

Exhibit No. 115

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Kimberly K. Bolin
Rebuttal Testimony (Cost of Service)
File No. WR-2022-0303

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MISSOURI PUBLIC SERVICE COMMISSION
FINANCIAL AND BUSINESS ANALYSIS DIVISION

REBUTTAL TESTIMONY

OF

KIMBERLY K. BOLIN

MISSOURI-AMERICAN WATER COMPANY

CASE NO. WR-2022-0303

Jefferson City, Missouri
January 2023

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KIMBERLY K. BOLIN
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1 explain the reasons why Staff is not persuaded that the use of the discrete adjustments as
2 proposed by MAWC is appropriate.

3 Also in this rebuttal testimony, I address MAWC's proposals included in
4 MAWC witness Brian W. LaGrand's direct testimony to eliminate regulatory lag by
5 establishing two regulatory assets. One is a depreciation deferral and the other would be
6 capitalized post-in-service carrying costs.

7 Finally, I address the Office of the Public Counsel's ("OPC's") witness
8 Dr. Geoff Marke's proposal to close Case No. AW-2018-0394 and open a "WX" water
9 rulemaking docket in its place.

10 **TRACKER PROPOSALS**

11 ***OVERVIEW***

12 Q. What is a "tracker"?

13 A. The term "tracker" refers to a rate mechanism in which the amount of a particular
14 cost of service item actually incurred by a utility is "tracked" and compared to the amount of
15 that item currently in a utility's rates. Any over-recovery or under-recovery of the item in rates
16 compared to the actual expenditures made by the utility is then booked to a regulatory asset or
17 regulatory liability account, and would be eligible to be included in the utility's rates set in its
18 next general rate proceeding through an amortization to expense.

19 Q. Should the use of trackers be common in Missouri rate regulation of utilities?

20 A. No. Rates are normally set in Missouri to allow a utility an opportunity to
21 recover its cost of service, measured as a whole, on an ongoing basis from the utility's
22 customers. However, under this approach, with rare exceptions, neither the utilities nor their
23 customers are allowed to be reimbursed through the rate case process for any prior under- or

1 over-recovery of costs experienced by the utilities in rates, measured either for its cost of service
2 as a whole or for individual cost of service components. For this reason, the use of trackers in
3 order to provide reimbursement in rates to utilities or customers of any over- or under-recovery
4 of individual rate component items is rare and should be dependent on unique and unusual
5 circumstances.

6 Q. Under what criteria might Staff consider the use of trackers justified?

7 A. The use of trackers may be justified under the following circumstances:
8 (1) when the applicable costs demonstrate significant fluctuation and up-and-down volatility
9 over time, and for which accurate estimation is difficult; (2) when there are new costs for which
10 there is little or no historical experience, and for which accurate estimation is accordingly
11 difficult; and (3) when there are costs imposed upon utilities by newly promulgated
12 Commission rules. In addition, the costs should be material in nature.

13 Q. Why are trackers sometimes justified by significantly fluctuating and
14 volatile costs?

15 A. If a utility's cost levels for a particular rate item over time demonstrate
16 significant up-and-down volatility, it can be appropriate to implement a tracker mechanism for
17 this type of item to reduce the amount of risk associated with a material inaccuracy in estimating
18 the particular costs for purposes of setting the utility's rates.

19 Q. What is an example of the Commission in the past authorizing a tracker for a
20 volatile cost?

21 A. All major utilities operating in Missouri, including MAWC, have tracker
22 mechanisms in place for their pension and other post-employment benefit ("OPEB") expenses.
23 Annual pension and OPEB expense amounts in the past have had significant annual volatility,

1 primarily because pension and OPEB funding amounts are impacted by investment outcomes
2 in equity and debt markets which, of course, can swing upward or downward based upon trends
3 in the general economy.

4 Q. Are there other unusual aspects to pension and OPEB expense that justify using
5 a tracker mechanism?

6 A. Yes. In Missouri, utilities place amounts intended for later payment to retired
7 employees for pension and OPEBs into external trust funds to help ensure that such funds are
8 available when due to utility employees. Staff believes it is good policy for utilities to keep as
9 current as possible on the funding of pension and OPEB amounts. The authorizing of a
10 tracker mechanism for these expense items encourages utilities to stay current on pension and
11 OPEB expense allowances currently included in their rate levels. Of course, if pension or
12 funding amounts turn out to be less than the amounts for these items currently included in a
13 utility's rate level, use of trackers also ensures that the funding/rate differential would ultimately
14 be flowed back to its customers.

