

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

In the Matter of Missouri-American Water )  
Company's Request for Authority to ) Case No. WR-2017-0285  
Implement General Rate Increase for )  
Water and Sewer Service Provided in )  
Missouri Service Areas )

**INITIAL BRIEF OF THE  
MISSOURI DIVISION OF ENERGY**

The Missouri Department of Economic Development - Division of Energy (“DE”) respectfully offers this initial brief on two contested issues before Public Service Commission (“Commission”) regarding Missouri American Water Company’s (“MAWC” or “Company”) request for a rate increase: (1) **residential customer charges**; and (2) MAWC’s **lead service line replacement program**. DE also briefly addresses three issues that were settled through filed agreements regarding: (1) **inclining block rate design**, (2) **special contract rates**, and (3) the **revenue stabilization mechanism** (“RSM”).

**I. Residential Customer Charge for Water Service**

**Issue:** *What is the appropriate customer charge for each customer class?*

The customer charge is the flat monthly or quarterly charge that MAWC customers pay regardless of whether they use an abundance of water or no water at all during a billing period. Determining what rate is “appropriate” provides the Commission with an opportunity to weigh important rate design considerations such as costs, equity, fairness, gradualism, and efficiency.<sup>1</sup> Regarding efficiency, properly designed rates can promote the important public policy goal of water efficiency by structuring rates to incent residential customers to manage their water usage. Water

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<sup>1</sup> Exhibit (Ex.) 602, Hyman Rate Design Direct, p. 8; Transcript (Tr.), pp. 860, 873.

efficiency results in energy efficiency because providing water service requires MAWC to use a substantial amount of power to pump, treat, distribute, and dispose of water and wastewater, and reduced water use results in reduced energy usage.<sup>2</sup>

Lower customer charges encourage water and energy efficiency because when a customer charge is low, the volumetric rates (rate paid per volume of water used) must necessarily be higher than they would be with a high customer charge. Rate designs that recover more revenues through the volumetric rate and less revenues through a flat charge provide customers with greater control over their water bills and promote efficiency because customers see greater benefits of efficiency through a lower bill.<sup>3</sup> In contrast, rate designs that include more cost recovery in a flat charge reduce the customer's ability to control his or her bill, and in turn, weaken the efficiency price signal.<sup>4</sup> If a customer knows he or she will be required to pay a high rate regardless of usage, the customer will have little or no price incentive to reduce his or her usage. However, if the customer knows his or her efficiency efforts will result in greater bill savings, an incentive to use water efficiently is provided with each billing statement. DE urges the Commission to issue an order finding that rate designs that encourage water efficiency are in the public interest, and to apply that finding to the Commission's decision on this issue.

The large majority of MAWC's water customers (84%) live in the St. Louis service area within District 1 and currently pay a quarterly customer charge of \$22.35.<sup>5</sup> The other sixteen percent (16%) of MAWC customers are billed monthly and charged a monthly customer charge of \$15.33. In this case, MAWC proposes to increase the customer charge for the large majority (84%) of

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<sup>2</sup> *Id.*, p. 5.

<sup>3</sup> *Id.*, p. 6.

<sup>4</sup> *Id.*

<sup>5</sup> Ex. 137 shows the following meters per district: District 1 (St. Louis): 481,263 meters (84%); District 2: 46,476 meters (8%); and District 3: 48,449 meters (8%).

customers by proposing a twenty-five percent (25%) increase to the quarterly customer charge by raising the rate to \$30.00 per quarter. This proposed rate increase is linked with a second proposal to reduce the customer charge to \$10.00 for the small minority of monthly-billed customers.

While the reduction in the monthly customer charge is a move in the right direction, the Company's proposal to raise the quarterly customer charge fails to recognize the opportunity to promote water and energy efficiency. Rather than raise the quarterly customer charge to \$30.00 to be in line with a \$10.00 monthly charge, a better policy from the perspective of efficiency is to maintain the \$22.35 customer charge for quarterly billed customers and set the monthly charge at one-third of the quarterly charge, or \$7.45 per month.<sup>6</sup>

The setting of the customer charge should also recognize other variables such as costs, equity, fairness, and gradualism.<sup>7</sup> In considering gradualism, DE asks the Commission to consider that MAWC's customers already experienced significant rate shifts in MAWC's last rate case. Less than two years ago, in Case No. WR-2015-0301, the Commission consolidated MAWC's many separate water systems into three water districts, which resulted in significant rate shifts between water systems.<sup>8</sup> For customers served by the St. Louis County and Jefferson County water systems, the quarterly rate just twenty months ago was \$14.44 before MAWC raised that rate by thirty-six percent (36%) to \$22.35.<sup>9</sup> MAWC now wants to increase the rate to \$30.00 before customers have had a sufficient time to adjust to the customer charge increase ordered by the Commission in the last rate

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<sup>6</sup> Ex. 602, Hyman Rate Design Rebuttal, pp. 5-7; Tr., p. 872.

