. The proposal for non-St. Louis County customers is to set the 5/8" monthly meter service charge at $13.39 per month which is an increase of $4.39 per month from the current level of $9.00. (Barnes RT, p.4). Quarterly service charges for St. Louis County customers are set to be three times that of the monthly meter charge. Monthly meter charges for larger size meters for St. Louis County and non-St. Louis County customers increase in size in relative proportion to increases seen in current rates, but increase proportionally from the proposed charges of $7.74 and $13.39 per month for St. Louis County and non-St. Louis Country customers respectively.

Q. Do you support Staff's proposal for monthly service charges?

A. No. The Commission previously approved consolidated meter service charges across the Company's service territory even though the Commission had not yet approved consolidated tariff pricing ("CTP") in total across the Company's service territory. Increasing monthly service charges for some customers and reducing them for other customers would create an even greater mismatch in rates than already exists. The Company's proposal is to set all 5/8" monthly meter service charges at $12.00 per month, which is supported by the Company's cost of service study and should be approved by the Commission in this case. At the very least, monthly meter fixed charges should not be reduced in this case. This is further supported by the direct testimony of Company witness Watkins wherein he addresses the disparity between fixed revenue and fixed costs. Reducing the meter charge in St. Louis county will further exacerbate this difference. (Watkins DT, p. 6).

Q. Please summarize Staff's proposal for Rate A volumetric rates.

A. Staff's proposal for volumetric rates for Rate A in this case is to set the volumetric rate for St. Louis County customers at $4.9727 per thousand gallons, which is an increase of $0.1913 from the current level of $4.7814 per thousand gallons. The proposal for non-St. Louis County customers is to set the volumetric rate at $5.4308 per thousand gallons, which is a decrease of $0.8161 from the current level of $6.2469 per thousand gallons (Barnes RT, p. 4).

Q. Do you support Staff's proposal for Rate A volumetric service charges?

A. The Company continues to support CTP and recommends that the Commission equalize volumetric rates for Rate A for St. Louis County and non-St. Louis County customers as part of its proposal in this case. Absent Commission approval for full CTP, alternatively, the Company supports moving volumetric rates for Rate A closer together between the two districts. Staff's proposal for volumetric rates for Rate A does indeed move volumetric rates closer together between the two districts, although this is likely a consequence of its monthly meter charge proposal that widens the gap in meter charges between the two districts, which the Company does not support.

Q. Please summarize Staff's proposal for Rate J volumetric rates.

A. Staff's proposal for volumetric rates for Rate J in this case is to set the volumetric rate for St. Louis County customers at $2.0312 per thousand gallons, which is an increase of $0.2632 from the current level of $1.7680 per thousand gallons. The proposal for non-St. Louis County customers is to set the volumetric rate at $2.3752 per thousand gallons, which is a decrease of $0.4516 from the current level of $2.8628 per thousand gallons. (Rebuttal Staff CCOS Proposal).

Q. Do you support Staff's proposal for Rate J volumetric service charges?

A. The Company continues to support its proposed Rate L and the movement of current Rate J customers that do not qualify for the proposed Rate L to Rate A. Absent Commission approval of the Company's Rate L proposal, alternatively the Company supports equalizing volumetric rates for Rate J under the Company's CTP proposal. If neither the Company's Rate L proposal nor the Company's CTP proposal are approved by the Commission, the Company supports Staff's proposal to move volumetric rates for Rate J closer together between the two districts.

<u>IV. LARGE USER TARIFF</u>

Q. What is Staff's position regarding the Company's proposal to implement the new Rate L tariff and transition current Rate J customers who would not qualify for Rate L to Rate A?

A. Staff does not support the Company's proposal for the new Rate L large user tariff at this time. (Barnes, RT, p. 11, lines 2-4).

Q. What is Staff's rationale for rejecting the Company's proposal for Rate L at this time?

A. Mr. Barnes states that in order to properly evaluate the Company's proposal, the Company should file a class cost of service study for the Company's proposed Rate L customers, and a separate cost of service study for Rate J customers that do not qualify for Rate L. (Barnes, RT, p. 11, lines 9-13). Effectively, Mr. Barnes is saying that the Company has not provided sufficient cost of service information upon which to evaluate the Company's proposal.

Q. Has the Company provided sufficient information to appropriately evaluate the Company's Rate L proposal?

A. Yes. The Company has provided sufficient information for the parties in this case to evaluate the Company's Rate L proposal. Specifically, the Company has provided a cost of service study that breaks out Rate L customers as a separate customer class and calculates the cost of providing service to that class. The Company has shown that Rate J customers not qualifying for Rate L use more of the distribution system on a per volume basis than the proposed Rate L customer group, and further that usage characteristics for the non-qualifying Rate J customers are more seasonal than the proposed Rate L customer group. Both of these conditions emphasize that the cost of providing service to non-qualifying Rate J customers on a dollars per unit basis is higher than for the Rate L customer group.

