

*Exhibit No.:*  
*Issues:* Security Accounting  
Authority Order; Roark  
Sewer Plant Operating Costs;  
and Acquisitions  
*Witness:* Paul R. Harrison  
*Sponsoring Party:* MoPSC Staff  
*Type of Exhibit:* Surrebuttal Testimony  
*Case No.:* WR-2011-0337  
*Date Testimony Prepared:* February 2, 2012

**MISSOURI PUBLIC SERVICE COMMISSION**  
**REGULATORY REVIEW DIVISION**  
**UTILITY SERVICES**

**SURREBUTTAL TESTIMONY**

**OF**

**PAUL R. HARRISON**

Staff Exhibit No. 24  
Date 2-2-12 Reporter JL  
File No WR-2011-0337

**MISSOURI-AMERICAN WATER COMPANY**

**CASE NO. WR-2011-0337**

*Jefferson City, Missouri*  
*February 2012*

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PAUL R. HARRISON  
MISSOURI-AMERICAN WATER COMPANY  
CASE NO. WR 2011-0337**

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1 **EXECUTIVE SUMMARY**

2 Q. In summary, what does your Surrebuttal Testimony cover?

3 A. This testimony will address three issues raised by the Company and Public  
4 Counsel witnesses in their Rebuttal Testimony.

5 The first issue concerns MAWC's witness Peter J. Thakadiyil's Rebuttal Testimony  
6 wherein he requests rate base treatment for security costs that were deferred pursuant to a  
7 Commission ordered Accounting Authority Order (AAO) in Case No. WO-2002-273.

8 The second issue addresses the Company's concerns with Staff's adjustment to  
9 eliminate Roark Sewer's test year chemical expense in its direct filing due to the lack of  
10 appropriate source documents supporting the costs.

11 Finally, I will address Public Counsel's proposal that the Commission should depart  
12 from its consistent practice of reflecting the net book value of the acquired properties in  
13 MAWC's rate base as proposed by MAWC and recommended by Staff in this case. I  
14 provided Staff's recommendation in my Rebuttal Testimony that the net book value of the  
15 acquired properties should be used in determining rates for this case.

16 **UNAMORTIZED BALANCE OF THE SECURITY AAO**

17 Q. What is MAWC's security cost AAO?

18 A. In Case No. WO-2002-273, the Commission approved the deferral of costs  
19 related to the improvement and enhancement of security at MAWC's facilities. The  
20 Company was allowed to accumulate the deferral for two years following the terror attacks of  
21 September 11, 2001, and continuing through September 11, 2003.

22 Q. How did the Commission's Order address the rate base treatment for these  
23 security costs?

1           A.     The Commission did not address rate base treatment of these security costs.  
2 MAWC started amortizing the deferral over a ten-year period beginning December 31, 2002,  
3 and the amortization of these costs will end December 31, 2012.

4           Q.     Has Staff's Cost of Service ever included recovery of the unamortized amounts  
5 of these security costs in MAWC's rate base?

6           A.     No. The unamortized amount of the security costs has never been included in  
7 rate base in Staff's Cost of Service in MAWC rate cases since the deferral began.

8           Q.     Has Staff's Cost of Service ever included the amortization of the deferred  
9 security costs in rate cases since the deferral began?

10          A.     Yes, the amortization has consistently been included since the deferral began.

11          Q.     Why does Staff oppose the Company's request to include the unamortized  
12 balance of the security cost AAO in rate base?

13          A.     Including the unamortized balance in rate base would inappropriately shift the  
14 regulatory balance in favor of MAWC. Since Case No. GR-98-140, addressing Missouri Gas  
15 Energy's (MGE's) service line replacement plan (SLRP) deferrals, the Commission deemed it  
16 proper for the ratepayers and shareholders to share the effect of the regulatory lag by allowing  
17 MGE to earn a return of, but not a return on, the deferred balance of those costs. The  
18 Commission recognized the balancing of interests in that MGE case by making use of a  
19 shorter amortization period than Staff had recommended (ten years), but not allowing  
20 recovery on the unamortized balance as part of MGE's rate base.

21                 Staff contends that the same principles of ratemaking equity should apply to this issue.  
22 Staff recommends the Commission not tip the balance, at this time, in favor of MAWC by  
23 modifying the rate base treatment of the deferral while maintaining the same deferral period.

1 To be consistent with previous Commission Orders, and to properly balance MAWC and  
2 ratepayer interests, Staff recommends a ten-year amortization of these deferred security costs  
3 in this proceeding with no inclusion in rate base.