<sup>7</sup> *Id.*, p. 8; Tr., p. 860.

<sup>8</sup> *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*, Case No. WR-2015-0301, Report and Order, May 26, 2016.

<sup>9</sup> Missouri American Water Co. Tariff, Form No. 13, P.S.C. Mo. No. 6, (15th revised) Sheet No. RT 1.0 for St. Louis County and Jefferson County, effective July 1, 2010 to July 19, 2017.

case. If approved, MAWC's proposal would result in more than double the customer charge in a short period of time. This change would add a *disincentive* to pursue efficiency for the most of MAWC's customers. DE urges the Commission to order MAWC to maintain the \$22.35 quarterly customer charge and reduce the monthly customer charge to \$7.45, i.e., one third of the current quarterly customer charge.

## II. Lead Service Line Replacement Program

**Issue:** *Should MAWC continue to replace the customer-owned portion of lead service lines (LSL) while performing water main repair and replacement?*

There are a number of issues before the Commission regarding MAWC's Lead Service Line Replacement Program. DE does not take a position on all lead line issues in this case, but on the primary issue identified above, DE encourages the Commission to order MAWC to continue replacing lead service lines as those lines are discovered and disturbed during main repair or replacement projects.

All public utilities in Missouri are required to provide safe service to their customers,<sup>10</sup> and the facts established in the evidentiary hearing support a conclusion that replacing lead service lines is consistent with providing safe service and is in the public interest. Section 393.140(2), RSMo. entrusts the Commission with the following oversight:

Investigate and ascertain, from time to time, the quality of gas or water supplied and sewer service furnished by persons and corporations, . . . , and have power to order such reasonable improvements as will best promote the public interest, preserve the public health and protect those using such gas, electricity, water, or sewer system, and those employed in the manufacture and distribution thereof, and have power to order reasonable improvements and extensions of the works, wires, poles, pipes, lines,

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<sup>10</sup> Section 393.130.1, RSMo.

conduits, ducts and other reasonable devices, apparatus and property of gas corporations, electrical corporations, water corporations, and sewer corporations.

There should be no question that the Commission has the authority to order MAWC to replace lead service lines to address water quality and public health concerns.

The facts of the case affirm that lead exposure is evident in St. Louis County,<sup>11</sup> and disruption of lead service lines creates the potential for additional exposure. According to the Centers for Disease Control and Prevention (“CDC”), there is no safe level of lead in the bloodstream of children – a population highly vulnerable to lead exposure.<sup>12</sup> The Commission recognized in its Report and Order in Case No. WU-2017-0296:

MAWC is embarking upon the [Lead Service Line Replacement] program because lead is a naturally occurring metal that is harmful if inhaled or swallowed, particularly to children and pregnant women. Lead exposure can cause a variety of adverse health effects. For example, lead exposure can cause developmental delays in babies and toddlers and deficits in the attention span, hearing and learning abilities of children. It can also cause hypertension, cardiovascular disease and decreased kidney function in adults. The most common sources of lead exposure are paint and dust, but lead can also be found in drinking water.<sup>13</sup>

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<sup>11</sup> Centers for Disease Control and Prevention, 2016, “Lead – State and Local Programs – Missouri Data, Statistics and Surveillance,” <https://www.cdc.gov/nceh/lead/data/state/modata.htm>, Ex. 601, Hyman Revenue Rebuttal, Schedule MRH-Reb-RR1, p. 7 of 13.

<sup>12</sup> Centers for Disease Control and Prevention, 2017, “Lead,” <https://www.cdc.gov/nceh/lead/>, Ex. 601, Hyman Revenue Rebuttal, Schedule MRH-Reb-RR1, p. 6 of 13; Tr., pp. 461, 469.

<sup>13</sup> *In the Matter of the Application of Missouri-American Water Co. for an Accounting Order Concerning MAWC’s Lead Service Line Replacement Program*, Case No. WU-2017-0296, Report and Order, November 30, 2016, p. 6.