15 Q. Does Staff continue to recommend that the Commission authorize
16 MAWC's pension and OPEB trackers?

17 A. Yes. Continued authorization of these trackers remains appropriate for
18 MAWC and other utilities that offer pension and OPEB benefits to their employees.

19 Q. Are there other instances in which trackers may be justified?

20 A. In rare circumstances, utilities will incur significant new expense for which they
21 have little or no history to aid in determining an appropriate ongoing level for those expenses
22 for ratemaking purposes. In those circumstances, it may be appropriate to authorize a tracker

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1 to protect both the utility and its customers from over- or under- recovery in rates of these
2 expenses due to erroneous estimates.

3 Q. Has Staff agreed to the use of a tracker for this reason?

4 A. Yes. In several electric utility rate cases when a new generating unit goes into
5 service, Staff has agreed to a tracker applicable to the operations and maintenance (“O&M”)
6 expenses associated with the new plant, given the lack of history for these expenses. However,
7 after several years of operation, Staff recommends discontinuation of the tracker when
8 adequate history of these expenses is known.

9 Q. Are there any other instances where the Commission has used trackers?

10 A. In some circumstances, the Commission has established, within the rules it
11 promulgates, provisions for tracking and recovery of incremental costs caused by utility
12 compliance with new rules. This was the case with the Commission rules requiring electric
13 utilities to take certain actions regarding vegetation management and infrastructure inspection
14 activities, which became effective in 2008.

15 Q. Are cost deferrals resulting from the use of trackers different from cost deferrals
16 resulting from an accounting authority order (“AAO”)?

17 A. Yes. An AAO is a Commission order that allows a utility to defer certain costs
18 on its balance sheet for potential recovery of the deferred costs in rates through amortizations
19 to expense in a general rate proceeding. This is similar to how deferrals resulting from trackers
20 may be treated in general rate proceedings. However, the nature of the costs to which AAOs
21 are normally granted, and the nature of the costs to which tracking treatment is normally granted
22 are quite different.

1 Q. Would you explain the major differences in how the Commission has allowed
2 utilities to use AAOs and trackers?

3 A. Typically, AAOs have been used to allow utilities to capture certain
4 unanticipated and “extraordinary” costs that are not included in their ongoing rate levels. The
5 term “extraordinary costs” is defined as costs associated with an event that is unusual,
6 unique, and non-recurring in nature. The classic example of an extraordinary event is the
7 occurrence of a natural disaster, such as a wind or ice storm, or a major flood that affects a
8 utility’s service territory.

9 In contrast, the Commission has allowed utilities to use trackers to track certain
10 costs that are ongoing to a utility and for which some allowance has been built into the
11 utility’s existing rate levels. For this reason, while costs subject to trackers exhibit some
12 highly unusual or unique attributes which justify the use of a tracker, these costs are not
13 “extraordinary” in the sense that this term is commonly applied to costs covered by AAOs.

14 Q. If trackers have not been limited to extraordinary costs, why not track all or
15 most costs?

16 A. There are at least two reasons. First, excessive use of trackers would tend to
17 skew ratemaking results either in favor of the utility or in favor of its customers. Secondly,
18 broad use of trackers offers no incentive for a utility to operate as efficiently and productively
19 under the rate regulation approach used in Missouri.

20 Q. Why would the widespread use of trackers tend to skew the ratemaking results
21 for a utility?

22 A. With certain exceptions, the policy in Missouri has been to set a utility’s rates
23 based upon measurement of “all relevant factors,” taking into account levels of revenues,

1 expenses, rate base, and rate of return that are calculated at or approximately at the
2 same point in time. Use of an “all relevant factors” approach is necessary to ensure that a
3 utility’s rate levels are based upon an accurate measurement of its cost of service at a
4 particular point in time.

5 When using trackers as part of setting rates, certain cost factors inevitably receive
6 different and inconsistent treatment compared to other cost factors. For example, if a utility
7 tracks expenses that tend to increase over time, but does not track factors that may reduce its
8 cost of service (such as revenue growth, or increases in rate base offsets for accumulated
9 depreciation or deferred taxes), the utility may receive retroactive dollar-for-dollar recovery of
10 certain cost increases in its customer rates through trackers, at the same time that it retains
11 beneficial changes in other cost of service components that occur over the same period. In this
12 manner, inappropriate use of trackers can lead to skewed and unfair ratemaking results.