4 **ROARK SEWER PLANT OPERATING EXPENSES**

5 Q. What is the issue with Roark Sewer Plant Operation Expenses?

6 A. In MAWC's direct filing, the Company included \$393,946 in test year  
7 chemical expense related to Roark Sewer operations. Staff disallowed this amount because the  
8 Company could not provide support for this expense. After further research, Mr. Thakadiyil  
9 states in his Rebuttal Testimony that it had misclassified plant operation expense as chemical  
10 expenses. He goes on to recommends that the amount in question be included in MAWC  
11 rates as an Operations & Maintenance (O&M) expense.

12 Q. How did MAWC determine that the plant operations expense was  
13 misclassified as chemical expense?

14 A. Mr. Thakadiyil states on page 14, lines 5 through 8 of his Rebuttal Testimony  
15 that "based on the 2010 Roark Water and Sewer, Inc. Annual Report that was filed with the  
16 Commission, \$393,946 of plant operation expense was incurred during the test year. The  
17 expense includes contracted maintenance expenses, repairs of sewer plant and utility bills."

18 Q. Did Staff review the 2010 Roark Water and Sewer, Inc. Annual Report that  
19 was filed with the Commission in an attempt to determine the correct amount of this expense?

20 A. Yes. The 2010 Roark Water and Sewer, Inc. Annual Report identifies  
21 contracted maintenance expense of \$11,667, repairs of sewer plant -- pump repair of \$57,395,  
22 repairs of sewer plant -- collecting sewers and manhole repair of \$304,489 and utility bills of  
23 \$20,395 for a total of \$393,946.

1 Q. Does Staff agree that these unaudited annual expense levels should be included  
2 in Roark Sewer's cost of service for this rate case as maintenance expense?

3 A. No. Staff has concerns with whether these expenses are actual expenses or  
4 whether some of them should be capitalized. In previous small water and sewer rate  
5 cases, including requests by Roark and Tri-State Utilities, Staff identified several instances  
6 where costs classified as O&M expenses by the utilities were actually capital in nature. Two  
7 of the maintenance expense items for Roark Sewer that I mentioned above (repairs of sewer  
8 plant – pump repair of \$57,395 and repairs of sewer plant – collecting sewers and manhole  
9 repair of \$304,489) are similar in nature to expense items that Staff reclassified as capital  
10 expenditures in Roark's last rate case. Staff has no way of determining if some of the costs  
11 booked by Roark as O&M expenses should be capitalized instead of expensed.

12 The Company has not provided any source documents, such as invoices, or prior  
13 year's information which would allow Staff to determine if these expenses are prudently  
14 incurred normal ongoing costs. Typically in rate cases, Staff reviews multiple years of data  
15 for each expense, so the Staff can include a normal ongoing level of expense in its cost of  
16 service. The last Roark Water and Sewer Inc. rate case was performed by Staff in calendar  
17 year 2003 and these operating expenses at that time were approximately \$90,000, which is  
18 significantly lower than the 2010 reported expenses in the Annual Report.

19 Q. Does Staff have additional concerns with including this level of expense in  
20 Roark Sewer's and the other Acquired Properties' Cost of Service?

21 A. Yes. MAWC acquired 14 separate properties since its last rate case and Staff  
22 conducted several meetings with the Company in order to ensure that the non-recurring  
23 expenses for these properties, that were either no longer necessary or should be capitalized,

1 were adjusted out of MAWC's test year for this proceeding. MAWC told Staff these costs  
2 had been removed from this case; however, when Staff reviewed these costs in Roark's  
3 Annual Report there were little to no change in the level of expense from what was included  
4 in MAWC's claimed test year expense. Staff is reviewing the last three years of Commission  
5 Annual reports for all 14 of these acquired properties (since there is no historical data  
6 available), in order to ensure that Staff has only included a normal on-going level of operating  
7 expenses in its Cost of Service for these operations.

8 Q. Does Staff agree with Mr. Thakadiyil's following statement on page 14,  
9 lines 10 through 20?

10 The Company pays to have its wastewater treated. The City of  
11 Branson treats the wastewater from the Roark sewer district and  
12 charges the Company \$4.80 per thousand gallons for residential  
13 service and \$9.23 per thousand gallons for commercial service.  
14 Based on the usage included in the Company's filing for Roark  
15 Water, the annualized level of expense for this contracted  
16 maintenance service alone would be \$288,739 or more than  
17 70% of the total test year plant operation expenses.

18 A. No, Staff does not agree this quantification of Roark wastewater treatment  
19 expenses is reasonable. Staff has received additional information from the Company  
20 (Company workpapers and contracts from the city of Branson) for this cost and we completed  
21 our own analysis to determine if these costs are reasonable.

