

Exhibit No.:

Issue(s):

Accounting Authority Order;
Water Treatment Plant Overview

Witness/Type:

Trippensee/Direct

Sponsoring Party:

Public Counsel

Case Nos.:

WR-2000-281

DIRECT TESTIMONY

OF

RUSSELL W. TRIPPENSEE

FILED²
APR 03 2000
Missouri Public
Service Commission

Submitted on Behalf of
the Office of the Public Counsel

MISSOURI-AMERICAN WATER COMPANY

Case No. WR-2000-281

APRIL 3, 2000

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

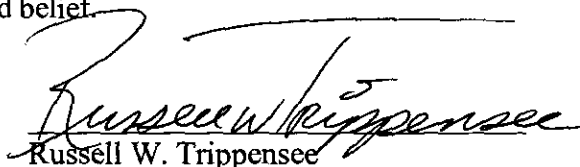
In the matter of Missouri-American Water)	
Company's tariff sheets designed to)	
Implement general rate increases for water)	Case Nos. WR-2000-281 and
And sewer service provided to customers)	SR-2000-282
In the Missouri area of the company.)	

AFFIDAVIT OF RUSSELL W. TRIPPENSEE

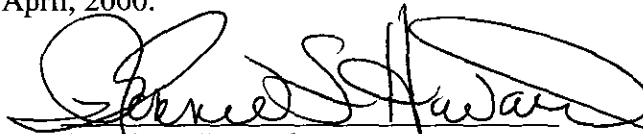
STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Russell W. Trippensee, of lawful age and being first duly sworn, deposes and states:

1. My name is Russell W. Trippensee. I am the Chief Public Utility Accountant for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my direct testimony consisting of pages 1 through 19 and Schedule RWT-1.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.


Russell W. Trippensee

Subscribed and sworn to me this 3rd day of April, 2000.


Bonnie S. Howard
Notary Public

My commission expires May 3, 2001

DIRECT TESTIMONY
OF
RUSSELL W. TRIPPENSEE
MISSOURI AMERICAN WATER COMPANY
CASE NO. WR-2000-281

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

2 A. Russell W. Trippensee. I reside at 1020 Satinwood Court, Jefferson City, Missouri 65109, and my
3 business address is P.O. Box 7800, Jefferson City, Missouri 65102.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am the Chief Utility Accountant for the Missouri Office of the Public Counsel (OPC or Public
6 Counsel).

7 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.**

8 A. I attended the University of Missouri at Columbia, from which I received a BSBA degree, major in
9 Accounting, in December 1977. I attended the 1981 NARUC Annual Regulatory Studies Program
10 at Michigan State University.

11 **Q. HAVE YOU PASSED THE UNIFORM CPA EXAM?**

12 A. Yes, I hold certificate number 14255 in the State of Missouri. I have not met the two-year
13 experience requirement necessary to hold a license to practice as a CPA.

14 **Q. PLEASE DESCRIBE YOUR WORK EXPERIENCE.**

15 A. From May through August, 1977, I was employed as an Accounting Intern by the Missouri Public
16 Service Commission (MPSC or Commission). In January 1978 I was employed by the MPSC as a

1 Public Utility Accountant I. I left the MPSC staff in June 1984 as a Public Utility Accountant III
2 and assumed my present position.

3 **Q. PLEASE DESCRIBE YOUR PROFESSIONAL AFFILIATIONS.**

4 A. I served as the chairman of the Accounting and Tax Committee for the National Association of
5 State Utility Consumer Advocates from 1990-1992 and am currently a member of the committee. I
6 am a member of the Missouri Society of Certified Public Accountants.

7 **Q. PLEASE DESCRIBE YOUR WORK WHILE YOU WERE EMPLOYED BY THE MPSC**
8 **STAFF.**

9 A. Under the direction of the Chief Accountant, I supervised and assisted with audits and examinations
10 of the books and records of public utility companies operating within the State of Missouri with
11 regard to proposed rate increases.

12 **Q. WHAT IS THE NATURE OF YOUR CURRENT DUTIES WITH THE OFFICE OF**
13 **THE PUBLIC COUNSEL?**

14 A. I am responsible for the Accounting and Financial Analysis sections of the Office of the Public
15 Counsel and coordinating their activities with the rest of our office and other parties in rate
16 proceedings. I am also responsible for performing audits and examinations of public utilities and
17 presenting the findings to the MPSC on behalf of the public of the State of Missouri.

