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WR-2024-0320

DIRECT/REBUTTAL TESTIMONY

OF

LENA M. MANTLE

Submitted on Behalf of the Office of the Public Counsel

MISSOURI-AMERICAN WATER COMPANY

FILE NO. WR-2024-0320

December 6, 2024

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DIRECT/REBUTTAL TESTIMONY

OF

LENA M. MANTLE, P.E.

MISSOURI AMERICAN WATER COMPANY

CASE NO. WR-2024-0320

Q. What is your name and business address?

A. My name is Lena M. Mantle and my business address is P.O. Box 2230, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am employed by the Missouri Office of the Public Counsel (“OPC”) as a Senior Analyst.

Q. On whose behalf are you testifying?

A. I am testifying on behalf of the OPC.

Q. What are your experience, education and other qualifications?

A. I began my employment with the OPC as Senior Analyst in August 2014. In this position, I have provided expert testimony in electric, gas, and water cases before the Public Service Commission of the State of Missouri (the “Commission”) on behalf of the OPC. I am a Registered Professional Engineer in the State of Missouri.

Prior to my employment by the OPC, I worked for the Staff of the Commission (“Staff”) from August 1983 until I retired as Manager of the Energy Unit in December 2012. During my employment at the Commission, I worked as an Economist, Engineer, Engineering Supervisor, and Manager.

Attached as Schedule LMM-1 is a brief summary of my experience with OPC and Staff and a list of the Commission cases in which I testified, Commission rulemakings in which I participated, and Commission reports in rate cases to which I contributed as Staff.

1 **Q. What is the purpose of your direct/rebuttal testimony?**

2 A. In this testimony I describe why the Commission should not approve the rate
3 stabilization mechanism (“RSM”) proposed by Missouri American Water
4 Company (“MAWC”). I also explain why the Commission should not approve the
5 production cost tracker requested by MAWC.

6 **Q. Which MAWC witnesses provided testimony regarding the RSM and
7 production cost tracker?**

8 A. MAWC witness Charles B. Rea provides direct testimony supporting MAWC’s
9 proposed RSM and MAWC’s proposed tariff sheets to implement the RSM
10 attached as Schedule CBR-5 to Mr. Rea’s testimony. MAWC witness LaGrand
11 provided testimony on the RSM and the Universal Affordability Tariff (“UAT”)
12 and requests a production cost tracker should the Commission not approve the RSM
13 as MAWC proposes it.

14 **Q. What are your recommendations to the Commission?**

15 A. I have three recommendations for the Commission.

- 16 1. The Commission should not approve a RSM for MAWC;
- 17 2. The Commission should not approve a tracker for MAWC’s production
18 costs; and
- 19 3. Should the Commission approve both the RSM and the UAT, it should also
20 order:
 - 21 a. The actual costs associated with the UAT program discounts not be
22 captured through the RSM; and
 - 23 b. The authorized revenues of the RSM be adjusted to account for the
24 revenue discounts provided to UAT participants.

1 **Q. Are any other OPC witnesses providing testimony regarding MAWC's**
2 **proposed RSM?**

3 A. Yes. OPC witness David Murray provides testimony that, if the Commission
4 approves the RSM proposed by MAWC, it should also make an adjustment to the
5 rate of return resulting in a reduction in revenue requirement of approximately \$4.6
6 million.¹

7 **THE COMMISSION SHOULD NOT APPROVE A REVENUE STABILIZATION**
8 **MECHANISM FOR MAWC**

9 **Q. What is a Revenue Stabilization Mechanism?**

10 A. A RSM is a mechanism that moves the risk of revenue collection from the utility to
11 its customers from changes in usage. It allows for interim rate changes between
12 general rate cases to ensure that the utility receives the full amount of revenue
13 requirement established by the Commission in the most recent general rate case.
14 The intent of the RSM is to assure the utility that it will receive the normalized
15 revenues set in the rate case regardless of changes in the number of customers,
16 customer usage, or changes in costs, *i.e.* the revenues billed by the utility are
17 assured regardless of customers' usage and without a review to determine if the
18 utility has prudently incurred its costs to serve the customers.²

19 **Q. Does a Missouri statute allow MAWC to have a RSM?**

20 A. Yes, but only if approved by the Commission. Section 386.266.4 RSMo. states:

21 Subject to the requirements of this section, a water corporation with
22 more than eight thousand Missouri retail customers may make an
23 application to the commission to approve rate schedules authorizing
24 periodic rate adjustments outside of general rate proceedings to
25 ensure revenues billed by such water corporation for regulated
26 services equal the revenue requirement for regulated services as

¹ Direct/rebuttal testimony, pages 73 – 75.

²https://www.brattle.com/wp-content/uploads/2017/10/6135_alternative_regulation_and_ratemaking_approaches_for_water_companies_wharton_villadsen_bishop_nawc_sep_23_2013.pdf, page 2. Also attached as Schedule LMM-2.

1 established in the water corporation's most recent general rate
2 proceeding or complaint proceeding, excluding any other
3 commission-approved surcharges and gross receipts tax, sales tax,
4 and other similar pass-through taxes not included in tariffed rates,
5 due to any revenue variation resulting from increases or decreases
6 in residential, commercial, public authority, and sale for resale
7 usage. (Emphasis added.)

8 **Q. What is the “revenue requirement” that this section is referring to?**

9 A. A utility’s revenue requirement represents the total amount of revenue a utility must
10 collect from customers to pay all the utility’s costs including a reasonable return on
11 investment. The Commission determines this amount in a general rate case after it
12 examines all expenses and costs. Rates are then designed to collect this amount of
13 revenue given a normalized customer count and usage amount.³ These rates are
14 intended to provide the utility an opportunity to bill its customers amounts to cover
15 expenses and earn a return on its investments.

16 **Q. Does § 386.266.4 RSMo *require* the Commission to grant a RSM if MAWC**
17 **makes an application for one?**

18 A. No. Section 386.266.5 RSMo. states:

19 The commission shall have the power to approve, modify, or reject
20 adjustment mechanisms submitted under subsections 1 to 4 of this
21 section only after providing the opportunity for a full hearing in a
22 general rate proceeding, including a general rate proceeding
23 initiated by complaint. The commission may approve such rate
24 schedules after considering all relevant factors which may affect the
25 costs or overall rates and charges of the corporation, provided that it
26 finds that the adjustment mechanism set forth in the schedules:

27 (Emphasis added)

28 While I am not an attorney, my reading of this section is that it gives the
29 Commission the discretion to approve, modify, or reject MAWC’s request for a
30 RSM after providing the opportunity for a full hearing in a general rate case. Based

³ Also referred to as billing determinants.

1 on this language, it is my understanding that the Missouri legislature did not regard
2 granting a RSM as a default option.

3 Section 386.266.5 also mandates that the Commission may only approve a
4 RSM “after considering all relevant factors which may affect the costs or overall
5 rates and charges of the corporation . . .” It is my opinion that, in making the
6 consideration of all relevant factors a requirement for approval of a RSM, the
7 legislature clearly realized that there needed to be a careful review of the design
8 and impact of a RSM, on not only MAWC, but also on MAWC’s customers.