22 Q. Based upon this analysis, what amount of Roark wastewater treatment expense  
23 does Staff recommend for inclusion in its cost of service?

24 A. \$105,126.

25 Q. Why is Staff's calculation of this expense different from the Company's  
26 calculation?



1           A.     Staff used its annualized and normalized **wastewater usage** to calculate this  
2 expense, while MAWC used its annualized and normalized **water usage** to determine this  
3 cost for this case.

4           Q.     What is Mr. Thakadiyil's recommendation regarding Roark Sewer plant  
5 operating expenses for this case?

6           A.     In Rebuttal Testimony, page 14, lines 29 through 33, Mr. Thakadiyil  
7 recommends that "Staff should reclassify the expenses in their respective accounts and allow  
8 the Company recovery of plant operation expenses in the amount of \$393,946."

9           Q.     Does Staff agree with Mr. Thakadiyil's recommendation that this plant  
10 operating expense should be recovered in rates?

11          A.     Yes, to some degree. As discussed above, Staff agrees that \$105,126 of  
12 expense should be recovered in rates for Roark Sewer. However, as also discussed above,  
13 Staff is reviewing the last three years of Commission Annual reports for all 14 of MAWC's  
14 Acquired Properties in order to ensure that Staff has included a normal ongoing level of  
15 operating expenses in its Cost of Service for all of the Acquired Properties. Staff will  
16 complete this review prior to filing its reconciliation February 9, 2012 and will make any  
17 necessary changes to its revenue requirement for these properties.

18           **MAWC'S ACQUISITIONS**

19          Q.     What properties has MAWC acquired since its last rate case?

20          A.     MAWC has purchased Loma Linda (File No. WO-2011-0015), AQUA  
21 Missouri (File No. WO-2011-0168), and Roark Water and Sewer (File No. WO-2011-0213) .

22          Q.     What was the effective date of the Commission Orders to transfer these assets  
23 to MAWC?

1           A.     The Loma Linda assets were transferred on January 21, 2011, while the AQUA  
2 Missouri assets were transferred on May 16, 2011, and the Roark Water and Sewer assets  
3 were transferred to MAWC on July 29, 2011.

4           Q.     What was the test year used by Staff to file its cost of service report?

5           A.     The test year for this case was the twelve months ending December 31, 2010.  
6 Staff's Cost of Service Report reflects known and measurable changes for net rate base items  
7 as of December 31, 2010. Staff will review and determine the Acquired Properties' net rate  
8 base as of December 31, 2011, when Staff conducts its true-up audit.

9           Q.     How will Staff value the Acquired Properties' net rate base in its true-up audit?

10          A.     Staff will review the plant records from MAWC's acquisition cases, previous  
11 rate cases, general ledgers, invoices and the acquired properties continuing property records  
12 (that are available) to determine the proper amount of rate base for the Acquired Properties as  
13 of December 31, 2011.

14          Q.     Public Counsel and Staff's calculations for the value of the Acquired  
15 Properties net rate base are different in the current MAWC rate case. Can you identify why  
16 there is a difference between Public Counsel and Staff in this value?

17          A.     Yes. In Mr. Robertson's Rebuttal Testimony, he compares the purchase prices  
18 for these properties with the plant, depreciation reserve, contributions in aid of constructions  
19 (CIAC), CIAC amortization and other rate base items as of the closing dates or dates when the  
20 property was transferred to MAWC ( i.e., early 2011). Staff has consistently used the net rate  
21 base that was recorded on the Company's books and records as of December 31, 2010, which  
22 is before the dates in which the assets were purchased by MAWC or transferred to MAWC.

1 Q. In the Rebuttal Testimony, page 16, lines 10 through 21, Public Counsel  
2 witness Mr. Robertson states the following Question and Answer:

3 Q. IS IT PROBABLE THAT WHITE RIVER VALLEY  
4 ELECTRIC COOPERATIVE, INC. WILL EVENTUALLY  
5 RECOVER A SIGNIFICANT PORTION OF THE LOSS IT  
6 INCURRED FROM THE PURCHASE PRICE BEING LESS  
7 THAT THE NET BOOK VALUE OF THE ASSETS IT  
8 SOLD?