18 **Q. HAVE YOU PREVIOUSLY FILED TESTIMONY BEFORE THE MPSC?**

19 A. Yes. I filed testimony in the cases listed on Schedule RWT-1 of my testimony on behalf of the
20 Missouri Office of the Public Counsel or MPSC Staff.

1 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

2 A. My testimony will summarize the position of the OPC regarding the appropriate regulatory
3 treatment of the water treatment facilities necessary to provide water to St. Joseph, Missouri. This
4 summary begins on page 15 of my direct testimony. I will also address the Company's request for
5 an Accounting Authority Order and the various Commission Report & Orders issued in this case
6 addressing this topic. My testimony addressing Accounting Authority Orders follows immediately.

7 **ACCOUNTING AUTHORITY ORDER**

8 **Q. WHAT IS THE ISSUE?**

9 A. On November 19, 1999, Missouri-American Water Company (Missouri-American or Company)
10 filed its Motion for an Accounting Authority Order (AAO). Missouri-American seeks authority to
11 continue to capitalize Allowance for Funds Used During Construction (AFUDC) and to defer
12 depreciation on its new plant in St. Joseph, Missouri. Company anticipates that the new plant will
13 be completed by April 30, 2000. The Company has requested a true-up to include plant-in-service
14 as of April 30, 2000 in its rate filing; however, the operation of law date for this rate filing is
15 September 14, 2000. Company wishes to accrue and defer "post-in-service" AFUDC and
16 depreciation on the new St. Joseph water treatment plant for the four and one-half months between
17 the date the new St. Joseph water treatment plant goes on-line and the date the new tariffs take
18 effect.

19 **Q. HOW WOULD YOU CLASSIFY THE COMPANY'S ACCOUNTING AUTHORITY**
20 **ORDER REQUEST?**

1 A. The Company's accounting authority order request is an attempt to insulate its shareholders from
2 regulatory lag. The Company has expended funds associated with the new water treatment plant
3 and associated other facilities to provide St. Joseph, Missouri with water. These facilities are
4 anticipated to be in-service prior to the operation of law date of this general rate case and therefore
5 before new rates (based on a cost of service study that specifically reflects the cost of the facilities)
6 can be put into effect.

7 **Q. PLEASE EXPLAIN THE CONCEPT OF REGULATORY LAG.**

8 A. This concept refers to the difference in timing of a decision by management and the Commission's
9 recognition of that decision, and its effect, if any, on the rate base/rate of return/revenue/expense
10 relationship in the determination of a company's revenue requirement. Prudent management
11 decisions may alter the rate base/rate of return/revenue/expense relationship that is the basis for the
12 overall cost of service (a.k.a., the Overall Revenue Requirement). The relationship change
13 increases the profitability of the firm in the short-run, until such time as the Commission
14 reestablishes rates which properly match the new levels of the overall cost of service components.
15 Companies are allowed to retain costs savings, i.e., excess profits during the lag period between rate
16 cases. When faced with escalating costs that will change the rate base/rate of
17 return/revenue/expense relationship adversely with respect to profits, regulatory lag places pressure
18 on management to take actions to minimize the change in the relationship and the resulting
19 decrease in profitability. Regulatory lag, stated another way, provides management with real
20 financial incentives to operate the business in an efficient manner.

1 Q. DO EVENTS SUCH AS EXPENDITURES FOR NEW TREATMENT FACILITIES
2 HAPPEN IN A VACUUM WITH RESPECT TO OTHER POSSIBLE CHANGES IN
3 THE OPERATIONS OF THE UTILITY?

4 A. No. The overall cost of service is made up of a multitude of factors. Isolating or focusing on only
5 one component, such as expenditures for new plant facilities, fails to look at all relevant factors in
6 determining the overall cost of service. Other factors may have changed that have a corresponding
7 decrease or increase on the overall cost of service. Unless all factors are analyzed, it is not
8 appropriate to single out one specific event.