9 **Q. What relevant factors should the Commission consider in deciding whether to**
10 **approve MAWC’s request for a RSM in this case?**

11 A. A RSM should not be considered a default option for MAWC. It is a special
12 treatment of revenue collection that should only be approved if it is necessary for
13 MAWC to provide safe and adequate service and earn a return on its investment. It
14 should also provide benefits to customers that surpass the transfer of risk to
15 customers. Therefore, there are two critical factors for the Commission to consider
16 when determining whether it approves, modifies, or rejects MAWC’s request for a
17 RSM:

18 1) Has the lack of a RSM resulted in MAWC having insufficient funds to
19 provide safe and adequate service and earn a sufficient rate of return
20 (“ROR”); and

21 2) Would an RSM provide benefits to MAWC’s customers that are greater
22 than the increase in risks that they are being asked to assume?

23 MAWC has neither shown that a RSM is necessary for it to earn a sufficient ROR
24 nor that having an RSM would provide benefits to the Company’s customers that
25 outweighed the shift of risks to them.

A RSM IS NOT NECESSARY FOR MAWC TO EARN A SUFFICIENT RETURN

Q. Did any of MAWC’s witnesses provide testimony that a RSM is *necessary* for MAWC to earn a return on its investments?

A. No. MAWC’s return on equity (“ROE”)⁴ witness Anne E. Bulkley testified that a RSM provides a regulated utility *a reasonable opportunity* to earn its ROE because it mitigates volumetric risk and stabilizes revenue.⁵

Q. Is this an accurate statement?

A. A RSM would mitigate volumetric risk and stabilize revenues billed the applicable customers. However, Ms. Bulkley did not show how a RSM would have resulted in a higher actual ROE in the recent past. In fact, as I provide below, having a RSM would have required MAWC to return revenue which would have lowered its actual ROE over the years 2017 through 2022.

Q. Are there other MAWC witnesses that provided testimony that a RSM was necessary for MAWC to earn its return on investment?

A. Yes. MAWC witness Brian W. LaGrand states that MAWC is proposing a RSM to address what he labels as “shortfalls” in MAWC’s ability to earn the ROE⁶ that he claims was “contemplated” in Stipulation and Agreements over the past ten years.⁷ However, Mr. LaGrand does not provide data showing how MAWC’s proposed RSM would have overcome that “shortfall” over that same time frame.

⁴ “While rate of return tells you how much profit you've made, or how much others have made, from a specific investment over a certain period of time, return on equity is a calculation specific to stocks that calculates how much money is made based on shareholders' investment in a company.” <https://www.nasdaq.com/articles/what-difference-between-return-equity-and-rate-return-2016-03-18>

⁵ Bulkley Direct, page 60-61.

⁶ LaGrand direct, pages 21 -22.

⁷ *Id.*, page 21.

1 **Q. What is Mr. LaGrand referring to as a “shortfall” in MAWC’s ability to earn**
2 **the ROE it contemplated in the past four cases?**

3 A. Mr. LaGrand compared MAWC’s actual return on equity for the last ten years to
4 the ROE range that he opines the Commission “has held” but not ordered in those
5 five cases.⁸ He defines shortfall as the difference between the ROE MAWC
6 achieved and what he believes was the ROE that the Commission would have
7 ordered had MAWC and the Parties to those cases not settled the issue.⁹

8 **Q. What ROE has MAWC earned over the last ten years?**

9 A. Mr. LaGrand calculates that MAWC has earned an average ROE of 8.31% over the
10 ten years of 2014 through 2023.¹⁰ He also gives his calculation of MAWC’s
11 earnings for each of those ten years that ranges from 7.46% to 8.86%.¹¹

12 **Q. How does the average 8.31% ROE compare to the ROEs set by the**
13 **Commission during this time period?**

14 A. As Mr. LaGrand pointed out, the Commission did not set a ROE for MAWC during
15 this time period.¹² Rather, MAWC entered into settlement agreements in which
16 MAWC, along with other parties to the cases, agreed to, among other items, a
17 normalized revenue requirement for MAWC.¹³ In agreeing to a revenue
18 requirement in each of these cases, MAWC agreed that the Stipulation allowed it
19 an opportunity to earn a sufficient ROE.

20 **Q. Do you agree that there has been a “shortfall” in the ROE earned by MAWC?**

21 A. No. Since MAWC’s cases have been black box settlements that did not include a
22 designated ROE, it is impossible to say whether MAWC has obtained the ROE that

⁸ *Id.*, page 20.

⁹ *Id.*, pages 19 – 22.

¹⁰ *Id.*, page 21.

¹¹ *Id.*, Table BWL-1, page 21.

¹² *Id.*, page 19.

¹³ *Id.*, pages 19-20.

1 it thought was included in the settled revenue requirement. MAWC was a willing
2 signatory in each of the cases and determined that it was satisfied with the agreed
3 to revenue requirement and the implied ROE in that revenue requirement.

4 **Q. If the Commission sets a ROE for MAWC, is MAWC guaranteed to earn that**
5 **ROE?**

6 A. No. The Commission sets rates in a manner that gives MAWC *an opportunity* to
7 earn the ROE included in revenue requirement. The ROE MAWC actually earns
8 is based on the revenues MAWC collects and the actions taken by MAWC in its
9 spending.

10 **Q. What does Mr. LaGrand point to as the reasons that MAWC did not have**
11 **higher ROE's during this time period?**

12 A. Mr. LaGrand pointed to two broad categories: (1) regulatory lag and (2) differences
13 between the billing determinants used to set rates and the actual billing
14 determinants experienced.¹⁴

15 **Q. What is regulatory lag?**

16 A. Regulatory lag refers to the difference between the time when costs change for a
17 utility and when the utility changes its rates to reflect the difference in costs. It is
18 possible for regulatory lag to contribute to a lower ROE in situations where costs
19 increase. This is what Mr. LaGrand is referring to when he discusses regulatory
20 lag that is primarily driven by new investments made by MAWC.¹⁵

21 However, regulatory lag can also contribute to a higher ROE when costs
22 are reduced. This second type of regulatory lag is highly beneficial to the utility.

¹⁴ *Id.*, page 22.

¹⁵ *Id.*

1 **Q. Would you give an example of regulatory lag that is beneficial to the utility?**

2 A. Revenue requirement includes both an amount collected from customers for
3 depreciation of assets and a return on the undepreciated portion of the cost of assets.
4 The first amount, the collection from customer for the depreciation of assets, is set
5 during a rate case based on what the Commission determines to be the “depreciable
6 life” of the asset. The second half, the return on the undepreciated portion of the
7 costs associated with the asset, is always set in the rate case based on the remaining
8 undepreciated cost of the capital investment as of the exact date that marks the end
9 of the true up period of the utility’s last rate case. Because this “return on”
10 component is set based on a fixed point in time, it generates beneficial regulatory
11 lag because the utility is receiving a fixed return for an asset while the asset is
12 constantly depreciating without that depreciation offsetting that return.

13 If rate making was instantaneous, the return on an asset would decrease
14 every month as the undepreciated cost of the asset is decreasing due to accruing
15 depreciation. However, because the rates customers pay recovers the return on the
16 undepreciated capital investment at the end of the true up period of the last rate
17 case, the true amount of the “return on” its investment lags behind constantly,
18 allowing the utility to earn more than it otherwise would in the absence of
19 regulatory lag. The difference between the return that customers pay and what the
20 return would be on that asset at any time between rate cases is therefore considered
21 beneficial or “positive” regulatory lag for the utility.