9 A. Yes. Depending on its financial situation, it is probable that  
10 the loss White River incurred from the sale of the assets at a  
11 price less than net book value will result in a tax benefit which  
12 will allow it to recoup a portion of the assets value which  
13 MAWC now seeks to earn a return on and a return of. Since it is  
14 likely White River will be allowed to write-off the loss on the  
15 sale for tax purposes, the associated tax benefit will allow it to  
16 recover an additional amount of the net book value of the assets  
17 it sold thereby reducing its actual loss. However, it is MAWC's  
18 position that ratepayers be forced to pay for those assets again  
19 even though they will have been fully recovered by White  
20 River.

21 Do you agree with his answer?

22 A. No. White River Electric (the parent company of Roark) is a Cooperative.  
23 Cooperatives are tax exempt organizations and do not pay taxes or receive tax benefits  
24 from the IRS. Please see the quote below from Section 12. Organizations Exempt Under  
25 IRC 501 (c) (12):

26 IRC 501 (c) (12) exempts the following organizations from  
27 federal income tax:

- 28 • mutual ditch or irrigation companies  
29 • mutual or cooperative telephone companies  
30 • mutual or cooperative electric companies  
31 • "like organizations"

32 1. Ditch and irrigation companies, telephone companies, electric  
33 companies, and "like organizations" that seek exemption under  
34 IRC 501(c)(12) must be organized and operated as mutual or  
35 cooperative organizations. The terms "mutual" and  
36 "cooperative" have no legal distinction for purposes of section

1 501(c)(12). The U.S. Tax Court defined "cooperative" as  
2 follows:

3 "A cooperative is an organization established by individuals to  
4 provide themselves with goods and services or to produce and  
5 dispose of the products of their labor. The means of production  
6 and distribution are those owned in common and the earnings  
7 revert to the members, not on the basis of their investment in the  
8 enterprise, but in proportion to their patronage or personal  
9 participation in it." Puget Sound Plywood, Inc. v.  
10 Commissioner, 44 T.C. 305 (1966), *acq.* 1966-2 C.B. 6.

11 Q. In Rebuttal Testimony, page 17, lines 2 through 19, Public Counsel witness

12 Mr. Robertson states the following:

13 Furthermore, in the Roark acquisition case, File No. WO-2011-  
14 0213, et al., the Commission's Order Granting Applications to  
15 Transfer Assets, Approving Stipulation and Agreement, And  
16 Granting Waiver, Dated April 27, 2011, approved a Unanimous  
17 Stipulation And Agreement attached as Appendix A to the  
18 Order). On page two of the Unanimous Stipulation And  
19 Agreement it states:

20 MAWC shall be authorized to file revised tariff sheets in the  
21 current Roark water and sewer tariffs containing new CIAC fees  
22 totaling \$2,450 per customer applicable to the next 300 new  
23 customers in Forest Lake subdivision, to expire twenty (20)  
24 years after the effective date of the revised tariff sheets.

25 Q How was the Roark acquisition case resolved?

26 A. On April 6, 2011, Staff, Public Counsel, MAWC and Roark filed a Unanimous  
27 Stipulation and Agreement.

28 Q. Did that Unanimous Stipulation and Agreement include the section pertaining  
29 to the authorization to file tariff sheets containing new CIAC fees for the Forest Lake  
30 subdivision in the Roark Water and Sewer Acquisition case?

31 A. Yes.

1           Q.    Do the new CIAC fees for the Forest Lake subdivision totaling \$735,000 have  
2 any impact on rates or the net book value of Roark district that is included on MAWC's  
3 books?

4           A.    No. Staff and the Company have both agreed to remove the entire \$735,000  
5 from rate base at the time of the acquisition.

6           Q.    Does this conclude your Surrebuttal Testimony?

7           A.    Yes, it does.



**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-2011-0337  
Implement A General Rate Increase for Water )  
and Sewer Service Provided in Missouri )  
Service Areas )

AFFIDAVIT OF PAUL R. HARRISON

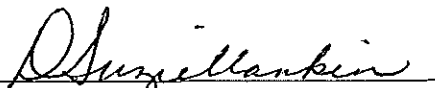
STATE OF MISSOURI     )  
                                  )     ss.  
COUNTY OF COLE     )

Paul R. Harrison, of lawful age, on his oath states: that he has participated in the preparation of the foregoing Surrebuttal Testimony in question and answer form, consisting of 11 pages to be presented in the above case; that the answers in the foregoing Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

  
\_\_\_\_\_  
Paul R. Harrison

Subscribed and sworn to before me this 1<sup>st</sup> day of February, 2012.

D. SUZIE MANKIN  
Notary Public - Notary Seal  
State of Missouri  
Commissioned for Cole County  
My Commission Expires: December 08, 2012  
Commission Number: 08412071

  
\_\_\_\_\_  
Notary Public