

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Application of Ozark)	
Meadows, Aqua Development Company,)	
d/b/a Aqua Missouri, Inc. Request for)	File No. SR-2010-0023
Increase in Annual Sewer System Operating)	
Revenues MPC Sewer Utility Small)	
Company Rate Increase Procedures)	

**AQUA MISSOURI BRIEF IN SUPPORT
OF A CONSOLIDATED RATE STRUCTURE**

On March 15, 2010, the Missouri Public Service Commission directed Aqua Missouri (“Aqua”) and parties in the above referenced dockets to file a brief delineating the arguments and social policy implications associated with whether the Commission should permit or require Aqua to consolidate all of its rate districts for the purpose of rate setting. In addition to this discussion, Aqua has provided several rate structure options based on the last allowed revenue requirement overall for all systems per Aqua Missouri’s last rate orders.

I. Introduction

Aqua Missouri appreciates the opportunity to file this brief in support of a consolidated rate structure policy. Single tariff pricing and a consolidated rate structure are best practices which provide benefits to customers over the long run in terms of lower rate increases, along with timely infrastructure improvements. This brief will discuss some of the unique issues associated with small water systems and how adopting a consolidated rate structure policy can be a solution to solving those issues. Rate consolidation takes different forms and means different things to regulators and the industries that they regulate. When Aqua refers to a consolidated rate structure and related benefits, it encompasses more than having a single tariff. A consolidated rate structure involves three separate, but related, items. All three allow a policy of addressing

and integrating, small, and sometimes troubled, systems and avoiding rate shock for current customers. Without a consolidated revenue requirement, there is less incentive for a larger water or wastewater utility to acquire another small company or troubled company because the smaller company simply becomes another division requiring additional administrative burdens. In Aqua's view, a consolidated rate structure policy includes:

- 1) consolidating a water revenue requirement and a wastewater revenue requirement going forward;
- 2) consolidating books and records so that the company can operate as one water company and one wastewater company; and
- 3) having one tariffed rate for water and one tariffed rate for wastewater or substantial movement towards that goal.

I. Why is a Consolidated Rate Structure Policy Beneficial?

Aqua Missouri is comprised of twelve separate rate divisions or systems with approximately 3,800 customers. Because Aqua Missouri does not have a consolidated rate structure, it essentially means that Aqua Missouri is operating twelve different companies. A consolidated rate structure reflects the use of a unified rate structure for multiple water and wastewater service areas that are owned or operated by a single utility. Under consolidated pricing, customers pay a utility the same rate for similar service, regardless of the physical location of their service area.

Adopting a consolidated rate structure policy has many benefits. It can protect against rate shock, address small system viability issues, and control administrative costs for the utility and agencies that regulate it. If a small, stand-alone system (like many of Aqua's systems in Missouri) needs major capital improvements, a consolidated rate structure will spread these costs over a larger customer base. Over the long term, a consolidated rate structure will strengthen Aqua's water and wastewater system as a whole. By being able to minimize rate shock to

customers and spread the increasing costs of capital improvements, Aqua is able to shift capital as priorities for improvements shift among the varied systems. If the risk of recovery is minimized, financial decisions can be more readily made to ensure compliance is achieved in an efficient and timely manner.

There are benefits to a fully consolidated rate structure for more than just customers. The regulator and Company will benefit as well. Not only does a consolidated rate structure facilitate affordability of rates for all customers, it also addresses ease of administration, customer understandability, fairness, rate continuity, revenue stability, predictability for the utility, and enables future acquisition of systems. A uniform rate structure can operate as an “insurance umbrella” to protect all customers – especially those of the smaller and more isolated systems – from the rate shock that could otherwise occur in the event of repairs necessitated by system failures or upgrades. Under the consolidated company approach, all customers share the risk of significant infusion of capital, and likewise all customers share in the benefit associated with a spreading of that risk across the larger body of customers.

II. Consolidated Revenue Requirement / Single Cost of Service

As mentioned above, an effective consolidation policy requires three separate, but related things: 1) consolidation of a water and wastewater revenue requirement going forward; 2) consolidating of books and records so that the company is operated as one water company and one wastewater company; and 3) having one tariffed rate for water and one tariffed rate for wastewater, or substantial movement towards that goal.

The first component of fully consolidated rate structure is to have one revenue requirement (also referred to as single cost of service) for water going forward and one revenue requirement for wastewater going forward. This request does not have anything to do with rate design or tariffs

per se. It allows the water company to essentially run as one water company and one wastewater company for ratemaking purposes. In addition, a consolidated revenue requirement (or single cost service) would treat Aqua Missouri's operations as one entity, instead of many separate systems. This is key to any consolidation policy. Without a consolidated revenue requirement, any movement toward a single tariff pricing structure does not remedy the inefficiencies associated with having twelve different revenue requirements as is the case now.