22 **Q. How does regulatory lag impact customers?**

23 A. Regulatory lag that is detrimental to the utility is beneficial to the customers.
24 Likewise, regulatory lag that is beneficial to the utility is detrimental to the
25 customers. Therefore, any mechanism that removes detrimental regulatory lag for
26 the utility is detrimental to the customers. Any mechanism that assures beneficial
27 regulatory lag for the utility is also detrimental to customers.

1 **Q. Would the impact of regulatory lag on a utility's ROE be resolved with a**
2 **RSM?**

3 A. No. A RSM would just make sure that the revenue requirement set in the last rate
4 case was recovered, *i.e.* it would assure the utility the positive regulatory lag, thus
5 harming customers.

6 **Q. Would a RSM impact negative regulatory lag for a utility?**

7 A. Not if the RSM was purely the reconciliation of billed revenues and authorized
8 revenues. However, the RSM proposed by MAWC includes an adjustment for
9 production costs thus resolving regulatory lag associated with any increases in
10 production costs.

11 In addition, Mr. LaGrand is asking that, if the Commission approves
12 MAWC's Universal Affordability Tariff ("UAT"), the RSM be used to collect the
13 discounts that would result from the implementation of this program.¹⁶ This
14 proposal would reduce negative regulatory lag for MAWC. Otherwise, MAWC
15 would have to wait until the next rate case for the recovery of the discounts from
16 customers.

17 **Q. Mr. LaGrand also cited changes in billing units as having an effect on ROE.**
18 **What are billing determinants?**

19 A. Billing determinants are the units used, along with revenue requirement, to
20 determine rates. For MAWC, billing determinants are usage and the size of the
21 customers' meters.

¹⁶ *Id.*, page 35. I explain later in this testimony why the Commission should not agree to this proposed method of cost recovery of the discounts of the UAT program.

1 **Q. Who determined the billing determinants in the last two MAWC general rate**
2 **cases?**

3 A. MAWC and other parties in MAWC's last three general rate increases agreed to
4 billing determinants in those cases.

5 **Q. Will a RSM resolve the differences between the billing determinants used and**
6 **the billing determinants realized?**

7 A. It should if the *revenue* requirement and the actual billed *revenue* are solely based
8 on the billing determinants. If a RSM includes adjustments for production costs or
9 a reconciliation for the Universal Affordability Tariff program as proposed by
10 MAWC, then it moves to just being a comparison of revenues, not a RSM that
11 tracks revenue variations due to changes in usage.

12 **Q. Would a RSM increase the possibility of a higher ROE for MAWC?**

13 A. Not necessarily. There are numerous components in the determination of ROE. A
14 RSM would only guarantee that MAWC would be able to bill the revenues set in
15 the last rate case. All else being equal, if the actual billed revenues are greater than
16 the revenue requirement, then having a RSM would result in a lower ROE because
17 MAWC would be required to return revenue to customers. If the actual billed
18 revenues were less than revenue requirement, then the RSM would allow MAWC
19 to bill for more revenue thus increasing its ROE.

20 **Q. How is ROE calculated?**

21 A. According to *Investopedia*, ROE is calculated as:¹⁷

22
$$\text{Return on Equity} = \frac{\text{Net Income}}{\text{Average Shareholders' Equity}}$$

¹⁷ <https://www.investopedia.com/terms/r/returnonequity.asp#toc-calculating-return-on-equity-roe>

Net Income is further defined as “the amount of income, net expenses, and taxes that a company generates for a given period.” The equation now becomes:

$$\text{Return on Equity} = \frac{\text{Income} - (\text{Expenses} + \text{Taxes})}{\text{Average Shareholders' Equity}}$$

A RSM only guarantees one part of the equation: income. Expenses and taxes are still variable and unknown.

Q. If having a RSM would not guarantee a higher ROE, why do you think MAWC is requesting a RSM?

A. A RSM would lower MAWC’s risk by removing uncertainty regarding the revenue MAWC bills its customers. This piece of the ROE equation provided above would be set. With a RSM, MAWC would receive a set amount of revenue regardless of the weather. MAWC would receive a set amount of revenue regardless of a drop in the number of customers. MAWC would receive a set amount of revenue regardless of any reduction in its customers’ usage and reduce MAWC’s incentive to control and reduce costs.

In addition, the RSM proposed by MAWC would assure recovery of one of the biggest components of MAWC’s expenses: production costs. MAWC also proposes using the RSM to capture the costs associated with the discounts provided customers billed on its UAT program between rate cases thus reducing the risk that these costs would be recovered.

Q. Should MAWC’s ROE be adjusted if the Commission approves its request for a RSM?

A. Please see OPC witness David Murray’s rebuttal testimony for recommended approaches to consider the lower business risk associated with an RSM. As Mr. Murray’s testimony explains, lower business risk allows for the use of more debt in a capital structure. The ability to utilize more debt reduces the ROR charged to

1 customers even if the ROE is held constant. However, if MAWC's capital structure
2 is not adjusted to include more debt, then the Commission should reduce the
3 authorized ROE. Again, see Mr. Murray's testimony for more detail on the
4 appropriate consideration for the lower business risk if an RSM is approved.

5 THE VOLATILITY OF MAWC'S BILLED REVENUES HAS NOT BEEN EXCESSIVE

6 **Q. In his direct testimony Mr. Rea¹⁸ discusses the factors that cause revenues to**
7 **be volatile year to year. Does he provide any evidence as to the impact of these**
8 **factors on MAWC's historical revenues?**

9 A. No. However, in MAWC's last general rate case WR-2022-0303, MAWC witness
10 John M. Watkins, provided in Schedule JMW-1 of his direct testimony the
11 Authorized Revenues and the Actual Revenues for the calendar years 2012 through
12 2021. I have attached his schedule from case no. WR-2022-0303 to this testimony
13 as Schedule LMM-3.

14 While this table does not have information for calendar years 2022 and
15 2023, it does show that the "volatility" of the authorized revenues vs. billed
16 revenues for the customer classes that MAWC is requesting be included in its RSM
17 for a recent ten-year period.

18 **Q. Can you estimate the revenue volatility that would have been avoided had a**
19 **RSM been in effect for the last five years of the time period provided by Mr.**
20 **Watkins in this schedule?**

21 A. Yes. Using this information, I calculated the following variances from the
22 normalized revenue requirement for the classes that the RSM would apply to.

¹⁸ Rea Direct, Pages 41 - 43.

1
2

Table 1
Revenue Variances

	Rate Case Revenue	Billed Revenue	Variance	% Diff
2017	\$258,553,015	\$259,688,901	\$1,135,886	0.44%
2018	\$274,074,840	\$286,326,807	\$12,251,967	4.47%
2019	\$281,650,968	\$276,050,243	(\$5,600,725)	-1.99%
2020	\$281,650,968	\$284,651,761	\$3,000,793	1.07%
2021	\$299,556,421	\$296,546,416	(\$3,010,005)	-1.00%
Total	\$1,395,486,212	\$1,403,264,128	\$7,777,916	0.56%

3
4
5
6
7
8
9

This table shows that the difference between the actual billed revenues and the rate case normalized revenues ranged from 4.47% (meaning MAWC collected 4.47% more revenues in that year than the normalized rate case revenues) and -1.99% (meaning the revenues MAWC billed were just 1.99% less than the normalized rate revenues.) For the total five years, MAWC billed for 0.56% more revenue than the rate case normalized revenues from these rate classes.

