

Exhibit No.:
Issues: Rate Design
Witness: Greg R. Meyer
Type of Exhibit: Direct Testimony
Sponsoring Party: MIEC
Case No.: WR-2020-0344
Date Testimony Prepared: December 9, 2020

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

_____)
In the Matter of the Application of)
Missouri-American Water Company's)
Request for Authority to Implement) **Case No. WR-2020-0344**
General Rate Increase for Water and)
Sewer Service Provided in Missouri)
Service Areas)
_____)

Direct Testimony of

Greg R. Meyer

On behalf of

Missouri Industrial Energy Consumers

December 9, 2020



Project 10995

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

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

Case No. WR-2020-0344

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

Affidavit of Greg R. Meyer

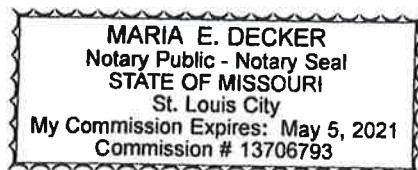
Greg R. Meyer, being first duly sworn, on his oath states:

1. My name is Greg R. Meyer. I am a consultant with Brubaker & Associates, Inc., having its principal place of business at 16690 Swingley Ridge Road, Suite 140, Chesterfield, Missouri 63017. We have been retained by the Missouri Industrial Energy Consumers in this proceeding on its behalf.
2. Attached hereto and made a part hereof for all purposes is my direct testimony which was prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. WR-2020-0344.
3. I hereby swear and affirm that the testimony is true and correct and that it shows the matters and things that it purports to show.

Greg R Meyer

Greg R. Meyer

Subscribed and sworn to before me this 8th day of December, 2020.



Maria E. Decker

Notary Public

1 substantial amounts of water from Missouri-American Water Company (“MAWC,”
2 “Missouri-American,” or “Company”).

3 **Q WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

4 A My testimony will address MAWC’s proposed Revenue Stabilization Mechanism
5 (“RSM”). In addition to my testimony on RSM, MIEC is also sponsoring the rate design
6 testimony of Jessica A. York on class cost of service; the creation of Rate L and
7 elimination of Rate J; and the MAWC’s proposal to consolidate districts into a single
8 statewide rate.

9 **Q WHAT MAWC WITNESS DISCUSSES THE RSM?**

10 A MAWC witness John M. Watkins discusses the RSM proposed by MAWC in his direct
11 testimony.

12 **Q PLEASE DESCRIBE AN RSM.**

13 A An RSM is a special regulatory tool that was authorized by the General Assembly in
14 2018 (Section 386.266.4). An RSM allows for the recovery/credit of revenues in
15 between rate cases to account for changes from the level of revenues set by the
16 Commission in the most recent rate case resulting from weather, conservation or both.
17 Effectively then, the RSM would guarantee the recovery of the level of Commission-
18 approved revenues in between rate cases regardless of the costs needed to operate
19 the utility. Looked at another way, customers get charged for water whether they use
20 that water or not.

1 **Q WHAT IS THE MIEC’S POSITION REGARDING THE RSM PROPOSED BY MAWC?**

2 A MIEC is opposed to the implementation of an RSM in this rate case.

3 **Q DOES MR. WATKINS OFFER ANY REASONS WHY THE COMMISSION SHOULD**
4 **ADOPT AN RSM?**

5 A Yes. Mr. Watkins offers the following reasons why an RSM should be adopted:

6 1. Most of Missouri-American’s costs are fixed. Therefore, anything that affects sales
7 will “drive a wedge between Authorized Revenues in this case and the actual level
8 experienced on a going forward basis.”¹

9 2. By adopting an RSM, the frequency of rate cases may be delayed, since the
10 necessity to file a rate case would only be necessary for increased costs and not
11 for updating sales forecasts.

12 3. Finally, an RSM will provide revenue stability for ongoing programs and
13 investments necessary to maintain and improve efficiency and service reliability by
14 removing a disincentive for Missouri-American to promote end-use efficiency.

15 **Q PLEASE DISCUSS THE CONCEPT OF FIXED COST RECOVERY THROUGH**
16 **VOLUMETRIC RATES.**

17 A The recovery of fixed costs as discussed by Mr. Watkins includes the recovery of
18 Missouri-American shareholder profits (return on equity and associated income taxes).
19 The profits built into ratepayer rates are considered a fixed cost by utilities. Mr. Watkins
20 seems to suggest that because so much of the Company’s costs are fixed and subject
21 to recovery through volumetric rates, the ability to recover all of its fixed costs (including
22 profits) when sales levels decline is not possible. What Mr. Watkins fails to discuss is
23 that MAWC has historically recovered enough revenues from ratepayers to pay all of
24 its operating expenses as well as debt costs and depreciation. Therefore, any shortfall

¹Direct testimony of John M. Watkins at 5.