13 Q. How do trackers affect a utility’s incentive to operate efficiently?

14 A. An inevitable byproduct of the Missouri ratemaking approach is
15 “regulatory lag.” “Regulatory lag” is simply the passage of time between when a utility
16 experiences a change in its cost of service, and the reflection of that change in its rate levels.
17 While regulatory lag is often portrayed by utilities as a phenomenon that is entirely negative or
18 harmful, the existence of regulatory lag provides utilities with incentive to be as efficient and
19 cost-effective over time as they can. Excessive use of trackers can eliminate or weaken these
20 beneficial incentives.

21 Q. What is MAWC seeking to track in this rate case?

22 A. MAWC is seeking to track bad debt (uncollectible) expense, production cost
23 expense, and property tax expense.

1 ***BAD DEBT TRACKER***

2 Q. Is it generally appropriate to track bad debt expense?

3 A. No. Bad debt expense is an ongoing cost of service item incurred by all
4 major utilities. In almost all circumstances, a reasonable allowance for bad debts can be
5 calculated in the context of a general rate case using historic data. Bad debt expense has been
6 a component of utility cost of service in all general rate cases that I have been involved with for
7 over 25 years.

8 Q. What ratemaking treatment does Staff recommend for the bad debt expense in
9 this case?

10 A. Staff calculated MAWC's bad debt expense by using a three-year average
11 (2018, 2019, and 2021) of net write-offs, as discussed in Staff witness Courtney Horton's direct
12 and rebuttal testimonies.

13 Q. Is Staff recommending re-examining bad debt expense as part of its true-up in
14 this case?

15 A. Yes.

16 Q. What level of bad debt expense does Staff recommend in this case?

17 A. Staff recommends a total company bad debt expense level of \$3,298,708.

18 ***PRODUCTION COST TRACKER***

19 Q. What types of costs has MAWC proposed to include in its production
20 cost tracker?

21 A. MAWC proposes to include costs related to Fuel & Power, Chemicals, Waste
22 Disposal, and Purchased Water.¹

¹ Direct Testimony of Brian W. LaGrand, WR-2022-0303, P. 17:11-15.

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1 Q. Is it generally appropriate to track these types of production costs?

2 A. No. These types of costs are ongoing cost of service items incurred by most
3 water and sewer utilities. Staff has analyzed each of these expense items and has determined a
4 normalized and annualized level of expense for each item.

5 Q. Would the production costs increase if revenues increase for MAWC due to
6 increased sales?

7 A. Yes. Production costs would increase if the amount of water MAWC sells
8 increases. For example, MAWC would need to use more chemicals to treat the additional water
9 and MAWC's cost of electricity would increase due to the need to pump additional water.

10 Q. Is MAWC seeking authorization to track revenues?

11 A. Yes. MAWC has requested a revenue stabilization mechanism ("RSM")
12 which is a type of mechanism commonly known as revenue "decoupling." MAWC stated if
13 the Commission approved the RSM as MAWC proposed, a production cost tracker would
14 not be necessary.²

15 Q. Is Staff suggesting that MAWC's RSM proposal should be viewed as an
16 alternative to the production cost tracker?

17 A. No. A RSM presents a host of practical and theoretical concerns and issues
18 which I am not addressing for Staff.³ At this time, Staff is not recommending that the
19 Commission adopt either the RSM or the production cost tracker for ratemaking purposes
20 in this case.

² *Direct Testimony of Brian W. LaGrand*, WR-2022-0303, P. 17:22-23.

³ Staff witness James A. Busch will be addressing MAWC's RSM proposal in his rate design rebuttal testimony.

1 **PROPERTY TAX TRACKER**

2 Q. Was legislation passed in 2022 that allows a utility to track and defer to the
3 utility's next general rate case the difference between property taxes actually paid and property
4 taxes included in the revenue requirement used to set rates?

5 A. Yes. Senate Bill 745 states, in part:

6 Electrical corporations, gas corporations, sewer corporations, and water
7 corporations shall defer to a regulatory asset or liability account any
8 difference in state or local property tax expense actually incurred, and
9 those on which the revenue requirement used to set rates in the
10 corporation's most recently completed general rate proceeding was
11 based. The regulatory asset or liability account balances shall be
12 included in the revenue requirement used to set rates through an
13 amortization over a reasonable period of time in such corporation's
14 subsequent general rate proceedings. The commission shall also adjust
15 the rate base used to establish the revenue requirement of such
16 corporation to reflect the unamortized regulatory asset or liability
17 account balances in such general rate proceedings. Such expenditures
18 deferred under the provisions of this section are subject to commission
19 prudence review in the next general rate proceeding after deferral.⁴

20 Q. Does MAWC explain in testimony when it intends to begin utilizing the property
21 tax tracker legislation?

22 A. Yes, Mr. Selinger states in his direct testimony, beginning on page 28, line 9,
23 "Therefore, MAWC has included within its case a property tax deferral, per the legislation,
24 for its 2022 property taxes. At the August 28th, 2022 effective date, MAWC will begin
25 deferring the difference between the property tax expense level approved in the last rate
26 proceeding, WR-2020-0344 and its actual property tax incurred as described in the legislation."