10 **Q. If MAWC had a RSM over this time period, would MAWC have earned a**
11 **higher ROE?**

12 A. No. If MAWC, over this time period, had a RSM that only accounted for revenue,
13 it would have returned almost \$8 million in revenues resulting in an even lower
14 ROE across these five years. In other words, all else being equal, having a RSM
15 would have lowered the ROE for MAWC over this time period.

16 **Q. To summarize this section of your testimony, would a RSM remove volatility**
17 **from MAWC’s ROE?**

18 A. No. A RSM would not assure MAWC of no volatility in its earned ROE. While
19 MAWC may not have earned the ROE it contemplated it was agreeing to in past
20 rate cases, fluctuations in ROE is consistent with the purpose of awarding an equity
21 risk premium.

IMPACTS OF A RSM ON CUSTOMERS

Q. Moving to the second factor that the Commission should consider: how would a RSM impact MAWC's customers?

A. A RSM will introduce uncertainty to customers. Customers would be faced with weather risks, small customers would face the risk of having to replace revenue due to very large customers leaving MAWC, and all customers would face the risk that their bills will be higher because other customers used less water.¹⁹ Customers would lose the predictability of how their actions affect their bills if the Commission approves a RSM for MAWC.

Q. Are there any benefits to MAWC's customers from MAWC receiving a RSM?

A. In the event that MAWC bills for more revenue than the revenue requirement set in the rate case, MAWC's customers will get a credit on their bills. Mr. Rea touts this as a sign of the equity of its proposed RSM,²⁰ but he also provides testimony that he expects water consumption per customer to decline.²¹ If he is correct, this means, everything else being the same, MAWC's revenues with a RSM will be greater than without a RSM.²² Net customer growth that includes usage greater than the decline in usage per customer is the only way that the RSM would provide a credit back to customers.

¹⁹ If production costs are included in the RSM, then customers also risk increasing costs of production costs and MAWC's loss of incentive to keep these costs as low as possible. If the UAT discounts are included in the RSM, then the customers would face the risk of variability in their bills dependent upon participation in the UAT program.

²⁰ Rea direct, pages 44-45.

²¹ *Id.*, page 42.

²² However, Schedule LMM-D-3 shows that, in contrast to Mr. Rea's testimony, actual revenues have not consistently declined below allowed revenues but instead have been both greater and lower than the allowed revenues.

1 **Q. Wouldn't customers get a credit if the weather was higher and drier than**
2 **normal?**

3 A. Yes, but they would first have to pay the higher bills. Also, due to the manner that
4 MAWC proposes for credits, the lower usage customers that did not pay the higher
5 costs receive the same credit as the customers with high bills. I will discuss the
6 inequities in this later in this testimony.

7 **Q. Mr. Rea states that MAWC has no control over the weather as a reason that**
8 **MAWC should be granted a RSM.²³ Do customers have control over the**
9 **weather?**

10 A. No. That same rationale makes it equally unjust for customers to have to pay the
11 RSM. The only difference between the customers and MAWC is that MAWC is
12 being permitted to earn a profit to compensate its shareholders for this risk while
13 MAWC's customers are being asked to shoulder more risk without compensation.

14 **Q. Mr. Rea states that MAWC does not have control of the drivers that result in**
15 **declining usage as a reason that MAWC should be granted a RSM.²⁴ Do**
16 **MAWC's customers have control over these drivers?**

17 A. No. MAWC witness Max W. McClellan explains in his testimony:

18 Water-efficient fixtures and other drivers such as conservation
19 education and government-mandated standards will continue to
20 drive further efficiency into residential and nonresidential usage per
21 customer.²⁵

22 Just as MAWC does not have control over these drivers, MAWC's customers do
23 not have control over the efficiencies of the fixtures that are available, government-
24 mandated standards, or the weather. Again, that is why it is equally unjust for
25 customers to have to pay the RSM.

²³ Rea Direct, page 42.

²⁴ *Id.*

²⁵ McClellan Direct, page 49.

1 **Q. Is MAWC acting in any manner that may contribute to a decline in usage?**

2 A. Mr. Rea states that MAWC “is committed to helping customers use water
3 efficiently and to provide quality water service that is affordable.”²⁶ This
4 commitment to help customers use less water, contributes to the decline in
5 customers’ water usage.

6 **Q. Is there any other action that MAWC is taking that is likely to lead to a decline
7 in usage?**

8 A. Yes. As MAWC is increasing its spending and asking for more and greater rate
9 increases, customers will believe that using less water will reduce their bills. If the
10 Commission approves a RSM that allows MAWC to charge more when customers
11 use less, this effort to reduce usage to reduce their water bills will be futile.

12 MAWC is influencing its customers to reduce their usage while asking for
13 a RSM that would assure a set amount of revenues regardless of the usage. In
14 essence, it creates a subsidy where customers are footing the bill for other
15 customers’ usage reductions. It is unjust for customers who cannot reduce their
16 usage to have to pay more through the RSM for revenues to MAWC that customers
17 that can reduce their usage would no longer pay.

18 **Q. Did MAWC provide any other ways a RSM would benefit MAWC’s
19 customers?**

20 A. Mr. Rea provided the following as the benefit of a RSM to MAWC’s customers:

21 As I explain below, the Company's ability to reliably recover its
22 revenue requirement over the long term through rates is an important
23 part of the Company's ability to properly operate, maintain, and
24 invest in the water system at a reasonable cost. This ability to
25 prudently manage the systems at a reasonable cost is in the long-
26 term best interests of our customers.²⁷

²⁶ Rea Direct, page 44.

²⁷ *Id.*

1 **Q. Will a RSM guarantee customers that MAWC will properly operate, maintain,**
2 **and invest in the water system?**

3 A. No. It only guarantees that MAWC will recover a set amount of revenues. In
4 addition, if the Commission approved the RSM proposed by MAWC with an
5 adjustment for production expenses, the RSM would remove the incentive for
6 MAWC to control these costs.

7 **Q. Will a RSM guarantee customers that MAWC will prudently manage its water**
8 **system?**

9 A. No. It only guarantees that MAWC will recover a set amount of revenues.

10 **Q. Are these the only benefits to customers mentioned by Mr. Rea?**

11 A. No. Mr. Rea also points out that a RSM would eliminate MAWC's financial
12 incentive to sell more water.²⁸

13 **Q. How is this a benefit to customers?**

14 A. Mr. Rea states that:

15 Improving water efficiency is a "win/win/win" providing a wide range of
16 benefits for consumers, utilities, businesses, and for communities as a
17 whole. Approving an RSM opens the path to achieving that winning
18 combination.²⁹

19 **Q. Do you agree that a RSM opens the path to improving water efficiency?**

20 A. No. A RSM will send mixed signals to customers. If all customers improve their
21 water efficiency equally, their bills will not change because the RSM charge will
22 increase to assure MAWC gets a set revenue. If their bill does not reflect monetary
23 savings, then many customers will be less likely to implement water saving
24 measures being frustrated that their past attempts to use less water does not impact
25 their monthly bills.

²⁸ *Id.*, page 51.

²⁹ *Id.*, page 49.

1 **Q. Would you explain how the bills of customers whose usage is declining would**
2 **change if the Commission approves a RSM?**

3 A. With a RSM, the total revenues billed are constant regardless of customers' usage.
4 Therefore, if actual revenues billed were below the revenue requirement set in the
5 RSM, customers can use less water and their bill may not reflect their reduced water
6 usage. This could occur if weather was wetter than normal and/or if their neighbors
7 used considerably less than they did the previous year since a RSM will require
8 MAWC's customers to replace the revenues not billed because of reduced usage.
9 With the RSM proposed by MAWC, a residential customer's bill would be likely
10 to see a large increase should one of the Sales for Resale customers leave the
11 system. I will provide a further explanation of this later in this testimony.