1 in sales simply affects the profits of the utility. I have prepared Table 1 that shows the
2 net income for each year from 2010-2019.

<u>Year</u>	<u>Net Income</u> (\$ Millions)
2010	\$22.0
2011	\$34.1
2012	\$49.7
2013	\$38.7
2014	\$42.8
2015	\$40.2
2016	\$47.8
2017	\$45.8
2018	\$56.9
2019	\$62.7

3 As Table 1 indicates, whenever MAWC is reporting positive net income for a year, it is
4 paying all of its operating and maintenance expenses, depreciation expenses, property
5 taxes, other taxes, income taxes and interest expense. The only component left after
6 paying all of these costs is the level of profits recognized by MAWC.

7 Therefore, the sole advantage of an RSM is to guarantee a certain level of
8 profits for MAWC.

9 **Q HAS AMERICAN WATER WORKS CONTINUED TO PAY DIVIDENDS TO ITS**
10 **SHAREHOLDERS WITHOUT AN RSM IN MISSOURI?**

11 A Yes I have prepared Table 2 that shows the quarterly dividend payments by year for
12 each year dating back to 2010.

TABLE 2

**December Quarterly
American Water Works'
Dividend Payments**

<u>Year</u>	<u>Quarterly Dividend Payment</u>
2010	\$0.22
2011	\$0.23
2012	\$0.25
2013	\$0.28
2014	\$0.31
2015	\$0.34
2016	\$0.375
2017	\$0.415
2018	\$0.455
2019	\$0.500
March 2020	\$0.500
June 2020	\$0.55
2020	\$0.55

1 The table clearly shows that American Water Works has consistently raised its dividend
2 payments over the years. In fact, during the 10-year period, American Water Works'
3 dividends have increased by 150%. I would also like to point out that without an RSM
4 and during the COVID-19 pandemic, American Water Works still increased its quarterly
5 dividend in June 2020 by five cents a share. This increase represents the largest
6 nominal increase in dividend payments dating back to 2010. As previously discussed,
7 the advantage of an RSM is to protect MAWC's profits. It is unquestionable that
8 American Water Works has grown its dividend payments to its shareholders
9 significantly without an RSM in Missouri dating back to 2010.

10 More specific to MAWC, American Water Works has continued to invest in
11 Missouri. Specifically, as detailed in my revenue requirement direct testimony,
12 American Water Works has continued to purchase other water and sewer systems in
13 Missouri. Additionally, MAWC has expanded many of its own systems to newly

1 certified areas. Clearly then, operations in Missouri have apparently generated
2 profits necessary to justify this increased expansion. This contrasts with other states
3 like Arizona, New Mexico, Ohio and Texas where American Water Works sold its
4 operations.

5 **Q HOW HAS AMERICAN WATER WORKS' STOCK PRICE PERFORMED OVER THE**
6 **SAME PERIOD OF TIME?**

7 A American Water Works' stock prices since 2010 are presented in Table 3.

<u>Year</u>	<u>Stock Price</u>
2010	\$24.78
2011	\$31.40
2012	\$37.96
2013	\$41.96
2014	\$52.28
2015	\$57.87
2016	\$71.72
2017	\$91.22
2018	\$95.78
2019	\$122.49
December 2, 2020	\$154.83

8 Clearly, the lack of an RSM in Missouri has not negatively affected the stock price of
9 American Water Works. In the last ten years, the stock has appreciated in value by
10 525%. While American Water Works' stock price has appreciated by 525% in the last
11 ten years, the Dow Jones Industrial Average has only increased by 165%. Clearly,
12 American Water Works is enjoying significant profits, including in Missouri, which is the
13 third largest state of operations of the 16 states in which it operates.

1 Q YOU MENTIONED THAT MAWC ASSERTED THAT RATE CASE ACTIVITY MAY
2 DECLINE WITH ADOPTION OF AN RSM. PLEASE COMMENT.

3 A Mr. Watkins does not guarantee that adopting an RSM will result in fewer rate cases.
4 Revenues is only one aspect of a rate case. In its current rate case, MAWC witness
5 Deborah Dewey described why the Company found it necessary to file the rate case.
6 In her response, Ms. Dewey stated the following at pages 8-9 of her direct testimony:

7 The Company has made and continues to make significant, ongoing
8 investment to replace aging infrastructure and make upgrades required
9 by environmental regulation and prudent investment to ensure the
10 safety of our customers and employees. The Company also incurs
11 substantial operations and maintenance (“O&M”) expense to provide
12 reliable and safe water and wastewater service.