9 Q. HAS THIS COMMISSION ADDRESSED WHETHER IT IS REASONABLE TO
10 PROTECT SHAREHOLDERS FROM ALL REGULATORY LAG?

11 A. Yes. This Commission has held that it is not reasonable to protect shareholders from all regulatory
12 lag. In Missouri Public Service Company, Cases Nos. EO-91-358 and EO-91-360, the Commission
13 stated:

14 Lessening the effect of regulatory lag by deferring costs is beneficial to a company
15 but not particularly beneficial to ratepayers. Companies do not propose to defer
16 profits to subsequent rate cases to lessen the effects of regulatory lag, but insist it is
17 a benefit to defer costs. Regulatory lag is a part of the regulatory process and can
18 be a benefit as well as a detriment. Lessening regulatory lag by deferring costs is
19 not a reasonable goal unless the costs are associated with an extraordinary event.

20 Maintaining the financial integrity of a utility is also a reasonable goal. The
21 deferral of costs to maintain current financial integrity though is of questionable
22 benefit. If a utility's financial integrity is threatened by high costs so that its ability
23 to provide service is threatened, then it should seek interim rate relief. If
24 maintaining financial integrity means sustaining a specific return on equity, this is
25 not the purpose of regulation. It is not reasonable to defer costs to insulate
26 shareholders from any risks. If costs are such that a utility considers its return on
27 equity unreasonably low, the proper approach is to file a rate case so that a new
28 revenue requirement can be developed which allows the company the opportunity

1 to earn its authorized rate of return. Deferral of costs just to support the current
2 financial picture distorts the balancing process used by the Commission to
3 establish just and reasonable rates. Rates are set to recover ongoing operating
4 expenses plus a reasonable return on investment. Only when an extraordinary
5 event occurs should this balance be adjusted and costs deferred for consideration in
6 a later period (Emphasis added).

7 **Q. WAS THE COMMISSION'S "EXTRAORDINARY AND NONRECURRING"**
8 **STANDARD AS OUTLINED IN RE: M.P.S. AFFIRMED BY THE WESTERN**
9 **DISTRICT COURT OF APPEALS?**

10 A. Yes, the Western District Court of Appeals states:

11 "[An AAO deferral] . . . distorts the balancing process utilized by the
12 Commission to establish just and reasonable rates. Because rates are set to
13 recover continuing operating expenses plus a reasonable return on
14 investment, only an extraordinary event should be permitted to adjust the
15 balance . . ." State ex. Rel. Missouri Office of the Public Counsel v.
16 Public Service Commission, 858 S.W. 2d 806, 810 (Mo. App. 1993).

17 The Court of Appeals also noted that the Uniform System of Accounts (USOA) defines
18 "extraordinary items" as:

19 [t]hose items related to the effects of events and transactions which have
20 occurred during the current period and which are not typical or customary
21 business activities of the company . . . Accordingly, they will be events
22 and transactions of significant effect which would not be expected to recur
23 frequently and which would not be considered as recurring factors on any
24 evaluation of the ordinary operating processes of business. . . Id. at 810.

25 **Q. WHAT DOES THE COMPANY MEAN WHEN IT USES THE TERM "DEFER"?**

26 A. When a cost that normally would be expensed and therefore reflected on the income statement is
27 deferred, the expenditure is entered on the balance sheet in a special section called Deferred Debits.
28 In this case, the specific account utilized is Account 186, Miscellaneous Deferred Debits. The

1 company's request to defer depreciation expense associated with the new water treatment facilities
2 in St. Joseph falls into this category.

3 The Company also proposes to be allowed to continue to compute Allowance for Funds Used
4 During Construction (AFUDC) after the facilities have been placed in service. This post-in-service
5 AFUDC would also be debited to Account 186 under Company's proposal. In contrast, AFUDC
6 recorded prior to the facilities being placed in-service is debited to Account 107, Construction
7 Work in Progress. After a facility is placed in-service, the related balance in Account 107 is closed
8 out and transferred to Account 101, Utility Plant-in-Service.

9 **Q. PLEASE DEFINE AN EXPENDITURE?**

10 A. An expenditure is any outflow of money paying for a good or service. An expenditure is either
11 capitalized (recorded on the balance sheet) or it is considered an expense (recorded on the income
12 statement).