12 In addition, customers can only reduce their usage so much without
13 impacting their quality of life. All else being equal, when a customer meets this
14 point, their bill will increase even though they have minimized their usage until all
15 the other customers have also reached this point.

16 **Q. In conclusion, should the Commission approve a RSM for MAWC because it**
17 **has not earned the ROE it thinks it should have earned?**

18 A. No. A RSM does not necessarily mean that MAWC will come any closer to
19 achieving the ROE that it expects. It would just mean that MAWC has successfully
20 moved the risk of revenue volatility to its customers. This risk should not be passed
21 on to customers creating confusion and improper price signals. The Commission
22 should not approve a RSM of any kind for MAWC.

23 **THE RSM PROPOSED BY MAWC HAS MANY ISSUES**

24 **Q. What are the problems of the RSM proposed by MAWC?**

25 A. The RSM proposed by MAWC has at least the following issues:

- 26 1) It improperly includes a mechanism to collect increases in production costs
27 between rate cases;

- 1 2) MAWC is requesting it be used to capture the impact of the Universal
2 Affordability Tariff program between rate cases;
3 3) It treats customers as if they are homogenous;
4 4) Revenue shortfalls are treated differently than revenue excesses; and
5 5) MAWC's proposed tariff sheets do not match the RSM proposed by Mr. Rea.

6 *PRODUCTION COSTS CANNOT BE INCLUDED IN A RSM*

7 **Q. What does the term "production costs" mean in this context?**

8 A. Mr. LaGrand provides this general explanation of production costs:

9 These costs are related to Fuel & Power, Chemicals, Waste
10 Disposal, and Purchased Water. This would include things such as
11 the costs of electricity at water treatment plants, the costs of
12 chemicals to treat and clean the water before it is delivered to
13 customers, sludge removal costs at a wastewater lagoon, and water
14 purchased from a neighboring community to supplement our
15 production capacity.³⁰

16 **Q. Why is MAWC including production costs in the RSM?**

17 A. MAWC witness Rea states that "excluding the incremental production costs would
18 reduce the Company's opportunity to earn a fair return on equity."³¹

19 **Q. In your opinion, does Section 386.266.4 RSMo. allow for recovery of
20 production costs in a RSM?**

21 A. No. Section 386.266.4 RSMo. only allows MAWC to request an interim rate
22 mechanism that ensures its revenues billed equal the revenue requirement set in the
23 last rate case for the residential, commercial, public authority, and sale for resale
24 customer classes. It does not include provisions for any costs incurred by MAWC.

25 By including the production costs in this calculation, MAWC is essentially
26 asking the Commission to approve two interim rate mechanism rolled together –

³⁰ LaGrand Direct, page 32.

³¹ Rea Direct, page 40.

one that guarantees that it recovers the revenue requirement set in this case (as allowed by statute) and one that guarantees that it recovers its production cost expense (not authorized by statute).

Q. How is this interim rate mechanism that MAWC is requesting different from a tracker for production costs?

A. With a tracker, the difference between the cost incurred and the production costs included in revenue requirement is tracked between cases. Interim rates are not charged between rate cases to recover these costs. In the next rate case, parties review the prudence of MAWC incurring those costs. Based on this review, testimony can be provided to the Commission regarding how much, if any, of the tracked costs MAWC should be allowed to recover in the revenue requirement of that future case.

By including these production costs in a RSM, MAWC would recover the production costs between rate cases with no prudence review of these costs.

Q. If actual production costs were less than the production cost “authorized” in the last rate case, would the mechanism proposed by MAWC give that cost savings back to the customers?

A. Yes. However, it would also guarantee recovery of increased production costs. There would thus be no reason for MAWC to strive to keep production costs low.

Q. Is there any indication that it is unlikely that production cost will be lower than what is included in revenue requirement in this case?

A. No. MAWC would not ask for a tracker if it thought there was a good probability that actual production costs it incurs would be less than what would be included in revenue requirement.

Q. Why is that?

A. Declining costs are positive regulatory lag for MAWC. If MAWC is able to acquire the products at a cost less than what was included in revenue requirement, MAWC keeps that savings without a tracker. The amount included in revenue requirement would not be changed until the next rate case so this savings will result in increasing earnings. The savings between rate cases would be positive regulatory lag for MAWC. This positive regulatory lag induces efficiencies between rate cases.

Q. Is there a circumstance where an increase in production costs could lead to a RSM charge when billed revenues were greater than revenue requirement set in this case?

A. Yes. When the difference between the actual billed revenue was greater than the revenue requirement set in the RSM but less than the increase in the production costs, the RSM would appear as an increase on MAWC’s customers’ bills. Table 2 below gives some examples of how increases in production costs would affect the RSM if production costs were included in the RSM as proposed by MAWC.

Table 2
RSM with Production Costs Examples

Scenario		A	B	C	D
Revenues	Rev Req	\$400	\$400	\$400	\$400
	Actual	\$405	\$405	\$395	\$395
	<i>Diff</i>	<i>(\$5)</i>	<i>(\$5)</i>	\$5	\$5
Production Costs	Rev Req	\$10	\$10	\$10	\$10
	Actual	\$18	\$8	\$18	\$8
	<i>Diff</i>	\$8	<i>(\$2)</i>	\$8	<i>(\$2)</i>
RSM Amount		\$3	<i>(\$7)</i>	\$13	\$3

In Scenario A, MAWC billed customers \$5 more than revenue requirement. Absent the inclusion of production costs, MAWC would return that \$5 to its customers. However, in this scenario production costs were \$18 which was \$8 more than what was included in revenue requirement. The inclusion of production costs in the RSM

1 resulted in a RSM amount of \$3. So even though customers paid \$5 more than the
2 revenue requirement, they will be charged an extra \$3 because of the increase in
3 production costs.

4 In Scenario B, MAWC again billed its customers \$5 more than revenue
5 requirement. Absent the inclusion of production costs, this \$5 would be returned
6 to the customers. However, in this scenario, production costs decreased by \$2 so
7 by including production costs in the RSM, MAWC would return \$7 to its
8 customers.

9 In Scenario C, MAWC billed customers \$5 less than the revenue
10 requirement. In this scenario, absent the production costs, MAWC would recover
11 the \$5 through the RSM. However, production costs increased by \$8 meaning that
12 MAWC would collect \$13 through the RSM.

13 In the final scenario, MAWC billed customers \$5 less than the revenue
14 requirement. A RSM without the production costs would result in MAWC billing
15 customers the extra \$5. In this scenario, the production costs went down \$2, so if
16 production costs are included, customers only pay \$3.

17 **Q. What conclusions can you draw from these scenarios?**

18 A. These scenarios, while just examples, show how the RSM that MAWC is proposing
19 is actually a netting of two different mechanisms; one mechanism to collect/return
20 the difference between the revenues billed and revenue requirement as allowed by
21 Section 386.266.4. RSMo. and the other mechanism to collect/return differences in
22 the production costs included in the rate case and the actual production costs – not
23 allowed by Missouri statute.