I would also note that the Company's cost of service study breaks out residential from non-residential customers separately, similar to the Company's cost of service studies in previous rate cases, but the rate design approved by the Commission in the Company's last rate case puts residential and nonresidential customers together into a single Rate A offering despite the fact that the cost of providing service on a volumetric basis to residential and nonresidential customers is different. This demonstrates that ties between rate design and cost of service are not absolute and that the Commission has already approved a rate design that is not explicitly supported by cost of service.

Q. Does Mr. Barnes object to the "Base Usage" and "Extra Usage" pricing structure proposed by the Company for its proposed Rate L?

A. He does not.

Q. Does Mr. Barnes dispute the issues the Company is attempting to resolve through its Rate L proposal?

A. He does not.

Q. Mr. Barnes states that if the Commission approves the Company's proposal to create this new Rate L, the Company has not stated when the current Rate J customers that would not qualify for the new Rate L would be fully transitioned to Rate A rates. (Barnes RT, p. 11, lines 17-24). Do you have an estimate of the time frame that would be needed to fully transition non-qualifying Rate J customers to Rate A?

A. The Company anticipates that if the Rate L proposal is approved by the Commission, the transition for non-qualifying Rate J customers to Rate A would take place over an approximate ten-year time period.

V. CONSOLIDATED TARIFF PRICING

Q. What is Staff's position regarding the Company's proposal for Consolidated Tariff Pricing ("CTP")?

A. Staff does not support the Company's proposal for CTP. Staff's position is that the current two-district approach to pricing approved in the Company's last rate case should continue. (Barnes RT, p. 5, lines 3-7).

Q. What arguments does Mr. Barnes make concerning CTP's impact on affordability for customers?

A. Mr. Barnes states that St. Louis County rates currently are lower than the rates for the rest of the state. If consolidation were to occur, rates in St. Louis County would necessarily increase and St. Louis County customers, which make up the majority of the Company's customers, would actually see less affordable rates. (Barnes RT, p. 6, lines 7-13).

Q. Do you agree with Mr. Barnes's argument on affordability?

A. No. Mr. Barnes is simply pointing out that under CTP, rates for some customers will go up and rates for other customers will go down (absent an overall revenue requirement increase), which is an accurate conclusion that the Company has also addressed in this filing. In my direct testimony, which Mr. Barnes does not rebut, I point out that CTP creates benefits for all customers in the long run. For instance, typically customers that are paying lower than average prices do so because of aging and therefore, depreciated infrastructure that will have to be replaced, and the new investment recovered in rates, sooner rather than later. At some point in the future, the utility will need to invest in all regions of the state; CTP mitigates the effect of lumpy investment for all customers.

Q. What arguments does Mr. Barnes make concerning CTP's ability to lower administrative and regulatory costs?

A. Mr. Barnes simply states that he does not agree that further consolidation would lower administrative or regulatory costs, such as the costs associated with filing multiple CCOS studies. (Barnes RT, p. 6, lines 15-19).

Q. Do you agree with Mr. Barnes's conclusion?

A. No. Even though such activities are difficult to quantify in terms of cost, it is evident that a regulatory proceeding that requires three sets of revenue requirement calculations and two sets of rate calculations is more complicated and costly than a regulatory proceeding with one revenue requirement calculation and one set of rates. It is also evident that even though such activities are also difficult to quantify, activities associated with tariff maintenance, bill testing, and rate administration are a significant activity that the Company engages in in order to provide high quality customer service. The more tariffs and rates there are to manage, the more significant and costly these activities tend to be, all of which add to the cost of providing service to the customer.

Q. What arguments does Mr. Barnes make regarding the CTP's advancements ensuring a consistent regulatory approach for all public utilities?

A. Mr. Barnes claims that there is not a consistent regulatory treatment now for all utility types regulated by the Commission for a variety of reasons and CTP will not change those differences. As an example, he discusses differences in rate design between sewer customers and water customers where most sewer customers are charged a flat fee and most water customers are subject to a flat fee plus a volumetric charge, but also points out that some water customers charged a flat fee, while some sewer customers are charged a volumetric charge. He claims that these conditions represent a higher level of inconsistency than the Company having two water districts with separate rates. (Barnes, RT, p. 7, lines 3-9).