13 **Q. WHAT IS AN EXPENSE?**

14 A. Expense is the use of assets and services in the creation of revenue during a specified period.
15 Expenses are recorded on the income statement and are subtracted from revenues in order to
16 determine net income for the period.

17 **Q. PLEASE DEFINE THE TERM " COST" .**

18 A. I use the term "cost" to refer to each component of the total revenue requirement of the utility. Cost
19 includes all expenses along with the earnings and interest expense associated with the rate base.
20 The total revenue requirement is also called the overall cost of service.

1 Q. HAVE YOU REVIEWED THE NATIONAL ASSOCIATION OF REGULATORY
2 UTILITY COMMISSIONERS (NARUC), UNIFORM SYSTEM OF ACCOUNTS FOR
3 CLASS A AND B WATER UTILITIES 1976 EDITION (USOA)?

4 A. Yes I have.

5 Q. ARE THE DEFINITIONS YOU PREVIOUSLY PROVIDED CONSISTENT WITH
6 HOW THE USOA APPLIES THESE TERMS?

7 A. Yes.

8 Q. PLEASE ADDRESS THE USOA ACCOUNT THAT SPECIFICALLY ADDRESSES
9 MISCELLANEOUS DEFERRED DEBITS.

10 A. On page 53 of the USOA the following definition can be found for Account 186, Miscellaneous
11 Deferred Debits:

12 186. Miscellaneous Deferred Debits.

13 A. This account shall include all debits not elsewhere provided for, such
14 as miscellaneous work in progress, losses on disposition of property, net of
15 income taxes, deferred by authorization of the Commission, and unusual
16 or extraordinary expenses, not included in other accounts, which are in
17 process of amortization and items the proper final disposition of which is
18 uncertain.

19 Q. ACCORDING TO THE USOA, IS EARNINGS A COST ITEM THAT COULD BE
20 RECORDED IN ACCOUNT 186, MISCELLANEOUS DEFERRED DEBITS?

1 A. No. Earnings (revenue minus expenses) are a component of the cost of service that USOA Account
2 186 does not provide specific authority to defer.

3 It is critical to realize that earnings are only recorded in two accounts, USOA Account 435, Balance
4 Transferred from Income, and USOA Account 216, Unappropriated Retained Earnings. Neither of
5 these accounts are expense accounts, nor are they asset accounts. Earnings are simply the product
6 of all activities of the firm during a specified period. Therefore as long as a utility's earnings for
7 any period are positive, all expenses associated with the revenue produced for the period have been
8 recouped by the utility.

9 **Q. HOW DOES AFUDC AFFECT EARNINGS IN THE CURRENT PERIOD?**

10 A. AFUDC is recorded as revenue for financial reporting purposes. Increased revenues obviously
11 mean increased earnings to report or to be used in the calculation of interest coverage.

12 **Q. WHEN DOES THE COMPANY ACTUALLY RECEIVE THE CASH ASSOCIATED**
13 **WITH THESE AFUDC REVENUES?**

14 A. The Company receives the cash over the depreciable life of the property on which the AFUDC has
15 been calculated.

16 The other half of the financial entry to record AFUDC is to debit a Construction Work in Progress
17 account. Therefore when the plant is placed in-service, the AFUDC along with the actual
18 expenditures on the project are transferred to USOA Account 101, Plant-in-Service. The total
19 balance of the project included in Account 101 is used to calculate the depreciation expense
20 recorded on the income statement for each year of its useful life. So long as the Company is able to

1 maintain a positive earnings level for utility operations, all expenses, including the AFUDC related
2 depreciation expense, are being recovered.

3 **Q. FROM A REGULATORY ACCOUNTING PERSPECTIVE, WHAT OCCURS WHEN A**
4 **COST IS DEFERRED PURSUANT TO AN ACCOUNTING AUTHORITY ORDER?**

5 A. From a regulatory accounting perspective, when a cost has been deferred it is not recognized on the
6 income statement as an expense in the current period nor is it recorded on the balance sheet as an
7 asset in an account that would normally be included in rate base. The expenditures are recorded on
8 the balance sheet in Account 186, Miscellaneous Deferred Debits, pending the final disposition of
9 the costs at some future point, usually in a rate case. Account 186 acts simply as a temporary
10 holding account until the appropriate accounting ratemaking treatment can be determined.