24 By adding production costs what MAWC is trying to do is tilt the RSM in
25 favor of MAWC in most scenarios even when the RSM would normally result in
26 returning money to ratepayers. It removes any sense of balance in the RSM and it
27 could be manipulated by simply spending more on production costs.

1 **Q. Do you disagree with Mr. Rea’s testimony that production costs vary with sales**
2 **volume and therefore should be included in a RSM?**³²

3 A. It makes sense that production costs would vary with the amount of usage.
4 Regardless of whether or not a cost varies with usage, Section 386.266.4 RSMo. is
5 very specific that the Commission can only authorize a mechanism that assures
6 MAWC recovers its revenue requirement. This section does not allow for recovery
7 of costs.

8 *UNIVERSAL AFFORDABILITY TARIFF AND THE RSM*

9 **Q. OPC witness Dr. Geoff Marke has filed testimony that OPC supports the**
10 **Universal Affordability Tariff (“UAT”). MAWC witness Brian LaGrand**
11 **requests that actual costs associated with the UAT program discounts be**
12 **captured through the RSM if the Commission approves MAWC’s proposed**
13 **RSM.**³³ **Should the costs associated with the UAT be captured through the**
14 **RSM if the Commission approves a RSM for MAWC?**

15 A. No. While this seems like an easy solution for recovery of revenues not billed in
16 the UAT, the RSM enabling statute, Section 386.266.4. RSMo. limits the RSM to
17 revenue variation resulting from increases or decreases in usage. It does not include
18 variation in revenues due to tariffed discounts.

19 **Q. What is your recommendation to the Commission regarding the RSM if it also**
20 **approves the UAT?**

21 A. My recommendation is that the Commission should not approve a RSM for all the
22 reasons cited in my testimony above. However, should the Commission approve
23 both the RSM and the UAT, it should also order:

- 24 1. The actual costs associated with the UAT program discounts not be captured
25 through the RSM; and

³² Rea Direct, page 40.

³³ LaGrand Direct, page 35.

2. The authorized revenues of the RSM should be adjusted to account for the expected revenue discounts provided to UAT participants just as it is modified to remove the industrial customer class.

MAWC'S RSM ASSUMES ALL ITS CUSTOMERS ARE HOMOGENOUS

Q. Would you explain your understanding of how MAWC is proposing the RSM rate be calculated?

A. Important in understanding how MAWCs RSM would work is understanding what Mr. Rea calls authorized revenues. While Mr. Rea did not specifically define authorized revenues, his description of how the RSM MAWC is proposing would work reveals that authorized revenues is the sum of the revenue requirement of the classes that the RSM would apply too. There would be no residential authorized revenues, no commercial authorized revenue, no other public authorities authorized revenue, and no sale for resale authorized revenues; only authorized revenues for these groups combined. These authorized revenues would be allocated to the months based on a proration of annual rate revenues to months using data from the last two years of system delivery. He did not provide the data or the allocation percentages resulting from his proposal.³⁴

In his description of how the RSM would work, Mr. Rea explains that the RSM amount to be charged/credited be a monthly comparison of the authorized revenues to actual billed revenues for the combined residential, commercial, other public authorities ("OPA") customer classes and Sale for Resale ("SFR") customers. There would be no tracking of differences by customer class.³⁵

Likewise, for the RSM proposed by MAWC, each month the actual production costs³⁶ will be compared to the production costs included in the rate case revenue requirement allocated to the months based on the last two years of

³⁴ Rea Direct, page 45.

³⁵ *Id.*

³⁶ *Id.*, with a percentage of usage removed for industrial customers.

1 system delivery. This difference, positive or negative, is added to the difference
2 between the authorized revenues and actual billed revenues for that month.³⁷

3 Differences between the monthly authorized revenue and billed revenue
4 would be deferred to a regulatory asset or liability account and accrue interest at
5 MAWC's short-term interest rate. At the end of the calendar year, these amounts
6 would be reconciled. If this reconciliation shows a revenue deficit, a volumetric
7 charge is calculated. If the reconciliation shows excess revenues were billed, a
8 credit is calculated as the revenue to be returned divided by the number of
9 customers in the combined classes.³⁸

10 **Q. Would you explain why having the same RSM rate for all rate classes is a**
11 **shortcoming of MAWC's proposed RSM?**

12 A. MAWC is requesting the RSM apply to all the customer classes that Section
13 386.266.4 RSMO. allows. Its proposed RSM treats each customer as if they were
14 the same. The mechanism assumes that each class is equally weather sensitive, *i.e.*
15 a St. Louis County residential customer reacts the same to a change in weather as
16 an Other Public Authority customer from St. Louis County.

17 It also assumes that the impact of a customer leaving the system is the same
18 regardless of what class the customer was in before leaving, *i.e.* the impact on the
19 revenue requirement of a residential customer leaving the system is the same as the
20 revenues from a Sale for Resale customer leaving the system.

21 **Q. Why are these not valid assumptions?**

22 A. In his direct testimony, MAWC witness Mr. McClellan provides the results of his
23 modeling of the residential, commercial and OPA classes that MAWC used to
24 develop adjustments to revenues in this case. He developed a model for each class

³⁷ The annual authorized revenues and the annual amount of expenses for all production costs would be prorated using MAWCs last two years of system delivery to obtain a monthly amount of Authorized Revenues and production costs. Rea Direct, page 45.

³⁸ Rea Direct, page 46.

that shows the weather sensitivity for each class is different. The table below provides the result of his modeling with respect to each class’s sensitivity to changes in temperatures in the summer.³⁹

Table 3
Class Differences in Weather Sensitivity

		CDD ⁴⁰ Sensitivity	t-Stat
Residential	St. Louis County	n/a	n/a
	Other	0.0030	3.3154
Commercial	St. Louis County	0.0317	2.6404
	Other	0.0142	2.7410
OPA	St. Louis County	0.0890	1.9557
	Other	0.0336	1.4512

Q. Would you explain how this information shows that these classes have different sensitivities to changes in temperature?

A. The larger the number in the column labeled “CDD Sensitivity” the greater the sensitivity to changes in temperature. The St. Louis County OPA class is the most weather sensitive with a value of 0.0890. The St. Louis County Residential class model shows no sensitivity to changes in temperature. This indicates that the usage of a St. Louis OPA customers are reactive to a change in weather and a St. Louis Residential customer is not.

As Mr. McClellan testified, the t-Stat number indicates the explanatory power of the variable.⁴¹ The higher the t-Stat the more meaningful temperature sensitivity is in explaining how the class uses water. Any t-Stat value of less than 2 has little explanatory power. In Mr. McClellan’s models, temperature sensitivity is a very significant explanatory variable for usage of the Residential Other class

³⁹ McClellan Direct, pages 45 - 46.

⁴⁰ Degree day is the difference between the mean daily temperature (high temperature plus low temperature divided by 2) and 65. If the number is positive, then it is a measure of cooling called cooling degree days or CDD. If the number is negative, the CDD for that day is zero.

⁴¹ McCellan Direct, page 46.

even though the response to weather is much smaller than the response of the St. Louis OPA customers.

Based on the results of the analysis conducted by Mr. McClellan, there is a significant difference in, not just the usage of the customers, but also the weather sensitivity of the classes that MAWC is proposing be combined in its RSM.

Q. You mentioned the usage of the customers in this group. Would the impact of a Sale for Resale customer leaving the system have the same impact as a residential customer leaving MAWC's system?