Q. Do you agree with Mr. Barnes's position?

A. No, I do not. The examples that Mr. Barnes cites exist largely because of differences in the way water and wastewater customers use the Company's services, which in turn drives policy decisions around how those rates are set. To the extent that there are differences in pricing largely due to circumstance, these are differences that CTP is intended to reduce and eliminate. It is not sound regulatory policy for utility regulatory commissions to keep rate design offerings across a utility service territory as disparate as possible based on local costs of providing service. It is more appropriate that policy towards rate design drive consolidation in territories in order to improve efficiency and transparency, and to standardize rate designs for similar services when possible.

VI. REVENUE STABILIZATION MECHANISM

Q. What issues are you addressing in your Surrebuttal Testimony related to the Company's proposed Revenue Stabilization Mechanism ("RSM")?

A. I will be addressing Mr. Busch's analyses of the Company's annual revenues from 2015 through 2019, as they relate to his testimony regarding the Company's RSM. I will also be discussing Mr. Busch's testimony as it relates to the discussion of fixed and stable revenues.

Q. Are other Company witnesses also addressing the issue of the Company's proposed RSM in surrebuttal testimony?

A. Yes. Company witness Watkins is also providing surrebuttal testimony in this case addressing the rebuttal testimony of Staff witness Busch.

Q. Company witness Watkins claims in his direct testimony that continued reduction in revenues constrains the utility's ability to make investments in its facilities and improvements in its operations. (Watkins DT, p. 5, lines 20-21). Is that correct?

A. Yes, that is correct.

Q. Does Staff witness Busch make arguments against that claim in his rebuttal testimony?

A. Yes, he does. Mr. Busch states that he has reviewed the Company's annual reports filed with the Commission over the last several years and has concluded that annual combined revenues for water and wastewater service have grown from a 2015 level of $268,845,673 to a 2019 level of $324,614,677. Mr. Busch uses this data to refute the Company's claims that revenue reductions constrain the utility's ability to make investments in its facilities and improvements in its operations. (Busch RT, p. 6 line 13 through p. 7 line 2),

Q. Do you agree with Mr. Busch's analysis?

A. I agree with his characterization of the Company's revenues from 2015 through 2019. His analysis, however, misses the point regarding annual changes in revenues as it relates to the proposed RSM.

Looking at revenue trends over the past five years could be highly misleading if revenue requirements have increased over time, resulting in higher rates approved by the Commission in prior Company rate cases and ISRS filings. In fact, if one considers only revenues, usage declines over time can be masked by such rate increases. Stated another way, simply looking at historical revenues, as Mr. Busch does, tells us nothing about customer behavior and usage when revenue increases are due to rate changes. The proposed RSM is intended to provide revenue stability over a future period of time when base rates are not changing, and the driver of future annual revenues is changes in consumption. If no base rate changes are assumed going forward, revenues will steadily decline in the longer term because use per customer for residential and commercial customers is steadily declining. A historical view of revenues, which Mr. Busch presents, fails to recognition the distinction between changes in consumption versus changes in rates. The proposed RSM is intended to stabilize revenues during the future period of time when there are no presumed changes in rates.

Q. Staff witness Busch also provides some commentary in his rebuttal testimony regarding the relatively fixed nature of the Company's revenues, correct?

A. Yes, he does. Mr. Busch states that it is appropriate to consider more of the Company's revenues to be stable than what the Company is claiming as fixed revenue, as opposed to volumetric revenue. Mr. Busch states that while an average (residential) customer’s monthly usage is approximately 6,000 gallons per month in St. Louis County and 4,000 gallons per month in other areas of the state, a certain percentage of that water is non-discretionary base usage, meaning that this usage is not impacted by the variability of weather and is used for basic service applications such as cooking, personal hygiene, washing, etc. (Busch RT p. 8, line 17 through p. 9, line 6). He goes on to say that because even in the months of December through March average monthly use per customer is at least 3,000 gallons per month, approximately half of the revenues that are collected from the variable commodity charge are, for the purposes of this discussion, fixed. (Busch RT, p. 9, lines 8-11).

Q. How do you respond?

A. I agree that usage over and above what Mr. Busch calls non-discretionary, or base use, is not subject to weather volatility. The usage that is subject to weather volatility is what I have described as extra usage in my discussion of the Company's proposed Rate L. This extra usage is seasonal in nature and is over and above the base use level. The non-discretionary usage that Mr. Busch describes is subject to the impact of declining use per customer. This usage, and the end uses associated with that usage, is where the declining use issue manifests itself, and as usage continues to decline, the volumetric revenues associated with this non-discretionary usage that is declining will also decline. If revenue from non-discretionary use was indeed "fixed" or "stable", declining use would not be an issue in the water utility industry.

Q. Does this conclude your Surrebuttal Testimony?

A. Yes.