

Exhibit No.:
Issues: Cost of Service, Rate Design
Witness: Brian C. Collins
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Sponsoring Party: MIEC
Case Nos.: WR-2015-0301
Date Testimony Prepared: March 4, 2016

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

**In the Matter of Missouri-American Water
Company's Request for Authority to Implement
a General Rate Increase for Water and Sewer
Service Provided in Missouri Service Areas**

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Surrebuttal Testimony of

Brian C. Collins

On behalf of

Missouri Industrial Energy Consumers

March 4, 2016



Project 10135

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Surrebuttal Testimony of Brian C. Collins

1 **Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A Brian C. Collins. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 **Q ARE YOU THE SAME BRIAN C. COLLINS WHO PREVIOUSLY FILED**
5 **TESTIMONY IN THIS CASE?**

6 A Yes, I am.

7 **Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?**

8 A This testimony is presented on behalf of the Missouri Industrial Energy Consumers
9 ("MIEC").

10 **Q WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY ON CLASS**
11 **COST OF SERVICE AND RATE DESIGN ISSUES?**

12 A The purpose of my surrebuttal testimony is to respond to the rebuttal testimonies of
13 Missouri-American Water Company ("Missouri-American" or "Company") witness
14 Dr. Karl A. McDermott and Commission Staff witness Mr. James A. Busch. I will also
15 comment on the testimony of Dr. Geoff Marke submitted on behalf of the Office of the

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1 Public Counsel ("OPC"). The fact that I do not address a particular position or
2 assumption of any witness in this proceeding should not be construed as agreement
3 with that position or assumption.

4 **Q WHAT IS THE MAIN POINT OF YOUR TESTIMONY?**

5 A I continue to recommend that District-Specific Pricing ("DSP") be used in Missouri
6 because it best reflects cost of service principles. Consolidated pricing should be
7 rejected.

8 **Response to Company Witness Dr. McDermott**

9 **Q IN HIS REBUTTAL TESTIMONY, DOES DR. MCDERMOTT CONTINUE TO**
10 **RECOMMEND CONSOLIDATED PRICING FOR THE COMPANY'S DISTRICTS?**

11 A Dr. McDermott appears to continue to recommend consolidating pricing for the
12 Company's districts.

13 **Q COULD YOU PLEASE SUMMARIZE THE REASONS FOR HIS**
14 **RECOMMENDATION?**

15 A Dr. McDermott questions whether embedded costs are the appropriate method for
16 determining cost of service in this case. He actually argues that marginal costs are
17 likely a better indicator of cost of service since it is his belief that marginal costs
18 should not differ much across the Company's districts.

1 Q HAS DR. MCDERMOTT PROVIDED ANY ANALYSIS OF THE COMPANY'S
2 MARGINAL COSTS TO SUPPORT HIS BELIEF?

3 A No.

4 Q HOW DO YOU RESPOND TO DR. MCDERMOTT'S REBUTTAL TESTIMONY?

5 A Dr. McDermott's rebuttal testimony attempts to minimize the significance of historical
6 embedded costs in determining the rates of the Company's customers in its districts.
7 These marginal cost arguments ignore the economies of scale created through large
8 water distribution systems relative to those of small systems. As such, the marginal
9 cost of service for a very large water district is likely not the same as the marginal
10 cost of service for a very small water distribution system. Even if the marginal costs
11 to serve were similar between districts, the embedded costs incurred to produce and
12 deliver the water in the districts are different and simply cannot be ignored. Hence,
13 Dr. McDermott's marginal cost of service argument is in error and without merit.

14 Q DOES DR. MCDERMOTT MAKE ANY ARGUMENTS YOU WOULD SPECIFICALLY
15 LIKE TO ADDRESS?

16 A Yes. At page 5 of his rebuttal testimony Dr. McDermott opines that allocated costs
17 would likely vary far more dramatically between individual customers in the same
18 district than across districts. As a result, Dr. McDermott appears to dismiss retaining
19 DSP for this reason. He claims that the logical conclusion to my recommendation to
20 continue to set district-specific rates based on historical embedded costs is individual
21 cost of service pricing since this would reduce subsidies between customers.

1 **Q HOW DO YOU RESPOND?**

2 A First, Dr. McDermott has not presented any empirical evidence to support his claim
3 that costs would not vary dramatically between districts. Second, as Dr. McDermott
4 correctly states at page 6 of his rebuttal testimony, neither I nor anyone else in this
5 proceeding, has recommended rates be set on individual customers' cost of service.
6 Reasonable customer classifications within districts is the accepted method of pricing.
7 Therefore, Dr. McDermott's attempt to take DSP to this extreme position (individual
8 customer pricing) is without merit.