11 **Q. IS THE DEFERRAL OF A COST FROM ONE ACCOUNTING PERIOD TO**
12 **ANOTHER ACCOUNTING PERIOD FOR THE DEVELOPMENT OF A REVENUE**
13 **REQUIREMENT CONSISTENT WITH TRADITIONAL RATEMAKING PRACTICES?**

14 A. No. Generally, the deferral of costs from one accounting period to another accounting period for
15 the development of a revenue requirement violates the traditional method for setting utility rates.
16 Rates in Missouri are usually established based upon a historical test year which focuses on four
17 factors: (1) the rate of return the utility has an opportunity to earn; (2) the rate base upon which a
18 return may be earned; (3) the depreciation expense related to plant and equipment; and (4) the
19 allowable operating expenses including income and other taxes.

1 The relationship of the four factors is such that the expenses and rate base necessary to produce the
2 revenues is synchronized. As example, the level of chemical expense for treating raw water is
3 developed based on the raw water necessary to provide the amount of water sold that is used in the
4 determination of revenue for the test period. Similarly, the plant-in-service necessary to produce or
5 deliver that water to customers is also based on the customers' demands for the same period. This
6 process is often referred to as the "Matching Principle".

7 Deferral of costs from one period to another results in costs associated with the production of
8 revenue in one period being charged against the revenue in a different period. This violates the
9 "Matching Principle" and if unfettered would allow a utility to manage its earnings in order to
10 avoid regulatory oversight or adverse reactions from the financial community. In my professional
11 opinion, avoiding this possibility is one of the fundamental purposes of Generally Accepted
12 Accounting Principles and the USOA.

13 **Q. HAS THE COMMISSION ALLOWED REGULATED UTILITIES SUCH AS**
14 **MISSOURI-AMERICAN WATER COMPANY TO DEVIATE FROM TRADITIONAL**
15 **RATEMAKING PRACTICES TO DEFER COSTS FROM ONE ACCOUNTING**
16 **PERIOD TO ANOTHER ACCOUNTING PERIOD VIA AN ACCOUNTING**
17 **AUTHORITY ORDER?**

18 **A.** Yes. The Commission has determined that utilities, when warranted, can be allowed to defer costs
19 from prior accounting periods on a limited basis when events occur during a period which are
20 extraordinary, unusual and unique, and nonrecurring.

1 **Q. IS THE CONSTRUCTION OF THE NEW ST. JOSEPH WATER TREATMENT**
2 **PLANT AN EXTRAORDINARY EVENT IN YOUR PROFESSIONAL OPINION?**

3 A. No. The construction of the new St. Joseph water treatment plant is an event that is completely
4 controlled by Company's management. Although the size of this project is extremely large and
5 could result in a dramatic increase of rates, it remains simply a construction project. Construction
6 of facilities is a normal part of doing business for any utility. A utility must construct or have
7 access to adequate production facilities to provide safe and adequate utility service. The
8 construction of facilities is a normal part of doing business for any utility.

9 The new facility itself is designed so that it can be expanded if additional capacity is needed. The
10 expansion capability reemphasizes that the construction of water treatment facilities is a normal
11 activity of a water company. The Company's new subsidiary, formerly known as United Water
12 Missouri Inc., recently had a major construction project at its water treatment plant that resulted in a
13 rate increase of approximately 24% phased in over a two-year period. There was no post-in-service
14 AFUDC or deferred depreciation expense authorized by the Commission related to that project.

15 **Q. IN RECENT REPORT AND ORDERS HAS THE COMMISSION EMPHASIZED**
16 **THAT AAOS MOST PROPERLY ADDRESS ONLY "UNPREDICTABLE" EVENTS?**

17 A. Yes. The commission stated in St. Louis County Water, Case No. WR-96-263, page 13:

18 As both the OPC and the Staff point out, the Commission has, to date,
19 granted AAO accounting treatment exclusively for one-time outlays of
20 capital caused by unpredictable events, acts of government, and other
21 matters outside the control of the utility or the Commission. It is also
22 pointed out that the terms "infrequent, unusual and extraordinary" connote
23 occurrences which are unpredictable in nature."