27 Q. Did the Commission establish the level of property tax expense in "the revenue
28 requirement used to set rates in [MAWC's] most recently completed general rate proceeding?"

⁴ Section 393.400, RSMo.

1 A. No, it did not. The Commission approved a *Stipulation and Agreement* in Case
2 No. WR-2020-0344 that resolved the case, but it did not base the revenue requirement on a
3 specific level of property tax expense.

4 Q. Does Staff agree that MAWC should begin tracking and deferring property tax
5 as of August 28, 2022?

6 A. No. As I stated above, the Commission did not base MAWC's revenue
7 requirement in its last general rate case (Case No. WR-2020-0344) upon a level of property
8 tax expense. In order to use the tracker authorized by Section 393.400 of the Missouri Statutes,
9 the Commission must have established in the utility's prior general rate proceeding a level
10 of property tax expense upon which it bases the utility's revenue requirement. The Commission
11 did not do this in MAWC's prior rate case; therefore, at this time there is nothing to
12 track MAWC's actual property tax expenses against. Section 393.400, RSMo does not
13 allow a utility to select an estimated level of property tax expense to be tracked
14 against unless the Commission ordered a specific level of property tax expense to be
15 tracked against.

16 For these reasons, Staff's position is that the base property tax level will be
17 established in the current proceeding and the deferral of property taxes should begin with
18 the effective date of rates in this current proceeding. Staff recommends the amount of
19 property tax expense to be tracked against actual expense in the property tax tracker
20 going forward is Staff's recommended level proposed in this present case.

21 Q. In this case what level of property tax expense does MAWC claim should be
22 used to track the property taxes incurred in 2022?

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1 A. MAWC uses \$28,573,695⁵ (amount paid December 31, 2020) as the property
2 tax level established in Case No. WR-2020-0344. MAWC also added a prorated amount
3 of \$2,148,291 based upon \$6,427,265 for the property taxes included in MAWC's Water and
4 Sewer Infrastructure Rate Adjustment ("WSIRA") case (Case No. WO-2022-0176), resulting
5 in a total base property tax amount of \$30,721,986.

6 Q. If the Commission determines that MAWC is eligible to take advantage of the
7 property tax tracker as of August 28, 2022, does Staff agree that MAWC's base property tax
8 level is \$30,721,986?

9 A. No. In MAWC's last rate case, Staff included \$25,421,771 for property taxes
10 in Staff's cost of service. Staff proposed to update the property taxes during the true-up
11 audit; however, the parties entered into a *Stipulation and Agreement* before Staff completed its
12 true-up audit.

13 Also, the amount of property taxes that was eventually included in Case No.
14 WO-2022-0176 (the WSIRA case) was \$3,036,211 not \$6,427,265.⁶ MAWC prorated this
15 amount since it was not in effect for a full year. Therefore, the total base property tax
16 level should be \$26,436,614 in the event that the Commission determines that use of a
17 property tax tracker is justified for MAWC as of August 28, 2022.

18 Q. Has Staff calculated what the regulatory asset should be if the Commission
19 allows MAWC to start tracking the property taxes as of August 28, 2022?

20 A. Yes, based upon MAWC's estimated property tax paid on December 31, 2022,
21 which is \$34,000,000, the regulatory asset should be \$1,913,135. Staff will provide an

⁵ Per response to Data Request No. 0121 in Case No. WR-2020-0344.

⁶ *Order Approving Agreement*, WO-2022-0176, P. 1 (July 21, 2022).

1 updated regulatory asset when the actual property taxes paid at year-end 2022 are known
2 and provided to Staff.