9 It is important to note that all of Dr. McDermott's attempts to minimize the
10 concept that rates should be set on DSP using historical embedded costs fail to
11 recognize that the Company's individual districts are not interconnected. As a result
12 of this lack of interconnectivity between districts, a water treatment plant in one district
13 that was designed and constructed to serve customers in that particular district,
14 cannot provide service to customers in other districts that are not interconnected.
15 Under Dr. McDermott's view of the world, it would be appropriate to recover these
16 costs from all Missouri-American customers under consolidated pricing. However, it
17 is important to keep in mind that his proposal ignores the concept of cost causation.
18 Under the Company's proposal for consolidated pricing, costs incurred to provide
19 service to customers in a specific district are not recovered from only customers in
20 that district. Instead, those costs are recovered from all customers in all districts. To
21 properly recognize the concept of cost causation, DSP should be continued to the
22 greatest extent possible.

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1 Q SHOULD THE COMPANY ABANDON THE EMBEDDED COST OF SERVICE
2 PRECEDENTS THAT ARE USED IN WATER AND OTHER UTILITY RATE-
3 SETTING CASES?

4 A No. To ignore the embedded costs of the Company is to ignore how the Company
5 has incurred costs to serve its customers in its various districts and to ignore the
6 differences in cost incurred to serve the Company's customers in its different districts.
7 Determining rates for the Company's districts using a method other than embedded
8 costs, such as marginal costs, would be a drastic departure from regulation in
9 Missouri and would not reflect the Company's cost of serving its customers.
10 Dr. McDermott is relying on economic principles which the Commission has not
11 recognized in setting rates for Missouri ratepayers and his proposals should be given
12 no consideration by the Commission.

13 **Response to Commission Staff Witness Mr. Busch**

14 Q MR. BUSCH INDICATES IN HIS REBUTTAL TESTIMONY THAT YOUR
15 RECOMMENDATION FOR DSP LACKS CLARITY WITH RESPECT TO THE RATE
16 DESIGN FOR BRUNSWICK AND NEWLY ACQUIRED SMALL WATER
17 DISTRICTS. COULD YOU PLEASE CLARIFY YOUR RECOMMENDATION WITH
18 RESPECT TO RATE DESIGN?

19 A As I stated in my rebuttal testimony, I recommend that the seven largest districts
20 remain on DSP, which is currently the Company's rate design. These seven districts
21 include: St. Louis Metro, St. Joseph, Joplin, Jefferson City, Platte County, Mexico,
22 and Warrensburg. My recommendation best reflects cost-causation principles and

1 recognizes the differences in the costs of providing water service among each of
2 these separate districts.

3 Further, I recommend that the remaining small districts,¹ including Brunswick
4 and newly acquired smaller districts, continue to be combined as a single water
5 district with multiple groups. Under present rates, one group consists of systems that
6 are charged a flat rate, while the other three groups' rates are based on similar
7 commodity charges within each group. I recommend this concept be continued for
8 the newly acquired water districts.

9 **Q DOES MR. BUSCH MAKE ANY ARGUMENTS THAT YOU WOULD**
10 **SPECIFICALLY LIKE TO ADDRESS?**

11 A Yes. At page 14 of his rebuttal testimony, Mr. Busch does not agree that under
12 consolidated pricing, some districts would be providing subsidies to other districts.
13 His reasoning is that since many costs, for example, corporate overhead costs, are
14 not directly allocated, and that any given allocation method could allocate more or
15 less costs to any given district, consolidating pricing does not really mean that one
16 district is subsidizing another.

17 **Q HOW DO YOU RESPOND?**

18 A Corporate overhead costs are typically allocated on a customer basis, and as a
19 result, are not generally the cause of subsidization between districts. Like
20 Dr. McDermott, Mr. Busch's arguments ignore how the Company has historically
21 incurred costs to serve its customers in its various districts that are not

¹Anna Meadows, Redfield, Lake Carmel, Brunswick, Stonebridge, White Branch, Lake Taneycomo, Lakewood Manor, Rankin Acres, Spring Valley, Tri-States, Emerald Pointe, Maplewood, and Riverside Estates.

1 interconnected. In addition, Mr. Busch's arguments also ignore the cost differences
2 that do indeed exist to serve the Company's customers in its different districts.
3 Ignoring the concept of cost causation, which Mr. Busch's arguments do, is
4 inappropriate.

5 **Comments on OPC Testimony**

6 **Q HAVE YOU REVIEWED THE REBUTTAL TESTIMONY OF OPC WITNESS**
7 **DR. GEOFF MARKE?**

8 A Yes. Dr. Marke at page 2 of his testimony states that OPC continues to maintain its
9 original position that further consolidation of the water districts is not presently
10 supported by the facts in this case. At page 9 of his testimony, he indicates that the
11 Company's proposal would be a complete departure from the regulatory principle of
12 cost causation. In general, I am supportive of the arguments that Dr. Marke
13 discusses in his opposition to rate consolidation. In fact, many of the arguments
14 presented by Dr. Marke I have also discussed in my rebuttal testimony.

15 **Q DOES DR. MARKE CONTINUE TO SUPPORT DSP?**

16 A Yes, he does and so does Ms. Leslie Haase, Financial Director of the City of Joplin,
17 who also submitted rebuttal testimony supporting DSP.

18 **Q DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

19 A Yes, it does.

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