A. No. Table 4 shows another fallacy of the assumption that all customers are similar.

Table 4
2023 Customer Numbers & Average Use⁴²

	# of Customers	Average 2021 Monthly Use/Customer (Gallons)
Residential	441,569	5,873
Commercial	26,997	36,458
Other Public Authorities	1,944	69,084
Sale for Resale	29	16,063,491
Total	470,539	8,879

While the bulk of MAWC's customers are residential, the average usage of a Sale for Resale customer is more than 2,700 times greater than the average residential customer.

Q. If the Commission approves MAWC's RSM as requested, what would be the impact of a Sale for Resale customer leaving the system?

A. The bills of all the other customers would increase to assure MAWC is still receiving the revenue that it would have billed that Sale for Resale customer that used approximately 16 million gallons per month.

⁴² MAWC 2023 Annual Report to the Missouri Public Service Commission, page W-1.

1 **Q. If the Commission approves MAWC's RSM as requested, what would be the**
2 **impact of a residential customer leaving the system?**

3 A. All other customers would have increased bills to assure MAWC is still receiving
4 the revenue that it would have billed that Residential customer. However, on
5 average, MAWC's residential customers in 2023 used approximately 5,873 gallons
6 per month. Therefore, this difference from one customer leaving the system is not
7 likely to impact the RSM rate due to rounding of the RSM rate to the nearest
8 \$0.00001 per 100 gallons.
9

10 REVENUE SHORTFALLS ARE TREATED DIFFERENTLY THAN REVENUE EXCESSES

11 **Q. How are RSM shortfalls treated in MAWC's proposed RSM?**

12 A. A RSM shortfall means the customers to which the proposed RSM would apply
13 need to pay more to assure MAWC gets full recovery of the revenue requirement
14 set in the last rate case. In the RSM proposed by MAWC, the shortfall amount is
15 divided by the expected water usage of the customers in the RSM classes in the
16 April to December months of the next year to determine the RSM rate. This same
17 rate is applied to the usage of *all* effected customers.

18 **Q. How does MAWC propose to return RSM excesses to customers?**

19 A. A credit would be determined based on the number of customers at the time the
20 credit is issued.

21 **Q. Why does this matter?**

22 A. Each customer would receive the same refund, i.e. the SFR customer with an
23 average usage of 16 million gallons would get the exact same refund as a residential
24 customer with an average usage of 5,873 gallons. For example, a \$10 million credit
25 to customers based on the number of customers in 2023, regardless of how much
26 they had paid MAWC over the previous year, would get a credit of \$21.25.⁴³ This

⁴³ \$10 million divided by 470,539 (the total number of customers that the RSM would have applied to.)

1 means each residential, commercial, OPA, and SFR customer would have received
2 a credit of \$24.17 regardless of how much each had overpaid in the accumulation
3 period.

4 **Q. Why is there a difference between the method of collecting when actual**
5 **revenues was lower than the revenue requirement and the method of returning**
6 **when actual revenue was greater than the revenue requirement?**

7 A. Mr. Rea testifies that this method for returning revenue collected above authorized
8 revenues would “reward” customers who conserve water at a higher percentage
9 than those that use more water.⁴⁴

10 **Q. Do you agree that this would be a reward for customers that conserve water?**

11 A. MAWC’s proposed method to return an over-collection provides the same credit to
12 every customer, whether they conserved or not. This means that every customer,
13 whether they are a Sales for Resale customer or a residential customer, receives the
14 exactly the same amount.

15 The purpose of the RSM is not to promote or reward conservation by
16 customers. In fact, the more customers conserve, the more likely they are to have
17 to pay more the next year. The purpose of the RSM is to make sure that MAWC
18 collects the same amount of revenues despite its customers’ efforts to conserve
19 water. If MAWC wants to incent its customers to conserve water, there are other,
20 more direct methods that provide incentives to only those customers who actually
21 conserve water.

22 This methodology for “crediting” customers really is just customers with
23 large usage subsidizing low-usage customers.

⁴⁴ Rea Direct, page 46.

1 **Q. With MAWC's RSM design, what is the impact on the customers that have**
2 **conserved when there is an under-collection of revenues?**

3 A. Despite their best conservation efforts to reduce their bills, customers' bills could
4 increase the next year because the previous summer was cool and rainy. Or their
5 bills could increase because many of the other customers are conserving due to a
6 recession. Customers' bills may also increase because customers are leaving the
7 system. This is the asymmetry of the RSM proposed by MAWC. This certainly is
8 not an appropriate "reward" for customers that conserve.

9 **Q. Mr. Rea states that the COVID-19 pandemic situation is a prime example of**
10 **an external event that causes fluctuations in revenues. He then discusses the**
11 **impact of the COVID-19 pandemic as an example of an external event when**
12 **MAWC saw increased sales volumes for residential customers.⁴⁵ If MAWC**
13 **had a RSM during the COVID-19 pandemic, would residential customers have**
14 **received a credit back of this increase in their bills?**

15 A. Not necessarily.

16 **Q. Would you please explain?**

17 A. In his analysis of MAWC customer water consumption for revenue normalization
18 in this case, MAWC witness Max McClellan included, as one of the adjustments,
19 an adjustment for the impact of COVID-19.⁴⁶ Mr. McClellan found "[t]he
20 COVID-19 impact variables generally indicate that residential usage increased and
21 usage for commercial and OPA customers decreased as a result of COVID-19."⁴⁷
22 If the billed revenue of the non-residential customers decreased more than the billed
23 revenues of the residential class increased, the RSM proposed by MAWC would

⁴⁵ *Id.*, page 43.

⁴⁶ McClellan Direct, page 33.

⁴⁷ *Id.*, page 46.

1 have resulted in all customers being billed more the next year regardless of the
2 residential customers increased usage.

3 In fact, the data provided by Mr. Watkins in the last rate case and attached
4 to this testimony as Schedule LMM-3 shows that had the RSM proposed by MAWC
5 been implemented in 2021,⁴⁸ there would have been a surcharge on all customers'
6 bills in 2022. Thus, despite paying higher bills in 2021, residential customers
7 would have had to pay more because the commercial customers used less.

8 **Q. Then is the RSM proposed by MAWC symmetrical as Mr. Rea testifies?⁴⁹**

9 A. It is symmetrical for MAWC in that it is guaranteed a set level of revenues. If
10 actual revenue billed is lower than revenue requirement, customers make up the
11 difference and if actual revenues billed are higher than revenue requirement,
12 MAWC returns the excess to the customers. However, it is not symmetrical to
13 MAWC's customers. If there is a shortfall in revenues, all customers make up the
14 difference according to their usage. If MAWC billed an excess amount of revenue,
15 the excess is returned to customers with the same amount credited to each customer
16 regardless of their usage thus resulting in large customers subsidizing small
17 customers.

18 **PROPOSED RSM IS INCONSISTENT WITH FILED TARIFF SHEETS**

19 **Q. What problems have you identified with MAWC's proposed RSM tariff**
20 **sheets?**

21 A. MAWC's proposed RSM tariff sheets are identical to the RSM tariff sheet it
22 proposed in its last rate case, case no. WR-2022-0303, and contains the same
23 problems that I identified in my class cost-of-service direct testimony that I filed in
24 that case. I will provide details on the inconsistencies I found with MAWC's

⁴⁸ The calendar year of 2021 was included in the months Mr. McClellan defined as the time period that COVID-19 impacted usage, page 43.