3 Q. How did Staff calculate the regulatory asset amount?

4 A. The new law was in effect for 126 days in 2022. Staff prorated the estimated
5 property taxes paid on December 31, 2022, and Staff's property tax amount included in
6 Staff's cost of service in Case No. WR-2020-0344, to reflect the law's effective date of
7 August 28, 2022. Staff also prorated the WSISRA property tax amount recovered in Case
8 No. WO-2022-0176 to reflect the effective date of the new tracker, if it is ordered by the
9 Commission.

10 **DISCRETE ADJUSTMENTS**

11 Q. What are discrete adjustments?

12 A. Discrete adjustments are adjustments made to the test year and/or true-up period
13 for known and measurable changes or events that occur after the test year and/or true-up period.

14 Q. Are discrete adjustments also commonly referred to in past Commission cases
15 as "isolated adjustments?"

16 A. Yes.

17 Q. In his direct testimony, MAWC witness Mr. Selinger proposes "discrete
18 adjustments" for select known and measurable changes through this case's operation of law
19 date, May 31, 2023.⁷ Does Staff agree that the discrete adjustments MAWC proposed are
20 representative of known and measurable changes?

21 A. No. MAWC has proposed to include in rates select non-WSIRA eligible plant
22 that goes into service prior to the operation of law date. However, not all of the actual costs

⁷ Direct Testimony of Wesley E. Selinger, WR-2022-0303, P. 21:18-19.

1 incurred for all of the plant that is to be placed in service between the true-up date of
2 December 31, 2022, and the operation of law date will be known or measurable at the time of
3 the Commission's decision in this case, especially if any of the plant is placed into service
4 shortly before May 31, 2023.

5 Q. Does Staff agree that MAWC's labor expense discrete adjustments will be
6 known and measurable as of the operation of law date?

7 A. The amount of MAWC's merit increases for non-bargaining unit employees
8 should be known in February 2023. However, while some of the union pay increases are
9 known at this time, they will not occur until as late as December 1, 2023, almost a year after
10 the true-up date in this proceeding.

11 Q. Does MAWC's proposal to include pay increases as late as December 1, 2023,
12 violate the "matching principle"?

13 A. Yes. By only updating select cost of service items through the operation of law
14 date, the "matching principle" is violated. The "matching principle" requires that all major
15 components of a utility's cost of service be measured at the same point in time when developing
16 customer rates.

17 Q. Is MAWC also proposing to make discrete adjustments to employee benefits
18 based upon the adjusted payroll expense?

19 A. Yes. MAWC is proposing to increase 401(k) expense, defined contribution
20 plan expense, and payroll taxes. These amounts are calculated based upon the annualized
21 payroll expense.

22 Q. What other items besides plant and payroll-related expenses has MAWC
23 proposed to adjust to the operation of law date?

1 A. MAWC proposes making discrete adjustments for:
2 Accumulated Deferred Income Taxes,
3 Contributions in Aid of Construction (“CIAC”),
4 Cash Working Capital,
5 Regulatory Deferral Balances (including pension and OPEBs trackers),
6 Capital Structure,
7 Cost of Debt,
8 Pensions & OPEBs,
9 Purchased Water,
10 Fuel and Power Expense,
11 Chemical Expense,
12 Insurance other than Group,
13 Support Services Expenses,
14 Uncollectible Expense,
15 Building Maintenance and Service Expense,
16 Revenues,
17 Lease Expense,
18 Maintenance Supplies and Services,
19 Miscellaneous Expenses,
20 Telecommunications Expense,
21 Transportation Expense,
22 Waste Disposal Expense,
23 Property Taxes, and

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1 Income Taxes.

2 Q. Does Staff believe the adjustments included within this lengthy list of items are
3 truly “discrete adjustments?”

4 A No. MAWC’s list of proposed discrete adjustments should be considered
5 akin to implementation of a future test year in that most items are already being updated and
6 trued-up as December 31, 2022, in Staff’s case. Most of these are adjustments that will not be
7 known and measurable as of the operation of law date, May 31, 2023. In order to review and
8 audit these items, and have the rates go into effect on May 31, 2023, forecasted and budgeted
9 information will have to be used in the same manner as required under a future test year.

10 Q. Mr. Selinger claims on page 21, lines 8 through 12 of his direct testimony,
11 “The purpose for selecting a test year and allowing adjustments is to arrive at results of
12 operation that are representative of ongoing levels. While a future test year would best serve
13 this purpose, discrete adjustments to a historical year will better serve this purpose than
14 adjustments that are cut off by an earlier true-up date.” Does Staff agree that a future test year
15 is better than a historic test year?

