

Exhibit No.

Regulatory Policy Testimony

B. K. Turner

Direct Testimony

St. Louis County Water Co.

WR-95-145

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. WR-95-145

DIRECT TESTIMONY

OF

B. K. TURNER

Exhibit No. 11
Date 6/19/95 Case No. WA-95-145
Reporter BAT

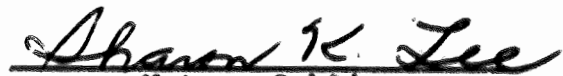
STATE OF MISSOURI)
) SS
COUNTY OF ST. LOUIS)

AFFIDAVIT OF B. K. TURNER

The undersigned, B. K. Turner, having been first duly sworn on his oath, states that the exhibit entitled "Direct Testimony of B. K. Turner", and consisting of 13 pages, contains his answers under oath to the questions therein propounded to him, and that the Appendix A, inclusive, to the testimony of B. K. Turner, Vice President, Rates and Operations Analysis of St. Louis County Water Company, St. Louis, Missouri, are true and correct copies of the appendix referred to in his testimony, all of which testimony and appendix have been prepared in written form by him for introduction into evidence in Public Service Commission Case No. WR-95-145 on behalf of St. Louis County Water Company.


B. K. Turner

Subscribed and sworn to before me this 6th day of
December, 1994.


Notary Public

SHARON K. LEE, Notary Public
STATE OF MISSOURI, ST. LOUIS COUNTY
MY COMMISSION EXPIRES FEBRUARY 21, 1995

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WITNESS INTRODUCTION

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Q. WHAT IS YOUR NAME AND BUSINESS ADDRESS?

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A. My name is B. K. Turner, and my business address is 535 N.
New Ballas Rd., St. Louis, Missouri.

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Q. WHAT IS YOUR POSITION WITH ST. LOUIS COUNTY WATER CO?

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A. I am Vice President of Rates And Operations Analysis.

13

Q. WOULD YOU DESCRIBE YOUR BACKGROUND AND QUALIFICATIONS?

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A. Yes. My background and qualifications are listed in
Appendix A of this testimony.

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PURPOSE AND SCOPE

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Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?

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A. Included in my responsibilities with the Company is to
direct regulatory activities and to provide guidance in
regulatory matters. Specifically, at the direction and
approval of the Chairman of the Board it is my
responsibility to establish and carry out the regulatory
philosophy of the Company to make certain the goals of the
Company and the regulatory environment in which we operate
are in sync.

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1 GOALS OF COMPANY FILING

2 Q. WHAT ARE THE GOALS OF THE COMPANY WITH REGARD TO THIS
3 FILING?

4 A. The Company has three major goals it hopes to accomplish
5 relative to this filing. First, the Company believes it
6 necessary to embark on a significant distribution system
7 infrastructure replacement program, the beginning of which
8 has been incorporated into this filing. Secondly, the
9 Company hopes to address and resolve regulatory lag
10 problems that have plagued its financial health over the
11 last several years. Finally, the Company seeks to address
12 and resolve several issues that have a significant impact
13 on its ability to generate adequate cash flows.

14 Q. WOULD YOU PLEASE EXPLAIN IN GREATER DETAIL EACH OF THESE
15 GOALS?

16 A. Yes, but it must be recognized from the beginning that
17 these goals are interdependent and each must be achieved
18 for the Company to continue to operate as it has in the
19 past.

20 With regard to the distribution system infrastructure
21 replacement program, both Mr. Buescher and Mr. Tinkey have
22 referred to presentations made to this Commission, the
23 Commission Staff, and Public Counsel. The conclusions
24 presented were based upon the belief that the Company has
25 an obligation to provide equivalent service to future
26 customers as it has provided to past customers. Any

1 contrary belief flies in the face of what regulation and
2 cost of service have always attempted to accomplish. It
3 would be wrong to allow past generations to enjoy reliable
4 service with absolutely no consideration for customers in
5 the future.

6 It is because of this that the Company has included
7 within the context of this case the beginning of an
8 infrastructure replacement program. This program will
9 begin the necessary replacements to insure that future
10 customers will enjoy the same reliable service the Company
11 has provided in the past.