1 **Q. DID THE COMPANY PLAN TO CONSTRUCT A NEW WATER TREATMENT PLANT**
2 **IN ST. JOSEPH?**

3 A. Yes. In fact the Company examined several options before choosing to construct a new water
4 treatment plant. This planning process dates back to studies produced as early as 1991. Options
5 included plans to stage the construction in segments or to complete replacement with simultaneous
6 retirement. This project and its implementation were completely within the control of MAWC
7 management. In no way was this event unpredictable.

8 **Q. IS THE PROJECT'S SCOPE OF SUCH MAGNITUDE THAT IT HAS AN**
9 **EXTRAORDINARY FINANCIAL IMPACT ON THE COMPANY?**

10 A. No. The Company has timed the filing of this case so that the new plant will be in-service
11 approximately four months prior to the time new rates will be placed into effect. The financial
12 impact due to the loss of AFUDC and the resulting reduction in earnings do not place this Company
13 in financial distress during this four-month period.

14 Earnings (Rate of Return on Equity) for the rolling twelve-month periods ending each month from
15 May, 2000 through August, 2000 are projected to remain above 8.6%. It is also projected that
16 interest coverage for the same rolling twelve- month periods will remain in excess of 2.5 times. It
17 is Public Counsel's understanding that the Company's indentures require that coverage ratios
18 remain above 1.5 times coverage.

19 Public Counsel believes these earnings and coverage ratios are adequate and in no way can be
20 construed to represent a extraordinary financial event.

1 **Q. PUBLIC COUNSEL SUPPORTED THE DEFERRAL OF REVENUE IN THE NON-**
2 **UNANIMOUS STIPULATION AND AGREEMENT FILED ON FEBRUARY 23,**
3 **2000 IN THIS CASE. PLEASE EXPLAIN WHY PUBLIC COUNSEL IS**
4 **OPPOSED TO AN AAO REQUESTING POST-IN-SERVICE AFUDC.**

5 A. The period of time before Missourians would have begun to pay higher rates to MAWC would
6 have been significantly longer if the Commission had approved the Stipulation and Agreement.
7 (This statement assumes the Company can prove that a rate increase is ultimately necessary.) The
8 Stipulation and Agreement provided that increased rates would not have been effective for MAWC
9 customers until seven and one-half months after the operation-of-law date in this case. The
10 cumulative effect of the loss of earnings would have caused the interest coverage to decline during
11 this extended period below the indenture limits previously discussed absent recognition of
12 deferred revenues. Such adverse effects are not present during the period prior to the operation-of-
13 law date in this case.

14 The calculations referred to above and also in my Direct Testimony filed on March 1, 2000 in
15 support of the Stipulation and Agreement are the same calculations.

OVERVIEW OF PUBLIC COUNSEL'S
RECOMMENDATION REGARDING ST. JOSEPH
WATER TREATMENT PLANT

Q. PLEASE SUMMARIZE PUBLIC COUNSEL'S RECOMMENDATION REGARDING THE ST. JOSEPH WATER TREATMENT PLANT.

A. Public Counsel recommends that the rate base used in the determination of MAWC's revenue requirement reflect the value of the most economical and efficient method of producing quality water for the citizens of St. Joseph, Missouri and delivering said water to the interconnection point with the Company's distribution system. Public Counsel witnesses Ted L. Bidy and Kimberly K. Bolin provide testimony that demonstrates that a 30 Million Gallon per Day (MGD) capacity for MAWC St. Joseph water treatment plant should have an economic value of no more than \$38,195,654.

Public Counsel also recommends the Commission recognize that the Company does not require 30 MGD of capacity. OPC witness Bidy's direct testimony supports a maximum plant capacity of 24.135 MGD for purposes of determining the level of used and useful treatment plant capacity to be included in rate base. Therefore, in order to recognize this excess capacity, Public Counsel recommends the Commission include 80.45% (24.135MGD / 30MGD) of the total St. Joseph water treatment plant value or \$30,728,404 in rate base initially.

Subsequent to the initial recording of \$30,728,404 in plant-in-service, Public Counsel would recommend that the Company be allowed to increase plant-in-service by \$1,273 for each .001

1 increase in the maximum MGD experienced by the Company's St. Joseph water treatment plant
2 until 30 MGD is experienced.