16 A. No. Staff does not agree that the use of a future test year approach instead of a
17 “modified” historic test year would produce more representative rates. In addition, Staff has
18 concerns regarding the effects of the use of a future test year on existing utility incentives to
19 provide safe and adequate service at the lowest reasonable cost of service.

20 Q. Is Staff opposed to discrete adjustments that occur past the true-up period?

21 A. Not in all cases. Staff is not necessarily opposed to limited inclusion of
22 discrete adjustments occurring past the true-up period in cost of service if certain criteria apply.
23 First, the adjustment must be known and measurable and second, if the timing of the event does

1 not skew the matching principle in relation to other cost of service items, it may be appropriate
2 to make a discrete adjustment. In its Cost of Service Report for Case No. ER-2019-0374, Staff
3 recommended isolated adjustments to rate base related to the retirement of the Asbury
4 generating plant for the Empire District Electric Company. The retirement adjustments were
5 known and measurable prior to the end of the filing of testimony in that proceeding and well
6 before the operation-of-law date in that proceeding.⁸

7 **DEPRECIATION AND CARRYING COST DEFERRALS**

8 Q. What is “regulatory lag?”

9 A. “Regulatory lag” is the lapse in time between when a utility experiences a
10 financial change and when that change is reflected in its rate levels. Regulatory lag can be
11 either detrimental or beneficial to a utility’s earnings and, under either scenario, the existence
12 of this phenomenon serves as an important incentive on the utility to be as cost-conscious and
13 efficient over time as possible, in order to maintain its earnings level.

14 Q. Does regulatory lag affect the earnings of a utility between general rate
15 proceedings?

16 A. Yes. The operation of regulatory lag as part of the normal ratemaking process
17 exposes a utility to the prospect of lower earnings if its cost of service increases between general
18 rate cases. However, it also allows the utility to experience higher earnings if the utility is able
19 to reduce its cost of service that was established in the most current rate proceeding. This
20 “penalty/reward” aspect of current Missouri ratemaking policy would be disturbed by use of
21 trackers applied to normal cost of service items. A company that experiences an increase in an
22 expense that is being tracked will experience no reduction in earnings related to that increased

⁸ *Staff Report, Cost of Service*, ER-2019-0374, P. 105-107 (Jan. 15, 2020).

1 cost, because the cost increase will be captured on its balance sheet and not on its income
2 statement. Under this scenario, the utility will have less incentive to minimize any such cost
3 increase. On the other hand, a utility that experiences a reduction in an expense that is being
4 tracked will experience no increase to its ongoing earnings level as a result of the decreased
5 costs (again, because the cost decrease will be captured on its balance sheet and not on its
6 income statement) and, therefore, would have less incentive to produce the lower cost levels in
7 the first place.

8 Q. MAWC's witness Brian LaGrand states on page 10, lines 17 through 18 of his
9 direct testimony that regulatory lag due to new investments is one of the primary drivers of
10 MAWC's alleged return on equity shortfall. Does Staff agree with this statement?

11 A. No. MAWC currently utilizes the WSIRA, which allows for periodic rate
12 changes associated with certain plant additions outside of a general rate case. Since
13 MAWC's last rate case, MAWC has included plant additions in the amount of \$411,330,492
14 in its WSIRA, while increasing total plant (including MAWC WSIRA-eligible plant)
15 by \$462,078,673. Only approximately 11% of newly added plant since the last rate case has
16 not already been currently included in MAWC's rates charged to customers, leaving
17 approximately 89% of newly added plant included in customer rates.

18 Q. On page 10 of Mr. LaGrand's direct testimony, he provides Table BWL-1 which
19 provides a calculation of the return on equity for the years 2012 through 2021. Is the WSIRA
20 a recently passed mechanism that MAWC is able to utilize to reduce regulatory lag that was not
21 in use during almost all of the period of time reflected in his table?

22 A. Yes. The WSIRA became effective August 28, 2021. Prior to the WSIRA
23 MAWC was able to utilize the Infrastructure System Replacement Surcharge ("ISRS")

1 mechanism. The WSIRA materially expanded the type of plant investment that could be
2 included for recovery through a mechanism outside of a rate case. The ISRS only allowed
3 recovery of eligible infrastructure system replacements for water utility plant main replacement
4 projects in St. Louis County. The WSIRA allows recovery of eligible water and sewer projects,
5 not just main replacements, located throughout Missouri. If the WSIRA was effective beginning
6 in 2012, MAWC's return on equity percentages for the years 2012 through 2020 probably
7 would likely have been higher than what Mr. LaGrand portrays in his Table BWL-1.