12 **Q. FACILITY REPLACEMENTS APPEAR TO BE A NORMAL PART OF THE**
13 **LIFE CYCLE OF BUSINESS. WHY HAS THE COMPANY PROCLAIMED**
14 **THIS TO BE A SIGNIFICANT GOAL IN THESE PROCEEDINGS?**

15 **A.** The implementation of this program marks the formal
16 recognition of the beginning of the second generation of
17 the Company's distribution system. The regulatory
18 significance of this is the inflation that has occurred
19 over the life of the first generation of pipe compounded by
20 the increased complexity of replacement versus initial
21 installation. These factors will cause dramatic increases
22 in the levels of capital investment required and in turn
23 become a driving force to the ultimate cost to the
24 consumer. How these costs are recovered make this a
25 significant goals of these proceedings.

26 As I stated previously, the three major goals of the
27 Company related to this filing are interdependent and it is

1 the significance of beginning this replacement program
2 which makes this so. If the Company is to embark on such a
3 significant course it must be able to maintain financial
4 health and stability.

5 Q. WOULD YOU PLEASE SUMMARIZE THE PROPOSED INFRASTRUCTURE
6 PROGRAM?

7 A. Yes. The program as a whole was discussed in great detail
8 in the presentations mentioned earlier. In short, however,
9 the Company proposes to begin a 5 year phase-in of a
10 program designed to establish an ongoing level of
11 guaranteed annual capital expenditures for main replacement
12 of \$19,200,000. This amount will be evaluated for
13 sufficiency at the end of that period. The phase-in
14 includes \$3,750,000, \$8,400,000, \$11,900,000, \$15,500,000
15 and \$19,200,000 for years 1 through 5 , inclusive.

16 Q. YOU STATED GUARANTEED ANNUAL CAPITAL EXPENDITURES, WHAT DO
17 YOU MEAN BY THIS?

18 A. Assuming the Company is able to accomplish the remaining
19 two significant goals with respect to this case, this means
20 the Company will guarantee to this Commission that it will
21 begin to make the five year levels of capital expenditures
22 covered in this filing. It is a commitment by the Company
23 to the infrastructure program both in the short-term and
24 long-term, assuming regulatory cooperation in maintaining
25 the financial health of the Company.

26 Q. TURNING TO THE REMAINING GOALS WOULD YOU CONTINUE WITH YOUR
27 EXPLANATION?

1 A. Yes. The second goal deals with regulatory lag. In this
2 case we are specifically talking about regulatory lag
3 associated with capital investment and related items. Even
4 before the infrastructure program the Company has been and
5 continues to be concerned about its inability to achieve
6 timely rate recovery for capital investments made and items
7 related to those capital investments (i.e. depreciation,
8 interest on debt) as a result of regulatory lag.

9 Throughout history the Company has been able to
10 effectively deal with regulatory lag because it was
11 experiencing growth which helped to offset the effects.
12 However, currently and for the foreseeable future this will
13 not be the case due to a limited growth rate combined with
14 increasing capital expenditures. This scenario will simply
15 be exacerbated if the infrastructure program is implemented
16 absent steps to counteract the effects of regulatory lag
17 creating the interdependency referred to previously.

18 It is because of this that we have included within the
19 context of this case an alternative to current practice to
20 reduce the effects of regulatory lag. The Company's
21 alternative is explained in detail by Witness Jenkins, who
22 also explains that it is not the only alternative. I echo
23 Mr. Jenkins' statements, and pledge the Company's
24 willingness to discuss and accept reasonable solutions to
25 this problem. From the Company's perspective, it is not
26 the method to solve the problem that is imperative, it is

1 that a solution be achieved allowing implementation of the
2 infrastructure program.

3 Q. WHY IS THIS ISSUE CRITICAL TO THE IMPLEMENTATION OF THE
4 INFRASTRUCTURE PROGRAM?

5 A. This program differs from many types of capital investment
6 programs because individual projects are completed in short
7 time periods, that cannot be synchronized with the
8 ratemaking process. Because of this, only minor amounts of
9 interest during construction accrue while depreciation
10 expenses on much higher amounts of plant than that retired
11 and that are not included in rates flow through the income
12 statement. This deteriorates the Company's financial
13 position.

14 Q. WOULD YOU CONTINUE WITH YOUR FINAL SIGNIFICANT GOAL?

15 A. The final significant goal deals with the Company's ability
16 to generate cash flow for capital investment. Again
17 reflecting the interdependency of our goals, the Company
18 could not possibly embark on the infrastructure program,
19 much less guarantee capital investment, with anything less
20 than stable cash flows.

21 If we are to be successful with our infrastructure
22 program we must investigate and maximize all cash flow
23 sources and insure their use for main replacement. Within
24 this case the Company proposed two rate treatments it
25 believes are imperative to adequacy and stabilization of
26 cash flow.