3 **Q. IS IT PUBLIC COUNSEL'S POSITION BASED ON THE DIRECT TESTIMONY**
4 **OF OPC WITNESS BIDDY THAT COMPANY'S DECISION TO CONSTRUCT THE**
5 **NEW WATER TREATMENT PLANT IN ST. JOSEPH INSTEAD OF**
6 **REHABILITATING THE EXISTING WATER PLANT WAS IMPRUDENT?**

7 **A.** Yes. Public Counsel believes that the Company's decision to abandon its old treatment facilities
8 and build a new treatment plant was imprudent. Mr. Biddy's professional opinion, as outlined in
9 his direct testimony, is that instead of constructing a new water treatment plant for approximately
10 \$78,000,00 (initial estimate), the Company could have expanded and updated existing water
11 treatment plant in St. Joseph in addition to upgrading the plant to a 30MGD capacity for
12 approximately \$36,307,591. Adding the existing net plant value of \$1,888,063 as developed by
13 OPC witness Bolin, results in the total maximum economic value of \$38,195,654 as recommended
14 by Public Counsel.

15 **Q. IS PUBLIC COUNSEL PROPOSING THAT THE COMPANY PHYSICALLY**
16 **ABANDON ITS NEW FACILITY AND REHABILITATE ITS EXISTING RIVER**
17 **SOURCE WATER TREATMENT FACILITY?**

18 **A.** No. Public Counsel is simply saying that the choice to build a completely new facility was not
19 prudent. The ratepayers should not be held responsible for the Company's imprudent management
20 decisions. Inclusion of the excess economic costs associated with the new facility would reward the
21 Company for making the imprudent decision of building an expensive new water treatment plant

1 instead of choosing the more economical decision of expanding and updating the existing water
2 treatment plant.

3 **Q. WHAT IS THE VALUE OF THE ST. JOSEPH WATER TREATMENT PLANT**
4 **ACCORDING TO THE COMPANY'S FILED CASE?**

5 A. \$74,684,000 (Direct Testimony of John S. Young, page 15, line 10)

6 **Q. WHAT IS THE ESTIMATED REVENUE REQUIREMENT EFFECT OF PUBLIC**
7 **COUNSEL'S PROPOSAL TO VALUE THE FACILITY AT ITS MAXIMUM**
8 **ECONOMIC VALUE?**

9 A. A \$5,141,208 reduction in the revenue requirement as requested by MAWC. This reduction
10 includes both the return on the excluded plant value, \$4,010,069 and the return of (i.e. depreciation
11 expense) of the excluded plant value, \$1,131,139.

12 The "return on" calculation is based on the overall rate of return of 8.24% which is recommended
13 by OPC witness Mark Burdette (Burdette Direct Testimony, Schedule MB-11, resulting in pre-tax
14 overall rate of return of 10.99%). This calculation is based on the difference between MAWC's
15 requested rate base and OPC's recommended maximum economic value (\$74,684,000 –
16 38,195,654 = \$36,488,346) times the pre-tax overall rate of return (10.99%).

17 The quantification of the revenue requirement associated with depreciation expense is based on a
18 composite depreciation rate of 3.01% multiplied by the excluded plant value, \$36,488,346.

1 **Q. WHAT IS THE ESTIMATED REVENUE REQUIREMENT EFFECT OF PUBLIC**
2 **COUNSEL'S PROPOSAL REGARDING ITS USED AND USEFUL CAPACITY**
3 **ADJUSTMENT?**

4 Q. A \$1,045,415 reduction in the revenue requirement as requested by MAWC. This reduction
5 includes both the return on the excluded plant value that is not used and useful capacity,
6 \$820,651 and the return of (i.e. depreciation expense) the excluded plant value, \$224,764.

7 The return on calculation is based on the overall rate of return of 8.24%, which is recommended by
8 OPC witness Mark Burdette (Burdette Direct Testimony, Schedule MB-11, resulting in a pre-tax
9 overall rate of return of 10.99%). This calculation is based on the difference between OPC's
10 maximum economic value to be included in rate base and OPC's used and useful capacity level
11 (\$38,195,654 - 30,728,404 = \$7,467,250) times the pre-tax overall rate of return (10.99%).