The Commission's findings are consistent with the findings of the CDC and the U.S. Environmental Protection Agency's ("EPA") listing of the risks from lead exposure.<sup>14</sup> In addition to the direct health benefits of reducing lead exposure, replacing lead lines provides the added benefit of improving economic development opportunities for communities by maintaining a high quality of life, supporting the growth of businesses, and avoiding the potential damage to economic development resulting from the known presence of lead service lines.<sup>15</sup>

DE is mindful of the concerns raised by the Office of the Public Counsel ("OPC") and OPC's proposed alternative for continuing lead service line replacement while studies are conducted. DE shares an interest in ensuring prudent expenditures under the program. In addition, DE agrees that there could be a more appropriate way to target ratepayer support for service line replacements. DE disagrees with placing a two-year limit on the replacement program or a cap on expenditures for lead service line replacement. While a two-year (or sooner) target for study completion could be reasonable, DE recommends the Commission order the lead service line replacements to continue until the study is complete and the Commission has had an opportunity to review the study results; DE also recommends that the Commission not impose a cap on the expenditures for lead service line replacements, which would risk the degradation of service due to the potential need for the Company to choose between disturbing lead service lines and avoiding areas with lead service lines (even if water mains need improvement in those areas). OPC also stated it would not object to continuing the program for a reasonable length of time if the study results are not available after two years.

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<sup>14</sup> U.S. Environmental Protection Agency, 2017, "Learn About Lead – What are the Health Effects of Lead?", <https://www.epa.gov/lead/learn-about-lead>, Ex. 601, Hyman Revenue Rebuttal, Schedule MRH-Reb-RR1, p. 5 of 13.

<sup>15</sup> Ex. 601, Hyman Revenue Rebuttal, p. 6.

In regard to the list of other lead service line issues, DE supports a program that prioritizes lead replacements towards at-risk populations such as children and expectant mothers, especially those in low-income households.<sup>16</sup> DE also supports full-disclosure of the existence of a lead line to the customer being served by that line. A collaborative effort could address lead service line issues that were not fully developed in the record of this case due to a lack of available information.

### **III. Inclining Block Rates**

DE sees significant value in inclining block rate designs and their ability to incent efficient usage, and seeks to ensure that inclining block rates are designed appropriately to better promote efficiency without penalizing customers for their non-discretionary usage.

DE's witness, Mr. Martin R. Hyman, addressed inclining blocks in his Direct, Rate Design Rebuttal and Surrebuttal testimonies. In Direct Testimony, Mr. Hyman provides three general goals to consider when designing an inclining block rate: (1) an inclining block rate, "... should encompass the basic amount of indoor water usage for an average household" while also considering, "... the balance between encouraging efficient water use and the fact that some households are larger than "average;"<sup>17</sup> (2) an inclining block rate requires consideration of the number of blocks and the rate difference between blocks, including a consideration of the price signals within each block;<sup>18</sup> and (3) an inclining block rate design should avoid severe bill impacts on high-use customers.<sup>19</sup>

In his Rate Design Rebuttal Testimony, Mr. Hyman urges caution when he states, "DE's recommendation is only to implement inclining block rates if such a rate design would not cause

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<sup>16</sup> Tr., pp. 458-459.

<sup>17</sup> Ex. 600, Hyman Direct Testimony, p. 11.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*, p. 12.

unduly adverse bill impacts on customers.”<sup>20</sup> DE’s concern is that the move to an inclining block rate design should be done with a full understanding of bill impacts resulting from any revenue requirement increase or other rate-impacting changes adopted by the Commission in this case and in MAWC’s last rate case.<sup>21</sup> For example, if the Commission orders all water service areas to be consolidated into a single statewide district, that decision could have significant and varying impacts on rates paid by MAWC’s customers; for example, with no increase to customer charges, Rate A customers in the current District 3 could see an increase of 18.4 percent at 5,000 gallons of usage per month.<sup>22</sup> Such impacts should be known before adopting an inclining block rate design to ensure the inclining block rate design does not unreasonably compound an already challenging rate increase for residential customers.

DE is a signatory to the March 1, 2018 Stipulation and Agreement (“Agreement”) that resolved the inclining block issue and a number of other issues.<sup>23</sup> The Agreement includes the statement that the parties are concerned with the lack of sufficient data regarding inclining blocks - a concern shared by DE. DE is also mindful of the Commission’s directive for the parties to provide sufficient information on inclining blocks in this case, and full compliance with the Commission’s directive could have avoided this information problem. However, looking at this issue prospectively, DE continues to support the terms of the Agreement, and urges the Commission to order the parties to abide by the Agreement’s terms. The Agreement requires the creation of a working docket to gather data necessary to evaluate the appropriateness of implementing inclining block rates, including

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<sup>20</sup> Ex. 602, Hyman Rate Design Rebuttal, p. 9.

<sup>21</sup> *Id.*

<sup>22</sup> Ex. 46, Response of Missouri-American Water Company to Commission Order Directing Filing of Additional Exhibits, p. 5.

<sup>23</sup> EFIS No. 261.



a detailed listing of information to be supplied by MAWC to help guide the Commission in its rate design decisions in MAWC's next rate case.