27 First, the Company has proposed a revenue based

1 accrual for costs associated with maintenance of mains.
2 Due to the nature of costs associated with maintenance of
3 mains (i.e. increasing levels, weather fluctuation, etc.)
4 past historical ratemaking practices have caused these
5 costs to significantly impact the availability and
6 stability of cash flow. Cash needed to support capital
7 investments has, out of necessity, had to be used to
8 support maintenance costs. If the Company is to push its
9 capital investment requirements to the maximum it is
10 imperative that all sources of cash flow be protected.
11 Witness Jenkins explains the details of this maintenance
12 accrual in his Direct Testimony.

13 **Q. YOU STATED THERE WERE TWO RATEMAKING PROPOSALS RELATED TO**
14 **CASH FLOW, WOULD YOU PLEASE EXPLAIN THE SECOND?**

15 **A. Yes, the second proposal deals with the adjustment or**
16 **true-up of the reserve for depreciation. Throughout the**
17 **life cycle of property, evaluations of estimated life,**
18 **salvage, and cost of removal are made. Each time there is**
19 **a significant change in any of these components, the**
20 **composite depreciation rate is changed. As property**
21 **reaches its true life, absent adjustment, the net property**
22 **value and the reserve for depreciation will not be**
23 **synchronized reflecting the over or under collection of the**
24 **net property value.**

25 This is the case with the Company's reserve for
26 depreciation. Changes to composite depreciation rates over
27 time have produced a reserve deficiency primarily due to

1 increasing costs related to the removal of property from
2 service. This is particularly important when viewed in
3 light of the proposed infrastructure program as the Company
4 begins to incur this cost of removal. If the Company has
5 not collected these removal costs from its ratepayers,
6 valuable capital investment cash flow will be usurped,
7 limiting the Company's ability to make the necessary
8 replacements.

9 Q. HOW DOES THE COMPANY PROPOSE TO COLLECT THIS RESERVE
10 DEFICIENCY FROM THE RATEPAYERS?

11 A. The Company is proposing a phased ten year amortization of
12 this reserve deficiency. The Company views this as vital
13 to the success of the infrastructure program and intends to
14 funnel all dollars collected to that program. In other
15 words this is not cash for the sake of cash, or to allow
16 the Company to liquidate its interests in the Company. To
17 the contrary it is necessary low-cost cash all of which
18 will be used to rebuild the Company's aging distribution
19 system infrastructure. Witness Jenkins provides the
20 details of this amortization in his Direct Testimony.

21 Q. BASED UPON YOUR TESTIMONY IT WOULD APPEAR THAT THE GOALS
22 YOU CITED ARE ALSO REQUIREMENTS THE COMPANY NEEDS TO
23 PROCEED WITH THE PROPOSED INFRASTRUCTURE PROGRAM. IS THIS
24 THE COMPANY'S POSITION?

25 A. Yes. The reality is that it would be a financial
26 impossibility for the Company to embark on such a program
27 absent successfully addressing these goals.

1 ratemaking process. Specifically, in this case, given the
2 short period of time that has transpired since our last
3 filing, the Company has chosen to cut back on the type and
4 amount of Cost of Money outside expertise employed. This
5 decision was made subsequent to discussions with Commission
6 Staff responsible for issues in this area and stands as an
7 excellent example of how all parties win through result
8 oriented open communications.

9 Q. ARE THERE ANY OTHER AREAS WHERE THE COMPANY HAS TAKEN A
10 DIFFERENT APPROACH?

11 A. Yes. The Company has cut back dramatically its defensive
12 direct testimony posture. Throughout the filing, the
13 Company has attempted to provide a "substance over form"
14 and "to the point" presentation allowing for easy
15 identification of issues believed significant to provide
16 for what it hopes to be a less complex and controversial
17 evaluation process. We have done so with much trepidation
18 from the resulting exposure to accusations of failure to
19 prove and inadequate documentation. Again, our actions are
20 a result of the ongoing discussions with the parties and
21 our desire to make the proceedings more manageable,
22 efficient, and cost effective. We can and will add
23 documentation or testimony on any issue which either Staff
24 or Public Counsel feels has been slighted.