12 The quantification of the revenue requirement associated with depreciation expense is based on a
13 composite depreciation rate of 3.01% multiplied by the excluded plant value that is not used and
14 useful capacity, \$7,467,250.

15 **Q. PLEASE EXPLAIN WHY IT IS APPROPRIATE TO ALLOW THE COMPANY TO**
16 **INCREASE ITS PLANT-IN-SERVICE AS THE MDG OF PRODUCTION**
17 **INCREASES ABOVE THE 24.135MGD CONTAINED IN OPC WITNESS**
18 **BIDDY'S DIRECT TESTIMONY.**

19 A. Rate base should only include values associated with plant that is used and useful in the provision
20 of service to current customers. If a utility has built excess capacity that is not currently necessary

1 for the provision of service to current customers, the associated cost or value should not be included
2 in the overall cost of service on which rates are set. Allowing the Company to increase its plant-in-
3 service as the plant becomes needed properly matches the rate base with the customers' needs. To
4 require the customers to pay for excess capacity provides utilities with incentives to make
5 uneconomical choices from the ratepayers perspective. The incentive is the opportunity to reap
6 greater returns. Inclusion of excess capacity in rate base also shifts the risk associated with the
7 financial impacts of management decisions from the stockholders to the ratepayers. Such a shifting
8 of risk is neither appropriate nor consistent with competitive markets. If the Commission decides
9 to allow this shifting of risk, the authorized return on equity should be lowered to reflect the
10 reduction in risk.

11 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

12 **A. Yes.**

Direct Testimony
Russell W. Trippensee
Case No. WR-2000-281

Laclede Gas Company, Case No. GR-90-120 (OPC)
Southwestern Bell Telephone Company, Case No. TR-90-98 (OPC)
Empire District Electric Company, Case No. ER-90-138 (OPC)
Associated Natural Gas Company, Case No. GR-90-152 (OPC)
Southwestern Bell Telephone Company, Case No. TO-91-163
Union Electric Company, Case No. ED-91-122
Missouri Public Service, Case Nos. EO-91-358 and EO-91-360
The Kansas Power and Light Company, Case No. GR-91-291
Southwestern Bell Telephone Co., Case No. TO-91-163
Union Electric Company, EM-92-225 and EM-92-253
Southwestern Bell Telephone Company, TO-93-116
Missouri Public Service Company, ER-93-37, (January, 1993)
Southwestern Bell Telephone Company, TO-93-192, TC-93-224
Saint Louis County Water Company, WR-93-204
United Telephone Company of Missouri, TR-93-181
Raytown Water Company, WR-94-300
Empire District Electric Company, ER-94-174
Raytown Water Company, WR-94-211
Missouri Gas Energy, GR-94-343
Capital City Water Company, WR-94-297
Southwestern Bell Telephone Company, TR-94-364
Missouri Gas Energy, GR-95-33
St. Louis County Water Company, WR-95-145
Missouri Gas Energy, GO-94-318
Alltel Telephone Company of Missouri, TM-95-87
Southwestern Bell Telephone Company, TR-96-28
Steelville Telephone Exchange, Inc., TR-96-123
Union Electric Company, EM-96-146
Imperial Utilites Corporation, SC-96-247
Laclede Gas Company, GR-96-193
Missouri Gas Energy, GR-96-285
St. Louis County Water Company, WR-96-263
Village Water and Sewer Company, Inc. WM-96-454
Empire District Electric Company, ER-97-82

Direct Testimony
Russell W. Trippensee
Case No. WR-2000-281

UtiliCorp d/b/a Missouri Public Service Company, GR-95-273
Associated Natural Gas, GR-97-272
Missouri Public Service, ER-97-394, ET-98-103
Missouri Gas Energy, GR-98-140
St. Louis County Water, WO-98-223
United Water Missouri, WA-98-187
Kansas City Power & Light/Western Resources, Inc. EM-97-515
St. Joseph Light & Power Company, HR-99-245
St. Joseph Light & Power Company, GR-99-246
St. Joseph Light & Power Company, ER-99-247
AmerenUE, EO-96-14, (prepared statement)
Missouri American Water Company, WR-2000-281
Missouri American Water Company, SR-2000-282