8 Q. How does MAWC propose to mitigate regulatory lag associated with plant
9 investments?

10 A. MAWC proposes a deferral of depreciation and capitalization of post-in-service
11 carrying costs.⁹

12 Q. Please describe MAWC's depreciation deferral proposal.

13 A. The depreciation deferral would begin deferring depreciation expense as soon
14 as the plant investment is placed in service and placing the depreciation expense in a regulatory
15 asset until MAWC's next rate case, at which time the deferred amount would be amortized over
16 25 years and the unamortized balance would be included in rate base.¹⁰

17 Q. Does Staff agree that a depreciation deferral is necessary?

18 A. No. Under normal ratemaking, depreciation expense for an item begins as soon
19 as it is placed in service; however, depreciation expense on that item is not included in rates
20 until the utility's next rate case. The same logic applies to plant that is retired, in that the
21 associated depreciation expense is not removed from rates until the next rate case even though

⁹ *Direct Testimony of Brian W. LaGrand*, WR-2022-0303, P. 13:9-11.

¹⁰ *Id.* at P. 13:17-21.

1 the plant is not in service. As shown above, most of MAWC's plant that has recently been
2 placed into service between rate cases are being recovered as part of WSIRA rates, thus a
3 deferral of depreciation expense is not needed.

4 Q. Does MAWC's proposal net the depreciation expense for retired plant
5 against the depreciation expense for newly placed in service plant for purposes of calculating
6 the deferral?

7 A. Not for all plant that is retired. MAWC stated in its response to Staff Data
8 Request ("DR") No. 0253, "MAWC has treated retired plant similar to how it is treated in the
9 Company's WSIRA cases. Not all investment replaces an existing asset, although it will in
10 many cases."

11 Q. How is retired plant accounted for in WSIRA cases?

12 A. The annual depreciation expense for the retired plant is netted against the annual
13 depreciation expense for the new plant that replaces the retired plant.

14 Q. Could plant be retired without being replaced?

15 A. Possibly. A piece of plant could possibly be retired because it is no longer
16 needed due to changes in the water or sewer system.

17 Q. Under MAWC's proposed depreciation deferral, should all retired plant that is
18 not eligible for inclusion in the WSIRA be treated the same as retired plant that is included in
19 the WSIRA?

20 A. Yes. If the depreciation deferral is allowed, the deferral should be offset with
21 the depreciation expense for all plant that will be retired during the course of the deferral. To
22 do otherwise would effectively lead to MAWC being made whole in rates for all depreciation

1 expense on new plant additions since its last rate case while not making customers whole for
2 depreciation expense they pay in rates related to plant retired since the last rate case.

3 Q. Does booking of depreciation expense require a cash outlay by MAWC?

4 A. No. Depreciation expense is not a cash outlay like other expenses or new
5 investments. Depreciation expense is the return of the investment over a period of time.

6 Q. If the unamortized balance is included in rate base will MAWC receive a return
7 on this non-cash outlay?

8 A. Yes.

9 Q. Please describe MAWC's proposed capitalization of post-in-service
10 carrying costs.

11 A. Under normal ratemaking, customer rates would not include any return on plant
12 that is placed into service until that plant has been included in a rate case. MAWC has proposed
13 to defer the return (carrying costs at the pre-tax rate of return) as soon as the plant is placed into
14 service until the plant is included in rate base in the next rate case. Like the depreciation
15 deferral, MAWC also proposed to amortize the return deferral over 25 years and include the
16 unamortized balance in rate base.¹¹

17 Q. Does Staff agree with this proposal?

18 A. No.

19 Q. Will the rates charged to customers continue to include retired plant?

20 A. Yes. MAWC will continue to earn a return on the retired plant while also
21 earning a return on new plant through the deferral of carrying costs. Customers will ultimately

¹¹ *Id.* at P. 15:2-5.

1 be inappropriately paying a return on both the retired plant and the new plant if the deferral of
2 carrying costs proposal is granted.

3 Q. Starting on page 14 of his direct testimony, Mr. LaGrand provides his
4 analysis of the financial impact of the estimated deferrals. He assumes an annual capital
5 investment of \$400 million. In the past five years has MAWC's net capital investment
6 averaged \$400 million a year?