DE is also a signatory to the March 8, 2018, Stipulation and Agreement Regarding Inclining Block Pilot Program ("Inclining Block Agreement"), and urges the Commission to also approve this agreement and order its terms followed.<sup>24</sup> In particular, the Inclining Block Agreement seeks to establish a pilot inclining block rate design for the Mexico, Missouri water system. Under the pilot, residential customers in Mexico would switch to an inclining block rate design that includes three usage-based rate blocks. The first block would include a volumetric rate applied to the first 3,000 gallons of usage; the second block would include a fifteen percent (15%) higher volumetric rate for the next 7,000 gallons of usage; and the final block would include another twenty-five (25%) volumetric rate increase for all usage above 10,000 gallons.<sup>25</sup> Additionally, the stipulation provides for the distribution of water efficiency kits to customers in the Mexico system and allows for one billing "leak adjustment" without regard to any leak adjustment such customer may have previously received.

The intent of the pilot inclining block design is to capture the majority of non-discretionary indoor water usage in the first block so that most customers would not be subject to an increased rate block for non-discretionary usage. The fifteen percent (15%) increase in the 2<sup>nd</sup> block was decreased from the initial proposal in an effort to lessen the impact on any customers that may have more than 3,000 gallons in non-discretionary indoor usage without the ability to manage their usage and avoid the higher block (e.g., larger than average households).<sup>26</sup> The third block was increased from the

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<sup>24</sup> EFIS No. 267.

<sup>25</sup> *Id.*

<sup>26</sup> Tr. 923.

initial proposal to a twenty-five percent (25%) increase to provide an added incentive for efficient usage, targeting discretionary usage such as watering a lawn.<sup>27</sup>

DE supports a Commission decision that approves the pilot inclining block rate design proposal and a decision that orders MAWC to gather the data necessary to fully evaluate the pilot program and its impacts on usage in the Company's next rate case.

#### **IV. Special Contract Rate for Triumph Foods, LLC**

Triumph Foods, LLC ("Triumph"), "... is a pork processing operation located in St. Joseph, Missouri" that, "... employs over 2,800 employees at its St. Joseph operation."<sup>28</sup> Triumph is the second largest employer in St. Joseph, and the single largest customer of MAWC.<sup>29</sup> According to Triumph witness Mr. Brian Collins, "... the other customers of St. Joseph are paying less for water service than if Triumph Foods were not on the MAWC system."<sup>30</sup> Testimony received at the local public hearing in St. Joseph indicates that Triumph, "... has an annual payroll of greater than \$120 million (with taxes), pays \$4.8 million per year in state and local payroll taxes, and pays \$1.5 million per year in local property taxes."<sup>31</sup>

The Agreement includes a "Special Contracts" term whereby the parties agree MAWC's special contracts will continue, and that the Triumph contract will be revised consistent with the Rebuttal Testimony of Staff witness Mr. Matthew Barnes. Mr. Barnes testified that Triumph meets the criteria for the special contract rate under MAWC's Economic Development Rider to its tariff, and that Triumph provides, "... numerous economic benefits to the St. Joseph area and the State of

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<sup>27</sup> *Id.*

<sup>28</sup> Ex. 505, Collins Surrebuttal, p. 2.

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> Ex. 603, Hyman Surrebuttal, p. 3.

Missouri.”<sup>32</sup> DE encourages the Commission to approve the Agreement and help Triumph remain a vital contributor to the economy of the St. Joseph area and the State of Missouri.

**V. Revenue Stabilization Mechanism (RSM)**

MAWC has withdrawn its request for an RSM rate design, contingent upon the Commission approving the Agreement. DE’s position on the RSM is that it should not be granted in this case, as explained by Mr. Hyman, in the following Q&A:

**Q. Does DE support the implementation of an RSM in this case?**

A. No, not at this time. The RSM request might be reasonable if the Company were implementing robust practices to encourage demand-side water and energy efficiency that resulted in a meaningful level of customer savings. As a form of “decoupling,” the RSM could theoretically make the Company indifferent to changes in customer usage, enabling better support of demand-side efficiency programs; better support of demand-side efficiency programs can be a reason to support the shifting of revenue recovery risk from the Company to ratepayers. However, the Company’s programs are in their initial phases, following an agreement in MAWC’s previous rate case. At a minimum, an RSM should not be adopted until the Company has shown the ability to effectively implement and manage demand-side efficiency programs, and the Company should first propose a detailed and robust plan to encourage demand-side water efficiency that includes target reductions in water and energy usage and evaluations of the plan’s effectiveness. (Citation omitted.)

For these reasons, DE urges the Commission to reject the request for an RSM in this case and approve the Agreement as written.

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<sup>32</sup> Ex. 115, Barnes Rebuttal, p. 4.

Respectfully submitted,

*Marc Poston*

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### **CERTIFICATE OF SERVICE**

I hereby certify that copies of the foregoing have been served electronically on all counsel of record this 30<sup>th</sup> day of March 2018.

*Marc Poston*

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Marc Poston