25 Q. COULD YOU PROVIDE SOME EXAMPLES THAT DEMONSTRATE THE
26 COMPANY'S ACTIONS?

1 A. Two prime examples are fair value rate base and assumptions
2 used in FAS 87 & 106 computations. The company has
3 traditionally filed voluminous testimony related to fair
4 value rate base, some of which had to be prepared by
5 outside consultants, for the sole purpose of preserving its
6 rights in the event of appeal. This testimony, while not
7 only time consuming and somewhat costly, simply added
8 another layer of data that had to be reviewed and evaluated
9 belaboring the process.

10 The second item and one that caused the Company a
11 great deal of consternation was the submission of extensive
12 direct testimony relative to the assumptions utilized in
13 the FAS 87 and FAS 106 calculations. These assumptions are
14 determined by outside consultants making the actuarial
15 calculations. Extensive in-depth direct testimony would
16 have required the employment these outside consultants with
17 costs ranging from \$200 to \$350 per hour. In the
18 alternative the Company has completed an in-house review of
19 the assumptions for reasonableness, as well as conducting
20 discussions with our actuaries to insure that all
21 assumptions utilized were based upon sound actuarial
22 practice. This action alone saved the ratepayers between
23 \$10,000 and \$15,000.

24 Q. WHY WAS THE COMPANY SO CONCERNED OVER THIS ACTION?

25 A. Over the past few years the Company's direct testimony has
26 grown to become a massive compilation of rhetoric designed
27 to circumvent accusations of "failure to prove" which in

1 some instances were used to advocate exclusion of
2 unavoidable costs in its rates. It is the concern over
3 this potential tactic again that makes the Company so
4 concerned.

5 Q. ARE YOU AWARE THAT THE BURDEN IS ON THE COMPANY TO PROVE
6 THAT COSTS TO BE INCLUDED IN RATES ARE FAIR AND REASONABLE?

7 A. Absolutely. However, an attempt to include every detail of
8 that proof in direct testimony is not productive given the
9 investigatory expertise and ability of both the Commission
10 Staff and Public Counsel, not to mention the extreme cost
11 to the ratepayer. The Company believes the same can be
12 accomplished much more efficiently during the investigation
13 process if all parties are willing to approach ratemaking
14 in an above board, professional manner.

15 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

16 A. Yes.

Qualifications of B. K. Turner

My name is B. K. Turner and I live at 3452 Texas Ave., St. Louis, Missouri 63118. I am Vice President, Rates and Operations Analysis for St. Louis County Water Company.

I graduated from Lincoln University in 1975 with a Bachelor of Science Degree in Business Administration with a major in Accounting. I received a Master of Science in Taxation degree from Fontbonne College in May 1993. I have been a Certified Public Accountant since 1981, and currently hold a license to practice in the State of Missouri.

Between 1975 and 1978 I was employed by the Missouri Public Service Commission as a Public Utility Accountant. My duties included conducting and assisting in audits and examinations of the books and records of utility companies operating within the State of Missouri in regard to proposed rate increases.

In 1978 I accepted the position of Accounting Manager with Financial Data Systems, Inc. a corporate holding company providing automated financial services to banks and savings and loans. I was responsible for all accounting and financial operations of the parent and its six subsidiaries. My areas of responsibility included general accounting, budgeting, bank relations, financing, leasing, internal data processing, and financial reporting.

Between 1982 and 1985 I was employed by the Missouri State Auditor. My responsibilities included conducting audits of and for the State of Missouri and the development and presentation of audit staff training.

I was employed by St. Louis County Water Company from 1979 to 1982 as a Rates and Internal Audit Accountant. In 1982 I was transferred to Continental Water Company, the parent company of St. Louis County Water Company as Accounting Manager. I was employed by Missouri Water Company, a sister company of St. Louis County Water Company, located in Independence, Missouri as Comptroller from 1985 to 1986. In 1986, I was employed by MWC Management Services, Inc., a sister company of St. Louis County Water Company as Comptroller until July 1, 1987. I have been employed by St. Louis County Water since July 1, 1987 and on December 1, 1993 the Board of Directors appointed me Vice President of Rates and Operations Analysis.

During the course of my career, I have prepared and submitted financial and accounting testimony in numerous rate proceedings primarily before this Commission. I have also provided consulting services to several utility companies in the areas of rate regulation, financial management, and rate design. I am currently Chairman of the Rates and Revenue Committee of the National Association of Water Companies.

I am a member of the American Institute of Certified Public Accountants, Missouri Society of Certified Public Accountants, Society of Depreciation Professionals, Society of Rate of Return Analysts, National Association of Water Companies and the American Water Works Association.