7 A. No. The following graph provides the annual net plant additions MAWC
8 incurred.

Year	Plant Additions	Retirements	% of Retirements to Plant Additions
2017	\$191,545,246	\$7,682,460	4.01%
2018	\$160,213,273	\$20,500,140	12.8%
2019	\$226,830,967	\$31,710,481	13.98%
2020	\$317,948,620	\$45,388,870	14.28%
2021	\$280,424,580	\$1,224,292	0.44%
Average	\$235,392,537	\$21,01,249	9.10%

9 Source: Staff DR No. 0260

10 Q. In his analysis, Mr. LaGrand also assumes 70% of the capital additions are
11 eligible for WSIRA.¹² Do you agree with this assessment?

12 A. No. As I stated above, the amount of plant additions since the last rate case that
13 were included in WSIRA was approximately 89%. This means that MAWC would only need
14 to recover in general rate cases a small percentage of its plant additions, meaning the amount

¹² *Id.* at P. 14:11-12.

1 of the depreciation and carrying cost deferrals will be significantly less than what Mr. LaGrand
2 estimated in its proposed deferral.

3 Q. Mr. LaGrand also assumes a 5% retirement rate. Does Staff agree with this rate?

4 A. No. As shown in the above graph the average retirement rate for the years
5 2017 through 2021 is 9.10%. By using the 9.10% retirement rate instead of the 5% rate,
6 the amount that is eligible for the depreciation deferral is less.

7 Q. Comparing your 9.10% retirement rate, your average yearly plant investment
8 and percentage of plant eligible for WSIRA, what would the balance of the deferred
9 depreciation and deferred carrying cost regulatory assets be after three years?

10 A. With my calculations, which are based upon historical data, after three years, the
11 balance of the depreciation deferral would be \$2,190,563 and the carrying cost deferral
12 would be \$11,385,185. Using MAWC's assumptions the deferrals would be approximately
13 \$10.4 million and \$52.4 million, respectively.

14 Q. What would the annual revenue requirement impact on customers be under these
15 two scenarios?

16 A. Under my scenarios the revenue requirement impact on customers would be
17 approximately \$1,725,478 annually. MAWC has estimated the annual revenue requirement
18 impact to be \$8 million.¹³

19 **AFFILIATE TRANSACTION RULES**

20 Q. OPC witness Dr. Geoff Marke recommends in his direct testimony, page 13,
21 lines 12 through 20, that the Commission close Case No. AW-2018-0394 and open a "WX"
22 water rulemaking docket in order to draft rules mirroring affiliate transaction rules in place for

¹³ *Id.* at P. 15:13-15.

1 electric and gas utilities by adding the word “water” where applicable. Does Staff support
2 OPC’s recommendation?

3 A. No. While Staff agrees that water or sewer utilities with over 8,000 customers
4 should have affiliate transactions rules, Staff prefers continuing to work with the other parties
5 and stakeholders in Case No. AW-2018-0394 to draft new affiliate transactions rules for
6 qualifying water utilities. Staff is committed to proposing new rules for review in this case in
7 the near future. Staff is aware of changes to the current rules for electric and gas utilities that
8 need to be made to provide clarity to the affiliate transaction rules, and should also be reflected
9 in draft water affiliate transaction rules language.

10 Q. Does Staff support Dr. Marke’s recommendation that MAWC create a new
11 Cost Allocation Manual (“CAM”) using existing standards for other regulated utilities and
12 stakeholder input?

13 A. Creation of a CAM is required under the existing affiliate transaction rules
14 for electric and gas utilities. If the Commission decides water and sewer utilities with
15 over 8,000 customers should be covered under affiliate transactions rules as part of Case No.
16 AW-2018-0394 or in a future WX rulemaking case, Staff supports a requirement within such a
17 rule that MAWC be required to submit a CAM as soon as reasonably possible.

18 Q. Does this conclude your rebuttal testimony?

19 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-2022-0303
Implement General Rate Increase for Water)
and Sewer Service Provided in Missouri)
Service Areas)

AFFIDAVIT OF KIMBERLY K. BOLIN

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

COMES NOW KIMBERLY K. BOLIN and on her oath declares that she is of sound mind and lawful age; that she contributed to the foregoing *Rebuttal Testimony of Kimberly K. Bolin*; and that the same is true and correct according to her best knowledge and belief.

Further the Affiant sayeth not.

Kimberly K. Bolin
KIMBERLY K. BOLIN

JURAT

Subscribed and sworn before me, a duly constituted and authorized Notary Public, in and for the County of Cole, State of Missouri, at my office in Jefferson City, on this 13th day of January 2023.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: April 04, 2025
Commission Number: 12412070

D. Suzie Mankin
Notary Public