13 Interestingly in the next page of Ms. Dewey’s testimony she states: “Nearly 90% of the
14 Company’s proposed revenue increase is driven by its ongoing investment in
15 infrastructure.” Given this statement, one must question the true impact that fluctuating
16 usage has in this rate case. I would note that in my direct revenue requirement
17 testimony, I took issue with the level of declining usage proposed by MAWC. I have
18 argued that the level of usage proposed by MAWC is not representative of ongoing
19 levels of revenues. I also believe the Staff has taken exception to MAWC’s proposed
20 level of revenues in this case. Given that 90% of this case is driven by investment in
21 MAWC’s infrastructure, an RSM would not delay the filing of this rate case.

22 Furthermore, the current water ISRS statute (Section 393.1003.3) and
23 Commission rules require a water utility to file a rate case essentially every four years.²
24 I doubt very seriously if MAWC would relinquish its ability to collect revenues subject

²The statute and rules require a rate case to be filed within three years of the date in which the utility begins to “collect” an ISRS. The utility has some delay between the date in which a rate case is completed (the date in which the ISRS is zeroed out) and the date in which it is authorized to begin collecting an ISRS amount again. This lag period would typically be about a year which would extend the period for filing another rate case to four years.

1 to the ISRS in exchange for an RSM. Therefore, given the current rate case filing
2 requirement, it is hard to imagine how an RSM would materially affect the filings of
3 MAWC rate cases.

4 **Q ANOTHER REASON GIVEN BY MAWC TO ADOPT AN RSM WAS REVENUE**
5 **STABILITY FOR ONGOING PROGRAMS AND INVESTMENTS NECESSARY TO**
6 **MAINTAIN AND IMPROVE EFFICIENCY AS WELL AS SERVICE RELIABILITY BY**
7 **REMOVING A DISINCENTIVE FOR MISSOURI-AMERICAN TO PROMOTE**
8 **END-USE EFFICIENCY. PLEASE COMMENT.**

9 A First, I will discuss the incentive to invest and then discuss the concept of the
10 through-put disincentive for promoting water use efficiency. Currently, MAWC has an
11 ISRS for its St. Louis County District operations. The St. Louis County District accounts
12 for approximately 87% of MAWC's water customers and 74% of water sales. The ISRS
13 allows for rate adjustments in between rate cases to account for the costs of
14 infrastructure replacement, but not infrastructure expansion that generates increased
15 revenues. The ISRS has benefited MAWC since 2004 in reducing regulatory lag for
16 much of St. Louis County investments. On pages 9-10 of his direct testimony, Mr.
17 Watkins stated that "most" of MAWC's future investment will be in the way of
18 infrastructure replacement (i.e., ISRS investment), and not infrastructure expansion
19 (non-ISRS investment):

20 Now and in the future, most of the Company's needed investments will
21 not be intended to serve new growth from either increasing consumption
22 or a population boom on the horizon; they will resemble the
23 infrastructure replacement and renewal investments the Company has
24 made through the Infrastructure System Replacement Surcharge
25 (ISRS) and other non-revenue generating assets.

26 This statement indicates that the ISRS for St. Louis County will be the principal method
27 for recovery of investment for MAWC in the future. Thus, the need for an RSM to

Greg R. Meyer
Page 8

1 provide investment opportunities is significantly reduced with the ISRS in St. Louis
2 County.

3 **Q PLEASE DISCUSS THE CONCEPT OF THE DISINCENTIVE TO PROMOTE WATER**
4 **EFFICIENCY.**

5 A The disincentive refers to the natural incentive for MAWC to want to promote all sales
6 of water. Given that MAWC collects its profit levels primarily through sales, it has an
7 incentive to increase sales and not to promote conservation. That said, however,
8 especially in areas where water is in scarce quantities, this sales incentive would not
9 be looked on favorably. Water sales are also affected by the replacement of more
10 efficient water appliances. Finally, water sales can be affected simply by customers
11 taking it upon themselves to conserve water. By engaging in efforts to conserve water
12 either through promoting the sales of efficient water appliances, or other forms of
13 conservation, MAWC is unable to maximize its profits. MAWC implies then that the
14 RSM would break the linkage between actual usage and profits thereby allowing it to
15 engage in water efficiency efforts.

16 **Q IS THE DISINCENTIVE MECHANISM, AND THE NEED TO PROMOTE EFFICIENCY,**
17 **THE SOLE REASON FOR SALES VARIATION THAT AN RSM WOULD ADDRESS?**

18 A Absolutely not. The largest cause for revenue variation is weather. Weather is the
19 number one cause that MAWC seeks to eliminate through adoption of the RSM. In his
20 direct testimony, Mr. Watkins recognizes the effect weather has on the variation of
21 revenues. On page 8 of his direct testimony, Mr. Watkins states: "In short, a water
22 utility's revenue is significantly influenced by the randomness of weather, which is
23 outside the utility's control, but more importantly, bears only a limited relationship to the

1 cost of providing water service.” In addition, in MAWC’s last rate case, Company
2 witness James Jenkins made almost the exact same statement in his direct testimony.³
3 Weather mitigation, in my opinion, is the primary reason MAWC is requesting an RSM.
4 Although other reasons are discussed by MAWC, guaranteeing profits through weather
5 mitigation is the primary objective of the RSM. Efforts to break the linkage between
6 conservation and usage is of much lower importance.