As mentioned previously, Aqua Missouri is made up approximately 3,800 customers in twelve separate systems or districts. A consolidated revenue requirement or single cost of service refers to treating Aqua Missouri's operations as one entity, instead of many separate systems, for purposes of establishing the Company's overall revenue requirement. The rationale behind it is that, similar to gas, electric, and telephone companies, there are many similar services being provided to the individual water and wastewater systems. To name a few, Aqua Missouri systems receive services from the same group of employees, transportation management, engineering, water quality experts and accountants. Adopting a consolidated revenue requirement policy would mean that the Company's costs and expenses would be tracked by water and wastewater function, rather than by each of the individual specific systems¹.

Currently, Aqua Missouri employs nine operators. This means that a utility operator who works for Aqua Missouri provides services for multiple systems. On a daily basis, he needs to record his time per system as he goes from system to system, which is burdensome and time consuming. Then, Aqua Missouri accountants must account for not only his time per system/per day, but also must track gas expenses, lease payments, maintenance expense, benefits, vehicle

¹ This does not include plant in service and CIAC. States that have adopted a single cost of service policy still track rate base and CIAC by system.

time, insurance coverage, administrative in-state overheads, etc. by accounting unit for each of the twelve districts. It is just like running twelve separate companies. This fragmentation is one of the problems in the water and wastewater industry and provides less incentives for larger companies to acquire small companies due to the administrative burden of acquiring an additional system. These administrative duties include separate tariff rates and the associated billing set up, training customer service representatives on an additional tariffed rate, setting up accounting procedures for the new small system, and other filing requirements that must be done on a system specific basis.

Commissions that have adopted a consolidated revenue requirement policy for the water and wastewater industry, just like those for electric, gas and telephone, have streamlined this accounting methodology by having one cost of service per utility service for all its systems. It further allows just one rate filing for all of the divisions saving rate case expense for customers and streamlining the process for both the regulator and the company.

The Missouri Commission has already approved a single tariff for parts of the Aqua Missouri footprint. Aqua Missouri's tariff for its Jefferson City wastewater system is consolidated. Thus, while all the plants are not physically connected, the Jefferson City wastewater system is comprised of one tariff and treated as one company for ratemaking purposes.

III. Consolidated Book and Records

The second component of a consolidated rate structure involves the consolidation of the company's books and records so that the company is operated as one water company and one wastewater company. This piece is essential to creating a single cost of service.

As stated above, Aqua Missouri is accounting for twelve systems as if they were each individual businesses. This fragmentation is one of the problems in the water and wastewater industry today and operating like this is not a viable, long-term option. It is extremely burdensome and Aqua Missouri spends an unnecessary amount of time splitting invoices and timesheets. With a fully consolidated rate structure, instead of different accounting units for example, transportation expense for each of the twelve systems, there would only be one accounting unit for water and one accounting unit for wastewater for this expense. In this example, to ensure that there is a process in place to review expenses for reasonableness, all invoices would still be maintained and tracked for later audits or review by parties.

IV. Single Tariff Pricing

The third piece of a consolidated rate structure deals specifically with rate design. Rate design is typically the last piece of a rate case and can take many various forms. The important part of rate design is not so much how many different tariff rates are proposed, but that there is one single cost of service/revenue requirement along with a plan to bring the rates closer together over time. As long as the Commission adopts a single revenue requirement policy which allows the Company to recover its full revenue requirement and allows Aqua to consolidate its books and records, the Company understands that there are lots of rate design scenarios that can be established. The key is designing rates that eliminate multiple tariff filings, confusion for customers and customer service representatives.

How does this work in practice? Even in jurisdictions where the particular commission has adopted a consolidated policy for several decades, there continues to be systems that have a rate different than the “main division” rate. In these situations, there typically is a plan to bring the outliers up to the “main division” rate over one or two rate cases. This often happens with

new acquisitions. For example, in states that have adopted a consolidated revenue requirement policy, a new acquisition that may have very low rates will be included in the Company's revenue requirement and the rates will be brought up to the "main division" rate over one or two rate cases.

In Aqua's past experience, the transition from system-specific rates to a consolidated approach can be difficult for some customers to understand and accept in the short run, particularly those customers whose tariffed rates do not fully reflect the cost of service to them. In these instances, it is important to note that as long as there is one revenue requirement and the utility is recovering its full revenue requirement, movement towards a consolidated rate can be done over several rate cases. When discussing possible drawbacks to a consolidated rate structure, the issue of fairness to certain customers is sometimes discussed. However, in a consolidated structure fairness issues are alleviated over time and Aqua asserts that the associated negatives are far outweighed by the positives of adopting this policy. As indicated above, with a consolidated rate structure in place, major infrastructure improvement costs, as well as unexpected costs, are levelized over a larger customer base; just like they are in the electric, gas and telecommunication industries. As a result, the impact of future rate increases are minimized over time.