⁴⁹ Rea Direct, page 46.

1 proposed RSM tariff sheet in the last rate case with a few new concerns in the class
2 Cost-of-Service and Rate Design Direct and Rebuttal testimony in this case on
3 December 20, 2024.

4 **THE COMMISSION SHOULD NOT APPROVE A PRODUCTION COST**
5 **TRACKER**

6 **Q. Which MAWC witness provided direct testimony requesting a tracker for**
7 **production costs and why is MAWC requesting a tracker for production**
8 **costs?**

9 A. Mr. LaGrand requests the Commission approve a tracker for production costs. He
10 states the following as the reason for his request.⁵⁰

11 Similar to the Company's Pension & OPEB trackers that have been
12 in place for nearly 15 years, the production cost tracker primarily
13 consists of costs that are outside the Company's control. These are
14 among the most critical costs incurred because they are critical for
15 providing safe, clean drinking water service to our customers and
16 their families. This is not a discretionary expense the Company can
17 choose to incur or not incur.

18 **Q. Are production costs new to MAWC?**

19 A. No, they are not.

20 **Q. Are production costs outside of the control of MAWC?**

21 A. Not completely. MAWC has control over contracts for products and the delivery
22 of the products.

23 **Q. Is the fact that the costs are somewhat outside of the control of MAWC a**
24 **reason for a tracker?**

25 A. No.

⁵⁰ LaGrand Direct, page 33.

1 **Q. Would you explain?**

2 A. MAWC receives a return on its investment for the risk that it is taking. The risk of
3 fluctuations in production costs is one of the risks it gets compensated for. Many of
4 the costs MAWC incurs are out of its control. For example, MAWC does not have
5 complete control over how much postage costs or the cost of health insurance for
6 its employees. Yet it does what it can, emailing instead of snail mail and shopping
7 for health insurance, to minimize these costs just as it should do to minimize
8 production costs.

9 **Q. Does Mr. LaGrand give specific costs that he is proposing be placed in this**
10 **tracker?**

11 A. No. He gives the following general definition of the costs that would be included.

12 These costs are related to Fuel & Power, Chemicals, Waste
13 Disposal, and Purchased Water. This would include things such as
14 the costs of electricity at water treatment plants, the costs of
15 chemicals to treat and clean the water before it is delivered to
16 customers, sludge removal costs at a wastewater lagoon, and water
17 purchased from a neighboring community to supplement our
18 production capacity.⁵¹

19 **Q. Is there a problem with having a general definition?**

20 A. Yes. It would be nearly impossible to audit whether or not the costs that MAWC
21 includes in the tracker are actually production costs increasing the likelihood of
22 future disagreements on how to interpret what is a “cost related to” a production
23 cost.

24 **Q. If the Commission approves a tracker, would there need to be a prudence audit**
25 **of these costs?**

26 A. Since a tracker would remove MAWC’s incentive to keep production costs low,
27 there should be a prudence audit of these costs in the next rate case. However, the

⁵¹ *Id.*, page 32.

1 reality is that in the next rate case there will be hundreds of costs and revenues to
2 audit and normalize. The other reality is that it is next to impossible to prove
3 imprudence. Given the enormous workload and the limited resources available for
4 a rate case audit, it is very unlikely that there would be a comprehensive prudence
5 audit of the production costs included in the tracker and an even lower likelihood
6 of a finding of imprudence. Therefore, although there should be a prudence audit,
7 reality is that there would not be an audit.

8 **Q. Without a tracker, when is the prudence of production expenses reviewed?**

9 A. Without a tracker, imprudently high costs are not recovered from customers; only
10 the amount included in the revenue requirement in the last rate case. While there
11 is not a formal prudence review of these expenses without a tracker, these costs are
12 reviewed in rate case audits to determine the normalized expenses. If it is
13 determined the costs are imprudently high, then the imprudent amount is not
14 included in the revenue requirement. MAWC can then determine whether or not
15 it wants to continue to incur the imprudent cost, thus lowering its opportunity for a
16 higher ROE.

17 **Q. Wouldn't the tracker Mr. LaGrand proposed return any savings to the**
18 **customers?**

19 A. Yes, if there is any savings. However, no utility asks for a tracker if it believes that
20 cost are going to decline. Declining costs are beneficial regulatory lag for utilities.
21 If MAWC can find a way to lower the production costs without lowering the water
22 standards, then it gets to keep that savings to either offset other cost increases or
23 increase its ROE. In addition a tracker would create a disincentive for MAWC to
24 actively look to keep these costs low.

1 **Q. Did MAWC show that absent a production cost tracker, there will be a strong**
2 **likelihood that it will have problems earning its authorized ROE?**

3 A. No. Mr. LaGrand filed very limited testimony on why MAWC should be granted
4 a tracker for these costs.

5 **CONCLUSION**

6 **Q. In conclusion, why should the Commission reject MAWC's request for a RSM**
7 **and a production cost tracker?**

8 A. A RSM, like trackers, changes the balance of risk and responsibility that has served
9 customers of regulated utilities in Missouri for well over a century. A utility comes
10 to the Commission and proves to the Commission the revenue requirement it needs
11 to pay its bills and to earn a return on the capital expenditures it invests in to serve
12 its captive customers. The return included in the utility's revenue requirement is
13 based on the risks the utility is taking in providing service to its customers. Risks
14 that include rising costs and fluctuations in the revenues it collects.

15 After being granted rates that are designed to collect the revenue
16 requirement determined by the Commission, the utility determines how to spend
17 the revenue that it collects from its customers. If the utility can find ways to
18 efficiently meet its customers' needs at lower costs, it keeps those savings even as
19 expenses covered by rates fall. This relationship drives efficiency in the utility's
20 expenditures.

21 If, between rate cases, revenues increase due to increased customer usage,
22 the utility keeps the revenue above what the Commission determined appropriate
23 in the last rate case. If the revenues decrease, then the utility must either find ways
24 to reduce its costs or file a general rate increase case with the Commission. This
25 risk-reward relationship has worked well for MAWC and its customers.

26 On the customers' side, under the current framework, customers have
27 stability in their rates. They are assured that their rates will not change without a
28 thorough review by the Commission of all of the utility's costs and revenues.

1 Changes in customers' bills are a result of their action or inaction. Because
2 customers have an understanding of the impact of a change in their behavior, they
3 can decide to reduce their bills by reducing their usage or, knowing the impact on
4 their bill, choose to water their lawn for an additional hour or two, thus increasing
5 their bill. Under the current framework, customers have information available to
6 them on which to make these types of decisions.

7 **Q. Does this conclude your direct/rebuttal testimony?**

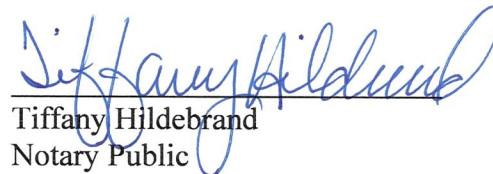
8 **A.** Yes, it does.

In the Matter of Missouri-American Water)
Company's Request for Authority to Implement)
a General Rate Increase for Water and Sewer) Case No. WR-2024-0320
Service Provided in Missouri Service Areas)

STATE OF MISSOURI)
)
COUNTY OF COLE) ss

1. My name is Lena M. Mantle. I am a Senior Analyst for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my direct/rebuttal testimony.
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.

Subscribed and sworn to me this 4th day of December 2024.



My Commission expires August 8, 2027.