7 **Q DOES MAWC’S PROPOSED RSM ADDRESS ANY OTHER IMPACT BESIDES**
8 **REVENUE LEVELS?**

9 A Yes, included in the MAWC proposed RSM is a current collection of production costs
10 (chemicals, power costs, purchased water and water waste disposal). In other words,
11 through the implementation of an RSM, MAWC wants to ensure the recovery of the
12 current cost of production costs. The MAWC’s proposed RSM will not only ensure a
13 certain level of revenues (profit restoration), but will also allow MAWC to collect any
14 changes in water production costs. Essentially, what MAWC is proposing is a revenue
15 surcharge mechanism (tracker) and a water production surcharge mechanism (tracker)
16 all rolled into an RSM.

³In its 10-K filing with the SEC, American Water Works also indicates that usage variation as a result of weather is one of its risk factors. “Climate variability may cause increased volatility in weather and may impact water usage and related revenue or require additional expenditures, all of which may not be fully recoverable in rates or otherwise.”

1 **Q IF THE COMMISSION WERE CONSIDERING THE ADOPTION OF AN RSM, DO**
2 **YOU BELIEVE CHANGES IN WATER PRODUCTION EXPENSES SHOULD BE**
3 **INCLUDED IN THE RSM?**

4 A No. The changes in water production expenses should not be a component of the
5 RSM. Those expense changes should only be addressed in a rate case.

6 **Q HOW WOULD YOU PROPOSE TO ELIMINATE THE WATER PRODUCTION COSTS**
7 **FROM AN RSM?**

8 A At the conclusion of a rate case, the annualized level of water production costs should
9 be calculated. That level of annualized water production costs then should be divided
10 by the annualized level of water sales (K gallons). The Rate per K gallon of production
11 costs should be subtracted from all revenue adjustments made in the RSM in between
12 rate cases. In this way the level of production costs are not subject to review during
13 the RSM. This method is very similar to how the calculation of base fuel costs occurs
14 for the FAC in an electric rate case.

15 **Q IN HIS DIRECT TESTIMONY ON PAGE 14, MR WATKINS IS ASKED , “DO YOU**
16 **BELIEVE THAT THE RSM DIFFERS FUNDAMENTALLY FROM OTHER**
17 **AUTOMATIC ADJUSTMENT CLAUSES?” MR. WATKINS RESPONDS, “YES, I DO,**
18 **IN SEVERAL SIGNIFICANT WAYS. FIRST AND FOREMOST, THE RSM IS NOT A**
19 **COST ADJUSTMENT CLAUSE. IT IS A REVENUE ADJUSTMENT CLAUSE.”**
20 **PLEASE RESPOND.**

21 A I am totally confused by this statement given the previous discussion about production
22 costs and how those costs are updated through the RSM. Clearly, Mr. Watkins is
23 ignoring the production cost surcharge mechanism (tracker) MAWC is proposing as a

1 part and parcel of its RSM. I hope the Commission is not confused by this attempt to
2 hide the fact that MAWC wants to true-up production costs within the RSM. Not only
3 is MAWC requesting a future test year in this case, but is hiding the fact that it wants
4 to continually adjust production costs in between rate cases through the RSM.

5 **Q PLEASE COMMENT ON MAWC'S PROPOSED RATE DESIGN FOR APPLICATION**
6 **OF ITS RSM?**

7 A MAWC proposes the following rate design for application of its RSM:

- 8 ➤ If current revenues are less than the level authorized, customer rates would be
9 adjusted on a volumetric basis.
- 10 ➤ If current revenues are greater than the level authorized, customer rates would be
11 adjusted through customer bill credits.

12 **Q DO YOU SUPPORT THIS RATE DESIGN PROPOSAL?**

13 A No, any RSM should focus on usage and not revenues as MAWC proposes. If an RSM
14 is adopted by the Commission, I would propose that all RSM adjustments be based on
15 volumetric changes, whether revenues are above or below the level authorized by the
16 Commission. This would align the revenues with the consumption of water for all
17 customers.

18 **Q PLEASE SUMMARIZE YOUR POSITION ON MAWC'S PROPOSED RSM.**

19 A I am opposed to the RSM. The RSM is a mechanism to guarantee a level of utility
20 profits. This is not necessary as Missouri is clearly providing adequate support to
21 shareholder earnings currently. The RSM as proposed by MAWC will also recover
22 changes in water production costs. For these reasons and my previous discussions, I
23 would recommend that the Commission reject MAWC's request for an RSM.

1 Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

2 A Yes, it does.

404547.docx