V. Regulatory Issues

As to the Commission's authority to impose single tariff pricing, Aqua Missouri asserts the Commission already has the authority to adopt this policy and there is nothing preventing it from applying it further. In fact, the Missouri Commission already has approved a consolidated rate strategy for Missouri electric and gas customers and for Aqua's Jefferson City systems. Almost all the states in the United States have rules and regulations that address the principles of

cost of service for ratemaking purposes and treating ratepayers fairly, similar to those in Missouri. These same states have adopted consolidated rate structure policies with the support of the state's respective consumer advocate and attorney general's office. The question really is how quickly or gradually the movement to a single tariff price takes place.

In addition, it is likely that Aqua Missouri would have to merge its corporate structures to become fully consolidated. In other jurisdictions, Aqua has filed its request to merge legal entities along with its request for consolidation.

In summary, a consolidated rate structure has been recognized by many commissions as sound public policy. A consolidated rate structure can facilitate small system viability throughout the state and encourages expansion and consolidation by way of future acquisitions of small systems. When discussing drawbacks, the Commission should consider long-term policy goals in determining the appropriate rate structure rather than short term results and how the adoption of such a policy encourages consolidation and finding solutions for small or troubled systems.

Per the request of the Commission, Aqua Missouri has also performed the following analysis based on 4,000 gallons per month of usage. All options produce the last allowed revenue requirement overall for all systems per the April 2010 rate decisions.

VI. Tariff Options

Option One – One Rate

Fixed base charge with no usage; all consumption priced the same per gallon

System	Current Monthly	New Monthly	Dollar Difference
Maplewood-water	17.19	35.16	17.97
Riverside –water	28.86	35.16	6.30
White Branch- water- fulltime	53.00	35.16	(17.84)
White Branch-water-parttime	42.40	35.16	(7.24)

Rankin Acres-water	50.08	35.16	(14.92)
Spring Valley-water	53.65	35.16	(18.49)
Ozark Mountain-water	45.03	35.16	(9.87)
Lakewood-water	55.15	35.16	(19.99)
LTA-water	40.20	35.16	(5.04)
Jefferson City-wastewater	53.22	47.00	(6.22)
Maplewood-wastewater	18.05	47.00	28.95
Ozark Meadows-wastewater	56.56	47.00	(9.56)

Option Two- Two Rates

Two rates for water and two rates for wastewater; minimum bill includes 2,000 gallons of usage per month.

System	Current Monthly	New Monthly	Dollar Difference
Maplewood-water	17.19	22.00	4.81
Riverside –water	28.86	22.00	(6.86)
White Branch- water-fulltime	53.00	52.00	(1.00)
White Branch-water-parttime	42.40	52.00	9.60
Rankin Acres-water	50.08	52.00	1.92
Spring Valley-water	53.65	52.00	(1.65)
Ozark Mountain-water	45.03	52.00	6.97
Lakewood-water	55.15	52.00	(3.15)
LTA-water	40.20	52.00	11.80
Jefferson City-wastewater	53.22	53.00	(0.22)
Maplewood-wastewater	18.05	19.00	.95
Ozark Meadows-wastewater	56.56	53.00	(3.56)

Option Three – Three Rates for Water and Two for Wastewater

Minimum bills include 2,000 gallons per month

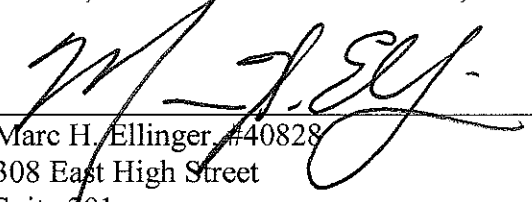
System	Current Monthly	New Monthly	Dollar Difference
Maplewood-water	17.19	22.00	4.81
Riverside –water	28.86	22.00	(6.86)
White Branch- water-fulltime	53.00	52.00	(1.00)
White Branch-water-parttime	42.40	43.00	.60
Rankin Acres-water	50.08	52.00	1.92
Spring Valley-water	53.65	52.00	(1.65)
Ozark Mountain-water	45.03	43.00	(2.03)
Lakewood-water	55.15	52.00	(3.15)
LTA-water	40.20	43.00	2.80

Jefferson City-wastewater	53.22	53.00	(0.22)
Maplewood-wastewater	18.05	19.00	.95
Ozark Meadows-wastewater	56.56	53.00	(3.56)

Respectfully submitted,

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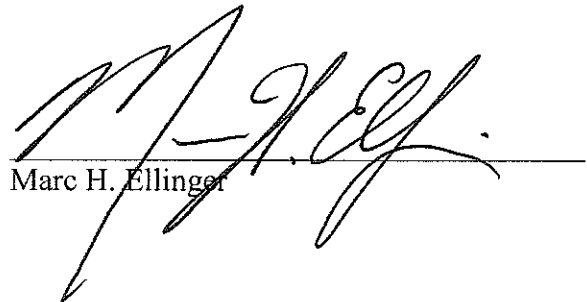
CERTIFICATE OF SERVICE

I hereby certify that a true copy of the above Aqua Missouri Brief in Support of a Consolidated Rate Structure was sent electronic mail to the following parties of record on this 1st day of September, 2010:

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